The management of the crisis is too Keynesian

Editorialist: Denis Kessler

Challenges

16.06.2011

All economic and financial crises involve significant costs, due to the contraction of business, the differential evolution of asset prices, the rise in unemployment, or public decisions with regard to taxes or resorting to debt, and so on. The way in which these costs are shared between economic players is an equally important issue. Four years after it broke out, which economic agents have borne the cost of the crisis in France? Households? Companies from the competitive sector? How has the distribution of added value in France become distorted? Thanks to the latest national accounting data, we can now give a specific answer to this question, which is at once economic and political. At the dawn of a major election, when the manifestos are being drawn up, it is crucial to assess the situation objectively in order to avoid stacking up all kinds of public measures that would be inappropriate, harmful or dangerous for competitiveness and the return to growth.

The first – very Keynesian – choice has been to postpone the cost of the crisis until later rather than making current generations shoulder it. Public and social deficits have exploded and public debt has increased sharply, rising from 1,152 billion at the end of 2006 to 1,591 billion at the end of 2010. Someone is going to have to honour this debt – and contrary to what Keynes, who had no children, said, in the long term we will not all be dead and there will be a new short term and new generations! Another choice would have been to prevent this exaggerated ballooning of debt by leaning on public and social welfare spending and by proportionally increasing obligatory contributions.

The second choice has been to protect consumers/employees rather than companies. The increase in salaries since 2006 has certainly been smaller during the crisis than it was previously, but it has happened much faster than the increase in the added value of companies, whose pace has slowed down considerably. Over the period 2006-2010, the added value of companies increased by 7.5% in nominal terms, representing a volume of EUR 74 billion. The vast majority of this increase, 82% to be precise, i.e. 61 billion out of 74 billion, went to employees in the form of salaries, social contributions or wage taxes! Thus, the proportion of added value devoted to work, whether directly or indirectly, rose from 66.9 to 67.9% over this
2006-2010 period. In business, therefore, employees have been indisputably and globally spared by the crisis, while company margins have been eroded. When you look at households rather than at business, you have to admit that the diagnosis is similar. The adjusted disposable income of households increased by 5.8% in real terms over the period 2006-2010, notably thanks to a rise in social welfare benefits of 10.1%, while net salaries increased by 3.6%.

The third choice made has been to “collectivize” national revenue even further through a deliberate policy of maintaining and even expanding social welfare payments, in the name of recovery or support for domestic demand…

These choices have had two consequences. The first is a fall in corporate investments. From 2006 to 2010, productive investments fell by 0.8% in volume. The second consequence is the inflation of external debt; support for consumption having largely benefitted…foreign companies. Imports rose by 6.5% between 2006 and 2010, while exports increased by just 1.3%. The Keynesian policy adopted actually has a very significant flaw: it has major adverse effects on the open economy. If the recovery had been coordinated throughout Europe or the world, these effects would have been minimised. In the absence of coordination, they are powerfully present. Also in this area, other choices would have been possible: massive support for company investments, and greater international specialisation of the French production system in order to re-establish external balance and generate the resources needed to facilitate debt reimbursement.

The cost of the crisis remains largely to be paid. The choice of distributing it between households and companies is crucial. If we continue to favour households to the detriment of productive companies, and social income to the detriment of business income, the inevitable subsequent slowdown of growth and the piling up of external debt will render this cost increasingly unbearable. Above all if interest rates and spreads increase, dramatically pushing up debt service.

*Exergue:* Between 2006 and 2010, employees were globally spared by the crisis, while company margins were eroded.