AGRON NICAJ
US Economist

Economic Research Office

anicaj@us.mufg.jp

MUFG Bank, Ltd.
A member of MUFG, a global financial group

The labor market remains defiant

10 March 2023

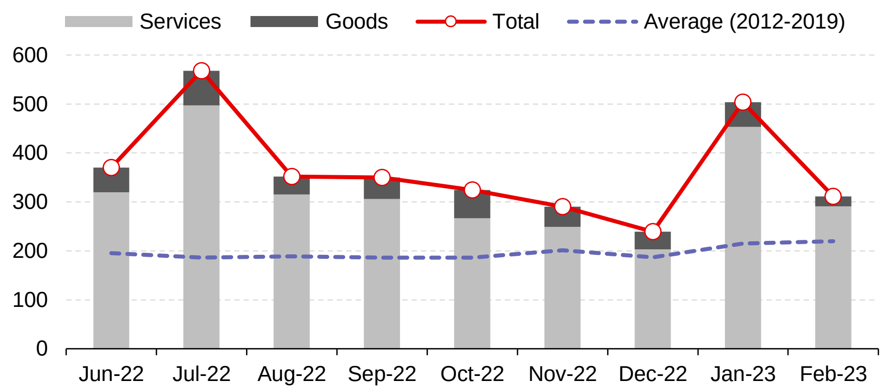
- The labor market continued to expand at a historically strong rate, adding 311,000 jobs in February. Consensus forecasts have consistently underestimated the strength of the labor market in 2022 and the trend is continuing in 2023. The Fed may be regretting their relatively dovish policy stance in the last FOMC meeting and may seek to compensate with a 50 basis point hike in the next.
- The services sector contributed to a slightly larger share of February's growth compared to previous months. Leisure and hospitality, retail trade, government, professional and business services, and health care led the expansion.
- The number of unemployed persons rose by 4% in February, pushing the unemployment rate up slightly to 3.6%. Labor force participation has returned to the pre-pandemic rate for prime-age workers, but there is no improvement in sight for older workers. The labor market remains very tight with 1.9 job openings per unemployed persons.
- Tech companies likely drove the large increase in layoffs in January, with nearly 80% of the rise coming from the professional and business services sector. Even so, the rise was completely offset by a drop in quits and other separations. Hiring accelerated in the industry resulting in net positive employment growth. Total separations were virtually unchanged across all private industries, highlighting the strength of labor demand.

Trends in employment have largely continued in February

February's employment report was short of remarkable, with much of the same trends from the second half of 2022 continuing into 2023. Employment strength relative to consensus estimates is of no surprise by now as forecasters continue to underestimate the strength of the labor market. Warmer than usual winter weather can potentially explain some of the expansion in the last 2 months, but fundamentally, the labor market is reflecting strong demand in the US economy.

Employment growth remained historically strong in February

Nonfarm payroll employment growth, thousands



Source: BLS, MUFG Bank Economic Research

Total nonfarm payrolls increased by 311,000 in February, 265,000 of which were in the private sector and many in key services industries. The leisure and hospitality industry added 105,000 jobs but employment is still 2.4% below the pre-pandemic level. It will take at least another 4 months of strong growth for the industry to reach that level. Health care added 44,000 jobs in February, but the industry is still, by many measures, understaffed. We can expect further expansion both in the short-run and long-run as the aging population increases demand for services in the industry.

Goods industries contributed a smaller share of the growth in February compared to previous months. Much of that can be attributed to manufacturing, where employment growth was virtually flat. However, construction expanded again, adding another 24,000 jobs despite the impact rising interest rates have had on new home construction.

Labor shortages are not showing signs of going away

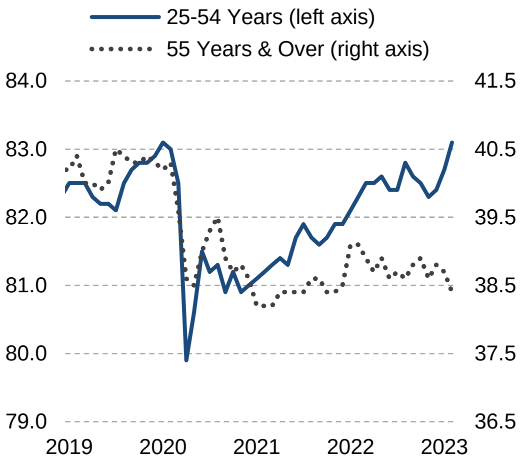
The labor force participation rate improved to 83.1% for prime-age workers, matching the pre-pandemic rate in January 2020. The improvement certainly bodes well for increasing the labor supply and if highly reflective of the abundance of labor demand. However, older workers are not showing any signs of returning to the labor force. The labor force participation rate for those 55 and older stands at 38.4%, compared to the pre-pandemic rate of 40.2% in January 2020.

The number of unemployed persons rose by 4% in February, pushing the unemployment up slightly to 3.6%, which is consistent with the average of the last 6 months. With employment expanding at a steady rate and above historical averages, we are not likely to see substantial rises in the unemployment rate.

Total nonfarm job openings fell in January to 10.8 million, but the level remains near historical highs and has not significantly trended downward since the summer of 2022. The vacancy to unemployed ratio stands at 1.9, signalling an abundance of available work with nearly 2 job openings per unemployed persons. There are no strong signs that the labor market is becoming less tight.

Participation rates have recovered for prime-age workers

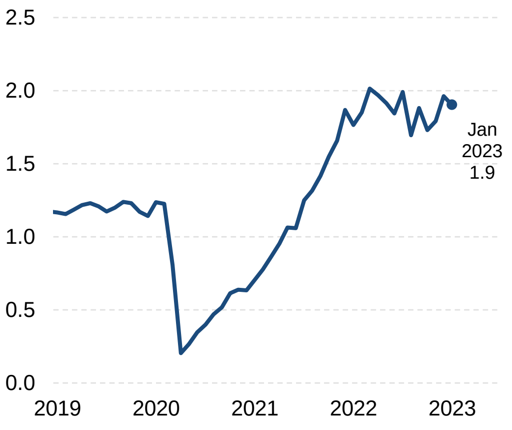
Labor force participation rates, %



Source: BLS, MUFG Bank Economic Research

Labor market remains very tight

Vacancy to unemployed ratio



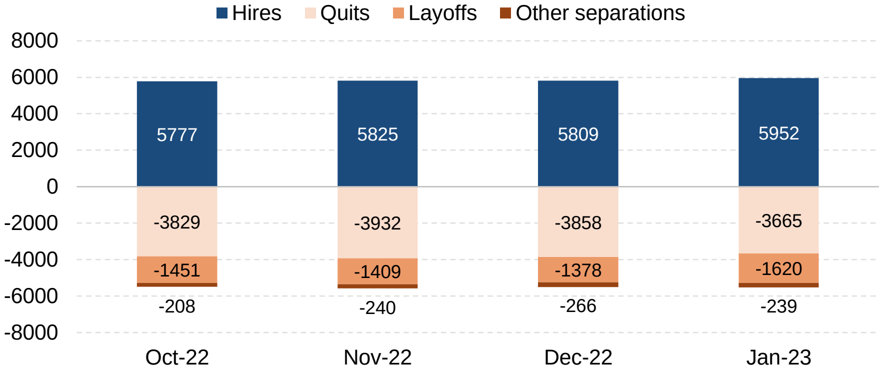
Source: BLS, MUFG Bank Economic Research

Even the January rise in layoffs is proving to be inconsequential. Layoffs and discharges rose by 242,000 in January, a 17.6% increase. Though substantial, this was entirely offset by a drop in quits of 193,000 and a drop in other separations of 27,000. Overall, total separations across all industries were virtually unchanged. Additionally, hiring accelerated which pushed net employment gains above 400,000 from the JOLTS survey, consistent with January payroll employment gains from the CES survey.

Nearly 80% of the increase in layoffs came from the professional and business services sector, and likely from the tech companies categorized within. The drop in quits were also concentrated in that industry and total separations actually fell despite the steep rise in layoffs. And like the rest of the economy, hiring accelerated in the industry bringing net employment gains. The professional and business services sector continues to grow, reflected both in hires less separations from JOLTS and payroll employment from CES.

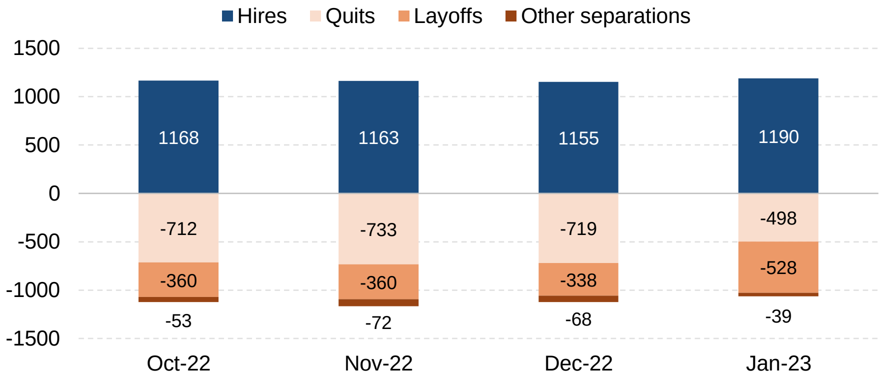
Accelerated hiring and decline in quits offset the rise in layoffs

Hires and separations, private industries, thousands



Source: BLS, MUFG Bank Economic Research

Hires and separations, professional & business services, thousands



Source: BLS. MUFG Bank Economic Research

The Fed is starting to sound more hawkish

The latest employment figures underscore Fed Chairman Jerome Powell's hawkish testimony in front of Congress. Fundamentally, the US is facing long run aggregate supply issues and it may have been premature of them to slow the pace of rate hikes after a couple of months of uplifting inflation data.

However, the latest collapse of Silicon Valley Bank does raise questions as to the health of the banking sector and whether aggressive monetary policy will bankrupt the industry. There has been spill over to the rest of the banking sector following SVB's collapse, with the largest US banks all losing billions in market cap. But given SVB's customer base of start-ups and venture capital firms, the bank's deposits relied heavily on companies dependent on low interest rates. Traditional US banks are likely in a more financially stable position.

SVB's collapse appears to a symptom of the tech bubble bursting, but it may make the Fed cautious of being too aggressive and risking additional spill over to other banks. There is still a strong likelihood of another 25 basis point hike at the next FOMC meeting, but given the strength of the labor market and slowing disinflation, the Fed may consider a 50 basis point hike.

Analyst Certification

The views expressed in this report solely reflect the personal views of Agron Nicaj, the primary analyst responsible for this report, about the subject securities or issuers referred to herein, and such views may not necessarily reflect the thoughts and opinions of MUFG Bank, Ltd. and its affiliates or management team. No part of such analyst's compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed herein.

Disclaimers

About Mitsubishi UFJ Financial Group, Inc.'s U.S. Operations including MUFG Americas Holdings Corporation

The U.S. operations of Mitsubishi UFJ Financial Group, Inc. (MUFG), one of the world's leading financial groups, has total assets of $332.4 billion at March 31, 2022. As part of that total, MUFG Americas Holdings Corporation (MUAH), a financial holding company, bank holding company, and intermediate holding company, has total assets of $159.2 billion at March 31, 2022. MUFG Securities Americas Inc. is a registered securities broker-dealer which engages in capital markets origination transactions, domestic and foreign debt and equities securities transactions, private placements, collateralized financings, and securities borrowing and lending transactions. MUAH is owned by MUFG Bank, Ltd. and Mitsubishi UFJ Financial Group, Inc. MUFG Bank, Ltd., a wholly owned subsidiary of Mitsubishi UFJ Financial Group, Inc., has offices in Argentina, Brazil, Chile, Colombia, Peru, Mexico, and Canada. Visit www.mufgamericas.com for more information.

About MUFG and MUFG Americas

Mitsubishi UFJ Financial Group, Inc. (MUFG) is one of the world's leading financial groups. Headquartered in Tokyo and with over 360 years of history, MUFG has a global network with approximately 2,100 locations in more than 50 countries. MUFG has nearly 160,000 employees and offers services including commercial banking, trust banking, securities, credit cards, consumer finance, asset management, and leasing. The Group aims to "be the world's most trusted financial group" through close collaboration among our operating companies and flexibly respond to all the financial needs of our customers, serving society, and fostering shared and sustainable growth for a better world. MUFG's shares trade on the Tokyo, Nagoya, and New York stock exchanges.

MUFG's Americas operations, including its offices in the U.S., Latin America, and Canada, are primarily organized under MUFG Bank, Ltd. and subsidiaries, and are focused on Global Corporate and Investment Banking, Japanese Corporate Banking, and Global Markets. MUFG is one of the largest foreign banking organizations in the Americas. For locations, banking capabilities and services, career opportunities, and more, visit www.mufgamericas.com.