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American manufacturing

Lean and unseen

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Unlike General Motors and Delphi, most of America's manufacturers are thriving

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BY LOSING over \$10 billion last year, General Motors (GM) at last managed to get its workers' attention. The troubled carmaker announced this week that 35,000 employees—nearly a third of its hourly paid workforce—have accepted the company's incentives to retire early on generous terms. GM expects that the job cuts will save it \$1 billion a year. They are part of an overhaul that GM says will lower its annual fixed costs by \$5 billion, giving it a better chance to reverse its fortunes. Delphi, a bankrupt car-parts maker that used to be part of GM, announced that 12,600 of its workers have also agreed to accept early retirement.

These huge cuts in an industry at the heart of American manufacturing have fed a popular belief that anyone who makes things in the United States is struggling against an onslaught of foreign competition. Whether American firms are building plants overseas as a way to exploit cheap labour, or closing down factories because they cannot compete any more, the widespread assumption is that the country's entire industrial base is being "hollowed out". "Our media act as if American manufacturing is going to grind to a halt at around two o'clock this afternoon," says Cliff Ransom, an independent analyst who scours America for the most assiduous metal-bashers.

But someone forgot to tell American manufacturers the bad news.

Most of them have enjoyed roaring success of late. Net profits have risen by nearly 9% a year since the recession in 2001 and productivity has been growing even more rapidly than is usual during economic expansions (see chart). The country's various widget-makers, moreover, show no sign of losing their innovative edge.

Even in the automotive industry, GM and Delphi are arguably the exceptions. America has hundreds of car-parts makers, most of which are profitably supplying the plants of foreign carmakers such as Toyota and Honda, which this week announced that it will build a new plant in Indiana, to open in 2008. Caterpillar, which drove a harder bargain than GM and Ford did a few years ago with the United Auto Workers union, has since achieved huge gains in efficiency.

Capital equipment and durable goods-makers such as Caterpillar, General Electric, an industrial conglomerate, and Boeing, an aerospace giant, have always been the strongest bits of America's manufacturing base. Their position is the most secure, says James Womack of the Lean Enterprise Institute, a think-tank in Cambridge, Massachusetts, because there is so much knowledge embedded in what they make. Even when a company such as Boeing stumbles over its efficiency, as it did a few years ago, its intellectual property gives it room to recover. These days, however, American manufacturers of all sorts—not just the big durable-goods makers—are quickly improving their efficiency.

Take Littelfuse, a firm that makes fuses and other equipment to protect the electrical circuits in everything from cars and mobile phones to the machines in its customers' factories. It recently started three new production lines in an area of its plant in Des Plaines, Illinois. The sophistication of the equipment, the skills of the workers and the quality of the output are all admirable. But something else about the new 10,000 square foot (930 square metres) assembly area is even more impressive: it used to be a warehouse for the site. Littelfuse gained the space by drastically cutting back its need to store raw materials, unused scrap, unfinished goods and other sorts of wasteful material. After starting a new "lean manufacturing" drive three years ago, the plant took inches off its waistline. It now receives its raw materials—such as resins and high-grade zinc—"just-in-time" to pull them through its production line.

The same sort of thing is happening all over America. Manufacturers were already outpacing their rivals in rich countries during 1995 to 2000, when their productivity was growing by 4.0% a year. After 2000, the country's metal-bashers somehow managed to raise their productivity growth by another notch, to 5.1% a year, according to the Bureau of Labour Statistics. No serious economist thinks that America can maintain such a torrid rate of productivity growth over a longer period; indeed, the pace has already eased in the past year or two. But there are signs that America's productivity in manufacturing has been boosted by forces inherent in the structure of the economy, so that the sector should continue to thrive.

Until recently, it was hard to judge whether America's manufacturers might eventually lose a step once the effects of the 1990s information-technology boom tailed off. Research by Dale Jorgenson of Harvard University and Kevin Stiroh of the New York Federal Reserve Bank showed that IT drove much of America's productivity burst between 1995 and 2000. In a new paper, Messrs Jorgenson and Stiroh, along with Mun Ho of Resources for the Future, a think-tank, have compared the late 1990s with the productivity growth of the past five years. Not only has productivity growth accelerated further—by another 0.7% a year, to 3.2%—but the forces behind it also appear to have become more broadly based.

The economists looked at the entire private sector, not just manufacturing, and suggested that there could be several explanations for the recent strong performance. Because American firms are finding myriad ways to raise productivity, and are not merely riding one wave of innovation from the IT boom, the economists think that productivity growth will settle at a rate above what America achieved in the two decades before 1995. Over the next decade, they expect private businesses as a whole to boost productivity by 2.6% a year. That would be good news. Manufacturers, which are boosting productivity even more rapidly than the rest of the economy, should do even better.

Gordon Hunter, Littelfuse's chief executive, is confident that America can maintain its edge in manufacturing. He is an engineer from the north of England who spent much of his earlier career working for Intel, a semiconductor firm, in California. American firms will keep on improving their productivity, he says, because of



a business environment that embraces innovation. "Being flexible and willing to learn are skills that America still excels at," he says. Eventually, perhaps even GM will get the hang of it.

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