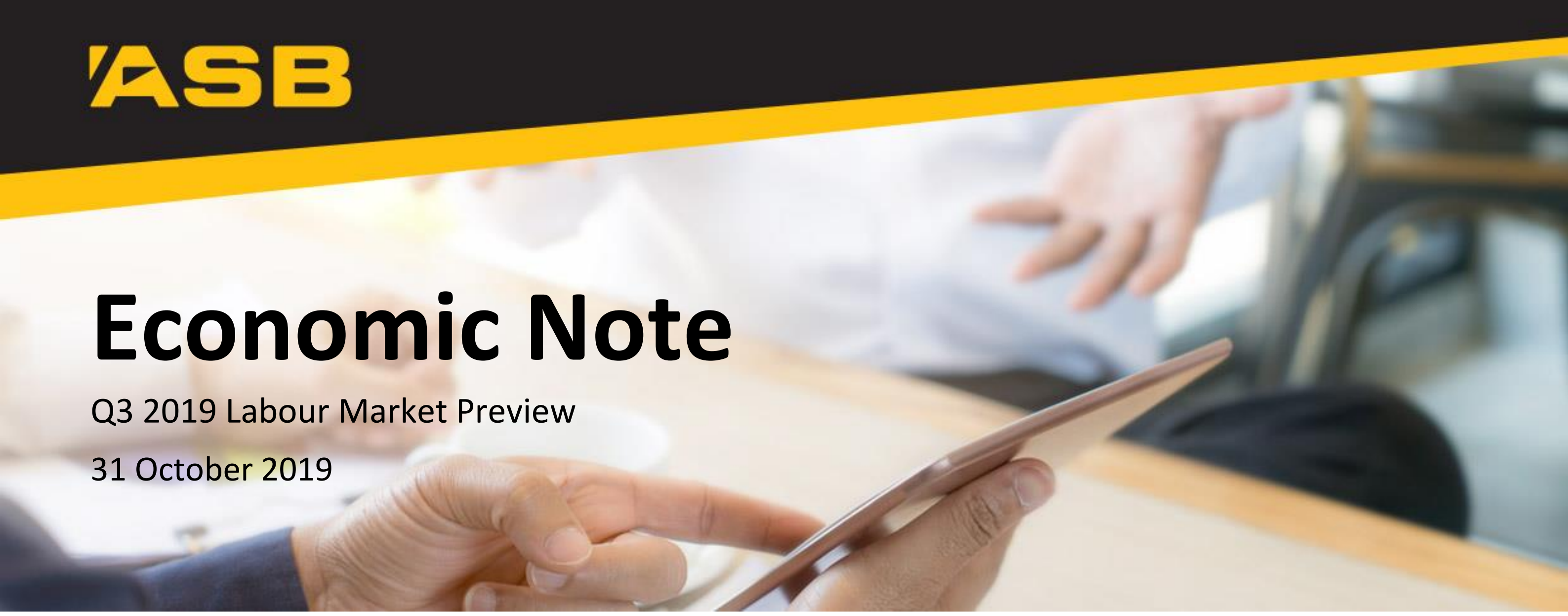

Economic Note

Q3 2019 Labour Market Preview

31 October 2019

Turning

- We expect September quarter labour market data to reveal a modest slackening in the labour market.
- The RBNZ is currently meeting its labour market objectives, but has more work to do to ensure employment remains around its “maximum sustainable” level.
- We continue to expect another 25bps RBNZ rate cut in November.

Q3 Labour Market Forecasts			
HLFS	**ASB**	Prior	RBNZ
Employment growth (QoQ)	0.3	0.7	0.4
Employment growth (YoY)	0.9	1.4	0.8
Unemployment Rate (%)	4.1	3.9	4.4
Participation Rate (%)	70.3	70.2	70.6
Labour Cost Index			
Private Sector (%, QoQ)	0.6	0.8	0.5
Private Sector (%, ann)	2.3	2.2	2.0

Summary and implications

The big question for Q3 labour market data (released 6 November) is how much of the recent weakness in the forward indicators will show up in the official statistics. The HLFS can be a tad unpredictable. We’re looking for a soft 0.3% lift in employment and a small rise in the unemployment rate to 4.1%. We’d caution though that the risks are tilted towards a weaker result.

Whatever the outcome, we’d advise against putting too much weight on the unemployment rate. In a downturn, reported unemployment can stay low even as discouraged jobseekers leave the labour force and capacity opens up. We will once again be looking across the array of labour market capacity indicators we know the RBNZ watches closely to get a broader view of labour market pressures.

We continue to believe the non-accelerating inflation rate of unemployment (NAIRU) is around 4%. This means the RBNZ is going to have its work cut out continuing to meet its “maximum sustainable employment” objective as labour market outcomes start to reflect the broader economic slowdown. The Bank has clearly demonstrated its intent to get ahead of the curve, but we think there is more work to do and retain our call for additional 25bps RBNZ rate cuts in both November and February.

We doubt a major surprise from the HLFS would throw the RBNZ off course. For a start, the labour market lags the broader cycle, and forward indicators have been weak. The Bank also appears happy to give the data a wide berth given its inherent volatility. Let’s not forget the RBNZ slashed the OCR 50bps a day after the Q2 HLFS showed unemployment at an 11-year low.

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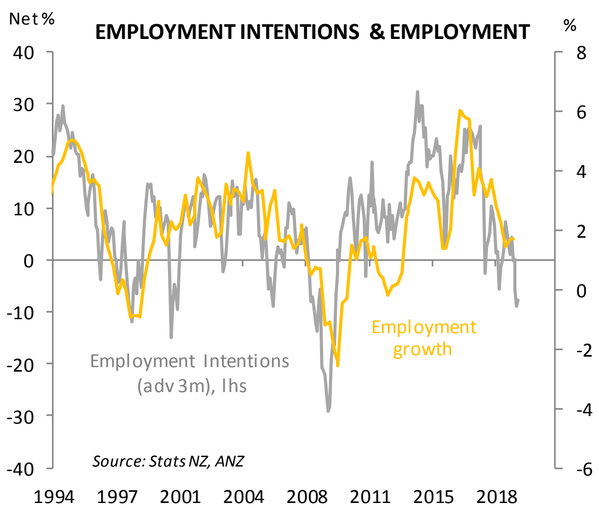
Labour market turning

We think the labour market has turned. The big question for the Q3 set of labour market statistics is really about the magnitude. In particular, how much of the weakness we have seen in the partial data and forward indicators will show up in the official statistics. After all, the HLFS can be a tad unpredictable. Quarter-to-quarter movements need to be taken with a large grain of salt. This is even more so for Q3 given recent revisions to working age population data.

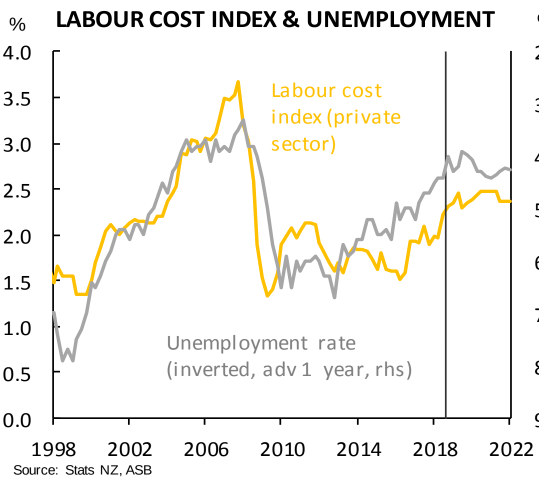
For this reason, we've deliberately erred on the conservative side with our forecasts. We expect a relatively soft 0.3% qoq lift in employment following last quarter's solid (revised) 0.7% expansion. This would leave annual employment growth at just 0.9%, indicative of the extent to which jobs growth has slowed over the past year. Assuming a labour force participation rate of 70.3%, the unemployment rate is expected to tick up slightly to 4.1%.

We see the risks as tilted towards a weaker outcome. Surveyed employment intentions have fallen appreciably and, on their own, suggest firms are actually shedding workers (see chart). Some of the other partial data we look at like Jobseeker numbers have been weak. Still, these downside risks need to be balanced against surveyed skill shortages and difficulties finding staff that remain at stretched levels.



Whatever the outcome, we'd caution against putting too much weight on the unemployment rate as the key indicator of labour market capacity. In a downturn, reported unemployment can stay low even as discouraged jobseekers leave the labour force and capacity opens up (i.e. labour supply falls with labour demand). We will once again be looking across the broad swathe of labour market capacity indicators we know the RBNZ watches closely: Maori unemployment; youth unemployment rates; the underutilisation rate[1], and the underemployment rate.[2] Recall, this suite of indicators unexpectedly tightened last quarter. But with the broader economic slowdown having since become entrenched we'd expect some slackening in Q3 and further ahead.

Indeed, there's probably already a little more slack in the labour market than many believe (see our recent note). We continue to believe the non-accelerating inflation rate of unemployment (NAIRU) is around 4%. This means the RBNZ is going to have its work cut out continuing to meet its "maximum sustainable employment" labour market objective. The Bank has clearly demonstrated its intent to get ahead of the curve, but we think there is more work to do and retain our call for a further two 25bps RBNZ rate cuts.



Pick up in wage growth to continue

We expect the recent pick-up in wage growth to continue in the third quarter. Annual growth in the key private sector Labour Cost Index (LCI) wage measure is expected to lift from 2.2% yoy to 2.3% in September via a 0.6% quarterly increase. Further modest wage appreciation is expected thereafter, reflecting past tightness in the labour

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[1] A broad group considered part of the potential labour supply. Includes underemployed workers, unavailable jobseekers, and available potential jobseekers.
[2] Part-time workers who would prefer to work more hours and are available to do so.

market. Various pay settlements will also remain a feature of the slow uplift in wage growth. Legislated minimum wage increases contributed over a third of last quarter's increase in the LCI and will impact wage growth figures until 2022. The July 2019 instalment of the Care and Support Workers Pay Equity settlement, as well as the mid-year teachers' pay settlement, will both make small contributions to the September quarter increase.

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