The strong January employment report offers one promising data point for Federal Reserve officials who are trying to gauge how the U.S. economy weathered increased market volatility and slowing global growth at the end of last year.

Fed officials signaled this week that after raising their benchmark interest rate four times last year, they are on hold until further notice. It will take more than one solid employment report for them to move again.
The Labor Department’s employment report isn’t likely to change their assessment of the risks facing the U.S. economy right now. It was a shift in this judgment—rather than any change in the data itself—that prompted the Fed to reverse its stance from mid-December, when it penciled in more rate increases in 2019.

In December, Fed officials raised their benchmark rate by a quarter percentage point to a range between 2.25% and 2.5% and signaled plans to continue lifting it to around 3% this year.

Fed Chairman Jerome Powell this past Wednesday said the case to raise rates had “weakened somewhat,” and more broadly signaled the Fed had little intention to resume quarterly rate rises anytime soon.

The jobs report shows why Fed officials will stick to their plan to remain patient, meaning they’re going to wait and see how the economy performs for a while before deciding whether to adjust rates.

One of the report’s surveys showed employers added 304,000 jobs in January, keeping the three-month average of monthly gains near a three-year high.

A separate survey showed the unemployment rate edged up to 4% from 3.9%, though some of the increase is likely due to the difficulty measuring who was working during a 35-day partial federal government shutdown.

More important, the number of people holding or seeking jobs—the labor force participation rate—keeps rising, the latest indication there may have been greater slack in the U.S. economy than many economists had previously anticipated. The rate rose to 63.2% in January, up 0.5 percentage point over the past year.

Wage growth was solid, rising 3.2% from a year ago, but there has been little sign over the past year that it is being accompanied by rising inflation.

It’s important to remember that when the Fed says it is data dependent, it means it is looking at a broad spectrum of economic and financial information to gauge the economy’s health as it decides policy.

This doesn’t mean it is data-point dependent, or likely to change policy based on one report. Economic data and financial markets have been telling two different stories about the U.S. economy in recent months.
The positive story comes from the labor market, which reflects broad underlying economic strength.

Financial markets and the global economy tell a gloomier story. Weakness abroad and concerns about trade tensions have squeezed U.S. multinationals and exporters. Manufacturing may be cooling, following a slowdown in interest-rate sensitive sectors of the economy.

Fed officials signaled this week they want more time to determine how these narratives play out over the course of the year. They recognize the full effects of a global slowdown, and recent rises in borrowing costs resulting from the Fed’s rate increases and December’s market spasms may not be fully reflected in economic data for a quarter or two.

Consider the example of 2016: Hiring over the past three months has averaged 241,000 jobs added per month. That’s the strongest such gain since December 2015, when the three-month average reached 283,000 jobs. Markets then fell in January 2016 amid worries about a sharp economic slowdown in China, and the three-month U.S. payroll growth steadily slowed to 148,000 jobs, on average, that May.

The Fed scrapped its plans to raise rates four times in 2016, and only moved once, in December.

“Twenty-sixteen was an example of a situation where linkages from U.S. monetary policy to global financial conditions and growth and back again—spillbacks to the U.S. outlook—did lead to a significant revision of what the appropriate path of policy should be,” said Janet Yellen, who was Fed chairwoman at the time, on a panel with Mr. Powell last month. “And I don’t have any regrets about that.”

The strong January 2019 jobs report does little to change the first story. But it would take solid employment reports for February, March, April and May to prove that second story is wrong.

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