Financial FAQs

WHY SUCH A POOR JOBS MARKET?

The nation's payrolls expanded by 113,000 in July, according to the Bureau of Labor Statistics, providing yet another month of evidence that the pace of U.S. job creation has significantly downshifted. Why such a poor jobs market in the midst of so much prosperity for corporations that have been making record double-digit gains in profits over the past 2 years?

In an analysis by the Economic Policy Institute's Jared Bernstein, 2005, excluding the two months depressed by hurricanes, monthly employment grew by 190,000 jobs on average. In the first quarter of this year that rate slowed to 176,000, and in the second quarter it dropped to 112,000, just about the same number added in July.

The unemployment rate also grew by two-tenths, to 4.8%, as about 250,000 job seekers joined the jobless rolls. The growth in joblessness was concentrated among African Americans, whose rate went up from 9.0% to 9.5%, their highest rate since November of last year.

"Today's report confirms that the various headwinds that have reduced overall economic growth are also being felt in the job market," said Bernstein in the EPI report. "The cooling housing sector can be seen in weak residential construction job growth, which has been flat over the first half of the year. The slowing of consumption growth can be seen in retail employment, which was flat in July and down 88,000 in the past year. U.S. manufacturers continue to face steep competition from abroad, as factory employment fell 15,000 last month, driven in part by an 8,000 monthly contraction in autos and car parts."

Of even greater concern is the effect a slowing real estate market will have on overall employment. Residential construction as measured by housing starts has been falling, along with the stock prices of home builders like Hovnanian Enterprises. Housing starts are down 5.3 percent from May-June, and approximately 9 percent from last year's highs on an annual basis.

Residential construction has been flat since April, and employment among residential contracting establishments is down 25,000 this year, including 9,000 last month.

This dynamic affects not only construction jobs, but it also dampens job growth in ancillary sectors. Real estate employment, for example, has been flat since April, and job growth among credit intermediaries, such as those who arrange mortgages and refinancing, is also slower. Such categories added 151,000 jobs in January through July of last year, compared to only 13,000 jobs this year.

All of this should convince Federal Reserve officials to vote for a pause in their interest rate hikes next week (August 8). Though inflation is still a problem in material costs (such as energy and raw materials), it is not rearing its ugly head in the wage sector, which accounts to two-thirds of product costs.

Hourly wage growth was up 0.4% for the second month in a row, and wages are up 3.8% on an annual basis. This is a notable acceleration from the 2.9% wage growth one year ago, though still below the most recent inflationary readings of 4.3% (June 2005-June 2006). The acceleration in wage growth is partly related to the tightening of the job market over the past year, but also a function of job composition, as employment has grown more quickly in higher-end sectors, like professional services, than in lower-end ones, such as retail.

But strong productivity gains are a reason why profit margins are at all-time highs, and Fed Chairman Bernanke has said in his latest congressional testimony that such high labor productivity and profit margins will keep rising wages from putting undue pressure on prices.

"In sum, the slowdown in employment growth appears to be consistent with slowing in the wider economy. This likely means longer job searches for new and returning workers entering the job market, and this could put upward pressure on the unemployment rate in coming months," concluded Bernstein.

We therefore hope that Fed officials will see inflation as the temporary phantom that it is. It is mostly based on geopolitical uncertainty, high-growth Asian economies (India and China), and U.S. and European economies that are already slowing. Otherwise, given the parlous state of U.S. government and consumer finances, a real recession (and deflation) could follow.