Jobs report proves Janet Yellen is wrong about the economy

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The August jobs report was disappointing with job gains of 151,000, below the consensus forecast of a gain of 180,000 jobs. The reported August job gains were also considerably below the gains in June and July. The unemployment rate was forecast to fall to 4.8 percent, but held steady at 4.9 percent. Both numbers are disappointing and make a September rate hike less likely.

At the recent Jackson Hole conference, **Federal Reserve** Chair **Janet Yellen** stated that the case for raising interest rates had strengthened. She suggested that good job growth would continue. Once again, the Fed Chair has been too bullish in her view of the economy. More generally, Fed officials have been over-predicting economic growth in this recovery.

It is time for Fed officials to recognize that their model of the economy is wrong. If the model was ever right, it is now broken.

Job growth has in any case been a weak reed on which to rest the case for a rate hike. This has been a weak jobs recovery. Even the forecasted growth of 180,000 jobs would have been nothing to brag about.

The unemployment rate is now a misleading number. Yes, the rate has fallen dramatically from its peak. But much of that decline has been the result of the fall in the labor force participation rate. It has fallen from a peak of over 67 percent in 2000 to 62.8 percent in August. So there is a long-term trend downwards, which accelerated in the Great Recession.

If the unemployment rate falls because discouraged workers are leaving the labor force, that is nothing to cheer. And it is certainly no basis for a Fed rate hike.

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Why the bullish sentiments of some Fed officials for a rate hike? I increasingly believe that there are unstated reasons buttressing their hawkish stance. They are likely concerns over financial stability issues. These officials certainly understand that a long period of low interest rates must result in financial bubbles. Capital has been mispriced and, hence, misallocated.

Additionally, margins have been squeezed for banks and other lenders. Finally, money market mutual funds have no sustainable business model at very low rates. These funds must pay to attract money, but can earn very little on their investments.

Negative interest rates would make these problems even worse, which surely explains the aversion of Fed officials to negative rates. The Fed has learned from the experience of countries that have taken rates into negative territory.

If Fed officials see a need to raise interest rates for financial stability reasons, they should make that case. Anemic economic growth and weak job growth just do not sustain the case for higher rates. For these and other reasons, I see no rate hike in September.

Notwithstanding the weak case for a September rate hike, Yellen has put the credibility of the FOMC on the line with her talk of a rate hike. I can still see the Fed hiking rates at the December meeting as it did in 2015. I cannot foresee two hikes in 2016. If there is an increase in rates in December, the Fed will pause again.

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