# POSITIVE OUTCOMES FROM THE PANDEMIC

Inflationary pressures – and the potential headwinds to corporate profit margins – remain a focus for market participants given the persistent perfect storm of strong (pent-up) consumer demand, rising commodity prices, and supply chain bottlenecks. Though only roughly half of corporate America has published Q2 earnings reports so far this earnings season, indications are that gross margins have remained fairly steady over the last couple of quarters.

This suggests that firms have been able to pass through higher input costs to customers, and/or offset increased expenses on raw materials, wages, and freight with cost savings in other areas. Examples of savings include reduced travel and entertainment expenses. In addition, productivity has increased in certain areas (employees can meet several clients in a day virtually instead of setting aside one or two days for a business trip to meet a single client).

## Productivity: Three Components

Aggregate productivity growth has three components: intra-firm, intra-sector and inter-sector.

The **first** component deals with 'within-firm' productivity growth, which focuses on the way existing firms utilize the resources at their disposal – labor, physical capital, and intangibles like organizational knowledge and management practices. Through Covid, companies and workers have been forced to embrace a wide range of new technologies and policies — online meetings, file sharing, flexible work schedules — that have made their operations more efficient.

Additionally, digital efficiencies have enabled existing workers to pick up the extra workload resulting from job layoffs of other colleagues, so the same amount of work is getting done with fewer workers.

**World War 2**

Economists have likened this post-Covid shift to the period after World War II. The war led to the development of new technologies and spread existing ones to factories across the country. Those advancements helped make the postwar period one of the best on record for productivity growth, as well as broader economic growth.

The **second** component relates to 'between-firm' shifts that reflect the gains achieved by reallocations of economic activity that affect utilization of resources within a sector. This can create productivity growth through 'cleansing' processes, like the exit of unproductive firms and reallocation of resources (labor and capital) to higher-efficiency firms with higher marginal products of these inputs.

The **third** component relates to the productivity generation created by the pure shifts of activities across sectors. Examples of these shifts include technology companies disrupting inefficiencies in existing industries such as transportation (Uber, Lyft), financial services and healthcare.

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## Accelerated Solutions

Covid has forced an acceleration in these shifts. The trend toward simpler, better, and faster products and services will continue to unfold, a natural result of the capitalist underpinnings of our economy (despite the Federal Reserve still extending cheap credit lifelines to inefficient 'zombie' companies that should otherwise no longer exist), and Corporate America will be stronger for it.

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