Economic Analysis

Backslide in Employment Not a Sign of Broader Weakening

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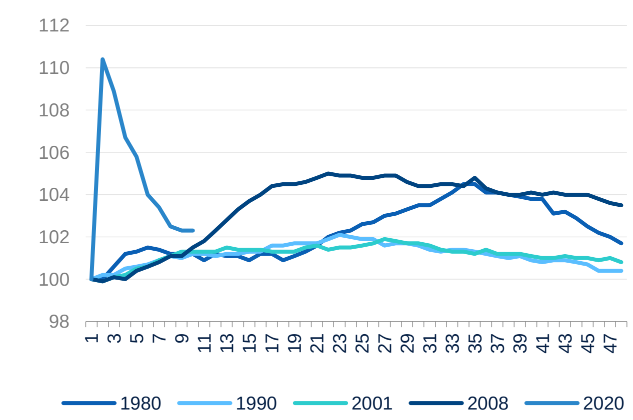
Surging Covid-19 cases and increased voluntary and compulsory distancing measures in some areas of the country produced the first drop in nonfarm payrolls (-140K) since April. Unsurprisingly, leisure and hospitality were most acutely affected by the rise in cases, losing 498K jobs over-the-month; three-fourths was explained by declines in employment in food service and drinking places. Excluding leisure and hospitality, nonfarm payroll increased 358K in December. Still, total nonfarm payroll has only recovered 56% of the 22.1M jobs lost due to the pandemic and remains 9.8M below February's level.

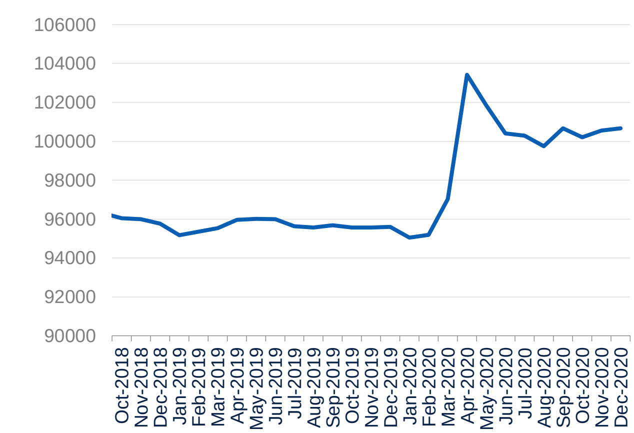
Despite the drop in payrolls, the unemployment rate remained unchanged at 6.7%, while the broader measure of labor underutilization (U6) declined to 11.7% from 12% in the previous month. However, the number of people unemployed for 27 weeks and over continued to edge up, accounting for more than 37% of total, the highest share since 2013. Similarly, the employment-to-population ratio and labor force participation were similar to last month at 57.4% and 61.5%, respectively. In fact, the number of people not in the labor force stands 5.1M above a year ago.

Figure 1. **UNEMPLOYMENT RATE** (INDEX: RECESSION START=100)



Source: BBVA Research & BLS

Figure 2. **NOT IN THE LABOR FORCE** (K)



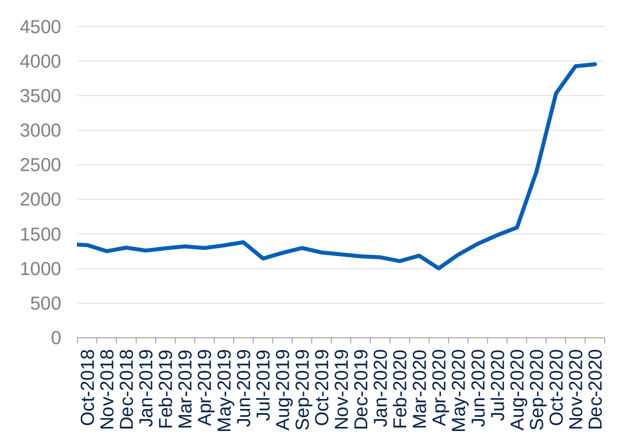
Source: BBVA Research & BLS

The pandemic's ongoing effects continue to weigh on the labor market, with the vaccine rollout moving slower-than-anticipated and case levels rising. For example, 23.7% of workers reported teleworking because of the coronavirus, up from 21.8% in November. In addition,15.8M people reported that they were unable to work due to business closures or lost sales due to the pandemic, which was 1M more than November, while 4.9M people reported that they were prevented from looking for work as a result of the rise in Covid-19, a 1.3M person increase from one month ago. The unemployment rate for teenagers and Hispanics, who disproportionately work in the most acutely impacted sectors, rose from 13.9 and 8.4% in November to 16 and 9.3% in December, respectively. For Blacks and Asians, it dropped to 9.9 and 5.9%, respectively. For Whites, it edged up 0.1pp to 6%.

To the upside, payrolls increased in professional business services by 161K, driven by a substantial gain in temporary help services. Computer system designs and other technical services that have seen increased demand during the pandemic grew 31K since November. Strong demand for residential housing, another pandemic-induced trend, pushed construction employment up 8.6% on an annualized basis. Retail trade, which also continues to adapt to the pandemic and shift in consumer preferences, added 121K, including 14K within nonstore retail. Transportation and warehousing (47K), healthcare (39K), manufacturing (38K), and wholesale trade (25K) also experienced meaningful employment growth. In contrast, educational services and government experienced a drop of 63K and 45K, respectively.

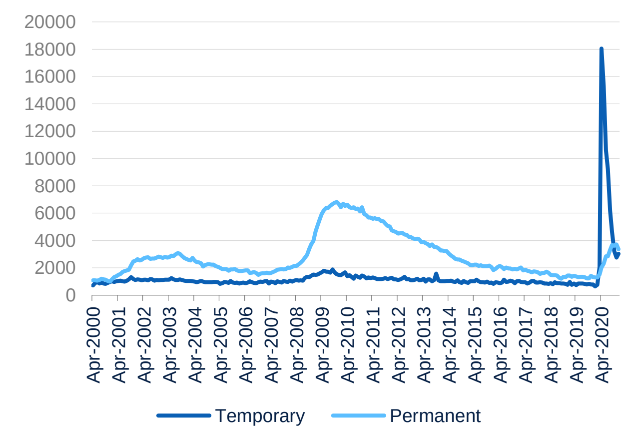
While December's payroll report is a pivot from the strong recovery since April, the underlying detail suggests that there remains nontrivial momentum in most sectors. The delay of fiscal aid and lapse in some key stimulus measures likely weighed on December's figures. However, the year-end fiscal relief package should alleviate some of the pressures on households and businesses still being impacted by the crisis and boost demand going forward.

Figure 3. **PERSONS UNEMEPLOYED 27+ WKS** (K)



Source: BBVA Research & BLS

Figure 4 **UNEMPLOYMENT** (K)



Source: BBVA Research & BLS

Until a significant portion of the population is vaccinated and case levels subside, supply-side headwinds will remain. Moreover, the vast amount of long-term unemployed workers risks permanent damage to the labor market, which could be addressed by the incoming administration through targeting work-based training and reemployment matching programs, and adequate economic stabilizers such as less onerous PPP awards and more generous unemployment benefits. As such, we continue to expect above-average gains in employment in 2021 and a meaningful decline in the unemployment rate, which we expect will reach 5.3% by the end of 2021. This, along with the slow recovery in participation, people not in the labor force, and other broader measures, would mean there is a considerable gap relative to "maximum employment" a key tenant for the Fed to consider tapering asset purchase and liftoff. This suggests interest rates will remain low for an extended period.

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