ECONOMIC UPDATE

REGIONS

March 10, 2017

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February Employment Report: The Last Hurdle Has Been Cleared . . . And Easily So

- Nonfarm employment rose by 235,000 jobs in February; prior estimates for December/January were revised up by a net 9,000 jobs.
- Average hourly earnings rose by 0.2 percent; aggregate private sector earnings rose by 0.4 percent (up 4.32 percent year-on-year).
- The unemployment rate fell to 4.7 percent in February (4.703 percent, unrounded); the broader U6 measure fell to 9.2 percent.

Total nonfarm employment rose by 235,000 jobs in February with private sector payrolls up by 227,000 jobs and public sector payrolls rising by 8,000 jobs. Prior estimates for December and January were revised higher by a net 9,000 for the two-month period, but the composition of the revision is striking, as private sector job gains were marked down by 31,000 jobs while job gains in the public sector were revised higher by 40,000 jobs. The unemployment rate fell to 4.7 percent in February while the broader U6 measure, which includes underemployment, fell to 9.2 percent. Average hourly earnings were up 0.2 percent, leaving them up 2.8 percent year-on-year. As with the January data, there is some noise from seasonal adjustment issues in the February report, but we'll say the same thing here we said last month – even after accounting for this seasonal noise, the underlying trend rate of job growth remains solid.

The one-month hiring diffusion index, a measure of the breadth of hiring across private sector industry groups, rose to 63.00 percent in February. Though it has gone largely underappreciated, broad based hiring has been one of the hallmarks of the current expansion. What is striking about the February data, however, is the jump in the hiring diffusion index for the manufacturing sector. In February, 65.4 percent of the industry groups within the manufacturing sector added workers, which is the highest share since November 2014, and as recently as last September this share was below 40 percent, which is basically recession territory. The payroll data are catching up with other indicators of manufacturing activity, such as the ISM Manufacturing Index and the various regional surveys, that are pointing to a rebound in U.S. manufacturing activity.

As in the January data, unseasonably warm weather impacted hiring in the construction industry. The not seasonally adjusted data show a much larger than normal increase in construction payrolls in February, and this was in turn amplified by seasonal adjustment geared for a much smaller increase in the raw data. This February, there were 157,000 people unable to work due to inclement weather, while 606,000 people worked fewer hours than normal due to weather issues, both of these numbers are well below normal for the month of February. As we routinely note, noise in the data due to seasonal adjustment noise in a given month will be reversed in subsequent months, and this will be true of reported hiring in construction. Such payback is evident in retail trade, where the reported decline of 26,000 jobs is payback for the seasonal adjustment noise that led to retail payrolls being overstated in January.

While average hourly earnings were up just 0.2. percent in February, this comes on top of upward revisions to both December and January. We repeatedly note the monthly earnings data are jumpy, and the underlying trend rate of growth, which we put at 2.7 percent, is much more relevant than any one month's data. While still well shy of what we would see were the economy at full employment, wage growth is steadily accelerating as labor market slack is further pared down. Aggregate private sector wage and salary earnings were up 0.4 percent in February, leaving them up 4.32 percent year-on-year, and annualized growth for Q1 is tracking at just shy of 5.0 percent.

How much slack remains in the labor market is of course a topic on which there is considerable debate. Our preferred measure, the number of underutilized labor resources, stood at 14.955 million people in February. This reflects the combined number of those either unemployed, working part-time for economic reasons, or marginally attached to the labor force (this total is the numerator in the calculation of the U6 rate). There were fewer people in each of these buckets in February, but the aggregate number remains well above the 13.0-to-13.5 million people we think is consistent with the economy being at full employment. 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 the year.

Aside from some seasonal adjustment noise, there is little to find fault with in the February employment report. It was said this report was the last hurdle between the FOMC and a March funds rate hike. It is safe to assume that hurdle has been cleared, and quite easily so.

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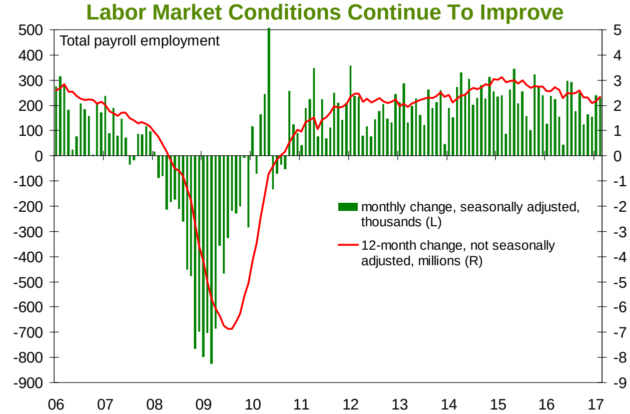
Labor Market Conditions Continue To Improve



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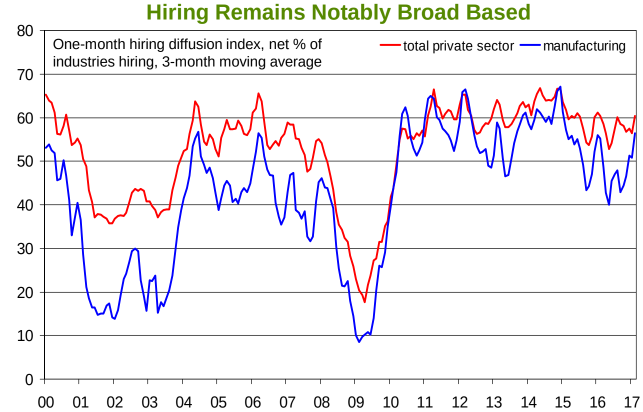
Hiring Remains Notably Broad Based



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