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Intereconomics

*Suggested Citation:* Wabe, J. Stuart (1987) : Third world industrialisation-The consequences for Western Europe, Intereconomics, ISSN 0020-5346, Verlag Weltarchiv, Hamburg, Vol. 22, Iss. 4, pp. 175-181,  
<https://doi.org/10.1007/BF02932250>

This Version is available at:

<https://hdl.handle.net/10419/140086>

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# Third World Industrialisation – The Consequences for Western Europe

by J. Stuart Wabe, Bath\*

**There is growing awareness that some fundamental change has for some time been affecting the major European economies, involving a shift of manufacturing away from the developed market economies of Europe towards the developing countries. The following article analyses the process of European deindustrialisation and discusses some of the possible consequences.**

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A shift of manufacturing away from the industrialised market economies of Western Europe and towards the developing world, such as the transition to the New International Economic Order (NIEO) would inevitably involve, has considerable implications because manufacturing exhibits growth characteristics which make it the single most dynamic element in economic advance. For example, Aldcroft<sup>1</sup> shows that the rate of growth in manufacturing output in the European economies from 1950-1970 was always higher than the growth in GDP. This paper argues that this dynamic role of manufacturing was brought about because investment in this sector yielded relatively “cheap” or low cost economic growth.

European deindustrialisation is then considered. It is argued that falling profitability had led to an increasing reluctance to invest in capacity expansion and the major European economies are approaching the point where they will have zero output growth in their manufacturing sectors. Developing countries have a clear and growing comparative advantage, and it seems reasonable to expect that world manufacturing production will be increasingly located in such countries.

Post-1945 trends in manufacturing employment are analysed, paying particular attention to the changing relationship between the growth in labour productivity and the growth in output. This analysis provides an understanding of how, within the space of only three decades, manufacturing has changed from a sector with a growing demand for labour to one which has a dramatically declining labour force. This falling level of manufacturing employment has been responsible, to a considerable extent, for the exceptionally high unemployment levels which are currently being experienced in Western Europe.

The shift of manufacturing towards the developing

world raises important issues for Europe, and some of the possible economic and political consequences are discussed in the conclusions. A potentially difficult political climate is likely to ensue, especially as pressure groups and some politicians advocate isolationist and protectionist measures in an attempt to halt or slow down a trend which is clearly yielding advantages to the developing world.

Table 1 shows the investment levels and output growth rates in manufacturing and other GDP, that is total GDP less the manufacturing sector, in the seven European countries for which there were available data for 1953-1960. In each country, the manufacturing sector was growing more rapidly than the rest of the economy, even though the level of investment in manufacturing was always significantly lower than the investment level for non-manufacturing GDP.

The productivity of investment can be computed by dividing the investment percentage by the growth rate to give the incremental capital-output ratio – the level of investment which gives a 1% growth in output. The value of this ratio for manufacturing in Denmark was considerably lower than in the other six countries indicating an extremely high rate of output growth from the modest (only 7.8%) investment level. However, comparisons of incremental capital-output ratios between countries are fraught with practical problems and are not the major concern here. In particular, the computation is based on gross investment, that is it includes replacement investment, and does not indicate the additions to output which are due to an expansion in capital stock.

The major point of significance is the final column which shows the ratio of the two incremental capital-

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<sup>1</sup> D. H. Aldcroft. *The European Economy 1914-1970*, Croom Helm, London 1978, cf. Table 5.2, p. 170

output ratios: the incremental capital-output ratio for non-manufacturing GDP was usually two and a half to three times greater than for the manufacturing sector. It is in this sense that the phrase "easy growth" can be used; investment in manufacturing makes a contribution to economic growth which is considerably greater than that which derives from investment in the rest of the economy. It will be argued below that the major European economies are ceasing to invest in manufacturing and are rapidly approaching the point where the long-run manufacturing growth rate is zero. It follows that, for any *given* national level of investment, the rate of economic growth will be lower than that achieved in the recent past (and especially 1950-73) when manufacturing output was expanding.

### European Deindustrialisation

Even before the recent stagnation in economic growth, economists were beginning to anticipate a change in the level of manufacturing employment in OECD countries. In line with the theory of comparative advantage, it was suggested that certain sectors of manufacturing should shift from developed market economies (DMEs) to less developed countries (LDCs). Balassa<sup>2</sup> reports the findings of his empirical research

<sup>2</sup> B. Balassa: The Changing Pattern of Comparative Advantage in Manufactured Goods, in *Review of Economics and Statistics*, Vol. LXI, No. 2, 1979.

<sup>3</sup> L. Reyher, M. Koller, E. Spitznagel: *Employment Policy Alternatives to Unemployment in the Federal Republic of Germany*, Anglo-German Foundation, London 1980.

<sup>4</sup> DIW (Deutsches Institut für Wirtschaftsforschung): Zur künftigen Dimension des Beschäftigungsproblems in der Europäischen Gemeinschaft, in: *Wochenbericht*, Vol. 44, 18th May 1977.

<sup>5</sup> C. J. F. Brown, T. D. Sheriff: *De-Industrialisation: A Background Paper*, in: F. Blackaby (ed.) *De-Industrialisation*, Heinemann Educational Books, London 1979, cf. Table 10.13.

<sup>6</sup> T. P. Hill: *Profits and Rates of Return*, OECD, Paris 1979, cf. Table 1.1.

which support the theory of "stages" in the evolution of comparative advantage, in which countries change the structure of their production and trade in line with their growing accumulation of physical and human capital.

Since the mid 1970's however, concern has increasingly focused on the issue of deindustrialisation, although this concept has never been precisely defined. There is growing awareness that some fundamental change has been taking place within the major European economies, and a growing labour force is no longer viewed as a major asset. Reyher et al.<sup>3</sup> discuss the difficulties posed in the Federal Republic of Germany by a growing labour force and static employment opportunities. Similar problems of rising supply for other European Community members are raised by the DIW.<sup>4</sup>

### Decline in Capital Formation

Profitability is the critical determinant of resource allocation in a capitalist economic system and there is considerable evidence of a long-run declining trend in the level of profitability within the manufacturing sector. Brown and Sheriff<sup>5</sup> show that gross profit amounted to 26.4% of net output in UK manufacturing in 1966 and that a decade later this figure had been almost halved to 13.6%. If capital consumption is deducted from gross profits then the decline becomes even more dramatic; adjusted profits as a proportion of net output in manufacturing being 20.8% in 1966 and only 3.8% in 1976. A study by Hill<sup>6</sup> in ten OECD countries (including Denmark, the Federal Republic of Germany, Italy, the Netherlands and the UK) showed that they all experienced a declining share of profits in manufacturing net output over the years 1958-1976.

It might be expected that this decline in profitability would be related to investment. In particular, companies

**Table 1**  
**Investment Levels and Output Growth in Selected European Countries in the 1950's**

	Gross Fixed Capital Formation as % of GDP in 1953-59		Annual % Growth Rate in 1953-60		Incremental Capital-Output Ratio		
	Manufacturing	Other GDP	Manufacturing	Other GDP	Manufacturing	Other GDP	Other GDP Manufac'g
Belgium	14.1	20.9	3.5	2.2	4.0	9.5	2.38
Denmark	7.8	20.6	5.0	3.1	1.6	6.6	4.12
Finland	17.0	33.0	6.5	4.9	2.6	6.7	2.58
Norway	17.9	38.4	4.5	3.3	4.0	11.6	2.90
Spain <sup>1</sup>	14.0	24.6	4.4	2.4	3.2	10.2	3.19
Sweden	13.4	26.3	4.6	3.4	2.9	7.7	2.66
United Kingdom	12.1	19.6	3.8	2.4	3.2	8.2	2.56

Source: United Nations: *Yearbook of National Accounts Statistics 1967 and 1969*.

<sup>1</sup> Manufacturing includes construction and data starts in 1955.

may have been less willing to invest in capacity expansion, with most capital formation being devoted to rationalisation and labour-saving in an attempt to reduce costs and improve profitability. "Blue Book" data for the United Kingdom presented in Table 2 show that gross capital formation in manufacturing, as a percentage of net output, has declined since 1970. This ratio, which

**Table 2**  
**Fixed Capital Formation as Percentage of**  
**Net Output in UK Manufacturing, 1960-1985**

	gross	net	including leasing	
			gross	net
1960-64	12.9	6.3		
1965-69	13.3	6.2		
1969	14.0	6.8		
1970	14.3	7.0		
1971	13.6	5.9		
1972	11.0	3.0		
1973	10.6	2.5		
1974	11.7	3.1		
1975	11.3	2.1	11.9	2.7
1976	11.0	1.5	11.7	2.1
1977	11.5	1.8	12.4	2.7
1978	12.2	2.2	13.3	3.4
1979	12.1	2.3	13.3	3.5
1980	11.4	0.4	12.9	1.9
1981	9.3	-2.7	10.9	-1.1
1982	8.9	-3.0	10.6	-1.3
1983	8.9	-2.8	10.4	-1.3
1984	10.2	-0.9	11.7	0.6
1985	10.1	-0.8	12.1	1.2

Source: Central Statistical Office: National Income and Expenditure.

**Table 3**  
**Gross Fixed Capital Formation as Percentage of**  
**Net Production and Percentage of Firms Investing**  
**in Capacity Expansion in West German**  
**Manufacturing 1970-1983**

	Gross Investment	Capacity Expansion (% of Firms)
1970	15.4	55
1971	15.5	49
1972	13.4	39
1973	11.5	41
1974	10.6	34
1975	10.1	24
1976	9.7	24
1977	9.8	26
1978	9.7	28
1979	10.1	31
1980	11.0	39
1981	10.4	30
1982	10.6	26
1983	10.7	25

Sources: Deutsches Institut für Wirtschaftsforschung (Berlin): Produktionsvolumen und -potential, and Ifo-Institut für Wirtschaftsforschung (Munich): Zahlen zur Investitionstätigkeit ausgewählter Wirtschaftsbereiche.

was averaging 13 % throughout the 1960's, fell to 11 % in the mid 1970's and was only 9 % in the early 1980's. However, the gross figure is not the most appropriate as we need to know the net addition to capital stock, that is, the level of investment after replacing scrapped or obsolete equipment. Estimates of capital consumption in manufacturing are not available for the years prior to 1960. In the early 1950's, in the period of recovery after the war, nearly all investment would have represented an addition to capital stock. The figure for net capital formation would have been very close to the gross percentage (13.0 % for 1951-1955) and would almost certainly have been in excess of 10 % of net output. Net capital formation was 6.2 % of net output for the years 1965-1969 and a decade later this figure had fallen to only 2.0 %. In 1981-1985 the level of gross investment was not sufficient to compensate for the loss of scrapped capital, and the net additions to capital stock were negative.

Capital leasing by manufacturing of assets owned by the financial sector has been a phenomenon of growing importance in the UK since the mid 1970's. National income accounts reflect the ownership of capital and so understate the real level of gross fixed capital formation within the manufacturing sector. Estimates of the value of assets leased by manufacturing are available from 1975 and the investment ratio is recalculated by adding this total to both the gross and net investment figures; see last two columns of Table 2. Leasing was comparatively unimportant in 1975 as the capital value of such assets was 0.6 % of manufacturing output. By 1985, however, the value of leased assets had increased to 2.0 % of manufacturing output.

### No Capacity Expansion

Recalculating the investment ratio shows that the decline in the level of gross investment was not as marked as had originally been suggested. However, allowing for the impact of leasing does not affect the conclusion reached regarding the dramatic decline in the level of net investment. By the end of the 1970's net additions to capital stock were averaging some 3 % of manufacturing output, half the level attained a decade earlier. In 1981-1983 gross investment, even with allowance made for leasing, was insufficient to replace scrapped capital. In the first six years of the 1980's, there was zero net investment – no capacity expansion – in UK manufacturing.

Table 3 indicates that similar trends have been operating in the Federal Republic of Germany. Gross capital formation was 15.4 % of manufacturing output in 1970 and 1971, a figure which was marginally greater

than that recorded for the UK. This investment ratio declined rapidly and reached a low of 9.7% for 1976-1978. The final column of Table 3 presents survey information on the percentage of manufacturing companies who were undertaking capacity expansion. This stood at more than half in 1970 when the gross investment ratio was some 15%, and had declined to one-quarter in the mid to late 1970's when the gross investment ratio had itself fallen below 10%. These last two pieces of information would suggest that the net addition to productive capacity in the late 1970's had fallen to a low level when they represented only 2.5% of manufacturing output. In the early 1980's the level of net investment in German manufacturing has shown a marginal recovery.

The data provide clear evidence, for both the UK and Germany, that net additions to capital stock have been declining and it may be that both countries are approaching the point where this becomes zero (this may already have happened in the UK). No capacity expansion over a period of several years implies zero long-term growth in manufacturing output; such a position surely represents the "ultimate" definition of deindustrialisation.

#### Growing Comparative Advantage for LDCs

The developing countries have long recognised the potential importance of manufacturing in their economic development. Table 4 shows the share of total manufacturing value added (MVA) attained by developing countries and developed market economies<sup>7</sup> in selected years since 1963. In the 1970's, the average annual growth rate of MVA in developing countries was 7.0%, slightly less than its average for 1960-1970, but substantially above the 3.1% recorded by the developed market economies from 1970 to 1979<sup>8</sup>. However, such an achievement still means that the developing countries are only producing less than 15% of the manufacturing output in the non-Communist world. Table 4 shows that the semi-industrialising developing countries, perhaps more commonly referred to as the newly industrialising countries, were particularly successful. This group of thirteen countries increased their share of "world" manufacturing output from 6.4% in 1963 to 10.1% by 1980.

<sup>7</sup> The centrally planned economies of Europe and Asia have been excluded as being largely self-contained

<sup>8</sup> UNIDO: World Industry Since 1960: Progress and Prospects (Special Issue of the Industrial Development Survey for the Third General Conference of UNIDO), Vienna 1979; UNIDO: Handbook of Industrial Statistics, Vienna 1982.

<sup>9</sup> Cf. UNIDO: World Industry. . . , op. cit.

The decline in the share of "world" manufacturing output produced in the developed market economies has not been dramatic over this nineteen-year period. If, however, the traditional industrial nations are facing a future where they have low, zero, or even negative output growth in their manufacturing sectors, it follows that the developing countries are presented with tremendous opportunities for the rapid development of their own manufacturing industries. In particular, the developing countries should be able to exploit their continually improving competitive position<sup>9</sup> to produce an ever increasing range of manufactures for export to the developed market economies. The expectation is that the developing countries' share of "world" manufacturing will increase dramatically over the next two decades. This will be an inevitable, and one would hope generally welcome, aspect of the NIEO. However, it has to be recognised that it will pose severe economic and political problems for Europe and these are discussed below.

#### Productivity Trends

It is well documented that, in a cross-section of manufacturing sectors, the growth in labour productivity tends to be higher, the larger is the level of output growth. This association, usually referred to as the Verdoorn relationship, is estimated by regressing the growth in output per worker on a constant term and the level of output growth.

Technical change and the investment process is seen as the underlying explanation for the Verdoorn relationship. There will be some level of investment where productive capacity is not growing, that is, all investment

**Table 4**  
**Percentage Share in "World" Manufacturing**  
**Value Added, by Economic Grouping,**  
**Selected Years**

	SIDCs	Other LDCs	Total LDCs	DMEs
1963	6.4	3.1	9.5	90.5
1970	7.3	3.4	10.7	89.3
1973	8.0	3.4	11.4	88.6
1975	9.0	3.9	12.9	87.1
1978	9.3	4.1	13.4	86.6
1980	10.1	4.3	14.4	85.6
1982	n.a.	n.a.	14.7	85.3

SIDCs = Semi-Industrialising Developing Countries.  
Includes Argentina, Brazil, Colombia, Egypt, Hong Kong, India, Malaysia, Mexico, Philippines, Republic of Korea, Singapore, Thailand and Turkey.

LDCs = Developing Countries.

DMEs = Developed Market Economies.

n.a. = Not Available.

Source: Industry in a Changing World, UNIDO, 1983.

is for the replacement of scrapped capital and the level of output is unchanged. Embodied technical progress, however, will mean that the new capital will have a higher level of labour productivity than the equipment which is scrapped. Thus we would expect labour productivity to be growing even when output growth is zero, and it is of interest to consider whether the constant in the Verdoorn relationship is significantly greater than zero. The higher the rate of output growth the greater will be the level of net investment and, as the additions to the capital stock will have a productivity level which is higher than the original stock, this leads to the positive correlation between productivity growth and output growth.

The discussion above established that there had been dramatic changes in the division of gross capital spending between replacement investment and that which represented an expansion of capacity. In the immediate post-war years, it was suggested that nearly all gross investment would have represented capacity expansion. This implies that sectors with low (or zero) growth would have been making low (or even zero) investment and would find it difficult to achieve any growth in labour productivity. Using growth rates for 1948-1950, derived from Salter<sup>10</sup>, provides some confirmation of this hypothesis, as the constant term in the Verdoorn relationship (see Table 5, equation 1) is not significantly greater than zero. The characteristic feature of manufacturing at this time was that output growth was almost always greater than productivity growth and nearly all sectors were taking on extra labour.

By the mid-1950's some part of gross investment was clearly being allocated to replacement purposes. Even

sectors with no growth in output, and hence not investing in capacity expansion, would have needed to replace their worn-out or obsolete capital and, via the vintage effect, would have been able to achieve some growth in labour productivity. Output and productivity growth rates for sectors of UK manufacturing in 1954-1963 are given in Wragg and Robertson<sup>11</sup> and the Verdoorn relationship for this period (equation 2) yields a highly significant constant term. It suggests that productivity growth in 1954-1963 was some one and a half percent per annum, even when output growth was zero.

In the late 1960's an even greater proportion of gross investment was for replacement purposes and, following the argument developed above, this would suggest a further upward shift in the Verdoorn relationship. Some confirmation of this hypothesis is provided when 1963-1973 growth rates for 70 sectors of UK manufacturing, again derived from Wragg and Robertson, are used for estimation (see equation 3). A rigorous test for a significant upward shift in the relationship can be provided by combining the observations for the two periods and introducing a dummy variable which specifically measures the post-1963 shift in the constant term.<sup>12</sup> The results, in equation 4, show that the dummy variable is highly significant and indicate that productivity growth in 1963-1973 was averaging 3% per annum (a doubling since 1954-1963) for those sectors with no growth in output.

<sup>10</sup> W. Salter. *Productivity and Technical Change*, Cambridge University Press, Cambridge 1966.

<sup>11</sup> R. Wragg, J. Robertson. *Post-War Trends in Employment*, Research Paper No. 3, Department of Employment, London, June 1978.

<sup>12</sup> The dummy variable takes the value unity for observation in 1963-1973, and zero for observations in 1954-1963.

**Table 5**  
**Regression Estimate<sup>1</sup> of Relationship Between Productivity Growth and Output Growth for UK Manufacturing**

	Salter Equation 1	← Equation 2	Wragg and Robertson Equation 3	→ Equation 4	UN Equation 5
	1948-50	1954-63	1963-73	1954-73	1970-79
Output Growth	0.50 (0.10)	0.41 (0.06)	0.46 (0.07)	0.44 (0.04)	0.55 (0.10)
Post-1963 Change in Constant Term				1.53 (0.24)	
Constant	0.94 (1.01)	1.57 (0.29)	2.91 (0.29)	1.48 (0.24)	2.85 (0.32)
R <sup>2</sup>	0.54	0.41	0.43	0.52	0.56
Number of Observations	21	60	70	130	24

<sup>1</sup> Number in brackets is estimated standard error of regression coefficient.

Sources: W. Salter: *Productivity and Technical Change*, Cambridge 1966; R. Wragg, J. Robertson: *Post-War Trends in Employment*, Research Paper No. 3, Department of Employment, London, June 1978; United Nations: *Yearbook of Industrial Statistics* 1980.

Output and labour productivity growth rates for sectors of UK manufacturing in the 1970's can be computed from the United Nations Yearbook of Industrial Statistics. The Verdoorn relationship for this period (see equation 5) is more or less unchanged from that estimated in equation 3.

Growth rates derived from Panic<sup>13</sup> are used to estimate the Verdoorn relationship for German manufacturing in 1954-1972 (see Table 6, equation 6, 7 and 8). The similarity of the results in the two countries is quite remarkable. Most importantly, there is again clear statistical evidence of an upward shift in the relationship. It is also interesting to note that the 1970-1979 growth rates for German manufacturing yield a constant term of 3.30 % (equation 9), which shows a marginal increase when compared with the earlier period. Broadly similar results are obtained when the Verdoorn equation is estimated for France, Italy and the Netherlands.

### Employment Consequences

It is the employment consequences of deindustrialisation which are causing greatest concern. The manufacturing sector in 1970 employed 8.25 million workers in the Federal Republic of Germany and 8.03 million in the UK. Thirteen years later, the number employed in manufacturing had fallen to 6.58 million in Germany (decline of 20.2 %) and to 5.11 million in the UK (decline of 36.4 %). The statistical analysis below shows that there has been a significant upward shift in the relationship between productivity growth and output growth since 1950, and that the constant term in this

relationship was averaging 3.0 % in 1963-1979. If, in future, the relationship remained at this level and output growth was low, say an average of only 1.0 % per annum, then labour productivity would be expected to grow by 3.4 % per annum<sup>14</sup> and employment would decrease by 2.4 % per annum. However, it seems inconceivable that there will not be a further upward shift in the Verdoorn relationship. The years prior to 1979 witnessed relatively little of the impact of new technologies, particularly the use of micro-electronics and robots. It would seem to be within the bounds of possibilities for the constant term to be at a value of 5.0 % for the rest of this century. With only a 1.0 % growth in output this would lead us to expect a productivity growth of 5.4 % and an employment decline of 4.4 % per annum. A constant of 5.0 % implies an output growth rate of 8.3 % if there is to be an unchanged total number employed within manufacturing. This analysis would suggest that it is extremely unlikely that a major European country can ever recapture the position where it has a constant number employed within manufacturing.

### Consequences for Europe

The economic argument presented in this paper can be quickly reiterated:

- ☐ Powerful economic forces are now at work which, if left unhindered, will shift "world" manufacturing activity away from the traditional industrialised nations of Europe and towards the developing world.
- ☐ Net additions to productive capacity in European manufacturing have been declining rapidly and may soon become zero. At this point, the long-run output growth rate for the manufacturing sector will be zero.
- ☐ Post-1945 growth in manufacturing output was relatively easy to achieve because it had dramatically lower capital requirements than all other sectors of the economy.
- ☐ It follows that, for any given level of investment (as a percentage of GDP), economic growth in the future will be lower than that achieved in the years since 1945.

It seems likely that this new economic climate will result in an especially difficult set of conflicting pressures which will pose a serious challenge for European politicians. In fact these problems may already be apparent in two inter-related areas:

**Table 6**  
**Regression Estimate<sup>1</sup> of Relationship Between**  
**Productivity Growth and Output Growth for**  
**West German Manufacturing**

	← Panic →		UN	
	Equation 6	Equation 7	Equation 8	Equation 9
	1954-63	1963-72	1954-72	1970-79
Output Growth	0.34 (0.11)	0.40 (0.12)	0.37 (0.08)	0.47 (0.19)
Post-1963 Change in Constant Term	.	.	1.69 (0.47)	.
Constant	1.70 (0.88)	2.96 (0.68)	1.47 (0.66)	3.30 (0.79)
R <sup>2</sup>	0.26	0.32	0.33	0.25
Number of Observations	27	28	55	20

<sup>1</sup> Number in brackets is estimated standard error of regression coefficient.  
Sources: M. Panic. The UK and West German Manufacturing Industry 1954-72, National Economic Development Office, London 1976. United Nations Yearbook of Industrial Statistics 1980.

<sup>13</sup> M. Panic: The UK and West German Manufacturing Industry 1954-72, National Economic Development Office, London 1976.

<sup>14</sup> Computations in this paragraph assume a coefficient in output growth of 0.40.

1. *Problems of income distribution* and the potentially divisive inequality between those who are lucky enough to remain in employment and the unemployed. The escalation of unemployment throughout the European Community over the last few years would seem to suggest that the real incomes of those in employment have been increasing at a time of static national income. This rising real income has clearly been at the expense of a declining standard of living for the unemployed. The problem of unemployment is especially severe for particular groups such as the unskilled, and for certain geographical locations such as the inner city and traditional manufacturing regions.<sup>15</sup>

A major question is raised because manufacturing has always provided a considerable number of employment opportunities for workers with limited amounts of skill and/or low levels of educational attainment. Will future employment for such people have to be supported by resource transfers within the domestic economy, or can employment be found in economic sectors which are internationally traded and hence capable of earning foreign exchange? The development of the service sector is often seen as the obvious alternative to manufacturing. Services tend to be labour-intensive and an increasingly important source of export earnings for European countries. However, many of the workers who are unemployed because of the loss of jobs in manufacturing may not have the qualifications and attributes which are necessary for employment in the service sector. An added complication is that services, and in particular office employment, are now being increasingly affected by automation and new technology.

2. *Problems in wage bargaining* and the development of a new inequality between those employed in sectors of the economy with rapidly growing labour productivity and those employed elsewhere. This is seen as a particularly serious issue for the UK. Workers still employed in manufacturing have been achieving unprecedentedly high growth in their labour productivity, and this has been reflected in the level of earnings increases which they have been able to negotiate in wage bargaining. Such workers will have done exceptionally well over the last few years, with wage increases which were several percentage points ahead of price increases and a growth in their real standard of living which probably bears comparison with the 1950's and 1960's. However, other workers, particularly public

sector employees, have not been so lucky and only achieved a modest advance in their standard of living.

High wage increases in parts of the economy with rapidly growing productivity represent a potential for wage induced inflation as other groups of workers will try to match these increases. The more successful they are, given the small growth in aggregate GDP, the greater will be the level of wage inflation. In so far as they are unsuccessful, they will feel aggrieved. Although they are clearly better off than the unemployed they will not make this comparison; they will only consider what workers in similar occupations have been able to achieve in those parts of the economy with high productivity growth.

The problems associated with wage bargaining would seem to point towards the need for some form of "policy for incomes", especially in the UK. It will certainly be difficult to convince workers in the manufacturing sector that the growth in their standard of living should be lower than in the past, perhaps half, when their individual productivity is growing faster, perhaps double, than at any time in the past. Enlightened leadership will be needed from politicians and trade union leaders so that the public accepts the need for some nationally agreed wage norm which is related to the expected or potential growth in total GDP. This will be less of a problem in Germany where a consensus among the social partners does seem to work effectively and minimises wage induced inflation.

The same process which removes the dynamism of manufacturing from Western Europe will make it possible for the Third World countries to narrow the gap between their living standards and those in Europe. Clearly the biggest challenge for European politicians is to resist the temptation to try and slow down the transfer of manufacturing to the developing world. Community countries which obey the logic of the stages approach to comparative advantage should progress to a further stage, that of applying high-technology research in the production process, but may be inhibited by the fact that this is not necessarily a labour-intensive sector. Wanting first and foremost to combat unemployment, they may wish to slow down the transfer of resources which they began in more prosperous times, and in particular, to create a trading environment which makes it harder for LDCs to adopt the industrialisation course. There has to be a recognition that the past rate of advance in living standards cannot be maintained. Given this reduction in economic growth, we have got to achieve an equitable outcome among the employed, and between the employed and the unemployed, while not being protectionist and hindering the industrialisation of the developing world.

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<sup>15</sup> For a regional analysis of deindustrialisation within the European Community cf. J. S. Wabe: *The Regional Impact of Deindustrialisation in the European Community*, in: *Regional Studies*, Vol. 20, No. 1, 1986.