HSBC Global Research

Economics
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Australia's unemployment rate falls

Expect a rate hike before year-end

The Australian unemployment rate fell to 5.8% in March (market had 6.1%) to be at its lowest level since November last year. Employment rose by a solid +18k jobs in the month (market had +2k jobs) and the participation rate declined to 64.7%. The main message from these data is that the labour market is stabilising and the unemployment rate may now have passed its peak. With growth rebalancing and domestic demand lifting, firms are boosting their hiring, albeit with a (typical) lag behind the lift in activity. We continue to expect that the RBA's next move is likely to be up and that it may arrive before the end of the year.

Facts

- Employment increased by +18k jobs (market had +2k jobs, HSBC had +10k) to be +1.1% higher y-o-y.

- The unemployment rate fell to 5.8%, which is its lowest level since November 2013 (market had 6.1%; HSBC had 6.0%).

- The participation rate fell to 64.7%.

Implications

Australia's employment numbers showed increasingly convincing signs that the labour market is improving. This improvement was clearest in the March unemployment rate, which fell to its lowest level since last November, of 5.8%. It appears that the lift in activity indicators, such as retail sales, housing approvals and business sentiment, is now feeding through to a pick-up in employment and some stabilisation of the unemployment rate.

Indeed, the improvement in the labour market is occurring in line with the typical lag that occurs between a lift in activity and an increase in hiring. History shows that it typically takes 2-4 quarters for the labour market to improve after a pick-up in activity and, in our view, the economy passed a turning point in September of last year (two quarters ago).

If these trends in the labour market continue, as we expect they will, the RBA may soon have little motivation to leave its cash rate at its current historical low of 2.50%. With activity lifting, the housing market continuing to boom and the labour market now seemingly past its trough, the RBA may soon need to consider shifting to a tightening bias, in preparation for lifting interest rates back towards neutral.

So far, the RBA's willingness to remain comfortable with the current very low interest rate setting, despite inflation already being passed its trough (2.6% y-o-y), has been because they expected that a weak labour market and low wages growth would put downward pressure on inflation in the future. But, if the labour market tightens from here, this source of disinflation may be less powerful than the RBA had been anticipating.

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However, the RBA may face another challenge. The recent improvement in local economic conditions has also seen the AUD rally back to around US94 cents, despite recent weaker conditions in China. If the AUD were to appreciate further, this could put downward pressure on inflation and the delay the need for the RBA to lift interest rates.

Bottom line

The labour market is improving, with the unemployment rate falling to 5.8%, and now likely to be passed its peak.

Combined with a lift in activity, and inflation that is already in the upper half of the RBA's target band, we see the RBA as likely to start considering that rates may need to head back towards neutral fairly soon.

We continue to expect the RBA to lift its cash rate before the end of the year.

Disclosure appendix

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