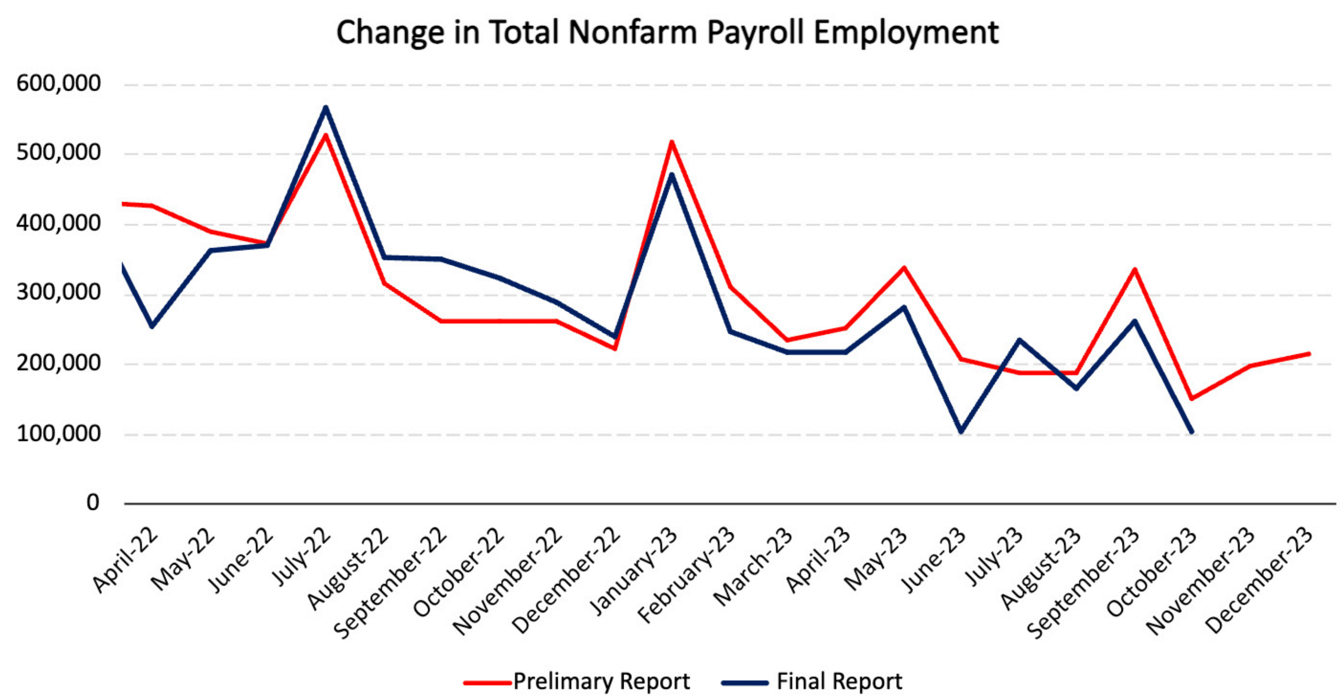
January 2024 Sunwest Bank Newsletter

- *9 of the first 10 employment reports in 2023 have been overstated in the preliminary release and subsequently revised lower by an average of 14.4%.*
- *Of the new jobs created since mid-2020, 2.8 million have been from people adding a second or third job.*
- *The unemployment rate remained unchanged last month, despite a reduction in overall jobs because labor market participation declined.*
- *The labor markets are much weaker than they appear on the surface and could continue weakening as higher wages and operating costs from inflation are causing small and large employers to perform layoffs in order to maintain profitability margins.*

The Bureau of Labor Statistics (BLS) releases its monthly jobs report on the first Friday of each month, which details the national unemployment rate, new jobs created and other key employment statistics. This report is widely anticipated by the financial markets and economists as they try to forecast the overall health of the US economy and corresponding Federal Reserve policy. Market participants and the media generally focus on two key data points, the number of new jobs created and the headline unemployment rate. However, understanding the many underlying statistics and their trends is very important in understanding the actual health of the labor market.

The first detail to understand is how the data is assembled for the monthly jobs report. This data is not based on actual counts but based on two large surveys; the Household Survey which surveys 60,000 households and the Establishment Survey which surveys 142,000 business and government agencies. The Household survey is what determines the unemployment rate and today reported an unemployment rate of 3.7% for December. The Establishment Survey is what determines the widely reported monthly job creation number and today reported 216,000 jobs for December.

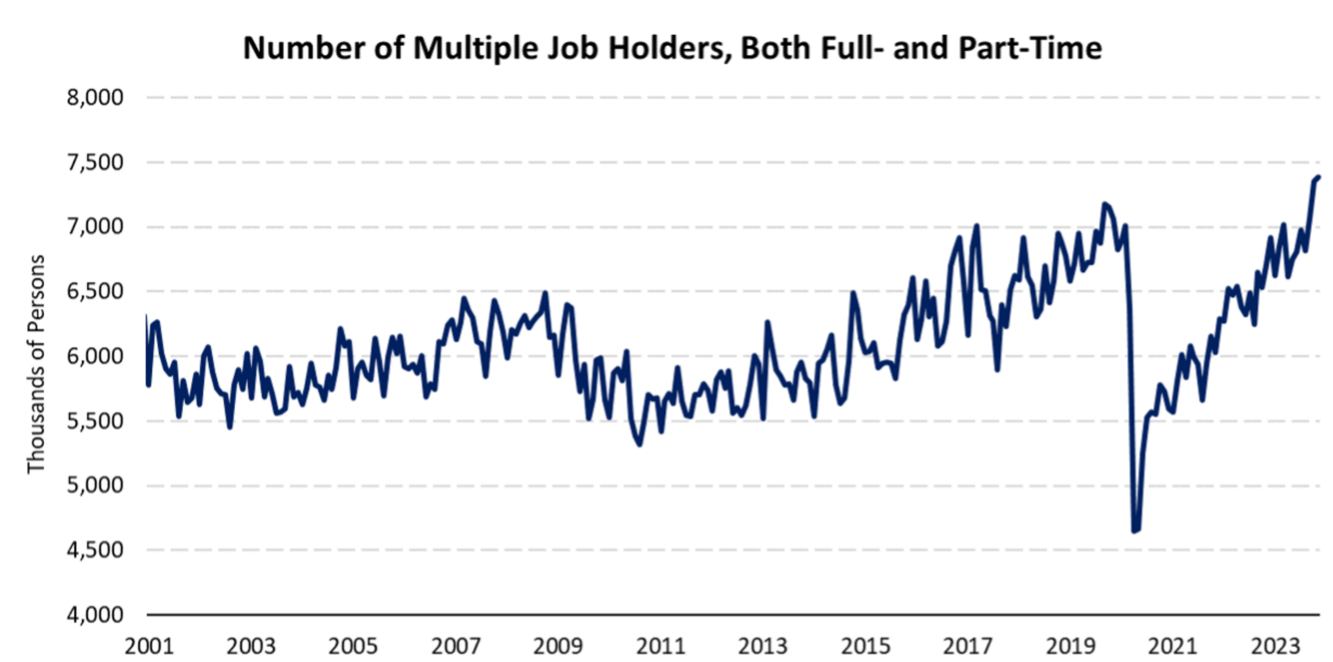
Since this data is compiled from surveys, the jobs numbers are consistently revised in subsequent monthly reports. The most significant revisions come from the Establishment Survey because of how the data is accumulated and its greater margin for error. Throughout 2023 and again today, the initial monthly job reports have largely outperformed expectations, and this labor market strength has been widely reported by financial media. However, in subsequent months following these initial reports, the prior months large job growth numbers have been consistently revised lower.



As you can see from the Total Nonfarm Payroll Employment graph above, nearly every employment report over the course of 2023 has been overstated in the preliminary release, only to be significantly revised lower by an average of 14.4%. It is particularly strange to have nearly an entire year of downward revisions because if you look back at every month from 2019-2022, the report is evenly split between upward and downward revisions.

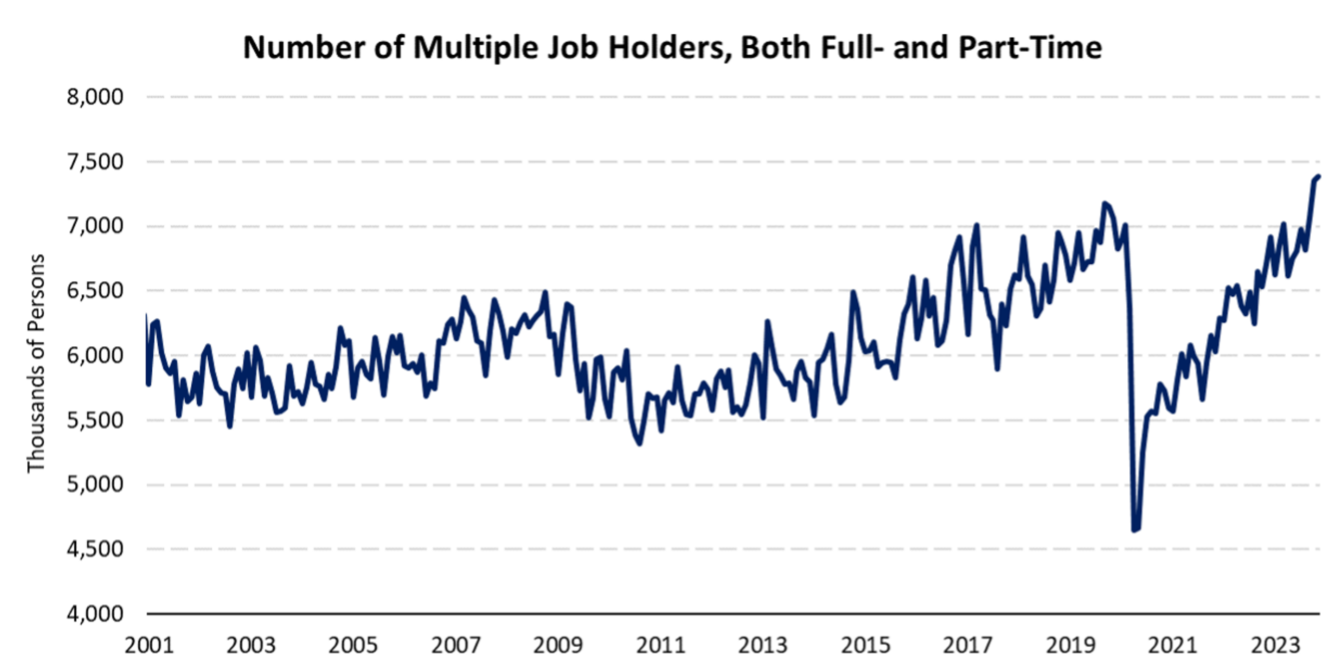
"There are three kinds of lies: lies, damn lies, and statistics." – Mark Twain

Another potentially misleading component of employment data in both the Household and Establishment Surveys is that nearly 2.8 million of the new jobs created since mid-2020 have been from people who already have a job and are adding a second or third job. This is a combination of our employment surveys not capturing the new gig economy accurately and Americans struggling with the higher cost of groceries, gas, housing, healthcare and other living essentials.



The overstated headline employment numbers are creating a false sense of confidence in the labor markets and misconceptions about what is happening in the underlying economy. For instance, the December Household report released today showed a 683,000 reduction in jobs month-over-month, but a corresponding 676,000 reduction in the overall labor force, leaving the unemployment rate unchanged at 3.7% (the unemployment rate is calculated by dividing reported unemployed individuals into the total number of people in the labor force, not the overall population). However, there are 683,000 less jobs being reported in the economy per the Household Survey. This is important because consumer spending is the primary driver of the US economy and consumer spending is highly correlated to stable employment markets. Further, employment data is a lagging economic indicator so when it declines, we are typically already in economic contraction. Many investors, particularly in the public markets, believe that the economy is in the process of a soft landing, but we believe there could be far greater trouble under the surface.

Over the past year, major companies have performed layoffs to reduce costs and protect their profit margins. These companies include Alphabet, BlackRock, IBM, Microsoft, Salesforce, FedEx, Disney, Dell, Boeing, Warner Music, Meta, Amazon, 3M, McDonalds, Lyft, Best Buy, Goldman Sachs, Ford Motor, CVS Health, T-Mobile, Charles Schwab, Citigroup, Spotify, Hasbro, General Motors, and Ernst & Young, to provide a broad list. This is also happening at small and medium size businesses throughout the country, as rising operating costs and wages are forcing employers to become more efficient to maintain profit margins. With layoffs typically paused during the holiday season, we anticipate an uptick in job losses as we enter the new year.



The labor markets are currently more fragile than the headline employment statistics or the broader media portrays. The consistent downward revisions show that the monthly new job creation numbers that are widely circulated are overstated. There is also limited quantification of the quality of these jobs and their earnings power, which we demonstrated with the increase in part-time jobs. On the surface, the employment markets are reported as being robust, but the underlying data tells a story of lesser job creation and lower quality jobs juxtaposed with ongoing layoffs from big corporations and the anticipation of more in 2024. These underlying statistics are telling a different story than the headline number and we highly suggest reviewing this underlying data each month when the jobs report is released.

