Tea Leaf

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Job Strength

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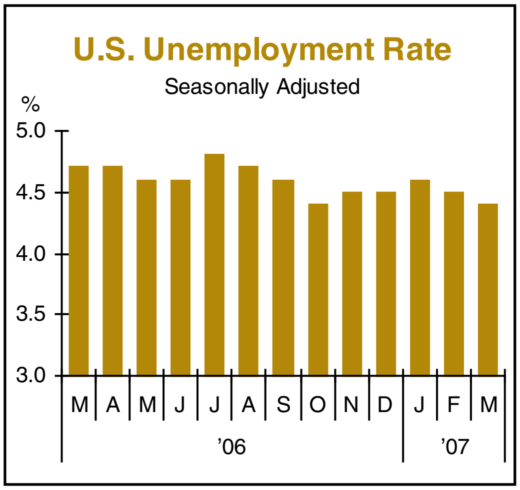
U.S. economic growth naysayers were slapped down again last Friday with the release of the March employment report, which showed solid employment gains and a drop in the nation's unemployment rate. Unfortunately, these loud "recession is imminent" forecasters will simply wait for the next less-than-rosy morsel of economic information to make their case.



I am not in the recession view camp…never have been…although a variety of unexpected factors could drive the American economy into decline. A significant worsening of housing market performance from current levels, as well as much greater financial market anxiety tied to sub-prime and traditional mortgage lenders, could disrupt spending and employment enough to tip the economy into recession…

…I just don't think it will happen

Perhaps the ultimate judge and jury of whether the U.S. economy is headed for a downturn is the stock market. If the Dow had continued to decline to the 11000-11500 range from February's all-time high of 12795, one could surmise that "the market" expected a recession. However, tens of thousands of stock market traders and investors have looked at the housing activity issue…have examined the sub-prime lender issue…and have studied dozens of other economic facets…

…the Dow average now north of 12550 again suggests that U.S. economic growth will continue—in the consensus view of market players

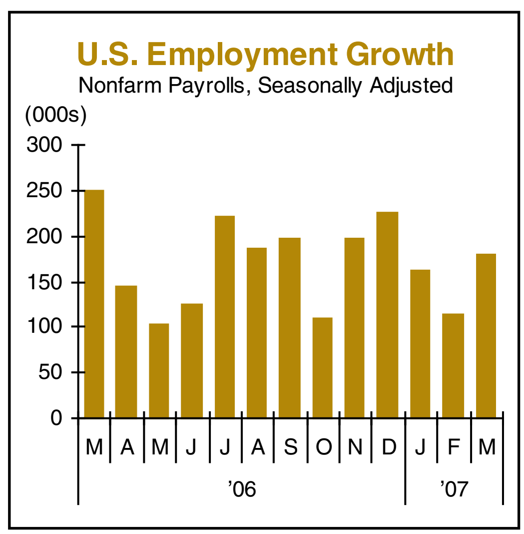
The Employment Data

The American economy added a stronger-than-expected 180,000 net new jobs during the month of March, roughly one-third more than the consensus forecast. As has been a regular pattern over recent months, job creation estimates of the two prior months were revised higher, in this case a combined upward revision of 32,000 jobs in January and February.

At the same time, the nation's unemployment rate declined to 4.4% in March, down from the 4.5% rate in February. Many financial market players had expected the rate to rise to 4.6%.

Why did the unemployment rate decline? Why did the number of unemployed people in the labor force decline by an estimated 141,000 persons to just over 6.7 million?

Because the other major employment survey—that of 60,000 households surveyed monthly and from which the nation's unemployment rate is derived—saw an estimated 335,000 net employment rise in March. The estimated labor force in March rose by 195,000 people to just under 153 million.



We have frequently noted our view that the job creation totals within the "household survey" are at times a better indicator

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of the labor market than is the monthly "establishment survey" of 375,000 medium and large businesses. The household survey *includes* job gain estimates tied to new small business creation and expansion of current small businesses. The establishment survey does not.

Posing a simple question can illustrate the point…Who (or what) in your community is creating new jobs…large businesses or small businesses? I would argue that small business is the job creation machine in this country more than ever before.

Jobs in March

Some surprises were contained within the March employment report, even as the net addition was impressive. The goods-production sector added a net 43,000 new jobs in March. The construction sector had a net gain of 56,000 jobs in March, reversing the 61,000 estimated construction job loss in February. Cold weather in February gave way to milder weather in March.

At the same time, however, job creation in the nonresidential (or commercial) construction sector has been adding jobs even as an overbuilt residential sector has been losing employment. It appears the ability of skilled construction workers to shift from building single-family homes to more recently building office, industrial, and retail properties is high. The news in manufacturing was less upbeat, with a loss of another 16,000 jobs, the ninth consecutive month of manufacturing employment declines.

The larger service-providing sector added 137,000 net new jobs in March. Professional & business services employment declined by 7,000 jobs in March, after solid gains in most of the past few years. The retail trade sector added an estimated 36,000 net new jobs, the strongest gain since July 2005.

No surprise here…the education and health services sector added another 54,000 jobs in March, mostly in health care. The health care sector has accounted for roughly one of every six net new jobs added during the past six months, according to the Labor Department's number crunchers. In addition, the government sector added 23,000 net new jobs during March, while the leisure & hospitality sector added 21,000 jobs.

The average hourly wage rose six cents (0.3%) to $17.22 hourly. The 4.0% rise over the latest 12-month period is good news for consumers as it exceeds a smaller rise in inflation during the past year. Such news is less positive to Federal Reserve officials, who see inflation under every rock.

The Value of Education?

As one might expect, unemployment rates in an increasingly sophisticated economy are lower for those with higher levels of education. The jobless rate for those with less than a high school diploma was 7.0% in March, while the jobless rate for those workers who finished high school and had no college was 4.1%.

The jobless rate for those workers with some college or an Associate's degree was 3.6%. The jobless rate for those workers with a Bachelor's degree or higher?…1.8%.

And as before, the earnings differential for college graduates versus high school graduates is enormous, with the average college graduate making nearly twice as much annually as the average high school graduate. Education pays!

At the Fed

Stronger-than-expected American job creation during March has—at least for now—slashed hopes of a near-term easing of monetary policy by the Federal Reserve. Based on numerous signs of U.S. economic slowing announced in recent weeks, financial markets had "priced in" solid expectations of a 0.25% cut in the Fed's critical federal funds rate (now at 5.25%) in late June 2007. Market expectations had also priced in another 0.25% rate cut in early August or mid-September.

Solid March employment data now suggests the Fed will remain in "pause" mode until September. Financial market players largely expect a rate cut at that time. However, a vocal minority of economists still expect the Fed to push its key interest rate higher in 2007's second half in order to confront lingering inflation pressures…

…stay tuned

Jeff

"TEA"ser

NEVER refer to your wife and mother-in-law as dual air bags.

—Scott Friedman

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