13 September 2021

US Labour Market Monitor

Weak jobs report - noise or a signal of something else?

One of the main topics for the rest of the year is the development in the US labour market. Despite GDP is now above the pre-covid peak (although still below the old GDP trend path), employment remains more than 5 million below its peak in February 2020. The reason why the labour market is a major theme is that the labour market is vital for the Federal Reserve's decision on when to start normalising monetary policy.

Jobs growth disappointed in August, as employment only grew by 235,000. The big question is whether the disappointing jobs report is just noise or a signal that the economy is slowing faster than anticipated amid a big delta outbreak across the country. It could also be a sign that there are supply issues in the US labour market.

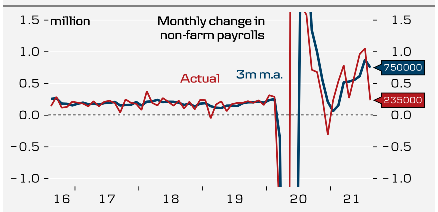
Noise: It is important to recognise the volatile nature of US jobs reports, which by the end of the day are based on surveys. So if one month was strong, it is not a big surprise if the next one disappoints, making the average more in line with underlying jobs growth. Therefore, it is usually better to look at the 3-month average jobs growth. Doing so we find that 3M average monthly jobs growth was 750,000.

Slower demand: Supporting the hypothesis that the weak jobs report is due to slower demand is the fact that employment growth in "Leisure & Hospitality" was in line with what we see in a "normal year". Employment in "food services and drinking places" moved sideways, which is in line with the fact that restaurant bookings moved sideways, probably related partly to delta fears. Other indicators like the employment subcomponent of US PMI have also indicated slower jobs growth. If delta is indeed to blame, we may soon see a small rebound, as delta seems to ease in the US (but may get worse again later in the autumn).

Supply side problems: There are plenty of signs that there are supply side problems in the US labour market. Labour demand is extremely high (both measured by number of job openings and hiring plans) and Americans think it is easy to find a job. At the same time businesses say that it is difficult to fill positions and there is a lack of qualified workers. Wage growth in the "Leisure & Hospitality" sector, where there are the most job openings, is extremely high in a historical perspective. Still, participation in the US labour market is low compared to the pre-covid levels.

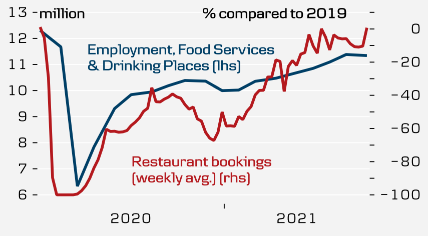
This may sound like a paradox but it is probably related to a couple of things: 1) We have seen a sharp increase in the number of job openings in the manufacturing sector, where jobs are usually more specialised, 2) mothers staying at home because of home-schooling (participation for women between 25-54 years fell more and is still further away from pre-COVID levels than men), 3) more people retired due to COVID-19 and 4) the incentive to work has been reduced by the temporarily higher unemployment benefits, which has been a drag on labour market participation (the extra benefits have now expired).

Noise? 3-month average jobs growth remains high



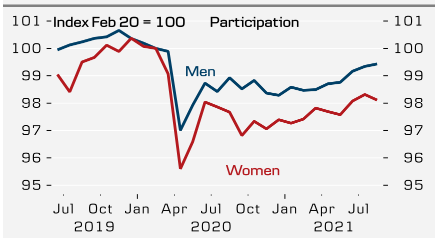
Sources: BLS, Macrobond Financial

Slower demand? Employment in "food services and drinking places" moved sideways, just like restaurant bookings



Sources: BLS, Open Table, Macrobond Financial

Supply side problems? More women have left the labour force, partly related to home schooling



Sources: BLS, Macrobond Financial

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The first problem is a difficult problem to fix, as it requires unemployed persons learning a certain skillset. If we are right that global manufacturing activity is peaking (as goods consumption normalises), this may ease some of the problems in the manufacturing sector, although it may take some time, as businesses still have a big backlog of orders.

The second problem may ease now that schools are starting to re-open in the US. Another wave when it gets colder is a risk, however.

The third problem is analysed by Dallas Fed, who estimates that 1.5 million more Americans than anticipated have retired in connection with COVID-19, see *blog post*. If they are not returning to the labour force, the labour market is tighter than just by looking at the absolute level of employment.

The fourth problem may ease as well now that the temporarily higher unemployment benefits have expired. This should make it easier to fill positions in "Leisure & Hospitality", where the required skillset is lower, hence supporting our view of stronger employment growth in coming months. It is important to recognise, however, that there are some evidence suggesting that we are yet to see a boost in Republican states, where the programmes ended earlier, see *CNBC*, so this is something we need to monitor. One reason may be that "reservation wages" (i.e. what is the lowest wage you are willing to work for) have risen, especially for people with less than a college degree, see *New York Fed*.

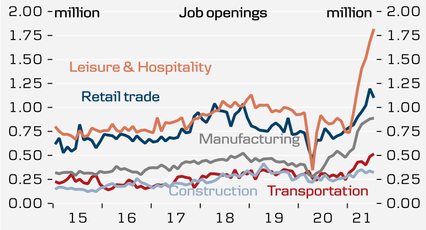
Overall, we expect stronger employment growth in coming months, now that the temporarily higher unemployment benefits have expired and the weak jobs report also partly was due to noise. This should ease some of the bottlenecks in "Leisure & hospitality". The lack of qualified workers in manufacturing is a harder problem to fix.

Fed is in a difficult position

Another question is of course what it means for the Fed. When the economy is hit by a negative demand shock, the Fed finds themselves in a benign situation, where it is appropriate to ease monetary policy looking at both the inflation and employment objectives. It is harder for the Fed when the economy is hit by a negative supply shock, which you could argue the current situation looks like (increasing price and wage pressure and bottlenecks). Higher inflation and wage pressure suggests monetary policy should tighten whereas weaker jobs growth and GDP growth suggest that monetary policy should ease. Based on Fed Chair Jerome Powell's speech at Jackson Hole, it is clear that the Fed looks more at the employment objective than the inflation objective at the moment, making it more likely that the Fed does not provide any new details on tapering at the upcoming meeting.

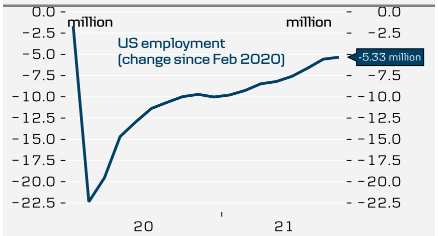
Given the Fed has already sent a strong signal that tapering is coming soon, we do not think the timing matters a lot. We think the tapering pace (3, 6, 9 or 12 months before QE buying ends?) is going to be much more important. We think there are good reasons to believe that the Fed will go with approximately six months. If it turns out that weak jobs growth is due to supply side problems and participation is permanently lower, we are closer to full employment than the Fed believes and it will be appropriate to start tightening monetary policy. If Americans return quickly back to work, we should see much stronger employment growth in coming months, also getting us closer to full employment. The same goes if the weak jobs growth was simply noise. The only situation where the Fed may postpone tightening is if it turns out that weak jobs growth reflects the impact of delta.

Supply side problems? Labour demand is high



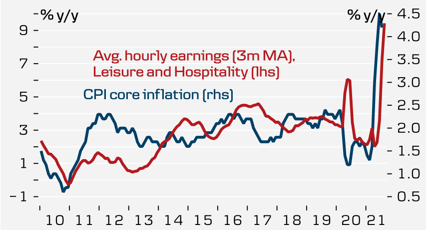
Sources: BLS, Macrobond Financial

Employment remains more than 5 million below the pre-covid level



Sources: BLS, Macrobond Financial

Higher inflation and wage growth pressure



Sources: BLS, Macrobond Financial

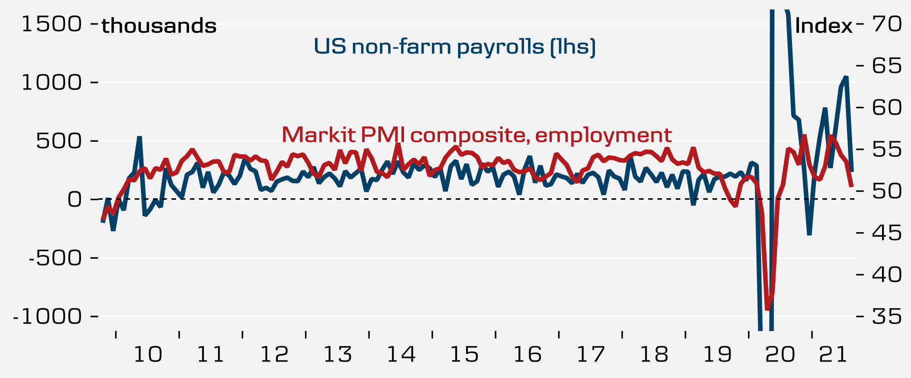
US labour market in one chart

Labour market strong but still slack left in the labour market – outward moves indicate stronger labour market

Note: the diagram shows the level of tightness of different US labour market key figures at different times, compared with the level of the same figures in December 2007 (index= 100) and December 2009 (index = 0). Counter-cyclical figures (jobless claims, marginally attached and working part time for economic reasons) are inverted; thus, the higher index (the further from the middle) the better (tighter) is the state of the labour market.
For JOLTS data we have used the average of the past two observations as the newest figures
Source: BLS (JOLTS), Atlanta Fed, Macrobond Financial

Models and leading indicators

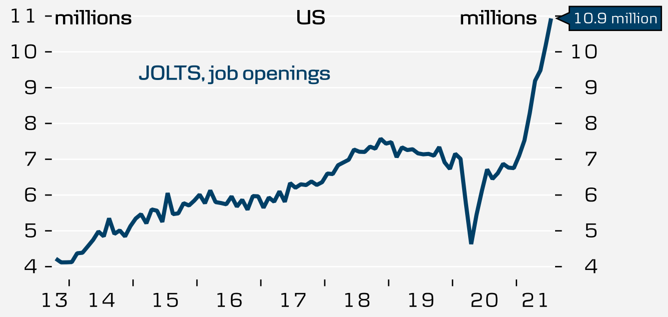
PMI composite employment indicated slower jobs growth



Source: Macrobond Financial, Markit Economics, BLS

Labour demand

Many available jobs

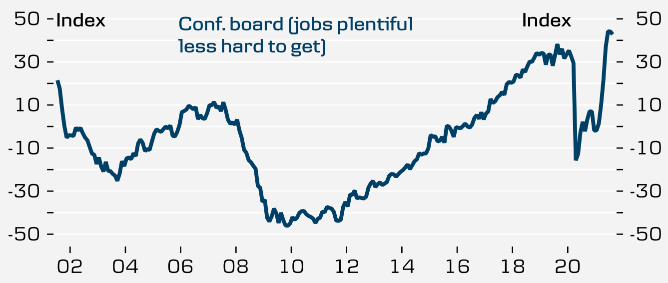


Source: Macrobond Financial, US Department of Labor, BLS

Small businesses expect to hire more

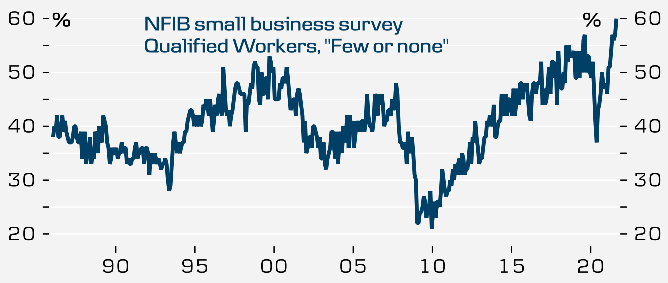
Source: Macrobond Financial, NFIB

Americans think that jobs are plentiful



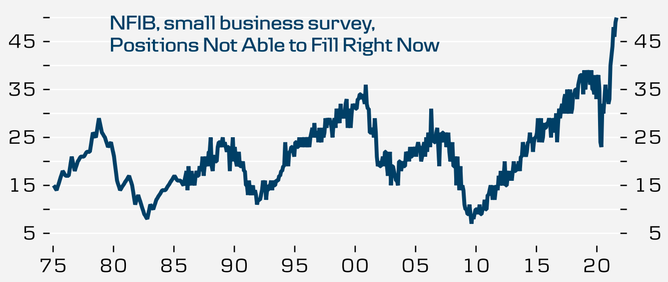
Source: Macrobond Financial, US Department of Labor, BLS

Mismatch between labour demand and labour supply? Difficult for businesses to find qualified workers



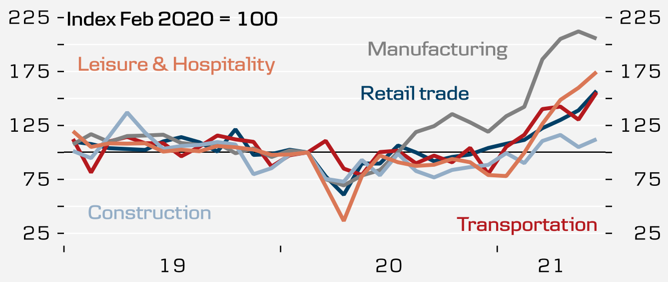
Source: Macrobond Financial, NFIB

Businesses are unable to fill positions



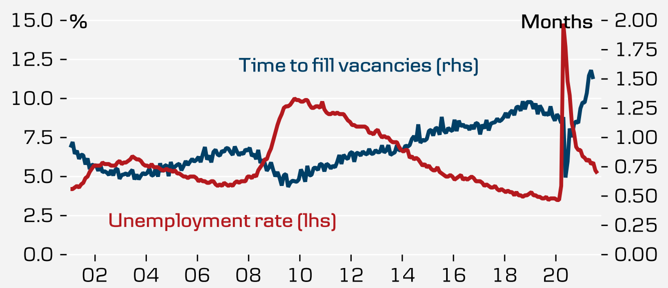
Source: Macrobond Financial, NFIB

Many job openings in manufacturing



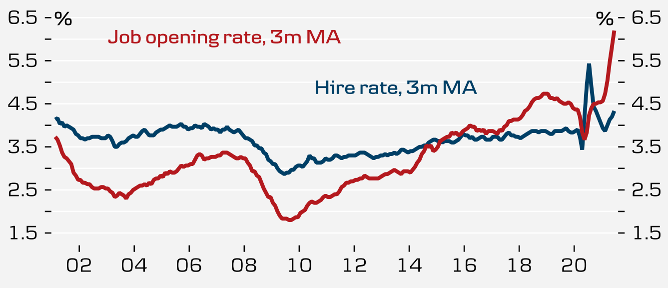
Sources: BLS, Macrobond Financial

Unemployment and time to fill vacancies



Source: Macrobond Financial, BLS

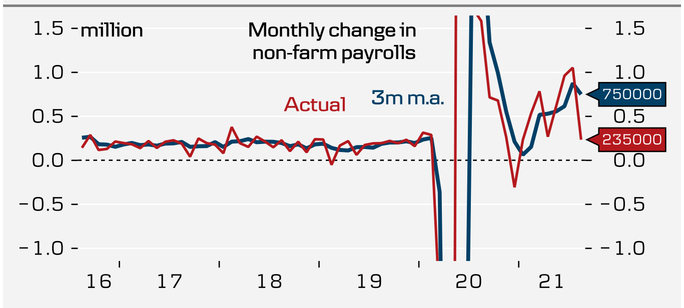
Businesses are unable to fill positions



Source: Macrobond Financial, BLS

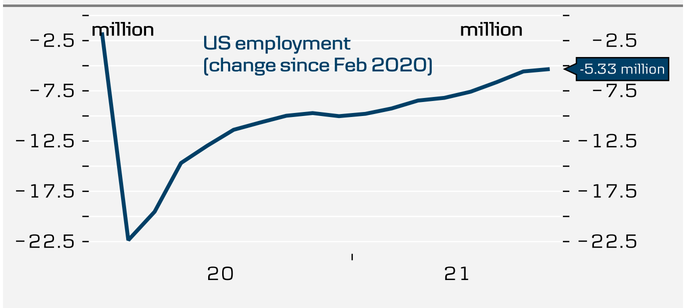
Employment measures

Jobs growth disappointed in August



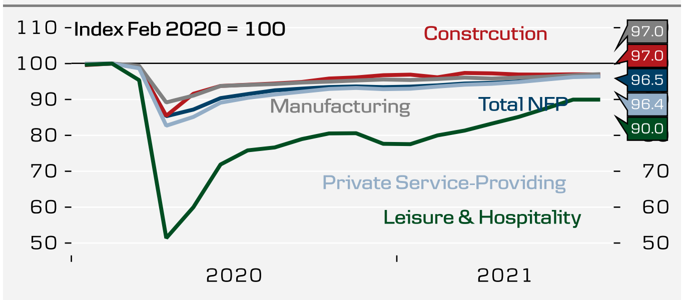
Source: Macrobond Financial, BLS

ADP private payrolls growth



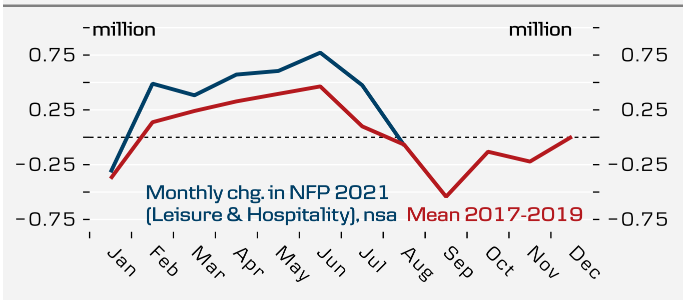
Source: Macrobond Financial, ADP

Employment in "Leisure & Hospitality" is still 10% below pre-covid levels



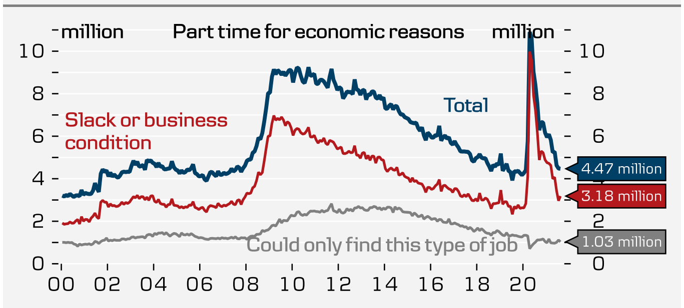
Source: Macrobond Financial, BLS

Monthly change in "leisure & hospitality" employment – re-opening indicator



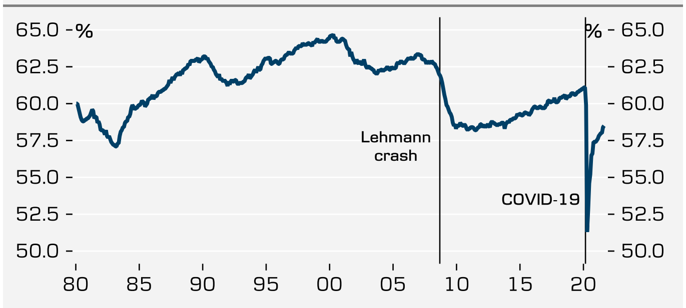
Source: Macrobond Financial, BLS

Fewer people working part-time for economic reasons



Source: Macrobond Financial, BLS

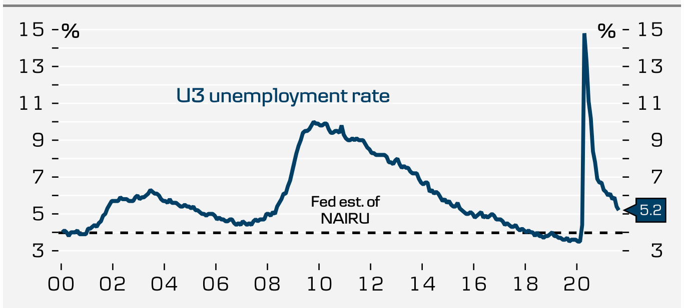
Employment to population ratio still below previous levels



Source: Macrobond Financial, BLS

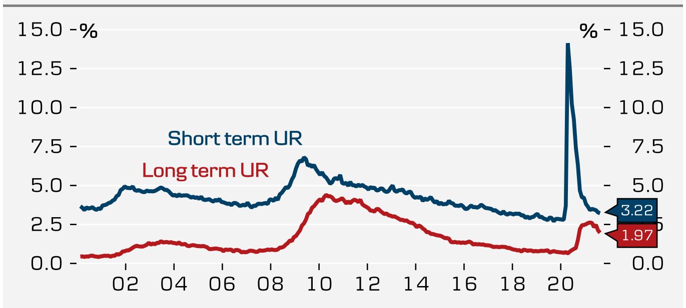
Unemployment measures

Unemployment rate slightly below Fed's NAIRU estimate



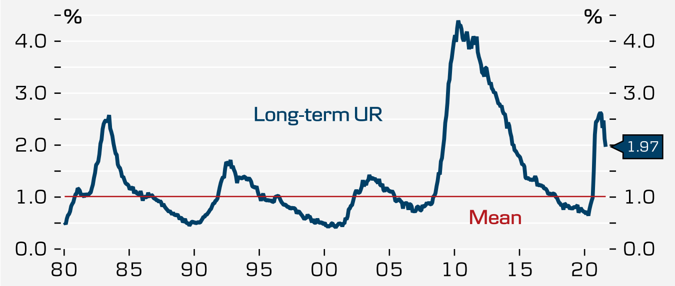
Source: Macrobond Financial, FOMC, BLS

Long-term unemployment still a bit elevated



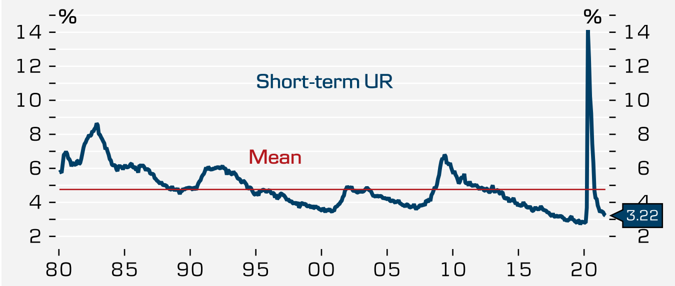
Source: Macrobond Financial, BLS

Long-term unemployment rate above the historical low



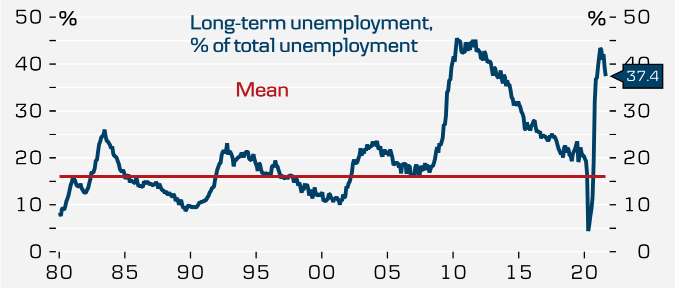
Source: Macrobond Financial, BLS

Short-term unemployment rate below historical average but higher than before COVID-19



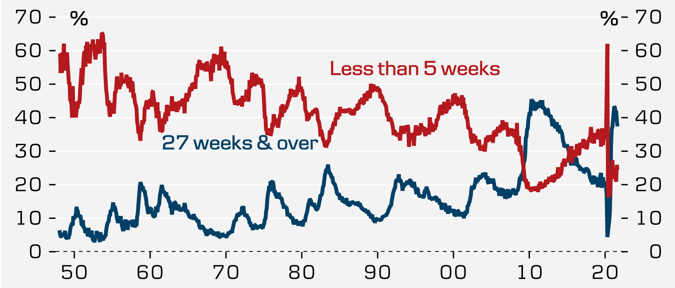
Source: Macrobond Financial, BLS

Long-term unemployment in % of total unemployment



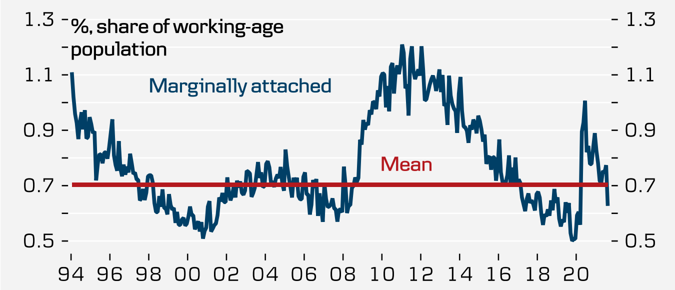
Source: Macrobond Financial, BLS

Unemployment - duration



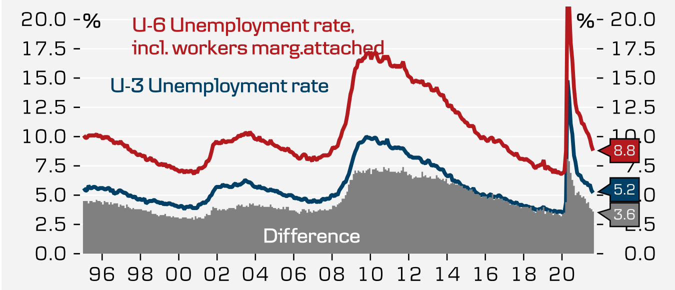
Source: Macrobond Financial, BLS

Marginally attached workers below average but not at record-lows



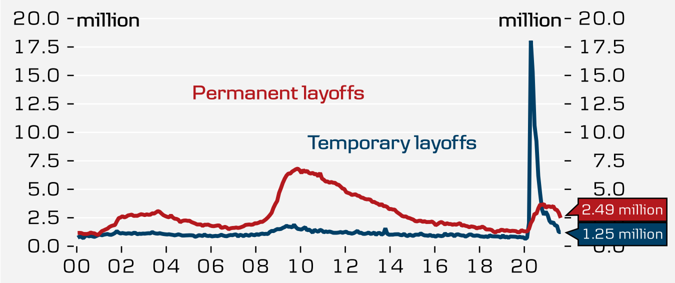
Source: Macrobond Financial, BLS

U6 unemployment also declining but remains elevated



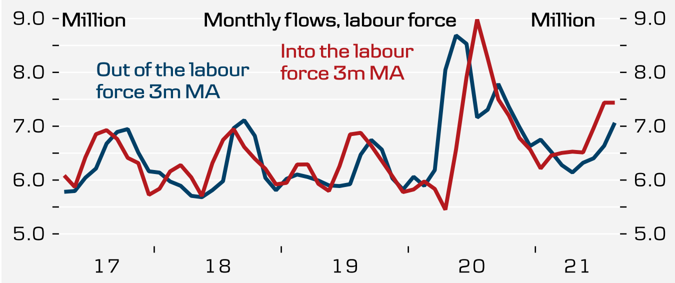
Source: Macrobond Financial, BLS

Permanent layoffs remain elevated



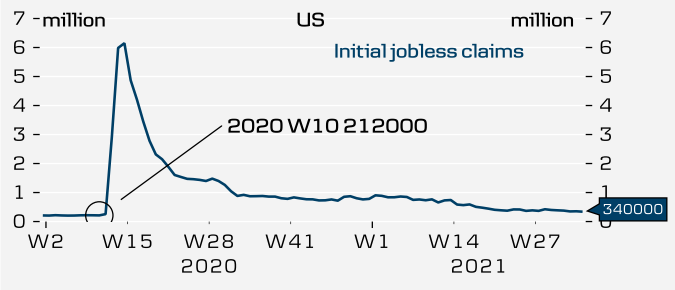
Source: Macrobond Financial, BLS

Labour market flows



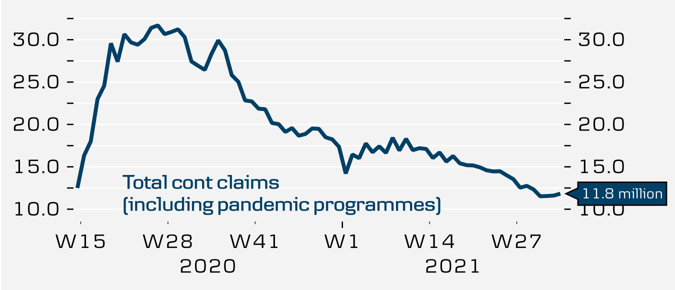
Source: Macrobond Financial, BLS

Initial jobless claims remain higher compared to pre-COVID



Source: Macrobond Financial, Department of Labor

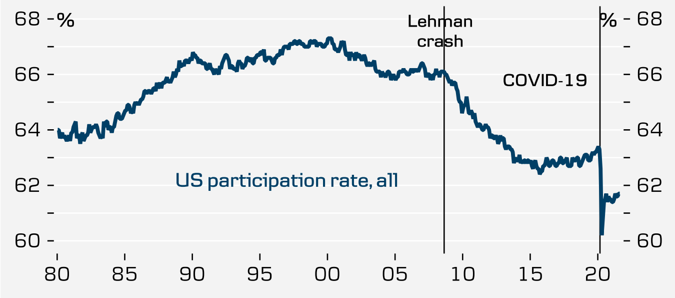
Total continuing claims remain high



Source: Macrobond Financial, Department of Labor

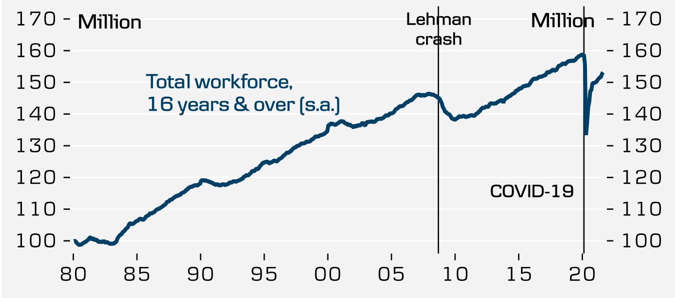
Participation

Participation remains low compared to pre-COVID levels



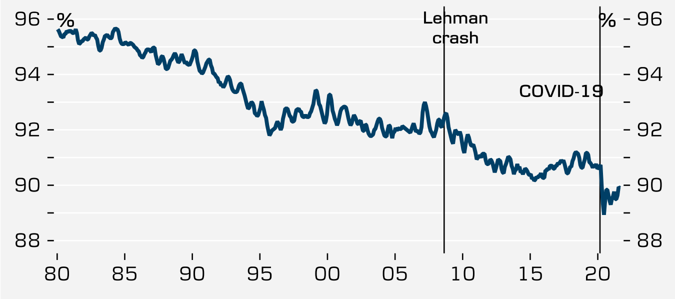
Source: Macrobond Financial, BLS

Labour force increasing but still below pre-COVID levels



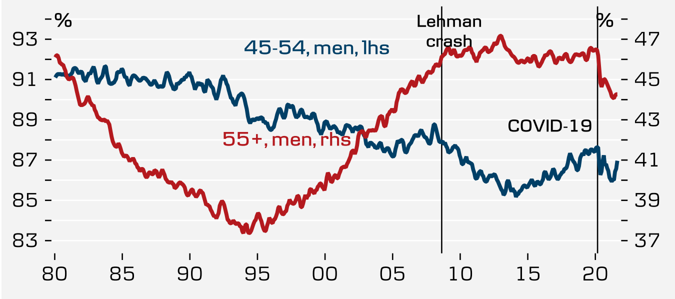
Source: Macrobond Financial, BLS

Participation rate, 35-44, men



Source: Macrobond Financial, BLS

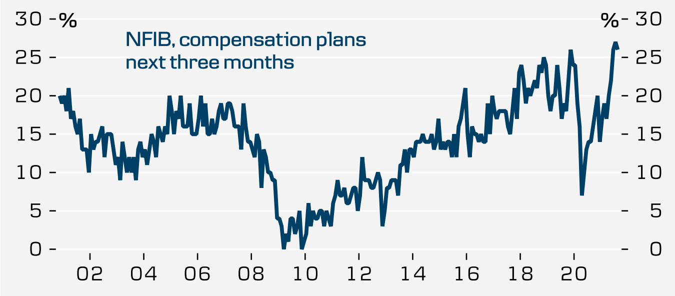
Participation rate, 45-54 and 55-plus, men



Source: Macrobond Financial, BLS

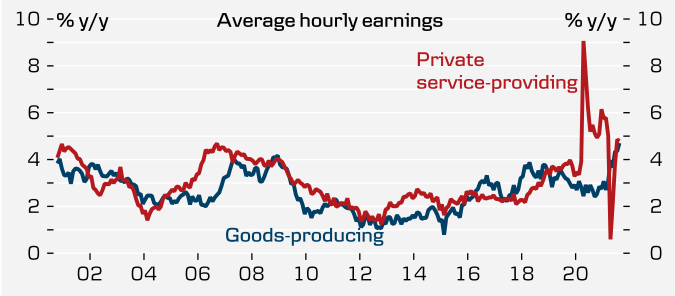
Wage growth and inflation

NFIB compensation plans are high



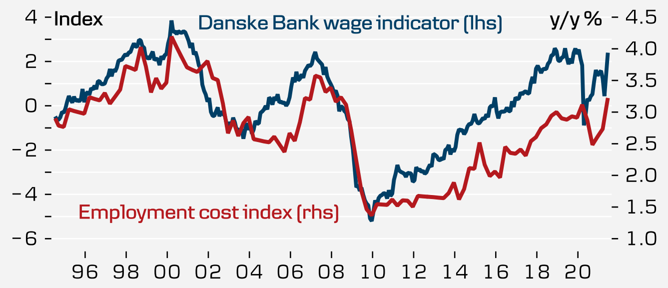
Source: Macrobond Financial, NFIB

Rising wage pressure?



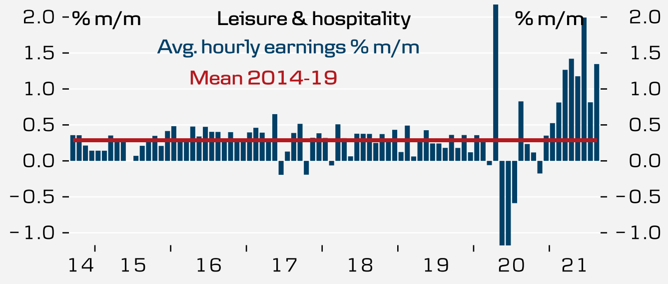
Source: Macrobond Financial, BLS

Rising wage pressure



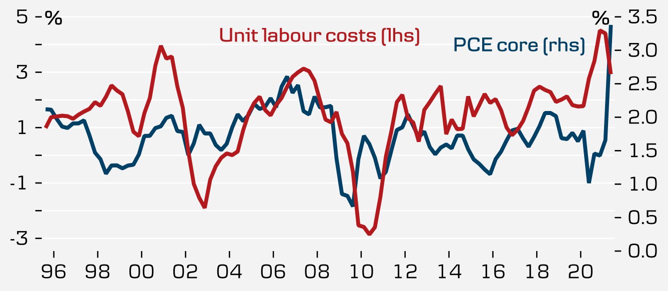
Source: BLS, Danske Bank Markets

Wage growth is high within "Leisure & Hospitality"



Source: BLS, Conference Board

Higher wage pressure => higher inflation down the road?



Source: Macrobond Financial, BLS, Census, BEA

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This research report has been prepared by Danske Bank A/S ('Danske Bank'). The author of this research report is Mikael Olai Milhøj, Senior Analyst.

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