

Q2 Productivity (Preliminary)

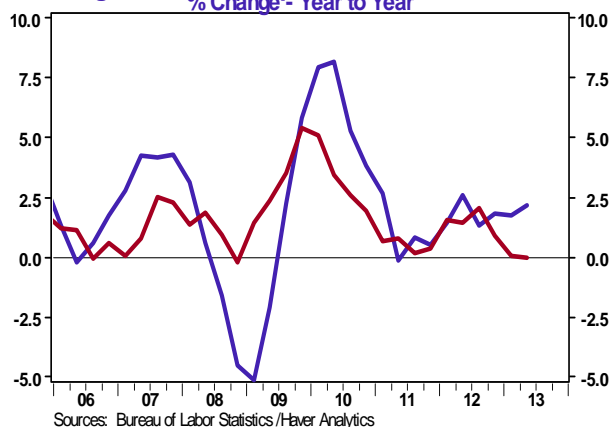
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- Nonfarm productivity (output per hour) increased at a 0.9% annual rate in the second quarter, coming in above the consensus expected gain of 0.6%. Non-farm productivity is unchanged versus last year.
- Real (inflation-adjusted) compensation per hour in the non-farm sector rose at a 2.3% annual rate in Q2, and is up 0.1% versus last year. Unit labor costs rose at a 1.4% rate in Q2 and are up 1.6% versus a year ago.
- In the manufacturing sector, productivity was up at a 2.7% annual rate in Q2, much faster than among nonfarm businesses as a whole. The gain in manufacturing productivity was due to a small gain in output combined with a larger decline in hours. Real compensation per hour was up 4.2% in the manufacturing sector, while unit labor costs increased at a 1.4% annual rate.

Implications: Nonfarm productivity increased at a Plow Horse-like 0.9% annual rate in Q2, as hours increased at a healthy clip, but output climbed even faster. After surging rapidly in 2009, productivity grew at a moderate pace in 2010 and has since slowed down even further. In fact, productivity is now unchanged from a year ago. One possibility is that the government is having a hard time measuring production in the increasingly important service sector, which means both output growth and productivity growth are higher than the official data show. (For example, do the data fully capture the value of smartphone apps, the tablet, the cloud,...etc.?) Another possibility is that we're just seeing what we've seen in the past at this stage of economic recoveries, where companies add hours (at relatively low wages) to meet higher demand and there is less pressure to squeeze out productivity gains from the existing workforce. Only this time, given the depth of the recession and still relatively high unemployment rate, that process could take longer than usual. Either way, these figures are consistent with a Plow Horse economy. From 1973 through 1995, productivity growth averaged 1.4% per year. Since then it's averaged 2.3%. Despite slower productivity growth in the past few years, we think the long-term trend in productivity growth is still strong, a result of the technological revolution that began in the 1980s. On the manufacturing side, where it's easier to measure output per hour, productivity rose at a 2.7% annual rate in Q2. Manufacturers, due to new technologies, are still able to increase output faster than hours. We anticipate an acceleration in productivity growth over the next two years. 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.

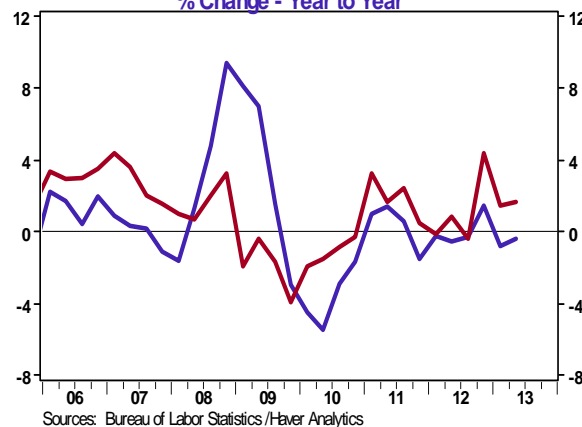
farm Business Sector: Real Output Per Hour of All Persons
 % Change - Year to Year

Manufacturing Sector: Real Output Per Hour of All Persons
 % Change - Year to Year



Nonfarm Business Sector: Unit Labor Cost
 % Change - Year to Year

Manufacturing Sector: Unit Labor Cost
 % Change - Year to Year



Productivity and Costs (% Change, All Data Seasonally Adjusted)	Q2-13	Q1-13	Q4-12	Q3-12	Y to Y % Ch. (Q2-13/Q2-12)	Y to Y % Ch. (Q2-12/Q2-11)
Nonfarm Productivity	0.9	-1.7	-1.7	2.5	0.0	1.4
- Output	2.6	-0.3	0.7	4.1	1.8	3.5
- Hours	1.7	1.5	2.4	1.6	1.8	2.1
- Compensation (Real)	2.3	-7.3	7.5	-1.3	0.1	0.3
- Unit Labor Costs	1.4	-4.2	11.8	-1.8	1.6	0.8
Manufacturing Productivity	2.7	3.9	2.3	-0.3	2.2	2.6
- Output	0.1	5.6	2.7	0.1	2.1	5.1
- Hours	-2.6	1.6	0.4	0.4	-0.1	2.4
- Compensation (Real)	4.2	-0.9	1.9	-3.8	0.3	0.1
- Unit Labor Costs	1.4	-3.2	1.8	-1.5	-0.4	-0.6

Source: US Department of Labor

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