

## Jean-Baptiste Hollande

Francesco Saraceno, January 15, 2014

*Le temps est venu de régler le principal problème de la France : sa production. Oui, je dis bien sa production. Il nous faut produire plus, il nous faut produire mieux. C'est donc sur l'offre qu'il faut agir. Sur l'offre ! Ce n'est pas contradictoire avec la demande. L'offre crée même la demande.* François Hollande – January 14, 2014

France is often pointed to as the “sick man of Europe”. Low growth, public finances in distress, increasing problems of competitiveness, a structural inability to reform its over-regulated economy. Reforms that, it goes without saying, would open the way to a new era of growth, productivity and affluence.

François Hollande has tackled the second half of his mandate subscribing to this view. In the third press conference since he became President, he outlined the main lines of intervention to revive the French economy, most notably a sharp reduction of social contributions for French firms (around € 30bn before 2017), financed by yet unspecified reductions in public spending. During the press conference, he justified this decision on the ground that growth will resume once firms start producing more. Thus, he tells us, “*It is upon supply that we need to act. On supply! This is not contradictory with demand. Supply actually creates demand*”. Hmm, let me think. Supply creates demand. Where did I read this?

From the time of Say and Ricardo the classical economists have taught that supply creates its own demand; meaning by this in some significant, but not clearly defined, sense that the whole of the costs of production must necessarily be spent in the aggregate, directly or indirectly, on purchasing the product. In J. S. Mill's *Principles of Political Economy* the doctrine is expressly set forth: “What constitutes the means of payment for commodities is simply commodities. Each person's means of paying for the productions of other people consist of those which he himself possesses. All sellers are inevitably, and by the meaning of the word, buyers. Could we suddenly double the productive powers of the country, we should double the supply of commodities in every market; but we should, by the same stroke, double the purchasing power. **Everybody would bring a double demand as well as supply; everybody would be able to buy twice as much, because every one would have twice as much to offer in exchange**”. [*Principles of Political Economy*, Book III, Chap. xiv. § 2.]

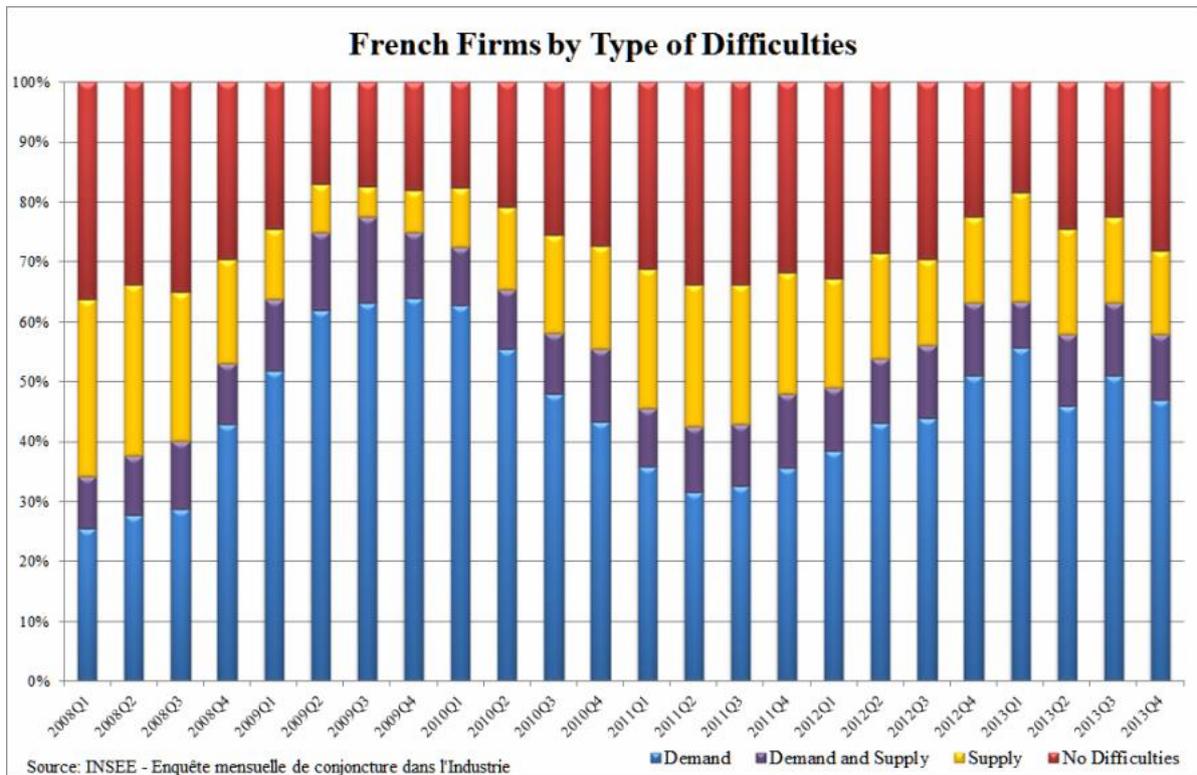
Yes, this is chapter two of Keynes' *General Theory* (bold is mine), where he famously challenges the (neo)classical view that price changes can generate demand capable of absorbing any level of supply.

So Hollande seems to embrace the view of his compatriot [Jean-Baptiste Say](#) that to boost growth and well-being one needs only to care about creating optimal condition for production and supply, and that demand will follow.

The theoretical discussion between neoclassical and Keynesian economists fed most of the debate in macroeconomics since the *General Theory* was published, in 1936. And I do not intend to open that Pandora box here. What I would like to assess is whether François Hollande is right in arguing that by lowering the tax burden of firms these will resume investing and hiring, thus triggering growth and prosperity.

Luckily, there is an almost straightforward way to assess Hollande's claim., thanks to an interesting quarterly survey conducted by the French Statistical Office, Insee, on [economic conditions faced by firms](#). The survey is conducted since 1991, and surveyed firms are asked to assess their situation along a number of dimensions, including the type of

difficulties they face (if any). In particular, they are asked whether their difficulties can be imputed to demand or to supply factors. And here is the result:



A number of interesting facts emerges in my opinion: First, the blue line, the number of firms facing demand problems, closely tracks the developments of the crisis: a peak in 2008-2009 along the global financial crisis, a strong improvement in 2010, and then a double-dip coinciding with the sovereign debt eurozone woes. The message seems to be clear: since the beginning of the crisis the trouble for French firms came from insufficient demand. Keynes: right; Say (and François Hollande, and the Commission, and Angela Merkel): wrong. The second interesting fact is that the ratio of firms claiming they have only supply problems (yellow) or both (purple), remains broadly unchanged along these cyclical movements. Firms move from demand difficulties to no difficulties and back, but in the past six years they did not substantially change opinion on red tape, regulation, labour costs. This means that Hollande's measures are not likely to drastically change the mood among French firms. The recovery will only come when demand resumes. Once again, Keynes: right, Hollande and the gang: wrong. Incidentally, this picture is confirmed if we take the longer series: just look at this table:

<b>French Firms by Type of Difficulties</b>		
<b>Period Averages</b>		
	<i>1991-2007</i>	<i>2008-2013</i>
Demand	44.2	45.4
Demand and Supply	6.9	11.0
Supply	20.6	17.1
No Difficulties	28.4	26.7
<i>Source: Enquête mensuelle de conjoncture dans l'Industrie</i>		

The number of firms facing supply difficulties alone or no difficulties shrank since 2008, and those facing demand difficulties (alone or together with supply) increased substantially. Does this mean that all is well in France? Of course not. The burden on French firms, and in particular the tax wedge, is a problem for their competitiveness. Finding ways to reduce it, *in principle* is a good thing. The problem is the sequencing and the priorities. French firms seem to agree with me that the top priority today is to restart demand, and that doing this “will create its own supply”. Otherwise, more competitive French firms in a context of stagnating aggregate demand will only be able to export. An adoption of the German model ten years late. I already said a few times that [sequencing in reforms is almost as important as the type of reforms implemented](#).

I am sure Hollande could do better than this...