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Productivity gains may be bad news for job seekers

By MARTIN CRUTSINGER and STEPHEN MANNING, AP Business Writers Martin Crutsinger And Stephen Manning, Ap Business Writers Thu Nov 5 (2009), 5:41 pm ET

WASHINGTON – Companies across the economy are finding ways to do more with fewer workers, dimming hopes that hiring will take off anytime soon.

Employers became leaner and more efficient in the third quarter. Wages, meantime, remain flat or falling. The result is that productivity — output per hour of work — jumped at the fastest pace in six years.

The good news for companies, though, may be bad news for the jobless. As long as companies can get their workers to produce more, they have little reason to hire — at least until consumer spending picks up. And the squeeze on incomes could depress consumer spending, putting the economic recovery at risk.

Still, some economists were encouraged by the productivity report. They say that eventually, employers won't be able to squeeze more from their staffs. They will then have to ramp up hiring — something that could happen next year, even though the jobless rate is expected to hit double digits.

Productivity rose at an annual rate of 9.5 percent in the July-September quarter, the Labor Department said Thursday. That was much better than the 6.4 percent gain economists had expected. Unit labor costs fell at a 5.2 percent rate.

While companies aren't doing much hiring, they're not cutting as many workers, either. The number of newly laid-off workers filing claims for unemployment benefits last week fell to the lowest level in 10 months.

On Wall Street, the better-than-expected jobless claims report and an upbeat forecast from Cisco Systems Inc. buoyed investors. The Dow Jones industrial average added nearly 204 points to 10,005.96, and broader indexes also gained.

The 9.5 percent productivity rise followed a 6.9 percent surge in the second quarter and was the fastest since a 9.7 percent increase in the third quarter of 2003.

The gain reflected that the overall economy, as measured by the gross domestic product, grew for the first time in a year — at an annual rate of 3.5 percent. The higher output came as companies continued to lay off workers. That meant employers produced more with fewer workers.

The 5.2 percent drop in unit labor costs marked the third straight decline and was larger than the 4 percent decrease economists were expecting.

Productivity is the key ingredient to rising living standards. It lets companies pay their workers higher wages. Those increases tend to be financed by increased output, rather than higher costs for products.

But as they struggled with the recession, companies boosted productivity while continuing to lay off workers. Many produced more goods; others kept their output down but slashed costs. Companies kept wages down by freezing pay or imposing unpaid furloughs.

"Survival meant cutting costs as rapidly as possible and fulfilling orders with the fewest number of workers," said Joel Naroff, chief economist at Naroff Economic Advisors.

Some companies in hard-hit sectors have managed to boost productivity despite job cuts. They've had to find ways to stretch their remaining workers to keep up with demand.

Fein Tool North America, a Cincinnati company that supplies auto parts manufacturers, has cut about 100 workers, or 33 percent of its staff. But Fein president Ralph Hardt said the company can still fill its orders by using more overtime shifts and temporary workers.

"We are asking more of our people than ever before," he said.

Fein also has made technical changes, including increasing their presses' strokes per minute so they can stamp more metal.

Hardt said he plans to rehire once the economy picks up again. But he's hesitant to do so quickly.

"If I see signs of recovery, I am going to hire back, but I am going to be very prudent," he said.

Elsewhere, Union Pacific has found ways to reduce the number of crews it needs and is using more fuel-efficient locomotives. The rail company also rewarded train engineers who saved fuel on their routes with free gas cards for their personal vehicles, all while furloughing nearly 10 percent of its 45,000 workers.

Naroff said hiring could remain sluggish for months. But other analysts are more optimistic. They were encouraged by the productivity report, noting that companies are starting to reach the limits of how much they can produce with their shrunken work forces.

"We believe businesses will have to start to increase hours worked and payrolls around the turn of the year since they cannot expect their current work force to sustain such rapid productivity growth," said Michelle Meyer, an economist at Barclays Capital.

The problem is that consumer demand could falter once the government removes the stimulus programs it has put in place, such as record-low interest rates and homebuyer tax credits. Companies could stop hiring if they think demand will slump again.

Temporary surges in labor productivity tend to follow the end of a downturn, said Cliff Waldman, an economist with trade group Manufacturers Alliance.

"You're having a turn in output from negative to positive with a significantly depleted labor force," he said. "It gives the illusion that productivity has increased. It's really just arithmetic more than reality."

In a separate report, the Labor Department said first-time claims for jobless benefits last week fell by 20,000 to a seasonally adjusted 512,000. That's better than economists' estimates of 523,000.

Economists closely watch initial claims, which are considered a gauge of the pace of layoffs and an indication of employers' willingness to hire new workers.

The four-week average of jobless claims, which smooths fluctuations, dropped to 523,750, its ninth straight decline. That's 135,000 below the peak for the recession, reached in early April.

Despite the improvement, initial claims remain well above the roughly 400,000 that economists say will signal job creation.

Another 4.1 million people claimed extended unemployment benefits in the week ended Oct. 17, the latest data available, an increase of about 100,000 from the previous week. Congress has added 53 weeks of emergency aid on top of the 26 weeks typically provided by states.

Still, as roughly 7,000 Americans run out of extended benefits every day, Congress has approved legislation that would add another 14 to 20 weeks. President Barack Obama is expected to sign the bill.

The National Employment Law Project, an advocacy group, estimates that up to 1.3 million people would exhaust their benefits without the extension.

Economists expect the nation lost a net total of 175,000 jobs last month, adding to the 7.2 million lost since the recession began in December 2007. And many expect the jobless rate could rise as high as 10.5 percent before the recovery gains enough steam to start pushing it down next summer.

AP Business Writers Christopher S. Rugaber in Washington and Tali Arbel in New York contributed to this report.