27 January 2010

A turning tide

2009Q4 employment and wage data preview

- **Employment expected to have grown for the first time in a year.**
- **Unemployment to rise slightly further to 6.7%.**
- **Hours worked to lift more convincingly.**

December quarter employment expectations

	Quarterly % change		Annual
	Previous	**Westpac**	**Westpac**
Employment growth	–0.8	0.3	–2.2
Unemployment Rate %	6.5	6.7	
Hours worked %	–0.7	1.1	-1.7
Participation Rate %	68.0	68.2	

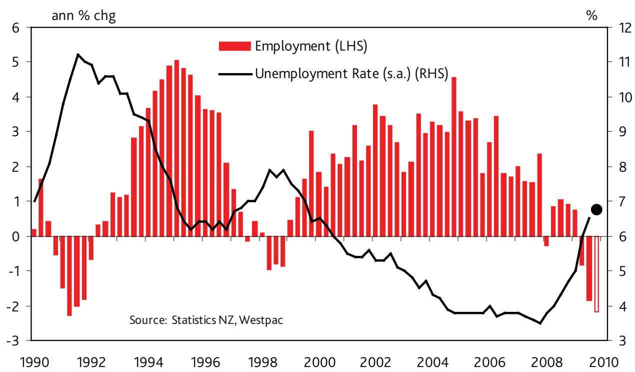
Employment and unemployment

At last! Indication are that New Zealand experienced employment growth in the fourth quarter of 2009, the first in a year. According to the NZIER's *Quarterly Survey of Business Opinion*, slightly more firms intend to increase staff numbers than those that intend to decrease. That suggests the quarterly rate of employment growth will be close to the historic average of 0.3%. The improvement in the Westpac McDermott Miller Employment Confidence Index over the September and December quarters is further evidence that the labour market from the employees' point of view.

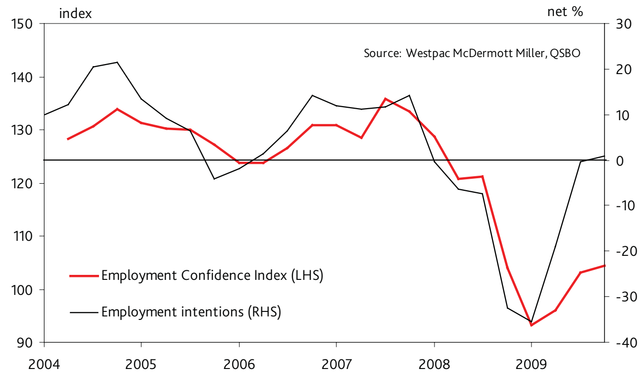
The final reason we expect positive employment growth for the fourth quarter is less encouraging. Employment growth figures have been predictably volatile for the past two years, quite possibly because of changes to the seasonal pattern that are difficult for Statistics NZ to correct for. For the past two years the December quarter has been strong, only to be followed by a shockingly weak March quarter. We are preparing for a repeat this year. In other words, the employment growth figures could well be rosier than the true situation on the ground.

After such a severe recession, merely average employment growth is not enough to prevent unemployment from rising further. Firms are telling us that it is still easy to find labour, although not as easy as it was in early-2009. We are forecasting a further slight increase in unemployment from 6.5% to 6.7%, which we expect will be the high-water mark following the recession of 2008/2009.

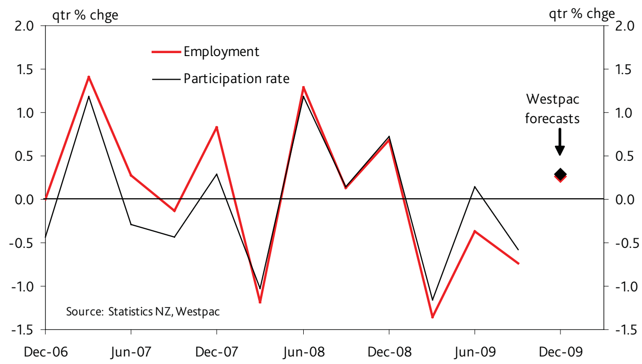
Household Labour Force Survey



Employment confidence and intentions



Employment vs participation rate



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The final piece in the employment data jigsaw is the participation rate. It has been volatile recently, moving in lock-step with employment growth. Participation has spiked up in each of the past two Decembers, and we expect a repeat this year.

A more reliable indication that the NZ labour market is recovering is likely to come via increased hours of work. Production gains in the early stages of recovery were most likely met by increasing the hours of existing staff, rather than by hiring new staff. We are forecasting a 1.1% increase in total hours worked, equating to a decent lift in hours worked per full-time equivalent worker.

Market implications

We think the risk to our unemployment forecast is balanced, but the risk to our employment forecast is skewed to the upside by that volatile seasonal pattern. The Reserve Bank's unemployment forecast is 6.6%, and we infer from the bank's published annual employment forecasts that it expects employment growth below our forecast of 0.3%. (To square the circle, they must be expecting no change in the participation rate). The Bank will pay more attention to the unemployment rate than to employment. An unemployment rate of 6.4% or lower would be required to bring a March OCR hike seriously into the frame – a higher outcome would strengthen our conviction that the Bank will remain on hold at the March *MPS*. The market seems to have learned that there is greater information content in the unemployment rate, and now tends to react more to unemployment surprises than employment surprises.

Wages

New Zealand's full suit of wage data is revealed on Tuesday 2 February at 10:45 NZST. The Labour Cost Index is the premier guide wage inflation, because it measures the cost of a given quantity and quality of labour input. We expect fourth quarter wage growth to run slightly ahead of the third quarter, partly because the wage-depressing effect of recession is beginning to blow over, and partly because of seasonality. Wage growth is strongest in the fourth quarter because that is when the largest number of people get their annual increase, but Statistics NZ does not seasonally adjust the LCI.

Private sector wage growth including overtime, which receives the most attention from the RBNZ, is expected to rise 0.5%, compared to 0.4% last quarter. Public sector wage growth, however, is expected to rise far slower than it did in the third quarter, when a large teachers' pay award affected the wage figures. If our quarterly forecasts are correct, annual wage growth will slow to an eight-year low.

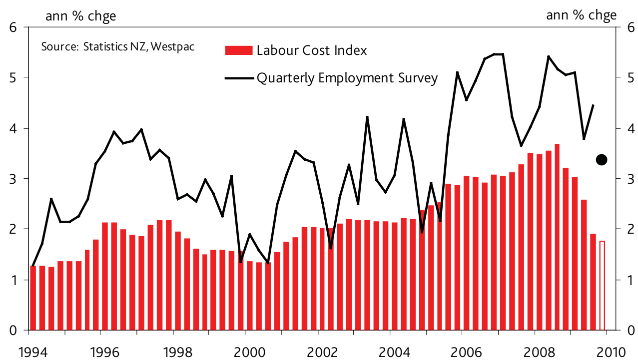
The Quarterly Employment Survey is released at the same time as the Labour Cost Index. Last quarter it threw up an absolutely wild read of 1.7% private sector ordinary time wage growth, and 2.1% total ordinary time wage growth. We never took that seriously. We expect some payback this quarter, with a drop in private sector wages. In any case, the QES wage measures are notoriously volatile and receive little attention from the market.

Of more interest to the market is the QES measure of paid hours, which gives a loose read on the state of economic activity over the October to December period. We expect a sharp increase in paid hours, commensurate with the generally improved tone in economic data relating to the quarter.

December quarter wage expectations

	Quarterly % change		Annual
	Previous	**Westpac**	**Westpac**
LCI – All sectors ex overtime	0.5	0.6	1.9
LCI – Pvt sector ex overtime	0.4	0.5	1.8
LCI – Pvt sector incl overtime	0.4	0.5	1.8
QES wages – All sectors	1.7	–0.2	3.4
QES wages – Pvt sector	2.1	0.0	4.2

Private Sector Earnings and Labour Costs



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