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PAY AND PRODUCTIVITY IN 2008: GOOD NEWS, BAD NEWS

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The good news is that productivity across the U.S. business sector, defined as output per labor hour and measured every quarter by the Bureau of Labor Statistics, increased by 2.7 percent in 2008 eclipsing the 1.6 percent rise in 2007 and the 0.9 percent gain in 2006. The improvement in 2008 compares favorably to the 2.2 percent average annual improvement since 1947. These data were released to the public recently by the BLS and include revised rates of productivity change for Q4 2008.

Output per labor hour measures how efficiently the business sector is utilizing resources to produce the entire spectrum of goods and services made in the United States. It is one indicator that in spite of other very troubling economic and financial news the U.S. economy has not completely lost its bearings.

The efficiency gains from productivity improvement help U.S. producers become more competitive against foreign producers because they allow U.S. companies to cut prices and prompt them to hire more workers in order to increase production for their growing export markets. Similarly, productivity improvement at a U.S. firm makes it more competitive against its domestic rivals by allowing it to cut prices and at the same time increase both wages and profits.

Virtually every economist, whether Keynesian, supply-sider, monetarist, or free-market, agrees that productivity improvement makes for a win-win-win outcome because by sharing the gains from that improvement prices for consumers are lower, wages for workers higher, and profits for owners greater. For those inclined to make partisan comparisons, the annual improvement in Clinton's eight years as president averaged 2.0 percent. For Bush II it was 3.2 percent.

In Q4 2008 there was a truly remarkable 15.6 percent increase in real hourly compensation due no doubt to a precipitous slide in fuel prices. However, this quarterly gain was washed away by the losses sustained earlier in the year such that real hourly compensation for the year declined by 0.2 percent. This bad news was compounded by a 1.9 percent decrease in hours worked over the entire year.

Over a longer time frame, the news is a mix of good and bad. Since 1992 output for the U.S. economy has advanced by 69 percent and output per labor hour has climbed by 42 percent. This improvement in productivity reflects advances across the whole range of inputs used

in the production process including work force effort, technological change, capital investment, organization of production, managerial skill, and utilization of capacity, energy, and materials.

Between 1992 and 2008 nominal compensation per hour jumped by 83 percent but due to a 34 percent overall rise in prices real compensation per hour increased by only 22 percent. If, for example, the typical worker was earning $15.00 per hour in 1992 that worker in real terms was taking home $18.26 sixteen years later. Assuming that worker had a year-round, full-time job in 2008 his/her annual compensation amounted to $37,970.

The Clinton vs. Bush II comparison regarding real compensation per hour demonstrates how easy it is to skew that comparison by extracting the data selectively. The average annual increase in real compensation per hour was higher in the Clinton years (1.50 percent) than in the Bush years (1.21 percent). However, real hourly compensation fell in the first three years under Clinton, whereas it fell only in the last year under Bush. Taking into account these two important data series – real hourly compensation and hourly output – raises this question: Was it Republican Bush's policies that failed or Democrat Clinton's?

The U.S. economy is an enormously complex system, more so today because of economic globalization than at any time in the past. At any given moment, literally millions of persons and organizations are making decisions in the marketplace and the workplace with regard to buying and selling, lending and borrowing, producing and consuming, saving and investing, innovating and retrenching, starting and closing a business in ways that cannot be predicted with confidence and therefore cannot be brought under control. Those decisions often are driven by the speed of electronic communication and without the necessary due diligence.

Decentralization of decision-making in the U.S. economy allows wider participation in the economic decision-making process and whenever those decisions are not well-taken limits the damage. A bigger role for government in the economy based on the shaky premise that government knows best narrows individual participation in economic affairs – at the very same time wider participation in political affairs is strongly promoted – and exposes everyone to even greater risk when those decisions are pushed through the legislative branch by an executive branch in a rush to reshape the economy to fit its own vision.

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