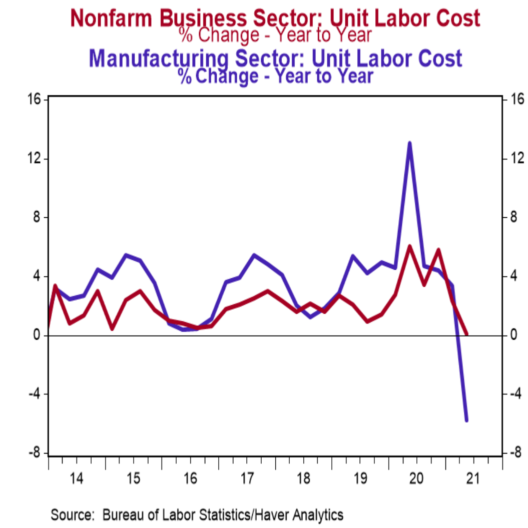
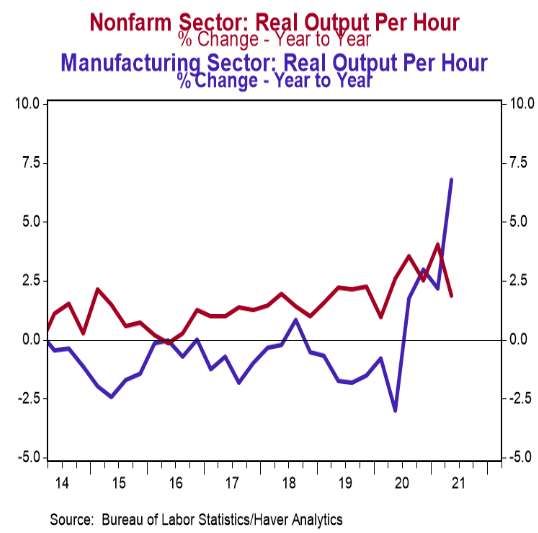
Q2 Productivity (Preliminary)

Brian S. Wesbury – Chief Economist
Robert Stein, CFA – Dep. Chief Economist
Strider Elass – Senior Economist
Andrew Opdyke, CFA – Senior Economist

- Nonfarm productivity (output per hour) increased 2.3% at an annual rate in the second quarter, lagging the consensus expected annualized gain of 3.2%. Nonfarm productivity is up 1.9% versus last year.
- Real (inflation-adjusted) compensation per hour in the nonfarm sector declined at a 4.8% annual rate in Q2 and is down 2.7% versus a year ago. Unit labor costs rose at a 1.0% annual rate in Q2 and are up 0.1% versus a year ago.
- In the manufacturing sector, productivity increased at a 6.9% annual rate in Q2. Real compensation per hour declined at a 3.3% annual rate in the manufacturing sector, while unit labor costs fell at a 1.9% annual rate.

Implications: Productivity grew at a robust pace in the second quarter, but despite increased hours and higher pay, rising inflation remains a key headwind impacting workers' purchasing power. The Q2 increase in nonfarm productivity came as output and hours worked both rose, but output rose at a faster pace than hours worked pushing output per hour higher. The 5.5% annualized increase in the hours worked index still leaves this measure 2.8% lower than it was in Q4 of 2019, the last quarter not affected by the COVID-19 pandemic. Output, however, with the 7.9% annualized increase in Q2, now stands 1.2% above the level in the fourth quarter of 2019. What this shows is that in spite of the pain of the COVID crisis, businesses made gains in enhancing efficiency. Now, as companies eagerly seek to hire more workers, the higher-wage bidding war for workers means businesses have to be careful where they hire, another incentive to enhanced efficiency per hour. Although "real" (inflation-adjusted) compensation per hour fell at a 4.8% annualized rate in Q2, that doesn't mean workers are being paid less. In fact, wages have been rising, they just haven't been able to keep up with the outsized rise in inflation. This is likely to remain an ongoing issue in the coming quarters, as inflation remains elevated while the rehiring of lower-paid workers puts downward pressure on the average amount paid per hour. On the manufacturing front, productivity grew at a 6.9% annualized rate as output rose while hours fell. This reflects ongoing supply chain issues, but also the shift in consumption from goods to services that has emerged as consumers got back to things they couldn't do throughout much of last year. We are now well into a recovery, but expect hours and output will continue to rise in the quarters ahead as the labor force continues to heal and we work to get back to the level of output the U.S. would have seen had COVID never happened.





Productivity and Costs (% Change, All Data Seasonally Adjusted)	Q2-21	Q1-21	Q4-20	Q3-20	Y to Y % Ch. (Q2-21/Q2-20)	Y to Y % Ch. (Q2-20/Q2-19)
Nonfarm Productivity	**2.3**	4.3	-3.4	4.6	1.9	2.6
- Output	**7.9**	8.4	6.2	44.6	15.8	-11.5
- Hours	**5.5**	4.0	9.9	38.2	13.6	-13.7
- Compensation (Real)	**-4.8**	-2.2	6.8	-10.0	-2.7	8.3
- Unit Labor Costs	**1.0**	-2.8	13.3	-9.9	0.1	6.0
Manufacturing Productivity	**6.9**	-1.3	3.1	19.4	6.8	-3.0
- Output	**3.8**	2.4	11.0	56.2	16.5	-15.3
- Hours	**-2.9**	3.8	7.6	30.8	9.1	-12.7
- Compensation (Real)	**-3.3**	-3.1	7.9	-16.0	-4.0	9.2
- Unit Labor Costs	**-1.9**	1.9	7.2	-26.3	-5.8	13.1

Source: US Department of Labor