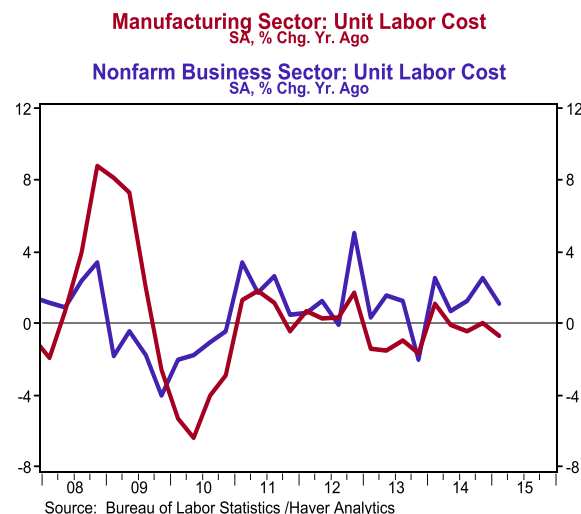
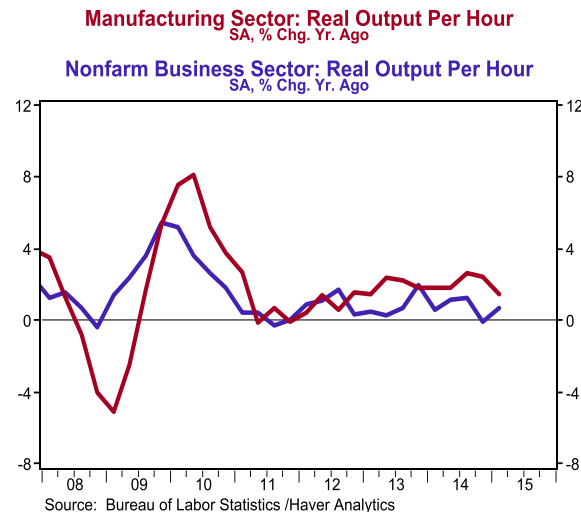


# Q1 Productivity (Preliminary)

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- Nonfarm productivity (output per hour) declined at a 1.9% annual rate in the first quarter, matching consensus expectations. Nonfarm productivity is up 0.6% versus last year.
- Real (inflation-adjusted) compensation per hour in the nonfarm sector was up at a 6.2% annual rate in Q1 and is up 1.8% versus last year. Unit labor costs rose at a 5.0% rate in Q1 and are up 1.1% versus a year ago.
- In the manufacturing sector, productivity declined at a 1.1% annual rate in Q1, a smaller dip than among nonfarm businesses as a whole. The smaller drop in manufacturing productivity was due to a decline in hours. Real compensation per hour rose at a 4.6% annual rate in the manufacturing sector, while unit labor costs increased at a 2.7% rate.

**Implications:** The government’s first report on real GDP growth in Q1 showed a scant gain of 0.2% at an annual rate, even though job growth continued during the quarter. So it should come as no surprise that nonfarm productivity declined in Q1. Output fell slightly, while hours climbed 1.7% at an annual rate, so output *per hour* declined at a 1.9% annual rate. In spite of the decline in Q1, productivity is up 0.6% from a year ago, exactly the same as the 0.6% annualized growth rate of the previous four years. However we suspect the government is underestimating output in the increasingly important service sector, which means growth and productivity are higher than the official data show. (For example, do the data fully capture the value of new technologies like smartphone apps, the tablet, the cloud,...etc.?) 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. 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 1.4% in the past year. This is consistent with overall productivity growth of 1.5% on average per year from 1973 through 1995. However its slower than the 2.1% 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, decline in labor force participation, 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 2015-16, we look for faster productivity growth than in the past five years. In other news this morning, the ADP index, which measures private-sector payrolls, showed a gain of 169,000 in April. Our models now forecast a nonfarm gain of 275,000, although the forecast may change slightly tomorrow based on new data for unemployment claims.



Productivity and Costs (% Change, All Data Seasonally Adjusted)	Q1-15	Q4-14	Q3-14	Q2-14	Y to Y % Ch. (Q1-15/Q1-14)	Y to Y % Ch. (Q1-14/Q1-13)
<b>Nonfarm Productivity</b>	-1.9	-2.1	3.9	2.9	0.6	0.6
- Output	-0.2	2.6	6.3	5.5	3.5	2.4
- Hours	1.7	4.9	2.4	2.5	2.9	1.8
- Compensation (Real)	6.2	2.8	1.7	-3.3	1.8	1.7
- Unit Labor Costs	5.0	4.2	-1.0	-3.7	1.1	2.5
<b>Manufacturing Productivity</b>	-1.1	-0.1	3.4	3.7	1.4	1.9
- Output	-1.2	4.3	4.9	7.3	3.8	2.4
- Hours	-0.1	4.4	1.4	3.4	2.3	0.5
- Compensation (Real)	4.6	2.2	1.0	-4.2	0.8	1.5
- Unit Labor Costs	2.7	1.5	-1.3	-5.4	-0.7	1.0

Source: US Department of Labor