

Weekly Economic Commentary

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Policymakers, Pundits, and Politicians Eye the May Jobs Report

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Highlights

The May jobs report is due out this Friday, June 1. The market is expecting a solid but not spectacular outcome for the labor market.

The pace of job growth has meaningful implications for the Federal Reserve (Fed) at their upcoming June 19–20 meeting.

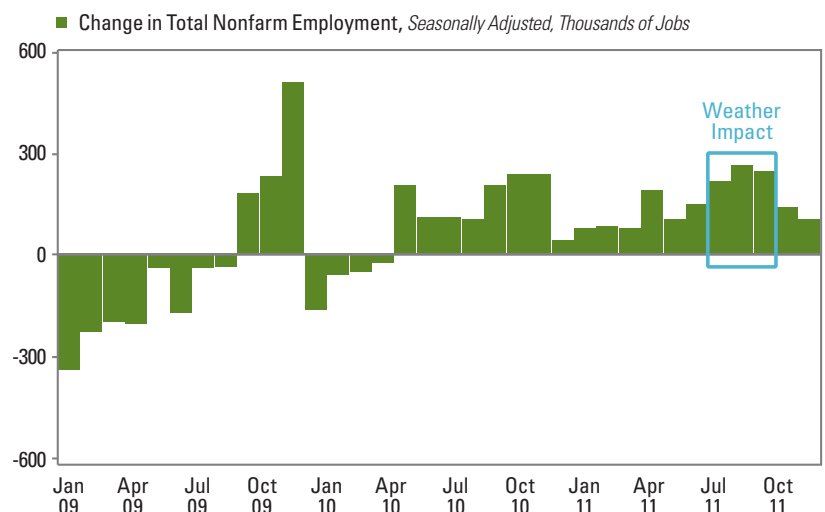
Among economic indicators, the unemployment rate is not the election determinant it is often thought to be.

Please See the LPL Financial Research Weekly Calendar on page 3

The May jobs report is due out on Friday June 1, 2012, and as always, market participants and policymakers will closely watch the report. This year is an election year, of course, so the politicians and political pundits will have plenty to say about the report as well.

Market participants are looking for an increase of 160,000 private sector jobs in May 2012, a slight acceleration from the 130,000 jobs created in April 2012, but well below the 250,000 per month pace of job creation seen between December 2011 and February 2012, which was likely inflated by much warmer-than-usual weather during those months. The 130,000 private sector jobs added in April 2012 were the fewest in any month since August 2011 (52,000), and most likely represented the final month of “payback” for the warmer-than-usual winter weather that likely inflated the payroll count between November 2011 and February 2012. Last fall, prior to the warmer weather, the economy was creating around 150,000 jobs per month. The true pace of underlying job growth is likely somewhere between 150,000 and 250,000. In our estimation the true pace of employment growth is in the 175,000 to 200,000 range.

1 Warmer-Than-Usual Weather Probably Boosted the Job Count Between November 2011 and February 2012



Source: Bureau of Labor Statistics, Haver Analytics 05/29/12

The U.S. Bureau of Labor Statics defines nonfarm employment as the total number of U.S. paid workers excluding general government employees, provide household employees, nonprofit organization employees who provide assistance to individuals, and farm employees.



Compared to last fall, when the level of initial claims for unemployment insurance was running over 400,000 per week, the level of initial claims filed each week in May 2012 (under 375,000 per week) suggests that hiring is a bit more robust today than it was last fall. Several other indicators suggest that the economy is probably creating more jobs than it was last fall (150,000 per month), but not many more:

- The increase in consumer sentiment,
- The better consumer spending in recent months,
- The near-record level of corporate profits and cash flows,
- The increase in job openings, and
- The number of job quitters as a percent of overall job separations.

Hiring is a bit more robust today than it was last fall.

Policymakers at the Federal Reserve (Fed) also will likely have a keen interest in the May jobs report, which will be the last one prior to the key June 19–20 Federal Open Market Committee (FOMC) meeting.

- If the economy is creating closer to 100,000 jobs per month in the coming months, the Fed is more likely to act to replace “Operation Twist” with some other type of monetary stimulus (QE3) when it ends at the end of June.
- If, however, the economy is creating around 150,000 jobs per month, it is likely to be a close call whether the Fed announces a new stimulus program.
- Based on Fed Chairman Ben Bernanke’s statements, job gains over 200,000 or so might see the Fed hold off on more stimulus, although events in Europe or the upcoming fiscal cliff here in the United States might force the Fed’s hand.

A quick review of Fed Chairman Bernanke’s most recent comments on the labor market may be a helpful guide on this topic. Other than a speech on bank regulation on May 10, 2012, Bernanke has not spoken publicly since his press conference following the April 25 FOMC meeting. And as this publication is being prepared, he is not scheduled to speak again until his press conference after the June 19–20 FOMC meeting.

If the last 10 election cycles are any guide, the President's chances of re-election would increase if the unemployment rate is at 7.8% or lower by October of this year.

In that April 25 press conference, Bernanke noted that the economy needs to generate around 100,000 or so jobs per month to keep the unemployment rate, currently at 8.1%, steady. He went on to say that the economy needs to generate between 150,000 and 200,000 jobs per month to achieve the Fed’s forecast of lowering the unemployment rate to under 8.0% by the end of 2012. Bernanke said that because of the warmer weather and an unusually strong labor market in the final few months of 2011 and in early 2012, he expected that jobs gains in the months ahead “will be somewhat less than the 250,000 a month that we’ve been seeing recently.” He also said that “we’ll continue to be watching the labor market. That’s a very important consideration. If unemployment looks like it’s no longer making progress, that’ll be an important consideration in thinking about policy options.”



LPL Financial Research Weekly Calendar

	 U.S. Data	 Fed	 Global Notables
2012			
28 May	<ul style="list-style-type: none"> Memorial Day 		<ul style="list-style-type: none"> Italy: Bond Auction
29 May	<ul style="list-style-type: none"> Case Shiller Home Price Index (Mar) Consumer Confidence (May) Dallas Fed Manufacturing Index (May) 		
30 May	<ul style="list-style-type: none"> Pending Home Sales (Apr) 	<ul style="list-style-type: none">  Fisher  Dudley*  Rosengren 	<ul style="list-style-type: none"> Brazil: Central Bank Meeting
31 May	<ul style="list-style-type: none"> Challenger Job Cuts (May) ADP Employment Report (May) GDP (Q1) Initial Claims (5/26) Chain Store Sales (May) 	<ul style="list-style-type: none">  Pinalto* 	<ul style="list-style-type: none"> India: GDP (Q1) Ireland: Referendum on EU Fiscal Pact Eurozone: CPI (May) Eurozone: ECB President Draghi Germany: Retail sales (Apr) Japan: Industrial production (Apr) China: PMI (May)
1 Jun	<ul style="list-style-type: none"> Employment Report (May) Personal Income (Apr) Personal Spending (Apr) ISM (May) Construction Spending (May) Vehicle Sales (May) Hurricane Season Begins 		<ul style="list-style-type: none"> Brazil: GDP (Q1) Eurozone: PMI (May) Eurozone: Unemployment (Apr)

 Hawks: Fed officials who favor the low inflation side of the Fed's dual mandate of low inflation and full employment

 Doves: Fed officials who favor the full employment side of the Fed's dual mandate

* Voting members of the Federal Open Market Committee (FOMC)

The Case-Shiller Indexes track changes home prices throughout the United States. Case-Shiller produces a national index and indexes representing metropolitan statistical areas.

The Consumer Confidence Report is produced by the Conference Board and is based on a monthly survey of 5,000 U.S. households.

The Dallas Fed conducts a monthly survey of manufacturers in Texas. The survey focuses on operations in the state includes a range of industries.

Challenger Job Cuts report is released monthly in the United States and provides information on the total number of announced corporate layoffs.

Chinese Purchasing Managers Index: The PMI includes a package of indices to measure manufacturing sector performance. A reading above 50 percent indicates economic expansion, while that below 50 percent indicates contraction.

The ISM index is based on surveys of more than 300 manufacturing firms by the Institute of Supply Management. The ISM Manufacturing Index monitors employment, production inventories, new orders, and supplier deliveries. A composite diffusion index is created that monitors conditions in national manufacturing based on the data from these surveys.

Politicians and pundits will also likely pick apart the May jobs report, although another five jobs reports will be released before the general election on November 6, 2012. When President Obama took office in January 2009, the unemployment rate was 7.8% and rising, hitting a peak of 10.0% in October 2009, four months after the end of the recession.

At the beginning of the 2007–2009 Great Recession, the unemployment rate was 5.0%; the rate hit a cycle low of 4.4% in late 2006 and early 2007.



The unemployment rate is currently at 8.1% and still above where it was (7.8%) when President Obama took office. Looking ahead, the Bloomberg consensus says that the unemployment rate will average 8.0% in the fourth quarter of 2012, little changed from where it is today. In fact, only four of the 64 economists recently surveyed by Bloomberg think the unemployment rate will be lower in the fourth quarter than it was when President Obama took office. How the unemployment rate performed during the past 10 presidential

2 A Higher Unemployment Rate Over the Four Years of a President's Term in Office Increases the Odds That the Incumbent Party Loses Power

Election Year	Unemployment Rate When Incumbent Took Office (%)	Unemployment Rate in October of Election Year (%)	Unemployment Rate Higher, the Same or Lower Over the Four Years	Incumbent Reelected?
1972	3.4	5.6	Higher	Yes
1976	4.9	7.7	Higher	No
1980	7.5	7.5	Same	No
1984	7.5	7.3	Lower	Yes
1988	7.3	5.4	Lower	Yes
1992	5.4	7.3	Higher	No
1996	7.3	5.2	Lower	Yes
2000	5.3	3.9	Lower	No
2004	4.2	5.5	Higher	Yes
2008	5.3	6.5	Higher	No
2012	7.8	8.1*	Higher	?

Source: Bureau of Labor Statistics; LPL Financial Research 05/29/12

*Unemployment rate as of April 2012

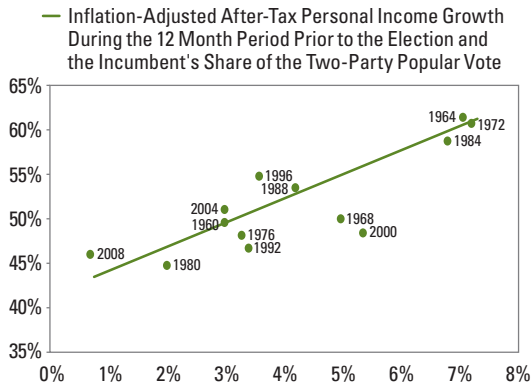
elections (1972–2008) provides plenty of history from which to draw comparisons.

Comparing the unemployment rate in October of each election year since 1972 to the unemployment rate in January of the first year of the first term, we find that in five election cycles the unemployment rate was the same or lower in October of the election year versus where it stood at the start of the term. Those elections were:

- 1980
- 1984
- 1988
- 1996
- 2000



3 3–4% Income Growth Is the Key to Getting Re-elected



Source: LPL Financial, Bloomberg Data 04/02/12

In three of those five elections (1984, 1988, and 1996) the incumbent was reelected. In the other five elections since 1972, the unemployment rate in October of the election year was higher than it was when the presidential term began. The incumbent party was reelected in two of those five elections: 1972 and 2004. Thus, if the last 10 election cycles are any guide, the President's chances of re-election would increase if the unemployment rate is at 7.8% or lower by October of this year.

Among economic indicators, while the unemployment rate is politically important, and garners a great deal of attention in the media, real after-tax personal income is probably a better economic indicator to rely on to help determine election outcomes. As noted in the April 2, 2012 *Weekly Market Commentary*, the impact of the economy on the election can most clearly be seen through the relationship between income growth in the year leading up to the election and election results. Inflation-adjusted, after-tax income growth of about 3–4% appears to be the threshold for incumbents to get 50% of the popular vote. This measure of per capita income, contained in the most recent (March 2012) Personal Income and spending report, is only growing at 0.6%. ■

LPL Financial Research 2012 Forecasts

- GDP 2%*
- Federal Funds Rate 0%^
- Private Payrolls +200K/mo.†

Please see our *2012 Outlook* for more details on LPL Financial Research forecasts.



IMPORTANT DISCLOSURES

The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual. To determine which investment(s) may be appropriate for you, consult your financial advisor prior to investing. All performance reference is historical and is no guarantee of future results. All indices are unmanaged and cannot be invested into directly.

* Gross Domestic Product (GDP) is the monetary value of all the finished goods and services produced within a country's borders in a specific time period, though GDP is usually calculated on an annual basis. It includes all of private and public consumption, government outlays, investments and exports less imports that occur within a defined territory.

^ Federal Funds Rate is the interest rate at which depository institutions actively trade balances held at the Federal Reserve, called federal funds, with each other, usually overnight, on an uncollateralized basis.

† Private Sector – the total nonfarm payroll accounts for approximately 80% of the workers who produce the entire gross domestic product of the United States. The nonfarm payroll statistic is reported monthly, on the first Friday of the month, and is used to assist government policy makers and economists determine the current state of the economy and predict future levels of economic activity. It doesn't include:

- general government employees
- private household employees
- employees of nonprofit organizations that provide assistance to individuals
- farm employees

The economic forecasts set forth in the presentation may not develop as predicted and there can be no guarantee that strategies promoted will be successful.

The fast price swings in commodities and currencies will result in significant volatility in an investor's holdings.

The Consumer Price Index (CPI) is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services.

Quantitative Easing is a government monetary policy occasionally used to increase the money supply by buying government securities or other securities from the market. Quantitative easing increases the money supply by flooding financial institutions with capital in an effort to promote increased lending and liquidity. This research material has been prepared by LPL Financial.

The Federal Open Market Committee action known as Operation Twist began in 1961. The intent was to flatten the yield curve in order to promote capital inflows and strengthen the dollar. The Fed utilized open market operations to shorten the maturity of public debt in the open market. The action has subsequently been reexamined in isolation and found to have been more effective than originally thought. As a result of this reappraisal, similar action has been suggested as an alternative to quantitative easing by central banks.

This research material has been prepared by LPL Financial.

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