



DOES THE CONVENTIONAL WISDOM ABOUT PRODUCTIVITY NEED TO BE RECONSIDERED?

Rudolph G. Penner

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The “conventional wisdom about productivity” might better be labeled a “state of ignorance”. We do not really understand productivity or the reason that its growth has slowed so significantly in recent years. Therefore, it is dangerous to assume that the slowdown is temporary phenomenon and that it will cure itself if we give it more time.

However, being in a “state of ignorance” does not mean that we are paralyzed when providing policy advice. We may not understand all the determinants of productivity, but we do understand a few and that limited understanding can shape policies. For example, enhanced business investment will improve labor productivity if it is efficiently allocated. Recent tax reform legislation probably could have done a better job doing that and could have focused more of its efforts on encouraging new investment. Expensing would do the latter and it is a shame that the legislation makes expensing temporary. The legislation’s tax rate cuts use up a lot of revenue and their main effect is to provide capital gains on old investments.

Of course, reducing future budget deficits would provide more domestic savings to finance investment, but neither political party is much interested in that.

Increasing the average skill level of the labor force would also increase labor productivity. It is difficult to design general purpose labor training programs that provide sufficient wage increases to compensate participants for taking time off for the program, but recent sector-specific training programs seem to hold more promise.

An immigration policy that emphasizes the importance of skills and education is a more direct approach to the problem. Canada does this and it appears to have been successful. Our policies emphasize humanitarian considerations

by giving priority to uniting families. We need not do less of that if we are willing to increase the total number of immigrants.

Increased federal nondefense spending on R & D should also help productivity growth. Its relative importance grew in the years after World War II to about one percent of GDP by the mid-1960s. It has been on a downward trend ever since. In fiscal year 2016 it was only 0.3 percent of GDP. It is but one of many federal activities that is being crowded out by the inexorable growth of Social Security and health spending.

My main point is that we do not have to fully understand the productivity problem in order to do something about it. The policies outlined above do not constitute a complete list of possible actions, but they provide a start. We think that we know the direction of their effects even if we do not know the magnitude.

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