PNC

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Very Weak July Jobs Report, With Huge Downward Revisions to May and June; Higher Tariffs to Weigh on Growth

- **The July jobs report was very weak. Job growth in July was 73,000, but with big downward revisions to employment in May and June, job growth has averaged just 35,000 over the past three months. This is by far the weakest period of job growth in the recovery from the pandemic.**
- **The unemployment rate ticked up slightly to 4.2% in July from 4.1% in June, as employment in a survey of households fell sharply.**
- **Education/health services has accounted for almost 60% of job growth over the past year; the breadth of job growth is a serious concern.**
- **The Trump administration announced much higher tariffs on many countries on July 31; this tax increase will be a drag on the economy.**
- **With the very weak jobs report and the tariff announcement the risk of recession is much higher today than it was yesterday, at around 50%.**

The July jobs report came in much weaker than expected. The U.S. only added 73,000 jobs over the month, according to a survey of employers from the Bureau of Labor Statistics. The consensus expectation was for job growth of around 100,000. Even more worrisome, job growth in May and June was revised sharply lower, by a combined 258,000. May job growth was revised lower to 19,000, from 144,000, with June job growth lowered to 14,000, from 144,000. Over the past three months job growth has averaged just 35,000, by far the slowest three-month pace of job creation since the economy was losing tens of millions of jobs during the pandemic. Job growth averaged above 200,000 per month in 2023, and 168,000 per month in 2024. Private-sector job growth was 83,000 in July, with net government job losses of 10,000. Over the past three months private-sector job growth has averaged 52,000, down from an average of 130,000 in 2024.

The unemployment rate rose slightly in July to 4.2% from 4.1% in June; it was 4.2% from March to May. The unemployment rate has been near 4% for the past year is still historically low, but is up from around 3.5% in mid-2022 to mid-2023. Employment in a survey of households (different from the survey of employers) fell by 260,000 in July from June, and has dropped by an average of almost 290,000 over the last three months. The household survey is more volatile than the employer survey, but can sometimes capture labor market trends before the employer survey.

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The labor force, the number of people working or looking for work, fell by 38,000 in July. The labor force participation rate, the share of adults in the labor force, fell to 62.2% in July from 62.3% in June. The labor force participation rate had been between 62.4% and 62.8% through all of 2023 and 2024, and the first five months of 2025. It could be that an aging population and stricter enforcement of immigration laws is starting to weigh on the labor force.

Other indicators in the report were mixed. The average workweek increased slightly, to 34.3 hours in July from 34.2 in June; it has been 34.2 or 34.3 hours since February. Average hourly earnings rose 0.3% on the month, and were up 3.9% over the past year, near the recent pace.

The breadth of job growth remains a serious concern. Education/health services added 79,000 jobs over the month, and over the past year the industry has accounted for 57% of all job growth; this is unsustainable over the longer run. Leisure/hospitality services has accounted for another 15% of job growth over the past year, although job gains in that industry have slowed noticeably over the summer; some of that may be due to issues with summer hiring and seasonal adjustment. Over the past four months manufacturing employment has fallen by 37,000, and employment in professional/business services is down by 48,000 since April. One positive is that the diffusion index, which measure the breadth of job growth, was 51.2 in July; it was below 50 in April through June, meaning more industries lost jobs in those months than added them.

For a third straight month employment in goods-producing industries fell by 13,000. Manufacturing employment dropped by 11,000 in July. Construction employment continues to rise, however; it has only fallen once in more than two years, although the pace of construction job growth has slowed this year (only 2,000 jobs added in July). Employment in private services-providing industries rose by 96,000 in July. In addition to the gain of 79,000 in education/health services, retail trade employment rose by 16,000, although that followed two months of similarly-sized declines. There were also job gains of 15,000 in financial activities in July. Professional/business services employment dropped by 14,000, with a decline in wholesale trade of 8,000.

Government employment fell by 10,000 in July. There were also big downward revisions to government employment in May (to a loss of 50,000 from an increase of 7,000) and June (to a gain of 11,000 from a gain of 73,000). Government employment has fallen by an average of 16,000 per month over the last three months, even as private-sector job growth has slowed significantly. And federal government employment has fallen by 84,000 since January as spending cuts have taken hold. For now federal workers who took buyouts and are still receiving their pay are counted as employed in the BLS data, but when those payments expire in a couple of months reported government job losses will be much larger.

Even as the jobs report came in much weaker than expected, the Trump administration announced big increases in tariffs on many countries the evening of July 31. This followed the expiration of a 90-day deadline the administration had set for negotiating new trade agreements. The tariffs are a significant tax increase on imported goods that will raise prices for consumers and firms, weighing on household spending and business investment. In addition, big swings in tariffs over the past few months are creating significant uncertainty, making consumers and businesses even more cautious about major spending decisions, causing further economic drag.

The jobs report for July was very weak, the weakest since the pandemic. Job growth in July was OK, but there were enormous downward revisions to job growth in May and June. With the revisions the labor market looks very different now than it did at the end of July: it is much weaker in mid-2025 than it was at the beginning of the year. Much smaller job gains mean weaker household income growth, and slower growth in consumer spending. The most likely outcome is still softer economic growth in the second half of 2025 and early 2026 compared to 2024 and the first half of this year, but no recession. But given the revised read on the labor market recession risks are now at roughly 50-50 over the next year, up from 35% in the spring and 15% at the beginning of 2025. It is easy to see how very weak job growth and higher tariffs could cause consumers to cut back on their spending and businesses to cut back on their investment, with the economy quickly devolving into recession. And in addition to the very weak July jobs report, the ISM manufacturing report for July, released on August 1, indicated contraction in the industry for a fourth straight month with a further deterioration in July.

The fed funds futures market is now pricing in an 89% probability of a federal funds rate cut at the Federal Open Market Committee's next meeting, on September 18, more than double yesterday's 38%. The Federal Open Market Committee held the fed funds rate unchanged at its meeting on July 30, in part because the labor market appeared to be holding up. But now that the stability of the labor market is in question, the central bank may be much more willing to consider rate cuts, even if the FOMC is concerned about a potential pickup in inflation from tariffs. PNC's July forecast had one 25 basis point cut in the fed funds rate in 2025, at the last FOMC meeting of the year in December, with additional 25 basis point cuts at each of the first two meetings of 2026. But that forecast is now in question with the weak July jobs report, and will be updated for August.

Market reaction has been very negative. The S&P 500 was already down in pre-market trading after the tariff announcement, and fell further with the weak jobs report: the S&P 500 was down 1.6% at the close. The yield on the 10-year Treasury note has fallen by 16 basis points to 4.22% on expectations for weaker U.S. and global economic growth and softer inflation. The yield on the 3-month Treasury bil is down by 5 basis points to 4.29%. The steep drop at the long end of the yield curve, with a much smaller drop at the short end, has raised the specter of the inverted yield curve, when long-term Treasury yields are below those on short-term yields. This has historically been a recession indicator, although the yield curve was inverted in 2023 and most of 2024 without a recession. The price of a barrel of West Texas Intermediate crude oil is down by 3% to around $67.20 due to increased recession concerns and lower expected oil demand. The dollar has weakened against a basket of currencies given increased expectations for near-term fed funds rate cuts and growing investor unease about the U.S. economy with higher tariffs and the weak jobs report.

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