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Falling Back into Place

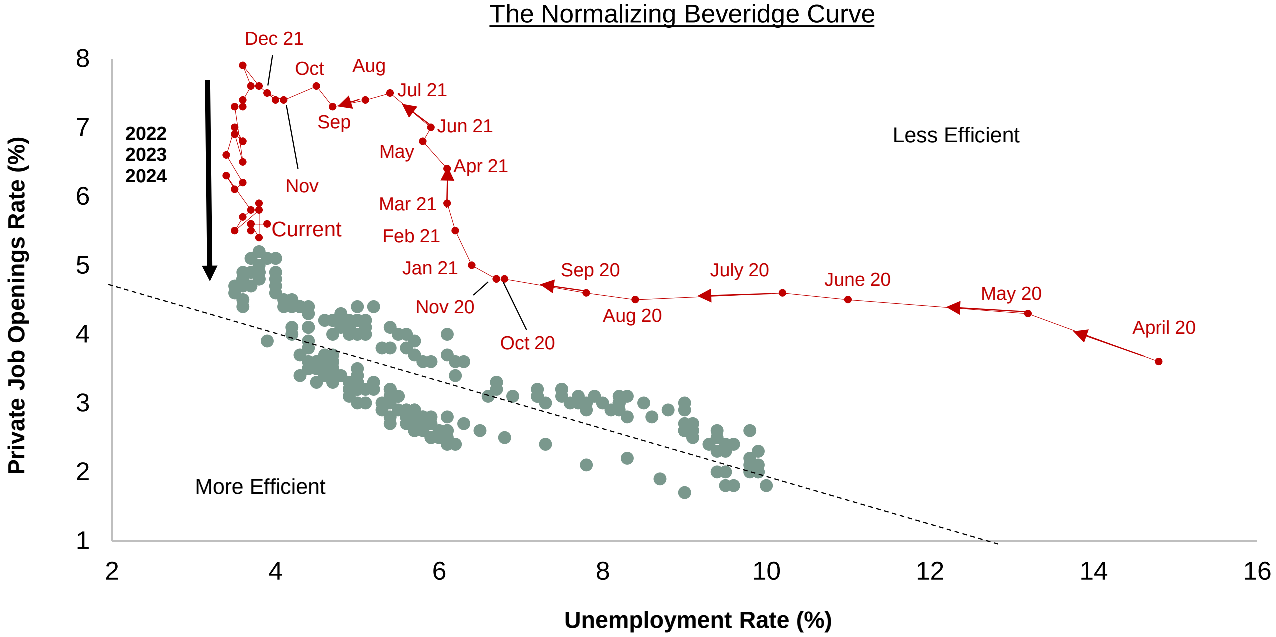
As a result of the pandemic and the ensuing government response, the labor market saw a significant, but ultimately temporary, shift off its structural moorings. This is best illustrated by the Beveridge Curve, which captures the inverse relationship between job openings and the unemployment rate. Not surprisingly, the efficiency of the job matching process broke down during the pandemic when nonessential businesses were forced to close.

These distortions are evident in the upward shift in the Beveridge Curve, as shown below. As we can see, following the pandemic shift, the 2022 and 2023 labor market saw a vertical move straight back to the pre-pandemic curve. The most recent data points are consistent with Beveridge Curve normalization. **This tells us that the efficiency in the job matching process has been almost fully restored to its pre-pandemic state, and this in turn brings important implications for monetary policy.**

As job openings continue to decline, the unemployment rate should rise. **For the Fed, this opening in labor market slack will mitigate inflation risk and potentially open the door for rate cuts.**

What stokes some concern is the *velocity* with which labor demand has decreased. The job openings rate has been falling since March 2022 and has dropped by a full percentage point over the last 12 months. Meanwhile, the February unemployment rate jumped to 3.9%, triggering the historically fatal 50 basis point rule. Normalization comes first, deficiency next.

The Normalizing Beveridge Curve



Sources: BLS, Haver, SMBC Nikko

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