ASB

Economic Note

Q4 2018 Labour Market Review

7 February 2019

HLFS volatility persists, making life difficult for the RBNZ

- As was generally expected, the HLFS showed retracement from the strong Q3 outturns. Employment was virtually flat in Q4, the unemployment rate ticked up to 4.3%, and other measures of labour market utilisation eased from decade highs.
- Wage inflation remained moderate with limited evidence that wage inflation is becoming more widespread.
- The labour market is still reasonably tight and the RBNZ looks to be meeting its objectives of "supporting maximum sustainable employment within the economy". However, the lack of an inflationary smoking gun keeps the prospect of possible OCR cuts alive.

Household labour Force Survey	Actual	ASB	Market
Employment growth (QoQ)	0.1	0.1	0.3
Employment growth (YoY)	2.3	2.4	2.6
Unemployment Rate (%)	4.3	4.1	4.1
Participation Rate (%)	70.9	70.9	71.1
Labour Cost Index			
Private Sector (%, QoQ)	0.5	0.6	0.6
Private Sector (%, ann)	2.0	2.0	2.0

Summary and implications

Following the strong Q3 HLFS report, there was some concern that the traditional volatility in the Household Labour Force Survey (HLFS) had returned. Today's report does not assuage those fears, with Statistics NZ making some methodological adjustments, which may have added to the 2018Q4 survey volatility, potentially making the task more difficult for the RBNZ to discern the true state of the labour market. Wage growth, however, is failing to fire. On the basis of today's figures the hurdle to an OCR hike is high, but if wage inflation remains low, the OCR could move lower.

HLFS figures retrace some of their 2018Q3 strength

In the December 2018Q4 labour market report, Statistics NZ introduced some methodological tweaks to the HLFS data to make the figures more robust. Specifically, Statistics NZ used the findings from the December survey of working life (SoWL) to adjust some of the employment, labour force and hours worked measures in the HLFS. While measures to increase the information content of the HLFS are welcome, it is hoped that the changes minimise recent volatility in the survey. We will be watching future HLFS outturns with interest.

As was generally expected, today's HLFS figures showed some retracement from the strong Q3 report for selected measures. The 0.1% qoq increase in Q4 HLFS employment was slightly weaker than the market consensus (+0.3% qoq), with annual employment growth easing to 2.3%, the lowest since 2016Q1. Hours worked fell 2% in Q4, the second consecutive quarterly decline, with the 0.4% annual decline the lowest in six years. The labour force

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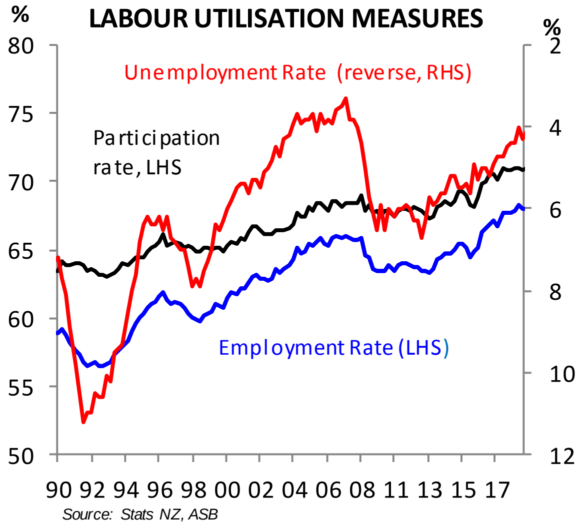
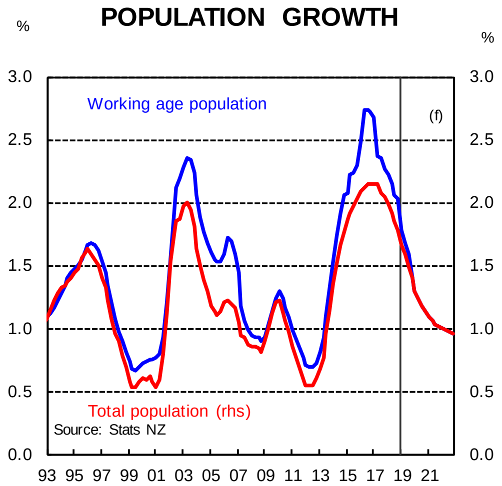
participation rate eased from decade highs (to 69.6% from 71% in Q3). The Quarterly Employment Survey (QES), by contrast, posted a moderate 0.4% qoq increase in full-time equivalent employment (1.2% yoy), and a benign 0.1% increase in paid hours (1.9% yoy).

The HLFS unemployment rate rose 0.3 percentage points to 4.3% in Q4 (from a revised 4.0% in Q3), but still lies within the RBNZ's estimated 3-5%-5.3% range for the Non-Accelerating Inflation Rate of Unemployment (NAIRU). The seasonally-adjusted underutilisation rate (a measure of slack within the existing employment market) edged up from record lows (to 12.1% from 11.4% in Q3).

Growth in the labour force rose 0.4% qoq (2.2% yoy) and working age population growth (2.2% yoy) plateaued in Q4. Despite Statistics NZ having revised down its estimates of net immigration there were minimal revisions to working age population estimates from the HLFS (3.902 million persons in 2018Q3 versus 3.901 million in the September 2018 release). **A lower (and declining) net inflow of immigrants points to further moderation in labour force growth and potentially a tighter labour market.**



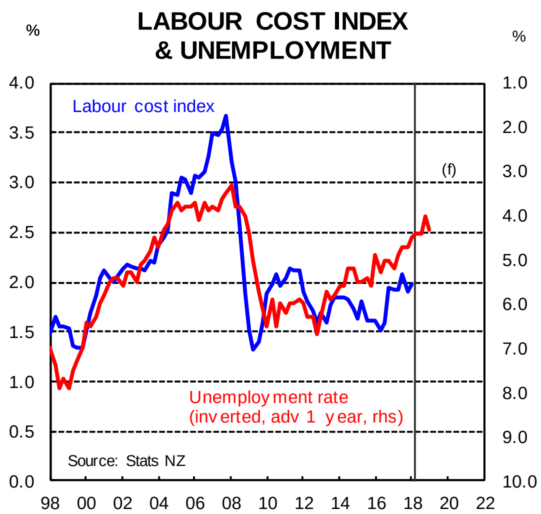
Wage growth, however, has remained modest in the context of a generally tight labour market. Private sector Labour Cost Index (LCI) wages rose 0.5% qoq in Q4, and annual LCI wage inflation ticked up to 2.0%. Boosted by higher local Government wages, LCI wages for the public sector rose 0.7% qoq (+1.7% yoy), with overall LCI wage inflation at 0.5% qoq (1.9% yoy). Wage inflation from the all-sector unadjusted LCI measure was stable at 0.9% qoq and 3.3% yoy. Average hourly earnings on the QES measure rose 1.0% qoq (+3.1% yoy).



Other measures from the Labour Cost Index provided mixed signs. In the 2018 year 44% of salary and wage rates had achieved a wage increase above 2% over the last 12 months (39% in Q3), with the 44% reporting no annual increase (47% in Q3) the lowest since June 2017. However, median and mean increases from the LCI eased in the December quarter, to 2.5% and 3.3% respectively.

Market reaction and policy implications

Today's figures suggest that the labour market is not as tight as suggested by the 2018Q3 report, which weakens the case for an OCR hike. Still-present survey volatility from the HLFS will add another layer of complexity for the RBNZ. Our expectation is that wage pressures will firm over the course of the year, but with little corroborating evidence having emerged and with firms under increasing margin pressures, there is risk around this. **If economic growth fails to strengthen after its 2018H2 lull and wage growth does not pick up, the OCR could test new lows.**



The softer than expected employment and unemployment rate prints and benign wage inflation readings contributed to a 60pip fall in the NZD/USD (currently 0.6770). **NZD interest rates eased following the HLFS report, with yields on the bellwether 2-year swap currently around record lows** (1.84%) as opposed to 1.92% at 8am this morning.

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