ANZ Research

Labour Market Statistics – Q2 2022

3 August 2022

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Contact

Finn Robinson or Sharon Zollner for more details.

Unemployment rises, but wages soar

Bottom line

- The unemployment rate increased to 3.3% in the June quarter (3.2% previously). That was higher than our expectation (2.8%) and the RBNZ's May MPS forecast of 3.1%. Employment was flat in Q2, while participation eased 0.1ppts to 70.8%. But employment growth is currently about labour supply, not demand. This remains an extremely tight labour market – as reflected in further increases in wage inflation.
- Private sector wage growth has almost caught up to CPI inflation, with average hourly earnings up 7.0% y/y (5.3% previously) in Q2, and productivity-adjusted labour costs rising 3.4% y/y (3.1% previously). With the Australian labour market hot and domestic labour demand still insatiable, there's plenty more wage pressure in the pipeline.
- While unemployment did increase, the continued surge in wage inflation is a serious concern for the RBNZ. The labour market is likely to remain a driver of persistently too-high domestic inflation over the next year, and with wages growing even faster than we or the RBNZ expected, the risk of a wage price spiral is certainly not abating. That should keep the RBNZ on track to hike the OCR to 4% by the end of the year as per our forecasts.

Data summary – Q2 2022

		Latest
Labour market		
HLFS unemployment rate (sa)		3.3%
HLFS participation rate (sa)		70.8%
HLFS employment (sa)	q/q	0.0%
HLFS employment	y/y	1.6%
HLFS hours worked (sa)	q/q	0.8%
Wages		
LCI private sector wages (ex-overtime)	q/q	1.3%
LCI private sector wages (ex-overtime)	y/y	3.4%
QES private sector hourly earnings (ex-overtime)	q/q	2.3%
QES private sector hourly earnings (ex-overtime)	y/y	7.0%
QES total gross earnings	y/y	7.9%

The view

Today's labour market report for the June quarter was a bit of a mixed bag. Employment was flat, participation ticked down, and the unemployment rate rose to 3.3% (3.2% previously). On the flip side, wage growth accelerated sharply, with private sector average hourly earnings (ordinary time) up 7.0% y/y – almost matching Q2's 7.3% inflation rate. That's the real news in today's data. Wage growth is rising even faster than anticipated, raising the risk of a wage-price spiral as high inflation gets embedded in wage-setting behaviour.

Looking at the details of the Q2 release:

- Measures of labour market stretch were mixed. The unemployment rate lifted 0.1ppts to 3.3% (3.2% previously), while the broader underutilisation rate ticked down to 9.2% (9.3% previously). The participation rate eased slightly to 70.8% (70.9% in Q2). Total hours worked lifted 0.8% q/q, after declining 0.2% in Q1.
- Employment was flat at 0.0% q/q for the second quarter in a row, which saw the annual rate of jobs growth slow to 1.6% y/y (2.7% previously). That's quite a soft print compared to the jump in monthly filled jobs seen over the quarter (although those data are conceptually different from the HLFS). Given how tight domestic and overseas labour markets are, jobs growth is unlikely to pick up strongly from here, despite two months of weak numbers. There just aren't the workers available.

- The real news in the labour market data today is wage growth. And here the numbers are looking pretty uncomfortable for the RBNZ:
  - Private sector average hourly earnings growth (ordinary time) lifted 7.0% y/y in Q2 (5.3% previously) – almost catching up to inflation (which was running at 7.3% in Q2).
  - The private sector labour cost index (LCI, which is adjusted for productivity) was up 3.4% y/y (3.1% previously). That's the largest increase since late 2008.
  - 26% of jobs surveyed in the LCI received a pay rise of more than 5% (also the highest proportion since 2008).
  - About two thirds of jobs received an increase in ordinary-time wage rates in the past year – the highest level of on record.
- Wage gains have been very broad based, with average total hourly earnings growth ranging from a low of 2.3% y/y in forestry and mining to 11.6% y/y in accommodation and food services.
- The only real (relative) weak spot on the wage front is public sector wages, which have increased by a more modest 4.4% y/y for ordinary time pay. But, overtime pay rates in the public sector are up a whopping 13.1% y/y (2.3% previously), versus 8.1% for the private sector.
- The upshot: despite the disappointing headline prints, the labour market is even more inflationary than we feared.

RBNZ implications

Unfortunately for the RBNZ, this further acceleration in wage growth only makes the inflation fight harder. Yes, the headline unemployment number came in a fair clip above our expectations – but that just shows that firms were not able to find as many suitable workers as we estimated they would have, not that they weren't looking. The extreme tightness in the labour market has just shown up in another form.

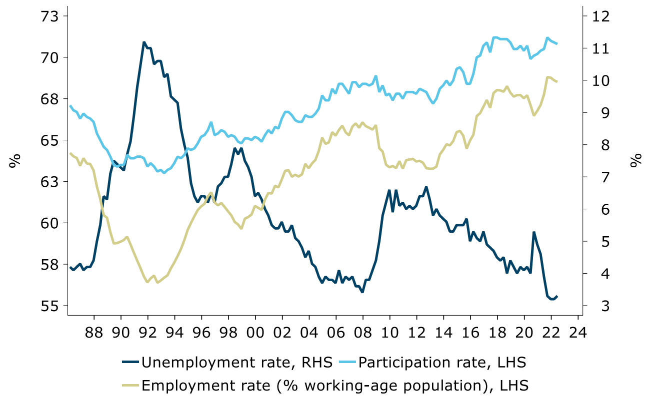
The surge in wage growth will be alarming for a central bank with inflation so far from target. Importantly, wage rises are being driven primarily by intense demand for workers and cost-of-living pressures, rather than productivity gains. Kiwi businesses are having to pay more for a given amount of output per worker, and that can only be absorbed into margins for so long before it has to be passed on to the end consumer, who will then demand inflation compensation in their next pay review. And when unemployment is this low, they are more likely to get it.

The concern for the RBNZ is that such a self-perpetuating inflation cycle could cause domestic inflation in New Zealand to remain high, even if global inflation pressures start to ease. Non-tradables inflation at 6.3% in Q2 is already worryingly high, and measures of core inflation now range between 4.8% and 6.1%, well above the upper limit of the RBNZ's 1-3% target band for CPI inflation. Further acceleration in wage growth only increases the probability that domestic inflation will continue to surge, feeding off high wages and high inflation expectations to generate a damaging wage-price spiral. So for the Monetary Policy Committee, this labour market report means their inflation fighting work is far from done. We think they'll lift the OCR by 50bps at each of the three meetings left in 2022. That will bring the OCR to 4% - which hopefully will be enough to break the back of inflation.

Probably the most sobering aspect of this jobs report is the fact that we've seen something of a plateau in the unemployment rate in recent quarters, while wage growth has continued to accelerate. That suggests the RBNZ may need to hit the labour market quite hard to bring inflation pressures back down – and that likely means higher unemployment than we previously expected to see.

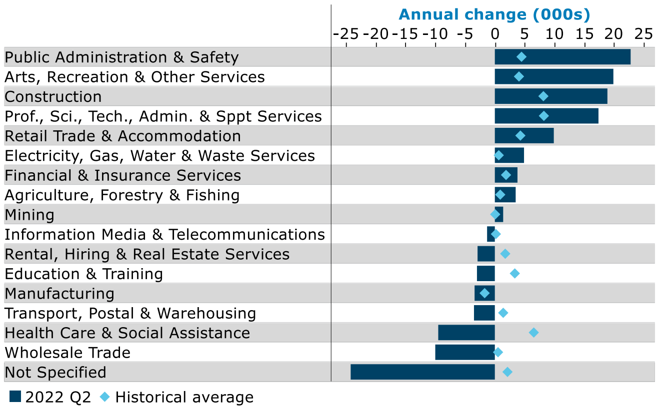
Stepping back, as alarming as the recent CPI and wage data look from an inflation-targeting perspective, it's important to remember that these tend to be lagging indicators, and reflect previous strength in the economy. We're now over a year beyond the 2021 trough in mortgage rates, and it's close to a year since the RBNZ's first hike in October 2021. Those rate hikes have been aggressive, and will take significant heat out of the economy. And there's nothing to suggest the RBNZ isn't getting traction – just look at the housing market. It just takes time for those rate hikes to flow through to the real economy, and the labour market is always one of the last things to adjust.

Figure 1. Unemployment, employment, and participation rates



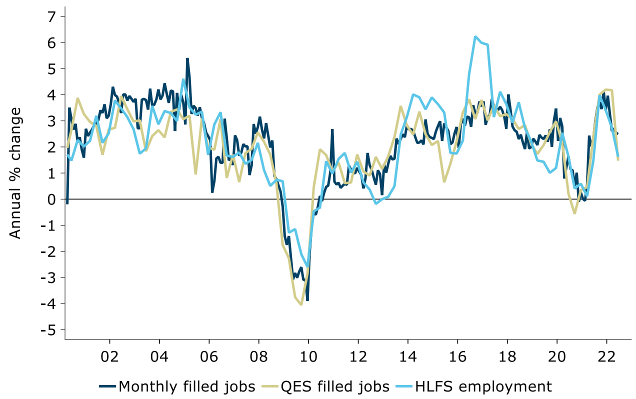
Source: Stats NZ, Macrobond, ANZ Research

Figure 3. Employment by industry



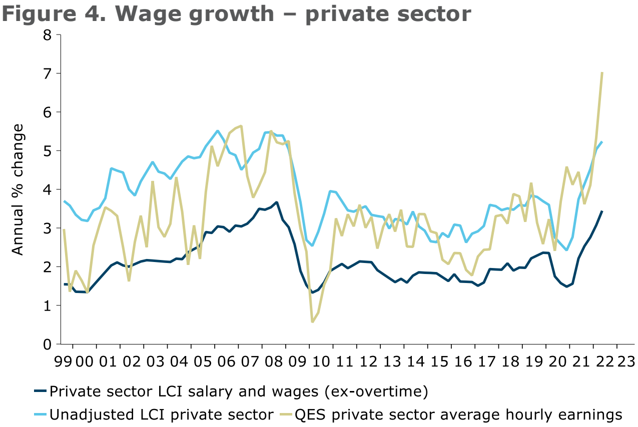
Source: Stats NZ, Macrobond, ANZ Research

Figure 3. Employment and filled jobs



Source: Stats NZ, Bloomberg, Macrobond, ANZ Research

Figure 4. Wage growth – private sector



Source: Stats NZ, Macrobond, ANZ Research

Contact us

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

Sharon Zollner
Chief Economist

Follow Sharon on Twitter
@sharon_zollner

Telephone: +64 9 357 4094
Email: sharon.zollner@anz.com

General enquiries:
research@anz.com

Follow ANZ Research
@ANZ_Research (global)

David Croy
Senior Strategist

Market developments, interest rates, FX, unconventional monetary policy, liaison with market participants.

Telephone: +64 4 576 1022
Email: david.croy@anz.com

Susan Kilsby
Agricultural Economist

Primary industry developments and outlook, structural change and regulation, liaison with industry.

Telephone: +64 21 633 469
Email: susan.kilsby@anz.com

Miles Workman
Senior Economist

Macroeconomic forecast co-ordinator, fiscal policy, economic risk assessment and credit developments.

Telephone: +64 21 661 792
Email: miles.workman@anz.com

Finn Robinson
Economist

Macroeconomic forecasting, economic developments, labour market dynamics, inflation and monetary policy.

Telephone: +64 21 629 553
Email: finn.robinson@anz.com

Kyle Uerata
Economic Statistician

Economic statistics, ANZ proprietary data (including ANZ Business Outlook), data capability and infrastructure.

Telephone: +64 21 633 894
Email: kyle.uerata@anz.com

Natalie Denne
PA / Desktop Publisher

Business management, general enquiries, mailing lists, publications, chief economist's diary.

Telephone: +64 4 802 2217
Email: natalie.denne@anz.com

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