Markit Economic Research

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United Kingdom

Unemployment falls and employment surges, but pay growth hits record low

- **Unemployment falls to 6.5%, lowest since December 2008**
- **Employment shows record increase over past year**
- **Pay growth at record low**

The labour market puzzle continues, with official data indicating that employee pay is at an all-time low despite record job creation, plunging unemployment and survey evidence of increasingly widespread skill shortages.

Policymakers will be reluctant to but the brakes on the economic boom that we are seeing at the moment, fearing weak pay growth means households will struggle to service higher borrowing costs if interest rates rise, potentially causing the recovery to stall. The weak wage growth also means inflation should remain subdued. The concern is that the official data may be understating actual pay growth, meaning policy could be inadvertently kept too loose for too long.

Data from the Office for National Statistics showed the headline rate of unemployment dropping from 6.6% in the three months to April to 6.5% in the three months to May. The single–month rate of unemployment in fact dropped to just 6.2% in May, the lowest since September 2008.

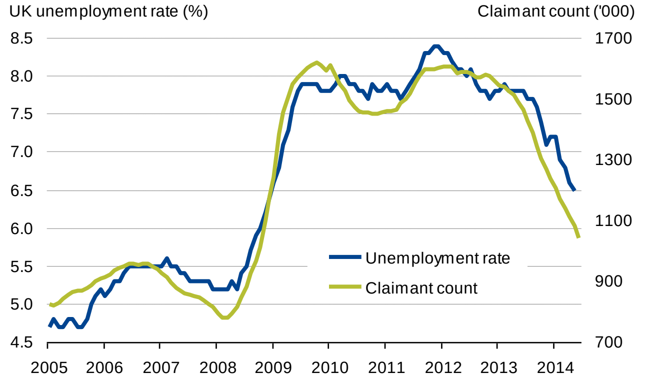
A further drop in the headline jobless rate in the three months to June is also likely, possibly down to 6.3%, after the more up-to-date claimant count figures showed a further 36,300 drop during the month. The number of people claiming job seekers allowance now stands at 1.044 million, its lowest since October 2008.

Record employment growth over past year

The jobless rate has plunged from 7.8% over the past year as employment has surged and, given current rates of job creation, should be below 6% by the end of the year.

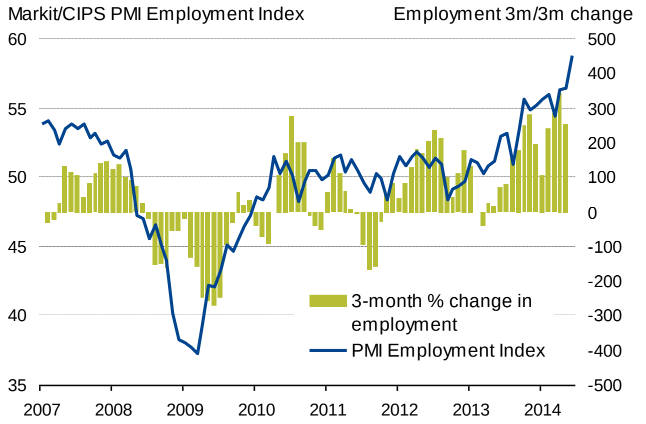
Employment has risen 929,000 in the year to May, the largest improvement seen since data were first available in 1971. While the latest data showed that the number of people in employment rose by 254,000

Unemployment indicators



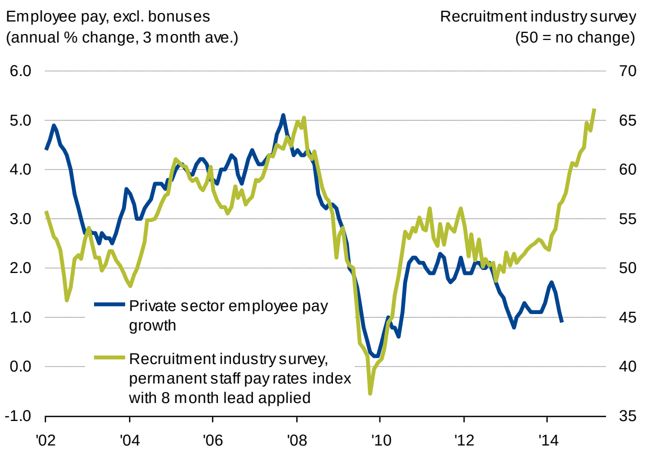
Source: ONS via Ecowin.

Employment



Sources: ONS, Markit.

Employee pay indicators



Sources: Markit, ONS via Ecowin.

in the three months to May, signalling a moderation in the pace of hiring in recent, this may be due to growing difficulties in finding suitable staff. However, the PMI surveys have shown record job creation by businesses in June, signalling no let-up in firms' appetite to expand as we move into the second half of the year. The official data on job vacancies likewise rose in May, up to a six-year high of 648,000.

Woeful pay growth

Despite the record rise in employment over the past year, pay growth remains woefully weak. Regular pay rose just 0.7% on a year ago in the three months to May, down from 0.9% in the three months to April and the lowest seen since comparable data were first available in 2001.

Pay including bonuses was up a miserly 0.3%, down from 0.7% in April and the weakest seen since the height of the financial crisis in 2009.

The data suggest the economic recovery has yet to feed through to the benefit of workers. However, we continue to question these official data. We believe pay growth is weak, but not this weak, and that pay pressures are building rather than abating. Recruitment consultancies hare reported that starting salaries are rising at the fastest rate seen since at least late-1997, when survey data were first available. Higher salaries are having to be offered due to widespread skill shortages in almost all sectors. This is precisely what one would expect to see, given the sheer pace of employment growth in the country at the moment.

According to the ONS data, private sector pay rose just 1.0% in the three months to May, despite the economy growing strongly. Dig a little deeper and the data are odder still. The booming construction sector paid its workers 1.0% less than a year ago, regular pay growth in the manufacturing sector has fallen from 2.8% in February to 1.8% and the retail sector has meanwhile seen pay growth slide from 3.7% in February to just 2.2% in May.

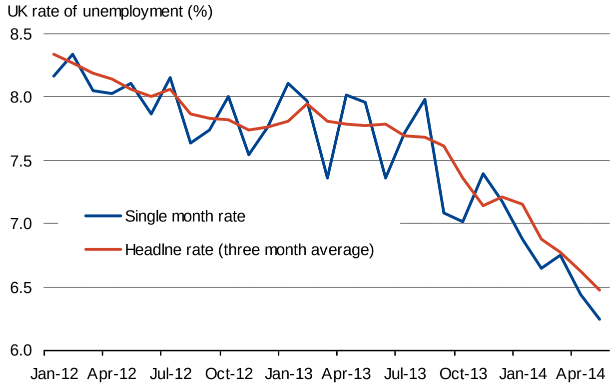
Public sector regular pay, excluding the bailed-out banks, is meanwhile up 1.2% and rising faster than pay in the buoyant private sector, if these data are to be believed.

Households worry about rate hikes

Irrespective of the doubts over the data, until pay growth starts to pick up, the Bank of England will be reluctant to raise interest rates for fear that households will be unable to withstand the higher mortgage costs.

Worries about higher interest rates are already becoming apparent. Markit's Household Finance Index survey, also published today, showed household finances deteriorating at the fastest rate for six months in June, with views on the outlook for finances over the coming year also deteriorating. Half of all households that expressed a view expect interest rates to start rising within the next six months, with one-in-five expecting a rise in the next three months.

Single month unemployment rate



Source: ONS.

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