Kallum Pickering, Senior UK Economist | Kallum.pickering@berenberg.com | +44 20 3465 2627

UK LABOUR MARKET STRONG IN AUGUST BUT HARD BREXIT RISK LOOMS LARGE

Berenberg Macro Flash

Aug	Unemployment rate	Average earnings, ex bonus 3m/yoy
Actual	**4.9%**	**2.3%**
Previous	4.9%	2.1% (revised 2.2%)
Consensus	4.9%	2.1%
Berenberg	4.9%	2.1%

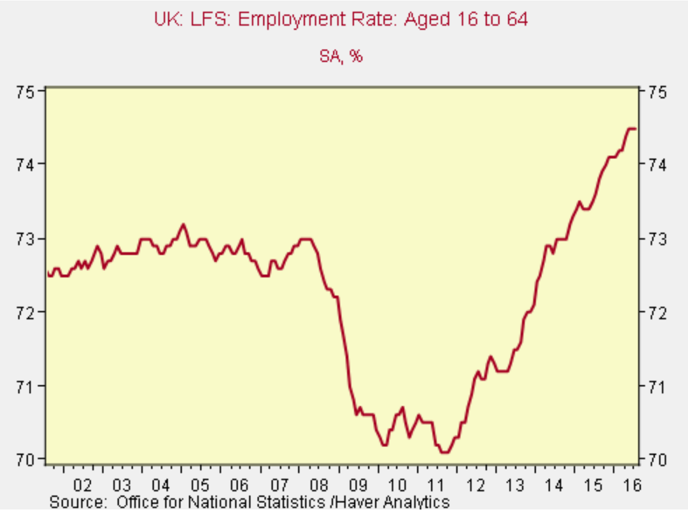
The UK labour market remained in good shape in August. The unemployment rate was unchanged mom at 4.9%. Average earnings ex. bonus rose faster than expected - by 2.3% yoy (expected 2.1%). The employment rate was 74.5% - the joint highest on record. Employment gains slowed to 106k on a 3m/3m basis - expected 76k - from 174k in July, but remained above the 10 year average of 66k.

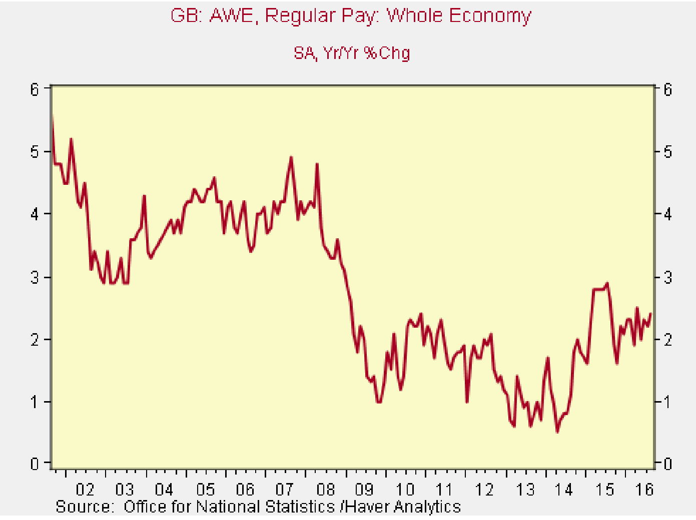
Early indicators for September showed continued stability. The claimant count, the number of people claiming jobseeker's allowance, was 776,400, or 2.3% - unchanged from the previous month. Jobless claims increased by just 0.7k after the August number was revised up to 7.1k from 2.4k. Despite the heighted uncertainty from Brexit, job vacancies - a proxy for labour demand - remained high at 749k. Job vacancies were 750k in August.

Hard Brexit risk is bad news for the labour market – heightened risks for employment and wage growth

Employment is a lagging indicator, it follows rather than leads fluctuations in aggregate demand. Nevertheless, it is reassuring to see that early indicators such as the number of vacancies have remained high some three months after the Brexit vote. Domestic demand has continued to expand at a healthy pace since the Brexit vote. Demand from the UK's main trading partners, the EU and the US, has continued to improve, bolstered by the large deprecation in sterling. Despite the initially strong negative confidence shock to the Brexit-vote, Theresa May's slow approach to Brexit has helped to steady the ship, leading to a rebound in confidence and business expectations. This explains why, despite the uncertainty over future UK-EU relations, the labour market has remained firm. But this could change in the coming months.

Theresa May's harder stance on Brexit since the Conservative Party annual conference two weeks ago could cause business confidence to decline again. Our base case is that, on the back of the continued expansion in demand both at home and abroad, most firms will need to maintain current headcounts in order to increase production to meet demand. We expect therefore, only a small rise in unemployment, to 5.3% next year. But the hard-Brexit risk could change this. UK based firms, particularly those with strong European exposure, or financial firms heavily reliant on the EU financial passport to do cross border business, may begin to trim their UK operations already. A bigger-than-expected rise in unemployment would in turn likely lead to a slowdown in nominal wage growth from its current rate of c2.3% yoy. We expect inflation to rise to 2.6% by Q2 next year. Real wage growth has already slowed in recent months. A sharp or protracted decline in real wages would create significant downside risks for household spending and GDP growth - consumption makes up 2/3 of GDP.


UK: LFS: Employment Rate: Aged 16 to 64
SA, %
75
74
73
72
71
70
02 03 04 05 06 07 08 09 10 11 12 13 14 15 16
Source: Office for National Statistics /Haver Analytics


GB: AWE, Regular Pay: Whole Economy
SA, Yr/Yr %Chg
6
5
4
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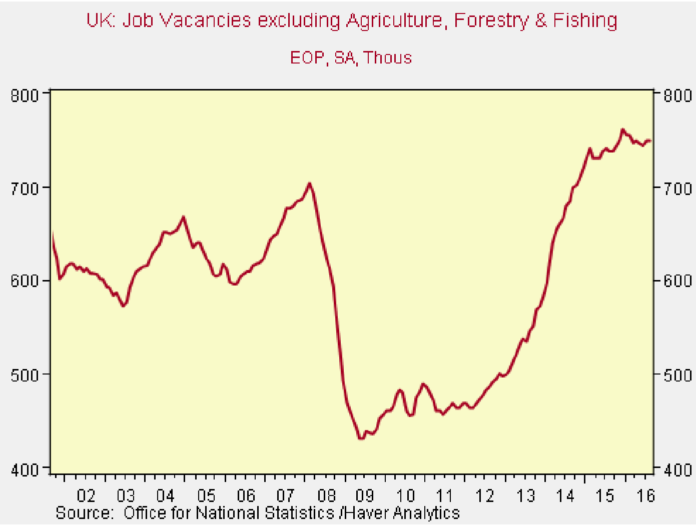
02 03 04 05 06 07 08 09 10 11 12 13 14 15 16
Source: Office for National Statistics /Haver Analytics


UK: Job Vacancies excluding Agriculture, Forestry & Fishing
EOP, SA, Thous
800
700
600
500
400
02 03 04 05 06 07 08 09 10 11 12 13 14 15 16
Source: Office for National Statistics /Haver Analytics

%		AUG	JUL	JUN	MAY	APR	MAR
Unemployment rate 3m	*Level*	4.9	4.9	4.9	4.9	5.0	5.1
Average earnings, ex bonus 3m/yoy	*Change*	2.3	2.2	2.3	2.2	2.3	2.2