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Q4 Productivity (Final)

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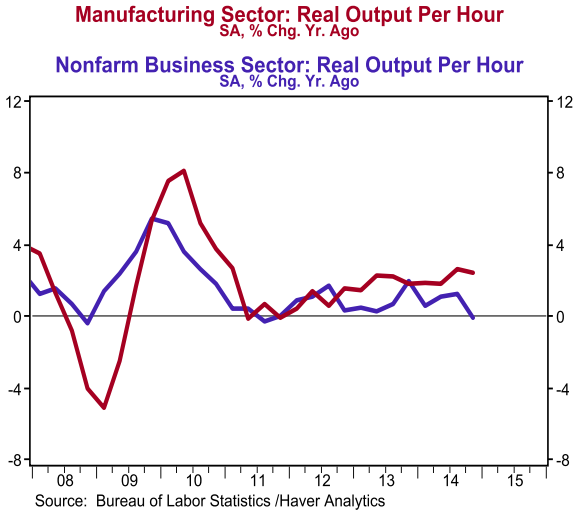
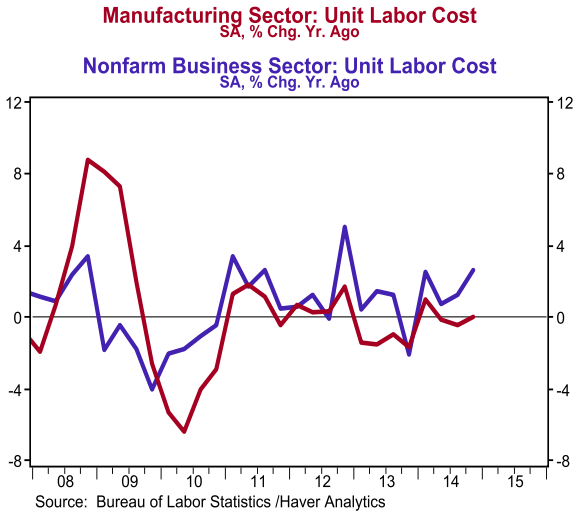
- Nonfarm productivity (output per hour) declined at a 2.2% annual rate in the fourth quarter, revised lower from last month's -1.8% estimate. Nonfarm productivity is down 0.1% versus last year.

- Real (inflation-adjusted) compensation per hour in the nonfarm sector rose at a 3.1% annual rate in Q4 and is up 1.3% versus last year. Unit labor costs rose at a 4.1% rate in Q4 and are up 2.6% versus a year ago.

- In the manufacturing sector, the -0.1% annual growth rate for productivity in Q4 was better than among all nonfarm businesses. The slower decline in productivity growth was due to faster growth in output and slower growth in hours than in the nonfarm sector as a whole. Real compensation per hour was up in the manufacturing sector (2.7%) and unit labor costs rose at a 1.5% annual rate.





Implications: Productivity growth in the fourth quarter was revised lower, consistent with last week's downward revision to real GDP. According to the official data, nonfarm productivity declined at a 2.2% annual rate in Q4. Output continued to increase at a healthy clip, but hours climbed at the fastest rate since 1998, so output *per hour* declined. Productivity is down 0.1% from a year ago, but 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. Do the data fully capture the value of smartphone apps, the tablet, the cloud...etc.? For example, many now deposit checks by using their phones, rather than going to the bank. This is just one example why we think the figures from the government miss the value of these improvements, which means our standard of living is improving faster than the official reports suggest. Note that on the manufacturing side, where it's easier to measure output per hour, productivity is up 2.4% in the past year. From 1973 through 1995, overall productivity growth averaged 1.5% per year. 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 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 two years. In other news, new claims for unemployment insurance increased 7,000 to 320,000 last week. Continuing claims rose 17,000 to 2.42 million. Plugging these figures into our models suggests tomorrow's employment report will show a nonfarm payroll gain of 240,000 for February, another solid month.

Productivity and Costs *(% Change, All Data Seasonally Adjusted)*	Q4-14	Q3-14	Q2-14	Q1-14	Y to Y % Ch. *(Q4-14/Q4-13)*	Y to Y % Ch. *(Q4-13/Q4-12)*
Nonfarm Productivity	**-2.2**	3.9	2.9	-4.7	-0.1	2.0
- Output	**2.6**	6.3	5.5	-2.4	2.9	3.7
- Hours	**4.9**	2.4	2.5	2.4	3.0	1.6
- Compensation (Real)	**3.1**	1.7	-3.8	4.3	1.3	-1.3
- Unit Labor Costs	**4.1**	-1.0	-3.7	11.5	2.6	-2.1
Manufacturing Productivity	**-0.1**	3.5	3.7	2.6	2.4	1.8
- Output	**4.3**	4.9	7.3	1.6	4.5	3.2
- Hours	**4.4**	1.4	3.4	-1.0	2.0	1.3
- Compensation (Real)	**2.7**	1.0	-4.8	6.3	1.2	-1.1
- Unit Labor Costs	**1.5**	-1.3	-5.4	5.5	0.0	-1.7

Source: US Department of Labor