ECONOMIC BULLETIN

NZ labour market review, September quarter 2024.

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

The kids are back at school, softening the unemployment blow.

- **The unemployment rate rose further to 4.8% in the September quarter, a smaller increase than we expected. This was mostly due to more young people exiting the labour force, with study providing an outlet for the rise in joblessness.**
- **This effect will tend to dampen both the peaks and troughs in the unemployment rate – hence we have shaved down the peak in our forecast for next year to 5.4%.**
- **Wage pressures have eased, and are more consistent with an economy maintaining overall inflation of around 2%.**
- **We don't see anything in these numbers that might alter the Reserve Bank's thinking ahead of this month's OCR decision.**

New Zealand's labour market has continued to soften, reflecting the shallow drawn-out recession that we've been experiencing over the last couple of years. The unemployment rate rose further in the September quarter, albeit by less than expected, and wage pressures are easing back to something more consistent with consumer price inflation of around 2%.

Overall, we don't see anything in today's figures that would alter the Reserve Bank's thinking. Rising unemployment points to a soft economy, but no softer than was expected at this stage, and moderating wage growth is helping to squeeze inflation pressures out of the domestic economy. In that light, monetary policy no longer needs to be as restrictive, but it's a matter of taking the foot off the brake rather than stomping on the accelerator. We continue to expect another 50-basis point OCR cut at the *Monetary Policy Statement* later this month, turning to a more gradual pace of easing over the first half of next year.

	Quarterly actual		Quarterly expected		Annual
	Q2	Q3	Market	Westpac	Q3
Household Labour Force Survey					
Unemployment rate	4.6	4.8	5.0	5.0	-
Underutilisation rate	11.8	11.6	-	-	-
Employment growth	0.2	-0.5	-0.4	-0.6	-0.4
Participation rate	71.7	71.2	71.5	71.4	-
Hours worked	-1.5	-0.1	-	-	-1.1
Quarterly Employment Survey					
Private sector average hourly earnings	1.1	1.2	-	-	3.2
Labour Cost Index					
All sectors, ordinary time	1.1	0.6	-	0.7	3.8
Private sector, all salary & wage rates	0.9	0.6	0.7	0.7	3.3
- Unadjusted LCI ordinary time	1.2	0.8	-	-	4.5
Public sector, all salary & wage rates	1.8	0.9	-	-	5.6

Details.

The unemployment rate rose from 4.6% to 4.8% in the September quarter. This was a smaller increase than expected: we were picking a rise to 5.0%, as were the Reserve Bank and the average of market forecasts. That doesn't mean that the jobs market was stronger than believed – the number of people employed fell by 0.5% for the quarter, broadly as expected (and as signalled by the Monthly Employment Indicator). Instead, the difference was entirely due to a bigger than expected fall in the participation rate from 71.7% to 71.2%, reaching its lowest level in more than years.

What we take from this is that we're learning a bit more about the flexibility in the labour force. Indeed, it has had to flex to an unusual degree in recent years. In the initial post-Covid period, when the economy was running hot, the border closure meant that employers couldn't use migrants to fill the demand for workers. Consequently, many young people, especially teenagers, were drawn into the labour force to fill the gaps – often at the expense of study. Teen employment rose by 24% over 2021-22, and youth participation reached its highest level in decades.

By 2023, the border had been reopened and net migration was surging to record highs, at the same time that higher interest rates were starting to cool the economy. As a result, the previous dynamic has since been going in reverse – young people have seen the steepest job losses. And while many of them are ending up in the ranks of the unemployed, a substantial number of them are also opting out of the active labour force, either returning to or remaining in study. In fact, the NEET ratio (young people not in employment, education or training) has actually fallen over the last few quarters.

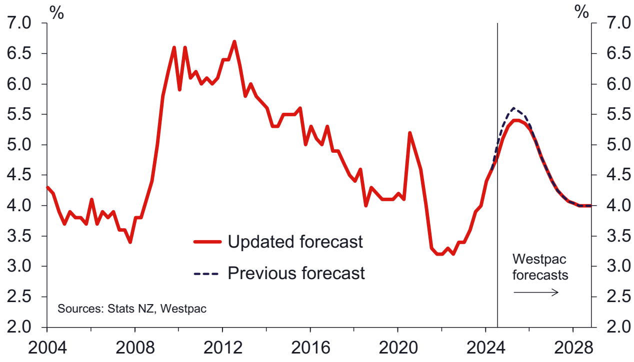
The bottom line is that changes in participation have been softening the swings in unemployment in both directions, perhaps to a greater degree than we've given it credit for. (It's possible that the 3.2% record low unemployment rate that we saw in 2022 was actually *understating* how tight the labour market was at the time.)

That suggests that the peak in unemployment for this cycle may end up lower than we were expecting – we were previously forecasting a 5.6% peak next year, but we've shaded that down to 5.4%. But it also suggests a more gradual fall in unemployment once the economy gets going again, as there's a pool of people who will be ready to re-enter the labour force if the job opportunities are there.

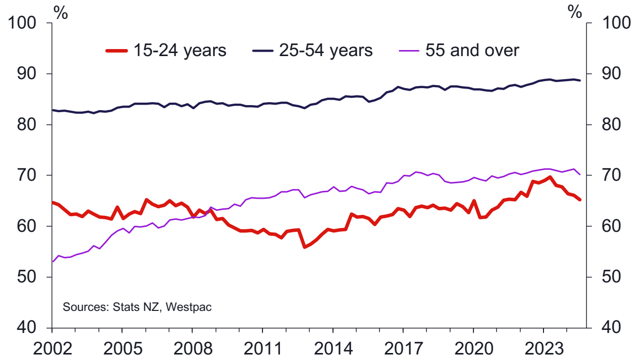
Turning to wages, the Labour Cost Index (LCI) rose by 0.6% for the quarter, slightly less than the 0.7% that we and the RBNZ expected. Public sector wages were up by 0.9%, boosted by a pay increase for police, but this didn't have a significant impact on the overall results. The unadjusted analytical LCI, which doesn't exclude pay increases that are related to productivity rose by 0.9% for the quarter, the slowest increase since March 2021.

While annual wage inflation is still running on the high side, the quarterly outturns were much more consistent with an economy running at 2% overall inflation. Slower wage growth was a necessary part of taming the stickier, domestically-driven elements of inflation, and these figures show that the RBNZ is finally getting the results that it was looking for.

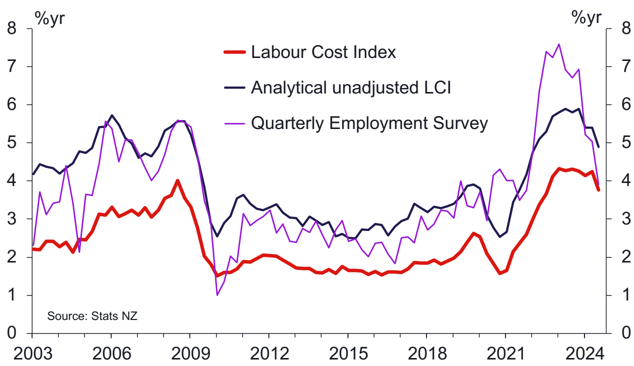
Unemployment rate



Participation rates by age group



Measures of wage growth



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