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Global Strategy

INVESTMENT TEAM

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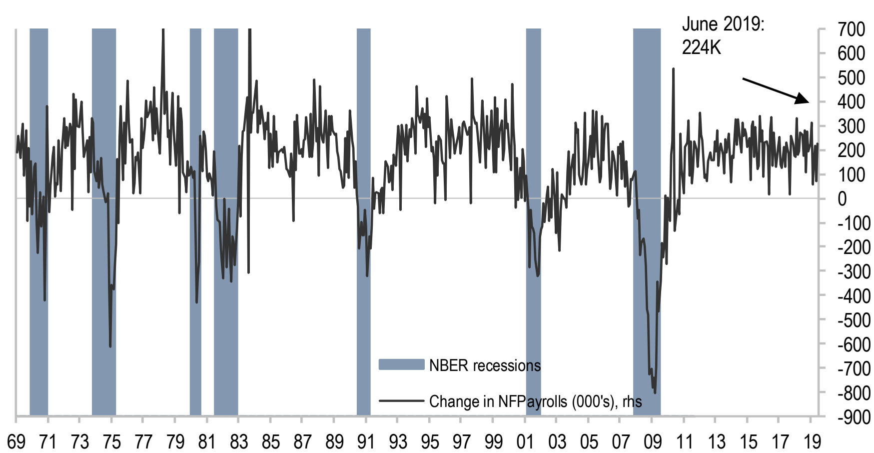
On Friday last week the US Payrolls report beat estimates recording 224k net new jobs in June, 74k more than expected. That takes the three-month average rate of job growth to more than 170k which, at face value, is more than consistent with robust economic expansion. These numbers may also dilute the case for a rate cut later this month, with the fixed income market selling off on the news, taking the ten-year government bond yield back above 2% for the first time in three weeks.

The Payrolls report (Figure 1) showed broad based growth across most industries with manufacturing showing the strongest jobs growth since January. That said, the surprising strength of jobs growth was not enough to keep hourly wage inflation at May levels, that dropped back to 3.1%, neither was it strong enough to maintain the record low level of unemployment, that ticked up one tenth to 3.7% in June. The small uptick in the unemployment rate was also partly due to the expansion of the labour force in June. The now record long economic expansion in the US continues to draw people back into the labour force, and that must be part of the story around the subdued level of wage growth which is below where one might expect it to be at this stage of the cycle.

Tucked away at the end of the June report, however, was a mention of the August release of provisional data for the annual benchmark revisions to the non-farm payrolls report. There is some evidence in the 2018 census data to suggest they are less optimistic about employment growth than the Non-Farm Payrolls survey. The August release may help explain the dichotomy between fixed income and equity markets.

Figure 1: US Non-Farm Payrolls (net change, thousands)

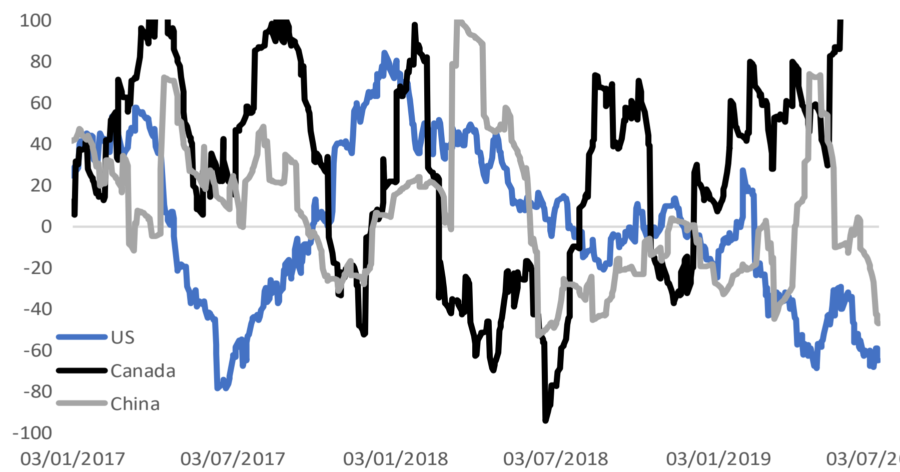


Source: DataStream, Bloomberg, Canaccord Genuity Wealth Management

That said, after the employment numbers on Friday, the fixed income markets had railed back from pricing a rate cut in July with certainty, to a small chance of no change. Probably because, whichever way you slice it, the June headline numbers were strong, and may also point to a low point in some of the softer survey data. The Economic Surprise Index (Figure 2) from Citi shows that data have been coming in below expectations for most of 2019 so far in the US, and it is a similar story elsewhere, with a few exceptions such as Canada. In Europe and Japan, the Surprise index has also been improving, but the low levels of growth in these regions is hardly going to move the dial on the lacklustre global growth numbers that are currently causing concern.

The expectation beating June Payrolls numbers have at least arrested the declining trend in the employment numbers through 2019, but they may yet prove to mark the low point in economic sentiment. As Dolly Parton sang in 1980, the US labour market may be coming back to life. "Tumble outta bed and stumble to the kitchen. Pour myself a cup of ambition. Yawnin' and stretchin' and try to come to life."

Figure 2: Economic Surprise Index



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