Scotiabank

GLOBAL ECONOMICS

SCOTIA FLASH

September 6, 2024

Contributors

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

Why the Fed Should Still Tread Carefully After Nonfarm Payrolls

- **Nonfarm payrolls met expectations…**
- **…as wage growth accelerated**
- **This could be the last month for weak seasonal adjustment factors to hold back jobs…**
- **…as SA factors will probably turn more favourable going forward**
- **Governor Waller's ensuing speech prompted wild volatility in fed funds pricing…**
- **…but is much more careful and balanced than selective media headlines**
- **The FOMC should stick to a measured, gradual pace**

US nonfarm payrolls m/m 000s / UR %, SA, August:
Actual: 142 / 4.2
Scotia: 140 / 4.2
Consensus: 165 / 4.2
Prior: 89 / 4.3 (revised from 114 / 4.3)

US nonfarm payrolls met my expectations—and basically consensus expectations after taking account of high statistical noise. Notwithstanding modest revisions, headlines about how they disappointed are a bit absurd in recognition of the 90% +/-130k confidence interval around the estimates.

Payrolls were up by 142k alongside negative revisions of 86k over the prior two months with –29k of that affecting July's initial estimate. Such a small revision to July has little effect on August's jumping off point.

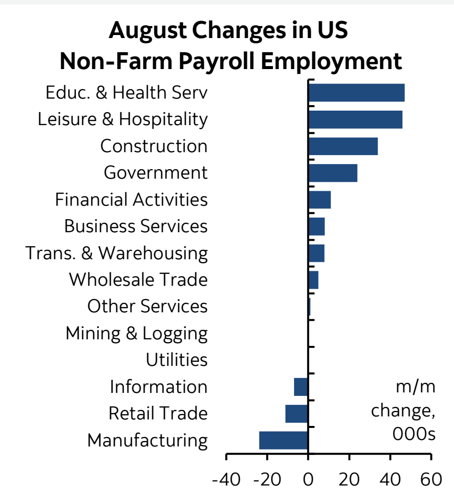
Payrolls were up modestly because of three main sectors (chart 1): US health/social assistance was up another 44k, leisure hospitality was up another 46k, and government added another 24k. There was not much breadth beyond that.

The companion household survey saw a job gain of 168k that exceeded the 120k rise in the size of the labour force that was slower than the reported 420k rise in the LF during July. This met expectations for how the unemployment rate would dip as job gains exceeded new entrants.

Wage growth was stronger than expected (chart 2). Wages were up by 0.4% m/m SA in the US which was higher than all estimates. That works out to 4.9% m/m at a seasonally adjusted and annualized rate. The three-month moving average now sits at 3.8% m/m SAAR.

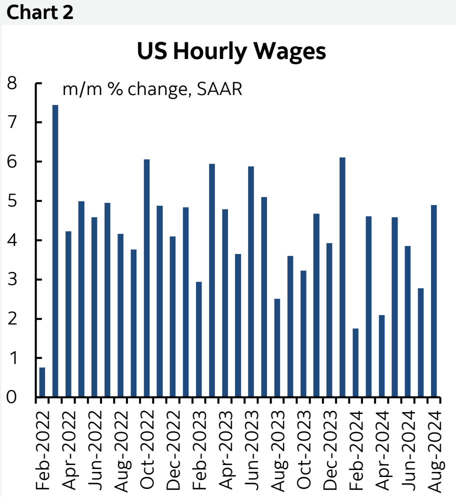
Hours worked were up by 0.3% m/m SA which reverses the prior month's similarly sized drop. That gives Q3 hours working tracking a modest rise of 0.5% q/q SAAR (chart 3) which leaves Q3 GDP growth more dependent upon productivity gains since GDP is an identity defined as hours worked in aggregate times labour productivity with the latter defined as real GDP divided by hours.

Chart 1



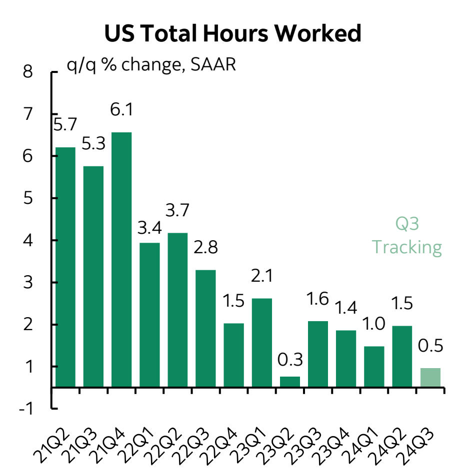
Sources: Scotiabank Economics, US BLS.

Chart 2



Sources: Scotiabank Economics, Statistics Canada.

Chart 3



Sources: Scotiabank Economics, BLS.

September 6, 2024

SEASONALS ABOUT TO TURN HIGHER?

Be careful here. This August's seasonal adjustment factor was also lower than past like months of August which extends the multi-month pattern (charts 4, 5). Chart 6 shows that the past couple of years have seen the September SA factor become among the strongest compared to like months in history; if that repeats next month, then altered seasonal adjustments compared to pre-pandemic adjustments could buoy payrolls by tamping down the NSA gain to a lesser extent than over recent months.

IMPLICATIONS FOR THE FEDERAL RESERVE

In my opinion, nothing screams out from the overall set of numbers that the Fed should be in panic mode and feeling a rush to upsize. The first cut shouldn't be the deepest in this case. The US economy remains in excess demand. Wage pressures remain significant. Tariffs—if employed—risk first-round inflationary effects and we'll be in a better position to judge this risk after the November 5th Presidential election. Ditto for high risks to US immigration policy that is tightening in the waning days of the Biden administration, and could massively tighten if Trump wins. Supply chains remain fragile. I think all of that says be careful in the opening salvos; the minute you cut –50bps once, you'll be pushed much faster.

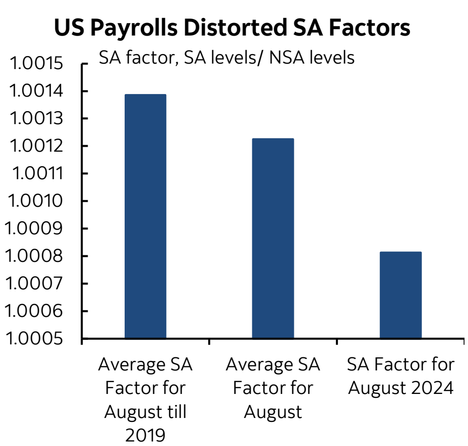
This is why I'm skeptical toward what Chicago Fed President Goolsbee says in reference to how policy tightens with each month of passive Fed policy and low inflation. He should craft his arguments in a forward-looking sense by invoking inflation expectations rather than using last month's data. Doing so should give at best very modest confidence—if any– in the ability to forecast inflation in future especially in light of the fact that the Fed simply isn't credible in its attempts at doing just that.

Enter Governor Waller's remarks (**here**). Selective interpretations of his remarks sparked high volatility in fed funds futures when the headlines landed. Those headlines made it sound like Waller is leaning toward upsizing cuts at the September meeting which drove pricing for this month's decision close to a full –50bps in their immediate aftermath before swinging around in the other direction toward –31bps or so and hence closer to a quarter point cut. I would strongly recommend reading his full speech. It is much more balanced and careful than the headlines.

The tricky thing for the FOMC is that they go into communications blackout tomorrow ahead of the September 18th communications and we're only hearing snippets from a small minority of officials in the aftermath of the report who may not be representative.

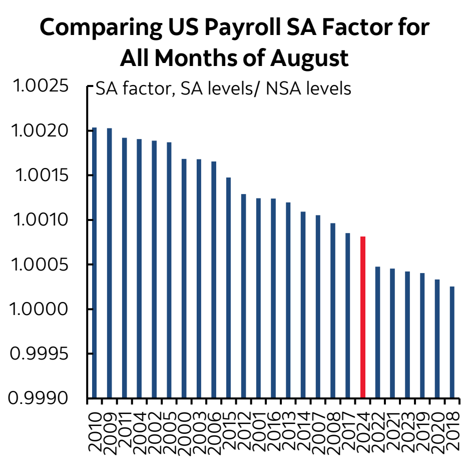
We get CPI next Tuesday with widespread expectations it will land at 0.2% m/m SA on core and with nowcasts around the same. If it surprises and/or if Chair Powell and the FOMC have a problem with where markets are pricing, then that could resurrect the possibility of using clandestine ways of communicating with markets through story plants. Powell never wanted to surprise markets on game day on the way up or the shift sideways, but is he still of that mindset? He has said a couple of times that the path going forward would involve less hand holding.

Chart 4



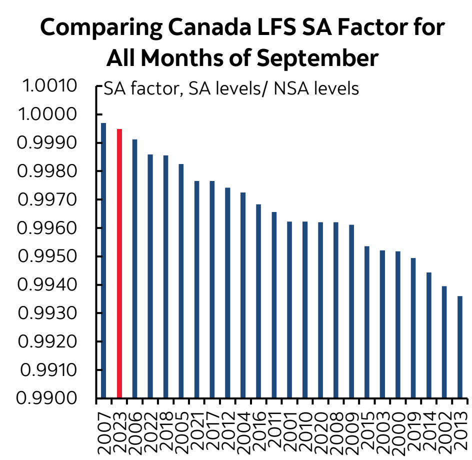
Sources: Scotiabank Economics, BLS.

Chart 5



Sources: Scotiabank Economics, BLS.

Chart 6



Sources: Scotiabank Economics, Statistics Canada.