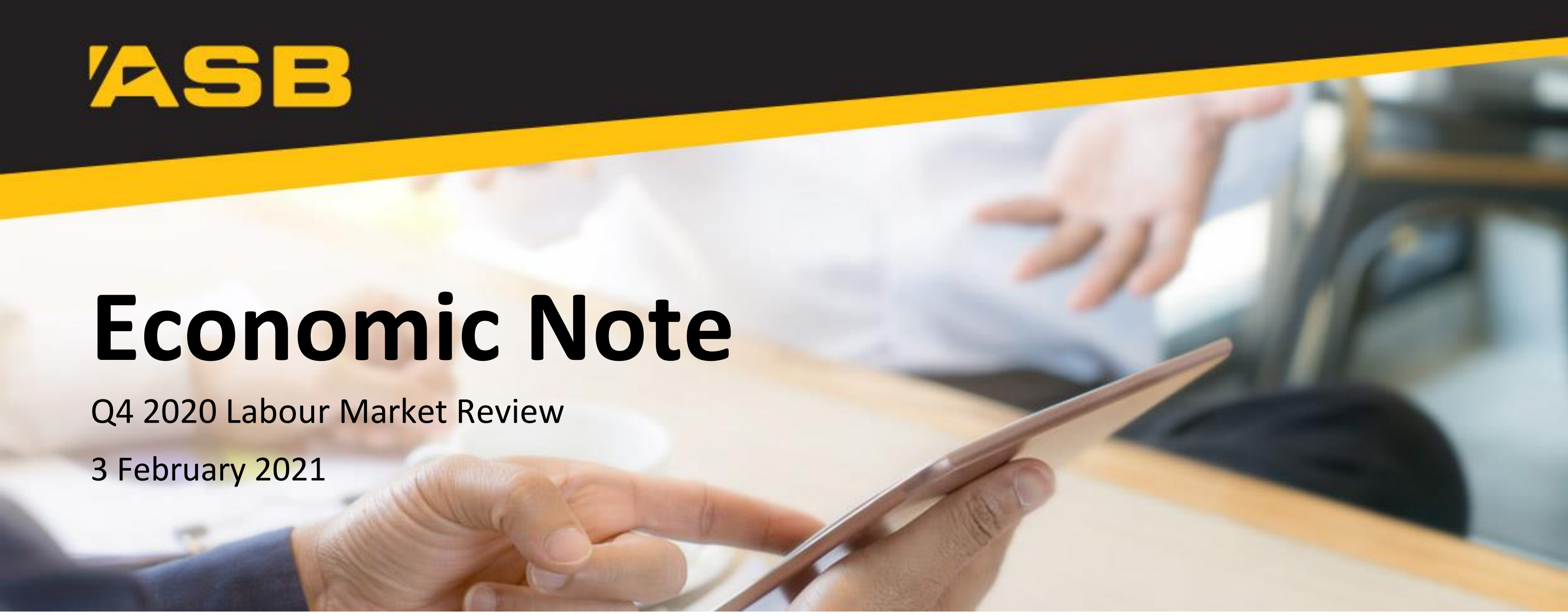

Economic Note

Q4 2020 Labour Market Review

3 February 2021

Has unemployment already peaked?

- NZ's amazing economic run continues, with an unemployment rate in the "4s" the latest example.
- Whether or not this can be believed, it's hard to escape the conclusion that the labour market was much tighter than anyone expected in the final quarter of 2020. Forecasts for a trend increase in the unemployment rate this year now look too pessimistic.
- Last year's flood of RBNZ (and fiscal) stimulus has done the trick, and no more is required. We agree with the market pricing some risk of a lift in interest rates in 2022.

Household labour Force Survey	Actual	ASB	Market
Employment growth (QoQ)	0.6	0.1	-0.1
Unemployment Rate (%)	4.9	5.6	5.6
Participation Rate (%)	70.2	70.2	70.3
Labour Cost Index			
Private Sector (%, QoQ)	0.5	0.5	0.5
Private Sector (%, ann)	1.5	1.5	1.5

We'd suggested the risk was for a stronger set of labour market indicators today, but we were nonetheless left gob-smacked at just how strong the labour market in Q4 proved to be. Unemployment not only fell, but fell a long way. The 0.4 percentage point decline to 4.9% was miles better than our and market expectations of an increase to 5.6%. This was thanks to a stronger-than-expected 0.6% qoq lift in jobs growth (ASB +0.1%, market -0.1%). Labour supply ticked up about as much as expected; the participation rate nudged up to 70.2%.

Genuine strength

The Household Labour Force Survey (HLFS) has a history of often jolting volatility. Thus, it normally pays to take the unemployment rate outturn with a grain of salt. But even doing so, as well as taking in the broader range of labour market indicators on offer today, it's hard to escape the conclusion that the labour market was much tighter in the final quarter of 2020 than anyone expected, the RBNZ included. Of course, this carries on the good vibes trend emanating from a range of NZ economic data. Recent business confidence, inflation, housing and now labour market data have all illustrated the enormous boost fiscal and monetary stimulus provided to the economy in 2020. The global picture remains far from dire too; this morning we revised up our Milk Price forecast.

The employment measures in the Quarterly Employment Survey (QES) often serve as a useful cross-check against any oddities in the HLFS. The key ones, paid hours and filled jobs, rose 1.3% and 0.8% qoq, respectively, suggesting the increase in the HLFS measure of employment can't be explained away as surveying volatility. Moreover, all of the jobs created in Q4 were full-time, with part-time employment actually retrenching 1.8%. The underutilisation rate, a

Mike Jones – Senior Economist (649) 301 5661 mike.jones@asb.co.nz

Please refer to the important disclosures at the end of this document.

broader and more detailed measure of labour market capacity than the unemployment rate, dropped 1.3 percentage points to 11.9% - all but confirming the reduction in labour market capacity through the quarter.

So where were the jobs created? Construction was a big part of the story. Construction-related hiring was responsible for about 25% of the Q4 jobs growth (not seasonally adjusted), indicative of the massive impulse for the economy from the construction and housing booms. An increase in healthcare workers was another large contributor, with the media and tourism industries unsurprisingly reporting modest jobs retrenchment.

Wage growth turning already

Wage growth was fairly tepid as expected, but we remain of the view that annual wage growth is close to troughing and will turn higher in coming quarters. Indeed, this view was strengthened today given the positive signs for labour demand. The Labour Cost Index (LCI) expanded 0.5% over the quarter, bringing annual wage growth according to this measure down to 1.5%. We expect a pick-up to 1.7% next quarter.

Market pricing risk of policy 'normalisation'

Looking ahead, some smoothing is always necessary when it comes to the choppy nature of the HLFS. That is, a 4.9% unemployment rate, in of itself, probably overstates just how strong labour market conditions really are. But taken as a whole, today's data certainly support the idea the labour market is in a tighter spot than most expected, and forecasts for a trend increase in the unemployment rate this year are now too pessimistic. We've trimmed our projections, such that the unemployment rate now bobbles around the low 5s for the rest of this year. Uncertainty is still marked and there are plenty of risks around. But, remarkable as it is to suggest, the unemployment rate may have already peaked.

There are some chunky implications for the RBNZ here. Achieving the Bank's two monetary policy objectives is suddenly a goal within reach, from a situation last year in which its inflation and employment projections were a long way from target. Last year's flood of RBNZ (and fiscal) stimulus has done the trick, and no more is required. By contrast, attention is quickly turning to when the stimulus taps, which are still gushing, might be wound back a little. The market is now factoring in a small (just under 10%) chance of a lift in the OCR by February 2022, which looks about right to us.

ASB Economics & Research			Phone
Chief Economist	Nick Tuffley	nick.tuffley@asb.co.nz	(649) 301 5659
Senior Economist	Mark Smith	mark.smith4@asb.co.nz	(649) 301 5657
Senior Economist	Jane Turner	Jane.turner@asb.co.nz	(649) 301 5957
Senior Economist	Mike Jones	Mike.jones@asb.co.nz	(649) 301 5661
Economist	Nat Keall	nathanial.keall@asb.co.nz	(649) 448 8778
Senior Economist, Wealth	Chris Tennent-Brown	chris.tennent-brown@asb.co.nz	(649) 301 5915
Data & Publication Manager	Judith Pinto	judith.pinto@asb.co.nz	(649) 301 5660

www.asb.co.nz/economics

@ASBMarkets

Disclaimer

This document is published solely for informational purposes. It has been prepared without taking account of your objectives, financial situation, or needs. Before acting on the information in this document, you should consider the appropriateness and suitability of the information, having regard to your objectives, financial situation and needs, and, if necessary seek appropriate professional or financial advice.
We believe that the information in this document is correct and any opinions, conclusions or recommendations are reasonably held or made, based on the information available at the time of its compilation, but no representation or warranty, either expressed or implied, is made or provided as to accuracy, reliability or completeness of any statement made in this document. Any opinions, conclusions or recommendations set forth in this document are subject to change without notice and may differ or be contrary to the opinions, conclusions or recommendations expressed elsewhere by ASB Bank Limited. We are under no obligation to, and do not, update or keep current the information contained in this document. Neither ASB nor any person involved in the preparation of this document accepts any liability for any loss or damage arising out of the use of all or any part of this document. Any valuations, projections and forecasts contained in this document are based on a number of assumptions and estimates and are subject to contingencies and uncertainties. Different assumptions and estimates could result in materially different results. ASB does not represent or warrant that any of these valuations, projections or forecasts, or any of the underlying assumptions or estimates, will be met.