LABOUR MARKET DATA PREVIEW – JUNE QUARTER 2007
(LCI and QES due 10.45am 6 August, HLFS due 10.45am 9 August)

Key points

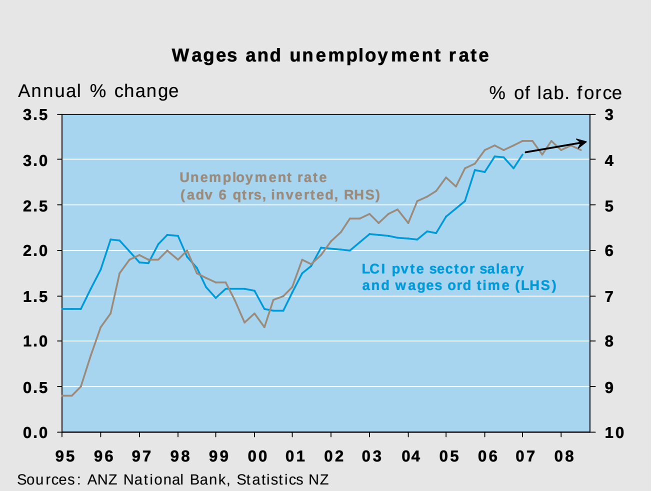
- **Wage growth is likely to be strong – hitting record highs – with changes to the statutory minimum wage contributing.**
- **We expect modest employment growth of 0.3 percent and an unchanged unemployment rate of 3.8 percent.**
- **Collectively, we expect the labour market data to confirm strong late-cycle support to the economy and pose an ongoing source of inflationary risks.**

Expectations		
	ANZ National	Market
LCI salary and wage ordinary time (private sector)	**0.9% q/q** **3.3% y/y**	0.7% q/q 3.0% y/y
QES salary and wage ordinary time (private sector)	**2.2% q/q** **5.4% y/y**	2.0% q/q 5.2% y/y
HLFS unemployment rate (s.a.)	**3.8%**	3.8%
HLFS participation rate (s.a.)	**68.6%**	68.5%
HLFS employment growth	**0.3% q/q** **1.1% y/y**	0.3% q/q 1.1% y/y

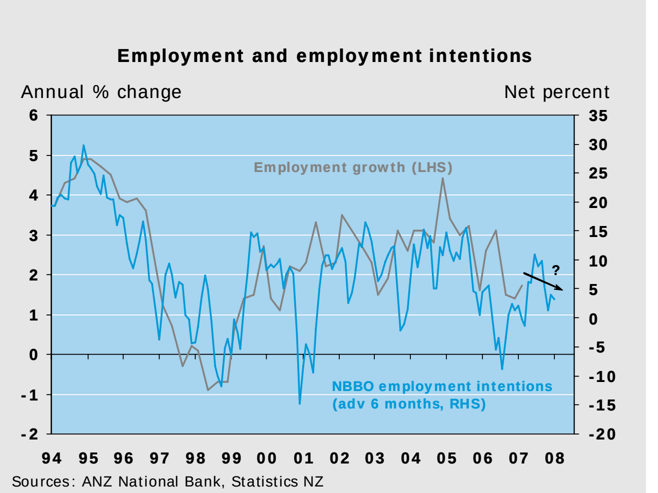
The June quarter wage data on Monday is expected to record new record highs for wage growth. The key gauge to watch is the Labour Cost Index (LCI) measure of private sector ordinary time earnings. We expect this to record a 0.9 percent increase in the June quarter, taking the annual increase to a new record high of 3.3 percent. A 9.8 percent increase in both the adult and youth minimum wage rates (which came into effect on 1 April) is expected to contribute to the strong wage growth in the quarter. For completeness, the less reliable Quarterly Employment Survey (QES) wage indicator – which is volatile and influenced by compositional changes – is expected to increase by 2.2 percent in the quarter, taking annual growth to 5.4 percent.

The recent resurgence in economic activity will ensure wage pressures remain elevated for some time. The labour market remains extremely tight, with firms continuing to report difficulty in finding both skilled and unskilled workers. Economic momentum from the end of last year has been sustained into the early parts of this year and will add to the already significant pressures on resources. The direct impact of minimum wage rate increases gets picked up this quarter. However, the indirect impact – as employees seek relativity adjustments – is likely to take some time to come through and portends of further wage inflation.

We expect a modest increase in employment growth in the June quarter, but as always, there is a large potential error-band around this estimate. After soft growth at the end of 2006, employment rebounded strongly in the March quarter, recording growth of 1.2 percent. Given the volatile nature of the Household Labour Force Survey (HLFS), the balance of probability rests with a more modest result in the June quarter, and we have pencilled in growth of 0.3 percent, which takes annual growth to 1.1 percent. The key uncertainty lies with the participation rate. It rose strongly to 68.6 percent in the March quarter, and although there is potential for it to increase again, we believe it will hold at this level in the June quarter. This will keep the unemployment rate unchanged at near record lows of 3.8 percent. Seasonally adjusted hours worked fell 0.4 percent in the March quarter, despite a 1.2 percent increase in employment growth and GDP growing strongly at 1.0 percent. Hours worked suffers from the same volatility as employment growth, and as a result we expect it to bounce back this quarter.



Sources: ANZ National Bank, Statistics NZ



Sources: ANZ National Bank, Statistics NZ

Assessment

We expect the labour market data to confirm strong late cycle support to the economy and pose an ongoing source of inflationary risks. As a late cycle indicator, wage and employment reports tend to be the last to turn. The Reserve Bank is likely to view the data as somewhat of a lagging indicator. However, with a lack of inflation headroom, the Reserve Bank will continue to see the labour market as a continuing source of inflationary pressure. In addition, strong labour income growth will continue to provide support to the housing market and consumer spending. As a result, interest rates look set to stay high for some time, with the bias remaining upwards.

In this environment, the collective message is one of rate cuts being a long way off. After hiking rates four times this year the Reserve Bank are now purely in data-watch mode and looking for evidence that any slowdown will be sustained. Given the change to a more neutral stance in the July *OCR Review*, the threshold for a further hike is likely to be very high. In this regard, we feel the labour market data will need to print incredibly strong to force the Bank to contemplate lifting interest rates again. From a financial markets perspective, the wage and employment reports will prevent the market from testing an early easing theme. Crucially for the Reserve Bank, this will allow them to maintain policy traction along the yield curve to foster the eventual moderation in growth they are seeking.

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