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TD Economics

Data Release: Weak job report will not dissuade the Fed from hiking in June, but 17H2 hikes up in the air

- Non-farm payrolls increased by 138k in May, well below the 182k expected by the street. Revisions to the previous two months' of payrolls subtracted 66k positions, with April and March hiring reduced to 174 and 50k, respectively. As a result, the three-month moving average of job growth slowed from 174k to 121k.

- Private payrolls rose by 147k, some 28k below consensus expectations. Private-services hiring was once again led by health care & education (+47k), business services (+38k), leisure & hospitality (+31k) and finance (+11k). Goods hiring was meager, with construction (+11k) and mining & logging (+5k) up slightly while manufacturing (-1k) was largely flat. Government hiring (-9k) was weak, as federal level hiring (+8k) was more than offset by sharp cutbacks at the local and state level (-17k).

- The unemployment rate ticked down by 0.1 percentage points to 4.3% as 429k Americans left the labor force in the month of May. As a result of the exodus from the workforce, the labor participation rate fell 0.2 percentage points to 62.7% - the lowest level in six months. The shrinkage of the labor force also led to an improvement broader underemployment measures, with the broadest measure (U-6) down 0.2pp to 8.4%.

- Average hourly earnings rose by 0.2% during the month, on par with expectations, with the year-over-year wage metric holding steady at 2.5% in May.

- Average weekly hours were unchanged at 34.4.

Key Implications

- It is hard to find good news in the May report. The headline print disappointed expectations, contrary to the strong ADP print mid-week. Alongside the large downward revisions to prior months', trend payroll growth slowed from 174k prior to the report to just 121k given the new data. Moreover, the diffusion index – which measures the breadth of the gains across industries – pulled back to sharply to 54.8 – the lowest level since November 2016.

- The one sliver of positive news was the decline in the jobless rates. The headline (U3) declined to 4.29%, or the lowest level in sixteen years, while the broadest measure (U6) fell to the lowest level since late-2007. Still, most of this is related to the decline in the labor force with participation rates lower in aggregate as well as for the core age group.

- To make matters worse the wage print, while decent at 0.2% m/m in May, did not show as much strength as would be suggested by the very low jobless rates. Having said that, this metric should begin to grind higher in the coming months, and should help put some upward pressure on inflation. As such, we still expect the Fed to hike rates by 25 basis points when the FOMC meets the Wednesday after next, but the probability of additional rate hikes later this year is diminishing.

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