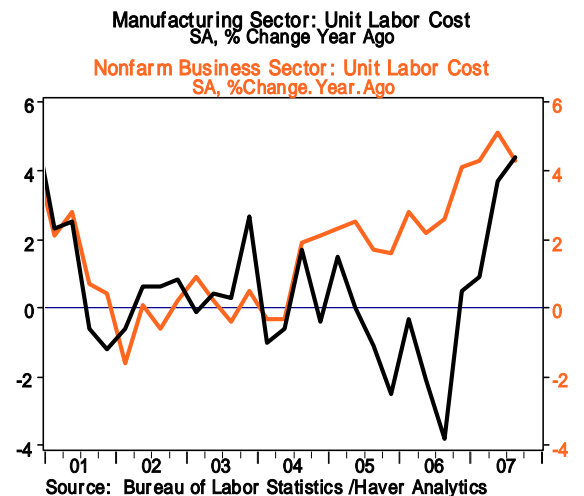
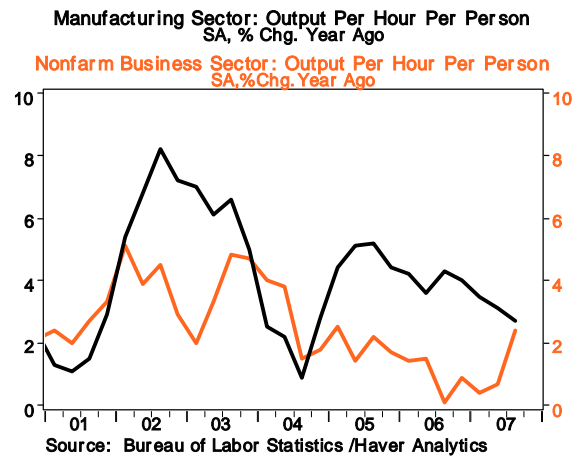


## Q3 PRODUCTIVITY (PRELIM)

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- Non-farm productivity (output per hour) grew at a 4.9% annual rate in Q3, the fastest quarter since 2003. The consensus forecast was 3.2%. Non-farm productivity is up 2.4% versus a year ago.
- Real (inflation-adjusted) compensation per hour in the non-farm sector increased at a 2.7% annual rate in Q3 and is up 4.3% versus a year ago. Non-farm unit labor costs declined at a 0.2% rate in Q3 but are up 4.3% versus a year ago.
- Manufacturing productivity increased at a 4.6% annual rate in Q3 and is up 2.7% versus a year ago.

**Implications:** Today's productivity report is bullish news for the U.S. economy. Productivity grew 4.9% in Q3, the fastest since 2003, and is up 2.4% versus a year ago, the best since 2004. Productivity growth gradually slowed from late 2003 through early 2007 as a rising share of GDP growth came from hiring more workers and giving them more hours rather than generating more output per hour. Now, with labor markets tighter and GDP growth re-accelerating, productivity growth has revived. A similar slowdown and rebound occurred in the mid-1990s. Although unit labor costs fell at a 0.2% rate in Q3, they are up 4.3% versus a year ago. Real compensation, which includes wages and salaries plus fringe benefits, increased at a 2.7% rate in Q3 and is also up 4.3% versus last year. Unlike most economists, we think higher inflation is a much bigger risk in the year ahead than slow growth. However, we do not view higher worker compensation as a problem in a solidly growing economy. Loose money causes inflation, not higher wages. Labor compensation grew relatively slowly in the early stages of the current expansion as profits surged. Now workers are catching up and the purchasing power of their wages and benefits will grow faster than the overall economy, supporting consumption even as average home prices continue to decline.



Productivity and Costs (% Change, All Data Seasonally Adjusted)	Q3-07	Q2-07	Q1-07	Q4-06	Y to Y % Ch. (Q3-07/Q3-06)	Y to Y % Ch. (Q3-06/Q3-05)
<b>Nonfarm Productivity</b>	<b>4.9</b>	2.2	0.7	1.8	2.4	0.1
- Output	4.3	4.2	0.3	2.6	2.9	2.4
- Hours	-0.5	2.0	-0.3	0.8	0.5	2.4
- Compensation	4.7	4.4	5.9	12.2	6.7	2.7
- Unit Labor Costs	-0.2	2.2	5.2	10.3	4.3	2.6
<b>Manufacturing Productivity</b>	<b>4.6</b>	2.4	1.7	2.0	2.7	4.3
- Output	4.3	4.4	0.9	-2.1	1.9	6.1
- Hours	-0.4	2.0	-0.8	-4.0	-0.8	1.7
- Compensation	2.3	3.7	8.9	14.2	7.2	0.3
- Unit Labor Costs	-2.2	1.3	7.0	12.0	4.4	-3.8
<b>Durable Goods Productivity</b>	<b>5.7</b>	5.2	1.6	2.7	3.8	6.9
<b>Nondurable Goods Productivity</b>	<b>4.1</b>	-0.8	1.2	1.0	1.3	1.4

Source: US Department of Labor