U.S. Economic Comment

- February employment: remarkable job growth, moderate wage gain
- Unemployment steady because of surge in the labor force
- Labor market slack: largely gone

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The February Employment Report

Nonfarm payrolls surged in February, as firms added 313,000 new workers. The gain was broad based, although a few industries stood out on the firm side. Construction employment jumped 61,000, the largest monthly gain of the current expansion, and the financial services industry matched its best month of the expansion. The retail trade sector broke from the pattern of job cuts or modest gains with a jump of 50,000. The manufacturing sector also was strong, and local governments hired actively as well. Upward revisions totaling 54,000 in December and January added to the strong tone of the report.

Not only did firms expand payrolls, but they also lengthened work times, as the average workweek rose 0.1 hour to 34.5 hours, a reading at the top of the range from the past two years. The index of total work time, a measure that combines the effects of job growth and the length of the workweek, rose 0.6 percent, suggesting a strong month for production.

The unemployment rate was unchanged at 4.1 percent, but the steady reading masked strong results for employment as measured by the household survey and the size of the labor force. Both measures rose by about the same amount (785,000 and 806,000, respectively), which left measured unemployment approximately unchanged. The broad unemployment rate also was unchanged. The number of involuntary part-time workers increased, but a drop in marginally attached workers provided a partial offset, and the modest net change was insignificant relative to the jump in the size of the labor force.

Employment Report*

	Nonfarm Payrolls		Private-Sector Payrolls	Unemp. Rate	Broad Unemp. Rate	Household Emp.	Labor Force	Emp.-Population Ratio	Median Duration of Unemp.	Part-Time Econ. Reasons	Avg. Hourly Earnings	Avg. Workweek
	(Chg., Thousands)			(Percent)		(Chg., Thousands)		(Pct.)	(Weeks)	(Thou.)	% Chg.	(Hours)
Annual Average												
2015	226		213	5.3	10.5	212	145	59.4	11.7	6,373	0.2	34.5
2016	195		178	4.9	9.6	175	141	59.7	10.8	5,945	0.2	34.4
2017	182		180	4.4	8.5	149	72	60.1	10.0	5,252	0.2	34.4
2018	276		263	4.1	8.2	597	662	60.3	9.4	5,075	0.2	34.5
Qtrly. Average												
17-Q1	177		175	4.7	9.1	277	166	60.0	10.3	5,649	0.2	34.4
17-Q2	190		186	4.3	8.5	62	-7	60.1	10.2	5,280	0.2	34.4
17-Q3	142		137	4.3	8.5	358	289	60.2	10.3	5,198	0.3	34.4
17-Q4	221		223	4.1	8.0	-101	-162	60.1	9.5	4,882	0.2	34.5
2017 Monthly												
July	190		188	4.3	8.5	261	253	60.2	10.4	5,236	0.3	34.4
Aug.	221		208	4.4	8.6	-40	131	60.1	10.3	5,209	0.2	34.4
Sept.	14		16	4.2	8.3	853	484	60.4	10.1	5,148	0.5	34.3
Oct.	271		277	4.1	8.0	-478	-711	60.2	9.8	4,880	-0.2	34.4
Nov.	216		217	4.1	8.0	71	162	60.1	9.5	4,851	0.3	34.5
Dec.	175	(160)	174	4.1	8.1	104	64	60.1	9.1	4,915	0.4	34.5
2018 Monthly												
Jan.	239	(200)	238	4.1	8.2	409	518	60.1	9.4	4,989	0.3	34.4
Feb.	313		287	4.1	8.2	785	806	60.4	9.3	5,160	0.1	34.5

** Preliminary readings on nonfarm payrolls shown in parenthesis*
Source: Bureau of Labor Statistics

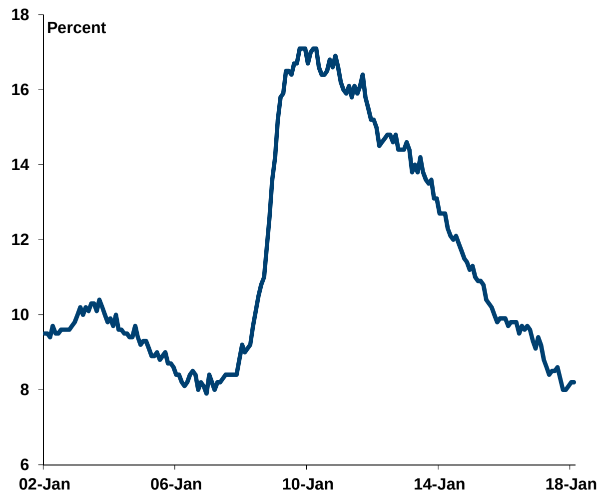
While most aspects of the February employment report were robust, the change in average hourly earnings was mildly disappointing with an increase of 0.1 percent (a touch firmer if rounded with more precision -- 0.1498 percent -- but still soft). The latest change left year-over-year growth at 2.6 percent, still within the recent range but down from 2.8 percent in the prior month. The increase in average hourly earnings for production workers only (i.e. excluding supervisors and managers) was firmer at 0.3 percent (0.269 percent), which pulled the year-over-year change one tick higher to 2.5 percent. The year-over-year change, while up, was still a touch below the cyclical high of 2.7 percent.

The Labor Market: Effectively at Full Employment

Many observers have argued in the past few years that the traditional unemployment rate was presenting a misleading picture of labor market conditions. As the jobless rate approached and breached most estimates of full employment (usually in the neighborhood of 4.5 percent), commentators noted that labor resources were available in the form of involuntary part-time employment and in the large number of potential workers who had dropped out of the labor force during the recession. Those arguments are losing force.

The broadest measure of unemployment -- the so-called U-6 rate -- captures most of the shadow slack in the labor market, and it is now in the low portion of the range evident before the recession (chart). This measure includes the number of unemployed captured by the traditional unemployment rate along with the number of involuntary part-time workers and the number of individuals marginally attached to the labor force (i.e. workers who would like a job and have searched in the past year, but have not looked actively in the past month). Both of these added components are now within their prerecession ranges.

Broad Unemployment Rate (U6)*

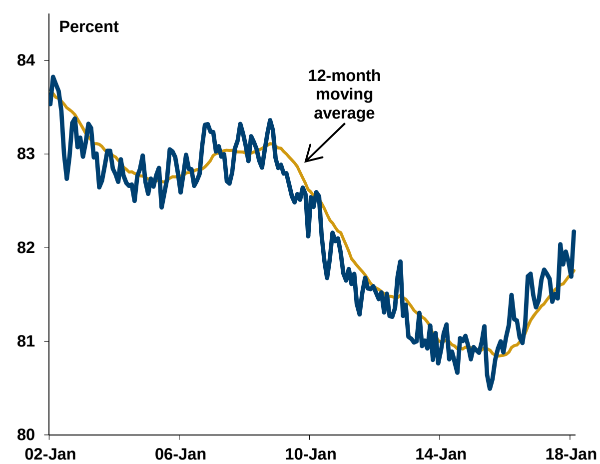


* The broad unemployment rate includes total unemployment plus all marginally attached workers (those who would like a job but are not actively searching) plus those employed part time for economic reasons; measured as a share of the civilian labor force plus marginally attached workers.

Source: Bureau of Labor Statistics

The number of involuntary part-time workers would probably be even lower than current readings if it were not for a structural change in the labor market. The total number of involuntary part-timers consists of two components: individuals whose hours were reduced because of slack work, and individuals who could not find full-time employment. The component associated with slack work is quite low, while the number of workers that could not find full-time employment is still above the prerecession range. We suspect that the elevated reading on the latter component is associated with businesses limiting the number of full-time positions to avoid the health-care mandates of the Affordable Care Act (Obamacare). Were it not for this structural change, the number of involuntary part-time workers would probably be minimal.

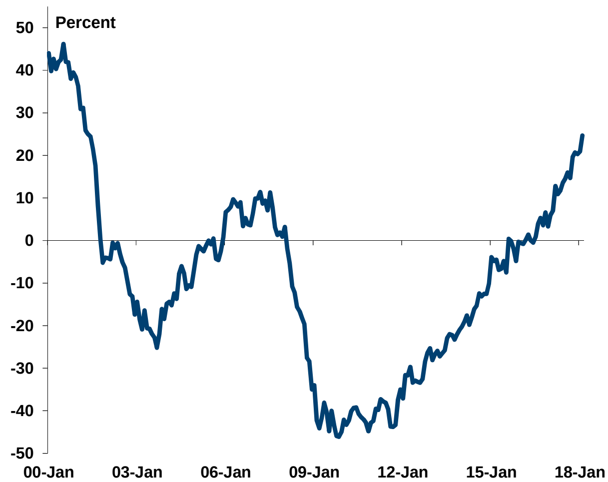
Labor-Force Participation, Prime-Age Workers*



* Labor-force participants aged 25 to 54 as a share of the civilian noninstitutional population aged 25 to 54.

Source: Bureau of Labor Statistics

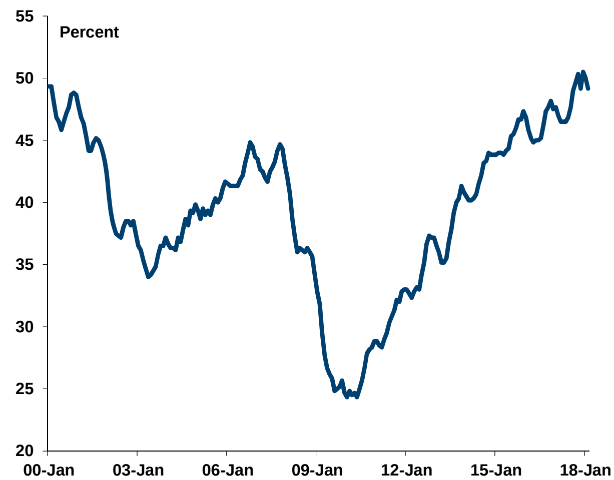
Labor Market Differential*



** The share of individuals reporting that jobs are plentiful less the share indicating that jobs are hard to get.*

Source: The Conference Board

NFIB: Few or No Qualified Applicants*



** The chart shows a six-month moving average of monthly data. The NFIB did not have observations for January and February 2009. The chart used straight-line interpolation from December 2008 to March 2009 as estimates for these missing months.*

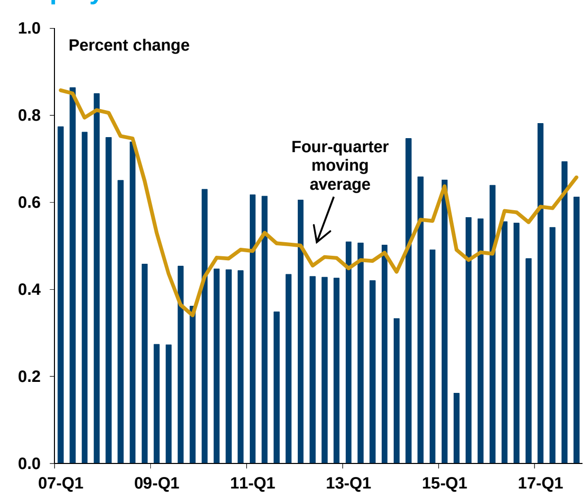
Source: National Federation of Independent Business

Some might still argue that individuals that have dropped out of the labor force could return in the future. That has occurred to a degree thus far, as the labor force participation rate for prime-aged individuals has increased 0.8 percentage point from the low in 2015 (chart prior page, based on 12-month moving average). Additional increases could emerge in coming months and quarters, as the current participation rate is still 1.5 percentage points below the prerecession level. The February reading was quite strong, but as evident on the graph, the figures change considerably from month-to-month.

However, we would not look for a pronounced increase, as the labor market is already firm enough to lure most of those interested in working. Potential workers seem to perceive that the labor market is firm and therefore opportunities are available. The Conference Board's survey of consumers has shown a marked pickup in perceptions of the labor market, as the share of individuals indicating that jobs are plentiful has climbed while the share indicating that jobs are hard to get has eased. The net reading (plentiful less hard to get) has climbed above the peak from the previous expansion (chart, above left). If individuals were inclined to reenter the labor force, they most likely would have done so by now.

We suspect that many individuals have dropped out of the labor force, and are not likely to return, because of a skills gap. Many jobs today have a large tech-related element, and some individuals do not have the necessary backgrounds. The lack of skills for today's labor market is evident in the survey conducted by the National Federation of Independent Business, which shows an elevated reading on the share of firms seeing few or no qualified workers for job openings (chart, above right). Of course, individuals could receive additional training and eventually reenter the labor force, but this process will occur slowly.

Employment Cost Index



Source: Bureau of Labor Statistics

A final argument for the existence of slack in the labor market is the absence of upward pressure on wages. If the economy were at full employment, the argument goes, wages would be accelerating. We believe that compensation growth is beginning to pickup. The growth of average hourly earnings from the employment report was bouncing around two percent in the early years of the expansion, but has fluctuated in a range of roughly 2.5 to 2.8 percent in the past two years (year-over-year growth of 2.6 percent in February). A better measure of labor compensation -- the employment cost index -- has registered a similar pattern, moving from a range centered on two percent during most of the expansion to 2.7 percent in the fourth quarter (chart, prior page).

We also were struck by a comment from the minutes of a recent FOMC meeting that firms were offering nonpecuniary compensation to workers, such as flexible hours and training opportunities. These items are valuable to many workers, and are a reflection of tight labor markets, but they most likely are not being picked up by wage and compensation measures.

Some of the observers arguing for the existence of slack in the past were Fed officials. Now, most seem to have come to the view that the labor market is fully employed, as the latest report on monetary policy that accompanied Chairman Powell's testimony noted: "the labor market in early 2018 appears to be near or a little beyond full employment."

The shift in views among Fed officials has perhaps been most pronounced for Governor Lael Brainard, one of the most dovish members of the FOMC. The title of her latest speech suggested a move in the hawkish direction (Navigating Monetary Policy as Headwinds Shift to Tailwinds), while the text revealed a marked shift in position. She noted several factors that had brightened the economic outlook: a pickup in economic growth abroad, a softening in the foreign exchange value of the dollar, an acceleration in business investment, and most important, an easing in fiscal policy through large tax cuts and generous spending provisions. Governor Brainard, who had previously urged caution in normalizing policy, now indicated that "continued gradual increases in the federal funds rate are likely to be appropriate."

Review

Week of March 5, 2018	Actual	Consensus	Comments
ISM Nonmanufacturing Index (February)	**59.5% (-0.4 Pct. Pt.)**	**59.0% (-0.9 Pct. Pt.)**	The decline in the ISM nonmanufacturing index was entirely the result of a drop of 6.6 percentage points in the employment component, which represented a return to the normal range after an unusually high reading in January (i.e. statistical noise). The new orders index rose 2.1 percentage points from an already elevated level, moving to 64.8%, which was the best of the current expansion and the fourth best in the history of the series. With orders firm, business activity was well maintained, with this index increasing 3.0 percentage points to 62.8%, a reading in the upper portion of the recent range.
Factory Orders (January)	**-1.4%**	**-1.4%**	The decline in factory orders occurred entirely in the durable component (-3.6%) and largely reflected a retreat of 32.9% in the volatile aircraft component. Durable orders ex-transportation dipped 0.3%, but the shift represented only a minuscule offset to the solid gains registered in the second half of last year. Orders for nondurable goods rose 0.8%. Most of the advance occurred in the petroleum and coal category (3.5%) where higher prices undoubtedly played a role, but nondurable orders ex-petroleum also had an influence (up 0.2%). The increase ex-petroleum marked the fifth consecutive increase and the 10th gain in the past 12 months, leaving a firm trend.
Revised Nonfarm Productivity (2017-Q4)	**0.0% (0.1 Pct. Pt. Rev.)**	**-0.1% (Unrevised)**	Output and hours worked changed only modestly from initially reported results, leaving almost no change from the first-reported tally on productivity growth in Q4. For the year, productivity advanced 1.2% -- faster than the flat reading in 2016, but still lagging relative to long-run historical standards. Unit labor costs were revised higher by 0.5 percentage point (2.5% versus 2.0%), as compensation per hour rose at a faster pace than first reported (2.4% versus 1.8%).
Trade Balance (January)	**-$56.6 Billion ($2.7 Billion Wider Deficit)**	**-$55.0 Billion ($1.9 Billion Wider Deficit)**	Imports were unchanged in January after robust growth in the prior four months, while slippage of 1.3% in exports followed solid advances in November and December and led to a widening in the monthly trade deficit. The January results raise the prospect of a drag from net exports on GDP growth. If trade in February and March match the January results, net exports would subtract approximately ¾ percentage point from GDP growth.

Review Continued

Week of March 5, 2018	Actual	Consensus	Comments
Payroll Employment (February)	**313,000**	**205,000**	A surge in nonfarm payrolls in February was joined by upward revisions of 54,000 in the prior two months. The gain was broad-based, with construction employment posting its best gain of the current expansion and financial services matching its best advance. The retail trade and manufacturing sectors also were strong. Average hourly earnings rose 0.1% (0.1498%, almost rounding up to 0.2%). The year-over-year advance of 2.6% slipped two ticks from the January reading, but it remained within the recent range. The unemployment rate held steady at 4.1%, but the reading masked strong results for both employment as measured by the household survey and the size of the labor force (up 785,000 and 806,000, respectively).

Source: Institute for Supply Management (ISM Nonmanufacturing Index); U.S. Census Bureau (Factory Orders); Bureau of Labor Statistics (Revised Nonfarm Productivity, Payroll Employment); Bureau of Economic Analysis (Trade Balance); Consensus forecasts are from Bloomberg

Preview

Week of March 12, 2018	Projected	Comments
Federal Budget (February) (Monday)	**$215 Billion Deficit**	With businesses beginning to reduce withholding from paychecks because of the Tax Cut and Jobs Act, revenues are likely to decline on a year-over-year basis. Outlays are likely to exceed the underlying average because February tends to be a heavy month for the payment of refundable tax credits. The budget deficit tends to be wide in February, and available data again suggest that this is the case in 2018, with the shortfall likely to exceed the average of $192 billion in the prior three years.
CPI (February) (Tuesday)	**0.2% Total, 0.2% Core**	Gasoline prices rose slightly in February, but the seasonal adjustment process will probably translate that change into a slight decrease. Core prices will probably increase by less than the 0.3% jump in January, but with the economy firm, the increase will probably exceed the 0.1% registered in several months last year.
Retail Sales (February) (Wednesday)	**0.3% Total, 0.4% Ex. Autos**	A drop in sales of new motor vehicles is likely to constrain the headline number, but rebounds in other areas after two slow months should lead to respectable results elsewhere.
PPI (February) (Wednesday)	**0.2% Total, 0.2% Core**	Gasoline prices rose in February, but the change was about in line with the normal seasonal movement, and thus the energy component of the PPI should be tame. Food prices have been well contained in recent months. Core goods prices are advancing at a firm pace (up 0.2% or 0.3% for six consecutive months), and the favorable economic performance is likely to keep them on this track. Service prices often provide surprises. They were about on trend in January, and thus could tilt in either direction in February.
Housing Starts (February) (Friday)	**1.270 Million (-4.2%)**	The index of buyer traffic is elevated, as is the sentiment index of home builders, which should translate to a gain in single-family construction. However, multi-family activity is likely to cool after a surprising burst in January, pulling total starts lower.
Industrial Production (February) (Friday)	**0.4%**	An increase in factory payrolls and an elevated reading on the ISM production index suggest that the manufacturing component of IP registered a robust gain. A pickup in the rotary rig count raises the possibility of a rebound in mining activity after declining in the prior two months. Utility output is likely to decline, as the number of heating days was far below the average (2.5 standard deviations below).

Source: *Forecasts provided by Daiwa Capital Markets America*

Economic Indicators

March 2018

Monday 5

ISM NON-MFG INDEX

	Index	Prices
Dec	56.0	59.9
Jan	59.9	61.9
Feb	59.5	61.0

Tuesday 6

FACTORY ORDERS

Nov	1.7%
Dec	1.8%
Jan	-1.4%

Wednesday 7

ADP EMPLOYMENT REPORT

	Private Payrolls
Dec	249,000
Jan	244,000
Feb	235,000

REVISED PRODUCTIVITY & COSTS

	Productivity	Unit Labor Costs
17-Q3	2.6%	1.0%
17-Q4(p)	-0.1%	2.0%
17-Q4(r)	0.0%	2.5%

TRADE BALANCE

Nov	-$50.9 billion
Dec	-$53.9 billion
Jan	-$56.6 billion

BEIGE BOOK

"Economic activity expanded at a modest to moderate pace across the 12 Federal Reserve Districts in January and February."

CONSUMER CREDIT

Nov	$30.9 billion
Dec	$19.2 billion
Jan	$13.9 billion

Thursday 8

INITIAL CLAIMS

Feb 17	220,000
Feb 24	210,000
Mar 03	231,000

Friday 9

EMPLOYMENT REPORT

	Payrolls	Un. Rate
Dec	175,000	4.1%
Jan	239,000	4.1%
Feb	313,000	4.1%

WHOLESALE TRADE

	Inventories	Sales
Nov	0.6%	1.9%
Dec	0.7%	0.8%
Jan	0.8%	-1.1%

Monday 12

FEDERAL BUDGET (2:00)

	FY2018	FY2017
Dec	-$23.2B	-$27.3B
Jan	$49.2B	$51.3B
Feb	**-$215.0B**	-$192.0B

Tuesday 13

NFIB SMALL BUSINESS OPTIMISM INDEX (6:00)

Dec	104.9
Jan	106.9
Feb	--

CPI (8:30)

	Headline	Core
Dec	0.2%	0.2%
Jan	0.5%	0.3%
Feb	**0.2%**	**0.2%**

Wednesday 14

RETAIL SALES (8:30)

	Total	Ex.Autos
Dec	0.0%	0.1%
Jan	-0.3%	0.0%
Feb	**0.3%**	**0.4%**

PPI (8:30)

	Final Demand	Core
Dec	0.0%	-0.1%
Jan	0.4%	0.4%
Feb	**0.2%**	**0.2%**

BUSINESS INVENTORIES (10:00)

	Inventories	Sales
Nov	0.4%	1.4%
Dec	0.5%	0.5%
Jan	**0.6%**	**-0.3%**

Thursday 15

INITIAL CLAIMS (8:30)

IMPORT/EXPORT PRICES (8:30)

	Non-fuel Imports	Nonagri. Exports
Dec	-0.1%	0.1%
Jan	0.4%	0.9%
Feb	--	--

EMPIRE MFG (8:30)

Jan	17.7
Feb	13.1
Mar	--

PHILLY FED INDEX (8:30)

Jan	22.2
Feb	25.8
Mar	--

NAHB HOUSING INDEX (10:00)

Jan	72
Feb	72
Mar	--

TIC DATA (4:00)

	Total	Net L-T
Nov	$33.5B	$57.5B
Dec	-$119.3B	$27.3B
Jan	--	--

Friday 16

HOUSING STARTS (8:30)

Dec	1.209 million
Jan	1.326 million
Feb	**1.270 million**

IP & CAP-U (9:15)

	IP	Cap.Util.
Dec	0.4%	77.7%
Jan	-0.1%	77.5%
Feb	**0.4%**	**77.7%**

JOLTS DATA (10:00)

	Openings (000)	Quit Rate
Nov	5,978	2.1%
Dec	5,811	2.2%
Jan	--	--

CONSUMER SENTIMENT (10:00)

Jan	95.7
Feb	99.7
Mar	**99.0**

Monday 19

Tuesday 20

FOMC MEETING

Wednesday 21

CURRENT ACCOUNT

EXISTING HOME SALES

FOMC DECISION

POWELL PRESS CONFERENCE

Thursday 22

INITIAL CLAIMS

FHFA HOME PRICE INDEX

LEADING INDICATORS

Friday 23

DURABLE GOODS ORDERS

NEW HOME SALES

Monday 26

CHICAGO FED NAT'L ACTIVITY INDEX

Tuesday 27

S&P CORELOGIC CASE-SHILLER HOME PRICE INDEX

CONSUMER CONFIDENCE

Wednesday 28

REVISED GDP

U.S. INTERNATIONAL TRADE IN GOODS

ADVANCE INVENTORIES

PENDING HOME SALES

Thursday 29

INITIAL CLAIMS

PERSONAL INCOME, CONSUMPTION, PRICE INDEXES

CHICAGO PURCHASING MANAGERS' INDEX

REVISED CONSUMER SENTIMENT

Friday 30

GOOD FRIDAY

Forecasts in Bold (p) = preliminary; (r) = revised

Treasury Financing

March 2018

Monday	Tuesday	Wednesday	Thursday	Friday
5	6	7	8	9
AUCTION RESULTS: Rate / Cover 3-mo bills 1.660% 3.26 6-mo bills 1.830% 3.19 **ANNOUNCE:** $65 billion 4-week bills for auction on March 6	**AUCTION RESULTS:** Rate / Cover 4-week bills 1.550% 3.01		**ANNOUNCE:** $96 billion 13-,26-week bills for auction on March 12 $28 billion 3-year notes for auction on March 12 $21 billion 10-year notes for auction on March 12 $13 billion 30-year bonds for auction on March 13 **SETTLE:** $96 billion 13-,26-week bills $65 billion 4-week bills	
12	13	14	15	16
AUCTION: $96 billion 13-,26-week bills $28 billion 3-year notes $21 billion 10-year notes **ANNOUNCE:** $65 billion* 4-week bills for auction on March 13	**AUCTION:** $65 billion* 4-week bills $13 billion 30-year bonds		**ANNOUNCE:** $96 billion* 13-,26-week bills for auction on March 19 $11 billion* 10-year TIPS for auction on March 22 **SETTLE:** $96 billion 13-,26-week bills $65 billion* 4-week bills $28 billion 3-year notes $21 billion 10-year notes $13 billion 30-year bonds	
19	20	21	22	23
AUCTION: $96 billion* 13-,26-week bills **ANNOUNCE:** $65 billion* 4-week bills for auction on March 20	**AUCTION:** $65 billion* 4-week bills		**AUCTION:** $11 billion* 10-year TIPS **ANNOUNCE:** $96 billion* 13-,26-week bills for auction on March 26 $22 billion* 52-week bills for auction on March 27 $15 billion* 2-year FRNs for auction on March 28 $30 billion* 2-year notes for auction on March 26 $35 billion* 5-year notes for auction on March 27 $29 billion* 7-year notes for auction on March 28 **SETTLE:** $96 billion* 13-,26-week bills $65 billion* 4-week bills	
26	27	28	29	30
AUCTION: $96 billion* 13-,26-week bills $30 billion* 2-year notes **ANNOUNCE:** $65 billion* 4-week bills for auction on March 27	**AUCTION:** $65 billion* 4-week bills $22 billion* 52-week bills $35 billion* 5-year notes	**AUCTION:** $15 billion* 2-year FRNs $29 billion* 7-year notes	**ANNOUNCE:** $96 billion* 13-,26-week bills for auction on April 2 **SETTLE:** $96 billion* 13-,26-week bills $65 billion* 4-week bills $22 billion* 52-week bills $11 billion* 10-year TIPS	***GOOD FRIDAY***

**Estimate*