The shift in timing of the interest rate rise brings forward the slowdown in economic growth we expect to flow from policy moving to a restrictive level. But inflation and wages growth will likely prove to be sticky. Consequently, we think the RBA's willingness to act pre-emptively in response to the economic slowdown will be limited. As a result, we don't see a modest easing cycle getting under way until around mid-2024, with a total of 50bp of cuts by the end of that year.

Unemployment to fall to a low of 2.9% in Q1 2023

Since February, we have forecast the unemployment rate to decline to the low 3s by the end of the year. But the combination of the sharp drop to 3.5% in June and the job vacancy rate escalating to a record 3.4% in Q2 suggests the labour market will get even tighter than that. We now expect unemployment to fall below 3% by early next year.

We also expect underemployment to continue to trend downwards this year and the participation rate to set more records, getting to 67.1% by Q1 2023. The upward trend in participation seems largely driven by pull factors, such as it being easier to find a job in a strong labour market and more flexible/remote arrangements reducing barriers to employment.

Figure 2. The job vacancy rate will take time to come back down

Source: ABS, Macrobond, ANZ Research

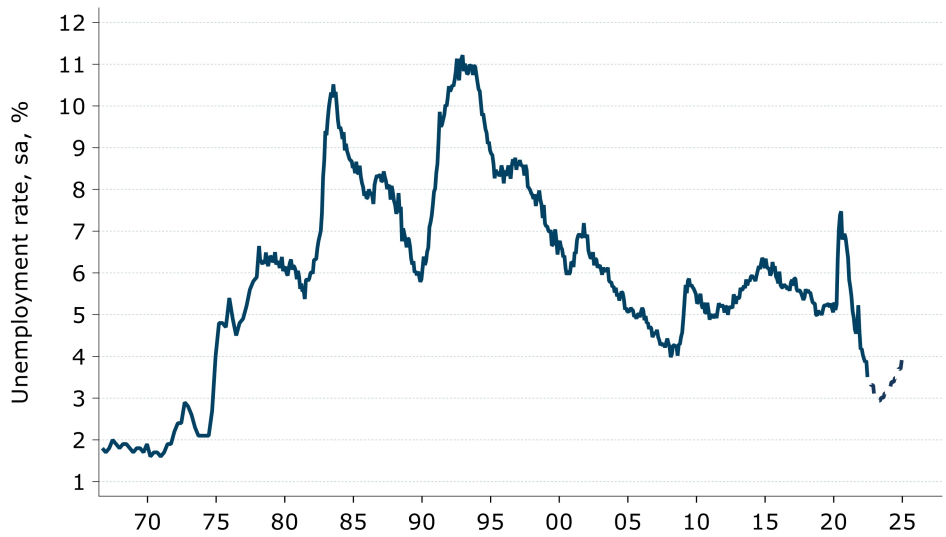
The 480,000 job vacancies across the economy represent a substantial gap between labour supply and demand, which is evident across industries and geographies. Consequently, as higher inflation and rising rates curtail demand growth, it will take time for this gap to close enough to put upward pressure on unemployment.

Newly arrived skilled migrants, temporary visa holders, students and backpackers are adding to the supply of workers, but also add to already strong demand. So, while the return of migration improves labour mobility and matching, it doesn't mean the gap between demand and supply is going to close quickly.

But with the economy tracking below trend by late-2023 and slowing further in 2024, we expect the labour market to start easing gradually later in 2023. A sharper slowdown in employment growth in 2024 will see a faster rise in unemployment, reaching around 4% by end-2024.

While a 4% unemployment rate is still very low relative to the past several decades, the change is important. A 1ppt rise means more people will lose their jobs and struggle to find another quickly. This will add to the case for the RBA to cut rates.

Figure 3. Unemployment to drop into the 2s by early-2023



Source: ABS, RBA, Macrobond, ANZ Research

Wage price index to accelerate to 3.3% y/y by end-2022

The Wage Price Index (WPI) should accelerate sharply in H2 2022, and our forecast of 3.3% y/y by the end of the year is unchanged. Minimum and award wages have increased by 5.2% and 4.6% respectively, and labour underutilisation is at a 40-year low. Job mobility has risen sharply, inflation expectations are up and businesses are reporting passing on larger wage increases.

On a quarterly basis, we expect real wage growth[1] to turn positive from Q1 2023. But it could take years for real wages to get back to their early-2021 peak.

Average earnings per hour rose 5.2% y/y in Q1, tracking well above the WPI's 2.4% y/y, and will accelerate further. This measure reflects compositional changes in the labour market, such as promotions and the rising share of workers in higher paying occupations. When considering the effect on individual and aggregate household income growth, and the ability of households to manage higher prices and rates, this measure is arguably more important than the WPI.

Figure 4. Nominal wage growth to reach a decade-high

Source: ABS, Macrobond, ANZ Research

1. Deflating the WPI using trimmed mean inflation