ECONOMIC UPDATE

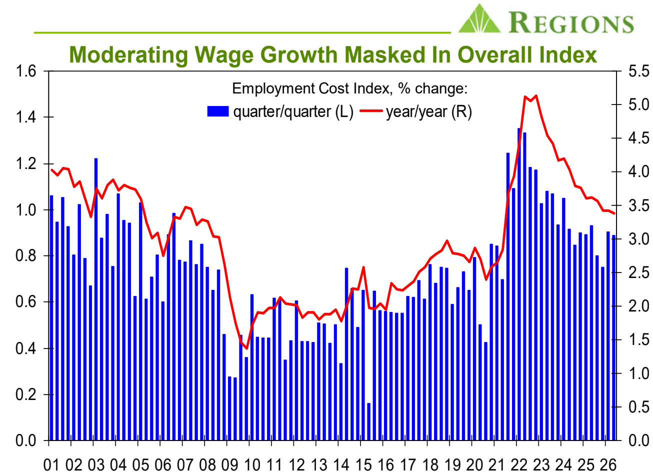
REGIONS

July 31, 2026

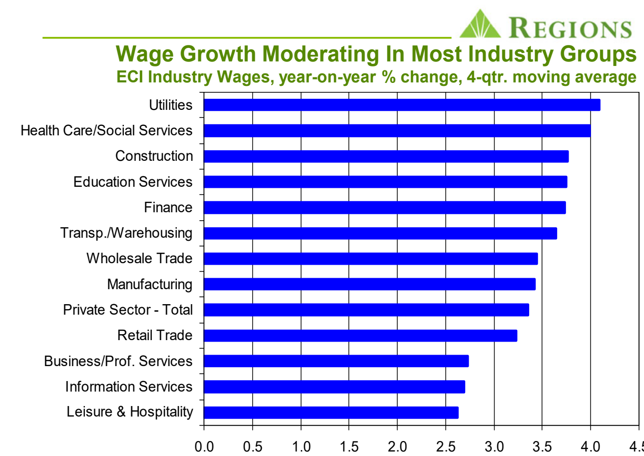
Q2 2026 Employment Cost Index: Bigger Push Coming From Benefit Costs

- The total ECI was up 0.9 percent in Q2 2026, with the wages/salaries component up 0.9 percent and the benefits component up 1.0 percent.
- As of Q2, the total ECI was up 3.4 percent year-on-year, with wage costs up 3.2 percent and benefit costs up 3.8 percent.

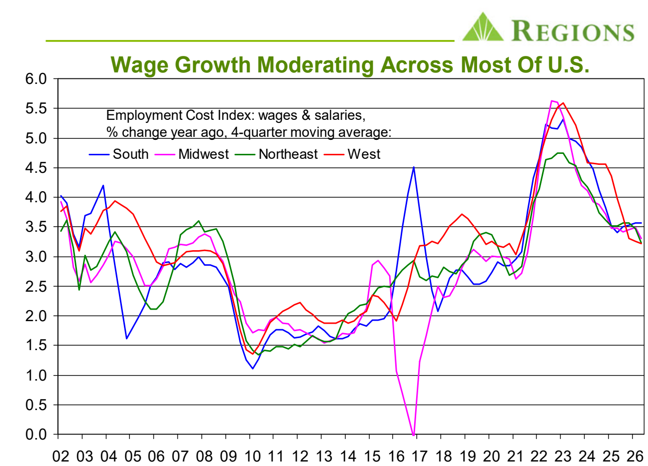
Total compensation costs, as measured by the Employment Cost Index (ECI), rose by 0.9 percent in Q2, above what we (0.7 percent) and the consensus (0.8 percent) expected, with wage costs up 0.9 percent and benefit costs up 1.0 percent. On a year-on-year basis, the total ECI is up 3.4 percent, the wages component is up 3.2 percent, and the benefits component is up 3.8 percent. While growth in both wage costs and benefit costs topped our forecasts, the reality is that wage growth continues to moderate but in terms of total compensation costs, that is being somewhat neutralized by accelerating growth in benefit costs. To that point, at 3.2 percent in Q2, the over-the-year increase in wage costs is the smallest such increase since Q2 2021, or, right at the start of the post-pandemic acceleration in wage growth. In contrast, the 3.8 percent year-on-year increase in the benefit costs component is the largest such increase since Q1 2025. To be sure, wages account for a much higher share of overall labor compensation costs, but that benefit costs are rising at an accelerating pace is acting to counter the ongoing deceleration in wage growth from the perspective of employers. The moderation in wage growth can be seen across industry groups and across geographic regions, with some exceptions that, amongst other factors, reflect labor shortages and stepped-up U.S. energy production. It is also worth noting that, as measured by the ECI, wage growth has fallen short of inflation, and while increased hours worked can provide somewhat of an offset, workers in many industry groups are finding their take-home pay is being stretched thinner and thinner. Granted, some of this reflects the extent to which higher energy costs have pushed overall measures of prices higher, but in many cases wage growth is running below core inflation. While there are other supports for consumer spending, supports from larger income tax refunds and the pool of household saving are becoming less powerful, and we think a meaningful, broadly based, and sustained reacceleration in wage growth is highly unlikely. This will, for many households, be a source of continued unease.



The ECI is one of the three main data series – the others being average hourly earnings from the monthly employment report and unit labor costs from the quarterly labor productivity and costs report – showing trends in labor costs. The ECI tends to get less attention than its two counterparts but to us is the most meaningful of the three series. The ECI is designed to measure changes in total labor costs, for both money wages and salaries and noncash fringe benefits (such as health insurance) and also includes employer-paid taxes such as Social Security and Medicare. One distinction between the wage component of the ECI and the more widely followed average hourly earnings metric is the ECI is not affected by shifts in the composition of employment across industry groups. Instead, the wage component of the ECI effectively measures wage costs for the same jobs over time and the total ECI measures labor costs (i.e., wages and benefits) for the same jobs over time. One drawback of the average hourly earnings metric is that it is skewed by changes in the composition of employment and hence will mask earnings differentials across industry groups, and these distortions have been even more pronounced since the onset of the pandemic.



That construction and health care/social services are posting some of the fastest wage growth amongst private sector industry groups to some extent reflects labor supply constraints that, in part, reflect sterner immigration policies. Industry groups such as landscaping services and household services, which ultimately roll up into the broad business services category, are seeing similar effects but as a share of the overall industry group are not large enough to push wage growth in the business services group higher to the extent seen in construction or health care. The sizable increase in wage costs in transportation/warehousing services from the UPS contract is washing out of the longer-term trends and moderating wage growth over recent quarters is more consistent with recent rounds of job cuts. Information services is another instance in which moderating wage growth has come hand-in-hand with ongoing job cuts. Wage growth is moderating across most regions, with the South appearing an exception. This primarily reflects faster growth in the West South Central sub-region, which includes Louisiana, Oklahoma, and Texas, where faster wage growth in the energy sector is likely propping up the overall average.



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