

Industry Engines 2018 – Estonian Economy and Manufacturing Industries in Global Competition

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ETLA's draft report and structure of this talk

- Report
 - Analytical synthesis & conclusions based on existing knowledge and extension to global context
- This talk:
 - Global Market in Transition
 - New paradigm globalization
 - "Second unbundling" – specialization in the global market does not (necessarily) take place by industries, but at much finer level of disaggregation (functions, tasks)
 - Challenges to industrial policies
 - Estonian economy and industries in transition
 - Estonian economy at the brink of a recession?
 - Is it too late – can the recession be turned into new opportunities?

Global Market in Transition

World Economy and Competition – Global Trends (I)

- World is becoming increasingly globalized and competitive – splitting of value chains into smaller pieces and relocating across the globe
- China and India (re)emerging as global big players
 - EU/OECD countries, and EU/OECD based firms, face increasing competition from Asia
 - China's export structure has become more similar to that of EU – China is competing across the whole range of industrial goods – not only in low-cost production
 - There are also new opportunities – global markets have been growing faster than for many years

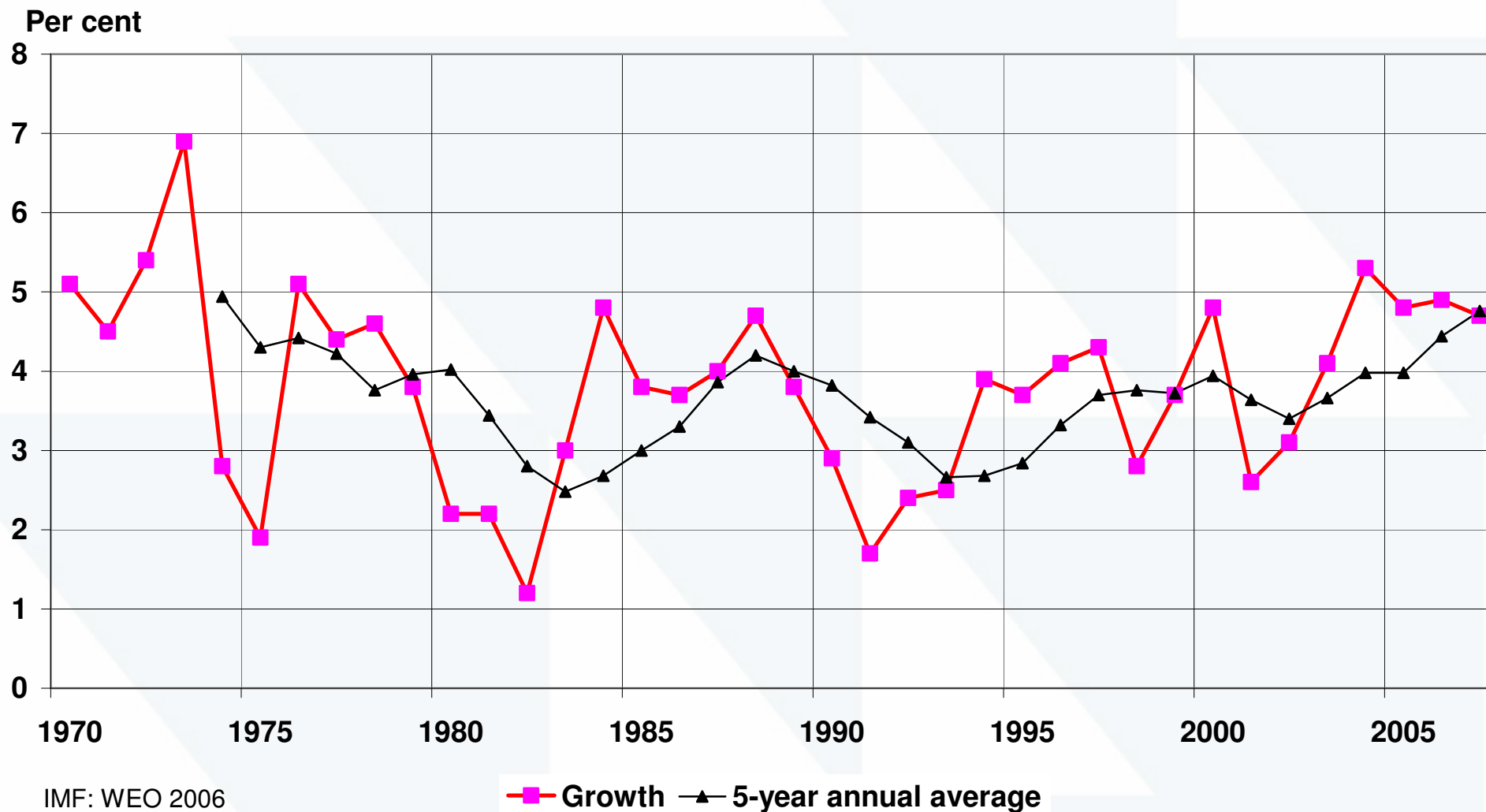
World Economy and Competition – Global Trends



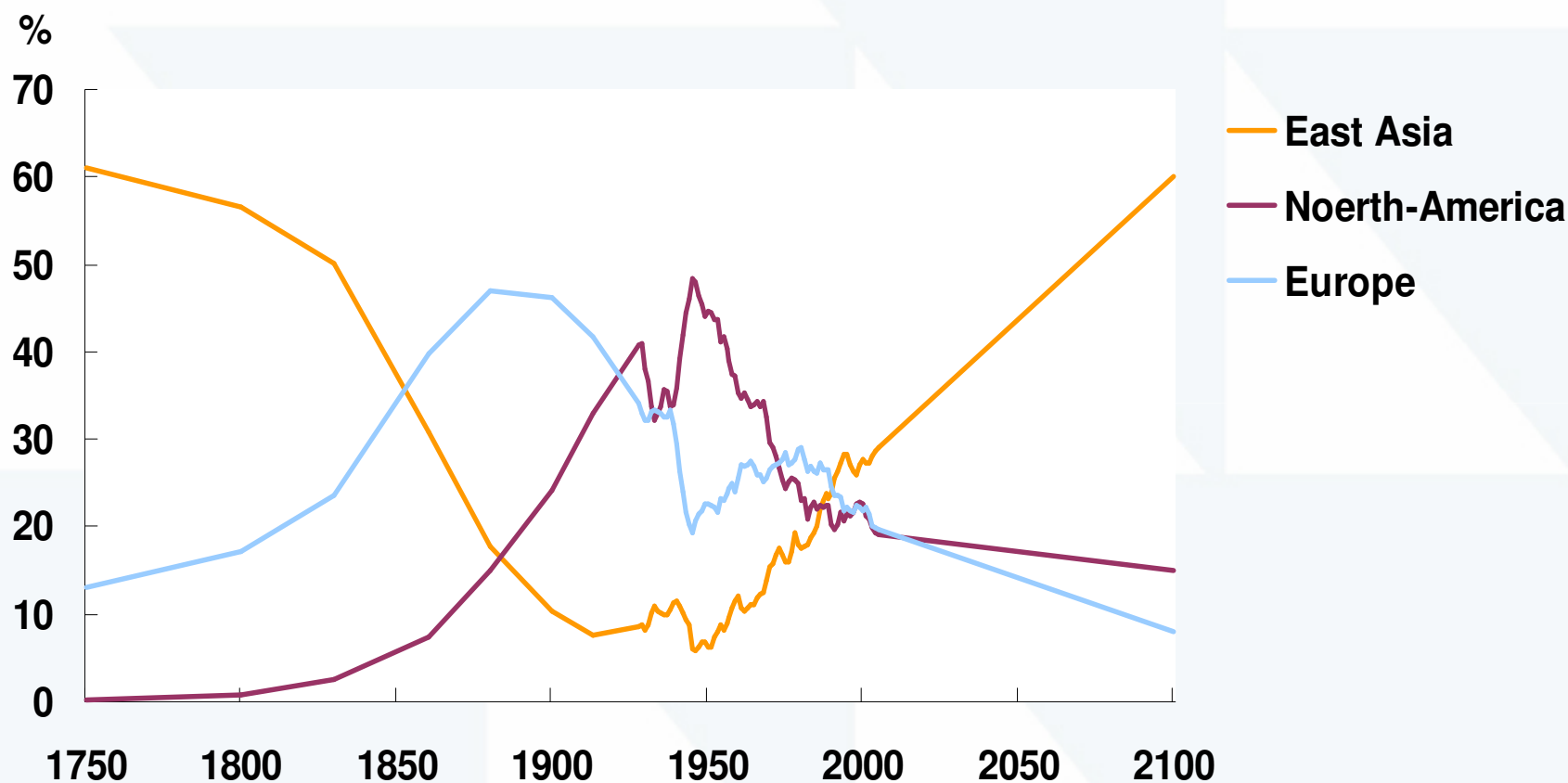
(II)

- ICT revolution is still strong -- its contribution to productivity is peaking, however
- Demographics: more than 2 bill. new employees to global labor market since mid-1980s – world population will peak around 2050 at 8-10 bill. => rapid ageing over the next decades
- Environmental issues and climate change are putting limits to economic growth but have created new opportunities/growth industries
 - comparable to ICT boom?
- Politics
 - new wealth and power distribution (oil producers & fast growing countries)
 - In search for new ways of global governance

World GDP Growth



Industrial production by regions, % of total



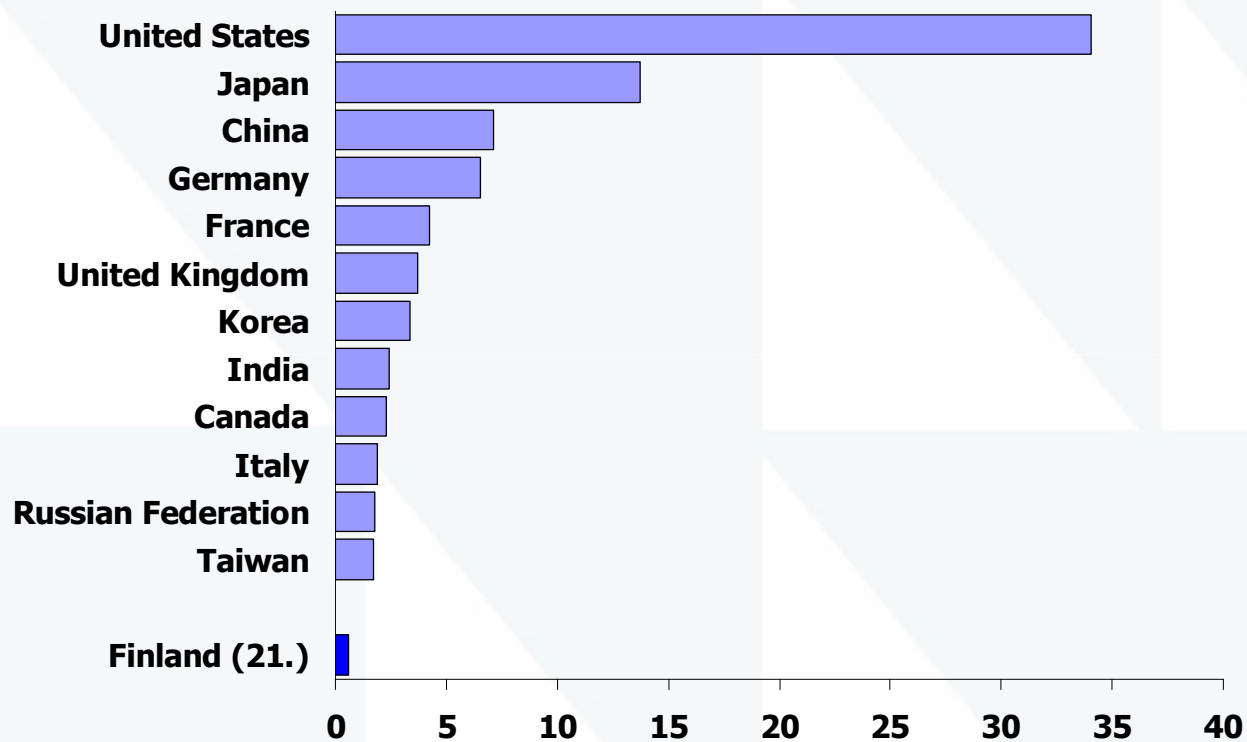
East Asia = China, Japan, India

North America = USA, Canada

Europe = Germany, Great Britain, France, Italy Spain, Sweden, Belgium, Switzerland

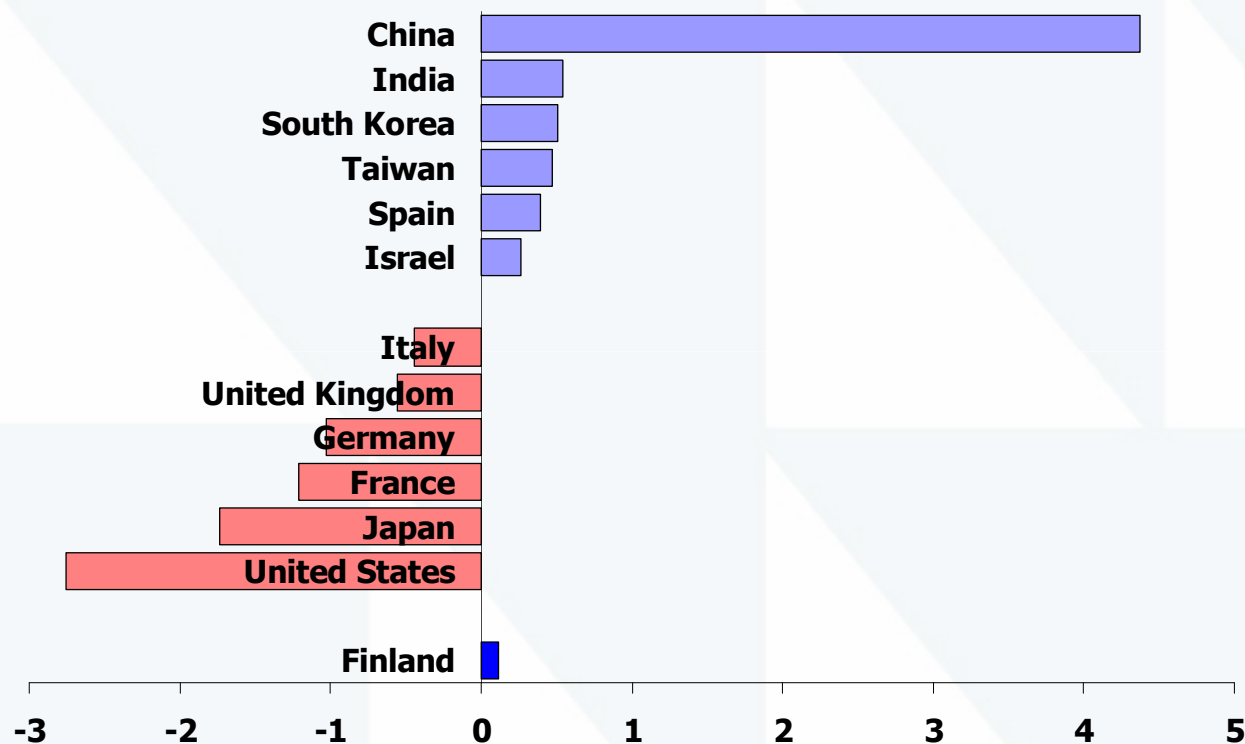
How is the global R&D landscape changing?

The largest countries in terms of R&D in 2005 (as % of total world R&D)



Source: ETLA/Maury.

Changes in the shares of the world R&D (1996-2005, percentage points)



Source: ETLA/Maury.

New paradigm globalization & Policy challenges

Industries and clusters in transition: policy challenges of globalization (1)



- “New-paradigm globalization” = “second unbundling” (Baldwin, 2007)
 - Globalization takes place at very fine level of disaggregation
 - Specialization and competition
 - Not at industry level, not at firm level...
 - But at level of tasks or functions
 - Firms have spilt their value chains globally
 - From collaborative and integrated national production and manufacturing systems to globally dispersed value chains

Hubs of specialization in the global value chains – How the value is created?

Breakdown of \$299 retail price
of a 30Gb Video iPod® in 2005

Manufacturing (assembly) \$7

Gross margin	\$76
Retailer	\$45
Distributor	\$30
Parts: Storage	\$74
Parts: Display	\$24
Parts: Chips	\$18
Parts: Others	\$25

Data source: Detrick,
Kraemer, Linden,
UC Irvine (PCIC),
mimeo, Sep. 2007.



Rouvinen, ETLA

Estonian economy – At the brink of a recession?

Causes and consequences

- Huge inflow of capital
 - FDI based on cost advantage
 - Real estate bubble
 - Only fraction of FDI to manufacturing
 - Consumption-led growth
 - Export sector (manufacturing) too small to support sustained economic growth
- Overheating of the economy, high inflation
 - Labor costs in relation to productivity at unsustainable level
 - Competitiveness lost

Industrial policies needed?

- Industrial policies never high in policy agenda
- No clear industrial strongholds to be identified
- Opportunities in upgrading traditional industries where Estonia has a *comparative advantage*
 - Wood based industries, glass and cement, etc.
- New potential growth industries?

Industrial policies needed?

- With whom and in which markets Estonia is competing globally?
 - Asia/China has become strong in *both* cost-driven industries *and* human capital-intensive industries
- There is always a niche in the global market for a small/tiny economy
- Competition and specialization does not – necessarily – take place at industry level – but at the level of tasks and functions
=> competitive hubs of specialization?
 - Conventional data and analyses is not sufficient to identify such potential hubs – unconventional sources of information are needed
- Estonia needs a national industrial strategy based on well-argued future vision which draws on industry studies and expert insights