



Weekly Notes on the **United States**

June 7, 2010. Worldwide Edition

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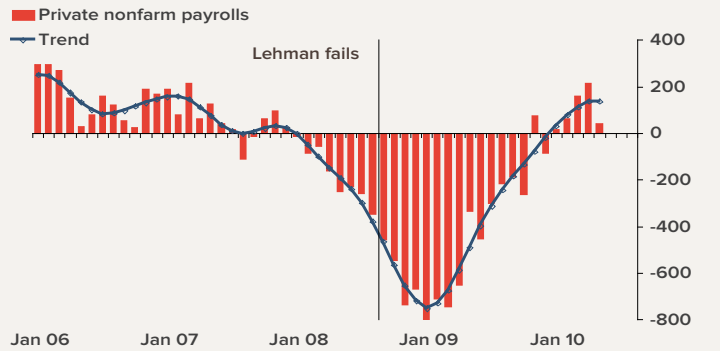
What To Make Of May Payrolls

The May payroll numbers suggest two broad possibilities. First, the bad news: *May's very modest 41K increase in private payrolls could mark the beginning of a normalization of the relationship between the ADP survey, which is the key independent indicator of employment trends, and the official numbers.* The ADP data have been rather weaker than the BLS numbers for some time now: In each of the six months to April, the ADP report under-predicted the official measure of private payrolls by an average of 117K. Our working assumption was that the shortfall would persist in May, when the ADP number was 55K. Instead, ADP over-predicted by 14K.

This might be nothing but a fluke; they do happen. For example, the ADP survey over-predicted by 65K in October last year, sandwiched between runs of three and six straight under-predictions. *But the history of the data tells us that sooner or later the two series will come back into line, and stay there, allowing for the usual monthly noise.* You could, therefore, choose to view the run of under-predictions through April as simply the reversal of the run of over-predictions which were a characteristic of the first year of the recession, as our first chart shows. The trend in the ADP numbers is rising, but the rate

of increase has slowed in recent months. ***With jobless claims marmooned at 450K or so, it is hard to have much confidence that more rapid increases are in the pipeline.***

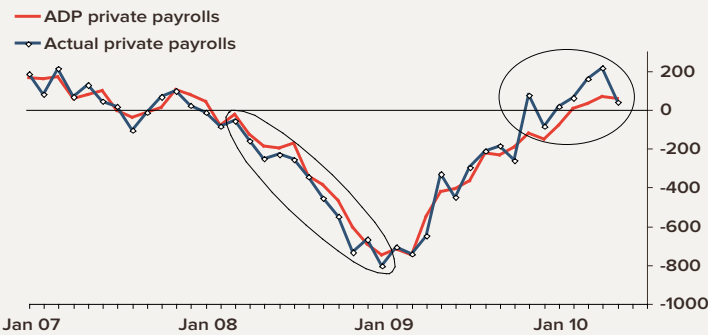
Running Out Of Steam?



The alternative view is that there is nothing much to worry about. *The rise in private payrolls in May was much smaller than in March or April, but the variation was not big enough to draw any firm conclusions, statistically speaking.* The BLS estimates that the published month-to-month change in private payrolls is accurate to within about plus or minus 100K. If the May number was towards the bottom of that range and April was towards the top—we have no way of knowing—then the difference between them will have no statistical significance whatever. *Looking beyond the monthly variations, most measures of the trend in private payrolls, whether simple moving averages or more sophisticated estimates, are improving.* It is possible the May data represent the start of a downshift in that trend, but markets seem to place a greater probability on that outcome than anything else, a judgment which is hard to justify on a purely statistical basis.

Our view, unfortunately, is that the first view of the numbers has the edge. *The bottom line here is that the ADP survey is designed*

Overshoot To Undershoot To Back In Line?



HFE's Economic Forecasts

GDP	Q3 final	2.2%	2007 year:	2.1%
	Q4 final	5.6%	2008 year:	0.4%
	Q1 second	3.0%	2009 year:	-2.4%
	Q2 forecast	2%	2010 year:	3%
	Q3 forecast	2%		

CPI	Apr.:	-0.1% (2.2% y/y); core 0.0% (0.9% y/y)
	Jun. 2010 forecast:	0.8% y/y; core 0.8% y/y
	Dec. 2010 forecast:	0.5% y/y; core 0.3% y/y

Unemployment: June 2010, 9.5%; Dec. 2010, 9.4%
Federal budget FY 10 forecast: -\$1.75T (12.3% of GDP)

HFE's Financial Forecasts

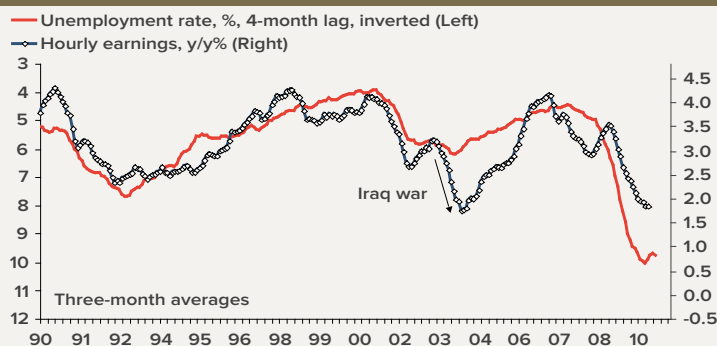
	End-month:				
	4:30pm Friday	Jun	Sep	Dec	Mar
Fed funds	0-to-0.25	0-to-0.25 through Dec 11			
2-yr	0.72	0.75	0.75	0.75	0.75
10-yr	3.20	3.25	3.25	2.75	2.50
30-yr	4.13	4.00	3.75	3.25	3.00
Curve 10-2	248	250	250	200	175
Curve 30-2	341	325	300	250	225
Dow Jones IA	9932	10250	10250	10250	10750

Dollar: Euro to sink to new lows, intervention will not help. C\$ to get a boost after BoC rate hike.

to mimic the payroll data, and most of the time it does. It was not designed to cope with a shock of the magnitude of the banking crisis, though, so we are inclined to believe that the unusual variations in the survey in the past couple of years, relative to the official numbers, are not evidence of some sort of structural breakdown in the correlation. **As always, anything can happen to payrolls in any given month, but we would put a much bigger bet on private payrolls averaging 100K over the next six months than, say, 200K.** If that view is correct, unemployment will not come down much this year.

Aside from the reversal of April's unexpected rise in the unemployment rate—noise followed by noise—the better news in the May report was in the wages data. Hourly earnings for all employees rose 0.3%, the biggest gain since January. One decent month does not change the trend, but we'll take the good news where we can get it, not least because we think the elevated unemployment rate will put downward pressure on wage growth for the foreseeable future. *So far at least, the speed of the downshift in wage gains has not been quite as rapid as we feared.*

Wage Growth Still Softening, But At A Slower Rate



Today brings only the consumer credit report for April. In March, the stock of credit outstanding unexpectedly rose by \$2.0B, the second gain in three months. In both January and March, the entire increase was more than accounted for by increases in the government component, which is dominated by student loans. That said, the rate of decline of credit outstanding excluding the government component is slowing. *This is not unduly surprising, given that the underlying trend in credit growth lags the rate of growth of consumers' spending on durable goods.* Spending tanked in the aftermath of the Lehman disaster but it has since recovered somewhat, though it remains far below the pre-crash peak. Accordingly, the stock of private consumer credit should stabilize over the next few months.

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This Week's Funding

Mon	Announcement—4-week bills (June 9) Auction—\$27B 3-month, \$27B 6-month bills
Tue	Auction—\$36B 3-year notes (settles June 15)
Wed	Auction—4-week bills Auction—\$21B 10-year notes (settles June 15)
Thu	Announcement—3-month, 6-month bills (June 14) Auction—\$13B 30-year bonds (June 15)

This Week in Brief

Note: "SS" prefix denotes Snapshot for these data.

Monday, June 7

- **Consumer Credit (4)/15:00 EDT**

We expect a **\$5B** decline in credit outstanding. The government component boosted March credit. **Consensus: \$1.0B.**

Tuesday, June 8

- **SS: NFIB Survey (5)/7:30 EDT**

We expect **little change** in the headline index, which rebounded to 90.6 in April after an unexpected March dip to 86.8. The index needs to breach about 92.5 to signal growth in the small business sector. **Consensus: N/A.**

- **Redbook Chain Store Sales (6/5)/9:00 EDT**

Sales growth should jump sharply from last week's **2.5%**; this week marks the anniversary of the cessation of publication of weekly sales numbers by Wal-Mart.

Wednesday, June 9

- **MBA Mortgage Applications (6/4)/7:00 EDT**

Surely no further decline after last week's 4.1% drop in the purchase index to a 13-year low of just **178.0**.

- **Wholesale Trade (4)/10:00 EDT**

We reckon inventories rose about **0.7%**, in line with the recent trend. The core inventory-to-sales ratio is more or less back to its pre-recession trend. **Consensus: 0.5%.**

- **Federal Reserve Beige Book/14:00 EDT**

Further anecdotal evidence of recovery, but smaller firms are doing less well than larger businesses. Price and wage pressures still very subdued.

Thursday, June 10

- **SS: Initial Jobless Claims (6/5)/8:30 EDT**

The trend seems to be about flat, so we look for claims to be close to last week's **453K**. **Consensus: 448K.**

- **SS: International Trade (4)/8:30 EDT**

The deficit should be little changed at about **\$41B**, after \$40.4B in March. The core deficit should be little changed, and a rebound in the aircraft surplus should offset most of the rise in the petroleum deficit. **Consensus: \$41.0B.**

- **Treasury Budget (5)/14:00 EDT**

The CBO reckons the May deficit was about **\$142B**, compared to \$190B in May last year. Calendar effects account for about half the decline. **Consensus: -\$140B.**

Friday, June 11

- **SS: Retail Sales (5)/8:30 EDT**

A combination of weaker chain store sales and a partial reversal of the recent surge in sales of building materials means total sales should fall about **0.5%**; sales ex-autos should also drop **0.5%**. **Consensus: Total sales 0.4%, ex-autos 0.2%.**

- **SS: University of Michigan Sentiment (6p)/9:55 EDT**

The index ought to slide to about **71** from 73.6, as the drop in stock prices starts to make itself felt. **Consensus: 74.6.**

- **Business Inventories (4)/10:00 EDT**

Total inventories should rise **0.5%**, marginally more than in March, when they rose 0.4%. **Consensus: 0.5%.**