ECONOMIC UPDATE

REGIONS

August 3, 2018

July Employment Report: Noisy July Report, But Trend Job Growth Remains Solid

- Nonfarm employment rose by 157,000 jobs in July; prior estimates for May/June were revised up by a net 59,000 jobs
- Average hourly earnings rose by 0.3 percent; aggregate private sector earnings rose by 0.1 percent in July (up 4.9 percent year-on-year)
- The unemployment rate fell to 3.9 percent in July (3.871 percent, unrounded); the broader U6 measure fell to 7.5 percent

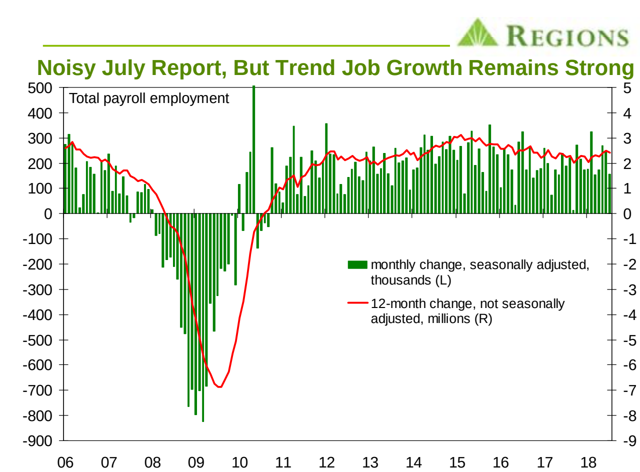
Noisy. If there is a single word to describe both the July employment report itself and the reaction to the July employment report, we're gonna have to go with "noisy." Total nonfarm employment increased by 157,000 jobs in July, below our forecast of 188,000, with private sector payrolls rising by 170,000 jobs and public sector payrolls falling by 13,000 jobs. Average hourly earnings rose by 0.3 percent, good for a year-on-year increase of 2.7 percent. The unemployment rate slipped to 3.9 percent and the broader U6 measure fell to 7.5 percent on a sharp decline in the number of those working part-time for economic reasons.

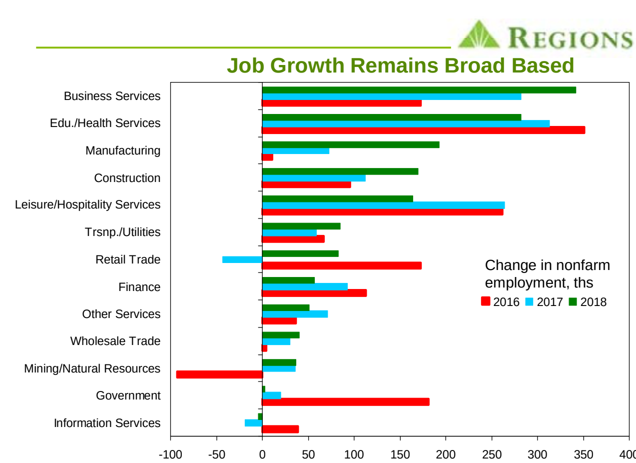
Those whose focus extends no further than the below-consensus increase in payrolls can pick between two explanations – firms are running out of workers to hire or tariffs are undermining business confidence so firms are pulling back on hiring. Hey, we didn't say there are two possible explanations that are actually correct, only that there are two possible explanations. The reality is that while there is a certain element of noise in any economic data release, there is considerably more noise in the July employment report than is typical, and the July employment has to be, or at least should be, put in the context to what were some significant revisions to prior estimates for May and June. For instance, net job growth for the two-month period was revised higher by 59,000 jobs, with 53,000 more jobs added in the private sector than previously reported. As such, even with the slower pace of job growth in July, which will surely be revised in subsequent months, over the past 12 months average monthly job growth still sits at 201,000 (not seasonally adjusted).

In our preview of the July employment report, we noted that response rates to the monthly establishment survey have been notably low in 2018, with each month's response rate lower than the same month of 2017. Our point was that these low response rates suggest sizeable revision to the initial estimate in any given month. This pattern persisted in July, which is one reason to expect the initial July print to be revised. The details of the report cast further suspicion on the initial estimate for July. For instance, retail trade payrolls are reported to have risen by 7,100 jobs, but beneath this seemingly innocuous estimate we see that payrolls amongst toy/hobby/book/sporting goods stores fell by 31,800 jobs while payrolls amongst general merchandise stores rose by 14,200 jobs. While the former can be attributed to the demise of Toys R Us, we can make no sense out of the latter. This of course doesn't mean it isn't a valid number but it is one to watch for revision. The decline in public sector payrolls also merits mention. The entire 13,000 job decline is more than accounted for by a 20,000 job decline in local government payrolls, of which 13,900 come from education. As we've often noted, the changing timing of the school year makes it difficult to properly adjust the data in this sector, so the reported decline for July is more noise than anything else

In our preview of the July employment report we also noted that the length of the average workweek in June was a rounding error away from having risen to 34.6 hours. As it turns out, the revised data show that indeed the length of the workweek did rise to 34.6 hours in June. This means growth in aggregate private sector wage and salary earnings is almost twice as fast as the initial estimate. The bad news, however, is that the initial estimate for July shows the length of the workweek slipped back to 34.5 hours (mainly due to the mining/natural resources sector). As such, even with a slightly larger increase in average hourly earnings than we had anticipated, aggregate private sector earnings rose by just 0.1 percent, leaving them up 4.9 percent year-on-year. As to the notion that firms are "running out of workers," it's still not the case despite the net change in the labor force being much smaller in July (105,000) than in June (601,000). The data on labor force flows show over 4.8 million people transitioned from not in the labor force in June to employed in July; for months we've been pointing to this metric as evidence of a still high degree of labor market slack, and that remains the case.

The "miss" on forecasts of July job growth does nothing to alter our view that the labor market remains rock solid. That is best seen in a trend rate of job growth hovering around 200,000 per month, and a still-heavy flow of people into the labor force should ease concerns of labor constraints.





Regions Financial Corporation, 1900 5th Avenue North, 17th Floor, Birmingham, Alabama 35203
Richard F. Moody, Chief Economist • 205.264.7545 • richard.moody@regions.com