ANZ Research

# Q2 Labour Market Data Preview

28 July 2021

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Contact

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## Now hiring

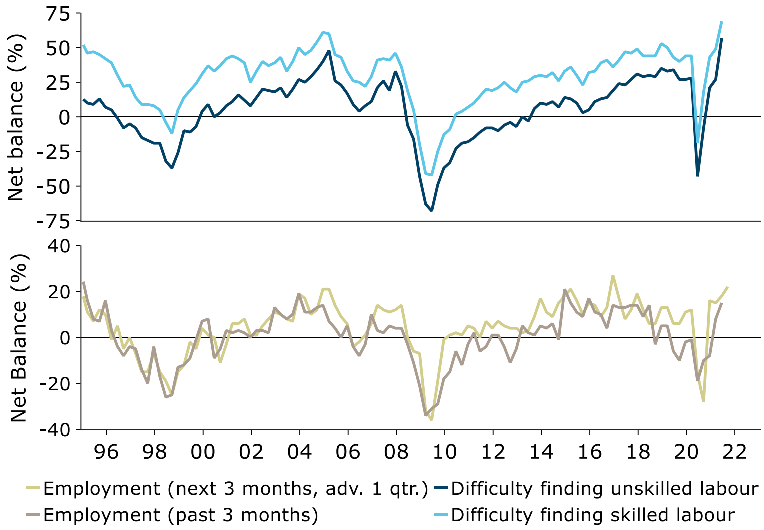
- Stats NZ release Q2 labour market data on 4 August next week.
- Robust labour demand is helping to drive a tightening in the labour market, with very strong prints for job ads, employment intentions, and monthly filled jobs over the June quarter. As a result, we expect that the unemployment rate declined from 4.7% in Q1 to 4.4% in Q2, driven by a 1.0% q/q (1.5% y/y) rise in employment.
- We expect wage inflation will have jumped as record labour market tightness, exacerbated by the closed border and the Q2 increase in minimum wage, sees firms willing to pay top dollar. We think labour costs rose 2.4% y/y, and that hourly earnings rose 4.5% y/y.
- Labour market indicators show that employment is already at or close to full employment, and with inflation running at 3.3% y/y in Q2, another strong labour market print will add further pressure for the RBNZ to hike the OCR on 18 August.

### Key points

Labour market data for the June 2021 quarter are released on 4 August.

The labour market has demonstrated remarkable resilience in the aftermath of the COVID recession, and timely indicators suggest that this strength continued over Q2. Actual and expected employment in the QSBO increased, while difficulty finding skilled and unskilled labour have both hit record highs (figure 1). Job ads have blown through records month after month, and combined with our unemployment forecast in Q2, imply a record level of labour market tightness. These indicators have contributed to our assessment that employment is probably already at or close to full employment. We've already reached a cyclically very tight labour market (although structurally, we still have room for improvement, in particular with Māori unemployment still at 8.4%, versus 4.7% nationwide).

**Figure 1. QSBO employment indicators**




Source: NZIER, Macrobond, ANZ Research

June 2021 Quarter

| | | Exp | Prev |
|---|---|---|---|
| **Labour Market** | | | |
| Unemployment rate (sa) | % | 4.4% | 4.7% |
| Participation rate (sa) | % | 70.6% | 70.4% |
| Employment (sa) | q/q | 1.0% | 0.5% |
| Employment | y/y | 1.5% | 0.3% |
| **Wages** | | | |
| LCI private sector wages (ex-overtime) | q/q | 1.0% | 0.4% |
| LCI private sector wages (ex-overtime) | y/y | 2.4% | 1.6% |
| QES private sector hourly earnings | q/q | 1.7% | -0.1% |
| QES private sector hourly earnings | y/y | 4.5% | 3.0% |

Monthly filled jobs data does suggest that firms are still filling vacancies at a surprisingly rapid pace, with jobs up 1.1% m/m (2.4% y/y) in June alone (figure 2). Consequently, we think that overall employment increased 1.0% q/q (1.5% y/y) in the June quarter. And that should see unemployment tick down from 4.7% in Q1 to 4.4% in Q2, despite our expectation that the participation rate will recover further to 70.6% from 70.4% previously (figure 3).

**Figure 2. HLFS Employment and monthly filled jobs**

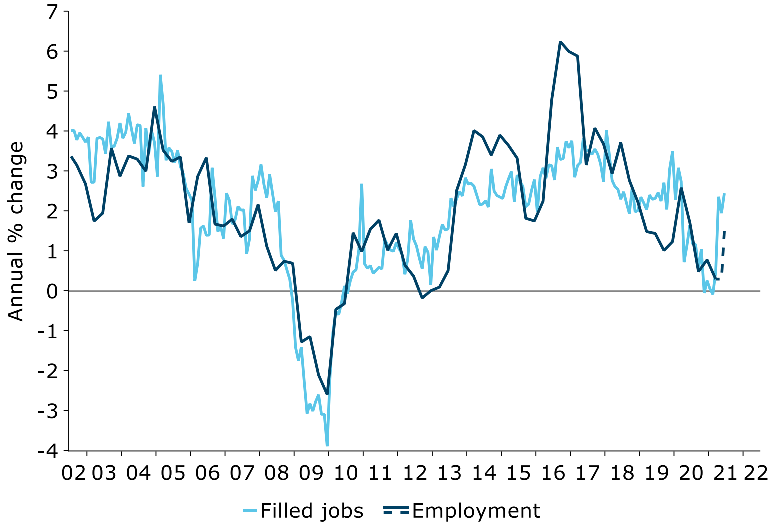



**Figure 3. Unemployment and participation rate forecasts**


Source: Stats NZ, Macrobond, ANZ Research

Not unusually, the main area of uncertainty around our forecast is the participation rate. This increased from 2013 to 2018 but then plateaued, with population aging offsetting the impact of higher participation by women and older workers. But we're now seeing a cyclical recovery in participation as the labour market bounces back from COVID. At some point, the net impact of these forces may become negative, leading to a lower participation rate than expected. Were this to happen in Q2, it would only exacerbate labour shortages, putting more upwards pressure on wages and wider inflation momentum.

Of course, employment growth could also come in slower than the 1.0% that we've pencilled in. But given the extremely high levels of labour market tightness and ongoing strong demand for labour (figure 1), we think a weak employment print would likely be due to a lower-than-expected participation rate, or residual matching issues due to COVID. Both of these are supply-side issues (ie inflationary for wages).

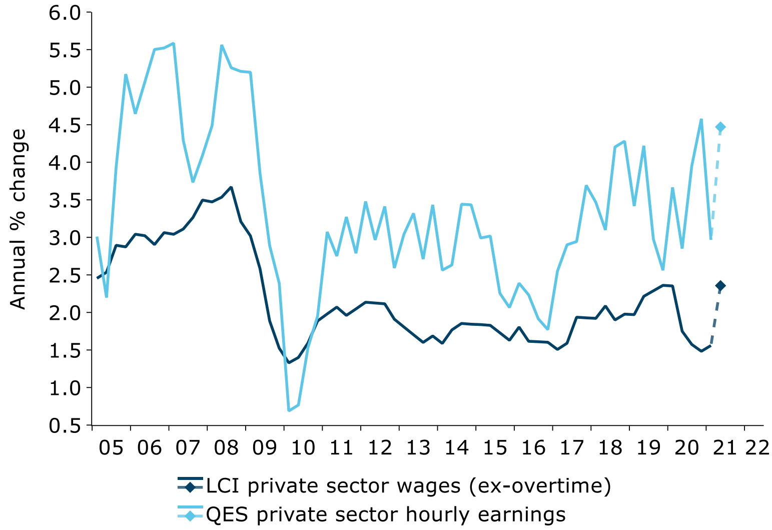
The increases in measures of labour market tightness (some to record levels) show that workers are in increasingly hot demand. And with living costs rising rapidly and household inflation expectations having soared to 5%, conditions are ripe for a surge in wages in New Zealand.

Across the country finding staff across all skill levels is becoming increasingly difficult – and that means that the labour market is a seller's market at the moment (ie workers have the bargaining power right now). If firms aren't willing to shell out top dollar for staff, then people can relatively easily jump ship and find jobs with businesses who will. This is something that we've also seen overseas, with quit rates in the US jumping in recent months. These 'job-to-job' transitions are actually a key driver of large wage rises in New Zealand (in fact, a lack of job-to-job movements was one explanation for low wage growth after the GFC).

The recent rise in the minimum wage to $20/hr will also put upward pressure on wages, particularly towards the bottom end of the income distribution. Given the sheer amount of labour demand, the higher minimum wage is less likely to have a negative impact on employment. And it likely means that workers who were previously only a bit above minimum wage may be more successful at extracting a larger salary increase so that they remain above the new minimum rate.

All up, we think that labour costs accelerated sharply in the June quarter, up 1.0% q/q (2.4% y/y – figure 4). That would be the largest quarterly increase since 2009. Looking at hourly earnings, we expect to see wages jump 1.7% q/q (4.5% y/y). It's not clear how long the tight labour market will take to feed through into wages – people need to go through pay reviews or the hiring process before bigger pay cheques land in their bank account. But with the labour market so tight, we do think we'll see very strong wage pressure this year, even if it takes a little longer to come through than we've forecast.

**Figure 4. Wage inflation measures**




Source: Stats NZ, Macrobond, ANZ Research

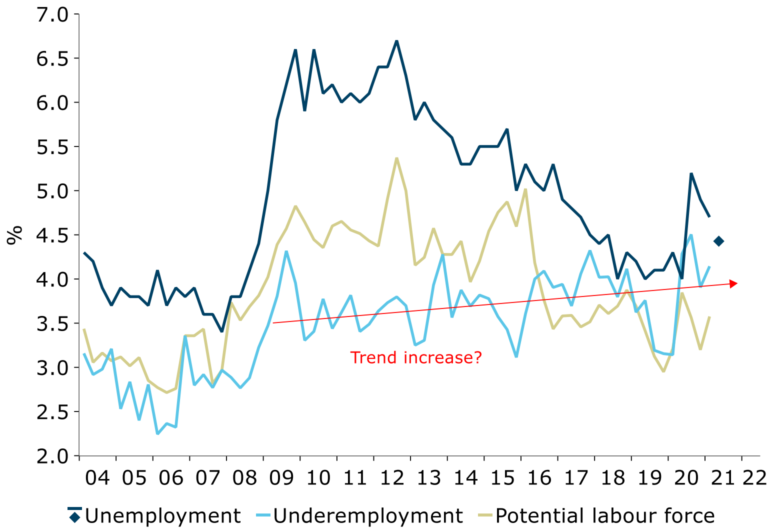
## RBNZ implications

Next week's labour market data is the final big piece of data the RBNZ will get before the August MPS (except the Q3 Survey of Expectations out 12 August, which will give them an update on their most-trusted measure of inflation expectations). It's hard to see a scenario where the data doesn't reaffirm that the OCR should to be hiked at that meeting. Given the sheer strength in indicators of labour demand, any disappointing headline unemployment or employment numbers will likely stem from supply-side factors like reduced participation or continued matching issues. These factors would all act to push wages and prices higher, consistent with our view that August is odds-on as the date of OCR lift-off, barring a COVID outbreak in the meantime.

A final thing to note is that in the most recent Monetary Policy Review the RBNZ was at pains to highlight the "reported underutilisation of labour" as one reason to be cautious about the outlook for inflation over the medium term. At the time, we noted that that was a conclusion one could make based on Q1 data, but given recent indicators of labour market slack for Q2, it's hard to make the case that there's much (if any) spare capacity left in the labour market.

It's true that in Q1, underemployment and unemployment were both still above pre-COVID levels (with underemployment possibly up in a structural sense since the GFC – figure 5). And that was probably still the case in Q2 as well.

**Figure 5. Components of underutilisation**




Note: The potential labour force captures people who don't quite meet the definition of unemployed. They are either 1. actively seeking work but not available in the reference week of the survey, or 2. not actively seeking work but were available in the reference week of the survey and want a job (this captures discouraged workers). See Stats NZ's introduction to underutilisation statistics for more detail.

Source: Stats NZ, Macrobond, ANZ Research

But it also looks like the NAIRU is currently higher. Distortions in the economy mean that matching employers and job-seekers is more difficult at the moment. If monetary policy tried to achieve pre-COVID unemployment and underutilisation numbers regardless, it would generate significant inflation and a boom-bust that wouldn't actually help workers (or firms) in the medium term.

Put another way, based on indicators like job ads, we're considerably more confident about the fact that we're already at or above full employment, than we are about what precisely that number is at the moment. Whatever the published employment and underutilisations numbers, unless something comes along to change the economic picture, we think robust wage inflation will support strong underlying inflation pressures over this year, necessitating OCR hikes to cool things down and put us onto a more sustainable path.

# Contact us

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


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