TD Economics

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Data Release: Labor market keeps on chugging in May, adding 175k jobs

- U.S. non-farm payrolls rose by 175K in May, edging out expectations for 163k. (Once revisions of -12k are taken into account, the result was bang on the consensus). Private sector hiring expanded by 178K, also a hair above the consensus for 175K. Government payrolls fell by 3k. The federal government shed 14k workers, but this was offset by +11k at the state and local level.

- Goods-producing employment edged down 1K as the manufacturing sector shed 8k, but was offset by +7k construction jobs.

- The unemployment rate edged up to 7.6% in May, due to rising labor force participation. Household survey employment rose a healthy 319k, but was outpaced by 420k people entering the labor force. The labor force participation rate rose to 63.4% from 63.3% in April.

- While job growth continues, wage growth remains muted. Average hourly and weekly earnings were both flat in May. Average hourly earnings are up 2.0% from a year ago.

Key Implications

- This is surely one of the most critical payroll reports of this year. Financial markets were looking for a signal of both the underlying strength of the economy and the future path of monetary policy. Today's report is perhaps the perfect number for nervous investors; it is strong enough to point to continued economic recovery, but not so strong as to bring forward expectations of Fed tapering.

- While the unemployment rate has been the traditional gauge of the labor market's health, today's outturn is a perfect example of its limitations. In fact, the current dynamics in the labor market are a bit perverse. If job growth stays muted, people are less likely to re-enter the workforce, which means a lower level of job growth will bring down the unemployment rate. If on the other hand, job growth is stronger, more people are likely to re-enter, therefore raising the threshold necessary for improvement. A rise in the unemployment rate that is accompanied by a rise in the participation rate is a good thing since it signals that formerly discouraged workers are re-starting their job search.

- The Federal Reserve has stated that it will continue its asset purchase program until the outlook for the labor market has shown substantial improvement. While today's report does not quite get us there, it is a foundation that can be built on. As the weight from sequestration lifts, U.S. economic growth is likely to accelerate. This is likely to become evident as the summer turns to fall, allowing the Fed to slowly back away from QE towards the end of this year.

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