Economic Analysis

Labor market collapse begins

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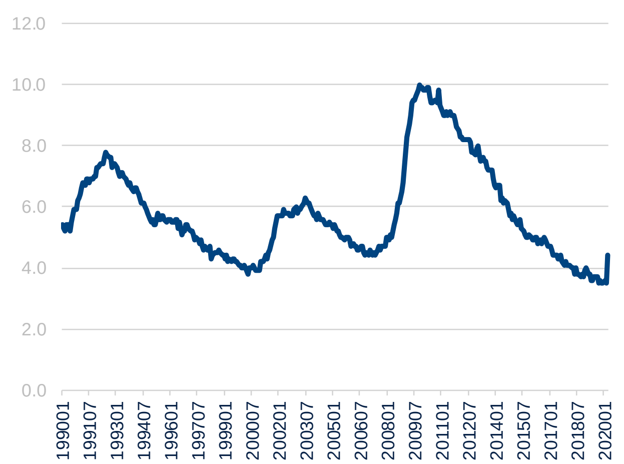
March's labor market report fell short of matching the unfathomable increases in initial unemployment insurance claims seen over the past two weeks with the unemployment rate increasing to 4.4% (the largest month-over-month percentage point increase since January 1975) and nonfarm payrolls decreasing by 701K. Ultimately, this report marks only the beginning of a period of unprecedented weakening in the labor market.

As expected, the majority of the weakness was in leisure and hospitality (-459K) of which 90% occurred in food service and drinking places. Areas such as health care and social assistance (-61K), professional and business services (-52K), retail trade (-46K), manufacturing (-18K) and construction (-29K) were not immune to the contagion with combined job losses of 206K.

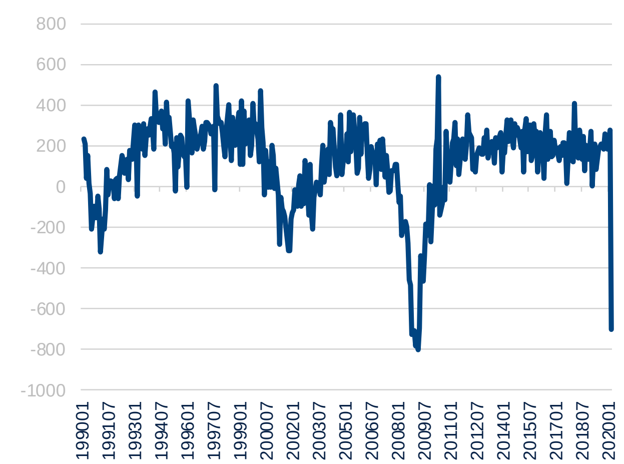
Based on the unprecedented churn in the labor market, the number of people reporting being temporarily laid off doubled to 1.8M while the number of permanent job losers increased from 177K to 1.5M. Similarly, the household measure of employment dropped by 3.0 million, pushing the employment-to-population ratio down 1.1pp to 60%. In addition, about 0.7 percent of the labor force exited due to the impact of COVID-19, pushing the labor force participation rate to 62.7%.

Figure 1. **Unemployment Rate** (%)



Source: BBVA Research and Haver Analytics

Figure 2. **Nonfarm Payroll** (MoM change, thousands)



Source: BBVA Research and Haver Analytics

Going forward, we expect there to be a nontrivial drop in employment leading to a dramatic rise in the number of unemployed. By the end of the second quarter, our baseline assumes around 14 million more people will become unemployed (around 20M total), pushing the unemployment rate above 12%.

The enhanced social insurance measures included in the recent fiscal stimulus package should moderate the impact to individuals and households, but could distort the incentives to remain working or in the labor force leading to greater outflows. How effective and efficiently the current policy measures are implemented will determine the rate of inflow and outflows and the magnitude of the contraction in the labor market.

In terms of the Fed, today's report falls within their range of expectations and is consistent with its strategy of doing whatever it takes. In the short-term, the measures taken to date are also consistent with a more dire economic scenario, suggesting that further weakening in upcoming economic data will not prompt more dramatic actions. That said, if the crisis is prolonged into the second half of 2020, or if there is a significant resurgence in cases and lockdown efforts in 2H20 or 1H21, there remains the potential for the Fed to reach further into their tool kit. On the fiscal policy side, an array of policymakers will look at the latest weakness in labor markets to push ahead with a Phase 4 stimulus package.