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Surprisingly Strong Hiring Sends Bond Yields Higher

U.S. employers added more jobs than forecast last month, keeping door open for Fed rate increases

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Surging U.S. job growth shattered investors' expectations, the latest sign of accelerating economic momentum stoking a bond market selloff that is sending longer-term borrowing rates to new 16-year highs.

Employers added 336,000 jobs in September, the strongest gain since January and up sharply from the prior month's upwardly revised 227,000 gain, the Labor Department said Friday. Job growth was also stronger in July than previously estimated.

Bond and stock prices fell sharply after the jobs report's release, reflecting concerns that it would push the Federal Reserve to raise short-term interest rates as early as its Oct. 31-Nov. 1 meeting. Both markets later recovered, however.

The yield on the 10-year U.S. Treasury note settled Friday at 4.783%, according to Tradeweb, compared with nearly 4.88% just after the jobs report was released and 4.715% at Thursday's close. The S&P 500 jumped 1.2%.

U.S. financial markets were unusually jittery in the run-up to Friday's report. Investors have sold longer-dated government bonds in recent weeks because of signs of economic strength that make less likely the prospects of a recession and Fed rate cuts.

September's burst of hiring defied forecasters' expectations for a slowdown driven by high interest rates, elevated inflation, the resumption of student-loan repayments and rising oil prices. Instead, the employment figures suggest the economy gathered strength through the summer, fueled partly by brisk consumer spending.

"It was a blockbuster jobs report, but just as important was how well-rounded hiring was," said Robert Frick, corporate economist with Navy Federal Credit Union.

The Fed's job gets more complicated

For the Fed, the report keeps the door open to another rate increase this year but won't easily settle the debate. The figures could make some officials less confident that inflation's decline this summer will be sustained. But it also offered some signs of softening labor demand. "This is a blowout report, and it will have people thinking that the Fed may pull the trigger on another hike before year-end," said Omair Sharif, founder and president of Inflation Insights. At the same time, he said it was striking how pay growth in service-providing jobs such as the leisure-and-hospitality sector "seem to be cooling even with a strong labor market."

Average hourly earnings rose 3.4% in September on a three-month annualized basis—a pace in line with the Fed's 2% inflation target.

The run-up in yields, if sustained, would be a new risk for the economy by raising the cost of home mortgages, auto loans and business debt. The average 30-year fixed rate mortgage rose to 7.53% for the week ending Sept. 29, the highest since 2000, according to the Mortgage Bankers Association.

"The higher yields go from this point on, the tighter the noose gets around the economy," said **Bernard Baumohl, chief global economist at the Economic Outlook Group.**

Fed officials held their key interest rate steady at a 22-year high at their meeting last month. In new economic projections, most thought one more increase would be appropriate this year.

The Fed raises rates to influence borrowing costs, which slows economic activity to combat inflation. The surge in Treasury yields means market participants are effectively doing the work of the central bank in cooling the economy.

"If financial conditions, which have tightened considerably in the past 90 days, remain tight, the need for us to take further action is diminished," San Francisco Fed President Mary Daly said Thursday during remarks in New York.

The increase in yields since Fed officials' last meeting is equivalent to a quarter-percentage point rate increase in the Fed's short-term rate, she said. "So then the need to do tightening additionally is not there."

But the jobs report could lead others to argue at the next Fed meeting that another increase is warranted. Cleveland Fed President Loretta Mester told reporters this week that she would support raising rates on Nov. 1 “if the economy looks the way it did…at our recent meeting.”

Investors in interest-rate futures markets assigned a nearly 30% probability on Friday of a rate increase at the next meeting, according to CME Group, and a nearly 45% probability that the Fed would raise rates one more time by December. Those expectations were up only slightly compared with before the release of the report.

Some industries are still catching up from pandemic disruptions

The unemployment rate held steady last month at 3.8%, near a historical low.

Industries with unusually strong job gains included retail, construction and air transportation. Public education employment also jumped as schools got back in session.

September hiring also was solid at restaurants, hotels, and nursing and residential-care centers—all job sectors still filling vacancies left by the pandemic.

Employment at restaurants and bars finally returned to prepandemic levels last month. While notable, the gains still leave those businesses behind from where they would be without pandemic disruptions. Overall private-sector jobs are up 3.5% from February 2020, before the pandemic.

Several healthcare sectors remain below prepandemic staffing levels, including at nursing and assisted-living facilities.

An upswing in high-profile labor strikes this year reflects how workers are capitalizing on the still-tight labor market. This week, some 75,000 employees at Kaiser Permanente, one of the nation’s largest healthcare providers, walked off the job—the largest healthcare strike on record. As of August, the U.S. had lost more workdays to labor disputes than any full year since 2000.

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