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GLOBAL ECONOMICS

SCOTIA FLASH

February 4, 2022

Dear Omicron: Americans are Moving On!

- **Nonfarm payrolls smashed expectations by 1.2 million jobs including revisions**
- **Wage growth is super accelerating**
- **The high contact leisure/hospitality sector surprisingly led the way**
- **Our 2% year-end target for fed funds is looking better by the day**

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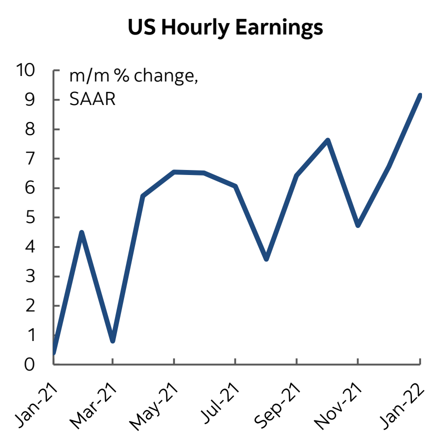
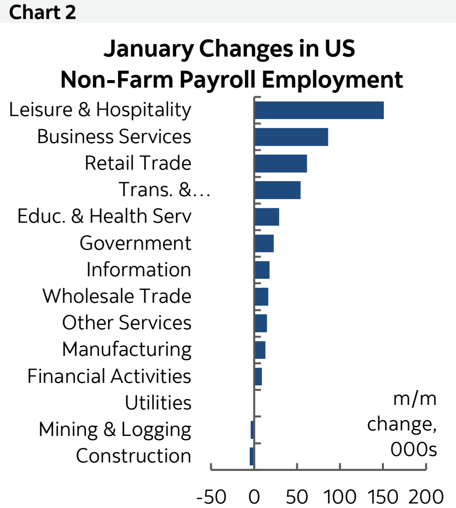
Chart 1



Sources: Scotiabank Economics, BLS.

Chart 2



Sources: Scotiabank Economics, US BLS.

US nonfarm payrolls, m/m 000s // UR %, SA, January:
Actual: 467 / 4.0
Scotia: -100 / 4.0
Consensus: 125 / 3.9
Prior: 510 / 3.9 (revised from 199 / 3.9)

Dear Omicron: We're so done with you. Signed, America.

That was the resounding message delivered by US employers and employees as nonfarm job growth smashed consensus expectations by almost 1.2 million jobs including large positive revisions. That includes a surprise gain of 467k in January and positive revisions of 709k extra jobs over the prior two months that were almost evenly split between December and November.

Bonds got crushed by the release. The two-year and the 10-year Treasury yields both spiked 9bps higher in the aftermath so far. The USD gained about 0.3% on a DXY basis. The S&P500 is down ¾% on the day so far; stocks will get the memo later that says if the Fed is tightening when the economy is very strong then they can continue moving higher.

Wage growth super-accelerated. The month-over-month gains in average hourly earnings accelerated to 9.2% SAAR in January. That's not driven by compositional shifts given the breadth of the job gains. It wasn't before either, given evidence of accelerating gains in the Atlanta Fed's Wage Tracker measures of median wage growth and wage growth by quartiles. This m/m annualized measure of wage growth from the payrolls survey has been running between about 4–9% dating back to last April (chart 1). The diminishing number of wage deniers need only look at the facts any day now. The trend is exceeding inflation and far exceeding soft trend growth in labour productivity, Q4 notwithstanding. A wage-price spiral is in motion in the United States economy.

Sector breadth was high and all of the gain was in services (+440k) as goods producing sectors were flat (+4k). Within goods, manufacturing payrolls were up 13k with construction little changed (-5k). Within services, the big gainers were surprisingly led by leisure/hospitality (+151k), then business services (+86k of which 26k was temp help), retail trade (+61k) and diversified smaller gains elsewhere shown in chart 2.

It's also surprising that the aggregate hours worked measure only fell 0.3% m/m and was up 0.2% in December. Not even hours worked were materially curtailed as the fear was that hours worked could have really plunged with folks taking to the sidelines. US hours worked were up 5.6% q/q SAAR in Q4 and are tracking flat q/q SAAR so far in Q1 (chart 3).

What's the revision risk to US payrolls? Very, very small. I mean in the sense that it probably would not be big enough to flip the sign. There has only been one time in the past decade when payrolls were revised by more than 467k (the number that January payrolls would have to fall by after revision to get toward negative territory) and the starting point that time (March 2020!) was a big negative.

US payrolls are now 2.9 million below pre-pandemic levels in February 2020 and the household survey shows that the labour force is only ~900k smaller than it was in

February 2020 pre-pandemic while the household survey also shows that employment is only 1.7 million below February 2020. Given reasonable estimates of retirements and exits, the US labour force is essentially at if not beyond maximum employment. See chart 4. Also see chart 5 for the sectoral breakdown of where jobs are still behind. Not surprisingly, despite January's gain, it's the leisure and hospitality sector that is accounting for most of it. If we keep seeing gains like this then maybe that sector will be back to normal soon this year.

A caution around the household survey's 1.2 million gain in January is that it's almost all explained away by revisions to population estimates that only get incorporated into January figures and not factored into revisions prior to January. Table C in **this** link explains this point. However, that does not negate the factor that the household survey was hugely gaining momentum over the 2021 with gains of 651k in December, 1.1 million in November, 428k in October, 639k in September and 463k in August following the 1.1 million gain in July. January's household survey gain may have been a statistical distortion, but the trend in this measure has been wildly positive for many months.

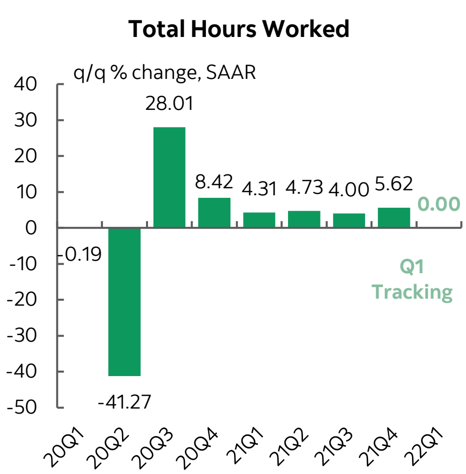
So where did I go wrong fwiw? Why was there rising negativity ahead of the number only to get very positively surprised? The US Census Bureau's Household Pulse Survey showed a mass exit of ~6 million people from the workforce between the December nonfarm reference period and the January nonfarm reference period because of an increase in people saying they were caring for folks sick with COVID-19. Why didn't that translate into a negative print this morning?

- maybe strength elsewhere in the labour force was that much stronger than the folks who say they took to the sidelines;
- maybe the folks who said they checked out of the labour force in January did so very fleetingly instead of for the two-week period required to drop off payroll estimates. Still, had even a fraction of the 6 million been out for longer than that should've driven a negative headline.
- or the survey that usually performs pretty decently had a very bad out-of-sample month.

Either way, perhaps the best job market indicator is to simply look at the maskless fans in the packed stands at sporting events. Toss normative assessments aside folks, the reality is that America is moving on, adapting to the pandemic and getting on with life. As a consequence of this behavioural adaptation that may motivate horrific shrieks from health care professionals, US monetary policy is far too stimulative.

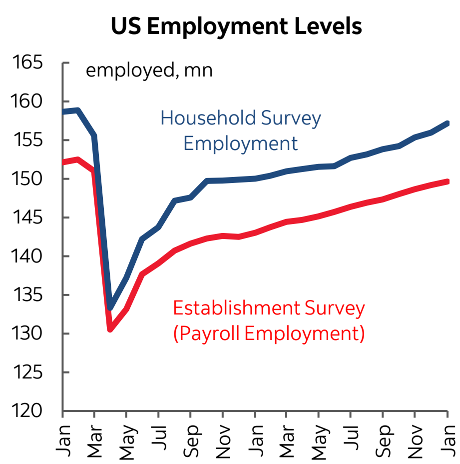
With that, fed funds futures are now pricing over 5 hikes this year and continuing to migrate toward our forecast for 175bps of tightening and pricing a decent chance at a fifty move in March.

Chart 3



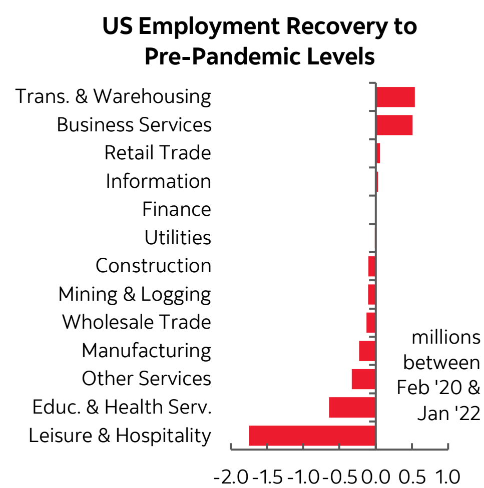
Sources: Scotiabank Economics, BLS.

Chart 4



Sources: Scotiabank Economics, BLS.

Chart 5



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