

Why Wages Are Growing Rapidly Now— And Will Continue to in the Future



In the first half of 2021, wages grew at the fastest pace in over 20 years. The sudden surge is likely to challenge organizations in recruitment, retention, and compensation strategies in the near term—and over the next decade.

Wage growth in the US through 2022 and beyond fits into three distinct phases: 1) strong wage growth in the spring and summer of 2021; 2) moderating wage growth by late 2021 and during 2022; and 3) renewed acceleration of wages in 2023 and beyond, most notably in blue-collar and manual services.

While beneficial for workers, higher wages probably reduced corporate profits and contributed in part to 2021's inflationary environment. Indeed, rapid wage growth might be one of the catalysts that prompts sooner-than-expected tightening of monetary policy (i.e., the Fed's decision about when to taper quantitative easing and increase interest rates).

There is some relief in sight from the employer perspective: wage growth in the final months of 2021 and 2022 should slow as the pandemic's demand-supply mismatches are resolved and more workers reenter the labor market. Wages likely will grow closer to the long-run average of 2.5-3 percent, especially in 2022. However, looking ahead to 2023 and beyond, wage pressures are likely to resurface.

The rapid decline in the working-age population without a bachelor's degree is likely to generate continuous labor shortages of blue-collar and manual services workers. The rate of wage growth in these jobs should be relatively robust in most years until the next recession.

Insights for What's Ahead

Heated wage growth in summer 2021

- **Through the summer of 2021, wages will continue to grow**, especially for blue-collar and manual services jobs as the economy reopens and willingness to work among some is limited.
- Spring of 2021 saw the fastest wage growth in the US in 20 years—and the trend has continued into summer at the time of this publication. According to the second quarter Employment Cost Index report, wages and salaries for private industry workers increased at a 4.3 percent annualized rate for the six-month period ending in June 2021. This was much higher than the growth rate over the past two decades, which has stayed mostly in the 2 to 3 percent range. The acceleration in wages is most noticeable in blue-collar and manual services occupations.
- Faster wage growth could have a significant impact on consumer and producer price inflation, and if higher costs are passed through, this would ultimately affect monetary policy. Indeed, rapid wage growth may prompt sooner-than-expected tightening of monetary policy (i.e., the timing of quantitative easing tapering and interest rate hikes).

Cooling off in late 2021 and 2022

- **Wage growth should slow by late 2021** and into 2022 as demand and supply mismatches are resolved and more workers reenter the labor market. Wages will likely grow closer to the long-run average of 2.5-3 percent, especially in 2022.
- However, another significant wave of coronavirus-related infections and limited school openings for in-person instruction in September could reduce the willingness to work among some unemployed persons and delay the beginning of the wage growth moderation phase beyond the summer of 2021.
- The acceleration in wages for new hires in 2021 could lead to a unique situation where new hires earn more than current employees with more experience. Such inequity could lead to higher labor turnover of more experienced workers who can easily find new jobs at higher wages in this tight labor market.
- Extreme labor shortages driving accelerated wage growth in the first part of 2021 are likely to be over by year-end, as individuals may be more willing to return to the workplace. The result would be fewer recruiting and retention difficulties and less upward pressures on wages for new hires.
- Overall, wage growth in 2022 will be lower than in 2021 but still in line with prepandemic rates of about 2.5-3 percent.
- Another source of wage growth in late 2021 and 2022 could be inflation. After being a non-issue in wage determination for several decades, strong inflation in 2021, and perhaps 2022 (if household's long-term expectations rise), is likely to push wages higher. In a more extreme and less likely scenario, high inflation and severe labor shortages could lead to a wage-price spiral, where higher prices and wages feed each other, leading to faster growth in both.

Demographics drive wages up again in 2023 and beyond

- **Wages will grow rapidly in some occupations in 2023 and onward**, most notably in blue-collar and manual services because of a shrinking working-age population and low unemployment rates, with some offset from increased automation.
- In 2023 and beyond, wage growth is likely to be stronger than in the decade prior to the pandemic because of a shrinking working-age population and low unemployment rates.
- Historically strong job growth from 2021 to 2022 is likely to significantly lower the unemployment rate, and if history is any guide, this trend is likely to continue until the next recession, which could occur five to ten years from now.
- How rapidly employment grows and the unemployment rate drops depends partly on the rate of automation. Ultimately, more automation will reduce the demand for labor and delay a decline in the unemployment rate.
- The projected rapid decline in the US working-age population without a bachelor's degree in the coming decade is likely to lead to a shortage of blue-collar and manual services workers, accelerating wages in those sectors as early as 2023.

- The shift to remote work will significantly impact not only how we work but also how wage trends develop in the near term. Employers operating in expensive labor markets may be able to lower overall labor costs by hiring more workers in cheaper US labor markets or abroad. Moreover, many companies are likely to have flexible wage structures allowing differentiation in compensation across regions.

Definitions

Professional and office occupations include management, business, financial, and professional jobs that generally require at least a bachelor's degree, as well as jobs that require less education, such as sales, office, and administrative support occupations.

Blue-collar and manual services occupations include construction, extraction, farming, installation, maintenance, repair, production, transportation, and material moving jobs, as well as those in manual services such as health care support, protective services, food preparation and serving, building and grounds cleaning, and personal care.

Strong Outlook for Wage Growth Over the Next 5-10 Years

Projected wage growth is expected to be robust over much of the next decade, above 3 percent. However, it will vary within this range in the short, medium, and long term. Demographics, automation, the shift to remote work, and the behaviors of firms and workers will influence wage levels.

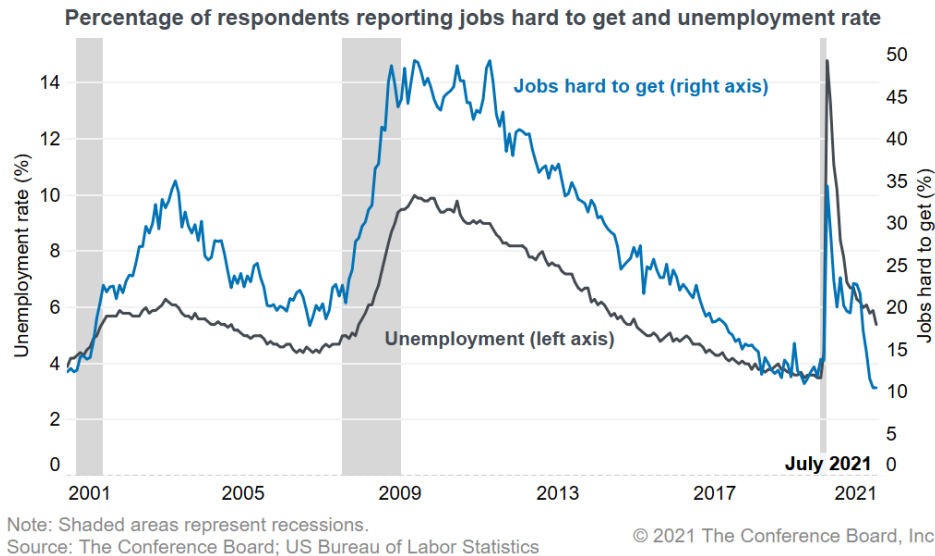
The trajectory for wage growth could be broken into three time horizons: 1) strong wage growth in the spring and summer of 2021, especially for blue-collar and manual services jobs as the economy reopens; 2) moderating wage growth by late 2021 and during 2022 as pandemic-induced demand and supply mismatches resolve; and 3) renewed acceleration of wages in 2023 and beyond, most notably in blue-collar and manual services because of a shrinking working-age population and low unemployment rates.

Historically high wage growth in the spring and summer of 2021

Typically, as in past recessions, and during periods of high unemployment rates, wage growth tends to slow. But that was not the case during the pandemic-induced recession. While unemployment rates are still presently elevated (5.4 percent in July 2021), wages have been growing much faster than at any other time in recent decades. This is because the US labor market is much tighter than expected. Consumers who report that “jobs are hard to get” is at a historic low of roughly 11 percent despite an unemployment rate still well above prepandemic levels.

Figure 1

Despite high unemployment, only 11 percent of consumers say it's hard to find a job



Labor markets are currently tight because of the unusual dynamics of the pandemic. The combination of a surge in demand for workers and stagnant labor supply created historic recruiting difficulties which began in March 2021. Usually, businesses form and expand gradually during periods of economic growth, creating a steady demand for workers. But now, as the in-person economy reopens all at once, the demand for workers is surging. Business activity in several industries, especially in the entertainment sector, more than doubled in a matter of months, an event with almost no historical precedent.

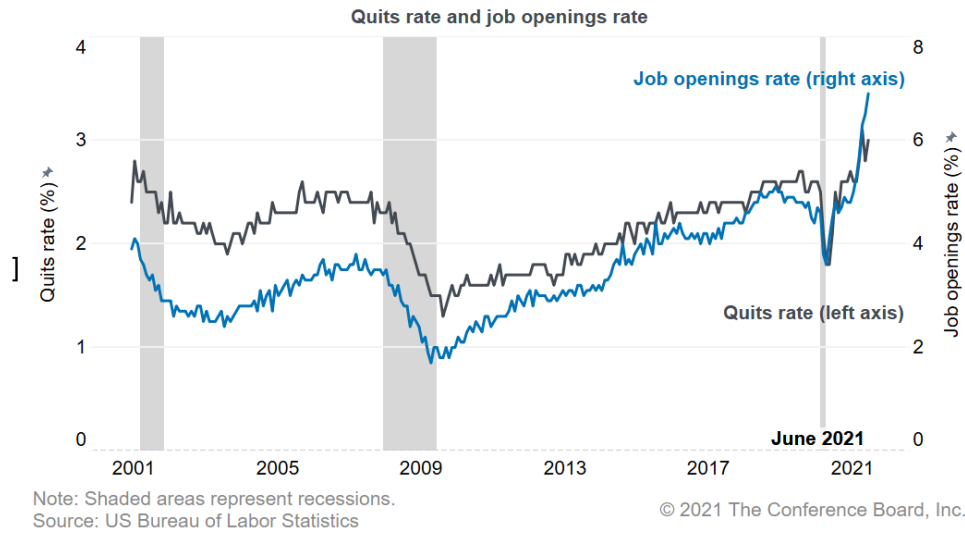
On the supply side, many working-age adults have been slow to reenter the workforce because of lingering factors associated with the pandemic (e.g., high federal unemployment benefits, fear of getting infected, the need to take care of young children during school closures/remote learning, and elder care) which have reduced the incentive to rejoin the labor force for some.

The Delta and other COVID-19 variants are causing a significant wave of infections during the summer, which is likely to continue into the fall and could limit the willingness to work due to the fear of getting infected. While not the most likely scenario, the spread of the virus may lead to limited school openings in September for in-person instruction and reduce the labor participation of parents. These developments may prolong this phase of rapid wage growth beyond the summer.

Indeed, these dynamics are evident in soundings from employers who cite that qualified labor is hard to find. According to the National Federation of Independent Business (NFIB) July survey, 49 percent of respondents—the highest rate in the 47-year history of the survey—had job openings they were unable to fill. In addition, the share of workers voluntarily quitting their jobs, usually for another job, was at a historic high, according to the Bureau of Labor Statistics Job Openings and Labor Turnover Survey.

Figure 2

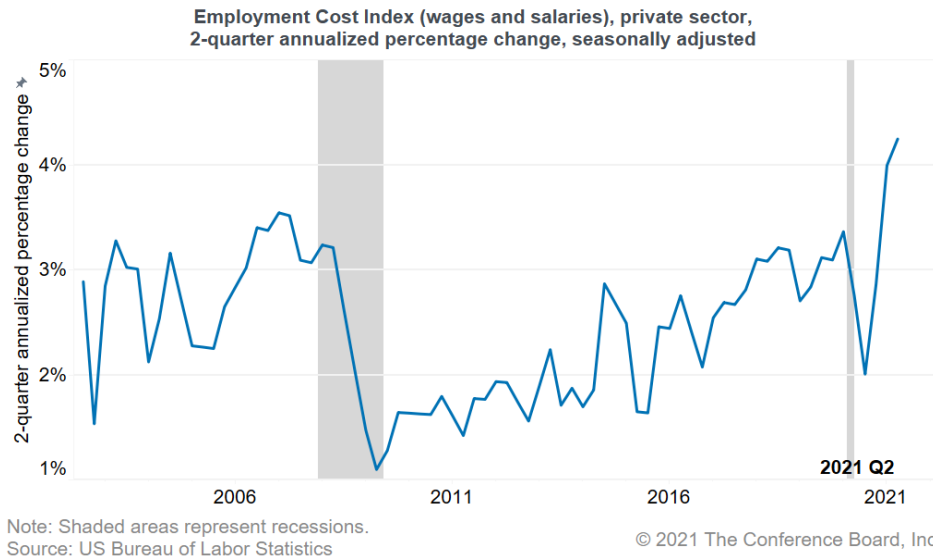
Number of workers quitting reaches historic high



When businesses have difficulty recruiting and retaining workers, wage acceleration generally follows. According to the second quarter Employment Cost Index report from the Bureau of Labor Statistics, wages and salaries for private industry workers increased at a rate of 4.3 percent (annualized) for the six-month period ending June 2021, the fastest rate in over 20 years.

Figure 3

Workers in private industry see fastest pay increases in 20 years



Recruiting and retention difficulties—and consequently upward wage pressures—are more pronounced in low-paid jobs, especially in blue-collar and manual services jobs. This is true for three reasons:

1. From the labor supply side, elevated unemployment benefits impact the willingness of low-paid workers to return to work. These benefits make up a large share of the potential salary low-paid workers would be paid if they worked. For some low-paid workers the additional benefits sum to more than 100 percent of available wages, thus reducing the urgency of finding a job.
2. In addition, low-paid workers are more likely to have in-person jobs with a high risk of infection, further reducing willingness to work for some.
3. From the labor demand side, a disproportionately large share of low-paid jobs are in the rapidly reopening in-person services industries, where recruiting difficulties are especially significant.

Consistent with these factors, much of the acceleration in wage growth comes from blue-collar and manual services occupations, while wage growth for management and professional occupations remains in line with prepandemic rates (Figure 4). Pay in the leisure and hospitality sector grew by 23.7 percent annually in the six months from January to July 2021 (Figure 5).

Figure 4

Wage increases are highest for blue collar and manual services jobs

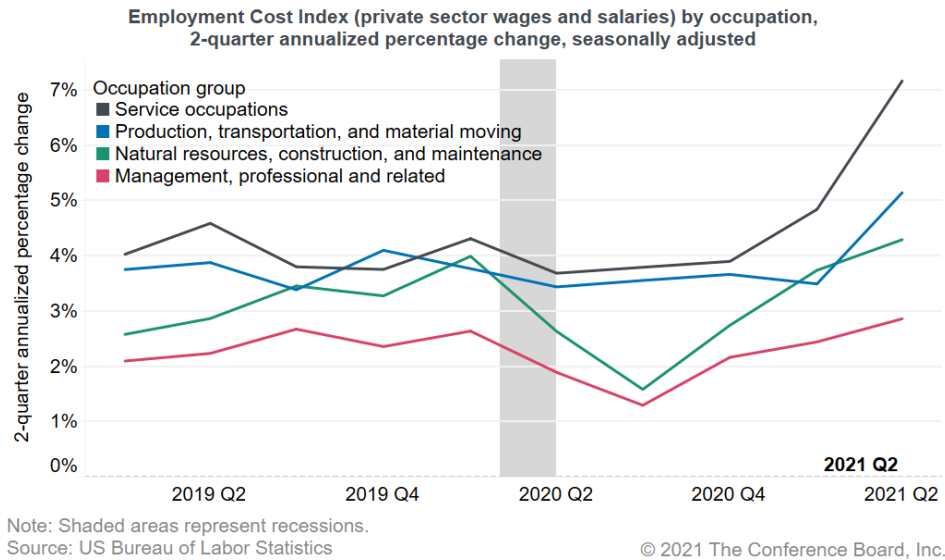
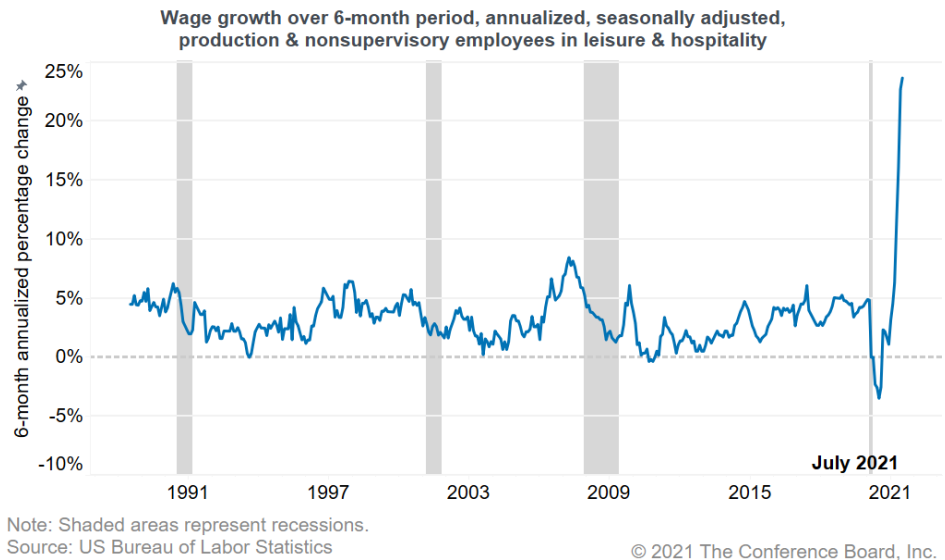


Figure 5

Wage growth in the leisure and hospitality sector has spiked



The acceleration in wages could have a significant impact on inflation and monetary policy. In recent months, inflation has been growing at the fastest rate in decades, probably mostly due to nonwage factors, such as a rapid rise in commodity, computer chips, and auto prices, some of which are [expected](#) to be [temporary](#).

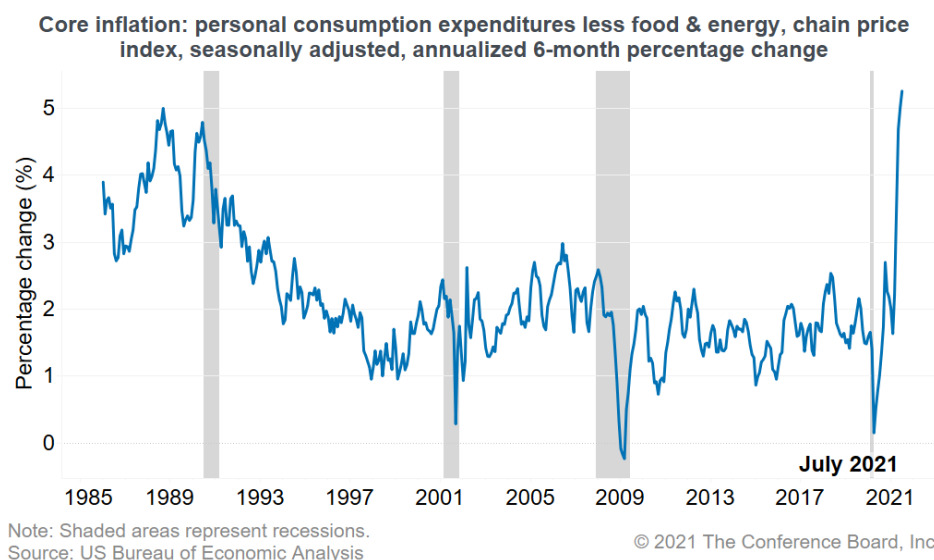
Strong inflation and severe labor shortages could lead to a [wage-price spiral](#), which used to be a central element of macroeconomics, but lost most of its importance in recent decades amid nearly 40 years of low inflation. In a wage-price spiral environment, characterized by labor shortages and rising inflation, workers demand and receive higher wages. Employers react by passing on the higher wage costs to consumers, pushing up the prices of goods

and services sold to consumers. This in turn leads to further wage demands by workers, and the process repeats itself again and again, potentially leading to rapid inflation and wage growth. The likelihood of a significant wage-price spiral is low, but at the same time, it is higher than at any other time in recent decades, when inflation was a nonissue in wage determination.

At the moment, the Federal Reserve views the latest inflationary pressures as temporary and has said it is [unlikely to raise interest rates in the short-run](#). Still, if inflation remains more persistent the Fed may begin raising rates sooner than what is currently expected and slow down economic growth, especially in sectors sensitive to interest rate changes, like housing. At present, the consensus forecast for Fed Funds tightening is Q2 2023 with tapering coming beforehand (see [The Conference Board Economic Forecast for the US Economy](#)).

Figure 6

Recent months show fastest rate of core inflation in decades



Moderating but Still Robust Wage Growth in Late 2021 and 2022

Labor shortages should ease toward the end of 2021, leading to slower wage growth in 2022—closer to 3 percent. However, other factors are likely to keep wage growth from dropping below the prepandemic rate of about 3 percent during that time.

In the fourth quarter of 2021, some pandemic-related supply constraints will likely loosen. Elevated Federal unemployment benefits will expire by September. And schools are likely to return to normal in-person attendance, reducing childcare challenges. Less severe labor shortages are expected to lower wage growth for new hires during 2022.

Still, the rapid wage growth of new hires in 2021 could lead to significant salary compression—when the pay of one employee is very close to the pay of more experienced ones. The premium for experience shrinks or even turns negative—and more experienced

workers may feel their pay advantage is no longer significant. Such salary compression could lead to higher labor turnover of more experienced workers who might easily find new jobs at higher wages in a tight labor market. In return, this could lead to higher average raises as employers attempt to keep the more experienced workers in their organizations. In fact, our latest survey results show that salary increase budgets may increase (for more about the survey, see box below).

The Salary Increase Budget Survey

Since 1985, The Conference Board has surveyed compensation executives about two main components of compensation: salary increase budgets and salary structure movements. The Conference Board fielded the 2021 survey between April 21 and May 14, 2021, and requested data for four employment categories: nonexempt hourly (nonunion), nonexempt salaried, exempt, and executive. For more details on the results as well as breakdowns by company size and industry, see [US Salary Increase Budgets for 2022](#).

Salary increase budget refers to the pool of money an organization dedicates to salary increases for the coming year. It is strongly related to the typical raise a worker would receive in a given year. It is generally represented as a percentage of current payroll. The salary increase budget is calculated using a predetermined total percentage of base pay (excluding overtime, bonuses, etc.) and used for awarding merit or performance increases to individual employees. It may also be used for pay adjustments such as promotional increases.

Salary structure movement or adjustment refers to the changes (usually annual) to the salary structure of a compensation program. Organizations make these adjustments to the minimums, midpoints, and maximums of their pay ranges to account for changes in the cost of living and salary markets within a given industry.

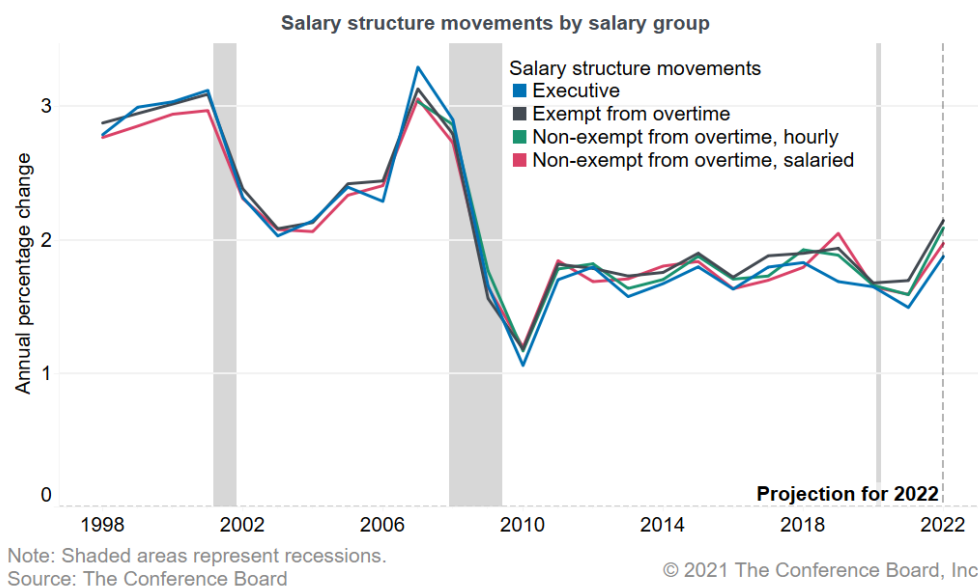
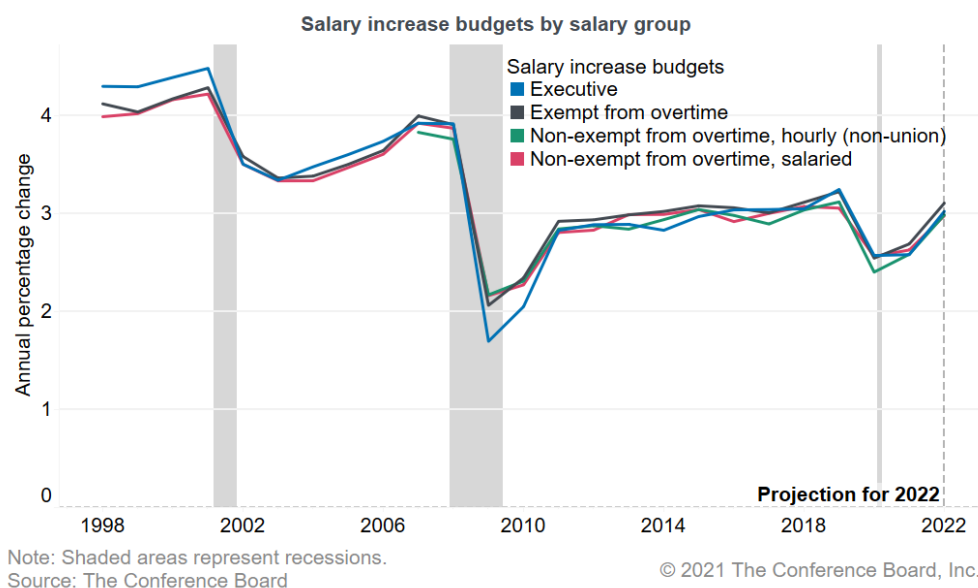
Outlook for 2022

According to [The Conference Board US Salary Increase Budget survey for 2022](#), salary increase budgets and salary structure adjustments were lower in 2020 and 2021 than in the years before the pandemic. At the same time, organizations estimate budgets and pay adjustments for 2022 will be higher and may return to prepandemic rates.

Almost all the responses to the survey arrived in April and early May. Since then, the rapid acceleration in wages and inflation has become more apparent. And as discussed above, the problem of salary compression has become more acute. Therefore, salary increase budgets for 2022 may end up being even larger in 2022 than organizations estimated in the survey.

Figure 7

Salary increase budgets and structure adjustments were low in 2020-2021 but will recover in 2022



Demographics Will Drive Wages Up Again in 2023 and Beyond

Demographic factors are likely to cause renewed upward wage pressures in key sectors in 2023 and beyond. The projected rapid decline in the US working-age population without a bachelor's degree in the coming decade is likely to lead to a shortage of blue-collar and manual services workers, accelerating wages in those sectors as early as 2023 and until the next recession, which could occur five to ten years from now.

In the current expansion, wage pressures due to low unemployment rates are likely to begin much more quickly than in most other expansions. Typically, it takes about four to seven years for unemployment to return to its natural rate, measured from the beginning of a recession. This time, this process is likely to be much faster: unemployment will most likely return to its natural rate, estimated at 4.5 percent, during 2022, about two years after the beginning of the recession. By 2023, the unemployment rate is likely to be below four percent, and the US labor market will again be very tight.

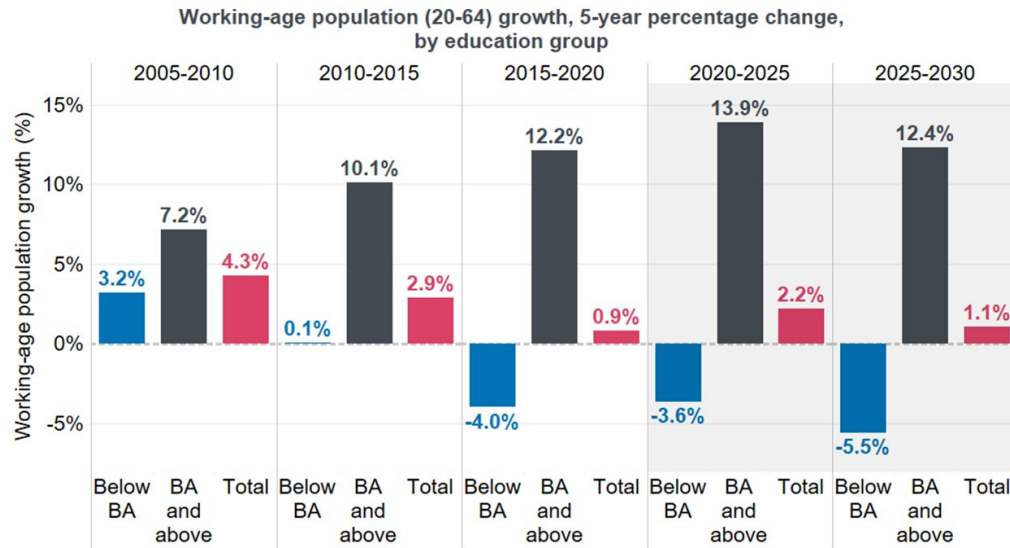
How rapidly employment grows, and the unemployment rate drops, partly depends on the rate of automation. Ultimately, more automation will reduce the demand for labor and slow the decline in the unemployment rate.

The downward pressure on the unemployment rate is likely to be stronger than usual because for the first time in US history, the working-age population is declining as the sizable Baby-Boomer generation is retiring.

Tightening labor markets and faster wage growth are likely to be more notable in blue-collar and manual services jobs due to trends in educational attainment. The share of new labor market entrants with college degrees is higher than the share of retirees with a college degree. The number of working-age people with a bachelor's degree is solidly increasing by about 2 percent annually. On the flip side, the population without a bachelor's degree, who work predominantly in blue-collar and manual services jobs, is shrinking. On top of that, the labor force participation of young men without a college degree, who comprise of a large share of blue-collar occupations in industries such as construction and transportation, is significantly declining over time.

Figure 8

The working-age population without a bachelor's degree is expected to shrink in the coming decade



Source: The Conference Board calculations using data from US Census Bureau and IPUMS-ACS, University of Minnesota

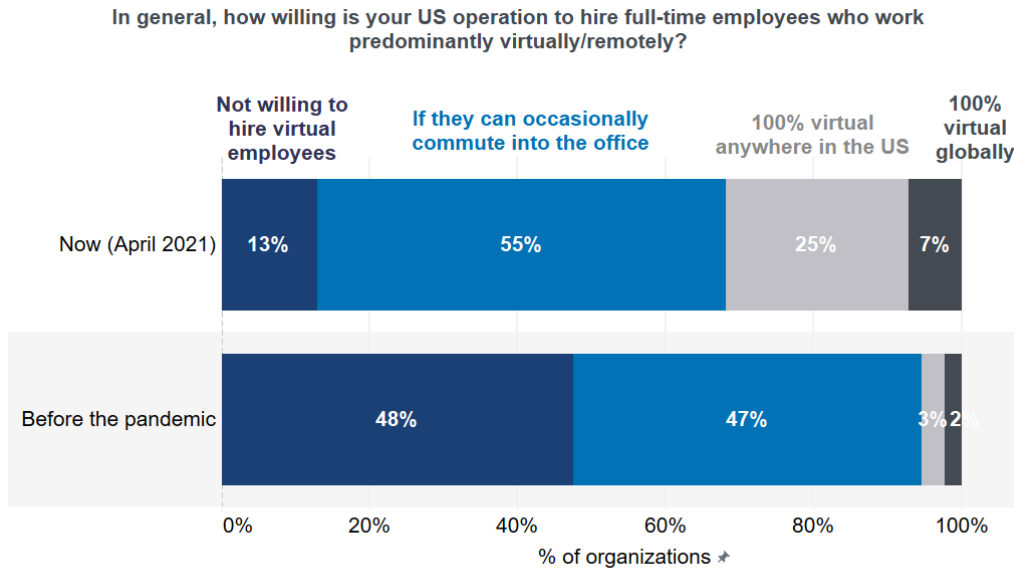
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The Impact of the Shift to Remote Work on Wages

Remote work's disinflationary effect may [partly offset](#) upward wage pressures. The shift to remote work provides an opportunity for firms to recruit candidates who were previously out of reach, at a potentially lower cost. In an [April 2021 survey of 231 HR leaders](#), 87 percent of respondents said they were willing to hire remote workers compared to just 48 percent before the pandemic. Moreover, some surveyed organizations were willing to hire 100 percent virtual employees anywhere in the United States (25 percent) or globally (7 percent), compared to a combined 5 percent before the pandemic (Figure 9, next page).

Figure 9

The pandemic changed hiring: most organizations are now willing to hire remote workers



Source: The Conference Board

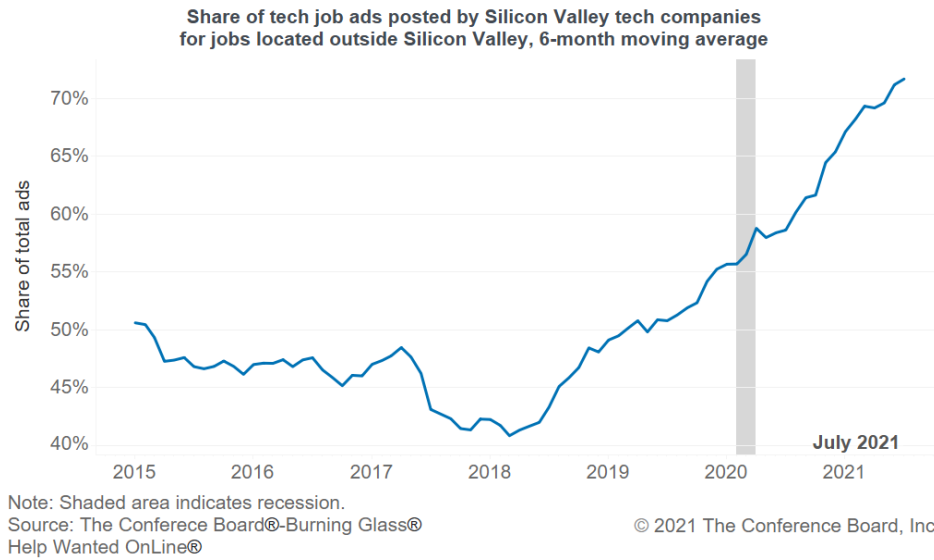
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The willingness to hire remote workers has three potential implications for wages:

1. Employers can now shift some of their payroll to cheaper labor markets, thus reducing overall labor costs. For example, the share of tech online job ads for Silicon Valley tech companies for jobs located in other metro areas has [increased significantly](#). This trend began in 2019 and accelerated in 2020 because of the pandemic and the increase in remote work opportunities. Over 65 percent of these job ads are now being posted in metro areas outside of Silicon Valley (Figure 10, next page).
2. Employees moving from high wage locations to lower wage locations may face downward adjustments to wages. Thus far, anecdotal evidence suggests that few compensation adjustments have been made in such situations, but more employers may consider making such adjustments in the future.
3. Anecdotally, companies that were firmly committed to “national” structures as part of their strategy are now more willing to consider variations by geography.

Figure 10

Silicon Valley employers are hiring more tech talent in other metro areas



Concluding Thoughts

Organizations should expect ongoing wage pressures in the coming years. While the current, historic wage burst is temporary, a tight labor market in blue-collar and manual services occupations will be the norm until the next recession because of a rapid decline in the supply of workers for these jobs. The tight labor market is likely to generate more automation and calls for increased immigration, which could partly offset the demographic squeeze. Business leaders will have to adapt their compensation strategies through the different phases of recruitment and retention difficulties over the course of the next decade.

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Related Resources

[The Conference Board Labor Markets Institute](#)

[The Conference Board Labor Markets Charts Hub](#)

[US Salary Increase Budgets for 2022](#)

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