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US Economics | North America

Employment Report Preview: A downshift in hiring

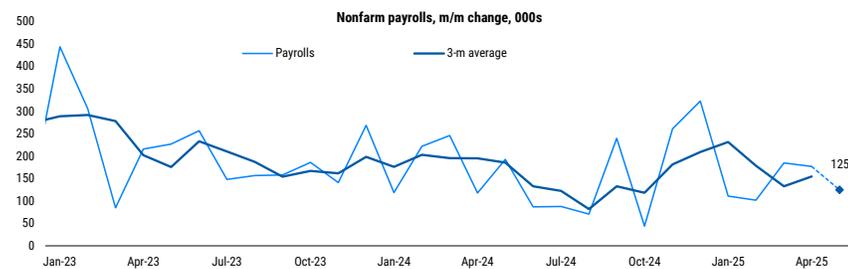
Payrolls rise 125k in May, with slowing in labor demand, payback for April, and a drag from federal gov't layoffs. Unemployment is unchanged at 4.2%. AHE rises 0.3% m/m and slips a tenth to 3.7% y/y.

Exhibit 1: Employment forecast details

	Est.		Consensus		Actual		
	May-25	May-25	Apr-25	Mar-25	3MMA	Year-Ago	
Change in nonfarm payrolls (thous.)	125	125	177	185	155	193	
Private payrolls	125	113	167	170	148	160	
Unemployment rate (%)	4.2	4.2	4.2	4.2	4.1	4.0	
Labor force participation rate (%)	62.6	62.6	62.6	62.5	62.5	62.6	
Average weekly hours	34.3	34.3	34.3	34.3	34.3	34.3	
Average hourly earnings (%M)	0.3	0.3	0.2	0.3	0.2	0.4	
%Y	3.7	3.7	3.8	3.8	3.8	4.1	

Source: Bureau of Labor Statistics, (BLS), Bloomberg, Morgan Stanley Research forecasts

Exhibit 2: We project payrolls rose 125k in May



Source: BLS, Morgan Stanley Research forecast

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Payrolls Forecast

We expect slowing in payrolls, with some slowing in labor demand, some payback for April, and a drag from federal government layoffs. Despite the slowing, we anticipate the unemployment rate is unchanged from April. Payroll breakevens appear to be falling as immigration is restricted, and we expect ongoing downward pressure on the unemployment rate even as payrolls slow.

High-frequency data suggest slowing in payrolls. From early April to early May, new jobless claims rose about 10k to 230k and continuing claims rose about 25k to nearly 1.9 million. Furthermore, both continued to rise into the end of the month. The rise in new claims indicates faster layoffs; the rise in continuing claims suggests that and slower re-employment as well. Separately, in consumer surveys, assessments of the labor market continued to worsen despite some rebound in confidence about other elements of the economy.

Job openings also suggest softening labor demand. They fell sharply in March, and the vacancy rate (job openings/unemployed) fell to 1.0, its lowest (apart from the pandemic) since early 2018. Yet April payrolls did not show obvious pullback in labor demand. We expect more impact in May.

We suspect that the timing of Easter—its swing from late March to late April—boosted April payrolls, with payback likely in May. Over the past 15 years, similar swings were associated with payrolls ~50k to 100k above trend, with a lot of noise and some suggestion that April first prints tend to be above trend regardless of Easter timing. We are assuming a 25k boost to April and drag on May.

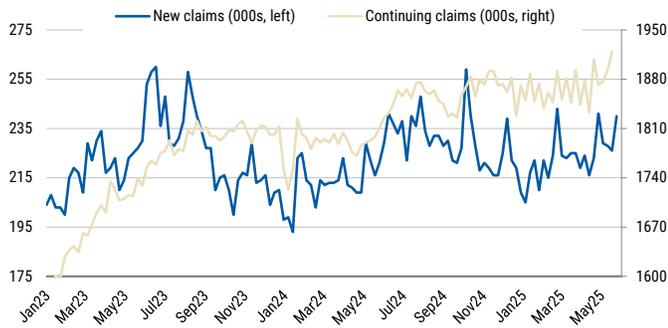
We expect government payrolls stall. A 20k decline in federal payrolls offsets ongoing increase in state and local government employment. We expect the layoffs of probationary employees, delayed by court order earlier this year, drag on federal payrolls. The wildcard in government employment may be federal hiring. One of President Trump's first executive orders was a limit on federal agency hiring of one new employee for every four in layoffs. In March, federal hiring was about ½ the pace of the prior year but still well above that 1:4 target. We expect some further slowing contributes to the 20k drop in federal payrolls in May.

There's been little sign yet that the slowdown in federal payrolls is spilling into private employment. In MD, VA, and DC, new jobless claims in May were about 3k above their pre-inauguration pace.

There's upside risk to our forecast if job openings do not hold onto their March decline. Data are reported June 3. And our estimate of the Easter effect has wide error bands.

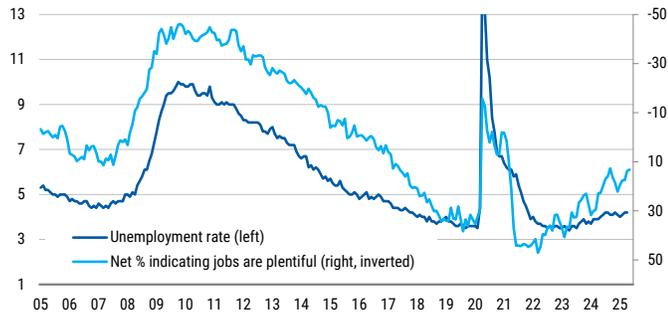
There's downside risk to our forecast if federal payrolls are spilling into private sector activity more than we understand or if the private sector pulls back more broadly in response to new policy and policy uncertainty.

Exhibit 3: New and continuing jobless claims rose between early April and early May



Source: Department of Labor, Morgan Stanley Research

Exhibit 5: Households' labor market assessments deteriorated slightly in May



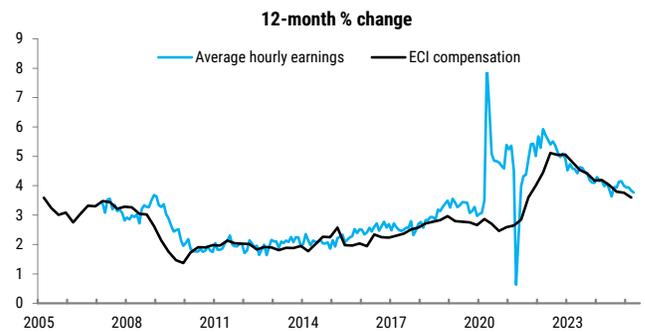
Conference Board, Morgan Stanley Research

Exhibit 4: Job openings fell beyond recent lows in March



Source: BLS, Morgan Stanley Research

Exhibit 6: Average hourly earnings continue to slow gradually



Source: BLS, Morgan Stanley Research

Exhibit 7:

Industry breakdown of payrolls, and our May forecast

monthly change, 000s	Average monthly change			Feb	Mar	Apr	May est
	3Q24	4Q24	1Q25				
Nonfarm	133	209	133	102	185	177	125
Private	94	177	119	107	170	167	125
Goods-producing	9	-6	7	24	9	11	5
Mining and logging	0	0	0	4	-1	1	0
Construction	21	7	5	12	7	11	0
Manufacturing	-13	-13	2	8	3	-1	5
Motor veh.	-4	-2	-2	6	-1	-5	
Service-producing	85	183	111	83	161	156	120
Wholesale	6	8	1	7	-1	6	5
Retail	-5	5	18	-4	22	-2	5
Trans. & warehousing	3	18	14	18	3	29	11
Utilities	1	-1	1	1	1	-1	2
Information	-8	5	-2	0	-2	0	0
Financial	3	10	12	15	6	14	12
Professional & business services	-21	13	-6	15	3	17	10
Temp help	-21	-1	-4	-2	-3	4	
Education	10	2	1	8	-2	12	5
Health care, social assistance	65	79	66	57	77	58	55
Leisure & hospitality	29	37	-3	-34	38	24	10
Other services	3	7	10	0	17	-1	5
Government	39	33	14	-5	15	10	0
Federal	3	1	-5	-13	-4	-9	-20
State and local	37	31	19	8	19	19	20

Source: BLS, Morgan Stanley Research forecasts

Hours and earnings

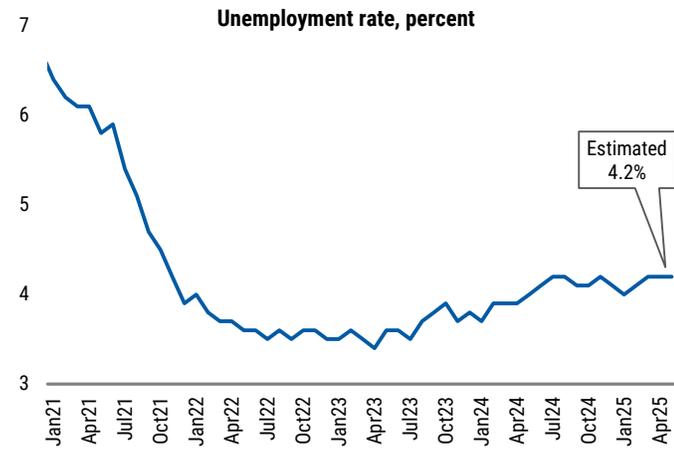
We expect the workweek unchanged from April's 34.3 hours. Average hourly earnings rise on trend 0.3% m/m but slow from 3.8% y/y to 3.7% y/y. Aggregate payroll incomes would be rising at a 5.5% pace in April-May versus 1Q—close to the pace of the last six months.

Unemployment Rate and Labor Force Participation

We forecast no change in the unemployment rate at 4.2%, up a tenth from the 1Q average but little changed from 2H 2024.

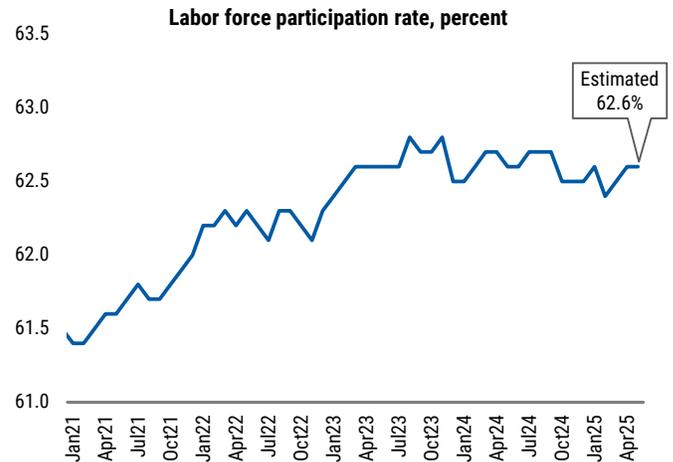
Low immigration makes it hard to push the unemployment rate higher. We continue to expect that immigration restriction limits labor force growth, putting downward pressure on the unemployment rate. There has been some evidence of that downward pressure. Last year's breakeven payroll pace was an estimated 210k per month. The breakeven pace slipped to about 170k year-to-date. In our [Immigration Tracker](#), we recently updated our estimates for the remainder of this year and next year. We revised down our expectations for immigration, labor force growth, and this year's breakeven, now expecting breakevens at 90k per month rather than 125k per month this year, and 80,000 next year.

Exhibit 8: We forecast the unemployment rate unchanged at 4.2%



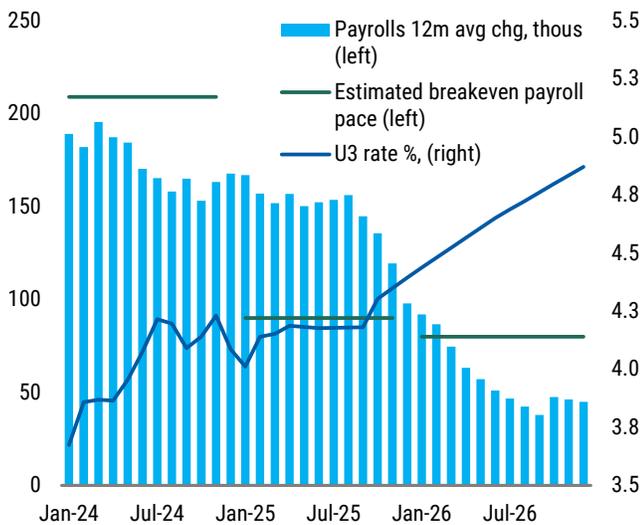
Source: Bureau of Labor Statistics, Morgan Stanley Research forecasts

Exhibit 9: We expect labor force participation unchanged at 62.5%



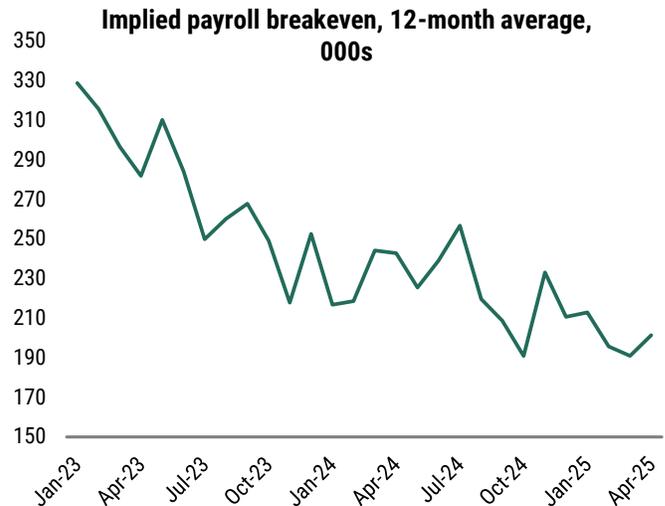
Source: Bureau of Labor Statistics, Morgan Stanley Research forecasts

Exhibit 10: Breakevens and our labor market forecasts



Source: BLS, Morgan Stanley Research

Exhibit 11: Estimated breakeven pace of payrolls



Source: BLS, Morgan Stanley Research

Risks

Downside: Uncertainty remains high. In business surveys, firms' capex and employment plans have been uneven, and their job openings have weakened. If firms follow through, slower hiring depresses employment growth more than we anticipate. The spillover from DOGE into federal contractors could also be larger than we anticipate.

Upside: We have allowed Easter timing to affect payroll estimates: +25k in April and -25k in May. This may not be so large a drag.

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