TD Economics

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Data Release: July employment report disappoints, with the lack of wage pressures allowing the Fed to bide its time before hiking rates

- Non-farm payrolls increased by 209k in July, below expectations for a 230k gain. However, revisions to the previous two months added 15k to the tally, offsetting some of the disappointment from the headline number.
- Private payrolls rose by 198k on the month with private service industries up 140k. Services growth was led by professional & business services (+47k, of which 9k were in temp services), retail trade (+27k), and health & social assistance (+25k).
- Goods-producing industries had a great month rising by 58k. Gains were driven by manufacturing (+28k, with half in transportation equipment manufacturing). Construction hiring accelerated to 22k in July, while mining & logging added 8k positions.
- Government hiring rose by 11k entirely driven by gains at the local level (+12k).
- The unemployment rose by 0.1 percentage points to 6.2% as gains in household-survey employment were not enough to keep up with a significant increase in the labor force (+329k). The labor force participation rate inched up by 0.1pp to 62.9%.
- Average hourly earnings were largely flat on the month, falling short of expectations for a 0.2% gain, with the year-over-year measure inching up slightly to 2.0%. After excluding remuneration of supervisory positions, average hourly earnings of production and non-supervisory employees rose by 0.2%.
- Average weekly hours remained unchanged at 34.5.

Key Implications

- The July employment report fell shy of expectations on several accounts, as both the headline gain disappointed and the jobless rate ticked up. However, the mitigating factors of positive revisions to previous months and an uptick in the labor force growth make the report more palatable.
- The solid gain in the labor force has led to an uptick in the participation rate from its lowest level in decades. We expect that as the labor market heals, more discouraged workers (or shadow unemployed) will begin to trickle back to the work force. The increase in the labor force should keep the pace of jobless rate declines relatively gradual relative to the experience over the previous quarters.
- The strong showing in goods employment is encouraging, with the strong rebound in the auto production helping manufacturing to the best month in job creation since November of last year. Construction hiring also accelerated, lending some hope that the housing recovery will gather pace in the coming months.
- Perhaps the most disappointing element in the report was the complete lack of wage gains and only marginal gain among production and non-supervisory employees. Lack of any evident wage pressures lends support to the notion shared by Fed Chair Yellen and much of the FOMC that the labor market still has far to go before it is fully healed. Lack of wage gains leaves the Fed with a strong case for keeping rates low for the next several quarters. With further improvement in the labor market, wage gains should materialize in the coming quarters, but the Fed's first rate hike is still likely a year away.

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