

# NEW ZEALAND ECONOMICS

## Labour Cost Index and Quarterly Employment Survey

### – December 2010 quarter

1 February 2011

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## WAGE GROWTH CONTAINED BUT EMPLOYMENT INDICATORS WEAK

#### KEY POINTS

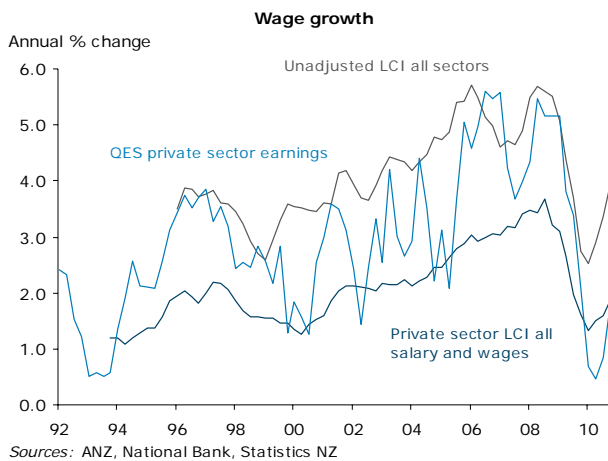
- Today's wage data showed a modest lift, but annual wage inflation remains moderate, and not of immediate concern to the Reserve Bank.
- LCI private sector wage inflation (excluding overtime) rose by 0.6 percent (1.9 percent y/y) in the December quarter, slightly above market expectations. Including overtime, quarterly private sector LCI wages increased by 0.6 percent (1.9 percent y/y).
- The unadjusted LCI rose by 1.0 percent (4.0 percent y/y). This is not the preferred measure, but the higher rates of wage inflation on this measure are worth noting.
- After showing strong rates of growth over the past few years, public sector ordinary time LCI wage growth continues to undershoot that seen in the private sector, increasing by only 0.4 percent in the December quarter (1.4 percent y/y).
- The QES wage measures are more volatile. QES private sector ordinary average hourly earnings rose by 0.6 percent (1.8 percent y/y).
- In seasonally adjusted terms, paid hours from the QES fell by 0.2 percent, whereas filled jobs fell by 0.9 percent in the December quarter. Although the correlation is loose, this suggests the Q4 employment readings from this Thursday's HLFS may be weaker than we thought.

	LCI private sector ordinary time		QES private sector ordinary time		QES paid hours	
	q/q	y/y	q/q	y/y	q/q	y/y
Mar-08	0.7	3.5	1.1	4.5	-0.2	2.3
Jun-08	0.8	3.5	2.1	5.6	0.1	1.3
Sep-08	1.1	3.7	1.0	5.2	-0.5	0.7
Dec-08	0.7	3.2	0.9	5.2	-1.4	-2.0
Mar-09	0.5	3.0	1.1	5.2	-0.8	-2.6
Jun-09	0.3	2.6	0.8	3.9	-1.4	-4.1
Sep-09	0.4	1.9	0.7	3.5	-0.3	-3.8
Dec-09	0.3	1.5	-0.4	2.2	0.0	-2.5
Mar-10	0.3	1.3	-0.4	0.6	1.0	-0.8
Jun-10	0.4	1.4	0.6	0.4	1.1	1.8
Sep-10	0.6	1.6	1.0	0.7	0.3	2.3
<b>Dec-10</b>	0.6	1.9	0.6	1.8	-0.2	2.1
<b>ANZ</b>	<b>0.6</b>	<b>1.9</b>	<b>0.4</b>	<b>1.6</b>	<b>0.6</b>	-
Market	0.5	1.8	0.6	1.8	-	-

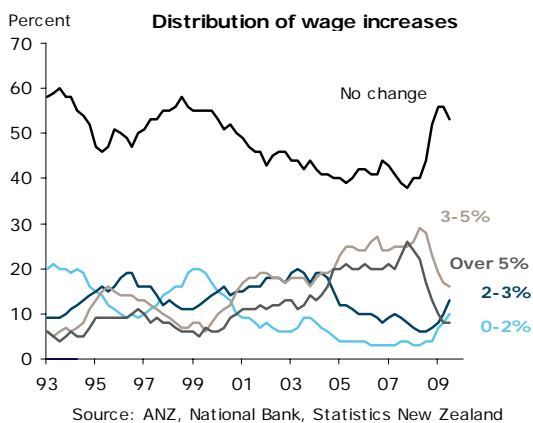
## DATA REVIEW

## DATA WRAP

**LCI private sector wage inflation (excluding overtime) rose by 0.6 percent** (1.9 percent for the December 2010 year). This was marginally stronger than the market consensus of a 0.5 percent increase. Public sector wage rates increased 0.4 percent, with annual wage inflation on this measure (1.4 percent) close to decade lows. Private sector ordinary time hourly earnings from the QES rose by a moderate 0.6 percent in December (+1.8 percent y/y).



**While moderate wage growth is to be expected at this stage in the cycle, not all of the wage measures were contained.** The private sector unadjusted LCI wage measure (which adjusts for employment shifts between industries and occupations but not for increases due to quality changes within occupations) recorded a 1.0 percent quarterly increase, with the annual rate of wage inflation jumping up to 4.0 percent.

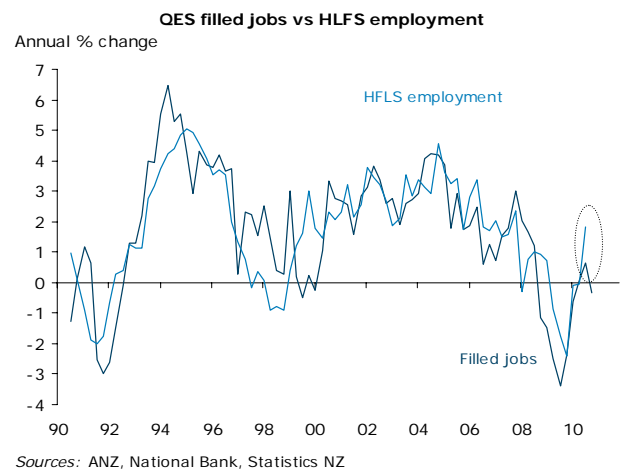


**The distribution of annual increases from the LCI did not highlight a broad based strengthening in wage pressure.** The portion of

wage increases greater than 3 percent (23 percent of the total in the December 2010 year) rose fractionally from their September year trough but remain well below 2008 levels. With nearly 50 percent of jobs not receiving a wage increase in the December year, bargaining power is still weighed towards employers.

**However, there still appear to be pockets of strength.** Across the occupation groups reported in the LCI, annual increases ranged from 0.1 percent (for printing) to 2.8 percent (for professional, scientific and technical services). Higher wage rates were generally in evidence for primary sector industries and manufacturing, with construction sector LCI wage inflation (at 1.6 percent y/y) remaining contained for now.

**Inflation from the government sector provided mixed signals.** Salary and wage rates from the local government sector registered a hefty 1 percent quarterly increase, although annual inflation (at 1.9 percent y/y) remains moderate. The tight fiscal rein is being increasingly reflected in low central government wage growth (+0.3 percent q/q, +1.4 percent y/y).

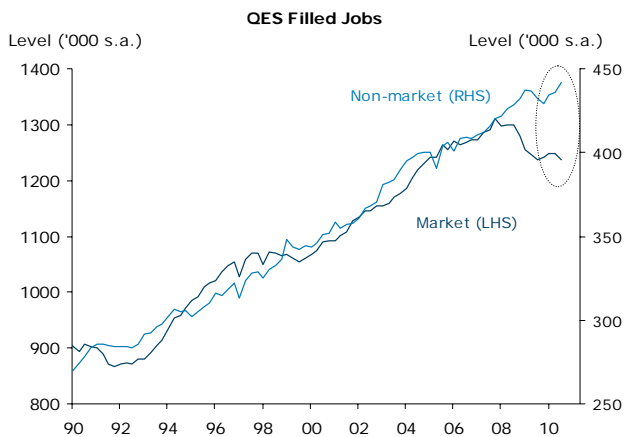


**An important focus leading up to Thursday's HLFS will be December quarter employment.** On this front the 0.9 percent seasonally adjusted fall in QES filled jobs in December was weaker than we had expected. The correlation between quarterly movements in employment from the HLFS and QES measures is not particularly tight (correlation coefficient of 0.5) but at face value it suggests some downside risk to our 0.2 percent pick for quarterly HLFS employment. QES measures for employment remain considerably below mid 2008 peaks (3.6 percent lower for QES filled jobs and 2.4 percent lower for QES paid hours).

## DATA REVIEW

**Filled jobs by sector showed a weak picture.**

Market sector filled jobs declined by 1.2 percent, with much of the weakness evident in filled jobs for domestic-orientated sectors, particularly services, although there were one or two exceptions. Retail employment fell 1 percent, with the 3.4 percent slump in accommodation and food services sector employment also likely to reflect the weak discretionary spending environment. Manufacturing filled job numbers were broadly unchanged, with construction sector jobs increasing 1 percent.

**Employment readings for the non-market sector showed offsetting movements.**

A 3.0 percent fall in public administration (which reversed the Q3 rise) was offset by strong increases in employment for education (up 1.5 percent) and health (up 0.4 percent) are consistent with the Government's strategy of redirecting funds to frontline public services.

**Of some concern for the rebalancing of the economy was a further drop in filled jobs for export-orientated firms** (-0.1 percent q/q), with employment in this sector now 14 percent below June 2008 levels.

**However, the QES suggests a more employment rich recovery may be in prospect.** With paid hours per employee now above historical average, with increasing demand for labour now likely to be met from more employment.

**On another positive note, the climb in average hourly earnings produced a 0.6 percent increase in gross earnings**, which were 4.0 percent higher than a year ago. With the October 2010 tax cuts, after tax earnings growth would have been even stronger. While the process of household balance sheet repair has some way to run, wage earners may convert some of their additional earnings into spending.



On the face of it, this suggests we could see a pick-up in consumer spending and housing market activity towards the middle of 2011.

**IMPLICATIONS**

**Today's labour market outturns suggest a softer than expected HLF5 outturn for Thursday.** There is a chance that the unemployment rate could come in higher than our above consensus forecast of 6.6 percent. A high unemployment rate may encourage wage earners to maintain precautionary saving and could limit the flow through into consumer spending.

**The RBNZ will be broadly comfortable with the moderate wage backdrop.** Wage growth typically lags the economic cycle, so relatively low rates of wage inflation at this juncture are of little surprise, with LCI annual wage inflation still tracking along at moderate levels.

**The RBNZ remain comfortable that the spike in consumer price inflation will not spill into higher wages.** So far so good, but wage data will need to be closely watched over the coming year or two. **We are not out of the woods yet. Annual CPI inflation is set to peak at a time when the demand for labour is improving.** With skill shortage measures in the QSBO moving up, and a risk of more permanent and long-term (PLT) departures to Australia to assist with reconstruction work following the Queensland floods, the risk is that upward wage inflation pressures could emerge much sooner than initially thought.

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