

11 August 2003

David A. Rosenberg
First Vice President
Chief North American Economist
(1) 212 449-4937
david_rosenberg@ml.com

Economic Commentary

Is 'stabilizing' Still an Apt Word to Describe the Labor Market?

Economics

"Recent signs point to a firming in spending, markedly improved financial conditions, and labor and product markets that are stabilizing". Fed press statement, June 25th, 2003.

What we take issue with is the widely-held view that labor markets are stabilizing or firming (is that really the same as 'less negative'?). The only data points suggesting this are the claims data, which in the past three years provided some pretty serious headfakes during the summer retooling season. Yes, at 390k, they are back to Feb/03 levels. But last we saw, payrolls were down 121k that month. Claims are still stuck, albeit at the lower end of the 370k-460k range established since early 2002. Note these other job market indicators:

- Non-Farm Payrolls fell 44k in July even as the consensus was looking for a modest increase. Employment in the past three months is down 192k.
- Temp employment is up in each of the past three months (+42k in July) but there is no better leading indicator for future job growth than hours worked, which fell to a fresh low of 33.6 hours. Hours come before bodies.
- The backlog of continuing claims rose again by 72k in the July 26th week to 3.691 mln after a 36k increase the week before.
- The jobs-related components of the July Conference Board confidence survey deteriorated ('jobs plentiful' fell to 10.5% from 11.2% and 'jobs hard to get' rose to a decade-high 33.1% from 31.9%.)
- Challenger layoff announcements may have peaked, but still bounced sharply to 85,177 in July from 59,715 (60% increase) in June. Note that layoff announcements were 5% higher than July/02 level of 80,966.
- The fact that productivity was up as much as 5.7% SAAR in Q2 and up 3.8% y/y likely means that businesses will remain reluctant to add to their staffing requirements. And without employment creation, doubts could resurface over the sustainability of the recent economic pickup. This is what ultimately undid the post-war euphoria in 1991.

Considering that the futures market is pricing in an aggressive Fed tightening cycle to commence as early as 2004Q1, we have this to offer from the early-1990s experience. By the time the Fed tightened in Feb/94, the economy had generated 4.5 million jobs from the job trough 32 months prior to the first rate hike. And it wasn't until the unemployment rate had fallen 130 basis points from the 1992 peak that the Fed began to step on the brakes. Waiting for a similar performance this time around could mean that the first tightening could well be years, not quarters, away.

Refer to important disclosures starting on page 2.
Analyst Certification on page 2.

Merrill Lynch Global Securities Research & Economics Group
Global Fundamental Equity Research Department

Investors should assume that Merrill Lynch is seeking or will seek investment banking or other business relationships with the companies in this report.

Analyst Certification

I, David Rosenberg, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

Investment Rating Distribution: Global Group (as of 31 March 2003)					
Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1027	42.02%	Buy	358	34.86%
Neutral	1229	50.29%	Neutral	304	24.74%
Sell	188	7.69%	Sell	39	20.74%

* Companies in respect of which MLPF&S or an affiliate has received compensation for investment banking services within the past 12 months.

Copyright 2003 Merrill Lynch, Pierce, Fenner & Smith Incorporated (MLPF&S). All rights reserved. Any unauthorized use or disclosure is prohibited. This report has been prepared and issued by MLPF&S and/or one of its affiliates and has been approved for publication in the United Kingdom by Merrill Lynch, Pierce, Fenner & Smith Limited, which is regulated by the FSA; has been considered and distributed in Australia by Merrill Lynch Equities (Australia) Limited (ACN 006 276 795), a licensed securities dealer under the Australian Corporations Law; is distributed in Hong Kong by Merrill Lynch (Asia Pacific) Ltd, which is regulated by the Hong Kong SFC; and is distributed in Singapore by Merrill Lynch International Bank Ltd (Merchant Bank) and Merrill Lynch (Singapore) Pte Ltd, which are regulated by the Monetary Authority of Singapore. The information herein was obtained from various sources; we do not guarantee its accuracy or completeness. Additional information available.

This research report is prepared for general circulation and is circulated for general information only. It does not have regard to the specific investment objectives, financial situation and the particular needs of any specific person who may receive this report. Investors should seek financial advice regarding the appropriateness of investing in any securities or investment strategies discussed or recommended in this report and should understand that statements regarding future prospects may not be realized. Investors should note that income from such securities, if any, may fluctuate and that each security's price or value may rise or fall. Accordingly, investors may receive back less than originally invested. Past performance is not necessarily a guide to future performance.

Neither the information nor any opinion expressed constitutes an offer to buy or sell any securities or options or futures contracts.

Foreign currency rates of exchange may adversely affect the value, price or income of any security or related investment mentioned in this report. In addition, investors in securities such as ADRs, whose values are influenced by the currency of the underlying security, effectively assume currency risk.