ECONOMIC UPDATE

REGIONS

February 3, 2017

January Employment Report: Strong Headline Covers Mixed Details

- Nonfarm employment rose by 227,000 jobs in January.
- Average hourly earnings rose by 0.1 percent; aggregate private sector earnings rose by 0.3 percent (up 3.7 percent year-on-year).
- The unemployment rate stood at 4.8 percent in January with the broader U6 measure at 9.4 percent.

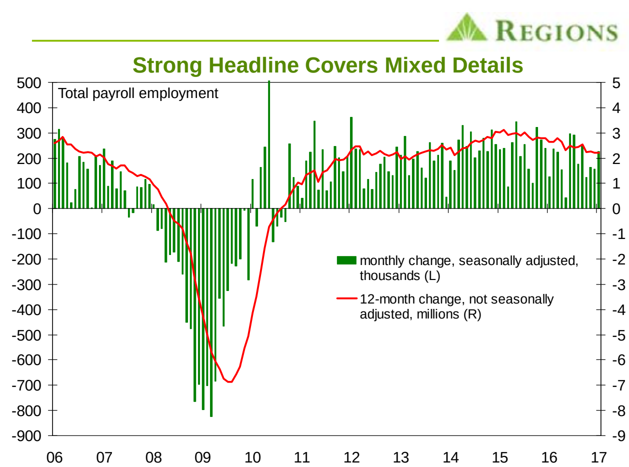
Total nonfarm employment rose by 227,000 jobs in January, with private sector payrolls up by 237,000 jobs and public sector payrolls down by 10,000 jobs. January marks the 76th consecutive month in which the level of nonfarm employment increased, easily the longest such streak on record. We will note that the January data incorporate the results of the annual benchmark revision process into the establishment data, and all seasonally adjusted data going back to 2012 have been revised. The January household data incorporate updated population controls in the CPS, and based on the updated sample the unemployment rate is reported at 4.8 percent in January with the broader U6 rate standing at 9.4 percent. While headline job growth as measured by the establishment survey beat expectations, the underlying details are mixed and, more significantly, the January employment report does not change the broader narrative of the labor market – considerable progress has been made but there is still a notable degree of slack remaining.

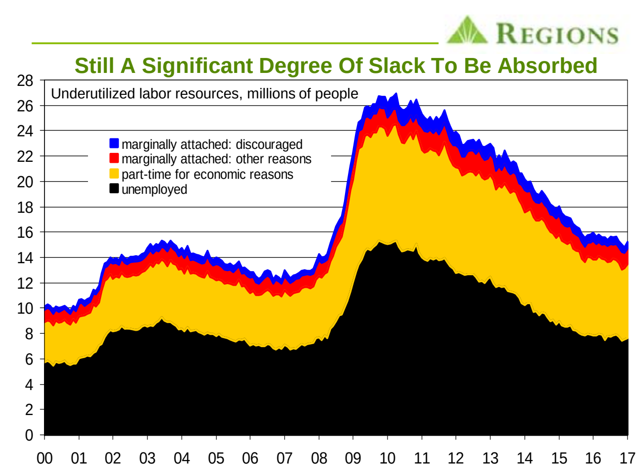
The benchmark revision process resulted in little net change to prior estimates of job growth – prior to the revisions it was reported that total nonfarm payrolls rose by 12.376 million from 2012 through 2016, the revised data put that count at 12.397 million jobs. As to job growth in January, there were broad based gains across private sector industries, led by retail trade, business services, construction, and leisure & hospitality services. We will caution that there is some seasonal adjustment noise in the reported job counts for retail trade and construction. Retailers hired fewer seasonal workers during the 2016 holiday season, meaning there were fewer to be let go in January, fewer than the seasonal adjustment factors were geared for, hence the seasonally adjusted job count is inflated. In construction, weather that was less harsh than normal for most of the month meant there was more construction activity than is typically seen in January, and the seasonal dip in unadjusted construction payrolls was smaller this January than in any year since 2006. This confounded the seasonal adjustment factors and, as with retail trade, reported seasonally adjusted job counts in construction are inflated.

We were encouraged that the length of the workweek is back up to 34.4 hours after having fallen to 34.3 hours in November. This seemingly small change in hours has, in the aggregate, a significant impact on growth in the economy's productive capacity and in total earnings. Still, average hourly earnings were up just one-tenth of one percent in January, leaving them up 2.5 percent year-on-year. To some extent, the "calendar effect" that plagues the hourly earnings series is in play here (the 15th day of January fell outside of the establishment survey week), but we continue to argue that what remains an elevated degree of labor market slack continues to act as a drag on wage growth.

Our point has for some time been that there remains a greater degree of slack in the labor market than is implied by the headline unemployment rate, and the January data do nothing to alter our view. One gauge of labor market slack is the number of "underutilized labor resources," or, the combined number of those unemployed, working part-time for economic reasons, or marginally attached to the labor force. This number, which is the numerator in the calculation of the U6 rate, stood at 15.222 million people as of January, which by our estimates is over 1.5 million above the level that would be seen in a fully healthy labor market. While this number will be further pared down over the course of 2017, we believe it will nonetheless remain a drag on wage growth over much of 2017.

The January employment report is full of mixed messages but yet we see it as an apt reflection of the labor market. As noted above, January's headline job growth number is somewhat boosted by seasonal adjustment noise, but even when accounting for that the underlying rate of job growth remains very healthy. At the same time, however, there remains ample capacity for firms to add to labor input, whether in the form of adding more workers or adding more hours for current workers, without sparking meaningfully faster earnings growth. That will change over coming months, but for now the evolution of the labor market will be encouraging to the FOMC without giving them reason to hasten their expected pace of Fed funds rate hikes.





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