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INVESTMENT SERVICES

Weekly Relative Value

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WEEK OF JANUARY 13, 2025

Jobs, Jobs, and More Jobs!

*"Participants generally noted, however, **that there were no signs of rapid deterioration in labor market conditions, as layoffs remained low**. Participants generally judged that current labor market conditions were **broadly consistent with the Committee's longer-run goal of maximum employment**."*

*"Several participants observed that the evaluation of **underlying trends in labor market developments had continued to be challenging** and that assessments of the **outlook for the labor market were associated with considerable uncertainty."***
- Federal Open Market Committee (FOMC) Minutes, December 18

Jobs are the "glue" that holds the economy together. In other words, employment provides income that allows people to consume, which drives the consumption driven U.S. economy. Thus, as jobs go, so goes the economy.

The first week of every month comes with a bevy of labor market reports. In this week's edition of the *Weekly Relative Value*, I take a deep dive into the most recent labor market reports.

THIS WEEK

- JOLTING THE LABOR DATA
- PRIVATE JOBS DISAPPOINT
- JOBLESS CLAIMS DIVERGE
- BAD NEWS FOR BONDS
- FLYING BLIND
- MARKET OUTLOOK AND PORTFOLIO STRATEGY

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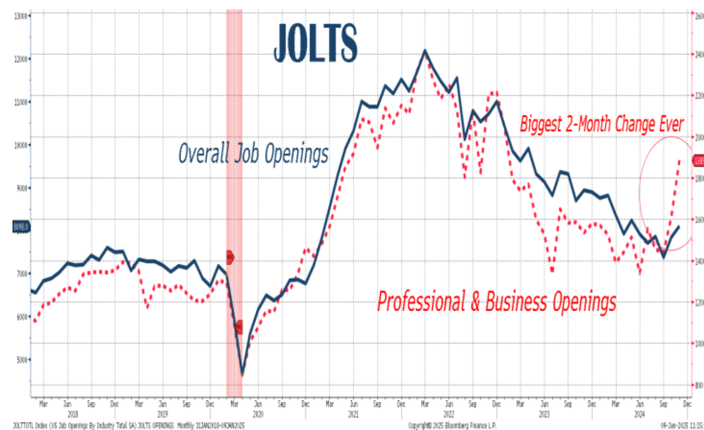
JOLTING THE LABOR DATA

The first labor report for the week was the Bureau of Labor Statistics' (BLS) Job Openings and Labor Turnover report (JOLTS) for November. This report showed a massive +259,000 run-up in job openings to 8.098 million, the highest level since May 2024 (and followed by a hefty +467,000 in October).

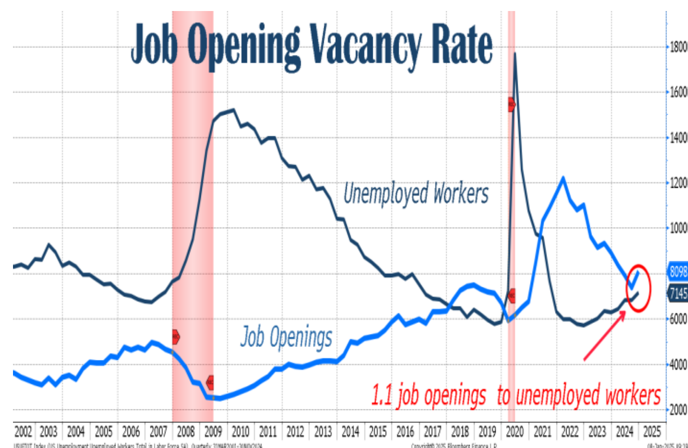
But this may be a giant head fake. The entire increase and then some was in "professional and business services" (+273,000), which is a proxy for temporary part-time employment. How realistic is this surge in professional services? I don't know, but I do know that the two-month increase in professional services job openings was the largest on record!

Outside of that sector, job openings shrunk -14,000, with declines in key sectors like retail (-4,000), manufacturing (-56,000 and down four months in a row), and leisure/hospitality (-83,000 in the steepest decline since May of last year).

Ignore the headline.



As far as job vacancies go, in November, the number of job openings was 953,000 more than the number of unemployed workers (7.145 million), up from last month's 855,000. Said otherwise, in July the number of job openings to unemployed was 1.1, a modest increase from last month, but on the low end of the pre-pandemic range in 2018-2019.

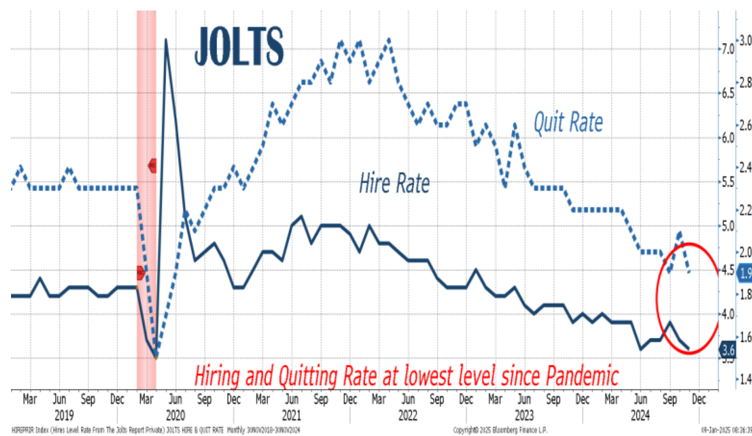


While the job openings data set was an upside shock, the true measure of what is happening in the labor market is *hiring and firing*. Job ads mean nothing.

So, when looking at the internals, layoffs held near low levels, but weakness continued in the hiring rate, sliding by 125,000 to 5.269 million to 10-year lows (excluding the lockdown months of 2020). This would be consistent with the prevailing *"No Hiring & No Firing Economy."* Nobody is getting let go. But nobody is getting hired either. Maybe because we're already at full employment? Or maybe because the outlook for many macro trends remains uncertain. Food for thought!

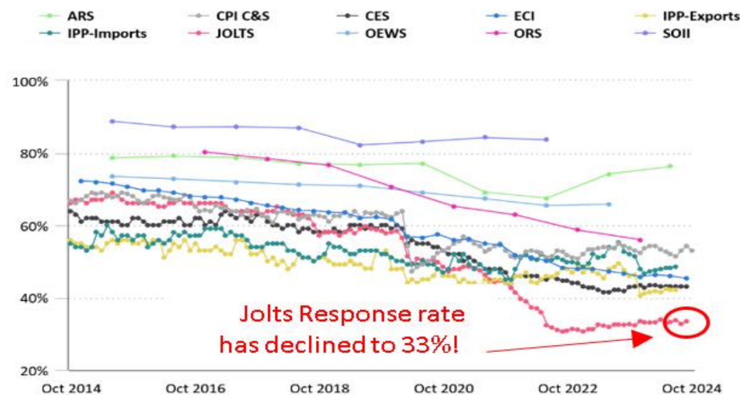
Likewise, the number of quits plunged to 3.1 million, the lowest since August 2020, as workers are clearly far less optimistic that they can find a higher paying job elsewhere and would rather be fired than quit.

On balance, this data point shows that worker confidence is waning sharply, and that will most likely feed into lower wage demands, and, as such, is disinflationary.



Finally, no matter what the "data" shows, let's not forget that it is all just "estimated," and it is safe to say that the real number of job openings remains still far lower since half of it — or some 70%, to be specific — is guesswork.

As the BLS itself admits, while the response rate to most of its various labor (and other) surveys has collapsed in recent years, nothing is as bad as the JOLTS report, where the actual response rate remains near a record low, at 33%! Is this a case of "garbage in, garbage out"?



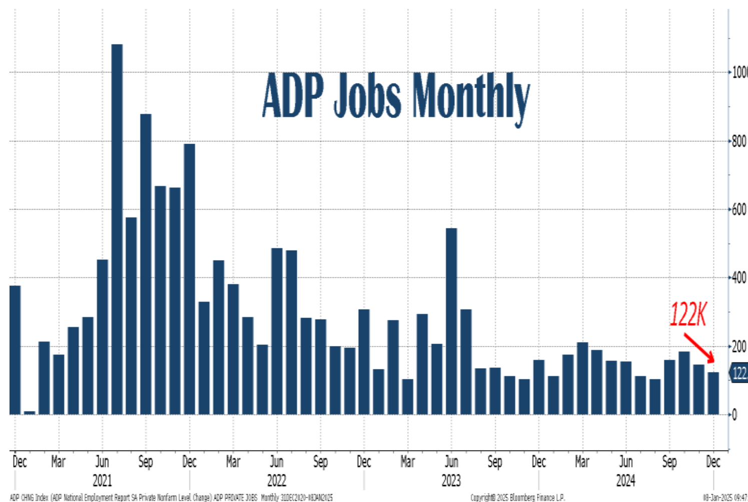
Source: BLS

Bottom line: When looking at the JOLTS data over the past 12 months, firings are up +14% while quitters are down 13%, job openings are down -9%, and hirings are down -5%. From my perch, this combination of data does not exactly point to a robust labor market. Do not be lulled into a false sense of complacency just because headline openings surprised to the high side. The U.S. labor market has more slack than commonly perceived, with important Fed and Treasury market implications

PRIVATE JOBS DISAPPOINT

"The labor market downshifted to a more modest pace of growth in the final month of 2024, with a slowdown in both hiring and pay gains. Health care stood out in the second half of the year, creating more jobs than any other sector. - Nela Richardson, Chief Economist, ADP

ADP's employment report (private jobs only) showed a disappointing addition of just 122,000 jobs in December (worse than the +140,000 expected). The December print represents a four-month low, bringing the 12-month moving average down to +152,000 compared to +209,000 at the same time last year.

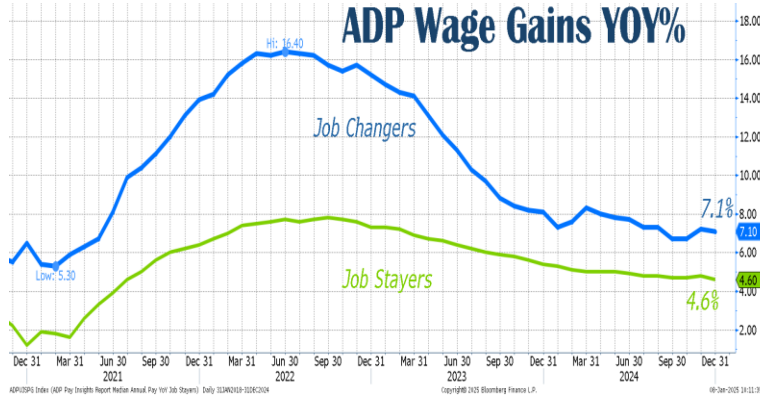


In a vivid sign of the ongoing industrial recession, manufacturing saw the biggest drop in jobs (the seventh monthly decline in manufacturing jobs in the last eight months)

Noticeably, there was virtually no pulse from the small business sector as small- and mid-sized firms cut employees (which is odd since the National Federation of Independent Business's Small Business sentiment literally exploded higher after Trump's election).

- Small companies (fewer than 50 workers), which represent the heartbeat of the economy, showed that jobs only rose +5,000 after last month's -15,000 falloff, having failed to show much verve over the past year.
- Medium sized businesses (50 to 499 employees) also saw a muted +9,000 increase in jobs, slowing from +44,000 in November and the worst tally since March 2023.
- The large companies (500+ employees) carried the load — rising by +97,000, though this represents the smallest increase in three months.

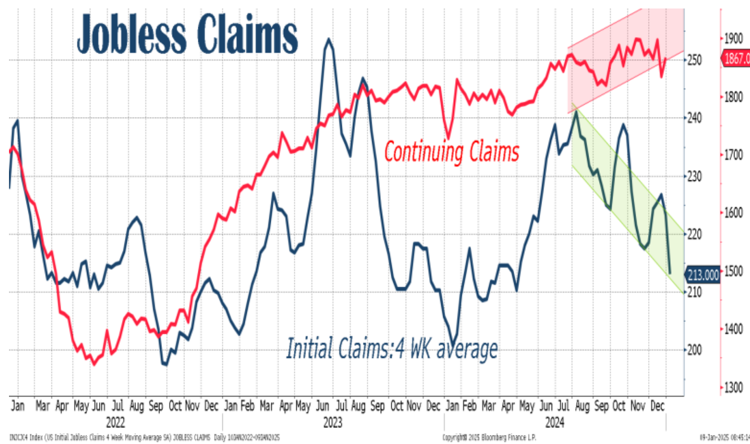
Helping on the disinflation front, the ADP report showed wage growth cooling further. Workers who changed jobs saw a 7.1% increase in pay, which is well off the peak of 16.4% in early 2022. Those who stayed put saw a 4.6% gain, the slowest since mid-2021.



Bottom line: The latest ADP employment report signaled a continued cooling off in the pace of wage and job growth in the private sector with sluggishness especially pronounced in small businesses.

JOBLESS CLAIMS DIVERGE

The high frequency weekly jobless claims continue to paint a mixed picture of the labor market. Initial jobless claims plunged to 201,000 – the lowest level since February 2024.



The initial claims data is inconsistent with other labor data. This could possibly be explained by fewer people claiming jobless benefits when laid off due to the paltry benefits. For example: The weekly unemployment benefit amount in Florida ranges from $32 to $275. This is hardly sufficient to pay the monthly bills.

Could it be that those receiving the dreaded pink slip have opted to drive for Uber or find a new gig elsewhere? Notably, the number of Uber drivers has risen by 15% to over seven million since Q4 2023.

Meanwhile, continuing "insured" claims were up to 1.867 million. As depicted in the graph above, from August of 2023 until April of 2024, it was easy to find a job if you lost one. That has not been the case since May of 2024.

I should also point out that "insured" unemployment generally ends at 26 weeks. After the benefits expire, those that have not landed a new job are no longer counted. This in turn suggests that the job market may be much tighter than advertised.

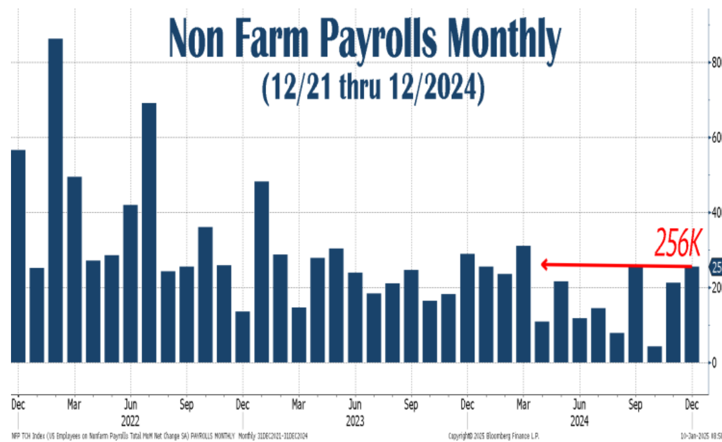
Bottom line: The "initial" jobless claims data may be distorting the true state of the labor market.

Regardless, if one loses a job in today's economy, it has become increasingly difficult to land a new position.

BAD NEWS FOR BONDS

*"**The only saving grace for the bond market at this point will be if risk markets really start to unravel**, otherwise there is no magical number that will be a line in the sand, **especially with all of the uncertainty ahead around the fiscal and government policies which may prove to be inflationary**."*
- George Goncalves, Head of U.S. Macro Strategy, Mitsubishi UFJ Financial Group

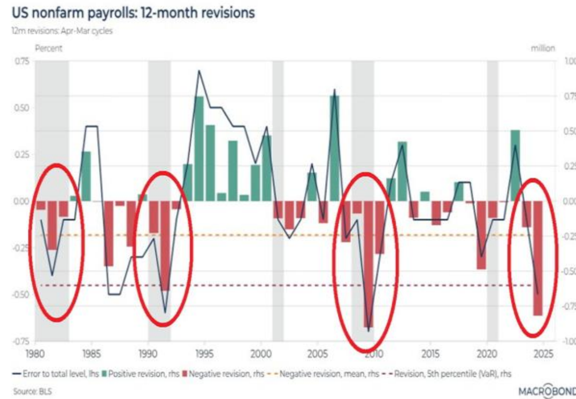
Flying in the face of the recent softness in the JOLTS data and ADP private payrolls reports, the December non-farm payroll report (NFP) payrolls blew the consensus forecast out of the water. According to this report, jobs rose by +256,000, nearly 100,000 higher above the median estimate of 165,000.



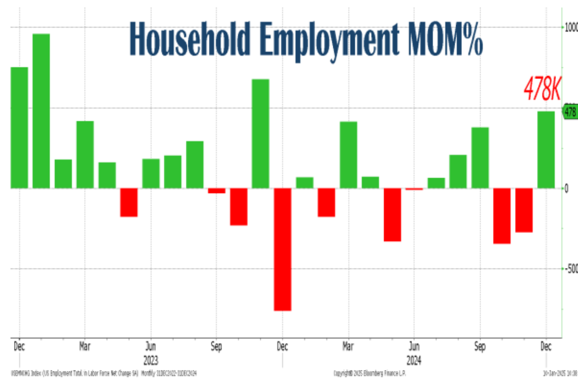
I should highlight that the raw non-seasonally adjusted payroll data showed a -81,000 DECLINE in a month that invariably sees an INCREASE (average of +162,000). Somehow, magically, the seasonally smoothed headline was +256,000! And that, my friends is cause for skepticism.

I also need to stress again that this report is famously inaccurate and revised quite often. In fact**,** non-farm payrolls have been revised DOWN for 23 consecutive months. Were you aware of that? And by a cumulative -686,000. The problem is that for the past year, the response rate to the first survey is only 60%. This is historically low and renders the BLS' first "take" on non-farm payrolls as a crapshoot.

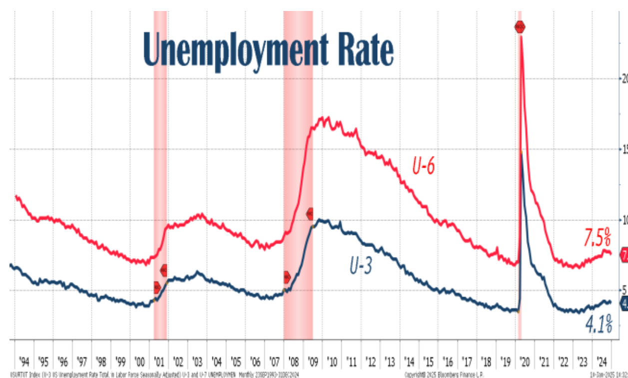
One should not forget that after a year of “robust” job growth, private payrolls were subsequently revised by nearly ONE MILLION for April 2023 - March 2024 (See graph below). The most recent data points to additional downward revisions in Q2 and Q3.



Confirming the strength of the establishment report, the household survey showed a sizable jump in employment, at 478,000, and comes after two big monthly losses.



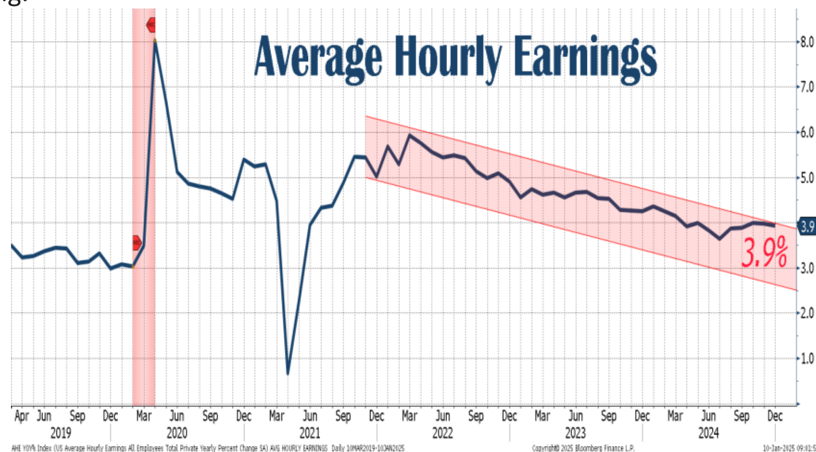
And in case the smoking hot payrolls print wasn't enough, the unemployment rate should have ended any hope of a rate cut, as it declined to 4.1% from 4.2%. The underemployment rate, tumbling to 7.5% from 7.8%, and a six-month low**,** was even hotter.



When drilling a bit deeper into the report, there were some nuggets that could possibly temper the strong headline data:

- Half of the growth came from the government, healthcare, and education sectors.
- The birth-death model accounted for +104,000 of the total increase in employment.
- **Nearly 80% of the employment creation was in part-time jobs, and 75% in youth aged 16-24.**

Another inconsistency with the red-hot headline number was average hourly earnings, which at 0.3% month over month and 3.9% year over year down from 4.0%. If the labor market truly is as tight as the NFP reports suggest (in contrast to the looser signal from alternative data sources), then we would expect to see that showing up in wage growth. Instead, wage growth is moderating.



Bottom line: The strong headline number can't be ignored. But the discrepancy with alternative sources like the JOLTS and ADP report put more importance on the upcoming February Quarterly Census of Employment and Wages (QCEW) benchmark revision. The QCEW is the broadest and most accurate read on the labor market, and as shown above, there were massive downward revisions last year. Thus, the strength in this report is suspect.

For now, however, the Fed will work with the data it has. If we were to see a string of reports like today's, we would run the risk of no rate hikes in 2025 and potentially seeing hikes being put back on the table.

FLYING BLIND

"Recent higher-than-expected readings on inflation, and the effects of potential changes in trade and immigration policy, suggested that the process could take longer than previously anticipated*. Several observed that the disinflationary process may have stalled temporarily or noted the risk that it could."*

*"**Almost all participants judged that upside risks to the inflation outlook had increased**. As reasons for this judgment, participants **cited recent stronger-than-expected readings on inflation and the likely effects of potential changes in trade and immigration policy**."*

- FOMC Minutes, December 18.

The Fed meeting minutes reflected the flip-flopping view that has occurred under Fed Chair Powell. After an emergency rate cut without an emergency in September, the FOMC is now favoring caution and not ease as aggressively as it indicated back in September.

Members did admit they're flying blind in the wake of President Trump's re-election and the impact of trade and immigration policies on inflation, where the majority of members deemed that the balance of risks tilts to the upside.

In other words, Donald Trump is making the economy harder to read.

Based on the FOMC minutes, it is obvious that medium term uncertainty about policy has spilled into monetary policy. But uncertainty cuts both ways, and the FOMC remains beholden to flawed real-time data as an indicator of the future direction of the economy.

I also find it quite interesting that at the November 7 FOMC meeting, just two days after the election, the Fed said it would not speculate and would not change policy until it had a full grasp of what President Trump was going to do. But apparently, something happened over the ensuing six weeks because the Fed changed its mind for whatever reason. So now the Fed is in the speculative game. I see a policy misstep in the making.

But not everyone at the Fed is playing yo-yo with the rates view. Governor Chris Waller stated:

*"If, **as I expect, tariffs do not have a significant or persistent effect on inflation**, they are unlikely to affect my view of appropriate monetary policy." … "**If the outlook evolves as I have described here, I will support continuing to cut our policy rate in 2025**."*

Now that the Treasury market has only one cut in the fed funds rate, the odds of a sharp reversal in the upward pressure on yields are rather high if Mr. Waller proves prescient.

MARKET OUTLOOK AND PORTFOLIO STRATEGY

"Change is the only constant in life." - Heraclitus, Greek philosopher

We head into the New Year with an extreme level of policy uncertainty from the incoming Trump Administration and a Fed that, in my opinion, has become overly anxious about inflation.

Yields on 10-year Treasuries closed the past week +16 basis points higher at 4.76% (with an intraday peak at 4.79% on Friday).

Moreover, since the Fed kicked off its easing cycle with a jumbo -50 basis point cut back in September, the 10-year Treasury yield has soared by over +100 basis points. Historically speaking, whenever the Fed has eased by this much, the 10-year yield fell -70 basis points. This is quite bizarre.

In fact, going back over the past six decades, only one time have 10-year yields risen more in a rate-cutting cycle, in 1981 when Volcker took the funds down from its world record high of 20%, and the bond market hated it (causing Edward Yardeni to coin the term, "Bond Market Vigilantes").

Even stranger, the two-year Treasury yield (which is hitched to the fed funds rate) has risen 81 basis points from 3.57% to 4.38%.

Why have bond yields risen so much?

First and foremost , the Fed has turned hawkish. At the end of last week, a number of FOMC members told markets not to expect any cuts in the immediate future.

Fed Governor Michelle Bowman said her vote for a cut in December was the “final step” in the Fed’s policy recalibration. Likewise, Kansas City Fed President Jeff Schmid said that the current policy settings are “near neutral,” and Boston Fed President Susan Collins called for “a gradual and patient approach to policymaking.”

Economist Paul Krugman thinks bond yields may be rising due to an “insanity premium.”

“Increases in long-term rates, like the 10-year Treasury rate, ***might reflect the horrible, creeping suspicion that Donald Trump actually believes the crazy things he says about economic policy and will act on those beliefs****,” – Paul Krugman, “Is There an Insanity Premium on Interest Rates?”*

That said, given that Trump’s first day is expected to see a flurry of announcements, it is possible to see this market backdrop persist for the weeks ahead.

It may well be the case that the Trump tariffs prove to be inflationary in the short-term, but that assumes that they live to see the light of day and aren’t just bargaining chips for other purposes. Either way, it is all speculation. What we do know from his first term was that the tariffs did not exert any lasting impact on U.S. inflation. When you look at the actual data and assess prices in the things you can actually see, touch, or feel, inflation is non-existent. It exists only in the land of government imputations and guesswork in the services sector.

- The Consumer Price Index (CPI) goods sector has now deflated year over year for six months running.
- Core goods, excluding food and energy, have experienced 11 months in a row of outright price decline.

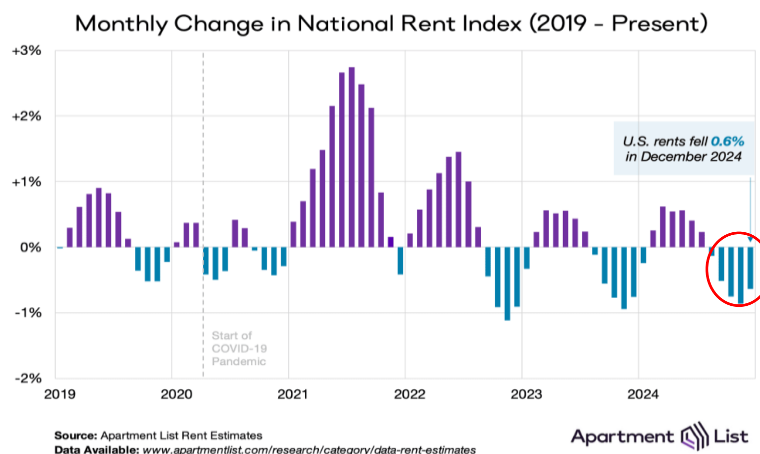
In the service sector, auto insurance premiums and residential rents have been the trouble spots. But the last couple of months show that these two frustrating areas are now coming off the boil in a material way.

Furthermore, while headline inflation prints have been a cause for pause in recent months, the key rental rate components (the dominant weighting in the CPI and the personal consumption expenditures index) are rolling over and will continue to filter through with a lag.

To make this point, the Apartment List rental data for December showed a -0.6% month-over-month decline — the fifth consecutive negative reading. Fully 88 of the nation's 100 largest cities saw rents decline last month (See following graph).

The year-over-year trend in rents in "real time" is running at -0.5%. It is not commonly known that once shelter is taken out of the data, the inflation rate is down to +1.6% on a year-over-year basis, and the core rate is at +2.2%.

Thus, while the Fed may be deservedly concerned about Trump's macro policy pledges, in the here-and-now, inflation is not an issue.



Not to mention, the composition of Congress (and specifically the House) is less favorable than in 2017 and also makes passage of any key policy announcements that add to the deficit that much harder.

Moreover, all the talk of the Department of Government Efficiency (DOGE) and deregulation are inherently disinflationary, not inflationary.

Against this backdrop, I should stress that this erratic Fed has shifted its views like a yo-yo time and time again. I believe that as quick as the Fed was to remove two rate cuts from its latest set of dot plots, don't be surprised how quickly they add them back in in the months ahead.

Finally, the bond market is currently viewed as the proverbial "ugly duckling," making it one of the most denigrated asset classes at the moment. This setup is incredibly positive from a contrarian perspective as any type of surprise can spark a massive shift in such a one-sided backdrop.

Bottom line: It's safe to say unless something changes, and fast, don't expect a rate cut in January. Beyond that, it looks like the Fed is trying to gain a better sense of the policy initiatives from the Trump Administration. But this Fed has reversed course repeatedly, so we'll see what happens over the next 12 months.

In the near term, the byproduct of a more hawkish Fed is that the front and middle portions of the Treasury yield curve —given an unpredictable and uncertain near-term policy outlook — offer the best value at this time. Investors can still

buy the 5-year and 7-year part of the yield curve with respective yields around 4.5%. Though I could not fault investors for wanting to move towards the front end of the curve with the 2-year Treasury at 4.38% or riding out the volatility with a portion of the investment portfolio in cash that is paying you to wait continues to make sense. Dips can be bought as attractive entry-points.

I feel that by year end the macro and inflationary backdrop will be more constructive for the Treasury market.

I'll leave you with this: The reason why I have advocated the "ladder strategy" for years is because of the inherent unpredictability of markets. Thus, rather than forecasting or trying to time the markets, credit unions would be well served by implementing this time tested, all-weather approach to portfolio risk management, especially in the bizarre climate we find ourselves in today.

MORE INFORMATION

For more information about credit union investment strategy, portfolio allocation and security selection, please contact the author at **tom.slefinger@alloyacorp.org** or (630) 276-2753.

As Alloya's Market Strategist, **Tom Slefinger** leverages nearly 40 years of investment strategy expertise to deliver insightful commentary on the economy and market events to optimize balance sheet performance at the credit union level. With thousands of subscribers, Tom's daily and weekly publications are widely read amongst credit union executives.

Prior to becoming the corporate's Market Strategist, Tom served as the Senior Vice President of Institutional Fixed Income Sales at Alloya Investment Services, a division of Alloya Solutions, LLC. In this role, Tom developed and managed operations associated with institutional fixed income sales in addition to developing investment portfolio strategies, identifying appropriate sectors and securities, and optimizing portfolio performance at the credit union level.

Tom holds a B.S. in business administration from the University of Maine. In addition, he holds a Series 7 and 63 through ISI.

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