Westpac Institutional Bank

Triple trouble

Preview of 2013 Q2 labour market data, 7 August

- **Statistics NZ is now publishing all three main labour market reports in one go.**
- **We expect a small lift in the unemployment rate, and modest employment growth, but as usual the numbers could surprise on either side.**
- **As the day progresses, markets will digest the full set of data. We expect the upshot will continue to be a gradually improving labour market.**
- **New Zealand's economic upswing is now well-entrenched, but the consequences for domestic inflation pressures are less certain. We expect soft overall LCI wage inflation, but will be parsing the data for signs of rising construction-related wage pressures.**

June quarter Household Labour Force Survey expectations

	Quarterly % change		
	Previous	Westpac	Market
Employment growth	1.7	0.3	0.3
Unemployment rate %	6.2	6.3	6.3
Hours worked	3.2	-1.1	-
Participation rate %	67.8	67.9	67.9

June quarter Labour Cost Index Expectations

	Quarterly % change		
	Previous	Westpac	Market
LCI - all sectors ex overtime	0.4	0.4	-
LCI - pvt sector ex overtime	0.4	0.4	0.5
LCI - pvt sector all salary and wage rates	0.3	0.4	0.5

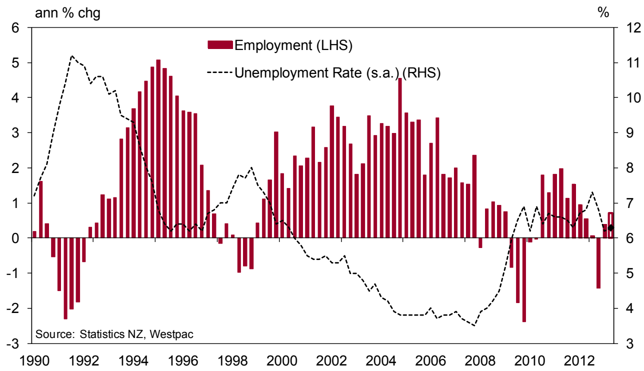
June quarter Quarterly Employment Survey Expectations

	Quarterly % change		
	Previous	Westpac	Market
QES filled jobs	0.4	0.6	-
QES FTE employment	0.4	0.6	-
QES hours paid	0.0	0.7	-
QES wages - pvt sect	1.0	0.7	0.6

Starting Wednesday, Statistics NZ will release all three of New Zealand's major labour market reports – the Household Labour Force Survey, the Quarterly Employment Survey, and the Labour Cost Index – in one go at 10:45 NZ time.

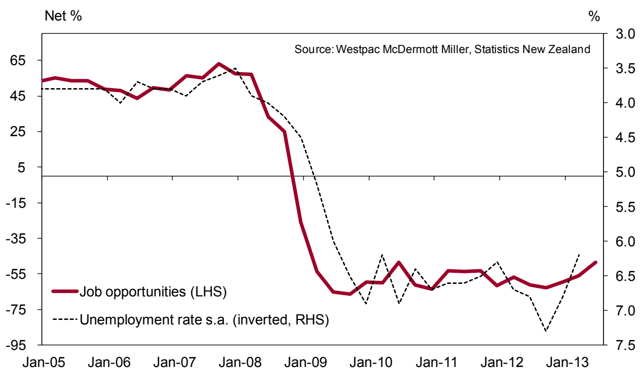
This is a good move. Previously, Tuesday's QES and wage data always felt like a teaser, and Thursday's HLFS inevitably became the 'last word' on the labour market. Releasing the data together will encourage a more holistic assessment. But it also raises the risk of 'information overload' and greater market volatility on the day.

Household Labour Force Survey



Firms' reported and expected hiring

Reported job opportunities and unemployment



In our view, markets' initial reaction will be to focus even more on the HLFS headlines than usual. If our forecasts hold true (more details on those below) there should be very little market response – but the HLFS is notorious for throwing curveballs.

As the day goes on, the 'big picture' emerging from the full set of data should percolate through.

As a rough guide, here is what we will focus on:

- The unemployment rate. This is the major 'value added' from the HLFS – though it, too, can be volatile. We expect a modest uptick after March quarter's plunge.
- The QES jobs and hours estimates. The QES excludes parts of the economy – notably agriculture, so it won't reflect the recent drought. But it's been more stable than the HLFS recently, and more in tune with other economic indicators. In our view it's an important guide to near-term economic activity. We expect to see moderate jobs growth.
- The Labour Cost Index. This gives by far the cleanest read of wage inflation. The QES average wage is much less informative, but contains more sectoral/regional detail.

Both on our part and at the RBNZ, the presumption will be that the labour market is now gradually improving on the back of a well-entrenched economic recovery. That is what the vast bulk of recent data have been saying. Wednesday's data would need to be pervasively strong or weak to significantly challenge that view.

What is more controversial is what this means for domestic inflation pressures. Accordingly, we will be paying close attention to the Labour Cost Index. To date the LCI has shown wage pressures firmly confined to the Canterbury construction sector. While we don't expect to see economy-wide wage inflation picking up yet, we will be alert to signs that those isolated pockets of wage pressure are spreading.

Forecast details – employment and unemployment

Most labour market indicators held up or improved over the June quarter. Unfortunately, when forecasting the Household Labour Force Survey things are never quite that simple.

On the one hand, there are good reasons to expect some statistical 'payback' from a very strong March quarter outturn. The 3.2% jump in hours worked was almost certainly too good to be true. And our own Westpac McDermott Miller employment confidence would be consistent with an unemployment rate somewhat north of March's 6.2%.

The March quarter numbers were also flattered by the 2013 Census, which led to more than 7,500 census collectors and other staff being hired in February and March. That's 0.3% of the labour force – though most of these jobs only lasted for about 6 weeks, so the impact will have been smaller over the quarter as a whole.

But there are also upside risks. The HLFS's estimates of construction sector employment have been suspiciously low. Since March 2011, the HLFS has recorded an increase in construction sector jobs of just 7,000 (4.3%), compared to 12,000 (11%) in the Quarterly Employment Survey, and a 13% rise in construction sector GDP. That gap could start shrinking as construction picks up outside Canterbury, or workers move out of temporary accommodation, which the HLFS doesn't capture.

Employment could also get a boost from a rise in labour force participation. Labour force participation among teenage students plunged in the December quarter, and only recovered modestly in March. That could reflect new benefits for teenagers in education and training introduced late last year, but it's too soon to tell.

Weighing up the risks, we've assumed a small rise in the unemployment rate (to 6.3%); a pull-back in hours worked; and a further modest increase in employment and labour force participation.

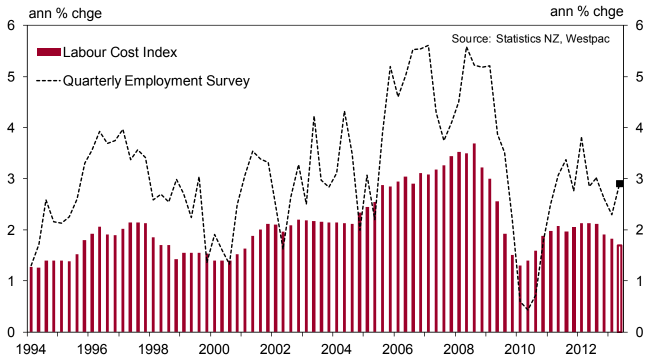
The outlook for the QES is less complicated. In the last two quarters QES filled jobs grew steadily at 0.4%. The recent pickup in other labour market indicators suggests a 0.6% rise this time. Hours paid could rise even more as payback for a weak March quarter.

Forecast details – wages and earnings

On its own, an improving labour market would point to accelerating wage growth, but a very benign inflation environment is keeping cost of living adjustments down. Accordingly, we expect private sector labour costs to rise just 0.4%, below average for a June quarter (the data aren't seasonally adjusted), and annual labour cost inflation to ease further to 1.7%.

As always our focus is firmly on the LCI rather than the QES's average hourly earnings, which get thrown around by swings in quarterly earnings and hours worked. For what it's worth, we expect the QES wage measure to rise just 0.7% - well below the June quarter average – on the back of a bounce-back in hours paid.

Private Sector Earnings and Labour Costs



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