TrendMacrolytics

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TRENDMACRO LIVE!

On the March Jobs Report

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David Gitlitz

Just as today's employment report shows the payroll jobs data finally moving to catch up with the reality of a thriving economy, so too with markets suddenly awakening to the glaring light of a new day. From our perspective the most encouraging signs could be found in the array of market prices reflecting the collapse of any semblance of a rationale for maintaining a 1% overnight rate target with payrolls growing at a 2 million job annual rate over the first three months of the year.

Thus fed funds futures, which came in to today's trading discounting no **Fed** tightening action before November, are now showing a first rate hike by August, and are priced odds-on for 75 bp by December. For a bond market feeding at the trough of the Fed-engineered carry trade, today's data landed with all the subtlety of a swift crowbar to the kneecaps, as the 10-year Treasury fell more than two points, its yield soaring more than 25 bps to around 4.15%. Under normal circumstances, this sort of event would likely have seen a pronounced curve flattening, with the shift in Fed expectations disproportionately hitting the short end of the curve. Today, though, the shape of the curve was left largely unaffected, as levered-up players in the 10-year sector were forced to bail in droves.

No doubt one theme of the commentary and media analyses over the next few days will be of the "Fed taking away the punch bowl" variety, warning of the potential threat to continued expansion posed by higher rates. In fact, though, we see far the greater threat in the Fed remaining inert in the face of growing inflation risks, and ultimately having to tighten more aggressively and over a longer period than if it begins taking action in the nearer term. For the purposes of sustainable, long-term growth, the sooner the Fed ends its head-in-the-sand policy approach, the better.

Bear in mind, as well, that a funds rate of 1.5% -- or even 1.75% -- would still leave the Fed in a highly accommodative posture. And, of course, one month of robust jobs data will not necessarily prove determinative for a central bank where key figures, including governors **Donald Kohn** and **Ben Bernanke**, continue to argue against moving the Fed to a less easy posture so as to absorb the economy's remaining "slack" and guard against the chance that inflation could decline further. For these reasons, the price of gold, after initially falling more than $10 to $417 on the jobs data, recovered and closed above $420 for the fourth consecutive session. Our best bet, though, is that today marks a pivot point, and more likely than not noises from the Fed will start confirming the market's altered expectations. In February we established a speculative **Model Position long gold and short the dollar** consistent with our analysis of the Fed's excess liquidity posture. Since that posture and the expectations climate associated with it now seems likely to move toward less excess, we are closing the position at what amounts to a break-even, booking a loss of 5 basis points since inception. TM

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