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Productivity gains appear to bolster our resilience

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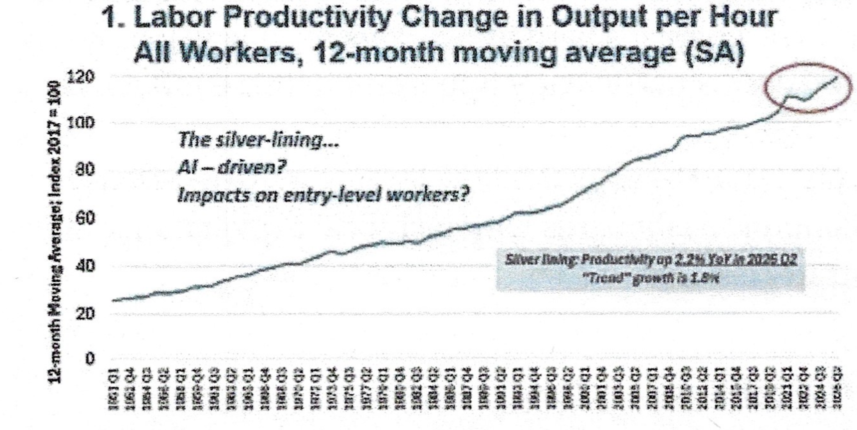
Between tariffs, exorbitant gas prices due to the Iran conflict and other significant price pressures, many people are wondering how the economy remains resilient.



Source: U.S. Bureau of Labor Statistics, non-farm workers only

Also puzzling is how the broader economy is holding up with such weak hiring and employment growth. Let's take a look.

Note

According to new research from the Federal Reserve of Boston, increases in worker productivity helps explain the resilience of the U.S. economy. Productivity measures how much workers produce for every hour worked. The researchers found that industries facing higher tariff costs also experienced stronger productivity gains, helping businesses absorb some of those costs rather than passing it all on to consumers.

And the latest productivity numbers are encouraging, with business productivity up 2.2% from a year ago. More importantly for inflation, unit labor costs, or what businesses pay workers relative to what those workers produce, rose only 1.4% over the past year. Hence, on average worker costs are not increasing as quickly as productivity is increasing.

Note

However, if businesses can produce more without adding many workers, economic growth doesn't necessarily translate into job growth. Since late 2019, productivity has grown at a 2.1% annual rate, while hours worked have increased only 0.4%.

Part of this puzzle is that hiring also is incredibly weak. The U.S. had negative job growth in July with 23,000 jobs lost, and over the past three months, the average monthly increase in jobs has only been about 20,000, which is quite low by historical standards.

By way of reference, the monthly average job increases from 2012 to 2019 were 197,000 per month. Yet, the unemployment rate stands at 4.1% (seasonally adjusted), because there simply aren't as many workers due to our aging demographic and fewer working-age people participating in the labor force. This is true even for prime-working-age men.

Note

I always get gasps at presentations when I state that in 1950, 1 in 50 working-age men was not working, and today that ratio stands at 1 in 9. I always joke this is not from menareslackers.com. This is data from the U.S. Bureau of Labor Statistics.

We also have fewer immigrant workers with roughly 50,000 deportations per month.

Is this the new normal? It's too early to know. But economists increasingly believe artificial-intelligence investment and higher productivity could allow the economy to grow faster without generating as much inflation.

Note

The tradeoff is that economic growth may become more capital-intensive while also becoming less labor-intensive.

This is a double-edged sword. We may (desperately) need more productivity due to fewer workers, but this also can translate into a non-dynamic labor force where it's hard for workers to change jobs, grow their skills and careers, or realize wage gains. The latter is particularly important in these inflationary times.

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