XpertHR
Cendex
Reimagining reward analytics

Your guide

Economic, pay and labour market update: February 2023

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The guide covers:

Key takeaways

1. UK economy holds off a recession

UK economic growth was stronger than expected in November 2022 according to the latest figures from the Office for National Statistics (ONS), easing concerns that the UK is heading for a recession. Monthly gross domestic product (GDP) is estimated to have grown by 0.1% in November 2022 following growth of 0.5% in October 2022. On a quarterly basis, the ONS figures show that GDP grew by 0.5% in the three months to November 2022. However, in its December 2022 Monetary Policy Report, the Bank of England forecast that the UK will record negative GDP growth in the fourth quarter 2022. In January 2023, the British Chambers of Commerce echoed this prediction, with its head of research, David Bharier, noting that it expects "five consecutive quarters of recession lasting until the end of 2023."

◊ See the economy section for more details

2. Labour market shows first signs of easing

While overall activity in the labour market remains high, there are signs that economic uncertainty is starting to be reflected in slower hiring by employers. According to the Recruitment & Employment Confederation's latest KPMG and REC, UK Report on Jobs survey compiled by S&P Global (published 12 January 2023), some employers held over hiring activity from the end of 2022 into January 2023, but the scarcity of talent still remains in the market and salary levels are therefore showing strong growth. Following publication of January 2023 labour market statistics from the ONS, the REC commented: "Today's official labour market data confirms the trends that business surveys have been suggesting for some time. Demand for workers is still higher than pre-pandemic, which combines with candidate shortages to make hiring workers a challenge. Slower economic performance and high inflation is starting to slow this trend, but it has not reversed. High inflation and a tight labour market have also fed into higher pay for existing and new staff, a challenge to companies who are facing rising costs across the board."

◊ See the labour market section for more details.

3. Pay awards rise but still fall short of inflation

Pay settlements remain at their highest level for 31 years and were worth a median 5% in the three months to the end of December 2022, according to XpertHR research. However, with a tight labour market and inflation remaining high, many organisations are struggling to balance employees' pay expectations with affordability. Given the unprecedented squeeze on living standards it is hardly surprising that there has been an outbreak of industrial unrest in recent months in both the public and private sectors, notably on the railways and in the civil service, NHS and Royal Mail. According to the ONS, which has now reinstated the publication of monthly strike data, the number of days lost due to industrial action was 467,000 in November 2022.

◊ See the inflation and pay awards section for more details.

4. Consumer confidence shows sustained low

Market analyst GfK's long-running Consumer Confidence Barometer fell by three points in January 2023, with a figure of -45. The forecast for personal finances over the next 12 months rose slightly to -29. Meanwhile, expectations for the general economic situation over the coming 12 months fell with a one-point drop to -54 (compared with -53 in December 2022).

Joe Staton, client strategy director at GfK said: "After a short-lived and weak rally in Q4 last year, UK consumer confidence has slipped to -45 in January. Consumers have a New Year hangover – but it's of the economic kind – with high levels of pessimism over the state of the wider economy. And unlike a conventional hangover, this one won't vanish quickly. The only glimmer of hope in the results is a slight uptick in the outlook for our personal financial situation, but this is of little comfort because it is still 25 points lower than this time last year. This month's six-point decline in the major purchase index does not augur well because consumer spending is a driving force of our economy and future growth. With inflation continuing to swallow up pay rises, and the prospect of some shocking energy bills landing soon, the forecast for consumer confidence this year is not looking good. One thing we can be sure of is that 2023 promises to be a bumpy ride."

◊ See the economy and inflation sections for more details

The economy

UK economy holds off a recession

Gross domestic product (GDP) measures the value of goods and services produced in the UK and estimates the size of and growth in the economy. According to the latest figures from the ONS, UK GDP is estimated to have risen by 0.1% in November 2022, following a rise of 0.5% in October 2022. Monthly GDP is estimated to be 0.3% below its pre-coronavirus levels (February 2020) (see Chart 1).

Services sector: growth recorded

ONS figures show that services grew by 0.2% in November 2022, following growth of 0.7% in October 2022. The strongest growth (compared with the previous month) was recorded in administrative and support service activities (2%), information and communication (1.7%) and accommodation and food service activities (1.5%). Transport and storage recorded -2.7% growth, while arts, entertainment and recreation fell by 2.1%. Output in consumer-facing services grew by 0.4% in November 2022, after growth of 1.5% in October 2022.

Production: falls further

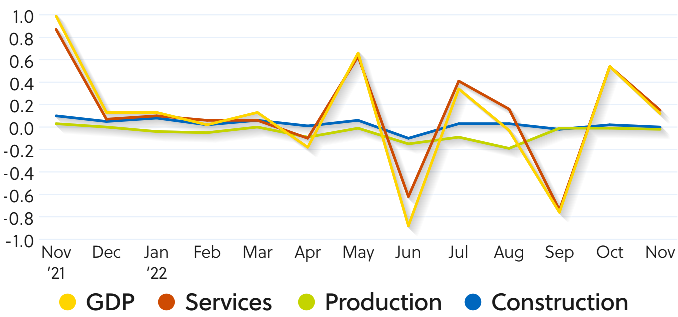
The ONS reports that production fell by 0.2% in November 2022 after a fall of 0.1% in October 2022 and was the main contributor to the fall in GDP. This fall was mainly due to a 0.5% decrease in manufacturing.

Construction: flat following previous growth

According to the latest ONS data, construction was flat in November 2022, after growth of 0.4% in October 2022. The lack of growth was due to a decrease in new work (down 0.4%), offset by an increase in repair and maintenance (up 0.6%). The next monthly update on GDP from the ONS (for December 2022) is due to be published on 10 February 2023.

The next monthly update on GDP from the ONS (for September 2022) is due to be published on 11 November 2022.

Chart 1. Contributions to monthly GDP growth, percentage points, November 2021 to November 2022



Source: Office for National Statistics.

Responding to the latest GDP figures, Alpesh Paleja, CBI lead economist, said: "While the economy performed better than expected in November, the data can't mask the underlining problems in the UK economy. High inflation is severely impacting household budgets and businesses are facing intense cost pressures. As a result, consumer spending and investment plans are weakening."

Economic forecasts

Used as an indicator of the health of a country's economy within a particular timescale, GDP is the total monetary or market value of all the finished goods and services produced within a country's borders in a specific time period. Figures from the **Treasury's Forecasts for the UK Economy: January 2023** predict that UK GDP will fall by -0.8% in 2023 (average of independent forecasts).

On a global level, the OECD's November 2022 **Economic Outlook** notes that the energy shock "has pushed up inflation to levels not seen for many decades and is lowering economic growth all around the world". Global growth is projected be just 2.2% in 2023 before improving slightly to 2.7% in 2024. However, it expects much of this grow to come from Asia, with little growth in Europe, North America and South America, For the UK, the OECD forecasts a decline in GDP of - 0.4% for 2023, before picking up only marginally to 0.2% growth in 2024.

The labour market

When employers make decisions about recruitment and retention, they need to consider the supply-side aspects to the equation: what is the current state of the labour market and how is that likely to impact resourcing? The information below summarises the current state of the UK labour market.

According to the latest ONS Labour market overview for the three months to November 2022 (published 17 January 2023):

Employment

- The employment rate for those aged 16 to 64 was 75.6% in the period September to November 2022, unchanged on the previous quarter (June to August 2022).
- There were 32.781 million people aged 16 and over in work, up 27,000 compared with June to August 2022 and up 219,000 on the same period a year ago.

Unemployment

- The unemployment rate for the three months to the end of November 2022 rose by 0.2 percentage points from the previous quarter to 3.7%
- There were 1.244 million unemployed, up 56,000 on the previous quarter but down 138,000 on the same period a year ago.

Job vacancies

- The estimated number of job vacancies in October to December 2022 fell by 75,000 on the quarter to 1,161,000 and the rate of quarterly growth in vacancies fell to negative 6.1%.

Commenting on the latest ONS labour market figures, David Bharier, head of research at the British Chambers of Commerce (BCC), said: "The UK's tight labour market is one of the top challenges preventing our businesses and economy from growing. If firms can't hire the staff to fulfil their order books, any room for growth is extremely limited. Businesses need to play their part, by engaging with local skills and employment opportunities, adopting flexible working policies where possible and helping older workers develop their skills for the changing workforce."

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David Bharier, head of research at the British Chambers of Commerce (BCC)

According to the latest KPMG and REC, UK Report on Jobs survey (published 12 January 2023):

Availability of workers

- The overall availability of workers to fill permanent and temporary vacancies fell again, although the rate of decline eased. The seasonally adjusted index for permanent roles stands at 45.8 in December, compared with 43.6 in November. The number of people available for temporary roles also deteriorated further in December. The index stands at 47.5, compared with 46.2 in November.
- The number of people placed in permanent jobs by recruitment consultancies across the UK fell for the third month in a row in December 2022. However, recruitment consultancies saw a pickup in billings received from the employment of short-term staff across the UK in December 2022.

Neil Carberry, REC chief executive, said: "A slowdown in permanent placements is not unusual in December, but this one comes as part of a wider softening in the permanent market. Recruiters tell us that this was enhanced by firms pushing hiring activity back into January in the face of high inflation and economic uncertainty. But overall activity levels remain high, with vacancies and starting rates of pay still growing."

Labour turnover

Given the effects of the pandemic and the labour market tightening, many organisations expected labour turnover to pick up in 2022 compared with the previous two years. XpertHR analysis of the Cendex dataset found that voluntary turnover among UK employers stood at 16.4% in the 2022 calendar year, compared with 9.6% in 2021. Total turnover also trended higher, at 22.5% in 2022 against 14.6% in 2021. The charities/not-for-profit sector recorded particularly high turnover levels, whilst the public sector was some way below the whole economy figure. The latest findings are based on a survey of 279 organisations that together employ 423,684 people.

Pay awards

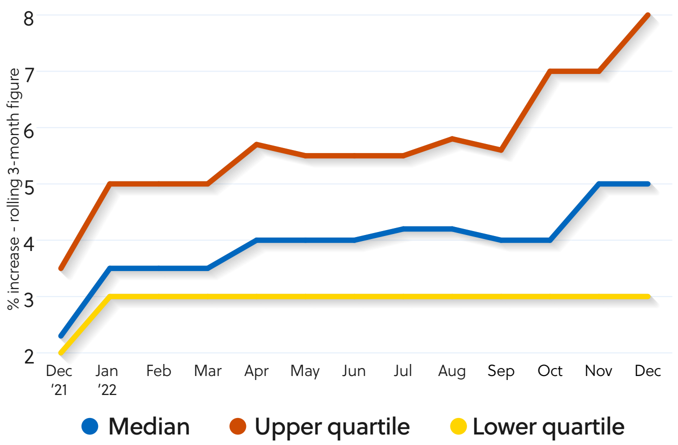
XpertHR collects details of around 1,200 pay settlements in the course of the year and adds them to the pay databank. The pay team analyses this data, reporting headline pay settlement figures each month on a three-month rolling basis. It is the most comprehensive whole-economy source of this type of information.

XpertHR pay researchers recorded details of 36 pay awards effective between 1 October 2022 and 31 December 2022, covering almost 65,000 employees. Our headline findings are based on 34 pay settlements that award an across-the-board rise (with two including an additional element based on merit).

Key findings

- **Median at 5%**. The midpoint basic pay award was 5% over the three months to the end of December 2022, exactly the same as in November. It is more than double the 2.3% figure we recorded for the same period in 2021.
- **Interquartile range widens**. The interquartile range covers the middle 50% of awards, thus excluding the 25% of deals at both the top and bottom of the pay pile when ranked by value. This is a useful tool for settlement analysts as it excludes any outliers that may skew calculations while at the same time indicating how closely pay awards are clustering around the median. Last month four percentage points covered the middle half of wage deals (7% upper quartile, 3% lower quartile). Now the gap between the top and bottom quartiles has widened to five percentage points (8% and 3% respectively).
- **Two-thirds of deals higher.** Taking a matched sample approach, where the 2022 pay review is compared to the 2021 increase for the same group of workers, two-thirds (65.2%) are higher in the three months to the end of December 2022 than in the same period a year ago. Around one in five (21.7%) received the same award in both years, with the remaining 13% subject to a lower increase in 2022 than 2021.

Chart 2: Pay settlements for the whole economy December 2021 to December 2022



Source: XpertHR.

A complementary analysis of the Cendex database shows that pay for incumbent employees increased by an average of 4.5% in the 12 months to December 2022 once the effect of promotions is stripped out. Lower pay growth in the public sector held down this headline figure - pay increases averaged over 6% for all other sectors of the economy, including the voluntary sector.

Pay awards forecasts for 2023

A year ago, pay awards were still subdued, running at a median of just 2.3% (in the three months to the end of

December 2021). However, as inflation accelerated so did the level of pay awards. Pay freezes, a key feature of pay agreements during the pandemic, started to diminish.

Findings from XpertHR's latest survey of **Pay planning and forecasts for 2022/2023** suggest that these patterns are expected to continue, with 91% of pay reviews over the next year forecast to result in a pay rise and just 2.5% to end with a pay freeze. The outcome for the remainder is uncertain at this stage, although several of these respondents put this down to uncertain business conditions or not yet knowing how to counter competitors' salaries and/or the cost of living.

Our key findings on pay awards for the coming year are as follows:

- **Median set to maintain recent high**. Private-sector employers are predicting a median 5% pay award over the year to 31 August 2022, up from 3.7% over the past year.
- **Wider spread of deals around the median**. Predicted pay awards over the coming year are worth between nil and 15%. The middle half of deals is expected to fall within the relatively wide range from 3.5% to 6%.
- **Pay freezes all but melt away**. Just 11 employee groups, representing 2.5% of forecasts, are expected to receive a pay freeze. The majority of these are in the services arm of the private sector.
- **Three in 10 pay awards predicted to be worth 5%**. A pay increase of 5% is not only the median value but also the most common prediction, with 29.2% of reviews forecast to result in this figure.
- **Manufacturing and services matched**. Employers in both manufacturing and production, and private-sector services companies, are expecting to award a median 5% pay rise over the coming year.

Minimum wage rates

The rates of the national living and national minimum wage will increase from 1 April 2023 as follows:

- national living wage for over-23s: from £9.50 to £10.42 an hour (a 9.7% rise);
- national minimum wage for those aged 21-22: from £9.18 to £10.18 (10.9%);
- national minimum wage for 18 to 20-year-olds: from £6.83 to £7.49 (9.7%);
- national minimum wage for 16-17 year old workers: from £4.81 to £5.28 (9.7%); and
- the apprentice rate: from £4.81 to £5.28 (9.7%).

Introduced in 2015, the national living wage aimed to increase pay and productivity without harming jobs, while reducing the Government's spend on benefits. In May 2022, the Low Pay Commission (LPC) carried out a **review of the national living wage** which found that although the national living wage increased wages and did not reduce employment, the increase in earnings did not lead to higher incomes and did not measurably improve productivity. However, it was found that the growth in earnings helped to reduce regional pay inequality and contributed to shrinking gender and ethnicity pay gaps. The review also found that after the introduction of the national living wage, minimum wage workers were less likely to move employers but continued to progress into higher-paid roles at the same rate as previously.

Living Wage Foundation rates

The living wage (commonly referred to as the Real Living Wage to distinguish it from the Government's national minimum and national living wages) as used by the Living Wage Foundation sets two recommended hourly pay rates for those aged 18 and over; one for employees working in London and the other for those working outside the capital. These figures are calculated annually by the Resolution Foundation and overseen by the Living Wage Commission, based on the best available evidence on living standards in the UK and in London.

Unlike the national living wage, the Real Living Wage is voluntary and has no statutory backing but nevertheless is paid by more than 11,000 employers, including many household names.

The living wage rates (effective from September 2022) are set at £11.95 per hour in London and £10.90 elsewhere, representing increases of 8.1% and 10.1% respectively on the previous year's rates. This year's increase was brought forward from its usual date of November in recognition of the sharp increase in living costs over the past year.

This increase moves the rate of the voluntary living wage significantly above the statutory national living wage. The Low Pay Commission (LPC), which makes recommendations to the Government on the rate of the national living wage, along with the national minimum wage, subsequently announced an increase in the national living wage to £10.42 an hour from April 2023.

The chart below shows the percentage increase in the national living and national minimum wage rates alongside the UK living wage rates recommended by the Living Wage Foundation. The table provides the full set of rates for all the levels of the national minimum wage and both the UK and London living wage rates as used by the Living Wage Foundation.

Chart 3: Percentage increase in minimum wage rates 2017-2023

Source: Low Pay Commission and Living Wage Foundation.

The Government has set a target for the national living wage to reach two-thirds of median earnings by 2024 but has said that the LPC should advise it to review the target or the timeframe should the economic evidence warrant this. In April 2021, the national living wage was extended to 23- and 24-year olds for the first time; the threshold will further reduce to age 21 by 2024.

Table 1: National living wage and national minimum wage rates 2017 to 2023

	2017	2018	2019	2020	2021	2022	2023
Apprentices aged under 19, or aged 19 and over but in the first year of their apprenticeship	£3.50	£3.70	£3.90	£4.15	£4.30	£4.81	£5.28
Workers aged 16 to 17 inclusive	£4.05	£4.20	£4.35	£4.55	£4.62	£4.81	£5.28
Workers aged 18 to 20 inclusive	£5.60	£5.90	£6.16	£6.45	£6.56	£6.83	£7.49
Workers aged 21 to 22 inclusive *	£7.05	£7.38	£7.70	£8.20	£8.36	£9.18	£10.18
Workers aged 23 and over - the national living wage	£7.50	£7.83	£8.21	£8.72	£8.91	£9.50	£10.42
LWF UK Living wage **	£8.75	£9.00	£9.30	£9.50	£9.90	£10.90	–
LWF London Living wage **	£10.20	£10.55	£10.75	£10.85	£11.05	£11.95	–

*Prior to 2021, this rate applied to workers aged 21-24.
**New rates announced on 22 September 2022 (brought forward from the usual November date in recognition of the sharp increase in living costs over the past year). Employers are recommended to implement the new rate within six months and by 14 May 2023 at the latest.

Inflation

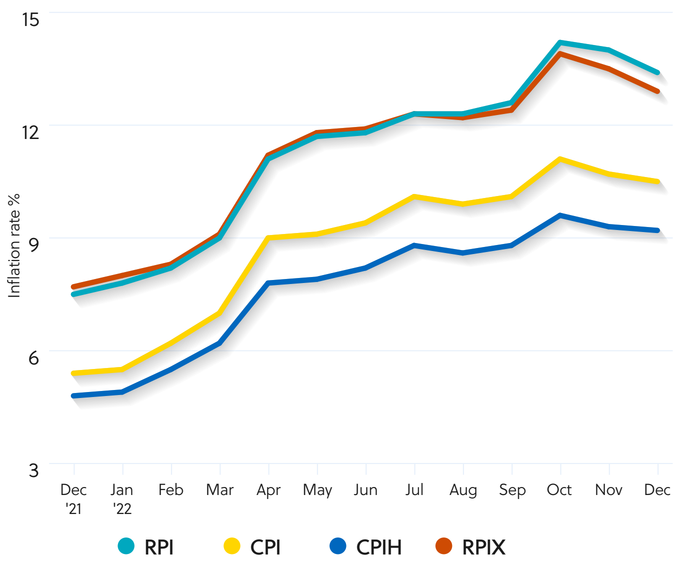
Consumer prices index (CPI) inflation reached 10.5% in December 2022, down from 10.7% in November 2022 (and marking the second month in a row of decline), according to the latest figures from the ONS. Retail prices index (RPI) inflation fell to 13.4%, down from 14.0% in November 2022; consumer prices index including owner-occupiers' housing costs (CPIH) fell to 9.2% (9.3% in November 2022); and RPI excluding mortgage payments (RPIX) stood at 12.9% (down from 13.5% in November 2022). With the XpertHR median pay award at 5% in the three months to the end of December 2022, the gap between pay rises and inflation remains stark.

The largest upward contributions to the annual CPIH inflation rate in December 2022 came from housing and household services (principally from electricity, gas and other fuels) and food and non-alcoholic beverages, the ONS reports.

Commenting on the latest inflation figures, Alpesh Paleja, lead economist at the CBI, said: "These figures add to a growing body of evidence that the UK has passed peak inflation. Over the coming year, inflation should fall further towards single digits, as global price pressures ease and an economic downturn takes some of the heat out of price setting.

"Despite this, the cost-of-living crisis will continue to be a very real problem for both households and businesses, as price pressures remain high in the short-term. Against the backdrop of a recession firms will continue to face higher costs and weak demand conditions."

Chart 4: Inflation December 2021 to December 2022



Source: Office for National Statistics.

On 14 December 2022, the Bank of England increased interest rates from 3.0% to 3.5%, after members of the Monetary Policy Committee (MPC) voted by a majority of six to three in favour of the 0.5 percentage point increase. The Bank said that "the labour market remains tight and there has been evidence of inflationary pressures in domestic prices and wages that could indicate greater persistence and thus justifies a further forceful monetary policy response." The Bank of England's next Monetary Policy Report is due to be published on 2 February 2023.

Responding to the MPC's decision on interest rates, Alpesh Paleja, CBI lead economist, said: "Another big interest rate rise from the Bank of England doesn't come as a surprise, in the face of historically high inflation. However, with global price pressures starting to wane, along with the economy set to fall into recession, it is likely that we'll see smaller interest rate rises for the foreseeable future."

Inflation forecasts

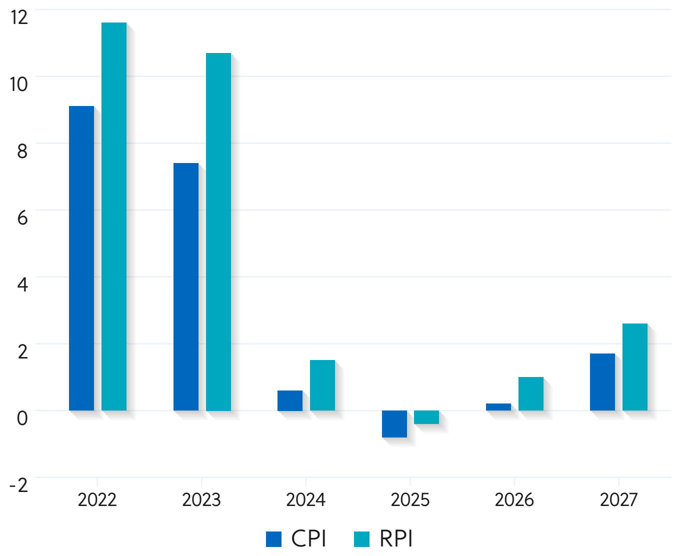
XpertHR routinely monitors a range of economic forecasters' predictions on pay and prices. Looking ahead, XpertHR's panel of economists expects RPI inflation to average 13.3% over the first quarter of 2023 and 10.2% over the year as a whole, while they forecast CPI inflation to average 10.1% in quarter one 2023 and 7.1% for the year as a whole.

Both CPI and RPI are widely used by employers as benchmarks when considering pay awards, though few tie increases directly to inflation. The ONS favours a move to the CPIH measure, which varies from CPI in taking account of housing costs and has designated CPIH as a national statistic. It is, however, seldom used by employers in pay setting. RPI had its status as a national statistic withdrawn in March 2013, but the ONS continues to publish data on this measure for legacy purposes.

According to the **OECD's Economic Outlook**, November 2022: "The unexpected persistence of inflationary pressures this year owes much to the outbreak of the war in Ukraine, which resulted in an immediate spike in a number of key commodity prices. Headline consumer price inflation in the major advanced economies is projected to moderate [through to] 2024 as tighter monetary policy takes effect, demand pressures wane, and transport costs and delivery times normalise, although the pace of decline will vary across countries." The OECD predicts that in the UK CPI inflation will average 8.9% in 2022, 6.6% in 2023 and 3.3% in 2024.

The Office for Budget Responsibility (OBR), which provides independent and authoritative analysis of the UK's public finances, produces a range of five-year economic forecasts twice a year, usually in March and November. The OBR's November 2022 update suggests that CPI inflation will peak at a 40-year high in the final quarter of 2022, before falling to below nil in 2025 and not returning to its 2% target until 2027. Such long-term forecasts are, however, reliant on many assumptions and are subject to frequent and sometimes radical revision. The OBR's next forecast is due to be published in March 2023.

Chart 5: OBR inflation forecasts (%) 2022-2027



Source: Office for Budget Responsibility.

Use of inflation in pay setting

For many years, the majority of employers tracked inflation using the RPI measure to inform decisions on cost-of-living pay awards. However, since the Government moved to target CPI, this measure has grown in popularity among pay setters. XpertHR research shows that most employers take into account either RPI or CPI or both. The inflation measures most likely to be referred to by employers when considering pay awards are (respondents could select more than one option):

- consumer prices index (CPI) - 51.7%;
- retail prices index (RPI) - 39.6%; and
- consumer prices index including owner-occupied housing (CPIH) - 20.4%.

In October 2016, the ONS announced that it intended to move to a third measure as its preferred statistic on inflation - CPIH. It is likely that pay setters will continue to adopt CPIH either instead of or alongside other measures as a guide to increases in employee living costs. Further information can be found in **How to use inflation measures in pay setting**.

Additional resources

This commentary draws together and is based on a range of data and information, primarily from XpertHR's ongoing research programme and from the Office for National Statistics. Subscribers to XpertHR can access the following resources:

Pay and benefits resources, including

- 2022 Cendex Employee Benefits report
- Pay trends and pay awards
- Pay planning and forecasts for 2022/2023
- Employers' response to the cost-of-living crisis: XpertHR survey 2022
- Hybrid working: XpertHR survey 2022
- Labour turnover rates: XpertHR data 2023

Economic data, including

- Inflation
- Unemployment
- Business confidence
- Recruitment

XpertHR Benchmarking – HR Metrics data on a range of HR policies and practices

Sources of official data can be found on the Office for National Statistics website, including:

- Inflation and price indices
- Employment and labour market
- Earnings and working hours
- GDP monthly and quarterly estimates

Additional resources include:

- Office for Budget Responsibility latest forecasts
- Bank of England publications
- HM Treasury forecasts
- British Chambers of Commerce economic data
- The OECD's Economic Outlook
- GfK's Consumer Confidence Barometer