Fed Not Fazed by Wage Increases

by Allie Collins-Anderson | 14 February, 2019

The Bureau of Labor Statistics' January Employment Situation report showed employment and wage statistics which should spur discussion about policy changes from the Fed. Whether such changes will be put in place is still uncertain, however. According to survey results, "the unemployment rate, at 4.0 percent … edged up in January" and the number of workers "who reported being on temporary layoff increased by 175,000." The BLS states that the recent partial federal government shutdown was partly responsible for these increases.

Perhaps most interestingly, however, average hourly earnings also increased in January – a potential catalyst for future policy changes from the Fed. The BLS reports that "in January, average hourly earnings for all employees on private nonfarm payrolls rose by 3 cents to $27.56, following a 10-cent gain in December." Furthermore, it states that "over the year, average hourly earnings have increased by 85 cents, or 3.2 percent." These wage increases could result in a decision by the Fed to raise the federal funds rate, which in turn would result in higher interest rates.

Increasing wages often have a cyclical effect on the overall economy. On one hand, consumers have more disposable income and therefore more money to spend on goods and services. On the other hand, producers are forced to raise the price of goods and services to offset the cost of paying workers a higher salary. This increase in prices results in higher inflation (the purchasing power of the dollar decreases) – a problem which the Fed corrects by raising interest rates. Higher interest rates provide more incentive to consumers to save money as any investments made will earn more money over time. When consumers save more, they inevitably spend less and therefore the demand for goods decreases. Producers are then forced to decrease prices in order to encourage consumers to buy more—in turn decreasing inflation.

Why then did the Fed announce on January 30 that it would most likely not be raising interest rates? As reported in the Wall Street Journal, Fed Chair, Jerome Powell stated in a press conference that global economic activity has to be factored in when making any decisions about interest rates. Slowdowns in China and Europe, potential risks from Brexit and still uncertain impacts from the recent US government shutdown all have to be considered.

In regard to the government shutdown, it is likely that it had a negative impact on some parts of the economy while others were unaffected. Many government workers who were temporarily unemployed between December 22, 2018 and January 25, 2019 were forced to tighten both consumption and saving during that period. While this may be reflected in a decrease in GDP for the first part of the year, "there were no discernible impacts of the partial federal government shutdown on the estimates of employment, hours, and earnings from the establishment survey."

41 Furthermore, while employment in government agencies decreased during the month, private
42 sector industries saw job growth in January, including "leisure and hospitality, construction,
43 health care, and transportation and warehousing."
44
45 All things considered, the Fed believes there are too many unknowns at the moment to make a
46 decision on interest rates. Even though the BLS report shows increased wages and higher than
47 expected job growth, it is uncertain whether or not spending will increase substantially as a
48 result. If it were to increase enough to create higher inflation, the Fed may decide to raise rates.
49 However, until that happens, there is no immediate need to raise rates—consumers are spending
50 and saving with enough balance at the moment to minimize any potential red flags for the Fed.