WESTPAC ECONOMIC BULLETIN

Labour market review, Q1 2022.

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Impressive... most impressive.

- The labour market remained extremely tight during the March quarter. The unemployment rate held at an equal-record low of 3.2%, and wage growth is accelerating.
- While inflation has outpaced wage growth so far, we expect this to change in the year ahead as the labour market remains tight.
- Rising wage growth will underscore the Reserve Bank's decision to step up the pace of monetary tightening.

Today's reports showed that the New Zealand labour market remained impressively tight in the March quarter, even if not quite living up to our forecasts in some ways. The unemployment rate remained at an equal-record low of 3.2%, and while wages haven't kept pace with the recent surge in inflation, they are still reaching some of the fastest rates of growth that we've seen in the inflation-targeting era.

For the Reserve Bank, it's the wage inflation measures that are where the rubber meets the road. So in that respect, today's figures represent a moderate upside surprise relative to the RBNZ's February forecasts. That underscores their decision to accelerate the pace of monetary tightening at the April review, and leaves us comfortable with our forecast of another 50 basis point OCR hike at the May review.

	Quarterly actual		Quarterly expected		Annual
	Q4	Q1	Market	Westpac	Q1
Household Labour Force Survey					
Unemployment rate	3.2	3.2	3.2	3.0	-
Underutilisation rate	9.2	9.3	-	-	-
Employment growth	0.0	0.1	0.1	0.2	2.9
Participation rate	71.0	70.9	71.0	71.0	-
Quarterly Employment Survey					
FTE employment	1.7	0.4	-	0.2	4.9
Hours paid	1.3	0.2	-	0.4	5.9
Private average hourly earnings	1.4	1.9	1.2	1.2	5.3
Labour Cost Index					
All sectors, ordinary time	0.6	0.8	-	0.7	3.0
Private sector, ordinary time	0.7	0.7	0.7	0.7	3.1

We expect the labour market to remain tight for some time, even with a slower pace of economic growth this year as the RBNZ applies the brakes. The demand for workers is very strong – well in excess of the local workforce's ability to meet it – and the reopening of the borders to international tourists is likely to give fresh impetus to that demand over the course of the next year.

Details.

The unemployment rate held steady at an equal-record low of 3.2% in the March quarter. That wasn't quite as positive as our forecast of a further decline to 3.0%, but in the key details it was similar to our view.

The number of people employed was just 0.1% higher for the quarter, similar to our forecast. That was also in line with Stats NZ's monthly filled jobs indicator, which is drawn from tax data and hence provides quite a comprehensive picture. Employment did drop a little in the February and March months, but it was still up for the quarter on average. Disruptions to hiring as the Omicron wave reached its peak may have been a factor here, although the experience overseas suggests that any impact from this will be short-lived.

Other measures of the labour market's spare capacity were mixed. The underemployment rate – those employed but wanting more hours – was down for the quarter, and indeed there was a marked shift from part-time to full-time work. However, the underutilisation rate – which includes a broader measure of potential jobseekers – rose slightly to 9.3%, having been flat at 9.2% in the December quarter.

As the Reserve Bank has noted, the economy is running above the 'maximum sustainable' level of employment. Identifying where that 'maximum' lies is an inexact science – the RBNZ looks at a range of indicators relative to their histories, and whether a consistent message is coming through from them. But the relevance of this concept is in what it means for wage inflation. And in that respect, today's figures support the idea that the labour market is unsustainably tight.

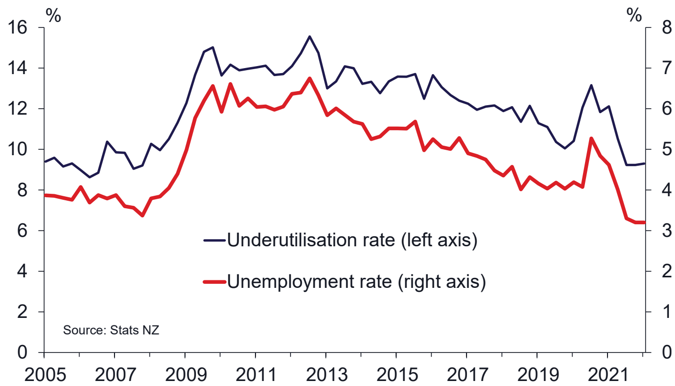
Wages have now built up a head of steam. The Labour Cost Index LCI) for all sectors rose by 0.8% for the quarter, to be up 3.0% on a year ago. As we noted in our preview, the LCI isn't a measure of what workers are actually receiving – to get a better handle on that, we should look at the analytical unadjusted measure, or the Quarterly Employment Survey (QES) measure of average hourly earnings. Both of these series were up 4.8% on a year ago. Moreover, on all of these measures, we're now running at the fastest annual pace since March 2009, just before the impact of the Global Financial Crisis.

Obviously wages haven't kept pace with the recent surge in the cost of living, with consumer prices up 6.9% over the same period. Nevertheless, we're now clearly seeing the acceleration in wage growth that we've been anticipating for some time. Wage growth tends to be the laggard in the economic cycle (hence why it was still running hot as late as 2009), but when it gets going it tend to carry a lot of momentum with it.

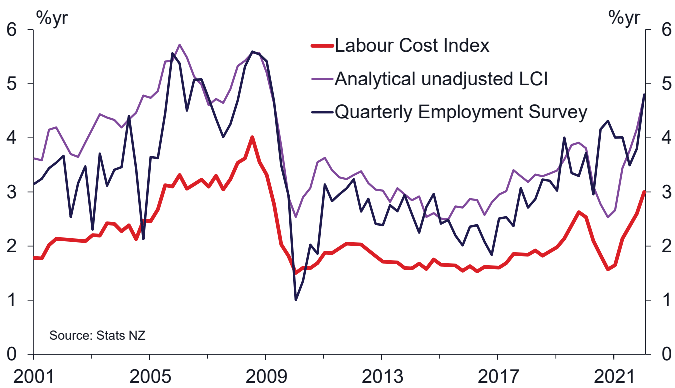
There is also encouraging evidence (for workers) that wage increases are broadening out. 64% of job roles have seen a pay increase in the last year, a new record for the survey going back to 1993. And nearly a third of those roles have seen pay rises of more than 5% in the last year. Notably, the reasons that employers give for wage rises are increasingly around matching market rates and retaining staff; cost of living adjustments are no more common now than they were a year ago.

Most sectors are seeing faster wage growth compared to a year ago, although where the biggest increases have been may come as a surprise to some. Near the top of the list is hospitality, a sector that has been under severe pressure in the last year. But this most likely reflects the prevalence of minimum wage roles in this sector, with the minimum wage rising by 5.8% last year (and another 6% this April). Construction and healthcare, two areas facing extreme levels of demand, understandably appear near the top of the list as well. The public sector actually appears at the low end of the range.

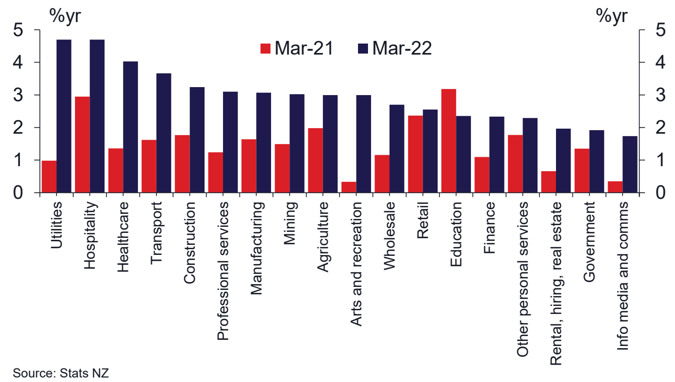
Unemployment and underutilisation rates



Measures of wage growth



Labour Cost Index, annual change by sector



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