Scotiabank

GLOBAL ECONOMICS

SCOTIA FLASH

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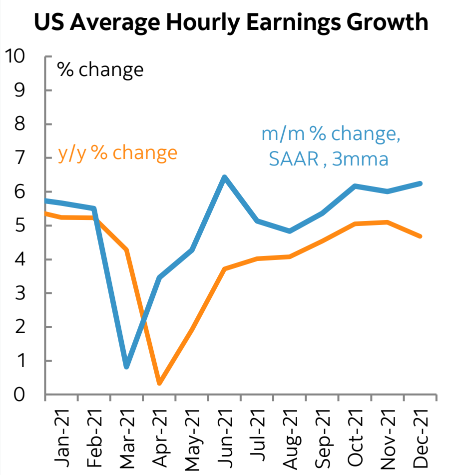
Contributors

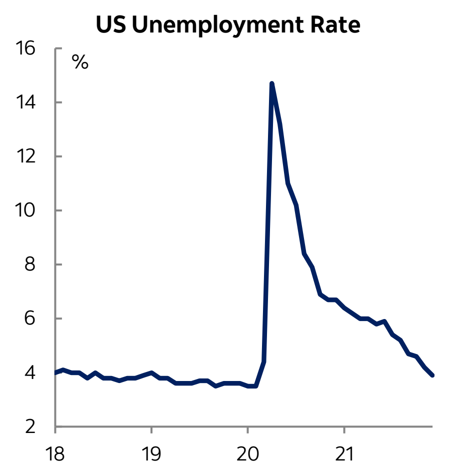
Derek Holt
VP & Head of Capital Markets Economics
Scotiabank Economics
416.863.7707
derek.holt@scotiabank.com

Chart 1



Sources: Scotiabank Economics, BLS.

Chart 2



Sources: Scotiabank Economics, BLS.

The US is Already at Full Employment

- **Bond yields lit up by wage pressures, pre-pandemic low for unemployment**
- **The miss on nonfarm payrolls is modest after considering revisions…**
- **…while the household survey continues to indicate much faster job growth**
- **Evidence points toward how the US may already be at maximum employment**
- **Fed lift-off in March is mostly priced, but markets remain lighter than our full-year forecast**
- **US vaccine mandate enforcement has begun**

US nonfarm payrolls, m/m 000s // UR (%), December, SA:
Actual: 199 / 3.9
Scotia: 600 / 4.2
Consensus: 450 / 4.1
Prior: 249 / 4.2 (revised from 210 / 4.2)

US nonfarm payrolls (+199k) disappointed loftier expectations, but what drove bond yields higher in a bear steepener Treasury move was the combined effect of the decline in the unemployment rate to a pre-pandemic low that signals tight job markets, plus the strength of wage gains that reinforces the point about tightening job markets. To the Fed's dual mandate, such evidence suggests that the wage-price connection is increasingly challenging its price stability goal while we may already be at maximum employment or very close to it.

Denting some of the consensus miss was the fact that nonfarm payrolls were revised up by 141k in the prior two months and mostly for October. Add positive revisions to the 199k for November and the combined 340k rise in payrolls wasn't as bad of a miss especially considering the 90% confidence interval on nonfarm payrolls of +/- about 110k.

Wage growth picked up to 0.6% m/m at a seasonally adjusted but non-annualized rate. That translates into an annualized pace of 7½%. It has run at this pace over three of the past four months. What's more, the annualized rate of monthly seasonally adjusted wage gains has been running at between 4.3% and 8.3% over the nine months since April. This month-over-month pace is outpacing the year-over-year gains (chart 1) and likely to begin putting upward pressure on the y/y rate.

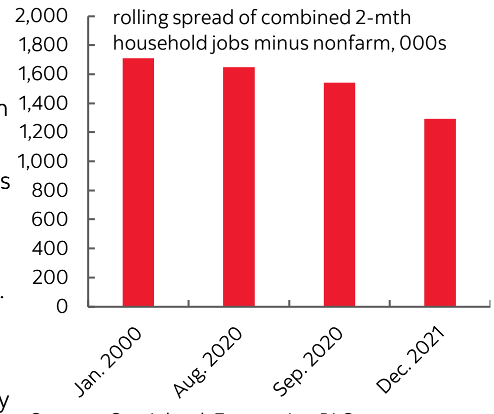
The unemployment rate fell three-tenths to 3.9% (chart 2). That's the lowest unemployment rate since February 2020 and hence just before masks and needles entered the picture. How come, when nonfarm disappointed? Because the unemployment rate is derived from the companion household survey which showed another explosive job gain of 651k after the prior month's household survey registered a gain of 1.74 million while that same survey showed that the labour force only expanded by 168k last month.

A key related issue is the massive difference between what the household survey and the establishment survey are reporting for job growth over the past two months which has only two other parallels in history (chart 3). For November and December combined, the household survey says that 1.74 million jobs have been created versus nonfarm's 448k for a whopping difference of 1.29 million jobs. There have only been three times in history when the household survey's reported job gain was this much higher than the nonfarm payrolls report over two consecutive months. One was during the dot com period at the start of 2000. Another was the summer of 2020.

I don't know why this deviation is occurring. We should be careful toward the bigger error bands around the household survey relative to the nonfarm figures, but the magnitude of the deviation is bigger than what can be explained by relative confidence bands. There is always revision risk to both surveys but sweeping aside this observation would require enormous revisions. It's not because people are become self-employed in droves since those numbers are falling as indicated by the same household survey (chart 4). This is pure conjecture on my behalf, but it's not intuitively unreasonable to think that maybe smaller incorporated businesses that are probably better captured in the household survey are picking up workers from the larger payroll employers. Maybe concern toward being in densely concentrated workplaces in urban centers in a pandemic is a driving force! Maybe smaller businesses are more nimble in keeping up with the compensation pressures.

Chart 3

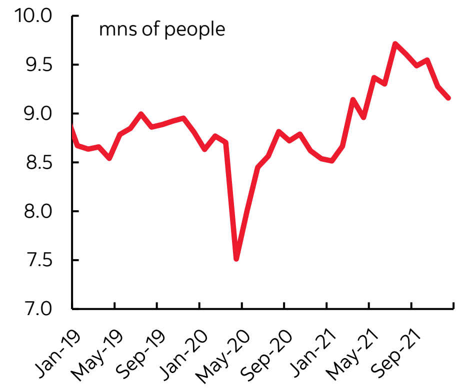
Household Survey Anomaly



Sources: Scotiabank Economics, BLS.

Chart 4

Household's Survey Measure of Self-Employed Individuals



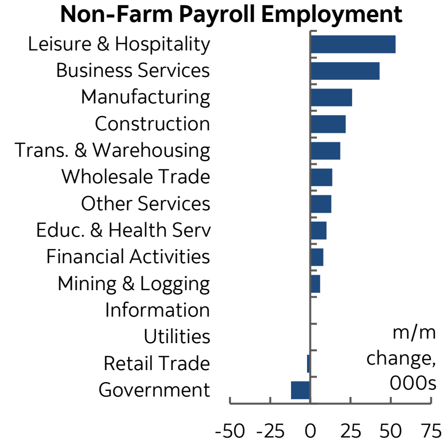
Sources: Scotiabank Economics, BLS.

OTHER DETAILS:

Chart 5 shows the breakdown of nonfarm payroll employment by sector. About half a dozen sectors played a similarly sized role in driving the overall employment gain. They were (in order) leisure and hospitality's 53k that may be about to get crushed in January, business services (+43k) but not via temp help, trade/transport (+30k) but with retail trade flat (-2k), manufacturing (26k), construction (22k) and education/health (10k).

Chart 5

December Changes in US Non-Farm Payroll Employment



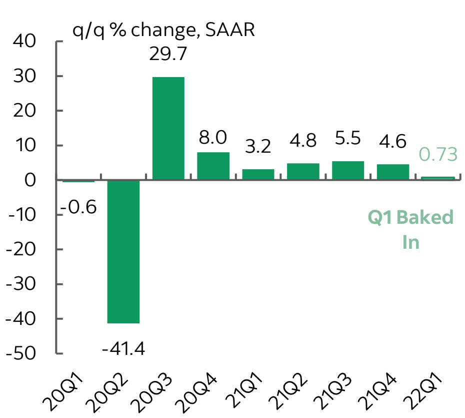
Sources: Scotiabank Economics, US BLS.

Hours worked were up 0.2% m/m in December and 4.6% q/q annualized in Q4 (chart 6). We already have another annualized gain of 0.7% baked into '22Q1 before any Q1 data given the way Q4 ended relative to the overall quarter. That's a strong supporting indication for GDP growth given GDP is an identity defined as hours worked times labour productivity.

The final two charts track employment progress to date in the pandemic. The household survey shows that the US is still 2.9 million jobs short of where things stood in February 2020. Nonfarm payrolls are still 3.6 million below that same point. My view all along has been that the goal isn't getting back to that point if labour supply is more significantly restrained now. The way I see it, the US is at full employment.

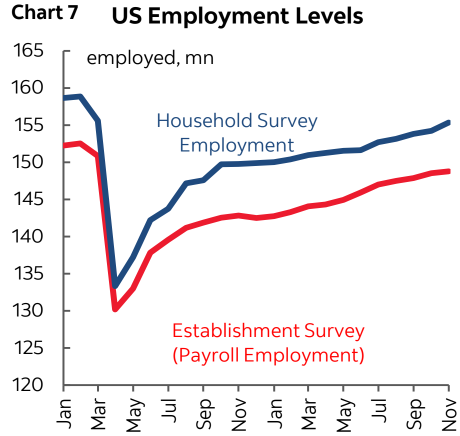
A near-term challenge to monitor will be omicron's effects and vaccine mandates given evidence of a push to enforce them at large employers in the US banking industry as one example. This is probably a nearer-term shock that monetary policy should look through.

Chart 6 **Total Hours Worked**



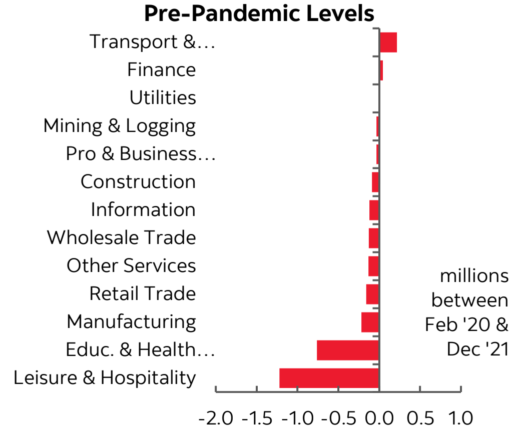
Sources: Scotiabank Economics, BLS.

Chart 7 **US Employment Levels**



Sources: Scotiabank Economics, BLS.

Chart 8 **US Employment Recovery to Pre-Pandemic Levels**



Sources: Scotiabank Economics, BLS.