

Sizing the productivity problem: international, national, regional and sectoral aspects

A short submission from the Joseph Rowntree Foundation to the Productivity Commission

The Joseph Rowntree Foundation is a social change organisation working to solve UK poverty.

This short submission to the Productivity Commission focuses on one of the questions posed:

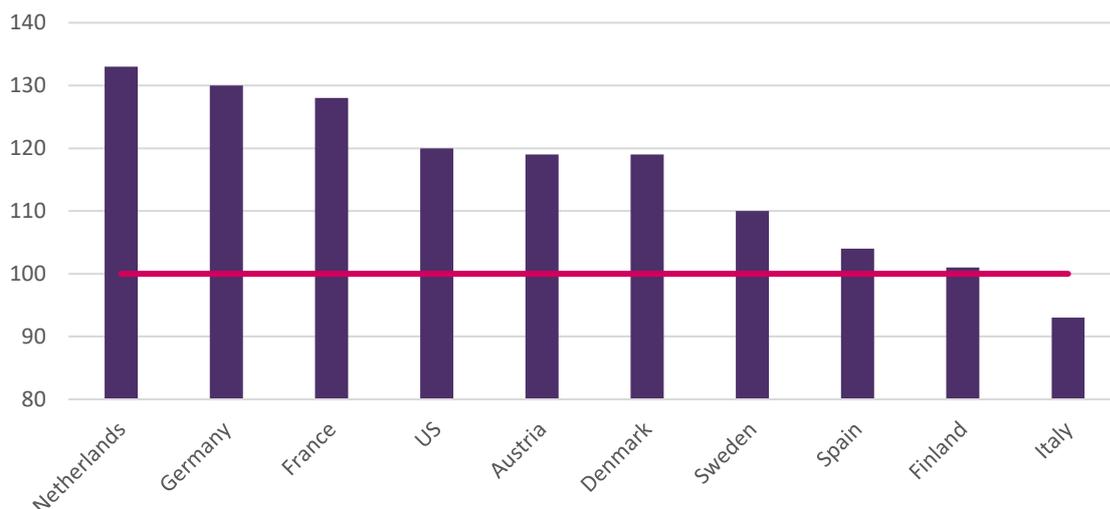
- How does the UK's productivity compare on a sectoral basis? Why do some sectors or firms have better productivity growth than others?

We would like to specifically highlight the role of low-wage sectors, such as retail and hospitality in the UK's productivity problem - that British workers produce less per hour than their counterparts in France, Germany and the US.

What role do low-wage sectors play in the UK's productivity gap with other countries?

Low-wage sectors matter for national productivity. Forth and Rincon-Aznar (2018) find that the UK's productivity problem appears across all sectors of the economy, including low-wage sectors. Of the comparison countries, only Italy had lower productivity than the UK in low-wage sectors (see Figure 1).

Figure 1: Productivity in low-wage sectors in the UK's competitors (UK=100)



Source: Forth and Rincon-Aznar (2018)

The UK's productivity gap with each of the US, France, Germany and the Netherlands ranges between a fifth and a third. German, French and Dutch workers in low-paying sectors produce more in four days than we produce in five.

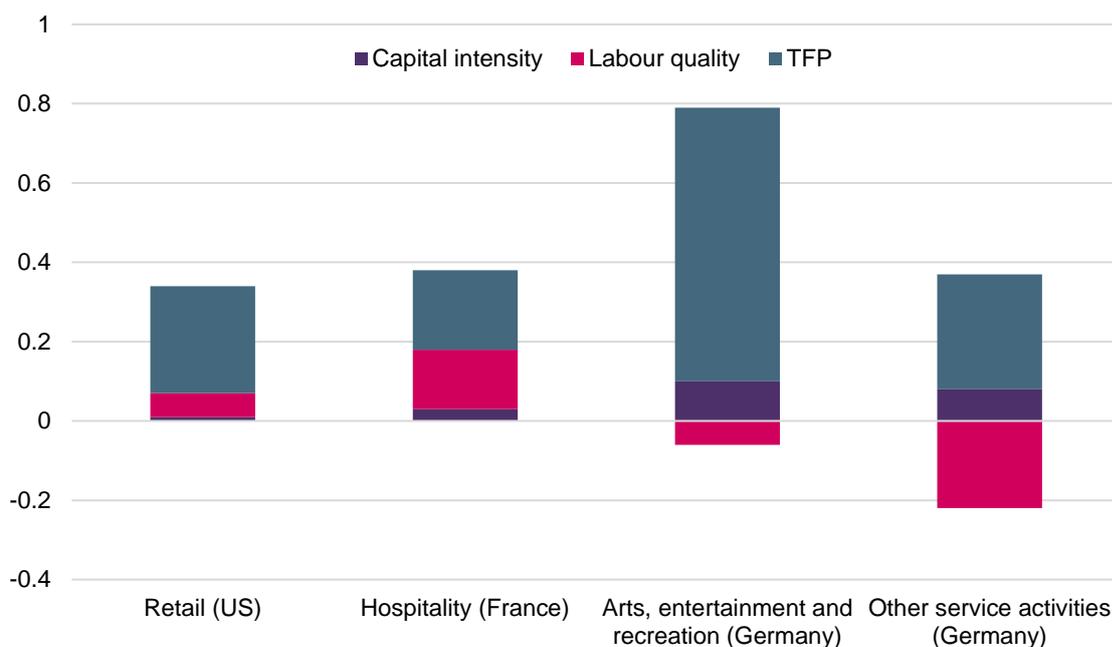
Closing the UK's productivity gap with its competitors in low-wage sectors could contribute substantially to overcoming the national productivity problem. Raising productivity in low-wage sectors to the levels in Germany, France and the Netherlands would close between a fifth and a quarter of our productivity gap with them.

Why is productivity in low-wage sectors lower in the UK than its competitors?

Differences in productivity in low-wage sectors between the UK and its competitors stem not from a lack of capital investment or workers' formal skills but how well we use workers in these sectors.

Forth and Rincon-Aznar (2018) decompose the UK's productivity gap in low-wage sectors into the contribution of physical capital – such as machinery, tools and equipment, labour 'quality' – taking into account formal qualifications and skills utilisation, and relative 'Total Factor Productivity' (TFP). TFP is the part of the productivity gap that can't be explained by differences in capital intensity or labour quality. It is an indicator of the differences in the efficiency of the production processes between the two countries.

Figure 2: Contribution of capital intensity, labour quality and TFP to the UK's productivity gap with the international sector leader



Source: Forth and Rincon-Aznar (2018)

In general, weaknesses in UK productivity in low-wage sectors are attributable primarily to differences in TFP, followed by differences in labour quality, with differences in capital intensity playing a more minor role. Figure 2 shows the decomposition of the UK's productivity gap with the competitor with highest productivity in four key low-wage sectors. In each case, TFP contributes the majority of the total productivity gap.

Why do UK low-wage sectors fall behind on TFP? The research finds four factors that are associated with higher TFP across countries and sectors and where UK low-wage sectors have significant scope to improve. TFP is highest in countries and sectors with:

- A higher proportion of workers in training;
- Better management practices, such as the use of performance related pay;
- A higher percentage of workers using ICT; and
- A lower share of temporary workers.

The research also found that a more competitive market for goods such as energy and transport increased TFP. However, the UK already has a less regulated market than many European competitors so there is little scope to close the TFP gap through further measures here.

The above four factors suggest that a set of measures that would improve productivity in the UK's low-wage sectors by bringing out the potential of workers.

The UK's productivity gap with its competitors in low-wage sectors is not due to a lack of capital investment or workers' formal skills but how well we use workers in these sectors – or Total Factor Productivity (TFP).

References

Innes, D. (2018) [The links between low productivity, low pay and in-work poverty](#)

Forth, J. and Rincon-Aznar, A. (2018) [Productivity in the UK's low-wage industries](#)