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TRENDMACRO LIVE!

On the May Jobs Report

Friday, June 2, 2023

Donald Luskin

It's easy to square big payroll gains with big employment losses. And it's bullish.

The big beat in net payrolls this morning – 339,000 versus a consensus for 195,000 – and what's more, that on the back of upward revisions of 93,000 to the previous two months – is astonishing. But there is an apparent conundrum at the same time: employment, as measured in the alternate Current Population Survey – the "household survey", fell by 310,000. With 130,000 new entrants to the labor market, that means the number of unemployed rose by 440,000 – and the unemployment rate rose from 3.44% to 3.65%, the biggest jump since the 2020 lockdowns.

- It's important to square this circle because continuing jobs gains are the *sine qua non* of a continuing business cycle expansion (see "Video: What you're not hearing about the recession signal in temporary payrolls" January 30, 2023).
- *We think the strong gains in the Current Employment Statistics survey – the "establishment survey," or the "payroll survey" – are painting a truer picture of the jobs situation.* We'll get to what this means for the Fed in a moment.
- First, the payroll survey results more closely match the estimate of

Generative AI token: "Payrolls way up employment way down. Why the contradiction? Which is right? Cinematic style"

Source: DreamStudio running SDXL beta

Update to strategic view

US MACRO, FEDERAL RESERVE: A huge payroll beat stands on the shoulders of upward revisions to the prior two months. But the household survey showed almost as many employment losses as the payroll survey showed gains. The payroll survey's result is more consistent with our model based on other contemporaneous labor market indicators. And when the household survey is re-tabulated on a payroll basis, the employment gains are even larger than the payroll gains. We are confident that the household survey is not indicative of the onset of recession. Powell and Jefferson have signaled unambiguously there will be no rate hike at the June FOMC, styling it as a "skip." This morning's jobs data doesn't change that, with the Fed focusing on the unemployment rate, which rose, and wage gains, which cooled. There will be no hike in June. It won't be a skip. It will be the end.

[Strategy dashboard]

our model based on a panoply of contemporaneous labor market indicators (to see the components, see "Data Insights: Jobs" June 2, 2023). That model had estimated 207,000 net payrolls. The actual number – at 399,000 – was a big beat to the model, but the model was very much directionally correct.

- Second, the payroll survey and the household survey are not only entirely different data-sets, but they are also tabulated differently. The former counts payrolls, the latter counts employment (so among several consequences, an "employed" person could have more than one "payroll"). When the employment loss of 310,000 in the household survey is retabulated on a payroll basis, that loss is transformed into a *gain* of 394,000.
- *We are confident that the employment losses in the household survey are not indicative of the end of this business cycle expansion or the onset of recession.*

How will all this affect the Fed, heading into the June FOMC the week after next?

- Chair Jerome Powell was clear – well, as clear as he ever is – in his panel discussion with former chair Ben Bernanke two weeks ago when he said, "Having come this far, we can afford to look at the data and the evolving outlook to make careful assessments."
- We know he meant it because he was shamelessly reading from prepared notes in what was supposed to be a free-form discussion.
- This was reaffirmed in a speech Wednesday by Governor Philip Jefferson: "…skipping a rate hike at a coming meeting would allow the Committee to see more data…"
- That's more than just chatter from the usual publicity-mad Fed spokespeople: Jefferson has been nominated for vice chair, so surely any utterance about policy would have been cleared with Powell.
- So going into this morning's jobs data, the clear signal is that there would be no rate hike in June. *Call it a "skip." Call it a "pause." Call it an "end." But unless you think this morning's data was so scorchingly hot that it would subvert the prior pronouncements of both the chair and the vice chair-designate, there's going to be no rate hike in June*. Besides, however hot the data was, the June FOMC will take place just as May CPI data will be released, and it's as near a certainty as you can get in this field that year-over-year headline inflation will print below 4.0%, having been at 9.1% just 11 months ago. CPI will be 78% back to the Fed's target for it in less than a year. Hell yeah, as we've said already, there will be no June rate hike (see "On the May FOMC" May 3, 2023).
- *Technically, this morning's jobs data doesn't count, because it will have been acquired before the "skip" designed to allow for data acquisition.* But be that as it may, the ambiguities in this morning's data ought to keep it from being decisive.
- *The Fed does follow the unemployment rate – wedded to the obsolete and historically incorrect Phillips Curve model that low unemployment leads to high inflation. And however it may stack up against payrolls this month, it is nevertheless a self-consistent time*

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series, and in May it moved in a direction that ought to comfort the hawks.

- *Of course the Fed also follows – obsessively so – the evolution of wage growth, believing just as wrongly that it leads to inflation.* Never mind that a new paper this week from the San Francisco Fed demonstrates quantitatively that wage growth has had no material effect on the supposedly wage-sensitive services inflation that Powell mono-focuses on now. *The good news is that average hourly earnings grew only 33 bp in May, down 6 bp from an upwardly revised April, and at the bottom of the range of the last 15 months.*
- As something of a counterpoint, Wednesday's Job Openings and Labor Turnover Survey (JOLTS) report showed vacancies rising by 358,000 to 10.103 million. We know from many statements over the last two years that Powell regards this as the most important indicator of labor market tightness – which he thinks leads to wage growth, which he thinks leads to inflation.
- One cannot know how to weigh all these factors in the minds of Fed officials – but our call is that their marker is down for no hike in June and at this point it can't be withdrawn. Nick Timiraos' no doubt directly sourced story in the *Wall Street Journal*, following Jefferson's remarks, locks it in. It's a contract with America.
- And we'll have more to say on this in an FOMC preview next week, but as a preview of the preview, let us say that we think this is a "skip" in name only – to preserve options (and dignity). Inflation is rolling over hard. By early 2024 it will be outright deflation (see "Inflation Has Peaked -- Get Ready for Deflation" May 24, 2023). This is no "skip." This is the end.

Bottom line

A huge payroll beat stands on the shoulders of upward revisions to the prior two months. But the household survey showed almost as many employment losses as the payroll survey showed gains. The payroll survey's result is more consistent with our model based on other contemporaneous labor market indicators. And when the household survey is re-tabulated on a payroll basis, the employment gains are even larger than the payroll gains. We are confident that the household survey is not indicative of the onset of recession. Powell and Jefferson have signaled unambiguously there will be no rate hike at the June FOMC, styling it as a "skip." This morning's jobs data doesn't change that, with the Fed focusing on the unemployment rate, which rose, and wage gains, which cooled. There will be no hike in June. It won't be a skip. It will be the end.