

Why U.S. Business Is Winning

The Washington Post

By Sebastian Mallaby

Monday, March 27, 2006

Newspapers bring us the dark stories about American business. The Enron trial serves up tales of lies and looting. The General Motors restructuring dramatizes the death of traditional U.S. manufacturing. Commentators from left and right agree that a growing swath of the economy, from accounting services to non-emergency health care, may one day move offshore. And yet something is going dramatically right inside American corporations. Despite all the nostalgia for the era when GM dominated the world's car industry, the heyday of American business may actually be now.

The dawn of this heyday came in 1995. In the two preceding decades, the productivity of American workers had grown more slowly than that of Japanese and European competitors. But in the decade since 1995, U.S. labor productivity growth has outstripped foreign rivals'. Meanwhile U.S. firms' return on equity -- that is, the efficiency with which they manage the capital entrusted to them -- has pulled away from that of Japan, France and Germany, according to data provided by Standard & Poor's Compustat.

Other measures tell a similar story. Up until the 1990s, management books were crammed with Japanese buzzwords, and the early Clinton administration was in awe of Germany's apprenticeship system. But today the United States provides most of the business role models, from Starbucks to Procter & Gamble, from Apple to Cisco. The (British) Financial Times publishes an annual list of the world's most respected companies. In 2004 and again in 2005, no fewer than 12 of the top 15 slots were occupied by American firms.

Or consider the database on management quality constructed by Nick Bloom and John Van Reenen of Stanford University and the London School of Economics. This duo organized a survey of 732 medium-sized American and European companies and measured their management procedures against benchmarks of best practice. The result: American firms, including the subsidiaries of American firms in Europe, are simply better managed than European rivals. In fact, superior American management accounts for more than half of the productivity gap between American and European firms.

Whence this American superiority? The first answer is that competition is fiercer. The United States has relatively few trade and regulatory barriers for firms to hide behind, so bad companies either shape up quickly or go bust. In retailing, for example, firms such as Wal-Mart and Target have been able to spread their super-efficient logistics systems all across the country -- at least until lately, when a perverse anti-Wal-Mart campaign has sprung up. In Europe and Japan, by contrast, a web of zoning laws entangles efficient retailers, sheltering unproductive companies that overcharge consumers.

The next explanation for American superiority is a healthy indifference to first sons. Bloom and Van Reenen report that the practice of handing a family firm down from father to oldest son is five times more common in France and Britain than in the United States. Not surprisingly, this anti-meritocratic practice does not always produce good managers. So even though the best European companies are managed roughly as well as the best American ones, there's a fat tail of second-rate firms in Europe that's absent in the United States.

Competition and meritocracy cannot explain all of America's superiority, however. The U.S. economy has always had these advantages but hasn't always trounced overseas rivals. Nor is it enough to say that Americans work harder than Europeans, since the productivity numbers show that Americans are boosting what they achieve per hour. And anyone who explains America's superiority by saying that the country is more "dynamic" or "creative" is merely relabeling the mystery we're trying to solve.

The best guess about the "X factor" is that America's business culture is peculiarly well-suited to contemporary challenges. American business is not especially good at coaxing productivity out of factory workers: The era when this was all-important was the heyday of Germany and Japan. But American business excels at managing service workers and knowledge workers: at equipping these people with technology, empowering them with the right level of independence and paying for performance. So the era of decentralized "network" businesses is the American era.

Moreover, America's business culture is perfectly matched to globalization. American executive suites and MBA courses are full of talented immigrants, so American managers think nothing of working in multicultural firms. The immigrants have links to their home countries, so Americans have an advantage in establishing global supply chains. The elites of Asia and Latin America compete to attend U.S. universities; when they return to their countries, they are keener to join the local operation of a U.S. company than of a German or Japanese one.

So the shift from manufacturing to services; the gallop of globalization; and the rise of information technology that flattens corporate hierarchies: All these forces come together to create an American moment. But you could be forgiven for missing this, because other forces spoil what ought to be a celebration. In the midst of this American moment, hatred of President Bush has simultaneously created an anti-American moment. And in the midst of American prosperity, rising inequality has prevented American workers from sharing in the success of American firms.

smallaby@washpost.com