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ECONOMY

U.S. productivity stagnates

Data showing wage growth is outpacing productivity in the United States sparked more inflation fears on Wall Street.

By Martin Crutsinger

Associated Press

Growth in productivity -- the key ingredient for rising living standards -- skidded to a standstill in the late summer while workers' wages and benefits shot up at the fastest clip in more than two decades.

The mix of slowing productivity and rising wages was seen as a formula for inflation down the road. It means the Federal Reserve may not cut interest rates anytime soon and may even hike them.

Productivity, or output per hour of work, showed no growth at all from July through September. Growth was just 1.3 percent over the past 12 months, the weakest showing in nine years.

But the cost of wages and benefits per unit of output grew at an annual rate of 3.8 percent in the third quarter.

Employee compensation climbed by 5.3 percent over the past year, faster than it has done since 1990.

Higher wages and benefits are good news for workers, but they also cost companies more. If productivity rises, companies can pay their workers more from the increased production. But otherwise, companies may pass on the costs to consumers by making products more expensive -- leading to inflation.

Companies could pay the higher salaries from their profit margins, which have jumped in recent years, but that would mean less in returns for shareholders.

IMPACT ON STOCKS

The weak economic news pushed stocks lower for a fifth consecutive day, the longest stretch of declines since June 2005. The Dow Jones industrial average dropped 12.48 points to close at 12,018.54.

Wall Street had hoped the slowing economy would translate into Fed rate cuts, something put into doubt by the slowdown in productivity and rising wage pressures.

Investors were also concerned about a mixed sales performance in October at major retailers. Many shoppers apparently took a breather last month after a shopping spree in September.

Wal-Mart Stores reported a meager 0.5 percent rise in same-store sales in October. The company said it would trim prices to gain market-share in such areas as toys and electronics. Consumers would benefit during the holiday shopping season but the move could mean lower profit margins as other stores struggle to compete.

In other economic news, orders to U.S. factories for manufactured goods rose by 2.1 percent in September. While that was the biggest increase in six months, it was heavily influenced by a huge surge in demand for commercial aircraft. Outside of transportation products, factory orders actually fell by 2.4 percent.

The Fed raised interest rates 17 consecutive times through June of this year in an effort to slow the economy enough to bring inflation pressures under control. The Fed has left rates unchanged for three straight meetings, hoping it has done enough to brake economic growth.

But the significant slowing in productivity growth and the continued rise in wage pressures could prompt the Fed to resume raising interest rates to fight inflation, analysts said. At the very least, it will mean a prolonged period before the Fed feels safe in cutting rates.

GRIM MESSAGE

"The Fed will not be easing anytime soon unless the economy absolutely falls apart," said Stephen Stanley, chief economist at RBS Greenwich Capital.

Since 1995, the United States has enjoyed a decade of strong gains in productivity. But as the economy has slowed this year, productivity has slowed too, even as the cost of labor has risen.

The 1.3 percent rise in productivity over the past four quarters ending in September represented a slowdown compared with rates averaging more than 3 percent annually from 2002 through 2005.

"Productivity is not growing fast enough to keep labor costs from pressuring firms," said Joel Naroff, chief economist at Naroff Economic Advisors.