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Payden & Rygel EconomicResearch

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Jobs Data Is An Early Christmas Present for Investors

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Highlights

- The US economy shed 11,000 jobs in November, which was much less than expected, and the unemployment rate dipped to 10%.
- The breadth of the improvement in the labor market is perhaps best reflected in the rise in the percentage of industries hiring from 20% in March to 41% today.

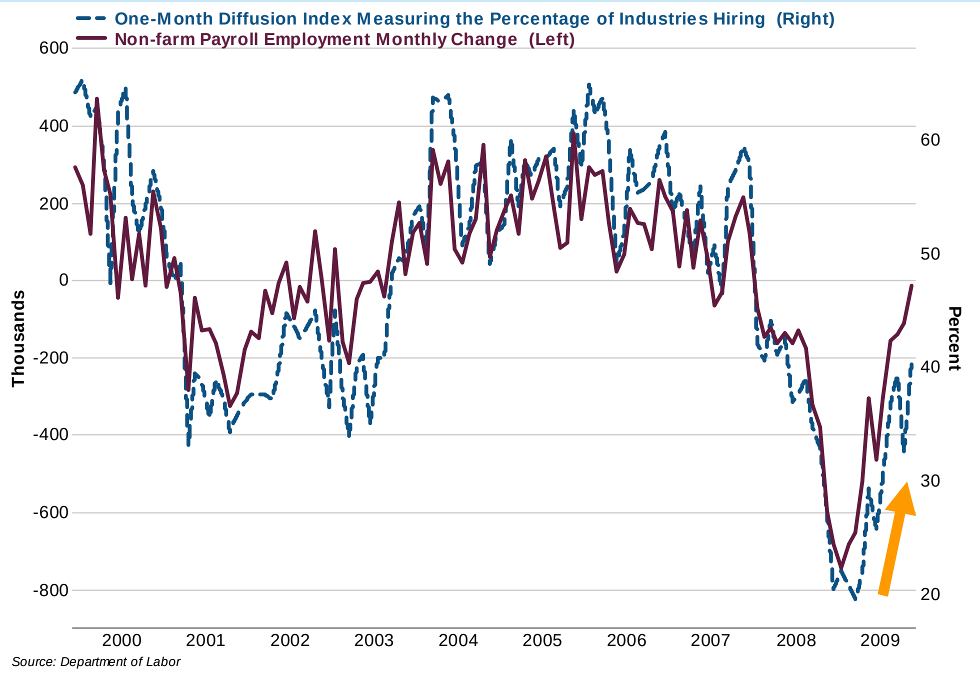
Santa arrived early for the labor market, with the US economy losing just 11,000 jobs in November compared to market expectations for a loss of 125,000 jobs. Moreover, as we suspected, the unemployment rate dipped to 10% in November from 10.2% in October as a divergence between the employment measures from the household and the payroll surveys was corrected in favor of the less volatile payroll survey. The unemployment rate is still likely to rise over the next few months, but perhaps not to the same degree as would have been suggested by October's report.

The details of today's report were quite strong, with upward revisions to job gains for the prior two months totaling 159,000. The health care and temporary help services industries both added jobs during the month and the rate of job losses continued to moderate in construction and manufacturing. As we mentioned previously, the pick up in temporary help services hiring is particularly important since employers will often test the waters with temporary hires before bringing on full-time employees. Another leading indicator of future job growth is the 0.6% gain in aggregate weekly hours in November –the first increase since August 2008. It is not uncommon for employers to have their existing employees work overtime before increasing hiring. Both indicators bode well for a job market recovery as we head into 2010.

More Industries Are Hiring

The breadth of the improvement in the labor market is perhaps best reflected in the rise in the percentage of industries hiring. Approximately 111 of the 271 industries surveyed (41%) reported they were increasing payrolls in November according to the one-month diffusion index. This is up from 53 industries (20%) back in March of this year. Historically, payrolls have broken into positive territory when this figure edges closer to 50%. Although it is possible that we will get a positive payroll figure early next month when the December employment data is released, we are more inclined to believe that the first breakthrough into positive territory will come when

A Growing Number of Industries Are Hiring



Source: Department of Labor

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- Today's employment report has certainly dealt a blow to those pessimists arguing that the US economy was headed for a double dip recession similar to the 1981-82 period.
- The increasingly transparent Fed will clearly telegraph any future rise in the fed funds rate to the markets well before the action is taken in order to lessen the disruptive impact on the bond market.

the January numbers are released in early February. The reason for our hesitation is that while the November jobs data are better than expected, they are an outlier and have not been confirmed by other measures of the labor market.

For example, though new claims for unemployment insurance fell to 457,000 last week, they remain well above the 400,000 threshold commonly associated with job creation. In addition, yesterday's ADP figure and the ISM non-manufacturing survey measure of employment suggest the labor market is still contracting. Therefore, we are hedging our bets and sticking by our forecast that the first positive payroll number will come with the release of the January jobs data in early February.

If we are correct in our forecast, there is some risk that financial markets could suffer a temporary setback next month given the increasing optimism that we may avoid a jobless recovery. Even if job growth were to turn positive next month, it will probably take a couple more quarters of trend GDP growth of around 2.5% before the economy is creating the 150,000 or so jobs necessary each month to absorb new entrants to the labor force and keep the unemployment rate from rising.

Still Too Soon To Hike Rates

Nevertheless, today's employment report has certainly dealt a blow to those pessimists arguing that the US economy was headed for a double dip recession similar to the 1981-82 period. However, it is still too soon for the Federal Reserve to hike its benchmark interest rate. Despite growing signs of a sustainable US recovery, bank lending is constrained and the financial system remains fragile. Fed funds futures are currently pricing in a 72% probability of an interest rate hike by August, which is in line with our own forecast.

As we mentioned last month, the central bank has typically waited about a year after the peak in the unemployment rate to start hiking interest rates. Even if this month marked the peak in the unemployment rate (which we do not believe it did) that would imply we still have some time before the Fed moves into tightening mode. In addition, inflation is still very low and the output gap, as measured by either the unemployment rate or industrial capacity utilization, suggests inflation rates are likely to fall further in the coming months.

In our opinion, the increasingly transparent central bank will clearly telegraph any future rise in the fed funds rate to the markets well before the action is taken in order to lessen the disruptive impact on the bond market. Treasury yields have already moved sharply higher on the employment news with 2-year yields, which tend to be closely correlated with fed funds, jumping 17 basis points this week from 0.67% to 0.84%. Treasuries are likely to remain range bound until we get closer to the point when the Fed will be hiking rates.