

Fundamental Forex Foundations

1. Non-Farm Payrolls Data

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Introduction

In this new series called “Fundamental Forex Foundations”, it is my desire to introduce some of the Key and Major Data Release Concepts that affect us in the Foreign Exchange World with the most Impact, and those which we simply need to be aware of as our Trading Days move along.

Instead of simply reiterating what each Topic actually is...it is my wish to give a more “Skewed” Explanation of what, why, and how these Data Points and Releases can be used by Currency Traders.

We will look into Ideas that are common with Forex Traders, and how many “generally” choose to use The Data Release Numbers and Results for Trading Purposes and General Analysis of the corresponding Currency Pair, Price, and so on.

Each Topic is different and has its own Characteristics in how it affects The FX Markets, with some being more “useful” from a Trader’s Point of View, than others.

For Example, the 1st in our Series... Non-Farm Payrolls... is without question the most significant Data Point Release that FX Traders, and ALL Traders for that matter, consider to have the most “Direct Impact” on The Markets in the Immediate-Term.

Other Releases, such as The Factory Orders Release, is clearly not as important to us from a Trading perspective, as much of the Data is considered to be “Redundant” with the GDP Data Point Release.

Approximately One Topic will be released weekly, *and I hope to compliment that particular Topic with the actual real Release during that week* so we may have a “real-world” Example to work with that Week.

I would then like to augment that Week’s Subject with additional Data and Commentary that may assist in the understanding of how the Data is being “Digested” by The markets and how Trader’s may be thinking about such Data.

Of course, *ALL* Comments and Thoughts will be most welcome, and *ALL* Inquiries will be addressed and answered in my blog, “Forex Trading Today”:
<http://blogs.fxstreet.com/fxtoday/>

Non-Farm Payrolls Data

The Role of NFP on the 1st Friday of each Month

The State of the U.S. Job Market

Non-Farm Payrolls Data is the most influential Data Point Figure released for ALL Financial Markets... due to the actual Numbers, Volatility, and Expectation. The Headline Unemployment Numbers provide Immediate Month-over-Month Variations, while the Household Survey and Payroll Survey provide detailed Insights into various Sectors of the Economy. The Data is released by The Bureau of Labor Statistics every first Friday of the Month at approximately 12:30 GMT.

Reactions to the Initial Release of NFP can cause deep Volatility as Sentiment and Expectation is measured in Real-Time. Wages & Salaries are the Main Sources of Income for literally ALL American Households, hence Two-Thirds of ALL Economic Output is derived from Household Expenditures. As Payrolls Increase and Decrease, the Level of Income is directly related to the Expenditures of each Household as it gives a Broader Indication of Economic Health in the Country.

The Household and Payroll Surveys

While The Headline Numbers receive much of the Focus, the Survey Numbers are just as crucial. The “Numbers inside the Numbers”, as most Traders refer to them, provide a broader view of actual and sentiment Indication looking out into the future of Labor. The Household Survey consists of about 60,000 Households from a cross-section of the U.S. Economy, with the Data Interviews done during the week that includes the 12th Day of the Month.

These include Employees in the Farm Vocations, the Self-Employed, Non-Farm Labor, Domestic and Household Sectors, Commuters, and so on for an objective Sampling to work with. The Response Rate is rather high, coming in about 95%, which is about 57,000 Households out of the 60K Sample. The Data is then disseminated by dividing the number over 16 Civilians, who are not working, by the total number in the Civilian Labor Force.

Example: If the size of The Labor Force is 100,000 and 10,000 are Unemployed... The Unemployment Rate is 10%.

The Payroll Survey gives a stronger measurement and more criteria and specifics for what our purposes in Trading are concerning NFP as an Entity. This Data/Survey comes from Businesses, Firms, and Agencies... as opposed to Households... and stems directly from The Bureau of Labor Statistics. (BLS).

In this Survey, the Current Employment Statistics (CES) surveys about 150,000 Total Businesses, which represent approximately 400,000 Firms, and Agencies are contacted, and include such diverse Entities as Non-Profit Groups, Small and

Independent Business, Non-Farm Mainstream Sectors, and all levels of Government from the Federal, State, and Local Jurisdictions. The Response Rate here consists of approximately 50% of the Non-Farm Labor Force (about 40-45 Million), and comes in around 65% to 68%, respectively.

(This Figure is in Actuality about 85%, since Small and Independent Businesses hold a higher Turnover with “Last Hired First Fired” Variants, so their Surveys tend to arrive later.

These become a large Factor Basis for the Future Revisions that are seen each Month.)

Most of the Specific Aspects of NFP that are considered are asked in The Payroll Survey.

Sample Criteria include:

- Total Overtime Worked
- Length of the Average Work Week
- Net Number of Jobs Lost or Created
- Average Hourly and Weekly Earnings
- Increase/Decrease Comparisons over the Previous Month

This Broader View allows for a revealing look into the overall Economy, and is why Traders, Investors, Economists, and Analysts place such high emphasis on “The Numbers inside the Numbers” as The Data is released.

Trading Thoughts and Ideas for NFP

Reactions to The Data are crucial for these Entities in their Criteria for altering Policies and Trading Positions.

Some Ideas are as follows:

- **EQUITIES:** A strong NFP Number will prove Buoyant for Stocks and Indices in general. As Employment increases, spending also increases and contributes to the overall Economic Health. Neutral or Weak NFP Numbers will correlate negatively to Stocks and Indices, resulting in Bearish Sentiment.
- **BONDS:** Strong NFP Numbers, and certainly “Better-Than-Expected” Numbers, tend to increase Inflationary Concerns. This, in turn, leads to rising Interest Rates and Lower Bond Prices. Weaker Data has an Inverse Effect with Higher Bond Futures Prices to be expected.
- **CURRENCIES:** Strong NFP Data increases the inherent Value of The U.S. Dollars making them more attractive to Foreign Investment. These Investors can then trade (Buy and Sell) their Own Currency by buying U.S. Dollars which will

be used to buy U.S. Treasuries. In turn, their Investment yields a higher Return than their own Native Currencies.

Negative NFP Data will do the Inverse and drive Value Rates lower, as Foreign Investors decrease their Inflows by selling their U.S. Treasuries and other Vehicles for a more attractive higher-yielding Scenario.

In these past few years, Initial NFP Data Consensus has derived a lot of Weight from the Private Payroll-Producing Firm of ADP (Automatic Data Processing, Inc) Report that is released a couple of Days before NFP each month. While the “Jury is still Out” on the actual Validity and Importance of this Release, it nonetheless is having an increasing Impact on Sentiment and is much more aligned to Governmental Data, so it is wise to be Mindful of Its release.

Another Data Point that will directly affect Market Expectation is the Weekly Jobless (Initial) Claims Data Point that is released the Thursday before the NFP Data Point. This Data is the Final and most Near-Term Data in terms of giving any Clues and Sentiment to NFP Release. It is considered as a “Lagging” Indicator, despite its importance concerning Consumer Spending and as a Bellwether of general Economic Health.

A Common Strategy for Setting up a Position ahead of the NFP Data is to check Current Support and Resistance Levels... irregardless of the Time-Cycle one has chosen. As is the case with literally *ALL* Data Point Releases... Price will usually always find a “Reversion back to The Mean”, as Market Memory comes into View with Price returning to its previous Areas prior to The Release.

Benchmark Revisions are Key to The NFP Data, and in most Cases... Revisions to the Upside will be Dollar Negative and Revisions to the Downside will be Dollar positive. Of course, these Concepts will certainly vary with Market Climate as we have seen all year with Risk Aversion. What is generally “Poor” NFP Data will actually fuel Dollar Strength in a “Counter-Intuitive” Fashion.

Another Common Thought is always allowing a couple of Price Candles or Bars to Close on the Time-Cycle to allow the Impulses in Price to settle... as this will assist in forming “new” Support and Resistance Areas for potential Trading Opportunities.

In many cases, Traders must focus on the actual Unemployment Rate as well, as the broader Measure and “Expectation” of the Country’s Unemployment Percentile will affect “Market Sentiment” moving into the Near-Term Futures. This will be especially true if the NFP Consensus Data comes relatively “In-Line” with Market Expectations. What we will then see is a broader Emphasis put on overall Unemployment as one Market Driving Factor.

For Example, even if we have deeply strong NFP Headline and Interior Numbers... this Data may be “eclipsed” in terms of Importance by a Higher-than-Expected overall Unemployment Percentile... since Unemployment is measured beyond a Month-over-Month Basis like NFP is.

In Conclusion, there are certainly a Myriad of ways and Considerations in working with NFP Data each month from a Trader's Perspective. The deep Volatility and Expectation make the Release exciting for newer Traders especially. This View is tempered by many more experienced and Professional Traders and Institutional Entities who avoid the Risk-Event Exposure altogether.

The Bottom Line is if the Release fits as an Asset or not into One's overall Risk Profile, which of course, is a highly-subjective Decision.



