

## Q2 PRODUCTIVITY (PRELIMINARY)

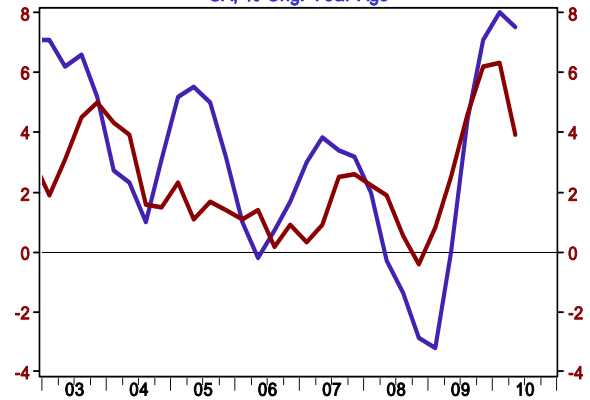
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- Non-farm productivity (output per hour) fell at a 0.9% annual rate in the second quarter. Non-farm productivity is up 3.9% versus last year.
- Real (inflation-adjusted) compensation per hour (non-farm) was unchanged in Q2, but is down 0.7% versus last year. Unit labor costs increased at a 0.2% rate in Q2 but are down 2.8% versus a year ago.
- In the manufacturing sector, the Q2 growth rate for productivity (4.5%) was much higher than among non-farm businesses as a whole. Output grew faster in manufacturing and the growth of hours worked were the same. Real compensation (-1.2%) and unit labor costs (-6.1%) were softer in manufacturing as productivity pushed down unit costs.

**Implications:** Productivity fell unexpectedly in the second quarter. But Q1 productivity was revised upwardly to 3.9% growth from 2.8%. Total non-farm output fell in the second quarter, while the number of hours worked rose. Some may fret that productivity has reached a plateau. We look at it as a pause. Hours worked have increased in each of the past three quarters, yet productivity has still grown at a 3.0% annual rate. As output rebounds, technology will continue to work its magic, allowing each and every worker to accomplish more. Longer-term trends paint the picture. Productivity in the past year has accelerated to a 3.9% annual rate from a 2.5% rate the year before. Unit labor costs – how much companies have to pay workers per unit of production – are down 2.8% in the past year. This means it is more profitable for companies to expand operations and boost hours worked. In the manufacturing sector, productivity grew 4.5% at an annual rate, and is up at a 7.5% rate from a year ago. Durable manufacturing productivity rose at an astounding 11.2% annual rate, while unit labor costs fell at an 11.4% annual rate. We view this as a benefit of the restructuring of the auto industry. While restructuring is a painful process for the individual people involved (auto workers and union members who lose jobs or see pay reduced), the economy benefits immediately. Productivity improvements free up resources to be used in other sectors. As long as government does not squander these gains, by taxing them away, or redistributing borrowed funds, the benefits will outweigh the costs. The same will be true as cuts occur in state and local government. There will be a benefit that helps offset the cost.

Nonfarm Business Sector: Output Per Hour Per Person  
SA, % Chg. Year Ago

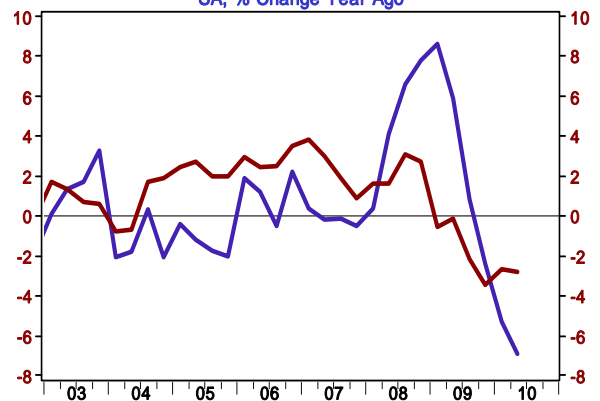
Manufacturing Sector: Output Per Hour Per Person  
SA, % Chg. Year Ago



Sources: Bureau of Labor Statistics /Haver Analytics

Nonfarm Business Sector: Unit Labor Cost  
SA, % Change Year Ago

Manufacturing Sector: Unit Labor Cost  
SA, % Change Year Ago



Sources: Bureau of Labor Statistics /Haver Analytics

Productivity and Costs (% Change, All Data Seasonally Adjusted)	Q2-10	Q1-10	Q4-09	Q3-09	Y to Y % Ch. (Q2-10/Q2-09)	Y to Y % Ch. (Q2-09/Q2-08)
<b>Nonfarm Productivity</b>	-0.9	3.9	6.0	7.0	3.9	2.5
- Output	2.6	5.0	6.7	1.4	3.9	-5.6
- Hours	3.6	1.1	0.7	-5.2	0.0	-8.0
- Compensation (Real)	0.0	-1.5	-1.1	-0.3	-0.7	3.4
- Unit Labor Costs	0.2	-3.7	-4.2	-3.3	-2.8	-0.1
<b>Manufacturing Productivity</b>	4.5	1.2	8.1	16.9	7.5	0.0
- Output	8.3	7.0	7.2	10.9	8.3	-14.7
- Hours	3.6	5.7	-0.8	-5.1	0.8	-14.7
- Compensation (Real)	-1.2	-6.4	1.6	-0.4	-1.6	7.0
- Unit Labor Costs	-6.1	-6.2	-3.5	-11.6	-6.9	5.9

Source: US Department of Labor

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