US: Jobs report highlights the positives

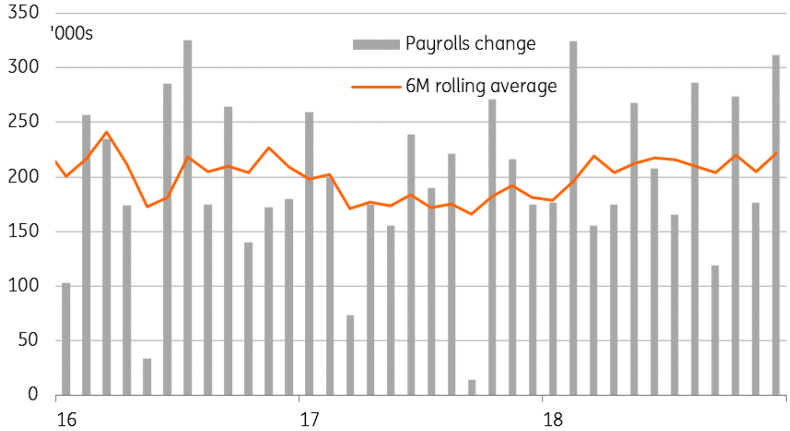
For all the current market doom and gloom over the US's prospects, there are some positives, such as the red-hot jobs market. Market expectations that the Federal Reserve could cut interest rates this year are wide of the mark, in our view

Source: iStockphoto

Too good to be true?

The December US jobs report is remarkable on a number of fronts. A 312,000 increase in non-farm payrolls plus a net 58,000 upward revision to the past two months of data yet the unemployment rate rises from 3.7% to 3.9% thanks to a surge in the labour participation rate. Wages jump another 0.4% MoM leaving the annual rate of wage growth up at 3.2% - the highest since April 2009. This really positive report should certainly ease creeping fears in the market that the Federal Reserve may be forced to cut interest rates. However, given the growing headwinds facing the US (fading support from the fiscal stimulus, a strong US dollar, lagged effects of higher interest rates and weaker external demand amidst worries over trade protectionism), there will be doubts over whether such strength is sustainable.

US monthly payrolls growth



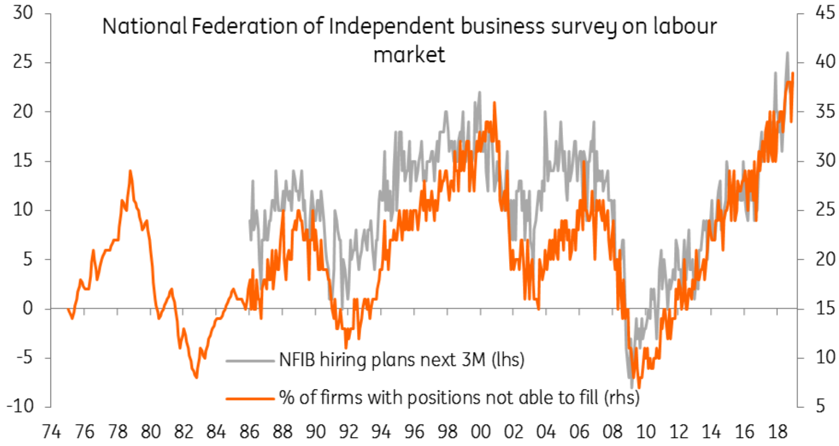
Source: Bloomberg, ING

Payrolls growth will slow, but wages will rise further

Now that we have data for the full year we know that payrolls growth averaged 220,000 per month, up from 182,000 in 2017 and 195,000 in 2016. We suspect payrolls growth will slow in 2019, but this more reflects the lack of supply to fill vacancies rather than a major drop-off in demand. In this regard, the National Federation of Independent Businesses yesterday reported that the proportion of member firms that can't fill their current vacancies is at an all-time high (39%). This analysis was backed by the December Federal Reserve Beige Book, which suggested that "over half of the Districts cited firms for which employment, production, and sometimes capacity expansion had been constrained by an inability to attract and retain qualified workers".

This lack of supply means wages are being bid up and employees are feeling the benefits. Wage growth is now 3.2% YoY and we think it will rise further, given the competition for suitable workers at a time when the unemployment rate is close to multi-decade lows. This is is becoming more noticeable in other forms of compensation with the Beige Book stating that "in addition to raising wages, most Districts noted examples of firms enhancing nonwage benefits, including health benefits, profit-sharing, bonuses, and paid vacation days." This should help underpin consumer confidence and keep spending relatively robust.

Employers can't fill vacancies, which will keep upward pressure on pay



Source: Macrobond

Financial markets had moved too far

Given recent turbulence, financial markets had been pricing in a 50% chance of a Federal Reserve rate cut this year ahead of this jobs report, with a full cut priced in by the end of 2020. Certainly the US economy does face more headwinds this year, but this in our view is likely to mean a slower and more modest set of rate hikes versus 2018 rather than actual policy easing. Given the recent financial market turbulence and uncertainty caused by the ongoing government shutdown we suspect there will be a pause in 1Q19, but in an environment of respectable economic growth and rising wage and core inflation pressures we still look for tighter monetary policy over the summer.

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