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A Look Behind the Employment Numbers

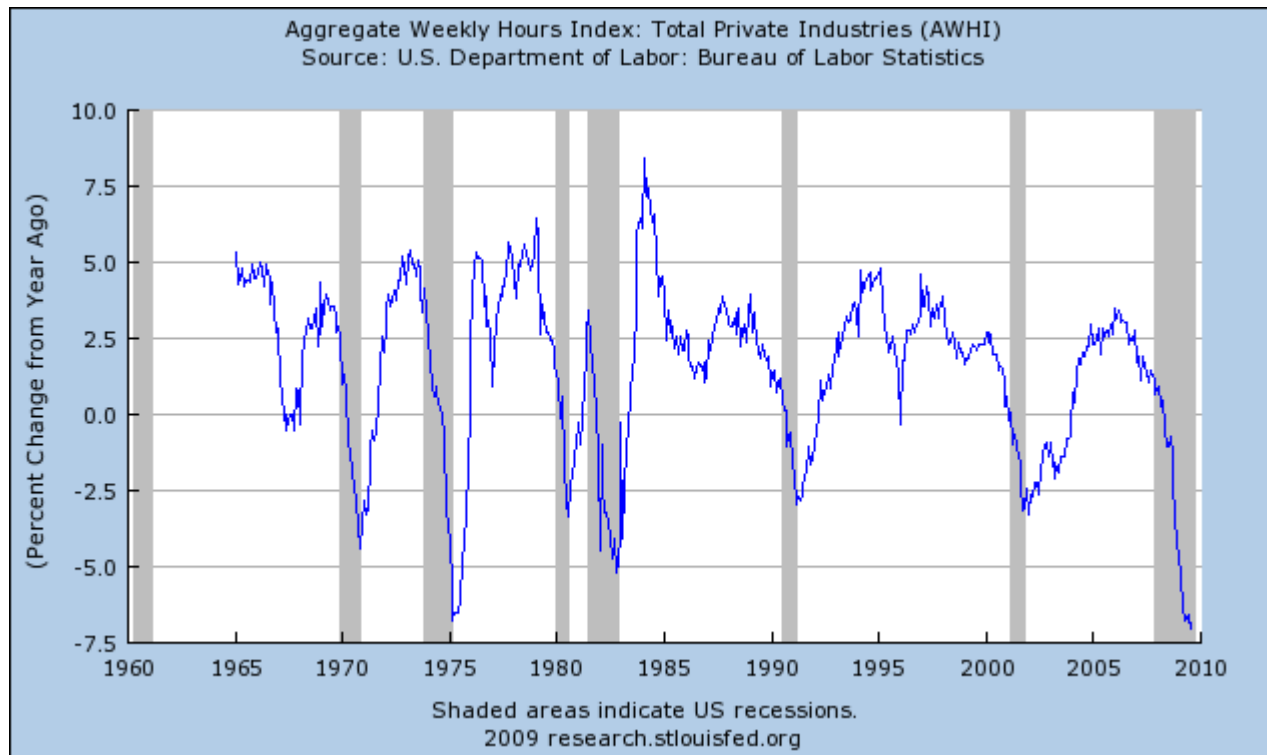
September 14, 2009

"We still have a long way to go before true recovery takes hold."

– Treasury Secretary Timothy F. Geithner

Markets cheered when the Bureau of Labor Statistics reported earlier this month that nonfarm payroll employment declined by “only” 216,000 in August. A closer look reveals a less encouraging picture than that single figure suggests. High debt levels and questionable employment prospects continue to weigh on financially stressed households as they deleverage amid economic uncertainty. Meanwhile, home foreclosures are hovering near record highs and are likely to remain a significant drag on economic growth.

The August headline number of 216,000 jobs lost was from the Establishment Survey. However, that survey also included downward revisions in nonfarm payrolls of 49,000 for July and 20,000 for June. Even more discouraging were details contained within the Household Survey, which reported a much-larger loss of 392,000 jobs. The aggregate weekly hours-worked index captures most of these effects and is presented below. The 7.0% drop from August 2008 to August 2009 is the largest year-over-year decline since this series began in 1964.



In recent months the declines in aggregate hours worked have slowed somewhat. For the three-month period from June through August, aggregate hours fell at a 4.5% annual rate vs. the preceding three months. From July to August they fell 0.30%, which is a 3.6% annual rate of decline. These improvements, as welcome as they are, provide little reason for excitement in view of massively expensive government-stimulus programs.

Beyond the Headlines

One factor contributing to falling aggregate hours worked is the growing army of people working part-time against their wishes. Their numbers swelled by 278,000 in August to a record 9.1 million – up from 4.7 million when the recession began in December 2007.

Within nonagricultural industries involuntary part-timers increased by 298,000 last month, while self-employed workers increased by 233,000. Though there is no separate breakout for the “involuntarily self-employed,” the numbers suggest much of the recent surge in self-employment may not be entirely by choice. In any event, the number of workers actually earning wages and salaries in nonagricultural occupations plummeted by 654,000 in August. This was the sharpest decline in five months, which was surprising given that the economy is supposed to be growing.

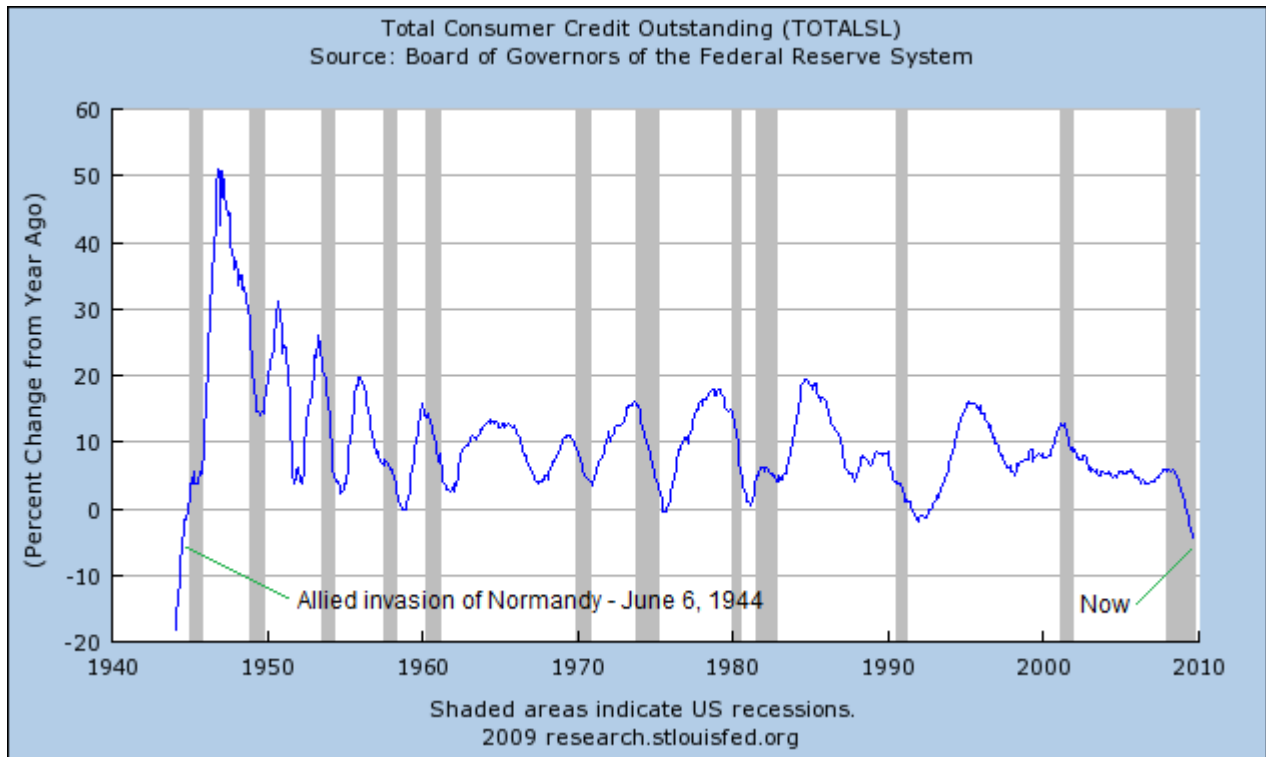
All in all, the unemployment rate rose to 9.7% in August as the number of unemployed Americans increased by 466,000 to 14.9 million. Unfortunately, the majority of them (8.1 million or 53.9% of the unemployed) have suffered permanent job loss – an increase of 220,000 from July. Only 11.4% of the unemployed are on temporary layoffs. The remaining 34.7% consist of job leavers, reentrants and new entrants into the work force.

In short, Secretary Geithner’s comment that “we still have a long way to go” appears well-substantiated. The weak labor market continues to restrain consumer spending and vice-versa. Ordinarily, a surge in consumer borrowing would break that dynamic. However, the current deleveraging cycle is preventing the credit expansion necessary for lasting recovery to occur.

Deleveraging Continues

Consumer credit contracted again in July as households continued to scale back borrowing and pay off debt. The monthly decline of 0.86% was the largest since June 1975 and the sixth in a row. Moreover, as the chart on the next page shows, July’s 4.2% year-over-year drop was the sharpest such pullback in consumer borrowing since June 1944. At that time much of Europe was under Nazi occupation, and the outcome of World War II was still uncertain. Confidence was restored and consumer borrowing skyrocketed, but achieving that outcome required the largest amphibious military operation in history. Whether the Fed and the administration can pull off a similarly impressive feat this time around is doubtful.

Additionally, RealtyTrac reported last week that home foreclosures remain near record highs. While August foreclosures were down 0.47% from July, the 358,471 filings still represented an 18% increase from year-ago levels. The foreclosure report came one day after the Treasury conceded millions of additional foreclosures are on the way despite a slew of mortgage-modification programs. Suffice it to say that deleveraging and foreclosures will remain important economic themes in the coming months and years.



The Picture

In our June 8 commentary we wrote: “The shallowness of the selloffs during this rally indicates that buyers have been coming in at the first sign of weakness. This could be setting up a buying panic that exhausts the buyers and ends the rally.” As the chart on the next page illustrates, that scenario remains very much in play as the S&P 500 Index pushes to new highs.

Although attempting to pick exact tops and bottoms is extremely difficult, the most recent action in the index does exhibit some characteristics of an exhaustion move. RSI traced out a negative divergence from the price chart in late August and completed another last week. MACD has behaved similarly although last week’s non-confirmation has not yet developed into a full-fledged divergence. These divergences and the non-confirmation are marked on the chart in green.

An important potential development to watch for is a move down followed by a weak move up into a lower high. Such a pattern of trending likely would mark the beginning of a deeper corrective move that ultimately could prove part of a broad topping formation. At the very least, the recent series of divergences in the indicators is a sign this cyclical bull market is starting to become frayed at the edges.

\$SPX (S&P 500 Large Cap Index) INDX © StockCharts.com

11-Sep-2009 **Open** 1043.92 **High** 1048.18 **Low** 1038.40 **Close** 1042.73 **Volume** 4.0B **Chg** -1.41 (-0.14%) ▼



Chart courtesy of StockCharts.com

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