SkyView Investment Advisors:

The Dismal Employment Report

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The Job Report

Economists projected that September would show a gain of about 200,000 payroll jobs. Instead, the Bureau of Labor Statistics (B.L.S.) released an employment report showing a (pick your word) dismal, grim, or terrible – all used in various headlines – gain of only 142,000 jobs. And of that total gain, the private economy generated only 118,000 new positions. Even more downbeat to us, the B.L.S. revised downward both July and August gains by 59,000 jobs. This brings second quarter average payroll gains to 167,000. That compares to a monthly average of 198,000 for all of 2015. In 2014, monthly gains averaged 260,000. Revisions, up or down, will typically reflect the trend of that data. So these downward revisions add further disappointment to the results. And for a reference, the economy needs to create about 150,000 jobs to support new entrants into the job force.

The current labor participation rate is the lowest rate during a period of recovery since 1977.

The unemployment number remained unchanged at 5.1% but only as a result of the civilian labor participation rate declining to 62.4%. That level represents the lowest rate since 1977 during a period of recovery from an economic recession. Roughly 350,000 workers dropped out of the labor force. Again for reference, if the participation rate remained at levels before the great recession, roughly 5 million more payroll jobs would now exist.

And finally, the report showed a small monthly decline in the average workweek and flat hourly earnings. Compared to last year, hourly earnings increased 2.2%.

With all this less than heartening news, *Barron's* offered a glimmer of hope this weekend. Their " Economic Beat" column pointed out that "over the past five years, in every case, there has been some upward revision to the change initially reported in September." On average, that upward revision totaled 46,000 jobs. As we have seen with the first reported economic numbers, such as G.D.P., the revisions can be substantial.

The Fed in a Box Canyon

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Friday's dismal jobs report moves the Fed's zero interest rate policy (ZIRP) further into a box canyon—meaning no exit. The Fed seems trapped between the limited economic impact from its accommodative monetary policies and a lack of fiscal policies to aid the economy from a what appears to be a politically dysfunctional Washington. And any hope from that source seems unlikely as we approach the presidential election year.

In the past, we suggested that the Fed waited too long to make a modest increase to its Fed funds rate. Recent speeches by F.O.M.C. officials suggested a high probability of liftoff by year-end (please refer to our commentary: "Today's Insight: Yellen and the Fed Rate Decision"). And now, unless the Friday results prove a blip in slowing payroll growth, the timing of liftoff seems more uncertain.

In the Federal Funds Futures market, the odds for a rate increase by year end fell to roughly 30% on Friday (10/2/15). The 10-year note sank below 2%. At the same time, the two-year note fell to 0.58% which compares to 0.81% earlier in September. The financial markets now give low credence to lift off in December. Therefore, any Fed liftoff by year end, with little change in the economic environment, would likely result in significant turbulence in the financial markets.

Liftoff and the Stock Market Outlook

Since 1953 the stock market has never peaked until after the Fed has begun raising interest rates.

Trying to add a note of cheer, Omega Advisors reports that since 1953 the stock market has never peaked until after the Fed has begun raising interest rates. On average, the stock market reaches this high 30 months after liftoff. Of course, that proved true in the "old normal." The question will be whether this history repeats itself in the so-called "new normal." To add to that comment, normally a recession does not show up before the yield curve inverts. At present, the yield curve, 2-10 year, remains positive.

Third Quarter Outlook

The Fed's October meeting takes place on October 27-28. The next day, October 29, the third quarter advance GDP report should be released. As we learned this year, the advance GDP report will be subject to revisions and they can be substantial.

We would expect that forecast range for GDP growth in the third quarter declined as a result of last Friday's payroll results.

The Atlanta's Fed " GDP Now" report shows GDP forecasts both from its own quantitative model as well as those of the "blue chip financial forecasts." As of October 1, 2015, the Atlanta Fed model projected third quarter growth of 0.9%. In comparison, the blue chip forecasters showed a range of 1.8-3.0% for GDP growth in the third quarter. The average came in at about 2.5%. We would expect that forecast range declined as a result of last Friday's payroll results.

What Does the Fed Know?

During periods of economic surprise (positive or not) I like to reprint from the 2012 speech given at the Harvard club of New York City by Richard W. Fisher, then president of the Federal Reserve Bank of Dallas. I find this speech offers some perspective on what the Fed and other central banks face in dealing with the recovery from the great recession. Here is that quote:

"The truth, however, is that nobody on the committee, nor on our staffs at the board of governors and the 12 banks, really knows what is holding back the economy. Nobody really knows what will work to get the economy back on course. And nobody, in fact, no central bank anywhere on the planet—has the experience of successfully navigating a return home from the place in which we now find ourselves. No central bank—not, at least the Federal Reserve— has ever been on this cruise before."

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