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Productivity: Doves See Support

Second-quarter productivity was on the firm side, rising an annualized 1.6% from the first quarter (Consensus: +1.4%; Decision Economics: +1.2%), but hourly compensation was also relatively strong, at +3.3% (Consensus: +1.8%; Decision Economics: +2.5%), so that unit labor costs still overshot, rising 1.7% (Consensus: +0.4%; Decision Economics: +1.3%).

Quarterly moves in these data are volatile, and mainly meaningless--so the better indication on trends is given by year-on-year changes. On that basis, productivity was up 1.1% in the second quarter, while compensation was up 1.9%, and unit labor costs were up 0.8%.

The latter figure is quite tame in relation to the GDP core price index (+1.7% year-on-year) and the core PCE price index (+1.8%), so that labor costs--at least crudely--are not limiting disinflation to any degree at the moment.

The 1.1% year-on-year productivity increase compares with an identical year-on-year result in the second quarter of 2011, and with +3.0% year-on-year in the second quarter of 2010.

Thinking on the sustainable trend rate of productivity growth--and on potential GDP and the GDP gap--will probably not be affected by these results, with the slowish productivity rates over the latest two years seen as being held down by slow goods-and-services demand growth, cautious investment, and lack of compelling compensation pressure. The high early-2010 figure, meanwhile, reflected the large employment declines over that four-quarter period.

Meanwhile, hourly compensation growth--reflecting immediate labor-market supply and demand conditions--has moderated, with the 1.9% year-on-year result in the second quarter comparing with +2.7% in the second quarter of 2011, and +1.7% in the second quarter of 2010.

Generally speaking, all these results support the argument of Fed doves that labor-market slack is constraining any upward cost-side pressure on prices. Hawks will respond that the issue is not current inflation, but inflation several years down the road, when the gross monetary stimulus now in place may be prompting very strong demand growth, outrunning then-available supply.

However, that argument will probably be ignored if nearer-term demand growth does not give signs of accelerating soon--and certainly so, if demand growth weakens outright.

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