HM Treasury

Economic Evidence to Pay Review Bodies: 2024-25 Pay Round

February 2024

HM Treasury

Economic Evidence to Pay Review Bodies: 2024-25 Pay Round

This publication is available at: www.gov.uk/official-documents.

Any enquiries regarding this publication should be sent to us at public.enquiries@hmtreasury.gov.uk

ISBN: 978-1-915596-46-8 PU: 3265

Contents

Chapter 1

Background & Executive Summary

1.1 At Spending Review 2021 (SR21), the Chancellor announced that all public sector workers will see pay rises from 2022-23 to 2024-25. The government accepted the pay recommendations of the independent Pay Review Bodies (PRBs) for the NHS, teachers, police and the armed forces for 2022-23 and subsequently accepted the headline recommendations of the PRBs in full for 2023-24. This has resulted in PRB workforces having received one of the highest pay increases over any two-year period since the PRBs were set up. This reflects the extraordinary macroeconomic context, the vital contributions that public sector workers make to our country and the importance that the government attaches to the recommendations of the independent PRBs.

1.2 The government has remitted PRBs for the 2024-25 Pay Round. PRBs will provide evidence-based advice to the government on levels of pay, taking account of a range of factors including the need to recruit, retain and motivate suitably able and qualified people, the government's inflation target, and the financial circumstances of the government.

1.3 This document sets out the economic, labour market and fiscal context within which we ask the independent PRBs to consider their recommendations for 2024-25 pay awards. In summary, the economy has faced an unprecedented series of shocks in recent years, notably the Covid-19 pandemic and Russia's illegal invasion of Ukraine, which drove up inflation through higher energy prices and led to a subsequent increase in domestically generated inflation. The Bank of England have taken necessary action to bring inflation back to target, which is working, but has inevitably led to slower growth over the past 18 months. In light of these shocks, the economy has performed better than first expected and whilst inflation is now on a downward trend, it remains elevated and returning inflation to target therefore remains a top priority for government. Wage growth has started to ease back from the historically high levels reached last year, and it is expected to fall to below 4% this year and fall further to around 2% next year as the labour market loosens. Vacancies across the economy remain on a downward trend and, whilst pinch-points exist, we have seen notable improvements in the recruitment and retention status of key public sector workforces over the last year.

1.4 Departments are facing their tightest year of this Spending Review period. Departments have faced two years of above-affordability pay awards, alongside an array of other pressures, including from inflation, as the economy has moved on from forecasts available at the time budgets were set in 2021. For example, expenditure on pay for PRB workforces is set to be ~£10bn more than planned in 2024-25, even before 2024-25 awards are considered. It is therefore vital that the PRBs consider the historic nature of the pay awards delivered over 2022-23 and 2023-24 and the Government's affordability position when forming their recommendations.

Chapter 2
Economic Context

Overview

2.1 Over recent years the UK economy has faced a series of unprecedented shocks which have caused price inflation to increase and weighed on growth. Reflecting these shocks and increases in interest rates, necessary to bring down inflation, growth has been subdued over the last 18 months in advanced economies including the UK. The economy ended 2023 in a technical recession, having contracted over the final two quarters of the year. Despite this, the economy fared better in 2023 than many forecasts had predicted, and revisions to gross domestic product (GDP) show that the economy also recovered more strongly from the pandemic than previously thought.

2.2 Consumer Prices Index (CPI) inflation has fallen materially from its peak in late 2022. The Bank of England's February forecast is that inflation will return to the 2% target temporarily in the second quarter of 2024, before rising again and returning to target by the end of the forecast period. Returning inflation to the 2% target is critical for sustainable growth.

Inflation

2.3 CPI inflation is on a downward trend, having ended 2023 at 4.0% in December, down from its peak in Autumn 2022 of over 11%. Lower wholesale energy prices throughout 2023 have been the main driver of lower inflation, which allowed Ofgem to reduce their price cap for household energy bills. However, inflation has been more persistent than initially expected and remains above target, with services inflation particularly high. The most recent inflation data for January 2024 was also 4.0%, slightly below market and Bank of England expectations for a small rise to 4.1%.

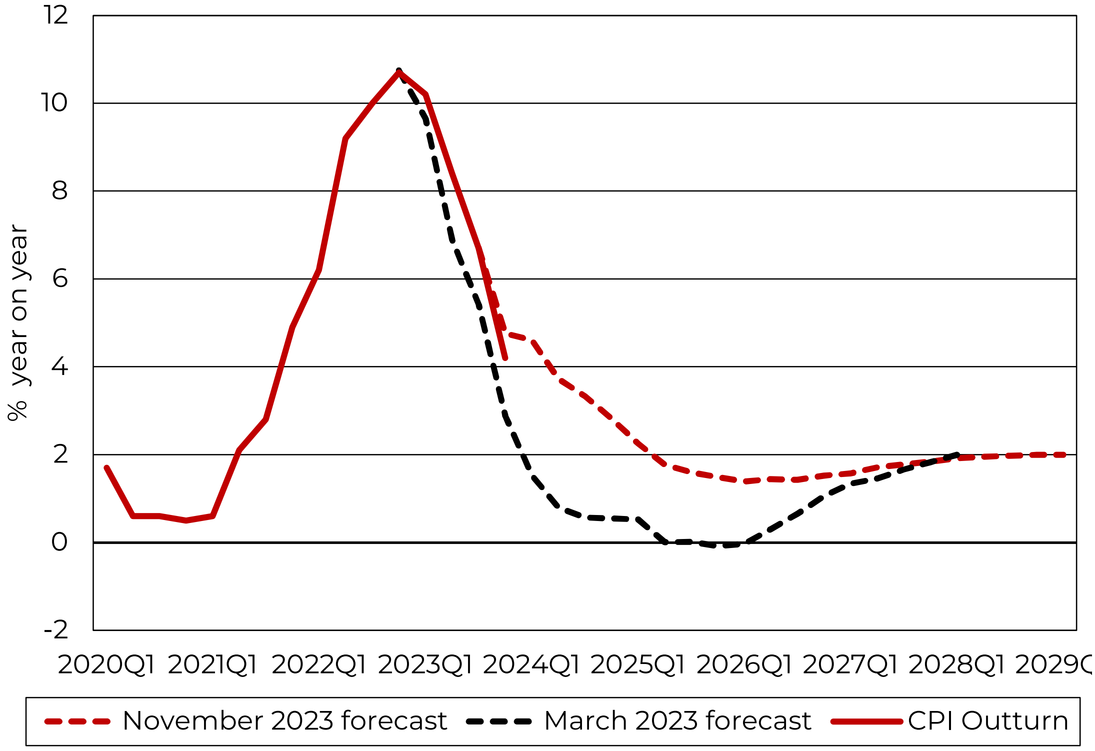
2.4 Household inflation expectations remain elevated but have fallen back from their 2022 peak. Short-term household inflation expectations were 3.9% in January 2024, as measured in YouGov-Citi's survey, but remain above the 2010-2019 average of 2.5%. Longer-term household expectations, for 5-10 years' time, were 3.6% in January, though also remain slightly above the 2010-2019 average of 3.2%.

2.5 In its most recent November 2023 forecast, the OBR expects CPI inflation to continue to fall gradually and average 3.0% in 2024-

25, before returning to the target rate of 2.0% by the first half of 2025. This is more than a year later than forecast in March 2023, with inflation having proven to be more persistent than expected, as illustrated in Figure 2.A. However, since November 2023, inflation has fallen more quickly than the OBR forecast. The Monetary Policy Committee (MPC) at the Bank of England forecast in its most recent February Monetary Policy Report (MPR)[1] that inflation will return to the 2% target in the second quarter of 2024, before rising again at the end of 2024, and returning to target towards the end of the forecast period.

2.6 The MPC has said that further inflation persistence would require interest rates to be maintained at their current level for longer. This would result in additional costs for many mortgage-holders, businesses and government. The government continues to support the independent MPC of the Bank of England to help bring inflation down to the 2.0% target.

Figure 2.A Consumer Prices Index (CPI) Inflation



Source: ONS, OBR's Economic & Fiscal Outlook (March 2023, November 2023)

[1] Bank of England Monetary Policy Report February 2024

Output

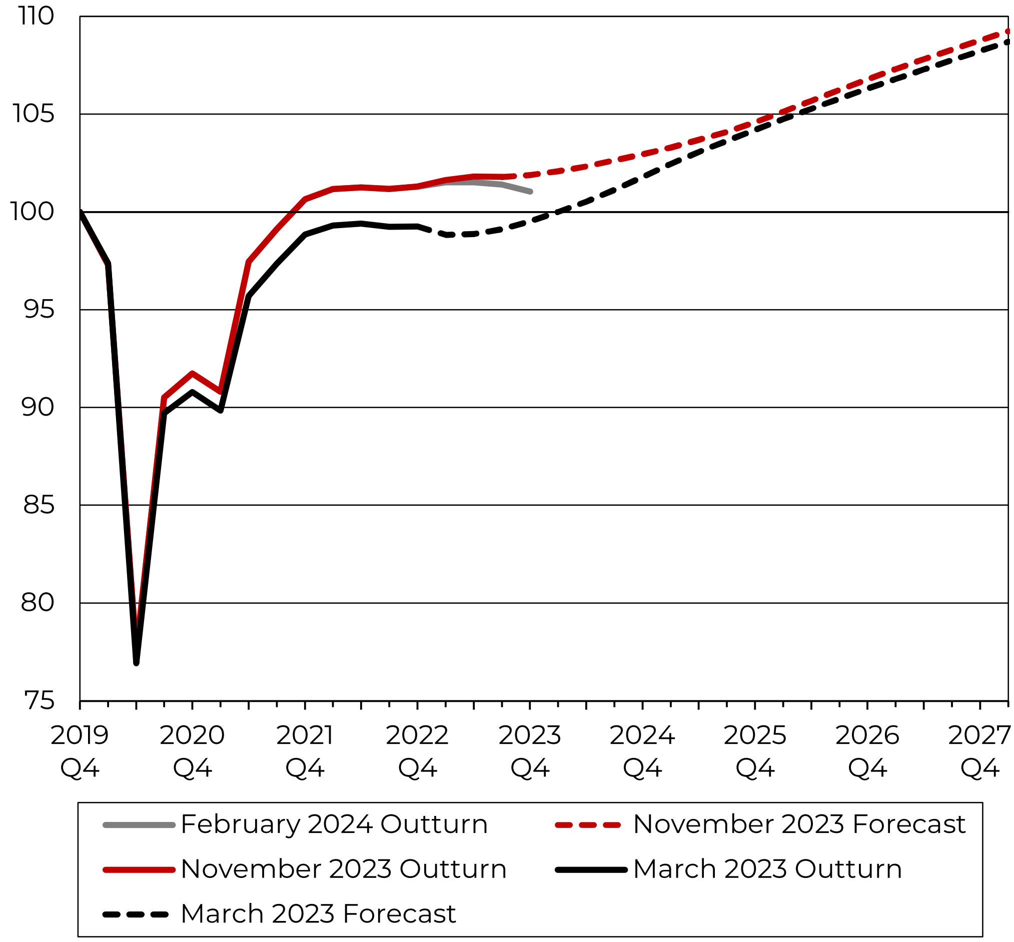
2.7 In response to the unprecedented series of shocks the economy has faced in recent years, which drove up inflation through higher energy prices and weighed on growth, the Bank of England have taken necessary action to bring inflation back to target. This has weighed on demand and output contracted over the second half of 2023 with declines of 0.1% in Q3 and 0.3% in Q4 respectively.

2.8 Despite this, GDP growth fared better in 2023 than had first been expected. Output grew by 0.1% during 2023, in contrast to the OBR's March 2023 and November 2022 forecasts for a contraction of -0.2% and –1.4% respectively, and the Bank of England's prediction in November 2022 for the longest recession seen in 100 years. Revisions to the National Accounts in October 2023 also mean that the *level* of GDP is higher than previously estimated. The revised data showed that public sector output – in particular in the health sector – was much stronger than previously estimated, and outstripped growth in the private sector. Public sector productivity, however, remains a challenge, lying below pre-pandemic levels.

2.9 The OBR and the Bank of England forecast that modest growth is likely to return in 2024, before strengthening throughout the remainder of the forecast period. Indeed, timely indicators are showing early positive signs for the first quarter of 2024. For example S&P Purchasing Managers Index (PMIs) have survey balances above the neutral 50 mark for the third consecutive month, suggesting that output in January is rising, driven by the construction and services sectors. The OBR's November 2023 forecast is for the economy to grow by 0.7% in 2024, 1.4% in 2025 and achieve an average annual growth rate of 1.9% between 2026 and 2028. The Bank of England forecast in its most recent February Monetary Policy Report for growth to increase by 0.2% in 2024 before picking up gradually throughout the rest of the forecast period as inflation falls and as the effect of past interest rate hikes fades.

2.10 The government remains focused on sustainable economic growth over the long term and the OBR has confirmed that the combined impact of the policies announced in Spring Budget 2023 and Autumn Statement 2023 provides a permanent 0.5% increase in the level of potential output by the end of its 5-year forecast horizon.

Figure 2.B Real GDP (2019, Q4 = 100)



Source: ONS, OBR's Economic & Fiscal Outlook (March 2023, November 2023)

Uncertainties

2.11 In its November 2023 Economic and Fiscal Outlook[2] the OBR said that uncertainty around the economic outlook remains "*significant*", with risks including a further escalation of existing geopolitical tensions and the possibility of elevated inflation expectations becoming embedded, primarily reflecting persistence in domestic wage and price-setting. In its February 2024 MPR, the MPC assessed that risks around the inflation outlook are evenly balanced, and remain skewed to the upside in the short term, also reflecting geopolitical risks which have intensified following events in the Middle East. While the conflict involving Israel and Gaza and disruption to shipping in the Red Sea have had a limited impact on the UK economy so far, a

[2] Economic and fiscal outlook – November 2023 – Office for Budget Responsibility (obr.uk)

widening of this conflict involving the broader region poses a significant risk of disruption to global energy markets and major trade routes, which would have material financial market and economic impacts.

2.12 The OBR has emphasised that its forecast is contingent on the path of fiscal policy, which affects growth, inflation and monetary policy as changes in spending and taxation add or withdraw demand to and from the economy. Fiscal policy is discussed in more detail in chapter 4.

Chapter 3
Labour Market Context

Overview

3.1 The public sector remuneration package is competitive when taking account of pay, pensions, and wider benefits including job security. Whilst pinch-points remain, we have seen notable improvements in the recruitment and retention status of key public sector workforces over the last year. This chapter will summarise the latest labour market data and recruitment and retention trends across PRB workforces, alongside what is forecast for the coming period.

Labour market context

Earnings

3.2 There are several data sources for measuring earnings, each with different strengths and limitations.

a) ONS Annual Survey of Hours and Earnings (ASHE) data

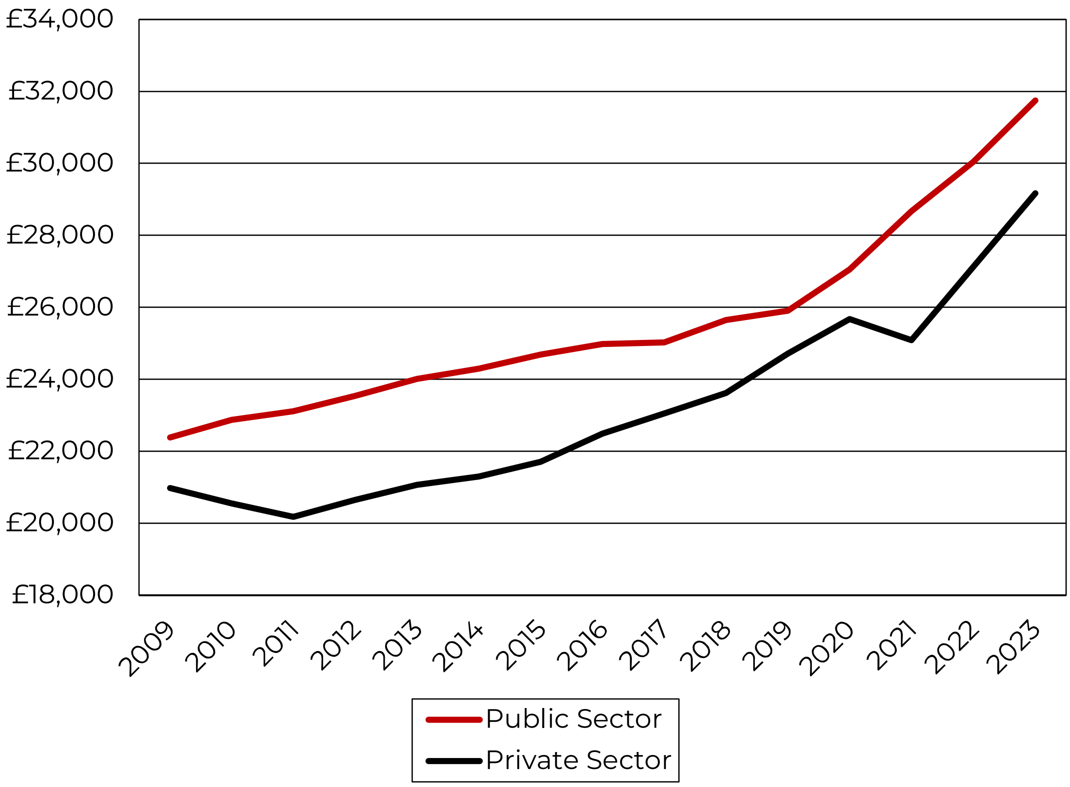
- ASHE is recommended by the ONS as the principal source of data for comparing public and private sector pay due to its large sample size and coverage of the entire United Kingdom.[3]
- According to ASHE data,[4] median pay, shown in Figure 3.A, was 9% greater in the public sector than the private sector in 2023, broadly in line with the gap that has existed between the two sectors over the past decade. ASHE data is measured in April of each year and therefore won't reflect 2023-24 awards to PRB workforces, which didn't reach pay packets until later in the year. However, it will

[3] Income and earnings statistics guide - Office for National Statistics (ons.gov.uk)

[4] https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/datasets/publicandprivatesectorashetable13

capture an effect from 2023-24 pay awards in the private sector, which are concentrated in January and April.[5]

Figure 3.A Median annual pay (all employees)



Source: ASHE[6]

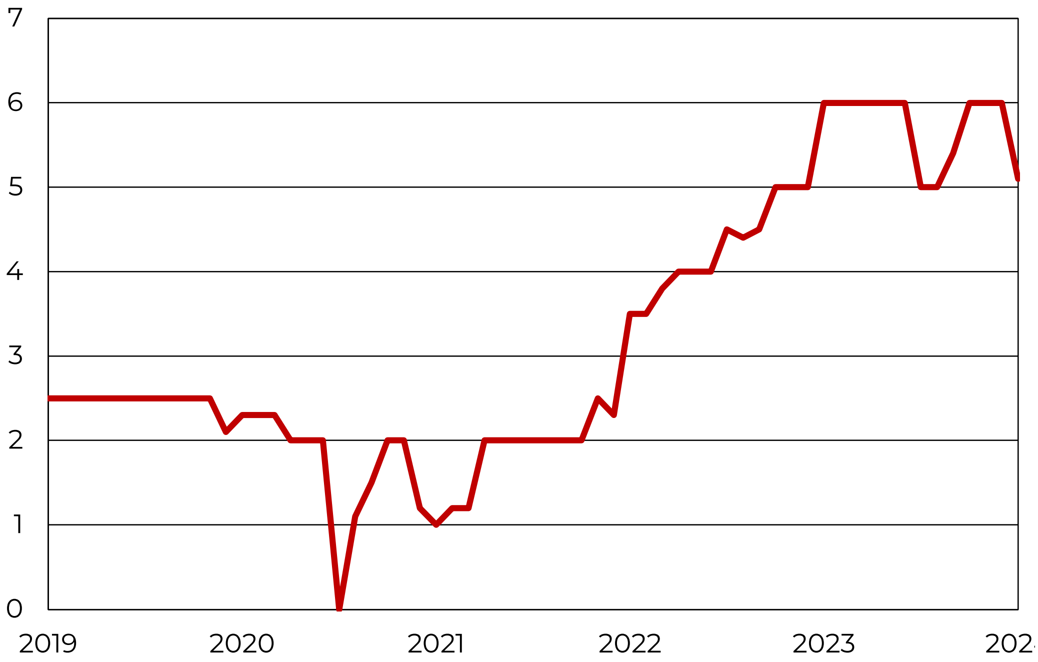
b) Settlement data

- Settlement data are the most comparable data to PRB decisions, as they are a direct measure of consolidated pay awards, and so are not affected by broader factors such as changes to working hours, unlike many other measures of earnings growth.
- 2023-24 awards across PRB workforces were broadly in line with those that have been made in the private sector this financial year. In cost terms, consolidated awards across PRB workforces averaged 6.0%, whilst according to XpertHR, median settlements across the economy have been between 5.0% and 6.0% so far in 2023-24.

[5] XpertHR data shows that by the end of April 2023, the majority (87.3%) of all 2023 pay deals had been delivered

[6] Annual Survey of Hours and Earnings (ASHE), UK: April 2023, Office for National Stastics, November 2023

Figure 3.B Median private sector pay settlements, three month rolling average (%)



Source: XpertHR

c) Average earnings growth

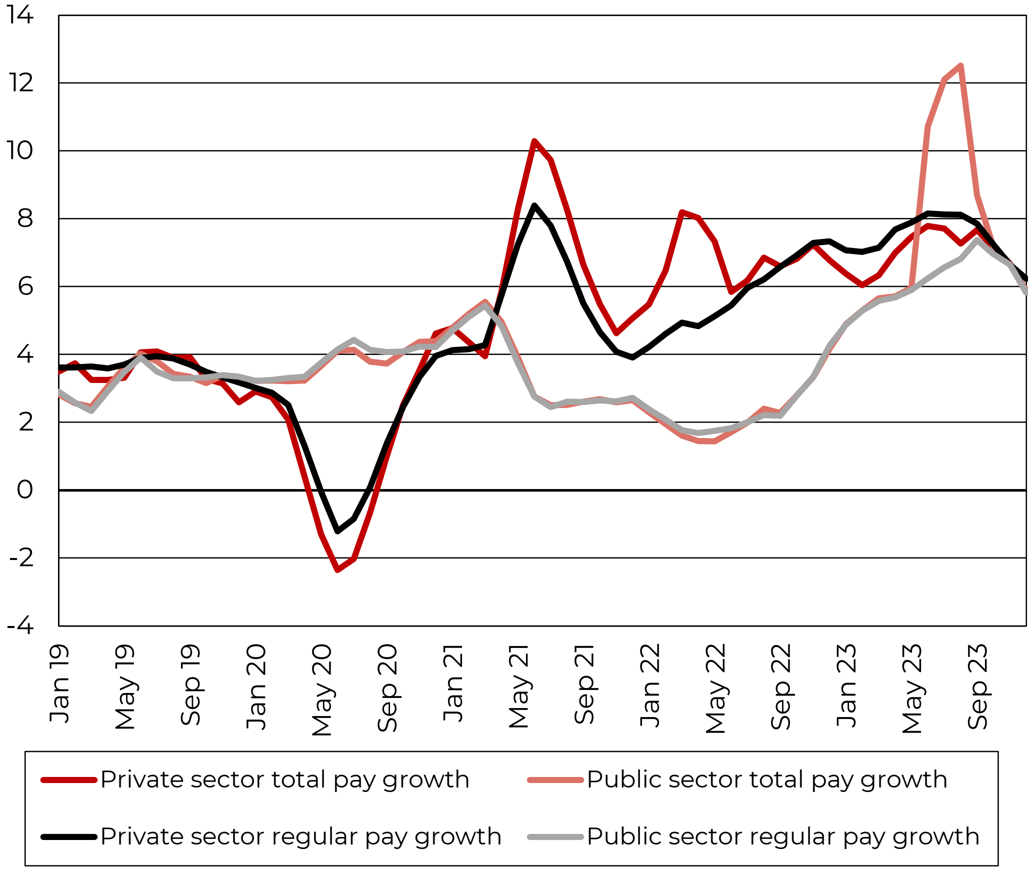
- Measures of growth in average earnings are generally higher than average pay settlements. This reflects the fact that average earnings growth is also affected by movements of people between jobs, generating a compositional effect which typically lifts average earnings growth above average pay settlements as people move to higher paying occupations. Average earnings data is also affected by broader pay drift from factors such as changes in working hours and overtime. These factors affect both measures of public and private sector average earnings. As a result of this, median pay settlements were typically 0.5-1.5 percentage points lower than headline average earnings growth prior to the pandemic.[7]
- ONS Average Weekly Earnings (AWE) data distinguishes between total pay growth, including bonuses and non-consolidated payments, and regular pay growth, excluding these payments.

[7] Page 13 UK-Economic-Outlook-Autumn-2021.pdf (niesr.ac.uk)

- According to AWE data[8], pay growth has eased in recent months. Whole economy total pay growth was 5.8% in the three months to December 2023, having peaked at 8.5% in the three months to July 2023. Public sector total pay growth peaked at 12.5% in the three months to August 2023, exceeding private sector total pay growth by 5.2ppts. This was due to one-off payments to parts of the public sector (notably the non-consolidated awards to the NHS Agenda for Change workforce which varied by grade and experience but averaged 6% of an individual's 2022-23 pay, and the £1,500 non-consolidated payments made in the Civil Service). Public sector total pay growth for the three months to December was 5.9%, broadly in line with private sector total pay growth of 5.8%.
- Whole economy regular pay growth, which excludes bonuses and non-consolidated payments, also eased to 6.2% in the three months to December. Public sector regular pay growth was 5.8% at this point, 0.4ppts below private sector regular pay growth. Public sector regular pay growth does not yet fully capture the effect of all public sector pay awards for 2023-24, which were mostly paid between June and November and therefore the full upwards pressure from these pay awards is not yet captured in latest headline estimates of earnings growth.
- Estimates of public sector pay do not capture the value of payments in arrears, as payments in arrears are not included in headline average weekly earnings data. Payments in arrears represented 1.5% of total public sector pay in 2022, and many public sector workforces will receive similar arrears payments in 2023, reflecting that many awards did not reach pay packets until after the start of the pay year.

[8] Average weekly earnings in Great Britain, December 2023, Office for National Statistics, February 2024

Figure 3.C Average weekly earnings total and regular pay growth (three month on year, %)



Source: ONS[9]

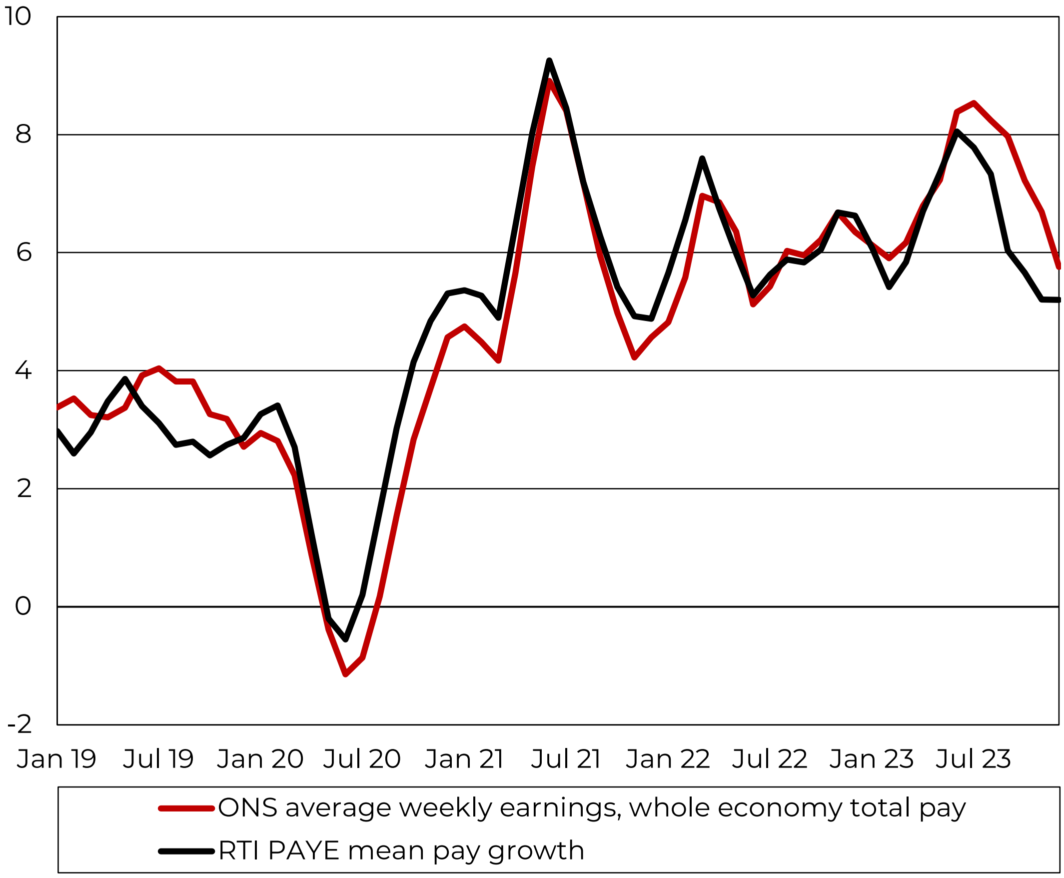
d) Other measures of wage growth

- Wider and more timely measures of earnings growth show a larger easing in earnings growth than implied by ONS AWE data. For example, the HMRC Real Time Information (RTI) measure of whole economy mean pay growth has fallen from its peak of 9.2% in June to 5.3% in December whilst the equivalent measure for median pay growth has fallen from 9.6% in June 2023 to 6.4% in January 2024. The REC/KPMG Report on Jobs for January indicates that salary growth for new hires has also fallen below its average level from 2017-19.[10]

[9] Average weekly earnings in Great Britain, December 2023, Office for National Statistics, February 2024

[10] KPMG and REC, UK Report on Jobs - February 2024 - KPMG UK

Figure 3.D : Pay growth measures (three month on year)



Source: ONS[11], HMRC[12]

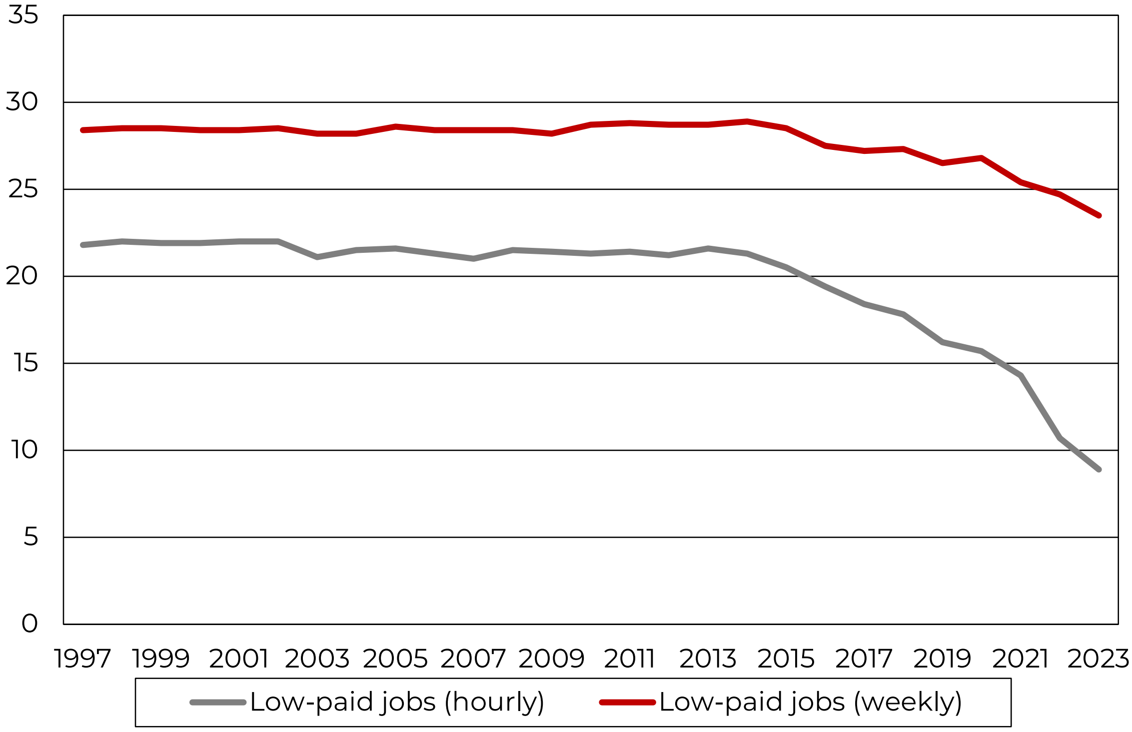
- Earnings growth has been highest at the lower end of the earnings distribution since 2010, a trend which has continued over the last year. The proportion of employees in low paid employee jobs on an hourly basis (defined as earning below two thirds of median hourly pay) has declined from 21.3% in 2010 to 8.9% in 2023.[13] The National Living Wage has increased in real terms by over 20% over this period, with the adult National Living Wage increasing by 9.8% in nominal terms in April 2024.

[11] Average weekly earnings in Great Britain, December 2023, Office for National Statistics, February 2024

[12] Earnings and employment from Pay As You Earn Real Time Information, January 2024, Office for National Statistics, February 2024

[13] Employee earnings in the UK - Office for National Statistics (ons.gov.uk)

Figure 3.E Proportion of low paid employee jobs for hourly pay and gross weekly pay, whole economy UK, 1997 to 2023

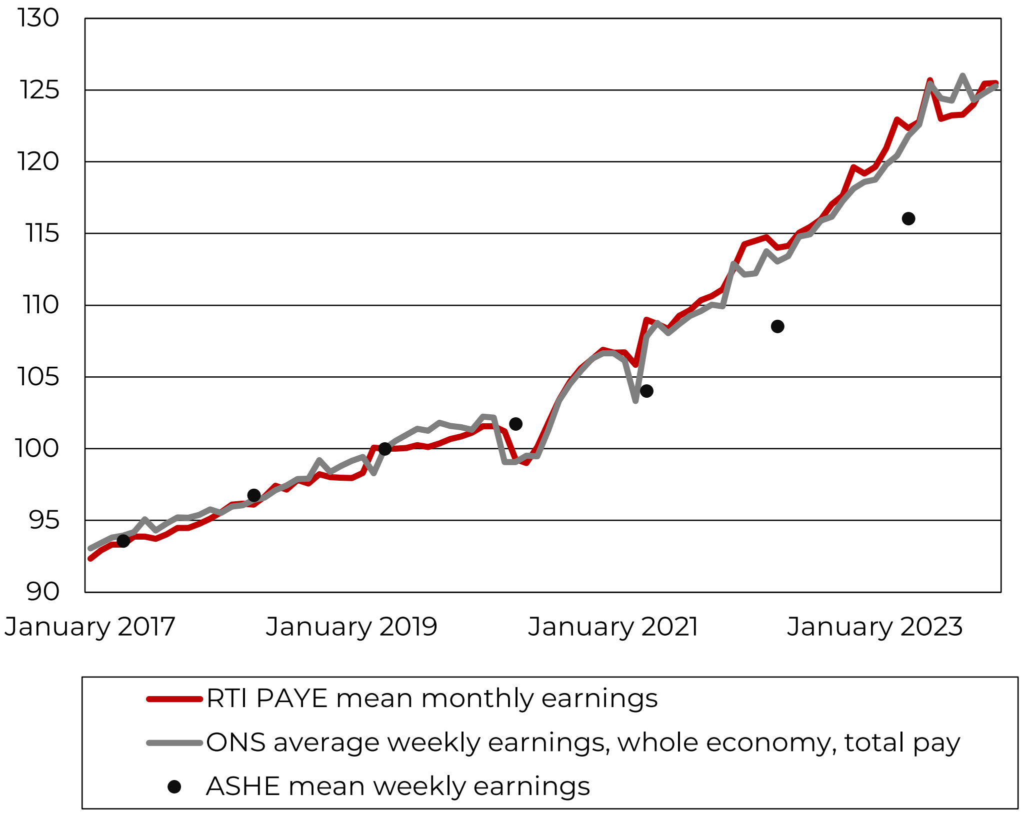


Source: ASHE[14]

3.3 The recent level of earnings growth is subject to elevated uncertainty. Data from the ASHE suggests that mean weekly earnings increased by 17% between April 2019 and April 2023, whereas both the measure of mean pay in HMRC RTI data and the total pay measure in average weekly earnings increased by 22% across this period.

[14] Annual Survey of Hours and Earnings (ASHE), UK: April 2023, Office for National Stastics, November 2023

Figure 3.F Average earnings level (indexed to April 2019)



Source: ONS[15], ASHE[16], HMRC[17]

Pensions

3.4 Pensions are an important part of the overall remuneration package and remain substantially more generous in the public sector than in the private sector. Over 80% of public sector workers are part of Defined Benefit schemes where employers contribute over 20% or more of earnings to the pension. This compares to most private sector employees who receive Defined Contribution pensions where employer contributions are significantly lower and where the vast majority (85%) of employees receive less than 10% employer contribution.[18] Indeed, in 2018 to 2020, for employees with a workplace pension, the

---

15 Average weekly earnings in Great Britain, December 2023, Office for National Statistics, February 2024

16 Annual Survey of Hours and Earnings (ASHE), UK: April 2023, Office for National Stastics, November 2023

17 Earnings and employment from Pay As You Earn Real Time Information, January 2024, Office for National Statistics, February 2024

18 Office for National Statistics, Employer contribution bands by industry and pension type: Table P10.

median value of accrued defined benefit and defined contribution pension pots was £65,400 in the public sector compared with £10,300 in the private sector.[19]

3.5 Some examples of the pensions received by PRB workforces are as follows:

- **NHS staff** currently receive an employer contribution in respect of future service of 17%[20] of salary (20.6% when including past deficit contributions). A nurse with typical earnings and a 40-year career will retire with a pension worth £37,900 per annum[21] whilst a consultant will retire with a pension worth £107,600 per annum.
- **Teachers** receive an employer contribution in respect of future service equivalent to 16.4% of salary (23.6% when including past deficit contributions). A teacher with typical earnings and a 40-year career will retire with a pension worth £43,800 per annum.
- **Prison Officers** are in the Civil Service Pension Scheme and receive an employer contribution in respect of future service equivalent to 23.9% of salary (27% when including past deficit contributions). A typical prison officer will retire after 40 years with a pension worth around £23,900 per annum.
- Members of **the armed forces** receive an employer contribution in respect of future service equivalent to 42.6% of salary (63.5% when including past deficit contributions). A typical member of the armed forces will retire after 30 years with a pension worth around £33,600 per annum.

3.6 Employer contributions for public service pension schemes are generally expected to increase further from April 2024 following the 2020 valuations. The increase will be met by the Exchequer for centrally funded employers. For example, employer contributions will increase from 20.6% to 23.7% for the NHS Pension Scheme for England and Wales and from 23.6% to 28.6% for the Teachers' Pension Scheme for England and Wales.

3.7 Remuneration for an NHS consultant with a salary of £105,000 per annum currently includes £21,630 in employer pension contributions (including contributions in respect of past scheme deficits), rising to £24,885 from April 2024. Remuneration for a member of the armed forces with a salary of £40,000 per annum currently includes £25,400 in employer pension contributions

[19] Employee workplace pensions in the UK - Office for National Statistics

[20] Employer contributions will change from April 2024 to reflect the results of the 2020 valuations.

[21] In today's money (as are all such examples in this paragraph). All estimates are as at July 2023.

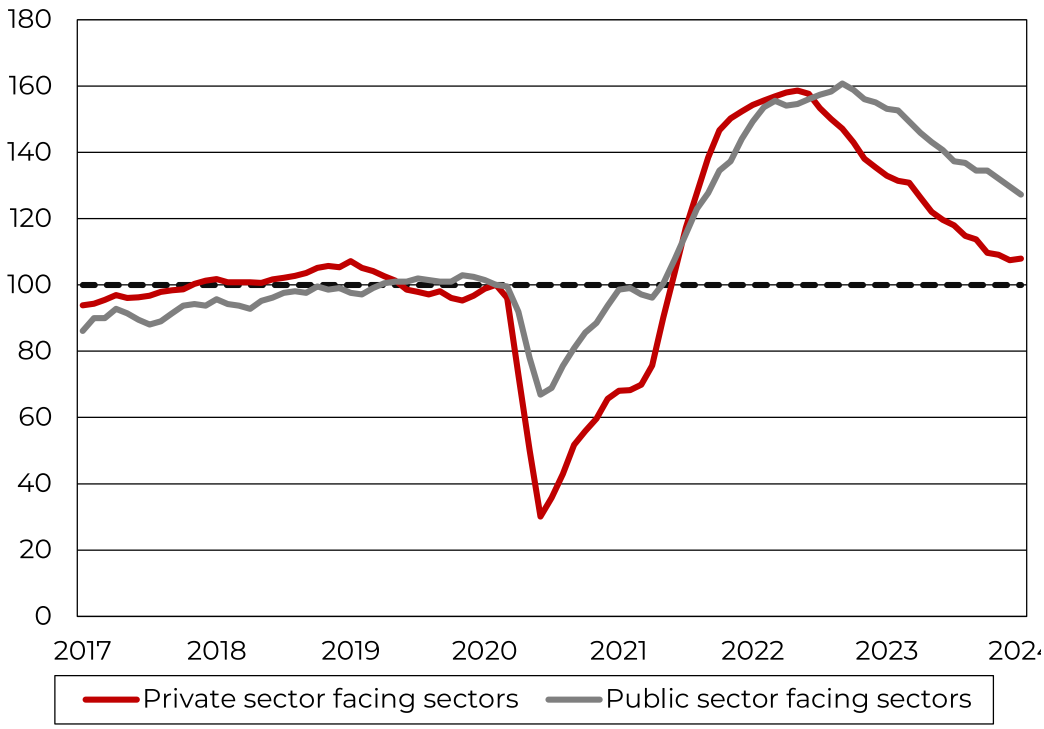
(including contributions in respect of past scheme deficits), rising to £28,600 from April 2024.

3.8 It should also be noted that the inflation protection offered as part of public sector pension schemes is particularly valuable in times of high inflation. Furthermore, public service pension schemes such as the NHS Pension Scheme contain provisions for annual revaluation of accrued pensions for active members by more than CPI.

Vacancies

3.9 Indicators suggest that recruitment difficulties have continued to ease. The number of vacancies has declined for 19 consecutive months. Based on data for the three months to January, the level of vacancies has fallen by 17% over the past year in public sector facing sectors[22] and by 19% in private sector facing sectors.

Figure 3.G Vacancies, indexed (three months to February 2020 = 100)



Source: ONS

[22] Public sector facing sectors are defined here as public administration and defence, education, and human health and social work activities. All other sectors are defined here as private sector facing sectors.

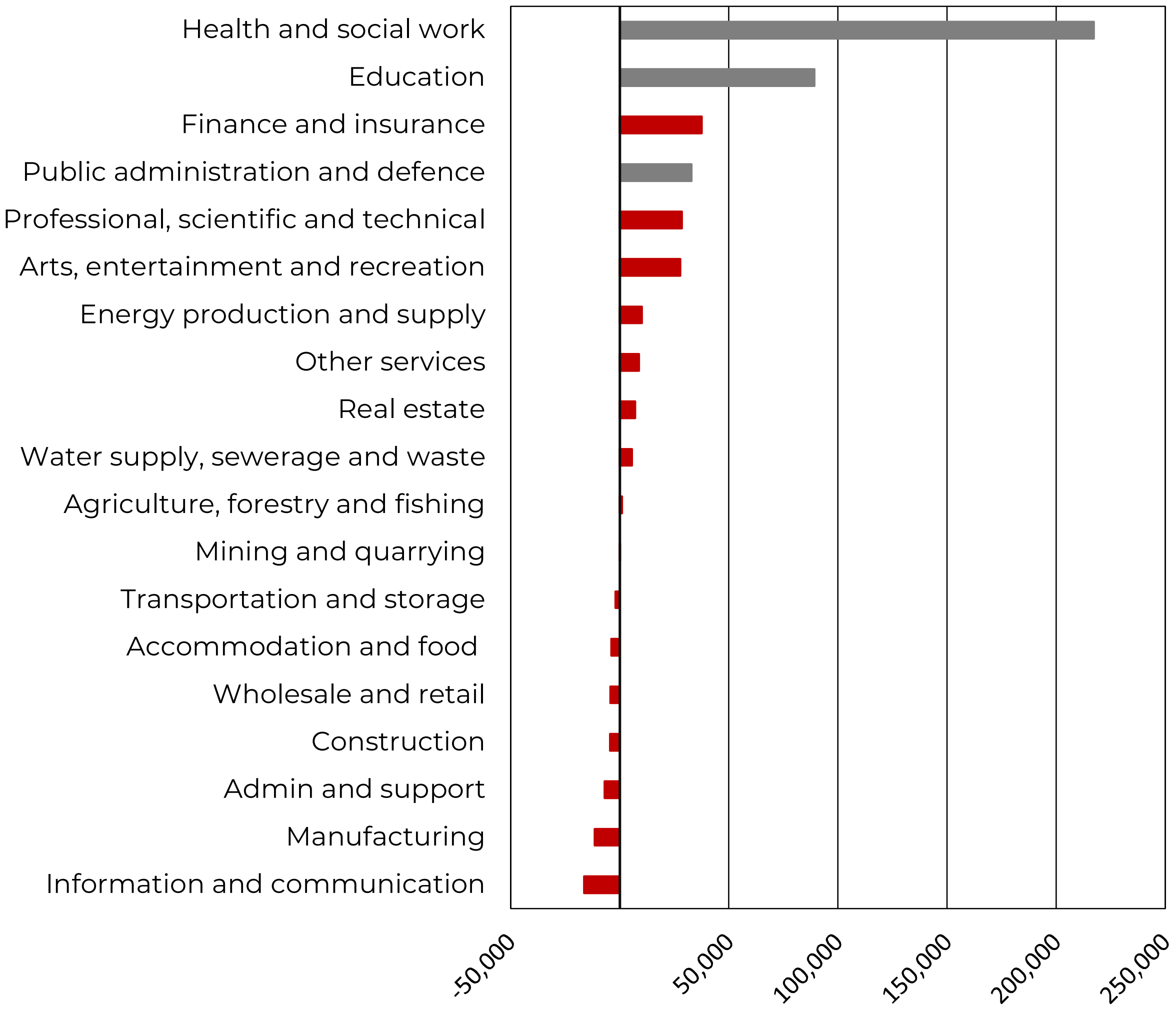
Employment[23]

3.10 HMRC data indicates that employee numbers increased sharply across 2021, 2022 and 2023 and reached a record high of 30.4m in January 2024. Employee numbers in private sector facing sectors have increased 74,000 on the year, whilst employee numbers in public sector facing sectors have increased by 339,000 over this period. In the ONS' measure of public and private sector employment, the proportion of total employment in the public sector is now the highest it has been since 2014, at 17.8% in June 2023.

3.11 The unemployment rate for the three months to December was 3.8%, which was unchanged on a year ago and a slight increase from 3.6% in the three months to August 2022, which was the lowest rate in almost fifty years.

[23] The Labour Force Survey currently is facing challenges due to falling response rates. In light of these challenges, we have focused on recent trends in payrolled employee numbers here to provide a steer on recent employment trends.

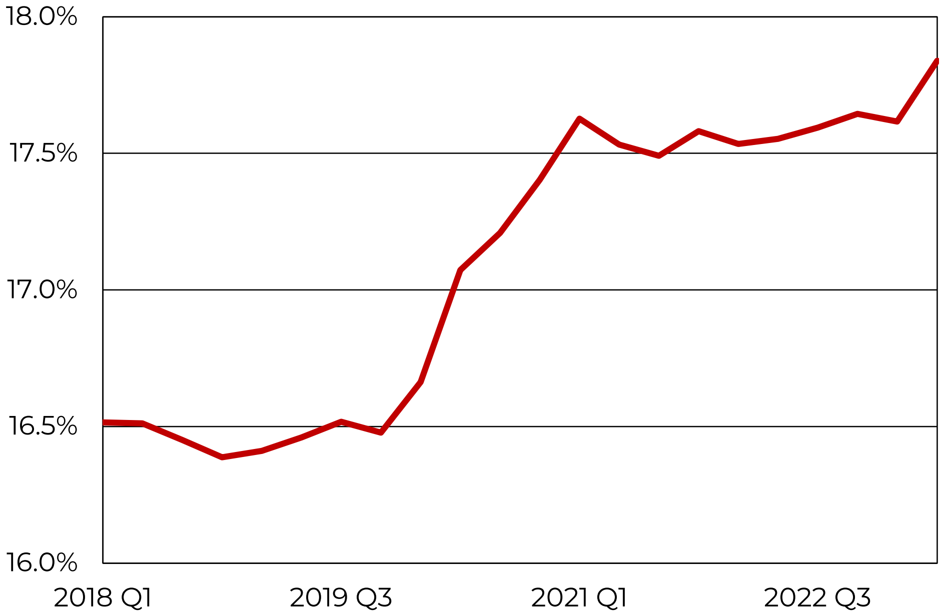
Figure 3.H Payrolled employees by sector, change on the year to January 2024 (grey bars highlight public facing sectors)



Source: HMRC[24]

[24] Earnings and employment from Pay As You Earn Real Time Information, January 2024, Office for National Statistics, February 2024

Figure 3.I Public sector employment as % of total employment



Source: ONS[25]

Recruitment & Retention across PRB workforces

3.12 Recruitment and retention across the public sector is now improving, after an initial worsening following the pandemic. As shown by charts 3.H and 3.I, public sector employment has continued to expand both in absolute terms and relative to the private sector. Falls in vacancies across the public sector have been achieved despite increased demand for public sector employees through a combination of improvements in retention, with reductions in public sector staff leaving their positions, along with successful recruitment, with marked increases in entrants across the board.

- In the **NHS** in England[26] full time equivalent staff numbers were up by 5.7% in October 2023 (the latest data covering the entire workforce) compared with the same month a year prior, and 22% and 35% compared with 5 and 10 years ago respectively. The government also met its manifesto commitment to recruit an additional 50,000 nurses six months early, with over 56,000 additional nurses in October

---

[25] Summary of labour market statistics, June 2023, Office for National Statistics, February 2024

[26] NHS Workforce Statistics, July 2023 - GOV.UK (www.gov.uk)

2023 compared to 2019[27]. Finally, October's data also shows that there are over 6,800 (5.2%) more doctors in the NHS compared to October 2022.

- The total number of entrants to the English **teaching workforce** in state-funded schools increased by 9% between 2021-22 and 2022-23 and the workforce is now the largest it has been since the school workforce census began in 2010-11, though growing pupil numbers mean pupil teacher ratios have increased slightly. [28]

- The number of **police officers** in England and Wales increased by 3.5%[29] in the latest data for the year to 30 September 2023, with the number of police officers peaking in the year to 31 March 2023 at the highest level since comparable records began[30]. The Government fulfilled its commitment to recruit 20,000 additional police officers by March 2023 and this is being maintained, with over 3,000 more officers protecting communities in the latest data compared with 2010.

- The size of the total **HM Prison and Probation Service (HMPPS) workforce** increased by 7.8%[31] in the year to 31 December 2023 – a result of the total HMPPS joiners in the year to 31 December 2023 increasing by 26.7% compared with the 12 months to 31 December 2022 and a fall in the total number of leavers across HMPPS by 8.5% across the same period.

3.13 The positive developments in recruitment and retention have been supported through the delivery of both pay and non-pay measures.

- **Headline pay:** The 2023-24 PRB process delivered historically high pay awards, many of which were targeted at the lower end of the earnings distribution where wage growth has been stronger across the wider economy. This includes a 10.3% pay increase for the lowest paid prison staff in

---

[27] Over 50,000 extra nurses in NHS - hitting government target early - GOV.UK (www.gov.uk)

[28] School workforce in England, Reporting year 2022 – Explore education statistics – GOV.UK (explore-education-statistics.service.gov.uk) (FTE basis)

[29] Full-time equivalent (FTE) basis, Police workforce, England and Wales: 30 September 2023 - GOV.UK (www.gov.uk)

[30] (in the year ending March 2003) https://www.gov.uk/government/statistics/police-workforce-england-and-wales-31-march-2023/police-workforce-england-and-wales-31-march-2023#promotions-joiners-and-leavers

[31] HM Prison and Probation Service workforce quarterly: December 2023 - GOV.UK (www.gov.uk)

operational support grades, along with lump sum consolidated payments to junior doctors and the armed forces meaning those on the bottom pay scales saw increases of 10.3% and 9.7% respectively. The deal reached with the Agenda for Change workforce also saw a 10.4% increase for the lowest paid as pay in band 1 and the bottom two points in band 2 was increased to match pay at the top of band 2.

- **Non-headline pay:** Recognising that headline pay is just one component of an individual's employment decision, the government has also continued to make use of other measures to address recruitment and retention challenges. In the teaching workforce these measures have included improvements in the Department for Education's bursary and apprenticeship offers and the introduction of a Workload Reduction Taskforce set up to make recommendations to government, Ofsted, and school and trust leaders on reducing teaching working hours. At Spring Budget 2023, the government increased tax relief on pensions: removing the Lifetime Allowance charge from April 2023 and raising the Annual Allowance to £60,000. These changes have made the relative weighting of public service remuneration towards pensions more attractive for the highest earners and those with the longest service, and were designed to ensure highly skilled individuals such as consultants have stronger incentives to remain in the workforce. The deal agreed by the government and NHS Staff Council also led to eligible Agenda for Change staff receiving two substantial one-off payments worth, in total, between £1,655 and £3,789 reflecting, in part, the sustained efforts of NHS staff following the pandemic. The deal also included support for nursing staff, in particular with regards to career development.

3.14 Whilst the overall recruitment and retention landscape has improved, there remains variation within workforces across grades and professions.

- Whilst the number of leavers in the lowest paid operational support grades in **prisons** has recently fallen (by 13.5% in the year ending 31 December 2023)[32] the leaving rate remains high, and greater than all other operational bands, at 15.8%. However, it is too early to judge the impact of the 2023-24 pay award, which did not reach pay packets until September 2023 and which was targeted at operational grades.

---

[32] HM Prison and Probation Service workforce quarterly: December 2023 - GOV.UK (www.gov.uk)

- In the **teaching workforce**, recruitment varies significantly by subject and is under target for most subjects. Challenges are especially acute for Science, Technology, Engineering and Mathematics (STEM), where the Initial Teacher Training Census[33] reports that providers only recruited 17% of the physics target and 36% of the computing target, whilst 63% of the maths and 65% of the chemistry targets were achieved respectively. Retention rates are also lower for STEM subjects than non-STEM subjects. Reflecting on these specific pressures, the Government will ask the STRB for its views on targeting remuneration by subject.
- There needs to be a continued focus on retention of staff in order to deliver the 'retention' ambitions outlined in the **NHS** Long Term Workforce Plan. Whilst easing on the previous year and now back at pre-pandemic levels, the leaving rate for midwives was 10.8% in the year to September 2023[34], which is higher than other professionally qualified staffing group leaver rates. To help address pinch-points in recruitment and retention DHSC are utilising a range of non-headline pay measures. For example, DHSC are offering non-repayable grants of at least £5,000 per academic year to eligible students studying pre-registration programmes across certain professions, including nursing and midwifery, whilst continuing to grow apprenticeship opportunities. This is one of a range of factors that has contributed to the government meeting its commitment to increasing the numbers of registered nurses in the NHS in England by 50,000 six months early.

3.15 Departments will set out in their evidence to PRBs any measures they are already taking to address recruitment and/or retention pinch-points, and whether they would like PRBs to consider targeting of pay awards within their workforces.

Labour market outlook

Unemployment

3.16 Recent forecasts are for unemployment to rise slightly over the coming year. The OBR forecasts that unemployment will rise to 4.6% in the middle of 2024, and remain at this rate until the end of 2025, before falling back to 4.1% at the end of the OBR's five-year forecast horizon. This reflects the impact of slower GDP

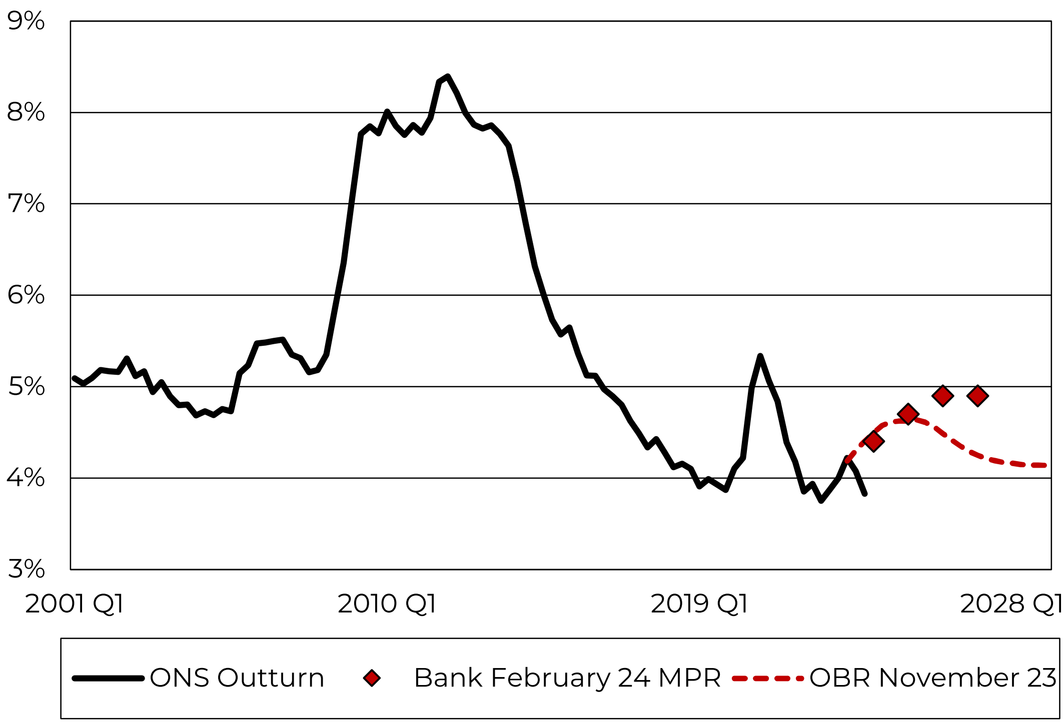
33 Initial Teacher Training Census, Academic year 2023/24 – Explore education statistics – GOV.UK (explore-education-statistics.service.gov.uk)

34 NHS Workforce Statistics - September 2023 (Including selected provisional statistics for October 2023) - NHS Digital

growth and higher interest rates weighing on labour demand. The Bank of England February 2024 MPR projects that unemployment will rise to 4.5% in 2024 Q4 and 5.0% in 2025 Q4. The average forecast in HMT's comparison of independent forecasts[35] also anticipates that unemployment will increase, to 4.6% in 2024 and 2025.

3.17 There remains considerable uncertainty over the unemployment outlook. This reflects both risks to the wider economic outlook and recent challenges in interpreting labour market data, which has been subject to elevated uncertainty and revision, partly reflecting falling response rates to the Labour Force Survey[36].

Figure 3.J Unemployment rate (%)



Source: ONS[37], OBR November Economic & Fiscal Outlook, Bank of England November MPR[38]

---

35 Forecasts for the UK economy - GOV.UK (www.gov.uk)

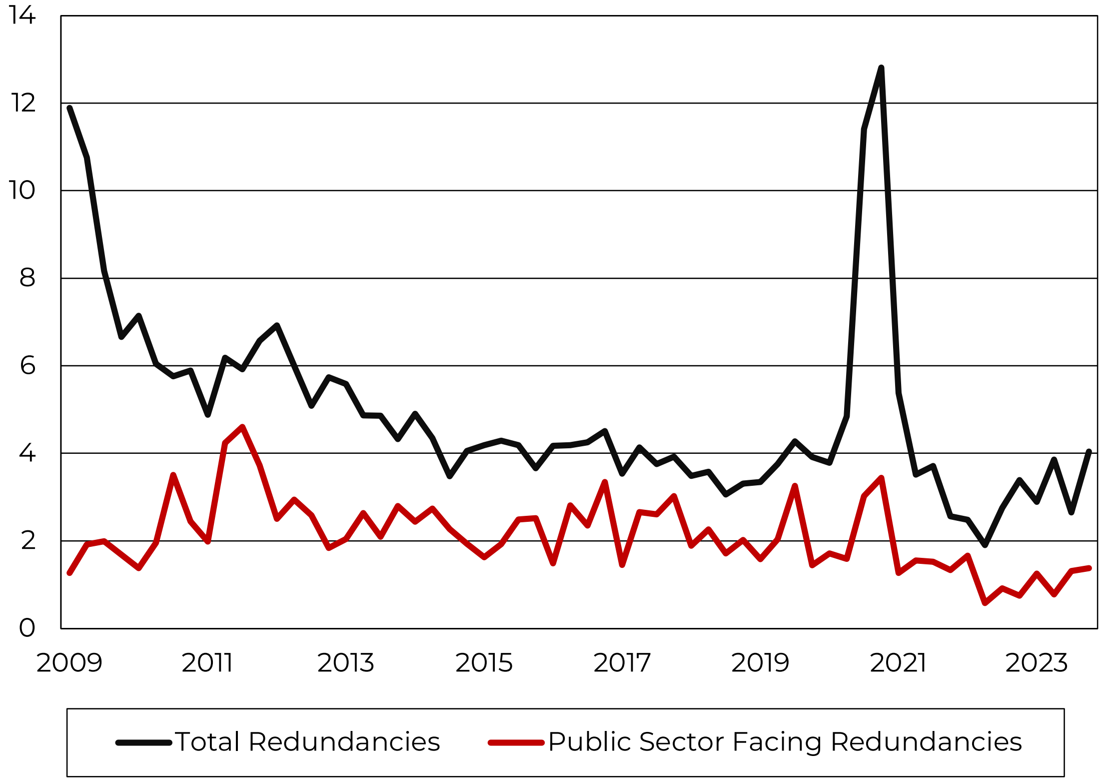
36 The ONS have set out their plans to address the current challenges facing the Labour Force Survey here.

37 Employment in the UK, December 2023, Office for National Statistics, February 2024

38 Monetary Policy Report, February 2024, Bank of England, February 2024

3.18 The public sector will provide greater job security during this period of rising unemployment, with redundancy rates in public sector facing sectors remaining significantly below the redundancy rate across the whole economy, a trend that is expected to continue.

Figure 3.K Redundancy rates (per 1000 employees)[39]



Source: ONS[40] (Data from 2022 Q3 onwards has been reweighted)

Wage growth

3.19 Wage growth is expected to continue to moderate across 2024-25 as the labour market loosens. In their November 2023 Economic and Fiscal Outlook the OBR forecasts that earnings growth will fall to 3.8% in 2024 and 2.2% in 2025. Other forecasts also point to a moderation in earnings growth, with the HMT's comparison of independent forecasts for February 2024 indicating an average forecast for earnings growth of 3.8% in Q4

---

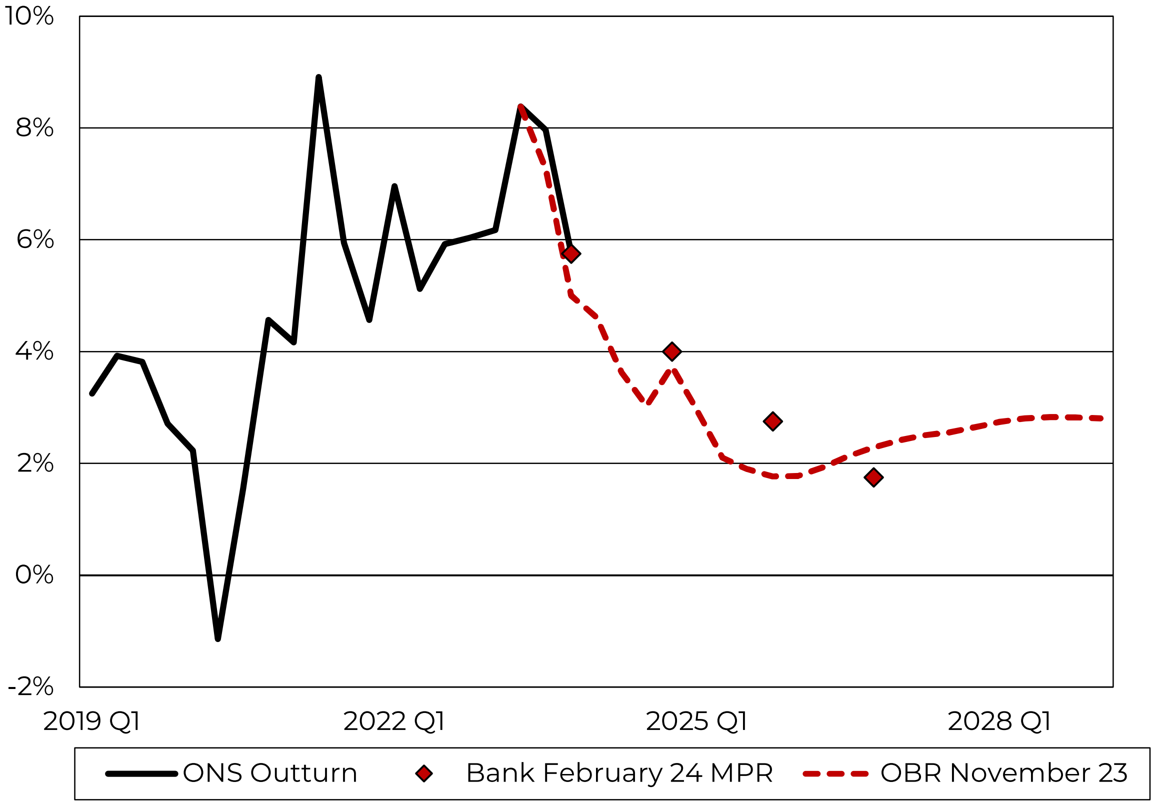
[39] Public sector redundancy rate calculated by dividing redundancy level in public sector facing sectors by the number of employees in those sectors. In some quarters in some sectors, the redundancy level is suppressed on disclosure grounds.

[40] Redundancies by age, industry and region, December 2023, Office for National Statistics, February 2024

2024. As discussed above, this measure of average earnings growth has historically been higher than average pay settlements, as it is affected by compositional changes in the labour force and broader pay drift.

3.20 Academic evidence highlights the possibility of short-run spillovers from public sector pay growth to the private sector. For example, NIESR[41] estimate a short-run public-to-private sector wage spillover in the UK between 2000 and 2019 ranging from -0.02 to 0.4, and averaging 0.1.

Figure 3.L Outturn and forecast wage growth (total pay)



Source: ONS[42], OBR November Economic & Fiscal Outlook, Bank of England November MPR[43]

---

[41] The-dynamics-of-public-and-private-sector-wages-pay-settlements-and-employment-Full-Report-4.pdf (niesr.ac.uk)

[42] Average weekly earnings in Great Britain, December 2023, Office for National Statistics, February 2024

[43] Monetary Policy Report, February 2024, Bank of England, February 2024

Chapter 4

Macroeconomic Policy Context

4.1 Low and stable inflation is essential for creating a stable macroeconomic environment, and a pre-requisite to achieving strong, sustainable, and balanced growth in all parts of the UK and sectors of the economy. The government must continue to support the Bank of England to bear down on inflation to get it back to the 2.0% target, building on achieving the Prime Minister's commitment to halve inflation.

4.2 The independent MPC of the Bank of England is responsible for controlling inflation in the UK. To combat high inflation, the Bank of England has already raised interest rates to 5.25%, from 0.1% in December 2021. This is the highest rate since March 2008 and has already resulted in additional costs for many mortgage-holders, whose mortgage payments have increased substantially, and businesses and government, who have faced higher borrowing costs.[44]

4.3 Markets expect interest rates to fall gradually but remain elevated, and the MPC has also said that monetary policy will need to remain restrictive for sufficiently long to return inflation back to target sustainably in the medium term. If inflationary pressures increase, the MPC may need to hold interest rates at their current level for longer to ensure inflation returns sustainably to the 2.0% target.

4.4 The government is committed to supporting the MPC to bring inflation back to target, to limit the difficulties faced by households and businesses due to high inflation. To do this the government must demonstrate fiscal discipline by aligning fiscal with monetary policy. This is achieved by gradually withdrawing fiscal support for the economy. All measures of the public sector deficit show this is forecast to happen in a measured way across the OBR's forecast horizon.

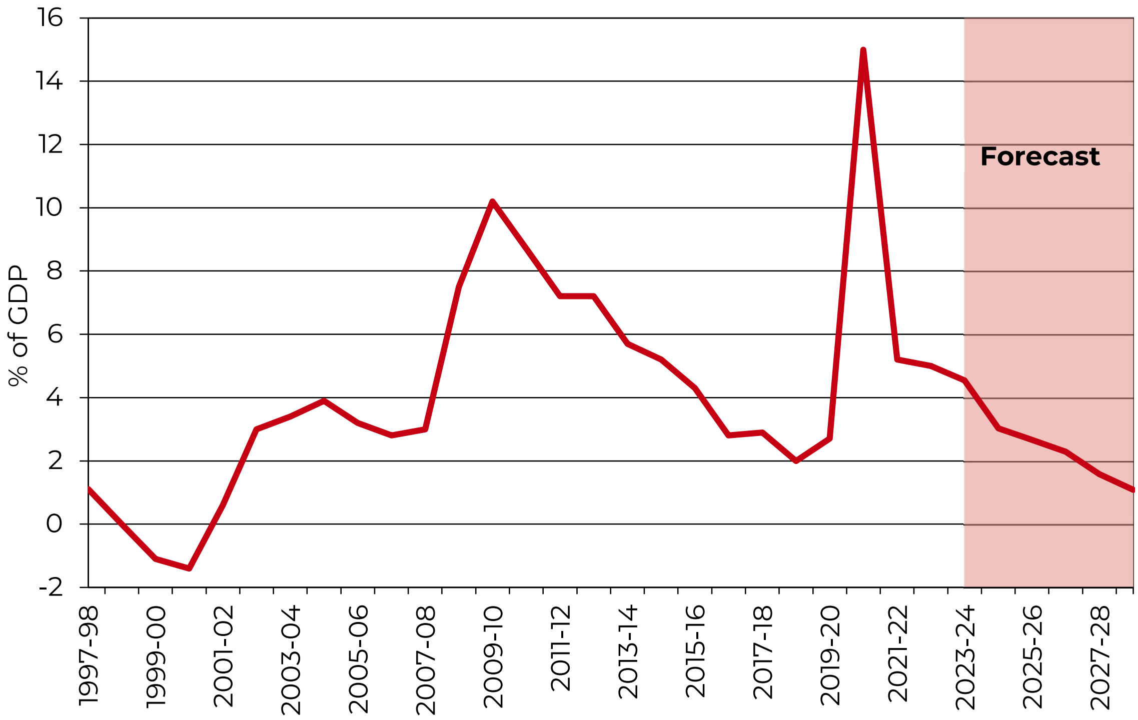
4.5 The government has made tough but responsible decisions to limit borrowing and work within the spending envelope set at

[44] A representative mortgage holder, with a term length of 20 years and an outstanding balance of £120,000, would be expected to see their annual mortgage payments increase by £840 if their interest rate rose from 5.00% to 6.00%.

SR21, including setting out the Public Sector Productivity Programme to ensure this happens. The OBR's November 2023 forecast shows that public sector net borrowing is falling across the forecast.

4.6 Whilst reducing borrowing, the government has prioritised decisions for the long term. The OBR estimates that government decisions at the 2023 Autumn Statement will boost business investment by £14 billion. Together with policies at Spring Budget 2023 the OBR assessed an additional 200,000 people would be in work by the end of the forecast period and potential output would be 0.5% higher.

Figure 4.A Public sector net borrowing, % GDP



Source: ONS, OBR November Economic & Fiscal Outlook

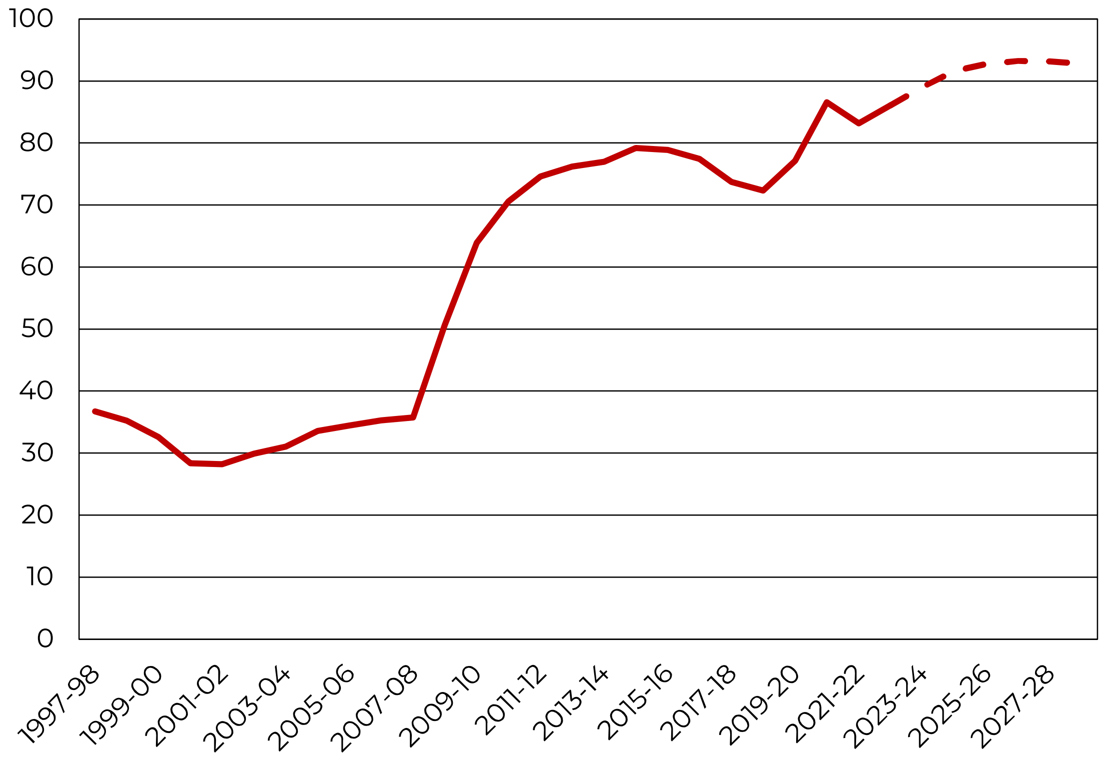
4.7 The OBR confirmed that as a result of the tough decisions the government has taken, the fiscal rules – to have debt falling as a % of GDP and for borrowing to remain below 3% of GDP – are on track to be met. According to the OBR's November forecast, public sector net debt excluding the Bank of England (underlying debt) falls as a percentage of GDP in the target year of the forecast (2028-29).

4.8 Although borrowing and debt are forecast to fall, they remain historically high, having been driven up by significant spending to support households and businesses through historic shocks. Discipline with the public finances is central to continuing to get borrowing down to levels where debt can sustainably fall.

4.9 Given that the level of debt still remains high by historic standards, the public finances are more exposed to changes in interest rates. Based on the OBR's November forecast, if debt interest spending were a government department, its departmental budget would be second only to the Department for Health and Social Care. This spending represents a significant opportunity cost, as it could have been used to fund vital public services. Therefore, the government must ensure that debt falls sustainably and stays on track to meet the debt falling fiscal rule, which will help avoid further rises in government borrowing costs.

4.10 Further significant borrowing would add to existing inflationary pressure, which would put upward pressure on interest rates and increase debt interest spending even further. The OBR's analysis shows a sustained one percentage point rise in short term interest rates and gilt rates would cost around £19 billion in debt interest spending by the end of the forecast.

Figure 4.B Public sector net debt (excluding Bank of England), % GDP



Source: ONS, OBR

4.11 Continued fiscal consolidation is necessary to maintain commitment to strong and stable public finances. Limiting borrowing and continuing to withdraw stimulus as set out at

Autumn Statement is central to supporting the Bank of England to fight inflation. Bringing down debt as a proportion of GDP and doing so by materially reducing borrowing in the next few years protects our resilience to future shocks, reduces the burden passed onto our children and grandchildren, and reduces spending on debt interest.

4.12 Given the need to maintain fiscal discipline, the government was clear through the evidence process of the 2023-24 pay round that any PRB recommendations above affordability figures set out in evidence would need to be carefully considered alongside other priorities and would involve trade-offs. In 2023-24 headline PRB recommendations did come in materially above affordability figures. Given the speed at which wage growth across the economy moved from the forecasts available at the time government evidence was published in early 2023, the government made the decision to accept headline PRB recommendations in full. However, doing so resulted in spending on pay for these workforces being over £2bn higher in 2023-24 and £3bn higher in 2024-25 compared with the affordability position set out in evidence.

4.13 Given the impact of additional borrowing on inflationary pressures, the decision was made to fund these pay awards through reprioritisation and increased fee income. At the time, the trade-offs involved in accepting 2023-24 PRB recommendations included, but were not limited to: increasing visa fees by 20% across most routes, increasing the Immigration Health Surcharge to £1,035 for the main rate and £776 for the discounted rate, cutting back on Civil Service recruitment at the Ministry of Defence, and exceptionally allowing the Department for Education to retain various one-off underspends.

4.14 Departments have set out detail on their individual spending positions within their evidence. Across departments, 2024-25 is the tightest year of this Spending Review period, with departments having faced significant headwinds since budgets were set, driven by inflation, pay, and an array of department-specific pressures.

- **Inflation.** Due to stronger and more persistent inflation, the OBR's November 2023 forecast has price levels 12% higher in 2024-25 than they had been forecast when departments budgets were set at SR21. This creates higher costs for departments for e.g. energy and procurement, and means that departments' budgets are around £10bn lower in real terms in 2024-25 compared with 2022-23,[45] in contrast to the planned real terms increase of 1% per annum at SR21.[46]

- **Pay.** Departments were generally funded for pay awards of 3% and 2%, across 2022-23 and 2023-24, whilst actual PRB awards were ~5% in 2022-23 and ~6% in 2023-24. This equates to spending ~£10bn more on pay in 2024-25 than planned at SR21 for PRB workforces alone, even before 2024-25 awards are considered. This is equivalent to the entire resource budget for the Ministry of Justice.
- **Department-specific pressures.** Departments have also faced their own specific pressures since budgets were set at SR21, driven by factors which include, but are not limited to: military, humanitarian, and economic support for Ukraine; the continued impacts of Covid-19 on the NHS; increasing costs of defence nuclear enterprise; and higher than expected costs in the asylum system.

4.15 The pressures outlined above mean that departments are already having to reprioritise and find efficiencies to enable funding to be available for pay awards this year. The proportion of departments' resource budgets spent on pay has on average been rising, with Public Expenditure Statistical Analyses (PESA) data showing that expenditure on pay has increased from 49% of total RDEL expenditure in 2021-22 to 53% in 2022-23 (the latest outturn data).[47]Each 1ppt of PRB pay awards costs an estimated £1.8bn across a full pay-year in 2024-25[48] and all else equal, increased spending on pay either reduces available room in budgets for non-pay expenditure, including funding for frontline services provision, or necessitates further borrowing which, as above, would increase pressures on interest rates at a time when they have already reached their highest level in 15 years. Given the reprioritisation towards pay already made to deliver 2022-23 and 2023-24 awards, the scope for further savings within departments' budgets is limited.

4.16 The Government will therefore have to carefully consider its response to the PRBs' recommendations in light of departments' spending positions, the overall fiscal context and other priorities including frontline service provision.

---

45 Slide 9 PowerPoint Presentation (obr.uk)

46 The implications of the Government's departmental spending plans - Office for Budget Responsibility (obr.uk)

47 Public Expenditure Statistical Analyses 2023 (publishing.service.gov.uk)

48 Excluding Barnett

Chapter 5
Conclusion

5.1 This evidence has outlined how the overall public sector remuneration package remains competitive when accounting for pay, pensions and wider benefits such as job security. Median pay remains higher in the public sector, pensions continue to be substantially more generous, whilst redundancies remain concentrated in the private sector.

5.2 Recruitment and retention trends across PRB workforces have improved over the last year following an initial deterioration after the pandemic, with vacancies falling and headcount increasing across public sector facing industries both in absolute terms and relative to the private sector. Vacancies across the economy remain elevated but are expected to continue to ease, with PRB workforces further supported through the historically high pay awards delivered for 2023-24 and an array of non-headline pay measures that have been delivered or committed to. Recruitment and retention pinch-points do remain, but these are generally limited to specific areas of workforces, as opposed to being broad-based.

5.3 The economy has faced an unprecedented series of shocks in recent years, which drove up inflation through higher energy prices and led to a subsequent increase in domestically generated inflation. The Bank of England have taken necessary action to bring inflation back to target, which is working, but has inevitably led to slower growth over the past 18 months. The OBR forecasts an increase in unemployment through this year and next. Wage growth has also started to ease from its historically high levels and as the economy loosens is forecast to fall below 4% this year and to around 2% in 2025.

5.4 Inflation has fallen significantly since its peak in October 2022 but remains elevated having proven more persistent than expected. Inflation is forecast to continue to fall over the remainder of this financial year and into 2024-25. There remains considerable uncertainty over the outlook and the Bank of England's Monetary Policy Committee has judged that risks remain skewed to the upside, in the short-term. Interest rates have increased to their highest levels in over fifteen years, increasing costs for households, businesses and the government. Significantly increasing borrowing would create further inflationary pressures, potentially necessitating interest rates to remain higher than currently expected. Continued fiscal consolidation is necessary to limit inflationary pressures and get debt falling and reduce the deficits that arose from pandemic and energy related support. Evidence indicates that possibility that the possibility of short-run spillovers from public sector pay growth to the private sector, which could also impact on inflationary pressures.

5.5 Departments are facing their tightest year of the spending review period in 2024-25, with significant pressures arising from inflation, pay and other areas. Departments are therefore having to reprioritise and continue to identify efficiency savings to enable funding to be available for pay awards. The Government will therefore have to carefully consider its response to the PRBs' recommendations in light of departments' spending positions, the overall fiscal context and other priorities including frontline service provision.

HM Treasury contacts

This document can be downloaded from www.gov.uk

If you require this information in an alternative format or have general enquiries about HM Treasury and its work, contact:

Correspondence Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Tel: 020 7270 5000

Email: public.enquiries@hmtreasury.gov.uk