February 3, 2022

Surging January U.S. employment adds upside to the Fed

- Payrolls added 517k jobs and the unemployment rate edged lower to 3.4%
- Total hours worked surged 1.2% but wage growth further decelerated
- Fed is still likely close to the end of its rate hiking cycle, although resilient labour market backdrop adds to the odds that the next 25 bp hike in March won't be its last

The U.S. labour market backdrop yet again proved surprisingly resilient in January with a 517k surge in employment, supported by gains in service industries such as leisure and hospitality (+128k), professional and business services (+82k) and health care (+58k). The unemployment ticked lower to 3.4%, the lowest rate since the 1960s. Total hours worked bounced back sharply, rising 1.2% after having contracted for two consecutive months before January. The gain in hours worked was widespread across sectors but was most notable in leisure and hospitality (+2.8%). Wage growth was the only spot where momentum decelerated. Average hourly earnings for all private non-farm employee increased by 0.3% from December to January. That's slower than the average monthly pace of 0.45% in 2022, and pushed the year-over-year growth in wages to a lower but still elevated 4.4%, down from a peak of 5.9% 10 months ago.

Strong labour market data is at odds with a slew of indicators including consumer spending, industrial production and business sentiment, all of which have been flagging slower growth momentum in the U.S. economy. Indeed, real PCE declined for two consecutive months in November and December, led by weaknesses in goods purchases. Spending on services has remained positive but also flattened out more significantly into late 2022. Still, labour markets tend to lag economic conditions and more weaknesses is expected to show up as the impact of 450 bps of Federal Reserve interest rate hikes continues to cut into household and business purchasing power with a lag. The Fed this week highlighted slowing core inflation readings and decelerating economic activities as key drivers for the downshift to a smaller 25 bp increase in the fed funds target range. Today's report clearly adds some upside to our expectation for another 25bp increase in March before the Fed opts for a pause. But the slowdown in wage growth in January despite record-low unemployment rate should be encouraging for the Fed, and if that's mirrored in slower inflation readings in the months ahead (including Powell's core services ex shelter) then we're still likely nearing the end of this tightening cycle.

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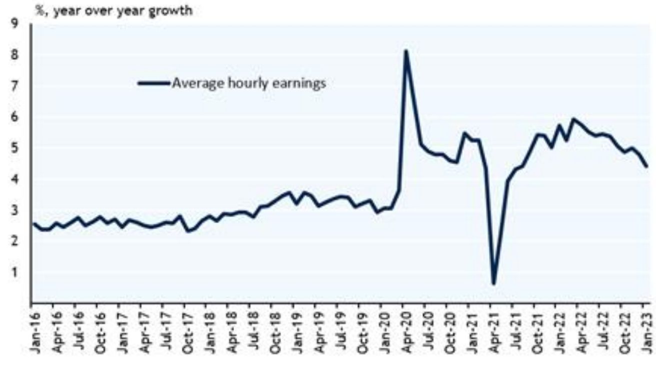
Data Summary:

	Nov-22	Dec-22	Jan-23	Jan-23
	m/m change, thousands			*12mth avg*
Payroll employment	290	260	517	414
Private	228	269	443	388
Public	62	-9	74	26
Hourly wages (m/m %)	0.4	0.4	0.3	4.4 (y/y %)
		%		*y/y change*
Unemployment rate	3.6	3.5	3.4	-0.6
U6	6.7	6.5	6.6	-0.5
Participation rate	62.2	62.3	62.4	0.2

Source: Haver, RBC Economics Research

Wage growth decelerating but still high in the U.S.



Source: BLS, RBC Economics