Real wages in both Europe and the US remain catastrophically negative. (UBS)

Could a wage-price spiral happen?

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Wage growth can be spun as a terrible inflation threat, or the reason inflation trends are subdued.

Nominal wage growth in most developed economies is higher than is compatible with inflation of around 2%. In the US, the Atlanta Fed wage tracker is showing 6.7% wage growth.

Of course, wages are not labor costs. Fewer workers, working harder, mean that wage cost pressures are a lot lower than the headline wage number. Today's macroeconomic data probably underestimates the productivity gains since the pandemic. Reports of headline pay settlements create a misleading impression of labor costs.

Real wages in both Europe and the US remain catastrophically negative. That suggests that today's labor market structures have not given workers strong pay bargaining power. The most basic goal of an employee negotiating a pay raise is to maintain their standard of living. Employees across the developed world fail to achieve that minimum aim.

If developed economy inflation falls (via weaker demand and squeezed profits), the current level of nominal wage growth is too high for central banks to achieve their inflation targets. However, the extremely negative real wage growth suggests that pay bargaining power is weak, and if inflation falls nominal wage growth will also slow (while turning positive in real terms).

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Important information