6 November 2024

Labour market deterioration gains pace

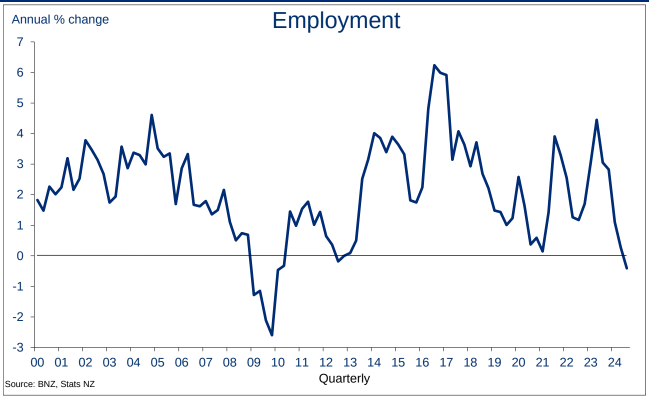
- **Employment track mimicking GFC times**
- **As unemployment rate rises further**
- **And labour cost inflation falls**
- **More RBNZ aggression needed**
- **But no need to press the panic button**

Those looking for a sharp jump in unemployment to justify the RBNZ cutting its cash rate by 75 basis points at its November 27 MPS will be sorely disappointed with the news today that the unemployment rate rose less than expected to 4.8% in September from 4.6% in June. The RBNZ was expecting a 5.0% headline reading.

Nonetheless, while the unemployment rate may have hinted at a relatively resilient labour market, not much else did.

To start with, employment fell 0.5% in the quarter, a tick higher than the RBNZ's -0.4% expectation. On an annual basis, employment contracted 0.4%. This is the biggest decline since March 2010. Despite this, there remain folk who continue to question whether we are in a recession or not. What more do they need?

Further proof of recession

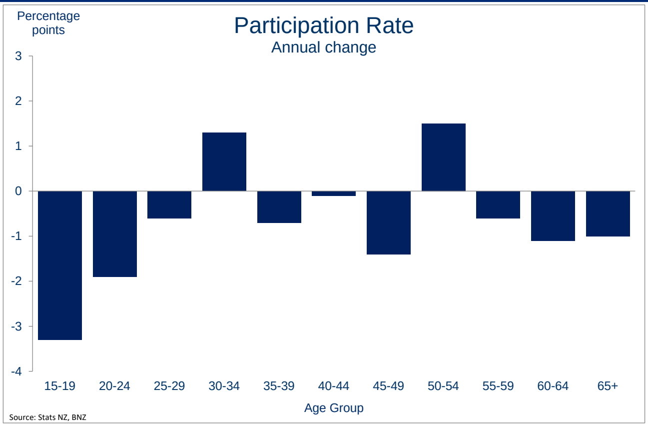


Notably, full time employment declined 0.7% in the quarter to be 0.7% down on a year earlier. It was the third consecutive quarterly drop. 2009, during the GFC, was the last time we saw three consecutive declines in this series.

Had the participation rate not slumped from 71.7% to 71.2% the unemployment rate would have been significantly higher. The "miss" by forecasters was the participation rate rather than the unemployment rate, per se.

A fall in participation means folk who were previously looking for work have given up doing so often because they have become disenfranchised and believe the search for work is pointless. With this in mind, note that the participation amongst youth (15 to 19 year olds) is plummeting. We are not surprised by this. This may in part reflect the fact that an increased labour supply (read migrants) of higher skilled workers is displacing teenagers who were being used by businesses because there were simply no other options, especially during the COVID era. If these youngsters are instead getting themselves better educated, then this development may be no bad thing but to the extent it means low-income families now have one less earner and/or it shows businesses simply can't take on youth now, it is worrying.

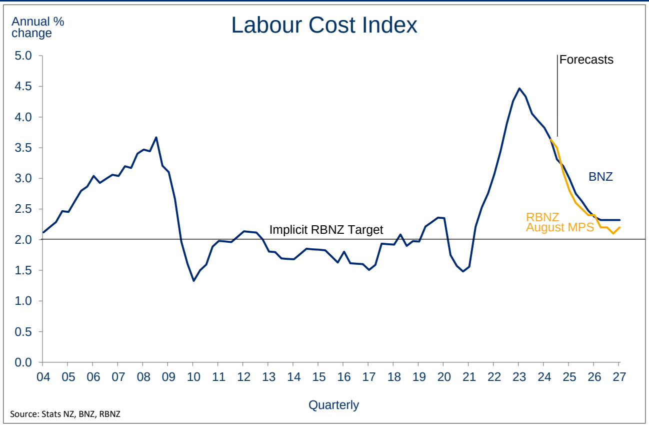
Disenfranchised youth



Ultimately, the Reserve Bank's appropriate obsession with the labour market is driven by what developments mean for inflation. Given this, the Bank will be happy with what it sees. Not only does the weakness in employment indicate domestic demand conditions are disinflationary but the ongoing drop in wage inflation also indicates a reduction in inflationary pressure via lower business input cost concerns.

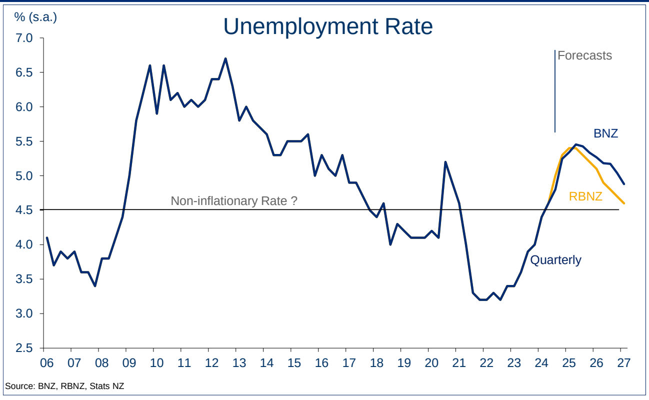
The Labour Cost Index (LCI) is the Bank's point of reference for wage pressure. Annual inflation in this measure fell to 3.3% in the September quarter, lower than the Bank's 3.5% projection. LCI inflation is a key determinant of pesky non-tradables inflation so its decline will help supress non-tradables price concerns going forward.

Wage pressure falling fast



There is little in today's data to cause us to change our forecasts of anything. Employment and the LCI were bang on our expectations. We missed on the participation rate so have adjusted our starting point for this series in our projections. The corollary to this is that we have edged down our expected peak in the unemployment rate to 5.5% (in June 2025). This is now only marginally higher than the RBNZ's expected peak of 5.4%.

Unemployment headed higher



Our view on wage growth and CPI inflation is unchanged therefore the same can be said for our interest rate projections.

From the Reserve Bank's perspective, we doubt whether it will view the labour market data, in its entirety, as being anything other than being broadly consistent with its August Monetary Policy Statement projections. Given the RBNZ has already cut the cash rate 25 basis points more than it had assumed in those forecasts and given that it's likely a further cut of 50 basis points (another 25 points ahead of forecast) will be delivered later this month, we see no reason to advocate anything more.

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