Trend Macrolytics, LLC
Donald Luskin, Chief Investment Officer
Thomas Demas, Managing Director
Michael Warren, Energy Strategist

TRENDMACRO LIVE!

On the June Jobs Report

Friday, July 8, 2022

Donald Luskin

How can the Fed believe the labor market is tight when payrolls keep growing like this?

This morning's June Employment Situation report with 372,000 net payrolls beat the consensus for 268,000, despite downward revisions to April and May of 74,000. Our model based on contemporaneous labor market indicators was expecting only 133,000 (see "Data Insights: Jobs" July 8, 2022). And employment in the "household survey" contracted by 315,000.

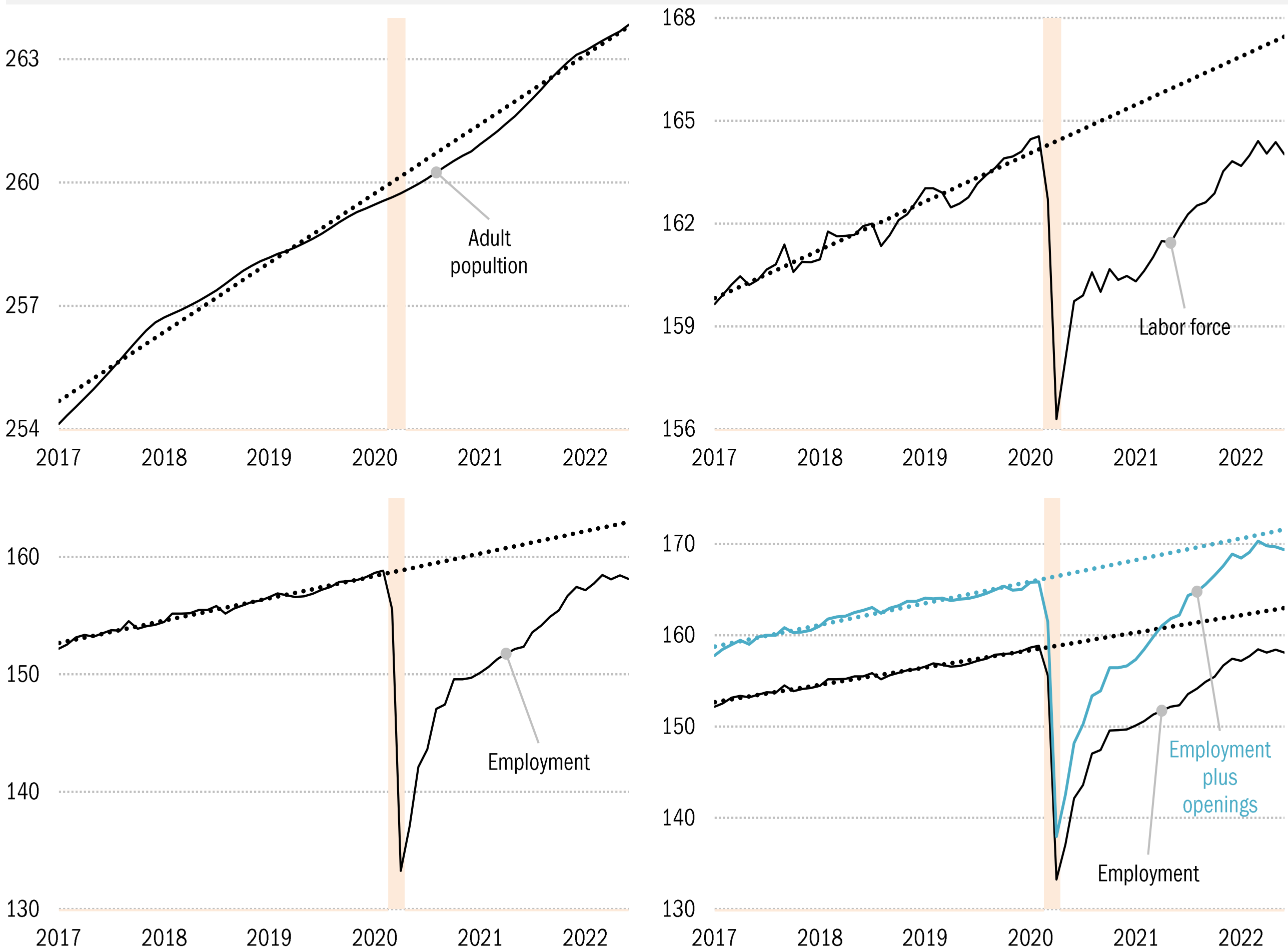
But the "household survey" and the "payroll survey" have contradicted

Update to strategic view

US MACRO, FEDERAL RESERVE: Another very strong jobs report in an…

[Continued on next page]

Labor market in the pandemic era (millions, revised for annual population controls) ••• Pre-pandemic trend Recession



Source: BLS, TrendMacro calculations

each other (in both directions) plenty this year. So let's take the payroll data at face value.

Payrolls expanded in every sector, which is unusual. This very strong report is in line with a string of strong ones this year, averaging 457,000 per month. The background growth rate of the adult population is 90,000 per month so this *continues to be evidence that, despite all appearances and despite Fed Chair Jay Powell's rhetoric* (see "On the June FOMC" June 15, 2022), *the labor market isn't really all that tight* (a tight labor market just couldn't continue to rack up payroll gains like this).

This would seem to not point to any risk of recession – at least not an endogenously caused one (the National Bureau of Economic Research relies primarily on labor market data to officially call a recession). *The problem is that the Fed seems bound and determined to exogenously cause a recession based on a cascade of false beliefs that (1) the labor market is too tight; (2) this leads to inflation; and (3) the Fed can fix the inflation by damaging the labor market.*

- Let's review where we are *really* at in the labor market, and what is making it possible to have this continuing string of great jobs reports. [The numbers we will now present may differ from data provided by the Bureau of Labor Statistics; their numbers are not backwardly revised to reflect annual adjustments for "population controls," making comparisons across more than a single year inaccurate; we have implemented the backward revisions ourselves so, yes, our numbers are better than their numbers.]
- *First, the adult population from which the labor market draws, at 264 million, is slightly above the pre-pandemic trend* (please see the upper left chart on the first page). This is despite over a million deaths attributed to Covid over the last 28 months (please see "Data Insights: Covid-2019 Monitor" July 8, 2022).
- *Second, the labor force at 164 million is still 527,000 below the pre-pandemic level, and 3.8 million below the pre-pandemic trend* (please see the upper right chart on the previous page). Yes, we know the standard explanation for this is a wave of pandemic-inspired retirements. There isn't good data on that, but even the most generous estimates we've seen don't fully explain the problem anyway.
- *Third, employment at 158 million is 725,000 below the pre-pandemic level, and 5.2 million below the pre-pandemic trend* (please see the lower left chart on the previous page). So even granting the shrinkage of the labor force in absolute and trend-relative terms, that shrunken labor force is not being fully utilized.
- That said, even assuming two weak quarters this year, *US GDP stands about 2% above its pre-pandemic level in real terms – so with employment 3.0% below trend, we are in a productivity boom*.
- *Fourth, job openings are near an all-time record at 11.3 million, 4.2 million above their pre-pandemic level and 3.2 million above the pre-pandemic trend.*
- *But the sum of employment and job openings – the potential size of the working labor market – at 169 million is 3.5 million above the*

[Continued from first page]

…unbroken string this year, demonstrating that the labor market is nowhere near as tight as the Fed believes it is. A tight jobs market cannot produce payroll gains like this, extending to all sectors this month. The labor force and the level of employment are below their pre-pandemic peaks, and further below the pre-pandemic trend, pointing to remaining millions who could come back to work (estimates of early retirement do not explain this away). Powell is focusing on the large number of unfilled job openings as a source of inflationary wage pressure, though he admits wages haven't caused inflation. He believes that higher rates will eliminate openings, not jobs. Yet the "dots" from the June FOMC imply a baseline assumption that 800,000 jobs will be lost. Openings have already fallen the last two months; this has always been an early warning on recession, with openings falling ahead of actual employment. Inflation has been caused by a jump in the money supply caused by pandemic relief spending. That spending has ended, and core inflation is already falling.

[Strategy Dashboard home]

pre-pandemic level, yet 2.0 million below the pre-pandemic trend (please see the bottom right chart on the previous page).

- *That's right – for all the job openings, the potential size of the working labor market is below trend. Yet the Fed seems to have made a mission of knocking it even further below*.
- As Powell explained it in the post-FOMC press conference in March:

  "…if you add job openings to those who are employed, that's actually substantially a larger number than the size of the workforce, than the number of people who actually count themselves as in the workforce. So this is a situation where demand is higher than supply. And when that happens, prices go up."

- Of course by "prices" he means wages:

  "…we're trying to better align demand and supply…in the labor market. So … if you were just moving down the number of job openings so that they were more like one to one, you would have less upward pressure on wages."

- *There you have it: the Fed is by its own admission trying to reduce the number of job openings, that is, to reduce the quantity of opportunity for economic growth and personal advancement in the economy.*
- *But to what end? Powell himself admitted at the post-FOMC presser in June,*

  "Wages are not principally responsible for the inflation that we're seeing…"

- Be that as it may, so far so good – or so bad – on the Fed's mission. The most recent Job Openings and Labor Turnover Survey (JOLTS) shows the second sequential monthly decline in job openings, from 11.8 million in March to 11.7 million in April to 11.3 million in May. *That's 601,000 potential jobs eliminated.*
- *JOLTS openings have a perfect record of peaking before every recession*, in advance of the peak in jobs (in the 2001 recession it was by 2 months, 2008 by 8 months and 2020 by 1 month). *So while today's jobs numbers surely don't point to the immediate onset of a recession, the drop in openings is certainly a warning shot.*
- Powell seems to believe that the record high ratio of openings to actual jobs gives him the opportunity to cool the labor market (and cool wage growth, even though he admits it hasn't contributed to inflation), without actually throwing people out of work (instead, to throw out their opportunities for future work).
- Yet in the June FOMC's Summary of Economic Projections, FOMC participants upgraded their central estimate of the 2024 unemployment rate from 3.6% in March to 4.1%. *Just so we're*

Contact TrendMacro

On the web at
trendmacro.com

Follow us on Twitter at
twitter.com/TweetMacro

Donald Luskin
Dallas TX
214 550 2121
don@trendmacro.com

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

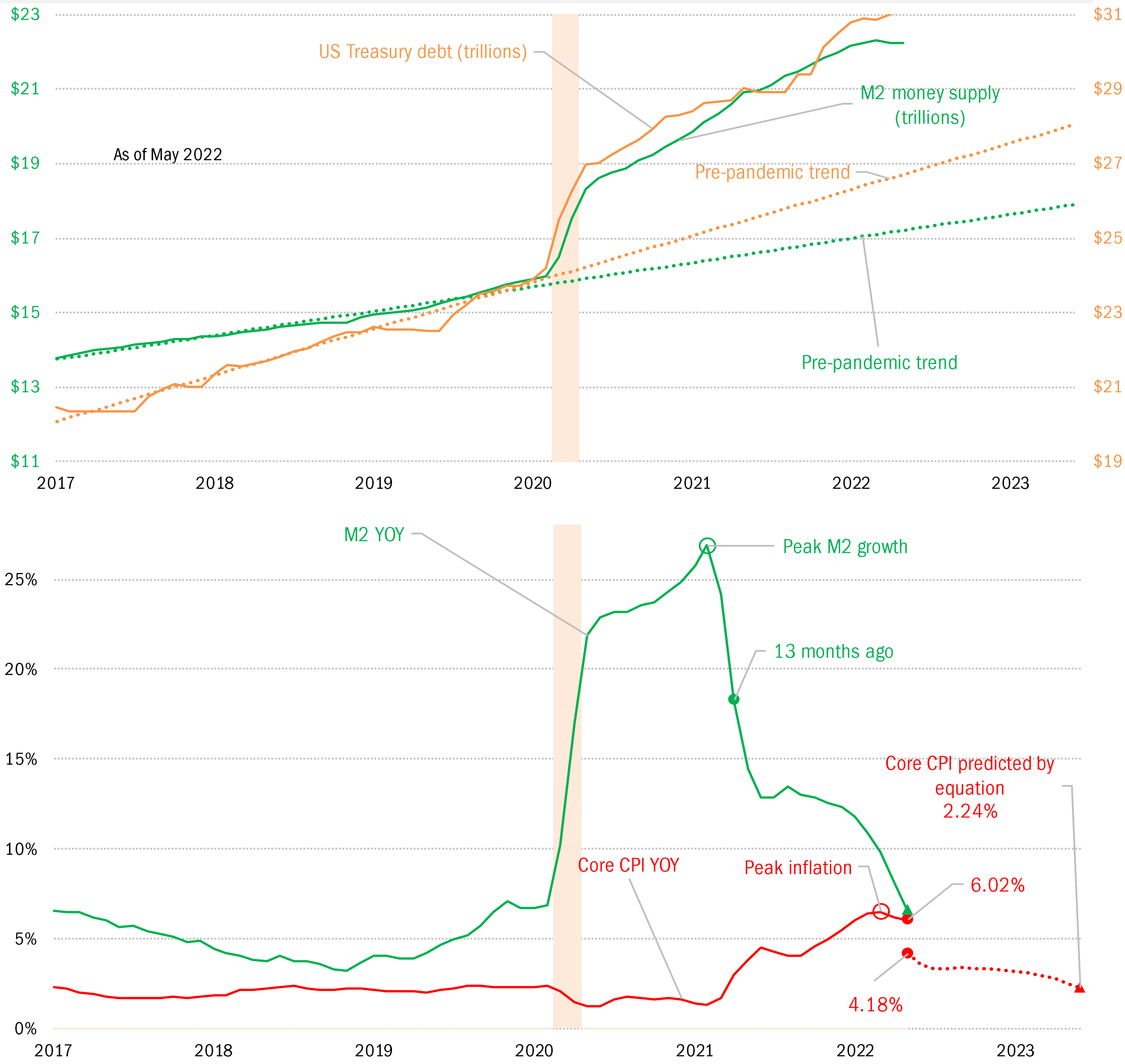
Michael Warren
Houston TX
713 893 1377
mike@trendmacro.energy

[About us]

clear, that half-a-percent increase in the unemployment rate throws 800,000 real people out of work – and that's assuming a soft landing.

- *Meanwhile, the post-pandemic inflation we're experiencing now, while pernicious in many ways, has nevertheless co-existed with an unemployment rate near the lowest in two generations, and the largest sum of jobs and jobs openings in history*. So rather then reduce the number of potential and actual jobs, why not let a growing economy lure more workers back into the labor force?
- *All the more so considering that we know for certain the inflation*

Relation of Treasury debt, M2 money supply and core CPI inflation rate



Source: Bloomberg, TrendMacro calculations *we're experiencing now is the straightforward consequence of $6 trillion in pandemic spending, which fed directly into an identical – and largest in history – increase in the money supply* (please see the charts on the previous page, and [“Video: What you're not hearing about what caused today's inflation, and where it's going”] June 9, 2022).

- *That, in turn, caused the inflation we are experiencing now with a statistical certainty that cannot be denied.*
- *That spending has ended. M2 growth has fallen back to normal levels after its record peak in February 2021. The 13-month lag between M2 growth and inflation caused core inflation to peak in March this year. Now if that lag in transmission from M2 to inflation continues to hold, inflation will be back at target levels near 2% about a year from now.*
- *All the Fed has to do now is nothing. And nobody has to lose their job…*

Bottom line

Another very strong jobs report in an unbroken string this year, demonstrating that the labor market is nowhere near as tight as the Fed believes it is. A tight jobs market cannot produce payroll gains like this, extending to all sectors this month. The labor force and the level of employment are below their pre-pandemic peaks, and further below the pre-pandemic trend, pointing to remaining millions who could come back to work (estimates of early retirement do not explain this away). Powell is focusing on the large number of unfilled job openings as a source of inflationary wage pressure, though he admits wages haven't caused inflation. He believes that higher rates will eliminate openings, not jobs. Yet the “dots” from the June FOMC imply a baseline assumption that 800,000 jobs will be lost. Openings have already fallen the last two months; this has always been an early warning on recession, with openings falling ahead of actual employment. Inflation has been caused by a jump in the money supply caused by pandemic relief spending. That spending has ended, and core inflation is already falling.