Productivity Up 6.6 Percent As Companies Cut Costs

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WASHINGTON (AP) — Worker productivity grew at the fastest pace in nearly six years in the spring while labor costs fell by the most in nine years, as companies slashed costs to survive the recession.

The Labor Department says productivity, the amount of output per hour of work, rose at an annual rate of 6.6 percent in the April-June quarter, the largest advance since the summer of 2003. Economists expected an increase of 6.4 percent, matching the government's initial estimate last month.

Labor costs fell at an annual rate of 5.9 percent. That's the largest drop since the second quarter of 2000, and slightly bigger than the 5.8 percent decline estimated a month ago.

New signs of economic recovery keep emerging, but with the American consumer still hamstrung by flat wages and job losses, it's unclear those signs will last.

Reports Tuesday showed the U.S. manufacturing sector grew in August for the first time in 19 months. A gauge of future home sales surged in July to its highest point in more than two years. And auto sales — boosted by the Cash for Clunkers program — appeared in August to have marked their first year-over-year monthly gain since October 2007.

On Wednesday, government data is expected to show that orders to U.S. factories likely posted another increase in July, providing further evidence that the U.S. economy is on the mend. Factory orders likely rose 2.2 percent in July after a 0.4 percent gain in June, according to economists surveyed by Thomson Reuters.

The government also will revise its estimates on durable goods in Wednesday's report and include a look at orders for nondurable goods, items such as energy products, food and chemicals.

And the Labor Department is slated to release its revised estimate for productivity and a revised figure for unit labor costs.

Productivity, the amount of output per hour of work, is expected to have surged to an annual rate of 6.4 percent in the April-June quarter, according to economists surveyed by Thomson Reuters. That would be the biggest quarterly increase in almost six years and represent no change from the government's initial estimate. Labor costs also are expected to have fallen at an annual rate of 5.8 percent.

Productivity is the single biggest factor determining living standards. Increases can help boost living standards because it means companies can pay their workers more with those wage increases financed by rising output. But struggling companies have been shoring up their bottom lines, not hiring more workers or paying them higher wages. At that means hopes for a sustained recovery remain clouded by a big concern: consumer spending, which fuels about 70 percent of U.S. economic activity.

Americans fearful of job losses or who are still searching for work aren't borrowing and spending enough to nourish a lasting rebound. That raises the vexing question of who will buy all the goods that manufacturers are producing?

Skepticism about a recovery contributed to a nasty tumble on Wall Street Tuesday, following a monthslong rally. All the major averages fell about 2 percent, with the Dow Jones industrials sliding 185 points, as concerns grew about the fragility of the banking industry and the global economy.

Stock market analysts noted that the manufacturing and housing gains were boosted by temporary government stimulus steps, including the Cash for Clunkers program, which has since expired. The clunkers program helped lift sales at Ford, Toyota and Honda in August, though Chrysler Group LLC and General Motors Co. withstood another month of falling sales.

"People reviewed the numbers and said this type of demand is just not sustainable," said Tom di Galoma, head of U.S. rates trading at Guggenheim Capital Markets LLC.

At the same time, the National Association of Realtors said its seasonally adjusted index of sales contracts signed in July for previously occupied homes rose 3.2 percent to 97.6. It was the sixth straight increase and 12 percent above the same month last year.

U.S. construction spending dipped in July as weakness in nonresidential building and government projects offset the best showing for home building in 10 months.

At the moment, manufacturers may be the economy's strongest pocket of strength. Yet even that might prove short-lived if demand doesn't pick up, analysts said.

The better-than-expected report from the Institute for Supply Management showed the highest number for its manufacturing index since June 2007. New customer orders jumped to a level not seen since late 2004.

"Manufacturing will continue to expand," said Daniel Meckstroth, chief economist for the Manufacturers Alliance, a trade group. But he said capital investment likely will slip because plants have too much excess capacity.

"You're going to see ups and downs," Meckstroth said.

Most manufacturers are simply restocking depleted stockpiles of goods — a process that will run its course within six months, said Joshua Shapiro, chief U.S. economist at MFR Research.

Beyond that, it's hard to say how much the U.S. manufacturing sector can expand as long as credit for consumers and businesses remains tight. If loans remain out of reach for many, shoppers and companies can't spend and grow.

Apart from the boost from the clunkers program, "we feel that the headwinds for consumer spending remain too brisk to expect much help on this front," Shapiro said.

The ISM, a trade group of purchasing executives, said its manufacturing index rose to 52.9 in August, from 48.9 in July. That was its first reading above 50, which indicates expansion, since January 2008. The index has been trending lower since a peak reading this decade of 61.4, in May 2004.

The index, based on a survey of the group's members, includes such factors as new orders, production, employment, inventories and prices. New orders jumped nearly 10 percentage points to 64.9 in August — their highest point since December 2004.

President Barack Obama said the manufacturing gains mean companies are starting to invest and produce more. "It is a sign that we're on the path to economic recovery," he said.

"The underpinnings for manufacturing in this country are solid," agreed Neil Dutta, U.S. economist at Bank of America Merrill Lynch — but noted that's mostly due to the Asian consumer, not the U.S. shopper. A weaker dollar helped exports grow for the second straight month, after shrinking for nine.