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News release

‘Compositional shifts in the labour market’ – a speech by Ben Broadbent, Deputy Governor for Monetary Policy

Speaking at a conference held at the Bank of England, Broadbent discusses recent changes in the make-up of employment and the impact of these “compositional effects” on the labour market.

Broadbent affirms that aggregate economic data – total employment, average wages and the like – remain critical for policy-makers’ decision-making. However, he argues that compositional shifts going on “underneath the surface” have been particularly significant of late. In particular, jobs lost in the 2008-09 downturn, and those regained during the recovery, have been skewed towards the lower-paid end of the spectrum. He states: “This has imparted a bias to average pay and productivity growth – upwards in the recession, downwards in the past couple of years – over that period.”

In and of itself, this isn’t unusual: it’s true in all countries that employment tends to be more cyclical for the young, the less experienced and those with fewer qualifications. One reason is that high-skilled jobs are more specialised, so firms retain their more experienced workers for longer in a downturn.

However, what is different about the UK’s recent experience is the scale of these effects. He said: “Compared with the cycle of the 1990s, [the compositional effects] appear to have been less positive during the recession – job losses weren’t as skewed towards the lower paid – but more negative during the recovery”.

Broadbent notes that this relatively pronounced compositional effect in the UK labour market may partly explain weak productivity growth since the financial crisis, reflecting a slower rate of improvement in the average “quality” of the employed workforce. He states: ““Human capital”, to use the economists’ terminology, has been growing at a slower rate, particularly compared with the first half of the 1990s.”

The skew towards the low paid can also help explain why average real wages have appeared to adapt relatively easily to slower productivity growth. Broadbent states: “In the past, it’s been hard for the labour market to absorb negative shocks to real take-home pay – whether from lower productivity, higher taxes or rises in import prices – without the unfortunate devices of higher inflation and/or higher unemployment”. To the extent that the weakness in productivity “has had nothing to do with existing jobs but instead reflects the skew in the creation of new jobs towards relatively less productive, less well-paid roles there would be no real-wage resistance, among existing employees, to overcome.”

He closes by noting that compositional effects of this sort have no direct bearing on inflationary pressure or, therefore, on monetary policy. But because they affect the aggregate variables we normally use to assess that pressure, it’s probably worth adjusting for them.

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