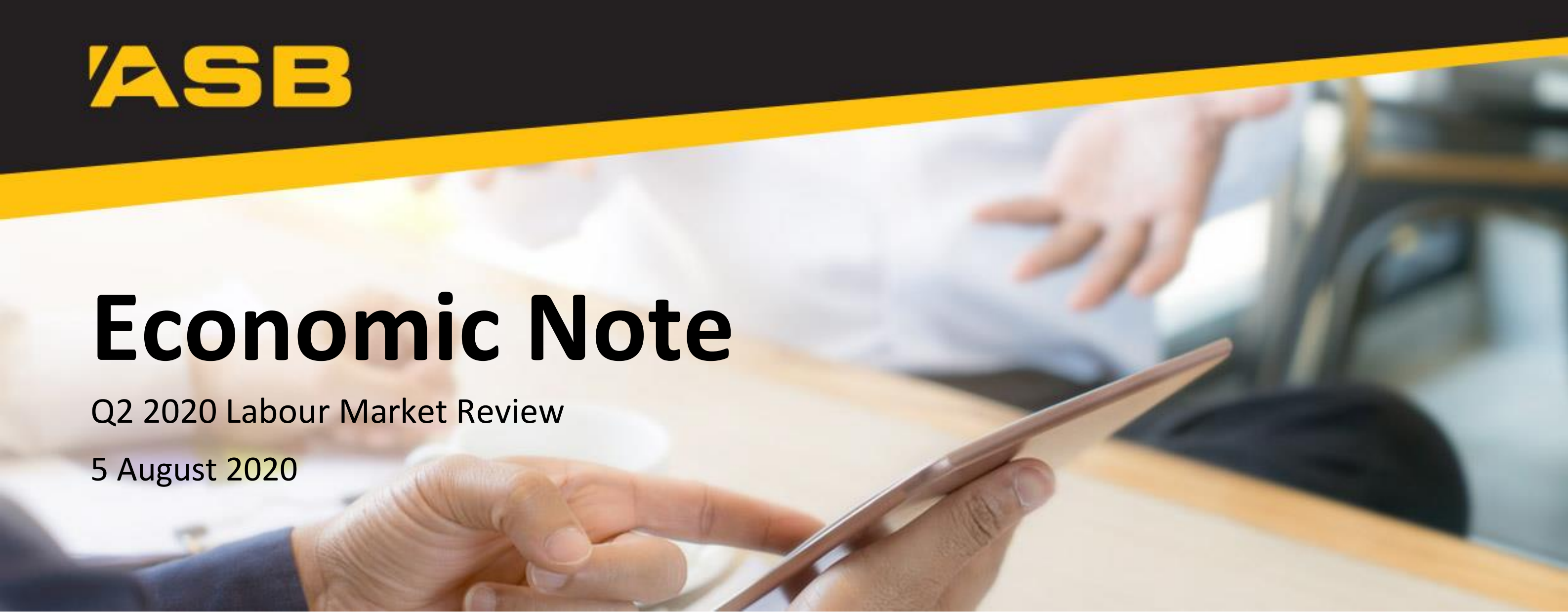

Economic Note

Q2 2020 Labour Market Review

5 August 2020

What a nice surprise

- Unemployment falls, quashing widespread expectations of a large increase
- Other measures paint a much weaker picture of labour market conditions
- We are wary of changing our labour market view on what looks to be a rouge result, but concede that the unemployment rate could peak at a lower rate than we thought earlier

Household labour Force Survey	Actual	ASB	Market
Employment growth (QoQ)	-0.4	-2.8	-2.0
Unemployment Rate (%)	4.0	6.4	5.6
Participation Rate (%)	69.7	69.4	69.7
Labour Cost Index			
Private Sector (%, QoQ)	0.2	0.5	0.4
Private Sector (%, ann)	1.8	2.0	1.9

Summary and implications

Today's labour market data was certainly welcome to the extent they indicate a stronger-than-expected starting point. However, their use is limited not only by measurement issues, but also the weight of evidence pointing to a subsequent deterioration in labour market conditions. The real question is still how the job market settles once the various wage subsidy schemes end and the economy adjusts to its post-COVID 'normal'? There are still around 450k people on the wage subsidy extension currently due to expire at the end of the month, roughly 17% of the labour force. This suggests further difficulties ahead. We expect the unemployment rate to rise from here but concede that the peak may be lower than first thought.

June quarter labour market statistics were undoubtedly stronger than expected, although an apparent 4.0% unemployment rate belies this. The reported *fall* in HLFS unemployment in Q2, to 4.0% from 4.2% last quarter, quashed widespread expectations (including our own) for a solid increase. This reflected both a much smaller-than-expected drop in employment of just 0.4% qoq, and a fall in the labour force participation rate to 69.7%. The fall in the latter owes in part to laid off workers being unable to actively seek work during lockdown and thus to be included in the labour force.

As we said in our preview, it's important to handle today's labour market data with care. It's notable that the financial markets certainly did. The NZD/USD rose barely 20 pips following what was an over 1½ percentage point surprise on the unemployment rate! That the data was left to go through to the keeper is telling. Not only did the COVID lockdown in April/May disrupt how some people were represented in labour market statistics, it also caused measurement headaches for Stats NZ.

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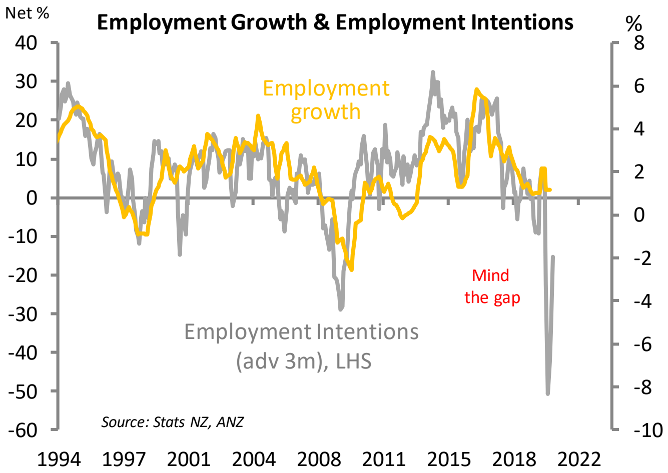
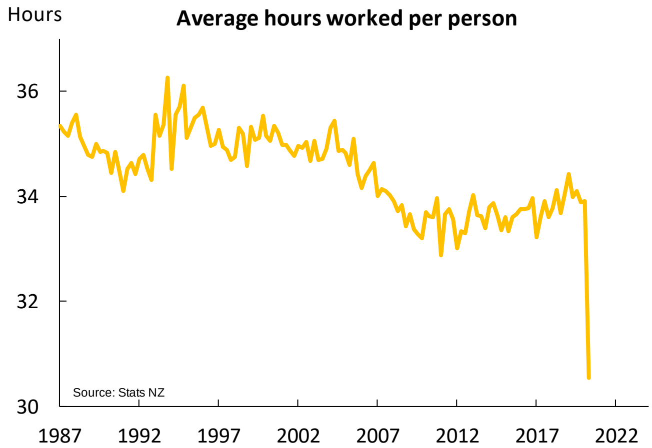
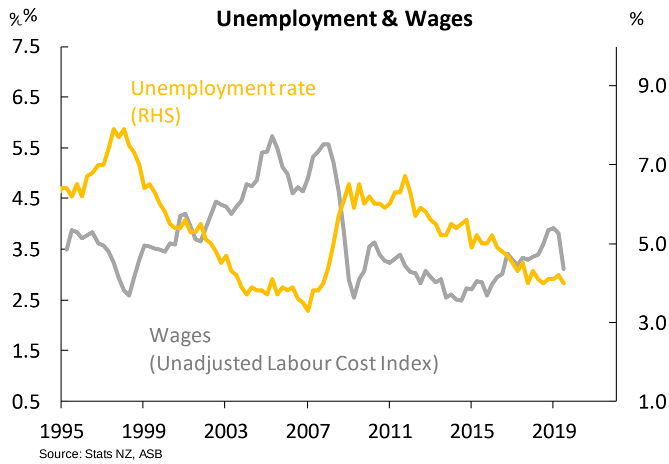
A look at the broader array of measures on offer provides a more accurate assessment of how the labour market has fared. Certainly, the reported drop in the unemployment rate understates the deterioration in the labour market during the quarter. The HLFS unemployment rate of 4% is an average across the quarter. But Stats NZ reported that the unemployment rose relatively steadily across the 13 weeks of the quarter from 2.7% (unadjusted) in Alert Level 4 through to 4.9% in Alert Level 1 at the end of June. As such, the "true" starting point for unemployment is closer to 5.0% than 4.0%.



Some of the broader measures of labour slack that we'd highlighted as important also painted a much weaker picture. Underutilisation rose from 10.4% in Q1 to 12.0% (seasonally adjusted), the largest quarterly increase since records began. In the current environment, underutilisation is probably a more useful measure of labour market capacity than the unemployment rate. It is defined such that jobseekers outside the labour force are captured (unlike the unemployment rate) and includes people working part-time who would like to work more hours.



Hours worked also collapsed just over 10% qoq in Q2 as expected, reflecting many employed workers being paid to sit at home and twiddle their thumbs through the more stringent lockdown restrictions in place for much of Q2. Some of the employment measures from the Quarterly Employment Survey were also noticeably weaker than HLFS employment. Paid hours, for example, fell 3.4% over the quarter.



Wage growth the lowest in 26 years

There were also signs in some of the wages data that wage growth has turned south sooner than we expected. This might appear somewhat at odds with the message from the HLFS but, again, some of this likely reflects surveying methodology. The LCI (and QES) were surveyed in the middle of the quarter (May) rather than averaged like the HLFS. The private sector Labour Cost Index – the key wage measure we look at – rose just 0.2% over the quarter. Importantly, this was despite the latest instalment of the minimum wage increase going through in April, which we estimate contributed around 0.2% percentage points to quarterly wage growth. Indeed, Stats NZ confirmed that, without it, LCI wages would have flat-lined on the quarter. Even as it was, it was the softish read on private sector quarterly wage growth since 1994. Broader wage measures were also a little soggy. The unadjusted LCI, more of a 'raw' measure of wage costs, rose just 0.4% qoq, with annual growth slowing from 3.8% to 3.1%. Average hourly earnings from the QES slowed to 2.5% yoy for private sector workers, a multi-year low.

End of wage subsidy still looms large

Overall, today's data are certainly welcome to the extent they indicate a stronger-than-expected starting point for the labour market. However, their use is limited to some extent not only by measurement issues, but also by the fact we know labour market conditions are likely to deteriorate from here. The real question is still how the jobs market settles once the various wage subsidy schemes end and the economy adjusts to its post-COVID 'normal'. According to Ministry of Social Development figures, there are still 450k people on the wage subsidy extension currently due to expire at the end of the month. This amounts to a sizeable 17% of the labour force. This suggests further difficulties ahead. We still expect the unemployment rate to rise from here, but the peak may be lower than first thought.

For the RBNZ, today's data are miles stronger than its May forecasts for Q2 (4.5% fall in employment, 7% unemployment rate), another data release that affords the Bank time in making its next move. The RBNZ is nevertheless forward-looking and will be wary of future deterioration. Employment is still likely to undershoot the Bank's Maximum Sustainable Employment target and the path of least regret for the Bank will thus be to keep monetary policy easy.

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