Stable – but not immune to risks

- The unemployment rate is expected to have been unchanged at 4.5% in Q3, consistent with continued tightness in the labour market. Further modest tightening is expected from here.
- Wage inflation is expected to have been modest in Q3 following a minimum-wage induced boost in Q2. But over the medium term, the underlying wage pulse is expected to improve gradually.
- Strength in the labour market is supporting household sentiment, but the recent moderation in firms’ employment intentions poses downside risk to both employment and spending. Such risks will keep the RBNZ cautious.

Key points

- The labour market is expected to have been broadly stable in Q3, with the unemployment rate flat at 4.5% (in seasonally adjusted terms). The labour market is “tight”, with spare capacity having been gradually absorbed over the past five years on the back of robust growth in the economy.
- Consistent with stability in the unemployment rate, we expect that employment growth matched growth in the labour force in Q3. However, HLFS employment data has been volatile of late and is an important source of uncertainty and potential volatility in next week’s release. For the record, we are picking a 0.5% q/q rise in seasonally adjusted employment – a fairly middle-of-the-road outcome. Labour force participation is expected to remain elevated at 71% of the working-age population (seasonally adjusted).
- Recent volatility aside, employment growth has been strong in recent years, boosted by growth in the economy. But strong jobs growth has also been symptomatic of firms’ increased reliance on labour to grow output, with productivity growth very weak. Annual employment growth is expected to have moderated to 2% y/y in Q3, consistent with the economy having lost some momentum, moderate growth in job ads, and the recent weakening in employment intentions in the ANZ Business Outlook Survey.
- Over the medium term, the labour market is expected to tighten modestly, with gradual declines in the unemployment rate expected as the migration cycle eases and population growth slows. We expect employment growth will remain firm but not spectacular, consistent with our expectation that the economy will struggle to grow above trend.
- Strength in the labour market is supporting consumer confidence, which has held up recently, despite softer business sentiment. With the unemployment rate expected to decline modestly in coming years, the labour market is expected to continue supporting household confidence and spending. But the extent of the recent moderation in employment intentions is an important source of downside risk to employment growth, which could see strength in the labour market eroded and spending retrench.
Nominal wage inflation is expected to have been modest in Q3, with a soft 0.4% q/q print expected. Wage growth was boosted by the higher minimum wage in Q2 (to the tune of 0.2%pts). But looking through this, wage inflation has been weak. Annual wage inflation is expected to moderate to 1.8% y/y, consistent with continuing weakness and as last year’s care worker settlement drops out of the annual calculation. Given the temporary strength in CPI inflation in Q3 (at 0.9% q/q), real wages are expected to have eased in the quarter. But wage gains have generally outpaced overall price increases recently, supporting household sentiment.

In coming years, nominal wage inflation is expected to increase gradually, with the labour market expected to tighten a little and lingering weakness expected to dissipate slowly. Future increases in the minimum wage are expected to provide a further boost, with planned increases to $20 per hour by 2021. We expect this will boost LCI wages by about 0.2%pts each year, including some spill-over effects to pay discussions more generally.

The labour market is close to full employment, but wage inflation remains weak. The RBNZ will want to see broad-based, persistent increases in wage and price inflation in order to meet their inflation objective, which we expect will occur only gradually. Risks have also increased that could make it harder to keep the labour market near maximum sustainable employment and inflation at target over the medium term. Given this, we expect that the RBNZ will remain cautious and willing to support the economy if required, with the OCR on hold for the foreseeable future.

Figure 1. Participation and unemployment rates
Figure 2. Job ads versus employment growth
Figure 3. Unemployment and ease of finding skilled labour
Figure 4. Measures of wage inflation

Source: ANZ, Statistics NZ, NZIER, Seek, Trade Me
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