

# The U.S. labor market 'puzzle': Both beginning and end of cycle characteristics



*By Bastien Drut, Chief Thematic Macro Strategist at CPR AM*

The April and May job reports disappointed, as job creations have been well below expectations, as the unemployment rate declined only very slowly and as the participation rate did not rebound. This would suggest that the US labor market is in a configuration typical of the early stages of the economic cycle. However, other indicators are consistent with an end-of-cycle configuration, which makes the analysis of the labor market more complicated than usual.

## Job creations have disappointed in April and May

Assuming that the statistics are not biased (we will see at the end of the text that some questions may arise), job creations disappointed in April and May (respectively 278,000 and 559,000 non-farm jobs), coming out clearly below expectations (nearly 1 million in April and 650,000 in May). The unemployment rate fell only slightly, to 5.8% of the labor force in May (and even 8% if we take into account the 3.5 million people who had left the labor force since February 2020). Intuitively, the fact that there are so many job seekers is reminiscent of the post-recession phases.

*See Appendices – Graphs 1 & 2*

One of the striking points about the US labor market is that the number of people in the labor force remains 3.5 million lower than in February 2020. One-third of these are above 55, which can be explained by early retirements (permanent withdrawal from the labor market) or by the fear of covid, this age category being more threatened than the others. Besides this age group, the participation rate rebounded the least for the 25-34 age group, probably because of childcare problems. In any case, it is really essential to look at the participation rate age group by age group because the participation rate calculated by the BLS makes less and less sense (see the box below).

*See Appendices – Graphs 3 & 4*

## The participation rate calculated by the BLS no longer makes sense

Each month, one of the most commented variables in the jobs report is the participation rate, which is the ratio of the labor force to the total population. The "catch" is that for the total population, the BLS considers the population aged 16 and over, with no upper limit, but population ageing means that the working-age population (15 to 64 years in Eurostat statistics or the OECD) has peaked in recent quarters and is starting to decline even as the population aged 16 and over continues to grow rapidly.

*See Appendices – Graphs 5 & 6*

Thus, the participation rate published by the BLS, which has stagnated for months, had also not recovered over the 2015-2019 period, while conditions in the labor market had improved markedly. On the contrary, a participation rate calculated on the basis of the working-age population was well consistent with such an improvement over the period and has risen gradually over the past year.

Finally, even if job creations were lower than expected, it is important to note that their pace has nevertheless been robust since the reopening in February (strong relaxation of health restrictions, in particular in the Republican States), with an average of 539,000 per month for the

February to May period. Staying at this pace, employment should return to its February 2020 level by summer 2022.

*See Appendices – Graph 7*

### But other indicators have some characteristics of the end-of-cycle periods

This may seem paradoxical in a period of high unemployment, but in recent weeks, press articles have mostly reported... on the hiring difficulties experienced by companies. In reality, the job supply observable today is consistent with an end-of-cycle period and this is understandable: in a certain number of sectors, the pandemic was managed quite smoothly with the introduction of teleworking or health protocols. Jerome Powell himself had underlined this "adaptation" during the FOMC press conference in January. In May, 48% of SMEs indicated that they had unfilled job openings, the highest proportion since the creation of this survey in 1975, whereas it is generally very low at the start of the cycle.

*See Appendices – Graph 8*

Another indicator in this direction is the number of job openings which reached 9.3 million in April, the highest level ever observed by far, which means that the number of unemployed per job opening is already close to 1, a level generally observed at the end of the cycle. This configuration is usually associated with wage pressures: in fact, the average hourly wage increased by 0.8% in April and then 0.5% in May, that is to say at a rate not observed since the beginning of the 1980s. There are obviously disparities between sectors or between geographical areas, but the trend is clearly downward for the ratio of unemployed to job openings. With the exception of the mining sector, this ratio is well below 2 and has fallen sharply in recent months. For some sectors, it's a bit like the cycle is coming back to where it was before the covid crisis. In general, the coincidence of high demand for labor and high unemployment can be explained by an imbalance between the skills of job seekers and those sought by companies ("skills mismatch"). This problem already existed before the covid crisis and did not disappear with it, but it is superimposed on specific adjustments to the crisis (change of course, change of sector, change of place of residence, etc.). Some time could be necessary for the supply and demand of labor to meet<sup>1</sup>, especially since unemployment benefits are much more generous than usual (until the beginning of September for states, mostly Democrats, which do not have not suspended them).

*See Appendices – Graphs 9 & 10*

### Statistics disrupted by the crisis?

For the second time in a row, job creations in the private sector announced by the jobs report were far below those announced by the ADP report: 219,000 for the job report in April against 654,000 for the ADP report and 492,000 for the job report in May against 978,000 for the ADP report (difference of 0.9 million over the whole of the two months). The differences are huge and surprising (as a reminder, the ADP report figure comes from payroll data for about one-fifth of private sector employees). In addition, the total number of people receiving unemployment benefits (all programs combined) fell by 2.8 million between the week of March 13 and the week of May 15 (the weeks including the 12th of the month are taken into account for the job report) whereas the number of unemployed fell by only 0.4 million over the whole of April and May for the job report (0.8 million if we consider underemployment U6) . Here too, the differences are very important.

**One of the sources of disruption to the job report statistics relates to seasonal adjustment.** Indeed, a number of seasonal factors relating to the education, hotel, restaurant and leisure sectors have not taken place the same month as in previous years because of health restrictions. Consequently, the application of seasonal adjustment methods automatically introduces biases into the figures published in the job report: the months of April and May are, together with the month of October, those for which non-seasonally adjusted job creation is usually the highest, and the statistical processing may have led to an underestimation of job creation in these months.

*See Appendices – Graph 11*

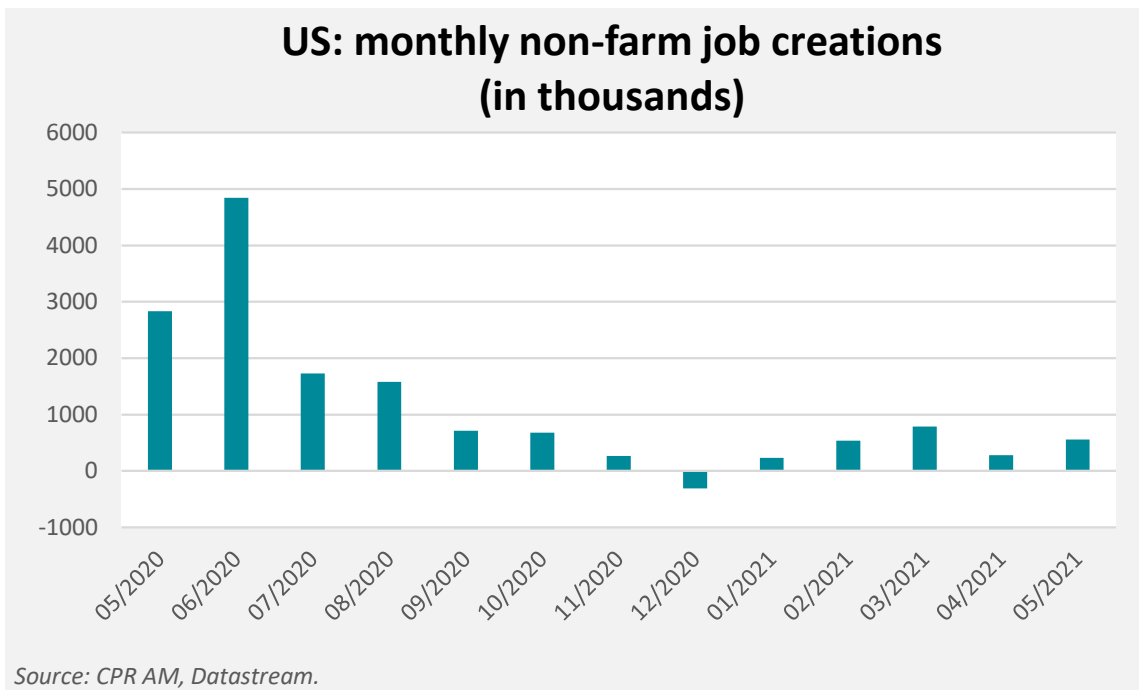
**The US labor market situation is atypical because it has both beginning and end of the economic cycle characteristics. Some sectors have adapted very well to the pandemic while others are still affected. While it is completely understandable that the Fed adopted a very accommodating monetary policy at first, especially with the very sharp rise in the unemployment rate, maintaining the same course will become increasingly difficult because the labor market is getting tight here and there. In fine, wage developments will probably be the decisive factor, which could lead for a quicker end to asset purchases. It is on these subjects that Jerome Powell will be expected to speak at the FOMC press conferences of June 16 and July 28 (with an announcement of the "tapering" at the Jackson Hole conference of August 26 to 28?).**

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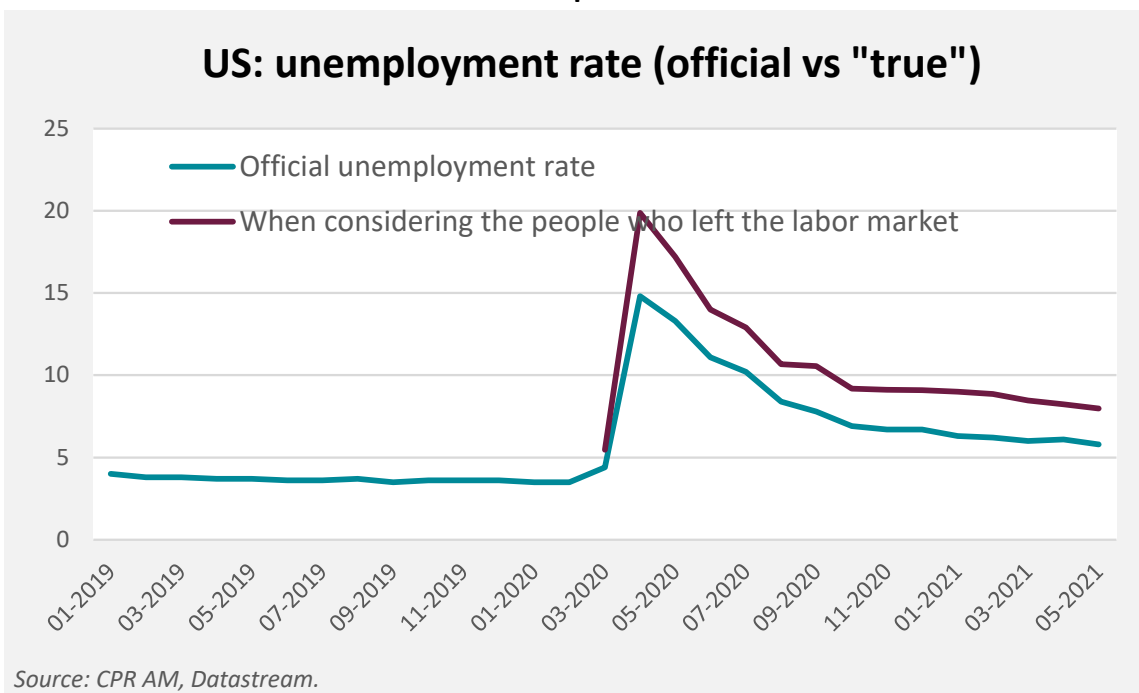
<sup>1</sup> On the subject, see the note "US labor market heated up in May as jobs grew and wages soared" from the Peterson Institute, June 2, 2021.

Annexes

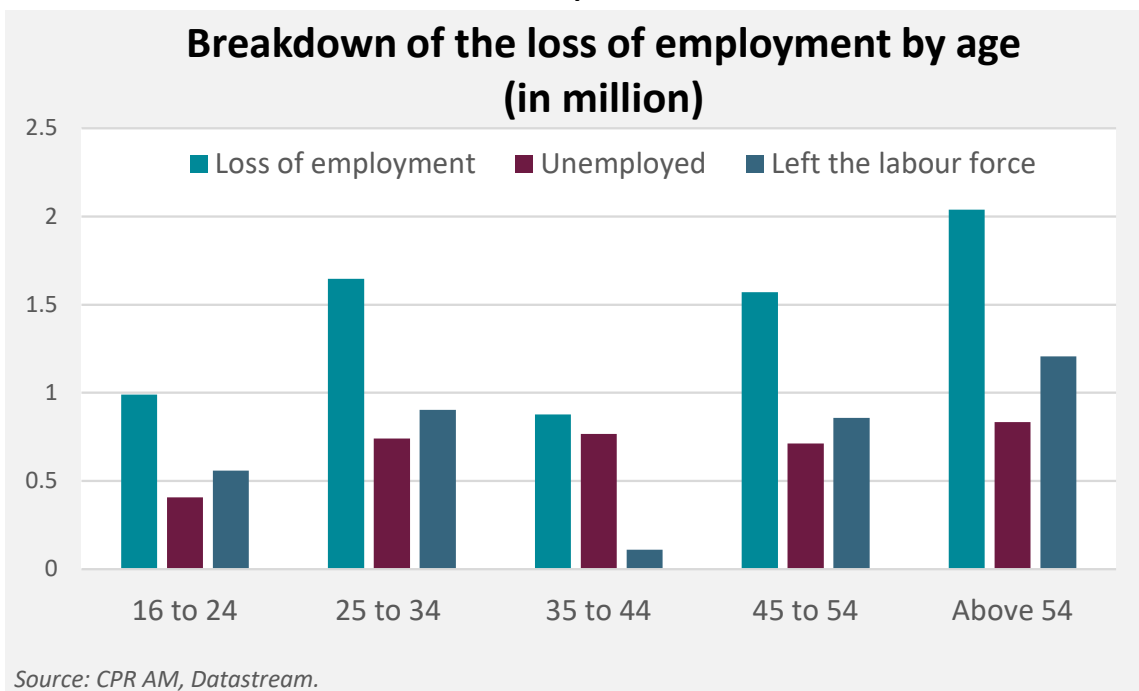
Graph 1



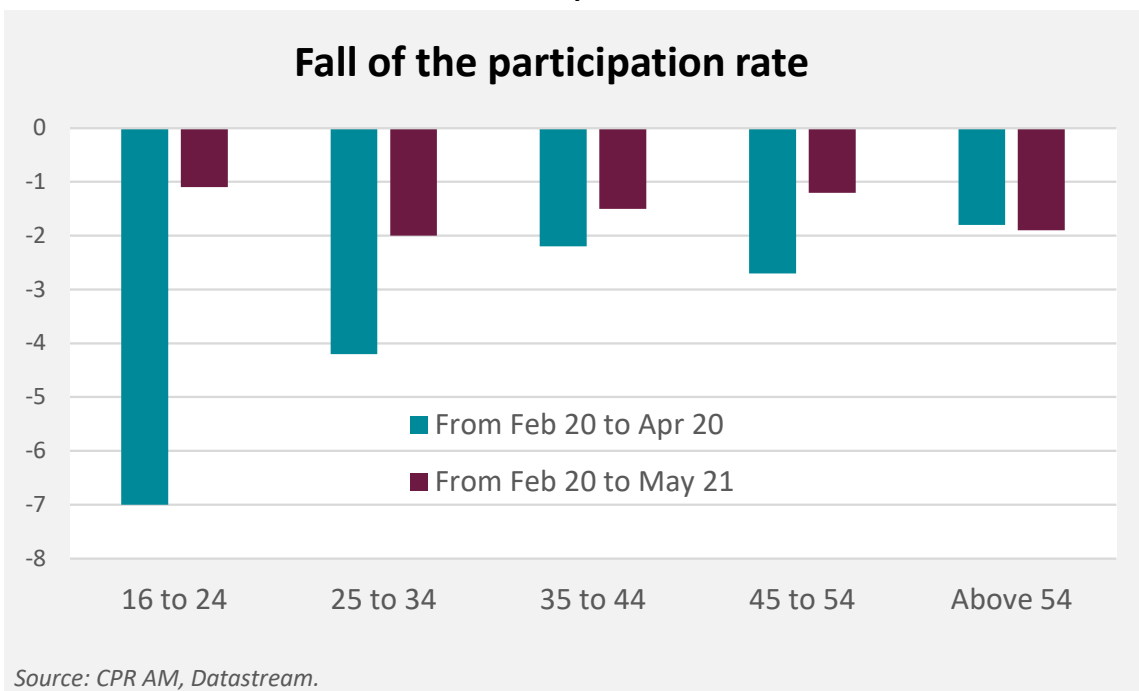
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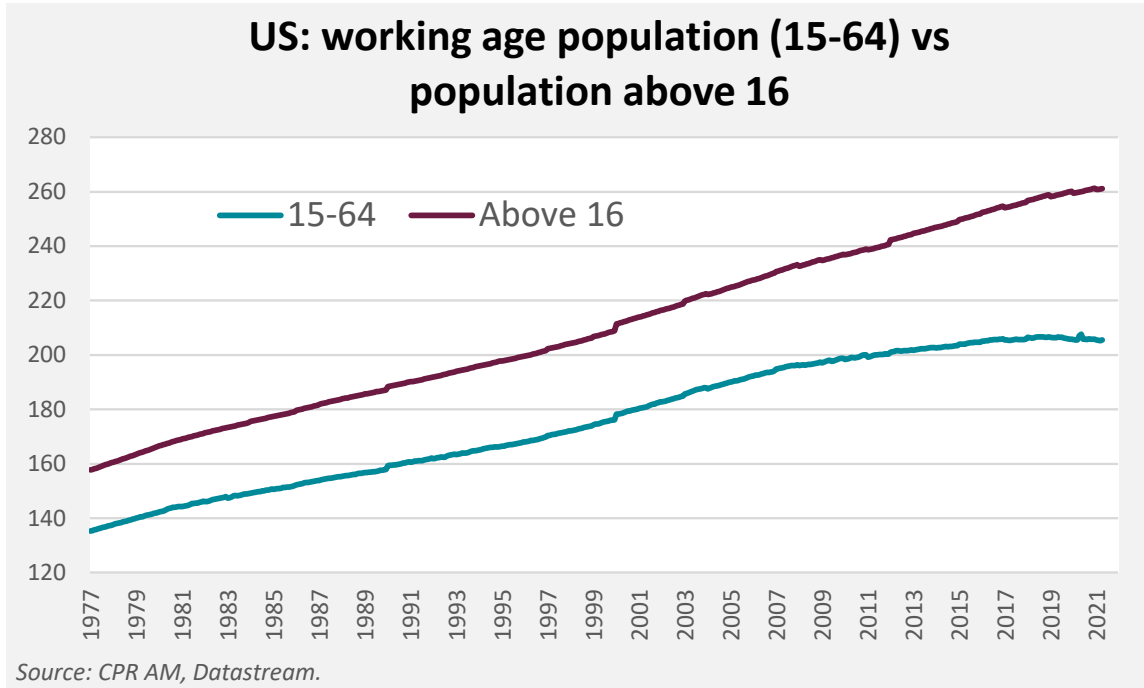
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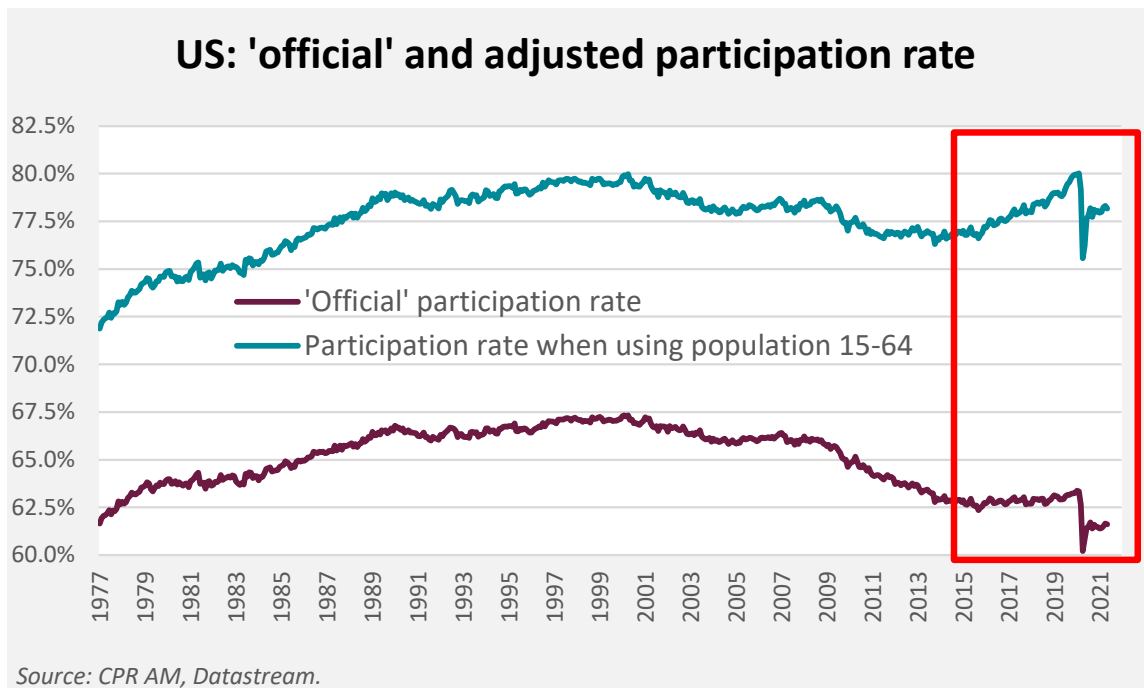
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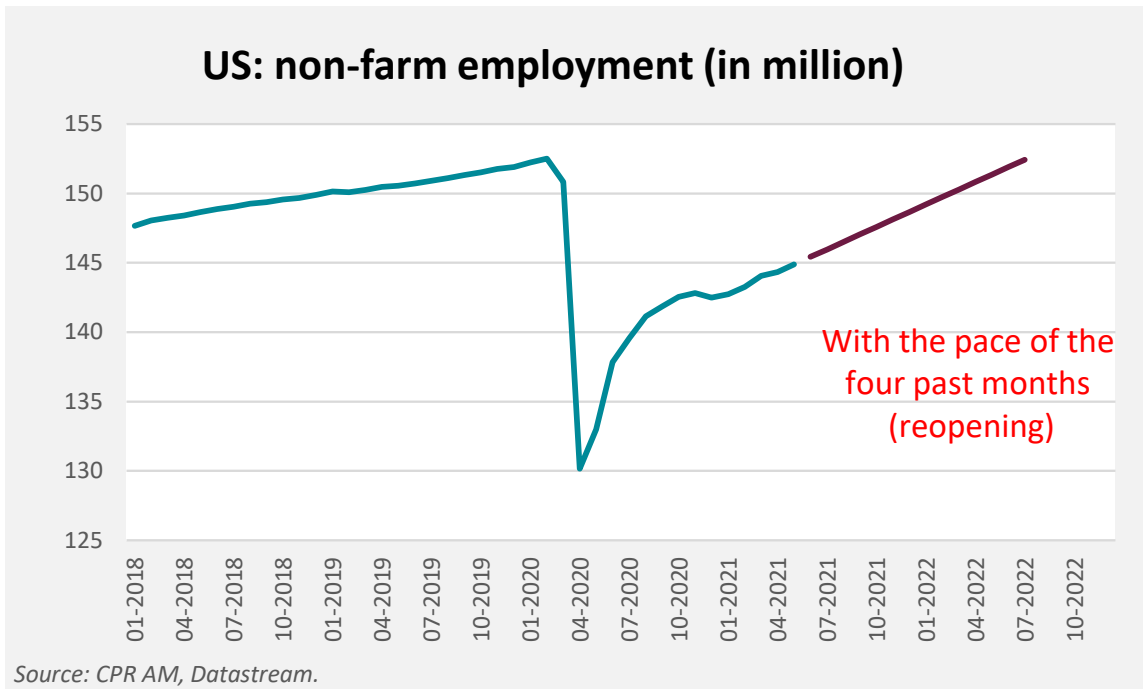
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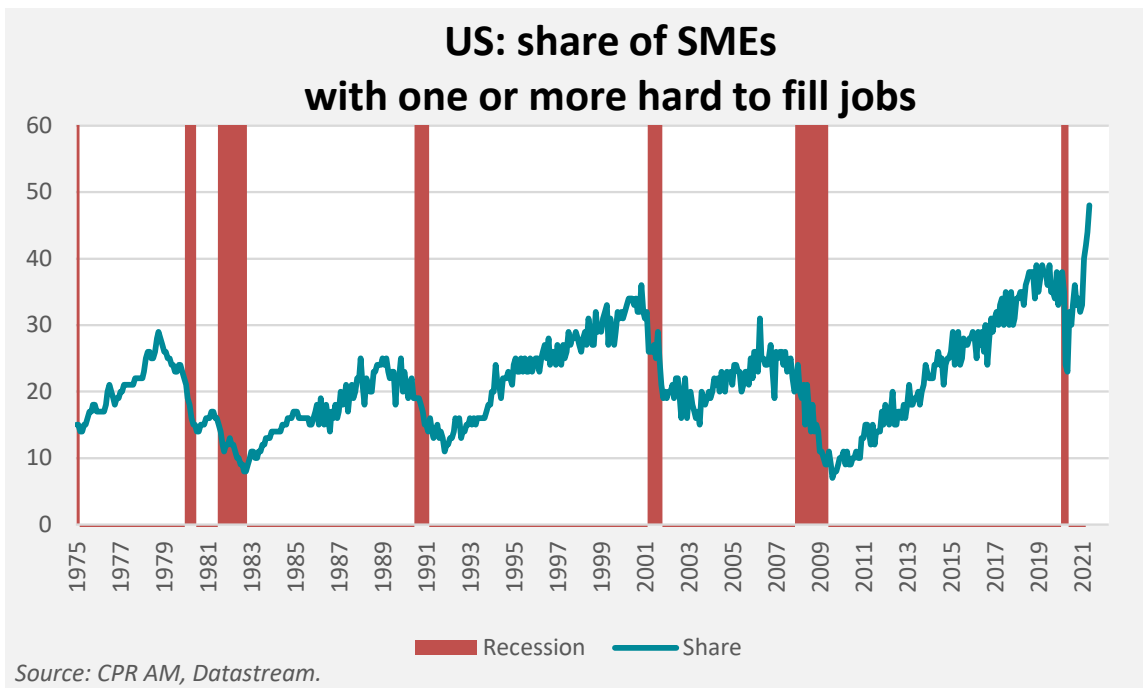
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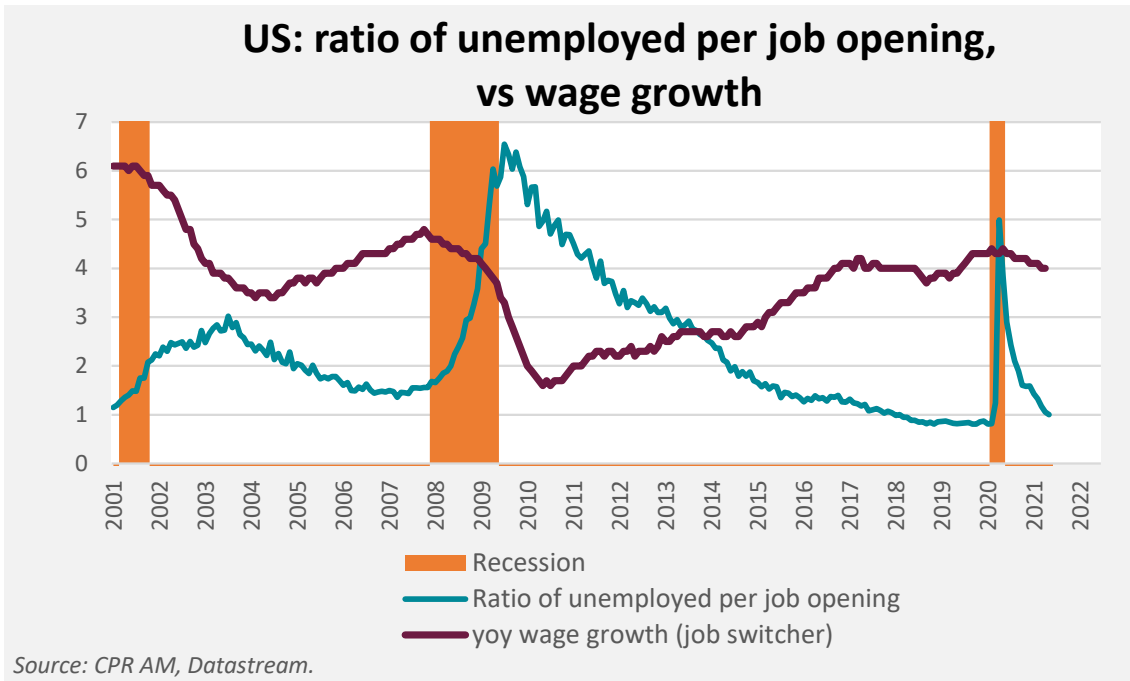
Graph 7



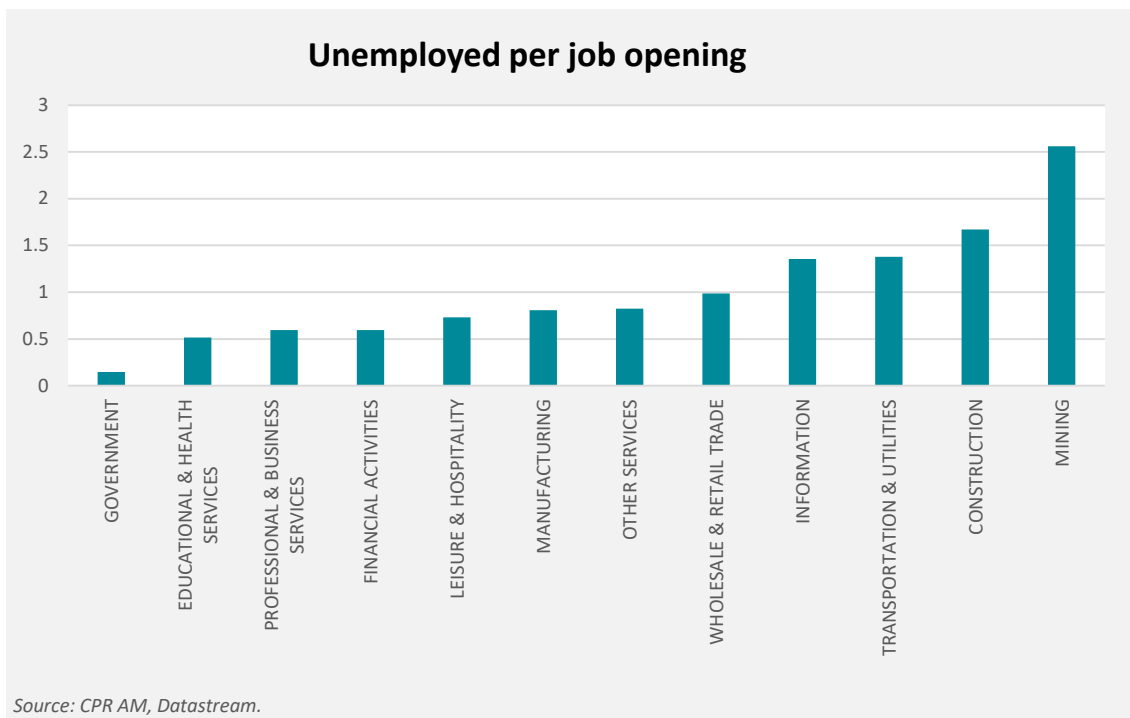
Graph 8



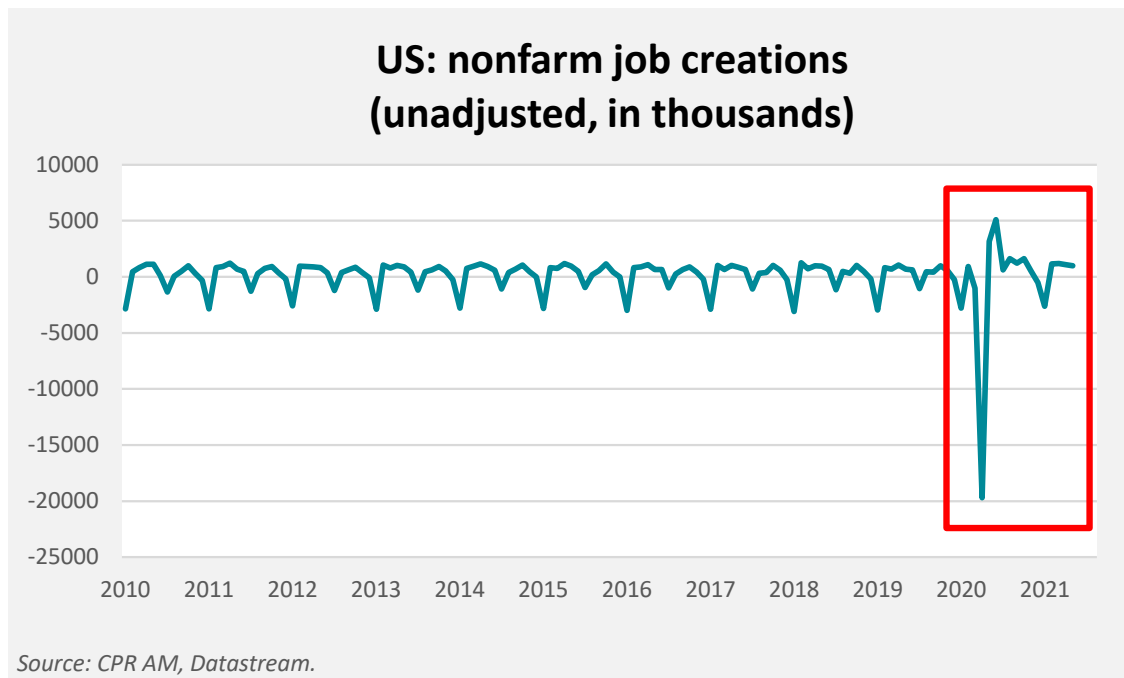
Graph 9



Graph 10



Graph 11

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