

A Very Serious Multidimensional Crisis, Creative Destruction and Territories

Henri Regnault
The University of Pau and Pays de l'Adour
henri.regnault@univ-pau.fr

This paper is based on a presentation made on 27 November 2009 at the Provence-Alpes-Côte d'Azur Regional Council in Marseille, during the seminar on "Leading Europe out of the Crisis: Proposals from the Regions" organised by the CPMR

What is the nature of the crisis we are going through? It is not merely a recession which can be identified by the yardstick of a fall in GDP over two consecutive quarters. Nor is it a repeat of the Depression of the 1930s: it is very different and much more complicated. We are in a Very Serious Multidimensional Crisis (VSMC) which is unprecedented and is initiating a process of creative destruction of exceptional intensity, of which territories will be a part to differing degrees depending on their ability to implement policies to contain the harmful impact of the destruction and enhance the creative effect.

The first part of this text, entitled **A Very Serious Multidimensional Crisis (VSMC) and Creative Destruction**, draws widely on the conclusion of *De la nature de la crise* (The Nature of the Crisis) in *Journal de Crise: août 2007 – novembre 2009, des subprimes à l'illusion de la reprise* (Crisis Diary: August 2007 - November 2009, from Subprimes to the Illusion of Recovery, to be published in 2010).¹ The second part, entitled **The Future of Territories Depends on their Ability to Manage Creative Destruction** has been devised especially for this meeting in Marseille, which gives me an opportunity to build a bridge between my general analysis of the crisis and the debate on territories. This represents a return to the early stages of my research career, when I was a regional expert and spatial planner specialising in the development economy and then the international economy.

1. A Very Serious Multidimensional Crisis and Creative Destruction

The VSMC is not a temporary economic phenomenon but a structural challenge, and policies aimed at tackling it cannot be termed as short-term action and thus Keynesian recovery solutions (which were extremely popular in the second half of the 20th century as a tool for recovering from recessions). The issue here is renewal rather than recovery. **The VSMC is a global multisystem crisis with high creative destruction potential.**

The VSMC is a multisystem crisis that is unprecedented in the history of mankind. It is systemic in the widest possible sense of this term. It does not just concern the chain collapse of banking institutions, with the bankruptcy of one bring about the bankruptcy of others and so on. Most luckily, we just managed to avoid such a collapse in the autumn of 2008, when the dreadful knock-on effects of the bankruptcy of Lehman Brothers were halted by the intervention of the central banks. However, during the current period, a much wider view of the systemic crisis is required: on one hand, the crisis affects the whole social system (economic, political, ideological)

¹ Some short extracts of my first quarterly diary entries (*La Crise*, No. 1 September 2007 to No.5 December 2008) are available at: http://www.imera.fr/PDF/Extraits_de_JOURNAL_DE_CRISE.pdf. See also: *La très grande crise et ses débats* (The Very Serious Crisis and Surrounding Issues), a speech at the IMERA seminar on 26 March 2009, which draws on points made in *La Crise* No. 6 : http://www.imera.fr/images/stories/PDF/3hr_expos_imra1.pdf.

and on the other hand, it also concerns the links between this social system and ecosystems (depletion of resources, the increasing disappearance of species, the environment and climate).

Furthermore, **the VSMC is a global phenomenon**, which is another aspect of its multidimensionality, in the spatial sense of the term: it is not just restricted to the countries in which it is taking place. The debate on whether the United States would be considered as separate from rest of the world (or whether the developed countries could be considered as separate from emerging countries) has now been settled and the answer is no: the crisis is contagious, although there are time lapses, due to how long it takes to spread, as well as differing degrees of intensity in different territories.

We are confronted with the **simultaneous occurrence of a regulatory crisis and a vital technological break with the past which has been made necessary by the mismatch between human society and the ecosystem**. The **regulatory crisis** is due to the breakdown of the Fordist model further to globalisation and the unsustainable Greenspan-inspired model of regulation via household debt: Fordist model, to be simple, refers to the 30-year period of economic expansion between 1945 and 1975 (called the *Trente Glorieuses* in France), during which wages progressed at the same rate as productivity, thus permitting an increase in demand for consumer goods; by Greenspanism (a neologism that is not at all recognised in academic circles!) I mean a whole range of monetary practices (low rates) and financial practices (very easily-granted loans, securitisation of uncertain debt, and so on) which led to the high level of household debt, setting off the subprime time bomb. **The mismatch between human society and the ecosystem** stems from the impossibility of prolonging the use of current technologies, especially the underlying energy model, due to the depletion of fossil resources and the likelihood (not absolute certainty) of the climate impact of the carbon energy model. It is this simultaneous occurrence which underlies the specific nature of the VSMC in comparison to previous crises: I am not just talking about short-term economic crises and the oil crises, but also the Great Depression of the 1930s, which firstly was not as global, as it did not affect the whole planet, and secondly was purely economic, social and political in its ramifications, not having to simultaneously manage the renewal of the energy technology model. The pre-1929 world was one in which oil was starting out, and the post 1930s world was one in which it was triumphant, in the same technological and energetic environment. We are now entering a crisis at a time when oil is its twilight years and there is thus an absolute need to renew the energy model. This fundamental difference between the current VSMC and the previous depression should dampen the enthusiasm for announcing the end of the crisis among all those who think that the progress of economic “science” means that a depression has been avoided and we are slowly coming to the end of an interlude of recession. The interlude is going to last very long time, because we cannot drive off as before and we will have to negotiate a complicated bend.

The difference with the Great Depression is striking. Let us take just two examples: in the 1940s and 1950s, agricultural foodstuffs were not produced very differently from in the 1930s (there were not yet any hybrid seeds), not including the ongoing development of automation; naturally there were improvements in the automobile industry, but the technology of locomotion was still the same, based on the piston engine. However, if we look 20 years ahead:

- it is probable that we will no longer grow the same plants (the process has already begun, despite significant reticence in Europe about the introduction of genetically-modified seeds). In the framework of biotechnological innovations, the range of plant health products will be

significantly smaller and the plant health sector will be extensively reorganised. This will be good for the health of users, the conservation of species and water resources (in quantitative terms if the new plants grown consume less water, and in qualitative terms if there is limited use of plant health products and nitrates). We are on the threshold of a new agricultural revolution: first there was crop rotation (in the 18th century), then hybrid seeds in the second half of the 20th century, and now there is biotechnology. Each has played a vital role in determining humankind's ability to manage demographic growth.

- it is also probable that we will still generally drive in our own cars over short and medium distances, without using petrol engines (at least in urban areas) and by developing the electric engine. This is a good thing both in terms of noise pollution and air quality. The continued use of those carbon-based energy sources that are still available, especially coal, will require the development of carbon capture techniques (the burial of CO₂), which will represent another important front in the necessary battle of technological innovation.

But how is this connected to the current crisis? People will say that this process of creative destruction would have taken place in any case: well yes, but it is going to be considerably faster. By violently casting consumer-citizens into uncertainty about their economic future, confronting them with a decrease in their purchasing power, and significantly reducing demand in the economy through debt reduction, the financial crisis, which began with subprimes, is a formidable driver of increased awareness among both consumers and producers about the shortcomings of our development model and the need to create, as rapidly as possible, the conditions for a socially-equitable, economically-viable and ideologically-healthy sustainable economic model. Consumers, confronted with the prospect of a lower purchasing power (during their working lives and even more so when in retirement) sense, in a confused way, that they can make no mistakes when purchasing their car or home: to start buying durable goods again, while controlling their debt, they must be sure they are being offered the latest technology, which saves energy and, quite simply, money. Producers will thus be confronted with the need to speed up the timetable for introducing innovations if they want to maintain demand, even if they have to see a decrease in the value of investments which they have not paid off, which in general they seek to avoid.

Keynes was the dominant economist at the end of the 1930s crisis, advocating demand-led economic policies to support growth. However, it is clear that he cannot help us understand the VSMC: while the crisis of the 1930s took place against a background of constant technological factors, the end of the current crisis can only come about if there is a technological break with the past. In such a situation, we should turn to Schumpeter² and his analysis of the creative destruction and the role of technological innovation. Where Keynes was the economist of crises with constant technological factors, Schumpeter should be seen as the economist of crises entailing a technological break with the past. It is not by digging holes to fill them up again (a way of paying wages and stimulating demand) or by having helicopters drop dollars from the sky as advocated by Bernanke that we will overcome the technological barrier of climate change, the depletion of non-renewable resources and the need to feed 9 billion people adequately in 2050.

The Very Serious Crisis is thus multidimensional *par excellence*, with its inextricably-linked economic, social, political and eco-systemic dimensions affecting every country in the world.

² Like Keynes, Schumpeter was born in 1883. This was also the year that Marx (the first great analyst of crises) died ... what a year for the history of economic thought!

After the period of stagnation which awaits in the short and medium-term (after a possible and yet-to-come violent purge), the real end of the economic crisis through the start of a new technological cycle is inseparable from the response to the food, energy and environmental challenges of humankind, which continues its demographic growth. Without such technological progress, each vague desire for a significant degree of economic recovery will come up against the barriers of food and energy: the increase in food and energy prices will lead to a decline in purchasing power, a reduction in demand for other goods and thus a spiral of recession. Each sign of recovery will contain the seeds of its own destruction within it. The real end of the crisis and start of a new long-term cycle will require a great leap past the food barrier via a biotechnological revolution, and past the oil barrier via energy conversion (renewable, nuclear, coal with carbon capture). Furthermore, these two barriers are not independent from one another, and are linked by the biofuel issue.

Finally, it must be accepted that the VSMC and the Great Depression of the 1930s are profoundly different, in their ultimate nature, their technological and economic profile, and the policies and theoretical references they require, as the table below attempts to summarise succinctly (and thus in no great detail):

The non-comparability between the Great Depression and VSMC

Criteria for comparison	The Great Depression of the 1930s	The VSMC ongoing since 2007
Profound nature of the crisis	<i>Crisis in the relationship between humans</i>	<i>Crisis in the relationship between humans, and the relationship between humans and nature</i>
Technological profile	<i>Crisis with constant technological factors</i>	<i>Crisis entailing a technological break with the past</i>
Economic profile	<i>Crisis of demand</i>	<i>Crisis of short-term demand + crisis of non-sustainable supply in the long term</i>
Policy for exiting the crisis	<i>Policy for recovery</i>	<i>Innovation policy</i>
Author of reference	<i>Keynes</i>	<i>Schumpeter</i>

Source: *De la nature de la crise* in Regnault H., Crisis Diary: August 2007 - November 2009, from Subprimes to the Illusion of Recovery (to be published in 2010).

2. The Future of Territories Depends on their Ability to Manage Creative Destruction

Those territories that incorporate creative destruction in their strategy thinking will end up victorious in VSMC and the others will be the losers.

As the definition of the word territory is relatively vague and subject to multiple variations, I will start by giving my own definition, which commits myself and nobody else, but I believe it is vital to build an intellectual bridge between the crisis and territories. **By territory, I thus mean a socialised and regulated area that can be appropriated by its inhabitants for themselves, can look to the future, develop strategies and allocate resources.** This is an economist's definition, in other words: if there is no budget, there is no territory! But it is also a profoundly political definition: if there is no freedom of movement, there is no territory either, because this is a minimal condition if its inhabitants are to appropriate it for themselves, thus enabling them to feel that it really is their territory.

Such a definition may be applied to areas of very different sizes, from the basic territorial administrative unit, which is a commune in France, to groups of countries accepting common rules and a minimum number of institutions with resources collected either directly or indirectly from individual people or legal entities which occupy or have a relationship with this area. Nations are clearly territories in this sense of the definition. Within nations, spatial subdivisions with their own budget (regions, departments and communes in France) are territories in the sense of my definition, even if doubts persist about whether resources are collected independently. As far as groups involving multiple nations are concerned, the European Union is a real territory, whereas NAFTA is not, nor is the Euro Mediterranean. Free trade agreements do not a territory make, as territories cannot just be concerned with facilitating trade relations, without pooling resources and ensuring the free movement of people. In contrast, as soon as there is a customs union, if customs' income is allocated to all the partners through an core institutional body, it is possible to start saying it is a territory if there is a minimum degree of freedom of movement, which is the vital condition enabling inhabitants to appropriate the space for themselves. However, aside from the European Union, it has to be accepted that there are few, if any, examples of multiple-nation territories. With no budget, NAFTA (even if it were a deep integration agreement) does not constitute a territory, as it lacks the power to collect and allocate resources. The Euromed zone, despite entailing financial transfers (MEDA and then neighbourhood policy) has no freedom of movement and cannot claim to be a territory either: as long as visas exist (and they are unlikely to disappear tomorrow!), the Euromed zone will not be territory but a juxtaposition of territories.

On the basis of this definition of the word territory, how can the relationship between a territory and the VSMC be broached? Some territories will emerge stronger, and others weaker. Three immediate questions arise, and I will try to give some initial answers, although these will be of a fairly general nature and it will be up to regional officials to apply them to the specific circumstances of their territories:

- 1. What criteria can be used to estimate the potential weakening or strengthening of a territory in the VSMC?**
- 2. To what extent might the current hierarchy of territories be called into question?**
- 3. What are the determining factors that can enhance a territory's position in face of the VSMC?**

There are two very different sorts of criteria that can be used to estimate the potential weakening or strengthening of a territory:

- the ability to maintain the territory's social cohesion, naturally as an end in itself, but also as a tool for civil peacekeeping, without which there can be no protection of human life and the right to property and thus attractiveness for investment, whether this be local, national or foreign. Possible failures will be very disabling for territories that face them.

- the capacity to incorporate new technologies, as part of a dual thrust towards creation (with highly-skilled jobs, patents and the associated profits from innovation) and/or large-scale application and implementation (with the resulting jobs).

The debate on **the extent to which the current hierarchy of territories might be called into question** boils down to thinking about the degree of inertia in hierarchies and the conditions for their disruption. As a general rule, inertia triumphs over disruption, because the positions acquired give all the advantages that are essential for the pursuit of progress: wealth goes to the rich and poverty persists. Nevertheless, in times of marked technological breaks with the past, and we are entering such a period, disruption can triumph over inertia: territories which fail to enter the new technological environment can rapidly drop down in the hierarchy. In the 1970s and 1980s, in the iron and steel industry (with the move to continuous casting) and clock making (with the move to electronics), we saw that barriers to entry (which are supposed to protect old members of the industry against new competitors) could be upturned, trapping the former in investments they had not paid off while the latter enjoyed optimal production conditions: European territories still bear the scars of this period, and it would be just as well not to start again! So care must be given to avoid missing the biotechnological revolution and energy conversion.

Lastly, let us say a few words about **the determining factors that can enhance a territory's position in face of the VSMC**. To manage creative destruction, territories have limited and even very limited quantities of resources. Keynesian policies adopted since the start of the collapse of global financial system have led to high levels of government debt, which is of course preferable to household debt but does have its limits if we want to avoid seeing multiple defaults on sovereign debt. It can thus only be expected that there will be significant tensions regarding territorial budgets and the need for increasingly selective targeting of expenditure. It will be even more important to avoid making mistakes when allocating funds, as resources are hard to find and the issues are decisive. I think that one imperative rule seems obvious: we must accompany decline without seeking to resist it, and go fully with the flow and if possible precede it.

The golden rule in the territorial management of the VSMC in face of creative destruction might be explained in the following way: let us accompany destruction by helping the people involved in activities³ that are in decline but not by helping these activities themselves; let us stimulate creation by fostering the emergence and dissemination of new technologies through research, training and support for R&D in emerging activities.

³ I use the word activity rather than sector intentionally. No sector is totally condemned to fail, as long as it meets certain human needs. However, certain ways of producing, with given inputs and using a combination of technology/capital/work (which I call activity), may be condemned entirely or in particular territories. The automobile sector is not condemned per se, but the activity which consists in producing heavy vehicles with petrol engines does not have a great future (even independently of income levels). On the other hand, lighter cars with electric engines have a promising future in urban areas.

However, it has to be acknowledged that territorial officials will face an awful dilemma: how can we strike a balance between support for people in activities of the past and support for the emergence of activities of the future? Confronted with such a responsibility in face of the future of their territories, I can only wish territorial officials much courage and good luck. They will no doubt rarely have had to cope with such a crucial issue, because one thing is clear: at the end of the VSMC, in 15 to 20 years' time, there will be winning territories and losing territories. Without yet being able to name the winners and losers, it can nevertheless be said that:

- **the winners will be Schumpeterian innovating territories;**
- **the losers will be Keynesian⁴ territories that pursue recovery.**

Henri Regnault
Pau, 9 December 2009

⁴ To avoid any misunderstanding, as far as the crisis we are going through is concerned, I am neither Keynesian nor anti-Keynesian : I am a-Keynesian in the sense that Keynes does not offer me the essential analytical structure I need in order to imagine possible future scenarios. However, I could again become a Keynesian in the analysis of a classical short-term crisis and recommend the use of automatic stabilisers and a recovery plan to support demand: but this is not what concerns us at the moment, as it is more important to refocus supply than to stimulate demand.