

Labour Market Data Preview: June 2008 quarter

(LCI and QES due 10.45am 4 August, HLFS due 10.45am 7 August)

Key points

- > Too early to see wage inflation figures turning yet in response to the economic cycle.
- > Employment figures a lottery given recent volatility.
- > The unemployment rate should rise to an 18-month high. Anecdotes suggest upside risk.
- > Market may entertain thoughts of 50 bps in September if the unemployment rate does surprise on the upside. To us though, the hurdle to such a move will remain high.

March quarter 2008 expectations		
	ANZ National	Market
LCI salary and wage ordinary time (private sector)	0.8% q/q 3.6% y/y	0.8% q/q 3.6% y/y
QES salary and wage ordinary time (private sector)	1.5% q/q 4.3% y/y	1.1% q/q 4.5% y/y
HLFS unemployment rate (s.a.)	3.8%	3.8%
HLFS participation rate (s.a.)	67.7%	67.7%
HLFS employment growth	0.2% q/q -0.6% y/y	0.1% q/q -0.6% y/y

Wage growth is expected to remain elevated in the June quarter. We expect the Labour Cost Index (LCI) measure of private sector ordinary time earnings (which is quality adjusted and hence a pure wage inflation measure) to record an increase of 0.8 percent in the June quarter, taking annual growth to 3.6 percent from 3.5 percent in March. This will be a record high for this survey. For completeness, the less reliable Quarterly Employment Survey (QES) wage indicator – which is volatile and influenced by compositional changes – is expected to increase by 1.5 percent in the quarter, taking annual growth to 4.3 percent. The 6.7 percent increase in the adult minimum wage from 1 April along with the scrapping of the youth minimum wage (except for new entrants) will have had some effect in the June quarter.

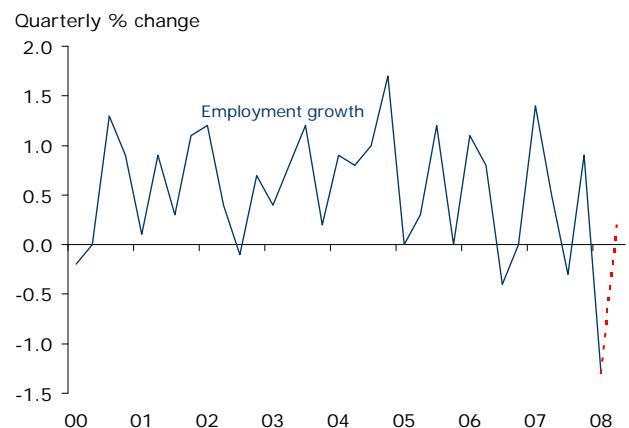
It is too early to see wage inflation figures turning yet in response to the economic cycle.

Wages are typically one of the last economic indicators to turn in response to a weaker economic environment and this cycle is expected to be no different. Looking forward we envisage a very “split personality” dynamic, with pockets which continue to report skill shortages such as health, IT and the like remaining robust, but other areas, and particularly less skilled, easing.

The HLFS is unlikely to lose its “volatile” tag. We expect employment to increase by 0.2 percent in the June quarter, but this largely reflects a rebound from

what looked like an outsized move in Q1. Rather than look at the quarters individually, we feel the March and June quarter results should be treated as one. An average fall in employment of 0.5 percent per quarter feels about right considering the anecdotes towards the labour market we have received and evidence suggested by recent business sentiment surveys, where employment intentions have trended lower since the start of the year.

Volatile employment growth



The participation rate, as always, poses a fair degree of risk to our estimates. We expect the participation rate to remain unchanged at 67.7 percent in the June quarter. But given the 0.9 percentage point fall in participation from the December quarter, the chance of a rebound appears high. We expect the unemployment rate – a more stable gauge and better indicator of the state of the labour market – to rise from 3.6 percent in March to 3.8 percent in June (an 18-month high), although would not rule out a bigger move higher.

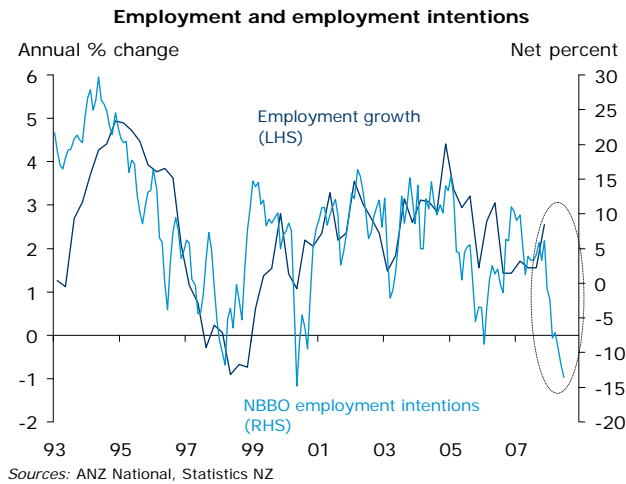
We see the participation rate as a key area to watch going forward. Historically it has tended to smooth out movements in the unemployment rate as people move in and out of the labour market. However, with growing pressure on household budgets, the participation rate may prove more sticky compared to the past, resulting in a sharper turn in the

unemployment rate itself over the second half of the year.

Just like in the March quarter, weakness in employment growth is likely to come through from housing-related sectors. Our seasonally adjusted estimates of jobs growth showed that the biggest falls in employment in March were recorded in the distribution sector (wholesale and retail), business and financial services, and also construction. Although the sectoral data is notoriously volatile on a quarterly basis (as is the whole HLFSS survey to be fair), we expect similar themes to be present in the June quarter. These sectors were at the forefront of the previous economic expansion and now look to be at the forefront on the other side as the economy enters a correction and rebalancing phase.

With the housing market yet to find a trough and corporates now clearly responding to a weaker outlook via costs, we expect the unemployment rate to quickly move towards 5 percent. Confidence surveys are flagging a 1 percent contraction in employment growth this year.

From a market perspective, any upside surprise in the unemployment will have the market thinking about a larger (50 bps) move in September. While we can sympathise, we believe the hurdle to a larger move will remain high given the inflationary backdrop. Financial stability is the wildcard in regard to seeing potentially larger moves. At this stage we continue to envisage a series of steady 25 basis point cuts at every meeting until the end of the year.



While pockets of strength (such as agriculture) will obviously support prospects, the reality is that 60 percent of employment growth has been centred in housing-centric industries over the past five years.

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ANZ, Level 7, 1 Victoria Street, Wellington 6011, New Zealand Phone 64-4-802 2000 Fax 64-4-496 8639 <http://www.anz.co.nz> e-mail ecnmcs@anz.com