Economic Indicator — September 3, 2021

August Payrolls: Quite the Delta

Summary

Hiring slowed sharply in August, with employers adding 235K new jobs after an upwardly revised gain of 1.05M in July. The toll from rising COVID concerns was evident amid a stalling in the leisure & hospitality sector. Labor availability remains an ongoing challenge, illustrated by labor force participation remaining unchanged. Wages continue to push higher as a result, but the dampened pace of hiring and bevy of workers still on the sidelines will keep the Fed awaiting more progress on the labor market. Today's report fully closed the door on the chance of a September taper announcement, in our view.

Economist(s)

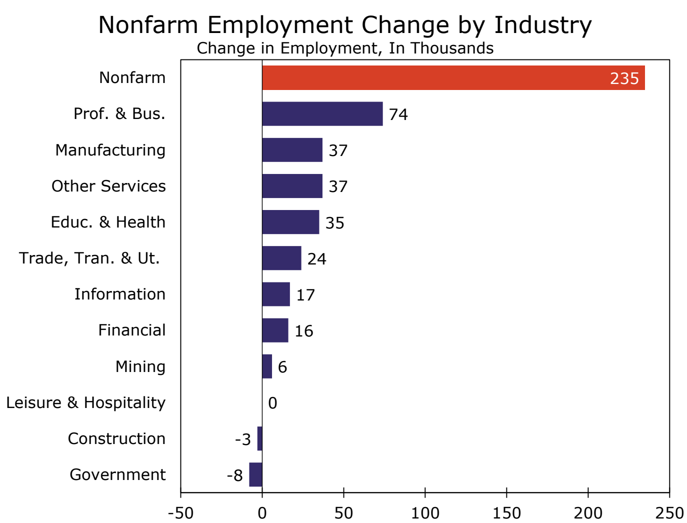
Sarah House
Senior Economist | Wells Fargo Securities, LLC
Sarah.House@wellsfargo.com | 704-410-3282

Michael Pugliese
Economist | Wells Fargo Securities, LLC
Michael.D.Pugliese@wellsfargo.com | 212-214-5058

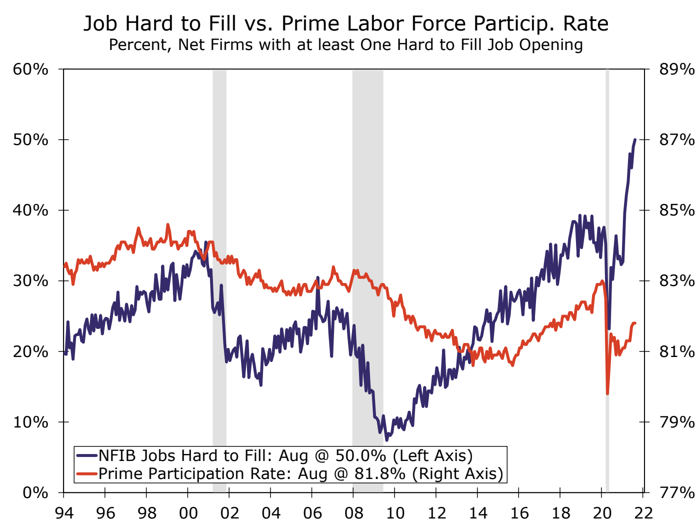
Whipsawed by the Virus Yet Again

Renewed concerns over COVID took a clear toll on hiring in August. Payrolls rose by 235K, coming in well-short of consensus expectations and marking a sharp slowdown from July when payrolls rose by an upwardly revised 1.05M. The clearest evidence of the Delta surge holding down job growth came from the leisure & hospitality sector. After increasing by more than 300K for four straight months, employment was unchanged in August. More broadly, the number of workers teleworking due to COVID rose last month for the first time since December, as the virus continues to impact working patterns.

While today's number was by no means good, the slowdown is not quite as bad as it looks. The past two months' phantom hiring in education, where there were fewer than usual layoffs because workers were never hired in the first place, was bound to fade. Public and private eduction put up a combined gain of 14K in August. The 29K drop in retail was more than explained by food & beverage and building material stores as spending has shifted away from stay-at-home categories in recent months. Manufacturers still managed to add 37K jobs, with most of them coming in motor vehicles despite ongoing struggles to source parts. Yet employment also slipped in construction and healthcare, and the net share of industries adding jobs was the lowest since February.



Source: U.S. Department of Labor and Wells Fargo Securities



Source: U.S. Department of Labor, NFIB and Wells Fargo Securities

Labor Supply Challenges Still Ongoing

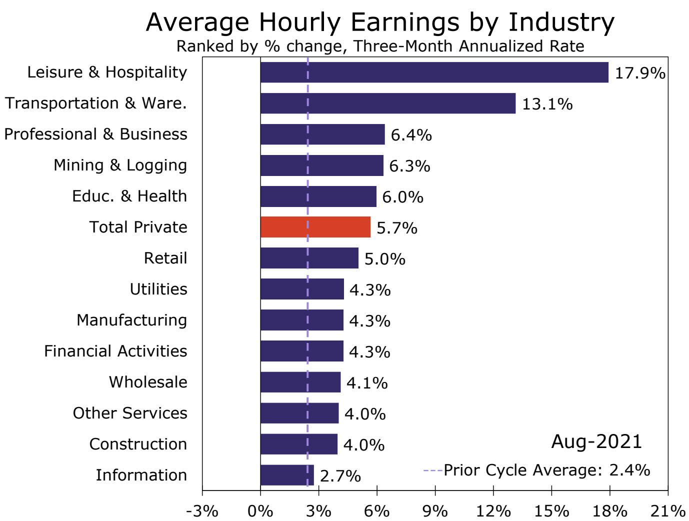
The availability of workers remains its own supply issue. Constraints that have held back hiring for months now showed little signs of easing in August. The labor force grew by just 190,000, and the labor force participation rate was left unchanged. The labor force participation rate has risen just 0.2ppts since December 2020, which suggests that employers have yet to have major success pulling new workers off the sideline. Perhaps unsurprisingly, half of small businesses reported having at least one job opening as hard to fill in August, again setting a new record high.

Many have looked to the Fall as a turning point for staffing challenges, but we are not there yet. Enhanced unemployment benefits have expired for only around a third of the unemployed. Meanwhile, the Delta wave has reignited health concerns and injected uncertainty about whether children will be able to stay in the classroom this fall without some intermittent periods of remote learning or daycare closures, keeping workers on the sidelines somewhat longer. While the September jobs report will reflect a relatively late period of the month (the survey weeks comes as late as possible, covering the 12-18th), we believe it is unlikely to show workers returning to the labor force in droves. Hiring challenges are likely to persist over the next few months, keeping the Fed uncertain about the extent to which workers will return to the labor force as the pandemic fades.

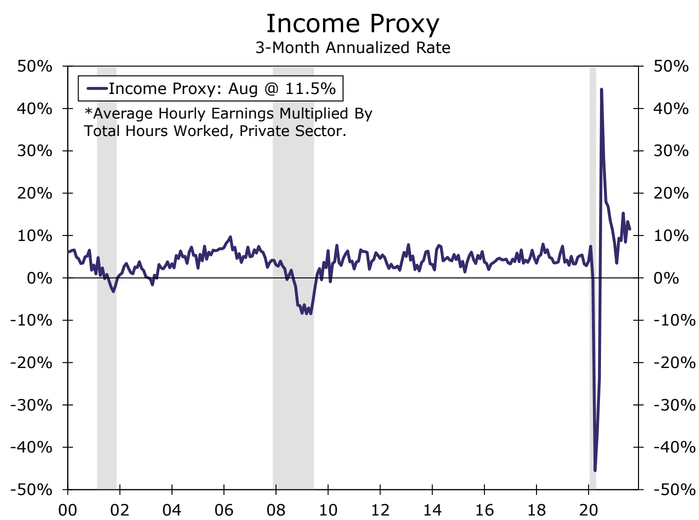
Wage Growth Overstated but Underlying Trend Still Strong

How quickly workers step back into the labor market looms large over the inflation debate. There is general agreement that supply bottlenecks pushing up goods prices will eventually ease, but wages are stickier and a larger share of costs in the service sector. Continued acceleration in pay greatly weakens the prospect of inflation being "transitory." The 0.6% headline jump in average hourly earnings for August lends itself to the argument that inflation will be higher for longer. To some extent, the headline beat is overstated given how the composition of job growth shook out. Weak job growth in some lower-income industries like leisure & hospitality and retail trade led to a situation where average hourly earnings were higher than we expected. That said, wage growth within industries still suggests employers are fighting dearly for workers. Despite zero employment growth in the leisure & hospitality sector, average hourly earnings rose a remarkable 1.3% over the month. This monthly move pushed the 12-month change to 10.3%.

While constraints on the supply of labor will persist somewhat longer, we expect hiring challenges to ease later this year as the availability of workers improves and slower spending leads to less fevered staffing efforts. That should stem the recent pace of pay hikes. In the meantime, however, higher pay and greater employment is boosting labor income and providing an offset to dwindling fiscal support. Our income proxy shows labor income rising 0.7% in August.



Source: U.S. Department of Labor and Wells Fargo Securities



Source: U.S. Department of Labor and Wells Fargo Securities

Door Fully Closed on a September Taper Announcement

It strikes us as highly unlikely the FOMC will announce a taper of its asset purchases at its September 21-22 meeting. Today's miss on nonfarm payroll growth will disappoint top Fed officials who have signaled that it would take a couple more reports of 500K-1M jobs per month in order for "substantial further progress" to be achieved. However, not all is lost. The monthly job numbers have been very volatile throughout the re-opening process, and it is quite possible August's miss will be offset by stronger numbers in September. A potential peak in COVID cases, school re-openings and the end of enhanced unemployment benefits all point towards a rebound in job growth in September.

If September 21-22 is a no-go, this leaves November 2-3 and December 14-15 as the two remaining FOMC meetings of the year. We suspect both of these meetings will be "live" in the sense that a taper could be announced at either one. All year our forecast has been for a taper to be announced at the December 14-15 FOMC meeting, with the actual reduction in asset purchases occurring shortly thereafter. The incoming inflation and jobs data over the next two months will be critical to the case for an earlier announcement on November 3. If the jobs numbers rebound by November and/or the inflation data surprise to the upside, we think a November announcement is a real possibility. However, if job growth is just a few hundred thousand in September and inflation shows additional signs of slowing, we suspect the FOMC would wait just a bit longer to observe a couple additional employment reports between the November and December meetings. For now, consider it a coin flip, with data dependency much more important than it has been at any point this year.

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Economics Group

Jay H. Bryson, Ph.D.	Chief Economist	(704) 410-3274	jay.bryson@wellsfargo.com
Mark Vitner	Senior Economist	(704) 410-3277	mark.vitner@wellsfargo.com
Sam Bullard	Senior Economist	(704) 410-3280	sam.bullard@wellsfargo.com
Nick Bennenbroek	International Economist	(212) 214-5636	nicholas.bennenbroek@wellsfargo.com
Tim Quinlan	Senior Economist	(704) 410-3283	tim.quinlan@wellsfargo.com
Azhar Iqbal	Econometrician	(212) 214-2029	azhar.iqbal@wellsfargo.com
Sarah House	Senior Economist	(704) 410-3282	sarah.house@wellsfargo.com
Charlie Dougherty	Economist	(704) 410-6542	charles.dougherty@wellsfargo.com
Michael Pugliese	Economist	(212) 214-5058	michael.d.pugliese@wellsfargo.com
Brendan McKenna	International Economist	(212) 214-5637	brendan.mckenna@wellsfargo.com
Shannon Seery	Economist	(704) 410-1681	shannon.seery@wellsfargo.com
Hop Mathews	Economic Analyst	(704) 383-5312	hop.mathews@wellsfargo.com
Nicole Cervi	Economic Analyst	(704) 410-3059	nicole.cervi@wellsfargo.com
Sara Cotsakis	Economic Analyst	(704) 410-1437	sara.cotsakis@wellsfargo.com
Coren Burton	Administrative Assistant	(704) 410-6010	coren.burton@wellsfargo.com

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