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www.eurobank.gr/research
research@eurobank.gr

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GLOBAL ECONOMIC & MARKET OUTLOOK

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FOCUS NOTES

US October employment report strengthens the case for a December fed funds rate hike

Olga Kosma
Economic Analyst
okosma@eurobank.gr

- US nonfarm payrolls increased by 271k in October -the largest rise since December 2014- surpassing consensus expectations for a rise of 185k. Adding to the positive tone of the report, the respective figures of August and September were revised higher by 12k cumulatively, with the three-month moving average increasing to 187k from 171k previously (Figure 1). The increase in nonfarm payrolls in October was mainly driven by the private sector, which rose by 268k.

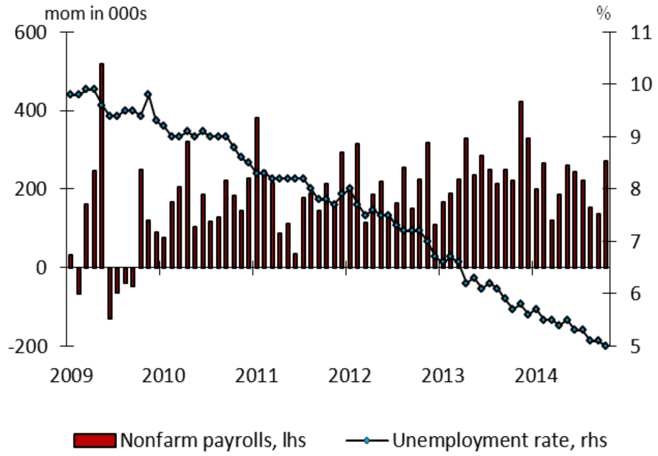
- Civilian household employment gained 320k, while the civilian labor force rebounded by +313k with the participation rate rising slightly to 62.43% from 62.36% in September. As a result, the unemployment rate improved marginally in October to 5.0% from 5.1% in the prior month (on an unrounded basis the improvement was minor to 5.04% from 5.05%), reversing May-to-September's trend where the cumulative improvement in the unemployment rate (-0.4 pps, from 5.5% to 5.1%) was due to a decline of 754k in the labor force which cut back the participation rate to multi decade lows.

- Average hourly earnings increased by a higher than expected 0.4%MoM, boosting the annual rate of growth to a six-year high of 2.5%, from 2.3% in September (Figure 2). Meanwhile, the average workweek was unchanged at 34.5 hours. The above mentioned acceleration was a very important aspect in the positive tone of October's US employment data, given that wage growth has been subdued for a long time in spite of the downtrend in the unemployment rate and the general improvement in labor market conditions.

- Responding to stronger than expected US nonfarm payroll data, US Treasuries weakened while the US dollar firmed across the board. The DXY was hovering within distance from last week's 6 ½ month high of 99.345 in early European trade on Monday and the EUR/USD was trading close to 1.0770/80, not far from a 7-month trough of 1.0706 hit in the last Friday's session. With diverging Fed and ECB monetary policy outlooks continuing to play a key role in FX markets, the EUR/USD seems vulnerable to further weakness in the coming sessions. Technically, a sustained move below recent lows could pave the way for further decline towards 1.0500 or lower.

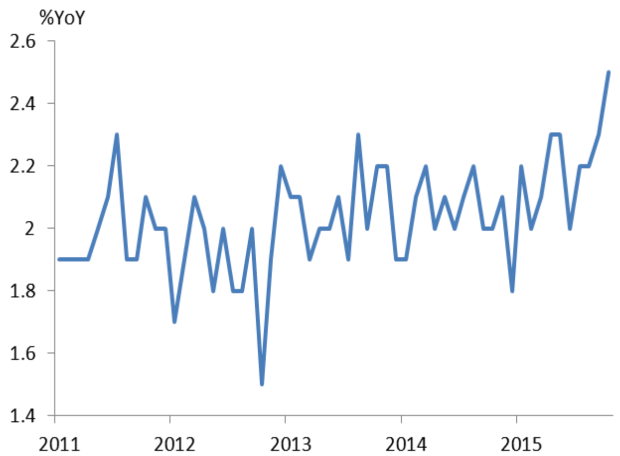
- Encouraging October labor market data prompted a hawkish shift in market expectations for a December Fed rate hike to ca. 80% from c. 40% late last week ahead of the release of the said report. Additionally, the tone of the policy statement released after the conclusion of the 27-28 FOMC meeting was more hawkish than expected, with the Fed downplaying global economic headwinds and making a specific reference on the factors the FOMC will have to assess "in determining whether it will be appropriate to raise the target range at its next meeting". Adding to this, in her testimony to the House Financial Services panel last week, Fed Chair Yellen highlighted that the US domestic economy is "pretty strong" and that the Fed expects the economy to continue to grow at a pace that could return inflation to the 2% medium-term target and generate further improvement in labor market conditions. That said, an increase in the fed funds range to 25-50bps at 15-16 December FOMC meeting from 0-25bps currently now seems highly likely. This holds provided that upcoming US data ahead of the FOMC December meeting will not yield any major negative surprise.

Figure 1: US nonfarm payrolls & the unemployment rate



Source: US Bureau of Labor Statistics (BLS), Bloomberg, Eurobank Economic Research

Figure 2: US average hourly earnings



Source: US Bureau of Labor Statistics (BLS), Bloomberg, Eurobank Economic Research

Eurobank Economic Analysis and Financial Markets Research

Dr. Platon Monokroussos: *Group Chief Economist*
pmonokrousos@eurobank.gr, + 30 210 37 18 903

Dr. Tassos Anastasatos: Deputy Chief Economist
tanastasatos@eurobank.gr, + 30 210 33 71 178

Research Team

Anna Dimitriadou: *Economic Analyst*
andimitriadou@eurobank.gr, + 30 210 37 18 793

Ioannis Gkionis: *Research Economist*
igkionis@eurobank.gr + 30 210 33 71 225

Stylianos Gogos: *Economic Analyst*
sgogos@eurobank.gr + 30 210 33 71 226

Olga Kosma: *Economic Analyst*
okosma@eurobank.gr + 30 210 33 71 227

Arkadia Konstantopoulou: *Research Assistant*
arkonstantopoulou@eurobank.gr + 30 210 33 71 224

Paraskevi Petropoulou: *G10 Markets Analyst*
ppetropoulou@eurobank.gr, + 30 210 37 18 991

Galatia Phoka: *Research Economist*
gphoka@eurobank.gr, + 30 210 37 18 922

Theodoros Stamatiou: *Senior Economist*
tstamatiou@eurobank.gr, + 30 210 33 7 1 228

Eurobank Ergasias S.A, 8 Othonos Str, 105 57 Athens, tel: +30 210 33 37 000, fax: +30 210 33 37 190, email: EurobankGlobalMarketsResearch@eurobank.gr

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