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US Economics | North America

Employment Report Preview: A Little Less Slow

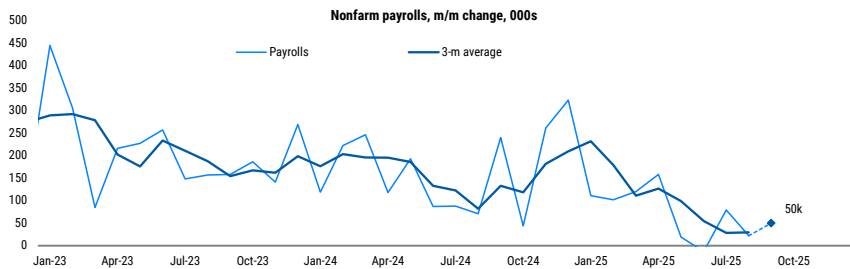
The jobs report will not be released if the government shuts down. Our 50k est for Aug. payrolls represents some stabilization in labor demand & the UE rate (4.3%). We expect average hourly earnings +0.3% and an unchanged workweek. Revisions likely tilt positive into the end of the year.

Exhibit 1: Employment forecast details

Employment Report: Forecasts & Recent History						
	Est. Sep-25	Consensus Sep-25	Aug-25	Actual		
				Jul-25	3MMA	Year-Ago
Change in nonfarm payrolls (thous.)	50	50	22	79	29	240
Private payrolls	50	50	38	77	29	208
Unemployment rate (%)	4.3	4.3	4.3	4.2	4.2	4.1
Labor force participation rate (%)	62.3	62.3	62.3	62.2	62.3	62.7
Average weekly hours	34.2	34.2	34.2	34.2	34.2	34.2
Average hourly earnings (%M)	0.3	0.3	0.3	0.3	0.3	0.3
%Y	3.7	3.8	3.7	3.9	3.8	3.9

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

Exhibit 2: We project payrolls rose 50k



Source: BLS, Morgan Stanley Research forecast

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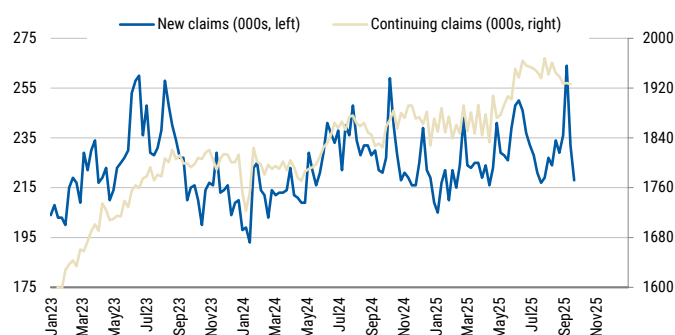
If the federal government shuts down, which looks increasingly likely, the employment report will not be released this Friday. Data releases from the BLS, BEA, and Census Bureau will be delayed: the employment report, CPI, retail sales, durables, GDP, among others. Jobless claims data also will be delayed.

Payrolls Forecast

We forecast headline and private payrolls rose 50k in September. For private payrolls, we expect no weaker than recent months, but barely any stronger. From May through August, private payrolls averaged +39k per month. For government payrolls, the single-month of large layoffs will be October payrolls (reported early November).

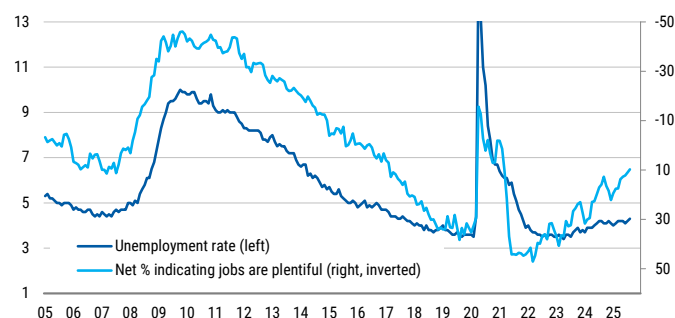
We believe that the slowdown in labor demand is still contained. Layoffs have remained low; it's hiring that has slowed. Looking at layoffs: new jobless claims remain very low and layoffs measured in the JOLTS report have risen only very modestly. Looking at hiring: the step-up in continuing jobless claims in April—even with some reversal recently—represents slower hiring out of unemployment. And the JOLTS hiring rate, though moving sideways, is very low and fell in August.

Exhibit 3: There's been noise in new and continuing claims—fraudulent applications, miscounts—but both are now lower than a month ago



Source: Department of Labor, Morgan Stanley Research

Exhibit 4: Households' labor market assessments continue to deteriorate gradually



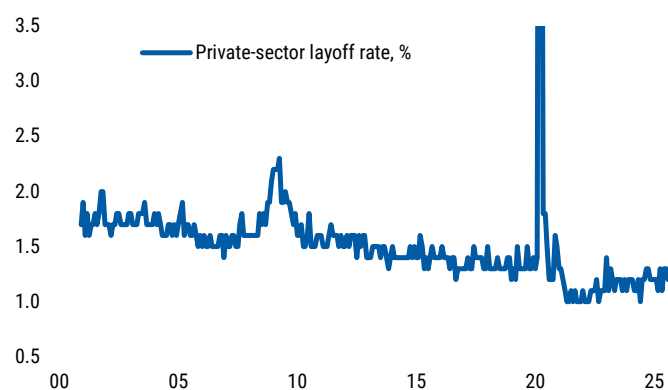
Conference Board, Morgan Stanley Research

Exhibit 5: The hires rate is a tenth below where it was a year ago



Source: BLS and Morgan Stanley Research

Exhibit 6: The layoff rate is unchanged from a year ago



Source: BLS and Morgan Stanley Research

The slowdown in hiring has been broadly spread across different industries. The diffusion index of private payroll growth, at 49.6, indicated slightly more industries shedding jobs in August than gaining them. Within manufacturing, it's softer at 45.8.

We expect narrow gains again in September: a slight pullback in goods-producing payrolls and, in services, continued strength in healthcare, some gains in consumer-facing retail and leisure industries, and little elsewhere.

Exhibit 7: Industry breakdown of payrolls, and our forecast

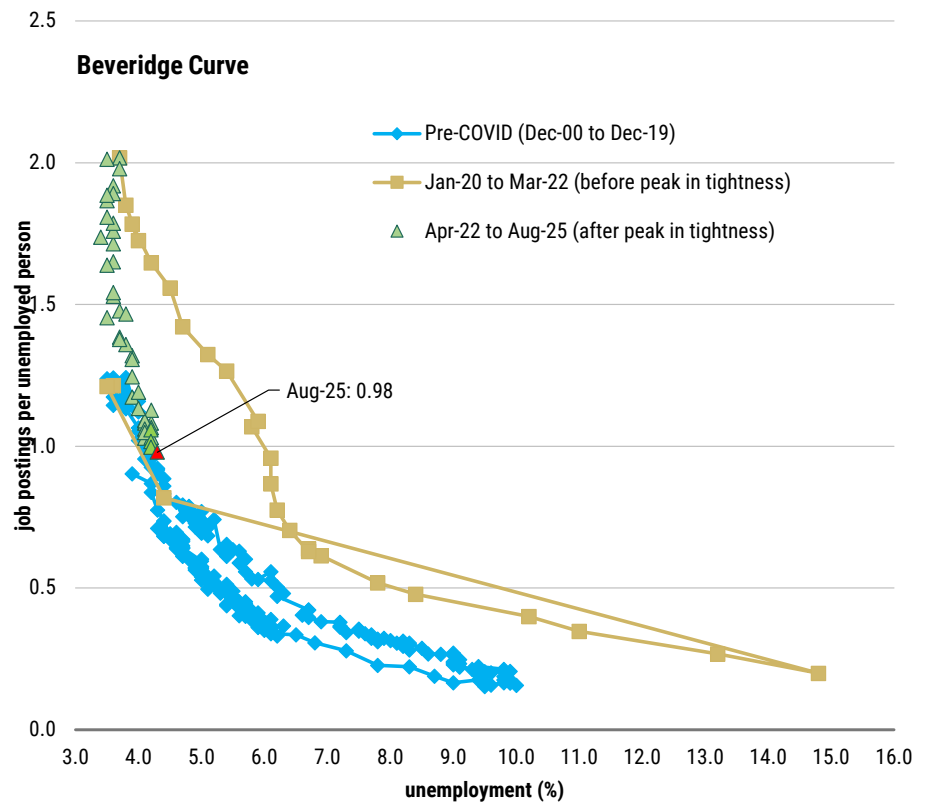
monthly change, 000s	Average monthly change							
	4Q24	1Q25	2Q25					
Nonfarm	209	111	55		-13	79	22	50
Private	177	100	58		-27	77	38	50
Goods-producing	-6	6	-11		-21	-8	-25	-10
Mining and logging	0	0	-1		-2	-5	-6	-5
Construction	7	5	0		-2	-1	-7	-5
Manufacturing	-13	1	-9		-17	-2	-12	0
Motor veh.	-2	-2	-1		-3	2	-7	
Service-producing	183	94	69		-6	85	63	60
Wholesale	8	-1	-3		-12	-8	-12	5
Retail	5	16	-5		-5	7	11	5
Trans. & warehousing	18	6	-1		4	6	4	5
Utilities	-1	1	1		0	1	-1	0
Information	5	-2	0		-3	-7	-5	-5
Financial	10	11	2		-6	9	-3	0
Professional & business services	13	-10	-7		-24	-10	-17	-5
Temp help	-1	-8	-3		-10	-10	-10	
Education	2	2	-1		-8	5	-1	0
Health care, social assistance	79	62	70		59	72	47	50
Leisure & hospitality	37	-1	13		-5	6	28	5
Other services	7	10	0		-6	5	12	0
Government	33	11	-4		14	2	-16	0
Federal	1	-7	-16		-9	-10	-15	-10
State and local	31	18	12		23	12	-1	10

Source: BLS, Morgan Stanley Research forecasts

As yet, the slowing in hiring has barely created more slack. Because immigration is limiting labor force growth, slower payroll gains represent slower labor input growth and slower payroll income growth, but by most measures they haven't created meaningful slack. The unemployment rate has barely risen over the past year, nor have wage gains slowed much.

But the deterioration in labor demand is threatening a higher unemployment rate. The ratio of job openings to unemployed has fallen enough to suggest the possibility of faster slackening in the labor market. The 0.98 job openings per unemployed that was reported for August puts the vacancy rate nearer to an inflection point: further decline often has been associated with a faster rise in the unemployment rate.

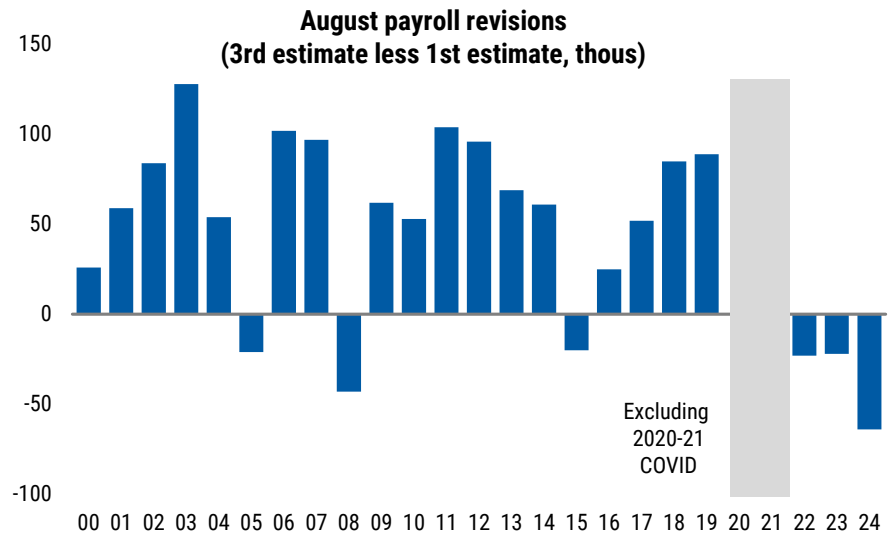
Exhibit 8: The Beveridge curve suggests that job openings are getting closer to the danger zone, where declines in job openings lead to faster rise in the unemployment rate



Source: BLS, Morgan Stanley Research

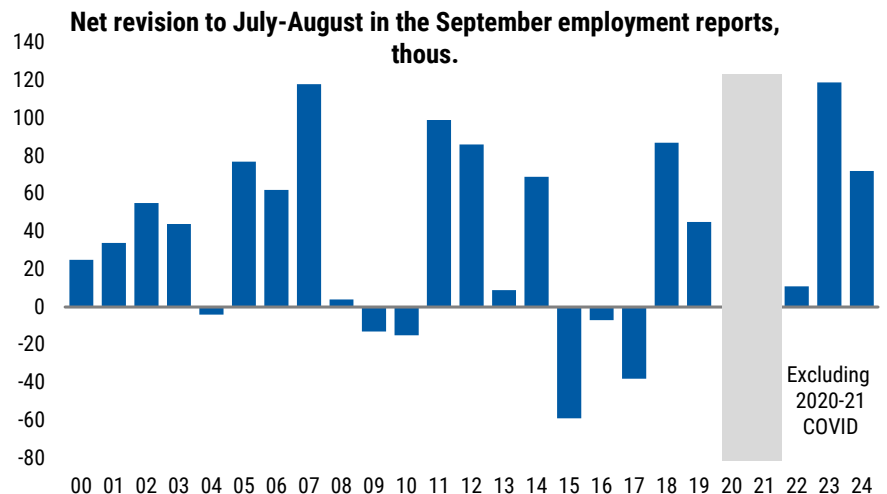
Revision risks. In [“Do August payrolls always get revised higher?”](#), we showed that prior to COVID, August payrolls tended to see upward revisions more often than other months but that this may have changed post-COVID. From 2022-24, the net revision to August payrolls over the course of the following two employment reports was negative. However, September employment reports like this one deliver revisions to both July and August, and the net of the second revision to July and the first revision to August has tended to tilt positive.

Exhibit 9: The pattern of upward revisions to August payrolls over the September and October payrolls reports may have changed post-COVID



Source: BLS, Haver Analytics, Morgan Stanley Research

Exhibit 10: But there is still some suggestion of net upward revision to July-August in September payrolls reports

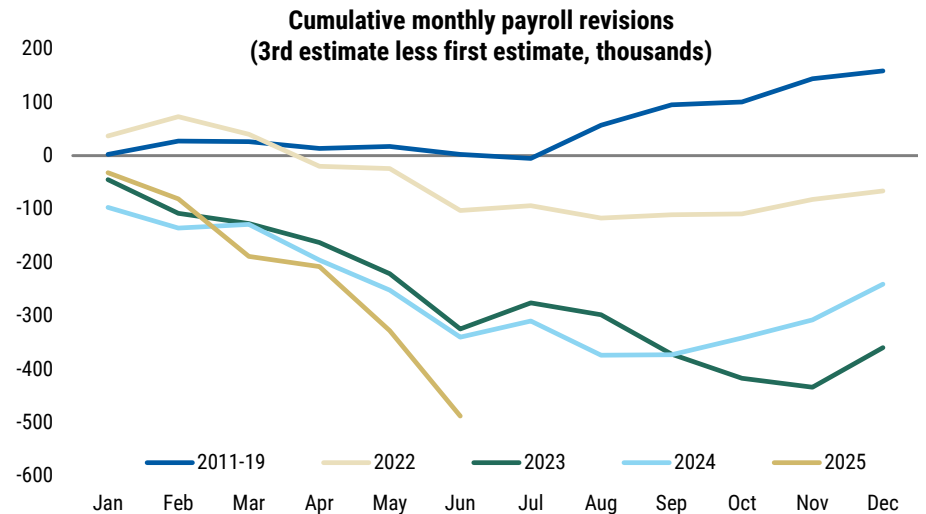


Source: BLS, Haver Analytics, Morgan Stanley Research

Revisions also are likely to tilt upwards from now through the end of the year. In [Exhibit 11](#), we cumulate monthly payroll revisions across the calendar year. For example, we add the two-month net revisions to February employment and add it to the two-month net revisions to January payrolls. We continue this throughout the year to arrive at the cumulative revisions to monthly payroll data in over that year. Revisions have been negative in recent years. However, the drag has come early in the year, and revisions have tended to turn positive late in the year.

We have a more complete assessment of these revision patterns in [“Do August payrolls always get revised higher?”](#).

Exhibit 11: Cumulative revisions to payrolls have been negative in recent years, though two-month revisions to monthly payroll data tend to turn positive late in the year



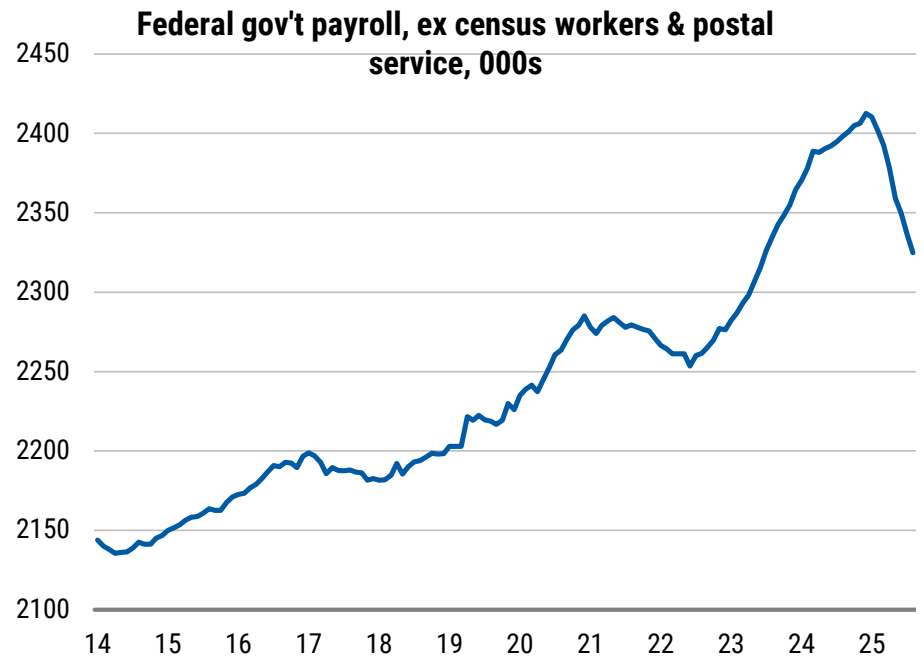
Source: BLS, Haver Analytics, Morgan Stanley Research

We expect no change in government payrolls in this report. Federal payrolls have fallen an average of 14k per month since February, which we expect continues. State government payrolls fell at about that same pace in August, well below trend, and we do not expect a repeat. Local government payrolls have been rising modestly, spread evenly across education and noneducation employment.

DOGE-related federal payroll cuts will depress October payrolls, scheduled to be published in early November. We don't expect cuts much beyond those who accepted deferred resignation agreements. In February and then in April, the federal government offered deferred resignation agreements to employees; an estimated 154k accepted them.

The administration asked Agencies to make plans for further employment cuts; a number of federal government officials indicated that they would be aiming for their payrolls to fall to 2019 levels by the end of the fiscal year. It looks to us that it will be accomplished with the deferred resignations. The level of federal government payrolls excluding the postal service was 2.328 million in August. It would fall to 2.174 million after the deferred resignations, below 2019's average of 2.224 million.

Exhibit 12: Federal government payrolls have already fallen quite a way toward 2019 levels. The deferred resignations would take them the rest of the way.



Source: BLS and Morgan Stanley Research

The decline in federal government employment has happened through slower hiring: 28k per month on average so far this year vs 39k per month in the first eight months of 2024. Total separations from federal government employment increased by 4k per month on average, mostly because of the layoffs of probationary employees. To our surprise, “other layoffs”—mostly retirements—increased by 3k per month on average—we had thought that those considering retirement would take the buyouts. In the other direction, quits slowed slightly, by 2k per month.

The immediate spillovers from federal employment to the rest of the economy probably have already happened. There’s been a 64k drop in (NSA) federal ex postal service payrolls since February, and the remaining 154k in deferred resignations are people who have not been working since either February or April even though they remained on payroll. So, some of the spillover into private payroll weakness is probably behind us.

Although we think that the October deferred resignations will get the federal government to the target employment level, there still is risk of further cuts: President Trump has threatened them if the government shuts down. In a shutdown, only those deemed essential are kept on, and there are some in the administration who would prefer to run the federal government on that skeleton crew.

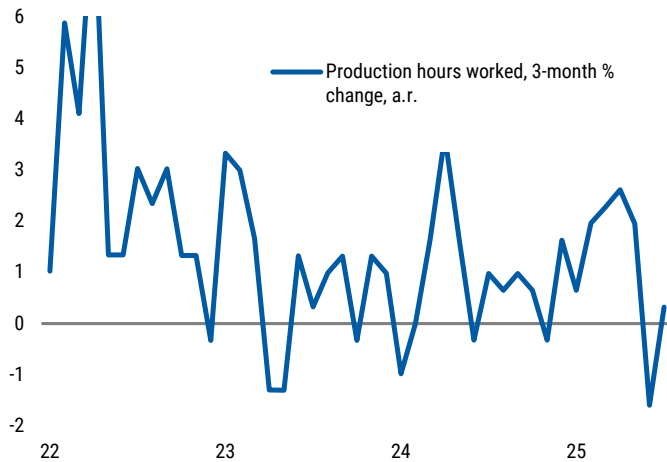
Hours and earnings

We expect the workweek, unchanged, and average hourly earnings, +0.3%, rise at about their recent pace. The 12-month pace of average hourly earnings stalls at 3.7%.

Production hours worked and aggregate payroll earnings have reaccelerated after their

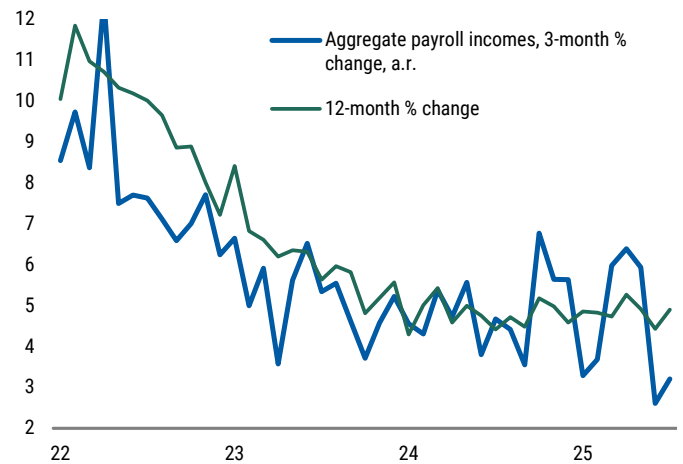
recent plunge, but growth through August remained depressed. They suggest that the early-summer falloff in labor demand may have been exaggerated in the data, but there is not enough rebound to calm doubts.

Exhibit 13: Some stabilization in production hours worked after a steep slowdown in 2Q



Source: Bureau of Labor Statistics and Morgan Stanley Research

Exhibit 14: Payroll income growth also slowed sharply



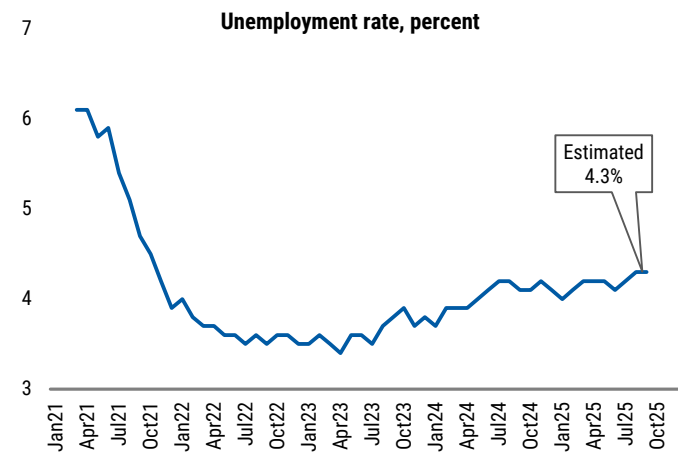
Source: Bureau of Labor Statistics and Morgan Stanley Research

Unemployment Rate and Labor Force Participation

The slowdown in payrolls appears to have created some new slack, but we do not expect further rise in the unemployment rate in September.

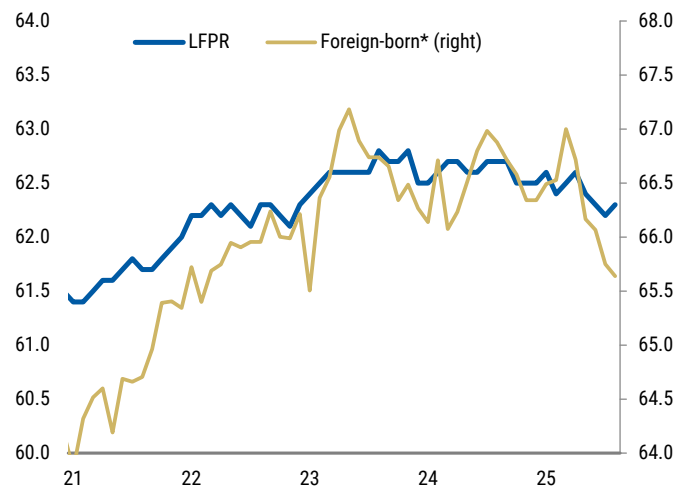
Labor force growth has slowed because of slower immigration. Labor demand was slowing in tandem, but it appears to have slowed more sharply this summer as the unemployment rate rose slightly. At the same time, downward pressure on the unemployment rate from labor force participation is increasing. The foreign-born participation rate has been falling since March.

Exhibit 15: We forecast the unemployment rate unchanged at 4.3%



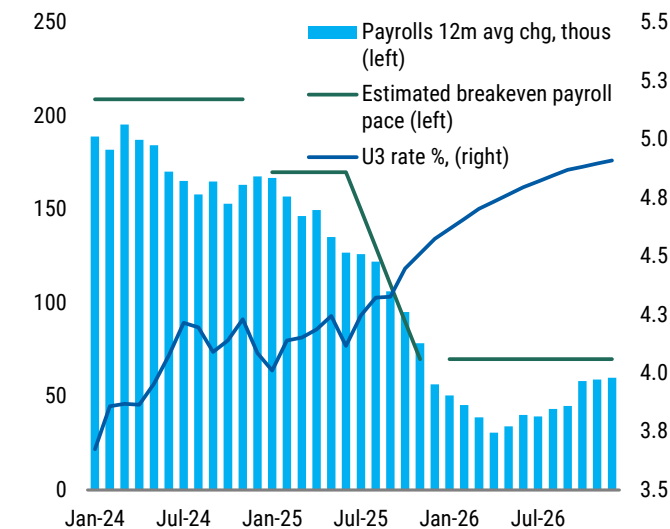
Source: Bureau of Labor Statistics, Morgan Stanley Research forecasts

Exhibit 16: We expect labor force participation unchanged, but immigration policy has been putting downward pressure on foreign-born participation since March



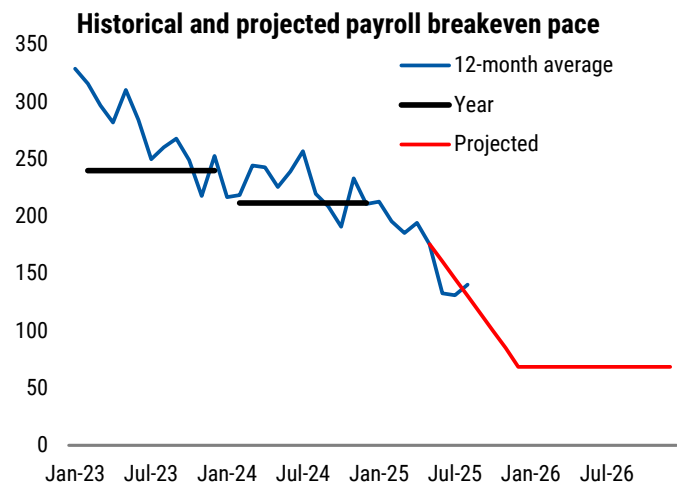
* Our seasonal adjustment.
Source: BLS, Morgan Stanley Research

Exhibit 17: Breakevens and our labor market forecasts



Source: BLS, Morgan Stanley Research

Exhibit 18: Breakevens have fallen at the pace we expect. By the end of the year, 70k per month in payrolls probably is consistent with flat UE rate.



Source: BLS, Morgan Stanley Research

Consensus, and Risks

The major risk is that the report is delayed. That looks increasingly likely each day. But the federal government is unlikely to remain closed all the way through the next FOMC meeting. If it did, the assumed drag from the federal shutdown probably keeps the Fed on

track for cuts.

There is upside risk from the pattern of revisions although for us the timing of those positive revisions—now, or through the end of the year—is uncertain.

Upside risks: A payroll report strong enough to unwind the appearance of sharp weakening from recent reports could change the chances of a rate cut at the upcoming FOMC meeting. A strong enough rise, combined with revisions, to put the three-month average at about 100k per month could tilt the FOMC away from its dovish scenarios.

Downside risks: Payrolls at -50k, spread across government, manufacturing, and services would exacerbate Fed fears and increase the chances of a 50bp cut. The unemployment rate probably rises to 4.4% or 4.5%.

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