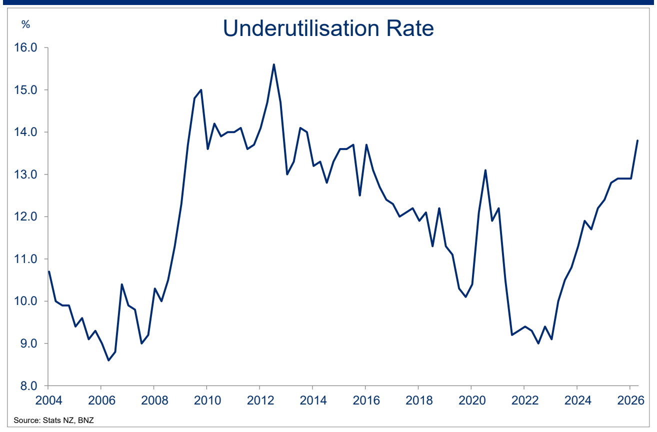
5 August 2026

Labour market at a turning point

- **Employment growth accelerating**
- **Over 65s lead the charge**
- **But unemployment rising too**
- **Wage growth has troughed**
- **Nothing to stop the RBNZ removing stimulus**

There was something for everyone in today's labour market data. Employment was surprisingly strong but so was unemployment. So is this an improving labour market or a deteriorating one? One thing's for sure: the media will focus almost exclusively on the fact that the unemployment rate, at 5.6%, has hit an 11-year high reflecting the parlous state of the New Zealand economy. And if you want to get really miserable take a look at the jump in the underutilisation rate to 13.8%. Both measures are a focal point of the central bank so, potentially, could give them the jitters.

Underutilisation rate soars

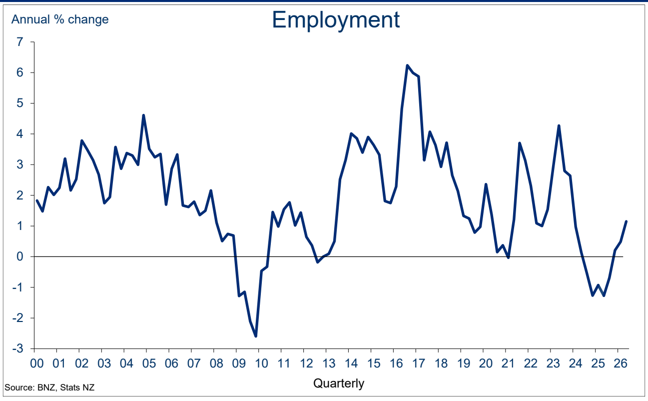


There is no doubting the state of the labour market is undesirable and, for many of those who are unemployed the situation has been grim for some time. But a singular focus on the unemployment rate overlooks the fact that the data confirm our view that the economy is turning the corner. And this despite the numbers referring to a June quarter in which the economy was battered by soaring oil prices and the chaos in the Middle East.

The unemployment rate rises when the number of people in the work force increases by more than the number of people gaining employment. An obvious example of this is when the number of folk employed actually falls. This is exactly what was happening through 2024 and most of 2025. But it's not the case now. Employment grew 0.5% in the June quarter, much more than the 0.2% we had anticipated. And annual employment growth increased to 1.2%, its highest pace since December 2023.

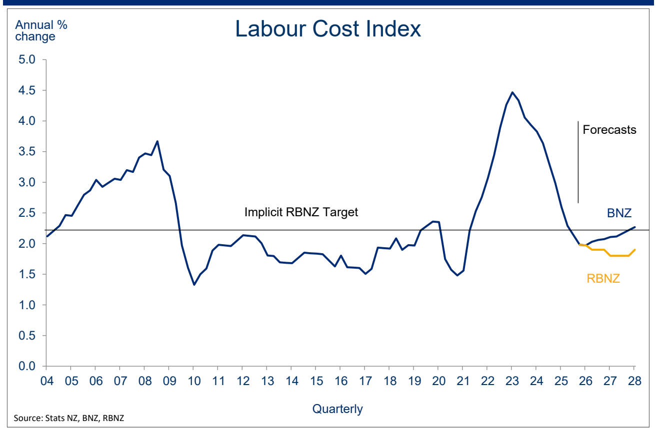
As the economy continues to expand job creation should grow with it. By the second half of 2027 we expect the annual increase in numbers employed to be twice what it is now.

Getting better



Meanwhile, wage inflation, as measured by the labour cost index (LCI), appears to have troughed. At 2.0% for the year the pace of increase in the private sector LCI was a smidgen above the Reserve Bank's 1.9% pick. At this level it is entirely consistent with achieving the 2.0% inflation target. But the Reserve Bank is assuming that wage growth is trending lower. We don't see it this way and think the gap between what the Bank has forecast and reality will grow.

Wage inflation troughed?



So all this says inflation is surprisingly high given how weak the labour market is thus implying there may not be as much spare capacity in the economy as the unemployment rate would have us think at first glance. With job ads and hiring intentions rising, yet job growth remaining modest, one reason for this may be a mismatch between skills needed and skills available. Or, in the economic vernacular, the NAIRU may well be higher than the 4.5%-ish the RBNZ has previously assumed.

We are not arguing that today's labour market report increases the pressure on the Reserve Bank to tighten monetary policy. But we are saying that the higher-than-anticipated unemployment rate is no reason to dissuade the RBNZ from continuing the tightening cycle it appears to have embarked upon as economic momentum lifts.

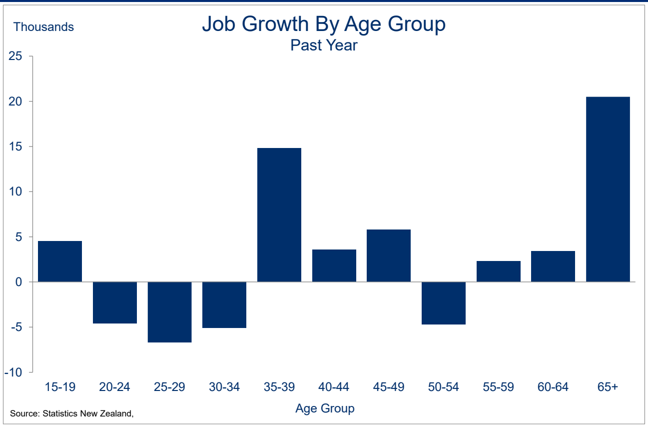
On this basis we still believe the RBNZ will push ahead with raising its cash rate to 2.75% at its September meeting with the intent of further reducing the stimulus easy monetary conditions currently impart.

Remember too that the labour market lags output. It takes time for growth in activity to convert into a meaningful pick up in employment. Nonetheless, we now think the unemployment rate is at or very near its peak. Our flash forecast for Q3 has employment growth of 0.4% which, assuming a constant participation rate, leaves the unemployment rate unchanged. We anticipate the unemployment rate will then head progressively lower through 2027. Were we to reconsider our labour market outlook and adopt a more pessimistic view of the world then we would look to moderate our interest rate track. That is clearly not the case now.

Through all this we are quick to note that there is significant variation in performance between regions and age groups. It will surprise no-one to learn that the South Island is dramatically outperforming the North. In the June quarter the South Island unemployment rate was a mere 3.7% while in the North Island it was 6.0%! As an aside, for those who think Wellington is miserable with its 4.9% unemployment rate, spare a thought for the 6.5% of the workforce who are unemployed in Auckland.

Another interesting observation is the age group with the strongest job growth. The winners here, by a significant margin, are those aged over 65 who accounted for 60% of the annual growth in total employment. In part this simply reflects demographics, i.e there are an increasing number of people who are aged over 65 in the economy. But, equally, the participation rate of those in the demographic is rising rapidly as more older folk decide to work. Some because they have to but an increasing number, we suspect, because they simply want to. At the other extreme it is disconcerting to see that there are 16,500 less people aged 20 to 34 in employment now compared to this time last year.

Distributional variance



Overall, the labour market is very weak. But, like elsewhere in the economy, there are signs of life which we hope will blossom as the year progresses.

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