

Is Manufacturing in the EU Disappearing and Does It Need Policy Intervention?

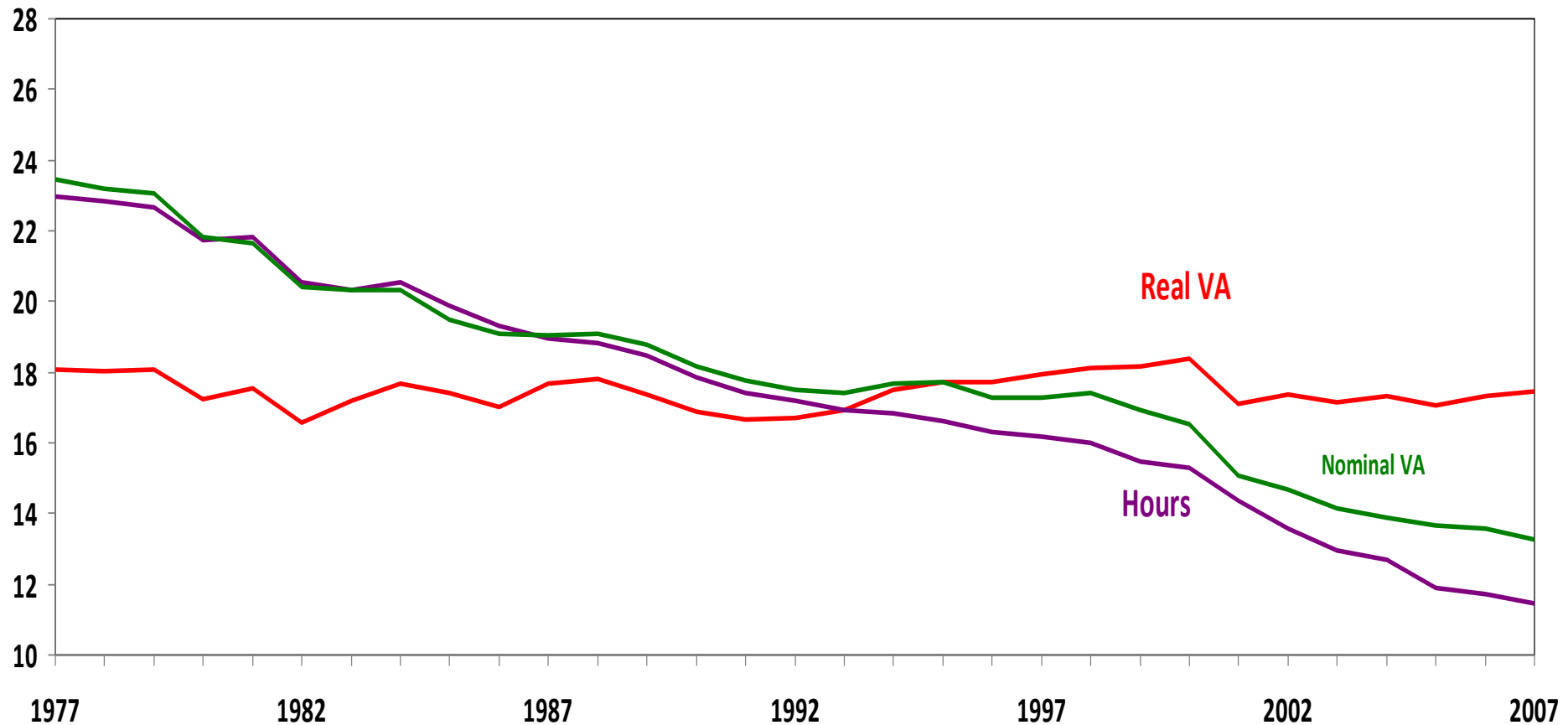
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Outline of Brief Initial Comments

- Is Manufacturing Declining?
 - Employment vs. Nominal vs. Real VA Shares
 - EU15 vs. US
- Manufacturing Productivity Growth in US and EU
- The Particular Problems of Southern Europe
 - Diagnosis of the problems
 - Policy Recommendations and Warnings about Murphy's Law

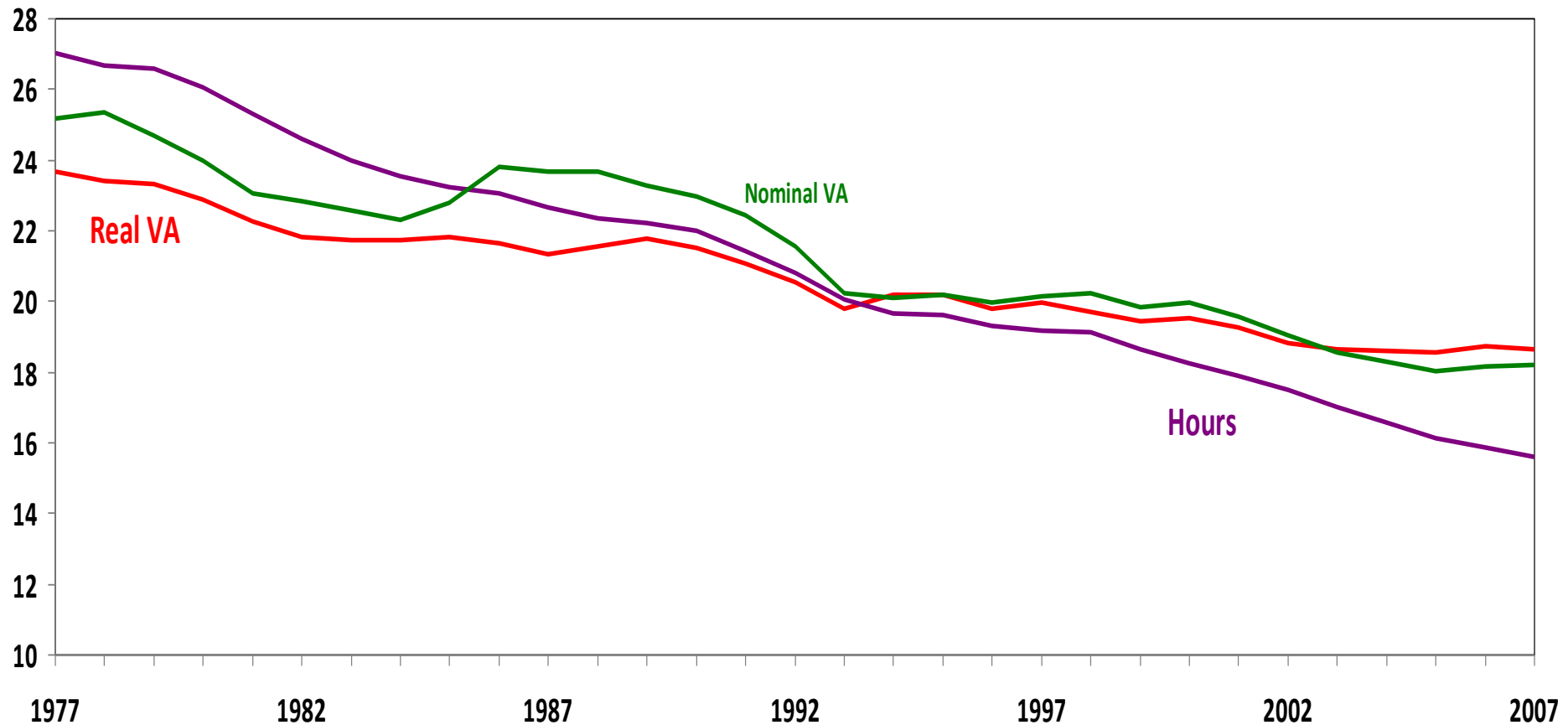
Manufacturing Shares of GDP for the US, 1977-2007

US- Hours v Nom and Real VA, Mfg as Share of Total GDP, 1977-2007



Manufacturing Shares of GDP for the EU-15, 1977-2007

EU- Hours v Nom and Real VA, Mfg as a Share of GDP, 1977-2007

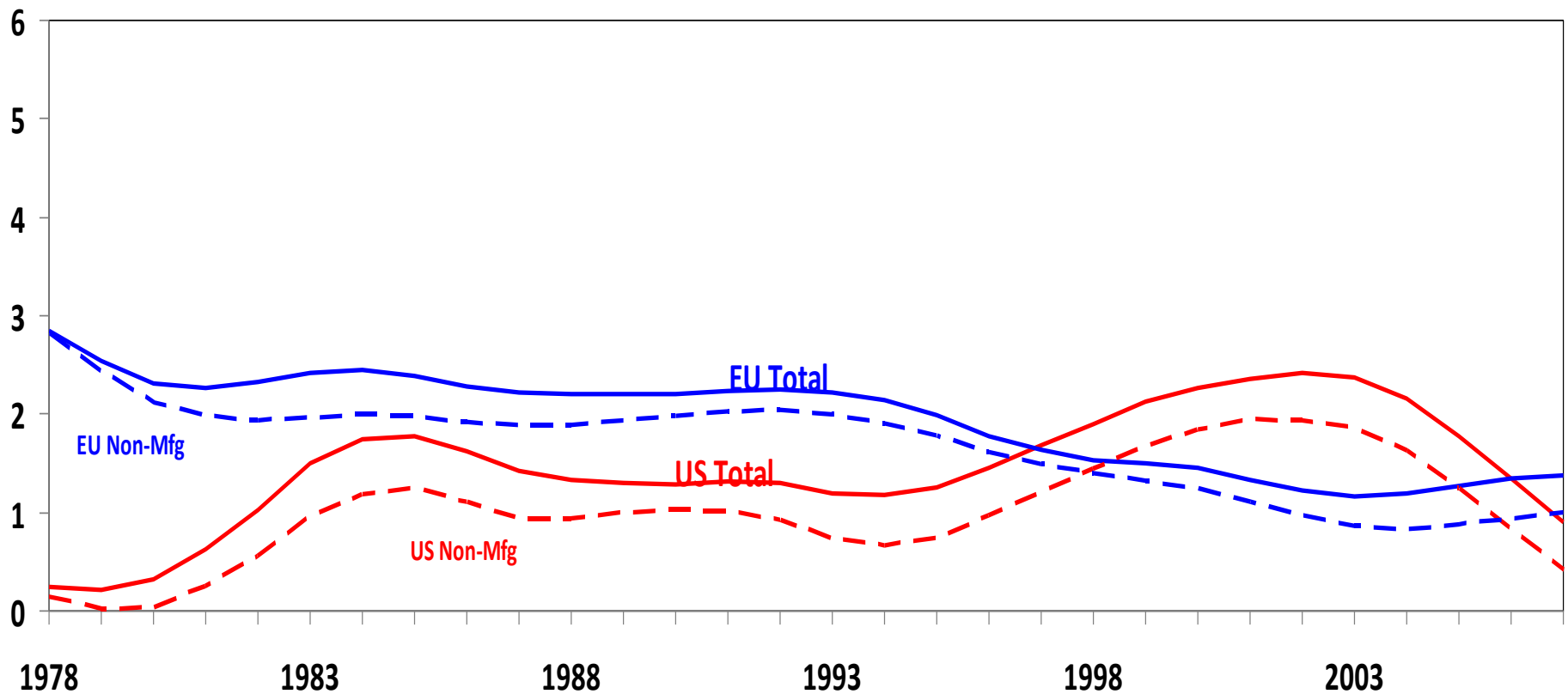


Summary of Ratios

- Employment Share
 - US 23 to 12. EU 27 to 16. EU higher but similar decline.
- Nominal VA Share
 - US 23.5 to 14. EU 25.2 to 19. EU higher but smaller decline
- Real VA Share
 - US 18.1 to 17.5. EU 23.7 to 18.7. US almost unchanged, EU converges downward
- Implications. EU implicit deflator hardly declines; US declines massively.
 - Annual rate 1977-07, US -1.8 vs. EU -0.3 *percent per year*
- Second Implication: *Relative* productivity growth in US manufacturing rises much faster than EU
 - Annual rate 1977-07, US 2.2 vs. EU 1.0 *percent per year*

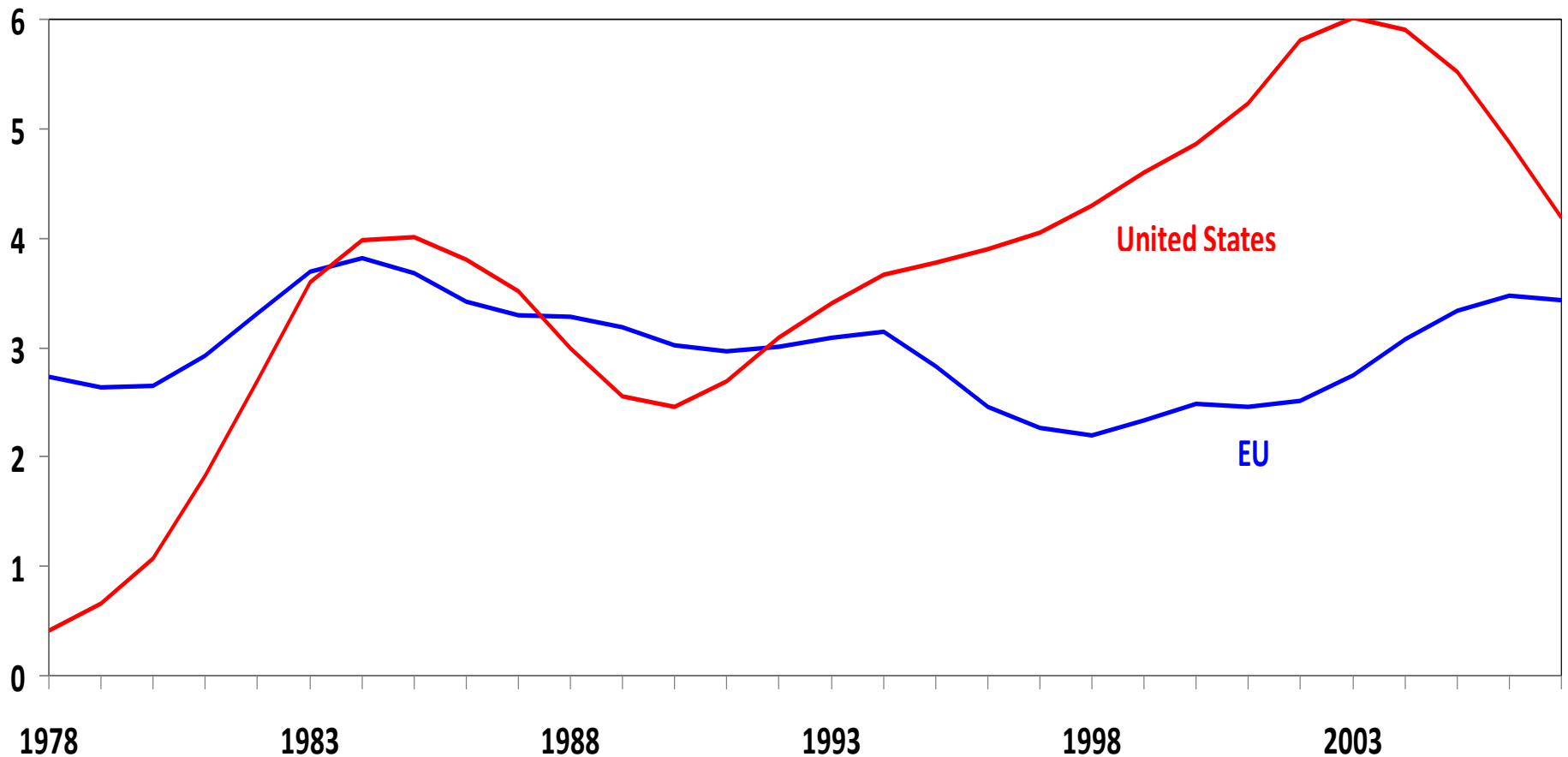
Smoothed Labor Productivity Growth, US vs. EU, Total and Non-Mfg, 1997-2007

Total Economy and Non-Mfg LP Growth Rate, US vs EU, 1978-2007



Smoothed Labor Productivity Growth, US vs. EU, Mfg, 1997-2007 *(note same scale)*

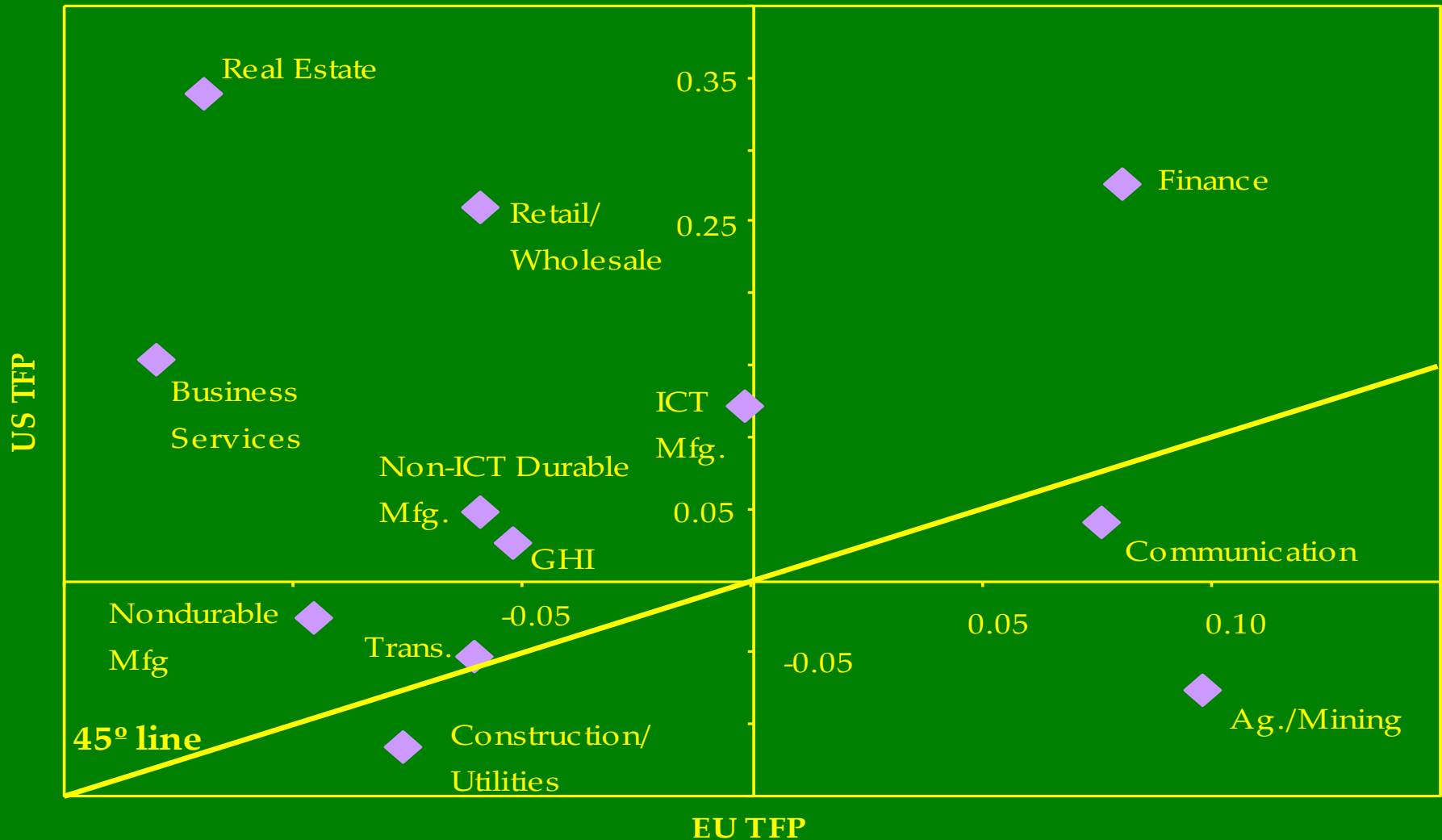
Manufacturing LP Growth Rate, US vs EU, 1978-2007



What Industries Contribute to Productivity Growth Success or Failure?

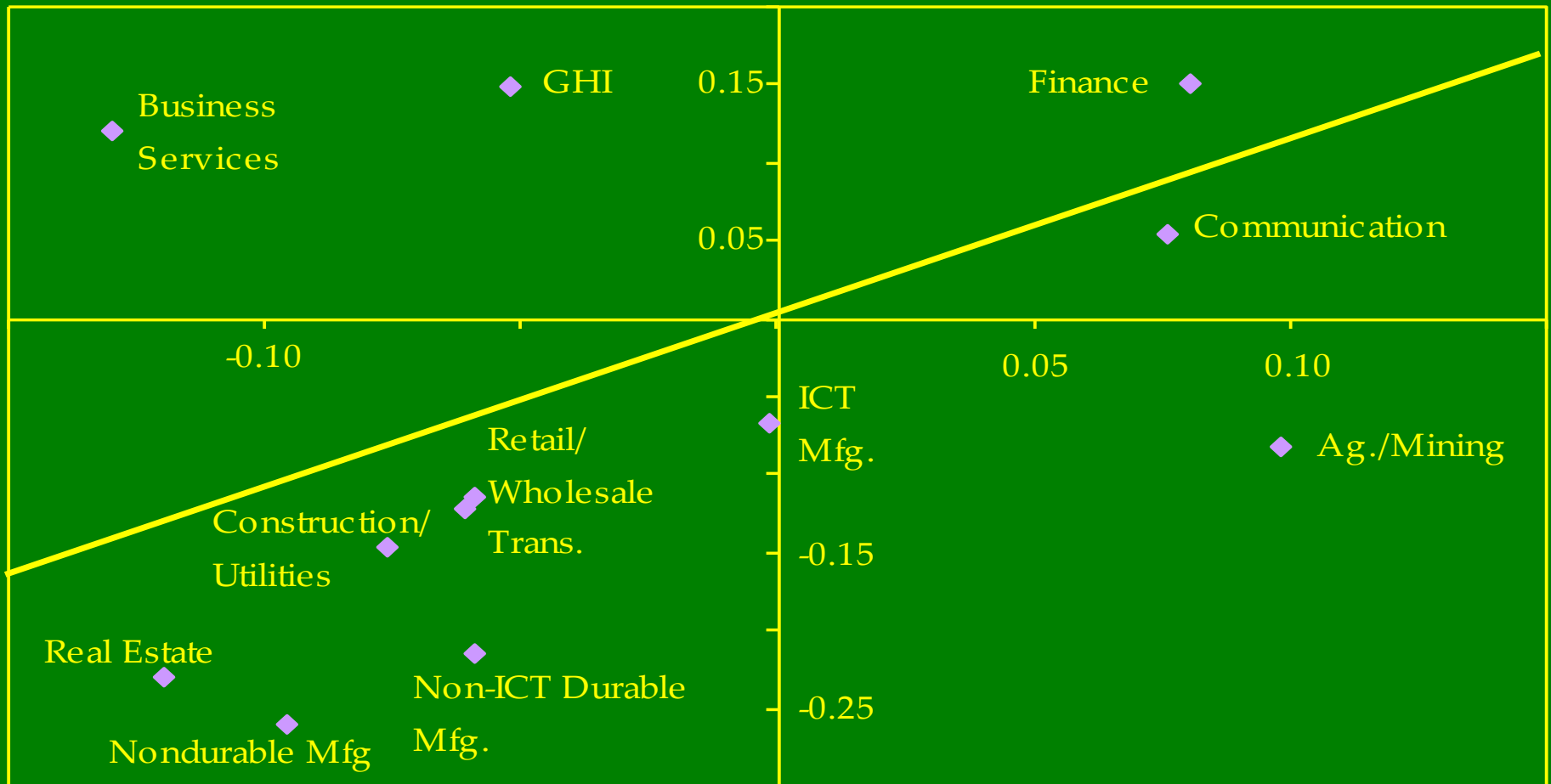
- Two next graphs compare
 - US vs. EU 15
 - EU15 vs. Mediterranean (GR, IT, SP)
- Horizontal axis is TFP growth in EU-15
- Vertical axis is TFP in US or Med
- Note zero vertical line, horizontal line
 - Lots of negative TFP growth observations

Comparing US with EU-15



Comparing Med with EU-15

Mediterranean



Diagnosing Problems: Italy Viewed from the 2010 LIGEP Report

- Nordic, UK, Ireland (until 2007) have not appreciably lagged the US
- Italy
 - The problem is that the firms are too small
 - Their main ambition is to keep control within the family, so there is no interest in individual or societal wealth building through IPOs.
 - Smallness fostered by “Worker’s Statute” in 1970. Must have union representation if >15 employees
 - Constraint on growth has shifted Italy from being a star growth performer in EU-15 before 1990 to a laggard after 1990

Initial Thoughts on Policy

- There is nothing special about manufacturing that would warrant policies to protect its GDP share
 - US manufacturing has not added anything to employment in last two decades but has not lost GDP share and its productivity soared.
- Reasons to question industrial policy to raise manufacturing share
 - Why resist comparative advantage?
 - Manufacturing is not the only home of innovation and technology

Innovation Outside of Manufacturing

- Arguably other sectors are as dynamic or more dynamic
 - Mobile telephones, retailing and supply chain
 - Retail, wholesale, finance, and business services are the key sectors in which US outperforms Europe
 - *Use of ICT innovations is as important as the manufacturing of ICT equipment.*
- The value-added of China in the iphone is only \$6.50 out of a retail price of \$499.
 - Less than the \$11 of components exported from US to China
 - Way less than the \$100+ that Apple adds as its mark-up for intellectual property developed in the U. S.

Final Comments on Industrial Policy

- Decades of Italian investment in the South has not paid off
- Similarly, UK has not been able to revive its northeast, Germany has poured trillions into East Germany which still lags, and US has not been able to revive Detroit or the Appalachian states
- Inequality of policy conception and administration can create rather than solve problems
 - Further example than just Italy imposing union legislation on employers > 15 employees.
 - US trade union laws have led all transplant foreign-owned auto plants to located in the south
 - Have hollowed out the city of Detroit
 - US devolution of power to the states leads to a wasteful competition of subsidies to lure new firms and keep old firms (Illinois' recent \$100 million to Motorola Mobility)

Controversial Thoughts

- The analogy of Detroit to Southern Italy raises many interesting questions:
- The history is different. Southern Italy is an age-old problem, Detroit has become a problem last two decades
- Policy indirectly created Detroit problem while Italian policy didn't fix South problem
 - Murphy's law (unintended consequences of well-intentioned policies)
 - Unions killed Detroit because they weren't enforced in South
 - Management killed Detroit by falling behind Japanese management & quality
 - Italian policies ineffective because of legal system, corruption, culture
 - Culture also played a difference in Detroit: white flight from a black majority
- Is there a difference in labor mobility? Flight from Detroit, century-long emigration from Southern Italy?