

### Labour Market Data Preview: December 2007 quarter

(LCI and QES due 10.45am 5 February, HLFS due 10.45am 7 February)

#### Key points

- > Wage inflation to keep the RBNZ on alert to pending cost-push inflation pressure.
- > The HLFS report is likely to throw up a mixed bag, showing a rebound in employment growth but a slightly higher unemployment rate courtesy of a rise in the participation rate.
- > On balance, the labour market will remain tight and continue to provide late cycle economic support.

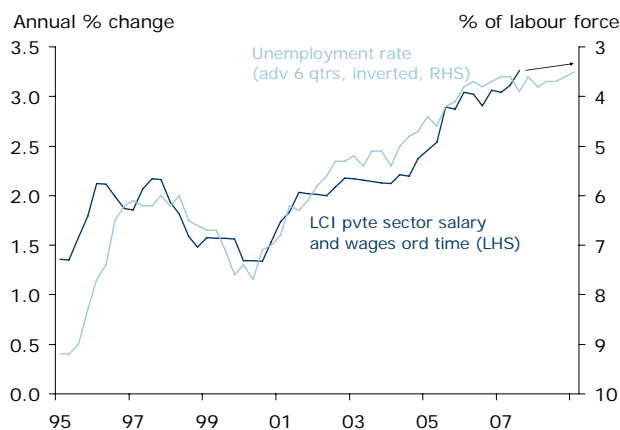
#### A new record high for wage growth is expected.

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 0.9 percent in the December quarter, taking annual growth to 3.3 percent – a new record high. Public sector wage growth is also expected to increase by 0.9 percent in the quarter, although annual growth will only sit at 3.0 percent. This will represent the third consecutive quarter where annual private sector wage growth has outpaced its public sector counterpart, although part of this strength is a result of catch-up to previously strong public sector wage growth. For completeness, the less reliable Quarterly Employment Survey (QES) wage indicator – which is volatile and influenced by compositional changes – is expected to increase by 0.8 percent in the quarter, taking annual growth to 3.9 percent.

#### Wage growth looks set to remain elevated for some time given the tightness in the labour market.

Firms reporting difficulty in finding both skilled and unskilled labour increased in the latest QSBO survey and remain well above historical averages. The historical lagged relationship between wages and the unemployment rate suggest wage growth could remain at current levels (or even trend up slightly) for the next 12 to 18 months.

Wages and unemployment rate



Sources: ANZ National, Statistics NZ

#### On the employment front, the HLFS results are expected to show a mixed bag.

The September quarter survey threw up a puzzling fall in employment along with a lower unemployment rate, caused by a sharp fall in the female participation rate. Quarter on quarter, the HLFS has been notable for volatile outcomes over the past five years with a standard deviation of 0.6 percent for employment growth.

Volatile employment growth



Sources: ANZ National, Statistics NZ

We expect the reciprocal to the September quarter results, with stronger employment but gains to be met via a rising participation rate. This should contribute to the unemployment rate increasing slightly from 3.5 percent to 3.6 percent.

#### Net-on-net, the message will remain that the labour market is tight

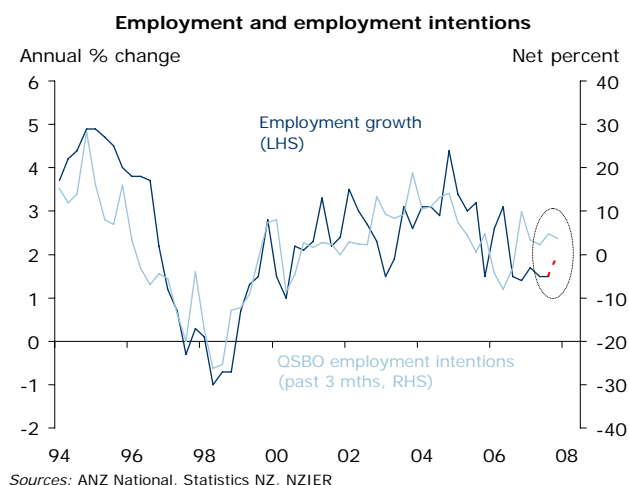
and a key source of inflationary risk for the Reserve Bank. Of course this can be countered by the observation that the labour market is a lagging indicator. And as the recent US experience shows, when the labour market turns, the horse has normally already bolted. With house prices already starting to ease, we are left wondering what could eventuate if (once) the labour market does indeed turn. But facing stronger core inflationary pressure than other central banks (apart from the RBA), the Reserve Bank has little choice but to take a stern line.

Looking at the forward picture, employment intention surveys continue to suggest strong demand,

as does the shop window test walking down main streets. The growing gap between such surveys and actual employment will no doubt be indicative of scarcity, which in turn should keep wage inflation elevated for a while yet.

Yet it is the relativity between employment intentions (solid) versus investment intentions (easing) that leaves us perplexed, particularly as pricing signals are supportive of a rotation from the former to the latter. The current picture is not only a harbinger of wage inflation, but of woeful productivity performance, which in turn is a key influence on inflation trends. The Reserve Bank's job could be greatly assisted by improvements in productivity growth, and while Q3 data suggested an uptick, HLFS data for Q4 and survey trends suggest it will not be sustained.

**The balance of risks on employment look skewed to the upside**, particularly given the autoregressive pattern in recent outturns. **While a likely reminder that rates are on hold for a considerable period, and a hike cannot be completely ruled out, we expect offshore developments to hold sway.**



December quarter 2007 expectations		
	ANZ National	Market
LCI salary and wage ordinary time (private sector)	0.9% q/q 3.3% y/y	0.8% q/q 3.2% y/y
QES salary and wage ordinary time (private sector)	0.8% q/q 3.9% y/y	0.9% q/q 4.0% y/y
HLFS unemployment rate (s.a.)	3.6%	3.6%
HLFS participation rate (s.a.)	68.5%	68.4%
HLFS employment growth	0.5% q/q 2.0% y/y	0.4% q/q 1.9% y/y

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