Disappointing wage data won't help the Fed's case for higher rates

Expect markets to remain sceptical about the Fed's hiking plans as Friday's all-important wage growth figure looks set to come in below consensus

Source: Federal Reserve

Wage growth to disappoint - but only because of a statistical quirk...

A surge in wage growth during July was a welcome development after a particularly lacklustre start to the year. But this time, markets could be left disappointed. There were two additional workdays in August relative to July, and this typically means that average hourly earnings growth is noticeably lower. Of course, this is a statistical quirk that tells us nothing about the fundamental backdrop, which given high job-to-job flows and a jobs market near full employment, looks very strong. We still expect wage growth to gradually pick-up, but it's a slow-moving ship and we may struggle to see a figure above 3% this year.

2.5 Average Hourly Earnings (YoY%)

(Consensus 2.6%)

Jobs growth would have to be horrendous to worry the Fed

Recent strength in jobs growth is a double-edged sword for the Fed. Whilst consistently large employment gains are no bad thing, it raises the possibility that the economy has more slack than previously thought. As the US nears full employment, logic says that job gains should slow. The Fed is well aware of this argument so even if payrolls corrects lower this month, policymakers are unlikely to bat an eyelid. It's also worth noting that this month's data will have been collected before Hurricane Harvey.

160k Change in non-farm payrolls

(Consensus 180k)

Unemployment rate to stay at post-crisis low

Another fall in July extended what has been a fairly remarkable decline in the unemployment rate so far this year. 350,000 people entered the labour force in July, with only 4k being left without a job. A fresh wave of individuals seeking work in August should keep the unemployment rate steady - although as always, it's worth saying that the household survey can be extremely choppy.

4.3% Unemployment rate

(Consensus 4.3%)

Hurricane won't blow the Fed off course - but inflation and wage growth might

Hurricane Harvey is set to be one of the costliest storms to hit the US since Katrina back in 2005, and along with the devastating human impact, early indications suggest the financial costs are likely to extend into the tens of billions. But at an aggregate, economic growth level, the effect could be more muted and most of the impact is likely to be felt through oil disruption. More broadly, third quarter growth looks set to be relatively strong, partly as firms increase inventories.

So with the growth backdrop looking fairly solid, the outlook for Fed hikes hinges on inflation. Whilst this week's wage data could disappoint and core PCE, the Fed's favoured measure of inflation, could hit a one-and-a-half year low, we're still optimistic on the outlook. That should ultimately see the Fed hike rates again in December. But with the turnaround in both core inflation and wage growth set to be gradual, markets are likely to remain wary of the Fed's rate hike plans.

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