

Room for more?

NZ labour market review, September quarter 2017

1 November 2017

- The unemployment rate fell to a nine-year low of 4.6% in the September quarter, slightly better than we and the market expected.
- Employment growth and labour force participation were very strong, but these are noisy on a quarterly basis and may have been affected by recent survey changes.
- Labour cost inflation remains very subdued, outside of the care workers' equal pay settlement.
- The jobs market has strengthened over recent years, but it's not clear that it has moved into tight territory yet.

Today's labour market report for the September quarter painted a stronger picture of employment than expected, even after allowing for some unusual quarterly moves in the details. However, wage growth has yet to show any signs of a pickup, even with consumer price inflation no longer at rock-bottom levels.

The unemployment rate fell from 4.8% to 4.6% in the September quarter, beating market forecasts of a fall to 4.7%. This is the lowest rate since December 2008, when the Global Financial Crisis was reaching full force.

Normally we recommend focusing on the unemployment rate as the most reliable measure of how the jobs market is performing, as the underlying details can swing around a lot on a quarterly basis. That's especially true for the latest figures.

Employment jumped by 2.2% in the September quarter, well ahead of market forecasts. But that followed a 0.1% fall in the June quarter, which didn't jibe with other labour market indicators at the time. Similarly, the labour force participation rate rebounded from a surprising drop to 70.1% in the June quarter, to reach a new all-time high of 71.1% in the September quarter.

We suspect that changes to the Household Labour Force Survey in June 2016, which resulted in a step-change in employment levels, may have also disrupted the seasonal

	Quarterly actual		Quarterly expected		Annual
	2017 Q2	2017 Q3	Market	Westpac	2017 Q3
Household Labour Force Survey					
Unemployment rate (s.a.)	4.8	4.6	4.7	4.7	-
Employment (s.a.)	-0.1	2.2	0.8	1.0	4.2
Participation rate (s.a.)	70.1	71.1	70.2	70.3	-
Quarterly Employment Survey					
FTE employment (s.a.)	0.7	0.8	-	0.9	2.7
Hours paid (s.a.)	0.9	0.8	-	0.9	3.0
Private ave hourly earnings, ord time (all sectors)	0.8	1.2	1.1	0.8	2.0
Labour Cost Index					
All sectors, ordinary time	0.4	0.6	-	0.9	1.8
Private sector, ordinary time	0.4	0.7	0.7	1.0	1.9
Private, all sal & wage rates	0.4	0.7	0.6	1.0	1.9

pattern of this series. We've looked into making our own adjustment for this effect, but even that doesn't overturn the fact that jobs growth was stronger than we expected over the quarter.

Employment has risen across most sectors in the last year. The strongest growth has been in professional, administrative and technical roles, up 12% compared to a year ago. Interestingly, this sector has seen the biggest decline in jobs in Australia over the last year. While employment in Australia has picked up strongly so far this year, the types of jobs being created may not be conducive to enticing New Zealanders across the Tasman.

The other sector that has seen significant jobs growth is, not surprisingly, construction – up by more than 22,000 people (10%) in the last year. There's no doubt that the building industry is running up against capacity constraints. But it's important to recognise that its capacity is growing over time.

Despite the improving trend in employment, wage growth remains subdued. The Labour Cost Index (LCI) rose by 1.9% in the year to September. However, about 0.3% of that increase was due to the equal pay settlement for aged and disability care workers. Excluding that impact, annual labour cost inflation actually slowed a little, from 1.7% in the June quarter to 1.6% today. That's despite a reasonably strong economy, and inflation no longer at rock-bottom levels.

That leads us to a crucial question: how tight is the labour market? That is, how close is the economy to 'full' employment, which is generally taken to mean the lowest rate that can be sustained over the long term.

The unemployment rate has improved substantially over the last couple of years, but history suggests that it can go further. Unemployment was below 5% for much of the 2000s, and even below 4% for a stretch. Wage growth picked up in that time, but it didn't really take off until unemployment was below 4%.

The record-high participation rate might also raise questions about how many more people can be attracted in to the workforce. It's not clear what has driven the surge in participation over the last year, but it doesn't seem to be a migration effect. Most of the rise in participation has been in the 50+ age group; the growth in foreign arrivals has been concentrated in student and work visas, both of which skew younger.

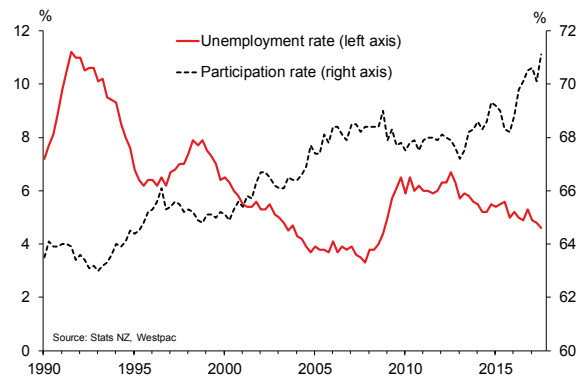
Ultimately, the test of whether the labour market is 'tight' is whether (real) wage growth is accelerating. Real wage growth has actually been reasonably strong compared to last decade, largely because inflation has been persistently and surprisingly low (whereas it was persistently and surprisingly high for much of the 2000s). But now that inflation is picking up from its lows, we have yet to see a matching lift in wage growth. And that provides at least circumstantial evidence that the labour market still has some slack left in it.

Today's release is unlikely to have much bearing on the Reserve Bank's thinking in next week's Monetary Policy Statement. The surprise for the RBNZ was in the same

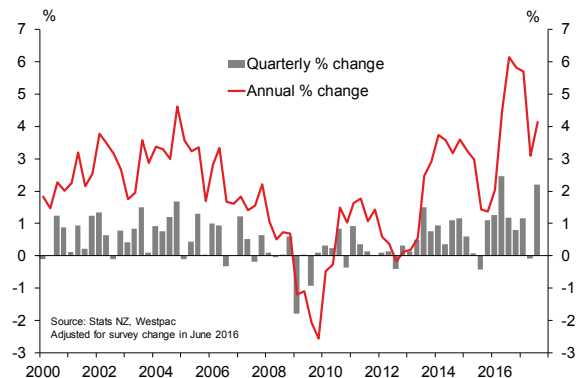
direction as for us: unemployment a bit lower than expected, but wage growth weaker.

However, with the new Labour-led Government looking to introduce some form of employment mandate for the RBNZ, the question of what constitutes 'full' employment is going to take on growing importance. Finance Minister Robertson has said that he doesn't plan to introduce a numerical target for the unemployment rate. But that would still leave the burden on the RBNZ to determine what a sustainable long-run unemployment rate is, and to defend its choices.

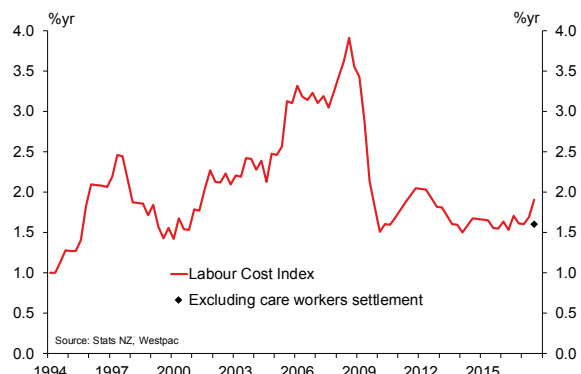
Labour force participation and unemployment



Employment growth



Labour Cost Index



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