WEEKLY
Economic Commentary

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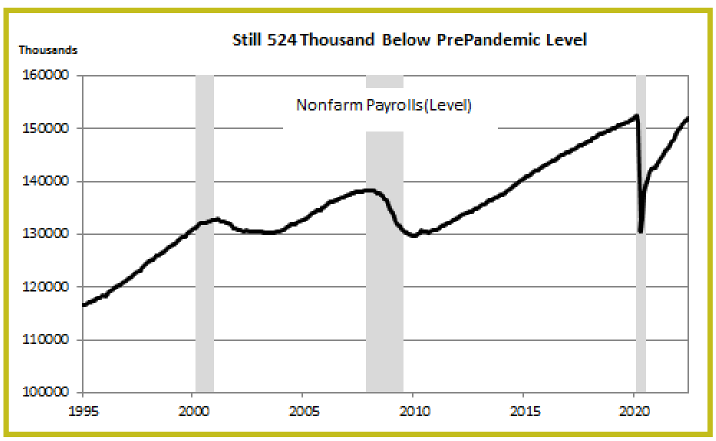
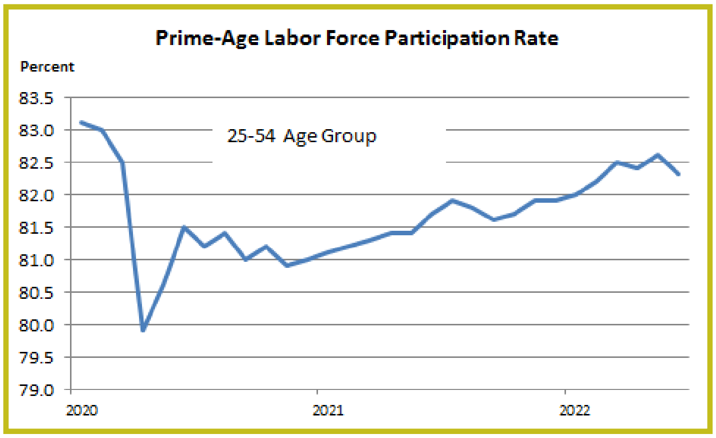
Millennium
CORPORATE CREDIT UNION

It wasn't exactly a Goldilocks report, but the latest jobs numbers were comforting enough to keep the bears at bay. For sure, fears that the economy is running too cold and on the precipice of a recession – if not already in one – received little support from the sturdy increase in nonfarm payrolls last month. The 372 thousand gain in June significantly exceeded the more Goldilocks-like consensus estimate of a 250 thousand increase. The latest advance in job growth follows hefty increases of 384 thousand in May and 364 thousand in April, although the latter was revised down by a sizeable 68 thousand from the previous estimate. Still, a job gain of close to 400 thousand is hardly consistent with an economy that is on the cusp of a downturn.

Conversely, the jobs report throws a splash of cold water on fears that the economy is overheating. Even with the above-consensus increase last month, the trend in job growth is cooling. The average monthly increase in nonfarm payrolls over the past three months slipped to 375 thousand from 539 thousand in the first quarter and a monthly average of 562 thousand in 2021. And while worker shortages are still a major complaint of companies seeking to fill positions, it is not as if the economy is running out of bodies. Even with the healthy payroll gains in recent months, the number of workers receiving paychecks is still 524 thousand below where it was just prior to the pandemic recession.



To be sure, with nearly two job openings for every unemployed person, that shortfall does not reflect insufficient demand for workers. Instead, companies are still having difficulty getting workers off the sidelines. The labor force participation rate unexpectedly slipped from 62.3 percent to 62.2 percent last month, arresting the grudging climb back to its 63.4 percent prepandemic level from a 60.2 percent recession low. Nor is it the fringe group of workers -- the older, teens or those in part-time jobs – that dropped out. The prime-age 25-54 year old cohort – the bed-rock of the workforce – exhibited the biggest drop in participation, as the rate fell 0.3 percent to 82.3 percent. The setback in participation may well be a one-month aberration, but the rise in Covid cases could also be having an impact. The seven-day positivity rate jumped above 100 thousand since the middle of May from around 30 thousand in March and early April.



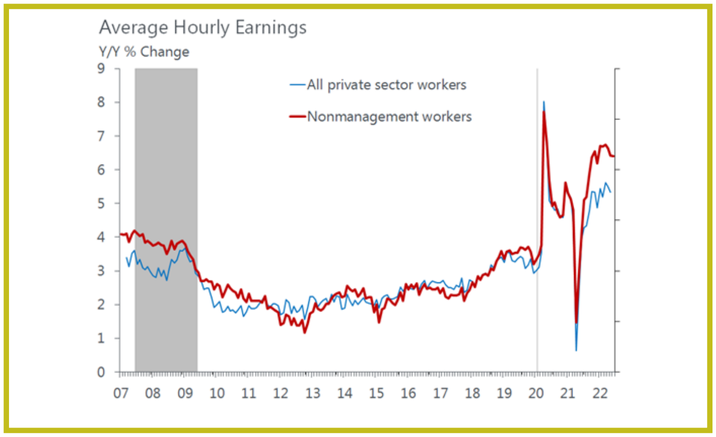
The setback in the participation rate is the main reason the unemployment rate held at a historically low 3.6 percent last month, just a tad above the 50-year prepandemic low of 3.5 percent. It also highlights the stark discrepancy in outcomes between the Labor Department surveys of households and businesses that occasionally occurs and throws out confusing signals on the job market. While the business survey revealed the headline payroll increase of 372 thousand last month, the household survey exhibited a more downbeat result, revealing a 315 thousand decline in employment. It is not unusual for the two surveys to show conflicting results for a single month, but household employment has fallen in two of the past three months, in sharp contrast to the sturdy three consecutive increases in nonfarm payrolls from the business survey.

Simply put, the latest jobs report provides ammunition for both the hawkish and dovish sides of the economic ledger. The hawks who believe the economy is still going full steam ahead and needs demand-stifling policies to rein in inflation can point to robust payroll gains and low unemployment to support their case. As long as the labor market is generating muscular increases in paychecks and plentiful job opportunities for those out of work or seeking a change in positions for better pay, the economy has ample fuel for growth. Against this backdrop, households would have the purchasing power to absorb higher prices and keep on spending and, hence, stoke the forces spurring inflation. That, in turn, stiffens the Fed's resolve to cool off demand and short-circuit a rise in inflationary expectations, resulting in steeper rate hikes than otherwise.

But the more dovish camp can also draw some encouragement from the jobs report. As noted, job growth, while exceeding expectations, is slowing. It's important to remember that the job market lags changes in the overall economy, particularly around cyclical turning points. In general, companies tend to retain workers amid signs of slowing growth until they are sure that the slowdown is lasting That lag in laying off workers is likely to be amplified now given the acute labor shortage that companies have faced over the past year. What's more, healthy balance sheets and still-elevated profit margins allow companies to absorb a temporary bulge in labor costs as a hedge against a staffing shortage if conditions quickly turn firmer.

That said, the economy faces mounting headwinds, including higher interest rates, deteriorating household sentiment, slowing global growth and lingering Covid-related health issues that will restrain activity and undermine the willingness of companies to hold on to workers. As the growth engine downshifts in coming quarters, which we expect, so too will job growth. Importantly, the latest jobs report provides a kernel of encouragement for inflation doves, as it suggests that upward pressure on prices from rising wages is losing steam. Average hourly earnings increased by 0.3 percent in June and are up at a 4.2 percent annual rate over the last three months, much slower than the 5.1 percent increase over the past year. Indeed, that year-over-year increase subsided from 5.3 percent in May and a nearby peak of 5.6 percent in March.

Happily for lower wage workers, the slowdown in wage gains is more pronounced among the more richly compensated workers. Average hourly earnings for non-management workers increased 6.4 percent from a year ago, matching the previous month's increase, and the monthly gains have exceeded the increases for all private workers by more than 40 percent over the past three months. Still, wage increases across the board have slowed in recent months, indicating that a wage-price spiral is not gaining traction. There are signs that businesses are losing some pricing power as consumers are shifting purchases to lower priced goods or foregoing some outlays entirely. That trend points to some feedback effect, as companies would resist giving ever-larger wage increases if the increased labor costs cannot be passed on in the form of higher prices.



From the Fed's perspective, the latest jobs report provides little reason to alter its near-term plans to keep hiking rates. In recent weeks, the financial markets had priced in lower odds that the Fed would hike rates by 75 basis points at its upcoming FOMC meeting on July 27-28, reflecting an array of incoming data that tracked weaker than expected activity and falling commodity prices that suggested inflation had peaked. However, market sentiment has shifted once again this week following the release of the FOMC minutes from the June meeting, which was more hawkish than expected, and comments of some Fed officials this week advocating a 75 basis point hike in the funds rate later this month.

From our lens, the June jobs report, while a mixed bag, does solidify the Fed's plan to raise its short-term rate by 75 basis points at its next policy meeting. The one development that would deter it from doing so is an abrupt deterioration in job conditions. The latest jobs report clearly indicates that is not happening yet, nor does anecdotal evidence of labor shortages suggest otherwise. Inflation may have peaked, but it remains well above the Fed's comfort level and is likely to stay elevated for at least several more months.

KEY FINANCIAL INDICATORS

INTEREST RATES	July 8	Week Ago	Month Ago	Year Ago
3-month Treasury bill	1.88%	1.67%	1.34%	0.05%
6-month Treasury bill	2.57	2.48	1.96	0.05
3-month LIBOR	2.43	2.29	1.72	0.12
2-year Treasury note	3.12	2.84	3.07	0.22
5-year Treasury note	3.13	2.89	3.27	0.79
10-year Treasury note	3.08	2.89	3.16	1.36
30-year Treasury bond	3.25	3.12	3.20	1.99
30-year fixed mortgage rate	5.30	5.70	5.23	2.90
15-year fixed mortgage rate	4.45	4.83	4.38	2.20
5/1-year adjustable rate	4.19	4.50	4.12	2.52
STOCK MARKET				
Dow Jones Industrial Index	31338.15	31097.26	31392.79	34870.16
S&P 500	3899.38	3825.33	3900.86	4369.55
NASDAQ	11635.31	11127.85	11340.02	14701.92
COMMODITIES				
Gold ($ per troy ounce)	1740.30	1810.10	1875.20	1808.80
Oil ($ per barrel) - Crude Futures (WTI)	104.36	108.40	120.49	74.67

KEY ECONOMIC INDICATORS

	Latest Month/Quarter	Previous Month/Quarter	Two-Months/ Quarters Ago	Average-Past 6 Months or Quarters
ISM Services Activity Index (June)	55.3	55.9	57.1	57.2
Nonfarm Payrolls (June) - 000s	372	384	368	457
Unemployment Rate (June) - Percent	3.6	3.6	3.6	3.7
Average Hurly Earnings (June) - % chg	0.3	0.4	0.3	0.4

Millennium Corporate Credit Union
8615 West Frazier Street
Wichita, Kansas 67212