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You’re not getting a raise and nobody knows why

By Ana Swanson May 9, 2017

The economy today has almost everything experts look for as a sign of health — new jobs are popping up around the country, the unemployment rate has fallen to the lowest level in a decade, and consumer and business confidence is high. But one thing that really matters for workers has been stubbornly absent: strong wage growth.

The pay that workers take home has risen a little since the depths of the recession, but not much. Once you factor in inflation, wages growth is so low that workers are hardly better off than they were a year ago. Over the past year, average hourly earnings have risen just 2.5 percent, according to Friday's report on April job growth.

The trend is disappointing — and somewhat surprising. Given strong job growth and low unemployment, many economists had been expecting that wages would be rising faster by now.

As the economy continues to heat up and companies create more job opportunities, employers should eventually have a harder time finding the caliber of workers that they want. To attract good workers, companies in theory have to start offering pay increases.

But in practice, wage growth has remained relatively sluggish. As **Bernard Baumohl of the Economic Outlook Group** pointed out Friday on American Public Media's "Marketplace," 2.5 percent is precisely the same wage growth seen in 2009, when the jobless rate stood at 10 percent — twice the current level.

Current wage growth "is not what we would expect at this point in a recovery," said Tara Sinclair, an economist at George Washington University and a senior fellow at jobs site Indeed. "We would think employers would be competing with each other and that we would see that competition reflected in wages."

No one knows precisely why wage growth has lagged behind, but economists have a few explanations.

• **Too many people left on the sidelines:** Since the recession, the unemployment rate has not been a great indicator of how much slack is left in the labor market.

That's because the unemployment rate, which was a low 4.4 percent in April, counts only workers who do not have a job but are still actively looking for one. Economists argue that the harsh conditions of the recession persuaded many Americans to give up looking for work altogether. Young people moved back in with their parents, workers went on disability and older employees opted for early retirement.

Some of those people have gradually started looking for jobs again as the economy has heated up. But sluggish wage growth may imply that a lot of these people are still left on the sidelines of the economy, and that they might be willing to start looking for work again as their prospects improve.

Elise Gould, a senior economist at the left-leaning Economic Policy Institute, said that relatively sluggish wage growth "tells us that there's still a fair amount of slack left in the labor market. The unemployment rate is missing part of the story of workers continuing to be sidelined."

Gould points to the employment-to-population ratio for prime-age workers, which measures the proportion of the population between the prime working ages of 25 and 54 who are employed. That figure stood at 78.6 percent in April, still significantly below where it was in 2007 and for most of 2008.

"We have recovered a fair amount, but we still have a way to go," Gould said. "If there was less slack, then employers would have to be offering better pay to attract and retain the workers they want, and they just don't have to yet."

• **We're not getting much more productive:** Other economists find different reasons for lagging wage growth. One is that gains in productivity — a measure of how much a given worker or machine can produce — have also been sluggish of late. That is a worrying sign, since productivity gains are what really determines improvements in wealth and living standards over generations.

But blaming productivity for slow wages is not a full explanation, because economists in turn debate the reasons behind sluggish productivity. Some fault measurement issues. Some point a finger at government policies that have failed to encourage investments in machinery and technology. Others say it could just be because of natural ebbs and flows in innovation.

If slow wage growth is tied to productivity, it's more important than ever that the Trump administration implement policies that boost it, said Jeremy Lawson, chief economist at Standard Life Investments. Yet Lawson said the policies the administration is focused on will not do the trick.

"The repeal of Obamacare, tax cuts, changes in trade policy — on net these things are not going to alter the longer-term trajectory of the economy," he said. "You need a lot more investment in infrastructure. ... I also think it's important there be further trade liberalization, not less."

In addition to trends in productivity, weak growth in wages may reflect the difficulty workers have asserting their bargaining position in the current environment, Lawson said.

A dramatic decline in unionization in recent decades has left workers less able to bargain with company owners for pay increases. At the same time, globalization has allowed companies to be more mobile than ever before. If labor gets too expensive in one location, companies can just move.

So what does that mean for the Federal Reserve? Gould and other labor-friendly economists see these trends as ample reason for the Federal Reserve to hold off on raising interest rates.

But other analysts see the threat of emerging inflation as a bigger risk, and believe the Fed should act now to raise interest rates to more normal levels.

The central bank raised its benchmark interest rate in March for just the third time since the financial crisis, and it has said it plans two more hikes this year if the economy holds steady. Higher interest rates raise the cost of borrowing and thus tend to slow economic activity. An interest rate that is too low, however, can stoke inflation and speculative bubbles in stocks or the housing market.

The Fed keeps a close watch on wages for two reasons, Sinclair said. If wages go up dramatically, employers end up passing on some of that cost in terms of prices. That translates into inflation, a force the central bank is charged with keeping in check.

Wages also tell the Federal Reserve how many unemployed and underemployed workers are still in the labor market. Once the labor market gets really tight, efforts to stimulate the economy don't translate into job growth anymore — they just raise wages and prices, Sinclair said. That's a signal to the Fed to cut back on the stimulus it provides the economy through lower interest rates.

Sinclair said current market signs are signaling the Fed that the economy still might have substantial room to grow.

"It makes me want to encourage the Fed not to rush, because there doesn't seem to be too much pressure on the wage cost side for employers yet," she said. "Waiting a little longer might allow us to see further improvements for people."

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