PICTET 1805

Flash Note

US employment update

Job creation is still healthy, but wage growth remains modest

Pictet Wealth Management - Asset Allocation & Macro Research | 1 September 2017

Nonfarm payrolls rose 156,000 in August. The key 3-month average is a robust 185,000/month.

Wage growth remained tepid as average hourly earnings rose only 0.1% m-o-m (2.5% y-o-y, unchanged from July).

This report keeps the Fed on track to announce a gradual balance sheet shrinkage at its 20 September meeting, in our view. We still see the next rate hike coming in December.

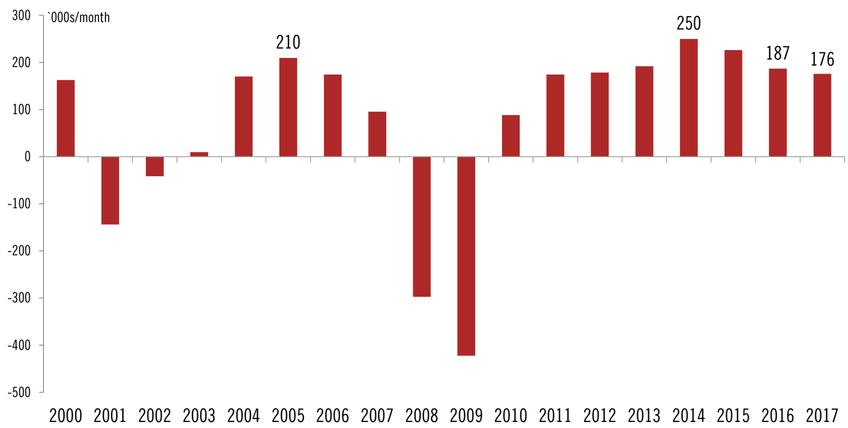
Aside from the near-term hit from Hurricane Harvey in Texas, we expect momentum in employment to remain robust into year end, but wage growth is unlikely to accelerate much.

Non-farm payrolls (NFPs) rose 156,000 in August, bringing the three-month average to a still-robust 185,000/month. The three-month average stands higher than the 12-month average of 175,000, suggesting that underlying momentum in the US labour market – and the broader economy – remains healthy. The unemployment rate increased marginally (+0.1%) to 4.4%, but this remains within the Federal Reserve's full-employment territory. (As an aside, the employment survey was conducted before Hurricane Harvey hit Texas. We expect the effects of the hurricane to show up in next month's job report, but we could see a v-shaped recovery in new jobs after an initial hit.)

The fly in the ointment was the ongoing softness in wage growth. Average hourly earnings rose only 0.1% m-o-m in August, compared with 0.3% in July, with the y-o-y reading unchanged at 2.5%. There are structural impediments to better wage growth, in our view, including ongoing technological change, low inflation, and the difficulties of the retail sector (retail employment was down 0.2% y-o-y). We see wage growth staying tepid in the coming months, as pressure from these sources is unlikely to abate.

From a Federal Reserve perspective, we think this report will be seen as 'more of the same'. The Fed is still likely to announce plans for balance sheet shrinkage at its 20 September meeting. While recent inflation prints and, to some degree, wage growth, have been mixed, we think loose financial conditions are front-and-centre of the Fed's concerns. While the market (Fed futures) is now only pricing in a 34% probability of a Fed hike by the end of this year, we expect one to come at the Fed's December meeting.

Employment growth has remained firm this year (+176,000/month on average)



Source: Pictet WM – AA&MR, Bloomberg

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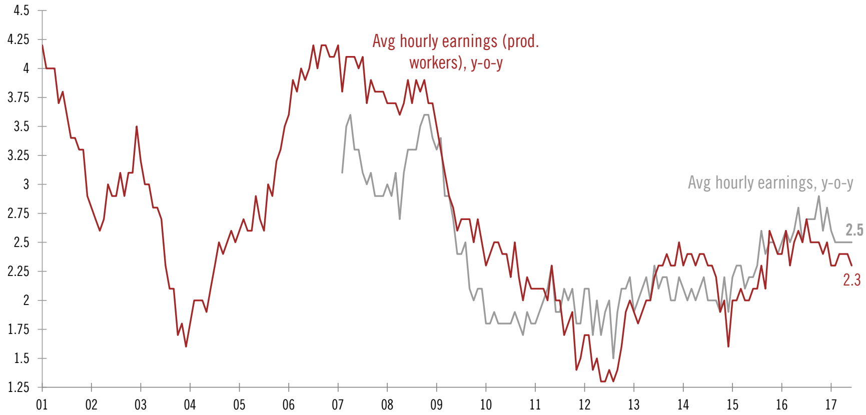
PAYROLL DATA RECAP

› Momentum	– Solid 3-month average at 185,000, above the 12-month average of 175,000 – Total employment up 1.4% y-o-y – Particularly robust momentum in manufacturing employment: 3-month average of 28,000/month versus 12-month average of 12,000/month, up 1.1% y-o-y – Employment in mining (including oil and gas) up a strong 9.8% y-o-y – Robust private-sector momentum contrasts with ongoing headwinds in government sector (employment flat y-o-y)
› Business cycle	– Manufacturing/mining employment on an upswing – Temporary help jobs (a key leading indicator for the business cycle) still looking firm at 7,000/month in the past three months, or +4.3% y-o-y – Job opening survey still showing robust hiring momentum, heralding solid job growth ahead – Still-low initial jobless claims data
› Structural trends	– Underlying technology shift continues – Bricks-and-mortar retail crisis deepens as retail employment falls 0.2% y-o-y (-0.1% in July) – Employment at newspaper publishers down 6.7% y-o-y in July (latest data available) – Employment at grocery stores down 0.6% y-o-y, while employment at non-store (internet) retailers up 10.4% y-o-y – Healthcare sector jobs continue steady expansion, albeit at a slower speed (+2.1% y-o-y, from +2.2% in July)
› Fed policy	– Solid 3-month average in NFP, the key metric for Fed officials, likely to comfort their assessment that there is decent underlying economic momentum, especially after Q2 GDP growth was raised to 3.0% q-o-q SAAR – Some Fed doves will highlight the ongoing softness in wage growth as a reason to stay cautious on rate hikes – The Fed is anxious to start shrinking its balance sheet, as QE has become politically toxic – The Fed is likely to argue for continued but gradual, normalisation in rates, especially as financial conditions remain very loose (maybe too loose in the Fed's view). It could hint next hike will be in December – Wage growth of above 3-3.5% y-o-y would warrant more rapid tightening (and a higher terminal rate), all things being equal, but we see such growth as unlikely

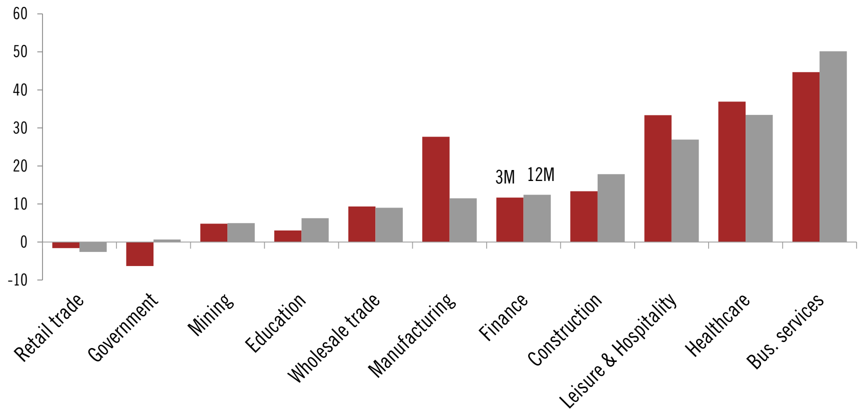
Source: Pictet WM-AA&MR, BLS

US wage growth remains moderate, despite a tight labour market



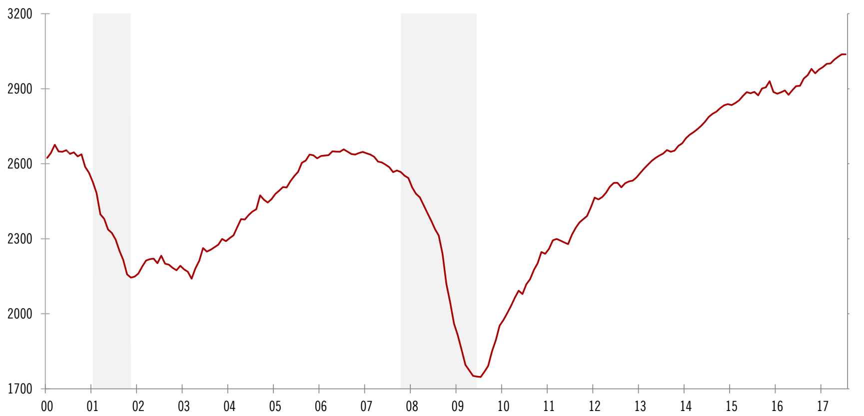
Source: Pictet WM – AA&MR, Bloomberg

Solid job growth in manufacturing lately (3-month vs. 12-month average in NFPs)



Source: Pictet WM – AA&MR, Bloomberg

Still-solid hiring in temporary help services suggests solid underlying momentum



Source: Pictet WM – AA&MR, Bloomberg