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TRENDMACRO LIVE!

On the September Jobs Report

Friday, October 2, 2015

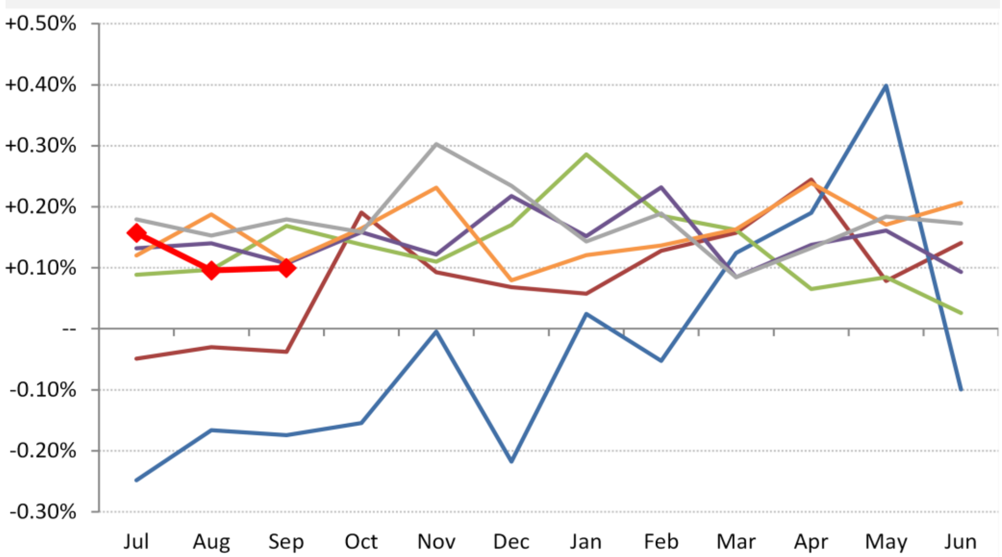
Donald Luskin

A big blow to the labor market, and an even bigger blow to what's left of the Fed's credibility.

This morning's September Employment Situation report was a huge miss. The headline 142,000 net payrolls missed consensus by 59,000 -- and then on top of that, August and July were revised down by 37,000 and 22,000 respectively. *Altogether, that's a miss of 118,000 payrolls. It supports our growing belief that the US economy has already begun to slip into the fist-ever recession caused by low oil prices* (see, among many, "Another 'Reverse Oil Shock'?" Tuesday, July 28, 2015).

- This big miss puts this seventh year of the Not So Great Expansion following the Great Recession, at best, in the middle of the pack in terms of payroll growth (please see the chart below).
- It is a strong rebuke to the Fed, from whom virtually every spokesman since the September FOMC has insisted that "lift off" will come "later this year."
- Chair Janet Yellen herself said in a speech last week, "labor market conditions will improve further as we head into 2016." Besides being wrong, during that speech Yellen became visibly ill, raising

Monthly payroll growth in post Great Recession expansion, starting July
2009-10 10-11 11-12 12-13 13-14 14-15 2105-16



Source: BLS, TrendMacro calculations

Update to strategic view

US MACRO, US FED: With a big headline miss and large downward revisions, this morning's payrolls fell short of consensus expectations by 118,000. This makes the Fed's relentless posturing of "liftoff" coming "later this year" both wrong and ridiculous, and the Fed can afford to be neither. This bolsters our concern that the US economy has slipped into the first-ever recession caused by low oil prices. The Fed's credibility-destroying wrong-headedness in the face of this reality is making matters worse. We continue to think that QE4 is more likely than "liftoff" at this point -- with the key question being when the Fed will admit it.

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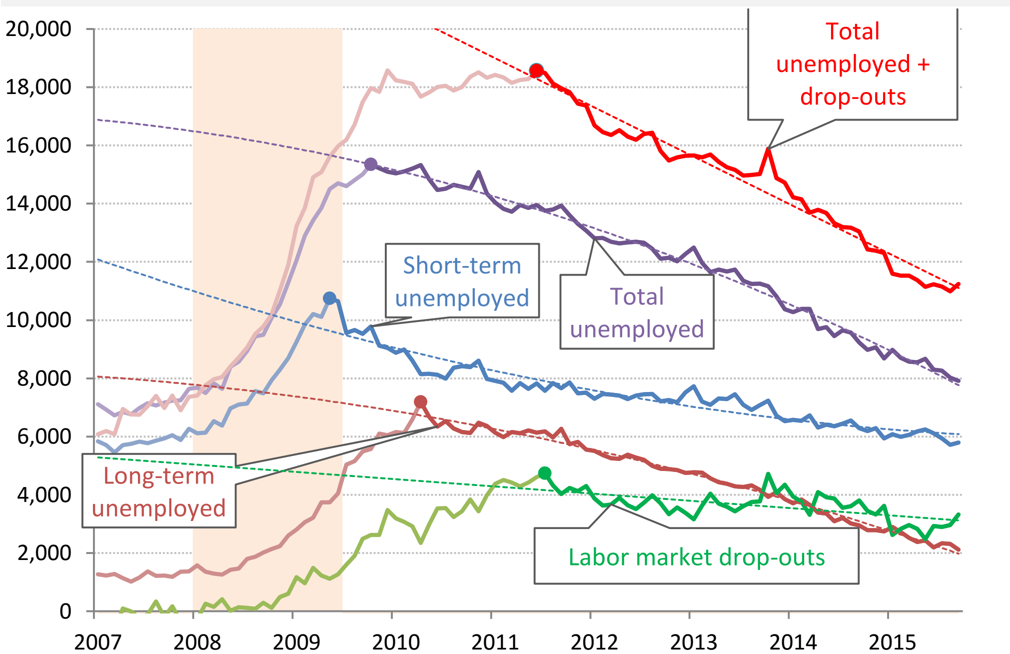
questions of competency and succession on top of the already urgent matter of why -- *dear God, why?* -- would the Fed hike rates in the face of a soggy labor market and what it itself admits are deteriorating long-term inflation expectations (see "On the September FOMC" September 17, 2015)?

- Facing such questions -- and impugning the Fed's credibility -- markets since the September FOMC have never assigned a majority probability to a rate hike in 2016, no matter what Fed spokespersons have said. As of this writing, markets assign only a 28% probability of "liftoff" for "later this year." Even as far out as April 2016 the probability is only 54%.

The headline miss, and the revisions, don't begin to capture the full awfulness in the details of this jobs report (see "Data Insights: Jobs" October 2, 2015).

- The labor force participation rate fell to a new cycle low at 62.4%, a rate not seen since 1977.
- That's because 350,000 persons left the labor force, about a third of them having been unemployed.
- The number of persons unemployed short-term rose -- while the number of persons unemployed long-term fell, suggesting that the drop-outs from the labor force were dead-enders who had finally given up (please see the chart below).
- As a result of a shrinking labor force, the unrounded unemployment rate *fell* six-tenths of a percent. This would seem to show the labor market improving, but all it shows is how the unemployment rate has become an increasingly useless indicator. It wasn't even three

Unemployment and drop-outs — Level • Peak ⋯Trend from peak
SA, thousands Underemployment = labor force vs 20-year trend **Recession**



Source: Bureau of Labor Statistics, NBER, TrendMacro calculations

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Recommended Reading

What is a Sustainable Public Debt?
Pablo D'Erasmo, Enrique G. Mendoza and Jing Zhang
NBER Working Paper 20574
September 2015

How low can you go?
Andrew G. Haldane
Bank of England
September 25, 2015

What Does Probability Mean in Your Profession?
Ben Orlin
Math with Bad Drawings
September 23, 2015

[Reading home]

years ago that the FOMC, guided by Yellen who then chaired the Communications Subcommittee, established the so-called "Evans Rule," enshrining 6.5% unemployment as the trigger for "liftoff." Then, the FOMC's economic projections set 5.5% unemployment as "normal" in the "longer run." Now the bar has had to be lowered -- the FOMC projections say 4.9%.

- Average hourly earnings were flat.
- Aggregate hours worked fell by 0.2%.

It must be said that were a few bright spots.

- The percentage of persons working involuntarily part-time fell to 4.1%, a cycle low.
- Both the "outflow rate" *from* unemployment, and the "inflow rate" *to* unemployment increased slightly, suggesting that a bit more dynamism is returning to the labor market, even as it cools off overall. Perhaps that's one of the positive dimensions of lower energy prices.

Now the question is how and when the Fed will own up to these realities, admit that they have been wrong, and start to bend their policy-guidance narrative away from "liftoff" and toward "whatever it takes." We reiterate our belief that, as this point, QE4 is more likely than "liftoff." We just need the Fed to admit it.

Bottom line

With a big headline miss and large downward revisions, this morning's payrolls fell short of consensus expectations by 118,000. This makes the Fed's relentless posturing of "liftoff" coming "later this year" both wrong and ridiculous, and the Fed can afford to be neither. This bolsters our concern that the US economy has slipped into the first-ever recession caused by low oil prices. The Fed's credibility-destroying wrong-headedness in the face of this reality is making matters worse. We continue to think that QE4 is more likely than "liftoff" at this point -- with the key question being when the Fed will admit it.