ECONOMIC UPDATE

REGIONS

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March Employment Report: Steady Job Gains Help Fuel Rising Participation

- Nonfarm employment rose by 215,000 jobs in March; prior estimates for January/February were revised down by a net 1,000 jobs.
- Average hourly earnings rose by 0.3 percent, with aggregate private sector earnings up 0.4 percent (up 4.25 percent year-over-year).
- The unemployment rate rose to 5.0 percent (5.001 percent unrounded); the broader U6 measure rose to 9.8 percent.

Total nonfarm employment rose by 215,000 jobs in March, with private sector payrolls rising by 195,000 jobs and government sector payrolls up by 20,000 jobs. Revisions to prior estimates for January and February were trivial, with a net downward revision of 1,000 jobs for the two-month period. The recent string of large increases in both the labor force and household employment continued in March, but the former slightly outweighed the latter, nudging the unemployment rate up to 5.0 percent, while the broader U6 rate rose to 9.8 percent. On the whole, this is a solid report, though there are enough soft spots to remind us that the labor market has not yet fully healed.

Somewhat counter to the regional ISM and Fed surveys, manufacturing payrolls dropped sharply in March. The 29,000 drop in factory payrolls was spread across both durable and nondurable goods, with producers of metals, industrial machinery, and transportation equipment posting the largest job losses. The one-month hiring diffusion index for the manufacturing sector, a gauge of the breadth of hiring across industry groups within the factory sector, slipped to 37.3 percent in March. Even more alarming than the low level is the extent of the decline in March; after having fallen sharply last fall the index had rebounded and stood at 57.6 percent in January before falling sharply in the next two months. This renewed decline calls into question whether the stability in the factory sector implied by the regional surveys is real or illusory.

As has been the case for the past several months, the private sector service providing industries accounted for the bulk of job growth in March. Payrolls in retail trade, leisure & hospitality services, education & health services, and business & professional services rose sharply, though we do suspect there are some seasonal adjustment issues at play in the first two of these industry groups. Construction payrolls were up 37,000 jobs, reflecting hiring by commercial and residential builders. Mining payrolls in mining & logging were down by 12,000 jobs. For the private sector as a whole, the one-month hiring diffusion index rose slightly, but at 58.4 percent in March stands well below the levels seen earlier in the expansion, and the narrower breadth of hiring mainly reflects the ongoing struggles in many goods producing industries. This mix of jobs is reflected in the shorter average workweek, with average weekly hours holding at 34.4 hours in March, which has implications for growth in aggregate wage and salary earnings. Aggregate earnings rose 0.4 percent in March, and for Q1 as a whole rose at an annualized rate of 4.1 percent, matching the gain seen in Q4 2015. Despite robust job growth, growth in aggregate earnings is not accelerating, reflecting lower hours worked and slow growth in hourly earnings, which rose 0.3 percent in March but are up just 2.3 percent year-on-year.

The rising labor force participation rate over the past few months is encouraging and, at least for now, is helping alleviate wage pressures despite what remains solid job growth. Historically, the majority of those entering the labor force in any given month are employed upon entry but, as seen in the chart below, that share has been growing rapidly over the past several months. We are seeing an unwinding of the cyclical component of the decline in the participation rate seen during and after the 2007-09 recession. What is uncertain, however, is how long this will persist, as it is but a matter of time before the structural component, a function of demographic trends, dominates the movement in the cyclical component and pushes the participation rate back down. The main measure of labor force slack – the combined number of those unemployed, working part-tine for economic reasons, and marginally attached to the labor force – rose to 15.8 million in March which, by our estimate, is over two million people higher than would be the case in a fully healthy labor market. It will take some time before this slack is fully pared down, we do not see this happening this year. Until it does, however, wage growth will have trouble gaining traction.

Amidst uneven domestic data and still-soft global growth, the U.S. labor market is more than holding its own. That will give the FOMC comfort as to the underlying health of the economy, while restrained wage growth should help ease concerns over rising inflation pressures.