Datanote: Employment, February

In one line: The current trend in payrolls is steady, but a clear downturn is coming

- February payrolls rose 275K, above the consensus, 200K. But the net revision was -167K, so the net number is just 108K.
- Average hourly earnings rose 0.1%, a tenth below the consensus, 0.2%. The net revision was -0.09%.

- The unemployment rate rose to 3.9% from 3.7%, above the consensus, 3.7%.
- Aggregate hours worked rose 0.4%, reversing the revised 0.4% drop in January.

The February headline comprises a 223K increase in private payrolls and a 52K increase in government jobs. The private print was rather stronger than our Homebase-driven model, but the huge downward revisions to December and January mean that the net number was in line. The trend in payrolls is now back in line with lagged NFIB hiring intentions numbers. The overshoot in Dec/Jan relative to the NFIB has now gone. The three-month average increase in private payrolls now stands at 205K, still higher than before the December jump, when it was about 150K, but likely to head down sharply over the next few months.

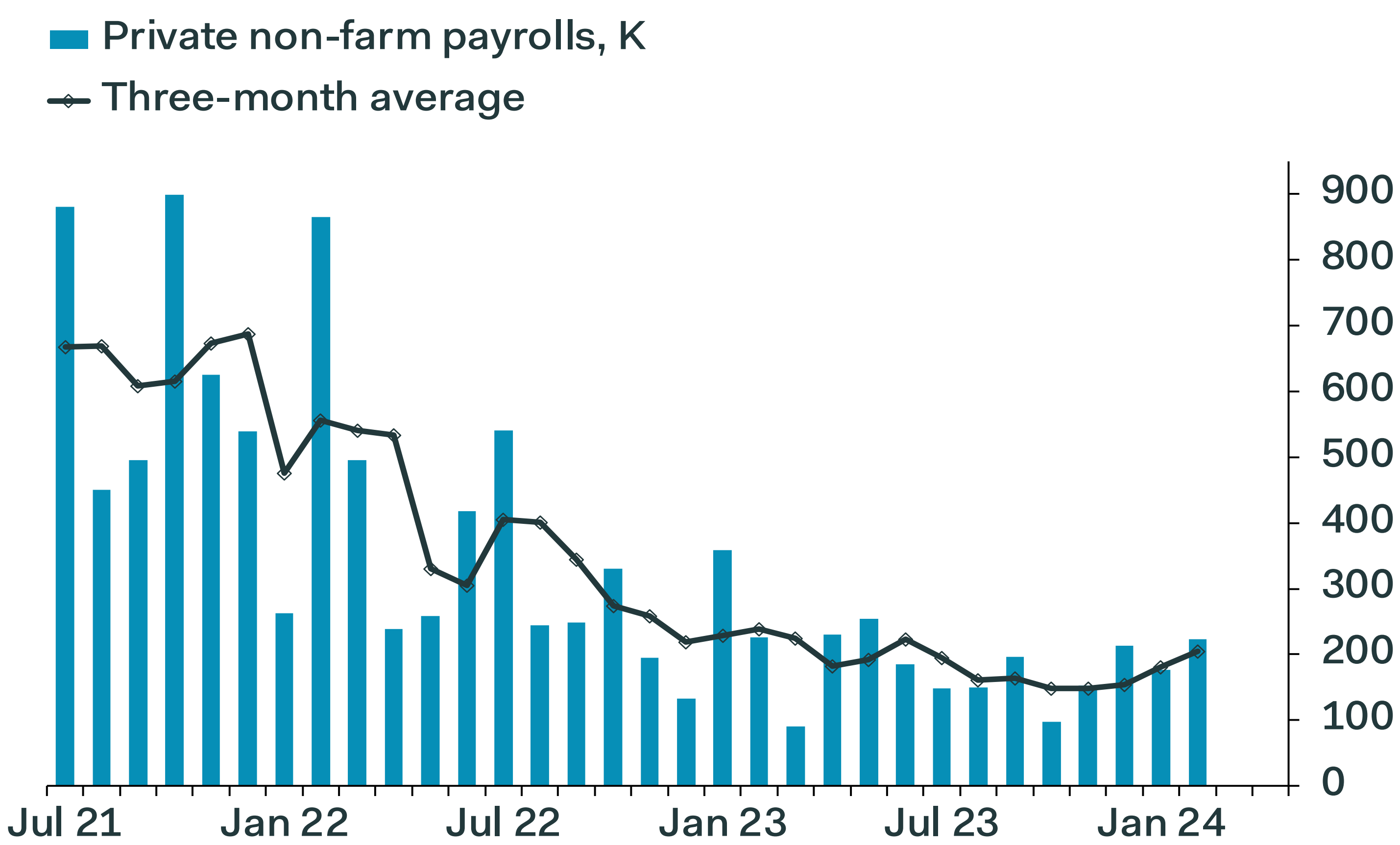
The clear message from three straight declines in the NFIB survey's measure of hiring intentions is that higher interest rates and tighter credit conditions are forcing small firms—which employ about half the workforce - to tighten their belts, and labor is their biggest variable cost. The drop in hiring plans is consistent with private payroll growth slowing sharply in the spring, and the February NFIB reading, released yesterday, is low enough to suggest a real risk of an outright drop in private jobs by mid-year. That risk is magnified by the emerging deterioration on the other side of the payroll equation, with leading indicators of layoffs now pointing uniformly upwards. For the first time in this cycle, the trends in both hiring and firing are worsening at the same time. We also wonder if the lag from the NFIB to payrolls might be shortening; perhaps once businesses have made the decision to cut back, they act more quickly than in the middle of the cycle.

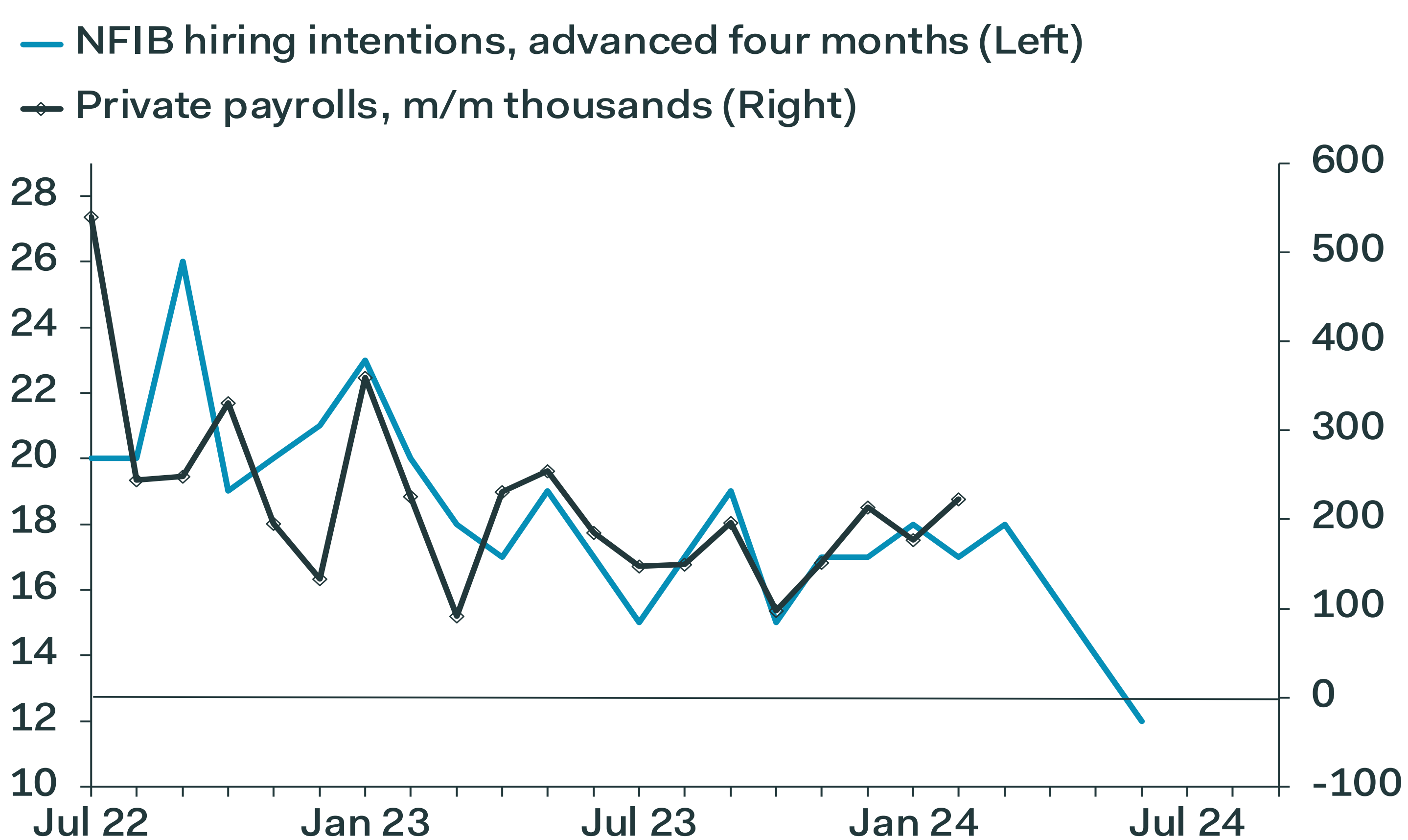
The rebound in February hours worked and softness in average hourly earnings are two sides of the same coin. AHE is a crude calculation of total earnings divided by hours worked, so when hours are depressed by weather conditions - January was relatively warm but snow cover across the US during the survey week was much higher than usual, limiting outdoor work - reported AHE tends to jump, and then correct in the following month.

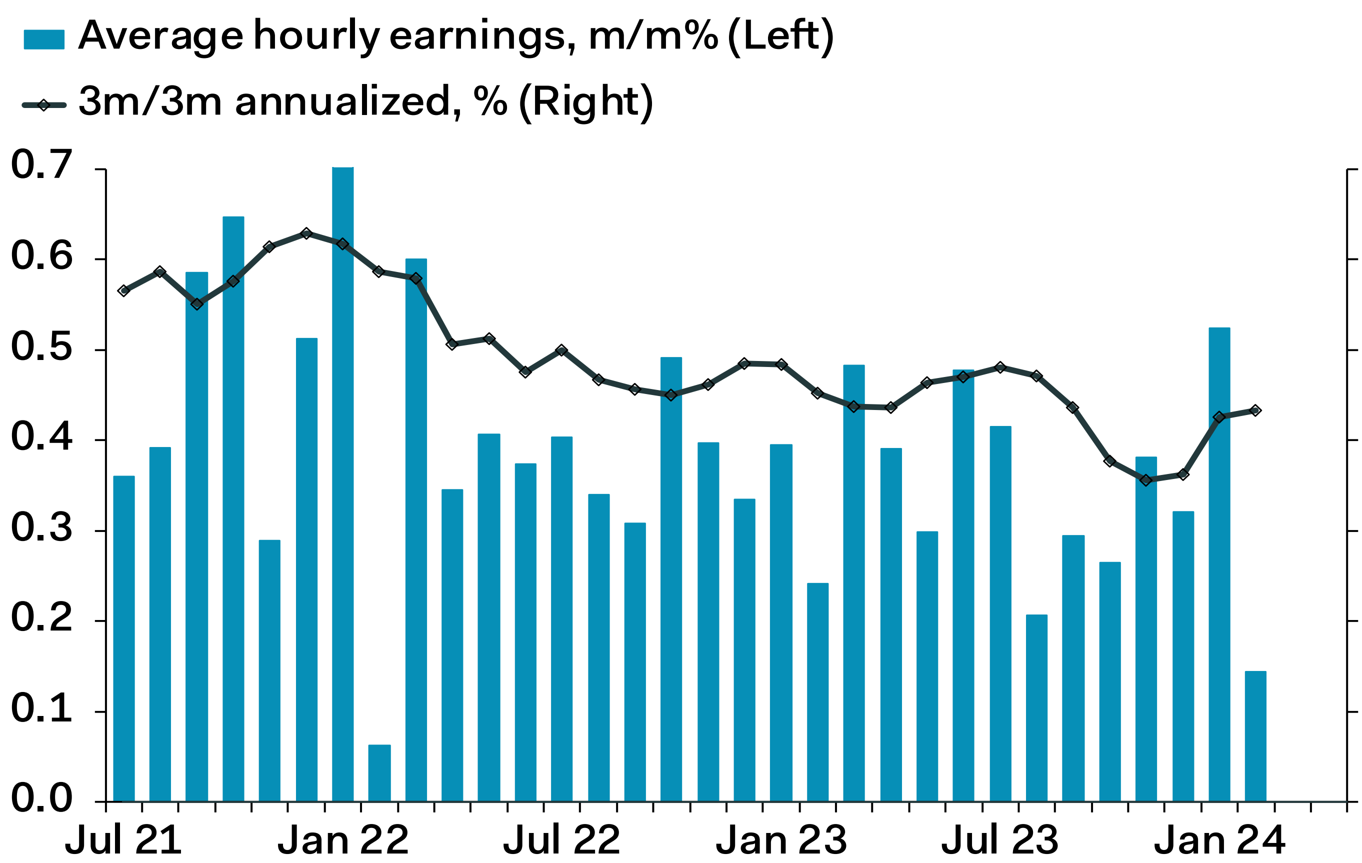
In any event, the Fed is much more interested in the mix-adjusted quarterly employment costs index as a measure of wage pressures, and the rate of growth of the ECI's private sector wage series is slowing relentlessly. Moreover, the ongoing drop in the quits rate - it hit a new cycle low in January - points clearly to a further slowing in wage gains and, hence, lower core services inflation.

The reported rise in the unemployment rate is statistically significant, but only just, and we need to see far more data to confirm any change in the trend. The household survey is based on a much smaller survey than the payroll numbers, so the employment, unemployment, labor force and participation rate data can’t be taken seriously month-to-month. Indeed, the changes in all these variables over the past six months, net, are statistically insignificant. That said, we expect the unemployment rate to rise, starting in the spring, as job growth slows.

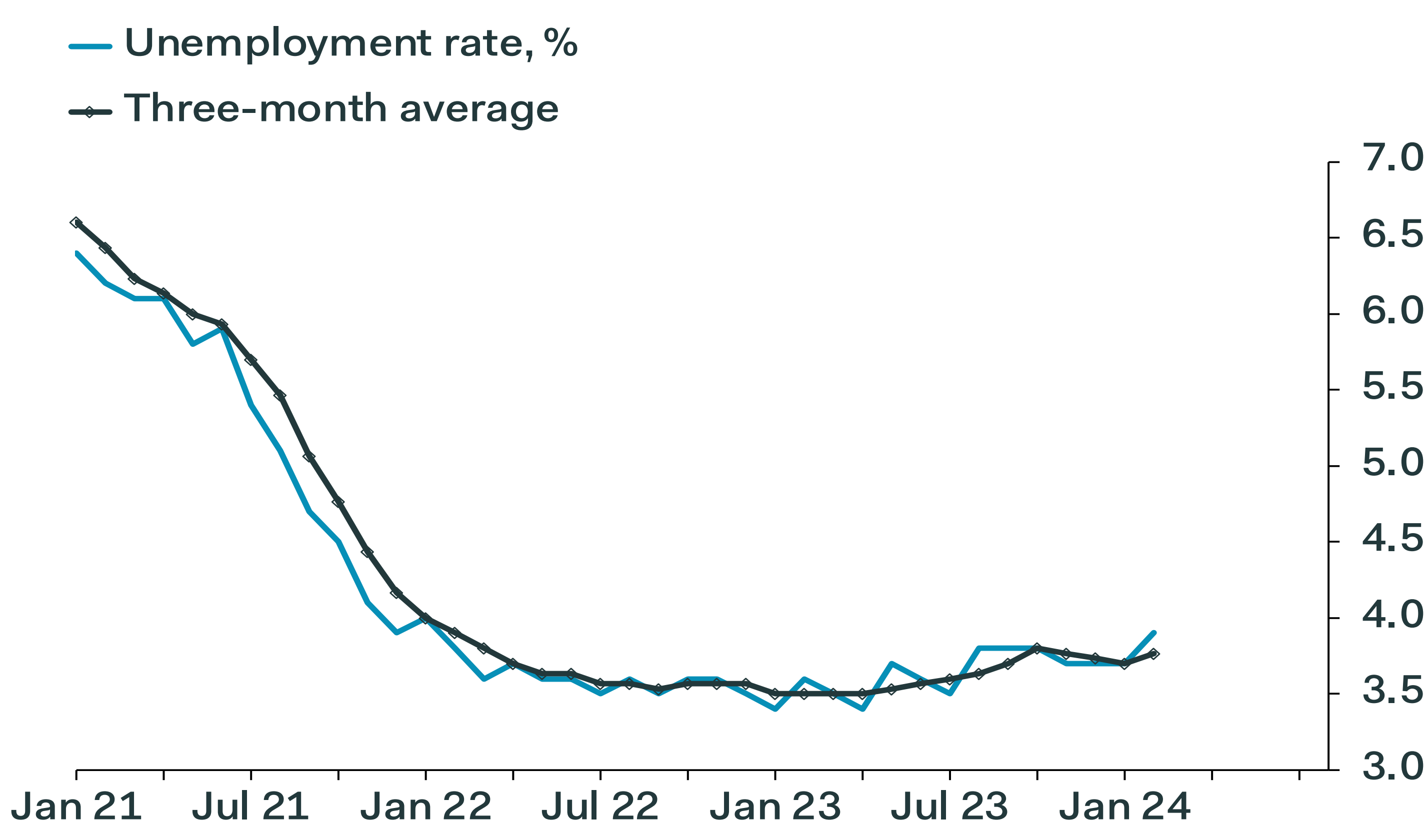
Whether this will be apparent in the data quickly enough for the Fed to ease in May is unclear. Only one more round of employment data will be released before the May 1 FOMC decision. But our base case is that these numbers will be soft, and that the ECI data released April 30 will confirm that labor cost pressures continue to ease. We also expect better inflation data for February and March, so we're sticking for now to our call that the first easing will come in May. But this is a 55/45 shot; it would be no surprise if the Fed waits until June.


Private non-farm payrolls, K
Three-month average
900
800
700
600
500
400
300
200
100
0
Jul 21
Jan 22
Jul 22
Jan 23
Jul 23
Jan 24


NFIB hiring intentions, advanced four months (Left)
Private payrolls, m/m thousands (Right)
28
26
24
22
20
18
16
14
12
10
600
500
400
300
200
100
0
-100
Jul 22
Jan 23
Jul 23
Jan 24
Jul 24



Average hourly earnings, m/m% (Left)
3m/3m annualized, % (Right)
0.7
0.6
0.5
0.4
0.3
0.2
0.1
0.0
7
6
5
4
3
2
1
0
Jul 21
Jan 22
Jul 22
Jan 23
Jul 23
Jan 24



Unemployment rate, %
Three-month average
7.0
6.5
6.0
5.5
5.0
4.5
4.0
3.5
3.0
Jan 21
Jul 21
Jan 22
Jul 22
Jan 23
Jul 23
Jan 24