Don't believe the evidence

***Kevin Gardiner** casts doubt on figures showing a slowdown in UK productivity. He believes they may be misleading and not reflect an increasingly intangible and digital economy*

The UK economy has rarely created jobs more quickly. Since early 2010, employment has risen by 3m, or 10 per cent. Some of this was the initial rebound from the financial crisis, but employment is now more than 2m above its pre-crisis peak, and trend growth has been stronger than at a similar phase in the "noughties".

Pundits who sniffily dismiss the new jobs as being "low quality" are mistaken. The new workers are predominantly full-time employees. They are mostly in the private sector and spread across a wide range of industries, except manufacturing. "Zero-hours contracts" have been growing faster, but still account for just 3 per cent (900,000) of all jobs. Meanwhile, unemployment has fallen steadily, and much further than predicted: the standardised rate is at a 42-year low and vacancies are high.

A cause for rejoicing, you would think. But true to form, economists have managed to wrap a cloud around this silver lining. Jobs have grown quickly, but output has not. Result: poor productivity performance. Output per person has rarely grown more slowly.

A productivity slowdown, if it is genuine and sustained, could spell trouble. Output per hour, or per person employed, is closely related to GDP per capita, a gauge of material prosperity. Poor productivity performance could lead, via higher unit costs, to renewed inflation pressure and squeezed profit margins. It might indicate a general lack of dynamism and innovation. But it may be neither genuine nor lasting and could prove misleading.

Economic statistics should be viewed much more sceptically than they are. It may be relatively easy to count people, but we rarely stop to think about just how difficult it is to measure the output of a large, diverse, constantly changing economy. GDP focuses on "final" output or value added. But the distinction between final and intermediate activity can be arbitrary – particularly perhaps at a time when the economy is becoming increasingly "informal". Product proliferation and complexity, quality change, innovation and altered delivery also get in the way of determining "final" output.

An increasingly service-oriented, intangible and digital economy poses special problems. A barrel of oil, for example, is visible, and little different from what it used to be. A car can be counted, but is a very different product from a car in the 1970s. Digital and virtual products are harder to count, and new. Many public sector services are not priced to begin with, and evolve similarly. Can inputs bought and wages paid accurately capture the quantity of health and defence services, for example? A letter can be weighed. An email cannot be – but can still add value. The market mechanism might capture that value – but perhaps not in ways that are easily traced by the official statisticians.

In the *Independent Review of UK Economic Statistics* (March, 2016), Professor Sir Charles Bean suggested: "The increased internet accessibility has led to a dramatic growth in the

> *You can see the computer age everywhere but in the productivity data*

digital product consumed online. One would expect to see similarly buoyant growth in the statistics meant to capture the digital sector. But this is far from the case, suggesting that official statistics may be missing an important aspect of the contemporary economy." And the US economist Robert Solow famously quipped: "You can see the computer age everywhere but in the productivity data."

Productivity trends also may have a larger pro-cyclical component than acknowledged: the slowdown, even if accurately measured, might yet prove temporary. There is no reason to think the potential for meaningful productivity growth has evaporated. Even if there were no dramatic technological breakthroughs and returns to scale left to discover, much productivity growth derives from the more mundane gains that happen continually as workers and managers move up the learning curve.

Until we get more corroborating evidence, maybe in the form of more obvious unit cost pressures and/or supply shortages, we should view the increase in employment as the more convincing, and welcome, macro trend. ■

***Kevin Gardiner** is global investment strategist at Rothschild. He is writing in a personal capacity*