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ABOUT BILL SULLIVAN

William V. Sullivan, Jr. serves as Chief Economist at JVB Financial Group, working closely with the firm's trading desk, providing analysis and commentary on the U.S. economy and the financial markets. Among his duties are authoring a weekly report on credit market trends and maintaining a regular schedule of conference calls that focus on interest rate developments. He appears frequently on Bloomberg TV and is often quoted in Barron's.

Mr. Sullivan is the familiar voice that JVB features on our weekly conference call, where he discusses the economy and the events that affect the marketplace.

He was previously associated with Morgan Stanley in New York City for more than twenty years, where he was an Executive Director and a Senior Economist in the firm's Retail Fixed Income Division. Bill published a widely quoted weekly letter on the financial markets and was a frequent guest commentator on several business networks, including Bloomberg TV, CNBC, and Fox News.

Prior to joining Morgan Stanley, he was affiliated with The Bank of New York, where he was a Senior Vice President in the Treasurer's Division.

Mr. Sullivan holds a Bachelor of Arts Degree in Economics from Fairfield University and an MBA in Investments from New York University.

JVB FINANCIAL

Weekly Commentary

by Bill Sullivan, JVB Chief Economist

March 8, 2010

Unemployment and gasoline: Heading higher?

Investors took comfort in the fact that the nationwide unemployment rate held steady at 9.7% of the total labor force during February. Indeed, many observers are now concluding that the peak level of joblessness for the current cycle was reached last October when the unemployment rate hit 10.1%, the highest reading since 1983. While the four-tenths of one percent drop in unemployment over the last four months is certainly a welcome development for American workers, it should be noted that, if history is any guide, such a decline over a relatively brief period doesn't necessarily guarantee that the cyclical high has been reached. In particular, there have been many instances in the post-World War II period when similar declines were quickly followed by sharp increases in the overall unemployment rate that would eventually generate new high watermarks for joblessness.

In 1980, for example, the jobless rate was climbing rapidly, adding more than two full percentage points in the twelve months that ended that July. By the end of the calendar year, the nationwide rate had dropped sixth-tenths of one percent, falling from 7.8% of the labor force to 7.2% by December. As 1981 got underway, the jobless rate resumed its upward trend, eventually exceeding 8.0% before the end of the year. Further increases were observed throughout 1982 before a cyclical peak of 10.8% was established during the fourth quarter. Another interesting episode transpired during 2000 which was the last time the U.S. Census was taken. After cresting at 4.3% of the labor force in July, 1999, the unemployment rate moved down to 3.8% by April, 2000. Despite the hiring associated with the decennial population count, the unemployment rate edged higher as the year progressed and by early 2001 was above 4.4%, before finishing the year at 5.7%. An additional example of a trend reversal was also evident during 1973. After peaking at 5.0% of the labor force in April, the unemployment rate dropped four-tenths of one percent over the next six months before resuming a sharp upward climb from that level, posting 7.2% by the end of 1974.

Admittedly, each cycle has its own attributes and, as a result, the past may not be an adequate reference for the present environment. The February, 2010 report, despite its positive reception in the financial marketplace, nonetheless did contain some worrisome input. The entire drop in unemployment was among teenagers. The jobless rate for adult women actually rose one-tenth of one percent while adult male unemployment remained at 10.0%. Full time employees, regardless of age, experienced a rise in joblessness from 10.4% to 10.5%. Clearly, if teenage unemployment begins to move higher in the months to come, an upward bias would be provided to the overall rate, as there is still no indication that business firms are willing to aggressively hire adult workers. Further upward pressure on

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the overall rate could be generated by an increased number of people reentering the labor force in the months ahead.

Should the unemployment rate hold at current levels or move higher later this year as seems possible, wage growth will remain anemic for the foreseeable future. Employers are unlikely to be overly generous in their compensation policies given the huge slack that is present in the labor force. Another disincentive for businesses to add to payrolls is the uncertainties attendant to health care reform. Until legislation is actually signed into law, corporations simply don't have a firm grasp of the additional expense that may be involved when adding to staff in a revised regimen for health care.

A relatively stagnant outlook for take home pay could begin to collide with an unexpected development for most households: markedly higher energy costs, especially for driving. Needless to say, the commodities arena is volatile and recent trading patterns can be quickly reversed. However, within the last month or so, a sharp run up in the price of crude oil and various refined products has been evident. On the wholesale market, the per gallon price of gasoline has moved up by over twenty percent since early February. Unless there is a meaningful pullback in prices over the next few weeks, the nationwide average price for regular gasoline at the retail pump could head towards $2.95 to $3.00 per gallon, or almost 40 cents above the levels that prevailed during the middle of last month. If the full pass through to the driver does occur, monthly outlays at gasoline service stations could rise by another $5.0 to $6.0 billion as compared to January when spending tallied $34.7 billion, according to the Department of Commerce. Such a sharp increase would obviously rob some discretionary spending power from U.S. consumers. The higher outlays mandated for energy would be transpiring in the context of soft employment conditions and minimal income growth, a combination that could hold the economy's performance in check for an extended period. ■

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