Employment report May 2024

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Labor market sending mixed signals

- While strong on the surface, the labor market sent some mixed signals in May. The combination of robust payroll job creation, firmer wage growth and weaker labor supply pointed to a labor market that remains tight. Yet, the plunge in household employment and rise in the unemployment rate to a two-and-a-half-year high painted a more nuanced picture and corroborated other data pointing to softer labor market conditions.
- The economy added 272,000 jobs in May, well above consensus expectations, while prior estimates of job growth in March and April were revised lower by a cumulative 15,000 jobs. The reacceleration in job gains was broad-based with the private sector adding 229,000 jobs and the government sector adding 43,000 jobs (confirming the weakness in April was likely a blip).
- Health care remained at the forefront of job creation, while leisure and hospitality and professional and business services reported solid rebounds in payrolls. Together, these three industries accounted for nearly 80% of total services job gains last month. Meanwhile, goods employment revived on stronger hiring in construction and continued sluggish manufacturing payroll gains.
- A 157,000 increase in unemployment helped push the unemployment rate 0.1 percentage points (ppt) higher to 4% in May, its highest level since January 2022. The unemployment rate has been slowly grinding higher over the past year, as the slower business environment has led companies to become increasingly discerning with their hiring.
- Disappointingly, the labor force participation fell 0.2ppt to 62.5% in May, reversing the progress made so far this year. The sharp rebound in immigration over the past two years had been a key factor driving the labor supply higher, so the recent slowdown in immigration flows is likely acting as a restraint.
- Average hourly earnings showed renewed momentum and grew a stronger-than-expected 0.4% month over month (m/m) in May, pushing wage growth 0.2ppt higher to 4.1% year over year (y/y). Despite the uptick, we continue to expect wage growth to moderate further as labor demand and supply have converged toward a better and less inflationary balance.
- Heading into next week's Federal Open Market Committee meeting, robust job creation and firmer wage growth will likely reinforce policymakers' backward-looking hawkish bias. We continue to believe a July onset of the easing cycle would be optimal given easing inflation and softening labor market conditions, but the risks of a delayed onset in September are growing.

- Overall, we expect the labor market to maintain enough forward momentum to carry the consumer throughout the rest of the year, but the pace of job creation is poised to slow as softer consumer demand, reduced pricing power and lower profitability lead companies to become more pragmatic with hiring and wage increases. Against this backdrop, job growth will likely slow below trend over the course of the year, and the unemployment rate will rise toward 4.2% by year-end.

In the details

Employment growth in May was broad-based with the employment diffusion index — a measure of how many private sector industries are adding jobs — rebounding to 63.4%, which is the highest level for this measure since January 2023. The private sector added 229,000 jobs last month, and the government sector added 43,000 jobs. Factoring the downward payroll revisions in March and April, the private sector added an average of 206,000 jobs over the past three months, somewhat higher than the 190,000 average of the prior month.

Looking into the details, the health care and social assistance sector continued to add jobs at a brisk pace. Employment in the sector rose by a robust 84,000 jobs and has accounted for nearly half of all jobs created in the services sector so far this year.

Employment in the leisure and hospitality sector rebounded markedly with a broad-based 42,000 increase in payrolls following a soft 12,000 gain in April. The professional and business services sector also surprised on the upside with a 33,000 increase in payrolls that comes on the heels of a 7,000 average gain over the prior three months.

The overall services payrolls gain was further supported by moderate gains of 13,000 and 11,000 in retail, and transportation and warehousing, respectively.

On the goods front, the 25,000 rebound in job gains was largely driven by stronger construction employment, which climbed by 21,000, while manufacturing payrolls saw another subdued increase of 8,000. Factory hiring has remained sluggish over the past year, as the sector faces challenges from weaker domestic and global demand for manufactured goods and higher borrowing costs.

Government employment resumed its strong uptrend with a 43,000 increase following the slowest monthly increase since December 2022. The gain was largely driven by employment in local government, which rose 34,000 in May. Following a strong and delayed post-pandemic rebound, the trend in job creation by state and local governments appears to be gradually slowing as economic conditions cool.

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