From Bust to Boom: New Chances for Lisbon Strategy

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Afterthoughts about the Crisis
(What remained out of presentation)

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Speaking about Schumpeterian approach to crisis reminds me on the Forest Fire dilemma. According to one of my Australian friends, a biologist, these fires are beneficial. They burn the sick and infected, including the parasites, while the strong and healthy usually survive. The next spring, in a few months, the forest revives with increased vigour and restores itself in a relatively short time. Of course, I do not speak about arsons or accidents, when settlements or peoples are threatened, about which we get media coverage from time to time, just from Australia or California. What I speak about are those mechanisms by which Mother Nature has cleaned and revived itself for many millions of years. Of course, Human Society could and should intervene. We can save all that is worth saving and we can accelerate the process of restoration. Not least, we can avert the revival of parasites. Human intervention can assure that we really get a better structure.

The same thoughts can be applied to the present crisis. And I hope that they do not conflict with Schumpeterian ideas. Let us take the case of the automobile industry. It shows all the patterns of a crisis industry. It has an about 92 million production capacity in the world, while, according to estimates, we are likely to buy no more an 60 million cars this year. This suggests a more than 30 percent shortfall. If we put it in the context of an about 3% decrease in GDP, this means ten times more shrinkage in the automobile sector than in world production. This is a typical crisis industry phenomenon. In the 1970s, shipbuilding, textiles etc. were considered the crisis industries of the epoch. Now, the automobile industry has taken on this crisis industry status.

The reasons are complex. One major reason is the sector's close integration with banking and credit. In the USA, about 90% of cars are sold on credit, while in Europe the proportion is also more than 2/3. In Hungary, we have similar proportions. The automobile industry got into a close symbiosis with banking. This is true, both in terms of production and consumption. A few years ago, if you wanted to buy a car for cash, the dealers were unhappy and they tried to persuade you to buy it for credit. For one simple reason, a dealer would insist on that, because his profit came not basically from the manufacturers but from the banks. It meant a certain sort of profit sharing between the different actors. Now, as the banking sector fell into crisis, it immediately affected the whole automobile sector. There are also some broader structural implications. Cars are major polluters. Global warming and the deterioration of the environment call for urgent actions. This would imply a fundamental restructuring of the whole industry. Actions in these areas could not be avoided. The fire is here. And there is no question that a broad and complex intervention is needed. It is not easy to tell what should be saved and what restructured and renewed in the future.

The main ways of interventions are more or less worked out, and the first steps were already taken. We all agreed that the short-term Keynesian and the longer term Schumpeterian type of interventions are equally important. Personal subsidies for replacing old cars (applied in some countries), or conditional state subsidies for fundamental restructuring in the direction of more energy saving and environmentally friendly cars are good ideas and could be strongly supported. The latter fully correspond to Schumpeterian thinking. The question is rather: Are they robust enough to exert real impact? It is more controversial if the subsidies aim at preserving jobs, which socially and politically might be important. But the question remains: After 1-2 years would there be enough demand for these preserved production capacities, or should they be closed? In the latter case it would be better to close them now.

An equally important question is who should intervene. Here, the consensus is far more uncertain. Should the national government intervene in accordance with their specific problems or, as far as the car industry is a typically globally integrated sector, are global interventions also needed? I am convinced that both are equally important.

But here we face certain disquieting and unacceptable trends. Some tried to limit state aid exclusively to their local car industry and condition it on reliance on only local suppliers. Similarly in some cases, replacements of old cars were also subsidised only when buying domestically produced cars. This, of course, is contrary to the principles of the internal market and it is nothing other than a special form of protectionism.

What is worse is that these measures were often argued for as a certain revenge or strike back against dislocation. That is totally wrong and proves that certain politicians do not understand anything about globalisation. Dislocation is nothing other than a normal process of reallocation and optimisation of resources, which brings substantial efficiency and welfare gains, in fact for all who are affected. It does not matter that in this case optimisation occurred in global dimensions. It was good for not only the receiver countries. It was beneficial also for foreign investor companies (they were the main beneficiaries) and for the "sending" country as well. It was not a zero sum game; everybody was gaining. A Schumpeterian economist knows, however, that there are related costs (among others, for those who lose their jobs) and it is just normal. Simply, the costs should have been addressed. Already at the beginning of the 1990s many predicted that among others the European automobile industry would move from West to East, due to lower costs and dynamically expanding markets there. There was nothing unexpected, but the old EU member governments failed to respond to this challenge and make the necessary steps to counterbalance the consequences. It was easier to blame their national companies and the "receivers". In fact, Hungary and some Central European countries "suffer" already from "dislocation", because capacities move further to even cheaper resources.

It is even worse when responsibility is disclaimed by "social" or "wage dumping", and this type of thinking has recently been again strengthened by the crisis. We know that dumping is a special offence in international trade law, and countermeasures or "punishments" are justified on the basis of that misbehaviour, which is related to lack of social security systems, the use of underpaid children and women or even a slave type of exploitation: For certain countries, it is a justified accusation. But that is not the case with Eastern and Central Europe. The wages, there, are market wages, and they have sophisticated welfare systems. In fact, the main recommendations of the IMF and the World Bank, and the main accusation and complaint of foreign investors is that these countries have too generous social systems, and the social security costs should be cut substantially. “Social dumping” which we could hear from the mouths of several responsible politicians, is totally unfounded, and it is nothing else than an attempt to criminalise increased competition. (It is true that CEE wages combined with highest productivity bring substantial wage cost comparative advantages.) That is totally unjust and unacceptable. Germany was wise enough, when offering bonuses for old car replacement, not to connect the process with an obligation to buy only domestically manufactured cars. This raises extraordinary demand for cheap Romanian Dacia cars, which at first glance may seem irrational in terms of promoting the domestic recovery of the German economy. But it is not irrational. Among highly integrated economies, the improvement of a partner can have equally strong impact as mere application of “local” incentives. These types of impacts, however, can be enhanced by an increased global and regional coordination among different governments. We must urge these kinds of co-operation. The G20 Meeting gave some encouraging signals, but only the future will tell whether they will be enough help in coping with the present crisis.