First Trust
Monday Morning OUTLOOK

Brian S. Wesbury – *Chief Economist*
Robert Stein, CFA – *Dep. Chief Economist*
Strider Elass – *Senior Economist*
Andrew Opdyke, CFA – *Senior Economist*
Bryce Gill – *Economist*
Nate Gerze, CFA – *Economic Analyst*

630-517-7756 • www.ftportfolios.com July 7, 2025

Not So Hot

In the immediate aftermath of Friday's much anticipated Employment Report it seemed like the judgement from analysts, talking heads, and even markets was unanimous (or nearly so) that there was good news to celebrate.

Superficially, it's not hard to see why that view of the report quickly became the conventional wisdom. Payrolls rose a respectable 147,000 in June and were revised up 16,000 in prior months, outstripping the consensus expected 106,000. At the same time, the unemployment rate, which the consensus expected to tick *up* slightly to 4.3% (from a prior 4.2%) instead ticked *down* to 4.1%.

The news was especially welcome because the ADP report released the day before showed a decline of 33,000 private payrolls. Unfortunately, while the ADP report probably overstated the weakness, the Labor Department's report overstated the strength. We expect weaker job growth and higher unemployment in the months ahead.

Why aren't we in the cheerleading chorus? Because *private* payrolls were up only 74,000 in June and were revised down 16,000 for prior months, bringing the net gain to a tepid 58,000. In other words, the overall payroll gain in June itself was roughly half due to government and all of the upward revisions in prior months were due to the government, as well. Long term, more government jobs are not a sign of a healthy economy nor are they going to make it healthier in the future.

We like to follow payrolls excluding three sectors: government, education & health services, and leisure & hospitality, all of which are heavily influenced by government spending and regulation (including COVID lockdowns and re-openings). This measure of "core payrolls" increased only 3,000 in June, the smallest gain so far this year.

Meanwhile, the main reason the unemployment rate ticked down in June was because of a 130,000 drop in the labor force (people who are either working or looking for work). Fewer people looking for work means a lower unemployment rate but also a questionable job market. Again, not good news.

Average hourly earnings increased a mild 0.2% in June, bringing the increase so far this year to 3.5% annualized. In a world with a 2.0% inflation target at the Federal Reserve and a long-term growth rate of 1.5%+ for productivity (output per hour of work), policymakers should anticipate 3.5% growth in wages and see it as a sign that monetary policy has been tight enough for long enough to control inflation.

Yes, real GDP is likely to rebound in the second quarter from the 0.5% annualized decline in Q1, but that should largely reflect the end of companies and consumers front-running the Trump Administration's tariffs earlier this year. It won't represent a lasting shift in the underlying trend in the economy.

Yes, President Trump recently signed the One Big Beautiful Bill Act, which made permanent the tax rate cuts on individuals from back in 2017 as well as some business incentives, like bonus depreciation and faster expensing for R&D. In addition, the law reduces the growth of welfare spending, which could induce more participation in the workforce. But the tax policies that are being extended permanently were already in place for the past several years, while the recent budget cuts are not large compared to total government entitlement spending, so don't expect a sudden miracle boost to economic growth. While the bill is an overall plus for the economy, it's not nearly as powerful as the Reagan tax cuts of the 1980s.

For the time being, we are withholding judgement on the US's fiscal outlook until we see the extent of spending cuts the Administration can get out of Congress later this year during the appropriations battles over Fiscal Year 2026, which starts October 1. Serious budget cuts would be good for the long run, but might cause some very short term economic pain.

In the meantime, manufacturing production is up only 0.5% from a year ago and Fed Chairman Jerome Powell seems determined to make excuses why short-term rates have to stay where they are for the time being, even though they remain well above the Fed's long-run average estimate of 3.0% on the federal funds rate.

We think Powell may be letting politics cloud his judgement, which is why we like Trump's apparent plan to name Powell's successor well in advance of the end of Powell's tenure as chairman next spring. That way Powell will remain on the job, but the public and investors can also listen to how the next chairman (as well as some current Fed members who disagree with Powell) will handle the same economic situations.

The economy is not in recession yet, but markets are not pricing in enough of a risk of a recession in the year ahead.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
7-8 / 2:00 pm	Consumer Credit – May	$10.5 Bil	**$4.0 Bil**		$17.9 Bil
7-11 / 7:30 am	Initial Claims – Jul 5	235K	**237K**		233K