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Recent Trends in G7 Productivity

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While many economic measures speak to short-run well-being—employment, wages, inflation, etc.—productivity growth is one of the most important measures for a society's long-run well-being. As workers and businesses become more productive, they can produce more goods and services with the same or fewer inputs, leading to increased output and income per capita. This growth in productivity translates directly into higher average incomes and improved material well-being for society as a whole. High productivity levels—generally a signal of technological progress or high *total factor productivity*—also make a country more competitive in the global marketplace. Productive economies can produce goods and services more efficiently, allowing them to offer competitive prices and maintain a strong position in international trade.

Productivity in the G7 has broadly been slowing over the past 50 years. However, there has been notable variation between countries, especially post-pandemic. This analysis will examine the productivity landscape in the G7 economies, focusing on key factors influencing productivity growth, recent developments, and potential future trajectories.

Current Labor Productivity Levels and Growth

Figures 1 and 2 show, respectively, harmonized labor productivity levels and growth for the G7. Productivity is defined as total real GDP per hour worked. Levels begin from 2019 Purchasing Power Parities (PPPs) and grow based on national accounts definition of real GDP.[1]

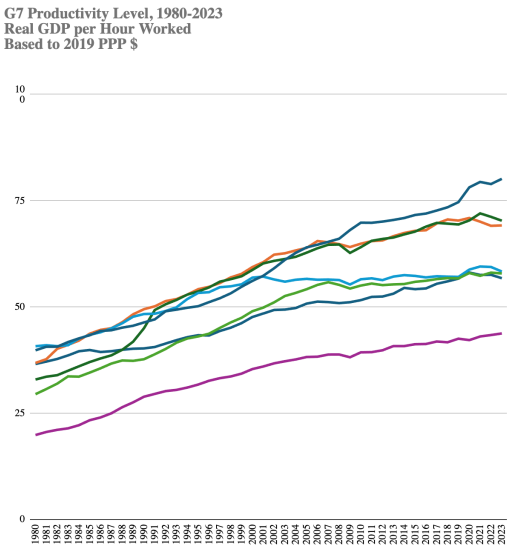

Figure 1

[1] PPPs in Figure 1 are used solely to adjust the base levels, not to adjust subsequent levels or growth rates. As Fernald, Inklaar, & Ruzic (2024) explain, PPPs can be significantly inconsistent with output deflators in each country's national accounts, so using PPPs to measure productivity over time can skew and bias the final measure. Even in this limited use, the choice of base year can affect the ordering of countries.

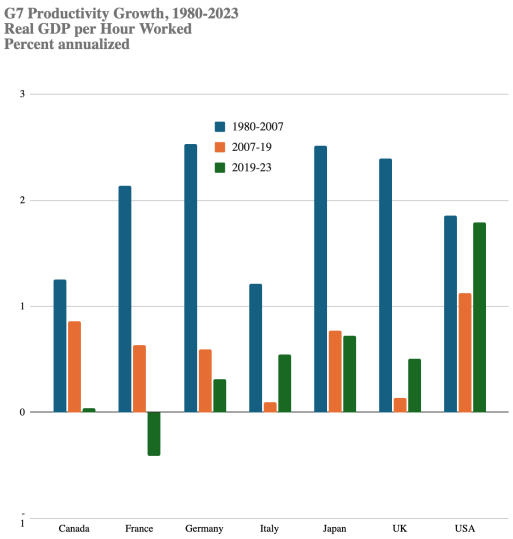

Figure 2

There are a couple of high-level conclusions to be drawn from Figures 1 and 2.

First, broadly speaking, labor productivity growth had been slowing down in the G7. In all of the countries, labor productivity growth was slower over the 2007-19 cycle than it was over the 1980-2007 period. In four countries, it was slower still during the pandemic; in two of the others, pandemic productivity growth exceeded the Great Recession but still fell short of 1980-2007.

The second takeaway is that the US is an outlier in both levels of productivity and growth. As recently as the mid-2000s, the level of US labor productivity in 2019 PPP terms was in line with Germany and France. During the Great Recession, the US began pulling away from the rest of the G7. This continued during the pandemic. US labor productivity growth was first in the G7 over the 2007-19 cycle (modestly ahead of 2nd place Canada) and first again over 2019-23 (by a much wider margin).

Common Themes & Challenges

Despite the variation between countries, several structural factors are common to G7 countries and drive recent labor productivity trends:

1. **Aging populations.** All G7 countries are experiencing demographic shifts as their societies age. Japan has been at the forefront of this phenomenon, while immigration has somewhat counteracted its effects elsewhere, especially in Canada and the US. An older population is one that compositionally pulls its economy toward potentially less productive services. An older population may also face more challenges when adapting to new technologies.

2. **Technological innovation**. The adoption of new technologies, particularly AI and automation, may be playing a role in productivity growth in some sectors and countries, notably the US where heavy investments in AI have been made. However, there is no definitive evidence that AI is affecting aggregate labor productivity figures yet, even in the US: as strong as US productivity has been, for example, it is still largely in line with pre-pandemic level projections absent AI. Structural increases in educational attainment around the world have helped as well.

3. **Pandemic dynamics.** Recent productivity data has clearly been affected by idiosyncratic pandemic factors, though one would expect those to have largely dissipated by 2023. Labor productivity saw an artificial compositional surge in the US in 2020 and 2021, for example. This is likely a direct result of the US's choice to deliver pandemic worker relief primarily in the form of augmented unemployment insurance payments—which allow for layoffs—rather than furloughs, which keep workers on the payroll. However, these effects may be more than mechanical. The labor market churn induced by augmented unemployment insurance may have led to lagged productivity dividends in the US. There may also be "creative destruction" effects at play.

4. **Regulatory barriers.** Regulatory barriers continue to pose challenges to productivity growth, particularly in Europe. Strict product market regulations and lack of regulatory reforms have been identified as key factors underlying the relatively poorer productivity performance of some European countries compared to the US. The cross-country variation in regulatory settings has increased in recent years, despite extensive liberalization efforts. Burdensome regulations have been exacerbated by geopolitical tensions and trade fragmentation. Furthermore, the lack of regulatory effectiveness and coherence at the EU level is often cited as a root cause of the still incomplete EU Single Market, which hinders the free flow of people, goods, services, and finance within the EU. These regulatory barriers not only impede business dynamism and innovation but also limit the adoption of new technologies and the reallocation of resources to more productive firms and sectors.

Conclusions

Labor productivity growth is broadly slowing across the advanced world, but there are signs it might be picking up—or at least slowing less—in the United States post-pandemic. The reasons for this are not entirely clear yet: both transitory pandemic factors and more structural explanations are possible. In the meantime, the G7 is experiencing common productivity dynamics too, especially aging populations and the uncertainty around new technological innovations.