Turn for the worse

Q2 labour market preview: 6 August, 10:45am

31 July 2019

- We expect the unemployment rate to rise to 4.3% in the June quarter, reflecting the recent softening in business conditions and hiring.
- However, we also expect some pick-up in employment and participation after they both surprisingly fell in the previous quarter.
- Given the risk of mixed signals, we recommend focusing on the unemployment rate and the QES measure of jobs growth.
- Wage growth is expected to accelerate, largely due to a big increase in the minimum wage.
- The labour market surveys are unlikely to influence next week's OCR review, where we expect a cut to 1.25%. However, a weaker than expected result would have a bearing on the timing and extent of further OCR cuts.

	Q1 actual	Q2 forecast	
	Quarter	Quarter	Annual
Household Labour Force Survey			
Employment growth	-0.2	0.8	1.7
Unemployment rate	4.2	4.3	-
Hours worked	4.9	-0.8	1.2
Participation rate %	70.4	70.7	-
Quarterly Employment Survey			
FTE employment (s.a.)	0.1	0.4	1.4
Hours paid (s.a.)	0.3	0.5	1.4
Private avg hourly earnings	1.1	0.4	4.0
Labour Cost Index			
All sectors, ordinary time	0.4	0.7	2.1
Private sector, ordinary time	0.3	0.7	2.1
Private , all salary & wage rates	0.3	0.7	2.1

There is mounting evidence that the New Zealand jobs market is softening, reflecting the business-led nature of the recent growth slowdown. Business confidence surveys show a drop in hiring intentions, job advertisements are down on a year ago, and the share of people receiving the jobseeker benefit has risen further.

What's not clear is how much of this softness will show through in next week's labour market reports for the June quarter. In fact, we think there's a risk of conflicting signals from the Household Labour Force Survey (HLFS), with both employment and unemployment expected to rise. Meanwhile, wage growth is expected to pop higher, with a boost from an especially large increase in the minimum wage this year.

For the HLFS, we expect a small rise in the unemployment rate from 4.2% to 4.3%, along with a solid 0.8% rise in employment. The previous quarter saw both measures drop unexpectedly, due to a sharp fall in the labour force participation rate. Looking at the details suggests that the fall in participation was due to a jump in retirees – more than what seems plausible in the space of three months. We've assumed that this will be partially reversed this time, though the risk is that this result 'sticks', given that the number of retirees is trending higher over time.

Given the potential for mixed signals, we recommend focusing on the unemployment rate, which tends to be more stable from quarter to quarter. The Quarterly Employment Survey (QES), which covers employers rather than households, also provides a valuable cross-check. Jobs growth in this survey has slowed in the last couple of years, and we expect another subdued outturn of +0.4% in the June quarter, in line with our forecast of GDP growth.

We expect the unemployment rate to rise further by the end of this year. The labour market tends to lag the broader economic cycle, and we think the slowdown in economic growth to date is yet to be fully reflected in the unemployment figures. We're also concerned that the recent slump in log export prices is likely to have a job-intensive impact, as forest owners respond by harvesting fewer trees.

Wages tend to lag even further behind the cycle, and the pre-existing tightness in the labour market means that wage growth still has some momentum. We're expecting a 0.7% rise in the Labour Cost Index (LCI) for the June quarter, which would lift annual growth to a ten-year high of 2.1%.

Much of that acceleration reflects a 7.3% rise in the minimum wage in April, the biggest annual increase since 2007. We estimate that this will add 0.2 percentage points to the LCI in the June quarter (with an even bigger impact on the more volatile QES average hourly earnings measure). The minimum wage hikes over the next two years are likely to have an even greater impact on wage costs, as each successive increase will affect a greater share of the workforce.

The labour market surveys will be released a day before the Reserve Bank's *Monetary Policy Statement*, and in the midst of the Monetary Policy Committee's deliberations. It's important to note that the RBNZ's previous forecasts had already factored in a rise in unemployment to 4.3%, in line with our view. As such, we don't expect the labour market reports to have a bearing on the OCR decision itself, where there is already sufficient support for a rate cut. However, a weaker than expected result could affect the extent and timing of further OCR moves.

Michael Gordon
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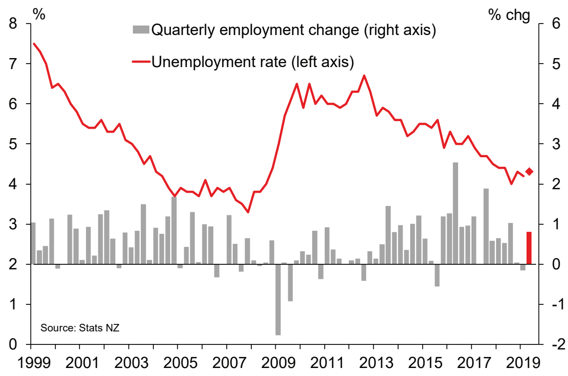
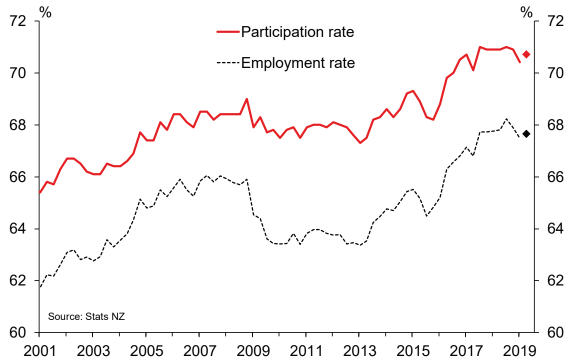
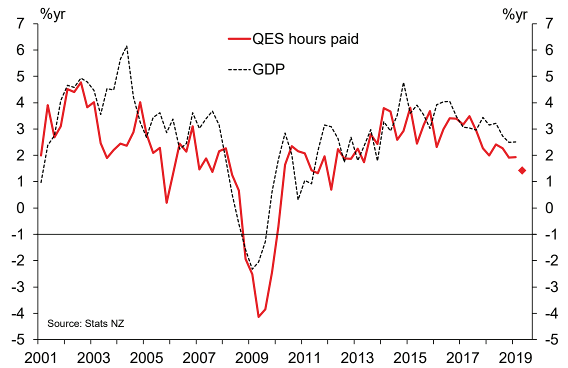
Unemployment rate and employment growth



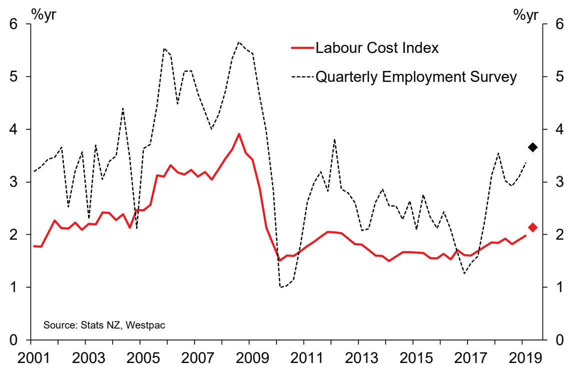
Employment and participation rates



Hours paid and GDP, annual change



Wage growth (all sectors, ordinary time)



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