Comments on Faini et al, "Contrasting Europe's decline: Do product market reforms help?"

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As usual at this conference, a tremendously useful paper. Both for:

- The general argument: Deregulation (Good regulation) in the service sector is crucial to overall productivity growth.
- The large amount of detailed information on the state of regulation in a number of service sectors. (from telecom to lawyers).

Shall expand briefly on six points.

1. Are things so bad (on the productivity front) ?

"Widespread rigidities in European markets are among the main culprits of Europe's poor productivity records"

Facts.

- Labor productivity levels quite close to the US.

Year	France	Italy	USA
1970	16.0	16.5	23.2
1990	30.4	30.7	30.1
2002	38.2	37.4	37.2

Source: OECD. GDP at PPP 1995 dollars, divided by total hours worked.

- Labor productivity growth substantially higher than the US, until 1995

Period	France	Italy	USA
1970-1980	3.5	3.8	1.3
1980-1990	2.8	2.3	1.3
1990-2000	1.6	1.2	1.4
(1995-2000)	1.6	1.0	2.2

(Percent.) Same source. Similar story for TFP, see Van Ark 2002, Table 19 and A7

Two ways to look at these evolutions:

  – A steady deterioration since the 1970s.
  – The end of catch up, plus the inability to match the recent turnaround in the US.

Not the same diagnosis, not the same guilty parties.

2. The post 1995 poor performance, and the role of regulation

From the work of Van Ark and others, the main sources of divergence:

- Production of IT. Does it point primarily to goods market regulation? Or education, R&D, venture and risk capital?
- Use of IT by firms does not seem that different. More spending in US, but post-2000 evidence of overspending. Case study evidence does not show large differences.
- Retail trade (the "Wal Mart" miracle), wholesale trade, and securities.

  Retail trade: Regulation? Conceivable, as most of them not under Bruxelles' mandate (zoning, opening hours). A closer look.

3. A closer look at retail trade

An accounting nightmare:

- Value added: Often gross margin.
- Price deflator corresponds to goods sold (PCE deflator), not services provided. (Highest productivity growth in computer stores...) No accounting for value of opening hours, baggers, and so on.
- Capital (if TFP): large role for value of land (much higher in Europe, so $K_F > K_{US}$), or square footage ($K_F = .5K_{US}$) Not a good proxy for use of IT.

Some numbers:

	FRA	DEU	U.K.	U.S.	E.U.
Labor pty growth					
Van Ark 1990-95 (%)	1.3	0.2	2.6	2.3	1.1
Van Ark 1995-00	0.9	-0.2	3.5	**6.9**	**1.4**
Labor productivity					
Mahony 1999	**98**	78	**61**	100*	
McKinsey 2000	98	90		100*	
Food retail (McKinsey)					
Modern segment	**107**	86		**100***	
Traditional segment	**77**	70		**48**	
Share of modern	60%	81%		92%	
Δ share trad 80-95	-23%	-17%		- 9%	

Regulation: Obvious effect on composition, not on productivity levels of each type. A social choice?

4. Deregulation and productivity growth

Whether bad regulation is the cause or not, deregulation can do wonders for productivity.

Examples from France (from the MGI studies.)

- Mobile telephony. Labor productivity twice as high in France as in the US. Cause: good regulation.
- Road freight. Easy to link high productivity growth to specific actions (load rate, truck size) and in turn to deregulation
- A contrario: Public notaries (goes beyond goods market reform). Employment at EDF.

In this light, low productivity growth since 1995 is a mystery. (other reasons? political/social pressure against layoffs, reemployment of low skill workers (Spain)?)

5. Deregulation and employment

- Deregulation should be good for employment for the economy as a whole (higher real wages (eq lower markups), and gains in productivity)

- But for the specific sector where deregulation takes place, unlikely in the short to medium run. Could not find many in our MGI studies.

- Depends obviously on the elasticity of demand.

- Depends more importantly on whether it allows for the introduction of new products (Telecom.) Or the reduction of x-inefficiency (most other sectors.)

6. Deregulation and labor market reforms

- Lower rents, need for more flexibility, both lead to pressure on some labor market institutions.

- Lower rents means weaker unions. (less to deliver to members).

- The danger. The squeezing of firms. More competition, and insufficient give in the labor market. Renault in the 1990s.