What leading labor market indicators should investors be watching? What are they showing now?

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As of August 19, initial jobless claims were at just 230k and have been flat since the end of February. These data are consistent with a tight job market. Continuing claims paint a similar picture at just 1.7M. These data are among the best high frequency indicators for determining an imminent labor market turning point. Important to note people collecting severance do not count in these figures!
In a slowdown, firms cut overtime first and then cut headcount outright if conditions warrant further cost cutting. As a result, overtime hours can be a leading indicator of payrolls. Manufacturing overtime hours continue to plunge. They are down 5.4% YoY and are in recessionary territory. These data jibe with the ISM manufacturing series which has contracted for nine straight months. Historically, this is a harbinger of cuts in cyclical sector employment.
Temporary Help Services — Negative

Temporary hiring allows services firms to carry a more easily adjustable workforce. Thus, it can be highly cyclical. Firms adjust the number of temporary hires first, before more actively investing in (or cutting) personnel. Temp payrolls are down nearly 5% YoY, which is historically consistent with recession and one that tends to precede broader job cuts.

Sources: BLS, NBER, Haver, SMBC Nikko
Quits — Negative

As the demand for labor increases, workers become more inclined to quit and take new jobs. As a result, the quits rate is a widely followed proxy for labor market strength. Since April 2022, the quits rate has fallen precipitously from a series high of 3.3% to just 2.5% (back to pre-pandemic levels). The quits rate indicates a quickly deteriorating labor market.

Sources: BLS, NBER, Haver, SMBC Nikko
The ISM’s manufacturing and services sector employment surveys score firms’ hiring plans. Readings above (below) 50 imply payrolls will grow (shrink). The manufacturing survey has been below this threshold for the last two months and for four of the last six. At the same time, services employment continues to slow (albeit still above 50).

Sources: ISM, NBER, Haver, SMBC Nikko
Since 2000, private payrolls contracted in 77% of the months (59 out of 77) where both employment indices (services and manufacturing) registered sub 50 readings. This is charted below where the blue highlights represent times when both ISM employment series were in contraction. *We are almost there. ISM manufacturing employment has been below 50. Meanwhile, ISM services has oscillated above and below the 50 mark since February.*
New Homes Under Construction — Almost Negative

In the nine months since the October pinnacle, new home construction is down 2.3% annualized, which is the worst decrease since October 2011. If this was indeed peak home construction, history says the sector could lose 1.1 million jobs between now and the trough of the recession. However, the transmission of Fed policy to construction is likely to take longer than average.

Sources: Census, BLS, NBER, Haver, SMBC Nikko
The NAHB’s Housing Market Index is comprised of three components: present home sales, expected sales, and the traffic of prospective buyers. Historically this has led the unemployment rate by 21 months and statistically implies that unemployment will rise to 6% by the end of 2024. However, the hit to construction employment will take longer than usual. For more on this, see our August 7th paper.
According to the Kansas City Federal Reserve, labor market momentum has been negative for the first six months of 2023. This has dragged measures of ‘activity’ substantially off its Q1 2022 cyclical peak of 1.4 to 0.981 in Q2 2023. We expect Q3 momentum and activity to decline further. Measures of momentum is at its poorest since the Global Financial Crisis.

Sources: Kansas City FRB, NBER, Haver, SMBC Nikko
Historically, peaks in the labor market activity indicator have corresponded with troughs in unemployment (shown below) and the former is deteriorating (see below).

If momentum continues to decline, which remains our call, then activity will decline further and the unemployment rate will rise.

Sources: Kansas City FRB, NBER, Haver, SMBC Nikko
Leading Indicators — Negative

The Conference Board’s index of leading economic indicators tends to lead employment for many large sectors. Below, we graph this series alongside manufacturing, professional and technical services and trucking employment which together account for 19% of private payrolls. Econometrically, leading economic indicators suggest that this amalgamation could decline 3.8% YoY by the end of the year, resulting in 960k job losses.

Sources: Conference Board, BLS, NBER, Haver, SMBC Nikko
### Conclusion

**In sum, the labor market is deteriorating but we are not yet at an inflexion point.**

Ultimately, the unemployment rate tends to rise over 400 basis points over a 20-month period in the event of recession (see below).

<table>
<thead>
<tr>
<th>Trough Month</th>
<th>Trough Rate</th>
<th>Peak Month</th>
<th>Peak Rate</th>
<th>Trough to Peak Change</th>
<th>Time Length (Months)</th>
</tr>
</thead>
<tbody>
<tr>
<td>January 1948</td>
<td>3.4</td>
<td>October 1949</td>
<td>7.9</td>
<td>4.5</td>
<td>21</td>
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<tr>
<td>June 1953</td>
<td>2.5</td>
<td>September 1954</td>
<td>6.1</td>
<td>3.6</td>
<td>15</td>
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<tr>
<td>March 1957</td>
<td>3.7</td>
<td>July 1958</td>
<td>7.5</td>
<td>3.8</td>
<td>16</td>
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<tr>
<td>March 1960</td>
<td>4.8</td>
<td>May 1961</td>
<td>7.1</td>
<td>2.3</td>
<td>14</td>
</tr>
<tr>
<td>May 1969</td>
<td>3.4</td>
<td>December 1970</td>
<td>6.1</td>
<td>2.7</td>
<td>19</td>
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<tr>
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<td>May 1975</td>
<td>9.0</td>
<td>4.4</td>
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<tr>
<td>May 1979</td>
<td>5.6</td>
<td>July 1980</td>
<td>7.8</td>
<td>2.2</td>
<td>14</td>
</tr>
<tr>
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<td>December 1982</td>
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<tr>
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<td>June 1992</td>
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<td>2.8</td>
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<tr>
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<td>June 2003</td>
<td>6.3</td>
<td>2.5</td>
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<tr>
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<td>October 2009</td>
<td>10.0</td>
<td>5.6</td>
<td>29</td>
</tr>
<tr>
<td>February 2020</td>
<td>3.5</td>
<td>April 2020</td>
<td>14.7</td>
<td>11.2</td>
<td>2</td>
</tr>
</tbody>
</table>

|               | 4.3         | 8.4           | 4.1       | 20.3                  | <- Avg               |
|               | +4.1%       | 7.8           | 3.6       | 18.0                  | <- Median            |

Source: BLS, SMBC Nikko

April 2023? 3.4 December 2024? 7.5?

+20 months
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