

December 9, 2024

Labor Data Confirm Rate Cuts in US, Canada

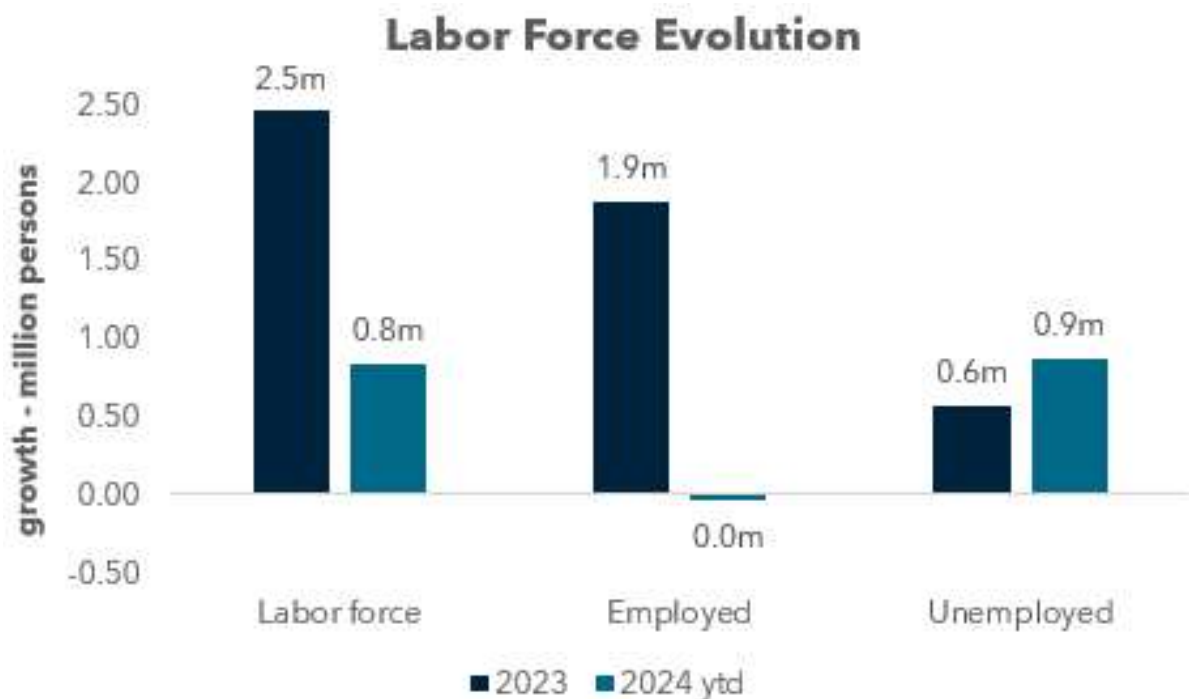
- Although the US establishment survey showed improvement, the household survey showed deterioration
- We are highly convinced on a 25bp rate cut next week from the Fed
- A rising unemployment rate and falling industrial capacity utilization point to a 50bp cut in Canada this week

It was a tale of two surveys in last week's jobs report. The good news was found in the establishment survey, which saw an impressive and above-consensus 227k jobs created, suggesting a strong rebound in job creation after the hurricane- and strike-affected report for October. More concerning developments in the household survey showed that the number of unemployed rose, the number of employed persons fell, and the unemployment rate nudged up one-tenth of a percent to 4.2%. While the report doesn't show that the labor market is weakening significantly or quickly, it does support our view for a 25bp cut next week from the FOMC.

Turning to the household survey, we note that for the second straight month, the number of unemployed workers rose by 161k (after an increase of 150k in October), while the number of employed persons fell by 355k, the second straight month where this figure topped 300k. The unemployment rate rose to 4.2%, defying expectations (which saw it remaining stable at 4.1%). To add to the concern, all this happened despite a slight decline in labor force participation, down from 62.6% to 62.5%. Typically, falling participation indicates a stable or declining unemployment rate, unlike what occurred this month.

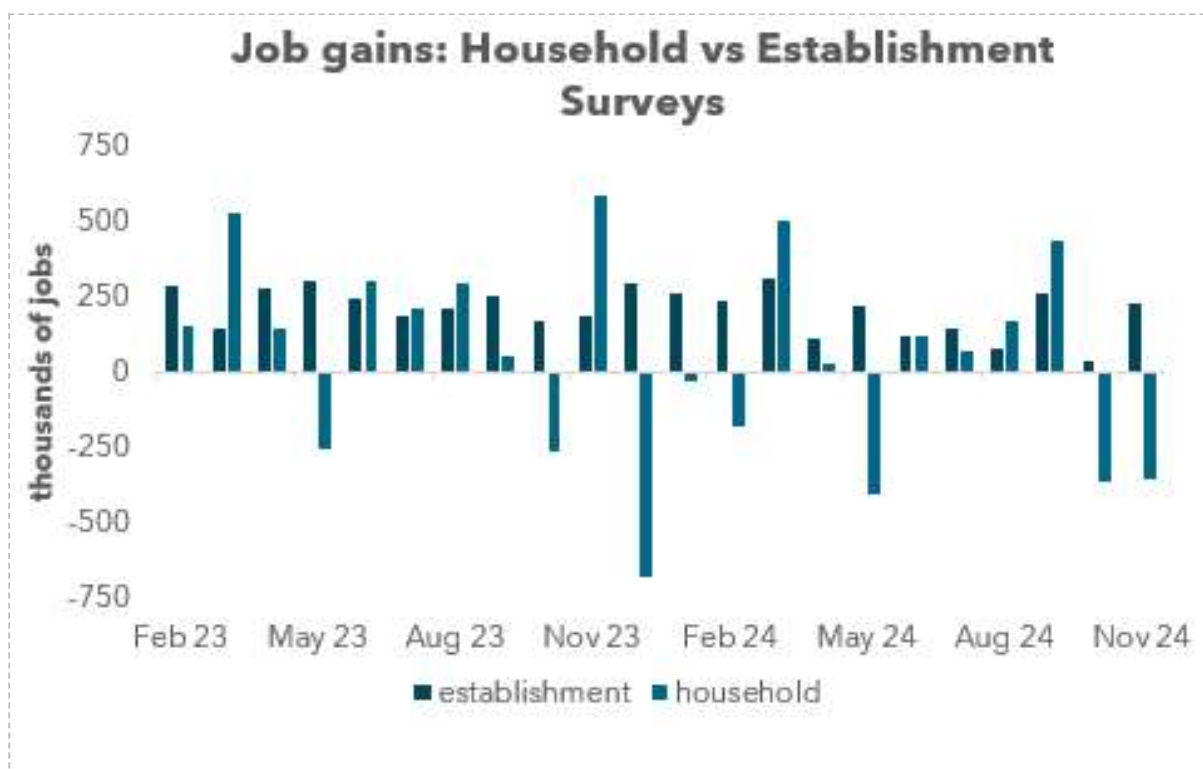
All told, 2024 hasn't been a banner year for the household survey. The level of employment has actually fallen slightly since the end of last year, by around 40k. New entrants to the labor market have been mostly unable to find work right away. All told, as Exhibit #1 shows, approximately 900k people have lost their jobs year-to-date. This year's labor market evolution contrasts markedly from 2023, a period where tight – and getting tighter – labor markets prevailed, keeping the Fed on a tightening bias. Exhibit #2 shows the monthly increases in employment produced by each survey, and we can see that the household survey has generally been running weaker over the last six months or so.

Exhibit #1: No Employment Growth in 2024



Source: BNY Markets, Bureau of Labor Statistics

Exhibit #2: A Tale of Two Labor Surveys



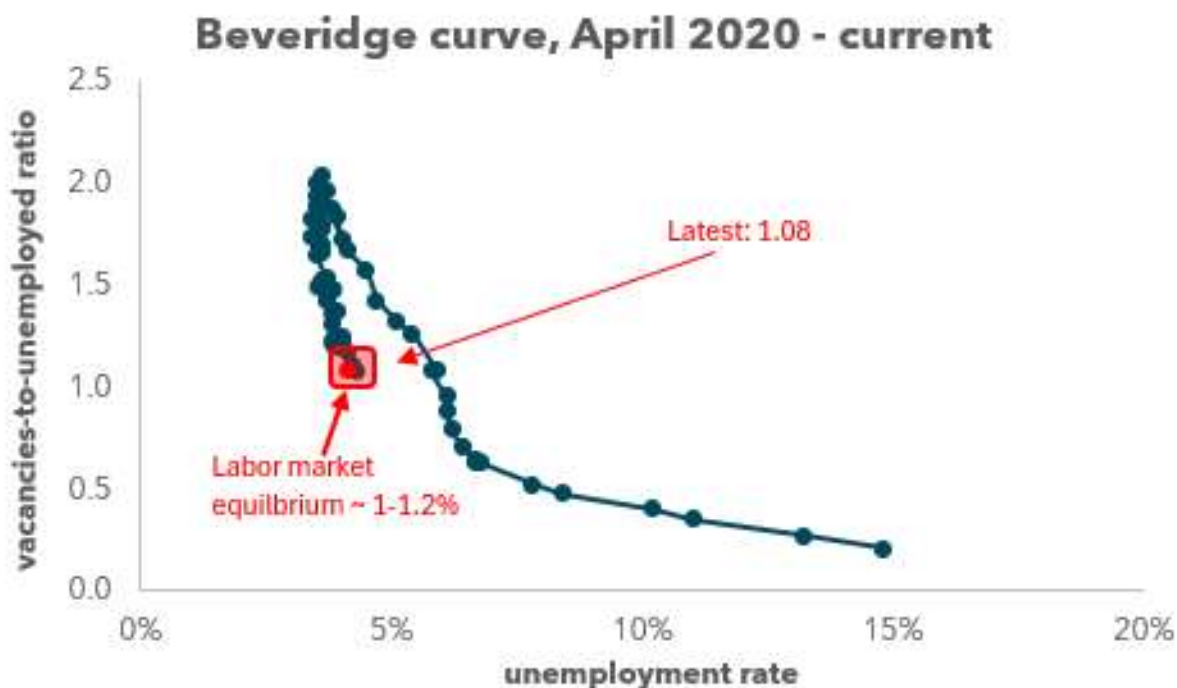
Source: BNY Markets, Bureau of Labor Statistics

This is not to claim that the job market is collapsing – far from it. An unemployment rate of 4.2% is hardly concerning, and if we were to examine just the prime-age portion of the labor force (workers between 25 and 54 years old), the unemployment rate remains at a historically low 3.7%. Nevertheless, it is loosening, although we – like the Fed – reckon it is in equilibrium.

From the JOLTS survey earlier in the week last week, we calculate a vacancies-to-unemployment ratio of just under 1.1. There is about one open job for every unemployed worker. We plot the relationship of this ratio to the unemployment rate (known as the Beveridge curve) in Exhibit #3 and note that for most of 2022 this ratio was near 2. The unemployment rate has risen only slightly in that time, indicating a “steep” Beveridge curve, and the ability of the economy to move to labor market equilibrium without a major increase in the unemployment rate.

All of this adds up to a rate cut next week in our eyes. Markets interpreted the Friday data as dovish, and the OIS curve sees an approximately 86% chance of such a move at the next meeting. Compared to the day before the labor report (70%), this a fairly big increase in the market's view of further policy easing. We'll preview the FOMC meeting next week, but for now, the rate cut looks assured (pending CPI data later this week), but the 2025 policy path remains murky.

Exhibit #3: Beveridge Curve Shows Labor Market Equilibrium Has Been Reached



Source: BNY Markets, Bureau of Labor Statistics

We also expect a rate cut from the Bank of Canada on Wednesday this week – another 50bp cut, matching the move from late October. We first posted our BoC view two weeks ago (see [here](#)), and in that write-up we concentrated on the behavior of inflation, which we still reckon is moving in the right direction in the Bank's view.

Friday's labor market data adds to our conviction on a half-point cut. Even though employment increased by an above-consensus 50.5k (versus expectations of just 25k), the unemployment rate moved up significantly, from 6.5% to 6.8%. Labor participation also increased from 64.8% to 65.1%. These data suggest that Bank is correct to claim that the Canadian economy is operating with excess capacity, indicating that policy rates need to come down.

While the Friday data indicate that the labor market is too loose, other data show the move to overcapacity in recent months in the industrial sector. Exhibit #4 shows a measure of capacity utilization in Canada going back to the turn of the century, and we can see a general decline in this measure since the pandemic ended. We also can see that the Bank of Canada responds to declining utilization by lower rates, as it had in in 2014-15. Of course, rates also fell as capacity utilization dropped in 2008-09 (GFC) and 2020 (Covid).

To us, this suggests a weaker Canadian dollar ahead, something we also argued in favor of in our note from two weeks ago. As we said then, a recent trip to Montreal in mid-November provided us with a stark view of pessimism over the economy and subsequently the currency.

We don't think data in the intervening weeks will have changed that bearish local sentiment – which we share – and see USD/CAD moving higher into the mid-140s before too long.

Exhibit #4: Excess Capacity Leads to Rate Cuts



Source: BNY Markets, Statistics Canada

Please direct questions or comments to: iFlow@bny.com

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