

Recent trends in wages

Philip Smith

For the first time in several years, workers have seen their earnings rise more rapidly than consumer prices. Wage and salary increases gained momentum in 1988 and 1989, after several years of slow growth, and this trend continued in the first half of 1990.

Remembering the inflationary spiral of the 1970s and early 1980s, when annual wage and price increases reached double digits, policy analysts have viewed the situation with some concern. Particularly worrisome are the effects of larger wage increases on unit labour costs and, consequently, on the international competitiveness of Canadian business. [\(1\)](#) This pickup in wages, combined with other factors, led to a tightening of monetary policy. Recently, some commentators have even suggested that the government consider reinstating a form of incomes policy, similar to the "Anti-Inflation Program" of 1976-78 or the "6 and 5 Program" of 1982-83, to deal with what they see as a problem. [\(2\)](#)

This study addresses three topics related to the recent pickup in wage inflation. It begins with a quick review of the available data sources on worker compensation and considers their suitability as measures of labour costs in the Canadian economy. Next, it describes a comparatively new fixed-weight earnings data set, derived from an already available source, and explains why these new data are superior for gauging the cost of labour as a factor of production of goods and services. Finally, the study examines the recent acceleration in wage rates, using the new data set.

Measures of labour compensation

The ideal source of data on the price of labour would be a broadly based survey of total labour compensation for well-defined occupations in specific industries and geographic regions. Unfortunately, no such source is currently available in Canada, [\(3\)](#) although the U.S. Employment Cost Index provides an excellent model for such a survey. [\(4\)](#) In Canada, aggregate wage changes must be studied indirectly, using time series data which, although related, are less than ideal. The available data on labour compensation come chiefly from three sources:

- Labour Canada's data on negotiated increases in base rates in collective agreements;
- Statistics Canada's estimates of wages, salaries and supplementary labour income;
- Statistics Canada's Survey of Employment, Payrolls and Hours (SEPH).

The first source, Labour Canada's compilations from collective agreements, provides reliable data on changes in base wage rates. These changes are calculated from labour contracts and then aggregated using employment weights. The data present an accurate overall picture of wage rate changes within their domain and are available on a consistent basis over a long period. However, these data are incomplete since they apply only to unionized workers and, within that group, only to workers covered by major collective agreements involving 500 or more employees. The tabulations use the contract base wage rate exclusively, that is, the wage applying to the lowest paid classification for workers in the bargaining unit. Contracts containing escalator or cost-of-living allowance clauses (COLAs) are valued initially using specified forecast inflation rates and are revised subsequently to reflect the actual inflation experience. The effective wage increase is calculated as a compound annual average rate over the life of the contract.

The second source, the estimates of wages, salaries and supplementary labour income in the national accounts, is based primarily on income tax records. At the end of the calendar year, all employers are required to submit T4 forms to Revenue Canada-Taxation. These forms provide information on company payrolls and personal income tax deductions that were remitted from employees regularly through the year. Quarterly and monthly estimates of labour income are derived by distributing and projecting the annual tax data with related series, most of which originate in SEPH and the Labour Force Survey. The labour income estimates provide comprehensive information on employment compensation but no information on actual wage rates. Dividing labour income by employment estimates yields another indicator of the overall trend in wage rates which, although comprehensive, must be interpreted very carefully. The chief difficulty with this indicator is that its movements can be dominated by the effects of compositional changes within and between industries, regions and occupational groups, between straight-time and overtime work, and between different kinds of labour compensation. ⁽⁵⁾ (See [*Average hourly earnings from SEPH.*](#))

The last source of labour compensation data is SEPH. This monthly survey of employers is designed to measure the levels and month-to-month changes in employment, paid hours and earnings. SEPH data are available from March 1983 and at detailed industrial and geographic levels. All industries are covered by SEPH except agriculture; fishing and trapping; private household services; religious organizations; and military services. SEPH questionnaires are mailed each month to all large reporting units and to a sample of the smaller units. Overall, about 70,000 units are surveyed out of a universe of 700,000. ⁽⁶⁾

Although SEPH does not collect data on actual wage rates, the information it gathers on employment, hours worked and payrolls can be used to derive measures of average weekly and hourly earnings. However, while earnings measures of this type are closely associated with wage rates, they are imperfect indicators of total labour compensation for two reasons. First, they exclude many compensation elements that are not directly reflected in the payrolls of firms. Benefits such as employer-financed health plans (for example, dental plans), pension funds and severance pay fall into this category. Second, average

earnings measures are subject to compositional change effects that are potentially misleading.

The last problem can be partially corrected by using a fixed-weight aggregation of average earnings. The next part of this study describes a set of SEPH-based fixed-weight earnings statistics of this kind; these data are the main source of information used in the final part of this article.

Fixed-weight average hourly earnings

A set of fixed-weight average hourly earnings (AHE) series has been constructed to deal with the problem of changes in the composition of employment. (7) These series are computed from the AHE data, excluding overtime payments. Overtime compensation is omitted because it is an important source of compositional change in some industries. Salaried as well as hourly-paid employees are included, with the assumption that the former work their "standard workweek". (8)

The fixed weights for the new series are calculated using SEPH employee paid hours data from the 1987 calendar year (the base year for this series). Separate weights are applied for 258 three-digit industry categories as defined in the 1970 Standard Industrial Classification. (9) The fixed-weight series are therefore unaffected by shifts in employment composition among these industries. Fixed weights are also applied separately within each of the provinces and territories, so that differential employment growth rates among these regions will not be a source of compositional variation in the fixed-weight series for Canada.

Finally, fixed weights are also used for employees paid by the hour and salaried employees. These two types of labour can be interpreted as very broad occupational classifications (similar to production and non-production workers). (10) Significant weight shifts between these two categories could occur over a full business cycle. For example, employers may retain highly qualified salaried workers during recessions in order to avoid delays when work activity recovers. The remaining "other" employee category reported by SEPH is excluded from the fixed-weight series. This category includes persons paid solely by commissions, piece rates, mileage allowances and similar remuneration and accounts for about 7% of total employment.

The limitations of the fixed-weight series must certainly be recognized. First, these series are not comprehensive since SEPH does not take into account non-wage fringe benefits such as employers' contributions to pension funds or health and insurance programs. Second, while the series exclude the effects of compositional change between the 258 industries, the provinces and territories and two employee categories, they cannot hold employment composition fixed within any of these categories. For example, changes in occupational mix within one of the two employee categories (salaried and hourly-paid employees) will continue to affect the series. Shifts in employment between sub-regions within a given province are also still present. Finally, the choice of 1987 as the base year for the series is arbitrary and the use of other years could, in principle, alter some aspects of the results significantly. This particular year was selected for two reasons: it is the first year following a major sampling "break" that

occurred in SEPH beginning in January 1987, [\(11\)](#) and it was a fairly typical year in Canada's labour market.

As a practical matter, the variable-weight and fixed-weight earnings series are unlikely to diverge dramatically, at least during normal periods. However, even seemingly small variations in growth between the two measures, such as the two percentage point cumulative difference between 1985 and 1987 ([Table 1](#)), can have important implications for the competitiveness and expansionary potential of the economy. In the following section, the fixed-weight AHE series are applied in an analysis of recent Canadian wage rate experience.



Table 1 Annual percentage change in several wage rate indicators

Sources: Labour Canada and Statistics Canada's National Income and Expenditure Accounts and Survey of Employment, Payrolls and Hours

Recent trends

Wage and price increases both dropped sharply after the 1982 recession, levelling off at about 4% annually between 1984 and 1987. Since then they have been edging up again. The rate of increase in wages was slightly below the inflation rate through the middle years of the decade, but has been somewhat higher since 1988.

The quickening pace of wage increases began in the second half of 1987, when the economy was growing at an extremely rapid rate. [\(12\)](#) Wage inflation advanced from about 3.5% in mid-1987 to over 4.5% by mid-1988, by which time wages were rising more rapidly than consumer prices. In early 1989, prices began to accelerate as well. In concert with wages, price inflation jumped to the 5%-5.5% range by mid-1989. It then stabilized and more recently has edged down somewhat, while wage increases have remained in the 5.5%-6% range.



Chart A Wages and price changes

Sources: Consumer Price Index and Labour Canada



Chart B Wages and price changes

Sources: Canadian Economic Observer and Consumer Price Index

Hourly-paid workers' earnings have been more responsive to economic forces than those of salaried workers. This is not surprising, since hourly-paid labour is typically less skilled and employers' hiring and termination costs are lower than for salaried employees. The rate of increase of wages for hourly-paid employees dropped quite sharply in 1984, fluctuated in the 2.5%-3.5% range in 1985 and 1986, and in early 1987 began a gradual but steady upward climb. This rise continued until late 1989, when wage growth appeared to have stabilized in the 5% to 6% range. Compensation increases for salaried employees, on the other hand, slowed more gradually through the mid-1980s, increased in early 1988 and surged to around 6% over the most recent 12 months.



Chart C Wage change by employee type

Source: Survey of Employment, Payrolls and Hours

Wage increases in the goods-producing sector fluctuated around 3% through much of 1986, edged up to the 3.5%-4% range in 1987, and in 1988 began a steep climb to their mid-1990 rate of about 5.5%. The services sector saw wage increases bottom out in the 3%-3.5% range in mid-1987 and then move upward to about 5% by mid-1988. They dropped back to around 4.5% by early 1989 before resuming their ascent to the current 6% range.

In the goods sector, wage increases picked up in 1988 in all industries except construction and forestry, where they moderated. Last year, they saw a further jump, with construction, forestry, and mines, quarries and oil wells recording particularly large increases.

Among the services industries, the largest wage increases occurred initially in finance, insurance and real estate. Wage growth jumped from about 3.5% in late 1986 to over 7% by the spring of 1988. Then the fallout from the stock market crash in October 1987 and the slowdown in residential construction that began around the same time, quickly put a damper on wage growth - by late 1988 the pace of wage inflation had moderated considerably. Lower increases continued until mid-1989, when renewed upward movement became evident. By early 1990, increases of about 6.5% range were once again prevalent in finance, insurance and real estate.



Chart D Wage change by sector

Source: Survey of Employment, Payrolls and Hours



Table 2 Annual percentage change in wages by industry and province

Source: SEPH-based fixed-weight average hourly earnings.

Community, business and personal services, and public administration have also experienced substantially higher wage increases over the past two to three years, and in recent months the pace has risen above 6%. In the latter case, particularly large wage gains occurred in Atlantic Canada, Saskatchewan and Alberta, beginning about the middle of 1989. On the other hand, the transportation, storage, communication and utilities industry, and the retail trade industry have both had rates of wage increase well below the average for several consecutive years, especially in Western Canada.

The wage acceleration (and the pickup in consumer price inflation) has been led by Ontario. Some regional convergence is evident lately, since both Atlantic Canada and Western Canada have experienced more rapid wage inflation. But Ontario continues to lead with wage increases averaging 4.6% in 1987, 5.1% in 1988, 5.9% in 1989 and 6.4% in the first half of 1990. The other provinces and territories, except for Prince Edward Island and the Yukon, have had much smaller increases until very recently. In most of Atlantic Canada, wage increases languished around 4% until mid-1989, when they jumped to the 5.5%-6% range, despite continuing high unemployment rates. Pay increases in Quebec were under 5% throughout the 1985-89 period but have moved slightly above that threshold in 1990. In Western Canada, wage increases slipped well below 3% in the mid-1980s. Depressed world markets for natural resources, particularly oil and gas, underlay this development. As Western Canada's economy gradually began to recover, wage increases moved up to the 3%-4% range in 1988 and above 5% in the second half of 1989 and early 1990.

Conclusion

Wage rates need to be monitored closely because they are such important indicators of the economy's health. SEPH-based fixed weight average hourly earnings statistics are the best available comprehensive indicator of changes in wage rates. These data reveal that over the past two to three years wage increases have picked up significantly, from a steady 3.5%-4% in 1985-87 to 5.5%-6% in 1990. The acceleration has been closely associated with strong economic growth, initially in Ontario and more recently in other regions of the country as well. Both goods and services industries have reflected the trend of higher wage

increases.

The more commonly used variable-weight average hourly earnings data, published with the monthly SEPH data release, provide a picture of recent wage trends that is generally similar, with some important differences. These differences are due to employment growth differentials, both industrial and regional. In the mid-1980s, two of the lowest-wage industries - retail trade, and community, business and personal services - recorded above-average growth in employee paid hours. At the same time, some of the high-wage industries, notably transportation and related industries and primary industries, experienced below-average growth. These divergent trends caused average hourly earnings to grow less rapidly than the fixed-weight series during the 1985-87 period. The relative weakness of employment growth in the western provinces, where wages are comparatively high, also contributed to this divergence. More recently, rapid growth in high-wage industries, such as public administration and construction, particularly in Alberta and British Columbia, coupled with slower growth in retail trade, has caused the reverse phenomenon: average hourly earnings have risen more rapidly than the fixed-weight series.

In sum, the statistical evidence on trends in wages shows a gradual but significant upturn over the past three years, with wages now rising somewhat more rapidly than prices. The wage pickup is visible both in the usual variable-weight earnings measure and in the relatively new fixed-weight indicator, and has affected most provinces and industries of Canada. The implications of this developing trend will depend on how long it persists, and on how soon productivity growth resumes at a stronger pace.

Average hourly earnings from SEPH

Average hourly earnings (AHE) data from the Survey of Employment, Payrolls and Hours (SEPH) are computed for hourly-paid personnel by dividing total earnings by total paid hours. This series is often used as an indicator of movements in the price of labour. However, it has one important limitation when used for this purpose: its movements can be influenced by compositional shifts. The overall AHE series are variable-weight indexes, in the sense that AHE data for particular industries, regions and employee categories are aggregated to higher industrial and regional levels using current rather than fixed employee paid hours weights.

The essence of this mix problem is as follows. Some industries, regions, or occupations pay relatively high wage rates and others pay relatively low wage rates. When employee paid hours expand more (or less) rapidly in the high-wage categories than in the low-wage categories, overall AHE will tend to grow more (or less) rapidly than underlying wage rates. The difference is potentially important; increases in AHE caused by compositional changes are not related to price increases for goods and services, whereas AHE increases caused by growth in underlying wage rates may well be.

The following example shows how significant the mix effect can be. Suppose, for simplicity, that there were only two industries in the economy, which might be called the "goods" industry and the "services" industry. Assume that half the employees worked in the "goods" industry and the other half worked in the "services" industry. Suppose also that all employees working in the "goods" industry received \$15 per hour regardless of their occupation or the region they worked in, and that all employees in the "services" industry received \$10. If all wage rates increased by 5% over a particular period in both industries, and if there were no compositional changes, then average hourly earnings would also rise by 5%.

But, suppose employee paid hours in the "goods" industry fell by 5% during the period, while paid hours in the "services" industry rose by 5%. Then overall average hourly earnings would rise only by about 4% even though all wage rates had increased by 5%. If the compositional change were 10% rather than 5%, the increase in total average hourly earnings would only be about 3%. Similarly, a faster-than-average employment increase in the high-wage sector would give the illusion that wages were increasing by more than 5%. As this example shows, the effects of compositional change on AHE growth rates can be substantial.

Notes

Note 1

See, for example, [A. Sharpe](#), *Perspectives on Labour and Income* (Summer 1990); [H. Solomon](#), *The Financial Post* (June 4, 1990); and [D. Fagan](#), *The Globe and Mail* (June 6, 1990).

Note 2

See, for example, [J. Vardy](#), *The Financial Post* (May 22, 1990); and [T. Rutley](#), *Bulletin of the Canadian Manufacturers' Association* (1990).

Note 3

Organizations such as the federal Pay Research Bureau and some private sector consultants specializing in the field of labour compensation collect data on occupational wage rates, but the information is not comprehensive and is not suitable for aggregate time series analyses. Two other larger and more comprehensive surveys of labour compensation, Labour Canada's Wage Rate Survey and Statistics Canada's Labour Costs Survey, were both terminated several years ago as cost-saving measures.

Note 4

The U.S. Employment Cost Index is published quarterly and is based on a sample of about 4,200 private non-farm establishments and 800 state and local government establishments. It is fixed-weight and is

derived from a detailed review of specific occupational categories in each of the sampled establishments. The 5,000 establishments in the sample provide some 26,200 carefully specified occupational observations from which the index is computed. For more information on the Employment Cost Index, see [Bureau of Labor Statistics](#), "Notes on Current Labor Statistics" and Tables 22-25, *Monthly Labor Review*.

Note 5

For a discussion of these issues, see [H. Pold and F. Wong](#), *Perspectives on Labour and Income* (Autumn 1990).

Note 6

Although Survey of Employment, Payrolls and Hours data are available only from 1983 on, data from a similar survey are available for the preceding period. See [Statistics Canada](#), *Employment, Earnings and Hours*.

Note 7

The fixed-weight average hourly earnings series are described more fully in [P. Smith](#), *Canadian Economic Observer* (1989). The data are available on a monthly basis in the regular *Canadian Economic Observer* tables and in the CANSIM data bank numbers D99995 through D100026. They are also available on diskette in greater detail, and on a monthly basis from the author.

Note 8

The SEPH questionnaire defines the standard workweek as "the average number of hours of work normally scheduled in a workweek".

Note 9

All SEPH tabulations are currently based on the 1970 Standard Industrial Classification. SEPH will be converted to the 1980 SIC in the coming year.

Note 10

The SEPH questionnaire does not collect any other information on the occupational dimension of employment and earnings, so it is not possible to have fixed occupational weights.

Note 11

In 1987, SEPH's estimation methods were substantially revamped and new weights were assigned to the survey frame. This reweighting caused an important compositional effect of the type referred to earlier in the text. For details, see [Statistics Canada](#), *Employment, Earnings and Hours*.

Note 12

Real gross domestic product grew at a 6.4% compound annual rate in the second half of 1987, more than double the 3.1% average annual growth rate for the decade as a whole.

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 HIGHLIGHTS

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Table 1

Annual percentage change in several wage rate indicators

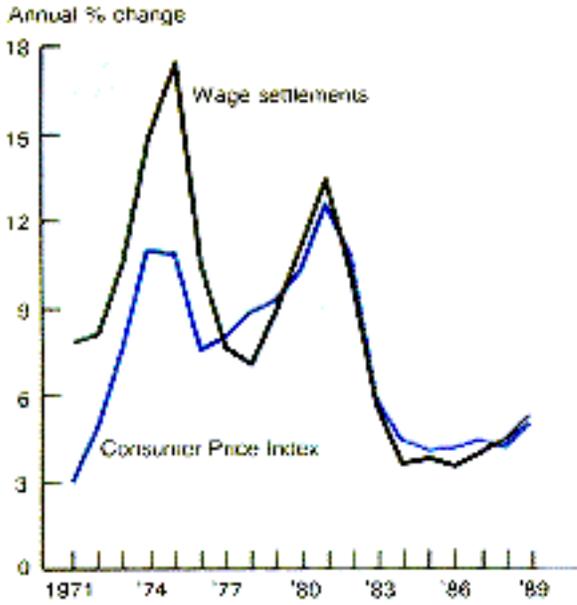
	1985	1986	1987	1988	1989	1990*
Labour Canada indicators						
Base wage rate settlements						
Commercial sector	3.6	3.1	3.9	4.6	5.1	5.7
Non-commercial sector	3.7	3.6	4.2	4.1	5.4	5.5
All industries	3.7	3.4	4.1	4.4	5.3	5.6
National accounts indicators						
Labour income per employee						
Wages and salaries	4.9	3.9	5.6	6.2	6.9	6.6
Supplementary labour income	6.3	3.5	7.6	5.6	4.9	14.1
Total labour income	5.0	3.8	5.8	6.1	6.6	7.4
SEPH-based indicators						
Average hourly earnings						
Hourly-paid employees	2.8	2.4	2.3	4.5	5.4	5.3
Salaried employees	4.6	4.4	3.4	4.7	5.4	6.3
All employees	3.6	3.3	2.6	4.5	5.4	6.0
Fixed-weight average hourly earnings						
Hourly-paid employees	2.9	3.0	3.4	4.2	5.2	5.3
Salaried employees	4.8	4.2	3.9	4.7	5.1	6.2
All employees	3.9	3.7	3.7	4.5	5.2	5.8

Sources: Labour Canada and Statistics Canada's National Income and Expenditure Accounts and Survey of Employment, Payrolls and Hours

** Data for 1990 are for the first seven months of the year, compared with the same period for 1989.*

Wage and price changes

During the 1980s, wages and prices generally followed similar paths.

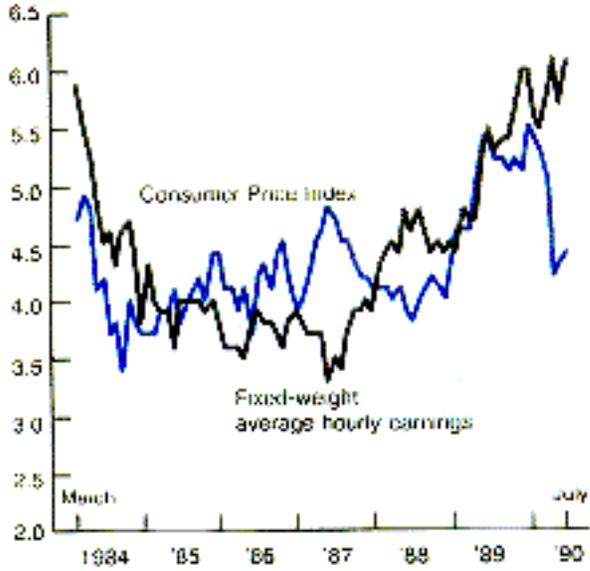


Sources: *Consumer Price Index and Labour Canada*

Wage and price changes

Hourly earnings rose more rapidly than consumer prices in 1988 and 1989, after several years of lagging.

Year-over-year % change



Sources: *Canadian Economic Observer* and *Consumer Price Index*

Wage change by employee type

Over the last five years, wage gains for salaried employees have generally exceeded those of hourly-paid personnel.

Year-over-year % change

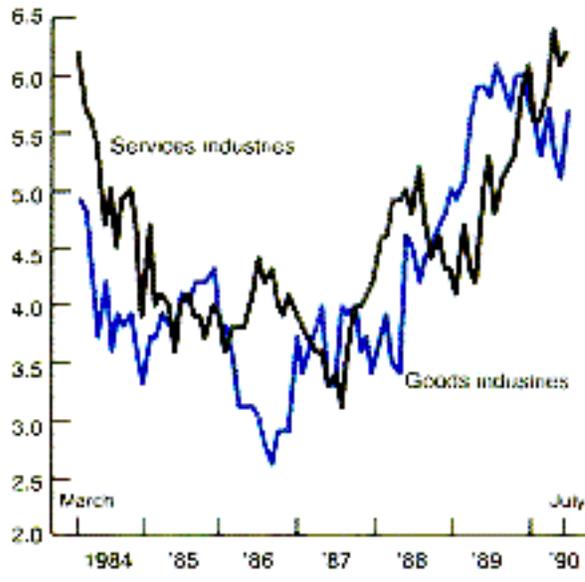


Source: Survey of Employment, Payrolls and Hours

Wage change by sector

Until 1989, wage increases in the goods sector were generally smaller than those in the services industries.

Year-over-year % change



Source: Survey of Employment, Payrolls and Hours

Table 2

Annual percentage change in wages by industry and province

	1985	1986	1987	1988	1989	1990*
By industry						
Goods-producing industries	3.9	3.1	3.7	4.1	5.8	5.5
Primary industries	4.7	2.0	2.3	4.5	6.2	5.5
Forestry	0.8	2.2	3.5	2.4	4.6	3.9
Mines, quarries and oil wells	5.7	1.9	2.0	5.0	6.7	5.9
Manufacturing	4.4	3.7	3.7	4.1	5.4	5.7
Durable goods	4.0	3.8	3.6	4.0	5.5	6.2
Non-durable goods	4.8	3.7	3.9	4.2	5.3	5.1
Construction	1.9	1.3	4.4	4.0	6.8	5.0
Services-producing industries	4.0	4.0	3.7	4.7	4.9	6.0
Transportation and related industries	3.6	3.3	2.4	3.3	3.7	4.6
Total trade	3.1	5.1	3.7	4.2	4.9	5.7
Retail trade	2.8	4.9	3.1	4.4	4.4	4.7
Wholesale trade	3.6	5.3	4.5	3.7	5.7	7.2
Finance, insurance and real estate	7.0	4.1	5.1	6.0	5.1	6.5
Community, business and personal services	4.3	3.7	3.8	5.0	5.0	6.0
Public administration	2.7	4.2	3.8	4.9	5.3	7.5
All industries	3.9	3.7	3.7	4.5	5.2	5.8
By province						
Atlantic Canada	4.4	3.6	4.1	4.0	5.0	6.0
Newfoundland	2.6	3.9	5.2	4.4	5.7	4.8
Prince Edward Island	4.1	3.4	6.3	5.9	5.6	6.4
Nova Scotia	5.3	3.9	4.1	3.7	4.7	7.5
New Brunswick	4.6	3.2	2.9	3.8	5.0	4.9
Quebec	4.1	3.2	3.7	4.9	3.9	5.4
Ontario	4.7	5.1	4.6	5.1	5.9	6.4
Prairies	2.5	2.4	2.0	3.0	4.8	5.0
Manitoba	3.3	3.3	2.7	4.0	4.2	4.1

Saskatchewan	2.9	2.0	2.9	1.3	4.5	4.3
Alberta	2.1	2.2	1.5	3.0	5.1	5.5
British Columbia	2.6	1.5	2.2	3.6	5.4	5.8
Northwest Territories	4.1	3.4	5.7	3.3	4.3	5.5
Yukon	5.4	2.4	2.2	5.3	7.1	2.2
Canada	3.9	3.7	3.7	4.5	5.2	5.8

Source: SEPH-based fixed-weight average hourly earnings.

** Data for 1990 are for the first seven months of the year, compared with the same period for 1989.*