

Q1 Productivity (Final)

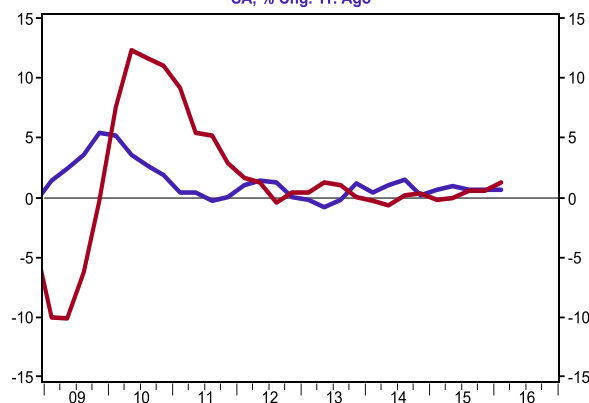
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- Nonfarm productivity (output per hour) declined at a 0.6% annual rate in the first quarter, revised higher from last month's -1.0% estimate. Nonfarm productivity is up 0.7% versus last year.
- Real (inflation-adjusted) compensation per hour in the nonfarm sector increased at a 4.2% annual rate in Q1 and is up 2.6% versus last year. Unit labor costs rose at a 4.5% rate in Q1 and are up 3.0% versus last year.
- In the manufacturing sector, productivity rose at a 1.3% annual rate in Q1, much better than among nonfarm business as a whole. The increase in productivity growth compared to the nonfarm sector as a whole was due to a decline in hours. Real compensation per hour was up in the manufacturing sector (2.8%) and unit labor costs rose at a 1.1% annual rate.

Implications: No surprise here. Productivity growth in the first quarter was revised slightly higher, consistent with the upward revision to real Q1 GDP. According to the official data, nonfarm productivity declined at a 0.6% annual rate in Q1. Output rose 0.9%, while hours climbed at a faster 1.5%, so output per hour fell. The key part of today's report was that unit labor costs – how much companies have to pay workers per unit of output – increased at a 4.5% annual rate in the first quarter and are up at a 2.1% annual rate in the past two years and 3% in the past year, signaling the kind of compensation pressure that will get the attention of the Keynesians at the Federal Reserve. That's why even with the weak payroll number for May, we still think the Fed will consider raising short-term rates at the meeting next week, but will most likely wait until July. The official measure of productivity is up 0.7% from a year ago, but we suspect the government is underestimating output in the service sector, which means economic growth and productivity are higher than the official data show. Remember when you had to look in separate places for the weather, directions, business contacts, email, news, taxis...? The list goes on and on. Now all you have to do is reach into your pocket, or for some, look at your watch. What's amazing is most of these technologies are free, but the problem is anything free, no matter how much it improves people's lives, isn't directly included in productivity because it can't be measured. For this reason, we believe the figures from the government miss the value of these improvements, which means our standard of living is improving faster than the official reports show. Still, even on the manufacturing side, where it's easier to measure output per hour, productivity is up only 1.3% in the past year. This is consistent with overall productivity growth of 1.5% on average per year from 1973 through 1995. However it's slower than the 2.0% average per year since 1995. In spite of the problems with measurement, we anticipate faster productivity growth over the next few years as new technology increases output in all areas of the economy. The declining unemployment rate and faster growth in wages should create more pressure for efficiency gains, while the technological revolution continues to provide the inventions that make those gains possible. Overall, for 2016-17, we look for faster productivity growth than in the past two years.

Manufacturing Sector: Real Output Per Hour
 SA, % Chg. Yr. Ago

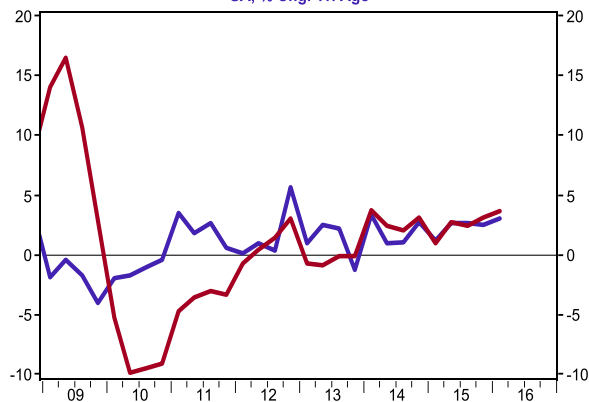
Nonfarm Business Sector: Real Output Per Hour
 SA, % Chg. Yr. Ago



Source: Bureau of Labor Statistics /Haver Analytics

Manufacturing Sector: Unit Labor Cost
 SA, % Chg. Yr. Ago

Nonfarm Business Sector: Unit Labor Cost
 SA, % Chg. Yr. Ago



Source: Bureau of Labor Statistics /Haver Analytics

Productivity and Costs (% Change, All Data Seasonally Adjusted)	Q1-16	Q4-15	Q3-15	Q2-15	Y to Y % Ch. (Q1-16/Q1-15)	Y to Y % Ch. (Q1-15/Q1-14)
Nonfarm Productivity	-0.6	-1.7	2.0	3.1	0.7	0.7
- Output	0.9	1.5	1.8	5.1	2.3	3.5
- Hours	1.5	3.3	-0.2	1.9	1.6	2.7
- Compensation (Real)	4.2	2.7	1.0	2.6	2.6	2.0
- Unit Labor Costs	4.5	5.4	0.4	2.0	3.0	1.2
Manufacturing Productivity	1.3	-1.2	3.7	1.5	1.3	-0.1
- Output	0.6	-0.5	1.9	0.6	0.6	2.1
- Hours	-0.7	0.6	-1.7	-0.9	-0.7	2.3
- Compensation (Real)	2.8	7.1	2.6	3.0	3.8	0.8
- Unit Labor Costs	1.1	9.2	0.3	4.0	3.6	0.9

Source: US Department of Labor