# Largest US unemployment spike in 22 years

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The US economy lost 49,000 net jobs in May and the official unemployment rate shot up by half a percentage point in the sharpest month-to-month increase since 1986, according to figures released Friday by the Labor Department. Oil prices rocketed upwards the same day, posting an increase of more than $10 a barrel.

Financial markets reacted violently to these developments, with both the New York Stock Exchange and NASDAQ plunging immediately after trading opened, each closing down by about 3 percent. The US exchange rate, which had been slightly bolstered by the Federal Reserve's hints that it might raise interest rates, fell against the euro as the oil price hit a new record.

The steep jump in unemployment—from 5.0 to 5.5 percent—came as a surprise to analysts, who had been predicting an increase rise of only 0.1 percent. May's net payroll reduction followed a drop of 28,000 jobs in April, and was the fifth consecutive monthly fall. Payrolls have fallen by 324,000 since the year began.

Factory payrolls were reduced by 26,000 last month, after a fall of 49,000 jobs in April,. The overall reduction in manufacturing jobs will be exacerbated by job cuts at General Motors, where most of the 19,000 workers who took a recent buyout package are scheduled to stop working by July 1.

The housing and financial downturns also took a toll on employment figures; housing construction payrolls fell by 34,000, after a drop of 52,000 in April. The service sector lost 8,000 jobs, and retail dropped by 27,000 jobs, while a further 1,000 jobs were lost in the finance. These figures correlate with the latest consumer confidence numbers, which dropped to their lowest level in 15 years. Consumer spending growth likewise reached its lowest level since the 2001 recession.

There have been similar rises in long-term workforce reduction announcements, with the firm Challenger, Gray & Christmas recently reporting that 100,000 job cuts were announced in May, 17 percent higher than the same month in 2007. A number of major US airlines announced significant cuts this week; most recently Continental Airlines, which said Thursday that it would cut 3,000 jobs, or seven percent of its workforce.

The unexpectedly large rise in the unemployment rate—which depends not only the number of jobless but the number of people actively looking for work—appears to have been affected by the influx of students looking to find summer jobs. Economists interviewed in major newspapers expected that part of the unemployment increase would later be amended, and noted that payroll figures were actually somewhat more favorable than expected.

Nevertheless, the announcement triggered a frenzy on Wall Street, as speculators dumped dollars and bought crude oil futures, driving prices up to $139.12 before the market closed up by $10.75 to $138.54. Other commodities saw smaller jumps, and the euro rose one percent against the dollar, hitting $1.58. Unexpectedly rapid trading forced the New York Mercantile Exchange to temporarily shut down some of its operations.

The steady increase in unemployment and fall in payrolls underscores the possibility of a severe US recession materializing in the coming months—an outcome that certain analysts had of late been discounting—and complicates problems for the Federal Reserve, which this week suggested that it might raise rates to shore up the dollar and limit US exposure to soaring commodities prices.

Wall Street's frenzied reaction to the news may be attributable to the critical role of consumer spending in propping up the US economy. Since consumers are so heavily in debt and have lost large amounts of equity through the collapse of the housing bubble, any decrease in employment—and hence income—will likely to manifest itself directly in further defaults and foreclosures. These would in turn further destabilize credit markets, restricting lending and leading to more layoffs.

James Knightley, at ING Group, told the *Financial Times*: "We expect that the labour market will continue to weaken... This is bad news for the household sector, which is already having to cope with negative real wage growth, falling house prices and more expensive borrowing. This will continue to depress consumer spending and will, in our view, help to keep activity depressed for longer than financial markets are currently discounting."

The Dow Jones Industrial Average suffered its worst sell-off in 15 months, closing down 394 points, or 3.13 percent, while the NASDAQ tumbled 2.96 percent. The S&P Financials Index was especially hard-hit, dropping 5 percent. The index fell to its lowest rate since March, despite the emergency lending and interest rate cuts initiated by the Fed during the past three months. Lehman Brothers, which had been rumored to be on the verge of bankrupcy during the Bear Stearns bailout three months ago and is reportedly particularly exposed to bad mortgage loans, responded to a credit rating downgrade earlier this week by preparing to raise an additional $5 billion of capital.

In tandem with the unemployment statistics, home foreclosures reached record levels in the first quarter. According to a figures released by the Mortgage Bankers Association, 8.82 percent of US home mortgages are either already in foreclosure or close to it. The association reported that 2.47 percent of home mortgages had been foreclosed upon in the first quarter, almost double the rate of 1.28 percent in the first quarter of 2007. The percentage of mortgages in default—i.e., those whose borrowers have fallen behind on their payments, but have not yet been foreclosed—jumped by 4.84 percent to 6.35 percent in the same period. This is despite the fact that the Federal Reserve has cut interest rates by more than half during that time.

As borrowers have increasingly run out of options for refinancing and as home values have continued to plummet, a greater proportion of those who fall behind on payments end up being foreclosed. Moreover, the newest figures indicate that mortgages previously considered to have low default risk are showing increasing rates of foreclosure. Christopher Mayer, a Real Estate professor at Columbia Business school, told the *Washington Post*: "The recent increases have been coming from the safer group of borrowers. They are the next shoe to come down."