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ECONOMIC TALKING POINTS

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Can job growth accelerate much more when the economy is losing steam?

It is quite extraordinary when you think about it. Washington has used virtually every tool in its arsenal to bolster economic growth. The actions taken so far have been unprecedented both in number and magnitude.

---- Never before have we had more than two years of near zero short-term interest rates from the Federal Reserve.
---- Never before have we seen the Fed pump such massive reserves into the financial system through its two tranches of quantitative easing.
---- Never before have we had such huge amounts of fiscal stimulus to fuel consumer and business spending.
---- Last, but certainly not least, the collapse of US interest rates has driven the value of the US dollar to its lowest since 2008, a depreciation that that should boost exports and add to GDP growth.

And yet….what has all this actually achieved?

Well, in terms of actual output, appallingly little. Washington spent a lot of bucks to evoke a bang that is only discernable with the help of a hearing aid. The economy managed to sweat out a microbic 1.8% growth rate in the first quarter (which Bernanke incredibly labeled as "moderate"). But let's not quibble about a single quarter. Over the last four quarters, GDP expanded by 2.3%, the meekest 12-month performance since the end of 2009.

We also received evidence the weakness in the first quarter has now spilled into the current quarter too.

- Manufacturing activity in April grew last month at the slowest pace of the year, according to the Institute for Supply Management. New orders eased back to a level we haven't seen since last November.

- More disconcerting is the ISM's report on service activity, which makes up nearly 90% of US GDP. It dropped to its slowest pace in 8 months. Most stunning was the historic plunge in new orders, a harbinger of future output and employment. It fell in April by the most EVER RECORDED!

- Yesterday, the BLS reported new applications for unemployment benefits shot up by 43,000 to 474,000 in the final week of April. That's the largest number of filings since last summer! It's even higher than the equivalent week of a year ago!

- And let's not forget the other worrisome report (by the National Federation of Independent Business) out in April showing that small and midsize businesses may slow future hiring. Why? Because their confidence in the economic outlook just plummeted to the lowest point since last October. As a consequence, the percentage of those planning to add workers in the next three months dropped to a four-month low.

Today's perplexing job report

So we have to ask the obvious follow-up question. Where is the incentive to ramp up hiring when all signs point to future lackluster growth? After all, if the US economy can already successfully produce more goods and services than ever before ---- and do so with 7 million fewer workers, what then is the justification to swell payrolls when analysts and corporate leaders warn of a pending slowdown in consumer and business spending?

And yet April's employment report show employers gleefully hired last month in numbers normally seen with much more robust economic growth. Despite a plethora of economic indicators showing a *deceleration* in business activity, the rise in nonfarm payrolls accelerated to 244,000 last month, after climbing by 221,000 in March and 68,000 in January. Private payrolls moved in tandem, shooting up 268,000 in April, after a 231,000 rise in March and 94,000 at the start of the year.

But before anyone starts to uncork Champaign bottles, lets put some of these numbers in perspective. Unless the pace of economic activity manifestly increases, the payroll numbers we saw for March and April are simply unsustainable. It will not be the first time we witnessed employment trends do a sudden u-turn. (A year ago, nonfarm payrolls climbed by 277,000 in April 2010, and then from June thru September the numbers all went negative.)

At best, this is a very self-contradictory report. In the household survey, the number of Americans who were employed fell by 190,000 last month. Another worrisome sign was the spike in those who found themselves out of work in just the last four weeks. That number jumped by 242,000, the largest one-month increase since October 2009. The newly unemployed now make up 20% of the jobless rate, the most since 2009. These are not stats you expect to see in an improving labor market.

If labor market conditions were getting better you would see ***fewer, not more,*** people feeling stuck with part time work. Yet, April's report showed that the number of Americans grudgingly accepting part time work because of a lack of full time opportunities shot up to 8.6 million, the highest of the year!

Certainly the top line unemployment rate went in the wrong direction, climbing to 9.0%, from 8.8%. So did the broader underemployment rate, which rose to 15.9%, from 15.7%. More revealing is that fewer Americans are even part of the workforce. The employment-population ratio actually dropped back to 58.4%, which is 0.3 percentage points lower than a year ago!

So we have to be cautious in how to interpret April's employment report. One must not place too much emphasis on a single economic indicator, especially when it belies an abundance of other credible and timely reports that portray a weakening economy.

Bottom line:

The decisions that go into hiring more workers rest on the expectation that the economy is turning up. But it is difficult to make the case that growth will accelerate enough to justify the current pace of hiring. You cannot have vibrant economy when Washington is planning to implement a major austerity program. You cannot have vibrant economy with the housing sector still in a comatose state. You cannot have vibrant economy when rising oil and gasoline prices serve as a punishing tax on consumers and businesses. You cannot have a vibrant economy when the cost of living races significantly ahead of personal income. You cannot have a healthy economy if the banks are still apprehensive about making loans to individuals and businesses. You cannot have a vibrant economy if virtually every country on the planet –except the US and the UK --- are raising interest rates to reign in growth, thereby putting US exports at risk.

The US recovery has thus lost considerable momentum since the start of the year and the headwinds have not diminished. Some forecasters even issued fresh warnings of a double dip recession. While we do not share that view, growth will remain well below the economy's non-inflationary potential, a subpar pace that will not be enough to sustain the latest pick up in hiring.
