PM Datanote: Employment, May

In one line: Normal service resumes, but this time, wages are accelerating.

May payrolls rose 280K, well above the consensus, 226K, but - ahem - dead in line with our forecast. The net revision was +32K, so overall very strong. The unemployment rate rose a tenth to 5.5%, above the consensus, 5.4%. Hourly earnings rose by 0.3%, a tenth above the consensus, 0.2%. The increase in the unemployment rate is noise, a distraction, reflecting a reported 397K jump in the labor force. This number is hyper-volatile and was depressed in the winter, now rebounding but it can't possibly keep rising so quickly. But if payrolls continue to rise at anything like this pace - and every indicator we follow says they will - the trend in the unemployment rate will continue to trend downwards rapidly.

The payroll gains are broad-based, with most sectors except IT returning to their pre-winter trends. The birth/death model, which was a fluke 60K drag on April payrolls, reverted to trend. The seasonal adjustment, however, was rather tougher than in May last year; had it been unchanged the headline print would have been 340K. But perhaps the most important number of all is hourly earnings, where the y/y rate rose to 2.3%, the highest since Aug 13, and the rolling quarterly - latest three months compared to previous three months - hit 2.9%, the fastest gain in six years. Hourly earnings are on the move, and, over the past 30 years, nothing has been more closely correlated with Fed action than wage gains. They will continue to accelerate, following the surge in the ECI, and if the Fed does not begin to raise rates very soon, markets will soon be pointing out to policymakers that they are behind the economy. If the June employment report is as strong as this one, a July hike can't be ruled out; if not then, we think Sep is the latest the Fed can dare to leave policy set for the end of the world.

The chart shows that the breakout in wage gains is not yet definitive, but it is enough, given the pace of payroll growth, to get the Fed’s attention.