

UK economy stable in 3m to May, while labour market shows signs of cooling

July 2023

The additional bank holiday for the King's Coronation reduced the number of working days in May and so lowered GDP accordingly, with GDP falling by 0.1%. This left output flat overall in the quarter to May. But a smaller-than-expected decline points to underlying resilience, in line with the CBI's recent surveys. The return to a normal number of working days in June suggests a likely rebound, raising the odds that the UK economy avoided a contraction in the second quarter. Meanwhile, although, earnings growth was higher than expected in the quarter to May, overall conditions cooled, with the unemployment rate up and vacancies down.

Is the glass half full or half empty?

This latest data from the ONS paints a fairly mixed picture for the UK economy. The economy saw no growth over the three months to May, but this was still better than was expected. Wage growth was also stronger than expected – for the three months to May, wage growth reached 7.7% for the private sector – but the unemployment rate rose to 4.0% and vacancies fell 84k, suggested demand for labour is easing. Overall, compared to a few months ago, wage and inflation data outturns with better activity data increase the likelihood that the Bank of England will increase interest rates further in the months ahead. Over the past month alone, market expectations for the peak in Bank Rate early next year have risen from 5.5% to 6.25%.

The latest set of labour market data for the quarter to May suggested that weak demand conditions over the past year have started to take their toll. Employment continued to move higher (by 102,000), but with the number of inactive people falling back further, the supply of workers expanded more rapidly than the demand for them, pushing the unemployment rate up to 4% (from 3.8% previously).

Nonetheless, the enduring strength of wage inflation is likely to draw the Bank's eye. Average regular pay rose at the fastest pace on record (outside of the pandemic when the JRS distorted wage data), with robust growth in both private (7.7%) and public (5.8%) sector pay, reflecting the persistent strength of inflation and the (still) high number of job vacancies across the economy. This will worry the Bank's Monetary Policy Committee (MPC), despite unemployment coming in higher than expected. Recent business surveys (including our own) suggest that firms expect wage growth to decelerate, but until the MPC sees this in official data they're likely to retain a hawkish bias.

Altogether, recent data paints a picture of a stagnant economy dogged by high inflation and a labour market that is still tight from a historical perspective. This is broadly what we expected in our latest [economic forecast](#), albeit with a couple more rate hikes now looking more likely. Looking ahead, we expect inflation to slow more rapidly in the months ahead, which will support household incomes. But given the countervailing trend of rising interest rates, growth is likely to remain fairly sluggish through the second half of the year, and downside risks have risen.

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Further details

UK economy slips with the Coronation bank holiday dampening activity

- **UK GDP fell by 0.1% month-on-month (m/m) in May** following growth of 0.2% in April. This leaves monthly GDP standing 0.2% above its pre-pandemic level (in February 2020).
- On a rolling 3-month basis – a better gauge of underlying growth – GDP was unchanged, continuing the broader trend of stagnation seen in the economy since Spring 2022.
- A contraction in production was the primary cause of the fall in GDP, with output down by 0.6% in May (following an upwardly revised -0.2% in April). Within this, manufacturing output fell by 0.2%, while electricity & gas supply fell by 2%, likely reflecting warmer weather in June. Output in construction also declined in May, by 0.2% (from a downwardly revised -0.9% in April), while services output was unchanged (from 0.3% last month).
 - Output in the broader consumer-facing services fell by 0.2%, following upwardly revised growth of 1.1% in April. The main drag came from a 1.1% fall in food & beverage service activities (following growth of 2.4% in April). This leaves consumer-facing services 8.8% below their February 2020 levels.
- The ONS noted that May's outturn data was affected by the additional bank holiday for the King's Coronation which led to reduced output in a range of manufacturing industries and construction businesses. But some businesses in the arts, entertainment & recreation sector benefitted from the extra holiday as people used extra leisure time.
 - Industrial action also impacted GDP as May saw strikes by nurses, rail workers, teachers and the civil service. In particular, strikes on the rail network had an adverse impact on footfall in food & beverage service activities.
- A contraction in May was widely expected, given the bank holiday, but analysts expected a larger decline (-0.3% m/m). Looking ahead, June's data will likely be flattered by a return to the usual number of working days.

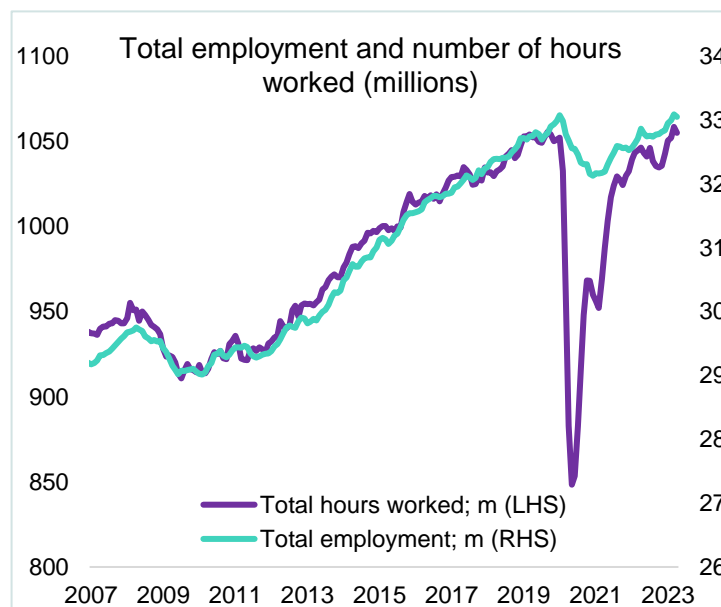
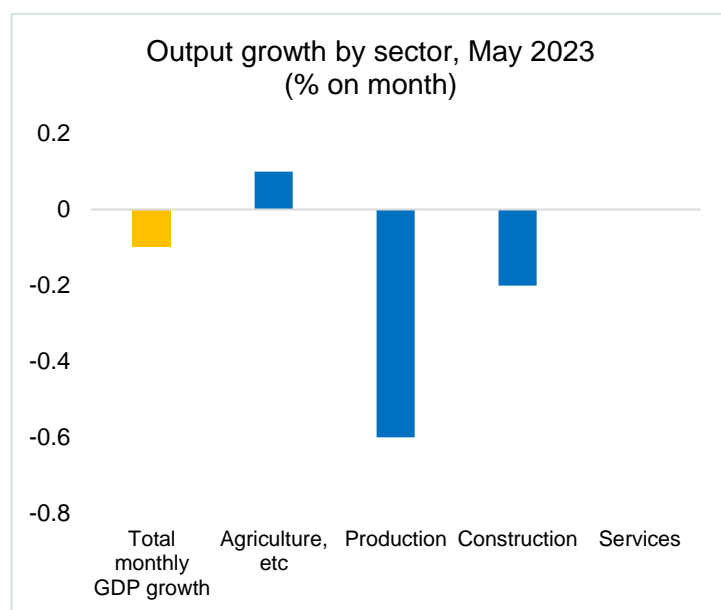
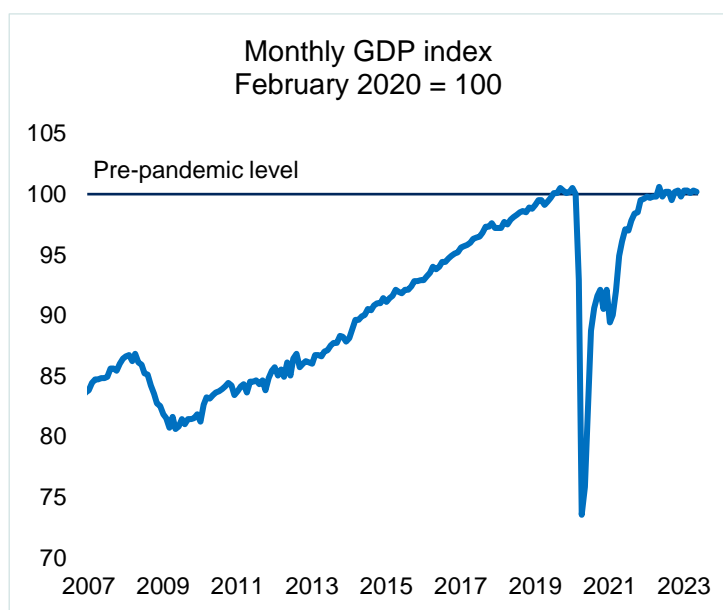
Employment picks up, but rising labour supply sees unemployment rise too

- Total employment rose by 102,000 in the three months to May, compared with the previous quarter. The employment rate increased by 0.2% points to 76%, still some 0.6% points below its pre-pandemic level in December 2019 to February 2020.
- The unemployment rate edged up to 4%, having risen by 0.2% points from the previous quarter.
- The number of inactive workers fell by 141,000 to 8.7 million. This is still 281,000 people higher than before the pandemic.
 - The main reason given for inactivity was long-term sickness, which remains close to record highs at 2.6 million.
- Job vacancies fell by 8% in the three months to June 2023, to 1,034,000. The number of vacancies has consistently fallen on a rolling basis for a year (though vacancies are still 25% above pre-pandemic levels).

- This also means the ratio of unemployed people per vacancy has risen to 1.30, from a record low of 0.95 in June-August 2022 and the highest in nearly two years.

Wage growth continues to rise in both the public and private sector, but still fails to keep up with inflation

- Nominal regular pay (excl. bonuses) rose by 7.3% over the year to March-May 2023, matching last month for the fastest rate of growth seen outside of the COVID-19 pandemic.
 - In the private sector, nominal regular pay growth rose to 7.7%, from 7.6% in the three months to April. In the public sector, nominal pay growth remained at its highest level since August-October 2001 (5.8%).
 - Finance & business services saw the fastest wage growth by sector (9.0%), followed by manufacturing (7.8%), construction (6.2%) and wholesaling, retailing, hotels & restaurants (5.2%).
- Adjusting for inflation, real regular pay across the economy fell by 1.2% in the year to March-May, a less steep decline than during the three months to April (-1.8%).



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