ECONOMIC UPDATE
REGIONS
June 3, 2016

May Employment Report: A Surprisingly Weak Report, But What Is It Saying?

- Nonfarm employment rose by 38,000 jobs in May; prior estimates for March/April were revised down by a net 59,000 jobs.
- Average hourly earnings rose by 0.2 percent, with aggregate private sector earnings up 0.2 percent (up 4.1 percent year-on-year).
- The unemployment rate fell to 4.7 percent (4.692 percent unrounded); the broader U6 measure held at 9.7 percent.

Having scoured the details of countless data releases over the course of many years, there have been instances in which we simply don't know what to make of the numbers. Not many, but it does happen, and the May employment report is one such instance. Total nonfarm payrolls rose by just 38,000 jobs, more than 100,000 jobs shy of the consensus estimate. While the Verizon strike did knock over 37,000 jobs of the headline job growth number, adding them back (as they will be in the June report with the strike now settled) still leaves us with a puzzlingly weak number. Moreover, revisions to prior estimates for March and April were revised down by a net 59,000 jobs for the two-month period. While the unemployment rate did fall to 4.7 percent, the lowest since November 2007, that merely reflects a sharp decline in the labor force.

The breadth of hiring across private sector industry groups narrowed sharply in May, with the one-month hiring diffusion index falling to 51.3 percent. This marks the lowest reading since February 2010, when the economy was only starting to dig out from the 2007-09 recession. Payrolls in health care rose by 55,400 jobs, leisure & hospitality services added 11,000 jobs, retail trade added 11,000 jobs, and business services added 10,000 jobs. Payrolls in telecommunications fell by 37,200 jobs, reflecting the Verizon strike, while payrolls also fell in manufacturing, transportation, construction, and mining.

With the paltry job gain and a shorter workweek, the earnings details of the May employment report are weak as well. Aggregate private sector earnings rose just 0.2 percent in May, leaving them up 4.1 percent year-on-year, still easily ahead of inflation but well below trend.

Over the past several months we have noted what we thought to be considerable seasonal adjustment noise in the employment data. For instance, warmer than normal weather over the winter months led to a higher than normal volume of construction, which was reflected in construction payrolls during the first quarter of 2016. As a result, some portion of the hiring that would normally have been done in April and May had been pulled forward, but the seasonal adjustment factors will not have accounted for this, and as a result the seasonally adjusted job counts in these two months have been pushed down. On a not seasonally adjusted basis, there were 340,000 construction jobs added over April and May, while the seasonally adjusted data show a decline of 20,000 jobs for the two-month period. We have also pointed to retail trade and, to a lesser degree, leisure and hospitality services as other industry groups where there seemed to be seasonal adjustment noise.

There is also some seasonal adjustment noise in the household data. May typically marks the start of the summer job season, and with that comes an influx of younger adults into the labor force. June typically sees much larger inflows but the split between May and June will be altered each year by the timing of the school year. In May, the unadjusted data show 293,000 people aged 16-to-19 entered the labor force, far fewer than normal number for the month. The seasonal adjustment factor would have been geared to a larger number and, as such, the seasonally adjusted number is artificially low. We'll know soon enough – next month to be specific – whether the May data are just skewed or, if we do not see a sizeable jump in younger entrants into the labor force, there is something more fundamental in play. To be sure, we're not trying to pass off the entire May report as seasonal adjustment noise, but do think it a valid point to make.

There are many more details of the May employment report we could convey, but almost all of them have one thing in common – they are notably weak. In the words of a wise old economist, the numbers are what the numbers are; the problem today is we simply do not know what to make of them. Neither, we suspect, will the FOMC. Today's report pretty much kills off any chance of a Fed funds rate hike this month. But, as the May employment data are so far out of alignment with other indicators, it is too soon to rule out a rate hike later in the summer. Like the rest of us, the FOMC will need more time – and more data – in order to put the May employment report in its proper context.

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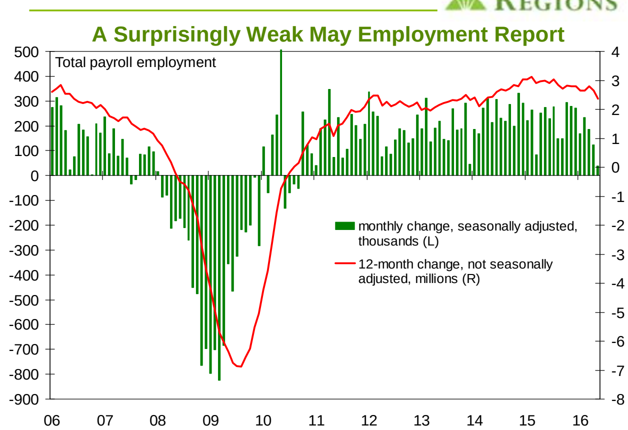

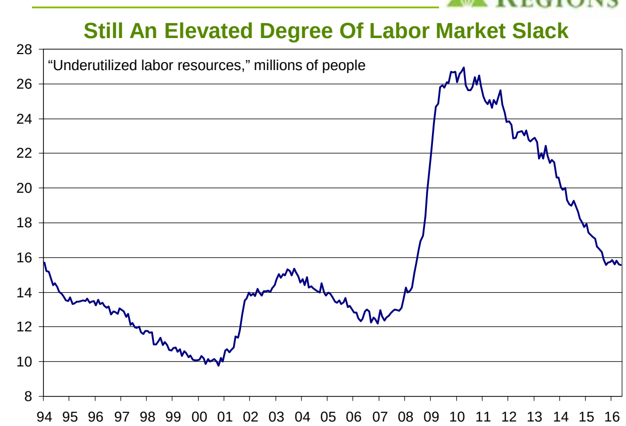

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