ECONOMIC UPDATE

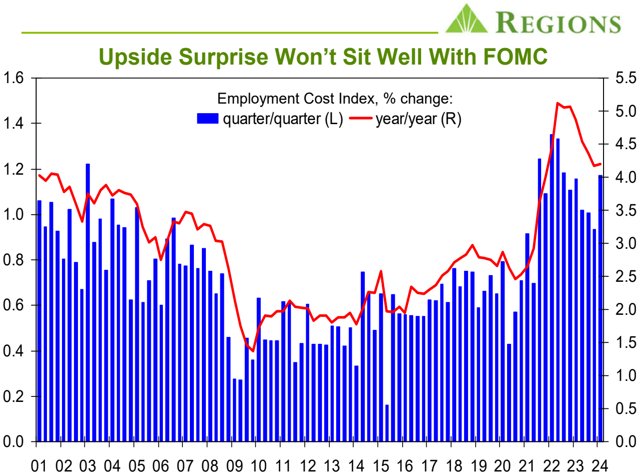
REGIONS

April 30, 2024

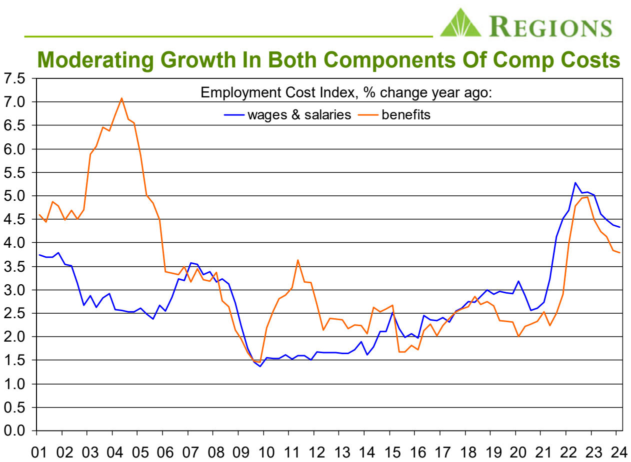
Q1 2024 Employment Cost Index: Benefit Costs Drive Upside Surprise

- The total ECI was up 1.2 percent in Q1 2024, with the wages/salaries component up 1.1 percent and the benefits component up 1.1 percent.
- The total ECI was up 4.2 percent year-on-year, with wage costs up 4.3 percent and benefit costs up 3.8 percent.

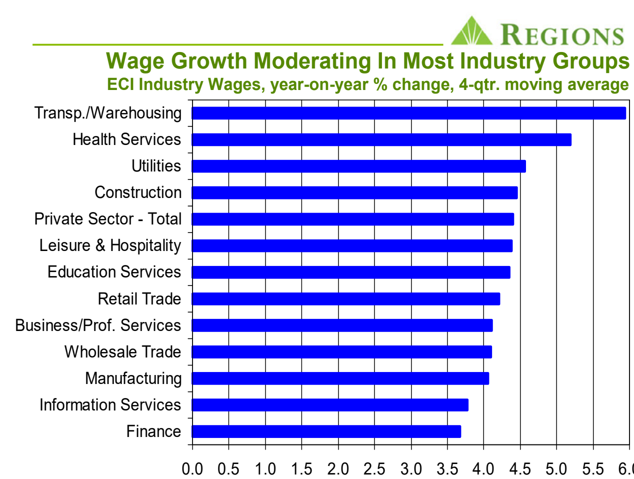
Total compensation costs, as measured by the Employment Cost Index (ECI), rose by 1.2 percent in Q1, topping our above-consensus forecast of a 1.1 percent increase, leaving the total ECI up 4.2 percent year-on-year. The wages component of the ECI was up by 1.1 percent, as our forecast anticipated, but the benefits component surprised us to the upside with a 1.1 percent increase; on a year-on-year basis, the wages component is up 4.3 percent, and the benefits component is up 3.8 percent. Recall that the year-on-year change in the wages component in the Q4 2023 data was 4.4 percent, so the Q1 data show only modestly slower growth in wage costs, while the year-on-year percentage changes in the benefits component and the total ECI match those posted in Q4 2023. So, on the whole, the Q1 data will be seen as a disappointment by those looking for more pronounced moderation in the growth of labor compensation costs.



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 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, and these distortions have been even more pronounced since the onset of the pandemic.



Wage growth has moderated across most of the broad industry groups over the past few quarters, and at the same time has, with a pair of notable outliers, settled into a fairly narrow range, which we illustrate with our middle chart showing a longer-term average rate of wage growth. The rapid pace of wage growth seen in the transportation and warehousing industry group is skewed to some degree by the new UPS contract, which brought significant wage increases for much of that company's workforce. Robust wage growth in the health care/social assistance industry group largely reflects what has been notably rapid job growth in the health care industry, consistently the main driver of overall private sector job growth over the past several months. Keep in mind that, due to the manner in which the ECI is constructed, the outsized increases in these two industry groups are not unduly impacting growth in the wage component. Absent these two industry groups, however, we do think it interesting that the range of wage growth across the broad industry groups has narrowed considerably over the past few quarters. It also bears noting that, after having led the private sector industry groups over the prior several quarters, wage growth in leisure and hospitality services and retail trade has come back to the field, as was bound to happen at some point given how rapid wage growth in these two industry groups was in 2021 and 2022.



Early market reactions to the Q1 ECI data were, not surprisingly, less than favorable, as the data are being seen as reinforcing speculation that the FOMC will remain on hold for longer than had been anticipated. We think the following points are in order. First, to the extent that it was faster growth in benefit costs that produced the upside surprise in the Q1 ECI, that is not something that would respond to monetary policy, particularly to the extent rising employer costs for health insurance plans is the catalyst. Second, keep in mind that recent quarters have seen a marked increase in labor productivity growth, though we expect Q1 to have been an outlier. But, if productivity growth continues to trend higher, that sets the stage for faster wage growth without threating profit margins, thus blunting any inflationary impulses from faster wage growth. So, while the FOMC may not love the Q1 ECI data, the data may not cause them as much angst as many market participants think will be the case.

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