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Flash Macro Update

U.S. Jobs Report | May 2024

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What You Need to Know

1 How are we thinking about the April U.S. jobs report?

The U.S. payrolls report for April showed a cooling but healthy labor market, consistent with the balanced economic backdrop that Chair Powell described in making his case for patience at the May FOMC.

Our Take: We continue to think the Fed will still be more focused on its inflation mandate than its employment mandate in coming months (which is why we see them holding short rates at 5.375% through year-end, versus the consensus expectation for 2 rate cuts).

WHAT DO WE THINK THIS MEANS FOR MARKETS?

- **In our view, this report will lead to some dollar weakness, higher equity markets, and lower bond yields.** Bigger picture, higher nominal GDP allows for faster earnings growth, which is an important driver for global risk assets.
- **The jobs details are market friendly and in-line with our 'Glass Half Full' thesis**. Employment was below consensus at 175,000, compared to a consensus of 240,000. Remember we believe that the steady state should be around 125,000-150,000 jobs. Besides upwards revisions for the last month (315k, up from 303k), most of the data was on the cooling side, including lower average annual earnings (3.9% versus 4.0% estimate) and a higher unemployment rate (3.9% versus 3.8% estimate).
- **Important change in job composition with Services narrowing:** While Services continues to be the key driver of employment growth (fully 87% of total jobs), it was

all almost all Healthcare/Education this month. All told, 95,000 job of the total 167,000 private sector jobs (or 57% of private sector total) came from just Healthcare/Education. By comparison, Leisure/Travel dropped to 5,000 jobs this month from 53,000 last month, while Government jobs dropped to 8,000 from a robust 72,000 last month. So, in aggregate, these three sectors accounted for 57% of total jobs, compared to almost 70% last month.

- **Does this more benign jobs report challenge our *Regime Change* thesis**? Our answer is no. Without question, wage growth dipping below four percent year-over-year is a good thing, but it still remains well north of the three percent year-over-year or so that was recorded during pre-pandemic periods. Beyond stickier wages, the other three factors central to our thesis are ongoing geopolitical tensions, a messy energy transition, and heightened fiscal spending. In aggregate, these four drivers continue to suggest a higher resting heart rate for inflation and nominal GDP, a backdrop which has huge implications for asset allocation. If we are wrong in our outlook, we would be most focused on a potential decline in productivity because it would unfortunately add the 'stag' to the ongoing 'flation' we continue to see. At present we do not see productivity softening, but its continued positive trajectory is increasingly becoming a bigger part of our Glass Half Full thesis heading into 2025.

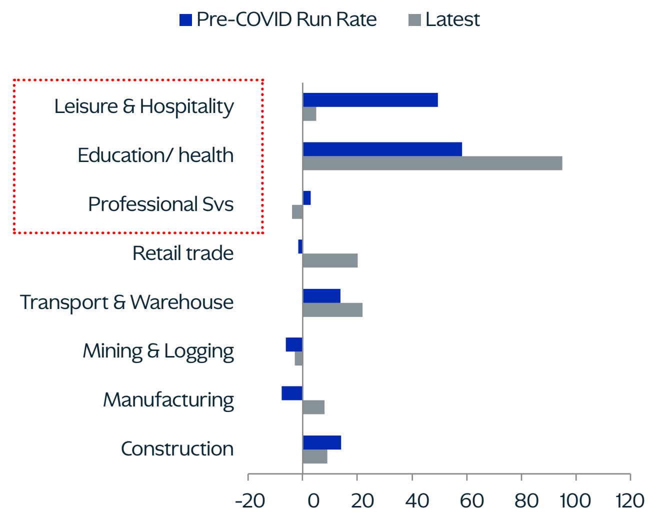
KEY TRENDS IN THE DATA

- April data – as well as revisions to prior-month data – suggest job gains are starting to run at a more normalized pace, which should help alleviate market anxiety about more Fed hikes. That said, we see this report as being broadly consistent with a labor market that is coming into balance (versus one that is slowing sharply) – e.g., the unemployment rate ticked up 10 basis points but remains below four percent, and household employment actually surged – which is why we still do not think Fed 'insurance cuts' are on the table.
- Participation held flat at 62.7% and remains about 70 basis points below pre-COVID levels. Immigration is helping to drive labor force growth in the near term, though we continue to think that slower demographic growth and an aging population will weigh on worker availability over the longer term.
- Private service-providing payroll (+153k, down from +204k in March) drove the bulk of private payroll gains this month, with job gains concentrated in stable Services categories like Education and Healthcare (+95k). However, Leisure and Hospitality employment was weak (+5k, down from an average of +25k in the last three months), and Temporary Help employment continues to contract. Our big-picture view is that labor demand is cooling, although we do not expect a GFC-like surge in layoffs this cycle.
- Goods producing payrolls added just 14k jobs, down from +39k in March. Construction hiring slowed meaningfully (+9k, versus +40k in March) while Manufacturing grew +8k after contracting for two months in a row. Overall, we think the Goods employment picture looks consistent with recent ISM data, which shows Goods activity toggling between expansion and contraction.
- By sector, employment across Finance, Tech, Professional Services, Construction, Manufacturing, Transport/Warehouse, Education/Healthcare, and Retail and Wholesale Trade are all well above pre-pandemic levels. By comparison, Leisure & Hospitality employment remains slightly below its pre-COVID peak, although hiring in the sector has slowed following a period of extensive backfilling in the last two years.
- Month-over-month wage growth slowed to +0.2% m/m from +0.3% m/m in March, and the year-over-year measure fell to 3.9% from 4.1% last month (the lowest reading since 2021). We think slowing wage growth should give markets and the Fed more confidence that the labor market is coming into balance, which should help ease pressure on wage and price growth in coming quarters.
- Non-cyclical sectors like Education/Healthcare are providing a ballast to overall hiring, while labor hoarding is helping to limit the 'tail risk' of widespread layoffs (with the exception of over-

hired Tech/Information jobs). Overall, our take is that the 'resting rate' for monthly job growth likely remains a bit North of this report, as the slowdown in Leisure and Hospitality looks anomalous (recall that employment in the sector is still more than five percent below pre-pandemic trend).

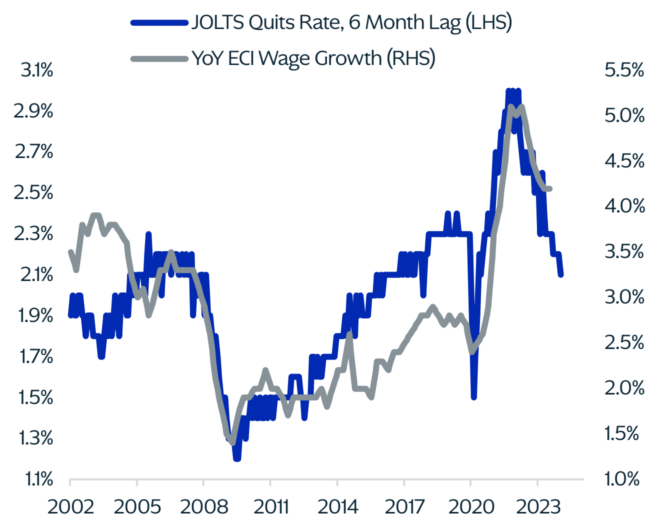
Against this backdrop, we continue to think the Fed will still be more focused on its inflation mandate than its employment mandate in coming months (which is why we see them holding short rates at 5.375% through year-end, versus the consensus expectation for 2 rate cuts).

Exhibit 1: Job Gains Are Narrowing as Labor Demand Starts to Normalize



Data as at April 30, 2024. Source: Bureau of Labor Statistics, KKR Global Macro & Asset Allocation analysis.

Exhibit 2: We Agree with Chair Powell that a Cooling Labor Market Will Result in Cooler Inflation in 2H24, Though We Think This Process May Take Longer to Play Out Than Markets Expect



Data as at March 31, 2024. Source: Evercore-ISI, Bloomberg.

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