



Wage-price spiral avoided... for now

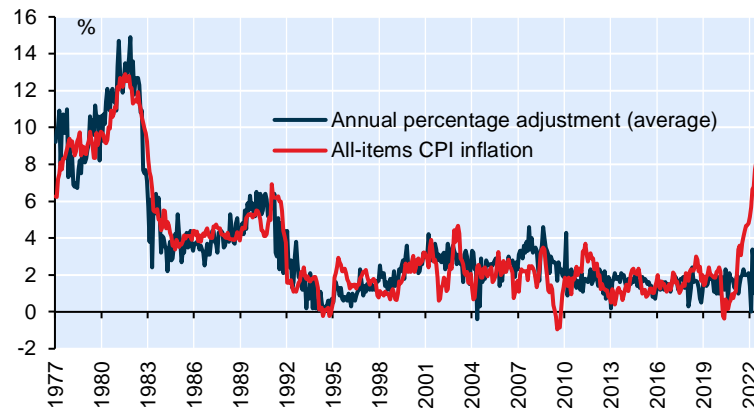
By Taylor Schleich & Warren Lovely

Inflation sucks. Ask any consumer, business or central banker. Nobody wants to see their cost of living/doing business violently increase. Unfortunately, that's the reality for most of the world and, based on the U.S. CPI report yesterday, getting relief on price pressures is proving hard to come by. The worry for central bankers, of course, is that high inflation becomes entrenched. Employees demand higher wages to compensate for higher costs of living; businesses raise prices to compensate for higher labour costs and the dreaded wage-price spiral sets in. You may have seen headlines last week regarding BC's largest public sector union (BCGEU) reaching an agreement with the province that will see employee pay rise by double digits (between 11.2% and 13.5%) over the next three years. You don't need to be a math whiz to see that the annual average is well above the Bank of Canada's mandated 2% inflation target. This development is hardly welcome news for monetary policymakers. Should this be used as the measuring stick for other collective bargaining agreements (there were roughly 5 million Canadians in a union and/or covered by a CBA in 2021), it could be a nascent sign of higher/stickier/stubbornly high wage growth, and ultimately, inflation.

But we try to avoid using anecdotal evidence to guide our outlook. Stepping back and looking at the broader picture, it's clear that higher inflation hadn't significantly affected Canadian union wage settlements, at least through July (the most recent data). Indeed, of the 19 'major' agreements signed through the first seven months of the year (covering 144K employees), the average annual wage adjustment was *less than* 2%. Hardly the stuff of central banking nightmares. But certainly, the longer inflation deviates from the previously ingrained low and stable level, the more pressure we'd expect to see on negotiated wage increases. As one would assume, the average wage adjustment has followed very closely to the rate of all-items inflation over the past five decades—including through the inflationary 1970s and 1980s. (Chart 1). In fact, you won't find a larger deviation between inflation and negotiated pay raises than you will right now (Chart 2). Will there be some catch-up in future negotiations, like we saw in the case of BCGEU? Probably. Workers would surely like to make back some of the *real* pay cut they've taken over the past year. For the Bank of Canada, it underscores the importance of quickly returning inflation back to its mandated target and means that in the near term, the BoC may tolerate (invite?) some employment weakness to the extent it opens up labour market slack and limits wage pressures. For now, the wage-price spiral has been avoided, and we do expect inflation to subside relatively quickly as we outline in our [Monthly Economic Monitor](#). Nonetheless, we imagine headlines like those of last week are presumably unsettling for a central bank already on edge, adding to risk that the BoC may have to move further into restrictive territory.

Chart 1: Wage settlements and inflation moved in lockstep...

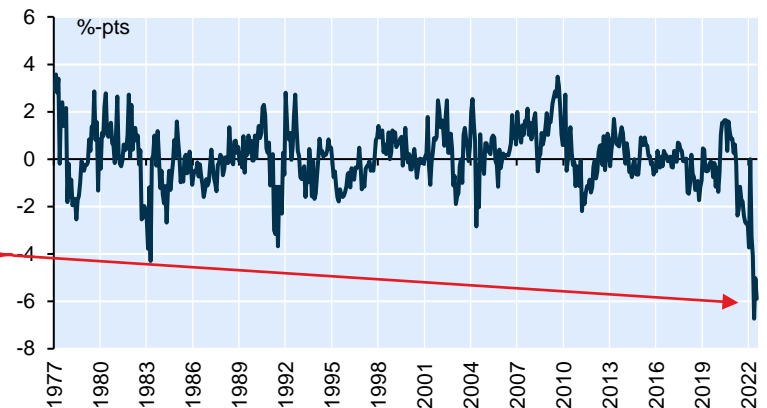
Average annual percentage wage adjustment and CPI inflation since 1977



Source: NBF, StatCan | Note: Includes 'major' settlements only (covering 500+ workers)

Chart 2: ... until this recent inflationary surge

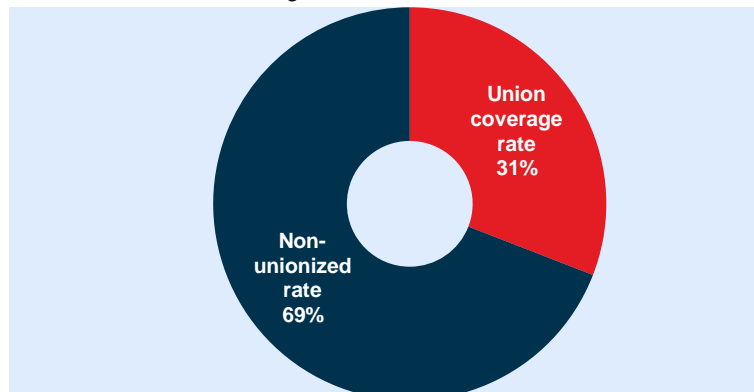
Average annual percentage wage adjustment less CPI inflation since 1977



Source: NBF, StatCan | Note: Includes 'major' settlements only (covering 500+ workers)

Chart 3: Unionized workers a decent share of labour market

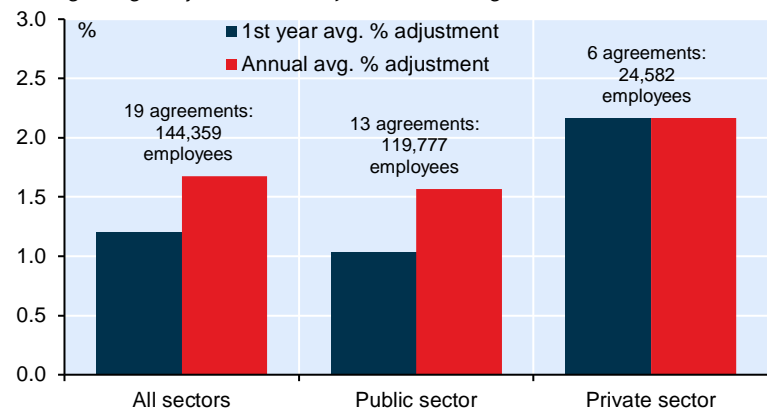
Union and non-union coverage rates in Canada: 2021



Source: NBF, StatCan | Note: Union coverage rate reflects employees who are members of a union and/or covered by a collective agreement as a percentage of all employees.

Chart 4: Breaking down 'major' 2022 wage settlements

Average wage adjustments: first year and over agreement duration



Source: NBF, StatCan | Note: Includes 'major' settlements only (covering 500+ workers)



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