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Economics Group

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Widespread Pay Cuts Not Evident in ECI Data

The ECI showed private wages rising at the slowest pace in five years, but suggests that outright pay cuts have not become widespread and/or severe. A more subdued pace of wage growth is ahead, however.

Move Over Average Hourly Earnings, Time for ECI to Shine

Like so many other aspects of the economy in this unique downturn, wages have not responded in the usual pattern. Average hourly earnings (AHE) soared more than 5% between February and April even as the jobs market crumbled, but the rocketing of AHE over that period reflected outsized job losses in lower-paid industries like leisure & hospitality. As a higher share of workers in low-pay industries were laid off, the average hourly pay of workers still on the payroll across the economy rose substantially. But without adjusting for a rapid shift in the composition of the labor market, the AHE figures have dispelled little about how companies are managing their labor costs beyond merely cutting jobs.

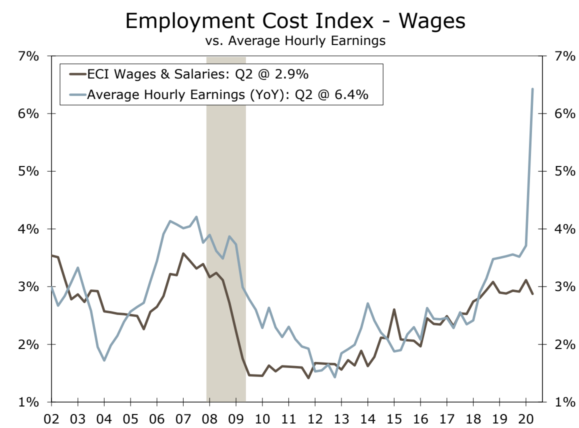
The Employment Cost Index (ECI) offers a better look at how companies are adjusting wages for a particular job in the COVID environment, as it holds the industry and occupational categories constant. Wage & salary costs rose 0.4% for private sector workers over the second quarter, the smallest increase in five years.

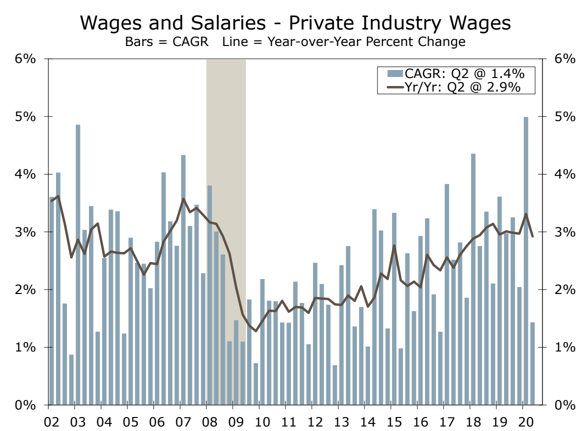
Employers are typically loathe to cut wages outright, fearing the departure of their best-performing workers and a broad hit to morale. But as the COVID-recession has posed an existential threat to some industries and decimated revenues even among businesses likely to make it to the other side of this crisis, the usual rules do not fully apply. A number of studies and surveys have shown companies cutting wages outright in response to the crisis. For example, a study by economists at the Fed and the University of Chicago found employers cutting nominal wages by about 10% and cancelling scheduled increases for others. Meanwhile, in the Fed's recent Beige Book reports, contacts have reported pay cuts, for salaried workers in particular.

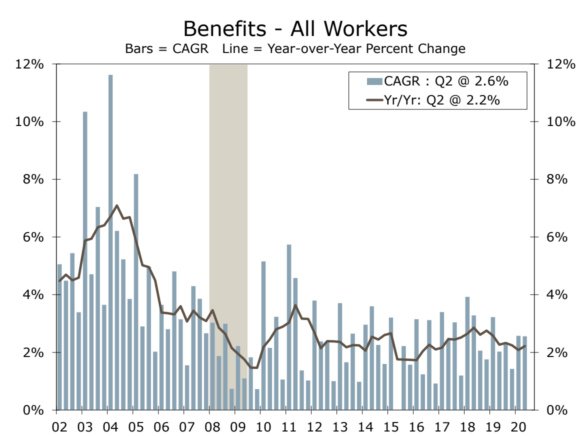
While weak, the second quarter's increase in wage & salary costs suggests that pay cuts to workers still on the books have not been terribly widespread or severe. On a year-ago basis, private sector wage & salary costs are up 2.9%, still within the range of recent years. That said, we are settling in for a period of much slower wage growth ahead with record high unemployment and pressure on firms' bottom line as spending and investment have plummeted.

Wages Tame, but More Pressure on Benefit Costs in COVID Era

As for benefits, private sector costs increased more substantially in the second quarter, up 0.7%. That comes on the heels of a particularly modest 0.2% increase the prior quarter, so the strengthening could merely be payback for the prior quarter's softness. Yet it could also reflect employers offering more paid leave like sick days or personal days to contend with the healthcare crisis and child care gaps with schools closed. Unfortunately, the ECI does not provide a breakdown on benefit costs. For that, we will be waiting for a separate BLS report to be released in September.







Source: U.S. Department of Labor and Wells Fargo Securities

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