ECONOMIC UPDATE

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WEEK ENDING 18 NOVEMBER 2022

Key points

- **The Q3 wages growth number was strong, as was the October jobs number;**
- **Neither of those outcomes is a major surprise given the current state of the economy;**
- **The RBA is on track to deliver another quarter percentage point rate hike in December;**
- **After a pause in January, the RBA is likely to deliver two more quarter percentage point hikes in H1 2023, taking the cash rate to 3.6%.**

Wages

For the first time in years a wages number came in higher than expected. The 'surprise' though wasn't much of a surprise given the strength of the jobs market and inflation. In one respect the bigger surprise was that wages growth hasn't been higher earlier. The headline wages number is now around the 3% mark that the RBA had been looking to achieve.

The headline number understates the strength of wages growth. Private-sector wages growth (more sensitive to changes in the economy) is stronger than that for public-sector wages. Wages growth once bonuses are added are now over 4% in the private sector. The proportion of workers that have had to wait less than a year for a pay rise is higher now than in pre-pandemic times.

Wages growth has risen strongly across almost all sectors of the economy over the past year. It is now above 3% in around two-thirds of industries, and above 3.5% in five. The recent pay rise granted in the national wage case played a role in stronger wages growth. Pay rises for workers on individual agreements played a bigger role.

The jobs market is likely to remain strong for at least another year. We are likely close to the peak of inflation although most forecasters don't expect the CPI to go below 3% until at least sometime in 2024. Public-sector wage growth will likely be stronger. This suggests that aggregate wages growth has further to rise.

A further strengthening of wages growth should not be a concern. We are near the cyclical peak in inflation, and the jobs market strength is likely to peak around the middle of next year. This means that wages growth should moderate over the course of 2024 if the RBA (and other forecasters) are right in their view that the unemployment rate will rise and inflation rate will decline.

Employment

The October jobs number highlighted the ongoing strength of the jobs market. Monthly jobs growth was around 17,000, full-time employment grew by 47,000. The unemployment rate declined to 3.4%, the participation rate remained high. The jobs market (using the underutilisation rate as the guide) is particularly tight in NSW, Victoria, and Western Australia.

Strong growth of full-time employment was one of the reasons behind the sharp jump in hours worked in the month. But there were also less workers taking holidays. Sick leave is still higher than pre-pandemic times although down from the levels of this winter. The bad weather of recent weeks was a factor that holding down hours worked.

A strong jobs market should continue to be expected in coming months. The number of job ads remains high, and surveys indicate that employers are still eager to hire. A lack of workers is the number one problem currently facing business. Households have little fear about unemployment.

The jobs market lags changes in the economy by 1-2 quarters. So even if the economy does slow in the next month or two, we should not expect to see that be reflected in the jobs market until at least well into H1 of next year. Any rise in the unemployment rate is likely to take longer given the current big number of unfilled jobs. And many employers are unlikely to make swinging jobs cuts any time soon given that they have spent much of the past year desperately looking for workers.

Rates view

Consumer confidence is weak and business confidence is declining (although firms still think business conditions are good). Some households are already being impacted by the high cost of living. And in coming months more households will struggle with the high level of interest rates and negative real wages growth. Firms unable to pass on cost rises are finding the going tougher. Global economic growth forecasts continue to be revised down.

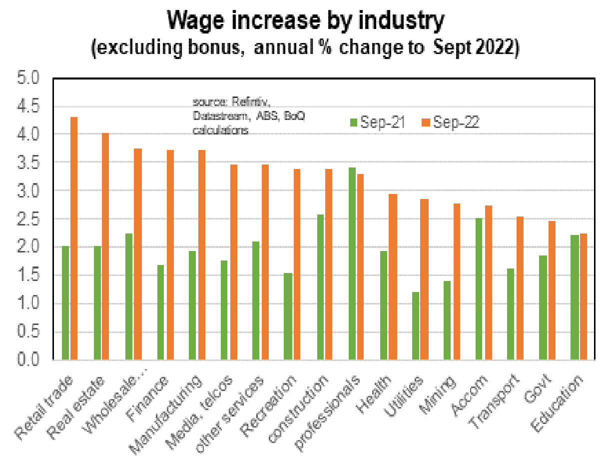
Inflation has yet to peak. Underlying inflation is not forecast to re-enter the RBA's 2-3% target band until 2025. Wages growth is heading higher, the labour market is strong and the economy in aggregate is doing well. The cash rate in developed economies is still going north.

Before the release of the wages and jobs data there was talk of a possible pause in cash rate hikes. The wages and jobs data made it is very likely that another quarter percentage point rate hike is on the way in December. The RBA can then sit back until February to gauge how the economy is coping. If the wider economy has not shown clear signs of slowing by then (as I suspect) then there will be another quarter percent point rate increase in February (my forecast).

The RBA might then want to take another break to gauge how the economy is faring. It is for this reason I expect a final quarter percentage point rate hike to be in April/May. Thereafter there should be clear signs that the economy has slowed, and inflation is heading back towards the RBA's 2-3% target.

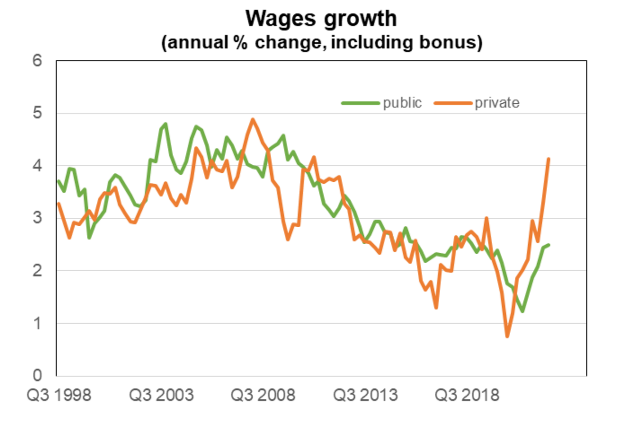
Wages growth is now around the level consistent with RBA's inflation target.

There has been significant growth in wages across most sectors of the economy over the past year.



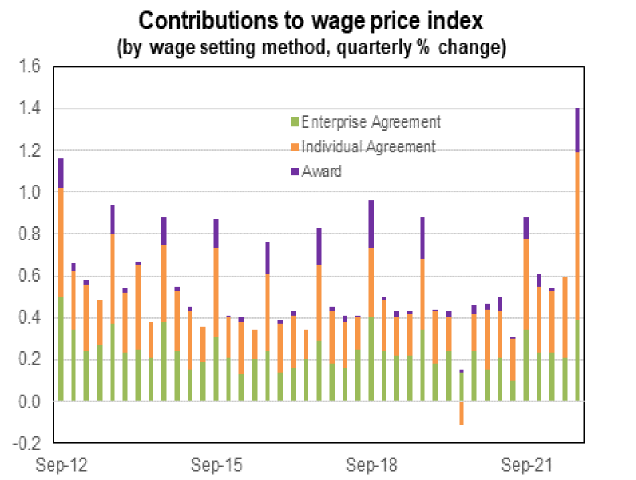
Private-sector wages growth is comfortably above that of the public sector.

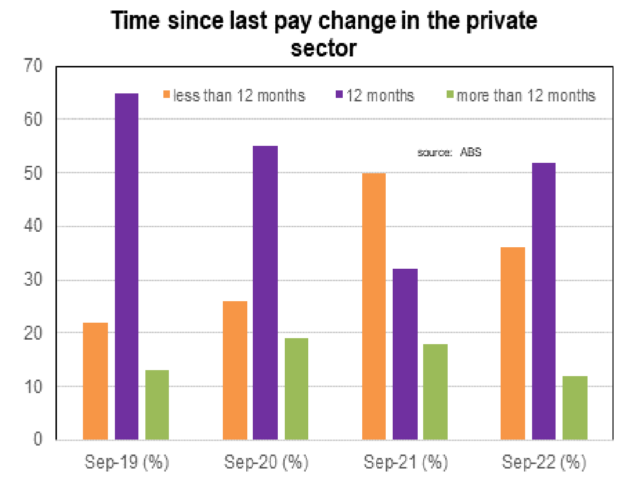
Once bonuses are included, private-sector wages growth is now above 4%.



Most of the rise in wages growth was down to those on individual agreements.

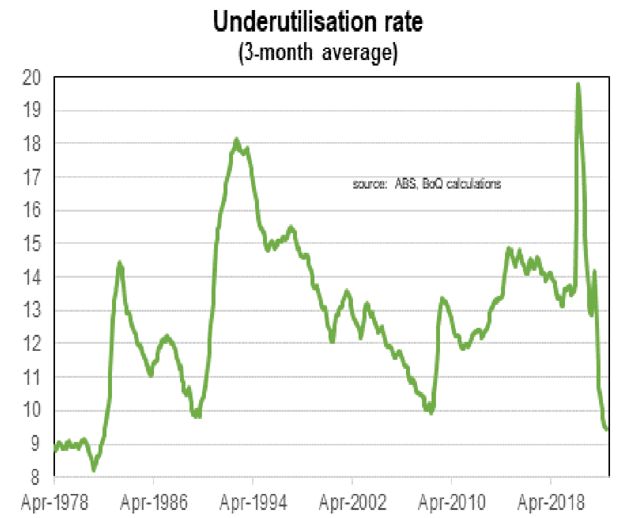
There are currently more regular wage reviews than there were in pre-pandemic times.

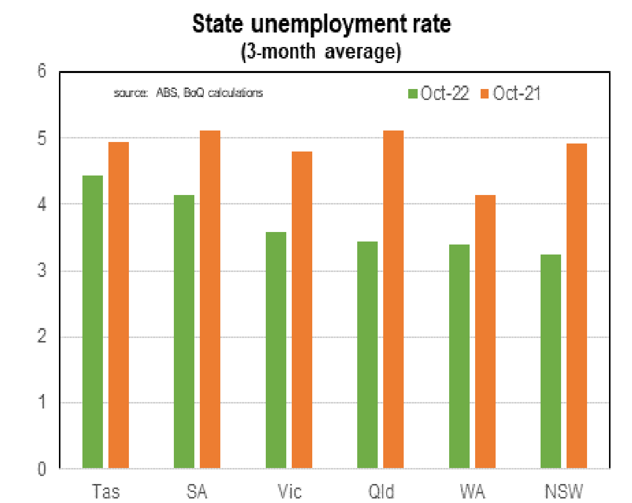




The labour market is very strong.

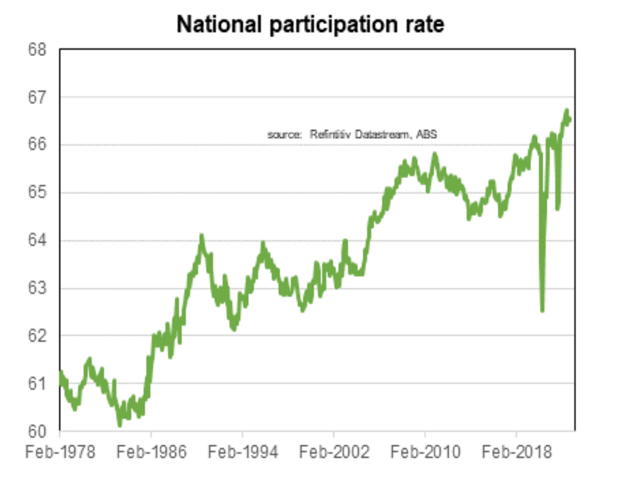
Then unemployment rate has declined significantly across all states over the past year.

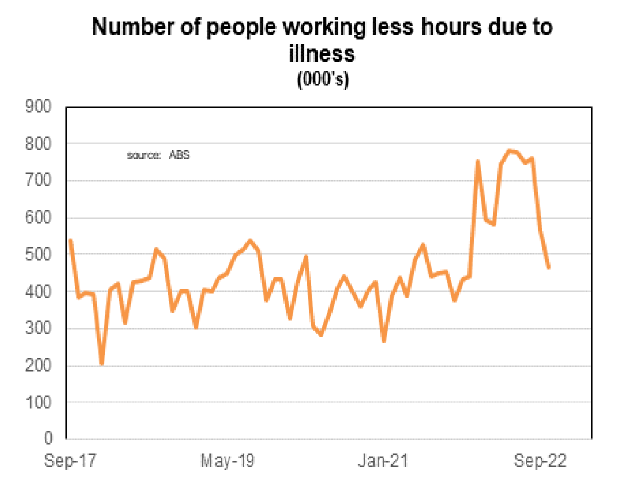




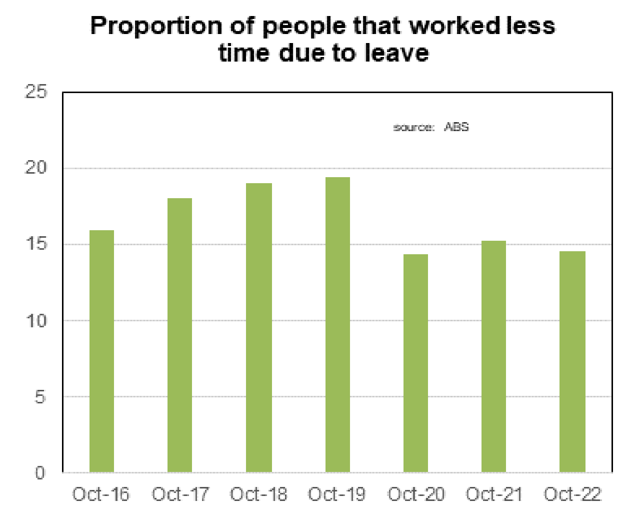
The participation rate remains near a record high.

Less people are away sick than during winter.

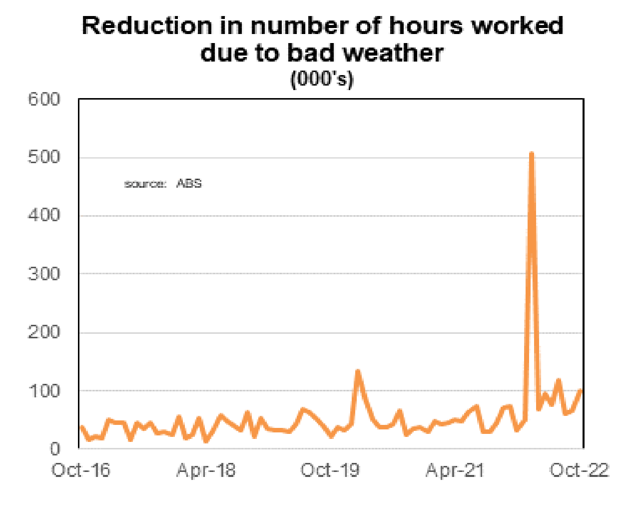




And less people were taking leave.



Bad weather continues to be a problem.



We live in interesting times.

Regards

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