BULLETIN

30 November 2023

Deeper insights on Australian wages
An upside surprise was prevented by seasonal reanalysis

- The Wage Price Index (WPI) index lifted 1.3% in the September quarter just as Westpac and the market had expected. There was the boost from the minimum wage (showing up in award wages) as well as CPI Indexation (in enterprise agreements) but the pace of growth from individual wage bargaining appears to have peaked.
- While the September rise was on expectations, the annual pace came in at 4.0%yr, a bit stronger than the 3.9%yr forecast. This was due to seasonal reanalysis which boosted the quarterly increases in Q1 and Q2, offset by a stronger seasonal factor in Q3 which limited the rise in the quarter to 1.3% – if we use the previous seasonal factors, the increase in September would have been 1.5%.
- Holding to our current original (not seasonally adjusted) estimates for the next two quarters, our seasonally adjusted estimates lift 0.1ppt to 0.9%qtr for both December 2023 and March 2024, as a result of the seasonal factors. We are now forecasting an annual pace of 4.1%yr at December 2023 and March 2024 compared to our previous forecast of 3.8%yr for both quarters.
- While there was an upside surprise in the original data, it appears wages bargained via Individual Arrangements may have peaked. Our back of the envelope estimates suggests that Enterprise Agreement wages lifted 2.2% compared to 1.1% in September 2022, Award/Minimum wages lifted 4.2% compared to 2.9% in September 2022 while Individual Arrangements wages lifted 1.3%, a touch softer than 1.4% in September 2022. As the data is not seasonally adjusted, we compare the quarterly change to the quarter a year earlier for some guidance on relative wage outcomes.
- While Award wages rose more than we had anticipated, 4.2%qtr vs. 3.4%qtr forecast, we don't see this rolling into a greater than expected outcome in the December quarter as unlike the 2021 and 2022 decisions, the increase were not spread over a number of quarters. So, we expect to see something more in line with pre-COVID outcomes of around 0.2%.
- Enterprise bargaining has already tipped over. Fortnightly agreements data from the Fair Work Commission reported a low in wage increases of 3.1% in mid-July which lifted to a peak of 4.8% in early September before easing back to an average of 3.5% in the four weeks to October 20th. It appears that any boost from the minimum wage to Enterprise Bargaining has been limited and very short lived.
- The rise in underemployment is pointing to a late 2023 peak in wage inflation. The cycle low for underemployment was 6.0% in the September and December quarters of 2022, lifting to 6.3% in the June quarter to then hold around 6.4% in the September and December quarters. This suggests annual wage inflation should peak in the December quarter before moderating through 2024.
- A number of leading wage indicators, including the NAB Labour Cost series and the Seek Asking Salary Index, have seen a moderation, and while wage expectations in the Melbourne Institute surveys are yet to moderate, it remains modest relative to pre-COVID surveys.

Various measures from the Wage Price Index*

% change	Dec-22	Mar-23	Jun-23	Sep-23
WPI %qtr	0.85	0.91	0.90	1.30
WPI %yr	3.3	3.6	3.6	4.0
Private WPI %yr	3.6	3.8	3.9	4.2
Public WPI %yr	2.5	2.9	3.1	3.5
Private WPI inc. bonuses %yr#	3.8	4.1	3.8	4.3
WA – fastest state/region %yr#	2.2	2.7	3.3	3.6
NT – slowest state/region %yr#	1.9	2.0	2.4	2.6
Arts & recreation – fastest ind. %yr#	4.2	4.4	4.2	3.7
Public admin – slowest ind. %yr#	2.5	2.9	2.8	3.4

* Total pay excluding bonuses, seasonally adjusted.
# Seasonally adjusted by Westpac.
Sources: ABS 6345.0

State Wage Price Index*

% change	Dec-22	Mar-23	Jun-23	Sep-23
NSW %qtr	0.9	0.8	0.7	1.4
NSW %yr	2.4	2.6	3.1	3.3
Victoria %qtr	0.8	0.8	0.9	1.0
Victoria %yr	2.3	2.6	3.1	3.3
Queensland %qtr	0.8	0.9	0.9	2.0
Queensland %yr	2.5	2.9	3.4	3.4
SA %qtr	0.9	0.9	1.0	1.1
SA %yr	2.2	2.3	3.3	3.5
WA %qtr	0.9	1.1	1.0	1.4
WA %yr	2.2	2.7	3.3	3.6
Tasmania %qtr	0.9	1.1	0.7	1.7
Tasmania %yr	2.7	2.9	3.6	3.6

* Total pay excluding bonuses, seasonally adjusted.
Sources: ABS 6345.0

Forecast Wage Price Index*

% change	Dec-23	Mar-24	Jun-24	Sep-24
WPI %qtr	0.9	0.9	0.8	0.8
WPI %yr	4.1	4.1	4.0	3.5
WPI six month ann. %yr	4.6	3.7	3.4	3.2
Private WPI %yr	4.2	4.1	4.0	3.5
Public WPI %yr	3.7	3.7	3.7	3.4

* Total pay excluding bonuses, seasonally adjusted.
Sources: ABS 6345.0

Seasonal reanalysis had a significant impact the outcome

The 1.3% rise in September was on expectations, both for Westpac and the market median, but the annual pace came in at 4.0%, a bit stronger than the 3.9% forecast. This upward revision was due to seasonal reanalysis which lowered the 2022 Q3 estimate from 1.1%qtr to 0.9%qtr but boosted the quarterly increases in 2023 Q1 and Q2 to 0.9%qtr from the original 0.8%qtr. It is the upgrading of two quarters by 0.1ppt, compared to one quarter being downgraded by 0.1%, that explains why the annual pace was stronger than expected even though the quarterly print was on expectations.

Normally, we would not make much of changes to seasonal factors but this time, such changes have had an impact our forecasts. Given the extreme seasonality in wages – Q3 being the start of the Australian financial year wherein a large majority of workers get a pay rise – we build up our forecasts based on original estimates for both private and public sector wages, using enterprise bargaining and minimum wage/awards increases as well as our judgement on individual wage bargaining outcomes. We then seasonally adjust this estimate with existing seasonal factors. As such, we can note that the original, not seasonally adjusted, increase for the September quarter WPI was 1.9%, quite a bit stronger than our forecast of 1.7%. Had the ABS used historical seasonal factors they would have reported a 1.5% rise in the September quarter, 0.2ppt greater than the reported 1.3% increase.

Holding our quarterly profile, in original terms, for the next two quarters at 0.8%qtr, our seasonally adjusted estimates have lifted to 0.9%qtr for each quarter. Along with the stronger than expected outcome in September for annual wage inflation (4.0%yr vs. 3.9%yr forecast), the 0.1ppt added to each of the next two quarters mean we are now forecasting an annual pace of 4.1% at December 2023 and March 2024. Our previous forecasts were 3.8%yr for both quarters.

The RBA's forecast for December 2023 and June 2024 is 4.0%yr.

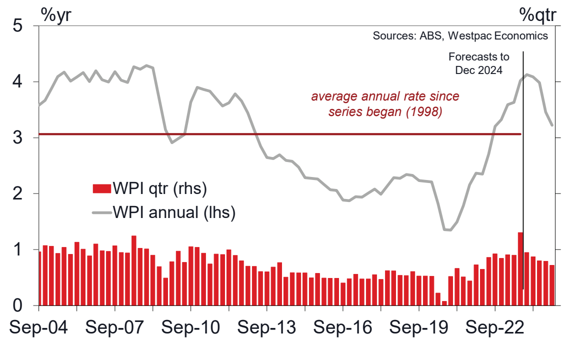
Given the stronger than expect print in original terms, why are we not boosting our near term forecasts more?

The detailed data suggested that the upside surprise in the original series was due to stronger than expected outcomes from Enterprise Agreements and Awards, while the most dynamic wages bargaining sector, Individual Arrangements, was not as strong as we had expected. The ABS provides, in original (not seasonally adjusted) terms, the contributions to the quarterly increase in the Wage Price Index from Awards/Minimum Wage, Enterprise Agreements and Individual Arrangements. Our back of the envelope estimates suggest that Enterprise Agreement wages lifted 2.2% compared to 1.1% in September 2022, Award/Minimum wages lifted 4.2% compared to 2.9% in September 2022 while Individual Arrangements wages lifted 1.3%, a touch softer than 1.4% in September 2022. As the data is not seasonally adjusted we compare the quarterly change to the quarter a year earlier for some guidance on relative wage outcomes.

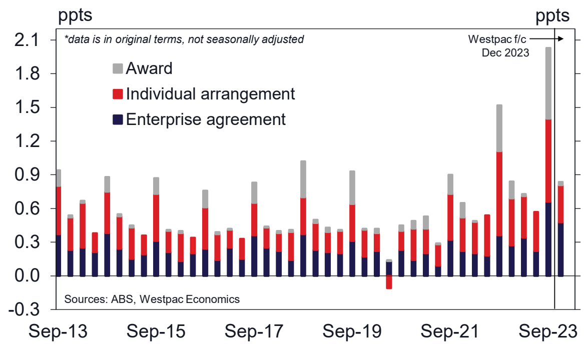
In both 2021 and 2022, the increase in the Minimum/Award wage was spread over a number of quarters while in 2023 the increase was to be applied to all relevant jobs from the 1st of July. So while Award wages rose more than we had anticipated, 4.2%qtr vs. 3.4%qtr forecast, we don't see this rolling into a greater than expected outcome in the December and therefore are looking for a very modest 0.2% increase, down from the 1.1% reported in December 2022 but a touch stronger than the pre-COVID print in December 2019 of 0.1%.

Enterprise Agreement wages lifted 2.2%qtr, significantly stronger than our 1.2%qtr forecast due to just stronger new agreements but also adjustments to current agreements linked to the increase in the Minimum/Award wages and/or indexation to the CPI. We are not expecting this to be repeated in the December quarter. In fact, the Fair Work Commission Agreement data base suggests the average annual wage increase for new agreements peaked in late August at 4.7%yr and has since eased back to around 3.6%yr in October. Our forecast is for a softer 1.6% increase in the December quarter but note it is still quite a bit stronger than the 0.8% increase in December 2022.

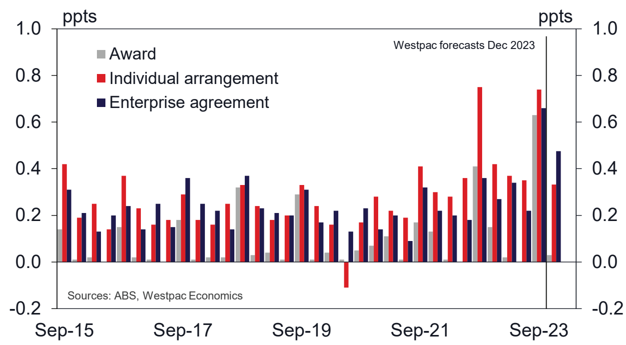
Wage inflation peaks in late 2023



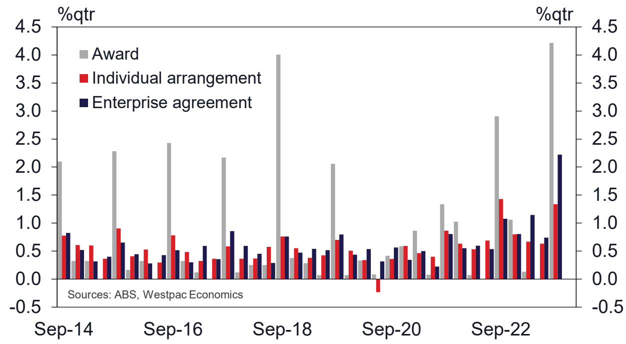
Wage inflation contributions



Contributions by bargaining arrangement



Wage rise by bargaining arrangement



Past performance is not a reliable indicator of future performance. The forecasts given above are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The results ultimately achieved may differ substantially from these forecasts.

As noted earlier, Individual Arrangements wages lifted 1.3%qtr which was a touch softer than 1.4%qtr in September 2022. We had expected that rising Award/Minimum wages may also be putting pressure on wages in this bargaining arrangement and thus forecast a 1.5% increase. We believe this moderation will continue into the December quarter with a 0.6% increase forecast compared to the 0.8% increase back in December 2022.

It is also important to note that in the September quarter, 49% of private sector jobs surveyed reported a wage increase, the largest share getting a pay increase in any quarter in the data back to 2010. Given so many had a pay rise this quarter we would expec that there will be less workers getting a pay rise in December 2023 than the 21% that did get a wage increase back in December 2022. As such, even if those getting an wage increase this December can match the 5.8% wage increase seen in the September quarter given a much smaller share will be getting that increase the average rise for all wokers will be significantly less that it was in the September quarter.

As noted above: ABS estimates of pay setting arrangement contributions to the WPI are NOT seasonally adjusted.

Bonuses boosted wages in the quarter but through the year the pace has levelled out

Businesses have increasingly made use of variable compensation during the current period of very tight labour markets to limit how much of a wage increase they permanently lock in. The WPI including bonuses lifted 2.0% in the quarter (the largest quarterly rise reported in the series), boosting the annual pace from 3.7%yr to 4.1%yr. Compare that to the 1.5%qtr increase in September 2022 as well as the 1.3% increase in wages excluding bonuses, suggesting that firms are still under pressure to lift compensation and they are using bonuses as part of the package, leaving some flexibility to adjust compensation should the labour market ease. Private sector WPI including bonuses accelerated from 3.8%yr to 4.3%yr; the fastest reported pace in this series was 4.9%yr back in March 2008 at the height of the mining boom. In the year to September, private sector wages excluding bonuses also rose 4.2%yr, suggesting we have seen some catch up in base wages compared to total remuneration.

Note these figures were seasonally adjusted by Westpac.

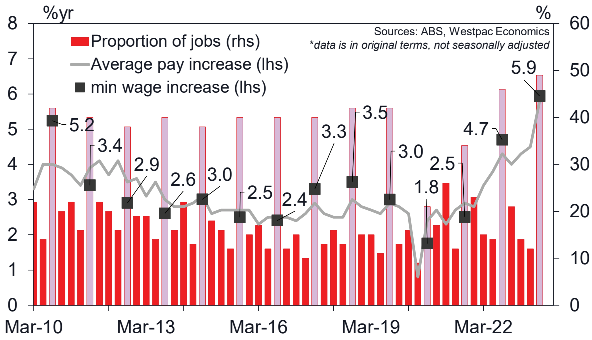
Enterprise Bargaining has already tipped over

In the June quarter, new Enterprise Bargaining Agreements (from the Department of Employment & Workplace Relations) reported an average annualised wage increase (AAWI) of 3.8%, the largest pay rise from this bargaining stream since March 2012 (4.1%). This data is very slow to be updated but we now get fortnightly approved agreements from the Fair Work Commission. From a low of 3.1% in mid July reported AAWI lifted to a peak of 4.8% in early September before easing back to an average of 3.5% in the four weeks to October 20th. If this holds, then any flow on from the out-sized gain in the minimum wage to Enterprise Bargaining has been limited and very short lived.

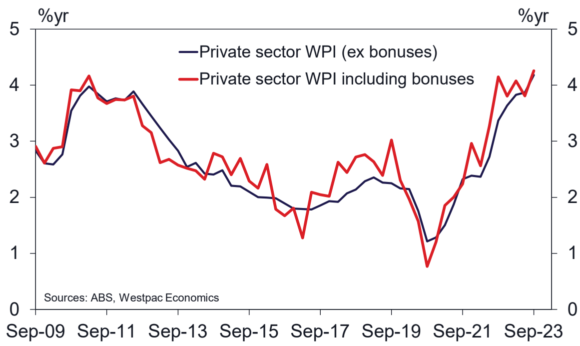
Australia's labour market has three separate, but interlinked, bargaining streams

As the Australian labour market was deregulated/decentralised, three wage barging streams emerged. The first was the residual of the original **Awards System** where wages were set at a national, or state, level defining employment conditions for specific jobs. It was complex and slow to change so a reformation was started in the 80s under the Hawke/Keating government that accelerated under the following Howard government. Now, awards are a much smaller share of employment contracts and mostly defined by the minimum wage outcome that is decided by the Fair Work Commission each year. We estimate those on Awards/Minimum Wages represent 15% if the Wage Price Index (WPI).

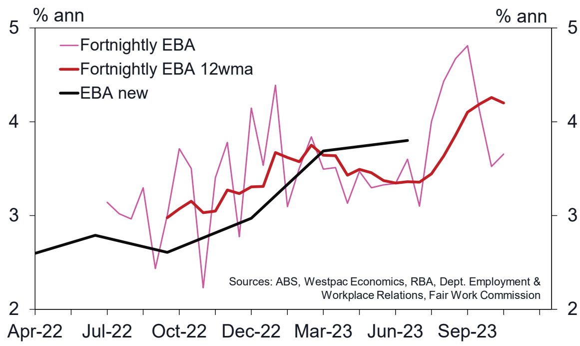
Private sector wage increase paid



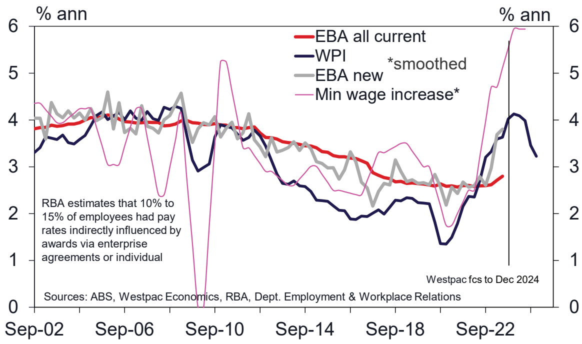
Wages plus bonuses



Enterprise bargaining wages tip over



Wages growth by bargaining sector



The second is the collective bargaining stream that evolved under the Hawke/Keating administration – **Enterprise Agreements**. They are negotiated at the workplace level, mostly with union involvement but there are some with non union agreements, and have a duration of between one to three years. We estimate the Enterprise Bargaining represent around 30% of the WPI.

The final group is the **Individual Arrangements** stream. These are employment contracts done on a individual basis and can be under formal Fair Work Commission agreements or the informal common law contracts (often used in business services/financial services sectors). But it is important to note that these contracts have to at least match the minimum wage, or relevant award wages. No one can be paid less than the minimum or the award wage for that job. This sector has grown under the reforms implemented by the Howard/ Costello administration and now represent around 55% of the WPI.

Underemployment is pointing to a late 2023 peak in wage inflation

The Phillips curve, where wage inflation is compared to unemployment, is the most common way to get a measure on how labour market conditions are impacting wage bargaining outcomes. However, Westpac's research suggests underemployment has far more explanatory power than unemployment or even underutilisation (which combines unemployment and underemployment). Using a simple exponential linear trend where the labour market indicator is lagged two quarter, the R^2 for unemployment is just 0.19 while for underemployment it is 0.75. For underutilisation it is 0.66, better than unemployment but still not as good as underemployment.

Taking quarterly averages – the WPI is a quarterly survey while the Labour Force is a monthly survey – the cycle low for underemployment was 6.0% in the September and December quarters of 2022. It since lifted to 6.3% in the June quarter and has held around 6.4% in the September and December quarters. Observing that underemployment leads annual wage inflation with a two quarter lag, this suggest annual wage inflation is set to peak in the December quarter before moderating through 2024 as underemployment continues to rise in a softening labour market.

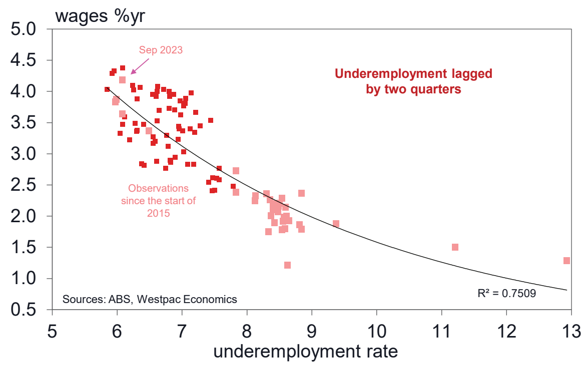
Other leading indicators also suggest a peak in wage inflation

There are also a number of alternative leading indicators that also suggest that wage inflation may be nearing a peak. The Labour Cost series from NAB's business survey peaked in the March quarter this year and has moderated steadily since.

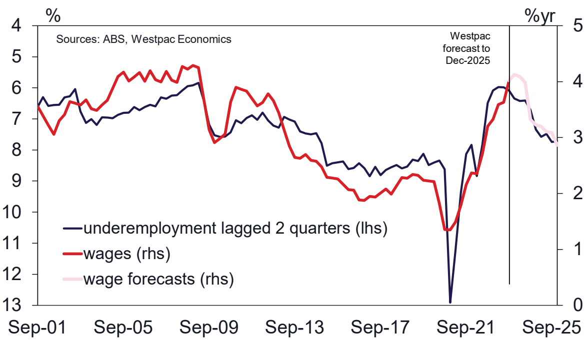
From the Melbourne Institute Survey of Wages, expected wage increases have lifted significantly from the COVID low and are now stronger than pre-COVID levels. But it is worth noting that in the chart over, it does appear that wage expectation are coincident with, if not slightly lagging, actual wage outcomes as reported by the WPI. There is a similar story for those reporting an actual wage increase. However, the share of those expecting a wage increase has lifted to 45%, on par with the pre-COVID levels peak in 2018 but still significantly less than the 62% that were expecting a wage increase in March-June 2014.

We have also seen a moderation in the Seek Asking Salary Index. Through most of 2023 the Index has held a 4.8%yr pace but moving into the December quarter the pace slowed to around a 4.2%yr.

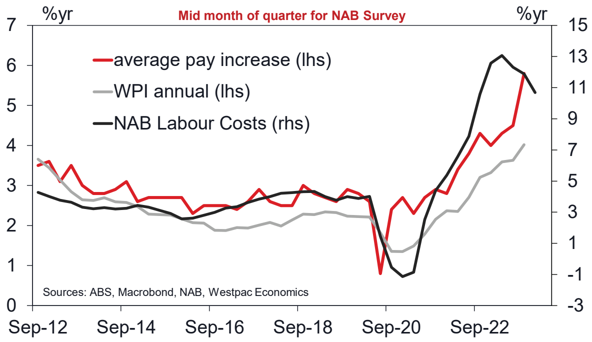
Underemployment & private wages



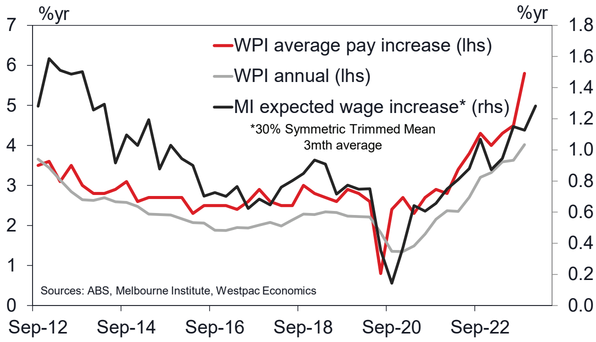
Underemployment & wages



Labour costs ease in business surveys



Av. pay increase vs. expected wage increase



Wage inflation moderates in 2024 in all three bargaining streams

Westpac WPI forecasts for 2024 have wage inflation moderating from a peak of 4.1%yr at December 2023 to 3.2%yr in December 2024. As noted above, our wage forecast is based on a projected softer labour market as identified by rising underemployment. We expect this to be reflected as a moderation in wage inflation from all three of the wage bargaining streams and while it is possible that the minimum wage increase in 2024 could be larger than usual, we are expecting it to be smaller than it was in 2023. When combined with the new seasonal factors, the more modest increase in original terms next September underpins our forecast for a more modest 0.9%qtr gain in seasonally adjusted terms.

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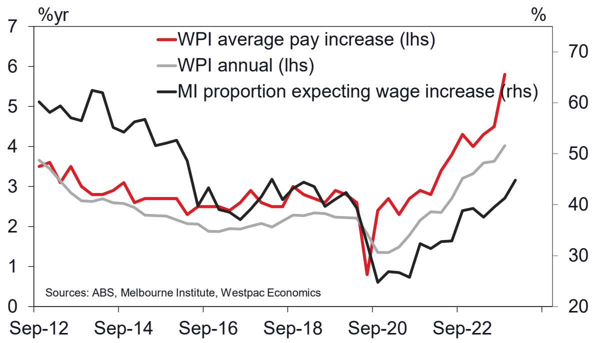
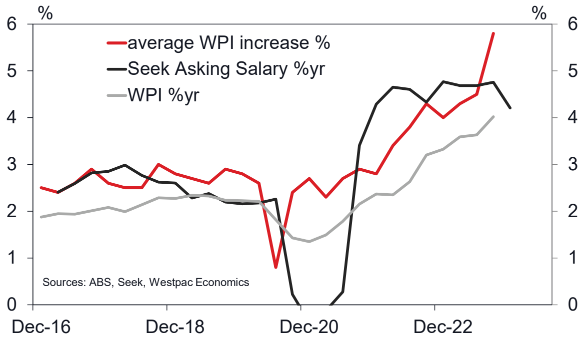
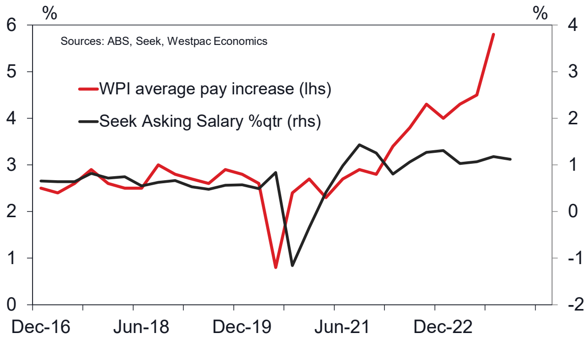
Ave pay increase vs expected pay increase



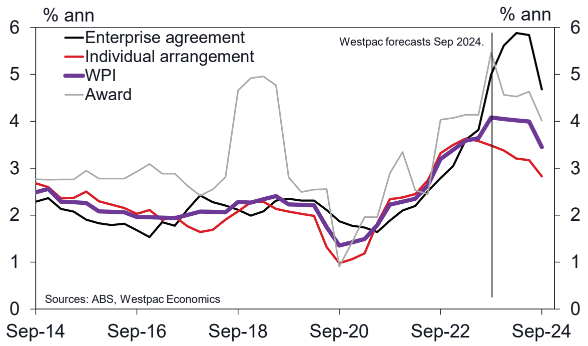
Ave pay increase vs annual renumeration



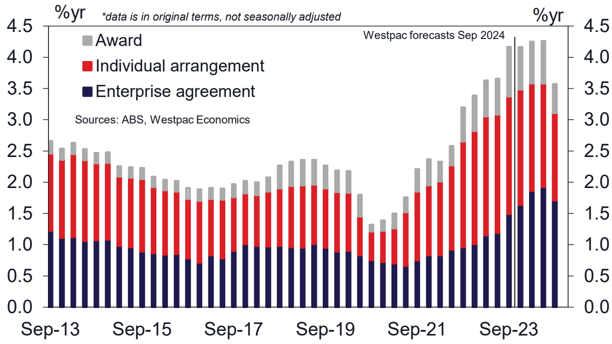
Ave pay increase in the quarter



Wage growth by bargaining method



Wage inflation contributions



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