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Eurozone wage growth drops drastically, paving the way for a September cut

The decline in eurozone negotiated wages from 4.7% to 3.6% in the second quarter was more than expected. While there could still be upside surprises to wage growth later in the year, today's wage growth reading makes a September cut by 25bp even more likely

While economic activity has remained sluggish and forecasts have moved in the right direction, the European Central Bank has remained uncomfortable with cutting interest rates while wage growth is elevated. Today's drop will bring some relief for those looking for a gradual cutting cycle as the 3.6% year-on-year negotiated wage growth is more in line with a benign inflation outlook in the medium term.

However, it has to be said that wage growth is still too high for the 2% inflation target given weak productivity growth. But forward-looking indicators do still show moderating wage growth over time as more purchasing power is recouped and economic activity is expected to remain moderate. With some productivity pickup to be expected, wage pressures on inflation in the medium term should ease further.

Still, the road to wage moderation could be bumpy and the second half of 2024 could still bring some upside surprises as unions – most notably in Germany – continue high wage demands at the start of negotiations. While that is great for consumers and would lift the economic outlook somewhat, it could potentially be a curveball for the ECB later in the year.

But for September, a barrier to another cut seems to have been lifted. ECB President Christine Lagarde already emphasised satisfaction with wage growth expectations and the fact that profits have been absorbing higher wage growth. With today's numbers showing a drop in wage growth, expectations of a September 25bp cut are growing increasingly firm.

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