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TRENDMACRO LIVE!

On the May Jobs Report, and Our 2020 Election Model

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Donald Luskin

The V-shaped recovery is showing even in this lagging data. Not enough for Trump, though.

This morning's May Employment Situation report was a shocking and wonderful "beat" by 10 million payrolls – a gain of 2.5 million versus a consensus expectation for a loss of 7.5 million. The unemployment rate fell from 14.7% to 13.3%, versus a consensus expectation for a rise to 19%. Some of the beat was enabled by sharp downward revisions of 669,000 payrolls to last month's April report (see "On the April Jobs Report, and Our 2020 Election Model" May 8, 2020). *But let's not get lost in the details – the V-shaped recovery we've been enthusiastically expecting is underway* (see, among others, "After the Crisis, the Work Begins" May 4, 2020).

We knew it was going to be a beat – not this much of one, of course – based on other contemporaneous higher-frequency labor market indicators. For two weeks we've been pointing to the turnaround in jobless claims (see, most recently, "Data Insights: High-Frequency Post-Virus US Recovery Monitor" June 4, 2020). *The unemployment rate reported today is close to the implied rate from claims. Nevertheless, this morning's report is a shocker, even though it surely reflects a lot of noise in the data,*

Update to strategic view

US MACRO, US ELECTION MODEL: A shocking beat, 2.5 million net payrolls gained versus consensus for 7.5 million lost. This confirms higher-frequency data such as claims that have shown sharp improvements in the labor market for two weeks. The unemployment rate fell despite 1.7 million workers entering the labor force. Average earnings fell as low-wage laid-off leisure, health care and retail workers got…

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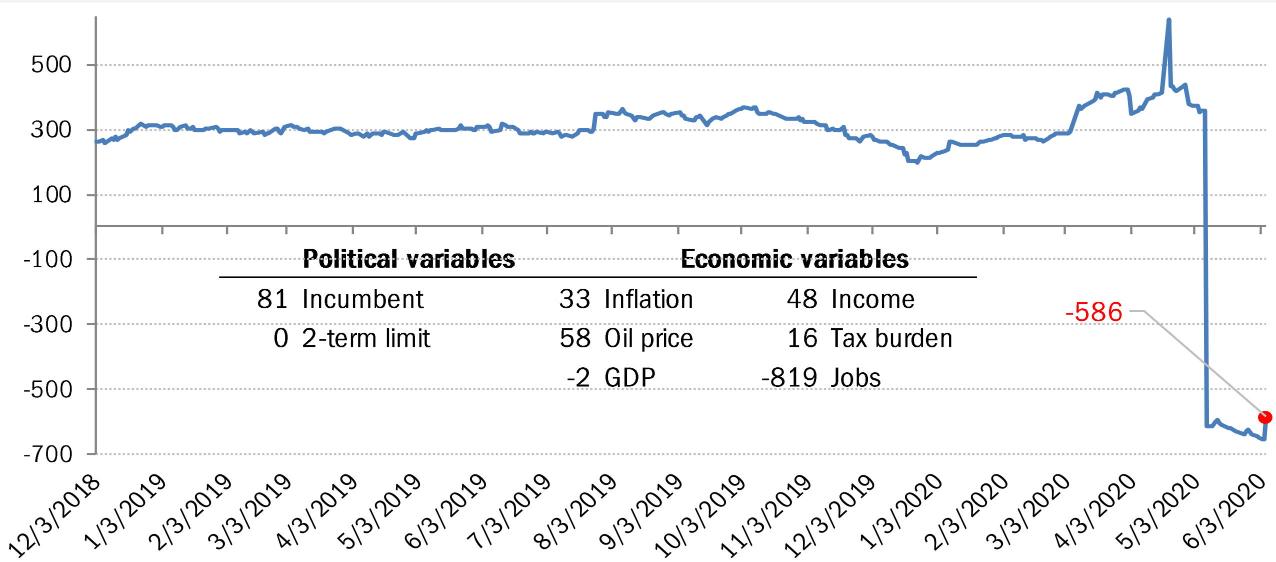
TrendMacro 2020 presidential election prediction model: margin in electoral college votes for incumbent party



Source: BLS, BEA, Bloomberg, TrendMacro calculations *improvised methodological changes, and shortfalls in the Bureau of Labor Statistics collection methods during the Covid-2019 lockdown.*

- As great as the difference may be between expectation and announcement, and as large as the 2.5 million payroll gain is anyway, it nevertheless leaves a great deal of damage in the labor market. In the context of the prior two months' horrific payroll losses, in our quantitative presidential election prediction model (see "Inside Our 2020 Presidential Election Prediction Model" March 18, 2019), *this morning's report only earns back President Donald J. Trump 70 electoral college votes, leaving him still very much the underdog.* (please see the chart on the previous page).
- But as we explained last month, our model has been pretty much broken by the high velocity and high magnitude of change in its economic input variables (again, see "On the April Jobs Report, and Our 2020 Election Model"). The model's estimate now makes little sense – it shows Biden winning by more electoral college votes than there even are.
- Ultimately what will matter is the state of the economy on election day. While things will be very much on the upswing, they will also be far below the wondrous levels seen at the peak in the first quarter. *To the extent that voters will determine whether to re-elect Trump based on the economy in the first place, they will have to decide whether to reward him for the upswing from the second quarter, or punish him for the drop from the first quarter.*

Let's turn back to the jobs report itself and consider a few interesting highlights.

- The fall in the unemployment rate, from 14.7% to 13.3%, was achieved the best possible way – it was *not* due to a contraction in the labor force. Instead, it was derived from a gain in employment of 3.8 million jobs, offset by a loss of 2.1 million – with *that net gain of 1.7 million perfectly matched by an expansion of the labor force, that is, workers returning not just to employment from unemployment, but to the labor force from outside it*.
- Average hourly earnings fell sharply despite major payroll gains – or, actually, *because* of them. 65% of payroll gains were bounce-back in the hard-hit leisure, health care and retail sectors, which are the lowest-paying.
- *This underscores our observation that the lockdowns in response to the Covid-2019 pandemic were hardest on the lowest-paid lowest-scale employment sectors – a pool of fungible human capital which, not to be dismissive of these workers as individuals – can easily be laid off and rehired, and easily compensated in the meantime by government relief programs. We believe the inherent flexibility in this sector of the labor market is a source of resiliency as we come out of lockdown* (again, see "After the Crisis, the Work Begins").
- What labor economists call the "inflow rate to unemployment" – which can be understood as the probability of losing your job in a given month – has repaired itself from last month's horrific record

Update to strategic view

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… re-hired. This large low-skill sector of the labor force is fungible human capital, easy both to fire and re-hire, and compensate in the meantime with government aid programs. This gives the US economy a great deal of resiliency in enduring a brief but deep recession. Today's payroll gains only marginally helped Trump's re-election prospects, according to our model.

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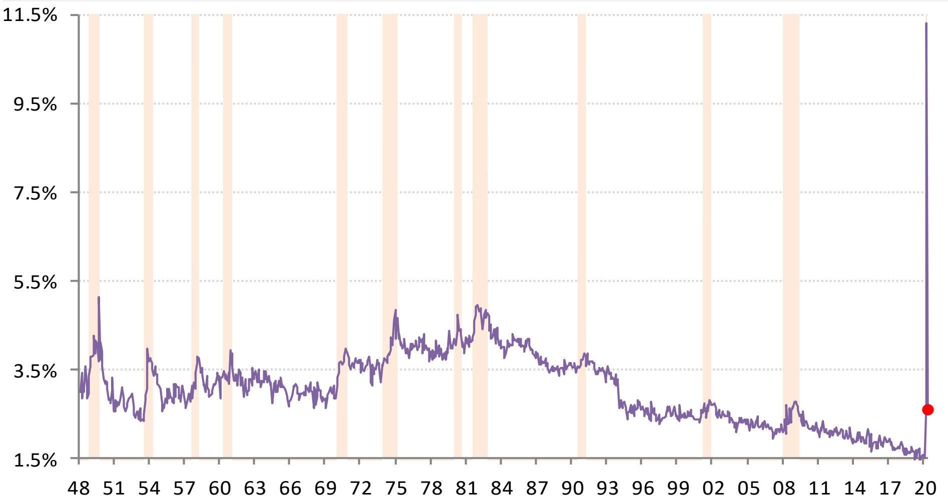
level of 11.3%. It has fallen to 2.6%, which is *consistent with peak levels seen in the prior two recessions – bringing the present crisis into perspective as pretty much just what recessions look like*. At least modern recessions. The "inflow rate" is now actually lower than rates seen in most business cycle *expansions* up through the 1990s (please see the chart below, and "Data Insights: Jobs" June 5, 2020).

The "inflow rate to unemployment" (1-month separation probability) Recession



Source: BLS, per Shimer 2005, TrendMacro calculations

- Similarly, the "outflow rate from unemployment" – the probability of getting a job in a given month – recovered from last month's horrific *negative* 23% (yes, a negative probability reflects a labor market so desperately bad that it broke our model). Now it has bounced back to 26% – which is actually better than it was in much of the prior business cycle expansion.

Bottom line

A shocking beat, 2.5 million net payrolls gained versus consensus for 7.5 million lost. This confirms higher-frequency data such as claims that have shown sharp improvements in the labor market for two weeks. The unemployment rate fell despite 1.7 million workers entering the labor force. Average earnings fell as low-wage laid-off leisure, health care and retail workers got re-hired. This large low-skill sector of the labor force is fungible human capital, easy both to fire and re-hire, and compensate in the meantime with government aid programs. This gives the US economy a great deal of resiliency in enduring a brief but deep recession. Today's payroll gains only marginally helped Trump's re-election prospects, according to our model.