US slowdown continues, which will hit jobs

Financial markets continue to price interest rate cuts later this year despite the Federal Reserve's pushback. The labour market looks to be key in determining who will be correct, with Friday's jobs report a critical piece of the jigsaw. A slowdown is coming and like the market, we expect the Fed to reverse course

+185,000 ING's forecast for January nonfarm payrolls

Fed's inflation wariness centres on job strength

The Federal Reserve continues to hike interest rates, but markets are increasingly of the view that the Fed will reverse course and rates will end the year where they started. We think they will end 2023 even lower.

The lagged effects of monetary policy tightening are weighing on economic activity with today's data now confirming the seventh consecutive monthly fall in residential construction. Manufacturing is fairing little better with three consecutive falls in industrial production set to turn into at least four after today's ISM headed deeper into contraction territory. Another hefty fall in new orders offers little hope of a swift turnaround in activity. On top of that, retail sales fell heavily in November and December while business surveys suggest sentiment is weaker than during the worst point in the pandemic and is on a par with the level of pessimism experienced during the Global Financial Crisis.

Nonetheless, the Fed continues to fret about inflation, arguing that a tight jobs market leaves open the risk that price pressures could linger. This means that Friday's jobs report will be a critical data point. The Fed will likely focus on another very strong set of numbers from today's JOLTS data that showed the number of job openings jumped by more than half a million to 11.01mn in December, well ahead of the 10.3mn expected and somewhat contradictory to evidence of rising layoffs. This indicates ongoing strong demand for workers that will keep wages bid higher. However, we have a little difficulty rationalising this given the softer economy and the increasingly defensive mindset of corporate America. We would have thought such pessimism would imply firms are more focused on cost control rather than looking to expand their business.

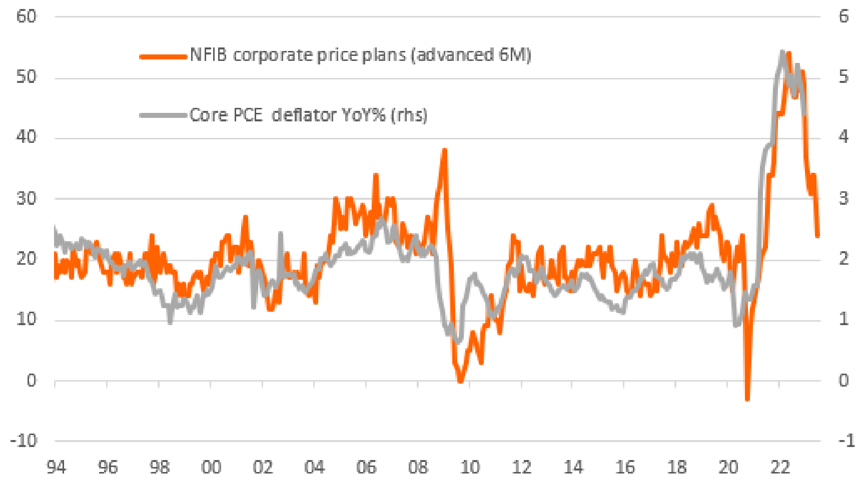
There are 1.9 job vacancies to every unemployed American

Source: Macrobond, ING

Payroll growth looks set to slow below 200,000

Today's ISM report suggested that manufacturing employment has stalled while the ADP employment report indicated manufacturing payrolls fell 3,000 as the service sector added 109,000. This 106,000 increase in private payrolls was well below the 180,000 consensus so while we have our reservations over the usefulness of the ADP report as a guide to the official payrolls number that is out on Friday, it hints at the risk of a downside miss. Given the current economic environment, we are favouring an increase in nonfarm payrolls of 185,000 in January, which would be the weakest outcome since December 2020 and would be down from 223,000 in December.

Temporary help leads broader shifts in payrolls (000s)



Source: Macrobond, ING

Weakness in temporary help could point to bad news ahead and an eventual Fed shift

Within the report, we will be closely following what happens to the temporary help component. By the nature of the position, these workers tend to be easier to hire and fire rather than permanent employees and so movements in this component tend to lead broader employment trends. The fact that this sector has seen employment fall for five consecutive months is a warning sign that firms are indeed looking at cost reductions. A sixth fall on Friday would make us even more concerned that private payrolls in general could turn negative at some point in the second quarter.

Wage pressures also look less threatening with MoM readings for average hourly earnings coming in around the 0.3% mark rather than the 0.4-0.6% rates seen over the past 18 months, and yesterday's Employment Cost Index showing moderation. As such, a weaker growth story, slowing inflation and a cooler jobs market mean we think the door will open to an even more substantive policy reversal from the Federal Reserve than the market currently anticipates. We forecast 250bp of rate cuts between late third quarter 2023 and the summer of 2024.

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