Solid Labor Report Unlikely to Alter Fed Mindset

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This morning, the June labor report surprised to the upside with +850k jobs added to U.S. company payrolls. It was the biggest monthly gain since last August and handily beat the +720k median forecast, but so far this morning the market reaction is muted. The best explanation is that we all *expect* payrolls to rise; it's not a question of if, but rather …*when*. The safety net of federal unemployment benefits expires in another two months. Although half of U.S. states have opted out early, the June employment report was compiled too early to reflect the millions of Americans who will be scrambling to replace that income.

May payroll gains were revised upward from +559k to +583k, while April was revised downward from +278k to +269k. The monthly trend is clearly up, and it would be a surprise if July didn't continue the climb. However, total payroll jobs are still almost 6.8 million below the February 2020 count, so there's a long way to go to before the Fed achieves its employment goal. The bond market's ho-hum reaction reflects this.

The unemployment rate actually ticked up a notch from +5.8% to +5.9%, although this means very little. It's not unusual for headline unemployment to move higher as labor market conditions improve and job searches resume.

As expected, a majority of the June payroll gains were concentered in leisure and hospitality (+343k) with more than half of these in food services and drinking establishments. BLS data shows the leisure and hospitality sector is still -12.9% or 2.2 million jobs below the pre-pandemic level from February 2020. The July report is likely to include large gains in this sector as federal support disappears.

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Education added +269k jobs, although the Labor Department cautions that seasonable adjustment factors have distorted the picture. At this point, total education jobs are still 837k below pre-pandemic levels, but with virtually all schools set to reopen in the next six to eight weeks, that shortfall is almost certain to narrow.

Retail added +67k jobs in June; now just -1.9% or 303k jobs short of pre-pandemic levels. This sector should benefit from an expected back-to-school shopping spree in upcoming weeks.

The number of construction jobs fell by -7k in June, a bit of a surprise in the midst of a red hot housing market, and remain 238k jobs below the February 2020 count.

Manufacturing added +15k total jobs, although the sector was weighed down by a -12k decline in motor vehicle and parts jobs. Total manufacturing jobs are still 481k below the February 2020 pre-pandemic count. Recent news of production pauses at U.S. auto plants suggests factory jobs will lag.

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There were some interesting gains in the "other services" category. In particular, personal and laundry services (+29k) and association and organization membership

(+18k), both signaling a welcome return to traditional in-person business.

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Average hourly earnings rose $0.10 to $30.40 in June, matching forecasts, and down from larger gains in April ($0.20) and May (0.13%). On a year-over-year basis, earnings for all employees are up +3.6%. Analysts will keep a sharp eye on wages as the year progresses, but today's number is still too noisy to provide true insight. Recent wage pressures are concentrated in traditionally low-paying jobs, and it's become clear that employers will be forced to raise pay in the future to attract and retain workers.

This morning's labor report, although solid, won't push the Fed any closer to tightening. In fact, the slight increase in the unemployment rate suggests more labor market slack. It will take payroll gains of over a million per month for the remainder of the year to get back to the total from before the virus hit, and that's a very tall order. *It's important to remember that when those 6.8 million payroll jobs finally return, net job creation over a two-year period will essentially be flat.* This argues for continued accommodation.

In other news from yesterday afternoon, U.S. vehicle sales for June came in at a 15.4 million unit pace. Sales have been dropping since April when the 18.5 million annual sales rate was the strongest in almost 16 years. Auto demand is fine: it's a lack of inventory, a problem unlikely to find a fix until the depleted microchip supply can be restored.

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We, at Hilltop, wish you all *a safe and Happy 4th of July weekend*.

Market Indications as of 11:03 A.M. Central Time

DOW	Up 110 to 34,744 (HIGH: 34,778)
NASDAQ	Up 69 to 14,592 (NEW HIGH)
S&P 500	Up 17 to 4,337 (NEW HIGH)
1-Yr T-bill	current yield 0.07%; opening yield 0.06%
2-Yr T-note	current yield 0.24%; opening yield 0.26%
3-Yr T-note	current yield 0.45%; opening yield 0.47%
5-Yr T-note	current yield 0.87%; opening yield 0.90%
10-Yr T-note	current yield 1.44%; opening yield 1.47%
30-Yr T-bond	current yield 2.05%; opening yield 2.07%