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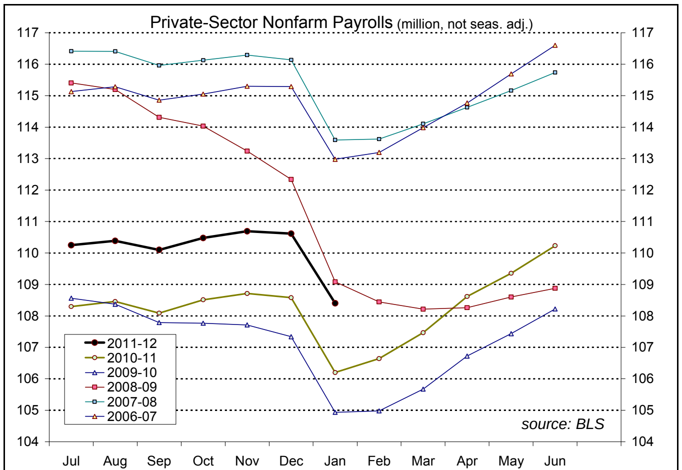
Weekly Market Monitor

The January Jobs Report

Nonfarm payrolls rose more than expected last month and the unemployment rate fell further. The report wasn't nearly as strong as it appears at first glance, but it was encouraging.

Recall that the Employment Report is composed of two separate surveys. The Household Survey, a telephone survey of 60,000 households, provides reasonably good estimates of ratios (labor force participation, the unemployment rate), but unreliable estimates of levels (the monthly number of employed individuals, for example). The Establishment Survey, which covers about 486,000 worksites, yields nonfarm payrolls, average weekly hours, and average hourly earnings.



Prior to seasonal adjustment, nonfarm payrolls fell by 2.689 million in January. Seasonal adjustment turned that into a 243,000 adjusted increase. In other words, we had fewer seasonal job losses than usual last month. Fewer jobs losses is a good thing, no doubt, but that's not the same as job gains. The bigger test for the job market will come in the spring. Unadjusted payrolls typically ramp up from February to June.

Monthly Change in Nonfarm Payrolls, selected sectors (BLS):

	unadjusted	adjusted
nonfarm payrolls, th.	-2689	+243
private sector	-2211	+257
construction	-281	+21
manufacturing	-62	+50
wholesale trade	-51.9	+14.0
retail trade	-592.1	+10.5
finance	-65	-5
temp help	-236.4	+20.1
leisure & hospitality	-289	+44
federal government	-25	-6
state & local gov't	-453	-8

The details of the Household Survey showed that 206,000 individuals were unable to work due to adverse weather during the survey week in January (the week that included the 12th of the month). That compares to an average of 425,000 over the five previous Januarys. This figure is not directly comparable to the payroll data (which come from the Establishment Survey), but it gives you an idea of the impact from January's mild weather.

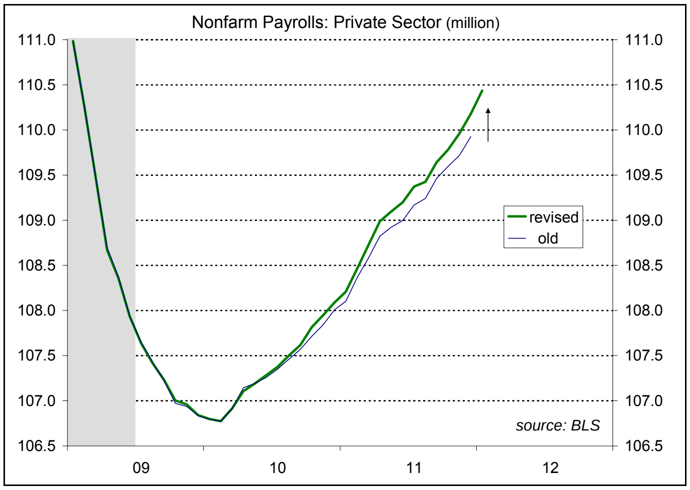
The unemployment rate fell to 8.3% in January, down from 8.5% in December, 9.1% a year ago, and a cycle peak of 10.0% in October 2009. However, the employment/population ratio held steady at 58.5%, the same level as when the unemployment rate peaked. Labor force participation fell in January, and has accounted for much of the improvement in the unemployment rate over the last two years. Labor force participation was expected to ebb as the baby-boom generation aged, but that's not what's happening. Rather, the rate for those aged 55 and over is trending higher, likely reflecting the impact of lower home prices (since many had counted on their homes being their chief retirement asset). In contrast, participation rates for younger workers have declined. This is the tragedy of the last few years. Unemployed workers are losing valuable job skills and young workers are not getting the job skills they would normally acquire if the economy were near full employment. The soft job market has resulted in a loss of output (relative to potential) over the last few years, but there is significant heartache for millions of people.

Make no mistake. The labor market is improving and there's hope for strong job growth this spring. Moreover, average weekly hours have been trending higher, consistent with an expected increase in new hiring in the months ahead. However, not to harsh your mellow, the January employment data were not as rosy as the headline figures would seem to suggest. These data should not change the picture for the Fed. We still have a lot of ground to make up in the labor market.

	Treasury Yields								Dollar				Equities		
	13-wk	26-wk	52-wk	2-yr	3-yr	5-yr	10-yr	30-yr	$/Euro	$/BP	JY/$	CD/$	NASD	SPX	DJIA
1/06/12	0.02	0.05	0.09	0.26	0.38	0.85	1.96	3.02	1.272	1.543	77.06	1.023	2674.22	1277.81	12359.92
1/27/12	0.05	0.08	0.10	0.22	0.31	0.75	1.89	3.06	1.319	1.572	76.68	1.001	2816.55	1316.33	12660.46
2/03/12	0.08	0.09	0.12	0.24	0.33	0.78	1.93	3.13	1.314	1.581	76.54	0.994	2905.66	1344.90	12862.23

Recent Economic Data and Outlook

The economic data were mixed. The January Employment Report was surprisingly strong, driving share prices higher, but the results were boosted by unusually mild weather.



Fed Chairman Bernanke testified that the recovery has been *"frustratingly slow"* and remains vulnerable to shocks. Asked whether the Fed's dual targeting system implies that the Fed will tolerate higher inflation in the short run to push the unemployment rate lower, Bernanke said that *"we are not seeking higher inflation, we do not want higher inflation, and we're not tolerating higher inflation."*

The January **Employment Report** was stronger than expected, but was supported by mild weather. Nonfarm payrolls rose by 243,000, and the two previous months were revised a net 60,000 higher. Prior to seasonal adjustment, payrolls fell by 2.689 million. Gains were widespread across industries, but mostly reflected lower-than-usual seasonal job losses. State and local government payrolls fell by 8,000, with federal down by 6,000. Annual benchmark revisions lifted the March 2011 level of payrolls by 162,000, a bit less than the 192,000 expected. The unemployment rate fell to 8.3% (8.263% before rounding), due largely to a drop in labor force participation (63.7%, vs. 64.0% in December). The employment/population ratio held steady at 58.5% (it was 58.4% in January 2011). Average weekly hours held steady at 34.5, with manufacturing hours jumping to 40.9 (vs. 40.6 in December). Average hourly earnings rose 0.2%, up 1.9% from a year earlier. Note that the Household Survey showed that 206,000 were not able to work because of the weather, vs. a 425,000 average over the five previous years.

Personal Income rose 0.5% in December (+3.8% y/y). Wages and salaries advanced 0.4% (+3.8%), up 0.5% in the private sector (+4.6% y/y). Government wage income was flat (+0.1% y/y). Income was partly boosted by the cost of living adjustment (+3.6%) in Social Security (some checks for January went out in December). **Personal Spending** was flat, following 0.1% gains in both October and November – and fell 0.1% adjusting for inflation. The **PCE Price Index** rose 0.1% (+2.4% y/y), up 0.2% (0.153% before rounding) ex-food & energy (+1.8% y/y).

Unit **Motor Vehicle Sales** rose to a 14.1 million seasonally adjusted annual rate in January, vs. 13.5 million in December and 12.6 million in January 2011.

Consumer Confidence fell to 61.1 in the advance estimate for January, vs. 64.8 in December and 55.2 in November, due largely to weaker evaluations of current business conditions. Labor market perceptions remained depressed.

The **Employment Cost Index** rose 0.4% q/q in 4Q11, +2.0% y/y.

The **ISM Manufacturing Index** rose to 54.1 in January, vs. 53.1 in December and 59.9 a year ago. New orders and employment continued to advance. Input price pressures were mild.

The **ISM Non-Manufacturing Index** rose to 56.8 in January, vs. 53.0 in December and 58.3 a year ago. New orders and employment advanced. Input price pressures were moderate.

Construction Spending rose 1.5% in December (+4,3% y/y), apparently helped by mild weather. Single-family construction rose 1.5% (following +1.7% in November. Nonresidential rose 3.3%, up 11.4% from a year earlier.

The **S&P/Case-Shiller Home Price Index** fell 0.7% (seasonally adjusted) in November, down 3.3% y/y. The index rose 4.2% in the 12 months ending June 2010, but has fallen 6.8% since.

Economic Outlook (1Q12): +1.5% to +2.5% GDP growth.

Employment: The job market continues to improve, helped partly by mild weather in December and January. Job destruction remains low and new hiring is picking up.

Consumers: Consumer spending appears to have been relatively lackluster in early 2012, although mild weather appears to have aided vehicle sales. Income is improving and bank credit to consumers is gradually easing.

Manufacturing: Activity has improved, but new orders and production have been mixed across industries. Export growth should be dampened slightly by weaker global growth.

Housing/Construction: Mild weather likely helped in recent months, but the level of activity is expected to remain relatively low. Mortgage rates are very low.

Prices: Headline inflation has moderated in recent months, reflecting an unwinding of food and energy price increases from the first half of 2011. There's not inflation coming through the labor market, the widest channel for inflation pressure. Core inflation is expected to remain below the Fed's target.

Interest Rates: Federal reserve officials expect to keep the overnight lending rate near zero through late 2014, although opinions vary and it depends on how the economy develops. Chairman Bernanke said recently that officials are still debating on whether to undertake another round of asset purchases.

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This Week:					*forecast*	last	last –1	comments
Monday	2/06		no significant data					Super Bowl hangover
Tuesday	2/07	1:00	Treasury Note Auction					$32 billion in 3-year notes
Wednesday	2/08	1:00	Treasury Note Auction					$24 billion in 10-year notes
Thursday	2/09	7:00	BOE Policy Decision		***0.50%***	0.50%	0.50%	a better-than-even chance of more QE
		7:45	ECB Policy Decision		***1.00%***	1.00%	1.00%	some change of another rate cut
		8:30	Jobless Claims, th.	2/04	***375***	367	379	still a bit noisy, but a low trend
		10:00	Wholesale Inventories	Dec	***+0.3%***	+0.1%	+1.2%	assumed up moderate in the adv GDP est
		1:00	Treasury Bond Auction					$16 billion in 30-year bonds
Friday	2/10	8:30	**Trade Balance, $bln**	Dec	***-49.3***	-47.8	-43.3	expected to have widened
			goods only		***-65.0***	-63.2	-58.6	GDP report assumed rise in oil imports
		9:55	Consumer Sentiment	m-Feb	***74.0***	75.0	69.9	gasoline prices may be a negative factor
		12:30	**Bernanke Speaks**					*"Housing Markets in Transition"*
		2:00	Treasury Budget, $bln	Jan	***NF***	-49.8	-42.6	a slightly smaller deficit than a year ago
Next Week:								
Monday	2/13		no significant data					
Tuesday ♥	2/14	7:30	Small Business Optimism	Jan	***NF***	93.8	92.0	trend is higher
		8:30	Import Prices	Jan	***NF***	-0.1%	+0.8%	oil prices rose
			ex-food & fuels		***NF***	+0.1%	-0.3%	moderate inflation pressure otherwise
		8:30	**Retail Sales**	Jan	***+0.4%***	+0.1%	+0.4%	a further pickup in auto sales
			ex-autos		***+0.2%***	-0.2%	+0.3%	lackluster otherwise
			ex-autos, bld mat, gasoline		***+0.1%***	-0.2%	+0.3%	a soft trend into early 2012
		10:00	Business Inventories	Dec	***+0.3%***	+0.3%	+0.8%	assumed moderately higher
Wednesday	2/15	8:30	Empire State Manf. Index	Feb	***NF***	13.5	8.2	mild weather may help
		9:15	**Industrial Production**	Jan	***+0.8%***	+0.4%	-0.3%	lower utility output
			Manufacturing Output		***+1.1%***	+0.9%	-0.4%	aggregate manufacturing hours rose 1.2%
			Capacity Utilization		***78.8%***	78.1%	77.8%	higher, but still relatively low
		10:00	Homebuilder Sentiment	Feb	***26***	25	21	up in recent months, but still very low
		2:00	**FOMC Minutes**	1/25				how close to another round of QE?
Thursday	2/16	8:30	Jobless Claims, th.	2/11	***370***	***375***	367	still a low trend
		8:30	**Producer Price Index**	Jan	***+0.3%***	-0.1%	+0.3%	some increase in energy prices
			ex-food & energy		***+0.1%***	+0.3%	+0.1%	low otherwise
		8:30	**Building Permits, th.**	Jan	***675***	671	680	mild weather may help
			% change		***+0.6***	-1.3	+5.6	multi-family is volatile
			Housing Starts		***665***	657	685	seen somewhat higher
			% change		***+1.2***	-4.0	+9.1	watch for revisions
		10:00	Philadelphia Fed Index	Feb	***NF***	7.3	6.8	should remain moderate
Friday	2/17	8:30	**Consumer Price Index**	Jan	***+0.3%***	0.0%	-0.0%	higher gasoline prices
			year-over-year		***+2.8%***	+3.0%	+3.4%	trend is moderating
			ex-food & energy		***+0.1%***	+0.1%	+0.2%	mild core inflation
			year-over-year		***+2.1%***	+2.2%	+2.2%	a lower trend in recent months
		8:30	Real Earnings	Jan	***-0.1%***	+0.5%	-0.3%	nominal weekly earnings rose 0.2%
		10:00	Leading Econ Indicators	Jan	***NF***	+0.4%	+0.2%	likely higher

This Week…

The economic calendar thins out considerably this week. Bernanke will repeat recent testimony (this time to the Senate Budget Committee). He will also speak on the housing market on Friday, and that could be more eventful for the markets (if he elaborates on the possibility of QE3). The trade figures are of not much interest for the markets, but the report has some implications for GDP revisions

Monday

No significant data.

Tuesday

Bernanke Testimony (Senate Budget Committee) – The Fed Chairman is expected to repeat the written testimony he gave last week to the House Budget Committee. However, Senators can still ask him about the state of the economy, the Fed's dual targeting system, and what might drive monetary policy changes in the months ahead (including the possibility of QE3).

Wednesday

No significant data.

Thursday

Bank of England Policy Meeting – The BOE is widely expected to leave short-term interest rates unchanged, but there's a good chance of an increase in the asset purchase program.

European Central Bank Policy Meeting – The ECB has changed significantly since Draghi took over in early November. The ECB lowered short-term interest rates in the first two policy meetings (but did not move in January). More importantly,

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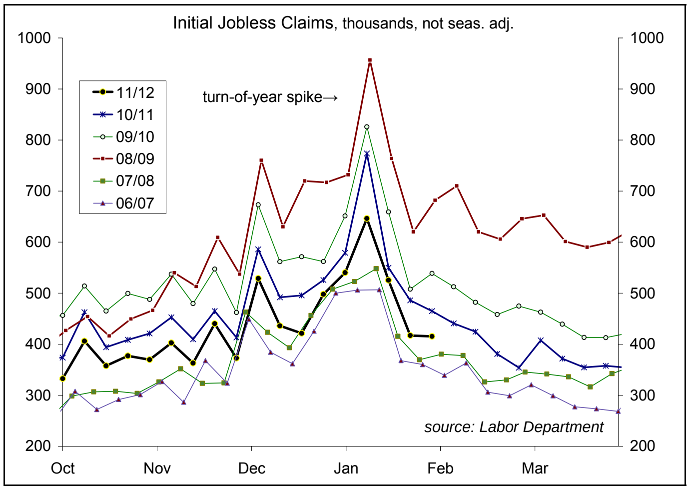
Draghi led the ECB to lend indirectly to stressed governments (that is, lend to the banks and have them buy sovereign debt). The ECB is widely expected to stand pat at this meeting.

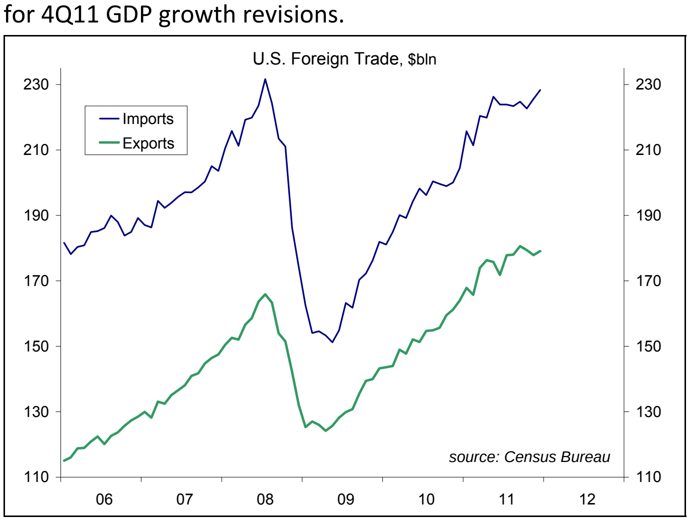
Jobless Claims (week ending January 28) – The weekly claims figure will remain subject to seasonal noise. However, the underlying trend has been relatively low in recent weeks, consistent with moderate job growth. Unusually mild weather has likely helped keep the trend low.



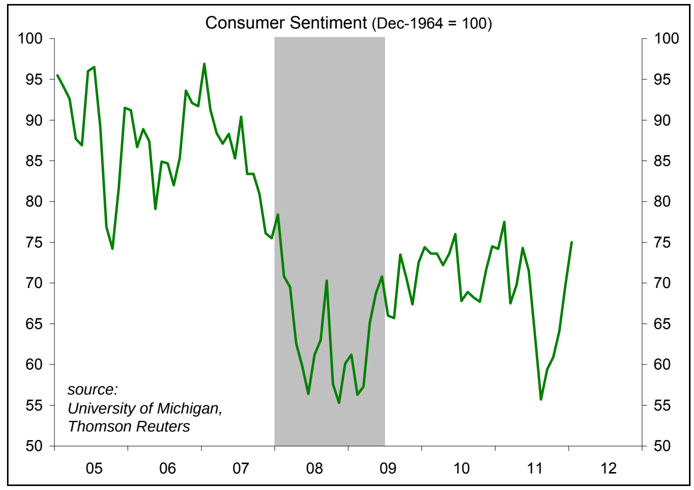
Wholesale Trade (December) – Likely to have risen moderately.

Friday

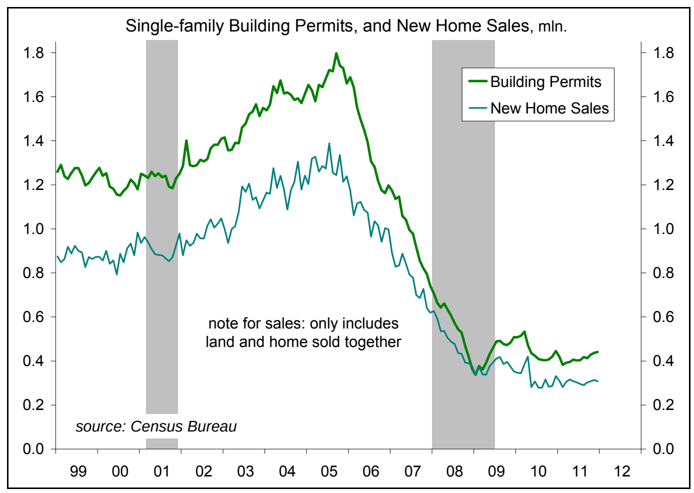
Trade Balance (December) – In the advance GDP report, the Bureau of Economic Analysis assumed that the trade deficit had widened in December, due in part to a surge in oil imports (partly prices). Exports are expected to trend modestly higher, reflecting softer global economic growth. There's a good chance for a surprise here, which would have minor implications for 4Q11 GDP growth revisions.



Consumer Sentiment (mid-February) – Sentiment improved sharply in January, although the level remained relatively low by historical standards. Higher gasoline prices may dampen enthusiasm somewhat into early February. These data tend to be more volatile, giving more false starts over time, than the Conference Board's Consumer Confidence Index.



Bernanke Speech (Housing) – It's no secret that the housing market has been a major disappointment for the Fed. Moreover, the weak housing market has muted the transmission of monetary policy. Will the Fed do something about this? Investors should listen for whether the Fed chairman will hint about further asset purchases (this time, centered in mortgage-backed securities).



Next Week ...

Lots of data heading into a holiday weekend.

Coming Events and Data Releases

February 20	Presidents Day (markets closed)
February ?	Bernanke Monetary policy Testimony
February 22	Existing Home Sales (January)
February 24	New Home Sales (January)
March 9	Employment Report (February)
March 13	FOMC Policy Meeting (no press briefing)
April 24-25	FOMC Policy Meeting Bernanke Press Briefing
June 19-20	FOMC Policy Meeting Bernanke Press Briefing

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