CenterState
CORRESPONDENT DIVISION

Market Update

Economic News

August 3, 2018

The July Employment Report missed on the headline jobs growth number (157,000 vs. 193,000 expected) but prior two-month revisions added 59,000 jobs and thereby more than recouping the 36,000 miss in today's report. Another positive is that the unemployment rate ticked back down to 3.9% after a brief foray at 4.0% in June. Meanwhile, what has become the key metric in the report, average hourly earnings, matched expectations and the June print with a 2.7% YoY rate. This remains shy of the 3.0%-3.5% pre-crisis levels and will have to move to those levels to spur longer-lasting demand and inflation pressure. In summary, despite the headline miss this is another solid jobs report that will keep the Fed on track for a rate hike in September. In fact, given the ongoing labor market gains and economic strength, the limiting factor to future rate hikes beyond September may be more the impact of trade actions and foreign economic trends (particularly China and Europe). For now, however, this report, and most other releases of late, will keep the Fed firmly on its quarterly hiking schedule for this year.

For the month, 157,000 jobs were created missing the 193,000 expected and below the 248,000 jobs created in June (upwardly revised from 213,000). Over the past year monthly job gains have averaged 198,000, so July's results were below that average. Private payrolls increased 170,000 versus 190,000 expected and 234,000 in June (revised up from 202,000). Two-month revisions added 59,000 jobs from prior prints, more than recouping the 36,000 miss this month. Digging into the categories, 118,000 service-providing jobs were added during the month (2/3rds of job growth) versus 182,000 in June. Gains were led by professional and business services (+51k), leisure and hospitality (+40k), and health care and social assistance (+34k). Meanwhile, 52,000 goods-producing jobs were added (1/3rd of the total) which is identical to the gain in June with manufacturing (+37k) and construction (+19k) leading the gains in that sector.

Perhaps the most important metric in the monthly jobs report are the numbers on wage gains. For July wages improved off a downwardly revised June number with both the monthly and year-over-year print matching pre-release expectations. Average hourly earnings for July increased 0.3% matching expectations but ahead of the 0.1% gain in June, which was revised down from 0.2%. Year-over-year earnings matched the June print of 2.7% which was also the consensus expectation. As has been the case in this nine-year expansion, the YoY wage gains remain shy of the 3.0% to 3.5% pre-recession rate. The Fed, and workers, want to see wage gains move back to that pre-recession rate before concluding the labor market is truly at full employment.

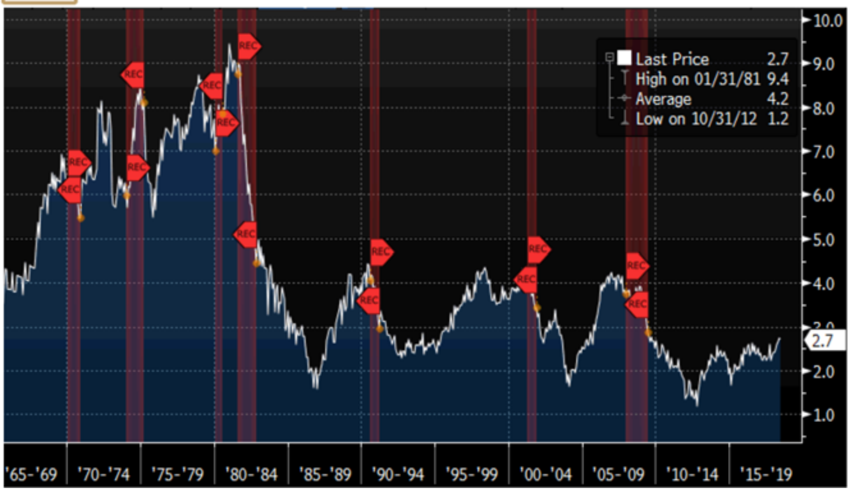
The unemployment rate, as expected, dipped 1/10th to 3.9% (3.871% to be exact) after rising from a cycle low of 3.8% in May to 4.0% in June. The rate drop stems both from a decrease in the ranks of the unemployed and also from a modest 105,000 increase in the labor force denominator, and that comes after a huge 601,000 labor force gain in June. The fact the labor force could still manage a modest gain following the huge June increase implies the strong economy is still drawing people into the labor force market, and those people, given the drop in the ranks of the unemployed, are finding jobs. That implies some slack remains, which, in turn, is probably suppressing more substantial wage gains.

The broader underemployment rate (unemployed plus part-timers seeking full-time work, plus the marginally attached divided by the labor force) dipped 3/10th to 7.5% representing a new cycle low after touching 7.6% in May. The rate drop was due to a decrease of -284,000 in the ranks of the unemployed, -176,000 in part-time workers and the aforementioned gain in the labor force denominator. Partially offsetting those positives was an increase of 61,000 in the ranks of the marginally attached (those willing to work but not actively looking). This rate bottomed in the 7.9% - 8.2% range prior to the recession.

The labor force participation rate (labor force divided by civilian population) remained at 62.9% as the 105,000 gain in the labor force was mostly offset by a 201,000 civilian population gain. Despite two straight months at 62.9% the current reading pales in comparison to the 66% level that prevailed pre-crisis. On the face of that it may seem to indicate remaining labor force slack but getting anywhere close to that pre-crisis level seems impossible given demographic forces of increasing boomer retirements, versus slowing population gains in working age people. The 62.7% to 63.0% participation rate range may well be the new full employment normal given the aging of the entire civilian population and slowing population gains.

In summary, this is another solid jobs report, with the headline miss offset by prior month revisions. This will keep the Fed firmly in hiking mode, In fact, given the labor market gains, and modest wage increases, the limiting factor to future rate hikes may be more the impact of trade actions and foreign economic growth and condition trends. For now, however, this report, and most other releases of late, will keep the Fed on its quarterly hiking schedule for this year.

Year-over-Year Change in Avg. Hourly Earnings



Average hourly earnings has become perhaps the most important metric in the monthly employment reports. With the unemployment rate hovering near cycle lows, and well below the Fed's long-run equilibrium rate of 4.5%, wage gains rose 0.3% matching expectations and ahead of June's 0.1%. The graph illustrates YoY earnings for workers dating back to the mid-60's. As shown, the current wage gains, while improving, pale in comparison to prior periods with the average over the 50-year period at 4.2%. The modest wage gains of today should keep inflation from moving materially higher, especially with the Fed sticking to its quarterly hiking schedule.

Market Rates

Treasury Curve	Today	Chg Last wk.	LIBOR Rates	Today	Chg Last wk.	FF/Prime	Rate	Swap Rates	Rate
3 Month	2.00%	+0.02%	1 Mo LIBOR	2.08%	UNCH	FF Target Rate	1.75%-2.00%	3 Year	2.948%
6 Month	2.21%	+0.04%	3 Mo LIBOR	2.35%	+0.01%	Prime Rate	5.00%	5 Year	2.986%
2 Year	2.66%	-0.01%	6 Mo LIBOR	2.53%	+0.01%			10 Year	3.072%
10 Year	2.98%	+0.03%	12 Mo LIBOR	2.83%	+0.02%				