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The Carlyle Compass

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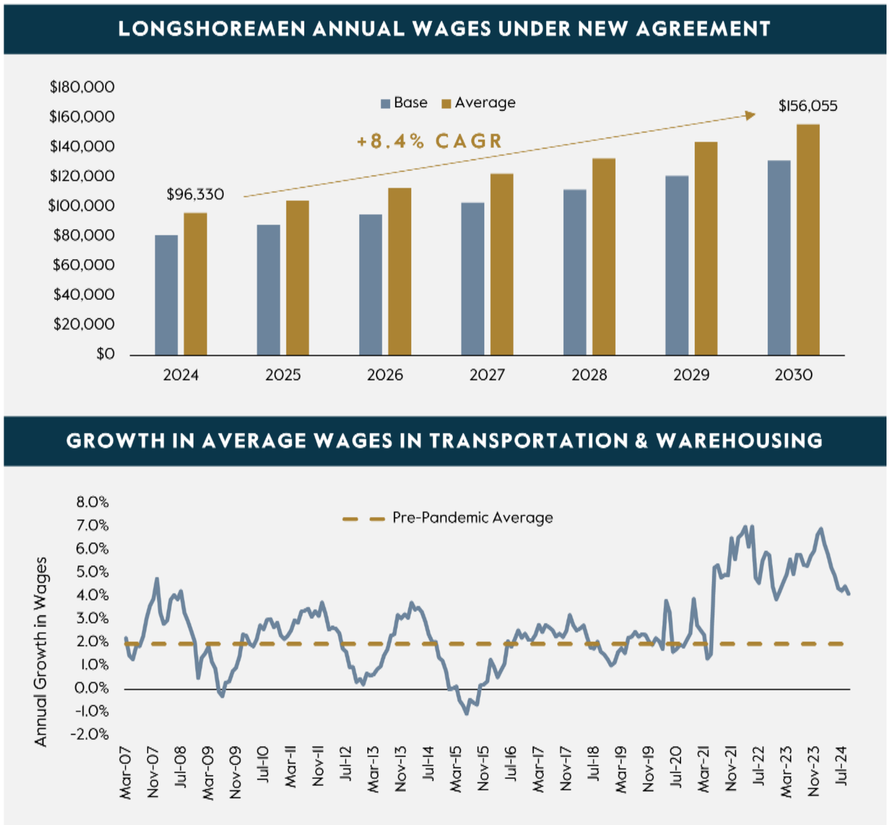
Welcome back to ***The Carlyle Compass****, your weekly newsletter that brings together the latest research and market insights from our global team.*

Literary critic Michael Wood once averred that movies send messages, even if there's no one there to receive them. Last week, the U.S. labor market sent two messages to investors. The first came in the form of a long-term labor market agreement; the second through September payroll and wage data. These messages were not ignored—Treasury yields backed up by 20-30 basis points on the news—but they don't seem to have been fully internalized either, judging by the aggressive series of rate cuts still implied by the forward curve.

On Thursday, the International Longshoremen's Association suspended its strike at East Coast ports after just three days. A tentative agreement on wages proved juicy enough to spur members to return to work while leaders haggle over outstanding items. The strike's suspension was great news for the near-term economic outlook. A lengthy work stoppage would have imperiled the incomes of more than 80,000 workers and over a trillion dollars' worth of trade volumes. But more than shoring-up Q4-2024 GDP, the agreement's 62% increase in wages will serve as a benchmark that also shores up medium-term wage expectations. Rather than revert back to trends that prevailed prior to the pandemic, the agreement would seem to cement post-2020 wage growth as a "new normal" (Figure I).

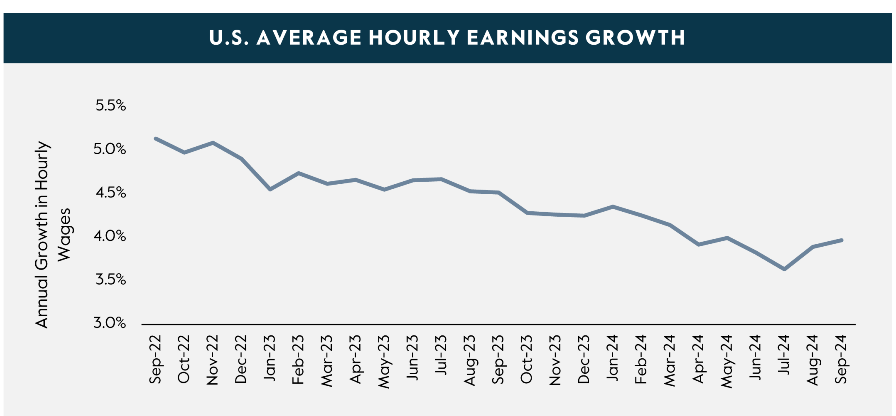
Figure 1: Could Wage Inflation Prove More Persistent Over Time?



Source: Carlyle Analysis; The New York Times, Federal Reserve, October 2024. There is no guarantee any trends will continue.

The next morning, the [jobs data revealed]() a sharp acceleration in net hiring that surprised virtually all forecasters, especially those convinced that high interest rates had pushed the U.S. economy into recession. U.S. payrolls increased by 254,000 in September, reversing the downtrend observed in July and August. Results from the household survey were even more encouraging. Growth in people with jobs (430,000) far outstripped the increase in the labor force (150,000), pushing the unemployment rate back down to 4.1%. With the number of unemployed people falling relative to job openings, average wages increased at a 4.0% annual rate, matching a five-month high (Figure 2).

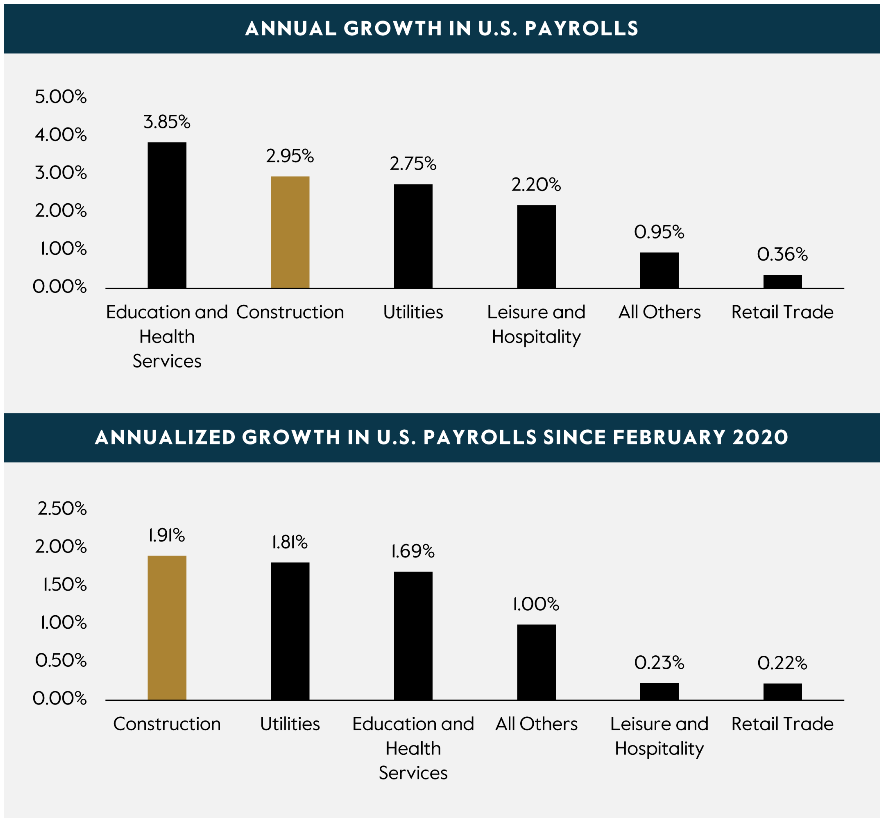
Figure 2: Surprise Rebound in Annual Hourly Earnings Growth



Source: Carlyle Analysis; Federal Reserve, October 2024. There is no guarantee any trends will continue.

High interest rates have badly dented traditional real estate development activity but done nothing to slow the growth in construction-related employment, which continues to expand at 2x the rate of overall payrolls (Figure 3). Workers not building homes, apartments, and office buildings are busy constructing data centers, renewable energy generation facilities, battery and electric vehicle factories, semiconductor fabrication plants, and other industrial structures. Over the past 12 months, industrial assets put-in-place [grew by 23%](). This generational surge in capex, propelled by industrial policy and AI enthusiasm, has inured the economy to levels of interest rates that would have likely proved catastrophic just five years ago.

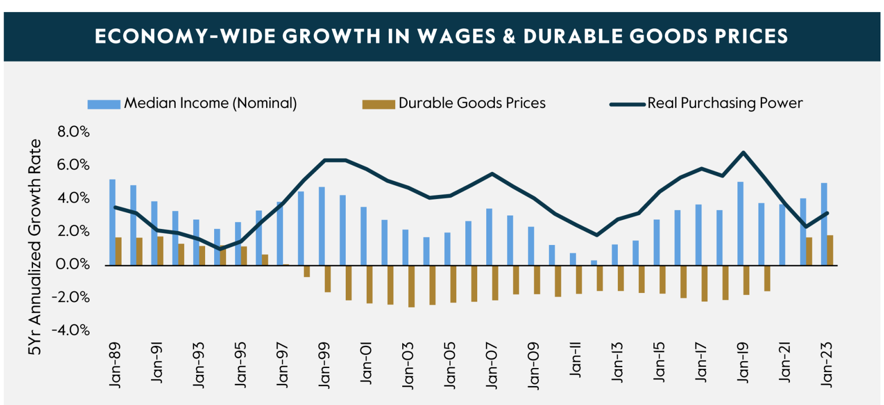
Figure 3: Construction Employment Grows 2x Faster than Overall Payrolls



Source: Carlyle Analysis; Bureau of Labor Statistics, October 2024. There is no guarantee any trends will continue.

Both the labor agreement and high-frequency data provide a taste of the fruits of a new political economy, or basic rules of the economic road, that's ripened in the past few years. Market forces no longer garner the trust they once did, with capital increasingly steered to policymakers' preferred destinations via tariffs and domestic subsidies. Members of both parties join picket lines, court union votes, and vilify the unbundling of production process and outsourcing that delivered persistent declines in durable goods prices (Figure 4). Fiscal deficits are 2.5x larger than the average of prior decades, after adjusting for the state of the economy.

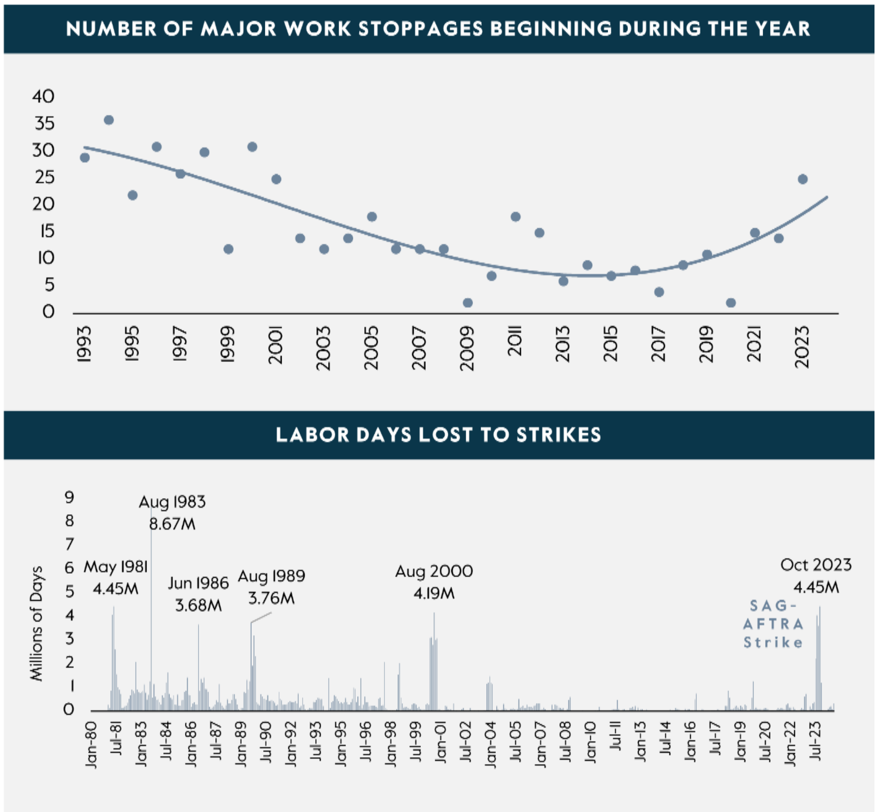
Figure 4: Persistent Goods Price Declines Boosted Purchasing Power



Source: Carlyle Analysis; Federal Reserve, October 2024. There is no guarantee any trends will continue.

After years on a downslope, work stoppages have exhibited an upward trend. And it's notable that the past two major strikes have involved questions about the future of AI and automation (Figure 5; the SAG-AFTRA being the other). The outstanding issues between the longshoremen and their interlocutors involve port automation, with the union demanding an outright ban on the adoption of 'jobs-killing' technology of the sort currently used in China. AI may ultimately prove the most powerful disinflationary force in human history. But thus far it's placed *upward* pressure on prices, as more societal resources are consumed by the hardware, applications, infrastructure, and electricity it demands, and laborers seek recompense for the risk it poses to their livelihood.

Figure 5: Incidence of Work Stoppages



Source: Carlyle Analysis; Bureau of Labor Statistics, October 2024. There is no guarantee any trends will continue.

The future is unknowable, with the evolution of interest rates, asset prices and other financial and economic variables contingent on events that have not yet arrived on our timeline. None of us can forecast it with any certainty, not even the bots. But how can anyone realistically plan for the future if they willfully disregard the messages arriving in the present?

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