Flash Economics

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The most serious anomaly in the European economy: stagnating productivity in manufacturing

The employment rate for the low-skilled has risen sharply in the euro zone since 2014. It is therefore not very surprising that labour productivity in services has stagnated since 2017. But labour productivity in manufacturing has also stagnated since 2018, which is abnormal and surprising. Four years after the Covid crisis, this stagnation in productivity in industry cannot be explained by the decision to retain employees in industrial companies despite the decline in activity. Rather, it is a consequence of insufficient investment in new technologies, robots and R&D by euro zone industry.

The decline in productivity in the euro zone's manufacturing industry, combined with weak pricing power due to foreign competition, explains the decline in the industry's profitability and the weak incentive to invest in euro zone industrial companies.

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It is normal for productivity to stagnate in services

The employment rate for the low-skilled has risen sharply in the euro zone (**Chart 1**), and their unemployment rate has fallen sharply (**Chart 2**), both since 2014.

Chart 1
Euro zone: Employment rate of people with low education level (less than primary, primary and lower secondary education, levels 0-2, as %)

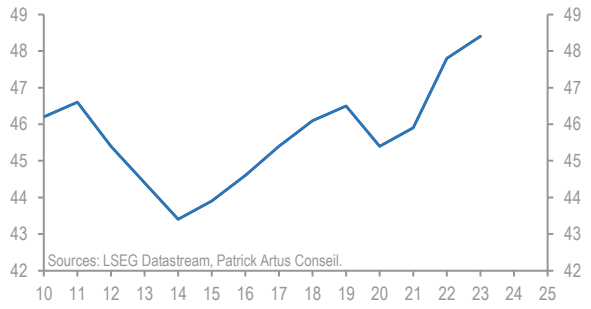
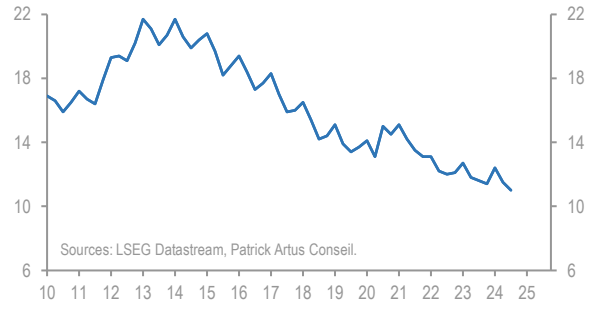
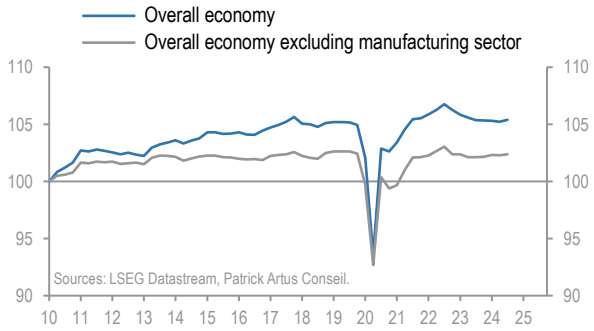


Chart 2
Euro zone: Unemployment rate of people with low education level (less than primary, primary and lower secondary education, levels 0-2, as %)



Since many people with low levels of education have entered the labour market, **it is not surprising that labour productivity in the economy as a whole and in services has stagnated** (**Chart 3**) since 2013.

Chart 3
Euro zone: Productivity per head in the overall economy and in the the overall economy excluding manufacturing sector (2010.Q1 = 100)



But it is not normal for labour productivity to have stagnated in manufacturing since 2018

Normally, labour productivity in manufacturing industry grows significantly faster than that in services or the economy as a whole. This was the case in the euro zone from 2010 to 2018 (**Charts 4A and 4B**).

Chart 4A
Euro zone: Productivity per head in the overall economy and in the manufacturing sector (2010.Q1 = 100)

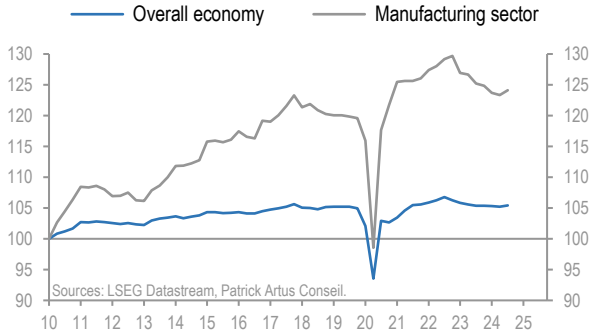


Chart 4B
Euro zone: Productivity per head in the overall economy and in the manufacturing sector (Y/Y as %)



However, since 2018, labour productivity in manufacturing has hardly risen at all (**Charts 4A and 4B**), which is surprising and anomalous.

Why is productivity stagnating in manufacturing?

Just after the Covid pandemic, an explanation often put forward for the low productivity in industry was that European industrial companies, to avoid recruitment difficulties and the loss of human capital, had chosen not to make people redundant despite the downturn in activity. But this argument is no longer valid four years after the Covid pandemic. Today's low productivity in the manufacturing industry is probably due to:

- **the weakness of investment in new technologies in the euro zone** (**Chart 5**);
- **the low level of robotisation in the euro zone, particularly in France, Spain and Italy** (**Chart 6**);
- **the low level of R&D spending by companies** (**Chart 7**).

Chart 5
ICT investment including software (in value terms, as % of nominal GDP)

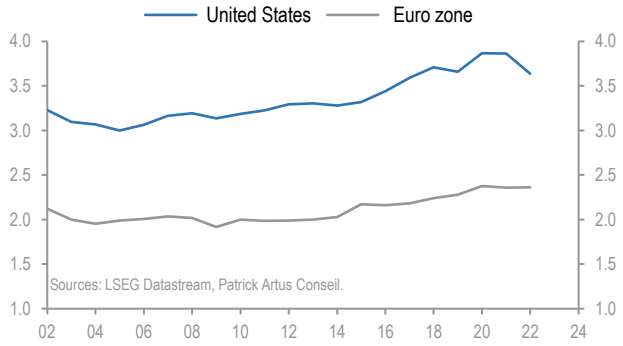


Chart 6
Stock of industrial robots (per 100 manufacturing jobs)

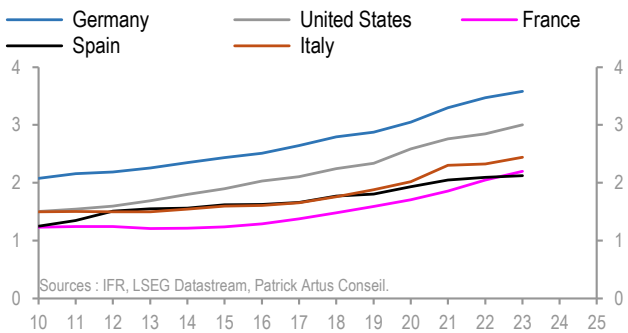
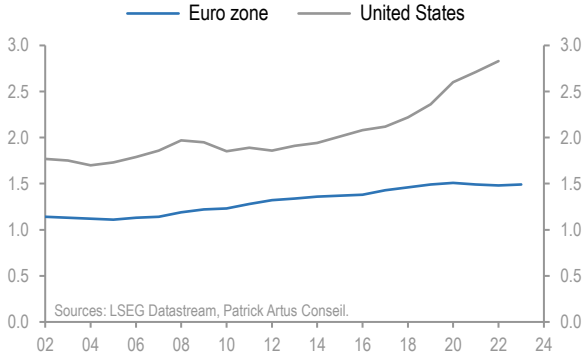


Chart 7
Corporate R&D spending (as % of nominal GDP)



Summary: explanations for the low incentive to invest in euro zone industry

Euro zone manufacturing, especially since 2018, shows:

- **a virtual stagnation in productivity**;
- **a decline in profit margins** (**Chart 8**), linked to the intensity of foreign competition.

This explains the **weak incentive to invest in European industry**, which is one of the reasons for the decline in manufacturing production in the euro zone (**Chart 9**).

Chart 8
Euro zone: Ratio between value added deflator and unit labour cost in manufacturing industry (2010.Q1 = 100)

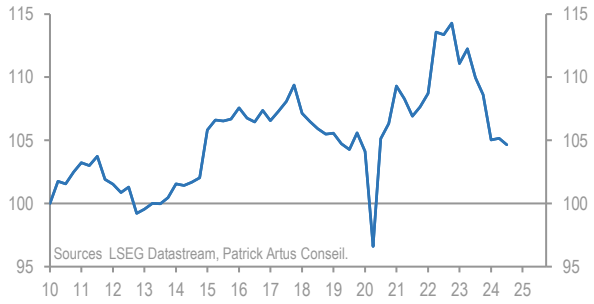
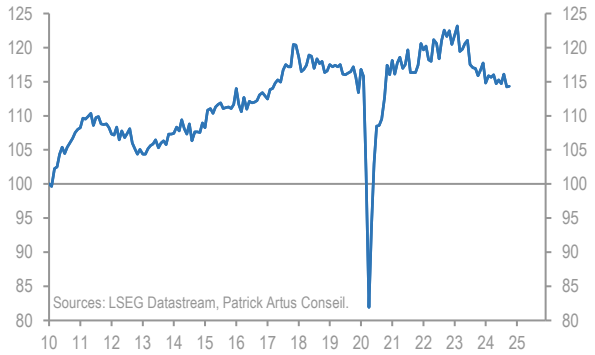


Chart 9
Euro zone: Manufacturing production (2010.M1 = 100)



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