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Payden & Rygel Economic**Research**

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The US Labor Market Is Hanging in There…For Now

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Highlights

- The US economy created 94,000 jobs in November and the unemployment rate held steady at 4.7%.
- Despite today's stronger than expected data, trends in underlying employment growth and unemployment claims raise a red flag.
- We expect the Fed to reduce the federal funds rate by 25 basis points to 4.25% when it meets on December 11. Further rate cuts are likely during the first half of 2008.

The US economy generated 94,000 jobs in November, slightly above market expectations for a gain of 80,000 jobs. The unemployment rate held steady at 4.7%.

The report's strength makes a 25 basis points cut more likely than a 50 basis point cut when the Federal Reserve meets next week. Stock market investors reacted positively to the numbers at first, viewing them as a signal that the economy will avert a recession. However, the S&P 500 stock index was essentially flat after an early rally. By contrast, bond investors pushed Treasury prices lower and the yield on the 10-year note rose 10 basis points to 4.10%.

Who Is Hiring?

Government payrolls have been a key contributor to payroll gains over the last two months, adding 30,000 jobs in November and 38,000 jobs in October. And with the holiday shopping season in full swing, the retail trade sector added 24,000 jobs after three consecutive monthly declines. Other areas of strength included healthcare, leisure and hospitality, and professional and business services.

The primary areas of weakness are still the housing-related industries. Construction payrolls lost 24,000 while credit intermediation, which includes mortgage brokers, dropped 13,000 jobs in November. Manufacturing employment has posted 19 consecutive months of decline, losing another 11,000 jobs during the month.

The Outlook Is Not As Rosy

Looking ahead, the trends in employment growth and unemployment claims raise a red flag. The six-month moving average for nonfarm payrolls slowed from 190,000 at the end of 2006 to less than half of that in November. At the same time, new claims for unemployment insurance have been on the rise. Though some of this may be seasonal, the sharp jump in the four-week moving average suggests labor market conditions have deteriorated and the unemployment rate is poised to rise. The four-week moving average of new claims rose to 336,000–its highest level since October 2005.

Housing-related woes have spread into other areas, particularly the financial sector. Retail trade employment and manufacturing have also been impacted. As a result, we see the unemployment rate rising above 5% in the first half of 2008. In this environment, we expect the Federal Reserve to cut the federal funds rate by 25 basis points to 4.25% when it meets on December 11. Further rate cuts are likely during the first half of 2008 as the Fed seeks to steepen the yield curve to improve financial conditions for the banking sector.