Preface to the English edition

This is a translation of a book that was originally published in France in 2002. It examines the driving forces behind growth during the previous decade, paying particular attention to the strengths and weaknesses of the ‘new economy’. How has the ‘new economy’ become old? In retrospect, what is the future of economic growth? These are two questions that this book addresses. The Anglophone reader may well question the relevance of such a book. What can a French researcher contribute to the analysis of a phenomenon which primarily took place in the USA? Why dwell on the concept of a ‘new economy’ that many people now consider to be a thing of the past? Do not a number of events that have taken place since the publication of this book in French invalidate some of its findings? These are questions to which this Preface seeks to respond.

THE ILLUSIONS OF THE ‘NEW ECONOMY’ MAY RE-EMERGE

One of the aims of this book is methodological and focuses on whether economists learn from their mistakes. During the late 1980s and subsequently, many economists became convinced by the emergence of a new growth regime, one driven by information technology. The drastic increase in share prices which took place at this time was seen to herald future growth patterns and future profits in the ICT-producing sector. The numerous adverse signals to the effect that this was a typical financial bubble that would eventually burst served little purpose. Such signals included massive capital investment in loss-making firms possessing little or no business experience; dramatic surges in share prices; and a reluctance on the part of public watchdogs to exercise their powers.

One of the fundamental messages of this book hinges on a paradox: in an era supposedly dedicated to the rationality of entrepreneurial and financial strategies and to maximizing shareholder value, the actions undertaken by the financial community and by investors were in fact governed by blind faith and by the tendency to mimic others. The shift in stock market prices, indeed, was so complete that in some cases many people no longer showed any regard for macroeconomic constraints or for long-established principles of business management.
At the root of the collective errors of judgment which resulted in so much capital loss was the lack of time available for actors to step back and take stock of events. People believed that what was a new phenomenon for them and their contemporaries had no connection to long-term trends and international history. In reality, the dot.com fever was part of a long succession of speculative periods brought into being by a supposedly radical innovation. The short-term horizon of finance is not the long-term one of technological innovation. We also need to ask how it was that sensible members of the financial community came to be convinced by promises of large and constant increases in profits without giving serious consideration to the uncertainties that mark all economic activity. Even before the collapse of Enron, suspicions about dubious accounting methods were widespread. How is it possible that a large community consisting of trained and experienced professionals could turn its back on its own teachings? In part, the explanation comes down to a lack of historical and comparative understanding. Would not such understanding have been the best antidote to an over-zealous prediction of a historical break from the past? The fact is analysts simply failed to put the ‘new economy’ into its larger framework and context.

This book will have achieved its aim if it successfully encourages the reader to critically reconsider periods in which seemingly typical economic rationality gave way to blind faith, and resulted in instability and later on crashes. History during the course of the last three centuries is rife with examples of this type. Clearly, today’s actors are in danger of repeating the mistakes of their predecessors if they do not actively seek to learn from this history.

THE SEDUCTIVE AND DANGEROUS NATURE OF TECHNOCLOGICAL DETERMINISM

Fundamental to the belief in the ‘new economy’ was a vision which reflected technological determinism. Many actors sincerely believed that technological breakthroughs in information processing and dissemination would lead to more efficient production methods and to product innovation, and that all of this would send profits soaring. However, the economics of technical change has long taught us that all innovations initially thought to herald the beginning of a new era do not result in viable ventures, nor sectors that are sufficiently important to generate growth at the macroeconomic level.

It is now apparent that computerization went through its formative stages at the end of the Second World War. Microelectronics, consequently, is simply an extension of a long-run trend which seeks to facilitate information processing within firms. That is why the financial gains achieved by such innovations did
not reach their expected levels. As will be discussed in Chapter 7, ICTs are generic technologies inasmuch as they can be successfully disseminated through a wide range of business activities and sectors, yet they do not themselves constitute a radical innovation capable of creating a whole sector and increasing productivity and profits across entire economies.

This book provides the reader with a series of analyses that demonstrates the inadequacy of arguments of a technologically determinist kind. To elaborate, electronic markets cannot operate without a specific set of rules, conventions and institutions ensuring their viability. Easy transmission of information is merely one of the material requisites for electronic business, not its unique condition. This point is all the more important when we realize that some technologies now considered to be outdated can actually be more efficient than more recent, and expensive, ones. This explains the widespread difficulties encountered regarding the measure of productivity of informational hardware and software capital. To assume, as does the methodology of growth accounting, that the productivity of informational capital is measured by the price of equipment ignores the costs involved in reorganizing the flow of production as well as the informational and decision-making structures needed if the full benefits of ICT are to be achieved.

Down with technological determinism then! This is one of the main themes running through this book.

**THE UNSUNG SUCCESS OF CERTAIN EUROPEAN COUNTRIES**

Most research into the ‘new economy’ has focused on the USA during the 1980s and the outstanding performances it clocked up in terms of growth and employment. Consequently, the institutions of a market-led capitalism that followed the US model were considered essential if a growth regime driven by information technology was to be achieved. Certain countries which lagged behind chose to create new financial markets in order to fund young, start-up firms. Such markets favoured stock options as incentive mechanisms, and in some cases even sought a relaxation of workers’ social rights in order to facilitate greater flexibility in employment adjustments, work schedules and pay. This one economic model led people to believe that the greater the adoption of typical institutions of market-led capitalism, the better a country’s macroeconomic performances would be.

A paradox lies in the fact that the comparative data compiled to support this view highlights at least two additional institutional configurations which underpin good macroeconomic performances. The first can be found in Finland,
Sweden and Denmark where the high quality and large democratization of education and training have considerably facilitated the implementation of ICT and helped shape production in at least some of these social-democratic countries. The institutional infrastructures of these nations are very different from those prevailing in the United States, yet their results are as good as, or even better than, the latter’s, the reason being that total productivity factors result in high growth and low unemployment. It is therefore possible to achieve economic efficiency at the same time as maintaining social solidarity. This is a very different configuration from the United States where social inequalities are large. The second configuration exists in those countries which lag behind. Such nations can benefit from internationalization and from the possibilities created by ICT by forging institutional perspectives compatible with the new environment. They are not hindered by the inertia engendered by the adhesion to a previous successful growth model. Ireland, and to a lesser extent Portugal, occupy this category.

These three different models have managed to coexist for a long period of time because the resilient institutional architecture on which they are built lies at the heart of their competitiveness. Herein we find the third of the book’s messages: this is that in an age of internationalization a large variety of capitalisms exists.

FINANCIALIZATION AND ITS DANGERS

This book insists that the synergy between new financial instruments and technological innovations is the factor explaining the rapid expansion and subsequent collapse of the Internet bubble. The financial community’s readiness to endorse the ‘new economy’ was largely responsible for US macroeconomic trends during the latter half of the 1990s. Indeed, without the enormous elasticity of supply of capital, the ICT sector would never have experienced its massive surge, nor its later devastating crash. Since the start of 2000 a number of events have served to emphasize the role played by financial innovation and by the new instruments it has created. The quest for higher financial gains, along with increased risk-taking and speculation, have affected most sectors of the economy. The fatalities of Enron, Tyco, Worldcom and other distribution companies demonstrate, however, how greed and the lure of managers’ gains served to govern company behaviour over and above efficient management of corporate assets and competencies. Experience has shown with regard to the stock option mechanism, for example, that far from harmonizing the objectives of managers and shareholders, it actually serves to encourage creative accounting and the misrepresentation of financial results. The same applies to the numerous mega-mergers, acquisitions and alliances based on the ‘big is
beautiful’ motto that became so fashionable during the 1990s. We have since realized that in the majority of cases such operations had detrimental, rather than positive, effects on the value of businesses. Financial logic clearly triumphed over rigorous analyses of complementarities and synergies between industrial activities and services.

Farewell then to the transparency that good governance and incentives such as stock options were supposed to produce. The US crisis that started with the bursting of the Internet bubble in March 2000 allowed for a double evaluation of the emergent growth regime. Firstly, it revealed that financial impatience stood in the way of a smooth development of technological innovation, something which normally takes place over decades. (This is another reason for demystifying the illusion of short-term technological determinism.) Secondly, it highlighted the instability peculiar to financial markets resulting precisely from their depth and liquidity. A growth regime led by finance is not only unlikely to correspond to the configuration of non-US economies, but is likely to endogenously spark further crises.

Events that have taken place since the publication of this book in France have confirmed the diagnosis that was then only implicit: namely that the 1990s were more about finance than about an information and real growth economy.

THE PROSPECTS FOR AN ANTHROPOGENETIC GROWTH MODEL

One might initially be led to believe that the main purpose of this book is to indulge in criticism. The suggestions made in the final chapters demonstrate otherwise. They indicate that the next growth regime could centre on education, training, health, leisure activities and urban planning. This view is based on an analysis of long-term changes in US household expenditures. On the one hand, the proportion of durable manufactured goods in relation to total consumption has stabilized owing to the relative fall in prices which spurred demand for mobile phones, microcomputers and other electronic goods. On the other hand, because apparent productivity gains are not observed in the service sector, particularly within areas of education and health, households have had to spend an increasingly larger percentage of their budgets as a means of satisfying their needs. This phenomenon is all too apparent from the viewpoint of the financial difficulties involved in social security cover and public budgets which regrettably overshadow the significance of a model based on human capital (to borrow the language of neo-classical theory). It would be more accurate, however, to describe the phenomenon as one that requires ‘the production of humans by humans’ and in the process to prolong and actually reverse the classical
approach that viewed the economy as the process of producing commodities by commodities. In more analytical terms, we could describe the challenge facing contemporary economics as being an anthropogenetic one.

We perceive the importance of such a model on a daily basis, if only by default. Virtually every month we hear about the misreporting and financial troubles of firms belonging to the ‘new economy’. By contrast, governments in almost every country are currently seeking to curb increases in health and pension expenditures by, for example, introducing reduced access to healthcare in those areas where provision and funding mostly rest in public hands. Hence the strikes by medical personnel and the moves of the North to import specialists from countries in the South as a means of compensating for staff shortages. One would be hard pushed to find a better homage to the anthropogenetic model, although it is currently seen – alas – in terms of costs rather than benefits. This book calls for some sort of response to its in-depth analysis from civil servants who seem more concerned with budgetary equilibrium than with meeting emergent social needs, particularly in areas pertaining to health and education.

Beyond information technology lies knowledge economics, a concept which international institutions, such as OECD and World Bank, are only now beginning to take seriously. This, however, is merely part of a much wider development involving ‘the production of humans by humans’.

I very much hope that readers of this book will find sufficient food for thought about contemporary developments, far away from the succession of fads that often obscure, rather than illuminate, social discussions. It will be left to the reader to decide whether the book successfully achieves what it sets out to do: that is, to make its song heard above the great cacophony of the ‘new economy’ and to bring some incisive and original analysis to what has effectively been ‘la grande illusion’.