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PREVIEW: US Nonfarm Payrolls (July) released on August 2nd at 13:30BST/08:30EDT

SUMMARY: The rate of payroll additions is expected to ease in July, below the previous and also below recent averages. Fed Chair Powell has suggested that this is merely normalisation of the labour market, which was coming back into better balance while the unemployment remains low. The jobless rate is expected to be unchanged in July, still above where the Fed forecast it would be this year. Labour market proxies also allude to a slowing in payroll gains, with the weekly initial jobless claims data that coincide with the BLS survey window ticking up a touch, and continuing claims increasing, while the ADP's gauge of employment also disappointed expectations in the month. While the wage data are expected to continue easing, Fed officials' focus is now pivoting back onto both sides of its mandate (rather than its recent heavy focus on just inflation); accordingly, analysts have suggested that any downside surprised in the headline nonfarm payrolls data, or any tick-up in the jobless rate, could embolden calls for the Fed to begin cutting rates. Currently, money markets are certain that the Fed will cut rates by 25bps in September, and have also fully priced a second cut this year, while retaining a very high probability that we could even see a third cut before the year is out.

EXPECTATIONS: The consensus expects 175k nonfarm payrolls will be added to the US economy in July (vs 206k in June, vs 3mth avg of 177k, 6mth avg of 222k, and 12mth avg of 218k). The unemployment rate is expected to hold at 4.1% (vs FOMC June projections of 4.0% in 2024).

LABOUR MARKET PROXIES: Weekly initial jobless claims, coinciding with the BLS reference week for the June and July jobs reports, have been little changed (235.25k into the July report vs 233k into the June report); in the same reference period, continuing claims have picked up to 1.853mln from 1.814mln. The ADP's gauge of national employment showed 122k payrolls were added in July (exp. 150.0k, prev. 155k), while measures of wages also declined; the payrolls provider said that "with wage growth abating, the labour market is playing along with the Fed's efforts to slow inflation" adding that "if inflation goes back up, it won't be because of labour."

SAHM RULE: Former NY Fed President Dudley recently noted that the three-month average unemployment rate is up 0.43ppts from the low seen in the last 12 months, which is close to the 0.5 threshold that the 'Sahm Rule' identifies as a recession signal. Other analysts have looked through the potential signal; Capital Economics said that "even if the unemployment rate continues to rise by another 0.1ppts in July, the Sahm rule is highly unlikely to be triggered, as the earlier low of 3.5% in July 2023 drops out of the 12-month comparison period, and is replaced with a higher value of 3.7%." Additionally, CapEco argues that the recent rise in unemployment has been driven by falls in employment among those aged 16-24, as weaker hiring intentions hinders their ability to find summer jobs. "July is typically another strong month for hiring, so employment is likely to struggle in seasonally adjusted terms, keeping the unemployment rate at 4.1%," CapEco says, but "this distortion will unwind in September, when students return to education."

WAGES: The rate of average hourly earnings is again likely to print +0.3% M/M in July, which may be enough to take the annual rate lower to 3.7% Y/Y (prev. 3.9%). Within the ADP data, the median change in annual pay for job stayers eased to 4.8% Y/Y from 4.9%, while for job changers it eased to 7.2% Y/Y from 7.7%. Additionally, while the periods do not coincide, analysts note that the Q2 Employment Cost Index printed 0.9% (exp. 1.0%; prev. 1.2%); Wells Fargo said the data shows how employment cost growth is now closely approaching a pace consistent with the FOMC's 2% inflation objective, once accounting for productivity growth. However, traders note that the wages data may begin to get less attention as the Fed shifts its focus back onto both sides of its dual mandate.

FED IS SHIFTING FOCUS: At its July policy meeting, Fed Chair Powell indicated that officials were now pivoting their heavy focus on inflation back onto its dual mandate. Powell said the labour market was coming into better balance, and unemployment remains low, with data now suggesting that conditions have returned to where they were on the eve of the pandemic. Powell does not think the labour market is currently a source of inflation pressures, and that is why the Fed does not want to see excess cooling. Still, the softening in labour market conditions gives the Committee more confidence that the economy is not overheating. The Fed boss reiterated that if something looks like a significant downturn in the labour market, then the Fed would respond, adding that policy was in a good place to meet any challenges to its dual mandate. (NOTE: previously, Powell had caveated that there would need to be 'unexpected' weakness in the labour market, not just a few tenths rise in the jobless rate - but this was not something he specifically fleshed out at the July press conference). Ultimately, Powell's message was that if the Fed sees inflation move down with expectations, and growth remains reasonably strong, the labour market remains as it is, a rate cut would be on the table in September. Accordingly, analysts have said that downside prints in the labour market could embolden the case for rate cuts in September.

ANNUAL BENCHMARK REVISIONS: Ahead, analysts note that the BLS will release its annual benchmark revisions to the payrolls data on August 21st, as well as its Quarterly Census of Employment & Wages; "the sizeable divergence between the QCEW and nonfarm payroll figures suggest that the estimate will point to a sharp downward revision – although the data won't be formally changed until early next year," Capital Economics says, adding that "if more of the strength in payroll gains earlier this year was expected to be revised away, that would remove another potential barrier to interest rate cuts."

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