CenterState
CORRESPONDENT DIVISION

# Market Update

## Economic News

June 7, 2019

The May jobs report was a disappointment as headline job growth of 75,000 widely missed the 175,000 expectation, and the past two months were revised lower by 75,000. Wage gains disappointed as well increasing 0.2% for the month but missing the 0.3% forecast and the YoY gain dipped to 3.1% missing the 3.2% pre-release forecast, and the lowest YoY print since September. While YoY wage gains were steadily increasing throughout last year, they seem to be plateauing just above 3.0% of late and that is with an unemployment rate that held at 3.6% for the second straight month and remains the low for this cycle. In summary, it's a mostly disappointing report and one that allows the Fed to move to an easing posture in the second-half of this year. With the market pricing in nearly 75bps of rate cuts by year-end this report gives the Fed the breathing room to begin positioning for a pre-emptive rate cute, perhaps at the July FOMC meeting. That will keep the front-end of the curve well bid and the longer-end as well until rate cuts become a reality.

For the month, only 75,000 jobs were created which fell well short of the 175,000 forecast and represents the lowest print since a weather-related 56,000 February. There were no one-off excuses this time. In addition, the prior two months were revised down 75,000 adding to the disappointing report.  Over the past year, monthly job gains have averaged 196,000 so the May results were well under expectations and well under the annual trend and that is something the Fed will be watching closely in the June numbers. While one report does not a trend make if June is similarly weak, the Fed could be forced to consider a rate cut as early as the July 31st meeting.

Away from the headline job growth numbers, and probably more important, wage gains also disappointed versus the month-over-month and yearly expectations.  Average hourly earnings rose 0.2% for the month versus 0.3% expected, while year-over-year earnings rose 3.1%, missing the 3.2% forecast and the lowest YoY print since September's 3.0% rate.  February's 3.4% YoY gain remains the  high for this cycle.  With lower job growth numbers and slowing wage gains, expect the Fed to start signaling very soon a switch from its patient pause approach to an easing bias.

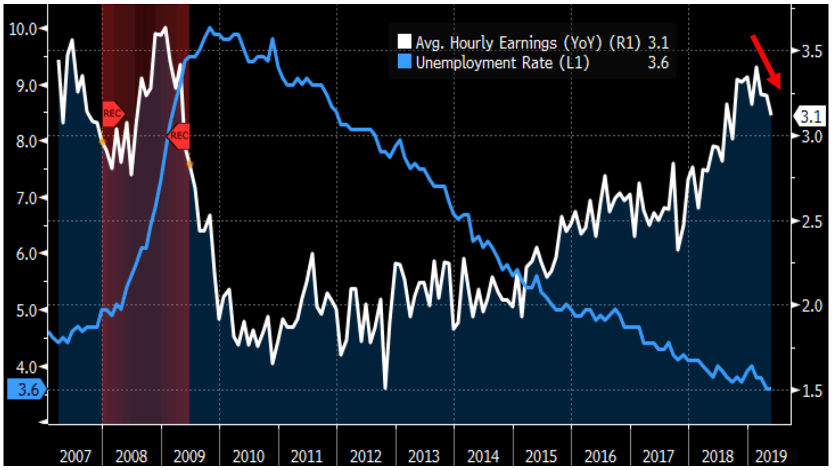
The unemployment rate remained at 3.6% (actually 3.620% vs. 3.585% in April) meeting the pre-release forecast. The 3.6% rate remains the cycle low and was essentially unchanged despite a 64,000 increase in the ranks of the unemployed. The Household Survey—which is used to generate the various employment ratios— reversed an unexpected drop in the labor force in April with an increase of 176,000 in May which worked to offset the increase in unemployed persons. The net of all this was to keep the unemployment rate effectively unchanged, but the increase in the labor force will ease some consternation of Fed officials who will see it as one positive in an otherwise disappointing report. It also looks like, given the still docile wage gains, the Fed's latest 4.3% equilibrium estimate of unemployment will need to be cut to something a little closer to the current 3.6% rate when they refresh the estimates at the June FOMC meeting.

Another positive is that the broader underemployment rate (unemployed plus part-timers seeking full-time work, plus the marginally attached divided by the labor force) fell to 7.1% after three consecutive months at 7.3%, and that sets a new low for this cycle. While unemployed persons increased 64,000, part-time workers decreased by 299,000 and 23,000 were subtracted from the ranks of the marginally attached (those willing to work but not actively looking). The smaller numerator was met with a slightly larger denominator as the labor force increased by 176,000 and that lowered the underemployment rate by 2/10ths of a percent.

The labor force participation rate (labor force divided by civilian population) remained at 62.8% for a second straight month and remains off the cycle high of 63.2% set back in February. The unchanged reading was driven by the afore-mentioned 176,000 increase in the labor force while the civilian population rose by a similar 168,000. While the current rate is fairly close to the cycle high, the rate still pales in comparison to the 66% level that prevailed pre-crisis. The 62.7% to 63.2% range over the past year appears to be the new full employment normal given the aging of the working population and slowing population gains.

In summary, this release is a something of a disappointment what with the headline number widely missing expectations and trending away from the declining twelve-month average, and wage gains seem to have plateaued after increasing earlier in the year. The report allows the Fed to move to an easing posture in the second-half of this year. With the market pricing in nearly 75bps of rate cuts by year-end this report gives the Fed the breathing room to begin positioning for a pre-emptive rate cute, perhaps at the July FOMC meeting. That will keep the front-end of the curve well bid and the longer-end well-bid as well until the rate cuts become reality.

## Average Hourly Earnings Trending Lower




Average hourly earnings and the unemployment rate have been the most important metrics in the monthly jobs report for some time. Despite the unemployment rate being well below the Fed's long-run equilibrium rate of 4.3%, wage gains rose 0.2% in May while the YoY print was 3.1%, both results missed pre-release expectations. The graph shows the unemployment rate along with the YoY wage gains dating back to 2007. While YoY wage gains were slowly improving since 2012, they have been trending lower over the last few months, despite the unemployment rate at a cycle low. The docile wage gains will give the Fed room to move to an easing bias at the June meeting.

## Market Rates

| Treasury Curve | Today | Chg Last wk. | LIBOR Rates | Today | Chg Last wk. | FF/Prime | Rate | Swap Rates | Rate |
|---|---|---|---|---|---|---|---|---|---|
| 3 Month | 2.25% | -0.10% | 1 Mo LIBOR | 2.42% | -0.01% | FF Target Rate | 2.25%-2.50% | 3 Year | 1.819% |
| 6 Month | 2.14% | -0.25% | 3 Mo LIBOR | 2.47% | -0.03% | Prime Rate | 5.50% | 5 Year | 1.851% |
| 2 Year | 1.81% | -0.11% | 6 Mo LIBOR | 2.41% | -0.11% | IOER | 2.35% | 10 Year | 2.056% |
| 10 Year | 2.07% | -0.05% | 12 Mo LIBOR | 2.38% | -0.13% | SOFR | 2.40% | | |