

Jobs growth may return in March

The direction of the USD may be nearing an inflection point with focus shifting away from concern about sovereign debt risk in the EU to improving risk sentiment. The USD rallied over 10% versus the EUR since December mainly in reaction to concern about the outlook for sovereign debt risk in the EU. This weekend French president Sarkozy said that the EU is prepared to help Greece. Sarkozy's comments helped ease concern about a Greek debt default and contributed to an improvement in risk sentiment. Friday's release of better than expected US February unemployment adds to improvement in risk sentiment and the USD traded mixed to lower Monday.

Despite two major February snowstorms February US unemployment rate was unchanged at 9.7% and nonfarm payroll (nfp) losses were significantly less than expected declining by 36k. The nfp decline was less than half the consensus of analysts. A number of analysts had expected the snowstorms to contribute to up to 100k to 200k of nfp losses. The Bureau of Labor Statistics said that the snowstorms may have depressed the payroll report but that they could not quantify the impact. This has led to the debate over whether the February jobs report would have been positive without impacting the snowstorms. The February unemployment report suggests that US labor market is stabilizing and that jobs growth lies ahead.

There were a number of positives in the US February unemployment report. The number of long-term unemployed workers fell by 180k to 6.1mln. This was the largest decline since June of 2006 in the number of long-term unemployed workers. Manufacturing jobs rose by 1k. Manufacturing jobs have gained for two months in a row. Temporary help jobs rose by 48k. Temporary help is seen as step closer to permanent employment. Health care added 20k in new jobs. Average hourly earnings rose by 0.1% and nfp losses were revised lower for the prior two months. This confirms that fewer jobs have been lost in December and January. One of the biggest negatives in the February report was the construction employment fell by 64k. Also 15k of census workers were added to the February report. Census jobs are temporary jobs that will not lead to permanent employment. On balance the February jobs report suggests that the February storms masked improvement in the US employment outlook.

Although the February unemployment report appears to suggest the beginning of a trend in job gains, the report does not suggest a strong recovery. Last week the US Labor Department reported that US productivity rose to 6.9% in the fourth quarter. The jump in productivity suggests that those still employed are being forced to increase productivity to make up for lost workers as business activity is picking up. The continued rise in productivity is not sustainable and this suggests that employers will soon need to hire more workers. A wave of hiring may be coming soon. The key issue is what impact the improving employment outlook will have on risk sentiment and Fed policy outlook.

January consumer confidence posts a sharp decline. A CBS poll shows that a majority of Americans are still worried about job losses and only 17% of Americans think the country's economy is in good shape. The decline in consumer confidence is a concern for the strength of the US recovery because 70% of GDP is made up of consumer demand. Despite uncertainty about consumer demand some of the Fed board members indicate that interest rates may have to rise even while unemployment remains elevated. An NABE survey of business economists finds that a Fed rate hike is expected within the next six months. There is increased speculation that the Fed may begin a shift in policy bias at the March 16th policy meeting amid signs of that the US labor market is stabilizing. Improvement in the US employment outlook may make it harder for the Fed to delay its exit strategy. This may mean that the current trend of improvement

in risk sentiment could give way to speculation that the Fed exit of stimulus presents a risk of a double dip recession in the US.

The February unemployment report suggests that there is jobs growth ahead. Despite the improvement in the outlook for jobs growth headline US unemployment rate may rise as frustrated workers began once again to look for work. Economist Mark Zandi of Moody's economy.com said Friday that the US jobless rate could hit 10.5% by Election Day. According to Zandi there are close to 2mln people who have left the official count of the labor market over the past years giving up looking for work. Zandi says that when these workers look to re-enter the workforce the economy may not be creating jobs fast enough to meet the demand.

The US February unemployment report suggests that jobs growth will return in March. In the short term we suspect that the trend in improving risk sentiment fueled by the February jobs report will continue. The glimmers of hope sparked by the February unemployment number may encourage frustrated workers to once again search for employment and this could send the US unemployment rate back above 10% in the months ahead. The CBS survey noted above suggests that despite signs of improvement in the US labor force there remains great concern about the risk of job loss. The troublesome reality is despite the stability in February employment report 15mln Americans are out of work and millions more are working part time or are underemployed. How the coming rise in headline employment impacts consumer sentiment will be key to the sustainability of the US recovery and risk sentiment. The February snow appears to have masked the recovery in employment during February and we expect an nfp rise in the March report. What the rise in nfp means for the US economy will depend on when the Fed and government cut back on monetary and fiscal stimulus. An early withdrawal of stimulus could curb the jobs recovery and increase the risk of a double dip recession. The return of jobs growth in March may not be sustainable if stimulus is withdrawn too soon. Pimco's Gross says the biggest worry is the Fed withdraws stimulus too quickly.

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