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Instant Analysis

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Instant Analysis of Today's Employment Report for August

Job Growth Slows in August; +173K vs. Consensus Exp. +217K
Unemployment Rate Drops two tenths to 5.1%
June and July Job Numbers Revised Up a Net +44K
Avg. Hourly Earnings Accelerate +0.3% (+2.2% y-o-y) Labor Force Participation Flat
Job Losses in Goods Producing Sectors- Service Sectors Solid
Business Services (+33K), Ed & Health (+62K), Leisure & Hospitality (+33K), Gov't (+33K)
Trade (+11K), Manufacturing (-17K), Information (-7K) and Construction (+3K)
September Rate Hike Still on the Table -Low Unemployment Rate Raises Probability
Market Reaction to Report; USD strengthens; S&P 500 -1.1%; 10-Yr Treasury -0.5 bps 2.15%

The August payroll was good enough to keep a September rate hike on the table though market turmoil is likely to continue and there are hints in the goods producing sectors that low oil prices and global overcapacity in manufacturing is starting to bite a bit harder. This could give a risk adverse FOMC the excuse they need to delay until December. Headline nonfarm payroll growth slipped to +173K, the lowest monthly gain since March from an upwardly revised +245K in July. However, after factoring in the net upward revisions for June and July of +44K, the 3-month moving average of monthly job gains held at a solid +221K. In short, taking a longer-term view and looking at the labor market performance over the past two years, the U.S. economy is probably strong enough to withstand the assault of an initial interest rate hike from the Fed in the absence of severe market turmoil and a global economic shock from abroad.

There is a solid case to be made that the labor market half of the Fed's mandate has been achieved and a zero interest rate policy is no longer appropriate. The drop in the headline unemployment rate to 5.1% in August from 5.3% in July was bigger than economist expected and could raise fears at the Fed that the labor market is tightening faster than forecasted and stronger wage growth won't be far behind. More FOMC members may become "reasonably confident" that inflation will return to their target over the medium-term as a result. Some may even say the Fed is behind the curve in normalizing interests. On that note, average hourly earnings growth accelerated in August up +0.3%, pushing the year-on-year gain in average hourly earnings up to 2.2%. How much longer will the Fed be able to say there are no wage pressures?

By sector, we saw job growth in most major sectors of the economy. Though job gains last month were clearly led by services businesses and government and not the goods producing sector, both manufacturing and mining lost jobs last month as low oil prices, sluggish demand from abroad, and bloated inventories weighed on activity, Education and health care led the way adding a net (+624K) jobs, while business services (+33K), government (+33K), leisure and hospitality (+33K), and finance (+19K) added a decent number of new jobs. Job growth in goods producing industries of the economy disappointed in August with manufacturing losing (-17K), mining losing (-10K) and construction (+3K). The disconnect between the services and goods sector in terms of job gains could be troubling for some doves on the FOMC, who are worried about the sustainability of labor market momentum in the face growing downside risks. Slower growth usually surfaces in cyclical industries like manufacturing before they are seen in more stable service businesses.

Bottom-line, the August jobs report was not the smoking-gun the markets were hoping for, and FOMC doves and hawks will find far different interpretations about what they see in the report. While the low unemployment rate raises the chances of a September rate hike, and will likely keep it on the table as an option, it is far from a certainty given the magnitude of recent stock declines and evidence of slowing in the manufacturing sector. A cautious FOMC could decide to remain data dependent for a few more months to see which direction the economic wind is blowing.

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