The Daily Dish

Labor Productivity

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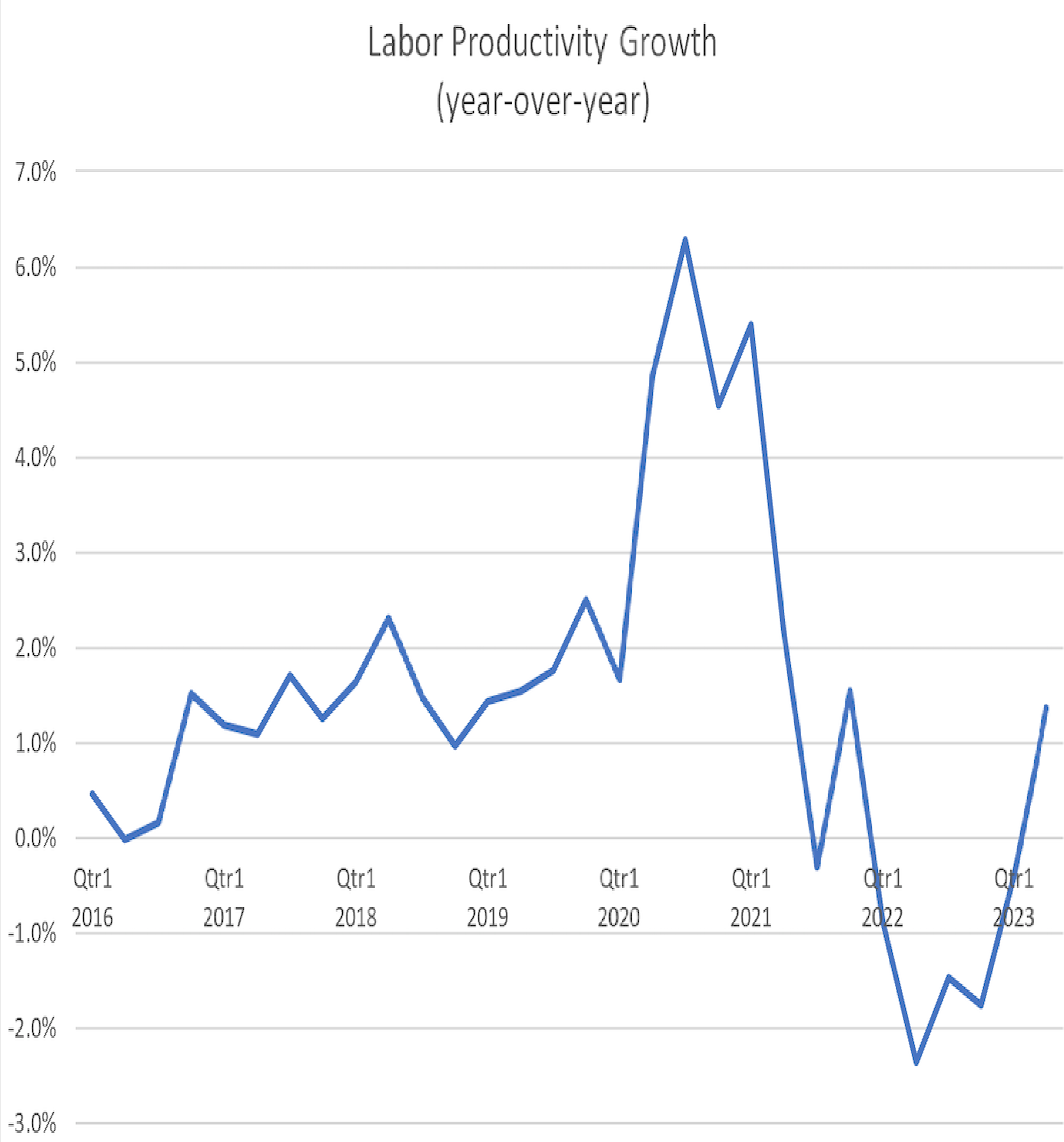
It's always a good idea to check in on labor productivity. Trust me. Over the long term, productivity growth is the route to higher real wages and an increase in the standard of living. In the near term, productivity growth allows labor compensation costs to be spread over a larger number of units of production, reducing the need for price increases to maintain margins. Productivity growth is a really good thing.

Unfortunately, the recent experience with productivity growth has been disappointing. Yesterday, however, brought some good news as the Bureau of Labor Statistics announced that labor productivity grew at an annual rate of 3.5 percent in the 2nd quarter, bringing the year-over-year growth rate into positive territory for the first time since the 4th quarter of 2021. (See chart, below.) The trick now is sustaining high productivity growth.


Labor Productivity Growth
(year-over-year)
7.0%
6.0%
5.0%
4.0%
3.0%
2.0%
1.0%
0.0%
-1.0%
-2.0%
-3.0%
Qtr1 2016
Qtr1 2017
Qtr1 2018
Qtr1 2019
Qtr1 2020
Qtr1 2021
Qtr1 2022
Qtr1 2023

As noted above, this is good news on the inflation front. In part because of the rapid productivity growth, unit labor costs rose at only a 1.9 percent annual rate in the 2nd quarter. That's the third supply-side break that the United States has caught. The first is de facto importing disinflation from China – import prices haven't risen in nearly a year. The second has been the decline in energy costs. Combined, all three have permitted inflation to decline without the Fed having done much to get demand down to the capacity of the economy.

In short, good news on the productivity front. Now the question is how durable that news will be.