# *Towards a Social Understanding of Productivity*: A Review Article

Jeff Madrick*

Productivity dominated the economic discourse in the United States and other OECD countries in the late 1990s. Slow growing productivity was the proximate cause of slow economic growth for more than two decades beginning in the early 1970s. There is nothing like scarcity to focus one's attention, which is the one thing an economist should know. At last, a surge in productivity, all agreed, led to prosperity in the United States in the late 1990s, and the U.S. experience was highly influential on the international public discourse. The relationship between rising productivity and rising living standards was hardly questioned. How to raise productivity was almost the sole concern.

But in the early 2000s, measured productivity in the United States has continued to rise even as the economic recovery remains jobless — if it is a recovery at all. In national surveys, many Americans feel the nation is still in recession. Telling them productivity is rising is no solace. In Canada and Europe, it is clear that productivity has risen as well over the 1990s, although not like the explosive growth seen in the United States in the late 1990s, but unemployment remains high and employment rates low. GDP per capita has not grown as rapidly as in the United States.

What is the relationship between productivity growth and social progress? This volume, *Towards a Social Understanding of Productivty*,[1] edited by Andrew Sharpe, Executive Director of the Centre for the Study of Living Standards, France St.-Hilaire, Vice-President, Research at the Institute for Research on Public Policy, and Keith Banting, Director of the School of Policy Studies at Queen's University, addresses a broad concern that is often neglected in academic circles, at least those in the United States with which I am familiar. Have we assumed too readily that the growth of productivity is all that matters? To what extent does social progress itself contribute to productivity growth? Do economists focus too much on traditional factors because they can measure them, and too little on factors that may be more important but are harder to assess quantitatively? When all is said and done, what do we truly know about the cause of productivity and what are we still guessing at or forcing into pre-determined theories or biases?

On balance, the answers these authors arrive at reinforce conventional views that productivity is essential to growth and a rising standard of living — and indeed that over time rising productivity will improve social conditions. But they also define finer shades of interpretation of the empirical data and their implications for public policy. They add considerably to a fuller understanding of how social factors affect economic growth and how economic growth is linked to social improvement. I hope rather strongly that such attention will interest others in doing more research in the field.

Each of these essays is, in fact, a literature review. The pedagogical uses of the book are considerable. Andrew Sharpe's first essay is a clear and up to date summary of growth theory. The second piece, by Tony Fisher and Doug Hostland, reiterates the basic case that productivity growth has been central to Canada's long-term rise in the standard of living. Recent deviations, the authors argue, are temporary.

The third essay by Bart Van Ark explains the deviation in the growth of GDP per capita in Europe and Canada and the United States despite similar levels of productivity. The United States is by no means the most productive nation in the world, yet it has the highest (or, depending on the source, second highest) GDP per capita. The differences are largely due to hours worked.

But the central questions of the volume have to do with the linkages between social progress and productivity. Among those that interested me most was the treatment of health. I have long wondered how serious economists can present what they consider a complete model of economic growth and make no room for how a healthy society might influence national productivity. Emile Tompa directly takes on this issue and summons the evidence to argue that health does indeed matter. It is one of the most valuable pieces in the book.

The one social cause of growth for which modern growth theory seems to have made a strong case is education. Still, there are ambiguities in the empirical research and the statistical models. Arthur Sweetman's piece on the subject faces the controversies directly. He strongly concludes that education matters, but it is not clear to me that he has adequately answered all the questions about the evidence that he has raised. The preponderance of evidence weighs in favor of the view. But the holes in the arguments are still there. To his credit, he presents the many issues clearly and forthrightly.

I find Richard G. Harris's essay on the links between social policy and productivity among the most useful in the book. In fact, Harris covers a lot of territory and does not ignore basic questions. Just how conclusive have studies based on traditional production functions really been?

The following is refreshing commentary for a growth economist steeped in modern theory. Referring to the basic Solow growth accounting model, he writes:

> "While this framework is conceptually simple and widely used because productivity growth can be identified by the residual method...it has long been recognized that this approach presents serious shortcomings. In particular, there is no institutional context describing how economic incentives are determined, where new technology comes from, or what factors determine investment. The major accounts of Industrial Revolution or of economic development offered by economic historians place great emphasis on these last factors."

Harris's basic case for broadening the factors that cause growth beyond the handful of traditional economic factors — mostly, capital investment, human capital and technology — is that they do not explain growth adequately. "So far," he goes on, "it has been difficult to show that the economic determinants do a fairly good job in explaining the growth experience of countries at all levels of economic development."

In fact, Harris notes, one of the few models that seemed to have had some explanatory power since the early 1970s (though even a quick glance at it raises questions about its susceptibility to shifting assumptions about timing and data sets) was not at all able to explain the sudden and surprising surge in productivity growth in the United States in the late 1990s.

Harris then examines the effects of inequality and government social spending on growth. He can come up with only suggestive evidence.

Rising inequality may indeed impede growth, but it is far from clear. High government social spending, however, must be disaggregated to find a relationship. Some kinds of social spending may affect growth, he argues, but more passive social spending does not.

Harris remains optimistic about the theoretical and statistical models in light of all these difficulties. I might argue he is too accepting of some studies. For example, he claims many studies show that high levels of government consumption impeded economic growth. But even the study he cites, by Easterly and Rebelo, conceded that the statistical analysis was unstable. Later work by Joel Slemrod casts considerable doubt on this contention. It would seem a slam dunk that high government spending, and their usual corollary high taxes, should impede growth. But the fact is that these techniques cannot yield such a conclusion. There seems to be little relationship between government spending and growth rates—or the techniques are too blunt to find them.

I would like to call attention to one final essay in this volume. Joseph Heath asks whether maximizing productivity growth should be a nation's primary objective. It is a fine summary of the issues. Has rapid productivity growth eliminated poverty? It has certainly reduced it, but not without considerable help from social policies. Has it led to greater social equality? Not in the last thirty years. Has it made people happier? The evidence is not very supportive.

Heath proffers this analogy. The time it takes to travel across London is slow. In the first half of the century, we would have tried to build faster cars. Now, we know that it not a complete solution. Alas, we may even need some central planning (my point, not his).

Unfortunately, Heath does not explore the differences between rapid productivity growth and slow productivity growth. The cursory evidence suggests that fast growth raises more boats than does slow growth. There are also considerable differences in the social and political character of nations to be considered. For example, I believe Europe and Canada can manage slow growth better than the United States, which has always has relied more on fast growth than community sharing to solve its social problems. Slow growth is more of a challenge to the welfare state in the United States than elsewhere.

Thus, the relatively slow growth of the last thirty years is not a perfect natural experiment for analyzing productivity growth in general. In the United States, productivity growth was on average much slower than it was over the previous one hundred years.

This volume addresses the very issues economists should be talking about, writing about, and thinking about all the time. In the United Ststes, in particular, such issues seem to be of secondary importance. Perhaps this neglect is more true in Canada and Europe than I realize. Other issues discussed in the volume include productivity and natural capital, aging, social divergence, the voluntary sector, and the attitudes of Canadians toward productivity. *Towards a Social Understanding of Productivity* makes an important contribution, but I also hope it influences others to take up and take further the issues it addresses.

## Notes

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