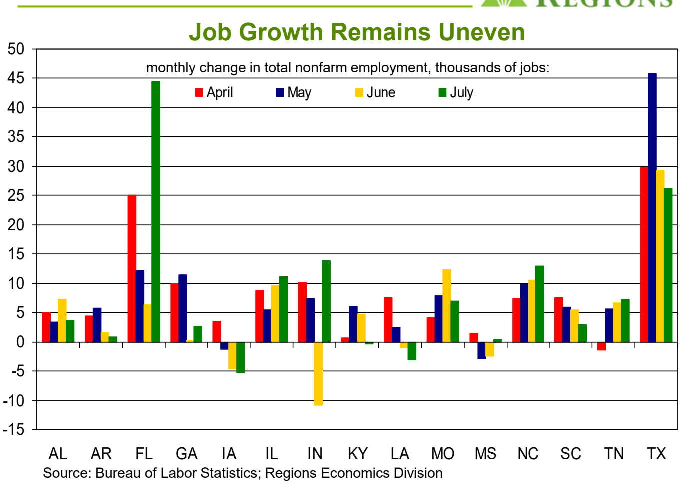
ECONOMIC UPDATE

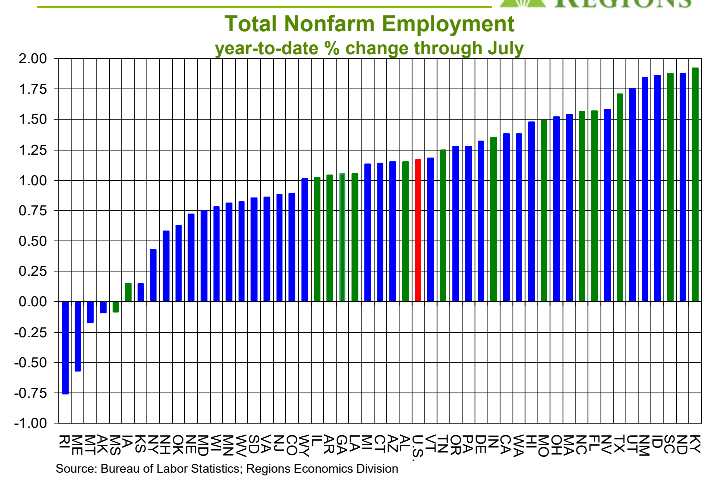
REGIONS

August 23, 2023

July 2023 Nonfarm Employment: Regions Footprint

Total nonfarm employment within the Regions footprint rose by 124,800 jobs in July, with private sector payrolls up by 117,500 jobs and public sector payrolls up by 7,300 jobs. There was a downward revision to the initial estimate of June job growth, which is now pegged at 75,400 jobs rather than the initially reported increase of 80,600 jobs. Twelve of the fifteen in-footprint states saw nonfarm payrolls increase in July, although barely so in Mississippi, with Iowa, Kentucky, and Louisiana seeing declines. Though softening labor demand is resulting in a slower pace of hiring, the extent to which hiring slowed in June seemed odd to us at the time, particularly the pronounced slowdown in hiring in Florida and the sizable drop in employment in Indiana. That the July data show a marked reversal in both states may seem to align with our qualms about the reliability of the June data, but even if taking the average of June and July job growth seems a reasonable compromise, the two-month average of 110,100 net new jobs per month for the Regions footprint is still easily below the average monthly increases seen over the several months prior to June. In other words, it seems clear that the underlying trend rate of job growth is slowing, and that is the case nationally and within the footprint. That said, it is significant that the slowing pace of job growth is, at least thus far, strictly a function of a slowing pace of hiring, as opposed to a rising pace of layoffs. The slowing pace of hiring is something we've been expecting, and discussing, for some time now and, as such, is not overly concerning. But, should the pace of layoffs pick up and continue to accelerate, that would be a clear sign that something less benign than the expected slowdown in the pace of overall economic activity is playing out.





We have for some time used this space to show, and discuss, how current levels of nonfarm employment in each state compare to the pre-pandemic peak. Those comparisons, though flattering most of the Regions footprint, haven't changed for some time, at least in a relative sense. The level of employment within the Regions footprint is much further above the pre-pandemic peak than is true for the U.S. as a whole, with eleven of the fifteen states seeing larger advances, including some of the largest in the nation, while payrolls in Iowa and Illinois are little changed from and payrolls in Louisiana remain well below their pre-pandemic peak. As such, in the second chart above we take another cut of the data – the year-to-date percentage change in the level of nonfarm employment – to show how the states within the Regions footprint stack up with the rest of the nation. As it turns out, Kentucky has seen nonfarm employment increase by 1.92 percent thus far in 2023, despite the wobble in July, edging out the 1.88 percent increases in North Dakota and South Carolina and the 1.86 percent increase in Idaho (we went to two digits to break the ties). At the other end of the spectrum, Mississippi is one of just five states in the U.S. in which nonfarm employment had declined on a year-to-date basis through July, while of all the states in which nonfarm payrolls have risen thus far in 2023, Iowa has posted the smallest advance. Note that while Louisiana has seen year-to-date job growth of 1.05 percent, a bit below the U.S. average of 1.17 percent, the level of nonfarm employment in the state remains 1.79 percent below the pre-pandemic peak, the fifth largest remaining shortfall in the U.S. This is indicative of how much longer

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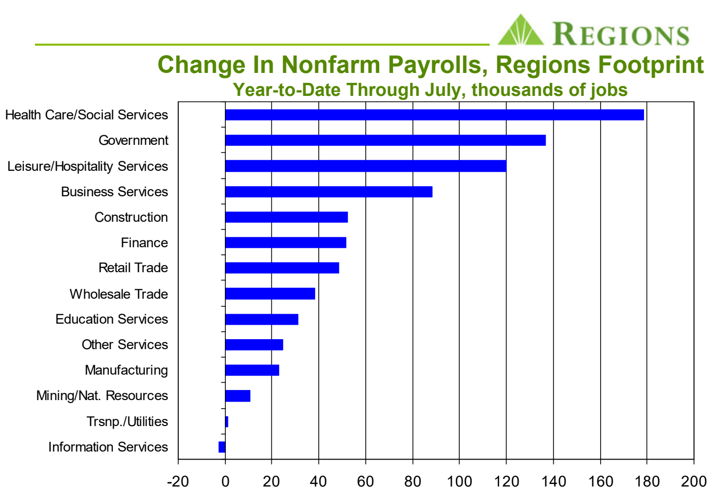
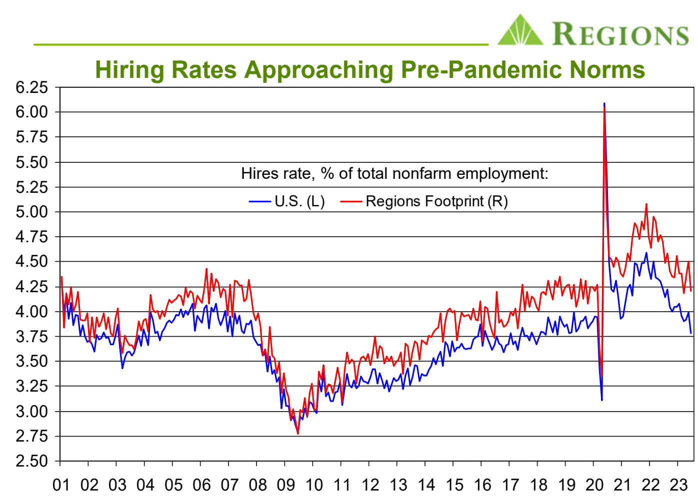
it took for Louisiana's labor market to gain traction after the pandemic-related distortions than was the case for most states, but of more relevance at present is that the state is making steady progress in closing that remaining shortfall.

Whether it is ranking year-to-date job growth or comparing current and pre-pandemic levels of employment, all of these comparisons come with a significant caveat in the wake of the recent preview of the looming benchmark revisions to the establishment survey data offered by the Bureau of Labor Statistics (BLS). The BLS's preliminary estimate suggests the level of nonfarm employment will be revised down by 306,000 jobs as of March 2023, with the level of private sector employment revised down by 358,000 jobs. Though larger than the typical benchmark revision, this is nonetheless smaller than we had anticipated. The biggest downward revisions will be to payrolls in the transportation & warehousing services, business services, and health care/social services industry groups. As a general rule, the revisions to the state level data are larger than those to the national level data, and the revisions to the metro area level data are larger than those to the state level data, but we will not know the details on the state and metro area levels until next spring. Keep in mind that the downward revisions to the level of nonfarm employment will in turn impact estimates of personal income.

Keep in mind that not only will the estimates of employment, hours, and earnings change across states in the revised establishment survey data, but so too will the estimates of job growth across the broad industry groups. Based on the data now at hand, however, it remains the case that job growth has become more narrowly based across private sector industry groups over recent months. For instance, health care/social services (health care accounts for over three-quarters of employment in this broad category) accounted for over one-third of all private sector job growth within the footprint in July and, as seen in the first chart below, has far and away added more jobs in 2023 than any of the other broad industry groups. At the same time, hiring amongst state and local governments, much of which has been fueled by the flow of federal funds to support infrastructure projects, has contributed mightily to the increase in public sector payrolls seen thus far in 2023, though it does bear noting that public sector payrolls within the Regions footprint remain over forty thousand jobs below the pre-pandemic peak. We'll also add that the reported July increases in payrolls in wholesale trade and leisure and hospitality services look oddly large to us, as job growth in both industry groups had softened considerably over the prior several months, so it remains to be seen whether these initial estimates for July withstand revision, to be reported next month with the August data. Even if these initial estimates do survive, it is highly unlikely that July heralded a sustained reacceleration in job growth in these two industry groups.





This gets to our point about the narrowing base of private sector job growth. As we discussed in last month's edition, shifting patterns in consumer spending have taken a toll on hiring in wholesale trade, retail trade, and warehousing/distribution services. At the same time, paring back of what had been aggressive hiring across the tech sector in 2020 and 2021 has taken a toll on payrolls in the information services industry group over the past several months. Though still up on a year-to-date basis, manufacturing payrolls have been most uneven over the past several months, and July's reported increase in manufacturing payrolls could reflect seasonal adjustment noise around employment amongst motor vehicle producers, the broader point being that the long-running contraction in the factory sector has weighed on employment. Even amongst the industry groups with the strongest year-to-date performance, it is fair to wonder how much longer this can be sustained. If, as we expect, consumer spending on discretionary services slows after the summer, that would take a toll on payrolls in leisure and hospitality services. At the same time, the rate at which state and local governments take on workers for infrastructure projects figures to slow at some point, as does the pace of hiring in the health care sector.

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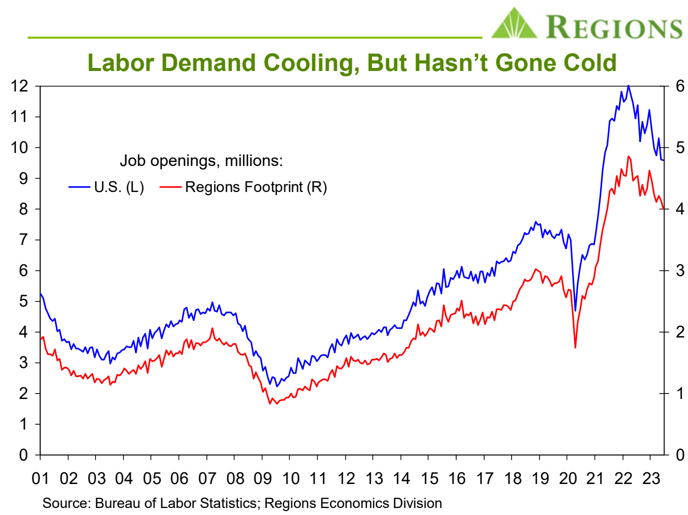
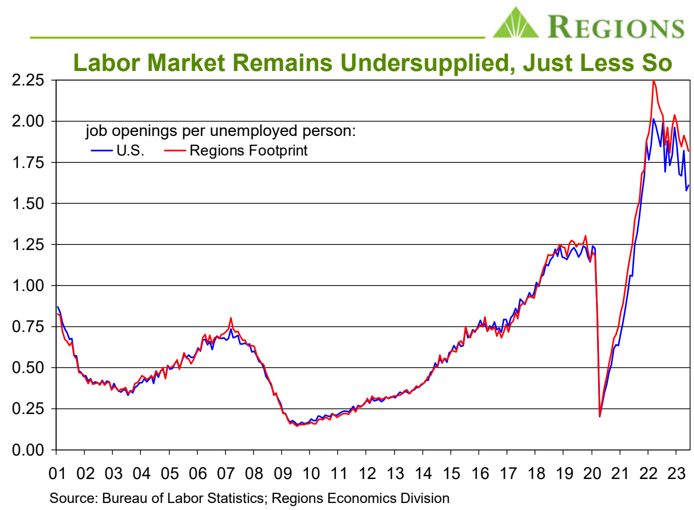
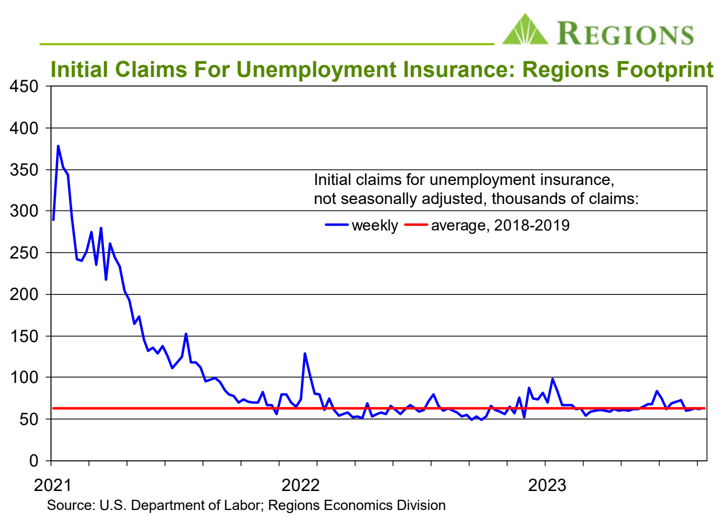
It is, then, reasonable to expect the hiring rate to slow further over coming months and, if so, this ensures continued deceleration in the pace of job growth even in the absence of a meaningful increase in layoffs given that the monthly job growth number is a net, not a gross, number. One indication that the pace of hiring is set to slow further is that the number of job vacancies continues to recede from the peak seen in early-2022, both nationally and across the Regions footprint. To be sure, the ongoing decline in job vacancies is not occurring in a straight line, in part because the economic data seldom, if ever, move in straight lines, but also in part because the sample from which the Job Openings and Labor Turnover Survey (JOLTS) data are drawn is so limited in nature, which all but ensures a high degree of volatility from one month to the next. To that point, we have considerably less confidence in any of the levels reported in the JOLTS data – vacancies, hirings, layoffs – than we do in the trends seen in the data. As the charts below make clear, those trends are firmly pointing downward when it comes to the number of vacancies and also when it comes to scaling the number of vacancies to the number of unemployed persons. It is also consistent that the ratio of job openings within the Regions footprint is higher than the national average given what has been consistently faster job growth within the footprint.





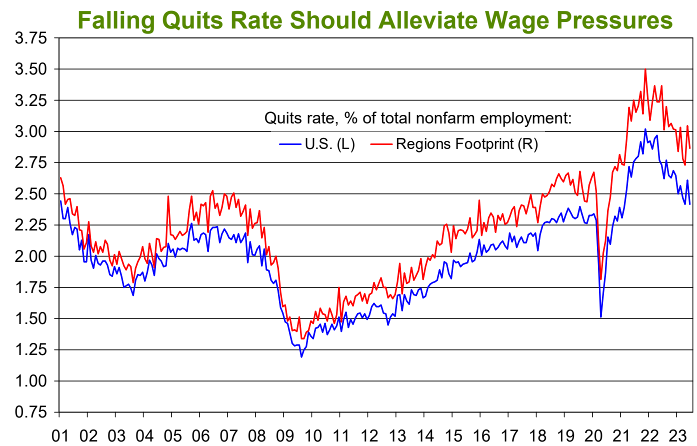
Though the pace of hiring has clearly slowed, thus far there has been no appreciable upturn in layoffs, whether one looks to the JOLTS data or to the weekly data on initial claims for unemployment insurance. The rate at which firms are laying off workers, i.e., the number of layoffs scaled to the level of nonfarm employment, continues to hover around one percent, nationally and within the Regions footprint, which in each case is lower than pre-pandemic norms. The weekly data on initial claims for unemployment insurance offer a more timely view of layoff patterns, and one way we've shown this is to compare current levels of filings to the average level in the two years leading up to the pandemic. Aside from what are normal seasonal bumps in the early weeks and middle weeks of any given year (we use the not seasonally adjusted data to get around what we believe to be seasonal adjustment issues in this series), claims continue to run below the pre-pandemic average, both nationally and within the Regions footprint.

Even as hiring has become more narrowly based across private sector industries, we have yet to see significant and widespread layoffs. This could suggest firms are to some degree engaging in "labor hoarding," hanging on to workers even when facing slowing demand on the expectation of demand picking up at some point in the future. That finding, and retaining, labor has been so difficult and so costly would motivate firms to engage in labor hoarding. Still, recent months have seen firms in the manufacturing sector begin to lay off workers after having given up on a rebound in demand any time soon, which should serve as a cautionary tale of the limits of labor hoarding. Moreover, that the trend in aggregate private sector hours worked has softened so considerably over recent months is another manifestation of easing demand for labor. While we believe there is further scope for firms to cut hours worked while retaining workers, absent a rebound in demand there will

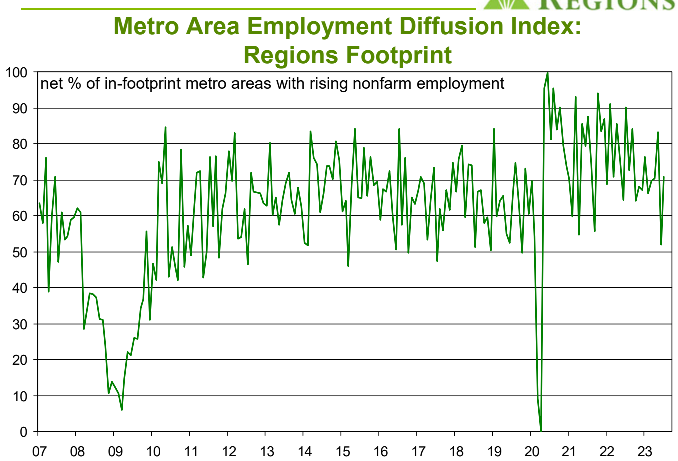


come a point when letting workers go is the more feasible option for firms.

It is also worth noting that the rate at which workers are voluntarily quitting jobs has fallen over the past several months but, both nationally and within the Regions footprint, remains above pre-pandemic norms. A falling quits rate could suggest workers are feeling less upbeat about labor market conditions and, as such, are becoming more inclined to stay put. One reason this matters is that there is ample evidence showing that job switchers tend to see much larger salary increases than do those workers who stay in the same job over time, so a falling quits rate could alleviate some of the upward pressure on wage growth. It is reasonable to think that, should job vacancies continue to fall as we expect, then so too will the quits rate, as falling job vacancies are a signal to prospective job switchers of dwindling opportunities for switching. It is noteworthy that quits rates in health care/social services and leisure and hospitality services, two of the industries in which job growth has been the strongest in 2023, have been slower to come down than has been the case in other industry groups, suggesting wage pressures in these industry groups have not subsided to the same degree as seen in other industry groups.



Source: Bureau of Labor Statistics; Regions Economics Division



Source: Bureau of Labor Statistics; Regions Economics Division

Finally, as we discussed last month, one thing that to us jumped out of the June data was a dramatic narrowing of job growth across the individual metro areas within the Regions footprint. The one-month hiring diffusion index, a measure of the breadth of job growth across in-footprint metro areas, fell sharply in June and the initial reading – 57.2 percent – was revised even lower and is now pegged at 52.0 percent. The hiring diffusion index bounced back to 70.7 percent in July. To be sure, the index is highly volatile from month to month, as seen in the chart to the side, but inherent volatility notwithstanding, there is a clear downward trend in the index. In other words, not only has job growth become more narrowly based across industry groups, but it is also becoming more narrowly based across in-footprint metro areas. This is not yet a concern, as the index remains above the upper end of the range that prevailed in the years prior to the pandemic, and we won't be surprised to see further declines in the months ahead. Keep in mind that the hiring diffusion index is a signal of the breadth of hiring, but not of the intensity of hiring, so the index settling back into the range that prevailed prior to the pandemic would not rule out further deceleration in the pace of job growth, which is what we expect to see in the months ahead.

We do expect the pace of hiring to continue to slow to the point that a much slower pace of hiring begins to push the unemployment rate higher despite labor force participation rates remaining below pre-pandemic norms, nationally and in most of the in-footprint states. As always, we will continue to monitor changes in labor market conditions for our in-footprint states and metro areas. In addition to these monthly updates of the state level employment data, we continue to produce our regular updates of state level claims for Unemployment Insurance and our regular monthly updates of state and metro area labor market, housing market, and personal income data, updates which can be found at either of the following sites:

https://www.regions.com/about-regions/economic-update or http://lifeatregions/Finance/MonthlyEconomicReports.rf