Jobs and economy monitor

July 2023

Workers are not to blame for cost-of-living crisis

Still enduring the longest pay crisis for two centuries, workers now face the steepest inflation for 40 years. But rather than acting to reduce the impacts of these pressures on people's living standards, the government has been quick to suggest pay needs to be further restrained, and even to blame working people for interest rate rises.

Inflation has not been driven by pay, it was driven by energy and commodity price shocks overseas. While wages have responded as workers sought to protect themselves, they are not driving price hikes.

But even though inflation originated in costs on international markets, government has focused on measures that seek to reduce demand in the economy. The Bank of England's response, strongly supported by the government, has been to hike rapidly interest rates from 0.1 to 5.25 per cent. This approach hits some groups far harder than others. While costs have rocketed for households with unsecured debt, renting properties or with outstanding mortgage payments, and businesses who have been relying on credit, bank and energy company profits, city bonuses and salaries for certain professional and business services have soared.

As well as leaving some people unable to protect themselves from substantial hikes in their living costs, this distributional inequality also brings the effectiveness of the approach into question. It is far from clear that rate rises will have the desired effect, at least not without triggering a substantial recession.

If this happens, those with less will be hit harder – with the loss of salary that comes with the loss of work more difficult to bear. The Bank of England and others have judged recession less likely, but previous forecasts may simply have been premature.

Government is also failing to act. Under previous periods of government-led austerity, the Bank were required to support the economy while the government operated to depress activity. But now, the Government are both supporting the Bank's monetary policy led contraction at the same time as failing to intervene to support those in most need and support growth.

Immediately the government *should* be acting proactively to protect workers and support the economy: the energy cap should operate more effectively so that cost falls feed quickly into the economy, social security should be strengthened and public sector workers properly compensated. The IMF has gone so far as suggesting inflation targets might be suspended. [1]

[1] '"We are not there yet, but that is a possibility," Gopinath told the Financial Times before her speech. "In that environment is when you could see central banks adjusting their reaction function and saying 'OK,

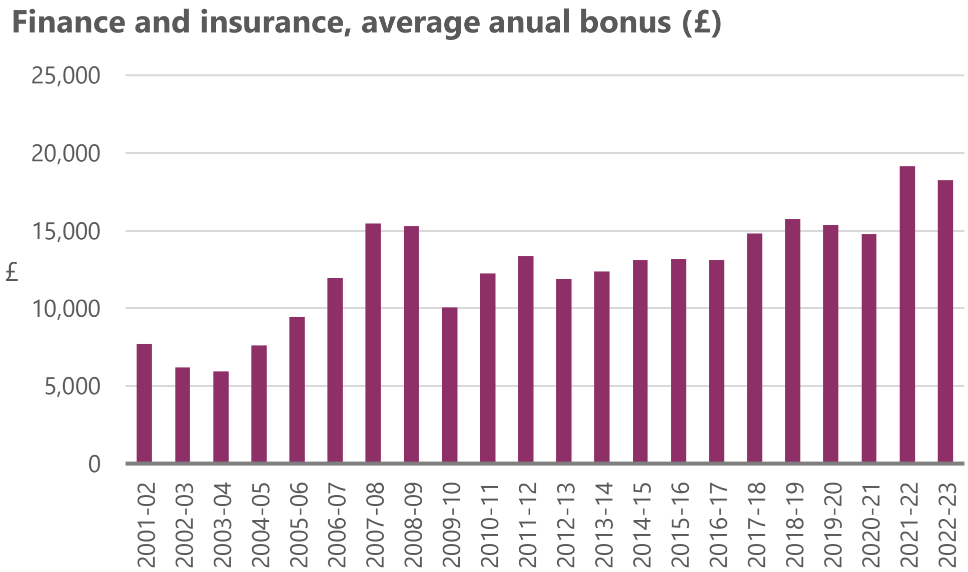
But overall, we need a different approach, with rewarding work not wealth delivering a virtuous circle of stronger and shared growth. We know that higher salaries, reduced debt and stronger production support sustainable growth in jobs and living standards, and that this is the change working people need.[2]

This monitor highlights new statistics and analysis, illustrating the scale of growing inequalities, the detrimental impacts of the government's current approach and the need to secure a better way forward. Key findings include:

- The second consecutive year for record city bonuses
- The highest pay growth coming in the best paid industries
- Profits in the financial sector up 25 per cent on before the pandemic, and big gains at individual banks
- Labour income accounting for a lower share of whole economy inflation than in other episodes of inflation, both over time and across countries.
- The threat of recession, with employment falling for 11 of 20 industries according to the real time jobs data.

Inequalities in rates of pay growth

The anecdotes are familiar – the best year for Porsche sales, and the *Daily Telegraph* reporting "Demand for Rolex watches jumps as super-rich shrug off inflation crisis".[3] Last summer TUC and the High Pay centre found CEO pay for FTSE 100 companies increased 39% in 2021.[4] In cash terms City bonuses (in the 'finance and insurance' category) have been at their highest for two consecutive financial years.



Source: ONS and TUC calculations

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maybe we tolerate inflation being higher for some more time.'": https://www.ft.com/content/7d3276bb-8ef8-444c-8356-2792a6f58a24

2 https://www.tuc.org.uk/research-analysis/reports/doom-loop-economy-work-not-wealth

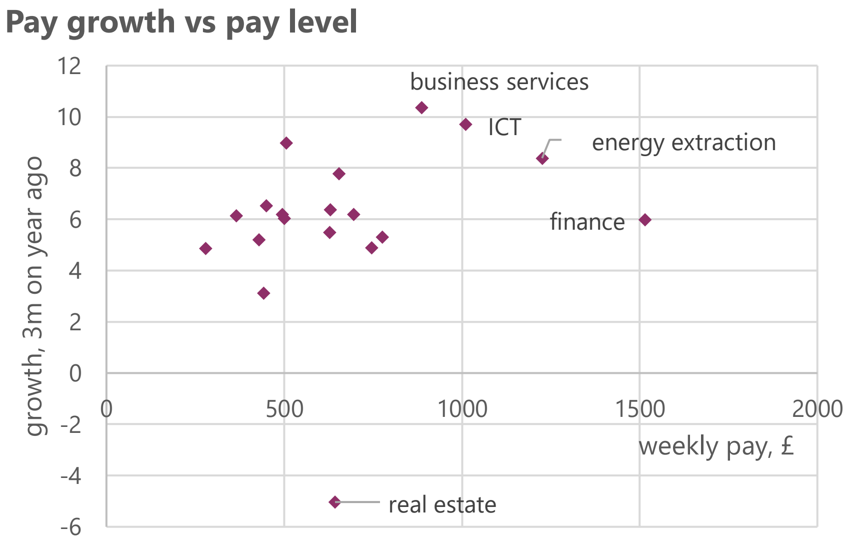
3 https://www.telegraph.co.uk/business/2023/07/13/demand-for-rolexes-jumps-as-super-rich-shrug-off-inflation/

4 https://www.tuc.org.uk/news/high-pay-centre-and-tuc-research-finds-median-ftse-100-ceo-pay-increased-39-2021

On pay more generally, the Bank of England draw attention to inequalities in rates of pay growth between sectors:

> *The pick-up in annual pay growth since the time of the May Report had been concentrated in higher-paying sectors such as financial and business services. Pay growth in lower-paid sectors like wholesaling, retailing, hotels and restaurants had been broadly flat.*[5]

Earnings by industry suggest a more systemic imbalance. The chart below shows that broadly the highest pay growth (on the vertical axis) is happening in the best paid industries (horizontal axis) and *vice-versa*. Pay growth in finance and real estate industries stand out as outliers: on the former bonuses are not captured (as above, and see next chart); on the latter, the steep decline in real estate pay is likely related to stress in the housing and commercial property markets.



source: ONS and TUC calculations

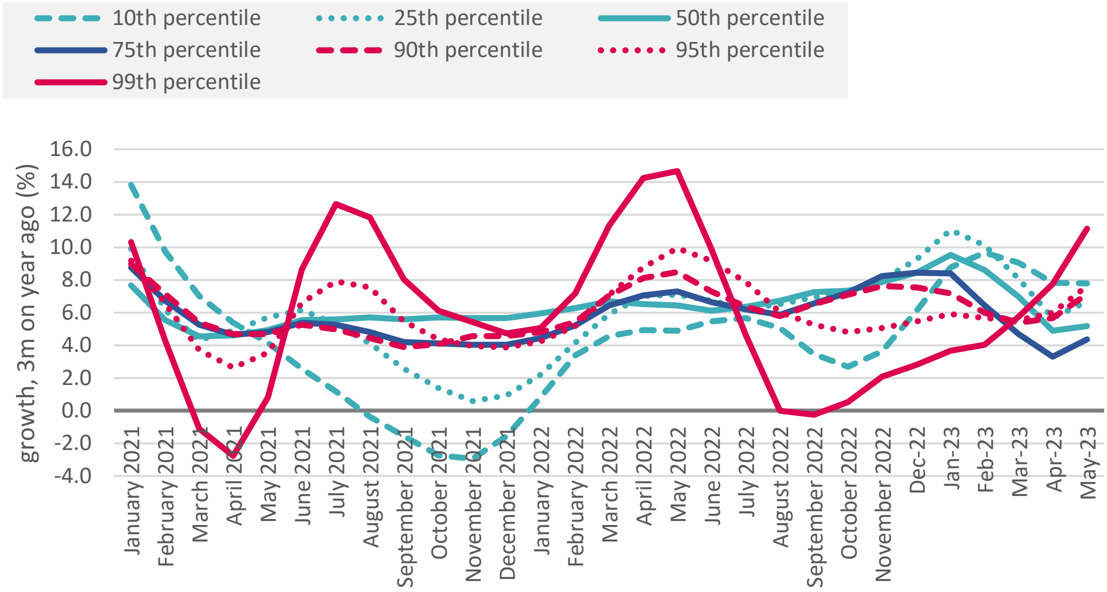
The majority of outcomes are grouped in a narrower range, and average pay growth across these is 5.9 per cent – in contrast to the headline rate of 7.3 per cent.

Last month the TUC published analysis showing any acceleration in pay has been driven only by high earners, further bolstering the Bank of England's observation.[6]

Looking at the 3m on previous 3m measure (which is a more-timely though potentially more erratic indicator of future pay growth), the only group showing significant acceleration since the start of the year is for the 99th percentile (the 95th and 90th are also up marginally). At all other percentiles pay growth has been slowing. Over January to May pay growth for the 99th percentile trebled to 11.1 per cent from 3.7 per cent, but median pay growth nearly halved to 5.2 per cent from 9.5 per cent.

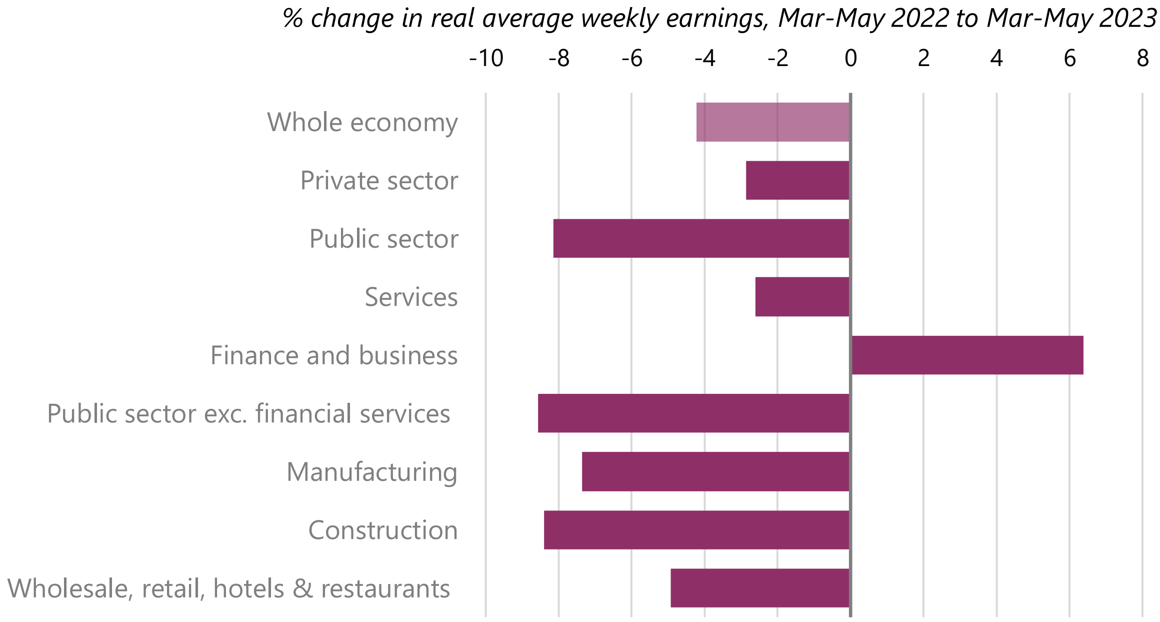
[5] https://www.bankofengland.co.uk/monetary-policy-summary-and-minutes/2023/june-2023
[6] https://www.theguardian.com/money/2023/jun/25/union-fury-as-figures-show-pay-rises-among-top-earners-driving-inflation

Real time employee earnings: quarterly growth (annualised) at different points of the distribution, per cent



On a longer view, the picture is even more categorical: finance and insurance is the only broad industry group with real pay ahead of the position in 2008.[7]

Annual change in real average wages since 2008



Source: ONS, TUC analysis, real wages calculated using CPI, May 2023=100

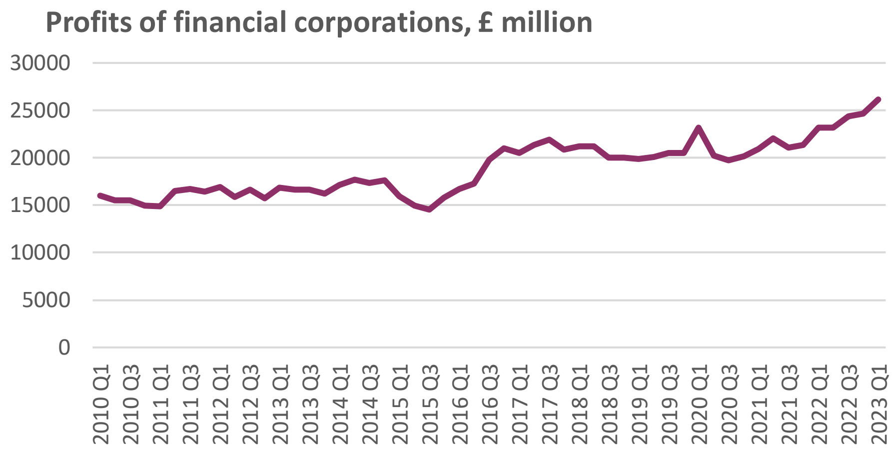
Corporate profit margins protected

Plainly some businesses are doing very well, and this emerges from various sources. Earlier this year Unite updated their 'Corporate profiteering and the cost-of-living crisis' (first issued on 17 June 2022): the headline finding is profits up 89% since before the pandemic. Extended analysis of individual industries (energy, oil and petrol, docks and

[7] A point echoed by the Institute for Fiscal Studies, with emphasis on regional inequalities: https://ifs.org.uk/articles/pay-growth-londons-top-earners-has-driven-geographical-inequality-mean-earnings

shipping, road freight, food and automotive) show huge gains in profits at various points of (some global) supply chains.[8,9]

National accounts figures for the cash amount of profits suggest similar trends. The headline numbers show these growing by 8.5% and 10.8% into each of the last two quarters (and by 23.1 per cent in the year to 2023Q1). However, some caution is needed because the figures are distorted by large subsides to reflect the energy price guarantee scheme, and in general can be volatile including taking adjustments to help balance the three different measures of GDP. The most vigorous growth over recent years has been in so-called *continental-shelf companies* (energy extraction and mining off the coastline), with profits up from £3bn in 2020 to £15bn in 2021 and £35bn in 2022. Financial corporation profits are also increasing very rapidly, up 25 per cent or around £6 billion since the start of the pandemic. Individual bank profits have been coming in even higher, over the past two weeks Lloyds have announced £3.6bn, Nat West £3.9bn and HSBC £16.9bn (globally) for the first half of the year.[10] Overall, it seems likely that while there will be varied trends between industries, there are certainly groups of companies who have seen a significant boost to their profits over the recent period.



Source: ONS

Others have focused on the relative importance of profits in the present inflation, with evidence focused on the US and EU.[11] In their *Employment Outlook* the OECD offers a broader overview, showing (over 19Q4 to 23Q1) the profit contribution greater than the labour contribution for 23 out of 29 countries, and for the OECD as a whole.[12] The UK is one of these countries.

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[8] https://www.unitetheunion.org/what-we-do/unite-investigates/

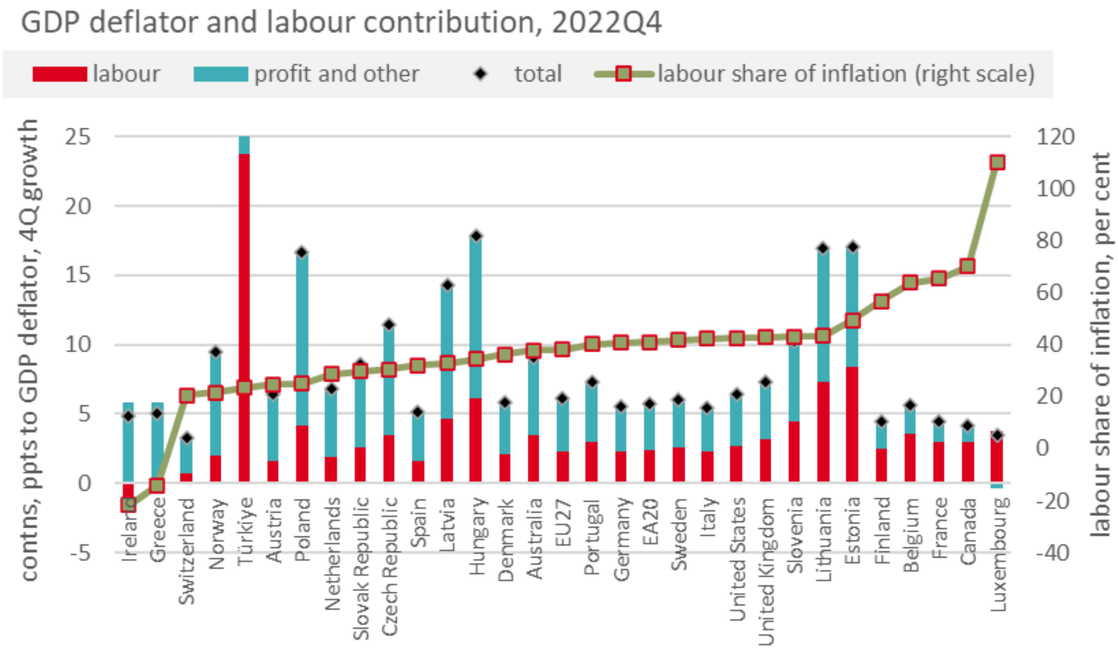
[9] IPPR analysis found the big gains concentrated among certain industries, with many industries seeing falls in profits: "The analysis shows that this increase is being driven by a small number of companies, with 90 per cent of increases in profits accounted for by only 25 companies": https://www.ippr.org/research/publications/prices-and-profits-after-the-pandemic

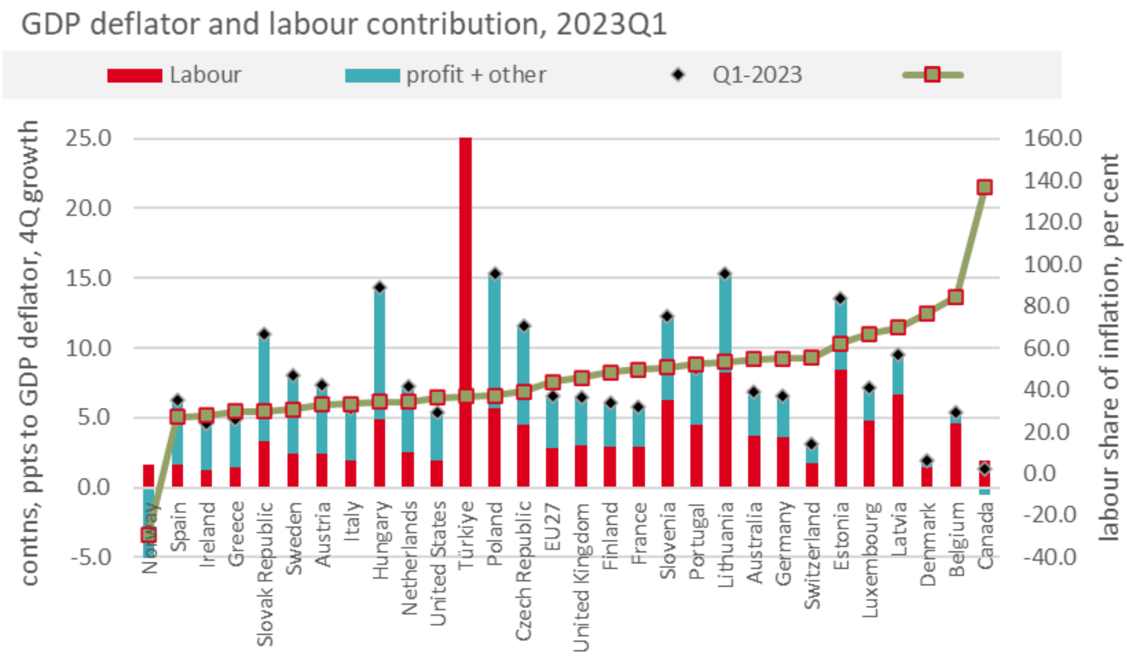
[10] https://www.reuters.com/business/finance/lloyds-upgrades-performance-outlook-improves-interim-dividend-2023-07-26/; https://www.cnbc.com/2023/07/28/natwest-reports-profit-rise-amid-fallout-from-farage-fiasco.html; https://www.bbc.co.uk/news/business-66368580.The national accounts measure is based on different definitions, so that some of interest income is not included.

[11] https://www.imf.org/en/Blogs/Articles/2023/06/26/europes-inflation-outlook-depends-on-how-corporate-profits-absorb-wage-gains

[12] These analyses break down the GDP deflator measure of inflation into the contributions of labour and profits. *The GDP deflator is a broader measure of inflation for the whole economy,* in contrast to the CPI that is based on the household experience of inflation.

Given uncertainties around profits and subsidies/taxes, TUC provisional analysis focuses on the labour contribution to inflation (measured by the GDP deflator),[13] with the charts below ranking the share of labour contribution (right axis) for 22Q4 and 2023Q1 across OECD countries. For 22Q4 a*cross each of the UK, EA and US about 40 per cent of inflation is accounted for by labour costs.* The UK is towards the upper end of OECD counties, but as part of a ('modal') group from Australia to Lithuania. For 2023 Q1 the share of the labour contribution had increased a little but is reduced in absolute terms, and the UK has moved down the ranking and closely matches the EU – again in contrast to the Bank claims.





Source: TUC calculations on OECD data

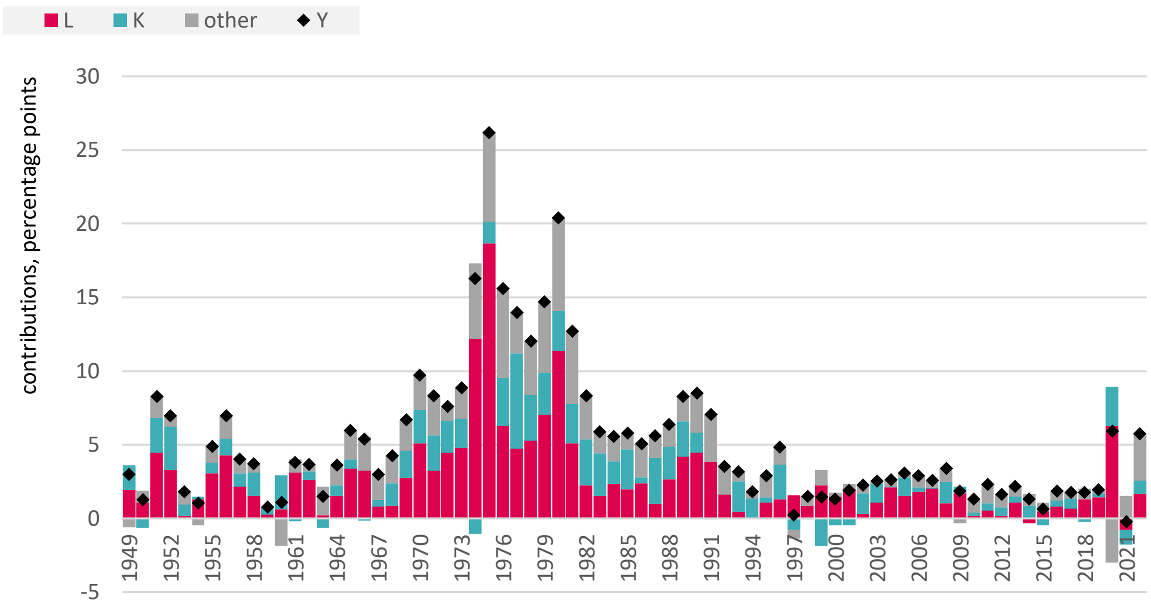
[13] In part because in the UK the 'other' component has moved like the inverse of the profit component.

A further point of interest is that the 22Q4 chart also shows the countries with the highest labour share (i.e. on the right) have among the lowest GDP deflators. And *vice-versa* (but not so cleanly) at the other end – so more chance of high inflation with a low labour share. The story is less tidy in 23Q1, but the same is still true of the low inflation countries.[14]

The UK 40–45 per cent contribution of labour costs to the GDP deflator is also *low on a historical view*. The chart (below) shows annual figures for the UK (here the non-labour contribution *is* split between profit and other). For previous inflation peaks, the labour contributions as a share of the GDP deflator are as follows:

- 1951 54%
- 1975 71%
- 1990 52%

Contributions to GDP deflator, percentage points



Source: ONS and TUC calculations

Overall, the analysis suggests profits are making a non-trivial contribution to inflation, and the contribution from wages in the UK is lower than in previous episodes of inflation and not out of line with other like countries.

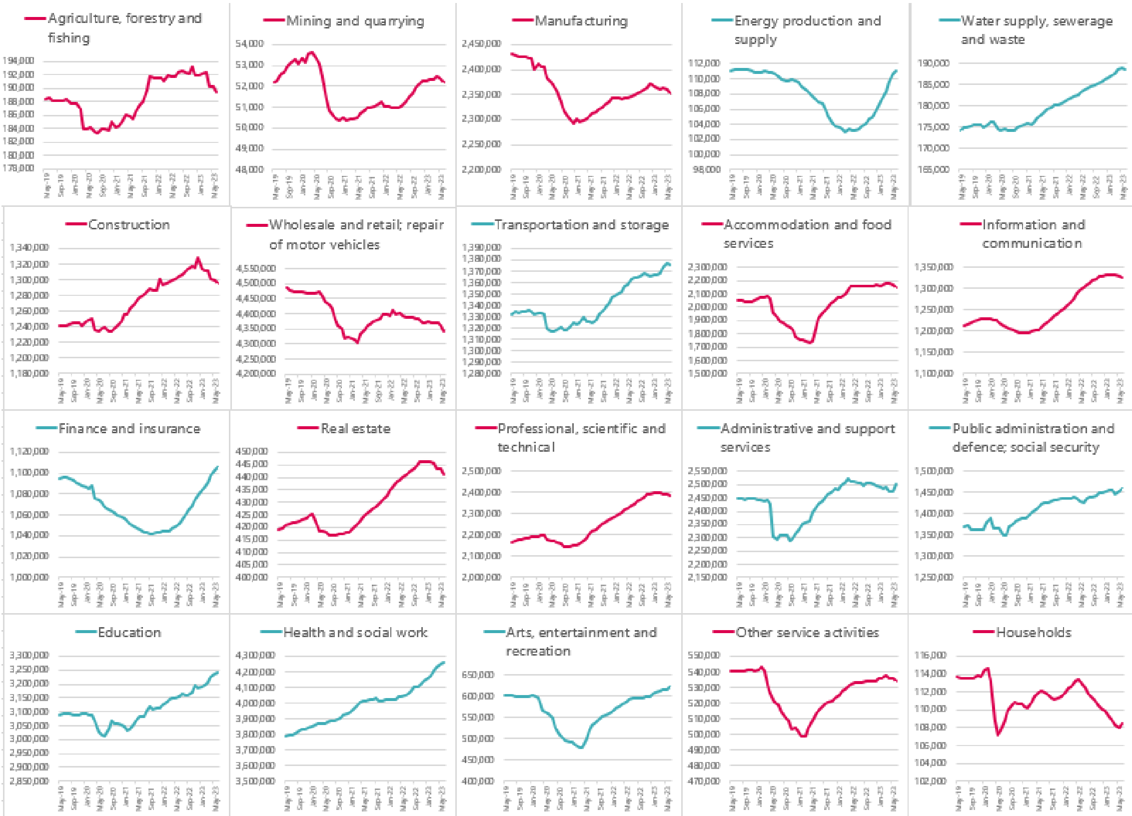
Risk of recession

The TUC has consistently warned of the risk of recession that the current approach may bring, and there are now increasing signs of the economy going into reverse. Perhaps most telling are the real time jobs data (charts below). From the ending of lockdowns to the end of Spring, the industry employment figures were growing strongly. But now the real time figures suggest jobs are falling in a majority – 11 of 20 – of industries, as shown on the charts below: material falls are seen for agriculture (-1.1 per cent on the quarter), manufacturing (-0.2 per cent), construction (-1.1 per cent), wholesale and retail (-0.3 per cent), accommodation and food services (-0.3 per cent), ICT (-0.3 per cent), real estate (-0.7 per cent), professional (-0.4 per cent), other (-0.2 per cent) and

[14] The New Economy Brief emphasises in particular the role of wage indexation in Belgium: https://www.neweconomybrief.net/the-digest/what-if-all-wages-went-up-by-inflation

households (i.e. funded domestic assistance, -0.9). The industries where jobs are still expanding are those dominated by the public sector. Though the wider labour market statistics suggest the rise in health numbers may be mainly outside the public sector, with in the first quarter 80 per cent of the increased employment accounted for by the private sector.[15]

Real time employee jobs by industry:



Separately the monthly GDP figures echo the downturns for a handful of industries, notably for manufacturing (-0.5 per cent comparing May with March), construction (-1.1 per cent), real estate (-0.4 per cent), professional services (-0.4 per cent), and other (-0.6 per cent). In aggregate, the GDP figures continued to fluctuate around zero, with a fall of 0.1 per cent in May, following a rise of 0.2 per cent in April. The three-monthly rate of 0.1 per cent is flat, but as above this is the sum of quite different parts.

Beyond ONS, insolvency service figures showed company insolvencies up very sharply by 40% on a year ago to 2,552.[16] So called 'purchasing manager indices' showed sharp deteriorations for each of manufacturing (down to 45.0 in July from 46.5 in June), services (51.5 from 53.7) and construction (48.9 from 51.6) (NB above 50 indicates expansion). This deterioration is not confined to the UK, not least Germany has been in recession and the euro area manufacturing PMI showed a steep decline at 42.7 in July.

Demand and supply

Fundamentally the Bank are raising rates because of judgements about supply and demand. While demand is recognised as weak, they maintain supply is weaker still. As most workers deal with sharply higher prices and lower real incomes there is unlikely to be excessive upward pressure on demand (household demand growth in the first

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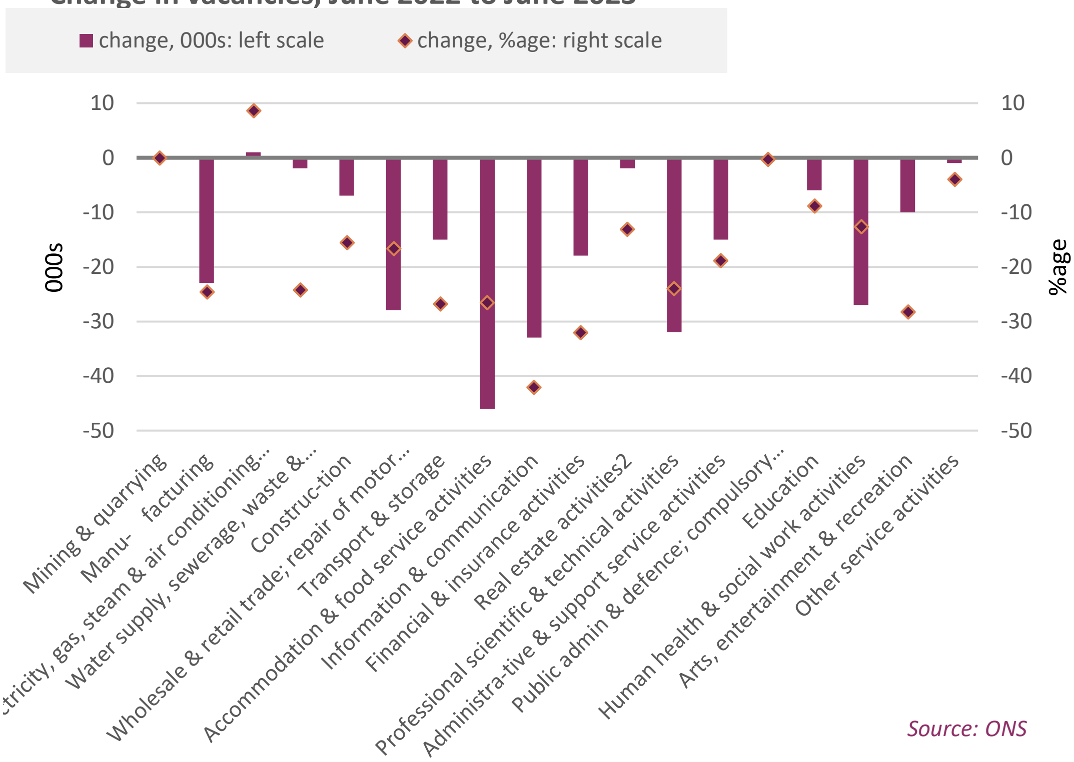
[15] Tables 4(1) and 6 of Labour market statistics release.

[16] https://www.ft.com/content/7ce2dd1b-ebe4-4f9d-9172-6d4b868df5af

quarter was flat). With statistics on banks showing a rise in interest bearing time deposits,[17] it also seems likely that even those who do have spare resources are choosing to save rather than spend.

Many have claimed that high vacancies reflected supply pressures, but over the last year these are now steeply down. Overall, since the peak at the start of 2022 vacancies are down by around 250,000 or 20 per cent. The chart below shows declines across nearly all industries – the main exceptions are energy extraction and supply and industries dominated by the public sector. The steepest fall in numbers is accommodation and food services (45,000) and as a percentage ICT (42 per cent).

Change in vacancies, June 2022 to June 2023



Source: ONS

To the extent these factors did play any role in the present inflation, they are now exerting downward pressure.

Furthermore, while the pressures on households are severe, from a macroeconomic perspective CPI inflation has been falling from a peak of 11.1 per cent in October 2022 to 7.9 per cent in June 2023. Other costs are falling more decisively: producer price input inflation fell by 2.7 per cent in the year to June 2023, down from a recent peak of 24.4 per cent in June 2022, and producer price output inflation is only 0.1 per cent, down from the recent peak of 19.6 per cent in July 2022. Service producer price annual inflation fell to 4.8 per cent in the second quarter from 5.3 per cent in the first.

Dissenting Monetary Policy Committee members Tenreyro and Dinghra have warned that the Bank have done more than enough to bring inflation. Ex-Bank chief economist Andy Haldane offers a metaphor: "Imagine a doctor, uncertain about the nature and severity of a disease, who has administered a large medicinal dose which has yet to take effect. Prudence would cause them to pause to see how the patient responded before doubling the dosage".[18]

[17] https://www.bankofengland.co.uk/statistics/money-and-credit/2023/june-2023
[18] https://www.ft.com/content/b70b7a8f-cc1a-4be9-b51a-866f5d0dab23