

# Q4 PRODUCTIVITY (PRELIMINARY)

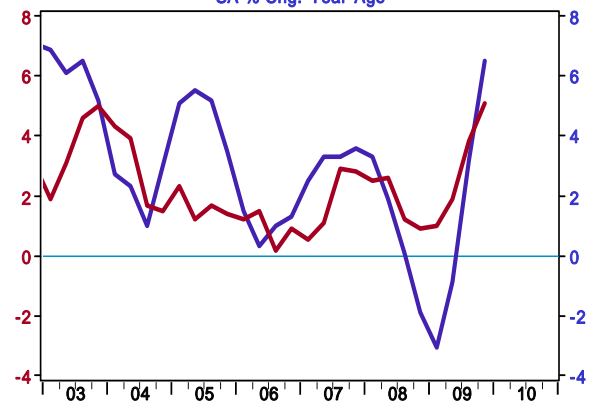
Chief Economist – Brian S. Wesbury  
Senior Economist – Robert Stein, CFA

- Non-farm productivity (output per hour) rose at a 6.2% annual rate in the fourth quarter, falling just short of the consensus expected 6.5% growth rate. Non-farm productivity is up 5.1% versus last year.
- Real (inflation-adjusted) compensation per hour in the non-farm sector fell at a 1.9% annual rate in Q4, but is up 0.7% versus last year. Unit labor costs dropped at a 4.4% rate in Q4 and are down 2.8% versus a year ago.
- In the manufacturing sector, the Q4 growth rate for productivity (7.8%) was higher than in non-farm businesses, but output (6.1%), and real compensation (-3.5%) were slower than in the non-farm sector. Due to a combination of faster productivity growth and lower compensation growth in manufacturing, the rate of decline in unit labor costs (-7.4%) was greater in that sector than among non-farm businesses.

**Implications:** You have to go back to the mid-1960s to find three straight quarters where productivity – output per hour worked – has boomed as rapidly as it did in Q2-Q4 of 2009. While many focus on the fact hours worked declined during the early (Q2 and Q3) part of this boom, this was not the case in the latest quarter. Output grew at a 7.2% annual rate in Q4, while the number of hours worked grew at a 1.0% annual rate. Contrary to popular belief, this surge in productivity does not mean that employment must grow slowly. Rapid productivity growth and falling unit labor costs mean it is getting more and more profitable for companies to expand operations and boost hours worked. In the past year alone, unit labor costs – labor compensation per unit of output – fell 2.8%, the largest drop since 2002. This will put upward pressure on labor demand, leading to net job creation very soon. It is clear, however, that the labor market will not return to its late 1990s or mid-2000s vibrancy (with unemployment rates below 5%) as long as the burdens of government remain as large as they are today. As an exclamation point on this fact, new claims for unemployment insurance increased 8,000 last week to 480,000. The four-week moving average rose to 469,000. We still expect a small increase in employment to show up in tomorrow’s January employment report.

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

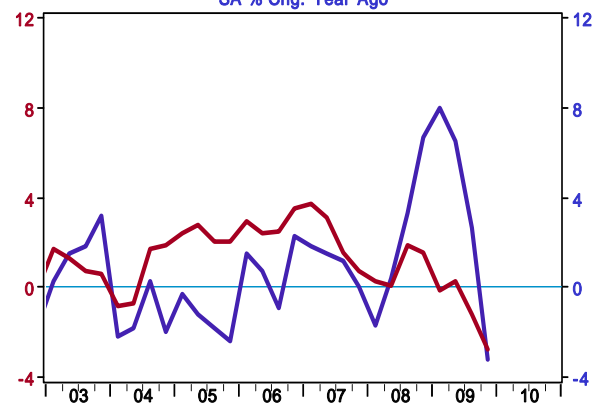
Manufacturing Sector: Output Per Hour Per Person  
SA % Chg. Year Ago



Source: Bureau of Labor Statistics /Haver Analytics

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

Manufacturing Sector: Unit Labor Cost  
SA % Chg. Year Ago



Source: Bureau of Labor Statistics /Haver Analytics

<b>Productivity and Costs</b> (% Change, All Data Seasonally Adjusted)	<b>Q4-09</b>	<b>Q3-09</b>	<b>Q2-09</b>	<b>Q1-09</b>	<b>Y to Y % Ch.</b> (Q4-09/Q4-08)	<b>Y to Y % Ch.</b> (Q4-08/Q4-07)
<b>Nonfarm Productivity</b>	<b>6.2</b>	7.2	6.9	0.3	5.1	0.9
- Output	7.2	2.2	-1.1	-8.8	-0.3	-3.0
- Hours	1.0	-4.7	-7.5	-9.0	-5.1	-4.0
- Compensation (Real)	-1.9	1.9	5.5	-2.4	0.7	1.0
- Unit Labor Costs	-4.4	-1.5	0.0	-5.0	-2.8	1.6
<b>Manufacturing Productivity</b>	<b>7.8</b>	14.4	6.8	-2.5	6.5	-1.9
- Output	6.1	9.5	-8.1	-21.7	-4.4	-8.7
- Hours	-1.6	-4.2	-13.9	-19.8	-10.2	-7.0
- Compensation (Real)	-3.5	2.7	5.1	2.0	1.5	3.1
- Unit Labor Costs	-7.4	-7.0	-0.2	2.2	-3.2	6.7

Source: US Department of Labor