7 May 2013

The real picture

Q1 Labour Cost Index and Quarterly Employment Survey

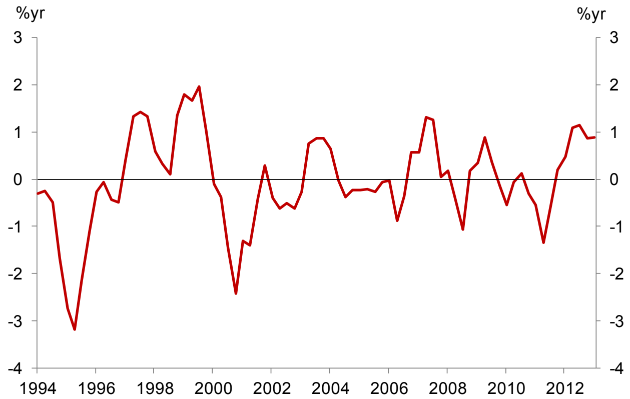
- **Wage inflation and employment growth remain subdued.**
- **In part that reflects the broader environment of very low inflation. In real (inflation-adjusted) terms wage inflation is actually at the upper end of the normal range over the past decade.**
- **That said the labour market remains firmly two-speed, with plenty of wage inflation (and jobs growth) in Canterbury but not much elsewhere.**

Today's labour market reports – the Labour Cost Index, which reports on wages, and the Quarterly Employment Survey, which is mainly useful as an alternative jobs indicator to Thursday's HLFS – were on the soft side of both market expectations and our own. Annual wage inflation eased and jobs growth continues to lag behind the broader economic recovery.

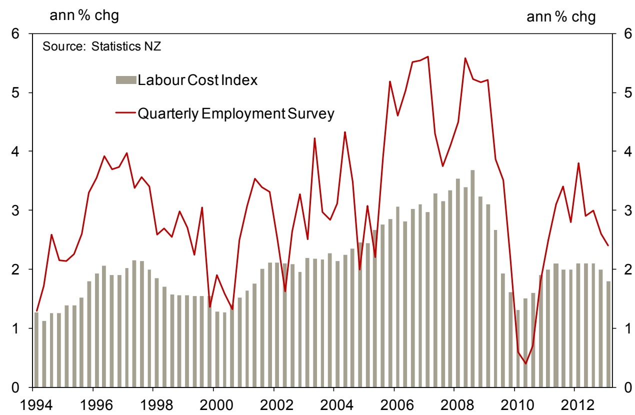
It's important not to overstate the weakness. While today's LCI report was soft in dollar terms, the low-inflation environment means that in real (inflation-adjusted) terms there has actually been decent wage growth over the past year. Indeed, since mid-2012 annual real wage inflation has been about 1%, which is similar to what we saw at the peak of the last cycle in 2007, and indeed higher than in the mid-2000s (when wage growth was much higher in dollar terms, but the increases were largely eroded by rising living costs).

Similarly, while the Quarterly Employment Survey showed only modest jobs growth, total earnings are now up a solid 4.4% on a year ago, suggesting that labour income growth is doing its bit to support the increases in retail spending we have seen over the past year.

Labour cost index (all groups, all salary and wage rates) minus inflation (ex GST)



NZ LCI and QES wages (private sector ordinary time)



However, jobs and wage growth remains highly localised. Wage pressures are largely confined to the Canterbury region and jobs growth remains much weaker elsewhere, particularly outside the main centres. Along with the soft headline wage result and lackluster overall jobs growth, this will leave the RBNZ comfortable keeping the OCR on hold for now. As time goes on we do expect the accelerating Canterbury rebuild and a rising housing market to result in broader inflation pressures and prompt interest rate rises - but not until next year.

Survey Details - LCI

The Labour Cost Index (private sector, all salary and wage rates - the RBNZ's preferred measure of wage inflation) rose just 0.3% in the March quarter, below the historical average of 0.5% for the quarter (the data aren't seasonally adjusted). Compared to a year ago the index was 1.8% higher, down from 2% three months ago.

The distribution of wage changes was much the same as in the December survey. 56% of surveyed wage rates saw an increase over last year, up a touch from 55% in December, but the mean wage increase eased back, to 3.5%. There is a little more pressure on overtime wage rates – 64% saw an increase, up from 62% in December and the highest proportion since March 2011.

The sectoral and regional divisions remain stark. At 2.5%yr, the construction sector is enjoying the second highest wage inflation among any industry (only mineral product manufacturing is higher). And those pressures remain largely confined within the Canterbury region. In the Canterbury construction sector, annual wage inflation ratcheted up to 4.3%, the highest since September 2011. By contrast, construction sector wage inflation in the rest of the country eased back, from 2.3% three months ago to 2.1%.

Table: LCI and QES Summary

	Labour Cost Index				Quarterly Employment Survey			
	Dec-12		Mar-13		Dec-12		Mar-13	
	qtrly	annual	qtrly	annual	qtrly	annual	qtrly	annual
Private sector (ordinary time)	0.5	1.9	0.4	1.8	-0.4	2.6	1.0	2.3
Public sector (ordinary time)	0.5	1.5	0.4	1.5	0.9	2.6	1.6	1.4
Total (ordinary time)	0.5	1.8	0.4	1.8	-0.1	2.6	0.8	2.1
FTE employment (s.a.)	-	-	-	-	0.4	1.5	0.4	1.7
Filled jobs (s.a.)	-	-	-	-	0.4	1.4	0.4	1.7
Hours paid (s.a.)	-	-	-	-	0.5	1.8	0.0	2.3
Total labour earnings (s.a.)	-	-	-	-	1.1	4.6	1.0	4.4

Source: Statistics NZ

Survey Details - QES

The Quarterly Employment Survey showed total earnings up 1% in the quarter (seasonally adjusted), down a touch from Q4's 1.1%. This suggests that the labour market exhibited similar momentum in the March quarter to three months ago. Filled jobs and full-time equivalent (FTE) employment rose 0.4% in the quarter, the same as in the December quarter. (That said, full-time employment growth slowed from 0.7% to 0.3%, while part-time employment bounced back from last quarter's 0.5% fall.)

The QES attributed the increase in earnings entirely to higher average wages – hours paid were flat. We'd caution, though, that this split can be quite volatile from quarter to quarter. We'd also note that the weak hours paid number doesn't by itself suggest significant downside risk to our forecast for Q1 GDP. In particular, those parts of the survey that directly feed into Stats NZ's estimates of some service sectors are consistent with our current GDP forecasts.

Today's QES has very little bearing on Thursday's Household Labour Force Survey, which has been significantly weaker than most other labour market indicators of late. We continue to expect the unemployment rate to fall to 6.8% - with plenty of scope for surprise on the day.

The continued two-speed nature of the labour market emerged particularly starkly in the QES job figures. Compared to a year ago FTE employment is up 7% in Canterbury, compared to 2.4% in Auckland, 1.7% in Wellington, and -0.6% in the rest of New Zealand! One division that does appear to be easing is between the public and private sectors. The QES is now recording some catchup in public sector employment (up 2.7% from a year ago, compared to 1.5% in the private sector), which may be a factor behind the fairly good performance of Wellington (which on our estimates enjoyed the highest quarterly FTE growth since September 2011).

Market reaction

There was negligible market reaction, despite a surprisingly soft LCI.

Felix Delbrück

Senior Economist

Westpac Economics Team Contact Details

Dominick Stephens, Chief Economist	Ph: (64-9) 336 5671	dominick_stephens@westpac.co.nz
Michael Gordon, Senior Economist	Ph: (64-9) 336 5670	michael_gordon@westpac.co.nz
Felix Delbrück, Senior Economist	Ph: (64-9) 336 5668	felix_delbruck@westpac.co.nz
Nathan Penny, Economist	Ph: (64-9) 336 5669	nathan_penny@westpac.co.nz