Economics
THE WEEK AHEAD

August 1-5, 2022

Employment: How slow is slow enough?

by **Avery Shenfeld** avery.shenfeld@cibc.com

Despite being supported by an army of PhD economists, Fed Chair Jay Powell seems as confused as we've been about the economic state of the union. But one thing is clear: the jobs data over the next few months, including the week ahead's tally for July, are going be decisive in setting market and central bank views on where we're headed.

We're going to need a cooler US labour market to contain inflation, as evidenced by yet another brisk climb in employment costs in the second quarter. But how slow is slow enough?

On that score, there's a wide gulf among the most pre-eminent names in the economics community. Former IMF chief economist Olivier Blanchard has argued that the non-inflationary or "natural" unemployment rate has moved up to 4.9%, which suggests the need for at least a mild recession. Former Treasury Secretary Larry Summers, using rules of thumb on the unemployment-inflation relationship from past cycles, sees the need for two years with a 7.5% unemployment rate to get inflation to target. If they're right, unlike what the market is now thinking, the Fed can't quickly back away from a tightening path on the first signs of a labour market slump.

But there are equally eminent economists, among them former Fed Governor Alan Blinder and Paul Krugman, who urge the Fed to tread more carefully from here, and don't see a recession or a huge increase in joblessness as a necessary condition for tumbling inflation. They see reasons to believe that what it took to unwind the last big inflation in the early 1980s, isn't a reliable guide for this cycle.

Of course, there's a saying that "this time is different" are the most dangerous words in economics. But different than when? Some point to the inflation spike right after the end of WWII, which has similarities to the post-Covid spike, with both seeing a sudden reopening in private sector demand, and disrupted global production; inflation was vanquished without a recession in that post-war period.

There are also some huge differences in the source of today's inflation versus the early 1980s, and the degree to which it's imbedded in long term expectations. There are countries that don't have overheated demand that are also experiencing elevated inflation, evidence that factors beyond an overly tight labour market are at play. If so, a reversal or at least a levelling off in those factors, as we might already be seeing in oil and food commodities, and in some encouraging words about auto supply for example, could, as Blinder argues, do the heaviest lifting in the inflation deceleration. If faster wage growth is reflecting employers' current ability to pass on costs in prices, a slower inflation track would also help cool compensation gains.

That's not to say that we don't need a material slowdown in hiring in both the US and Canada if inflation is to come under control. But it would mean that a few decimal points, not a few percentage points, on the unemployment rate might do the trick.

There are hints that we might see such a turn soon in the US, with the confidence surveys reporting less job availability, and the household survey numbers not seeing the same uptrend as payrolls. Jobless claims have also trended higher in both raw and seaonally adjusted terms in the latest months. In the casino game known as "guess the next US payrolls number", these signals are enough to have us on the low side of the July consensus. But our tally of a bit under 200K is still about twice what we'll need to average for a while to open up a bit of slack in the labour market. Slower, but not yet slow enough.

In Canada, even including June's employment dip, we've had a lot of hiring relative to GDP performance in the past year or so, and that might also auger for smaller job gains ahead. As in the US, less hiring, but not mass firing, is what we'll need to see if we're going to avoid the shoals of recession or excessive inflation.

Week Ahead Calendar And Forecast—Canada

H, M, L = High, Medium or Low Priority
SAAR = Seasonally Adjusted Annual Rate
Consensus Source: Bloomberg

Date	Time	Economic Releases, Auctions and Speakers	Month	Priority	CIBC	Consensus	Prior
Monday, August 1	-	Markets Closed (Civic Holiday)	-	-	-	-	-
Tuesday, August 2	-	AUCTION: 3-M BILLS $9.2B, 6-M BILLS $3.4B, 1-YR BILLS $3.4B	-	-	-	-	-
Wednesday, August 3	-	-	-	-	-	-	-
Thursday, August 4	-	AUCTION: 10-YR CANADAS $3B	-	-	-	-	-
Thursday, August 4	8:30 AM	BUILDING PERMITS M/M	(Jun)	(M)	-	-2.0%	2.3%
Thursday, August 4	8:30 AM	MERCHANDISE TRADE BALANCE	(Jun)	(H)	$4.4B	$4.99B	$5.32B
Friday, August 5	8:30 AM	EMPLOYMENT CHANGE	(Jul)	(H)	15.0K	18.1K	-43.2K
Friday, August 5	8:30 AM	UNEMPLOYMENT RATE	(Jul)	(H)	5.0%	5.0%	4.9%
Friday, August 5	10:00 AM	IVEY PMI	(Jul)	(L)	-	-	62.2

Week Ahead Calendar And Forecast—United States

H, M, L = High, Medium or Low Priority
SAAR = Seasonally Adjusted Annual Rate
Consensus Source: Bloomberg

Date	Time	Economic Releases, Auctions and Speakers	Month	Priority	CIBC	Consensus	Prior
Monday, August 1	10:00 AM	ISM - MANUFACTURING	(Jul)	(H)	51.8	52.1	53.0
Monday, August 1	10:00 AM	CONSTRUCTION SPENDING M/M	(Jun)	(M)	-	0.2%	-0.1%
Tuesday, August 2	10:00 AM	JOLTS Job Openings	(Jun)	-	-	10994K	11254K
Tuesday, August 2	-	NEW VEHICLE SALES	(Jul)	(M)	-	13.5M	13.0M
Tuesday, August 2	10:00 AM	Speaker: Charles L. Evans (President, Chicago) (Non-Voter)	-	-	-	-	-
Tuesday, August 2	6:45 PM	Speaker: James Bullard (President, St Louis) (Voter)	-	-	-	-	-
Wednesday, August 3	7:00 AM	MBA-APPLICATIONS	(Jul 29)	(L)	-	-	-1.8%
Wednesday, August 3	10:00 AM	FACTORY ORDERS M/M	(Jun)	(M)	1.2%	0.9%	1.6%
Wednesday, August 3	10:00 AM	ISM - SERVICES	(Jul)	(M)	54.5	53.9	55.3
Thursday, August 4	8:30 AM	INITIAL CLAIMS	(Jul 30)	(M)	-	-	256K
Thursday, August 4	8:30 AM	CONTINUING CLAIMS	(Jul 23)	(L)	-	-	1359K
Thursday, August 4	8:30 AM	GOODS & SERVICES TRADE BALANCE	(Jun)	(H)	-$79.4B	-$81.5B	-$85.5B
Thursday, August 4	12:00 PM	Speaker: Loretta Mester (President, Cleveland) (Voter)	-	-	-	-	-
Friday, August 5	8:30 AM	NON-FARM PAYROLLS	(Jul)	(H)	180K	250K	372K
Friday, August 5	8:30 AM	UNEMPLOYMENT RATE	(Jul)	(H)	3.6%	3.6%	3.6%
Friday, August 5	8:30 AM	AVERAGE HOURLY EARNINGS ALL EMPLOYEES M/M	(Jul)	(H)	0.3%	0.3%	0.3%
Friday, August 5	8:30 AM	AVERAGE WEEKLY HOURS ALL EMPLOYEES	(Jul)	(H)	-	34.5	34.5
Friday, August 5	8:30 AM	MANUFACTURING PAYROLLS	(Jul)	(H)	-	15K	29K
Friday, August 5	3:00 PM	CONSUMER CREDIT	(Jun)	(L)	-	$25.0B	$22.3B

Week Ahead's market call

by Avery Shenfeld

In the **US**, markets will be hanging in suspense as we await Friday's payrolls report, since the jobs trend has been one key reason why no serious economists have defined the first half GDP decline as a recession. We're below consensus in looking for the net hiring pace to be cut in half from what we saw for June, since even if GDP sees growth in Q3, we're due for some softer employment figures to better align payrolls with measures of output. Average hourly earnings aren't yet likely to decelerate further while the labour market is still so tight. Both the manufacturing and services ISM figures should head lower, which again would be more about aligning them to what's already happened to growth indicators than a signal of worse times ahead.

In **Canada**, the employment figures rest on a more volatile household survey, and June's deep dive should be somewhat offset by a return to positive net hiring in July. But we're not looking for a full recouping of the June drop, and a rebound in participation could see the jobless rate move up a tick. Canada's June goods trade balance will remain solidly in the black, but the softening we've seen in commodity prices of late, and the acceleration in Canadians travelling abroad, point to a softer overall nominal goods and services balance ahead.

Week Ahead's key Canadian number: Labour force survey—July

(Friday, 8:30 am)

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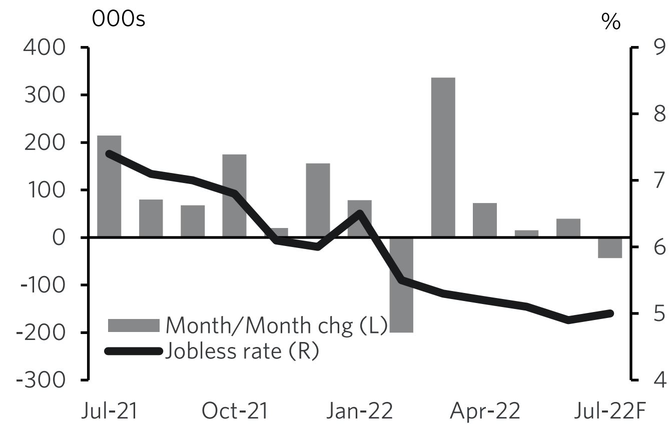
Variable	CIBC	Mkt	Prior
Employment (m/m)	15.0K	18.1K	-43.2K
Unemployment rate	5.0%	5.0%	4.9%

Chart: Canadian employment



Source: Statistics Canada, Haver Analytics, CIBC

Employment took an unexpected step back in June, but with that largely reflecting a decline in labour force participation the unemployment rate still managed to reach another record low. With signs that the economy is starting to slow, any rebound in staffing levels during July is expected to be only modest and below the pace of population growth. As such, the 15K gain in jobs we expect would be consistent with a tick up in the unemployment rate to 5.0%. Any further acceleration in wage growth should be more modest than the sharp uptick seen in the prior month.

Forecast implications — While the supply of labour appeared to be a primary factor behind the last month's weakness, this time around a muted rebound is expected to be the result of weakening demand for staff particularly in areas such as real estate and construction which are being hit hardest by the rapid climb in interest rates.

Other Canadian releases: Merchandise trade—June

(Thursday, 8:30 am)

Canada's trade surplus widened sharply in May, due to a combination of higher energy prices, strong overseas demand for non-Russian commodities and a surprising decline in imports. While energy exports likely stayed close to their highs, with prices edging a little higher but volumes down, a rebound in imports will likely see the trade surplus narrow somewhat. We expect a surplus of $4.4bn, from $5.3bn in the prior month.

Week Ahead's key US number: Employment situation—July

(Friday, 8:30 am)

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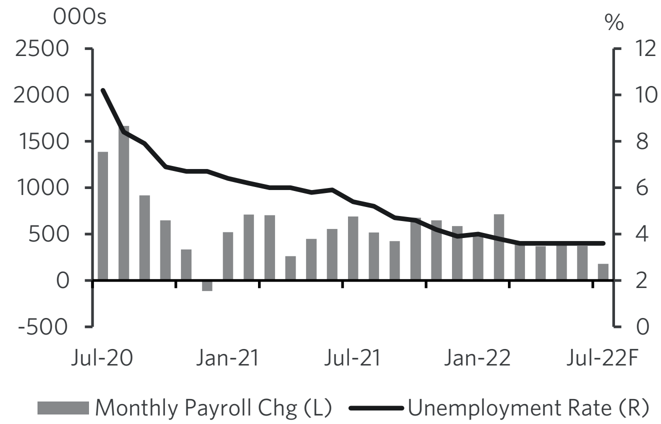
Variable	CIBC	Mkt	Prior
Employment (m/m)	180K	250K	372K
Unemployment rate	3.6%	3.6%	3.6%
Avg hourly earnings (m/m)	0.3%	0.3%	0.3%

Chart: US payroll employment



Source: BLS, Haver Analytics, CIBC

The outperformance in the labor market relative to GDP growth in the US was highlighted again in the Q2 GDP report, suggesting that recent gains in payrolls may be overstated. We therefore expect a slowdown in hiring to a 180K pace in July. That's also consistent with the data on jobless claims, which were rising into the reference week in both non-adjusted and seasonally-adjusted terms, as well as the underperformance in the household survey.

The jobs gained in July could reflect further growth in the leisure and hospitality sector in particular, which more than accounts for the 524K deficit in payrolls relative to pre-pandemic levels, against a slowdown in interest-sensitive and goods-producing sectors that have seen demand wane. That would leave the unemployment rate unchanged at 3.6%, while wage growth likely continued at a 0.3% pace.

Forecast implications — We expect slower employment growth to continue ahead as the cautiousness in business investment and weakening in demand in interest-sensitive areas translates into the labor market. A cooling in hiring is a precursor for the Fed to slow the pace of rate hikes, and if sustained in August, that could portend a 50bps hike at the September FOMC.

Market impact — We're below the consensus which could be negative for the USD and see bond yields fall.

Other US Releases: ISM Manufacturing—July

(Monday, 10:00 am)

Global manufacturing prospects have deteriorated lately with the slowdown in growth as real household incomes are under pressure due to higher prices. That sets the stage for another potential drop in the ISM's manufacturing index in July, to 51.8, also driven by a further alleviation of supply chain bottlenecks which could lower the component tracking supplier delivery delays.

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