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TRENDMACRO LIVE!

On the December Jobs Report

Friday, January 5, 2024

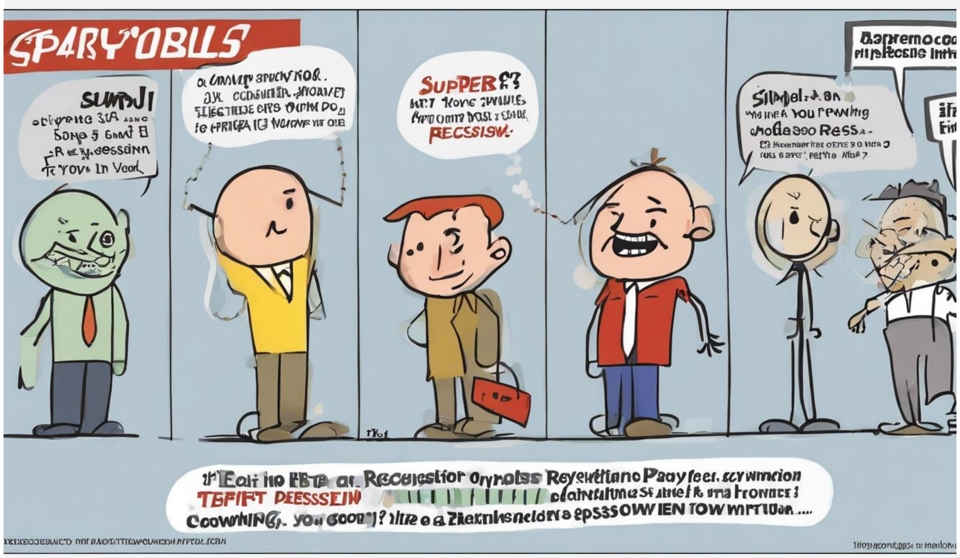
Donald Luskin

It's two labor markets in one. But for our two Feds in one, now it's all about disinflation.

Today's December 2023 Employment Situation Report with 216,000 net new payrolls beats the consensus for 175,000 and our model estimate of 168,000 based on a broad variety of contemporaneous labor market indicators (see "Data Insights: Jobs" January 5, 2024). Arguably the beat is explained away by downward revisions of 26,000 and 45,000 to November and October respectively. Also, about 20,000 payrolls are probably attributable to better-than-usual weather in December. The unemployment rate moved up ever so slightly, to 3.74% from 3.72%.

- *With something like 90,000 persons attaining working age and likely to participate in the labor force every month, 216,000 is a solid number. It's just below the average of 227,000 for the prior twelve months, and comfortably above the average of 174,000 for the past six months.*
- *Anyone waiting to see drop-dead evidence of impending recession is going to have to wait another month*. But of course the statistical waters are turbulent and muddy, so if you absolutely insist on seeing bad news here, you can find it.

Generative AI token: It's super simple. If payrolls are growing you are in an expansion. If you are in an expansion you are not in a recession. Any questions?



Source: DreamStudio running SDXL 1.0

Update to strategic view

US MACRO, FEDERAL RESERVE: A beat for payrolls at 216,000, supported by downward revisions to prior months. The "household survey" shows a stark contradiction with a contraction of 683,000 jobs, but this just unwinds last month's stark contradiction in the opposite direction. Supported by a wide variety of other labor market data, the payrolls number is about right. Revisions to seasonal adjustment factors in the "household" data are inconsequential. The Fed may focus on December's large gain in average hourly earnings, but this is contradicted by the sharp drop in jobs vacancies to below the pre-pandemic trend. At this point the Fed is likely focused exclusively on inflation data, which it already openly admits has mostly come back into line. We stand by our call for ongoing disinflation, the emergence of deflation, and the first rate cut at the March FOMC.

[Strategy dashboard]

- Employment as measured by Current Population Survey – the "household survey" fell by 683,000 – wildly contradicting the Current Employment Statistics survey – the "payroll survey" – at 216,000 net gains.
- We don't know how to tell you that's good news, because it's not. But context is everything (yes, that is a freighted word now). These two Bureau of Labor Statistics surveys – entirely separate – often give conflicting signals. Last month payrolls grew by a revised 175,000 (originally reported at 199,000) while employment grew by a revised 586,000 (originally reported at 747,00). At least last month the signs were the same, but the discrepancy was quite large. It probably doesn't mean much.
- This is why we have a model that looks at eight contemporaneous labor market statistics and produces a payrolls-equivalent estimate. Again, this month the model estimated 168,000 – adjusted for revisions, it's about perfect and it argues that *the payroll number at 216,000 is broadly consistent with reality*.
- Data nerds among you may be aware that the "household survey" this month underwent a periodic recalibration of its season adjustment factors, resulting in the revision of employment, unemployment, labor force and unemployment rate data from January 2019 to November 2023. There is no reappraisal here of the underlying data to which the adjustments are applied. And seasonal adjustment factors, by definition, sum to zero over a year – so this makes no difference in the grand scheme of things. Of the last twelve months, the unemployment rate is only changed at all in a single one – October, and by a mere one tenth of one percent (an improvement to 3.8% from 3.9%). Move along, folks.

But what will the nerds at the Fed think?

- This jobs report comes at the end of the first week of the New Year, during which a risk-back-off mood has prevailed as, for some reason, investors seem to be backing off their conviction that the first Fed rate cut will come at the March FOMC.
- In the days following the dovish December FOMC (see "On the December FOMC" December 13, 2023), the futures-implied probability for that March cut exceeded 100%. This morning before the jobs report, it was down to 68%. We're not really sure why. The absurd contradictions of Chair Jerome Powell's December dovish pivot by other Fed officials (see "It's Two! Two Feds in One!" December 15, 2023) have been in the market for three weeks. And as far as we're concerned, any reasonable reading of the minutes of the December FOMC, released Wednesday (see "Data Insights: FOMC Minutes" January 3, 2024) can only be seen as backing up Powell's stance.
- Now, after the jobs report, as of this writing, the futures-implied probability of a cut has risen to 86%, *so apparently the report was Fed-friendly* (although a miss in US services PMI might have helped – see "Data Insights: Global PMI" January 5, 2024).
- But then again who knows what motivates the Fed's seemingly arbitrary decisions at this point? Surely evolving inflation and labor

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statistics play a large role, but as far as we're concerned those statistics had already supported for several months the pivot Powell finally made in December (see "2023: Our Greatest Hits, Our Gravest Misses" December 29, 2023).

- If you insist on treating incoming labor data as algorithmically determining the Fed's stance, then you might be alarmed at the 44 bp increase in average hourly earnings in December, on top of an upwardly revised November number. This is the second largest increase over 24 months, and the largest in six months.
- On the other hand, this would seem to be contradicted by another labor statistic also thought to drive the Fed algorithmically – the number of job vacancies in the Job Openings and Labor Turnover Survey (JOLTS). Powell has argued *ad nauseam* that record levels of vacancies indicate a tight labor market, which in turn leads to wage inflation. What will he think now, with vacancies at 8.79 million, the lowest in 32 months, and 511,000 below the pre-pandemic trend – while at the same time wages have grown the second fastest in 24 months?
- To be sure, he might cling to the idea that wage growth causes consumer inflation (as you know, we disagree) – but even if he did, he'd have to see that raising rates in order to slow economic growth – and reduce those pesky jobs vacancies – wouldn't help (and might hurt). (see "2023: Our Greatest Hits, Our Gravest Misses" December 29, 2023).
- For all these considerations, we don't see this morning's jobs report as in any way decisive to the Fed. *They can see inflation as having substantially come down – they admit it openly* (again, see "Data Insights: FOMC Minutes"). *That's all they care about. The only reason they care about the labor market at all is because they believe it has been too strong, and contributed to inflation. With inflation coming down, they don't care about the labor market at all. They would only care about it again if it started falling apart and they had to rescue it.*
- *We still think the first cut will come at the March FOMC, supported by continuing great news on disinflation, beginning to verge on deflation* (see "2024: Deflation, Election, and No Recession" January 3, 2024).

Bottom line

A beat for payrolls at 216,000, supported by downward revisions to prior months. The "household survey" shows a stark contradiction with a contraction of 683,000 jobs, but this just unwinds last month's stark contradiction in the opposite direction. Supported by a wide variety of other labor market data, the payrolls number is about right. Revisions to seasonal adjustment factors in the "household" data are inconsequential. The Fed may focus on December's large gain in average hourly earnings, but this is contradicted by the sharp drop in jobs vacancies to below the pre-pandemic trend. At this point the Fed is likely focused exclusively on inflation data, which it already openly admits has mostly come back into line. We stand by our call for ongoing disinflation, the emergence of deflation, and the first rate cut at the March FOMC.