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Finally, real wage gains

Lower unemployment, higher minimum wage spur recent wage growth

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By many important indicators, the American economy is soaring. Unemployment in early 1998 fell to its lowest point in 30 years, real wages for most workers are finally on the rise, and even productivity — a broad measure of the efficiency of the labor force — is speeding up. Yet even with these recent gains, the pay of the typical worker in mid-1998 is still not as high as it was in 1989, the year of the last business cycle peak. Moreover, these recent wage gains, dependent upon current tight labor markets, low inflation, and one-time increases in the minimum wage, are unlikely to withstand the inevitable shift in the business cycle.

In other words, recent trends provide little basis for optimism that America has permanently turned the corner on wages.

The good news of 1996-98

Wage growth on an inflation-adjusted basis from 1996 through the first half of 1998 has been both strong and equalizing (see the table on the following page) and far better than in the earlier portion of this business cycle from 1989 to 1996. For example:

- Real wages grew 2.6% per year for the typical (50th percentile) worker, reversing declines of 0.8% per year from 1989 to 1996.
- Real wages grew 4.1% per year for low-wage (20th percentile) male workers and 2.0% per year for the median male workers, indicating a narrowing of the wage gap between middle- and low-wage men. By contrast, male wages at the 20th and 50th percentiles fell about 1% per year in the 1989-96 period.
- While wages fell for low- and middle-wage female workers at an annual rate of 0.2% from 1989 to 1996, they reversed course and grew at annual rates of 2.7% and 2.6% respectively over the last year and a half.
- Wages for high-wage male and female workers also grew relatively quickly in the 1996-98 period, but in both cases wage growth at the 90th percentile was slower than that at the 20th.

Data in this issue brief are drawn from the forthcoming State of Working America 1998-99 *(Cornell University Press 1999), to be released to the press on Labor Day 1998.*

Wage growth in the 1990s

	1989	1996	1998**	Annual change 1989-96	1996-98**	1989-98**
Hourly wages* (1998 dollars)						
All						
90th percentile	$23.72	$23.81	$24.63	0.0	2.3	0.4
50th percentile	11.30	10.71	11.13	-0.8	2.6	-0.2
20th percentile	6.79	6.63	6.99	-0.3	3.6	0.3
Male						
90th percentile	$26.41	$26.14	$27.20	-0.1	2.7	0.3
50th percentile	13.22	12.26	12.63	-1.1	2.0	-0.5
20th percentile	7.82	7.32	7.77	-0.9	4.1	-0.1
Female						
90th percentile	$19.55	$20.59	$21.14	0.7	1.8	0.9
50th percentile	9.66	9.51	9.88	-0.2	2.6	0.3
20th percentile	6.25	6.15	6.40	-0.2	2.7	0.3
Unemployment rates***						
All	5.3	5.4	4.5	0.1	-0.9	-0.8
White	4.5	4.7	3.9	0.2	-0.8	-0.6
Black	11.4	10.5	9.0	-0.9	-1.5	-2.4
Hispanic	8.0	8.9	6.9	0.9	-2.0	-1.1
Young (18-35), minority, HS educated						
Black	15.9	16.3	12.8	0.4	-3.5	-3.1
Hispanic	8.3	9.9	7.9	1.6	-2.0	-0.4
Real minimum wage* (1998 dollars)	$4.39	$4.53	$5.15	0.5	9.0	1.9
Consumer price index*	124.0	156.9	162.4	3.4	2.3	3.2

* Annualized percent changes.
** These columns reflect seasonally adjusted data for the first six months of 1998.
*** Percentage-point changes.

Source: *State of Working America 1998-99* (forthcoming).

This pattern of growth indicates a narrowing of the wage gap between the top and the bottom of the wage scale, an uncharacteristic pattern given inequality's persistent increase over the past two decades. The gap between the top and the middle, however, continues to expand for men.

The other panels in the table show the primary factors responsible for the recent growth spurt of real wages: falling unemployment, the increase in the inflation-adjusted value of the minimum wage, and an unexpected decline in the growth of inflation.

The role of low unemployment

The overall unemployment rate was 4.5% in the first half of 1998, down almost a full percentage point since 1996. Moreover, this 0.9-point decline overall was accompanied by larger declines among groups of workers who are traditionally further down the hiring queue. For example, the unemployment rate for African Americans and Hispanics fell by 1.5 and 2.0 points over this recent period. Looking at a particularly disadvantaged group — young (18-35), minority high school graduates — reveals an even larger decline of 3.5 percentage points for young blacks. Of course, even with these large declines, unemployment rates for young minority workers are still many times higher than the overall rate (e.g., the unemployment rate for young African Americans with a high school degree was more than three times that of whites in each of the years shown). Nevertheless, these recent improvements provide clear evidence that persistently tight labor markets have greatly increased the employment opportunities of the least well-off.

The role of a higher minimum wage

The Congress mandated two $0.90 increases in the federal minimum wage in the 1990s, the first of which was implemented in 1990/91, the second in 1996/97. By 1996 inflation had eroded much of the value of the first increase, but the second increase, which raised the real value of the minimum wage 9% per year over the 1996-98 period, clearly helped to lift wages at the lower end of the wage scale.

The role of lower inflation

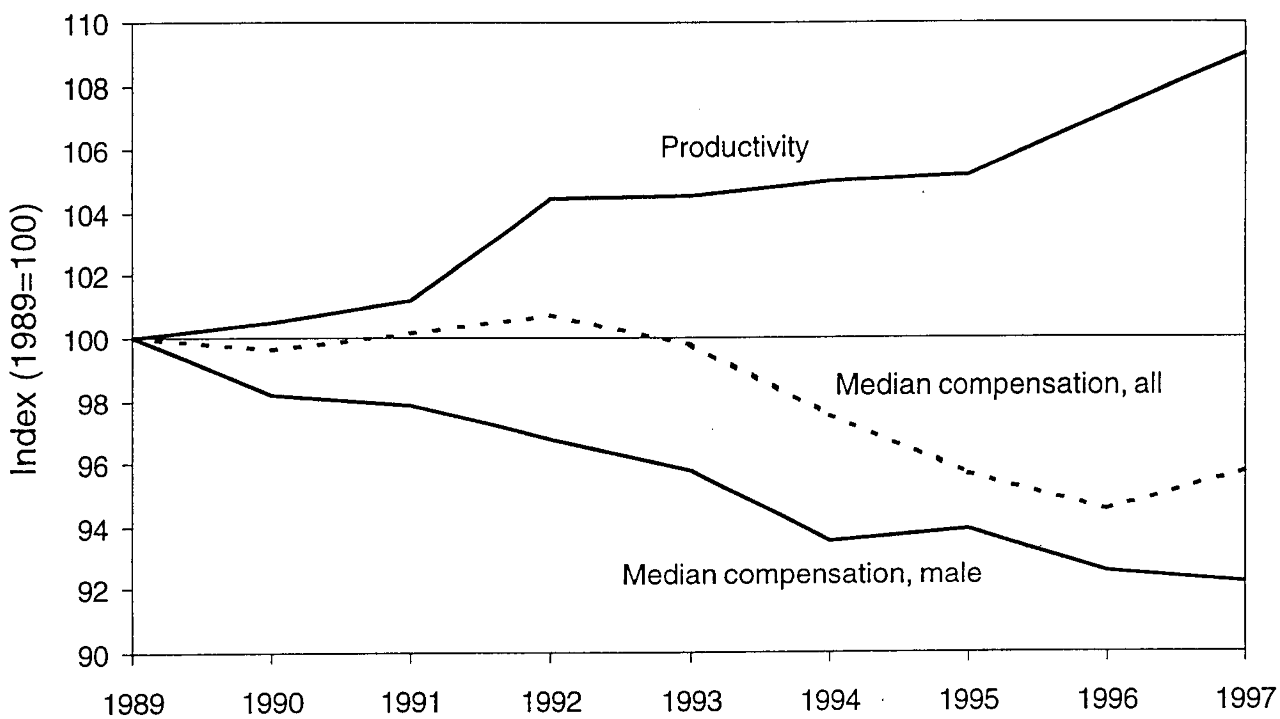
Inflation, as measured by the annualized growth rate of the consumer price index, grew by 3.4% per year in the 1989-96 period but slowed to 2.3% in 1996-98. This unexpected deceleration in inflation means that wage increases given by employers simply to offset anticipated higher inflation have translated into real wage increases. Thus, some of the wage growth over the past year and a half is a result of inflation temporarily growing more slowly than expected. As inflationary expectations begin to conform more closely to the actual path of price growth, real wage growth is likely to slow down.

These recent wage and employment trends are a welcome reversal of the long-term trend toward rising inequality despite overall economic growth. This long-term problem has led numerous analysts to view low unemployment levels as well as increases in the minimum wage as desirable policies that could be implemented without adversely affecting the economy or hurting the workers they are meant to help. As the data in the table show, low unemployment has not led to runaway inflation, nor has the increase in the minimum wage hurt the job prospects of low-wage workers.

But will these positive trends continue? Unfortunately, the fundamental problems that have kept working families from realizing their share of the benefits of economic growth and that have led to widespread wage erosion for most of the past two decades have not been corrected. They have simply been temporarily suppressed by low unemployment and, for low-wage workers, a federally mandated wage increase.

Because of the long-term erosion of the institutions that have historically protected workers from the vicissitudes of market forces, along with the increased adversity of such forces, the typical American worker has less bargaining power than ever before. At the moment, tight labor market are substituting for these eroded protections, but business cycles inevitably come to an end. When unemployment begins to rise, the gains documented above will almost certainly prove to be short lived.

Hourly productivity and compensation growth in the 1990s



Source: *State of Working America 1998-99* (forthcoming).

The bigger picture of the 1989-98 business cycle

Our examination of the past few years provides important insights into the short-term condition of the economy and underscores the importance of low unemployment. But to accurately assess the economy, it is best to examine an entire business cycle (in this case 1989-98) and compare it to trends in other cycles.

From this perspective, the typical worker has lost ground since 1989, the last business cycle peak, and the typical male worker is still well behind his pre-recession wage level. The final column in the table shows the annualized percent change in wages over the 1989-98 period. Despite the growth since 1996, the wage of the median male has fallen 0.5% per year since 1989, representing a decline of $0.59 per hour. Clearly, most of the damage was done in the 1989-96 period, when the median male wage fell 1.1% annually. Strong growth in the recent period has helped low-wage male workers regain much of the ground lost over the 1989-96 period; their wage in the first half of 1998 was only slightly below that of 1989.

The wage of the median female worker, which rose consistently over the 1980s, fell 0.2% per year from 1989 to 1996. The increase over the last 18 months, however, led to a 0.3% annual growth rate over the full period. A similar pattern prevailed for low-wage female workers.

At the top of the wage scale, the wage of the 90th percentile worker grew more quickly for both men and women over the full 1989-98 period than it did for other groups. Thus, despite the equalizing pattern of wage growth in the very recent past, wage inequality has continued to grow for both men and women, as workers at the top of the wage scale have pulled away from both those in the middle and at the bottom.

Adding fringe benefits to these wage data does not brighten the picture. Although the compensation (wages plus benefits) of the median worker is not directly available, assigning the *average* benefit package to the *median* worker in proportional terms (which certainly overstates the typical worker's benefits) reveals that the typical worker actually lost more in terms of compensation than in terms of wages. For example, the inflation-adjusted decline in the median wage for all workers was 3.2% from 1989 to 1997; the fall in median compensation was 4.2% (the most recent data of this type are for 1997).

It is also important to put recent wage gains into the context of the overall growth of the economy. As the accompanying figure shows, productivity grew 9% from 1989 to 1997, while the compensation of the typical worker, and particularly that of the median male worker, actually fell (these data are available only through 1997). Thus, the pay of the typical worker has lagged far behind the capacity of the economy to pay more.

Conclusion

The wage trends of the 1990s, despite dramatic improvements in recent months, have still left many workers behind their pre-recession levels. In this regard, getting back to the level of 1989 serves as a minimal benchmark, but even this measure of success sets a low standard given the higher productivity of the 1990s economy. Certainly the median worker has played a nontrivial role in the 9% increase in productivity over the 1990s, and one might expect his or her compensation to reflect that growth. By this measure, the economy's performance falls short.

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