

Do You Still Think the Fed Is Going to Raise Rates in 2016?

As we suggested in April, the macroeconomic landscape argues for no more rate hikes in 2016.



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The [May jobs report](#) showing an increase of 38,000 in nonfarm payrolls was the worst print since June 2012. April's gain was also revised down to 123,000. Presumably, expectations of a **Federal Reserve** rate hike in June are completely dashed, and July is not looking so likely either.

We hate to have to say it, but we [told you so](#). The false narrative of U.S. economic strength and a "tight" jobs market simply does not hold up to objective scrutiny. A faltering global economic landscape offers little promise of a sudden acceleration in growth. Let's face it, this may be the worst economic recovery since World War II in terms of growth, but it remains the fourth longest streak between recessions in that time at 83 months and counting. As underutilized as the U.S. economy may still be, is this recovery getting a little long in the tooth?

It is amazing to see the BLS resorting to euphemisms to downplay the horrendous print: "Unemployment rate declines to 4.7% in May; payroll employment changes little (+38,000)." Really? Leading with the "decline" in unemployment when it was transparently obvious that the decline was another misleading fluke of the two-survey approach seems a bit disingenuous.

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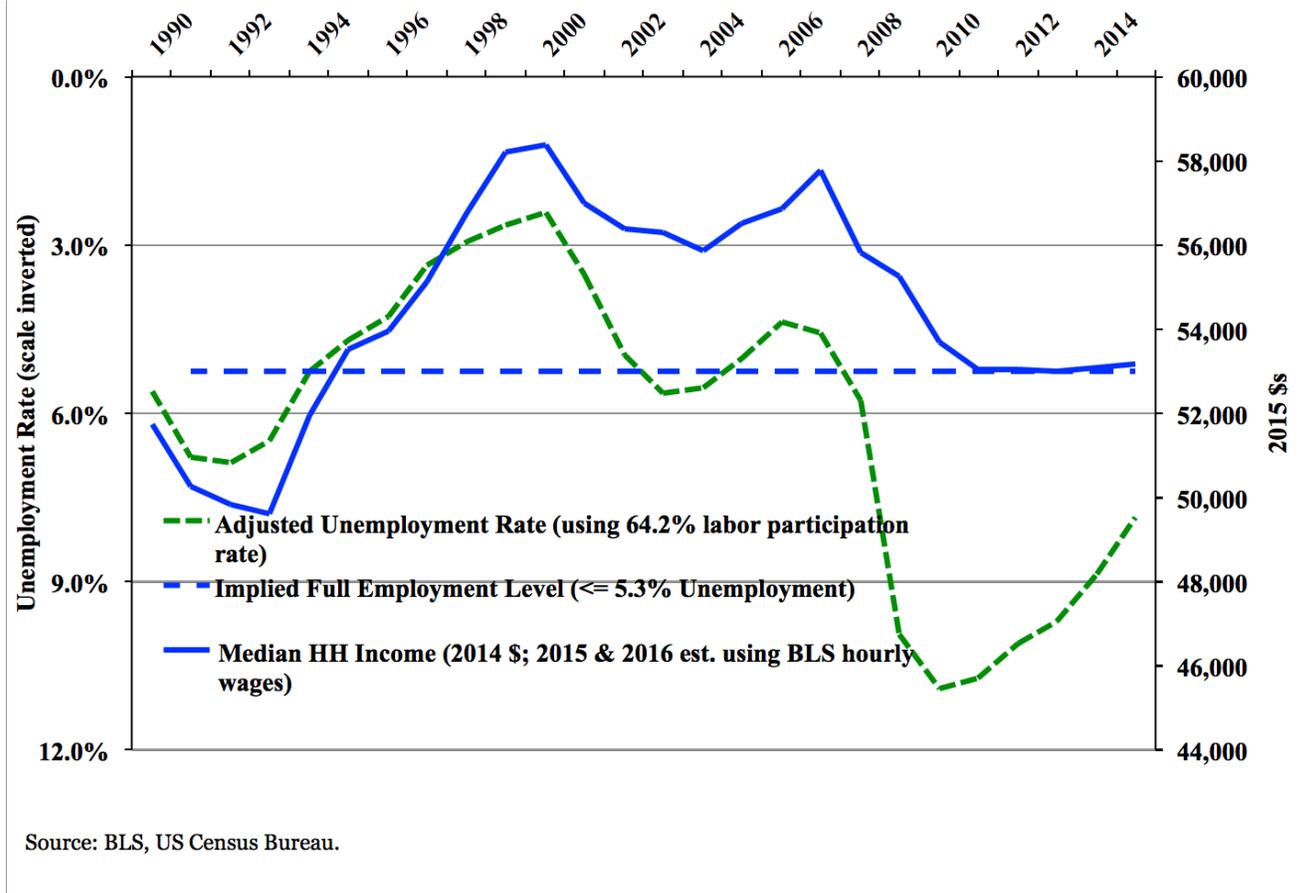
How is it that the unemployment rate declined from 5.0% (itself a joke) to 4.7% in a month when jobs grew by 38,000? There are around 110,000 net new entrants to the labor force each month, which suggests that unemployed worker ranks increased by roughly 72,000 in May. Not so, according to official numbers, the unemployed dropped by almost 500,000 this month! That's because the participation rate dropped back to 62.6% and the "official" labor force dropped by roughly that amount.

Never mind, this is getting confusing.

Just know the "official" U.S. unemployment rate of 4.7% is a total fiction. We estimate the real, historically comparable unemployment rate is just over 7%, and has risen modestly for two straight months. On the same apple-to-apples basis, unemployment needs to fall to 5.3% to reach full employment and trigger real wage increases (see the chart below). It would take 3.5 years of 150,000 jobs added per month to get there.

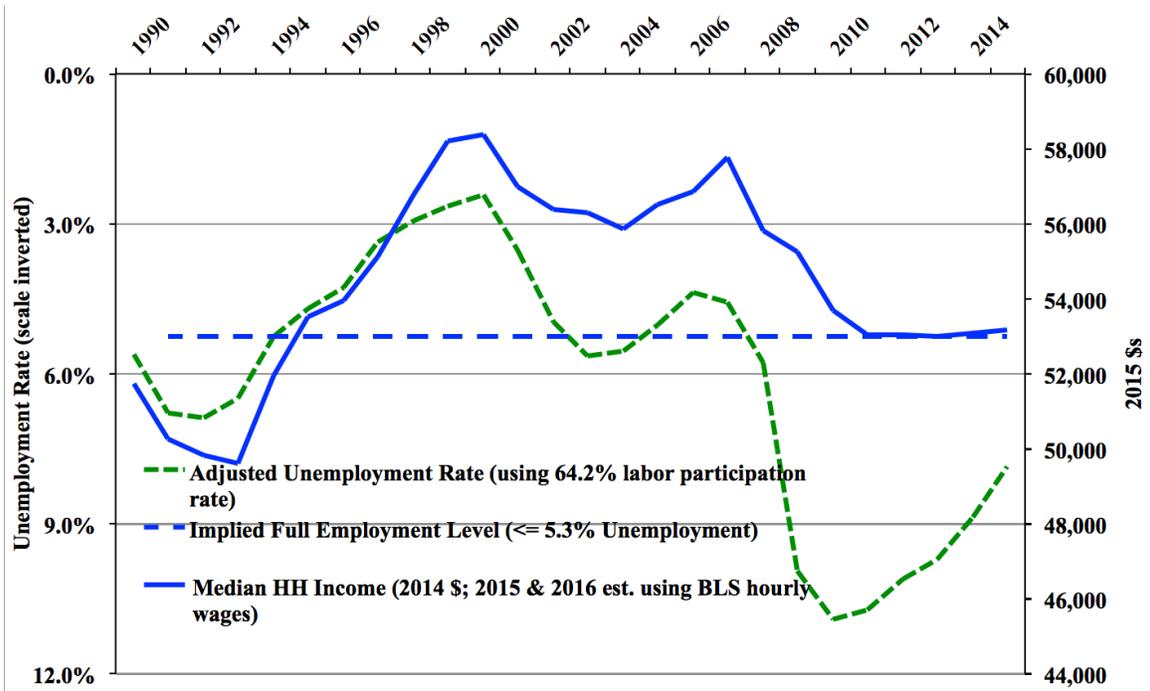
As we have argued before, if the Fed raises rates more, it is purely in order to position itself to "do something" in the event of the next recession. It is not a response to fundamentals related to its mandate regarding full employment and stable prices. Long-term rates are not going up in the foreseeable future, and we don't see the Fed going forward with higher federal funds rates in 2016. That probably means more fun at the risk assets punch bowl, and a more severe correction that may rival the 50% peak-to-trough corrections observed after the tech bubble and financial crisis.

Employment and Real Wage Growth History



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This article is commentary by an independent contributor. At the time of publication, the author held no positions in the stocks mentioned.



Source: BLS, US Census Bureau.