Bad news for UK consumers as wage growth falls sharply

The gap between inflation and pay growth is widening but we don't think the Bank of England will hike rates before 2019.

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The lives of UK consumers aren't getting any easier, according to the latest jobs report. The key measure of wage growth, which excludes bonuses, fell sharply and is now much lower than the 2.6 - 2.7% readings we saw towards the tail-end of 2016. Employment growth stayed relatively elevated at 109k, but it is worth noting that this is being lifted by a large 340k "single month" reading for March.

1.7% Average weekly earnings (3M/3M YoY%)

Worse than expected

In its May Inflation Report, the Bank of England noted that it doesn't expect this weakness in wage growth to persist. It pointed to other labour costs, including the apprenticeship levy and workplace pension changes, as putting a temporary cap on salary growth. The Bank forecasts that average weekly earnings could return to 3.5% next year.

The widening gap between price and wage growth appears to be hitting spending

However, given the uncertainty related to Brexit, and also now the overall UK political environment, we suspect that this forecast might prove to be optimistic. A survey recently conducted by the Institute of Directors suggested that 57% of members were either “quite” or “very” pessimistic about the UK economy of the coming year. We anticipate that this uncertainty will depress investment and hiring over coming months.

But whatever happens, what is clear now is that real incomes are falling noticeably. The sharp fall in the value of sterling, and more recently a pick-up in utility costs, has pushed headline inflation to 2.9%. This widening gap between price and wage growth appears to be hitting spending, and we are likely to see further evidence of this squeeze in tomorrow’s retail sales report.

Whilst yesterday’s spike in inflation might ruffle some feathers among Bank of England hawks, we think that the downside risks to growth from lower spending and uncertainty means that the MPC will not hike rates before 2019.

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