US September jobs report

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US September jobs report shows economic strength continues

The September US jobs report was surprisingly strong, with 254k jobs created and the unemployment rate unexpectedly falling from 4.2% to 4.1%. The financial markets and the US Fed had been concerned that the jobs market would weaken after the unemployment rate spiked higher to 4.3% in July. This was one of the reasons the Fed cut rates by a larger than expected 0.50% at its September meeting. However, over the past two months, the employment data has been stronger than expected and shows the economy continuing to expand at a healthy pace, despite the still high Fed rates.

Highlights of the economic data released include:

- 254k non-farm payroll jobs added during the month versus an expected 150k. The previous month (August) was revised higher by 17k to 159k and July was revised higher by 55k to 144k. Services added 233k jobs, the strongest monthly gain since March.

- The unemployment rate was expected to stay steady at 4.2% but instead it fell to 4.1%. It was last at 4.1% in June and then had jumped higher to 4.3% in July, before falling in August and September. It does look like the economy had experienced a brief weak period around July as the weekly jobless claims numbers had increased to 250k. But since then, weekly claims have decreased to the 220k range. If weekly claims can remain in this range, we believe the unemployment rate could stabilize in the 4%-4.1% range, which would be lower than the Fed's 4.2% longer-run full employment estimate.

- Average hourly earnings accelerated in September to 4% YoY, from 3.9% in August. The month-on-month was higher than expected at 0.4% versus an upwardly revised 0.5% in August. The latest JOLTS report showed available jobs rising to 8 million, indicating labor demand remains strong. Strong labor demand could drive higher wage pressures and this could drive overall inflation higher, or at least prevent further declines in inflation to the Fed's 2% target. If this were to occur, the Fed could possibly be limited in how many rate cuts it could ultimately achieve.

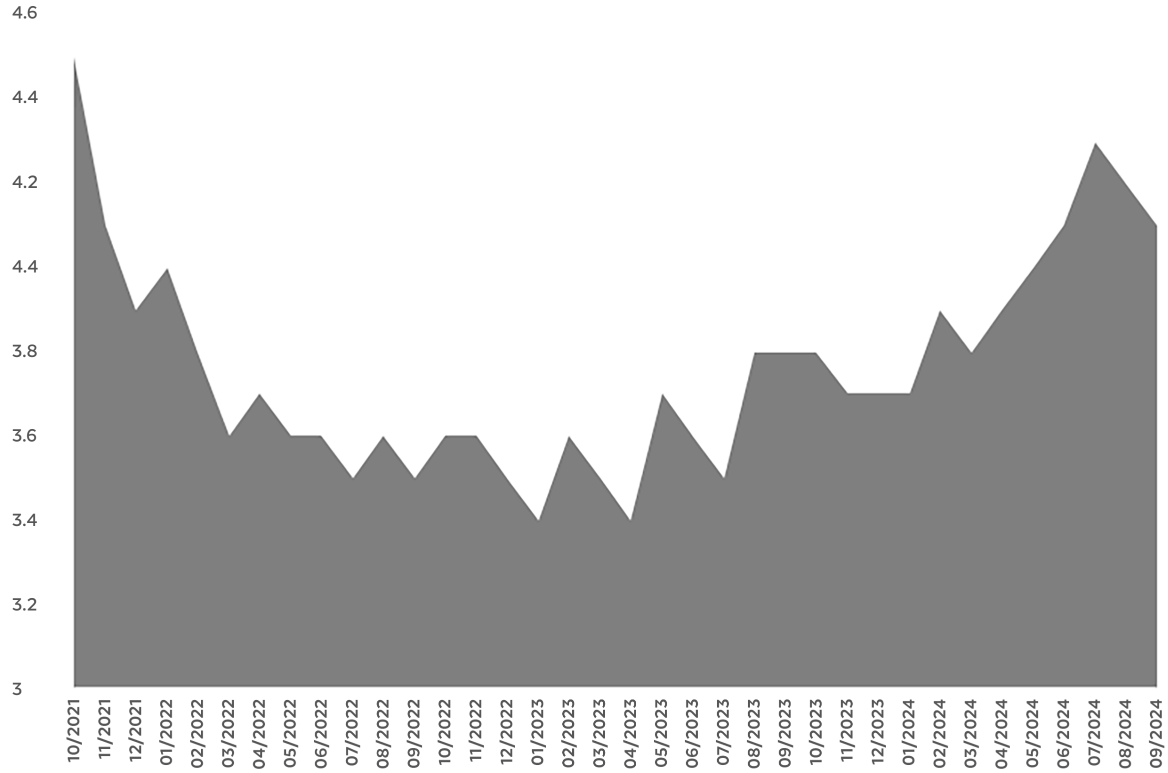
At the latest Fed meeting in September, the Fed had cut rates by a larger than expected 0.50% to 4.75%-5.0%, saying that it wanted to prevent a deterioration in the jobs market. The Fed had expected the unemployment rate to increase to 4.4% by the end of this year, but the economy and jobs market seems stronger than what the Fed had predicted.

Financial markets had been even more sceptical than the Fed on the state of the US economy as market pricing showed expectations for 0.75% in rate cuts by the end of this year and a further 1.25% in 2025, versus the Fed's outlook of a further 0.50% in cuts this year and then 1% more in 2025. The strong data shows the market pricing and possibly even the Fed have been too sceptical on the strength of the economy.

US Treasury yields increased sharply after the release of the jobs data as the stronger economy means a soft-landing and even no-landing scenario (where economic growth continues in the 2.5%-3% range) is more more likely than a recession. Financial market pricing had been more sceptical than the Fed's assumptions for the economy so Treasury yields were very low with the 10-year US Treasury yield reaching a low of 3.6% just before the Fed meeting. Since then the 10-year yield has increased to near 4% and we believe the overall Treasury yield curve could continue to move higher in the short-term as the strong jobs market, economic growth and potentially higher inflation are priced in by the markets.

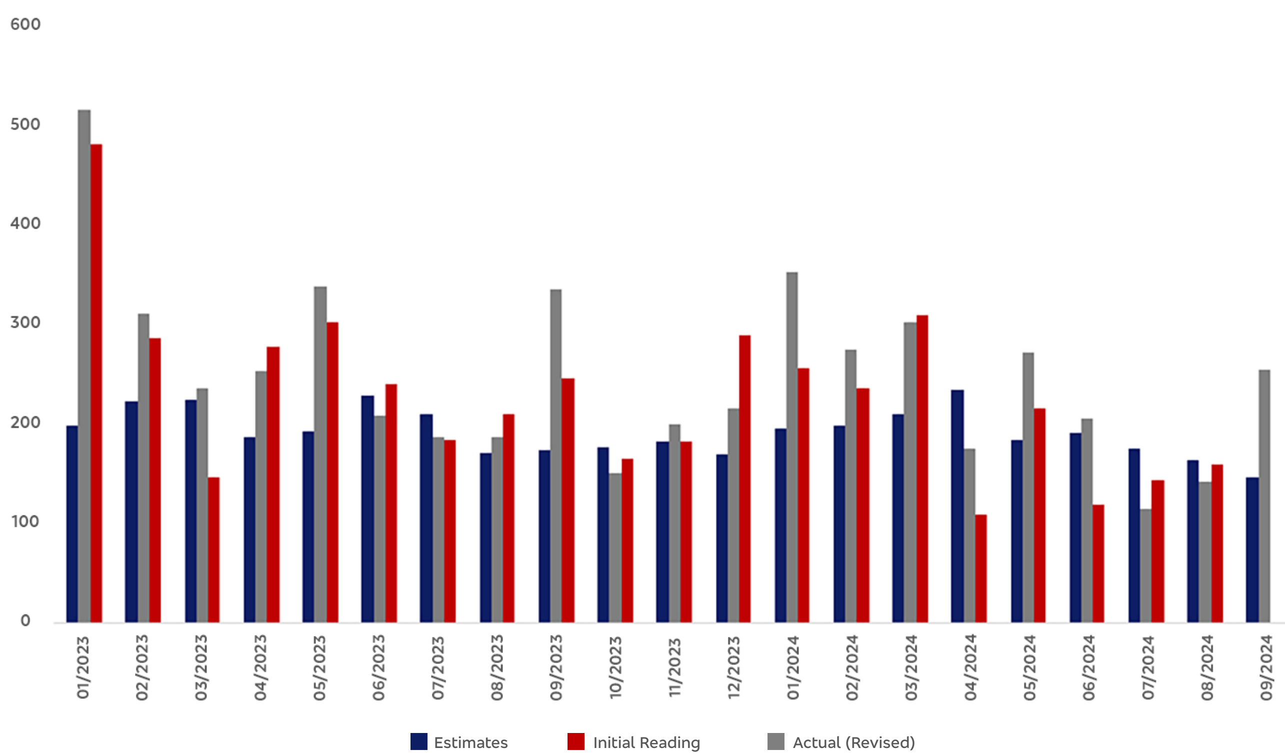
The strong data also mean the Fed must face more fundamental questions. The initial 0.50% rate cut from the 5.25%-5.50% range was because this level was seen as very restrictive. But if the economy can continue expanding at above trend growth and the jobs market can remain so strong, then are rates really so restrictive? Maybe the Fed will not need to cut rates as much as it currently expects (a further 0.50% this year and a further 1% next year). And perhaps the long-run expectation of Fed rates to reach 2.9% are too low if the economy can handle 5% rates without much difficulty.

Unemployment rate falls to 4.1% from 4.2%



Source: Bloomberg/Bradesco

Stronger than expected 254k jobs created in September



Source: Bloomberg/Bradesco

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