aegon asset management

Macro Perspective
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AEGON **INSIGHTS**

The Fed's job just got easier

Friday's payroll data turns down the heat on the raucous monetary policy debates likely occurring in the inner sanctum of the Eccles building (the Washington, D.C. home of the interest-rate-setting Federal Open Markets Committee).

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Frank Rybinski, CFA, is head of macro strategy responsible for guiding the firm's global macroeconomic view as it pertains to tactical and strategic asset allocation. This includes analysis of the economy, interest rates, and the relative value between asset classes. In this capacity, Frank frequently appears in leading financial media outlets like Bloomberg, CNBC, Fox Business and the Wall Street Journal. Prior to his current role, Frank was a credit strategist for UBS Investment Bank. Prior to that, he worked as an analyst for ZT Zurich Trust in Zurich, Switzerland. Frank began his career as a trader for Spear, Leeds & Kellogg and held a similar position at The Royal Bank of Scotland. He has been in the industry since 1996 and started with the firm in 2008. Frank received his BA in economics from Boston College. He is a CFA® charterholder.

We've used the analogy that the Federal Reserve has the 50-basis-point (bps) torpedo tubes flooded, so that it can quickly respond with another 50-bps cut if needed. The latest payroll data likely lowers the Defcon level—but doesn't make the central bankers drain the torpedo tubes just yet.

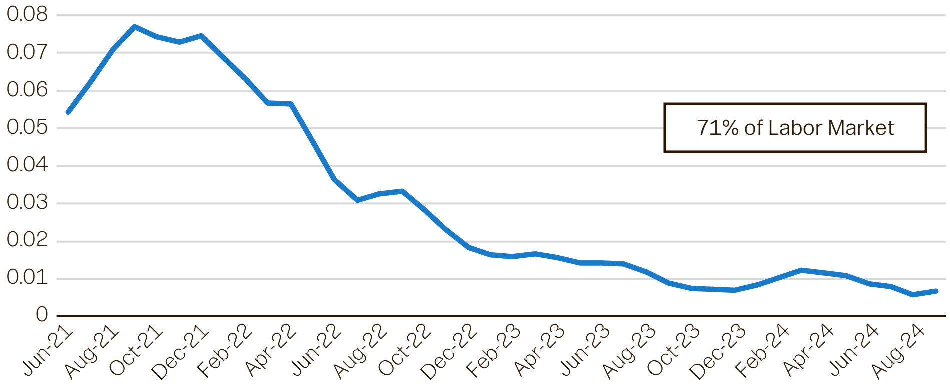
In short, this is exactly why the Fed loves to have optionality with regard to its policy function.

So, what's all the fuss about?

September's monthly payroll data came in at a very solid 254,000 jobs added to the US economy In addition, the job gains for July and August were revised higher by a combined 72,000.

A deeper dive into those numbers shows that private payrolls rose by 223,000. While the non-cyclical health-care sector continues to outperform other sectors, there was an impressive jump in private ex-health-care jobs (which comprise 71% of labor force), where the number of jobs rose 151,000 in September. That's nearly twice the recent run-rate. Naturally, the question now becomes how sustainable is this pace?

Private payroll growth, excluding health care
3-month annualized return



Sources: US Bureau of Labor Statistics, Haver Analytics. Data as of October 2024.

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Meanwhile, the household survey reflected strong employment trends as well. The employment gains of 430,000, coupled with a labor force that only grew by 150,000 workers, pushed the widely watched U-3 unemployment rate down to 4.05% in September (from 4.22% in August).

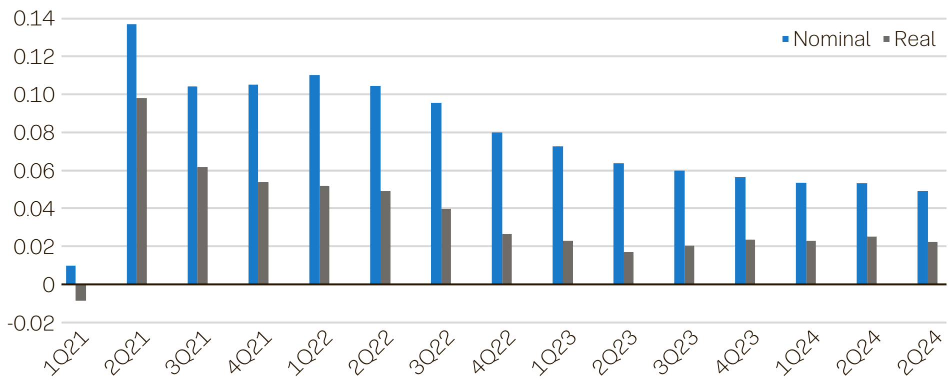
Average hourly earnings (AHE) jumped 37 bps. While this fueled fears of an acceleration in wage growth (and inflation), we are less concerned at this point since the gain was largely due to a drop in weekly hours worked to an unsustainably low level of 34.2.

The AHE reading can also be skewed by compositional effects, which is why we much prefer the labor income proxy (LIP) measurement. In our opinion, the LIP is the best representation of the aggregate amount of firepower the consumer has since it represents the aggregate wage growth of the economy. (It factors in how many people are working, how long they work and what their wages are). While the LIP can be volatile month to month, the quarterly numbers and moving averages are very telling:

- The third-quarter 2024 nominal LIP showed its 10th straight quarterly moderation and its first print below 5% on a year-over-year basis. That dovetails with our overarching macro narrative of an economy that is cooling, but not collapsing.
- The LIP is a nominal number, so we deflate it to see what the consumer's spending fuel tank looks like in real terms. In that regard, it continues to grow in the low 2% range, which is consistent with a moderate—but not excessive—level of consumer spending.

Quarterly labor income proxy

Year-over-year % change



Sources: US Bureau of Labor Statistics, Haver Analytics. Data as of October 2024..

Overall, the September payroll data was strong, but it remains to be seen whether the pace will be sustainable over the long term. Nonetheless, the latest numbers do lower the risk of a negative acceleration pushing the economy into a recession and also make the Fed's job at its November meeting easier. On that front, it's encouraging that the key LIP reading continues to show moderating trends but is still supportive of decent consumer spending growth.

So, in all, nothing in the latest labor data reduces the Fed's intention to cut the fed-funds rate 25 bps at its next meeting. But it does raise the bar much higher for a 50-bps cut.

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