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Rise in unemployment may be temporary

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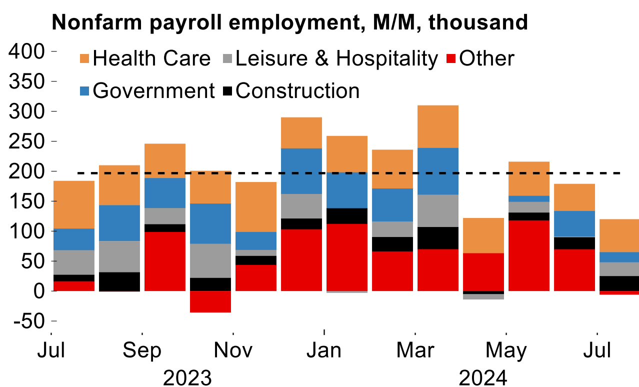
- Yet again, employment growth was strong in the “big four” industries, including health care, government, leisure and hospitality, and construction. For the remaining industries, growth was largely unchanged and illustrative of the weakest monthly jobs growth since October of last year. Employment growth has become less dispersed and more concentrated.
- The unemployment rate jumped to 4.3% in July, marking three consecutive months of growth. Unlike in prior months where growth was largely driven by new and re-entrants to the labor force, a sudden rise in layoffs is responsible for July’s increase. However, the share of job losers on permanent layoff fell, indicating that this latest rise in unemployment may be temporary.
- The ratio of job openings to unemployed shows a dramatic cooling in labor demand over the past several months, especially when excluding noncyclical government and health care. Additionally, the number of business bankruptcies rose sharply in June, exceeding the pre-pandemic level. It isn’t clear how well the birth-death model in the payroll survey is currently capturing jobs lost due to firm deaths, but signs are pointing to increased pressure on small businesses.

Weaker jobs growth and rising unemployment

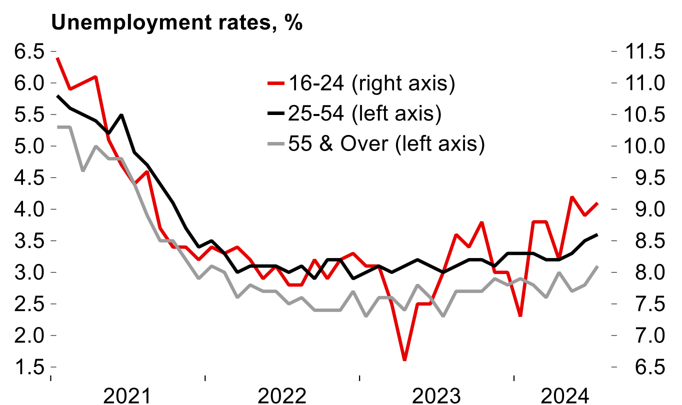
The labor market added 114,000 jobs in July, below the pre-pandemic average and the average over the last 12 months. As in prior months this year, health care, government, leisure and hospitality, and construction industries added the majority of jobs. Growth was effectively zero for the “other” industries, in aggregate, with the 14,000 jobs added in transportation and warehousing being offset by little to no change in other industries.

Chart 1: The “big four” industries continue to dominate employment growth



Note: Dotted line shows 2012-19 pre-pandemic average
Source: BLS, MUFG Bank Economic Research Office

Chart 2: The unemployment rate rose for all age groups in July, with growth in prime-age workers being the most consequential



Source: BLS, MUFG Bank Economic Research Office

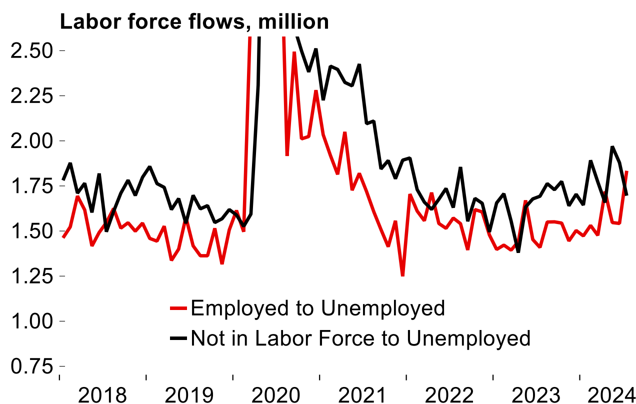
The last time growth was this weak in industries outside of the "big four" was in October 2023, when 36,000 jobs in "other" industries were lost (Chart 1). Back then, most of the jobs lost were in manufacturing due to the auto union strikes. Jobs growth did end up recovering in the auto sector in the following month, but other industries also experienced accelerated growth, notably in professional and business services.

There is some expectation that a similar type of recovery will occur next month in August, where certain industries return to positive jobs growth, but it is much less certain. Growth has been consistently weak in key industries, especially those in the goods sector, including manufacturing and retail trade. Any recovery in growth next month will likely be concentrated in services industries.

Consistent with the weak payroll numbers, the unemployment rate jumped to 4.3% in July, up from 4.1% in June. Shown in Chart 2, all age groups experienced a rise in unemployment, with growth in prime-age workers (25-54) being the most consequential given the outsized share of the labor force they represent. But up until now, rising unemployment could largely be attributed to growth in the labor supply, where new and re-entrants to the labor force produced a rising flow of persons not in the labor force to persons unemployed (Chart 3). July's rise is different, where the primary flow of labor went from employed to unemployed. In other words, a considerable rise in job losses drove the unemployment rate up in July.

However, most of these job losses are likely temporary. Shown in Chart 4, the share of job losses that are permanent fell sharply in July, indicating that temporary layoffs were the primary driver of job losses and the subsequent unemployment rate. The effects of Hurricane Beryl may have had some impact, even though the BLS officially stated "no discernible effect" on unemployment. Persistent heat waves in other parts of the country may have also contributed to growth in temporary layoffs.

Chart 3: Labor flows from employed to unemployed accelerated in July, indicating a rise in layoffs



Source: BLS, MUFG Bank Economic Research Office

Chart 4: Permanent job losers as a share of all job losers fell in July, with temporary layoffs leading the rise in unemployment

Source: BLS, MUFG Bank Economic Research Office

When observing unemployment growth by education, those with a high school diploma or less were the primary cause of July's rise. Workers with this educational background are concentrated in in-person and manual service jobs, many of which are hourly paid, where disruptions from extreme weather events are more likely to result in temporary job losses, as opposed to salaried office workers. Overall, the exact cause of the rise in temporary layoffs isn't certain, but it is expected to partially reverse in August.

Easing of labor shortages

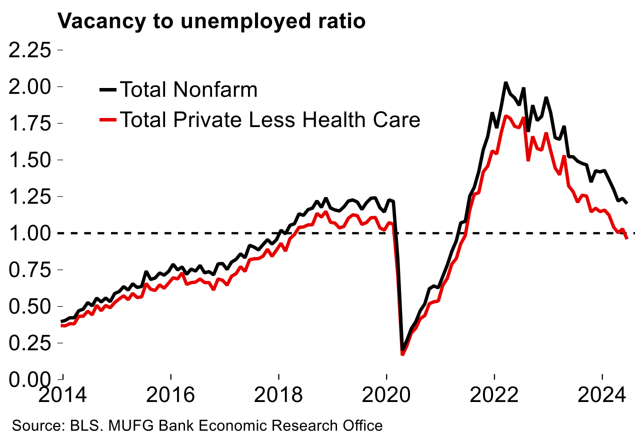
By nearly all metrics, the labor market is cooling relative to the last 6-12 months. However, caution should be used in interpreting some of these data and using them as definite signals. One such indicator is the hiring rate, which has fallen below its pre-

pandemic level, and continues to trend downward. At a surface level, this does represent a significant slowdown, but it has to be taken within the context of job quits and total separations, which have also fallen below their respective pre-pandemic levels. It is important to note that JOLTS hiring and separations data, which together equal jobs added, are level and trend adjusted to the CES payroll employment data. If payroll jobs numbers show employment growth, then JOLTS hires minus separations will show a similar level of jobs added. The focus should instead be on job openings, the most unique element of JOLTS data.

The good news, for consistency's sake, is that job openings also show a significant slowdown in the labor market. Shown in Chart 5, the total nonfarm vacancy to unemployed ratio fell to 1.2 in June and it is following along a relatively consistent downward trend. When excluding noncyclical government and health care industries, the ratio is below its pre-pandemic level and at the threshold that represents an equal number of job openings and unemployed persons (i.e., fewer labor shortages).

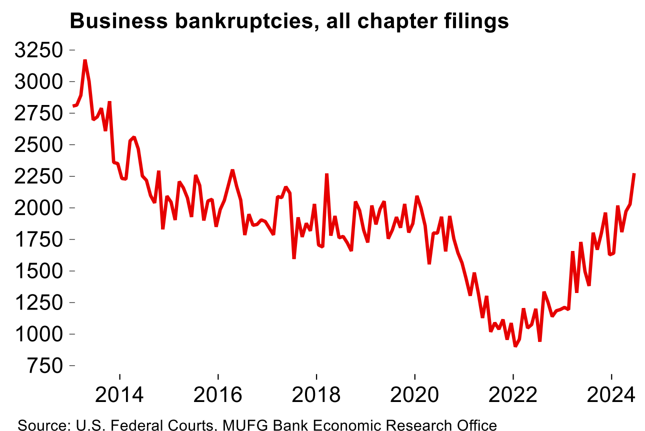
This cooling of labor shortages is also consistent with wage growth figures, with annual growth in wages and salaries for non-union workers from the Employment Cost Index (ECI) falling to 3.8% in Q2, down from 4.1% in Q1. Union workers exhibit a different trend with wages continuing to rise exponentially as a result of the many wage re-negotiations that occurred in Q4 2023.

Chart 5: The vacancy to unemployed ratio has fallen below 2020 levels when excluding government and health care



Source: BLS, MUFG Bank Economic Research Office

Chart 6: Business bankruptcies have risen sharply in June and are trending upward



Source: U.S. Federal Courts, MUFG Bank Economic Research Office

Though not explicitly a labor market indicator, there has been a considerable rise in the number of business bankruptcies that may or may not be fully reflected in current employment figures (Chart 6). Because it is difficult to capture employment losses in real time from firm deaths, the BLS utilizes a birth-death model that attempts to capture the jobs added from new firms and jobs lost from firms that go under. The relative accuracy of the model is typically not known until benchmark revisions are done, but the current rise in bankruptcies suggests that restrictive monetary policy is having a negative effect on firm profitability, which eventually translates into job losses in the labor market.

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