The labor market for goods industries is starting to cool
7 April 2023

- Several indicators from production to consumption have signalled a slowdown in goods industries for months, and the labor market is finally beginning to reflect that. Employment in goods industries did not grow in March for the first time since April 2021, and we may begin to see job losses in the coming months.

- Overall, the labor market is still tight and the unemployment rate remains historically low. The strongest signs of cooling are present in job openings, where the vacancy to unemployed ratio fell to 1.67. Though trending in the right direction, labor demand is still well above the pre-pandemic level.

- Based purely on the labor market, the Fed will certainly consider another 25 bps hike in May. However, the fallout from the banking situation has yet to fully materialize. Banks are likely to tighten credit conditions in the coming weeks and months and the Fed may view this as a replacement for more interest rate increases. Right now, the odds of no change vs another hike in May are 50/50.

The beginning of the slowdown in goods industries

Overall employment expanded by 236,000 in March, closely in line with most expectations. Leisure and hospitality again led the expansion, adding 72,000 jobs in March. Employment in the industry is still 2.2% below its pre-pandemic level, and growth is likely to continue as long as consumption in food services and accommodation remains elevated. Employment growth in government was second in March, adding 47,000 jobs. There are still 314,000 fewer jobs in the industry compared to February 2020.

Health care also continued to expand, adding 34,000 jobs in March. Even though employment has exceeded its pre-pandemic level, the industry is still by many measures understaffed. Consumption in health care is less dependent on economic conditions, compared to leisure and hospitality. Demographic forces have a big impact, and the aging population will ensure demand stays relatively high even in the event of a recession.

Employment growth in goods has finally stopped

Employment growth in goods industries, data from BLS, MUFG Bank Economic Research
The story is different for goods employment. In March, good producing industries lost 7,000 jobs in total, virtually equivalent to no change. This is the first month where these industries have collectively not expanded since April 2021. Employment change in manufacturing, construction, and mining have all been essentially flat in March.

While one month of no growth isn’t indicative of a trend on its own, other economic indicators have pointed to slowdown in goods for a few months. Real personal consumption has been flat since the start of 2022 for both durable goods and non-durable goods excluding gasoline. Additionally, the ISM Manufacturing index has been pointing to a slowdown for months, and construction of single-family residential properties has dropped drastically since the Fed started raising interest rates.

This broad slowdown in goods industries is just now beginning to be reflected in the labor market. We are likely to experience job losses in industries such as manufacturing and construction sometime in Q3, and perhaps even in the later months of Q2.

**The labor market is beginning to loosen**

The labor force participation rate stayed at 83.1% in March for prime-age workers (25-54 years old). Further acceleration is unlikely for this age group since it has already reached the pre-pandemic rate from January 2020. There continues to be no progress in the participation rate of older workers (55 and older). Early retirements since the pandemic appear to have permanently shifted participation rates down. At this point, only a recession is likely to bring older workers back to the labor force. But even then, we may not see them return the rate seen immediately before the pandemic.

The good news is, while the labor supply isn’t substantially growing, labor demand is finally showing signs of cooling. Job openings fell in February by 632,000, bringing the vacancy to unemployed ratio down to 1.67. These figures still indicate a historically tight labor market, but the trend is finally beginning to move in the right direction.

Hiring fell in February from 5.92 million to 5.77 million. This, along with the drop in vacancies and flat employment growth in goods industries, are the strongest signals of a cooling labor market. However, quits and layoff have not changed by much and the unemployment rate still stands near historic lows at 3.5% as of March. Demand still exceeds supply in the US labor market.
The Fed is in a difficult position

From the Fed’s perspective, March’s labor market data may not be enough to warrant a pause on interest rate hikes. While yes, demand is finally showing signs of trending downward, the level is still far too high to be consistent with a 2% inflation target. On this labor market data alone, the Fed would likely be leaning toward more hikes.

However, the latest banking situation is sure to further tighten credit conditions in the US. The full effect likely won’t materialize for another few weeks or months, so balancing the impact of raising the Federal Funds Rate with additional credit restrictions from the banking sector is going to be the Fed’s biggest challenge. Given this reality, the odds of another hike are 50/50.
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

The information and views contained herein are not intended for distribution to, or use by, any person or entity in any jurisdiction or country where such distribution or use would be contrary to law or regulation or which would subject MUFG Bank, Ltd. (collectively with its various offices and affiliates, “MUFG Bank”) to any registration requirement within such jurisdiction or country. The information and views contained herein are provided for general informational purposes only, are subject to change, and are not intended to be, nor should be used, or considered, as an offer, or the solicitation of an offer, to sell or to buy or to subscribe to or for securities or any other financial instruments, and do not constitute specific investment, legal, tax or other advice or recommendations. The information contained herein reflects the thoughts and opinions of the noted authors only, and such information does not necessarily reflect the thoughts and opinions of MUFG or its management team. Neither this nor any other communication prepared by MUFG Bank should be construed as investment advice, a recommendation to enter into a particular transaction or pursue a particular strategy, or any statement as to the likelihood that a particular transaction or strategy will be effective and it does not take into account the specific investment objectives, financial situation, or the particular needs of any specific person who may receive this information. Any information relating to performance contained herein is illustrative and no assurance is given that any indicative returns, performance or results, whether historical or hypothetical, will be achieved. Before entering into any particular transaction, you should consult an independent financial, legal, accounting, tax, or other advisor as may be appropriate under the circumstances. In any event, any decision to enter into a transaction will be yours alone, not based on information prepared or provided by MUFG Bank. MUFG Bank hereby disclaims any responsibility to you concerning the characterization or identification of terms, conditions, and legal or accounting, or other issues or risks that may arise in connection with any particular transaction or business strategy. While MUFG Bank believes that any relevant factual statements contained herein, and any assumptions on which such statements are based, are in each case accurate, neither the authors nor MUFG have independently verified its accuracy, and such information may be incomplete or condensed. The information is provided “AS IS”. The authors and MUFG do not warrant the accuracy of the materials provided herein, either expressly or implied, for any particular purpose and expressly disclaims any warranties of merchantability or fitness for a particular purpose. The authors and MUFG cannot and do not guarantee the accuracy, validity, timeliness or completeness of any information or data made available to you for any particular purpose. MUFG Bank may have issued, and may in the future issue, other reports that are inconsistent with or that reach conclusions different from the information and views contained herein. Such other reports, if any, reflect the different assumptions, views and/or analytical methods of the analysts who prepared them, and MUFG Bank is under no obligation to ensure that such other reports are brought to your attention.

© 2023, MUFG Bank, Ltd. All Rights Reserved.

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 (MUAG), 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. MUAG 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.