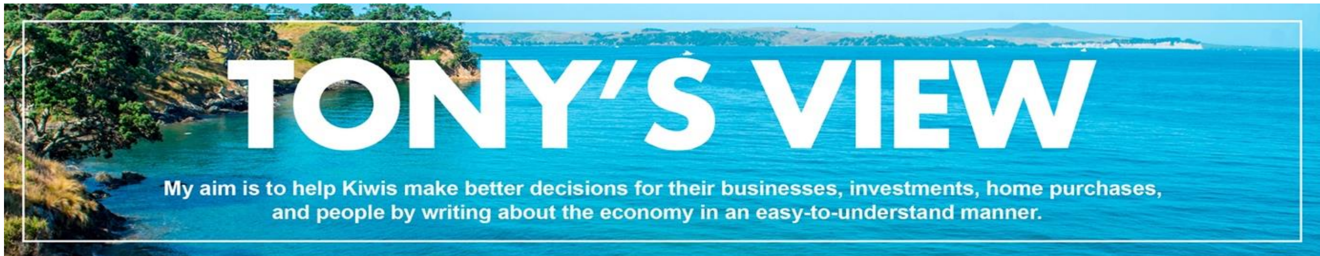

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Endgame back on

Just for your guide in case you have been living under a rock these past three months, I have updated my disclaimer on the last page. I expect many others will soon be doing the same. It's the future, man.

The highlight of the NZ economic calendar this past week was the release of labour market data yesterday. This is not because the data tell us where the pace of growth in the economy is headed as is the case for things like shifts in consumer sentiment, commodity prices, the exchange rate, dwelling consent numbers, etc. The labour market data in fact lag the economic cycle. They largely reflect where we have been.

This arises because when we get something which causes the rate of growth in the economy to slow down businesses are not going to (usually) immediately respond by laying off staff. It is a costly exercise to show staff the door then try to rehire people down the track when sales prospects look better.

So, businesses wait a while to see whether a dip in sales looks like being a blip or something sustained. Then they will look to slim staff numbers by either sacking people or cutting back on new hiring.

This does not however mean that the data are unimportant. People pay a lot of attention to the unemployment rate as a measure of how healthy an economy is. As a rule we all want the unemployment rate to be low because that means people are being usefully engaged, incomes are being earned, taxes are flowing in, aspirations are being met.

But the key importance of the data currently is the insight they can give us into the degree of tightness in the labour market. This matters because inflation is at 7.2% and the Reserve Bank has raised interest rates to try and slow down the pace of economic growth, strip away the pricing power of businesses, and get the inflation rate on track to the desired 1% - 3% target range within 18-24 months.

In New Zealand the pace of wages growth has responded strongly to the lack of staff. This reflects the highly deregulated nature of our labour market. In contrast, in Australian wages growth has not been such a bugbear for their

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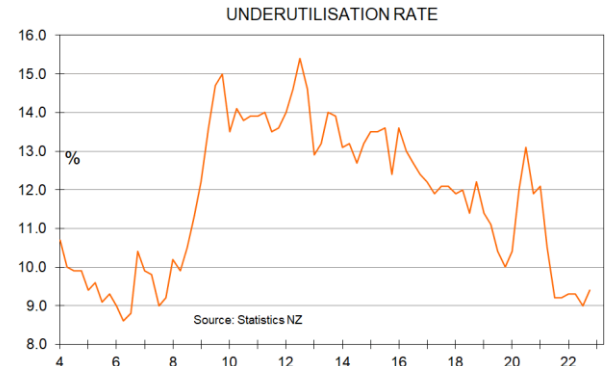
central bank because wage rates are more rigidly influenced by union/employer negotiations.

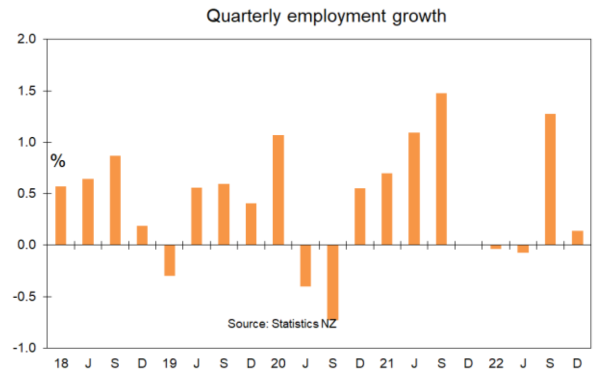
Here, if we look at measures of wage rates for particular jobs then there has been growth. Yet when we take into account the way in which people have gained good increases by changing employers the average hourly earnings measures which we economists track have been pushed to high rates of growth.

So, what did we learn yesterday? Thankfully the news was good. The unemployment rate crept up from 3.3% to 3.4% and the wider measure called the under-utilisation rate rose from 9% to 9.4%.

There is a bit more slack in the labour market than we feared and than the Reserve Bank put into the forecasts they used when deciding to boost the cash rate by a record 0.75% on November 23, predict recession, and pencil in a peak official cash rate of 5.5%.



The second piece of good news was that job numbers only rose by 0.1% in the December quarter. This was a lot less than 1.3% growth in the September quarter.



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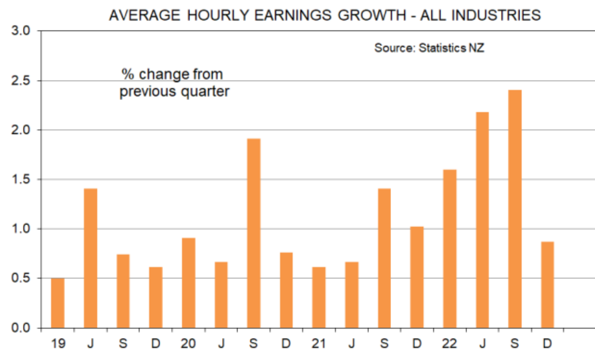
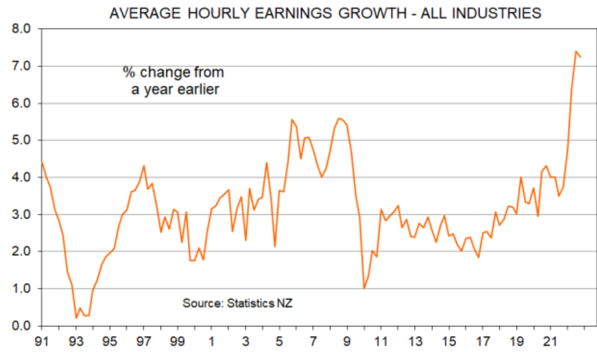
For your guide, the Reserve Bank had expected the unemployment rate to be 3.2%.

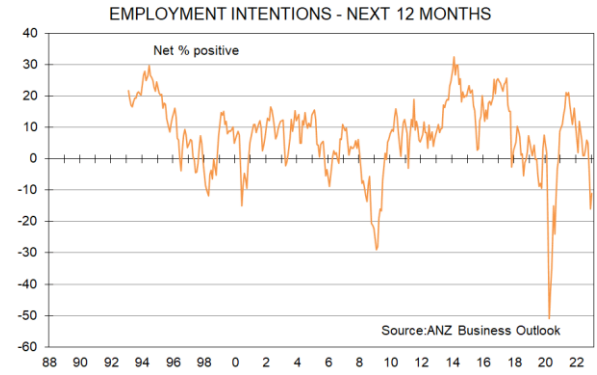
The best news from the labour market release came in the wages area. Average hourly ordinary time earnings only grew by 0.9% in the December quarter after rising 2.4% in the September quarter, 2.2% in the June quarter, and 1.9% in the Marc quarter. The 0.9% gain was the slowest since June 2021.



The labour market in New Zealand is still very tight. But it is starting to ease and the direction of change matters a lot when it comes to monetary policy. Forward-looking indicators are also telling us that the unemployment rate is going to go higher and wages growth will be restrained.



The net proportion of businesses in the ANZ Business Outlook Survey for instance who plan to hire more people over the coming year stands at -11%. This is well below the ten year average of +11%.



Job advertisement numbers are also falling away. As yet however the average person is not showing

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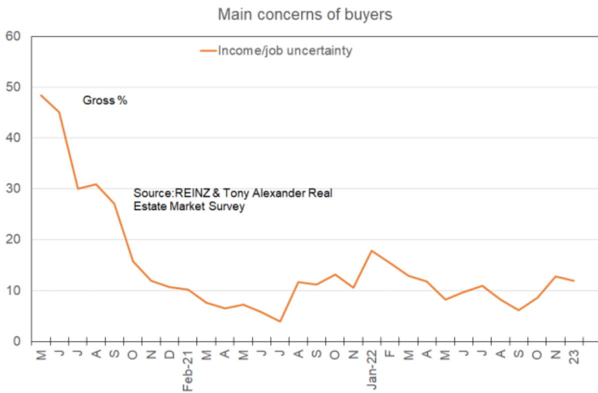
much concern about their employment prospects. I get some insight into this from my monthly survey of residential real estate agents undertaken with REINZ. This month's survey is underway at the moment and results will come out next week. But with most numbers in I can see that agents are not reporting rising concerns amongst potential buyers about their jobs and incomes.



What are the main implications of the employment numbers? Mainly the fresh news is on the inflation and interest rates side. Forecasting groups are cutting their predictions for where the official cash rate will peak from its current 4.25% level. On February 22 the Reserve Bank is now strongly expected to only raise the rate by 0.5% rather than the previously expected 0.75%.

The chances of more mortgage rate cuts have risen and we can start to talk about people pulling back now from their willing embrace of the worst case scenarios for borrowing costs. This won't bring a fresh wave of buyers back into the market anytime soon. But it will take away the prevailing negative influence which has encouraged buyers to go on strike. The chances of the market bottoming out by mid-year have risen. But this does not mean any firm sort of a recovery is in the offing. There are way too many uncertainties to be able to make any strong claims regarding the strength of the period after the decline has ended.

But it does mean I am willing to bring back my comment about the endgame for the housing market decline being underway. That position had to go into the dustbin for a while after the September quarter inflation number came in 0.6% higher than expected at 7.2% back on October 18.

If I were a borrower, what would I do?

As noted last week and warned about from over a year and a half ago, with the mortgage yield curve turning inverse and long rates lower than short rates for some lenders, I would not touch the five year rate with a bargepole. Or the four year rate. I'd probably not go anywhere near fixing three years – or two years.

Personally, if I were fixing in the near future I wouldn't look beyond one year with an expectation of riding easing monetary policy downward over 2024-25, but without any firm idea on when that easing will start and how much it will add up to.

From now on the Interest Rates section in Tview Premium will be larger than before to help the many people rolling onto higher fixed mortgage rates this year. As a one-off I have made this week's TVP available to all and you can access it here.

https://www.tonyalexander.nz/wp-content/uploads/Tview-Premium-2-February-2023.pdf

Anyone wanting to subscribe to TVP will find the necessary details in the email used for sending out this week's Tony's View.

Nothing I write here or anywhere else in this publication is intended to be personal advice.

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