Research

Economy Watch

1 November 2023

Labour Market Tightness Abating

- **Clear signs labour market tightness reducing**
- **Unemployment rate lifts to 3.9%**
- **Employment indicators mixed**
- **Unit labour cost inflation easing**
- **Adds to case for no more RBNZ OCR hikes**

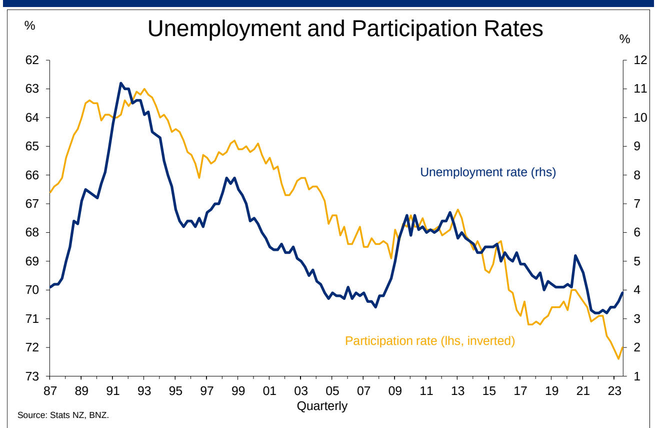
It felt like today's labour market data were always going to struggle to deny the clear messages, from a host of other indicators, suggesting that prior tightness in the market is abating, and rather rapidly.

In the event, the plethora of today's data simply confirmed and reinforced that message. It was writ large across the headline indicators from higher unemployment, slowing wage inflation, and falling employment.

The unemployment rate rose to 3.9% in Q3 from 3.6% in Q2, according to today's Household Labour Force Survey (HLFS). The unemployment is now at its highest in more than two years and meaningfully off its prior low of 3.2% (most recently seen a year ago).

The move in the unemployment rate is a firm pointer to tightness reducing. That assessment is strengthened by the participation rate dropping at the same time, to 72.0% from 72.4%. Another way of looking at it is through the employment rate, which dropped to 69.1% from 69.8% a quarter before.

Labour Market Tightness Abating

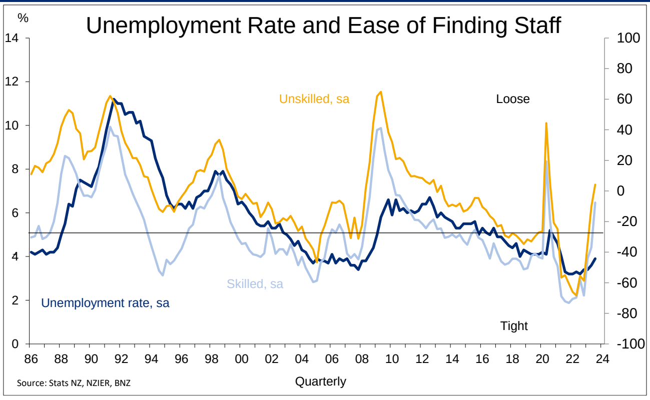


Importantly, all of this was on the 'less tight' side of RBNZ expectations. It might have only been by a tick on the unemployment rate, given the Bank's forecast of 3.8% in its August MPS, but it was another four ticks via the participation rate (the Bank expected 72.4%). To us, it is clear the labour market has turned. And indicators like firms' difficulty finding labour from the Quarterly Survey of Business Opinion (QSBO) point to further increases in the unemployment rate ahead.

HLFS/LCI - Q3 2023				
	Actual	Mkt Expected	RBNZ Aug MPS	Previous
Employment - qtly % ch	**-0.2**	+0.4	+0.3	**+1.0**
Employment - ann % ch	**+2.4**	+3.2	+3.1	**+4.1R**
Participation rate %	**72.0**	72.5	72.4	**72.4**
Unemployment rate %	**3.9**	3.9	3.8	**3.6**
LCI, private sector - qtly % ch	**+0.9**	+1.0	+1.0	**+1.1**

HLFS data seasonally adjusted

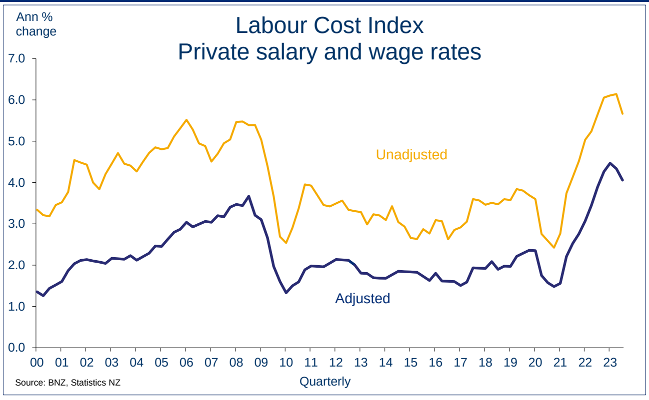
Unemployment Rate Expected To Lift Further



Less labour market tightness is one thing, but from a monetary policy point of view it is mostly a means to an end of getting inflation out of the system. On that front, it is notable that LCI wage inflation came in a tick under (RBNZ, market, and our) expectations. For example, the private sector including overtime LCI measure rose 0.9% in Q3, against expectations of a 1.0% increase. Annual wage inflation, on this measure, eased to 4.1% from 4.3%. Total LCI annual wage inflation remained at 4.3%, supported by stronger public sector wage growth.

The unadjusted private sector LCI wage measure rose 1.1% in Q3, slower than Q2's 1.6%. Q3's outturn was also closer to the adjusted LCI measure in another hint wage inflation heat is reducing.

Annual Wage Inflation Turns



The private sector LCI is our preferred wage inflation measure as a type of unit labour cost indicator. Of course, generally higher wage growth is desirable but needs to be supported by productivity growth to be sustained in the longer term.

LCI wage inflation coming in under RBNZ expectations is important in this relatively slow-moving series. Likewise, it is important that unit labour cost inflation is already easing, given its usual lag to wider labour market conditions.

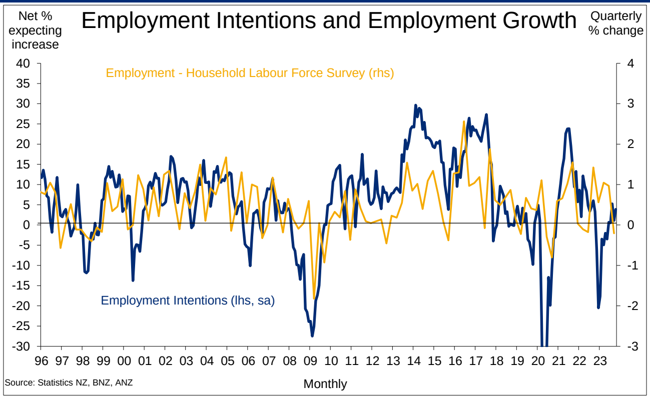
We think the dynamics of labour market tightness reducing and unit labour cost inflation easing is more reason for the RBNZ to not hike the cash rate further. We have long thought no more hikes are necessary and continue to see some easing next year. The market has moved in this direction post today's data, further reducing the chance of another OCR hike and is now contemplating an OCR reduction later next year.

HLFS employment fell 0.2% in Q3. This surprised us. We had a 0.5% gain pencilled in. While the general tenor of less tightness in the labour market in today's mass of labour market information fits with our broad economic view, we thought it would be driven by labour force growth outpacing employment growth rather than outright employment declines, especially given other monthly indicators suggesting job numbers are still increasing. HLFS annual employment growth eased to 2.4% from 4.1%.

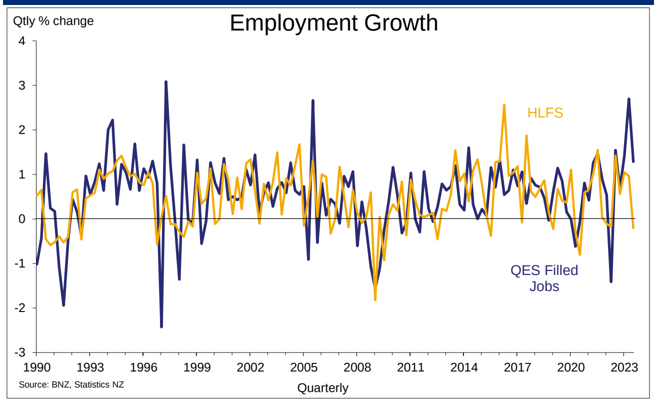
Firms' current employment intentions are positive, but do not look strong enough to prevent further increases in the unemployment rate.

The QES certainly wasn't weak on the jobs front, with filled jobs up 1.3% in the quarter and up 6.2% on a year ago. And paid hours from that survey was up 1.5% in Q3. It makes us wonder if the QES, as a business survey, is better reflecting, or directly picking up, the influence of large net migrant inflows. It certainly fits with the anecdotes that we are hearing that businesses are reporting it much easier to find staff.

Employment Declines



Or Does It?



In any case, the ongoing volatility in the data suggests caution with precise interpretation. But the broad thrust of today's labour market information is difficult to avoid. That is of prior market tightness easing – corroborating a host of other labour market indicators and anecdotes.

The mixed results of falling HLFS employment, but stronger QES filled jobs and paid hours gives mixed signals for Q3 GDP. Perhaps the balance suggests some upside risk to our current estimate of flat for the quarter, but we stay there pending many direct indicators of production to assess before the GDP data is out in December.

Other wage measures, like average hourly earnings from the Quarterly Employment Survey (QES), which increased 2.0% in Q3, can also be affected by compositional shifts in employment. Average hourly earnings were 7.1% higher than a year ago. That still suggests decent income growth accruing to the household sector overall at present, even though the dynamics of the HLFS and LCI suggest that softer growth lies ahead as tightness in the labour market abates.

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