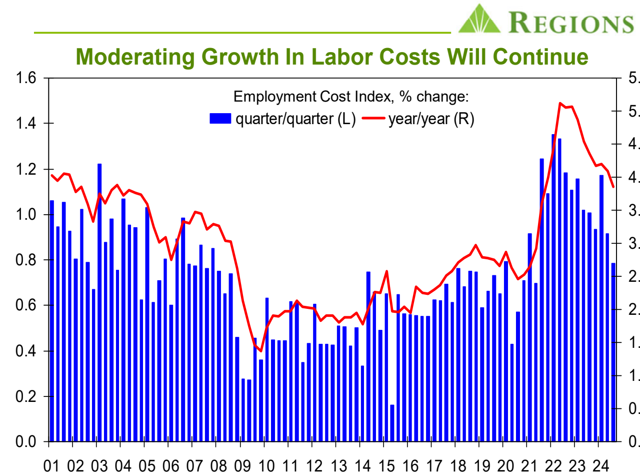
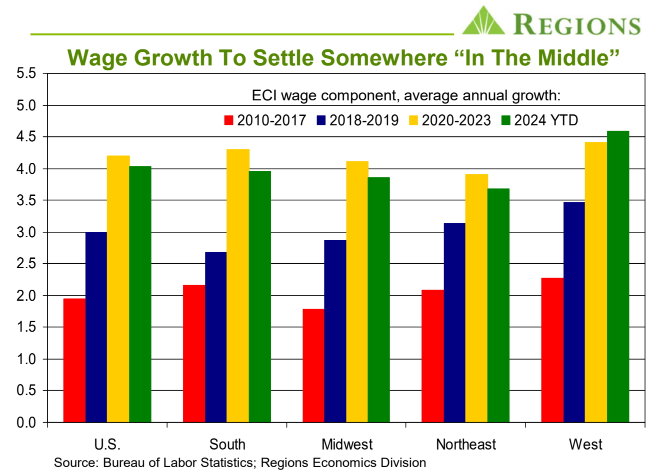
Q3 2024 Employment Cost Index: Growth In Comp Costs Continues To Slow

- The total ECI was up 0.8 percent in Q3 2024, with the wages/salaries component up 0.8 percent and the benefits component up 0.8 percent.
- The total ECI was up 3.9 percent year-on-year, with wage costs up 3.9 percent and benefit costs up 3.7 percent.

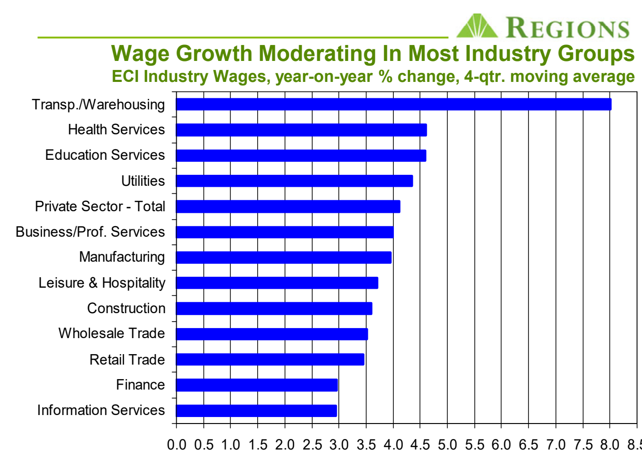
Total compensation costs, as measured by the Employment Cost Index (ECI), rose by 0.8 percent in Q3, matching our below-consensus forecast, leaving the total ECI up 3.9 percent year-on-year. The wages component and the benefits component of the ECI were each up by 0.8 percent, with the former in line with our forecast and the latter a touch lighter than the 0.9 percent our forecast anticipated; the 0.8 percent increase in the wages component is the smallest quarterly advance since Q2 2021. On a year-on-year basis, the wages component is up 3.9 percent, the smallest such increase since Q2 2021, and the benefits component is up 3.7 percent. In keeping with a host of other indicators showing cooling labor market conditions, the ECI shows clearly decelerating growth in labor compensation costs, with the surprisingly strong Q1 ECI data an obvious outlier. It should also be pointed out that, though moderating, wage growth continues to easily outpace inflation which, of late, coincides with the trend rate of labor productivity growth perking up. This is pretty much the ideal set of circumstances for workers, firms, and, oh by the way, central bankers. While we do expect further moderation in the growth of labor costs, we nonetheless expect wage growth to settle into a trend rate higher than that seen prior to the pandemic. If we are correct on that point, how comfortable central bankers are with that will very much depend on whether the pickup in underlying productivity growth is sustained, as we expect will be the case.



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.



Our middle chart helps set up an argument we've been making over the past couple years, which is that we do not expect wage growth to settle all the way back to the pace seen prior to the pandemic. Recall that after a lengthy run of middling wage growth, reflecting the degree of labor market slack wrought by the 2007-09 recession, we finally began to see faster and more broadly based (across industries and geographies) wage growth in 2018. That wage growth took a great leap forward after the onset of the pandemic was not surprising given the disruptions in labor supply triggered by the pandemic. Our argument has been that wage growth would ultimately settle somewhere between the average rate seen over 2018-19 and the rate seen over 2020-23, in part because we did not expect the labor force participation rate to fully rebound from the sharp decline seen at the onset of the pandemic, and in part because we've looked for an increase in trend productivity growth. The significant increase in foreign born labor over the past couple years has likely helped dampen wage growth, but whether or to what extent that increase will be sustained remains to be seen. Our sense is that the magnitude of this inflow will begin to diminish, which would support wage growth ahead of the pace seen over 2018-19. That remains to be seen, but barring a more pronounced slowing in the broader economy and, in turn, the labor market, than we anticipate, we do see a higher floor for wage growth.



Decelerating wage growth is seen across most industry groups, and we'll note that the effects of the UPS contract will fade from the wage data in transportation and warehousing with the Q4 data. It is no surprise that health care leads wage growth amongst other industry groups given the extent to which health care continues to dominate overall job growth.

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