May employment preview: another step down

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- **We expect nonfarm payrolls to rise by +115k in May, a second consecutive step down compared to +185k in March and +177k in April. Despite the slowdown, however, our forecast would actually see the three-month moving average edging up to +159k compared to +155k last month, remaining at a solid level given that trend employment growth has likely fallen due to changes in immigration policy.**
- **Our forecast is below the latest consensus of +130k, with weaker prints for some employment metrics such as ADP contributing to this view, even if we acknowledge that ADP has not been a great signal for NFP. However, a very low layoffs rate that continues to suggest a low-firing environment keeps our expectation from dipping lower.**
- **With job gains expected to hold up okay for the time being, we look for the unemployment rate to hold steady at 4.2% for a third straight month. However, we would note that household survey employment has been more volatile than NFP, and an unexpected swing could tip the rate in either direction with last month's unrounded number at 4.19%.**
- **That said, we do anticipate some additional slowdown going forward and think the coming months could cool a bit further compared to May, in line with our view that the economy may be set for a soft patch around mid-year due to policy sequencing. In our base case, this cooling is relatively modest, but still sees the unemployment rate hitting 4.5%, and we think risks are tilted to the upside.**
- **We look for average hourly earnings to rise 0.3% MoM, with the YoY rate ticking down to 3.7% from 3.8%. Wage growth is well down from the peak but has stalled a bit above pre-Covid levels, and we expect this to remain the case. The Fed has not been overly concerned, however, and should continue to express the view that the labour market is not a major source of inflationary pressure at the moment.**
- **Overall, the Fed seems comfortable with the current state of the labour market, and a report in line with expectations would suggest little urgency to cut again. A sharp downside surprise could add some urgency, though we think that a cut is still unlikely to materialise before Q325, and continue to expect that sticky inflation may prevent the Fed from easing as aggressively as the market expects, even if the labour market cools further.**

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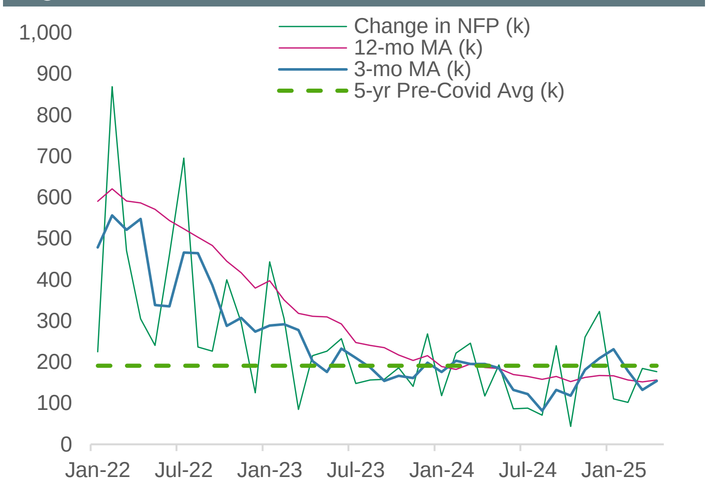
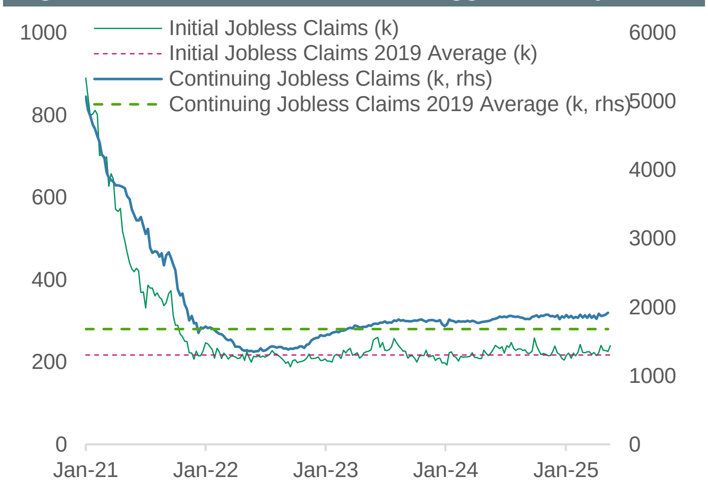
Fig 1. NFP momentum has stabilised in recent months



Source: Bloomberg, Crédit Agricole CIB

Fig 2. Jobless claims continue to suggest low layoffs

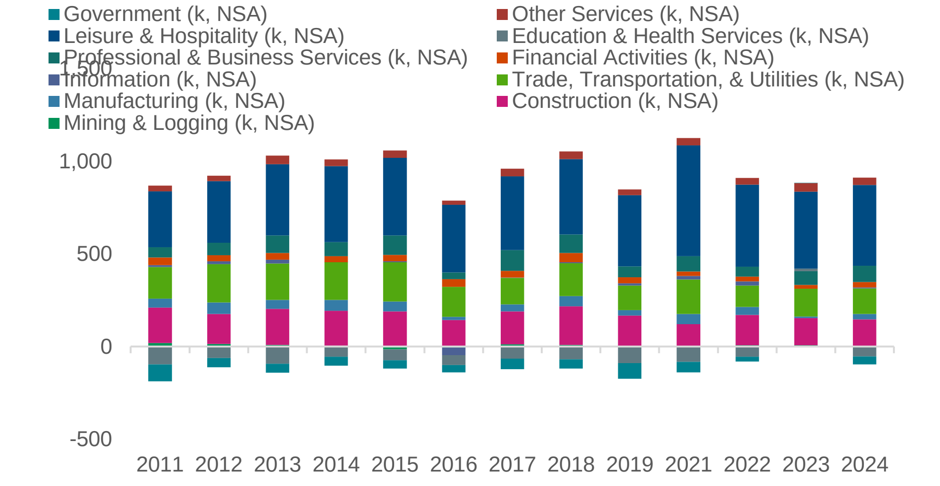


Source: Bloomberg, Crédit Agricole CIB

We expect nonfarm payrolls to rise by +115k in May, a second consecutive step down compared to +185k in March and +177k in April. Our forecast is below the latest consensus of +130k, with the range of forecasts submitted to BBG spanning +75k to +190k.

If our forecast is on track, it would actually result in the three-month moving average edging up to +159k compared to +155k last month, despite the projected slowdown on the month. This measure has shown signs of stabilising through early 2025, steadily increasing to +232k in January after dipping as low as +82k last August (see Figure 1). While recent months have moved down from there, a pace in the +160k range would still be a solid one given that trend employment has likely moved back down towards +100k, or even a bit below, due to changes in immigration policy.

Fig 3. May job gains by sector: leisure & hospitality typically leads



Source: Bloomberg, Crédit Agricole CIB; note: we have omitted 2020 as the recovery from Covid lockdowns skews the data

Contributing to our below-consensus forecast for May is the fact that a number of employment-related metrics have come in on the softer side. These include an ADP jobs report that showed gains of only +37k, even if we acknowledge that ADP has not always provided a great signal for NFP, and some increase in continuing jobless claims in recent weeks.

We would also highlight the typical seasonal pattern, where leisure & hospitality tends to lead non-seasonally adjusted job gains in May (see Figure 3). In fact, leisure & hospitality has typically provided somewhere between 45-55% of total NSA job gains in May over the past few years, indicating that this sector plays a key role on the month. While we admit that this is somewhat anecdotal, we see some risk that leisure & hospitality could be a bit weaker than usual this May given reports of lower travel demand due to the fact that some foreigners have been staying away from the US, helping to shade our forecast below consensus.

However, we are not taking the forecast too low as other employment indicators suggest the labour market remains in a decent spot still, even if it has slowed. These include initial jobless claims that remain very low, despite some week-to-week choppiness (see Figure 2), and a subdued layoffs rate that combine to indicate that we are still in a low-firing environment for now.

As a quick aside, we would note that the Supreme Court's recent ruling allowing the Trump administration to revoke Temporary Protected Status from Venezuelans could have some impact moving forward, as it could mean removing work authorisation for many. However, this will not materialise in May as the Court's ruling arrived closer to late May, or after the reference period for the May jobs report. We do not have a strong view at the moment in terms of quantifying the potential impact, though we plan to try and dig into this a bit more ahead of the release of the June report.

With job gains expected to hold up okay for the time being, we look for the unemployment rate to hold steady at 4.2% for a third straight month.

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However, we would note that household survey employment has been more volatile than NFP (see Figure 4), and an unexpected swing could tip the unemployment rate in either direction with last month's unrounded number at 4.19%.

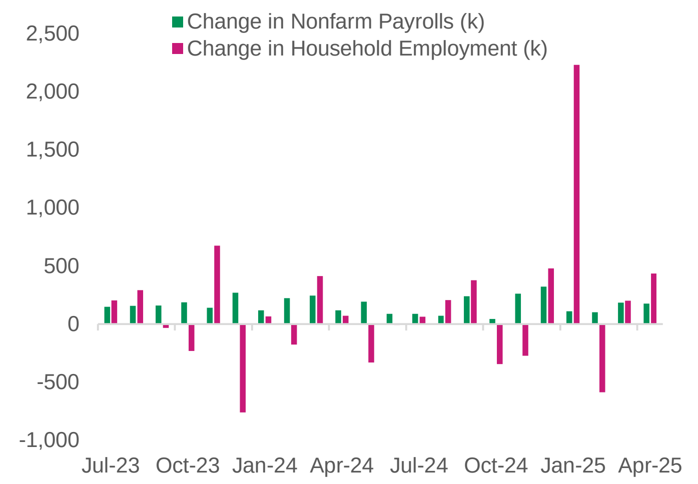
The unemployment rate is up from the cycle low of 3.4%, but has been fairly steady in hovering in the low-4% range in recent months. **This means that the Sahm Rule recession signal is no longer being triggered, after having done so for three months from last July through September.**

Sticking within the household survey, we would also keep an eye on the series showing those working part time for economic reasons, which jumped in February, leading to an uptick in the U6 underemployment rate. This series covers those who would prefer full-time work but were unable to find it, and thus a surge would be a sign of labour market cooling.

Despite the February jump, March and April provided a bit of relief in showing consecutive declines in the number working part time for economic reasons that resulted in the U6 edging down to 7.8% from 8.0%. However, the U6 is still up from 7.5% at the end of last year, so any renewed increase in the coming months would not be a great sign.

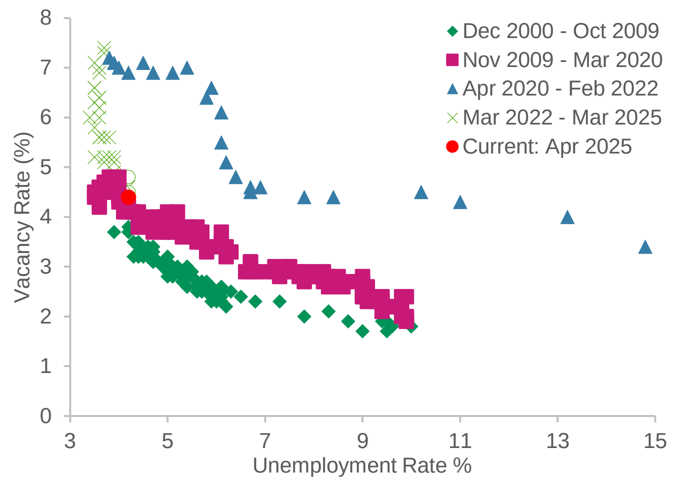
Elsewhere, we look for average hourly earnings to rise 0.3% MoM in May, stepping slightly up from 0.2% MoM in April, though this would result in the YoY rate ticking down to 3.7% from 3.8%. Wage growth is well down from the peak but has stalled a bit above pre-Covid levels in recent months, and we think this trend could persist given the likely addition of headwinds to labour supply from changes to immigration policy. The Fed has not been overly concerned, however, and should continue to express the view that the labour market is not a major source of inflationary pressure at the moment.

Fig 4. Household survey has been more volatile than establishment survey



Source: Bloomberg, Crédit Agricole CIB

Fig 5. Beveridge curve suggests inflection point could be near



Source: Bloomberg, Crédit Agricole CIB

Overall, the labour market has clearly cooled, but it has done so in a relatively gradual and orderly fashion to this point. This is illustrated by a look at the Beveridge curve (see Figure 5), which shows that cooling so far has largely taken place through declining job openings. That said, the Beveridge curve is also close to a point where historical data indicates a shift from the steep portion to a flatter portion of the curve, suggesting that an inflection point could be near whereby additional cooling risks being skewed more towards rising layoffs.

Moving forward, we continue to think that policy uncertainty and the sequencing of actual policy changes, including tariffs being at the forefront of Trump's early actions, could lead to a soft patch for the economy through mid-year. In this vein, we expect some additional deterioration in the labour market, and believe that the coming months could be weaker than what we expect to see in May. In our base case, this cooling is relatively modest but still sees the unemployment rate hitting 4.5%, and we think risks are tilted to the upside.

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For the time being, however, the Fed seems comfortable with the current state of the labour market, and a report in line with expectations would do little to alter this view. With the Fed clearly signalling that it is firmly on hold as it awaits additional clarity on the policy front, we think that the Fed will continue to see little urgency to cut after Friday's data.

That said, a sharp downside surprise approaching 50k or below could add some urgency, though we think that a cut is still unlikely to materialise before Q325, even in the case of a weaker-than-expected report. Additionally, we continue to expect that sticky inflation may prevent the Fed from easing as aggressively as the market expects, even if the labour market cools further.

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