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Blog Post

Brexit, the Bank of England and the Gig Economy: How not to interpret today's labour market

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News that the Bank of England's Monetary Policy Committee (MPC) unanimously agreed to raise the base interest from 0.5% to 0.75% yesterday was not unexpected, but nevertheless raises eyebrows at a time when the economy remains fragile and Brexit uncertainty continues to cast a cloud over expectations on the economy going forward. In their official statement released yesterday, the Bank attempted to justify the rate increase by pointing to recent labour market developments:

"*The MPC continues to judge that the UK economy currently has a very limited degree of slack. Unemployment is low and is projected to fall a little further. In the MPC's central projection, therefore, a small margin of excess demand emerges by late 2019 and builds thereafter, feeding through into higher growth in domestic costs than has been seen over recent years*…. [and] *CPI inflation was 2.4% in June, pushed above the 2% target by external cost pressures resulting from the effects of sterling's past depreciation and higher energy prices*."[1]

Conventional opinion has it that the Bank has been warning for some time now of an interest rate rise to come given the recent performance of the economy, and that financial market expectations were such that for the Bank to continue crying wolf would eventually lead to a loss of "credibility", and that a rate rise now would give it some "wriggle room" to lower the base rate again should Brexit negotiations fail spectacularly (i.e., "No Deal").

It is therefore worth pondering their assumptions further. The Bank essentially is tasked by the UK Government to keep inflation within range of the set target of 2% p.a. and has to consider a range of economic factors in assessing this, unemployment and wage rates being two of them. In their decision, an official unemployment rate of 4.2% during the March-May quarter (its lowest rate since March 1975)[2], means that there is little "slack" left in the economy. The Bank clearly feels that this will feed into inflationary pressures, as the unemployment rate has seemingly dipped below the NAIRU (Non Accelerating Inflation Rate of Unemployment).

But is the UK economy really at "full employment"? Whilst it is notable that the Bank's regional officers have been feeding in reports of businesses struggling to fill vacancies (no doubt in part caused by the decline in the number of EU nationals wanting to work in the UK since the 2016 referendum), does this still translate into wage inflation pressures? That is, are we still living in a

[1] https://www.bankofengland.co.uk/monetary-policy-summary-and-minutes/2018/august-2018
[2] https://www.ons.gov.uk/employmentandlabourmarket/peoplenotinwork/unemployment/timeseries/mgsx/lms

world akin to the 1970s, when trade union membership as a % of the workforce (i.e., density) hovered around 50%?

I would say, "no". Or, to put it more precisely, that whilst there are skills gaps and shortages in certain areas manifest in the UK economy, "full employment" today should not be implicitly equated with a saturated jobs market dominated by permanent full-time employment, with strong trade union representation (as per the 1970s). As such, there is evidence to suggest that the wage pressures cited by the Bank have eased, with Larry Elliott reporting that growth in total pay has fallen rather than risen: annual growth in total earnings fell from 3.1% in December to 2.5% in May, whilst regular pay (this doesn't include bonuses) fell slightly from 2.7% to 2.6.[3] In today's UK labour market, trade union membership is at record lows, with a density of around 23% during 2016; and much jobs growth over the last 10 years has been in what can be labelled "precarious jobs".

Analysis by John Philpott for the Resolution Foundation[4] reported that over 7 million workers, or some 22.2% of the workforce in 2016 (up from 18.1% in 2006) were in precarious forms of employment. Of these, a breakdown of this 22.2% suggests that 15.1% were "self-employed", 4.3% on a temporary contract, and 2.9% on "zero hours" contracts (which only comprised 0.5% of the workforce in 2006). Of the self-employed category, Philpott's analysis suggested that half were low paid and took home less than two-thirds of median earnings and that 2 million self-employed workers were earning less than £8 per hour. These are the people that we often associate with the "Gig Economy".

The variable hours associated with these jobs suggest that there may be more "slack" (or *underemployment*) in the labour market than the MPC thinks. The essential precariousness of work for many in the UK now is reinforced by findings from the Resolution Foundation that reported that real weekly earnings were expected to only grow by about 1.6% over this decade, as opposed to 12.7% during 2000-2009, and over 20% during all decades prior to this, since the 1920s. In the tax year 2016/2017, the median average salary was estimated to be £26,500[5].

It is only in the context of understanding the relatively weak bargaining power of workers and stagnant real wages today that we can resolve the seeming contradiction between "full employment" and record use of food banks in the UK. It goes without saying that for these people in particular (and especially in the current period of Brexit-induced uncertainty), the last thing needed is a rate rise by a Central Bank that could be accused of using an outmoded view of the UK labour market.

[3] https://www.theguardian.com/business/2018/aug/02/interest-rate-rise-the-lack-of-dissenting-voices-came-as-a-surprise
[4] https://www.theguardian.com/uk-news/2016/nov/15/more-than-7m-britons-in-precarious-employment
[5] https://www.incometaxcalculator.org.uk/average-salary-uk.php