Financial Market Weekly

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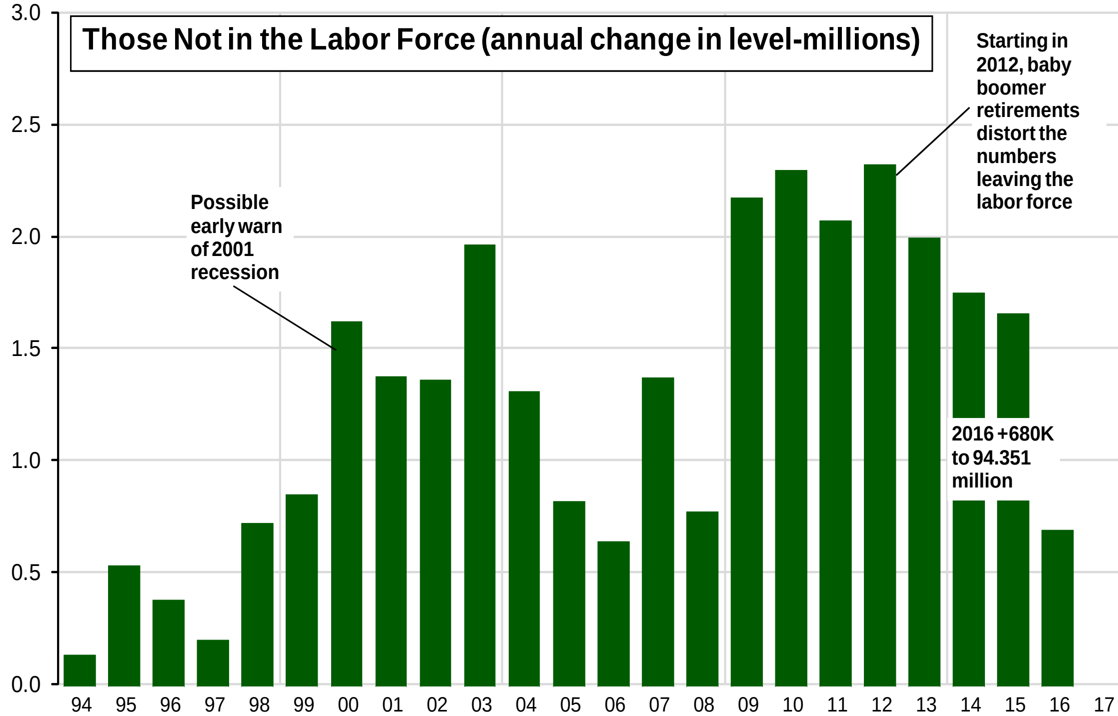
20 JANUARY 2017

ALL TOGETHER NOW: 95 MILLION AMERICANS NOT IN THE LABOR FORCE



This week we give our quick 95 bottles of beer on the wall analysis of the millions of American's not participating in the labor force. Not working. All's we can say is that if this is an economic problem that needs a solution and that swings presidential elections, get used to it: the trend is for the number of Americans not in the labor force to go up every year with the growth in the population just as sure as the sun rises every day. In boom times, sure, maybe the increase in those out of the labor force is not as great or a slight decline. And in the not-so Great Recession more Americans fell out of the labor force for at least a few years anyway in 2009, 2010, 2011. These years 2009-11 count as "economic stress." Labor force dropouts. Fine. But generally, this is not an indicator to hang your hat on when it comes to judging the strength of overall labor market or broader economic conditions. Once you leave the labor force, you're gone, there's no coming back. Government policy makers should not focus on bringing down the numbers of Americans not in the labor force (95.102 million in December 2016) because it is simply going to grow larger and larger in the years to come. Economics isn't a science, but the population statistics are. The die is cast. From the moment you were born, you were destined to leave the labor force.

Those Not in the Labor Force are counted from the population of everyone 16-years of age or older. This is the civilian noninstitutional population. The table here shows the annual change in the number of people not in the labor force. The count can be affected by various idiosyncratic factors, but generally before the 2008-09 recession there were no serious dropouts from the labor force. Nothing for Washington to step in and fix, or better, talk and talk about fixing. The first of an 80 million wave of baby boomers born 1946-64 hit 65-years old in 2011 and started retiring and leaving the labor force. Thank you for your service. Retirement is not a symptom of a weak economy. If we subtract out those 65-years or older from the statistics, the labor market stopped worsening in 2012. In fact in 2016, the number of dropouts from 16 to 64 years of age actually declined by 375K (just what House Speaker Ryan said he wanted.)

House Speaker Paul D. Ryan (R-WI)

Look -- look, not to get into statistics, but our labor force participation rates are pretty awful. We haven't seen these since like the Carter years. What it means -- what that means is, able-bodied adults aren't working or aren't looking for work. They're marginalized. They're on the sidelines. We've got to get them back into the economy.

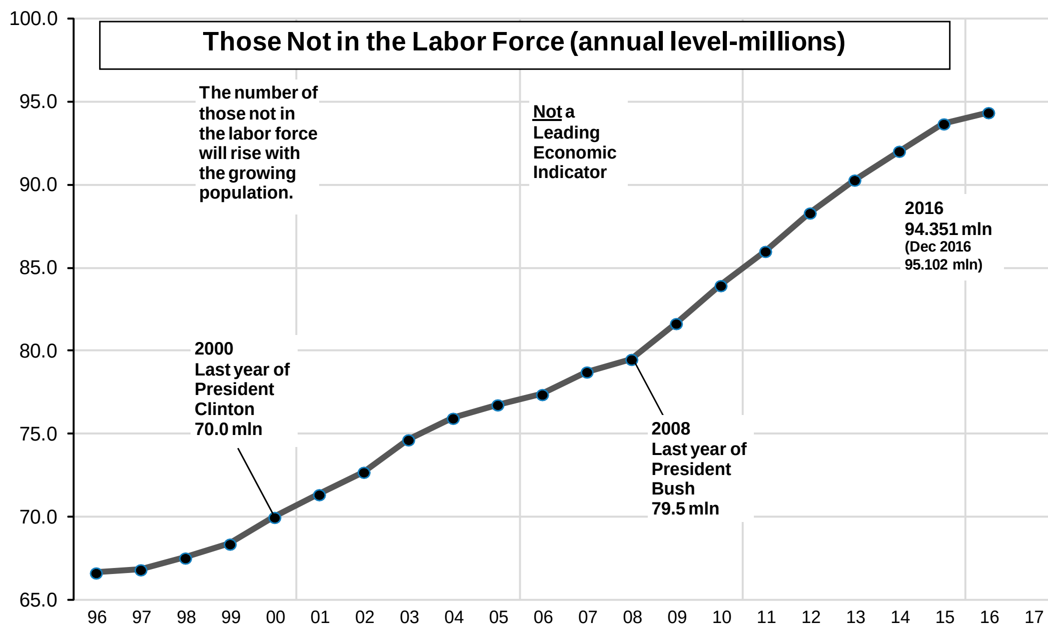
Annual Change in Number Not in Labor Force			
(Thousands)			Total ex-
	Total	65-plus	65-plus
2006	625	339	286
2007	1356	294	1062
2008	758	494	264
2009	2158	546	1612
2010	2282	524	1758
2011	2060	629	1431
2012	2309	1525	784
2013	1980	1154	826
2014	1735	1306	429
2015	1646	1106	540
2016	680	1055	-375
Some economic stress 2009-11, but			
mostly retirees dropping out since.			
Those not in Labor Force increased			
680K to 94.351 million in 2016			

So we know that Those Not in the Labor Force are made up of civilians not in prison who are 16-years of age or older. But there is another way to look at these 95 million not in the labor force. The Federal government does ask people why they aren't looking for work. Why aren't they in the labor force?

BREAKDOWN OF THOSE NOT IN THE LABOR FORCE			
Thousands, NSA	Dec 16	Dec 15	Change
Total not in labor force	95,774	94,691	1,083
Don't want job now	90,325	88,985	1,340
Want a job	5,499	5,705	-206
Did not search for work in a year	3,206	3,301	-95
Searched in last year, not in the past 4 weeks	2,243	2,404	-161
Not available to work now	559	571	-12
Marginally attached, can work now	1,684	1,833	-149
Discouraged	426	663	-237
Reasons other than discouraged	1,258	1,170	88
Family obligantions	235	204	31
In school or training	247	216	31
Poor health or disability	148	156	-8
Other	627	594	33

There were 95.774 million not in the labor force in December 2016, and just 5.499 million said they want a job. If you like conspiracies in your economic data, we suppose you can think that millions of the 90.325 million who said they "Don't want job now" did not tell the government pollster the truth. The 5.499 million who said they want work? Well, 3.206 million did not look for a job in a year. And 2.243 million looked in the last year, just not in the last 4 weeks. A subset of these are the 1.684 million famous "Marginally attached" that Yellen has talked about in the past. Not sure why you want to keep interest rates down at zero and hurt the 152 million Americans with jobs and incomes who prudently save for the future just to help the 1.684 million Marginally attached. And only 426 thousand of the Marginals say they are "Discouraged." There are not that many discouraged out there.

To conclude, the 95 million Americans out there who are not part of the labor force should not be a rallying cry in anyone's election campaign. The 95 million is not a sign of economic weakness. The economy is not still secretly in a recession. Don't ask when the economic good times are going to roll, they're here already. The best statistic on economic well-being for the country (better than 3 to 4 percent GDP) is the unemployment rate which at 4.7% right now cannot fall much further. The economy is better than you think. Bet on it.



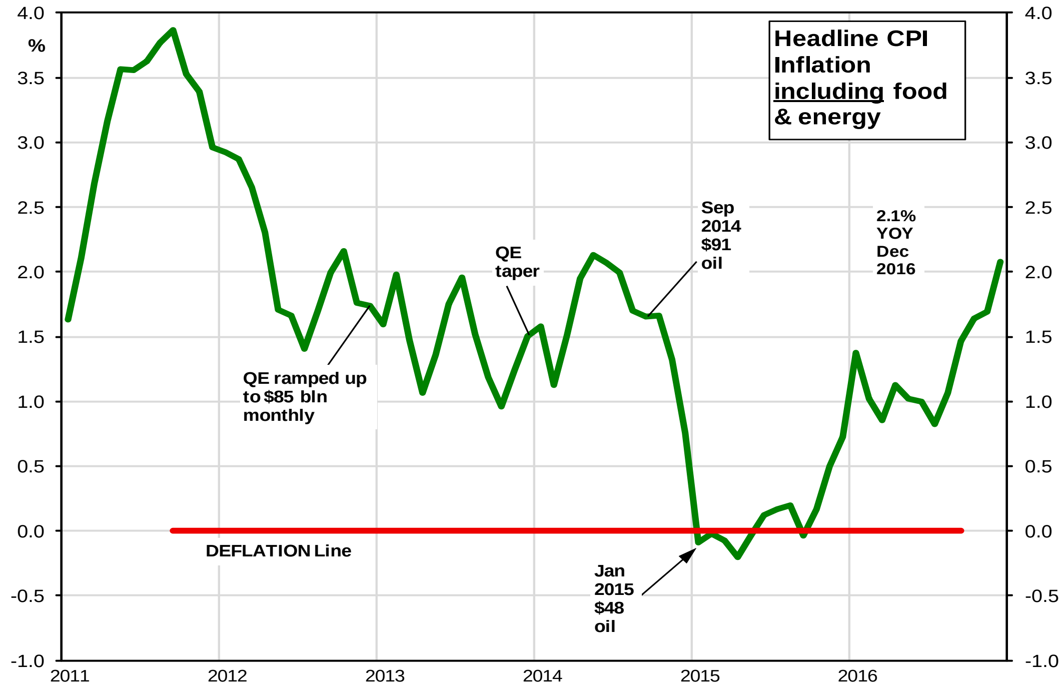
MARKETS OUTLOOK

	30-Dec 2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	Q3 2019	Q4 2019
30-Yr Bond	3.07	3.10	3.10	3.20	3.40	3.60	3.70	3.80	4.00	4.10	4.10	4.20	4.30
10-Yr Note	2.45	2.40	2.50	2.70	3.00	3.20	3.40	3.50	3.70	3.80	3.90	4.00	4.10
5-Yr Note	1.93	2.00	2.10	2.40	2.70	3.00	3.20	3.30	3.50	3.60	3.70	3.80	4.00
2-Yr Note	1.19	1.60	1.80	2.00	2.20	2.50	2.75	2.85	3.10	3.30	3.50	3.50	3.70
3-month Libor	1.00	1.25	1.50	1.70	1.95	2.20	2.45	2.70	2.95	3.20	3.45	3.45	3.70
Federal Fund Rate	0.75	1.00	1.25	1.50	1.75	2.00	2.25	2.50	2.75	3.00	3.25	3.25	3.50
2s/10s spread	126	80	70	70	80	70	65	65	60	50	40	50	40
Libor/funds spread	25	25	25	20	20	20	20	20	20	20	20	20	20

Wide-ranging week with 2.30% 10-yr Treasury yields Tuesday to 2.51% on Friday, closing the week at 2.47%. There was more CPI inflation and Fedspeak from Yellen and notable Fed Dove Brainard. Yellen said Thursday that letting the economy run hot would be risky and unwise. Brainard said fiscal policy could pose upside risks. We left the December 2016 Fed meeting thinking two or three rate hikes in 2017 and now it looks like three rate hikes are more likely.

Other News This Week

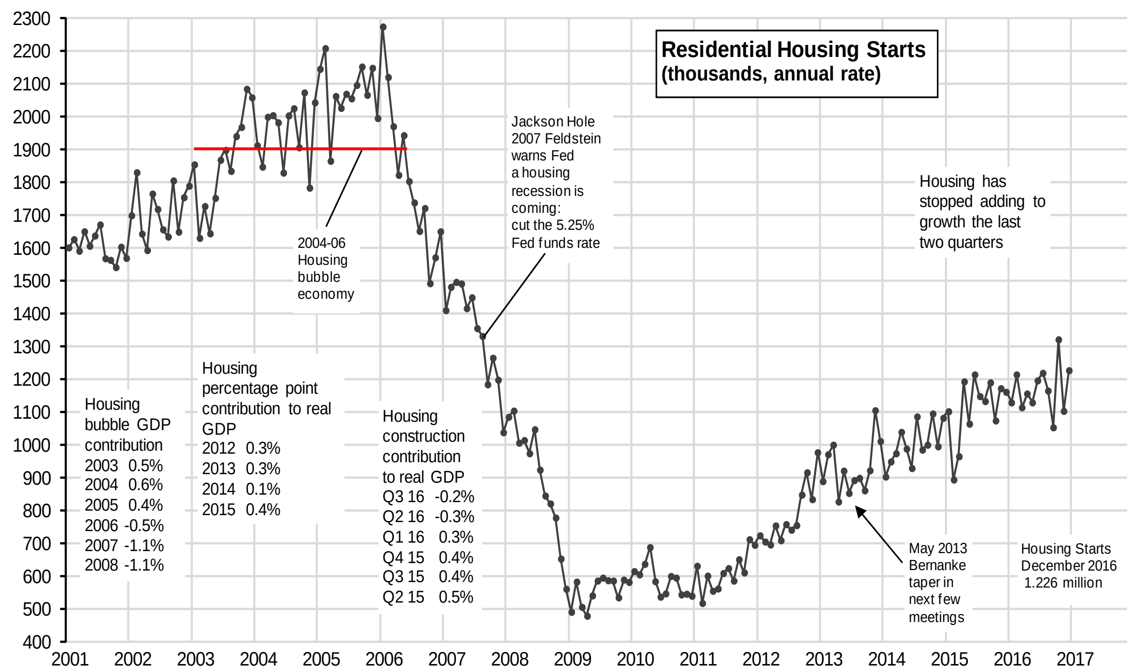
Consumer inflation hits the Fed's 2.0% target



Headline CPI inflation hit the Fed's 2.0% target this week for the first time in a couple of years. Headline CPI was up 1.7% the last year in November, and now this week December CPI is up 2.1% year-on-year. Made it. Knew it all the time. Victory over too-low inflation is sweet.

Unfortunately, CPI is no longer the Fed's preferred inflation measure. PCE consumer inflation is and the December data won't be out until Monday, January 30. PCE headline inflation was up 1.6% year-on-year in November. Stay tuned. Story developing.

Housing starts-biggest risk for the economy in 2017?



Housing starts have been bouncing around the last 4-5 months, but ended the year at 1.226 million in December. Residential home construction was a slight drag on real GDP growth in the second and third quarters of 2016. Q4 2016 GDP data is due out on Friday, January 27. It looks like housing construction could now swing back the other way and add a couple of tenths to growth in Q4 2016. We don't see a lot of risks out there on the horizon normally, but mortgage rates have risen 60 bps from 3.5 to 4.1 percent in the Trump yield rally, and it will be interesting to see if higher financing costs take a toll on homebuilder confidence.

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