Payden&Rygel

Economic Update

THOUGHTS FROM OUR ECONOMICS TEAM

MAY 2, 2014

IS THIS WHAT WE'VE ALL BEEN WAITING FOR?

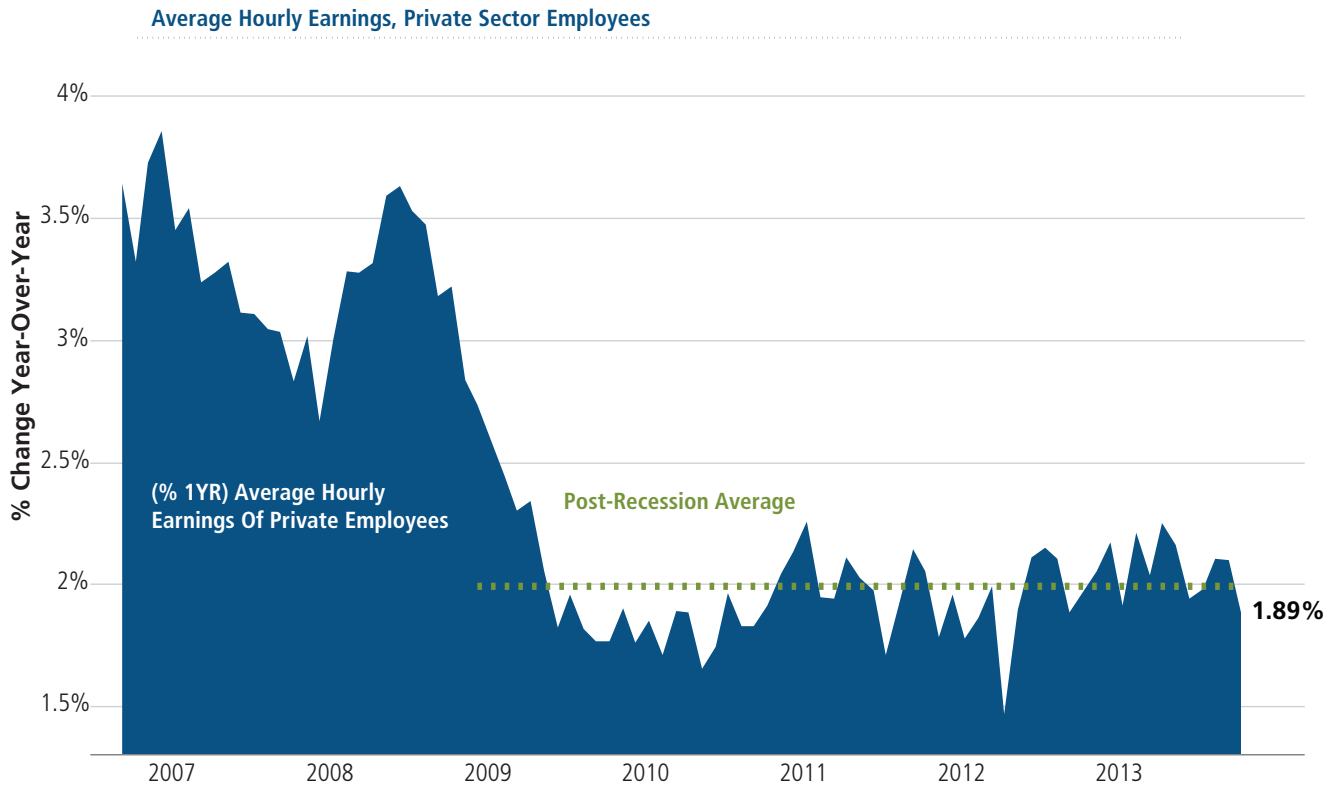
Nonfarm payroll employment rose 288,000 and the unemployment rate tumbled 0.4 percentage points to 6.3% in the month of April, according to the Bureau of Labor Statistics. Employment gains were widespread as employment increased in 67% of industries: professional and business services, retail trade, food services and drinking places, and even construction all saw net job creation. The March report was also revised higher, putting in place three months of +200,000 job gains. All told, the three month average lifted to 238,000—a solid run indeed.

But the data conundrum continues: bad news on wage growth—up only 1.9% year-over-year (see chart 1 below)—and on labor force participation offset good news on the headline payroll figure. In fact, in April, 806,000 people left the labor force, bringing the participation rate down to 62.8%, a 36-year low.

While we hope the 288,000 nonfarm payroll number represents an acceleration in job gains, investors ought not draw conclusions from one month of data. We could be seeing some catch up from an unusually sluggish winter period and each month's report carries an error bar of +/- 90,000 (!) jobs. For those interested, a New York Times article this week lays out the case brilliantly, showing just how hard it is to separate signal from noise in the first release of each month's jobs report.

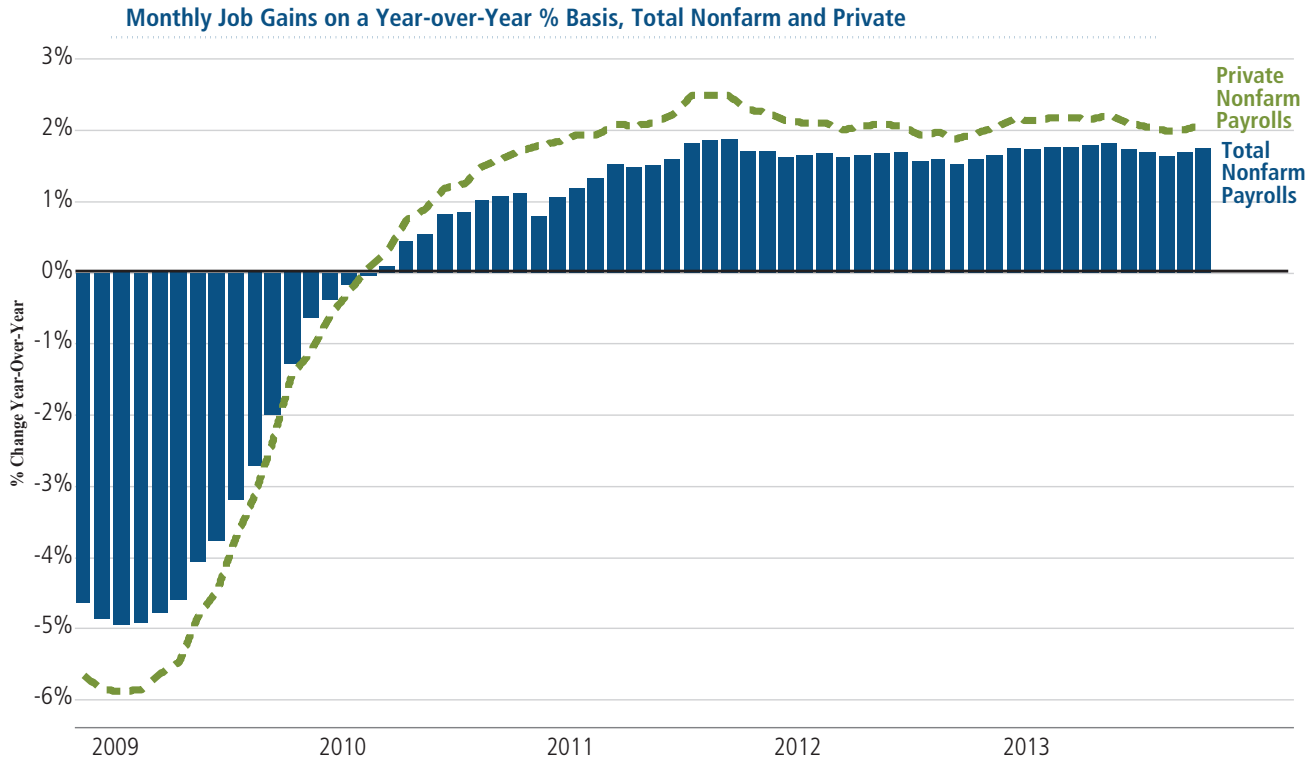
Instead of watching only the headline number from the most recent month, longer term metrics such as a six month average (+202k) or a twelve month average (+197k) give us a better sense of labor market health. We can also look at year-over-year changes, to smooth the monthly noise: this month, we see a very stable trend of 2% year-over-year private sector job growth and 1.8% year-over-year total nonfarm payroll employment (see chart on next page). On these broader measures, a return to 200,000 monthly job growth looks more like a return to normal than an upside development.

WHERE'S THE WAGE GROWTH WE'VE BEEN HEARING SO MUCH ABOUT? LOTS OF NOISE AROUND A 2% TREND. WAGE PRESSURES ABSENT.



Source: Payden Calculations, Bureau of Labor Statics

PAYROLLS DEMONSTRATE A REMARKABLY STEADY TREND OVER THE LAST FOUR YEARS



Source: Bureau of Labor Statistics

We think Fed policymakers welcome the return to normalcy as most were expecting a rebound in activity. The April jobs report certainly helped support the FOMC's policy decision to continue tapering asset purchases. However, the data conundrum highlighted above persists and provides little motivation for a higher federal funds rate anytime soon. A glance at Janet Yellen's favorite data nuggets shows that the labor market is far from normal (see table below).

Overall, despite our delight at the headline job gains, we think we are still in a moderate payroll growth, low wage growth, low inflation environment with a great distance to a normal labor market. We feel the FOMC draws similar conclusions and will therefore be patient before hiking interest rates. We look forward to Janet Yellen's testimony on May 7th on Capitol Hill for an opportunity to update our view.

AFTER A STRONG REPORT IN APRIL, SOME LABOR MARKET INDICATORS RETURNED TO "NORMAL" LEVELS…HOWEVER, THE FED WILL AWAIT FURTHER HEALING

Janet Yellen's Data Dashboard – Labor Market Indicators

Indicator	April 2013	April 2014	Labor Market Norm	Distance from Normal
Unemployment Rate	7.5%	6.3%	5.5%	0.8%
Nonfarm Payrolls	203	288	200	88
6 month Avg. Non Farm Payrolls	206.3	202.5	200	2.5
Labor Force Participation Rate	63.4%	62.8%	64.0%	-1.2%
Quits Rate	1.6%	1.7%	2.1%	-0.4%
Hire Rate	3.3%	3.3%	3.8%	-0.5%
% Unemployed for > 27 wks	37.4%	35.3%	18.2%	17.1%
Average Hourly Earnings (%YoY)	2.0%	1.9%	3.5%	-1.6%

Sources: Bureau of Labor Statistics, Payden Estimates