US: What to expect from the January jobs report

Sustained jobs growth, record low unemployment and benign wage pressures are a recipe for stable interest rates, but with coronavirus fears intensifying the risks remain skewed towards policy action

A Donald Trump supporter at a presidential rally in Michigan

150,000

ING's forecast for payrolls growth in January

versus 160,000 consensus

Jobs growth - manufacturing woes continue

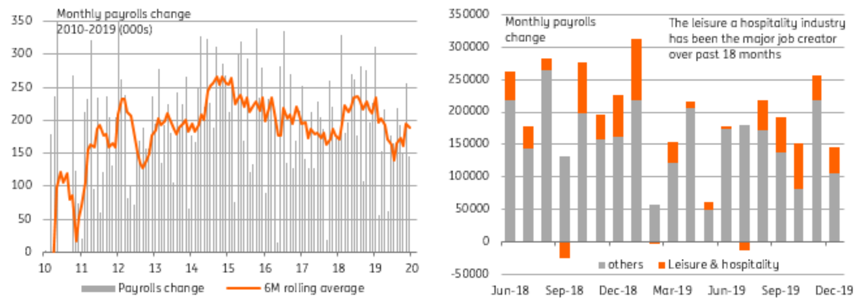
Payrolls growth was choppy through the second half of 2019, with the strike by General Motors staff contributing significantly to the volatility. That story has fully unwound, but the next issue is Boeing given it has stopped production of the 737 Max aircraft. With 600 suppliers impacted by the decision, we strongly suspect there will be a renewed drop in manufacturing employment. The January ISM manufacturing employment component remained in contraction territory at levels historically consistent with 15,000 of job losses. Note too that the January Beige Book published by the Federal Reserve reported "job cuts or reduced hiring among manufacturers, and there were scattered reports of job cuts in the transportation and energy sectors."

Construction job gains should offset this. The plunge in mortgage rates has reignited interest in the housing market with the National Association of Home Builders sentiment index at 20-year highs. Warmer-than-usual January weather may also mean that there hasn't been the usual building halt and associated temporary worker lay-offs, adding to upside risk for jobs in this sector (remember it is seasonally adjusted). With housing starts and building permits on the rise and construction spending more broadly showing decent gains, this sector is likely to be a key driver of employment growth over the next six months.

Service sector employment growth has been gradually softening from decent levels, reflecting the slowing of activity more broadly in the economy. We also caution that 20% of all the jobs created in the US over the past 18 months or so have come from the leisure and hospitality industries, which is generally viewed as being a low skill, low wage, low security sector. We see little reason to expect any meaningful resurgence in service sector employment growth this month, although hiring for the Census is likely to accelerate in coming months. These are of course only going to be temporary jobs.

Taking this altogether we look for payrolls growth of 150,000 versus the 160,000 consensus forecast. 2019 saw on average payrolls growth 176,000 per month while 2018 experienced average monthly gains of 223,000.

Employment creation



Source: Macrobond, ING

3.0% YoY

ING's forecast for wage growth

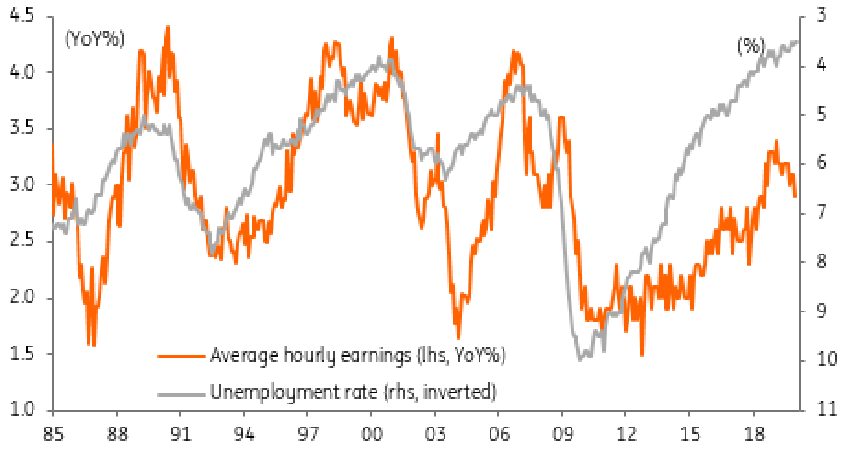
versus 3% consensus

Wage growth remains underwhelming

Given the economy continues to create jobs in significant numbers and the fact that the unemployment rate is the lowest it's been since the late 1960s, we would have thought wage growth should have picked up more than it has done. It peaked at 3.4% year on year last February, but as of December, was back down to just 2.9%.

The Federal Reseve's Beige Book continues to talk of extreme worker shortages in some industries so if companies are so desperate for staff with the right skill set why are they not paying more in the form of wage hikes? All we are seeing is "modest or moderate" pay increases resulting largely from "scattered reports of wage increases from year-end hikes in minimum wages", according to the Federal Reserve. We doubt this conundrum will be solved soon and look for a modest correction higher in the month on month rate of wage growth to 0.3% from 0.1% in December. This would leave the annual rate of wage growth at 3% YoY.

Low unemployment suggests wage growth should be much stronger



Source: Macrobond, ING

3.5%

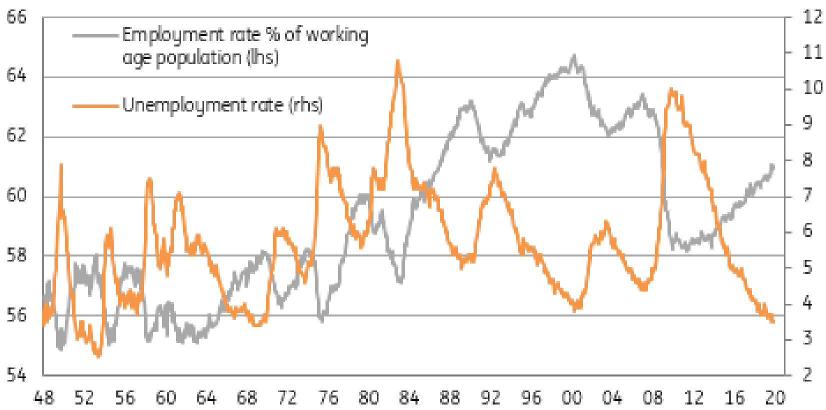
ING's forecast for the unemployment rate

versus 3.5% consensus

Unemployment rate - can it go lower?

The unemployment rate was last below its current level of 3.5% more than 50 years ago in 1969. However, as we have written on a number of occasions, this is probably not the best measure of how "tight" the jobs market is. If we look at employment as a proportion of working age population we see that while the ratio has been rising, it remains well below the pre Global Financial Crisis peak and is in fact still below the levels experienced in the recessions of the early 1990s and the early 2000s. Therefore, if we continue to see more of these economically disenfranchised people returning to the jobs market the upside for wage growth may continue to be rather limited. It also means that the unemployment rate would struggle to move much lower.

Employment versus unemployment



Source: Macrobond, ING

What it means for interest rates

Jobs continue to be created in decent numbers, but there is little wage inflation threat despite apparently tight labour markets. Consequently, with the Federal Reserve seemingly content with its current monetary policy stance, the prospect of any near-term interest rate moves seems limited.

This could change though should coronavirus fears increase in the US. Market nervousness about the virus has seen US$850bn wiped of the value of S&P500 stocks since the start of the year with 10Y Treasury yields testing the 1.50% level. So far there are no more than a handful of cases in the US, but should that change the reaction from consumers and business is likely to be significant. If we do see sentiment and spending patterns being impacted – remember that 15% of US consumer spending is on hotels, eating out, transport and recreational services – this will have a significant knock-on effect for the economy and the jobs market. Policymakers will respond in such a situation.

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