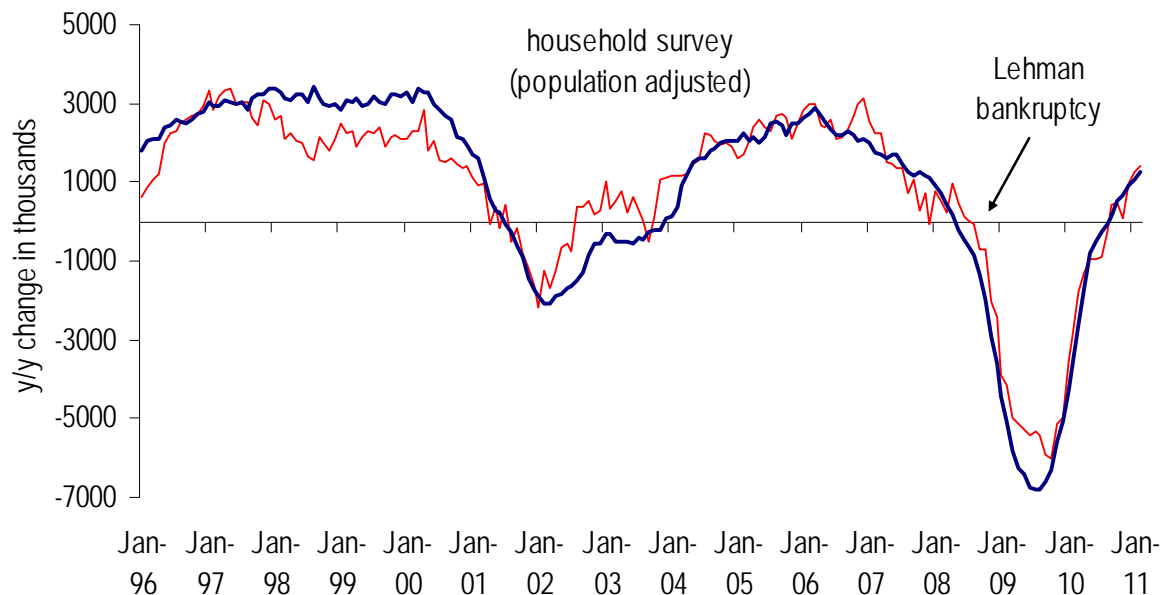


# Payrolls Improving; Unemployment at 8.9%; Millions To Hit 99 Week UI Limit

All surveys are now showing a meaningful improvement in the labor environment. In February, the establishment survey (our least favorite at inflection points) joined the already strong signals coming from initial claims, ISM, ADP and the household survey.

- Payrolls grew 192,000 in February with an additional 58,000 in upward revisions from December and January.
- The household survey added 250,000 jobs in February on top of the 589,000 added in January. Bloomberg is still showing only 117,000 gains in January, but that doesn't correctly factor in the annual population adjustment, instead comparing the estimated number employed based on the smaller January 2011 population to the estimate for the larger, unadjusted December 2010 population. Based on the Department of Labor's population adjustment technique, **the household survey is finally showing stronger gains than the establishment survey -- up 1.1 million in the last three months versus 407,000 for the establishment survey -- an important inflection point.**

## Annual Growth in Employment (last obs. February 2011)



Source: Bureau of Labor Statistics; Encima Global

**This is still a weaker-than-normal expansion. Unemployment is high at 8.9%, underemployment is 15.9%, and most measures of income growth are weak.**

- **14.5 million people are unemployed (13.7 million on a seasonally adjusted basis). Of them, 9.2 million are collecting unemployment insurance. Underemployment is 24.7 million.**
- Hourly wages rose \$0.01 to \$22.87 in February and have been increasing less than 2% per year since 2009, one of the weakest periods on record. This is below the inflation rate many people are feeling, meaning living standards are falling for them. We think the weak dollar contributes to this by driving up commodity prices more than wages.

**Average Hourly Earnings (last obs. February 2011)**

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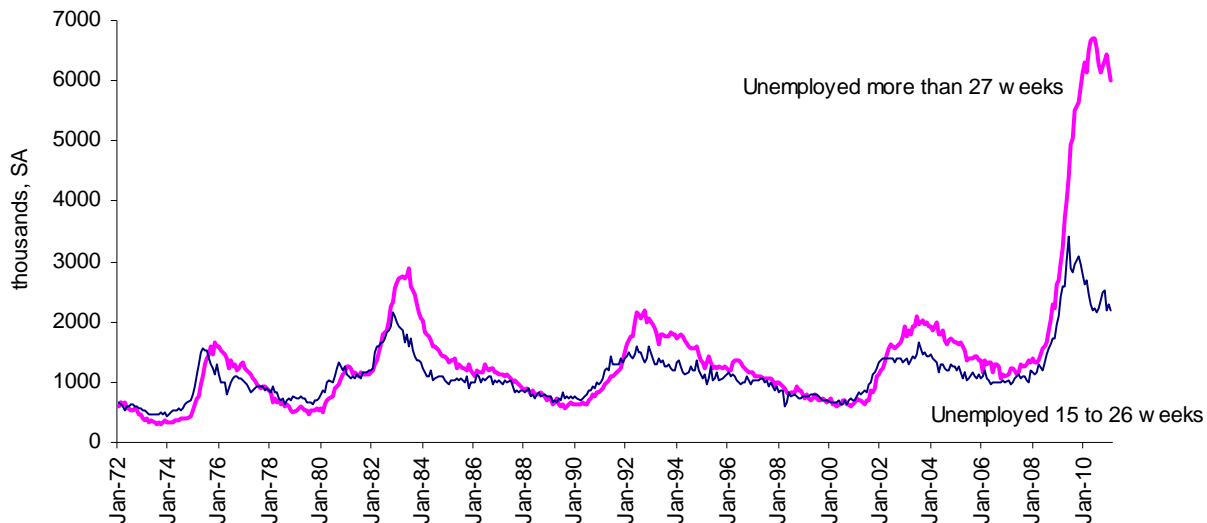



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Source: Bureau of Labor Statistics; Encima Global

- Most of the net job gains are going to the short-term unemployed. Fewer new jobs are going to the long-term unemployed, pointing to **a new under-class – people who used to work but won't be able to after the 2008 Lehman bankruptcy**. Early retirement applies to some, but even in those cases, incomes are probably below their expectations.
- There are now 6.0 million workers unemployed for more than 27 weeks (peak was 6.7M in May). The number of unemployed between 15 and 26 weeks stands at 2.2 million, well below the peak of 3.4 million in June 2009. The average duration of unemployment is particularly long at 37.1 weeks, while the median duration of unemployment has fallen to 21.2. This shows a bifurcation – long-term unemployed are not finding jobs as readily as those who lost their jobs more recently.

### Unemployed Longer than 27 Weeks (last obs. February 2011)

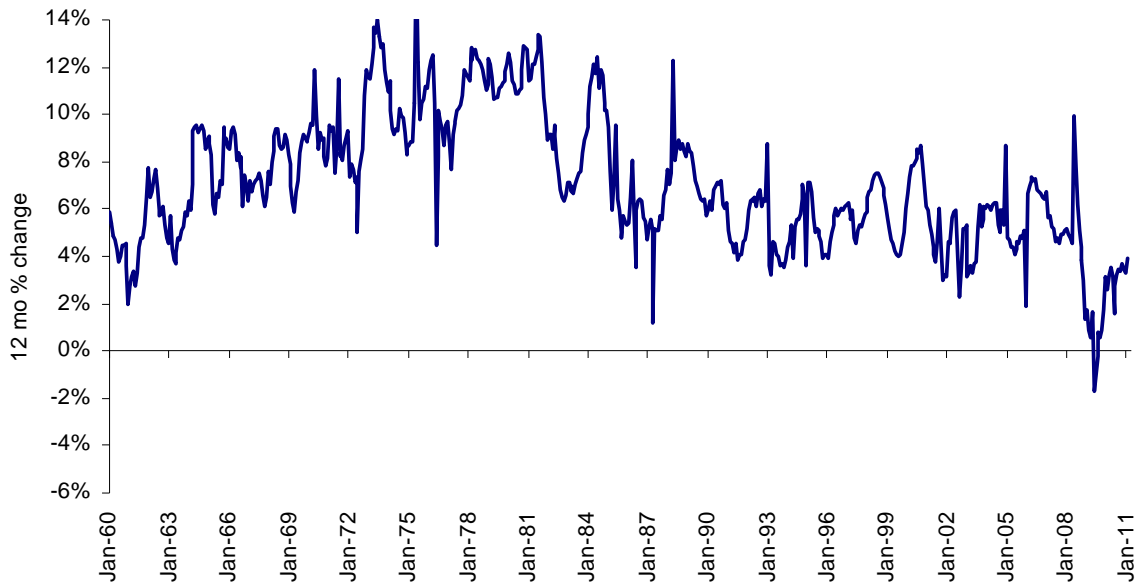


Source: Bureau of Labor Statistics; Encima Global

- Roughly 3.3 million long-term unemployed will reach the 99 week insurance limit during the remainder of 2011, with roughly another million losing federal unemployment benefits in January 2012 assuming federal benefits are discontinued then. Some will find work and many will drop out of the labor force, creating substantial downward pressure on the unemployment rate partially offset by the overhang in the labor force.

- Hitting the 99 week limit will also put downward pressure on already-weak income growth. Disposable personal income is up only 3.9% year-over-year, less than almost any pre-2008 rate. There will be a boost in personal income and DPI in 2011 due to the 2% reduction in the social security tax, but most of this is offset in DPI by the end of the Making Work Pay credit.

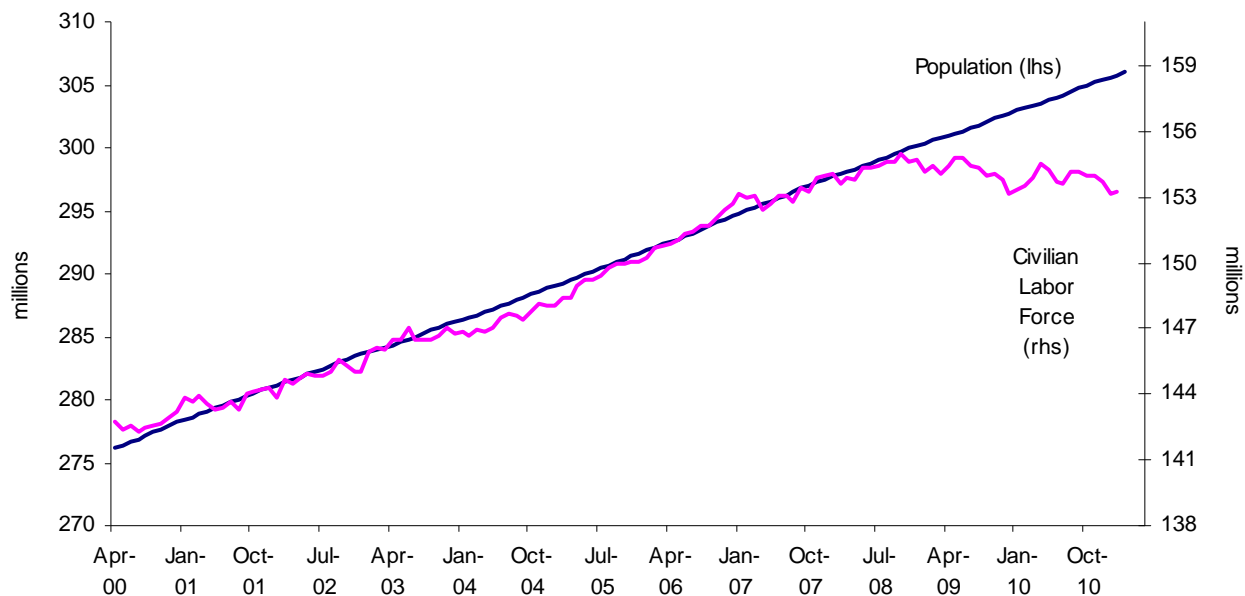
### Disposable Personal Income (last obs. January 2011)



Source: Bureau of Economic Analysis; Encima Global

- While part of the decline in unemployment is due to job growth, part is due to the ongoing decline in the labor force as workers stop looking. The civilian labor force peaked at 155 million in October 2008 and stood at 153.2 million in February (up 60,000 from January.) With the baby boom entering retirement, we expect only slow labor force growth in coming decades, one of several factors arguing for below average GDP growth in coming business cycles. Japan has been seeing a decline in its labor force since the late 1990s, while China's labor force is expected to peak late this decade. In contrast, the U.S. labor force, after a pause over the next two decades is expected to grow into the middle of the century, setting the U.S. apart from other industrialized countries and from China.

### Civilian Labor Force and Population (last obs. February 2011)



Source: Bureau of Labor Statistics; Encima Global

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