

# No pressure

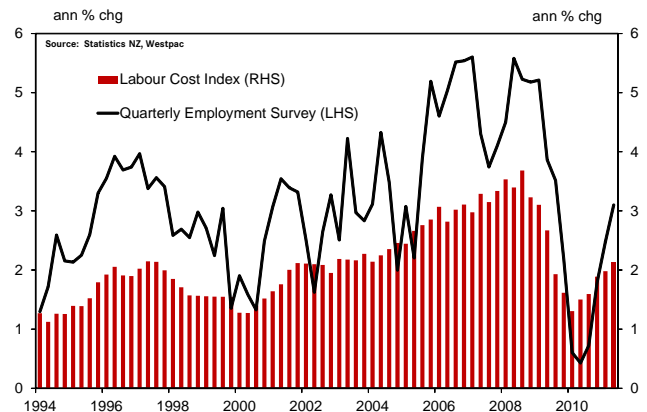
## 2011 Q2 Labour Cost Index and Quarterly Employment Survey

- Wage growth was slightly weaker than expected, and shows underlying inflation pressures remain contained.
- But rising construction sector wages hint at the inflation pressures to come once Christchurch reconstruction really gets going.
- QES employment rose modestly, suggesting that the labour market has weathered the Christchurch earthquake better than we feared.

Today's wage and employment data are the first snapshot of the New Zealand labour market following the February Christchurch earthquake, ahead of Thursday's Household Labour Force Survey. And that snapshot is comforting on two fronts: it points to ongoing (though modest) employment growth, and it also shows very little sign of rising inflation expectations passing through to higher wage inflation. What it does show, like the June Quarter CPI report, is inflation pressures in the construction sector already starting to build, even at this early stage of Christchurch reconstruction.

Limited wage inflation will be welcome news to the Reserve Bank, though it won't dissuade it from removing the 50 basis point 'insurance' cut it made in March. Likewise, the positive employment signals from today's data shouldn't affect the RBNZ's broad view of the economic recovery, given that it was already expecting the unemployment rate to edge down to 6.4% in June.

NZ LCI and QES wages (private sector ordinary time)



However, rising construction sector wages at such an early stage of the Christchurch rebuild are a sign that employers in the sector are preparing themselves for a significant ramp-up in activity further down the track. The Reserve Bank has been assuming that centralized project management will keep the costs of reconstruction down – we're sceptical. And as the income from reconstruction gets spent, we expect to see unemployment falling rapidly and wages rising rather higher than the RBNZ is assuming (the Reserve Bank's latest forecast is for labour cost inflation to peak below 2.5%). Our view remains that over the coming years the RBNZ will have to take the OCR to 6%, well above its current projections.

Table: LCI and QES Summary

	Labour Cost Index				Quarterly Employment Survey			
	Mar-11		Jun-11		Mar-11		Jun-11	
	qtrly	annual	qtrly	annual	qtrly	annual	qtrly	annual
Private Sector (ordinary time)	0.4	2.0	0.5	2.1	0.3	2.5	1.2	3.1
Public Sector (ordinary time)	0.5	1.4	0.3	1.5	2.3	2.8	-0.7	2.2
Total (ordinary time)	0.4	1.8	0.5	1.9	0.4	2.6	1.1	3.0
FTEs (s.a.)*	-	-	-	-	1.1	0.6	0.3	0.4
Paid Hours (s.a.)	-	-	-	-	0.7	2.0	0.7	1.6

Source: Statistics NZ

\*Westpac estimate

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## Wages

Wage inflation remained moderate in the June quarter. The Labour Cost Index (private sector, all salary and wage rates – the RBNZ’s preferred measure) increased by 0.5% over the quarter, slightly below our 0.6% forecast. This is around average for this time of year (the LCI isn’t seasonally adjusted) and leaves annual labour cost inflation unchanged at 2% over the year. Meanwhile, the Quarterly Employment Survey’s average hourly earnings – a more volatile measure of wage inflation which doesn’t control for changes in job mix or productivity gains – also increased at around average rates for the June quarter, rising 1.2%.

Another sign of limited wage pressures was that rising labour costs are still mainly due to more people getting pay increases, rather than due to those pay increases getting bigger. The percentage of employees who have received a pay increase over the past year rose to 58% (up from 56% in March), whereas the median pay increase over the year edged down to 2.9% (from 3% in March).

## Employment and hours

The main reason for being interested in the Quarterly Employment Survey is its measures of employment and hours worked, which give an advance read on the state of the labour market ahead of Thursday’s Household Labour Force Survey. They don’t give a perfect read, by any means – the QES often moves in different direction from the HLFS, and because it’s a survey of businesses, rather than workers, it tends to underestimate the degree to which new businesses add to jobs growth after downturns. But at the moment the QES is pointing to a somewhat more resilient labour market, post-earthquake, than we were anticipating. On our seasonally adjusted measures, full-time-equivalent employment was up 0.3%, and filled jobs were flat. Based on historical relationships with the HLFS, that suggests mildly positive employment growth in Q2.

QES paid hours were up 0.7% in the quarter (seasonally adjusted), after rising 0.7% in Q1. Again, because the March quarter QES was surveyed pre-quake, the timing of that growth is likely to be off: we know from the HLFS that the earthquake caused hours worked to drop in Q1. But 1.4% growth in hours paid over the first half of 2011 is, again, a bit stronger than the 1.1% we’d pencilled in for hours worked.

Industry breakdown

Though overall the labour market appears to have been stronger in June than expected, the QES did confirm that Christchurch has seen substantial labour market disruption from the February earthquake: on our seasonally adjusted measure, Canterbury full-time equivalent employment fell 4.7% in the June quarter. However, this was more than offset by employment growth in Auckland and the regions. Wellington saw a slightly dip in employment.

The industry breakdown also hints at some earthquake disruption, with seasonally adjusted full-time equivalent employment declining in the manufacturing, construction and accommodation sectors (the latter possibly reflecting the hit to tourism). That aside, the divergence between the export-oriented and domestic parts of the economy that we’ve seen over the past year – the former growing strongly, the latter subdued – continued. There were ongoing employment declines in retail and real estate services, but strong growth in wholesale trade (which includes exporters) and specialist professional roles.

There are signs that construction sector wages are starting to rise following the Christchurch earthquake. Construction workers received among the highest increases in salary and wage rates for the quarter – the only other occupational group to match them, teachers, had won a collective pay agreement. However, at this stage these wage pressures still seem quite localized. Statistics New Zealand reported that both the proportion of people getting pay rises, and median wage increases, were significantly higher for Christchurch construction industry workers than elsewhere.

## Market reaction

Both the LCI and QES employment outturns were in line with the market consensus, and there was no discernable market reaction to today’s data.

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