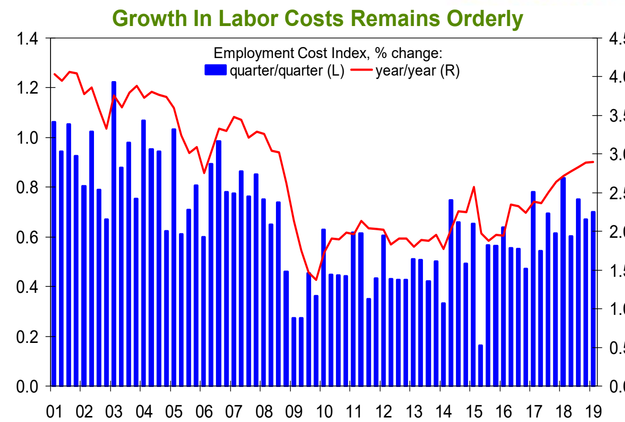
ECONOMIC UPDATE
REGIONS
April 30, 2019

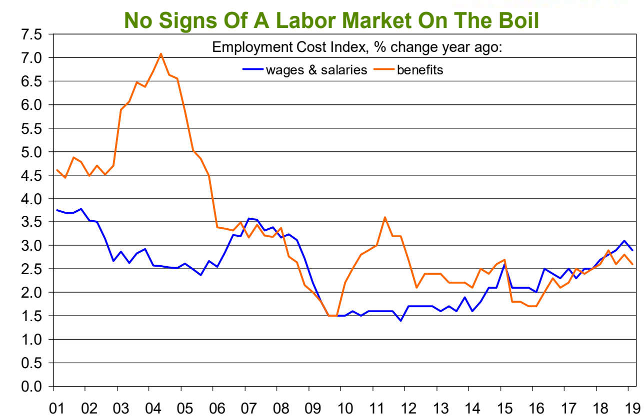
Q1 2019 Employment Cost Index: Wage Growth Accelerating, But At A Gentle Pace

- The total ECI was up 0.7 percent in Q1 2019, with the wages/salaries component up 0.7 percent and the benefits component up 0.7 percent.
- Year-on-year, the total ECI was up by 2.8 percent in Q1 with wage costs up 2.9 percent and benefit costs up 2.6 percent.

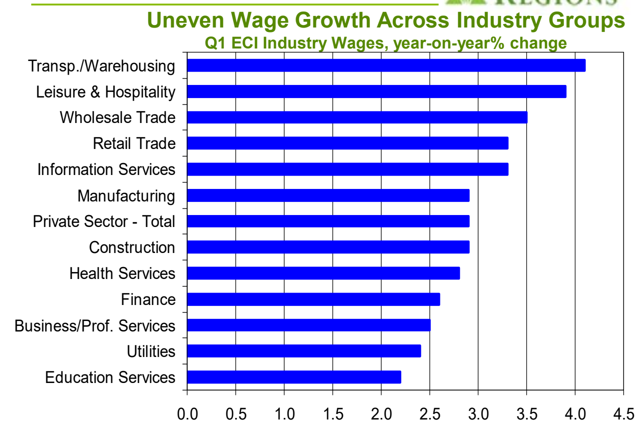
Total compensation costs, as measured by the Employment Cost Index (ECI), rose by 0.7 percent in Q1, slightly below our forecast of a 0.8 percent increase, with wage costs and benefit costs as measured by the ECI each logging a 0.7 percent increase. As of Q1, the total ECI is up 2.8 percent year-on-year, with wage costs up 2.9 percent and benefit costs up 2.6 percent. Today's release incorporates benchmark revisions to the prior five years of ECI data, but the revisions don't alter the underlying story, which is that growth in labor costs is steadily accelerating, but not at a pace which suggests a labor market on the boil despite an unemployment rate below 4.0 percent and likely to head even lower over coming quarters. This is in line with the message being sent by other measures of labor costs, and while we're not big on the wage growth-inflation link, many FOMC members are and, as such, the Q1 ECI data will make them more comfortable with the patient approach to monetary policy the Committee has for now settled upon.



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), and also includes employer-paid taxes such as Social Security and Medicare. 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.



One advantage of the ECI is that it gives us detailed data on compensation costs across the major industry groups, which is a more informative way to look at growth in labor costs than the broad average hourly earnings metric. On an over-the-year basis as of Q1, wage costs in the transportation/warehousing industry group rose by 4.1 percent after a 4.0 percent increase in Q4 2018. Growth in wages in transportation/warehousing reflects what has been rapid job growth in this industry group, in large measure fueled by shifting consumer shopping patterns, and we expect wages in this industry group to continue to post solid increases in wages over coming quarters. Wages in leisure & hospitality services were up 3.9 percent after a 4.6 percent increase in Q4 2018, while wages in retail trade were up 3.3 percent – it is worth noting that wage growth in these two industry groups has benefitted from higher mandated minimum wages as well as firms voluntarily raising entry-level wages, with the latter tending to filter up through the seniority ranks. Construction wages were up 2.9 percent year-on-year, with wage growth in this industry group oddly out of alignment with what has been a steady stream of complaints about shortages of construction labor, and given that total compensation costs in construction were also up 2.9 percent year-on-year, it does not appear that firms are offering more generous benefits in lieu of higher wages as a means of attracting workers. On the whole, however, there is no single industry group in which wage growth suggests labor supply constraints are fueling intense wage pressures. Amongst the broad geographic regions, the West saw private sector wages rise by 3.5 percent, with a 3.2 percent increase in the Midwest, a 3.1 percent increase in the Northeast, and a 2.4 percent increase in the South.



The ECI data are in line with other measures showing moderately accelerating labor costs. We expect to see a continuation of orderly acceleration in the growth of labor costs as the labor market tightens further in 2019, which will be a source of comfort to the FOMC.

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