Overall good news on the labour market for employment – but much less so for productivity and real wages

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*Though the employment figures released yesterday, showing a big drop in the unemployment rate, were remarkably good, there is an awful lot of head scratching going on. This is because job creation has been comfortably outpacing economic growth, and productivity performance as measured by GDP per hour has been dire, writes **Ian Brinkley**.*

The labour market figures released yesterday morning are remarkably good. Compared to the last three months of 2013 (October to December) and the previous three months of 2013 (July to September), the economy generated just over 250,000 jobs. This takes the unemployment rate down from 7.7 to 7.1 per cent. The Bank may have to review monetary policy much sooner than it expected, reflecting the Governor's commitment to look again when unemployment hits 7%.

Just as encouraging was the composition. Almost all of the employee jobs created were full time and all of them were permanent. To be sure, the lack of part time job creation creates its own problems for those who either want, or have no choice, to work part time. But it was full time jobs that received the biggest blow over the recession and these losses are being rapidly replaced.

But if economists were completely honest – as of course they always are – there is an awful lot of head scratching going on. We can safely say there is an economic recovery underway and it is picking up legs – economic forecast are steadily being revised upwards. Yet job creation has been comfortably outpacing economic growth, and productivity performance as measured by GDP per hour has been dire. In manufacturing and services alike productivity has fallen in every quarter since the start of 2012.

Why private sector employers are hiring in large numbers despite this trend is hard to explain, especially as employers were supposed to have hoarded labour during the recession. We have had to resort to complicated explanations combining cheap labour (real wages have been falling for several years) with inaccessible or dear capital for SMEs, and exceptionally high levels of investment uncertainty which deter big companies. Measurement could also be a problem in a world where hard to value "intangible" knowledge based assets play such a big role in business development and growth. But a fully convincing explanation for the productivity puzzle still has to be found.

That labour is cheap compared with many other business inputs is undeniable. The figures show that regular pay – measured by average weekly earnings excluding bonuses – grew by 0.9% (averaged over the three months to November and compared with the same three months a year ago). For many firms charges on energy, rents, and some raw materials will have increased by far more. Even so, it is clear that many wage earners will continue to feel the squeeze on real wages. One response is to work more hours. This may help explain why despite the increase in full time jobs, the number of "involuntary" part time workers who say they only took part time work because no full time jobs were available has remained stubbornly high.

So overall good news on the labour market for employment – but much less so for productivity and real wages. We need to see improvements in both of the latter if living standards are to rise and competitiveness sustained. Economic forecasts for 2014 suggest we will see more jobs – but with growth picking up we should also see productivity start to recover. That and lower inflation should also deliver some increase in real wages. But who benefits from the recovery and by how much will determine whether the Coalition gets the popular credit for the good overall jobs performance.

Note: This article gives the views of the author, and not the position of the British Politics and Policy blog, nor of the

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