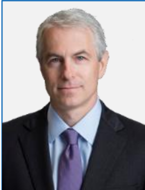
MACKAY SHIELDS
A NEW YORK LIFE INVESTMENTS COMPANY
MACRO RESEARCH

A Close VIEW

No, Record-High Job Openings Do Not Improve Prospects for a Soft Landing

MAY 17, 2022



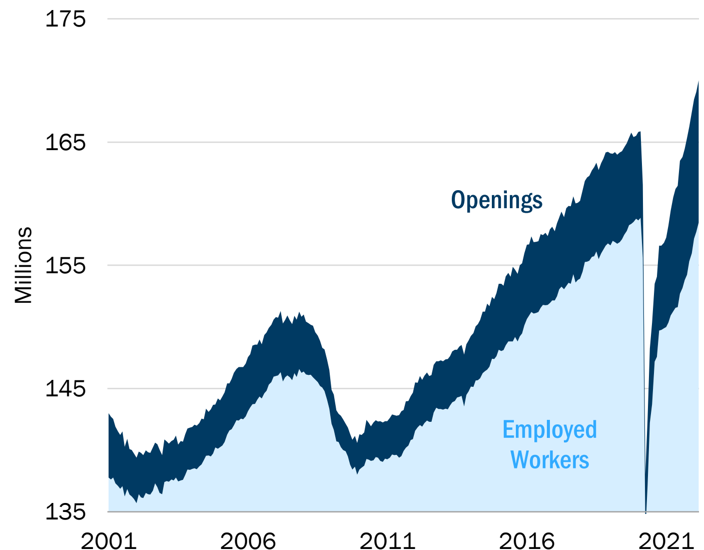
Authored by Steven Friedman
Senior Macro Economist

Chair Powell has stated that the high level of openings affords policy-makers the opportunity to fine-tune labor demand without causing a recession. The historical record indicates otherwise.

Market movements following the May 4 Federal Open Market Committee meeting suggest that investors have grown more cautious regarding prospects for the economy over the medium term. Since the market close on May 3, the S&P500 index is down four percent, high yield nonfinancial corporate spreads to Treasuries have widened by over 70 basis points, and the dollar extended its recent appreciation against other major currencies.[1] This market reaction comes even as Powell laid out a possible path to lower inflation and a continued expansion – a soft landing.

In addition to the fading of pandemic-related supply constraints, Powell's soft landing assigns an important role to the record-high level of job openings in the economy (Figure 1). Specifically, Powell noted that tighter monetary policy can slow the economy just enough to lead to a decline in openings without increasing the unemployment rate. This decline in openings would in turn bring overall labor demand into better alignment with supply, reducing upward pressure on wages and, hence, inflation. But with little to no change in the unemployment rate, consumer spending would not moderate, and a contraction could be avoided.

FIGURE 1: COMPONENTS OF LABOR DEMAND



Source: Bureau of Labor Statistics

That a moderation in job openings can serve as a release valve for inflation without jeopardizing the expansion is an interesting idea. It is also an idea that is testable, by examining the historical relationship between openings and the unemployment rate. The Bureau of Labor Statistics' Job Openings and Labor Turnover Survey (JOLTS) is an excellent source of information on openings in the economy, but only goes back to 2001. I use data from the National Federation of Independent Businesses (NFIB) as a proxy for job openings over a longer time period. The NFIB's monthly survey has asked member firms since 1973 if they have open positions that they are unable to fill; the NFIB reports the percent of firms that answer in the affirmative. As seen in Figure 2 on the next page, the results from this question correlate well with the number of openings reported in the JOLTS.

1. Equity and high yield spread moves are through May 16. Corporate spreads based on the ICE BofA US High Yield Index.

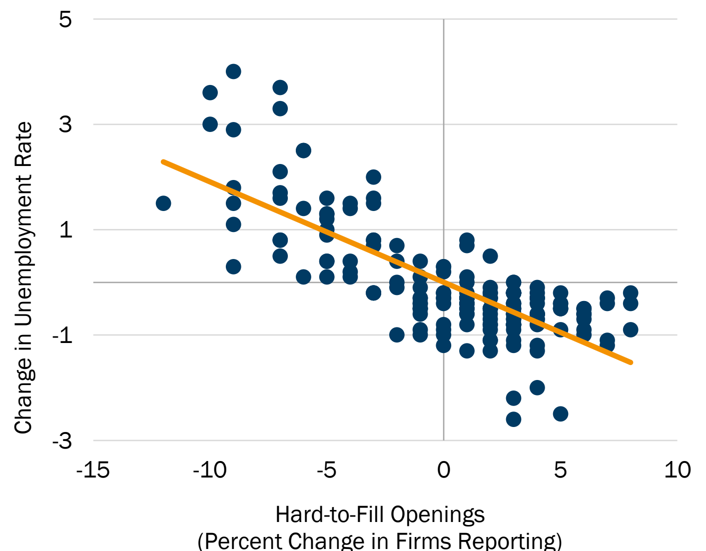
Figure 3 shows the year-over-year change in firms reporting hard-to-fill openings along the horizontal axis, and the year-over-year change in the unemployment rate on the vertical axis. A decline in hard-to-fill openings – my proxy for job openings in the economy – is associated with an increase in the unemployment rate. In fact, once the number of firms reporting hard-to-fill openings falls by four percentage points over a given year, there are no observations in the data of a stable or falling unemployment rate. And it is likely that hard-to-fill openings would have to fall by much more than this to bring labor demand into better balance with labor supply. For example, the pre-pandemic peak in firms reporting hard-to-fill openings was 39 percent, eight percentage points below the most recent reading for April. The historical record suggests that sort of decline in openings would likely see an increase in the unemployment rate of more than half a percentage point, an increase that has been associated with the start of recessions.[2]

Chair Powell has kept a brave face when discussing the path ahead for the economy. Unfortunately, the historical relationship between job openings and the unemployment rate suggests that it will be extremely difficult for monetary policy to fine-tune labor demand so carefully that inflation can fall back down to two percent without causing an economic contraction. The reason is straightforward – the reduction in job openings would come about from a decline in aggregate demand, the very same condition that leads to an increase in unemployment. Risks of a contraction may not be imminent, but history suggests that they will rise materially as policymakers work to cool off labor demand.

FIGURE 2: PROXYING OPENINGS WITH FIRMS REPORTING POSITIONS NOT ABLE TO FILL

Source: National Federation of Independent Businesses, Bureau of Labor Statistics. Shaded areas represent recessions.

FIGURE 3: A REDUCTION IN OPENINGS TENDS TO INCREASE THE UNEMPLOYMENT RATE



Source: National Federation of Independent Businesses, Bureau of Labor Statistics. Data from 1975 - 2019. Unemployment rate changes lagged by one quarter.

2. For example, economist Claudia Sahm has tied a 0.5 percentage point rise in the three-month moving average of the unemployment rate from its low of the previous 12 months to the start of a recession. See Claudia Sahm, "Direct Stimulus Payments to Individuals", Brookings, May 16, 2019.

IMPORTANT DISCLOSURE

Availability of this document and products and services provided by MacKay Shields LLC may be limited by applicable laws and regulations in certain jurisdictions and this document is provided only for persons to whom this document and the products and services of MacKay Shields LLC may otherwise lawfully be issued or made available. None of the products and services provided by MacKay Shields LLC are offered to any person in any jurisdiction where such offering would be contrary to local law or regulation. It does not constitute investment advice and should not be construed as an offer to buy securities. The contents of this document have not been reviewed by any regulatory authority in any jurisdiction. This material contains the opinions that are incorporated into portfolios managed by MacKay Shields Global Fixed Income and Global Credit teams. The opinions expressed herein are subject to change without notice. This material is distributed for informational purposes only. Forecasts, estimates, and opinions contained herein should not be considered as investment advice or a recommendation of any particular security, strategy or investment product. Information contained herein has been obtained from sources believed to be reliable, but not guaranteed. Any forward-looking statements speak only as of the date they are made and MacKay Shields assumes no duty and does not undertake to update forward-looking statements. No part of this document may be reproduced in any form, or referred to in any other publication, without express written permission of MacKay Shields LLC. ©2022, MacKay Shields LLC. All Rights Reserved.

NOTE TO EUROPEAN INVESTORS

This document is intended for the use of professional and qualifying investors (as defined in the Alternative Investment Fund Manager's Directive) only. Where applicable, this document has been issued by MacKay Shields Europe Investment Management Limited, Hamilton House, 28 Fitzwilliam Place, Dublin 2 Ireland, which is authorized and regulated by the Central Bank of Ireland.