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MACRO MORNING BRIEFING

November 4, 2024

After Storm Damaged Payrolls, Fed to Cut 25bp

- Even adjusting for weather-related distortions and strike activity, the labor market shows signs of slowing
- The household survey suggests employment growth is stabilizing
- PCE inflation was well-behaved, allowing the Fed to cut 25bp this week
- Vols have risen ahead of the election, but may have reached their upper levels

Beyond the Weather, Labor Continues to Slow

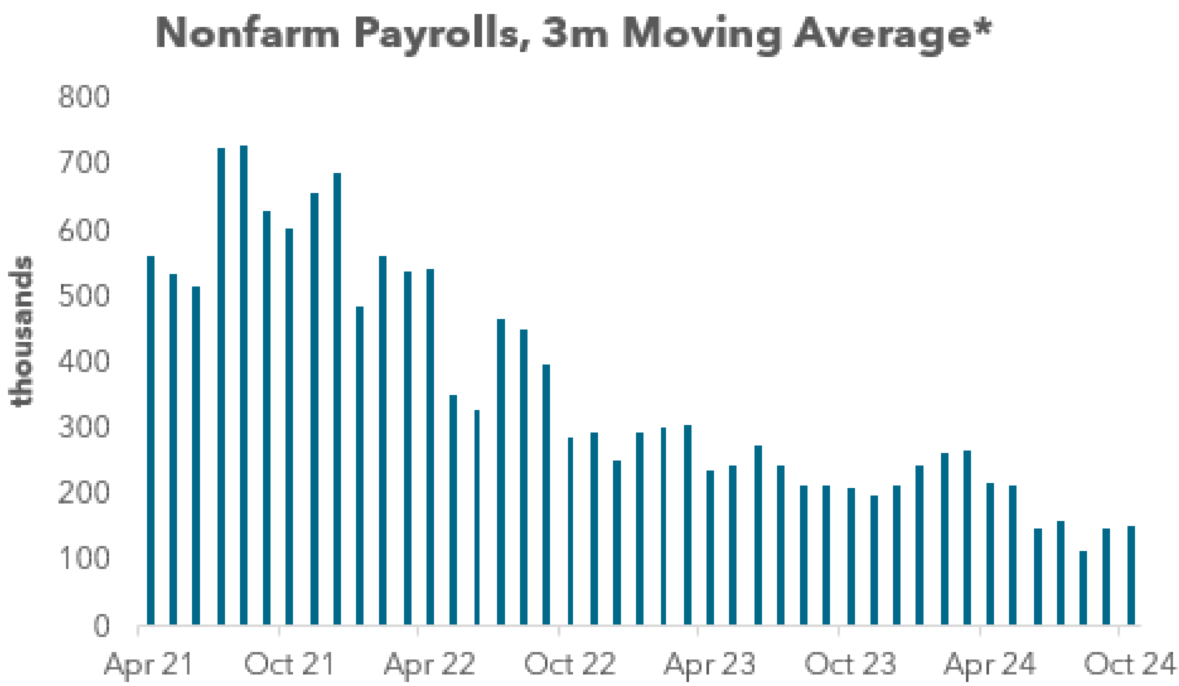
The October jobs report was marred by hurricane- and strike-related distortions and printed surprisingly low 12k new jobs. Consensus expectations, which presumably incorporated the weather and industrial action, were expecting 100k jobs to be produced, but the range of expectations was particularly high. Even if adjusted for these distortions, we think that the pace of job creation is decelerating, keeping the Fed on track to cut rates by 25bp later this week.

We tend to agree with estimates that put the jobs understatement at approximately 100k-150k, which, if accurate, would have put the final print near 150k new jobs for October. This, in turn, would put the current three-month average for job creation at 150k also, close to recent lows, as seen in Exhibit #1. For reference, the average monthly pace of job creation in the seven years before the pandemic was just under 200k, and in 2019, it was 166k. Recall, in 2019 the Fed was initiating a rate easing policy.

Given the difficulties presented in the establishment survey this month, we prefer to look at the household survey for a good read on the employment situation. The unemployment rate was steady at 4.1%. To two decimal places, however, the unemployment rate went up nearly one-tenth of a percent, from 4.05% to 4.14%.

Nevertheless, the Sahm rule is no longer triggered. This rule, which we have written about quite a bit in the past months (see here, for example), states that if the three-month average of the unemployment rate sits 0.5% or more above the lowest unemployment rate achieved in the past 12 months, the US economy is recession. This threshold was reached with the July jobs report and maintained through this October report.

Exhibit #1: Inching Lower



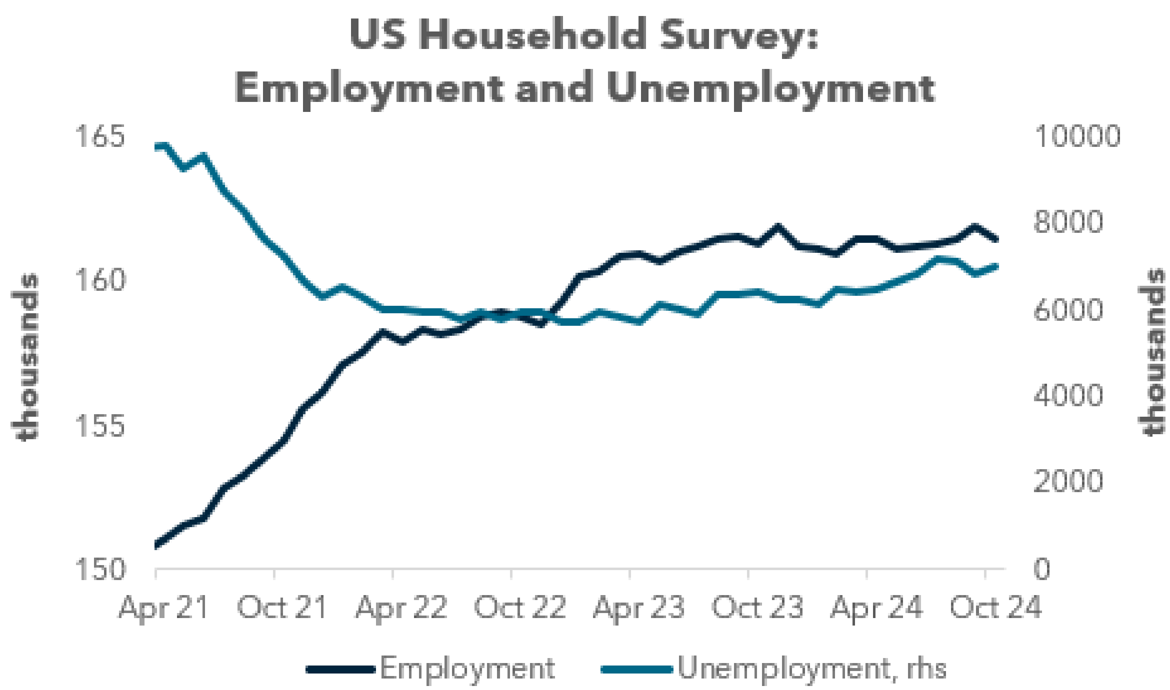
Source: BNY Markets, Bureau of Labor Statistics

*Note: Includes an assumed NFP growth of 150k in October, adjusting for weather- and strike-related distortions

Distortions or not this month, we view the labor market as slowly weakening, enough so that the Federal Reserve will not be deterred in lowering rates at its next two FOMC meetings, this coming Thursday and again on December 18. Looking at Exhibit #2, we see from the household survey that employment growth (dark line) has leveled off in 2024, while unemployment is slowly creeping higher.

Furthermore, from the household survey, job losers – who are defined as workers who were laid off or ended temporary employment – jumped up to 1.835m, having averaged 1.642m people in the 12 months prior. This, combined with a rising layoff figure from the September JOLTS survey, also released last week (1.833m vs. a 12m average of 1.623m), suggest firms are slowly starting to shed labor. It should be pointed out, however, that the job losers and layoffs data are still commensurate with levels seen before the pandemic, which averaged 1.820m and 1.342m, respectively, in 2019.

Exhibit #2: Employment Growth Stalling



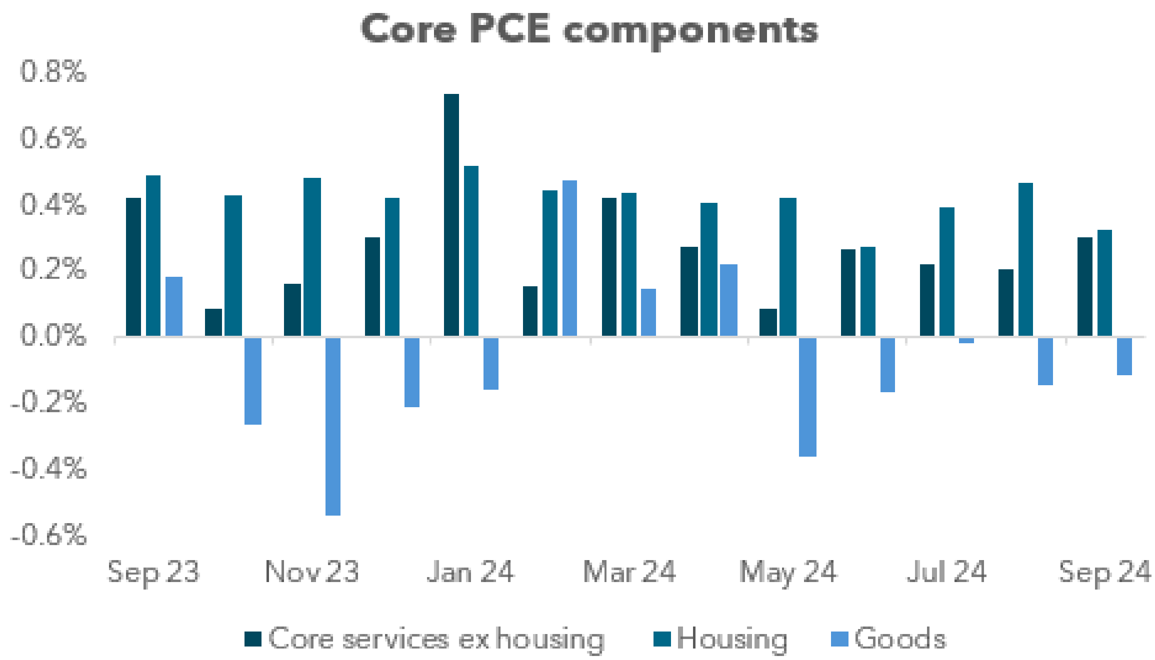
Source: BNY Markets, Federal Reserve Bank of San Francisco

In short, the labor market is slowing still and, as we said, will keep the Fed in easing mode. However, it is more of a levelling off from a period of excessive tightness, and compatible with a soft landing, provide the Fed continues to ease from its restrictive policy stance.

Assisting to keep the Fed in easing move was the constructive PCE inflation print last Thursday. Headline inflation was down to 2.1%, in line with expectations, although core PCE did nudge higher to 2.7%. This progress on disinflation should be more than enough, when combined with the labor data, to keep the easing cycle intact.

From Exhibit #3 we can see that the three main components of core PCE – housing, core services ex housing, and core goods – have different profiles, however. Goods price inflation was negative, consistent with recent months. Housing is still elevated but continues its very slow descent – commensurate with the behavior observed with rental prices “on the street.” Core services ex housing remains volatile and elevated. This is the biggest impediment to getting overall core prices lower. As the labor market and wages continue to ease, we would expect this measure to slowly resume its decline.

Exhibit #3: Core PCE Components Mixed



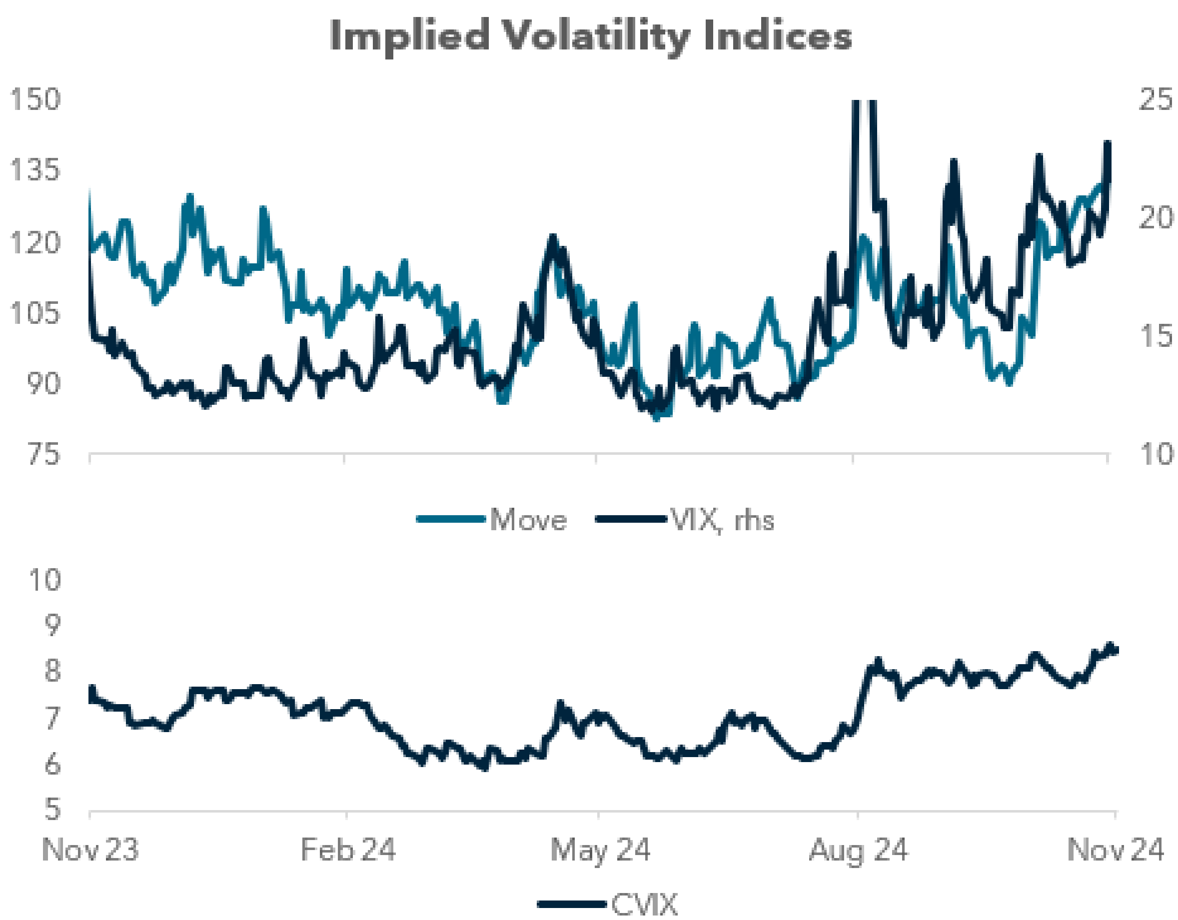
Source: BNY Markets, Bureau of Economic Analysis

Of course, the Fed meeting will take place this week just two days after a national election which promises to be too close to call from where we sit. The future occupant of the White House, as well as the composition of both houses of Congress are up for grabs and remain open questions. We don't think any political fall out in the immediate post-election period will dissuade the Fed from making monetary policy this week.

Volatility in financial markets has been increasing this month. Exhibit #4 shows the implied volatilities, derived from options prices, for equities (VIX, dark line), sovereign bonds (MOVE, light blue line) and currencies (CVIX, bottom panel). Not that volatilities are rising across asset classes. The VIX in particular has settled down somewhat from levels it reached during the market sell-off in early August (literally "off the charts" at 39 on August 5) but is still elevated above earlier levels. CVIX and MOVE are clearly rising going into the vote.

We're not sure if there will be much scope for these vols to rise during the week. Even though a winner may well not be formally declared on Tuesday night or Wednesday morning, if events resemble 2020, the market could have a good idea within a day or two who the likely winner will be based on the distribution of any remaining uncounted ballots. This is how things played out in the last cycle. Even though Joe Biden wasn't officially declared the winner until the Saturday after the Tuesday vote, it was quite clear by Wednesday that uncounted swing state ballots were sufficient to put Biden over the top. If events play out in the next few days according to this script, we may avoid a messy and volatile "interregnum" period.

Exhibit #4: Vols Rising – Can They Go Higher?



Source: BNY Markets, Bloomberg

Disclaimer & Disclosures

Please direct questions or comments to: iFlow@BNY.com

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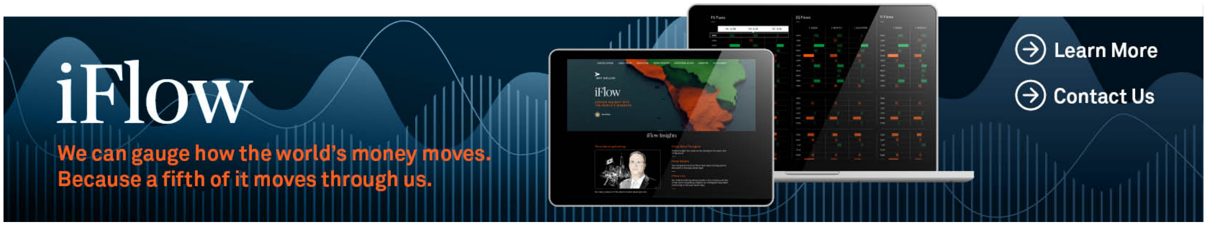

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