ANZ Research

NZ Insight: Our record breaking labour market

7 November 2022

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Contact

Finn Robinson or Miles Workman for more details.

Our record breaking labour market

Introduction

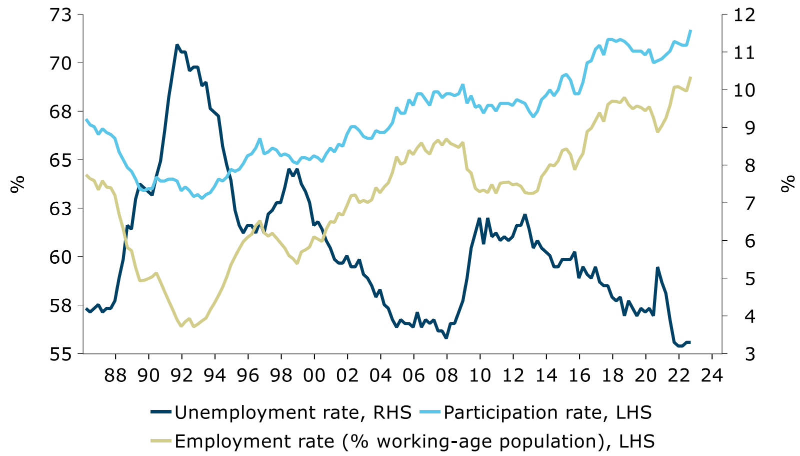
There are a lot of gloomy economic headlines out there at the moment, and that's not too surprising. Domestic inflation is way too high and still increasing, and the cure for this economic ailment – the RBNZ raising the OCR to a restrictive level to slow the economy, and likely keeping it high for some time – is not a pleasant process.

In this note we take a step back to look at some of the good news out there, by going through some of the key records that were broken by our labour market in the September quarter 2022. It's mixed news, to be fair, in that such a strong labour market means more persistent domestic inflation pressures and therefore higher interest rates than otherwise, with all the risks down the track that brings. And as a rule, the labour market does tell you more about where the economy has been than where it's going. But here and now, it means households – on average – are in a resilient position from a job security and income growth point of view as we head into 2023 and the economic headwinds start to intensify.

The labour force and employment

The unemployment remained flat at 3.3% in the September quarter – an historically low level relative to the past four decades. And the only reason it didn't fall below 3% to what would have been a fresh record low (since the HLFS data started in 1986 Q1) was that the labour force participation rate surged to a new record high of 71.7%, likely due to a combination of push factors (the rising cost of living) and pull factors (firms luring people into the labour force with high wage offers). The jump in participation helped the employment rate lift to a record high of 69.3% (figure 1), with the number of people employed in New Zealand rising 1.3% q/q – pretty remarkable considering that a record share of firms are still reporting scarce labour as the primary constraint on output.

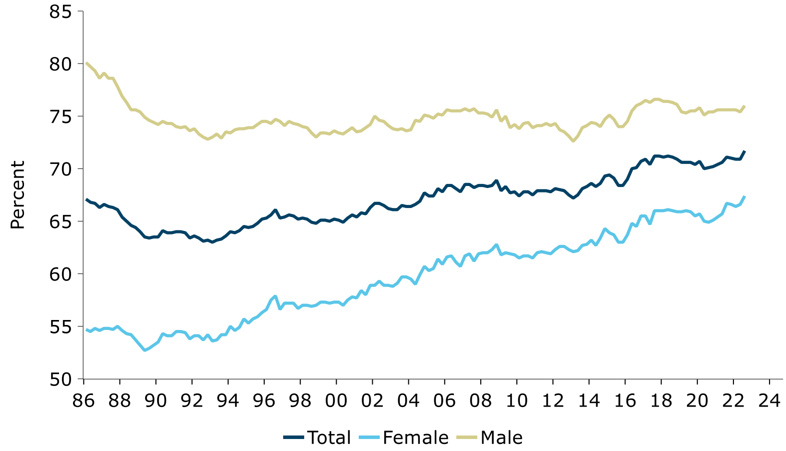
Figure 1. Participation, unemployment, and employment rates



Source: Stats NZ, Macrobond, ANZ Research

The female participation rate drove overall participation higher, reaching a new record high of 67.4% in September 2022, versus a low of just 52.7% in 1989 (figure 2).

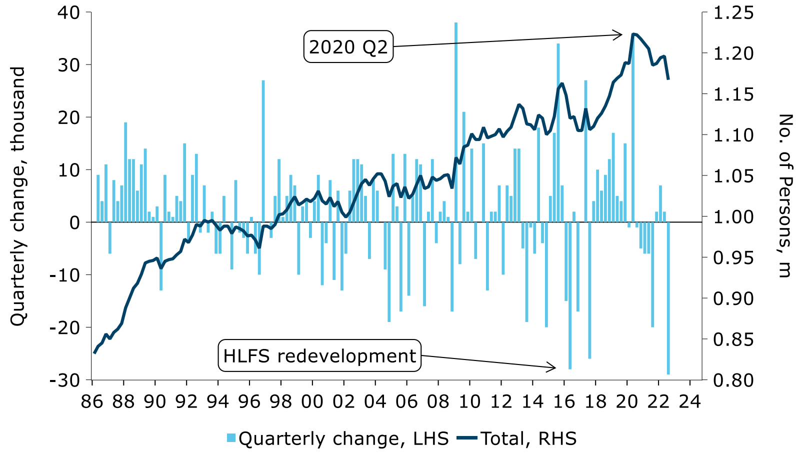
Figure 2. Participation rates



Source: Stats NZ, Macrobond, ANZ Research

Given the leap in the participation rate, it's probably no surprise that we saw the largest-ever quarterly decline in the number of people who are not in the labour force (figure 3). This is a stark contrast to other countries like the US, where significant shrinkage in the labour force in the wake of COVID is exacerbating labour shortages.

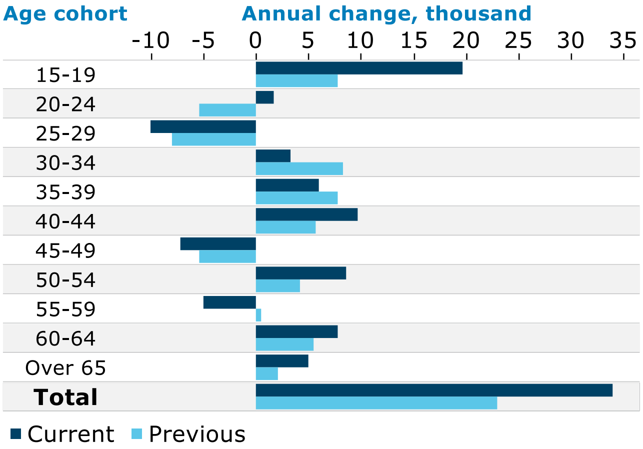
Figure 3. Figure 3. People not in the labour force



Source: Stats NZ, Macrobond, ANZ Research

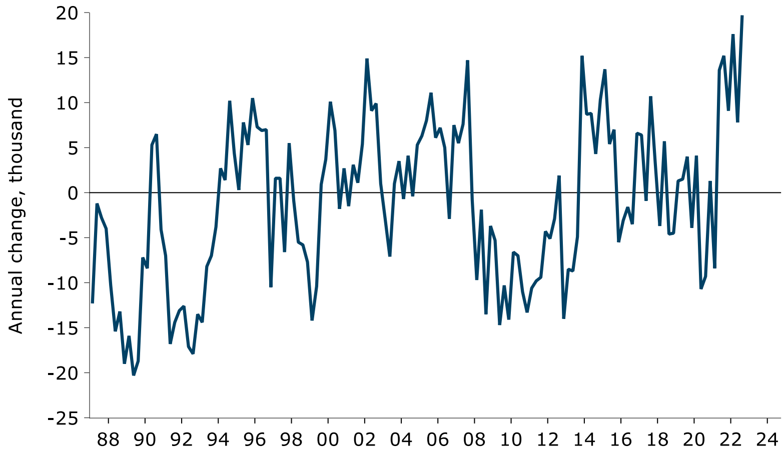
So where are all these new workers coming from? A big part of the answer is a 19.7k annual increase in the number of 15-19 year-olds in the labour force, representing by far the largest contribution to labour force growth of any age group in the year to September 2022 (figure 4). That's another record, by the way. We've never seen a larger increase in the size of the 15-19 year-old labour force (figure 5). It's important to note that this isn't necessarily all 'good' news. An after-school job for a few hours a week is one thing, but some of the higher participation in this age group probably represents people dropping out of education, and in many cases, this could be to supplement household income during this cost of living surge.

Figure 4. Annual change in labour force size by age group



Source: Stats NZ, Macrobond, ANZ Research

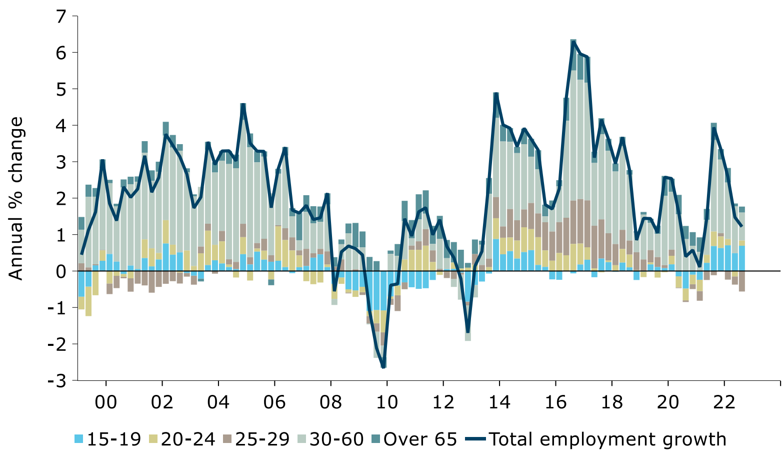
Figure 5. Annual change in 15-19 year-old labour force



Source: Stats NZ, Macrobond, ANZ Research

We can see how this record surge in youth labour force participation is flowing into stronger employment in figure 6. Of the 1.2% increase in employment in the year to September 2022, 0.7ppt came from the 15-19 age cohort. Interestingly, the 25-29 year-old age group is now a drag on employment numbers, with the working-age population for this group falling rapidly over the past two years, after peaking in early 2020. A lack of immigration, and many young Kiwis heading off on their OEs after two years of border closure, means this dynamic is unlikely to change any time soon, putting further pressure on other parts of the labour force.

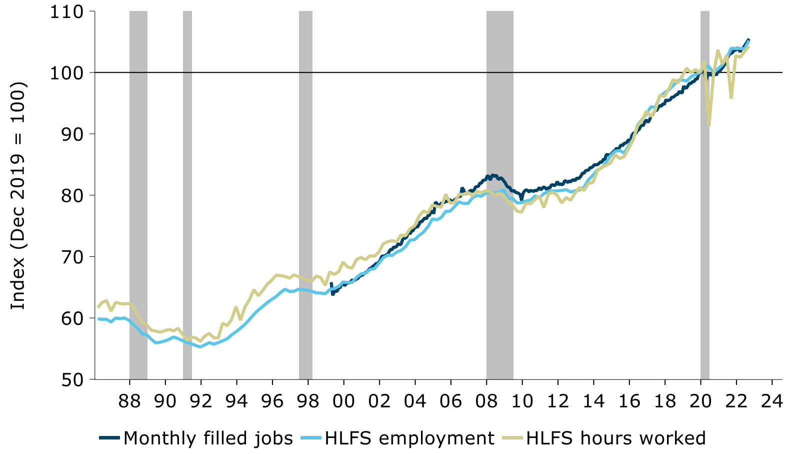
Figure 6. Contributions to annual employment growth by age cohort



Source: Stats NZ, Macrobond, ANZ Research

Aggregate measures of employment, filled jobs, and total hours worked are all now at record highs, bouncing back impressively from nearly three years of lockdowns, the border closure, and general disruption from COVID (figure 7). The rapid recovery in the labour market compared to the deep, drawn-out declines seen during previous economic downturns is striking – and was a key reason for the widespread underestimation of looming domestic inflation pressures.

Figure 7. Filled jobs, employment, and hours worked (relative to December 2019)



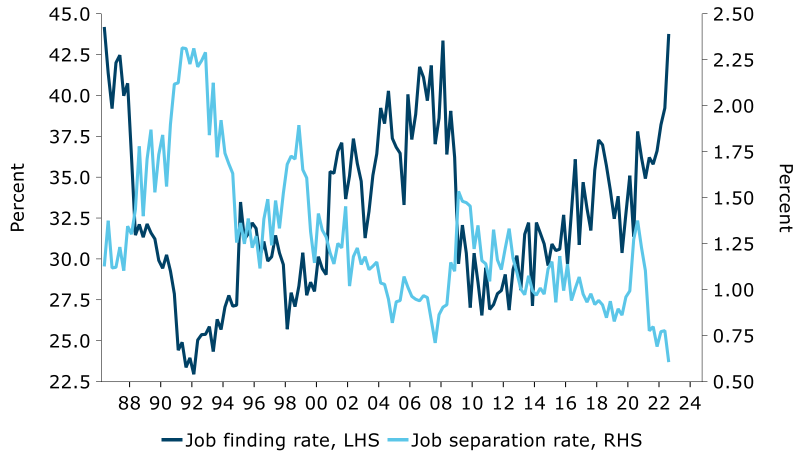
Source: Stats NZ, Macrobond, ANZ Research

Note: Grey shading represents recessions in New Zealand.

Job finding and separations

Changing tack slightly, we can look at the probability of someone losing their job (the job-separation rate), and the probability of an unemployed person finding work (the job-finding rate). The job-separation rate fell to a record low of just 0.6% in the September quarter, meaning that on this measure at least, job security has never been higher (figure 8). The job-finding rate didn't quite pip Q2 1986's record of 44.2%, but it came in a close second place, with 43.8% of unemployed people in Q2 finding jobs in Q3 (but inflows into unemployment, which happen even in a very tight labour market, mean that overall unemployment numbers remained broadly flat).

Figure 8. Job-finding and separation rates (ANZ seasonal adjustment)

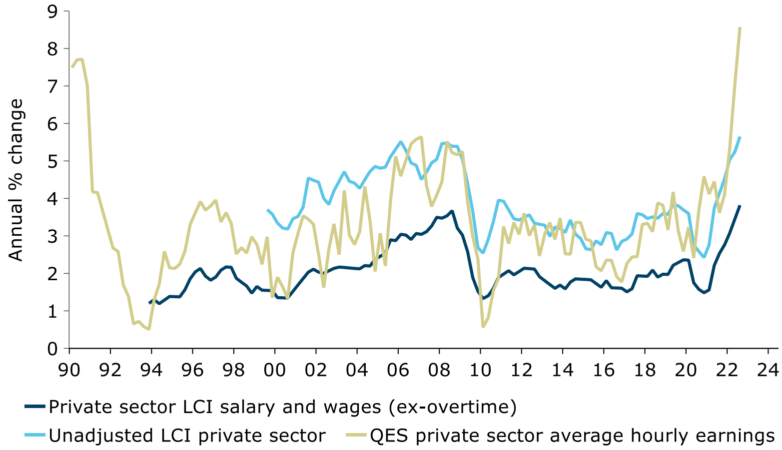


Source: Stats NZ, Macrobond, ANZ Research

Wage growth

Given the amount of records set by the labour market data, it will come as little surprise that measures of annual private sector wage growth also hit fresh highs in Q3 (in data going back to the 1990s). Private sector average hourly earnings lifted a whopping 8.6% y/y – comfortably outpacing the 7.2% lift in consumer prices over that period (figure 9). And while a lot of that 8.6% gain is gobbled up by inflation, it does still mean that Kiwi households on average are clawing back 'real' spending power from the inflation gremlin. We now anticipate private sector average hourly earnings growth will peak above 9% y/y in coming months. Income growth at the lower end of the income scale is looking likely to be higher than average, based on some recent pay settlements. That's definitely the way you want it to skew in terms of helping households through the cost of living shock.

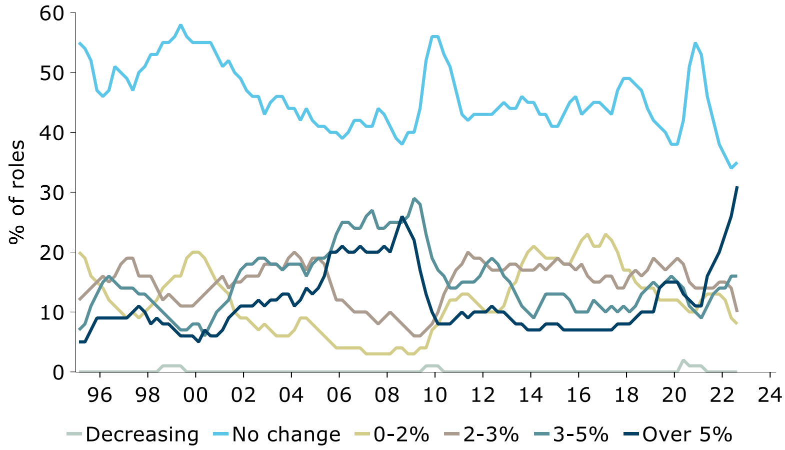
Figure 9. Private sector wage growth



Source: Stats NZ, Macrobond, ANZ Research

Illustrating the degree of wage pressure that's currently in the economy, the share of roles experiencing a larger-than-5% pay rise hit a new record high of 31% in Q3 (figure 10). Over the past year, we've seen a drop in the share of jobs seeing no change in wages, and in those receiving a smaller raise of 0-3%.

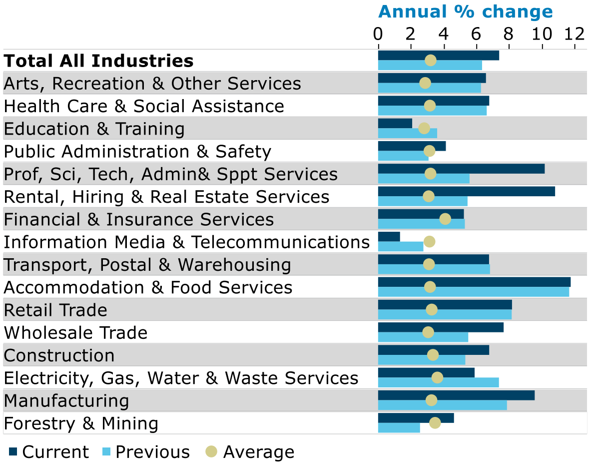
Figure 10. Distribution of annual wage rises



Source: Stats NZ, Macrobond, ANZ Research

Looking at average hourly earnings growth across industries, it's also clear how broad-based strong wage growth is (figure 11). All but two industries have above-average wage growth, and the standout is accommodation and food services, up 12% y/y in Q3, versus the historical average of 3.2% y/y.

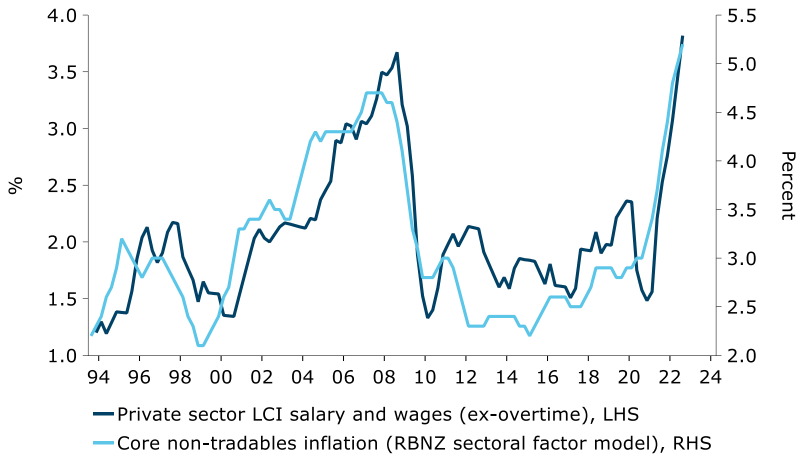
Figure 11. Wage growth by industry (including private and public sector workers)



Source: Stats NZ, Macrobond, ANZ Research

Of course, we wouldn't be economists if we didn't get our 'other hand' out and also highlight some of the challenges that can emerge from such an extremely tight labour market. The record wage gains that households are seeing are a fair and genuine reflection of current labour market dynamics (not to mentioned being a massive relief for those who have been watching their real incomes being eroded by inflation). But, steeply rising wages absent a commensurate rise in productivity are a challenge for firms to manage without passing on some of the cost, and are likely to see domestic core inflation pressures being stronger and more persistent than otherwise. That means there's a risk these large wage gains may not buy as much extra purchasing power as hoped. Figure 12 plots the close relationship between private sector labour cost inflation and the RBNZ's estimate of core non-tradables, which also hit a record in Q3. The causality runs both ways between wages and core inflation.

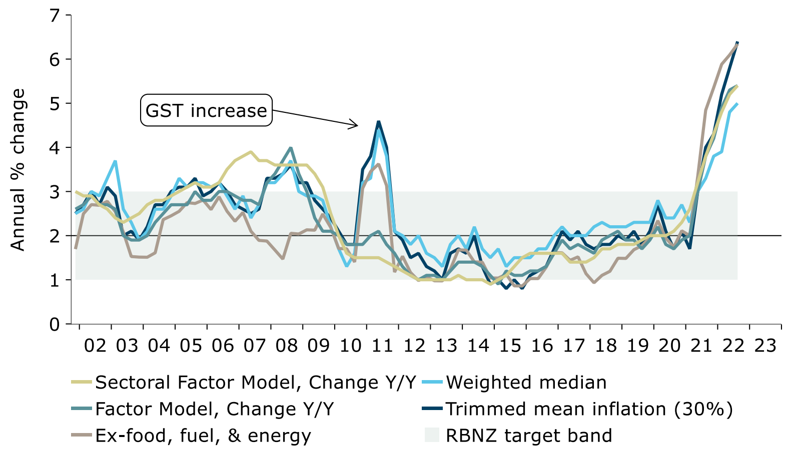
Figure 12. Labour cost inflation and core domestic inflation



Source: Stats NZ, RBNZ, Macrobond, ANZ Research

With core inflation measures also at record levels and showing no signs of turning around any time soon, the cost of living pressure that households are facing is likely to remain intense for some time yet (figure 13). And the RBNZ has no choice but to add to those pressures for indebted households by raising interest rates further.

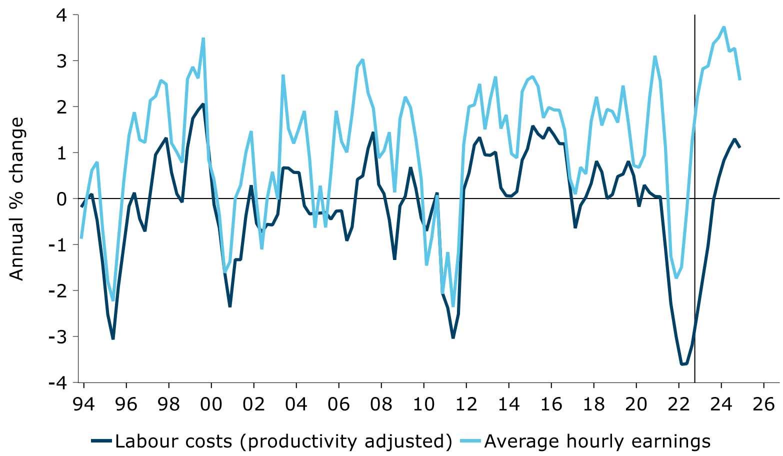
Figure 13. Core inflation measures



Source: Stats NZ, RBNZ, Macrobond, ANZ Research

But to finish on a positive note, private sector average hourly earnings are growing much faster than inflation, up 1.3% y/y on an inflation-adjusted basis in September (figure 14). And our forecast for a steady decline in CPI inflation from Q2's peak of 7.3%, if realised, implies real wage growth numbers will improve from here, possibly hitting a record high in early 2024. Just as wages lagged inflation on the way up, they are likely to lag inflation on the way down, giving households the chance to improve their real purchasing power after several years of seeing it eroded by too-high inflation.

Figure 14. Real wage growth forecast (private sector)



Source: Stats NZ, Macrobond, ANZ Research

While this note has focused on a more positive feature of New Zealand's current economic environment, that's not to suggest that things are 'easy' out there. Households aren't all 'average'. There's a distribution of wage outcomes, a distribution of wealth and a distribution of debt. Our economy is going to go through a tough time, especially over 2023 (as if the past few years haven't been difficult enough!). The Reserve Bank is battling to bring inflation down from unsustainably high levels, and while it's really important that they do this for the long-term health of the domestic economy and labour market, the bitter medicine of higher interest rates is still going to be a challenge for many households (especially heavily indebted ones) to endure. But our extraordinarily strong labour market means households are, on average, starting from a good place when it comes to income growth and job security.

Contact us

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We welcome your questions and feedback. Click here for more information about our team.

Sharon Zollner
Chief Economist

Follow Sharon on Twitter
@sharon_zollner

Telephone: +64 27 664 3554
Email: sharon.zollner@anz.com

General enquiries:
research@anz.com

Follow ANZ Research
@ANZ_Research (global)

David Croy
Senior Strategist

Market developments, interest rates, FX, unconventional monetary policy, liaison with market participants.

Telephone: +64 4 576 1022
Email: david.croy@anz.com

Susan Kilsby
Agricultural Economist

Primary industry developments and outlook, structural change and regulation, liaison with industry.

Telephone: +64 21 633 469
Email: susan.kilsby@anz.com

Miles Workman
Senior Economist

Macroeconomic forecast co-ordinator, fiscal policy, economic risk assessment and credit developments.

Telephone: +64 21 661 792
Email: miles.workman@anz.com

Finn Robinson
Economist

Macroeconomic forecasting, economic developments, labour market dynamics, inflation and monetary policy.

Telephone: +64 21 629 553
Email: finn.robinson@anz.com

Kyle Uerata
Economic Statistician

Economic statistics, ANZ proprietary data (including ANZ Business Outlook), data capability and infrastructure.

Telephone: +64 21 633 894
Email: kyle.uerata@anz.com

Natalie Denne
PA / Desktop Publisher

Business management, general enquiries, mailing lists, publications, chief economist's diary.

Telephone: +64 21 253 6808
Email: natalie.denne@anz.com

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