ECONOMIC BULLETIN

Preview of Q2 labour market statistics: 7 August, 10:45am.

31 Jul 2024 | **Michael Gordon**, Senior Economist | +64 9 336 5670 | +64 21 749 506 | michael.gordon@westpac.co.nz

Controlled descent

- **We estimate that the unemployment rate rose from 4.3% to 4.7% in the June quarter.**
- **The labour market is clearly softening, with higher-frequency indicators pointing to outright job losses in recent months.**
- **However, the slowdown doesn't appear to be outside the bounds of what the Reserve Bank was looking for.**
- **Wage growth is slowing from its highs, though this may be masked again in the June quarter by public sector pay agreements.**

	Q1 actual	Q2 forecast	
	Quarter	Quarter	Annual
Household Labour Force Survey			
Unemployment rate	4.3	4.7	-
Employment growth	-0.2	-0.4	-0.2
Participation rate	71.5	71.2	-
Labour Cost Index			
All sectors, ordinary time	0.9	0.8	3.9
Private sector, ordinary time	0.8	0.7	3.4

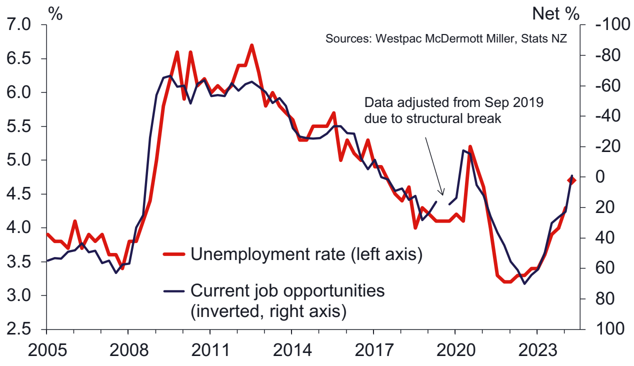
The June quarter labour market surveys, to be released next Wednesday, are shaping up to be crucial for interest rate watchers. The Reserve Bank's change of tone in its policy review earlier this month has opened the door for an earlier start to OCR cuts, with financial markets speculating that the first move could come as soon as the *August Monetary Policy Statement*. It's possible that the labour data could force the RBNZ's hand in this way, if it turns out significantly weaker than they anticipated in their May forecasts. However, we don't expect next week's figures to clear that hurdle – the labour market is softening, but it appears to be at a controlled pace.

Details

We expect the unemployment rate to rise to 4.7% for the June quarter, from 4.3% in March (which was already very close to 4.4% before rounding). The rise in unemployment from its lows was gradual at first, but has picked up the pace in recent quarters.

A range of indicators show that the labour shortages that plagued employers in previous years are now a distant memory. That's due to a combination of a surge of migrant workers to fill the gaps once the border was reopened, and a drop in demand for new workers as the economy has cooled off. Job advertisements are now below pre-Covid levels, businesses report that labour is no longer hard to find, and our Employment Confidence Index shows that households are finding job opportunities much harder to come by.

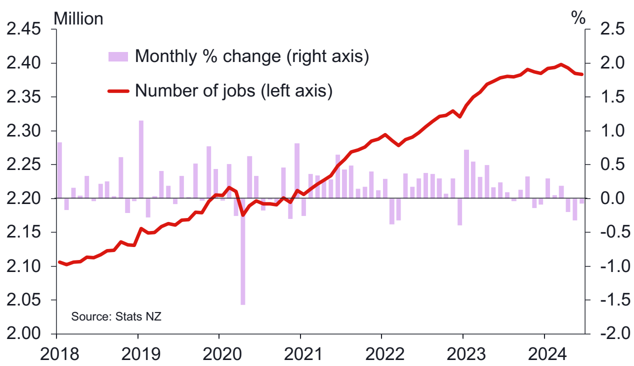
Unemployment rate and employment confidence



The monthly employment indicator (MEI) shows that we're now seeing an outright decline in the number of jobs. On that basis, we're picking a 0.4% fall in employment in the Household Labour Force Survey (HLFS) for the June quarter. While there are some conceptual differences between the two measures that we need to be wary of, the MEI has proven to be a reasonable predictor of the HLFS.

To the extent that there is a divergence between the two, it's most likely to be due to sampling error in the household survey, whereas the MEI is a comprehensive record drawn from income tax data. Indeed, the 0.2% fall in HLFS employment last quarter was out of step with both the MEI and the employer-focused Quarterly Employment Survey (QES), as well as its own measure of the number of hours worked.

Monthly Employment Indicator filled jobs

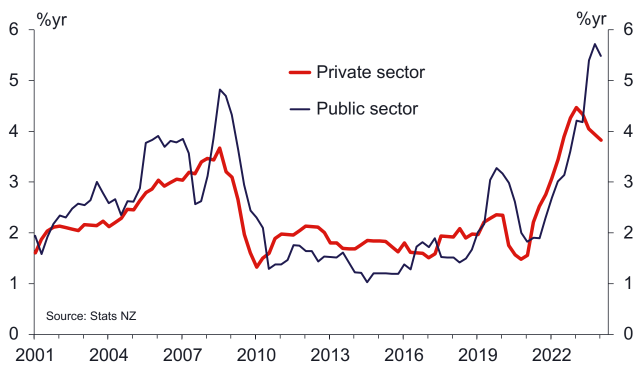


Falling employment tends to be accompanied by falling participation in the labour force – that's especially true for younger age groups, which is where much of the recent job losses have been concentrated. We expect the participation rate to fall to 71.2%, from 71.5% in March and an all-time high of 72.4% a year ago. Lower participation has the effect of softening the overall impact on the unemployment rate.

The easing in labour market conditions is now also leading to a softening in wage growth – usually one of the last things to turn around in the economic cycle. We expect the Labour Cost Index (LCI) to rise by 0.8% for the quarter, which would see the annual growth rate slow from 4.1% to 3.9%.

The slowdown in wage inflation has been masked to some degree by public sector pay agreements, which were set by the previous government and staggered over several periods. That will be a factor again in the June quarter, with a 4% increase for teachers and a 3% rise for nurses and midwives. On the other hand, the minimum wage increase that took effect in April was just 2%, compared to increases of 6-7% in each of the previous five years. As a result, we expect to see clearer evidence of slowing in the private sector measure of wage growth, down from 3.8% to 3.4% annually.

Private and public sector wage growth



Market implications

Our forecasts for next week's releases are a little softer than what the Reserve Bank expected in its May Monetary Policy Statement. The RBNZ assumed a rise in the unemployment rate to 4.6%, with a modest rise in employment and a steady participation rate. High-frequency indicators since then have pointed towards something softer than that, although with much of the weakness coming late in the June quarter, that's perhaps more of a risk for their view on the following quarter.

We think that for the RBNZ to begin cutting rates in August, we'd need to see a significant upside surprise on the unemployment rate next week, perhaps close to 5% (from 4.3% currently). That would be a very large one-quarter increase – outside of the temporary Covid shock, we haven't had one of that size since the 2008 Global Financial Crisis, and before that the severe recession in 1991.

Similarly, the RBNZ would need to see evidence that wage inflation is dissipating more quickly than they expected. While wages don't play a big role in the RBNZ's modelling, they are nevertheless a major source of the remaining 'stickiness' in non-tradables inflation. Our wage growth forecast of 0.8% for the June quarter is only marginally softer than the 0.9% that the RBNZ was expecting.

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