Trend Macrolytics, LLC
Donald Luskin, Chief Investment Officer
Thomas Demas, Managing Director
Lorcan Roche Kelly, Chief Europe Strategist

TRENDMACRO LIVE!

On the August Jobs Report

Friday, September 6, 2013

Donald Luskin

Same old labor market. But Syria and nominating Bernanke's successor could defer tapering.

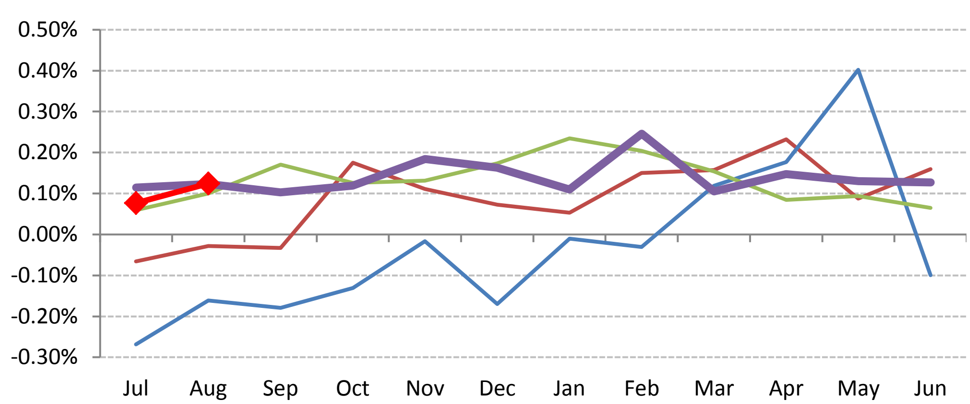
And everything was going so well for the bulls, with two sensational ISM reports this week (see "Data Insights: Global PMI" September 5, 2013). Now comes this morning's Employment Situation report, throwing us right back into the sad dynamics of the Not So Great Expansion following the Great Recession.

- The headline gain of 169,000 non-farm payrolls was a miss, and there were downward revisions for the prior two months totaling 74,000.
- So now the payroll growth rate is precisely what it was last year and the year before (please see the chart below). *Where's that second-half growth acceleration we keep hearing about?*
- The unemployment rate fell to a new cycle low of 7.3%. But that's only because 312,000 persons left the workforce, bringing the labor force participation rate to a new cycle low of 63.2%. If we were to normalize for labor force participation, the unemployment rate would actually be 12.8% (see "Data Insights: Jobs" September 6, 2013).
- *On the face of it, this keeps us perfectly on-trend to hit the Fed's so-called "Evans Rule" 6.5% unemployment rate threshold in*

Non-farm payrolls, sequential month growth rate

From Great Recession trough, by year ending June

2009-2010 — 2010-2011 — 2011-2012 — 2012-2013 ◆ 2013-2014 data



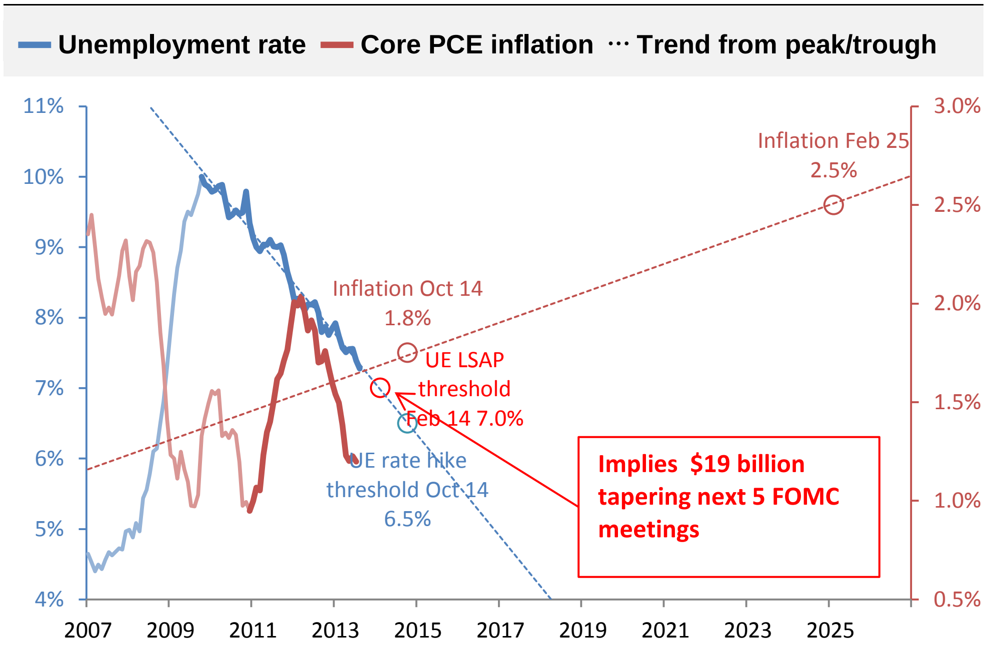
Source: BLS, TrendMacro calculations

Update to strategic view

US MACRO, US FED: Another disappointing jobs report -- yet perfectly in-line with the labor market trends dominating the four-plus years of the Not So Great Expansion. The drop in the unemployment rate keeps the existing trend perfectly intact, pointing to reaching the Fed's "Evans Rule" threshold of 6.5% in October 2014, and the 7% threshold for terminating LSAPs in February. But the politics of choosing Ben Bernanke's successor -- and the flare-up geopolitical risk in the Syria strike decision -- may well cause the Fed to stand pat and not commence tapering at the upcoming September FOMC, instead opting to wait one or even two more meetings.

[Strategy Dashboard home]

October 2014 (please see the chart below). This very durable trend brings the unemployment rate to 7.0%, where Large-Scale Asset Purchases are said to end, in February. *If LSAP tapering begins at the September FOMC meeting and is equal across future meetings, this implies $19 billion in tapering each meeting, concluding at the March 2014 meeting.*



Source: BLS, BEA, TrendMacro calculations

- Yes, one could argue that the Fed will defer the onset of tapering past the September FOMC meeting in light of today's poor data. *But the most important aspect of today's data is that it is not different at all.* Remember, last month's report was a miss, too (see "On the July Jobs Report" August 2, 2013).
- As we keep saying, labor market trends in the Not So Great Expansion have been quite consistent -- and it has been against this dreary background that the Fed has announced and repeatedly reaffirmed its intention to taper LSAPs. Nothing in the trends has changed, so why should the Fed's plans change?
- Remember, the whole point of QE3 was an insurance policy against systemic risk, which was regarded an unacceptably high a year ago (see "Rethinking QE3" September 18, 2012). Those risks have receded, so QE3 can be tapered and terminated (see, among many, "No Guns this August" August 19, 2013).
- All that said, there's nothing in that framework that insists that tapering begin at the upcoming September FOMC, as opposed to a meeting later. To be sure, the September meeting is a particularly convenient one, with its scheduled post-meeting press conference at which Bernanke could explain the nuances of what will be seen as a momentous step. The next FOMC meeting with a scheduled press conference isn't until December, a full three months later --

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On the web at
trendmacro.com

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Donald Luskin
Chicago IL
312 273 6766
don@trendmacro.com

Thomas Demas
Charlotte NC
704 552 3625
tdemas@trendmacro.com

Lorcan Roche Kelly
Sixmilebridge Ireland
617 600 6969
lorcan@trendmacro.com

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Recommended Reading

Fiscal Policy and Monetary Policy: Restoring the Boundaries
by Charles I. Plosser
Federal Reserve Bank of Philadelphia Annual Report
September 4, 2013

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perhaps too long to wait for tapering to begin, and then requiring a more rapid pace of tapering.

- Nevertheless, there are two reasons to think that the Fed may decide to sit this one out.
- With the nomination of Bernanke's successor as Fed chair still unannounced, the FOMC may wish to emphasize continuity and not make any headline-grabbing changes. We believe the FOMC would be delighted with familiar and well-liked Vice-Chair Janet Yellen at the helm. And it has great trepidation about the prospect of Larry Summers, an unknown, an outsider, something of a bully, and a threat to the Fed's independence (he would be the first former Treasury secretary to chair the Fed). *So why taper now, and give Summers an issue with which he can wage his backroom campaign for the chairmanship?*
- Second, if the main purpose of QE3 was to insure against systemic risk, then perhaps *this isn't the precise moment to go uninsured -- facing the political and geopolitical unknown unknowns that could flow from the present debate about striking Syria* (see "A Little Distant Gunfire" August 29, 2013).

Bottom line

Another disappointing jobs report -- yet perfectly in-line with the labor market trends dominating the four-plus years of the Not So Great Expansion. The drop in the unemployment rate keeps the existing trend perfectly intact, pointing to reaching the Fed's "Evans Rule" threshold of 6.5% in October 2014, and the 7% threshold for terminating LSAPs in February. But the politics of choosing Ben Bernanke's successor -- and the flare-up geopolitical risk in the Syria strike decision -- may well cause the Fed to stand pat and not commence tapering at the upcoming September FOMC, instead opting to wait one or even two more meetings.