

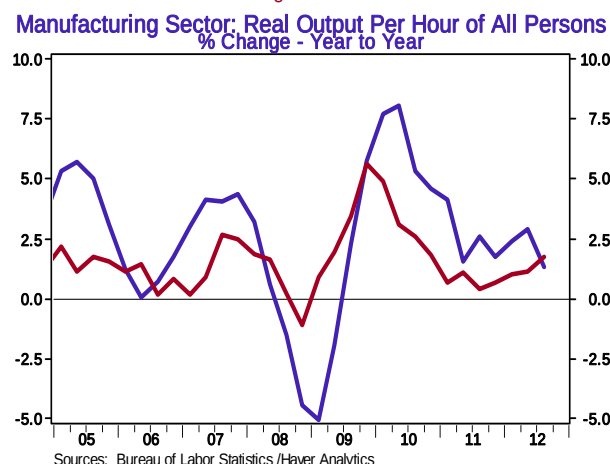
Q3 Productivity (Final)

Brian S. Wesbury – Chief Economist
Robert Stein, CFA – Senior Economist
Strider Elass – Economic Analyst

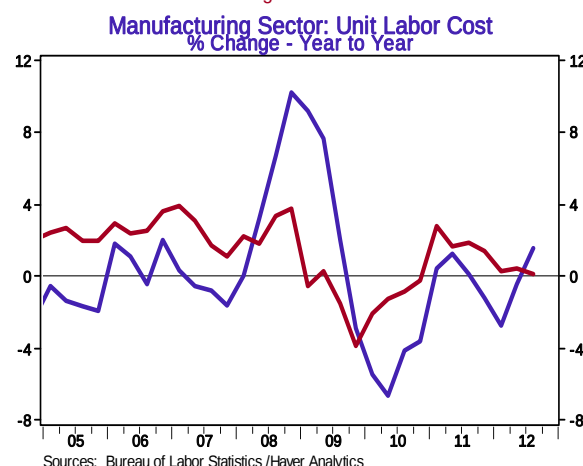
- Nonfarm productivity (output per hour) rose at a 2.9% annual rate in the third quarter, revised up from last month's estimate of 1.9%. Nonfarm productivity is up 1.7% versus last year.
- Real (inflation-adjusted) compensation per hour in the nonfarm sector fell at a 1.4% annual rate in Q3 but is up 0.1% versus last year. Unit labor costs declined at a 1.9% rate in Q3 but are also up 0.1% versus a year ago.
- In the manufacturing sector, the Q3 growth rate for productivity (-0.7%) was substantially lower than among nonfarm businesses as a whole. The slower pace in productivity growth was due to hours remaining unchanged while output fell. Real compensation per hour was up in the manufacturing sector (0.1%), and due to the decline in output, unit labor costs rose at a 3.2% annual rate.

Implications: Productivity was revised up substantially for the third quarter, consistent with last week's upward revision for real GDP growth. Output was revised up while the number of hours worked stayed the same, which means more output per hour. Productivity is up 1.7% in the past year, versus an average annual growth rate of about 2% over the past couple of decades. However, we do not think this means the productivity revolution has come to an end. It is not unusual for productivity to surge at the very beginning of a recovery and then temporarily slow down as hours worked increase more sharply. We believe the long-term trend in productivity growth will remain strong, due to a technological revolution centered in computer and communications advances. In fact, Q3 productivity rose at the fastest rate in two years. It's nothing to write home about, but it's consistent with a plow horse economy. In other news this morning, the ADP employment index, which measures private sector payrolls, increased 118,000 in November. Plugging all these figures into our employment models suggests Friday's official Labor Department report will show a 75,000 gain in payrolls, both nonfarm and private. We may tweak this forecast one more time, though, when we get tomorrow morning's report on unemployment claims.

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



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



Productivity and Costs (% Change, All Data Seasonally Adjusted)	Q3-12	Q2-12	Q1-12	Q4-11	Y to Y % Ch. (Q3-12/Q3-11)	Y to Y % Ch. (Q3-11/Q3-10)
Nonfarm Productivity	2.9	1.9	-0.5	2.8	1.7	0.4
- Output	4.2	2.1	2.7	5.3	3.5	2.2
- Hours	1.3	0.2	3.2	2.4	1.8	1.7
- Compensation (Real)	-1.4	0.6	3.3	-1.9	0.1	-1.4
- Unit Labor Costs	-1.9	-0.5	6.4	-3.3	0.1	1.9
Manufacturing Productivity	-0.7	-0.1	5.5	0.7	1.3	2.6
- Output	-0.7	1.2	10.2	5.5	4.0	3.9
- Hours	0.0	1.3	4.4	4.8	2.6	1.3
- Compensation (Real)	0.1	8.1	4.2	-7.2	1.1	-1.0
- Unit Labor Costs	3.2	9.0	1.1	-6.6	1.5	0.1

Source: US Department of Labor