U.S. Manufacturing Retaining Its Competitive Edge

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(Manufacturing Leadership – Jeff Moad: 3-22-16) Despite significant headwinds brought on by the dramatically strengthening U.S. dollar and upheaval in the oil and gas industry, the U.S. manufacturing sector remains the most competitive worldwide, according to a new report by economics forecasting and modeling company Oxford Economics.

Impressive and ongoing productivity gains among U.S. manufacturers over the past few years as well as easy access to robust domestic markets have offset the strong dollar, collapsing oil prices, and other factors such as moderately rising wages, are continuing to provide the U.S. manufacturing sector a sustained competitive advantage over most other countries, according to the report from Oxford, which is a commercial venture that partners with Oxford University's business college.

The report also predicts that, barring an unexpected additional surge in the dollar's value on global markets, the U.S. manufacturing sector will continue to enjoy a competitive advantage over at least the next year.

"Since the US manufacturing sector's competitive edge emanates from a combination of higher absolute productivity than most of its peers, solid productivity growth partially offsetting wage growth, and a myriad of other indirect advantages, including low energy costs, a stable regulatory environment, and proximity to a large domestic market, we believe it would take a substantial further appreciation of the US dollar to make it lose its global leader position," states the report, authored by Oxford Economics' Head of US Macroeconomics Gregory Daco and Director of Industry Services Jeremy Leonard.

The report said the basis of U.S. manufacturing's continued strong competitive position is increasing productivity. The productivity of U.S. manufacturers has risen by 40% since 2003, outpacing competitors such as Germany (23%), the UK (30%), and Mexico (18%). While productivity of manufacturers in China and India has more than doubled over the same period, the report notes, U.S. manufacturers in 2016 are still nine times as productive per employee than manufacturers in China.

"In 2016, US manufacturing productivity was 25% higher than the second best economy, Japan, and 45% higher than in Germany," the report says. "Compared with emerging economies, the US manufacturing sector remains 80-90% more productive than Mexico, India, Brazil and China."

Besides enjoying a continued productivity advantage, U.S. manufacturers benefit from a wide range of other factors including higher research-and-development spending, access to an agile and well-educated workforce, relatively less bureaucratic red tape, better intellectual property protection, lower energy costs, and proximity to large markets.

The competitiveness of U.S. manufacturers has also benefited from rising labor costs in some countries, particularly China, the report finds. While hourly compensation in the U.S. was 42 times higher than in China in 2003, it has since fallen to 9 times higher than China in 2009. The hourly compensation disparity between the U.S. and Mexico has been much more stable over that period, and today U.S. labor costs are 7 times those in Mexico.

But when hourly wages are factored with productivity rates and exchange rates, the Oxford Economics study says, labor unit costs of U.S. manufacturers has essentially reached parity with those facing manufacturers in China. While unit labor costs in China were 2.5 times cheaper than those in the U.S. in 2003, the report says, today they are only 4% cheaper in China than in the U.S.

Due to fairly flat wage growth between 2003 and 2016, unit labor costs in Mexico are now 10% cheaper than in China and 16% cheaper than in the U.S.
The only major economy to have pressed a significant competitive advantage over that period compared to the U.S. has been Japan, where unit labor costs are now 25% less than those faced by U.S. manufacturers thanks largely to slow wage growth over that period, improved productivity, and a massive devaluation of the yen.

U.S. manufacturing verticals that have enjoyed the greatest drops in unit labor costs, the report says, are computers and electronics, transportation equipment, and primary metals. Less effective at reducing unit labor costs have been U.S. manufacturers in the chemicals, fabricated metals, and apparel sectors.

The report predicts that U.S. manufacturers will retain their competitive advantage, particularly if, as expected, the rise of the dollar slows. “If, however, the dollar were to appreciate another 20% over the next five years, and remain at that level, this would represent a much more important dent in U.S. competitiveness,” the report warns.

(Jeff Moad is Research Director and Executive Editor with the Manufacturing Leadership Community. He also directs the Manufacturing Leadership Awards Program.)