

## Has the US labour market turned a corner?

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US core CPI came in ahead of expectations last week, for the third month in a row. At 3.8% year-on-year, core inflation is clearly still too high for Fed officials to relax.

With core goods inflation at -0.1%,<sup>1</sup> blame lies with the service sector, which, once one strips out housing-related items (referred to as shelter) is mainly driven by labour costs.

Median nominal wage growth in the US in 2023 was 5.2%<sup>2</sup>, which sounds high versus a target inflation rate of around 2-2.5% on CPI. However, considering productivity growth of 2.6%<sup>3</sup> over the same period, businesses only needed to raise prices by 2.6% on average in order to maintain margins (5.2% minus 2.6% productivity growth). In other words, 2-2.5% inflation is in sight.

Looking forward, the concern is what will happen if productivity growth falls closer towards its medium term<sup>4</sup> average of 1.4%. What are the prospects for nominal wage growth following suit? This question is the reason why there is so much interest in the labour market at present.

When trying to capture a market consisting of hundreds of millions of people, it's no surprise that the data isn't perfect. Different definitions mean individuals fall in and out of certain categories at different times, which serves to reduce the usefulness of any one labour market indicator (by way of example, I recently read a great article by TwentyFour Asset Management's David Norris<sup>5</sup>, which describes the different methodologies used to calculate US employment and how they end up giving different signals at times).

Hence it's important to look at a range of time series. For consistency, I've included observations over the last 20 years for each of them. Headline US unemployment at 3.9% at the end of February is low: 18th percentile<sup>6</sup>. Underemployment, which is a broader measure of unemployment that includes categories like discouraged

workers, is currently 15th percentile<sup>7</sup>. Initial jobless claims is 3rd percentile<sup>8</sup> and continuing jobless claims are 29th percentile<sup>9</sup>. For all these indicators, a low percentile rank indicates a tight labour market. Switching to indicators where high rankings indicate the same, the three-month average increase in nonfarm payrolls is 72nd percentile<sup>10</sup> and unfilled positions amongst small businesses is currently in the 79th percentile<sup>11</sup>, the latter according to the monthly survey by the national federation of independent business (NFIB). All looking pretty hot.

However, all are demonstrating more slack compared to 6 months ago, with the exception of initial and ongoing jobless claims which underwent a revision last week. Moreover, hiring plans amongst small businesses, which is one of the best forward looking indicators for the labour market, have swung from tight to relatively slack: 44th percentile vs 68th percentile 6 months ago<sup>12</sup>.

Taken together, the US labour market does appear to have turned a corner and to be making steady, albeit slow, progress. Other things being equal, this is good news for inflation looking forwards and more good news re the state of the US economy.

Sources: <sup>1</sup>Bloomberg Finance L.P., US CPI Commodities Excluding Food and Energy Commodities contribution to All Items Less Food and Energy NSA YoY (ECANYA4K). <sup>2</sup>Bloomberg Finance L.P., US Atlanta Fed Wage Growth Tracker Median (WGTRMEDI). <sup>3</sup>Bloomberg Finance L.P., US Nonfarm Business Sector Output per hour of all persons YoY SA (PRODNFRY). <sup>4</sup>10 year and 20 year averages, to 1 d.p. <sup>5</sup>Unemployment in the US: a tale of two surveys by David Norris, Partner and Head of US Credit. The TwentyFour Blog, 12 March 2024. <sup>6</sup>Bloomberg Finance L.P., U-3 US Unemployment Rate Total in Labor Force Seasonally Adjusted (USURTOT). <sup>7</sup>Bloomberg Finance L.P., US U-6 Unemployed & Part Time & Margin % Labor Force & Margin SA (USUDMAER). <sup>8</sup>Bloomberg Finance L.P., US Initial Jobless Claims 4-Week Moving Average SA (INJC4). <sup>9</sup>Bloomberg Finance L.P., US Continuing Jobless Claims NSA (INJCSPNS). <sup>10</sup>Bloomberg Finance L.P., US Employees on Nonfarm Payrolls Total MoM Net Change SA (NFP TCH). <sup>11</sup>Bloomberg Finance L.P., NFIB Small Business Job Openings Hard to Fill (SBOEMPL). <sup>12</sup>Bloomberg Finance L.P., NFIB Small Business Hiring Plans Index (SBOIHIRE).

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