ECONOMIC BULLETIN

NZ labour market review, September quarter 2023.

1 Nov 2023 | **Darren Gibbs**, Senior Economist | +64 9 367 3368 | +64 21 794 292 | darren.gibbs@westpac.co.nz

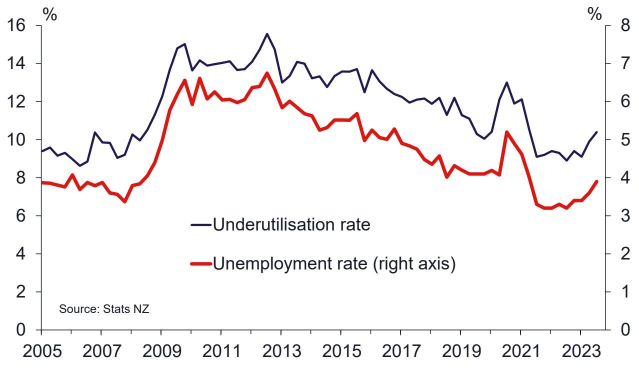
Progress

- **The labour market unambiguously weakened in the September quarter, with the unemployment rate increasing 0.3ppts to 3.9% – in line with our forecast.**
- **Employment fell modestly in the quarter – a weaker than expected outcome that might in part reflect survey sample variability.**
- **Private sector wage growth was softer than expected for a second consecutive quarter, and now appears to have passed its peak.**
- **The key components of the surveys were slightly softer than the RBNZ had expected, reinforcing the likelihood that the OCR will be left at 5.5% at this month's meeting.**

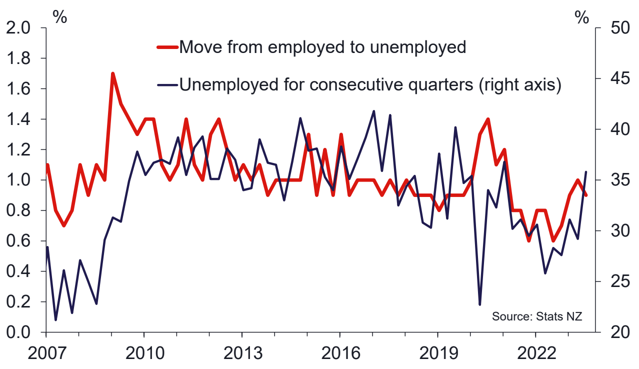
Today's surveys pointed to an unambiguous easing of labour market conditions in the September quarter – an outcome that had been well foreshadowed by business survey data pointing to a marked reduction in reported skill shortages and fewer firms citing labour as the main constraint on output. This was most obviously demonstrated by the 0.3ppt increase in the unemployment rate to 3.9% – the highest level since the June 2021 quarter and in line with our expectations (and that of the market). Also of note, a broader measure of unemployment known as the underutilisation rate – which amongst other things also captures those people that would like more work – increased by 0.5ppts to 10.4% (also the highest reading since the June 2021 quarter). Longitudinal data from the survey also paints a weaker picture, with just over 35% of those who were unemployed in the June quarter remaining unemployed in the September quarter – the highest proportion to remain unemployed across consecutive quarters since the March 2021 quarter.

	Quarterly actual		Quarterly expected		Annual
	Q2	Q3	Market	Westpac	Q3
Household Labour Force Survey					
Unemployment rate	3.6	3.9	3.9	3.9	-
Underutilisation rate	9.9	10.4	-	-	-
Employment growth	1.1	-0.2	0.4	0.4	2.4
Participation rate	72.4	72.0	72.5	75.5	-
Hours worked	0.3	0.1	-	-	1.4
Quarterly Employment Survey					
Private sector average hourly earnings	1.8	1.9	-	-	7.0
Labour Cost Index					
All sectors, ordinary time	1.1	1.0	-	1.1	4.2
Private sector, all salary & wage rates	1.1	0.9	1.0	1.0	4.1
- Unadjusted LCI ordinary time	1.6	1.1	-	-	5.7
Public sector, all salary & wage rates	0.6	2.2	-	-	5.4

Unemployment and underutilisation rates



Transition probabilities

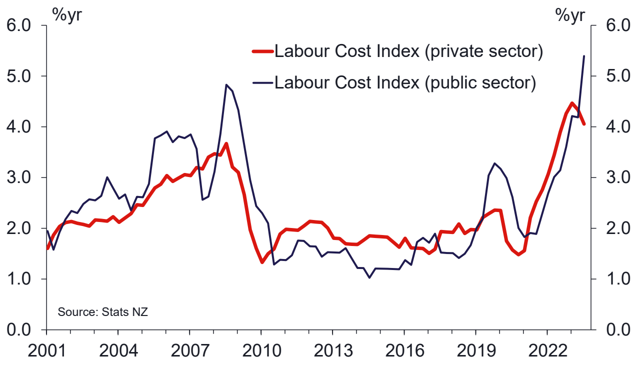


Elsewhere in the report, employment fell 0.2% in the September quarter, causing annual growth to slow to 2.4 from 4.1% previously. This was a weaker outcome than suggested by the tax-based Monthly Employment Indicator (MEI), which rose 0.4% during the quarter. Such differences can reflect the fact that the MEI counts filled jobs (rather than people employed) and does not cover the self-employed. However, today's household survey indicated that the number of people who were self-employed increased during the September quarter.

Given the above, we are more inclined to think that at least some of the unexpected weakness in employment reflects variability in the survey sample. Each quarter, one-eighth of the respondents to the survey are replaced by a new cohort, which can have a different employment and labour force participation rate than the cohort it is replacing, even if the unemployment rate within two cohorts is identical. On this occasion, the surprise decline in employment was also accompanied by a surprise 0.4ppts decline in the labour force participation rate to 74.0%. As a result of the decline in participation, the estimated labour force barely grew during the quarter despite continued strong migrant inflows and a 0.6% increase in the working age population. But as is usually the case, differences in survey samples tend to wash out in the unemployment rate, which as noted increased in line with expectations.

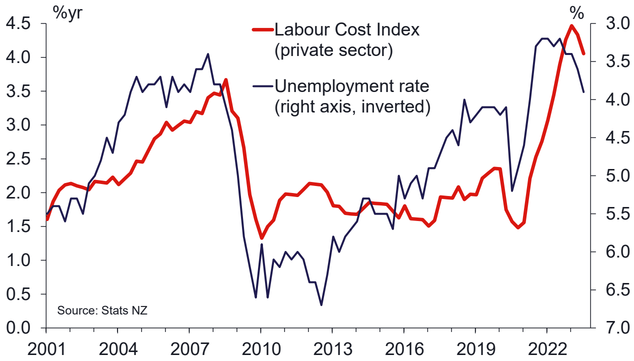
Perhaps the most important information today concerned wage growth – a reduction in which is crucial if the RBNZ is to get on top of inflation in the non-tradeables sector. The overall Labour Cost Index (LCI) rose 1.1% for the quarter – in line with our expectations – leaving the annual growth rate at 4.3%. However, as we expected, that relatively firm result owed to large settlements in parts of the public sector (in particular, the settlement with teachers, with education sector wages lifting 3.3% during the quarter). The public sector LCI increased 2.2% during the September quarter, lifting annual growth to 5.4%. Importantly, with the labour market loosening and the new government looking for cost savings, we expect public sector wage claims to moderate over the coming year, lagging developments in private sector wages as per usual.

Public and private sector wage growth

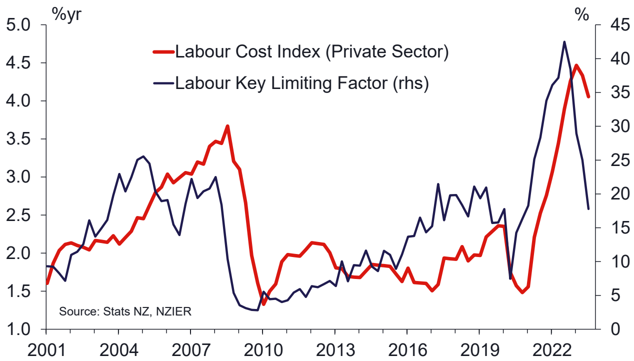


More importantly for the RBNZ, with the unemployment rate now well above the historic lows seen last year, wage growth in the private sector is showing clear signs that it has peaked. The LCI for the private sector increased just 0.9% in the September quarter – 0.1ppts below our forecast and that of the market. And for the second quarter in a row, the outcome was 0.2ppts lower than the same quarter a year earlier, causing annual growth to slow to 4.1% from a peak of 4.5% in the March quarter. The proportion of private sector salary and wage rates rising in the year to September was the least since the December 2021 quarter. The unadjusted LCI – which better represents developments in take-home pay – increased 1.1% during the quarter. This was also the smallest increase since the December 2021 quarter and lowered annual growth by 0.4ppts to 5.7% (thus tracking broadly in line with CPI inflation of 5.6%). Annual growth in private sector average hourly earnings, as measured by the more volatile Quarterly Employment Survey, dropped back to 7.1% from 7.7% previously.

Wage growth and unemployment rate



Wage growth and labour as limiting factor



Implications for the RBNZ.

In our view, today's news should leave the RBNZ comfortable with the projections made in the August Monetary Policy Statement, which depicted a further easing in labour market conditions. Indeed, at least at face value, employment growth was weaker than the RBNZ had forecast and the unemployment rate exceeded the RBNZ's forecast of 3.8%. In addition, growth in the private sector LCI was 0.1ppts less than the RBNZ had forecast. As a result, coming on top of the recent downside surprise to CPI inflation in the September quarter, a hike in the OCR at the RBNZ's 29 November meeting seems very unlikely (as reflected in market pricing).

Looking ahead, the RBNZ is forecasting the unemployment rate to rise to 4.4% by the end of this year (data to be released in early February). Together with the outcome of the December quarter CPI (released mid-January), ongoing developments in the labour market will have a significant bearing on the RBNZ's assessment of whether inflation will track down as quickly as has been forecast. More robust than expected inflation and/or labour market data would increase the likelihood that the RBNZ opts to lift the OCR at the February 2024 MPS meeting (as remains Westpac's forecast).

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