



Wage growth remains subdued

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Compensation has been growing moderately since the recession despite higher increases in the cost of benefits. Wages, the largest subcomponent of compensation, have been growing more slowly, suggesting that they are not putting much upward pressure on inflation.

Expanding wages are central to rising living standards, but only when accompanied by rising productivity. Looking at wage and productivity growth also reveals insights about inflationary trends. Conceptually, when wage growth exceeds the growth in the productivity of the workforce, it puts upward pressure on other prices. This makes wage pressures a strong predictive element for medium-term inflation forecasts. So what's been happening to wages and, more generally, overall compensation (which includes the cost of employer-provided benefits)?

One measure that shows underlying compensation trends is the Employment Cost Index, or ECI. The benefits of using the

ECI to inform policy decisions are threefold: construction, volatility, and flexibility. The ECI is *constructed* as a price index with a fixed set of occupations that represent the typical U.S. workforce. Thus, it provides a consistent apples-to-apples comparison of compensation patterns over time. In addition, the ECI is less *volatile* and not subject to significant revisions, as is the case with some other compensation measures. Finally, the ECI's total compensation series can be broken out into wages/salaries *and* benefits. That makes it possible to disentangle the movements to determine what is driving overall compensation growth.

Recent trends in the ECI point to subdued compensation growth. Over the past year, total compensation for private workers is up 2.1 percent, while wages and salaries are up 1.9 percent. A striking feature of the recent trend is that compensation growth has consistently remained below its prerecession levels. During the last business cycle, compensation growth was as high as 4 percent before it fell to 1.2 percent and then stabilized slightly above 2 percent, where it has remained for the past seven quarters. In fact, this pattern has occurred after each of the recessions in which ECI data are available.

lower levels following each recession. During the last recession, wage and salary growth fell from just below 4 percent to less than 2 percent, and has remained there.

In sum, much of the recent upward movement in compensation growth has been driven from benefits and not from wages and salaries. Given recent productivity rates, which have averaged 2.2 percent over the expansion, it is hard to argue that there is any meaningful inflationary pressure coming from wages.

A quick look at the split of compensation into its components highlights three points. First, wages have a much tighter relationship with overall compensation growth than benefits. Second, benefits growth can be subject to large movements that may not be part of the business cycle, leading to some prolonged shifts in the overall compensation series; this appears to be the case currently. Third, wage growth has fallen even more reliably after each recession and has remained at

Employment Cost Index (ECI)

