Tight US jobs market will keep the 50bp hikes coming

The US economy added more jobs than expected in May, but with nearly two job vacancies available for every unemployed American the numbers would be even stronger if there was a better supply of quality labour. This is both a constraint on growth while contributing to ongoing elevated inflation via higher wages. 50bp hikes remain the default for June and July

The US economy added more jobs than expected in May

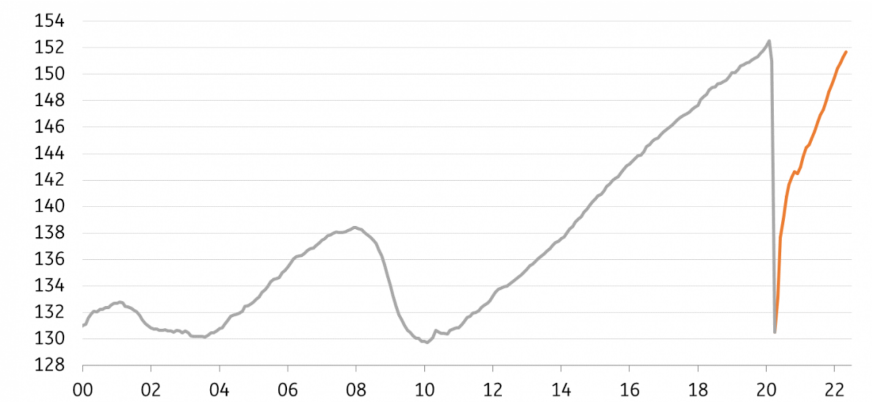
390k The number of jobs added in May

Jobs beat expectations yet again

US non-farm payrolls rose 390k in May versus the 318k consensus forecast, although there were a modest 22k of downward revisions to the past two months of data. This is the seventh month in the last eight where payrolls growth has beaten consensus predictions. Job gains were solid throughout aside from a surprise 61k drop in retail. The unemployment rate remains at 3.6% versus 3.5% expected with the participation rate ticking a tenth higher to 62.3%. Meanwhile wage growth was a touch softer than forecast at 0.3%MoM/5.2%YoY so it seems the bigger gains of 0.5% or 0.6% seen through 2H 2021 may well be past. This report will likely please the Fed in that the job creation story is pretty good, but inflationary pressures in the labour market may well be starting to top-out.

This is especially encouraging given a slowdown in hiring had been hinted at in other reports. The Homebase worker scheduling and time tracking data had indicated a moderation, while the Fed's Beige Book suggested employment grew "modestly or moderately" although "one District explicitly reported that the pace of job growth had slowed". Meanwhile the ISM manufacturing employment index fell below the break-even 50, indicating contraction.

Level of US non-farm payrolls (mn)



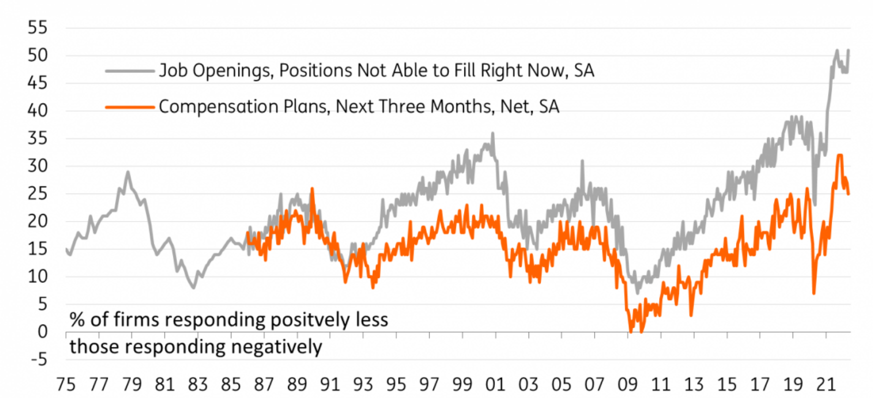
Source: Macrobond, ING

Slower growth ahead is likely

Admittedly we do expect to see slower payrolls growth in coming month, but this should not come as a huge surprise given that 21.2mn of the 22mn jobs lost in March and April 2020 have now been filled. Moreover, the prospect of big job gains has also been dampened by likely corporate caution relating to recent falls in equity markets and growing concern about the economic outlook in the face of geopolitical uncertainty, rising costs and Federal Reserve interest rate hikes.

Nonetheless we still see the biggest constraint on employment growth being the lack of available labour with the right skill sets. After all, as of April there were 11.4mn job vacancies in the US, equivalent to nearly two job vacancies for every unemployed American, double what it is in the UK while in Germany there are just 0.4 vacancies for every unemployed person. Then there is yesterday's National Federation of Independent Businesses jobs survey which showed that a record 51% of small businesses had vacancies they were unable to fill. Most tellingly, the Beige Book noted that "worker shortages continued to force many firms to operate below capacity".

NFIB survey shows record proportion of firms struggling to find workers, but pay growth may be topping out



Source: Macrobond, ING

Tight labour market will keep the Fed hiking by 50bp

This mismatch between demand and supply continues to bid wages higher with average hourly earnings rising in an environment where worker participation rates is still just 62.3% versus the peak of 67.3% in January 2000. However, as already mentioned, the momentum in wage growth shows signs of peaking with the NFIB survey (as the earlier chart shows) reporting that a net 25% of small businesses expecting to raise worker pay over the next three months, down from 32% last December. The Beige Book also noted that "in a few Districts, firms noted that wage rate increases were levelling off or edging down".

That said, a tight jobs market with worker shortages and rising pay is both a constraint on growth and will keep inflation higher for longer. This means there is nothing in this report to deter the Federal Reserve from their roadmap of 50bp hikes at the June and July FOMC meetings, especially with GDP likely to rebound at around a 4% annualised rate in the second quarter based off decent consumer spending, investment and trade data.

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