JOBS AUDIT

Jobs outlook 2013

The JOBS ECONOMIST

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Introduction

A year ago the consensus view of economists was that a slow growing economy would at best fail to create any net new jobs in 2012 and with the overall supply of labour expanding the rate of unemployment was widely forecast to rise to around 8.8% of the workforce (2.8 million people). In the event this proved completely wrong, despite the fact that economic growth proved even worse than expected. Total employment instead increased by 0.5 million in the year to the third quarter of 2012 while the unemployment rate fell to 7.8% (2.5 million).

This *Jobs Audit* reviews what turned out to be a remarkable 12 months in the UK labour market and, accepting that this year's jobs outcome highlights the inherent uncertainty of economic forecasting, offers a judgment on what is likely to happen in 2013.

Why 2012 was remarkable year for jobs

The overall UK jobs outcome since the start of the deep and prolonged recession in 2008-9 has generally been better than expected but with a number of surprising twists and turns. Job cuts were smaller than expected given the severity of the recession. There was a correspondingly smaller than expected rise in unemployment (to 2.5 million rather than 3 million), and an early recovery in employment in 2010. However, the jobs recovery quickly dissipated as the economy relapsed and government austerity measures began to hit public sector employment. 2011 therefore witnessed a disappointing return to rising unemployment, which eventually reached (8.3%), or just below 2.7 million. But although the economy contracted for three quarters from autumn 2011 onward, this did not result in further rise in unemployment. On the contrary, employment rocketed and unemployment fell.

The total number of people in employment increased by 499,000 (1.7%) in the year to August-October 2012. Men account for two-thirds of the net increase and also registered a far faster rate of employment growth (2.1%) than women (1.2%). Employees account for 70% of the net increase, though in percentage terms employee numbers grew slightly less quickly (1.4%) than self-employment (1.8%). Well over half (57%) of the additional people in employment were working part-time, with part-time employment growing at a much faster rate than full-time employment (3.7% and 1% respectively). The number of people working in temporary jobs increased by 97,000 (6.3%), half of these net new temp jobs being taken by people who would have preferred a full-time job.

Unemployment fell from 2.63 million (8.3%) to 2.51 million (7.8%). The fall in unemployment of 128, 000 was much smaller than the rise in employment the difference accounted for by an increase of 371,000 in the size of the workforce. The number of young people aged 16–24 who were unemployed but not in full-time education fell by 100,000 to 626,000, though the number of unemployed people without work for more than a year increased by 37,000 to 904,000. As with employment, men fared better than women. The number of men unemployed fell by 103,000, reducing the male unemployment rate from 9% to 8.3%. Female unemployment fell 25,000, the unemployment rate falling from 7.5% to 7.3%. However, the relative preponderance of part-time job creation also resulted in an increase of 223,000 (7.8%) in underemployment (i.e. people in employment working fewer hours than they want).

Aside from an exceptional temporary boost to employment from the London Olympics, the surprise jobs outcome is best explained as the result of the confluence of three factors, which together served to at least partially decouple labour market outcomes from weakness in the wider economy.

Firstly, although a rise in employment at a time of economic stagnation caused a slump in labour productivity (in the year to the second quarter of 2012, output per worker and output per hour fell by 1.3% and 2.7%) a continued pay squeeze contained the impact of this on unit labour costs. The annual average rate of growth of regular pay (that is, excluding bonuses) fell from 1.8% to 1.7% against a corresponding fall in the rate of price inflation as measured by the Consumer Prices Index from 4.8% to 2.7%. While even this degree of squeeze could not prevent acceleration in the rate of growth of unit costs to above 3% per annum the latter increase did not prove big enough to trigger net private sector job cuts.

Secondly, the flow of available job vacancies was filled far more quickly. The stock of unfilled vacancies increased by only 26,000 year on year but jobless people were so desperate to find work that any vacancies that did appear were eagerly snapped up, no matter what the pay or hours on offer. It appears that jobseekers are far less choosy than in previous recessions, perhaps because of ever increased pressure on welfare benefit claimants to actively seek work. This latter change in jobseeker behavior along with high immigration also helps explain why, contrary to previous experience, the number of people active in the workforce has increased at a time of economic weakness. And thirdly, jobseekers unable to find an employer to hire them seem to be more willing than ever before to go it alone as self-employed, even though not always able to generate more than a limited amount of paid work.

The jobs outlook for 2013

The Jobs Economist forecasts that the UK will create fewer new jobs in 2013 than in 2012 despite stronger economic growth. And although there will be only a modest rise in unemployment, people in work face longer hours and will have to work harder for no extra real reward.

The background economic forecast underpinning this 2013 jobs outlook assumes that the base interest rate set by the Bank of England will be unchanged at 0.5%, that the Bank of England will maintain its policy of quantitative easing as at the end of 2012, and that the trajectory of fiscal policy is that as last set out in the Chancellor's November 2012 Autumn Statement. Our resulting forecast for consumer spending, government spending, investment, net exports and price inflation suggests growth in GDP of 1%, roughly in line with the latest Office for Budget Responsibility (OBR) forecast.

Private sector employment (including self-employment) is forecast to grow by 200,000, more than offsetting a fall in public sector employment of 120,000. The forecast net increase in total employment (80,000) is less than a fifth of the net increase in 2012 but higher than the OBR forecast which indicates no net employment growth in 2013. Our forecast draws upon surveys of employers' hiring intentions which suggest substantial net hiring by private sector employers in the early months of 2013. Although we expect the hiring momentum to slow during the course of the year, growth in the first two quarters should be enough to result in net employment growth for 2013 as a whole.

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The private sector employment forecast is based on the expectation that the acceleration in unit labour costs which began in 2012 will eventually lead more employers to seek substantial staff cost reductions. It is difficult to know to what extent this will result in increased redundancies, lower recruitment, longer working hours, greater work intensity per hour to boost productivity, or instead further pay restraint to support employment growth. But it is our assessment that after several years of real pay cuts, the exercise of nominal pay restraint has already reached workplace tolerance levels. Consequently, we forecast a return to growth in labour productivity in 2013.

This will slow the pace of employment growth but with somewhat stronger economic growth helping to improve business confidence we expect increased hours and greater work intensity to be the main driver of higher productivity rather than significantly more redundancies or blanket recruitment freezes.

With business confidence growing we expect the balance of net job creation to shift toward full-time and permanent employment. More full-time jobs and increased hours for people already in work will in turn reduce underemployment to below 3 million and increase the annual rate of growth of average earnings to 2.2% by the end of 2013. However, pay settlements will continue to be dampened by high and rising unemployment and average earnings growth will continue to lag behind price inflation (which we expect to be running at 2.3% by the end of 2013). 2013 will thus be the fifth consecutive year of average real pay cuts albeit the squeeze will be less severe than in 2010, 2011 or 2012.

The level of unemployment is forecast to rise by 120,000 to 2.63 million during the course of the year because growth in the size of the economically active population will exceed the more moderate pace of employment growth. The unemployment rate will reach 8.1%, up from 7.8% at the end of 2012 but below the previous peak of 8.3% in 2011. The forecast is lower than the corresponding OBR unemployment forecast for 2013, the OBR expecting no net employment growth (and implicitly even stronger productivity growth) and slightly greater expansion in the economically active population.

By contrast, the Job Economist's additional measures of labour market strength, the Work Shortage rate and the Labour Market Temperature Index (LMTI) (see the December 2012 *Jobs Audit* for details) suggest no net change in the overall state of the labour market. Higher unemployment will offset lower underemployment. With the number of economically inactive people who want a paid job expected to be unchanged, the total number of people short of work will remain at around 8 million (a Work Shortage rate of above 23%). Higher unemployment will also offset a softer squeeze on real earnings growth, with the LMTI expected to be giving a sub-zero reading of -5 at the end of 2013.

Within the total rise in unemployment we expect policy effects, notably the impact of the government's Youth Contract and Work Programme measures, to favour unemployed youths and the long-term unemployed relative to older people and the short-term unemployed. As a result we expect total (16-24 age) youth unemployment to fall below 900,000 (below 600,000 for those not in full-time education) with the number of long-term unemployed broadly stable and thus falling slightly as a proportion of total unemployment.

For the workforce as a whole, we expect job insecurity to remain at the heightened levels prevailing since the financial crisis first struck in 2008. People in work will thus maintain 'a grin and bear it' attitude to their jobs and work as hard as required by their employers, indeed in many cases welcoming the opportunity of longer hours to support squeezed incomes. As a result there will be limited active support on the part of private sector workers for public sector union opposition to government austerity measures even though the latter is likely to be more widespread and potentially more rancorous in 2013 than in 2012. Disgruntlement amongst private sector workers will instead take the form of simmering distrust of bosses, especially those who adopt the trendy management speak mantra of ‘employee engagement’ while piling the pressure on overstretched staff.