March 30 2015

MARCH EMPLOYMENT REPORT PREVIEW

John Canally, CFA *Chief Economic Strategist, LPL Financial*

KEY TAKEAWAYS

We continue to expect the broad economy could potentially create between 225,000 and 250,000 net new jobs per month in 2015.

Although job growth has improved, wage inflation, an important measure of labor market health, is not yet back to "normal."

A more robust pace of job growth should coincide with an upturn in wage inflation, yet the relationship between the two has been mixed over the past 30 years or so.

The Bureau of Labor Statistics (BLS) of the U.S. Department of Labor will release its always widely anticipated Employment Situation report for March 2015 on Friday, April 3, 2015. April 3, 2015, is Good Friday, and as a result, U.S. (and many European) equity markets will be closed, although the U.S. bond market will be open in the morning to allow markets to react to the report.

As of March 30, 2015, the consensus of economists (as surveyed by Bloomberg News) is expecting the economy to add 250,000 net new jobs in March 2015, following the 295,000 gain in February 2015, and the average gain of 275,000 per month in the 12 months ending in February 2015. The consensus is looking for the unemployment rate to remain at 5.5% and for growth in average hourly earnings—the best proxy for wages in this report—to accelerate to 2.1% year over year from the 2.0% year-over-year gain posted in February 2015. As always, the members of Federal Reserve's (Fed) policymaking arm, the Federal Open Market Committee (FOMC), will be watching the report closely, especially the wage readings, as it deliberates on when to begin raising rates. (Please see our *Weekly Economic Commentary*, "Forecast for Clear Skies: LEI Shows Low Odds of Recession," from March 23, 2015, for more details on what the FOMC is watching.)

In our *Outlook 2015: In Transit*, we noted Fed Chair Janet Yellen and the other members of the FOMC are tracking a "broad range" of labor market indicators [Figure 1]. When the BLS releases the March 2015 Employment Situation report this Friday, market participants and the financial media will likely focus on the payroll job count, the unemployment rate, and wage inflation. In addition, 11 more of the so-called "Yellen indicators" will be updated for March 2015 in this report, which also merit watching.

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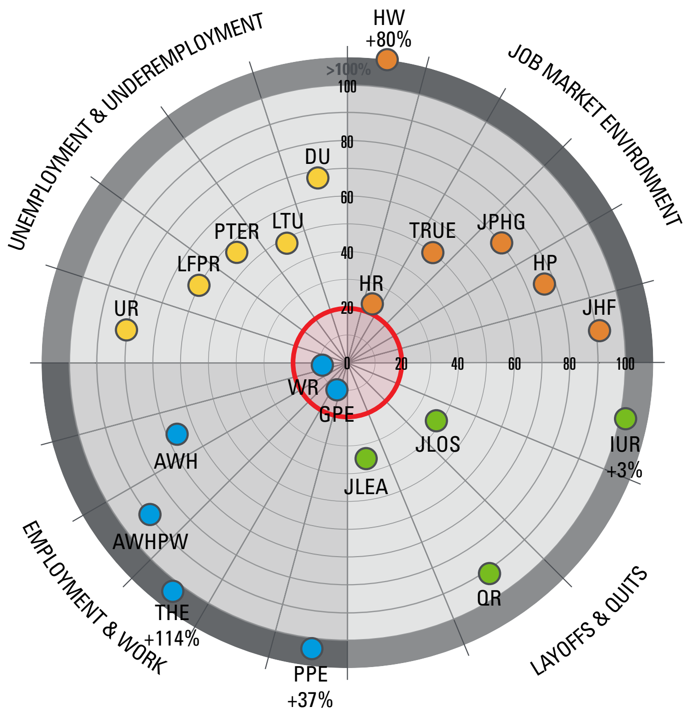
In short, the FOMC and Fed Chair Yellen seemed to be pleased with the progress the labor market has made in the past 12 to 18 months, but remain concerned that the solid performance of the labor market has not yet translated into wage acceleration. A decisive upturn in wage inflation remains key to moving inflation and inflation expectations higher, and in the past several months Yellen and the FOMC have emphasized the inflation side of the Fed's dual mandate (low and stable inflation) rather than the employment side (promote full employment).

1 TRACKING YELLEN'S INDICATORS

Values are scaled.
100% = Prerecession High
0% = Cycle Low

The further the dot is from the center, the closer it is to prerecession levels.

Indicators in the outer ring have exceeded their prerecession levels.



Label	Description
UR	Unemployment rate: % of labor force
LFPR	Labor force participation rate: year-over-year change, % of unemployed
PTER	Part time for economic reasons: % of labor force
LTU	Long-term unemployed: 27 weeks or more, % of unemployed
DU	Duration of unemployment: weeks
HW	Composite help-wanted: index
HR	Hiring rate: % of payroll employment
TRUE	Transition rate from unemployment to employment: % of unemployment
JPHG	Jobs plentiful vs. hard to get: diffusion index
HP	Hiring plans: diffusion index
JHF	Jobs hard to fill: %
IUR	Insured unemployment rate: % of covered employment
JLEA	Job leavers unemployed less than 5 weeks: % of employment
QR	Quit rate: % of payroll employment
JLOS	Job losers unemployed less than 5 weeks: % of employment
PPE	Private payroll employment: millions
GPE	Government payroll employment: millions
THE	Temporary help employment: millions
AWHPW	Average weekly hours (production): hours
AWH	Average weekly hours of persons at work: hours
WR	Wage rates: average hourly earnings, year-over-year % change

Source: LPL Research, Bureau of Labor Statistics, Haver Analytics 03/29/15

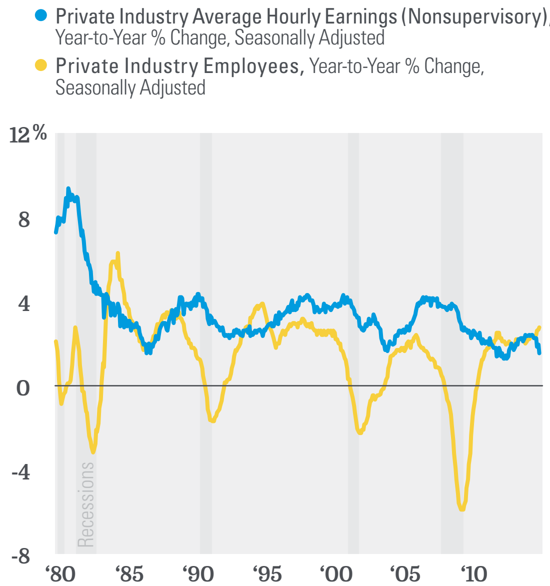
The time frame for all data is the last 10 years: 2004–2014.

JOB GROWTH IMPROVING, BUT WAGE INFLATION STILL BELOW "NORMAL"

Although, in theory, a more robust pace of job growth should coincide with an upturn in wage inflation, the relationship between wages and job creation has been mixed over the past 30 years or so [Figure 2]. In the mid-1980s, the year-over-year percent change in wages began to accelerate just as the year-over-year percent change in private sector jobs did. But in the aftermath of the early 1990s recession, wage acceleration lagged significantly behind acceleration in overall employment as wages didn't begin to accelerate until early 1995, more than three and a half years after job growth began to accelerate.

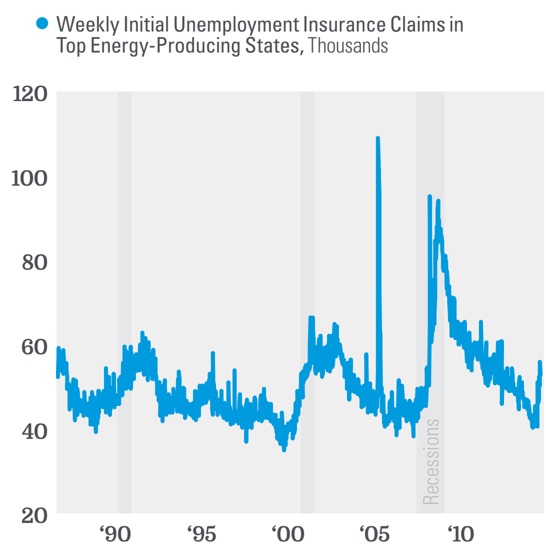
Similarly, the mild 2001 recession ended in late 2001, and job growth didn't begin to accelerate until April 2002. It would be another year or so (March 2003) until wages began accelerating. In the economic recovery that commenced in June 2009, employment began to accelerate in the fall of 2009. Wage growth, however, continued to decelerate for another three

2 THE RELATIONSHIP BETWEEN JOB GROWTH AND WAGE ACCELERATION HAS BEEN MIXED OVER THE PAST 30 YEARS



Source: LPL Research, Bureau of Labor Statistics, Haver Analytics 03/29/15

3 THE DROP IN OIL PRICES IS LEADING TO JOB CUTS IN THE TOP ENERGY-PRODUCING STATES



Source: LPL Research, Haver Analytics 03/29/15

years, and didn't begin to accelerate decisively until late 2012, only to roll over again in late 2014—despite robust (225,000+ per month) job growth in 2013 and 2014. We continue to expect a modest acceleration in wage inflation in the second half of 2015.

OIL'S IMPACT ON THE LABOR MARKET

While the broad labor market continues to heal, the precipitous drop in oil prices has raised concerns about the health of the overall U.S. economy, wages, and in particular, the labor market. (See our *Weekly Economic Commentary*, "Before and After: Monitoring the Effects of Falling Oil Prices," from December 22, 2014, for more details.) Since the start of the year, announcements of job cuts in the oil and gas sector have made headlines, but, as we expected, have not had a major impact on the labor market. For example, in the week ending March 21, 2015, 53,000 people filed claims for unemployment insurance in the eight largest oil-producing states [Figure 3]. Back in June 2014, when oil prices peaked, claims in these eight states were running in the 40,000–45,000 range, so the drop in oil prices and the concomitant cuts to capital spending in the energy sector are now clearly leading to job cuts.

In January 2015, the mining sector (which includes oil and gas extraction and mining support activities) shed 6,000 jobs, and another 9,000 mining and mining-related jobs disappeared in February 2015. We expect these cuts may continue throughout 2015. For reference, this sector of the economy created an average of 4,000 net new jobs per month in the four years ending in December 2014.

Our view is that although mining jobs (where oil production jobs are counted) have increased more than four times as fast as overall private sector jobs since 2009—and pay 30% more per hour—the size of the mining economy relative to the size of the entire U.S. economy is just not big enough to make a meaningful difference economy-wide. However, in certain states, where the mining economy and mining employment is large enough, the expected drop in mining-related employment and economic output may have an impact. (Please see our *Weekly Economic Commentary*, "Drilling into the Labor Market," from January 12, 2015, for more details on the impact of the drop in oil prices on the labor market.)

CONCLUSION

We continue to expect the broad economy could potentially create between 225,000 and 250,000 net new jobs per month in 2015, which should further tighten the labor market and push wage inflation higher in the second half of 2015. We also continue to expect the Fed may begin raising rates in late 2015. But other measures of labor market health—hiring rates, the quit rate, the unemployment rate, and most importantly, wages—still show the labor market is not yet back to normal, and argue against the Fed taking aggressive action to raise rates anytime soon. ■

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