Macro Roundup Article

Headline: Increasing Returns: Identifying Forms of Increasing Returns and What Drives Them

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Tweet: Increasing returns on capital may be driven by superstar firms that outspend their competitors on R&D; and better management practices which they can then scale. @mjmauboussin

Summary: The gap in productivity between the best and worst companies within industries is large. For instance, economists measured the productivity of U.S. manufacturing plants and found that the output at the 90th percentile was nearly double that of those at the 10th percentile. Economists do not fully understand why that difference is so large, but they commonly attribute it to management talent. Organizations do not always identify and implement best practices. Superstar firms substantially outspend their competitors on intangible assets. They are spending big on "ideas": software, training, and research and development (R&D). James Bessen documents that spending for proprietary software has grown substantially faster than that for R&D, acquisitions, advertising, and lobbying. U.S. firms spend more than $200 billion per year on proprietary software and the big firms represent the bulk of that outlay. They are investing heavily in nonrival goods. Bessen then makes the case that proprietary software enables superstar firms to capture classic economies of scale and to offer differentiated products.

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