# ECONOMIC UPDATE

REGIONS

October 31, 2018

*This Economic Update may include opinions, forecasts, projections, estimates, assumptions, and speculations (the "Contents") based on currently available information which is believed to be reliable and on past, current and projected economic, political, and other conditions. There is no guarantee as to the accuracy or completeness of the Contents of this Economic Update. The Contents of this Economic Update reflect judgments made at this time and are subject to change without notice, and the information and opinions herein are for general information use only. Regions specifically disclaims all warranties, express or implied, with respect to the use of or reliance on the Contents of this Economic Update or with respect to any results arising therefrom. The Contents of this Economic Update shall in no way be construed as a recommendation or advice with respect to the taking of any action or the making of any economic, financial, or other plan or decision.*

## Q3 2018 Employment Cost Index: Faster Growth, But Not "Full Employment" Fast

- The total ECI was up 0.8 percent in Q3 2018, with the wages/salaries component up 0.9 percent and the benefits component up 0.4 percent.
- Year-on-year, the total ECI was up by 2.8 percent in Q4 with wage costs up 2.9 percent and benefit costs up 2.6 percent.

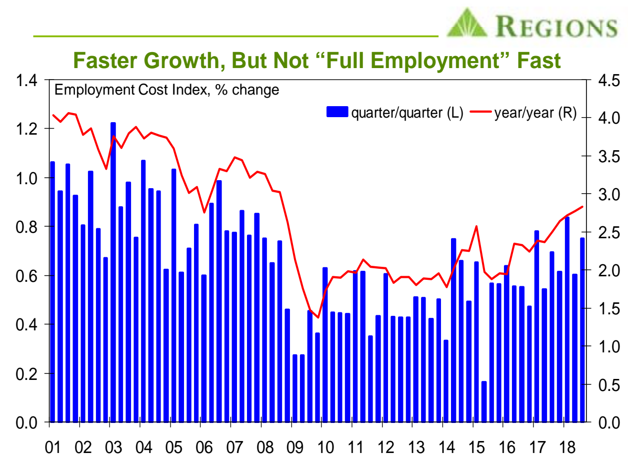
Total compensation costs, as measured by the Employment Cost Index (ECI), rose by 0.8 percent in Q3, matching our above-consensus forecast. Wage costs as measured in the ECI were up 0.9 percent in Q3, matching the increase seen in Q1 2018 as the largest quarterly increase since Q1 2007, while benefit costs were up 0.4 percent, the smallest quarterly advance in benefit costs since Q2 2016. As of Q3, the total ECI is up 2.8 percent year-on-year, with wage costs up 2.9 percent and benefit costs up 2.6 percent. Growth in labor costs has clearly been accelerating, as would be expected given what has been a prolonged period of steady improvement in labor market conditions. At the same time, however, the ECI data do not paint the picture of a labor market on the boil despite an unemployment rate having pushed below 4.0 percent and likely to go even lower.

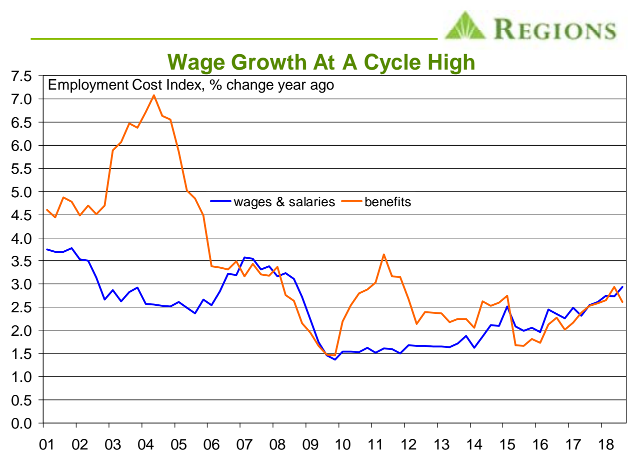
The ECI is one of the three main data series – the others being average hourly earnings from the monthly employment report and unit labor costs from the quarterly labor productivity and costs report – showing trends in labor costs. The ECI tends to get less attention than its two counterparts but to us is the most meaningful of the three series. The ECI is designed to measure changes in total labor costs, for both money wages and salaries and noncash fringe benefits (such as health insurance and pensions). One distinction between the wage component of the ECI and the more widely followed average hourly earnings metric is the ECI is not affected by shifts in the composition of employment across industry groups. Instead, the wage component of the ECI effectively measures wage costs for the same jobs over time and the total ECI measures labor costs (i.e., wages and benefits) for the same jobs over time. One drawback of the average hourly earnings metric is that it is skewed by changes in the composition of employment and hence will mask earnings differentials across industry groups. These differences aside, the alternative series are showing faster, but not full employment fast, wage growth.

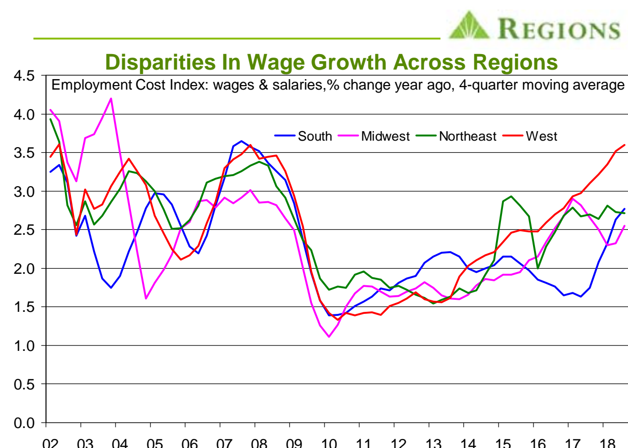
That said, labor market conditions have tightened to the point that wage growth has picked up across industry groups, benefitting workers at various skill levels. The Q3 ECI data show transportation & warehousing (up 1.47 percent), leisure & hospitality services (up 1.04 percent), and information services (up 1.00 percent) posted the largest quarterly increases in wages. On a year-on-year basis, transportation & warehousing (up 4.30 percent), leisure & hospitality services (up 3.80 percent), retail trade (up 3.63 percent), and education & health services (up 3.17 percent) posted the fastest wage growth. To be sure, wage growth in industry groups such as retail trade and leisure & hospitality services has over the past couple of years gotten a push from mandated increases in minimum wages, and wage growth in retail trade has been lifted by voluntary increases in entry level wages that have tended to filter up through the ranks. But, these "base" effects are beginning to wash from the data and that quarterly wage gains in these industry groups remain above-average is more a reflection of tightening labor market conditions.

Aside from differentials in wage growth across industry groups, there are also significant divergences in wage growth across geographies, as seen in our bottom chart (we use 4-quarter moving averages to smooth out what is considerable quarter/quarter volatility). For some time now wage growth has been faster in the West region than in the other three broad regions. Wage growth in the Midwest and South regions came together in Q1 but clearly is moving in opposite directions. The geographic splits reflect not only the different mix of industries from one region to the next but also underlying labor market conditions.

The ECI data are consistent with other measures showing gradually accelerating growth in labor costs. While this will continue as the labor market tightens further, what will matter more to FOMC members is whether wage growth shifts into an even faster gear, which would lead them to push the Fed funds rate higher at a faster pace. Our view is that there is still a way to go before we get to that point.




**Regions Financial Corporation, 1900 5th Avenue North, 17th Floor, Birmingham, Alabama 35203**
Richard F. Moody, Chief Economist • 205.264.7545 • richard.moody@regions.com