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POWERFUL FORCES SEEN RESTRAINING U.S. PAY GROWTH

Economists surveyed by WSJ point to low productivity growth and other factors holding down pace of wage gains

By Ben Leubsdorf
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U.S. wage growth is set to pick up modestly in the coming years, but economists think pay raises are being depressed by powerful forces – sluggish productivity gains, an aging population and overseas competition – that could persist despite low unemployment.

It is one of the lingering mysteries of the economic expansion that began nearly nine years ago: Why has growth in Americans' paychecks remained anemic despite the unemployment rate plunging to its lowest level in 17 years?

Larger raises may be coming after average hourly earnings for private-sector workers rose 2.7 percent in each of the past two years. Private-sector forecasters surveyed in recent days by The Wall Street Journal on average predicted 3 percent earnings growth in 2018, followed by gains of 3.2 percent in 2019 and 3.1 percent in 2020.

"The shift in the anecdotal reports I am hearing on wages has hit a critical mass," said Diane Swonk, chief economist at Grant Thornton. "Employers are taking the trifecta of tight labor markets for workers: signing bonuses, wage gains and poaching."

While those forecasts exceed the pace of recent years, they would still be historically modest gains given economists also on average expect U.S. unemployment will fall below 4 percent by the end of this year and stay there through 2020. When the unemployment rate was last below 4 percent in December 2000, wages for production and nonsupervisory workers rose 4.3 percent on the year, according to Labor Department data.

In theory, low unemployment forces employers to raise pay as they compete to retain employees and hire from a shrinking pool of available workers. The Federal Reserve is gradually raising short-term interest rates to keep inflation in check because many officials think low and falling unemployment puts upward pressure on wages and prices.

But at the same time, other forces may be holding down wage gains.

A majority of the 60 economists surveyed this month by the Journal said three factors are meaningfully holding down readings on wage growth: low productivity growth, demographic changes, and foreign competition and globalization. Other possible explanations, such as hidden slack in the labor market or government regulation, were cited by fewer than half of forecasters.

Gains in labor productivity can allow employers to boost workers' take-home pay, but the recent trend has been historically weak. The aging of the U.S. population may be depressing wage data as highly paid baby boomers retire and are replaced by younger, lower-paid workers. Globalization might put pressure on some U.S. companies to remain competitive with rivals located overseas in low-wage regions.

Those factors represent long-running trends and wouldn't necessarily fade if the economy continued to expand. Still, the tightening labor market should put more upward pressure on wages over time, pushing up against those barriers and perhaps overcoming them to an extent.

"Further job market tightening is likely to begin dominating structural constraints," said Lynn Reaser of Point Loma Nazarene University.

More broadly, the economists surveyed by the Journal expect healthy economic growth this year bolstered by fiscal stimulus including tax cuts, but increasingly worry the economy's performance might disappoint.

Gross domestic product on average was seen rising 2.8 percent in the fourth quarter of 2018 from a year earlier, which would exceed the 2.6 percent growth in 2017. Growth was projected easing to 2.5 percent in 2019 and 2 percent in 2020, a trend similar to recent Congressional Budget Office and Fed forecasts.

Most economists, however, saw better-than-even risk that growth will come in weaker than expected. Some 62 percent said risks were tilted to the downside – the highest share since October 2016, just before the presidential election.

One downside risk mentioned by many economists in recent months: international trade. The potential for escalating disputes between the U.S. and major trading partners such as China has rattled financial markets. Negotiations continue among Canada, Mexico and the U.S. on possible revisions to the North American Free Trade Agreement, which President Donald Trump has criticized; forecasters had previously warned pulling out of Nafta would slow U.S. growth.

Economists this month on average saw a 26 percent chance of the U.S. pulling out of Nafta under the Trump administration, from 29 percent in March and 26 percent last November.

In general, economists remain optimistic about the health of the current expansion. The average probability of a recession in the next 12 months was 15 percent in April's survey, ticking up from the prior month but remaining low.

"Despite all the noise, fundamentals are strong," said Russell Price, senior economist at Ameriprise Financial.

The Journal's survey of 60 business, financial and academic economists was conducted April 6-10. Not every economist answered every question.