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Inconsequential easing of jobs growth

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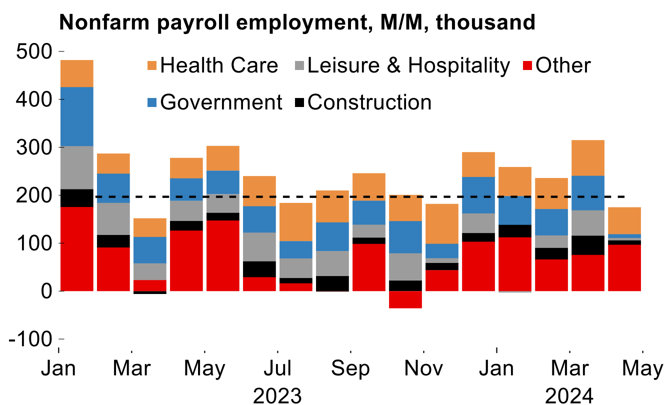
- Headline jobs growth decelerated in April, much of which was driven by slower growth in three of the "big four" industry groups that have been sustaining labor demand since 2023. Growth was nearly flat in government, leisure and hospitality, and construction, but it remained strong in health care. Jobs in "other" industries, which includes professional and business services, continue to be added at a rate similar to the past four months.
- The unemployment rate ticked up to 3.9%, with unemployment falling for younger workers (16-24) but rising for older workers (55 and older). Job openings continue to gradually fall, with the vacancy to unemployed ratio dropping to 1.3 in March, but the slower pace of openings is matching the slower hiring rate. Shortages of skilled labor combined with low turnover can help explain the elevated time it takes to fill an open position.
- Annual wage growth from the Employment Cost Index (ECI) was flat in Q1 2024, but an acceleration in union wage growth was a major contributor. Wage growth for those not in unions, the vast majority of workers, continued to decelerate and the falling quits rate points to further deceleration in 2024. Overall growth in unit labor costs remains relatively low, indicating less passthrough of wages into prices, but the trend is different in manufacturing.

Flat growth for 3 of the "big 4" industries

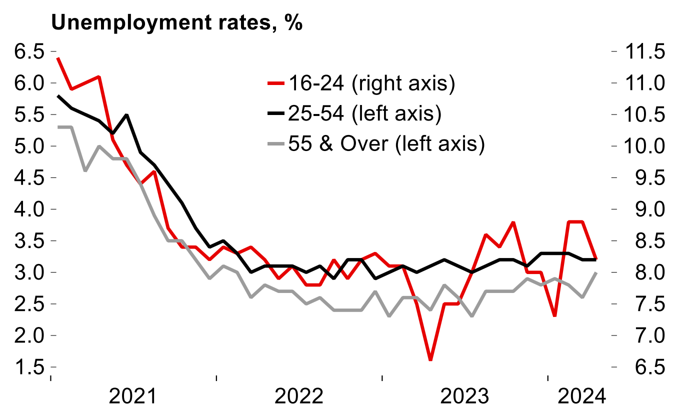
The labor market added 175,000 jobs in April, the slowest monthly growth since October of last year (Chart 1). Employment growth in health care continued to be strong (+56,000), but the trend reversed in government, leisure and hospitality, and construction where growth was flat. Since 2023, these four industries drove jobs growth and that's unlikely to change in the coming months, despite weakness in April.

Chart 1: Employment growth in "other" industries was steady over the past several months



Source: BLS, MUFG Bank Economic Research Office

Chart 2: A drop in unemployment of younger workers was offset by a rise in older workers



Source: BLS, MUFG Bank Economic Research Office

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It is unlikely that local government jobs growth will remain flat, considering it had strongly expanded for 15 straight months. New home construction is continuing along an upward trend, which will support further jobs growth in the industry, and continued spending on food services and accommodation will help increase employment levels in leisure and hospitality. For better indications of weakness in the labor market, look to employment growth in the “other” industry sectors.

In April, jobs growth in retail trade and transportation and warehousing helped keep monthly growth in the “other” category relatively strong. But growth in professional and business services continues to be weak, a historically strong recession signal.

With all of that said, there is little new information to go off of with respect to how the Fed will conduct monetary policy. The “new” weakness described above (flat growth in the 3 major industries) will likely be short lived, and the “existing” weakness (slow growth in professional and business services) has been going on for quite some time.

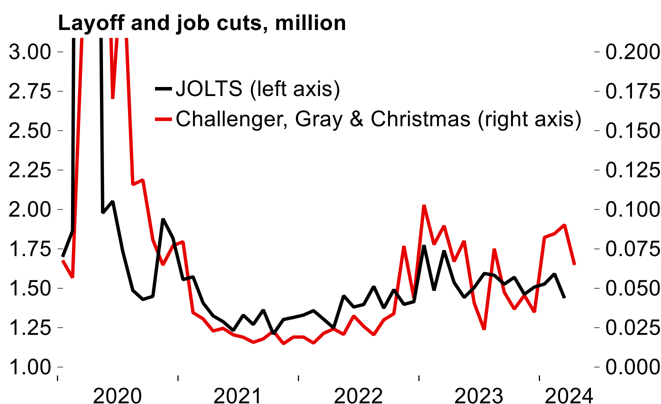
Additionally, the unemployment rate continues to hover between 3.7-3.9%, much of which is being driven by volatility of younger workers (Chart 2). In April, the drop in unemployment of younger workers (16-24) was offset by a rise in unemployment of older workers (55 and older). The unemployment rate for prime-age workers (25-54) has been flat for several months.

When Fed Chairman Powell stated that the labor market “in and of itself” will not direct Fed interest rate policy, it was implied to be in relation to inflation. If inflation “sustainably” reaches 2% (plus or minus a certain margin of error), strong wage and employment growth will likely not put off rate cuts. However, if inflation does not reach target, and it looks as though it will not until Q4 at the very earliest, then the labor market will be the deciding factor. More specifically, if the unemployment rate rises to around 4.2%, that may trigger the beginning of the rate cutting cycle, in adherence to the Fed’s dual mandate of maximum employment and stable prices.

Low layoffs and persistent hiring difficulties

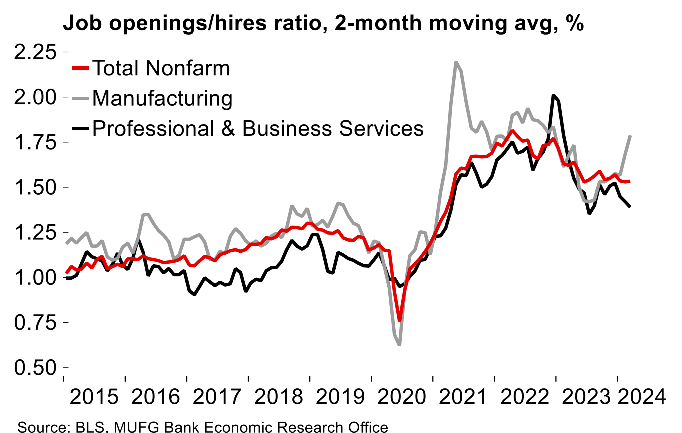
The general trend of falling job opening continued in April, and the vacancy to unemployed ratio fell to 1.3, indicating a further loosening of the labor market. Layoffs also remain low, despite prior indications of an upward trend (Chart 3). Together, these indicators portray what is sometimes referred to as the “immaculate cooling,” where job openings fall without rising unemployment.

Chart 3: Layoffs fell in March, partially reversing a slight upward trend that had built up in the months prior



Source: BLS, Challenger, Gray & Christmas, MUFG Bank Economic Research Office

Chart 4: Elevated job openings to hires ratio shows continued hiring difficulties



Source: BLS, MUFG Bank Economic Research Office

This phenomenon was not expected due to the potential high levels of employee mismatch or skills gap where the skills that an employer desires are not present in the available workers. In this environment, job openings can stay elevated for certain types

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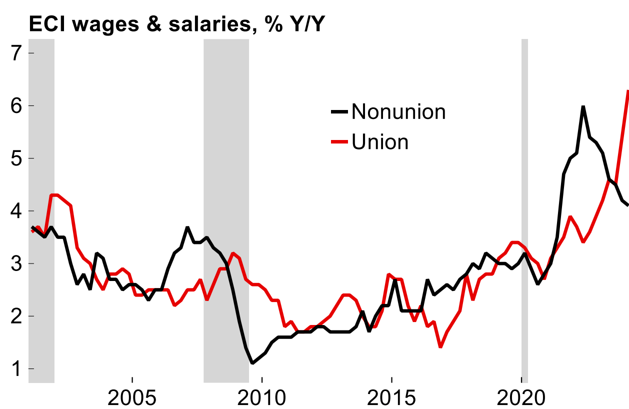
of workers while job losses increase for other types. The fact that this has not been occurring may indeed be "immaculate" because a skills gap is still very likely present.

The job openings to hires ratio, a proxy for time to fill a position, has been flat for several months with the hiring rate falling below its pre-pandemic level (Chart 4). This has been occurring at the same time that the quits rate is falling. Less turnover from one company to the next and less mobility of workers with relevant skills can keep hiring rates low, while maintaining elevated job openings. How much longer the "immaculate" cooling can continue is unknown, but it will likely not be due to a narrowing of the skills gap.

Union workers are driving wage gains

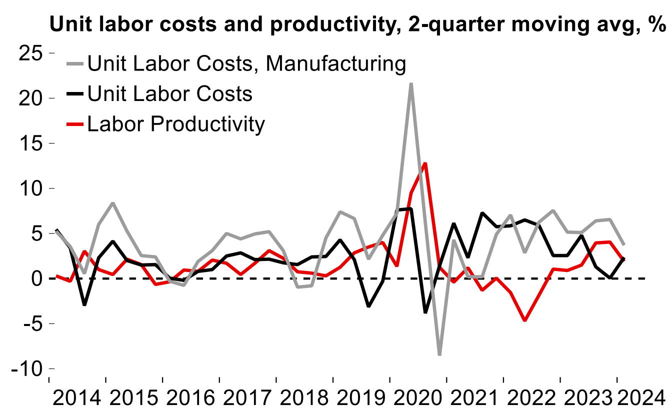
The Q1 2024 Employment Cost Index (ECI) showed flat annual wage growth of 4.3%. A major contributor was union workers, whose wage growth accelerated to 6.3%, up from 4.5% in Q4 2023 (Chart 5). Wage growth for the majority of workers (i.e., nonunion) decelerated to 4.1% in Q1. With that context, we should expect further deceleration in 2024 for the majority of the labor market given the strong relationship between the quits rate and wage growth as discussed in a previous brief.

Chart 5: Union workers drove much of the wage growth in Q1 2024



Source: BLS, MUFG Bank Economic Research Office

Chart 6: Growth in labor productivity is helping keep growth in unit labor costs relatively low



Source: BLS, MUFG Bank Economic Research Office

Though wage growth is easing, it remains elevated and above what would historically be consistent with 2% inflation. However, the passthrough into prices may be limited this time around. Labor productivity growth has remained comfortably in positive territory since 2023, and unit labor costs have been falling as a result (Chart 6). These developments are good news with respect to inflation, indicating that wages will apply less of an upward pressure on prices. However, the situation is different in the manufacturing sector, where sluggish productivity growth and accelerating wage growth (in part from union wage negotiations) have growth in unit labor costs well into positive territory. Though not definitive, this presents an upward price pressure on manufactured goods and a downward pressure on profit margins for manufacturing firms.

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