U.S.: SEPTEMBER EMPLOYMENT REPORT SOLID DESPITE LOWER-THAN-EXPECTED HEADLINE

*The September Employment Report was solid despite slower-than-expected job growth, as there were strong upward revisions to prior months and a larger-than-expected drop in the unemployment rate, while Hurricane Florence probably dented hiring in some sectors as well, which should reverse in the coming months:

- Establishments added a net new 134k jobs to payrolls in September (Consensus: 185k), and upward revisions totaled 87k (August: +69k to 270k, July: +18k to 165k), pushing the 12-month moving average of average job gains to 211k, the best since September 2016 (Chart 1).
- The unemployment rate declined by 0.2pp to 3.7%, its lowest rate since 1969 and down 0.5pp from a year ago; this is the 18th consecutive month that the unemployment rate has been below the Fed’s estimate of the natural rate of unemployment (“full employment”), 4.5% (Chart 2).
- Average hourly earnings rose a solid 0.3% m/m, lowering its yr/yr rise to 2.8% from 2.9%, reflecting the unfavorable base comparison from last September when the two hurricanes generated a temporarily outsized jump in wages (Chart 3). Average hourly earnings growth has risen at a 3.4% annualized pace in the last four months and the trend looks solid.

The decline in the unemployment rate to a near 50-year low reflects the Household Survey’s measured 270k decline in unemployment coupled with the 150k increase in the labor force. In the Household Survey, employment rose 420k, reversing August’s 423k fall, and labor force participation rate remained at 62.7%. We expect the overall LFPR to remain steady in coming years as rising prime working-age labor force participation outweighs the drag from an aging population. The prime working-age LFPR ticked down by 0.2pp to 81.8% in September, but its 2018 average is 82%, on pace to be the highest since 2010 (Chart 4).

The broader measure of labor underutilization, U-6, which measures total unemployed plus marginally attached workers plus part-time workers for economic reasons, is at 7.5%, near its all-time low of 6.8% recorded in 2000.

The softer-than-expected gain in establishment payrolls in September reflects several temporary factors: 1) the Bureau of Labor Statistics’ first estimate of September nonfarm payroll growth has consistently underperformed expectations only to be revised up markedly in subsequent reports, a pattern similar to August (Chart 5); and 2) hurricane Florence dented measured jobs, but by a lesser extent than the bigger hurricanes of September 2017. According to the BLS, 1) the 37k m/m swing from August (from +21k to -17k) in leisure and hospitality jobs likely reflects this impact; and 2) 313k persons were not at work because of weather — a sizable amount but less than in September 2017 (Chart 6).

Job growth has accelerated this year after decelerating in three prior years (2014: 250k, 2015: 226k, 2016: 195k, 2017: 182k, 2018 ytd: 208k). If the labor market were as tight as implied by the Fed’s estimate of full employment, job growth this strong would likely place significant upward pressure on wages. Our research shows that the potential labor supply is sizable and elastic, especially along prime working-age persons, and as business demand for workers continues to rise, attractive wages and benefits are luring a growing number of persons from the sidelines back into the workforce (*Rising US prime working-age labor participation*, September 20, 2018). We expect average hourly earnings to rise to 3% by year-end. The combination of gains in employment and moderate increases in wages is lifting disposable incomes.

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The goods-producing sector added 46k jobs in September, with construction employment increasing by 23k, bringing its 2018 total to 214k despite constant complaints about the shortage of construction workers and manufacturing jobs increasing by 18k and remaining on track to surpass its 2017 gain (2018 ytd: 189k, 2017: 207k). However, the service-providing sectors added a below-trend 75k jobs after the massive 217k August gain. Jobs in leisure and hospitality (-17k), education and health services (+18k), retail (-20k), wholesale trade (+4k) underperformed, while transportation and warehousing (+24k), financial (+13k), professional and business services (+54k) were strong.

Chart 1: Change in Total Nonfarm Employment

Chart 2: Unemployment Rate
Chart 3: Average Hourly Earnings for Private Industry Workers (year-over-year, %)

Source: Bureau of Labor Statistics/Haver Analytics

Source: Monthly data. Source: Bureau of Labor Statistics and Haver Analytics

Chart 4: Labor Force Participation Rate for the 25-54 Age Cohort

Source: Bureau of Labor Statistics/Haver Analytics

Source: Monthly data. Source: Bureau of Labor Statistics and Haver Analytics
Chart 5: Average of the difference between the second and initial estimates of nonfarm payrolls since 2011

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Source: Bureau of Labor Statistics and Berenberg Capital Markets

Chart 6: Number of persons not at work because of bad weather in September, 2011-2018 (Not seasonally adjusted)

Source: Bureau of Labor Statistics and Berenberg Capital Markets
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