Global Macro Research

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#US / #Labour market / #Monetary policy

What do our US labour market indicators say about the state of the cycle?

Data on the US jobs market are sending conflicting signals. So, we have built some composite indicators to measure its health. While the headline measure is below its long-run average, the index has stabilised and we see nascent signs of recovery. This suggests the Fed's three "insurance cuts" in 2025 sufficiently reduced downside risks, and we expect the Fed to pause cuts until the next chair takes office in May.

Key Takeaways

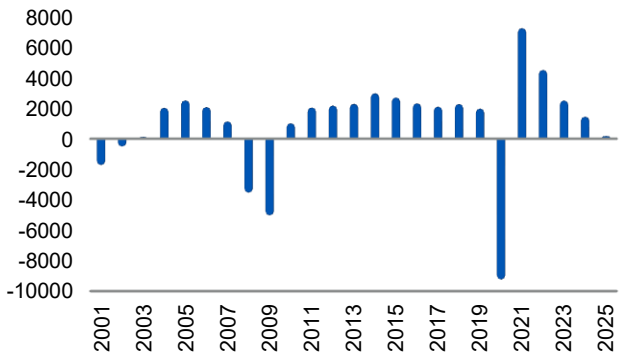
- US economic data have diverged recently. GDP growth in H2 2025 was very strong, but employment data softened.
- The labour market deterioration has not triggered the Sahm rule, and the rise in unemployment partly reflects higher participation. Indeed, the combination of strong GDP and weak employment means US productivity growth is surging.
- Given these conflicting signals, we developed a series of composite labour market indicators to cut through the noise.
- The headline indicator is below its long-run average, driven by weak demand and dynamism, as elevated trade uncertainty has held back hiring.
- But the indicator has recovered from its lows, suggesting the Fed's three "insurance cuts" have headed off downside risks, and we see early signs of recovery, supported by reduced uncertainty.
- This is consistent with our expectation that policy is on hold until a new Fed chair takes office. But the recovery is fragile, and the possibility of geopolitical uncertainty spiking means risks are perhaps skewed to the downside, prompting earlier Fed action.

Is the US economy facing boom or bust?

Different parts of the US economy seem to be heading in different directions. On the one hand, GDP is strong, expanding at a 4.4% annualised rate in Q3 2025 and on track to grow by 2.0-2.5% in 2025 and 2026.

On the other hand, labour market data have been more consistent with an economy flirting with recession. US non-farm payrolls increased by just 181k over 2025 – the first time in 20 years that growth dipped below one million, outside of the pandemic in 2020 and the 2008-2009 financial crisis (see Figure 1).

Figure 1: Non-farm payrolls additions in 2025 near recessionary levels



Source: Haver, Aberdeen, February 2026

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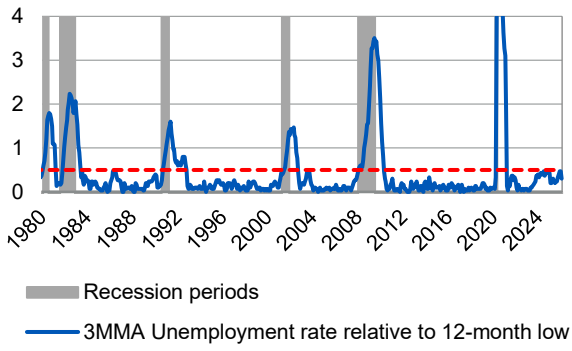
In addition, the unemployment rate crept higher in late 2025 and came close to triggering the Sahm rule. The rule is based on the empirical regularity that, if the three-month average of the unemployment rate is 0.5% or more above its 12-month low point, the US economy has entered a recession. That measurement reached 0.47% in November and December, although it has since eased in January (see Figure 2).

Figure 2: Rising unemployment points to elevated recession risk



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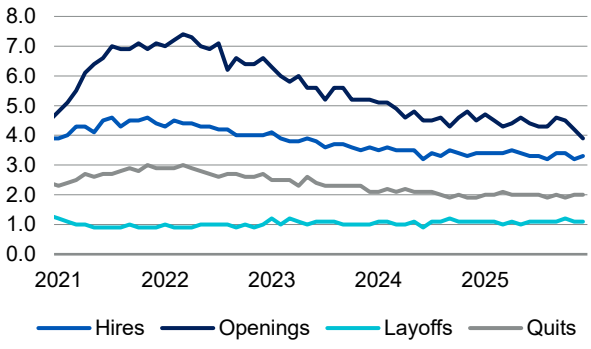
The intuition behind this rule is that rising unemployment is self-reinforcing, in that as the economy slows and job losses begin, the deterioration in sentiment prompts further job losses and cuts to investment. The economy can "stall" and then fall into recession.

But what this rule can miss is that not all increases in unemployment are created equally. The rise in unemployment in late 2025 was in part a result of people entering the labour force and looking for work. This implies something very different about the underlying health of the economy than a rise in unemployment driven by job destruction. In fact, the layoffs rate remains low by historical standards and is not rising (see Figure 3) suggesting that the labour market is not yet signalling elevated recession risk.

Figure 3: Job openings, hires, layoffs and quits rates are all low, pointing to minimal churn



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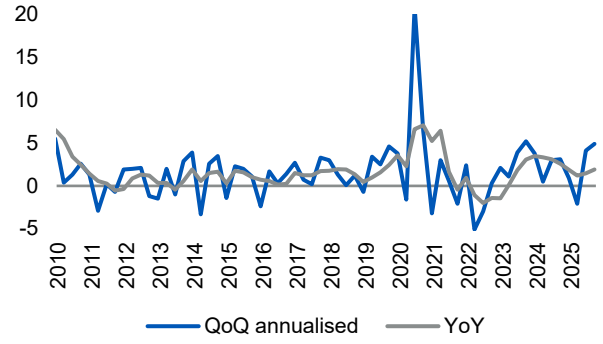
This divergence between economic growth and employment by definition implies that productivity is improving. Indeed, output per hour worked increased by 4.9% quarter on quarter annualised in Q3 2025, or 1.9% year on year (see Figure 4).

Figure 4: US labour productivity is rising rapidly, after the Q1 2025 dip



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This strong productivity growth may in part be an endogenous response to the rapid pace of activity growth, with firms having to find ways to boost productivity to meet demand, especially given the fall in labour supply growth. But labour availability does not yet seem to be a significant constraint. More likely is that firms are reaping the benefits of a hiring boom in the post-pandemic period.

Productivity growth is the only path to sustainable increases in real wage growth. But, for now, productivity growth seems to be showing up in the distribution of income, with the benefits of gains going more to shareholders than workers. The share of GDP going to labour income fell to 53.8% in Q3 2025, its lowest level since records began in 1947.

Ultimately, the divergence between employment and economic growth is not sustainable, and we expect the gap to narrow somewhat in 2026 as employment growth picks up.

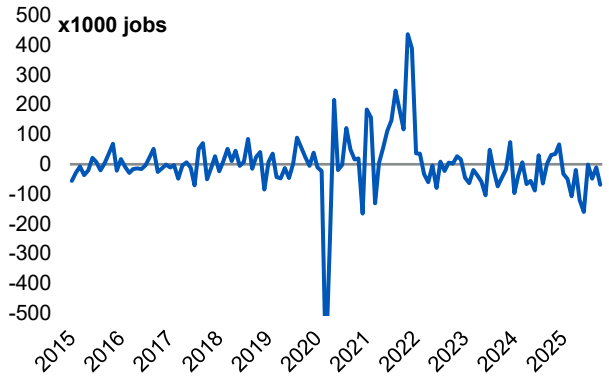
But one additional takeaway of this diverging picture is the importance of reliable labour market measures to fully capture the outlook for the economy.

Most labour market metrics have limitations

The US has an abundance of labour market data. So much so that it is easy to get lost in the noise. On top of this, the most cited metrics have limitations and often concerns about reliability.

Payrolls data are a great example. The monthly non-farm payrolls report, which is perhaps the most closely watched labour market indicator, is useful because it is released rapidly. However, it has issues with double counting, does not include self-employed or gig workers, and is subject to large revisions. In the past three years, the monthly payroll figure has been revised downward by an average of 36k between the first and third released (see Figure 5). This does not even include the larger revisions that occur as part of the Quarterly Census of Employment and Wages.

Figure 5: Revisions to non-farm payrolls from initial release to third release have been downward in past few years



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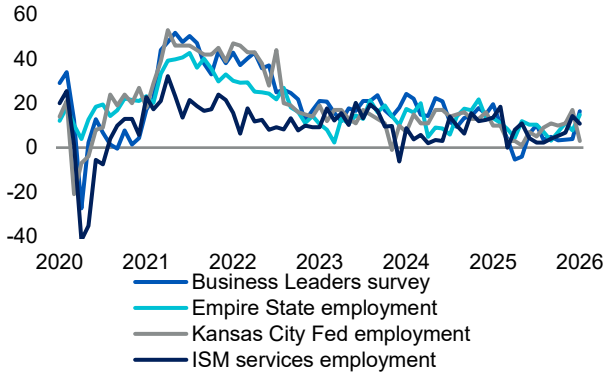
Other indicators also suffer from issues. Changes to the headline unemployment rate often reflect changes to the participation rate as much as changes to the number of unemployed people, and it does not capture underemployment. The JOLTS data, particularly for openings, are subject to industry bias and posting of jobs that are not intended to be filled.

On top of this, many of these metrics are inherently backward-looking. There are however several less referenced metrics that give a better indication of the future, as well as a wide range of surveys that capture the intent of businesses when it comes to hiring plans and expectations, which frequently are leading indicators for employment (see Figure 6).

Figure 6: Surveys of expectations point to a labour market recovery that is little evidenced in the hard data



Source: Haver, Aberdeen, February 2026

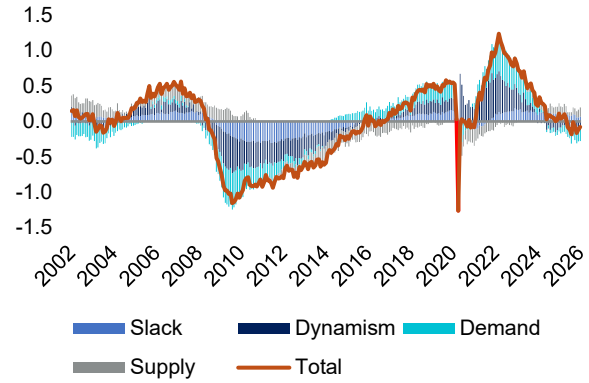
In short, though, no single data series gives a reliable indication of the state of the labour market or where it is heading. For that, a more holistic approach is required.

In-house indicators help gauge the jobs market's health

With this in mind, we have developed two composite indices designed to give a clearer indication of current labour market health and the future direction of travel.

The concurrent index is a real-time labour health snapshot. It draws on 14 different indicators, putting them into four pillars: labour market supply, demand, slack, and dynamism (see Figure 7). For a more detailed explanation of how the index is calculated, see the appendix on selection of inputs and calculation methodology.

Figure 7: Our "concurrent" US labour market index points to low demand and a lack of dynamism



Source: Aberdeen, February 2026

We have also developed a forward-looking index, designed to give a predictive signal for labour trends. This index draws on two main categories of indicators: cyclically sensitive metrics such as overtime hours and demand for temporary services, and survey-based expectations from institutions such as ISM, the regional Federal Reserve banks, and industry bodies. It's a good indicator for what happens to the current index two to three months later.

The inputs are normalised and standardised, such that a reading above zero indicates a net-positive state of the labour market, and vice-versa.

What do the indices show?

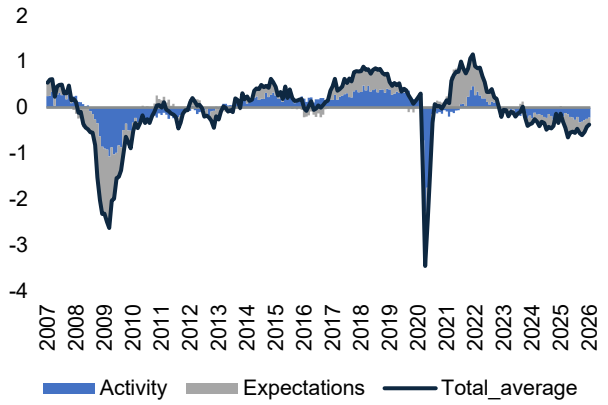
Our concurrent labour index stands at -0.08 in January, indicating the health of the labour market is below its long-run average but only marginally. It fell below zero in June 2025, as a deterioration in labour demand added to the lack of dynamism that had developed through 2024. However, the index has shown some signs of stabilisation and is above the low point reached in August.

The measures for slack and supply suggest that, despite the reduction in immigration over the past year, labour availability is not an issue. The main problems are the lack of hiring and low labour market turnover. Both of these are symptomatic of increased uncertainty leading to caution from both employers and employees. While uncertainty from tariffs has eased and should support some recovery in hiring and turnover, other political risks mean uncertainty is not likely to go away soon.

Our forward-looking index is also below zero, with both cyclical leading indicators and expectations below their long-run averages. However, cyclical indicators have been trending lower since late 2022, well before the recent slump in demand.

Most of the decline in 2025 came from reduced expectations. However, this reached a low point in Q2 around peak tariff uncertainty and recovered somewhat since (see Figure 8).

Figure 8: The forward-looking US labour market index shows some signs of improvement following mid-2025 lows



Source: Aberdeen, February 2026

The modest pickup in our forward-looking index and the expectations component in particular is a good indication of a nascent recovery in hiring, but it is also a fragile one. In short, we expect a modest improvement in the demand for labour in early 2026, but this could easily be disrupted by turbulent politics.

Monetary policy implications

The three cuts to US interest rates in late 2025 were framed as a risk-management response to mounting labour market risks. In his December statement, Chair Jay Powell suggested that the Fed would wait to see if these cuts were sufficient to stabilise the labour market.

Our labour indices suggest that the Fed has indeed done enough to stabilise the labour market, and we may be heading into a period of recovery. With inflation remaining above target, we judge the balance of risks has shifted, justifying keeping interest rates on hold for the time being. We maintain our forecast that the Fed will hold rates steady until after the new chair is appointed in May, with some further easing expected later in the year.

Conclusions

The US economy has been sending mixed messages. This has not been helped by the uncertainty and disruption caused by liberation day and the Q4 government shutdown.

The divergence in economic growth and the labour market is unlikely to disappear completely in 2026, but we do see it narrowing, with strong business investment and improved confidence leading to a modest pick-up in hiring.

There is, however, an outside risk that shocks cause unemployment to rise further, which, along with a deterioration in sentiment, could tip the economy into recession. We will be monitoring our proprietary labour indices closely to see which way the pendulum swings.

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Appendix:

Aberdeen US Labour Market Composite Indices

The Aberdeen US labour market indices provide compact, timely views of labour market conditions by combining multiple indicators into two summary measures:

The Aberdeen Labour Conditions index captures present labour market conditions (tightness/slack, demand, supply, and dynamism) using 14 selected indicators.

The Aberdeen Labour Expectations index anticipates future labour market moves by emphasising leading, expectations-based, and vacancy/turnover signals.

Using composites rather than single series mitigates noise in any one indicator, provides broader coverage of labour-market dimensions, and improves interpretability for macro narratives, risk monitoring, and policy assessment.

Component indicators and rationale

The indicators selected were chosen to capture different aspects of the labour market. A low unemployment rate tells little about turnover in the jobs market, for example. It was important to choose indicators that captured labour market slack, dynamism, demand, and supply.

Components of the Labour Conditions index:

Indicator	Category	Economic rationale
U3 unemployment rate (total)	Slack	High U3 ⇒ more slack; low U3 ⇒ tighter market.
Long-term share of unemployed	Slack	Persistent joblessness increases structural slack.
Marginally attached share of workforce	Slack	Captures hidden slack beyond U3.
Youth unemployment rate	Slack	Sensitive segment; signals cyclical slack.
Part-time for economic reasons	Slack	Measures underemployment.
Vacancy to unemployed ratio	Demand	Vacancy pressure relative to available workers; classic tightness metric.
Temporary help services as share of employment	Demand	Cyclically sensitive demand indicator
Participation rate (ages 25-54)	Supply	Prime-age supply availability; higher participation shows supply response.
Female participation	Supply	Additional supply depth and demographic breadth.
55+ participation	Supply	Labour-force extension via older cohorts.
Foreign-born share of hires	Supply	Supply augmentation via immigration channels.
Hires rate	Dynamism	Hiring velocity; indicates churn and matching activity.
Quits rate	Dynamism	Confidence in finding better jobs; signals tight conditions.
Employment-to-Employment flows	Dynamism	Higher job-to-job transitions reflect strong demand for labour.

For the Labour Expectations index, the indicators fall into two categories; activity indicators that tend to be cyclically leading, and sentiment indicators that capture expectations.

Indicator	Category	Economic rationale
Average weekly hours	Activity	Changes in hours worked signal demand changes.
Change in temporary help services	Activity	Temp workers are often the first to be fired/hired.
Initial unemployment claims	Activity	High frequency indicator that captures job losses.
Overtime in manufacturing	Activity	Sensitive labour demand indicator.
NFIB employment expectations	Expectations	Captures hiring expectations for small businesses.
ISM employment indices	Expectations	Good indicator of business hiring/firing expectations
Business Leaders Survey	Expectations	Capture 6-month ahead expectations for employment
Richmond Fed survey	Expectations	Capture 6-month ahead expectations for employment
Empire State	Expectations	Capture 6-month ahead expectations for employment
Kansas City Fed	Expectations	Capture 6-month ahead expectations for employment
Dallas Fed	Expectations	Capture 6-month ahead expectations for employment

Data transformation

Seasonality: most input series are seasonally adjusted by at source (e.g. BLS), but where non-seasonally adjusted variables are selected, they are transformed into seasonally adjusted series first.

Directionality: for some variables such as unemployment, higher values correspond to worse conditions. We invert these so that higher = more positive across all metrics.

Standardising scale: Z-scores are calculated for each input variable over the historical window (2002 to present for current conditions, 2007 present for expectations index).

Pillar grouping: The indicators are combined into pillars, slack, demand, supply and dynamism for the current conditions index, activity and expectations for the forward-looking index. The standardized input variables are equally weighted within their respective pillars.

Index Aggregation

The pillars are then aggregated into the composite indices. We employed two parallel aggregation methods.

1. Equal weighted average. The average of the four/two pillars combined.

2. Principal component analysis, a technique that looks to maximise explained variance while removing multicollinearity and noise from the input series.

While PCA is a more sophisticated statistical approach, we decided to use the simple average aggregation method instead due to its greater transparency. There was little difference between the results of the two approaches, with the PCA indices showing a higher degree of volatility due to the approach putting a greater weight on the variables with most significance.

Final scaling

The resulting indices were then standardized once more where the series mean = 0 and standard deviation = 1. This allows for easy interpretation of the index, where a reading greater than zero indicates stronger than average, and below zero the opposite.

Other adjustments

The input variables are released at different times. So that calculation of the indices is not dependent on all input variables being up to date, the formulae are set to use the last non-zero number from each series. In effect, this means we get a preliminary index reading for each month when the employment report is released on the first Friday of each month, and a finalised number when the JOLTS report is released on the first Tuesday of the following month.

Potential improvements

Structural breaks and extreme outliers, such as around COVID, can affect input standardization and the robustness of z-scores. Winsorisation of the data to remove outliers and a moving window for calculation of z-scores could help mitigate this.

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