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The Fraser of Allander Institute (FAI) is a leading economic research institute with over 40 years of experience researching, analysing and commentating on the Scottish economy. The FAI undertakes a unique blend of cutting-edge academic research alongside applied commissioned economic consultancy in partnership with business, local and national government and the third sector.

The Scottish Centre for Employment Research (SCER) has an international reputation for high quality research and knowledge exchange on work and employment. SCER works collaboratively with academic, policy and practitioner stakeholders to generate high impact research that delivers shared benefit. The Centre has particular expertise in supporting workplace innovation, job quality and fair work, key priorities for Scotland.

Labour Market Trends is jointly produced by the FAI and SCER and aims to shed light on key developments in Scotland's labour market. Alongside a summary of recent trends and the outlook, the report also highlights longer trend developments and areas for discussion.

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Summary

Key Labour Market Indicators: January-March 2018

	Employment (16-64)	Unemployment (16+)	Inactivity (16-64)
Scotland	74.7	4.3	21.9
England	76.0	4.2	20.6
Wales	73.4	4.4	23.0
N.Ireland	69.7	3.1	28.0

Source: ONS, Labour Force Survey

The Scottish labour market has been relatively robust in recent times with high employment and low unemployment.

In the latest data, we are seeing these trends continuing with further increases in employment and decreases in unemployment.

There are 10,000 more people in work than a year ago; 2,000 fewer people in unemployment than a year ago; and 19,000 fewer people economically inactive than a year ago.

The quarterly unemployment rate dropped slightly to 4.3% over the period Jan-Mar, with the employment rate rising by 0.3% points over the same 3 months.

Scotland now has an unemployment rate slightly above that of the UK, but with an employment rate which is nearly a whole percentage point lower.

Tying these together is that Scotland has a higher rate of economic inactivity (21.9%) than the UK as a whole (21.0%).

Although as we have discussed before, such small variations are not statistically significant.

One of the most notable trends in the Scottish labour market over the past two years has

been the substantial falls in youth (16-24 year old) unemployment.

In the most recent data released today – covering 2017– youth unemployment is at a record low of 9.2%. This is less than half what it was five years ago.

In the same period in 2012, youth unemployment was 20.5%.

Encouragingly these declines have been seen in both the male and female statistics with male youth unemployment at a record low of 10.1%, down from 23.1% in 2012.

As always, these headline numbers give us a snapshot of the health of the labour market, but growth remains weak in the Scottish economy.

Furthermore, the latest productivity data show that – even with a bounce back in the final quarter of the year – labour productivity fell 1.9% in real terms in 2017.

This does not bode particularly well for growth in take home pay.

Official forecasts from the Scottish Fiscal Commission (SFC) are for this to continue for the foreseeable future.

We remain slightly more optimistic than the SFC believing that activity will pick-up this year. But there remains significant uncertainty around the future outlook for the economy – so the next few months promise to be an interesting time for Scottish labour market data.

Fraser of Allander Institute & Scottish Centre for Employment Research

May 2018

Overview and Analysis

Table 1: UK labour market, Jan-Mar 2018

	Employment (16-64)	Unemployment (16+)	Inactivity (16-64)
Scotland	74.7%	4.3%	21.9%
Quarterly Change	0.3	-0.2	-0.1
Annual Change	0.6	-0.1	-0.5
UK	75.6%	4.2%	21.0%
Quarterly Change	0.4	-0.2	-0.3
Annual Change	0.8	-0.4	-0.5

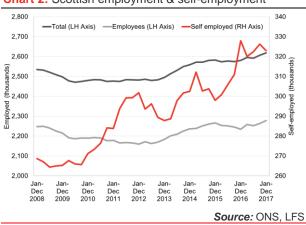
Source: ONS, Labour Force Survey (LFS)

Chart 1: Scottish employment & unemployment rate



Source: ONS, LFS

Chart 2: Scottish employment & self-employment



Introduction

On headline indicators the Scottish labour market appears to be in relatively robust health. (Table 1)

However, as we will chart out in the following pages, challenges remain, particularly with respect to productivity growth and real earnings growth.

The employment rate in Scotland is 74.7%, up 0.3%-points in the most recent data. This continues a sustained period of growth in employment over the past few years. (Chart 1)

Employment growth has been strong across the whole UK in recent years. But with more rapid growth in employment in the UK as a whole, Scotland no longer has a higher employment rate than the UK average.

The Scottish unemployment rate continued to decrease, falling by 0.2%-points to 4.3%. Again given improvements in the rest of the UK, this is no longer better than the average for the UK.

It is worth noting however that the confidence intervals around these figures mean that these small differences are not statistically significant. More important than small fluctuations are the overall trends in these headline statistics.

One of the features of the labour market over the past decade is that employment has become more flexible, and there has been substantial growth in self-employment as shown in Chart 2.

While self-employment remains a relatively small proportion of those in employment in the Scottish labour market, it is a growing proportion.

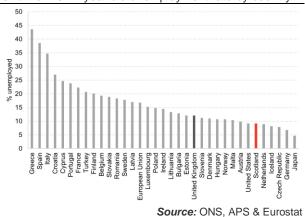
Indeed, it remains the case that 70% of the growth in employment over the past two years in Scotland comes from growth in self-employment.

Source: ONS, LFS

Chart 4: Youth (16-24) employment and unemployment



Chart 5: 16-24 year old unemployment rate by country



Labour market outcomes by age and gender

Just as the labour market has become more flexible in terms of the types of employment people find themselves in, we have also seen substantial increases in employment among those above the state retirement age.

As Chart 3 shows, the employment rate for those aged 65+ has increased by over 40% over the past decade.

In contrast the employment rate for those aged 16-24, commonly referred to as the 'youth' labour market, is actually still lower than it was a decade ago. The same is true for those aged 35-49.

At the same time, the youth unemployment rate hit a new record low in 2017. (Chart 4)

Tying these features together is what has happened to economic inactivity, which has increased over this period.

Economic inactivity refers to a broad category of situations including the more positive (being a fulltime student for instance) and the less positive (for example being unable to work as a result of being sick).

The data shows that for the whole working age population in Scotland recent years have seen an increase in economic activity in Scotland as a result of being in fulltime education.

Scotland's record low rate of youth unemployment is impressive in its own right, but particularly so when compared to other parts of Europe and beyond, only a handful of which have youth unemployment rates lower than Scotland's. (Chart 5)

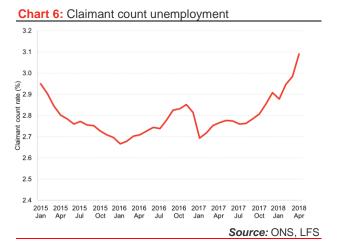
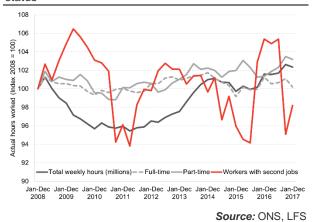


Chart 7: Employment by gender



Chart 8: Average weekly hours worked by employment status



One of the key messages at a UK level emerging from the most recent release of labour market data was that there had been a noticeable increase in the claimant count.

Recall that this alternative measure of unemployment is based on administrative data of those accessing out of work benefits.

Since the roll out of Universal Credit, the UK Government's flagship welfare policy, the claimant count measure of unemployment has seen its importance in understanding the dynamics of the labour market decline.

Prior to the introduction of Universal Credit, it was relatively straightforward to calculate the number of people accessing benefits as a result of being unemployed.

Since Universal Credit was introduced, which aimed to produce a single welfare payment combining a range of different benefits together, statisticians have been working to produce a comparable measure of those accessing benefits as a result of being unemployed.

While these statistics are still experimental, they have now been produced on a consistent basis for a sufficient period that they are attracting attention once more.

Chart 6 shows that there appears to be an increasing trend of people accessing out-of-work benefits in Scotland. This contrasts with the headline unemployment data which suggests that unemployment in Scotland has declined over the past year.

The past decade has also seen a narrowing of the gap in the employment rate between men and women, as Chart 7 shows, albeit that gap appears to be widening again in recent times.

With the increasing flexibility in the labour market, the past decade has also seen changes in working hours. Chart 8 shows that part-time workers have seen their hours grow, on average, but around 3% over the past decade, in contrast the hours worked by full time workers are now back to 2008 levels. Growth in overall hours worked in the Scottish economy is coming from increases in hours worked by part-time workers.

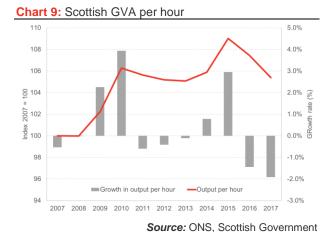


Chart 10: Scottish GVA and hours worked 2007-2017

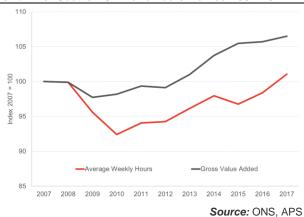
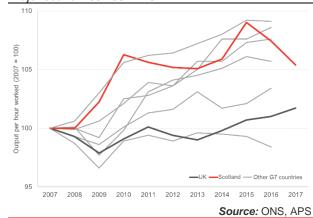


Chart 11: Scottish labour productivity growth relative to major economies 2007 - 2017



Productivity

Perhaps the biggest economic narrative of the past decade, not just in Scotland but in the UK and a number of advanced economies, is what has happened to productivity and in particular labour productivity.

Labour productivity is measured in terms of either output (GVA) per hour worked or output per job. Labour productivity is key to long term economic growth, and increases in the wages of workers. Without improvements in labour productivity, firms are struggling to increase wages of workers.

In Scotland, data released this month show that the past two years have seen real-terms labour productivity fall. (Chart 9) The past decade has seen labour productivity increase by just over 5%, in total. This compares to average labour productivity improvements in the decade between 1998 and 2008 of 1.5% per year.

Underpinning this calculation is the evolution of GVA growth and growth in average weekly hours worked, shown in Chart 10. Average hours worked declined in the immediate period following the financial crisis, but since 2010 has tracked growth in overall GVA relatively closely. As a result, productivity has been flat.

While Scotland's labour productivity has been disappointing, compared to other advanced economies Scotland's productivity growth has not been that bad – although performance has dipped in recent years.

As we have shown before, while the UK has grown more quickly than the Scottish economy over this period, the UK has seen even faster growth in hours worked and jobs. The effect of this, as shown in Chart 11, is that Scotland's labour productivity has grown more quickly than in the UK as a whole over the last 10 years.

The effect of this is that Scotland has been 'catching up' with the rest of the UK. Nevertheless, UK labour productivity remains poor and matching the UK is not much of an achievement. Indeed, Scotland remains locked in the 3rd Quartile of OECD countries for productivity.

Chart 12: Median real earnings in Scotland and UK CPI inflation

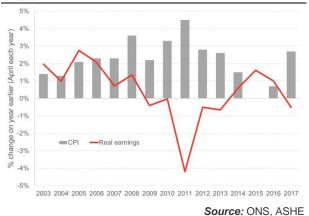
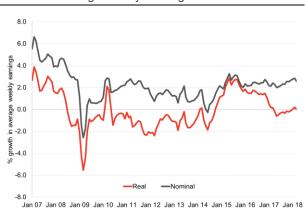
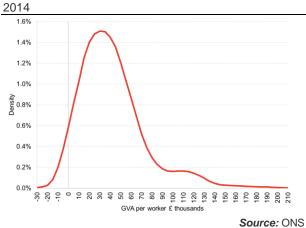


Chart 13: Average weekly earnings in the UK



Source: ONS, AWE

Chart 14: Distribution of labour productivity, Scotland 2014



Earnings and consumer confidence

With weak growth in labour productivity, firms will struggle to offer higher wages.

We have highlighted before that the latest reliable earnings data for Scotland shows that median real wages decreased in 2017 as a result of increases in inflation and limited nominal wage growth. (Chart 12)

More recent data released this week, for the UK as a whole, shows that real wage growth continues to be weak.

Nominal wage growth in the UK since 2015 has tended to sit around 2 to 2.5%.

Since the EU referendum, the resulting depreciation of Sterling against major international currencies and the consequent increase in inflation, the UK has struggled for real earnings growth. (Chart 13)

It is important to understand that underpinning each of these summary statistics is a range of experiences.

Median earnings growth, like average labour productivity growth, masks the fact that some people will be seeing their earnings grow in real terms, just as some firms will be seeing their labour productivity increase.

Chart 14 shows the firm level labour productivity distribution for Scotland in 2014. With the least productive firms, including those with a negative value-added per worker, at the left hand side and the most productive firms at the right hand side of the distribution.

From a policy perspective, this distribution of experiences is often overlooked, but if we're to see improvements in productivity we must focus on learning from those firms which are highly productive and improving their productivity (frontier firms) as well as focussing on helping those firms which have low labour productivity and aren't seeing improvements in their productivity (laggard firms) to improve.

Chart 15: Consumer savings ratio, Scotland

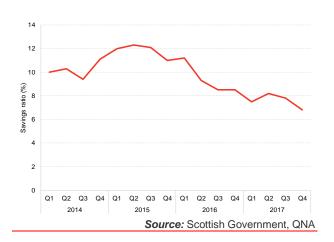


Chart 16: Consumer confidence, Scotland and UK

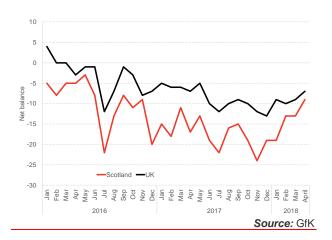
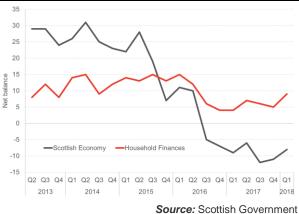


Chart 17: Scottish Consumer Sentiment Indicator: expectations for Scottish economy and household finances



As a result of weak earnings growth, driven by low productivity performance, and increasing inflation, household finances are feeling the squeeze.

One consequence of this is that households are not saving as much as they used to, with the households saving ratio in Scotland now dipping below 7% on the latest data. (Chart 15)

Reinforcing the assessment of household finances, the headline consumer confidence indicators produced for Scotland and the UK as a whole on a consistent basis show that on balance households remain pessimistic.

However, on the whole, households appear to becoming slightly less pessimistic. The gap in confidence between Scotland and the UK has narrowed. (Chart 16)

An additional measure of consumer confidence produced for the Scottish Government, but not available for the UK as a whole, asks consumers about their future expectations for the economy and their own personal household finances. (Chart 17)

On this measure households also appear to be becoming slightly more optimistic. Notably however, households are more optimistic about their own finances than they are about the overall prospects for the economy.

Over the period that these data have been available, it is clear that since 2016 we have been in a period of weaker household expectations about their own financial situation.

If the most recent improvement in this indicator at the start of 2018 is sustained, this may suggest a return to earlier levels of household optimism about their own situation.

Therefore, whilst there seems little sign of expectations returning to previously witnessed levels anytime soon, the latest data – coupled with the positive figures for retail sales in Q1 – offer some tentative evidence that the Scottish economy has started 2018 on a slightly stronger footing than the tail end of last year.



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