ANZ Research

Q1 Labour Market Data Preview

29 April 2021

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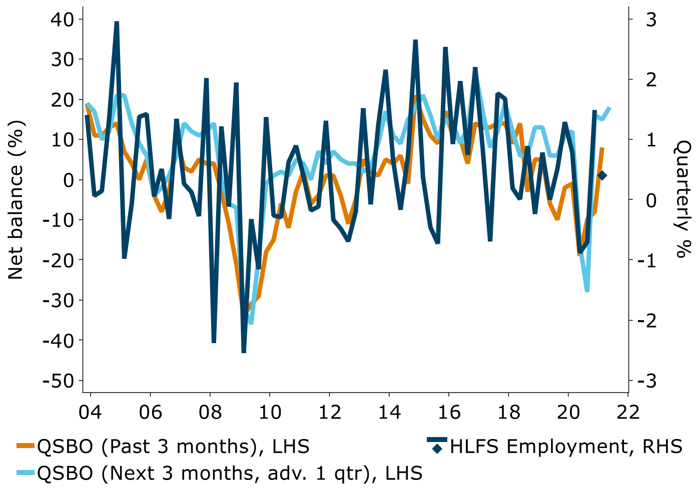
Participation puzzle

- Next week Stats NZ release labour market data for the March quarter.
- We expect that strong labour demand saw employment rise 0.4% q/q in Q1 (0.6% in Q4 2020), although a summer without international tourists means some sectors will have lost workers. Rising participation rates are likely to see the unemployment rate tick up to 5.1% (4.9% previously).
- A key uncertainty is to what extent rising labour force participation rates may offset jobs growth, leaving unemployment higher. Feasible unemployment outcomes for Q1 range from 4.5%-5.5%, depending on what happens to participation.
- The RBNZ will be unmoved by next week's data, even if it's a stronger print than expected. Current inflation pressures are from mostly transitory sources, and a tight labour market would be a welcome source of more-sustained inflation pressure. But, the RBNZ will be looking for confirmation that the labour market will continue improving into the medium term, and it won't get that for a while yet.

Key points

March quarter labour market data are released next week (Wednesday 5 May). There's considerable scope for surprise this quarter (again), with many mixed signals complicating the picture. We've seen very strong labour demand over Q1, with job ads at record highs, and employment intentions in the ANZ Business Outlook rising over Q1. But firms also report that they simply cannot find the workers they need, despite there being an extra 25,000 unemployed job seekers at the end of 2020, compared with 2019. And some sectors will likely have shed more jobs, especially in tourism and hospitality, after enduring a March quarter without international tourists – usually the busiest time for our tourism operators.

Figure 1. HLFS employment vs QSBO experienced and expected employment



Source: Stats NZ, NZIER, Macrobond, ANZ Research

March 2021 Quarter

		Exp	Prev
Labour Market			
Unemployment rate (sa)	%	5.1%	4.9%
Participation rate (sa)	%	70.5%	70.2%
Employment (sa)	q/q	0.4%	0.6%
Employment	y/y	0.1%	0.7%
Wages			
LCI private sector wages (ex-overtime)	q/q	0.5%	0.5%
LCI private sector wages (ex-overtime)	y/y	1.7%	1.5%
QES private sector hourly earnings	q/q	1.1%	1.1%
QES private sector hourly earnings	y/y	4.1%	4.4%

The challenge is to try to work out how all of these moving parts translate into quarterly labour market statistics. One thing we can say with some confidence is that overall employment is unlikely to have declined, and has probably increased. The recent QSBO, for example, showed a strong rise in experienced employment in Q1, while the forward-looking measure (which has actually correlated better with actual employment in recent quarters) points to high levels of labour demand over mid-2021 (figure 1).

If we were to take the QSBO at face value, we'd probably forecast a 1.0% q/q rise in employment over the March quarter, which would see employment up 0.7% y/y, and unemployment down into the low 4s (if participation was unchanged). However, it's impossible to ignore the matching issues and difficulty finding labour that's plaguing hiring managers across the country. So we've landed on a modest rise of 0.4% q/q, which sees employment up just 0.1% y/y. That's also broadly consistent with the monthly filled jobs data published by Stats NZ this morning, which shows jobs growth was 0.5% y/y in year to March 2021.

Strong employment growth is good news, but it doesn't necessarily mean that the unemployment rate will fall. A quick back-of-the-envelope calculation shows that depending on what happens to the labour force participation rate, even a strong 1.0% q/q rise in employment could see unemployment rise if participation recovers faster than expected (table 1).

Table 1. Range of possible unemployment rate outcomes

Employment growth (q/q, last 0.6%)		Participation rate (last 70.2%)		
	Darker blue = more likely	*Small fall to 70.0%*	*Moderate increase (Central = 70.5%)*	*Strong rise to 71.0%*
	Strong bounce 0.6%-1.0%	3.8%-4.2%	4.5%-4.9%	5.2%-5.5%
	Moderate increase 0.3% - 0.5% (central = 0.4%)	4.3%-4.5%	**5.0%-5.1% Central 5.1%**	5.6%-5.8%
	Fall -0.1% to -0.3%	4.9%-5.0%	5.5%-5.7%	6.2%-6.4%

Source: Stats NZ, ANZ Research

So what's going to happen to labour force participation? It's difficult to tell. Prior to COVID-19, labour force participation had hit something of a turning point, declining from a peak of 71.2% in 2017, to 70.4% at the end of 2019 (figure 2). As we show in figure 3, falling participation reflects population aging (orange bars), which has started to offset higher participation among certain parts of the population (blue bars), in particular working-age women, leading to a fall in overall participation.[1] These are long-term, slow-moving trends, and could weigh on participation (and therefore labour supply) in coming years.

[1] The figure shows the result of a shift-share decomposition of the labour force participation rate, which allows us to show the effect of population aging on participation (which is a negative), and the effect of higher participation amongst certain age and sex cohorts (which has been a big positive, with female participation rates rising sharply over the last few decades). For more details about the decomposition, see this note.

Figure 2. Labour force participation rate

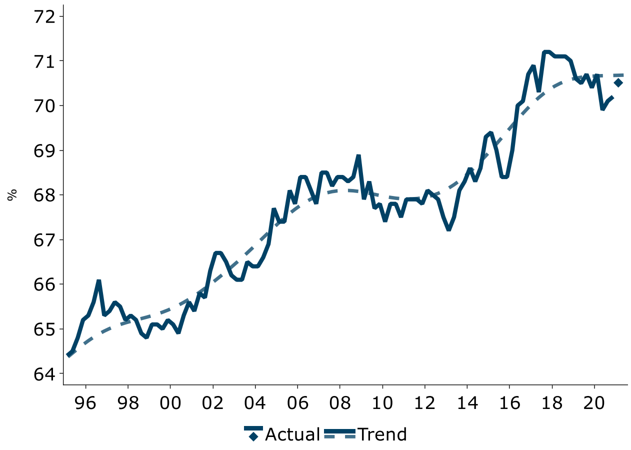
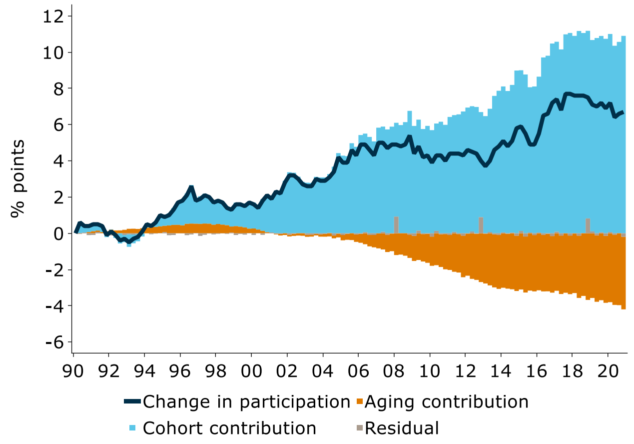


Figure 3. Contribution to change in participation rate since 1990



Source: Stats NZ, Macrobond, ANZ Research

However, participation also dropped sharply in the wake of COVID, and this is a temporary factor that we expect will be reversed in coming quarters. This rebound reflects that:

- Fiscal support for households has eased, so people may need to re-enter the workforce to supplement the family's income.
- Women were disproportionately impacted by the pandemic, so we may see a large number re-join the labour force.
- There was optimism during Q1 about the improving domestic and global economic outlook, which might encourage people to enter the labour force.

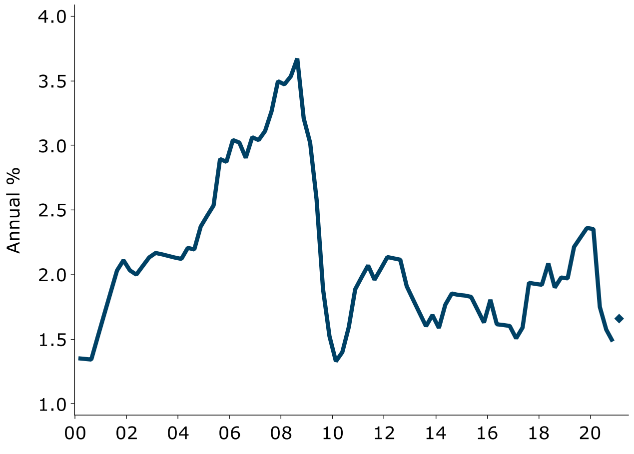
So while the longer-term outlook for participation is fairly soft, we expect that near-term movements will see participation bounce back to 70.5% in Q1 – almost back to trend (figure 2). A big risk to our forecast is if participation doesn't recover as quickly as we expect, which would see unemployment come in below expectations.

When we combine a 70.5% participation rate with a 0.4% q/q rise in employment, that adds up to a 5.1% unemployment rate – a slight uptick from the surprisingly good 4.9% Q4 print (figure 4), but still a respectable number given that we were in recession this time last year. However, as we noted above, a lot depends on participation, and we could feasibly see unemployment of 4.5%-5.5%, even if employment comes in as expected.

The labour market is undoubtedly in a much better place than anyone dared hope it would be when COVID hit, and labour has become a scarce resource in a number of pockets of the economy. As we outlined in a forecast update last week, we expect that strong labour demand and difficulty finding labour will translate into higher wage inflation. We think wages were up 1.7% y/y in Q1 (figure 5). That's a bit stronger than a rising unemployment rate would normally suggest. But, with many firms struggling to find people to fill vacancies, demand is likely to result in higher wages, rather than strong employment growth, over the next few quarters.

Figure 4. Unemployment rate

Figure 5. Wage inflation



Source: Stats NZ, Macrobond, ANZ Research

Monetary policy implications

In the February Monetary Policy Statement, the RBNZ expected a slight increase in unemployment from 4.9% in Q4 to 5.0% in Q1. A lift in the unemployment rate in next week's data will only reinforce the RBNZ's confidence in their cautious approach. As they have repeatedly emphasised, the Monetary Policy Committee need to be 'confident' that inflation is sustainably at 2% *and* employment is 'at or above' its maximum sustainable level before they consider moving from their stimulatory stance.

A large positive surprise next week could shift the balance of risks for monetary policy, since a stronger labour market also supports higher inflation through rising wage pressures. However, the inflation side of the dual mandate still has a way to go before the RBNZ will be happy, and current inflation pressures are coming from largely temporary sources (eg high oil prices in Q1, shipping disruptions, and base effects as weak 2020 inflation prints drop out of annual calculations). So the RBNZ will be happy to sit back and let the labour market tighten further, especially if it means they can lock in some sustainable rises in inflationary pressure.

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