Productivity and the press

Productivity is currently portrayed as the Big Bad Wolf in much of continental Europe's popular press. In the first place, it is seen as the cause of a growing number of corporate projects to restructure, outsource, and offshore—in other words, shed jobs. Firms in the "old" core of the EU, particularly in France, Germany, and Italy, are struggling to remain competitive in the single European market, let alone globally. Now that the cheap labor-cost countries of central Europe are members of the EU, companies can easily move their manufacturing facilities east. There, sometimes just a few kilometers across the border, labor costs are at most 20% of those at home. And in traditional industries such as automobiles, textiles, and steel, labor costs really count.

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Although it might make the headlines, there is comparatively little outsourcing, especially compared with the number of instances of downsizing. By reducing the cost of the components of finished products, skilled manufacturing in old Europe can actually increase its employment. Adam Smith's rules of comparative advantage still hold true, provided that there is a will to change and learn.

Another corporate productivity approach disdained by the popular press is that of "beauty contests," i.e., management forcing factories of a single company to compete with each other for future investments. Yet this means that local managers and employees work together to improve their productivity and quality, a wholly laudable approach. The results are flexibility in work patterns, increased working hours, and improved efficiency without raising wages. Thus, greater labor market flexibility in Sweden has boosted labor productivity annually by 6% since the early

1990s. Yet, for the popular press, higher productivity in old Europe equals still higher unemployment, which is now well on the wrong side of 10%.

But labor costs are not the whole productivity story; unit labor costs are all-important. Under growing competitive pressures, Germany's unit labor costs have declined by 10% since 1999, contributing to its 10% rise in exports in 2004, essentially in high-tech, high-value niche products. Conversely, with less competitive pressure, Italy's unit labor costs rose by almost 10% in the same period. Not unconnectedly, Italy, like the Netherlands and Portugal, has been experiencing negative productivity growth, declining exports, and rising unemployment.

Corporate profits have also hit press headlines. Those of Europe's largest firms rose by 78% in 2004 and are forecast to rise by a further 30% in 2005. A major reason for higher profits is higher productivity. Although nowadays few have ideological hang-ups about the necessity for profits, society does question why top executives persistently couple the announcement of rising profits with their intention to slim down corporate workforces still further. Admittedly, a firm can only maintain its competitive position for a while by continuously rationalizing. However, gurus proclaim that productivity increases are a win-win situation: that all who contribute to raising a company's value should benefit from its results. Now this tenet is being contravened as top executives compress their payrolls but increase their own share of the take.

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The more serious press expounds a two-pronged path of productivity development in Europe:

1) moving out of traditional industries or at least investing more heavily in R&D and going upmarket, especially since China's challenge is not only in manufacturing but also increasingly in R&D; and
2) making labor and product markets more flexible.

This logic is in fact being applied not only in Scandinavia. The UK government countenances the loss of 2,500 manufacturing jobs every week while seeing better jobs created elsewhere in the economy, especially in skilled services. But when such a course is advocated in continental Europe, the political outcry can be deafening, as the proposed EU directive on the freedom of movement of services currently illustrates. A report commissioned by the French government indicated that 1.2 million more jobs could be created in services (hotels, shops, and restaurants) if France had proportionately as many service jobs as Germany, which is not a paragon of virtue in this respect. To achieve this, regulations to protect incumbent producers and employees would need scrapping. No action is being taken, however. Deregulation remains a dirty word in the non-Anglo-Saxon world.

The need for continuous change is much better understood in the new EU states. Their competitiveness in manufacturing stems from coupling advantageous labor costs and high educational levels with attractive governmental policies. Thus they have made great efforts to simplify bureaucracy, enabling firms to be established rapidly; and they have reduced taxes to unitary levels of 20–25% for both companies and individuals. One result: all new facilities of the international automotive companies are being set up in these states.

But gradually the need for spring-cleaning is being recognized in old Europe. The business environment is being made more favorable for entrepreneurship. Thus Germany has reformed its labor laws from 2005 to get more unemployed off of welfare and into work and self-employment. Italy's new €4 billion competitiveness program aims to cut red tape as well as boost the use of information technology, soften the impact of bankruptcy laws, and induce smaller companies to merge since most are too small to invest adequate resources in R&D. The UK government has announced a significant reduction in the number and variety of agencies overseeing firms as well as simplification of the tax payment system. Even the French government has, despite national strikes, made the 35-hour-a-week law more flexible.

The new European Commission will henceforth focus on "productivity growth and employing more people... [which] is needed to secure [Europe's] social cohesion and to make further progress toward environmental sustainability." Thus, it will continue to fight "abusive monopolies, murky cartels, anticompetitive mergers and market-distorting state aid." This means making it easier to start a business, taking a common approach on corporate governance, pursuing trade-promoting customs rules, and continuing to work for the opening of the single market. Those are fine words; let's hope that they are not sabotaged by, among others, the popular press.

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