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US Economics | North America

Employment Report Preview: Slower job growth

June payrolls slow to 210k because of softening demand for and supply of labor. We forecast no change in the unemployment rate at 4.0%; if weaker demand dominates, unemployment instead rises to 4.1%; if weaker supply, it could fall to 3.9%. AHE rises 0.3%M, slowing to 3.9%Y.

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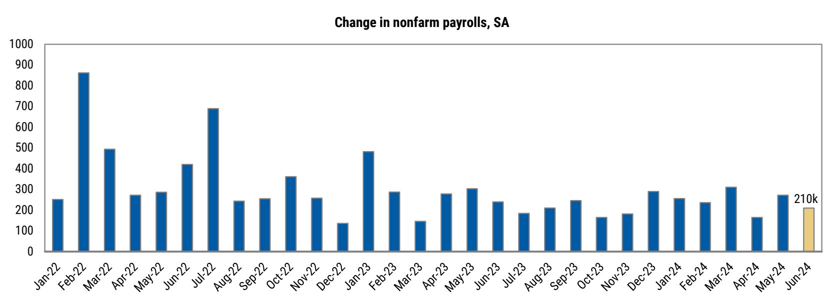
Exhibit 1: June employment forecast details

Employment Report: Forecasts & Recent History	Est. Jun-24	Consensus Jun-24	Actual May-24	Apr-24	3MMA	Year-Ago
Change in nonfarm payrolls (thous.)	210	180	272	165	249	240
Private payrolls	160	155	229	158	206	185
Unemployment rate (%)	4.0	3.9	4.0	3.9	3.8	3.6
Labor force participation rate (%)	62.6		62.5	62.7	62.6	62.6
Average weekly hours	34.3	34.3	34.3	34.3	34.3	34.4
Average hourly earnings (%M)	0.3	0.3	0.4	0.2	0.3	0.5
%Y	3.9		4.1	4.0	4.1	4.7

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

Exhibit 2: We project payrolls slowed to 210k in June from their 248k per month average year to date



Source: BLS, Morgan Stanley Research forecasts

June Employment

Our forecast that payrolls slow to 210k in June (and private payrolls to 165k) reflects an interruption to labor supply and some softening in labor demand. Limiting labor supply, immigration flows slowed in March and remained slower in April and May after a year of strength. Hinting at softer demand, openings have fallen and new jobless claims have risen although continuing claims have not increased as convincingly.

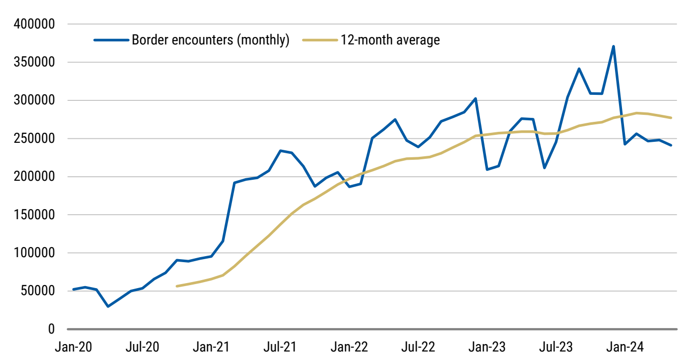
Immigration began slowing in March. In the six months through February, Customs and Border Protection had reported "encounters" with unauthorized immigrants between ports of entry were rising 10-20% from a year earlier. But in March, April, and May, encounters were below year-earlier levels (Exhibit 3). It appears that Mexico has stemmed the flow of migrants into the US, reportedly busing migrants away from the US border. We estimate a three month lag between the unauthorized immigration (border encounters) and payroll employment. The March decline in immigration should begin to affect construction and leisure payrolls in June or soon after.

We have been expecting some slowing in labor demand because of the downtrend in job openings (Exhibit 4). New and continuing job claims also suggest more layoffs and slower reemployment (Exhibit 5).

A shock to supply and a shock to demand have opposite effects on the unemployment rate: lower supply tightens the labor market and decreases the unemployment rate. Lower demand eases the labor market and raises the unemployment rate. Similarly, in households' labor market assessments, for the same pace of employment growth, lower labor supply would tend to improve household labor market assessments while lower demand would tend to depress them. In June, labor market assessments improved slightly from strong levels (Exhibit 6). If payrolls did slow as we expect, tighter supply probably contributed.

This is an interruption of the pattern of the past year and a half, when increased labor supply allowed faster payroll growth and a slackening labor market at the same time.

Exhibit 3: Immigration no longer rising as fast as it was

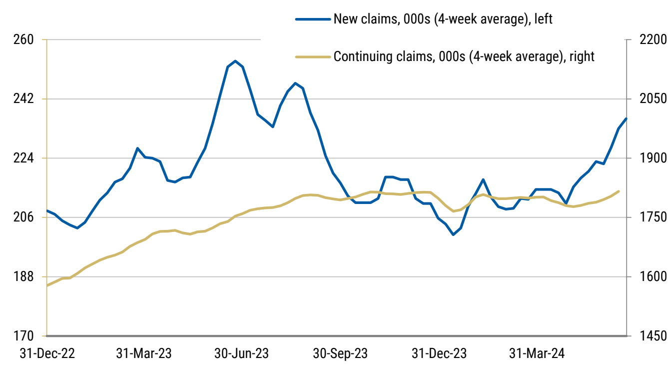


Source: Customs and Border Protection, Morgan Stanley Research

Exhibit 4: The vacancy rate is slipping again

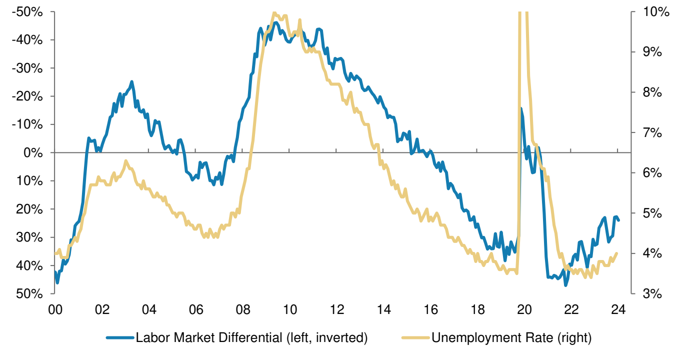
Source: BLS, Morgan Stanley Research

Exhibit 5: New claims have risen notably, continuing claims also up



Source: Department of Labor, Morgan Stanley Research

Exhibit 6: Households' labor market assessments improved in June from strong levels



Source: BLS, Conference Board, Morgan Stanley Research

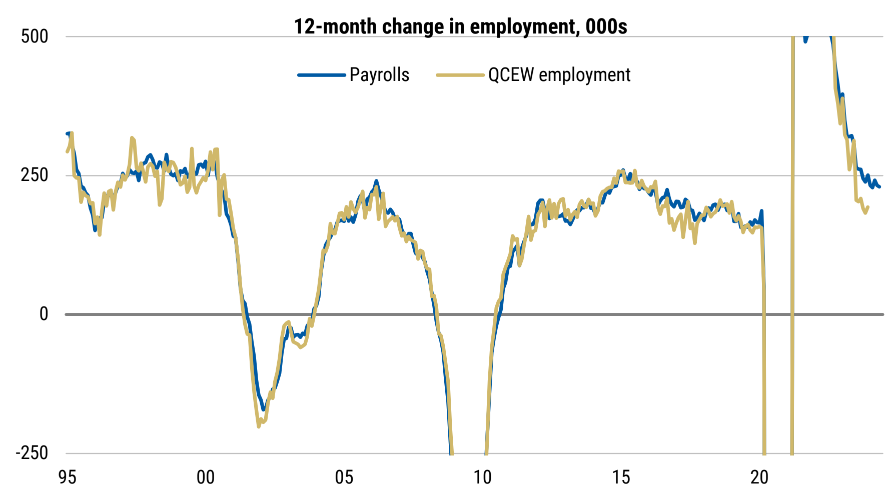
Are payrolls overstating employment growth?

We have heard a number of questions about the QCEW (Quarterly Census of Employment and Wages) because, through 4Q, it shows slower employment growth than does the payroll data. The QCEW shows 194k per month in payroll increase in the 12 months through December, versus 251k in payrolls (Exhibit 7). The discrepancy is important: the QCEW is the basis of the annual benchmark revisions to payrolls. The result: payrolls are on track to be revised downward – but we believe that's not because payrolls are overcounting but because QCEW is undercounting.

The QCEW is a count of employment based on administrative filings with the unemployment insurance system. Because it's based on UI records, it likely misses counting those who are not authorized to work: if one's not authorized to work, one also is not eligible for unemployment insurance benefits. In contrast, the payroll survey asks that employees be counted regardless of legal status.

Our note: Friday Finish – US Economics: Are Payrolls Overstated?

Exhibit 7: Employment growth is slower in the QCEW estimates than in payrolls



Source: Bureau of Labor Statistics, Morgan Stanley Research

By Industry

We expect slower employment growth in construction and leisure & hospitality because of restriction in labor supply. With the rise in claims, we also expect some softening in professional and business services employment. We also continue to wait for slowing in retail and transport; they've remained remarkably resilient even while retail sales have softened this year and job openings have come down. We also expect slightly slower education payrolls in June.

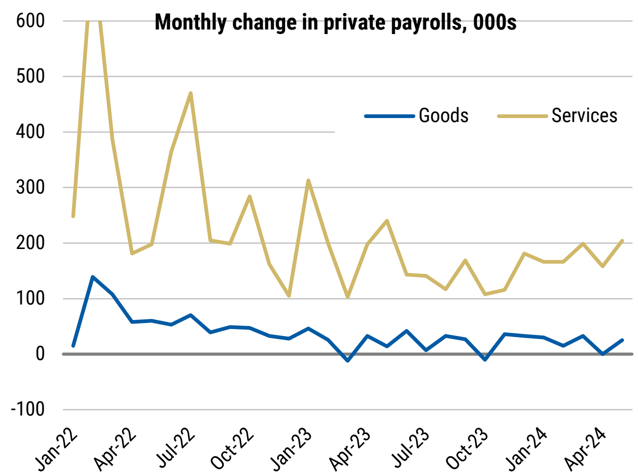
Exhibit 8 provides a sector breakdown of job gains through May and our June forecasts.

Exhibit 8: Sectoral breakdown of payroll gains and our June forecast

	Average monthly change								
monthly change, 000s	**2Q 23**	**3Q 23**	**4Q 23**	**1Q24**		**Mar**	**Apr**	**May**	**Jun est**
Nonfarm	**274**	**213**	**212**	**267**		**310**	**165**	**272**	**210**
Private	223	165	155	203		232	158	229	**165**
Goods-producing	30	22	20	26		33	0	25	**15**
Mining and logging	2	1	-1	0		2	-6	-4	0
Construction	23	18	18	29		37	0	21	10
Manufacturing	4	3	2	-3		-6	6	8	5
Motor veh.	6	3	3	1		5	0	3	
Service-producing	194	142	135	177		199	158	204	**150**
Wholesale	3	10	9	0		10	1	3	4
Retail	5	6	-3	20		19	23	13	10
Trans. & warehousing	5	-10	-12	11		5	20	11	5
Utilities	1	1	2	1		-1	-1	1	2
Information	-4	-12	1	2		2	-5	0	2
Financial	17	7	3	-2		4	-2	10	2
Professional & business services	29	-6	6	24		17	-1	33	15
Temp help	-17	-23	-19	-3		-1	-12	-14	
Education	10	1	5	5		-4	6	2	5
Health care, social assistance	72	94	85	81		80	101	84	80
Leisure & hospitality	47	40	36	26		54	12	42	15
Other services	9	11	3	11		12	5	6	10
Government	50	49	58	64		78	7	43	**45**
Federal	7	8	5	11		12	2	4	
State and local	44	40	52	54		66	5	39	

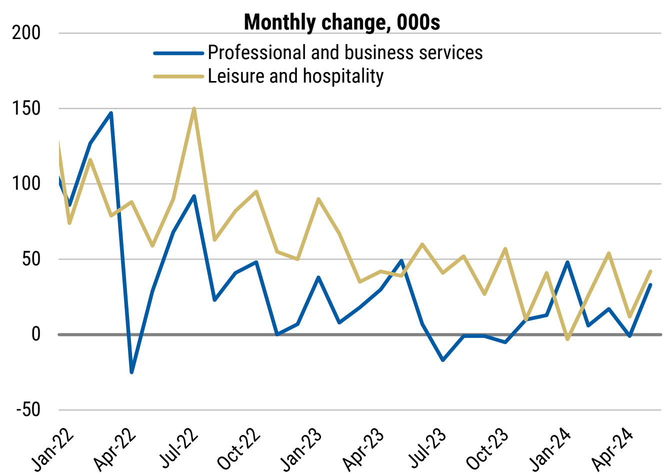
Source: BLS, Morgan Stanley Research forecasts

Exhibit 9: Services payrolls reaccelerated throughout 1Q. A slight reversal in April was followed by rebound in May.



Source: BLS, Morgan Stanley Research

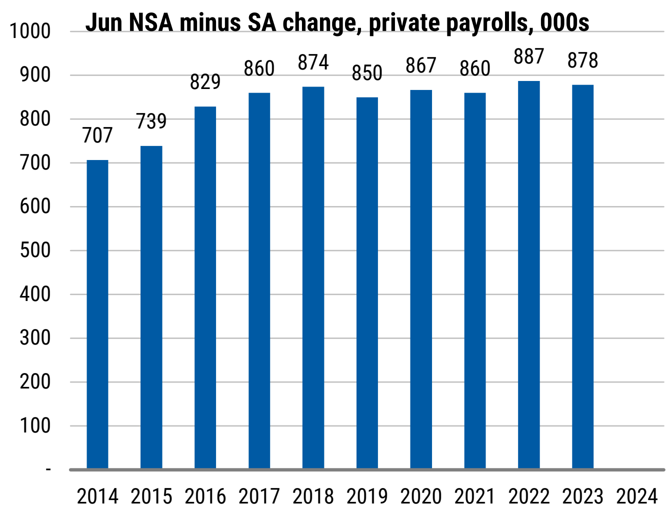
Exhibit 10: Reacceleration in leisure payrolls and in professional & business services payrolls in May



Source: Bureau of Labor Statistics, Morgan Stanley Research

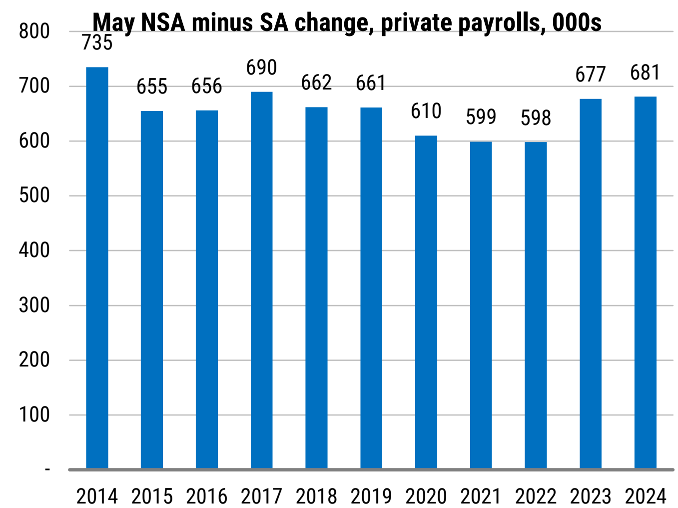
We do not expect a distortion from seasonal factors. NSA private payrolls tend to rise in May and June. Both last June and this May, seasonal factors subtracted about what they had pre-Covid (Exhibit 11 , Exhibit 12). There was no obvious distortion to the aggregate seasonal factor. That said, some particular industries may pose risk. The seasonal adjustments for construction and leisure & hospitality assumes large increases in employment in June—a high hurdle. Local government noneducational payrolls also tend to rise sharply, but we don't expect a change from their recent strong trend. (Exhibit 13). We have built in slightly softer education payrolls to our forecast.

Exhibit 11: Payrolls tend to rise in June. Last year, seasonal factors subtracted about what they had pre-Covid.



Source: BLS, Morgan Stanley Research

Exhibit 12: Payrolls tend to rise in May. Last month, seasonal factors subtracted about what they had pre-Covid.



Source: BLS, Morgan Stanley Research

Exhibit 13:

Payrolls tend to rise in most industries in May. Leisure & hospitality and construction are the biggest movers.

	June	May hurdle	May NSA	May SA
Leisure & Hospitality	480	402	444	42
Local Government, excluding Education	184	81	105	24
Construction	137	141	162	21
Manufacturing	98	25	33	8
Financial Activities	79	16	26	10
Professional & Business Services	77	47	80	33
Retail Trade	76	71	84	13
Other Services	60	31	37	6
Information	39	-1	-1	0
Health Care & Social Assistance	33	17	101	84
Wholesale Trade	27	23	26	3
State Government, excluding Education	11	9	14	5
Federal	7	6	10	4
Mining & Logging	5	4	0	-4
Utilities	3	1	2	1
Transportation & Warehousing	-24	36	46	11
Educational Services	-234	-132	-130	2
State Government Education	-323	-141	-141	-1
Local Government Education	-357	10	19	10
Total	**451**	**645**	**917**	**271**

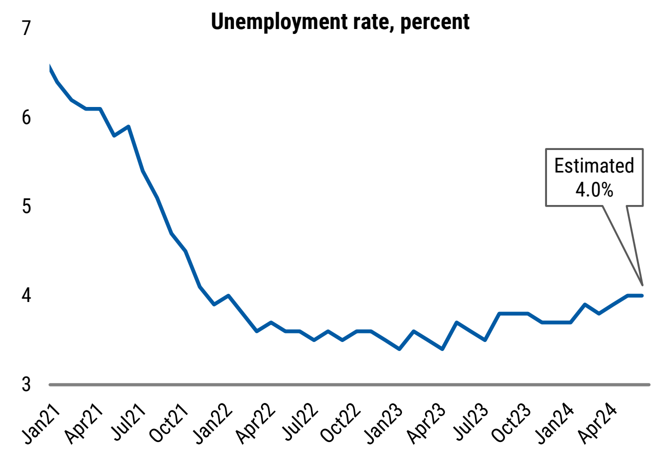
Source: BLS, Morgan Stanley Research

The 0.3% rise in average hourly earnings that we forecast would lower the 12-month pace to 3.9% from 4.1%. The pace is its slowest since early pandemic, but 3.9% is still fairly rapid. There is some upside risk as unauthorized immigrants have been filling lower-wage jobs and a compositional shift in employment away from lower-paid industries would eventually be reflected in faster average hourly earnings growth.

The unemployment rate is probably unchanged at 4.0%. We're assuming slightly stronger demand than supply effects in our slower employment forecast. But if the supply interruption is larger than we imagine, the labor market will tighten, and the unemployment rate can fall despite slower employment growth. If the demand pullback is more important, the labor market is easing and the unemployment rate is likely to show more of a rise than we estimate. We expect the labor force participation rate rises to 62.6% (Exhibit 14 & Exhibit 15).

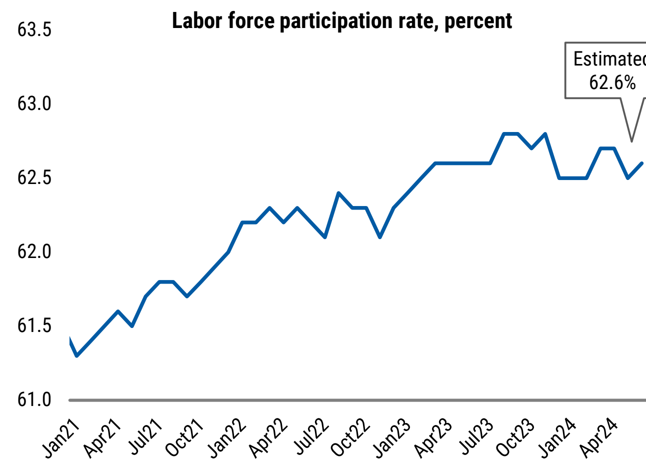
Through May, the unemployment rate had risen about ⅓ point from 12-months earlier despite rapid payroll growth of 232k per month on average. Labor force growth has been large enough to absorb rapid employment growth. With fast immigration, we estimate that payroll increase of about 265k per month has been consistent with an unchanged unemployment rate. See Exhibit 16 .

Exhibit 14: We forecast the unemployment rate stalls at 3.9%



Source: Bureau of Labor Statistics, Morgan Stanley Research forecasts

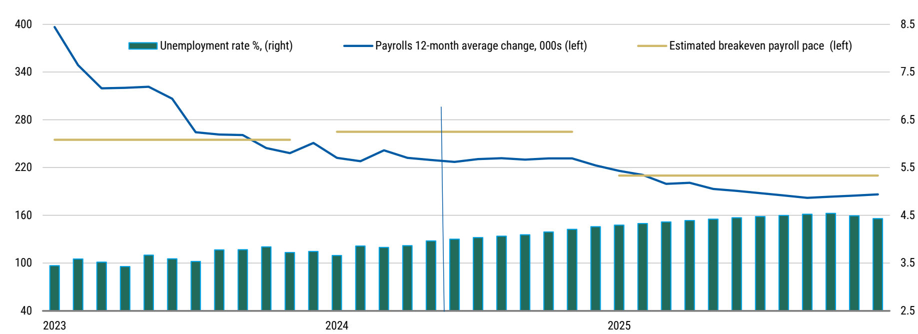
Exhibit 15: We expect labor force participation remains at 62.7%



Source: Bureau of Labor Statistics, Morgan Stanley Research forecasts

Exhibit 16:

We estimate that payrolls are running somewhat below the breakeven pace that holds the unemployment rate unchanged. We expect the unemployment rate to continue to inch up.



Source: BLS, Morgan Stanley Research

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