Research
Economy Watch

4 November 2026

Labour market surprises

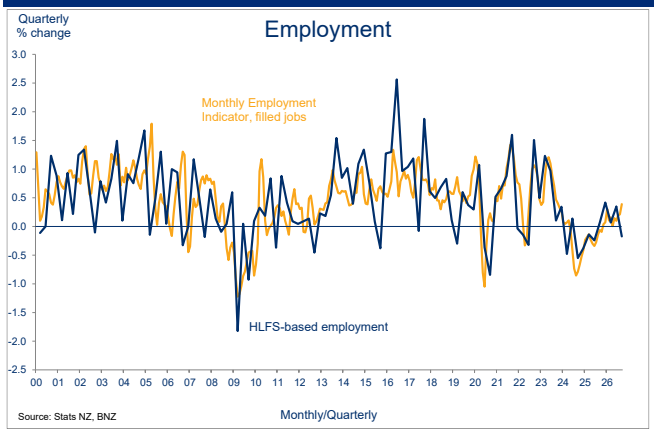
- **Labour market softer than expected**
- **Employment dips in Q3**
- **Unemployment nudges higher**
- **Real disposable incomes under pressure**
- **LCI annual inflation ticks higher**
- **Employment intentions positive**

Economic recovery seldom follows an orderly, uniform, or straight-line path. And, boy, did the Q3 labour market provide a stark reminder of that fact today.

Perhaps the biggest surprise was the quarterly drop in employment. It was a tiny fall at just 0.1%, but quite different to widespread expectations of a moderate lift. The market expected a gain of 0.4%, as did we, while the RBNZ forecast a 0.3% increase.

The employment decline in the Household Labour Force Survey (HLFS) is diametrically opposed to the reasonable looking growth in the monthly employment indicators over recent months.

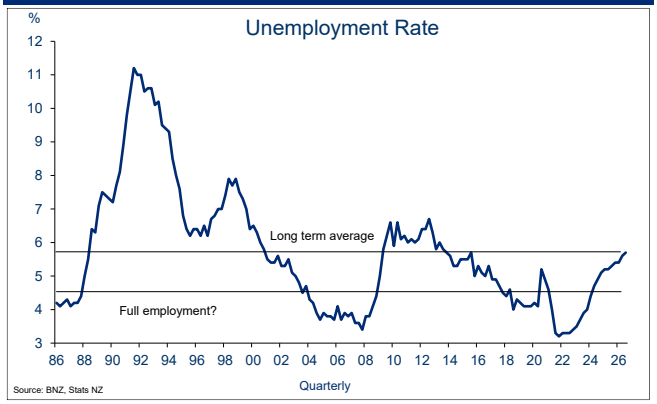
Employment unexpectedly dips in Q3



Downward revisions added to the weaker tone of HLFS. Annual employment growth eased to 0.7%, from 0.9%, and against market expectations of a lift to 1.6%.

Weaker employment flowed through to unemployment. The unemployment rate unexpectedly lifted to 5.7% from 5.6%. This was against market and RBNZ expectations of a tick down to 5.5% and even a tick above our expectations of the unemployment rate remaining steady at 5.6%.

Unemployment rises

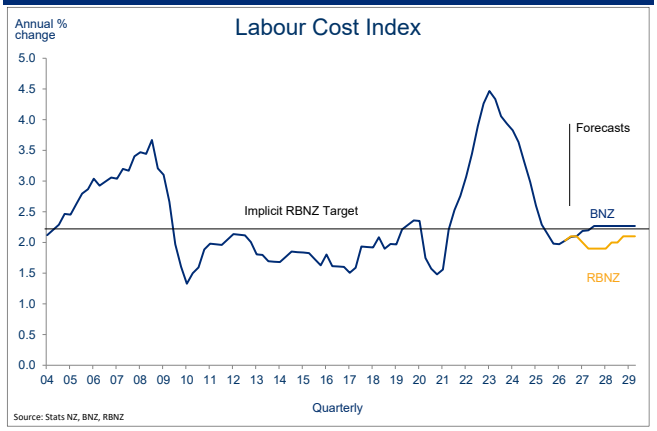


Disconcertingly, the unemployment rate rose despite the participation rate easing to 70.4% from (a downwardly revised) 70.6%.

Sometimes the unemployment rate can push higher when more people enter the labour market. That wasn't the case in Q3. That gives the release a clearly slacker feel than was anticipated.

In that context, it makes the wage inflation outcomes even more intriguing. The private sector Labour Cost Index (LCI) rose 0.5% q/q. This matched the RBNZ's pick while it was a tick lower than we had. Annual LCI wage inflation edged up to 2.1% from 2.0%.

LCI annual inflation edges upward



Wages matching the RBNZ's forecast means that today's labour market data was not uniformly softer than it expected. However, the employment and unemployment readings were clearly on the slacker side of the Bank's expectations. It must raise questions around the pace at which the Bank will lift its cash rate ahead.

For now, we'll stick with our view that the cash rate peaks at 3.75% and will be lifted by 25bps at each of the next four meetings. However, today's data increases the chance of more pauses along the way. Picking the timing of any potential pauses is fraught with difficulty, especially when data and the Bank's guidance are at odds.

The fact that annual wage inflation is not only not falling but starting to edge upwards despite the feeling of labour market slack is worth monitoring.

This may well reflect the typical lags from economic activity, to employment, to wage growth. But the unemployment rate has been trending higher for 5 years and yet wage disinflation has stopped.

It supports a view we have held for a while now, that we may well see more wage inflation for any given level of unemployment rate than we have observed in the past.

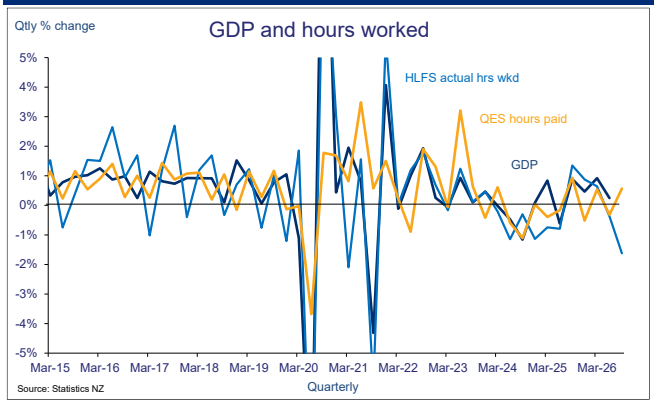
While the unemployment rate has pushed up to its highest level since 2015, it is also notable that it has reached its average level since the HLFS survey started back in 1986.

That is not to say the real LCI has not fallen. The oil shock and associated inflation have put pressure on real incomes for people and businesses alike. It is the painful nature of the beast. What is worse, in the face of such a shock, a process of trying to recoup lost ground can be a catalyst for inflation to persist.

To increase real wages (and/or profits) on a sustained and enduring basis requires a lift in the terms of trade or productivity. Feeble growth in the latter over many years has been well-documented while the former has recently been hit hard by the oil shock.

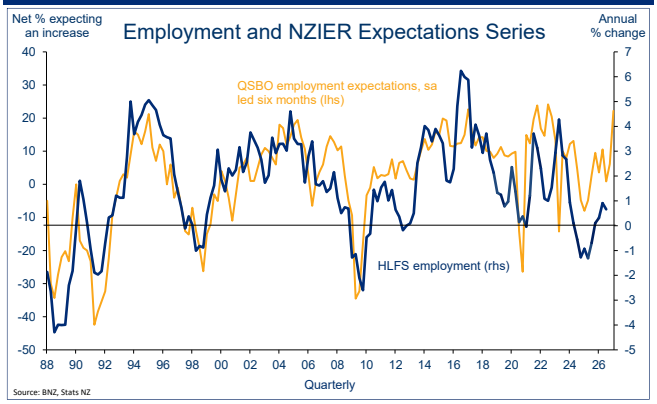
There were mixed messages for Q3 GDP in today's figures. The dip in employment and 1.6% slump in HLFS hours worked suggest downside risk to our thoughts of modest growth, while the 0.6% q/q expansion in hours paid in the Quarterly Employment Survey (QES) is more supportive. The QES is more directly linked to GDP than the HLFS.

Mixed signals for Q3 GDP



On a more positive note, we shouldn't lose sight of genuinely strong employment intentions from the likes of the Quarterly Survey of Business Opinion. While we very much doubt annual employment growth will follow the extent of its positivity, it gives reason to believe that employment will trend higher and unemployment lower over the coming year.

Positive intentions



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