

TRENDMACRO LIVE!

On the December Jobs Report

Friday, January 6, 2017

Donald Luskin

The Fed says it's tolerant of an "undershoot" in unemployment – which we now don't have.

[This morning's December Employment Situation report](#) was a miss, with 156,000 net payrolls versus consensus 178,000. According to our model, this miss is about in line with other contemporaneous labor market indicators; it is the consensus that was out of line. There was a modest upward revision of 19,000 net payrolls across the two prior months.

- The immediate market reaction is focusing on the 0.4% increase in average hourly earnings, which supposedly the Fed focuses on to detect so-called "wage pressure." We don't see anything especially outstanding about this number, especially as it follows a reading of -0.1% last month.
- But it was a beat versus 0.3% consensus, and enough to nudge 3-year forward market-implied expectations for the funds rate higher by about 10 basis points. Don't panic. That's just back to where expectations were *before* the Fed hikes rates in December (see ["On the December FOMC"](#) December 14 2016).
- *Looking beyond that one number, this jobs report actually had more for doves to get excited about.*
- According to the "household survey," there were only 62,000 net new jobs in December. If the "household survey" data were tabulated on the same basis as the "payroll survey" that produces the headline numbers, that would be a loss of 685,000 jobs.
- The unemployment rate ticked up to 4.72% from 4.65% as 184,000 persons entered the labor force, two-thirds of whom weren't able to immediately find a job.
- The probability of finding a job within a month (the "outflow rate from unemployment" fell sharply, from 35% to 30% (see ["Data Insights: Jobs"](#) January 6, 2017).
- *All of this must be put carefully in context with how the Fed is actually looking at the labor market now, in terms of producing a policy signal!*
- [The minutes of the December FOMC](#) recorded that "...with inflation still below the Committee's 2 percent objective, it was noted that downside risks to inflation remained and that a moderate undershooting of the longer-run normal unemployment rate could help return inflation to 2 percent."
- *But having said that there is tolerance for some "undershoot" on unemployment, there is now in fact no "undershoot" to be tolerant*

Update to strategic view

US MACRO, US FED:

Following a miss in net payrolls this morning, markets have focused on the hawkish implications for the Fed of the beat in average hourly earnings – which we think should not have been a surprise considering last month's negative reading. Overall this report had more for the doves. The "household survey" showed only 62,000 net new jobs, and a loss of 685,000 on a "payroll basis." The unemployment rate ticked up as the labor market expanded, with most new entrants unemployed. The probability of finding a job fell sharply. The Fed has now said it is tolerant of an "undershoot" in unemployment, but now at 4.72%, the unemployment rate is within the Fed's normal range of 4.7% to 5.0%.

[\[Strategy dashboard\]](#)

of. With the unemployment rate at 4.72%, it is within [the FOMC's definition of "longer-run normal unemployment."](#) which is a range from 4.7% to 5.0%.

Bottom line

Following a miss in net payrolls this morning, markets have focused on the hawkish implications for the Fed of the beat in average hourly earnings – which we think should not have been a surprise considering last month's negative reading. Overall this report had more for the doves. The "household survey" showed only 62,000 net new jobs, and a loss of 685,000 on a "payroll basis." The unemployment rate ticked up as the labor market expanded, with most new entrants unemployed. The probability of finding a job fell sharply. The Fed has now said it is tolerant of an "undershoot" in unemployment, but now at 4.72%, the unemployment rate is within the Fed's normal range of 4.7% to 5.0%. ▶

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Recommended Reading

[The House GOP's Good Tax Trade-Off](#)

Martin Feldstein
Wall Street Journal
January 6, 2017

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