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New Economic Thinking

THE GLOBAL ECONOMY: SECULAR STAGNATION OR RECOVERY AT LAST?

Adair Turner

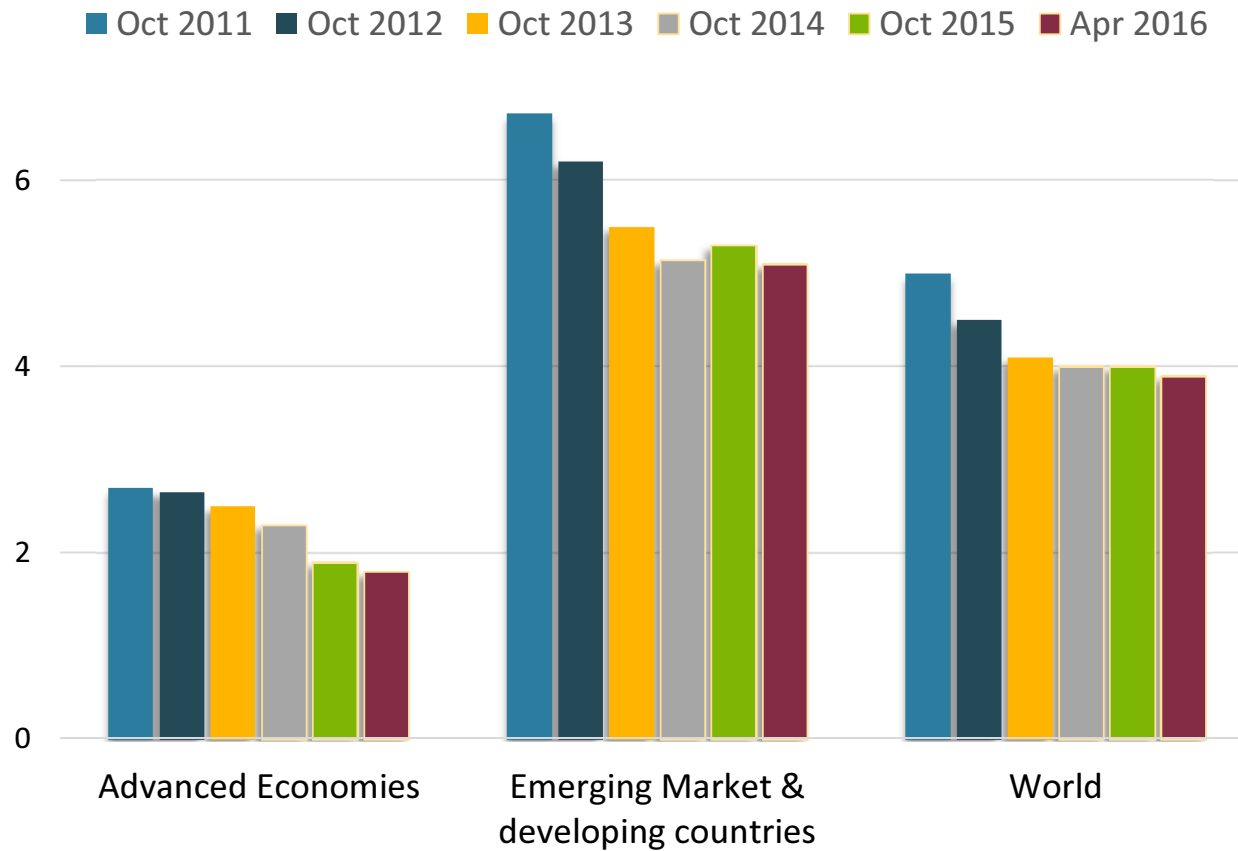
Chairman

Institute for New Economic Thinking

Institutional Money Kongress

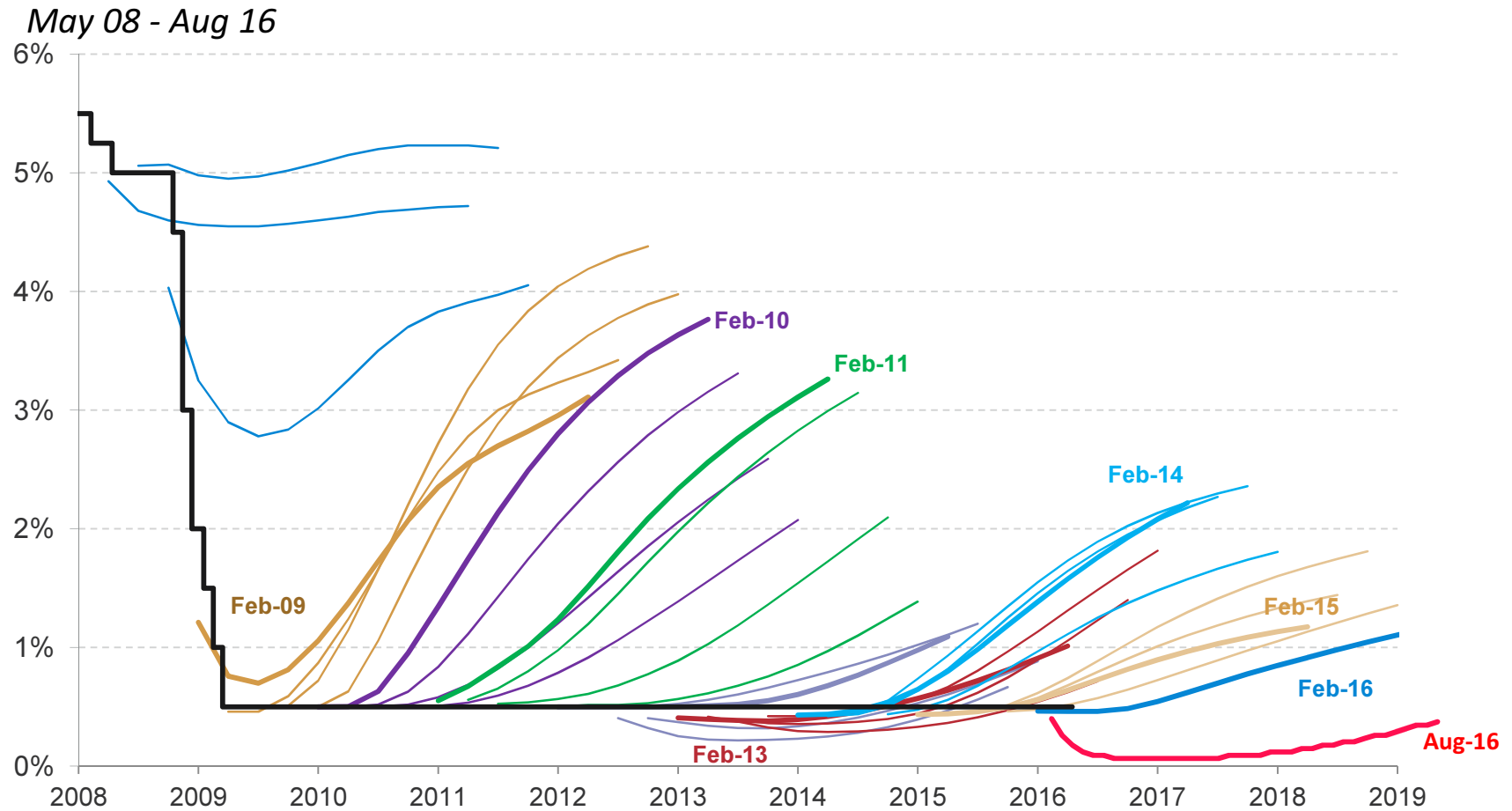
Frankfurt, 21 February 2017

IMF Medium term growth projections



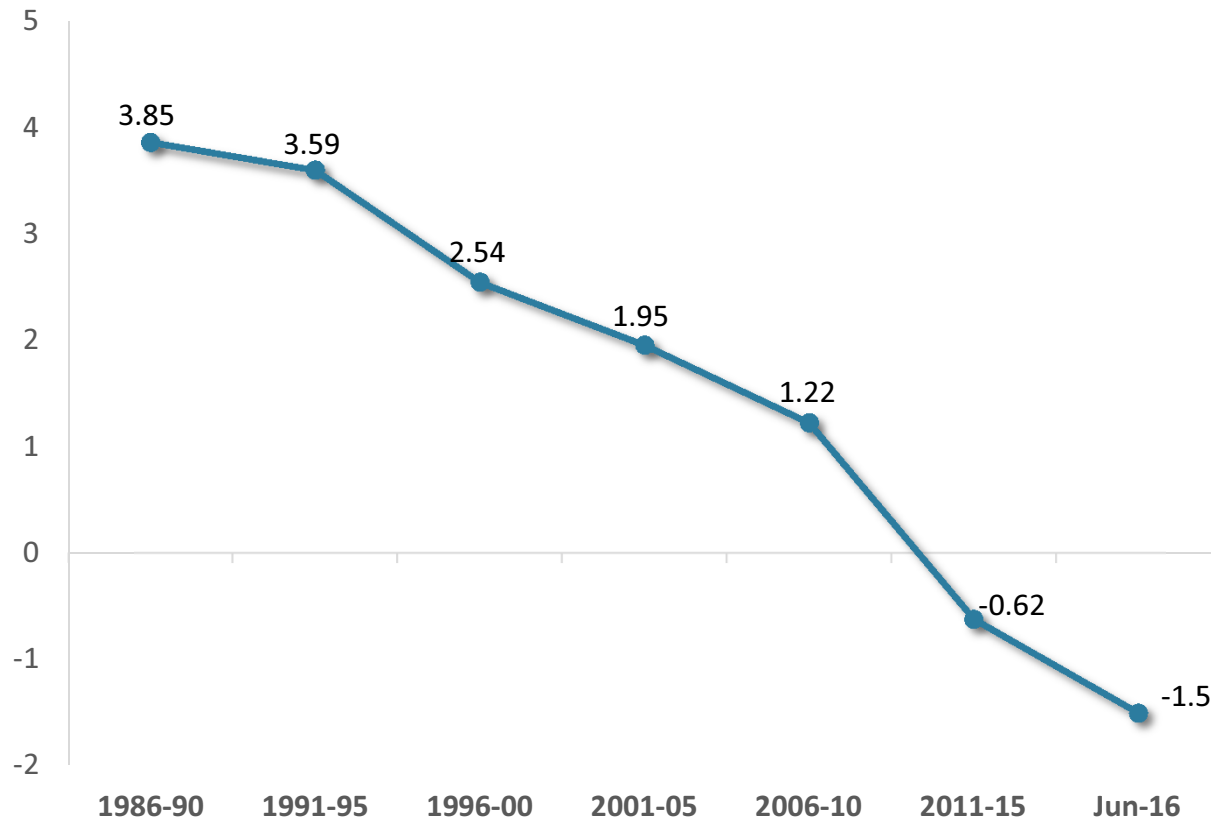
Source: Data for 2011-2013 from the IMF World Economic Outlook, April 2014, Figure3.1. Data from 2014-2016 are the furthest year out forecast annual growth from relevant IMF WEO

Successive market forecasts of BoFE interest rates



Source: Resolution Foundation and Bank of England Inflation Report, August 2016

Sterling 10 year index-linked gilt: YTM 1985 – 2016



Source: Bank of England Statistics



**INTERNATIONAL
MONETARY FUND**

World Economic Outlook

Update
JANUARY 2016

**WORLD ECONOMIC OUTLOOK (WEO)
UPDATE**

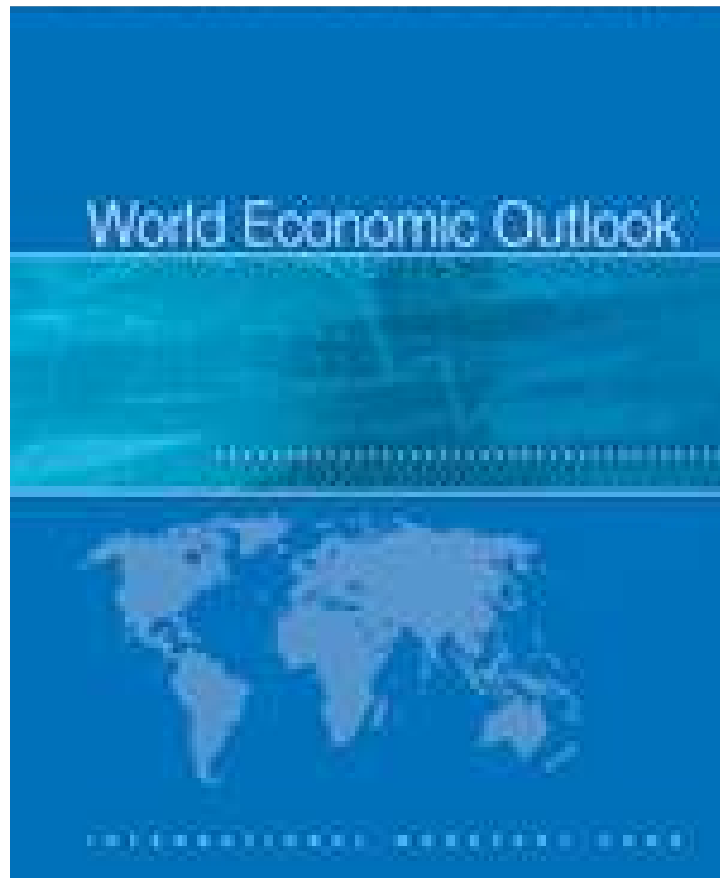
**Subdued Demand,
Diminished Prospects**

January 2016



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WORLD ECONOMIC OUTLOOK (WEO)

**Subdued Demand,
Symptoms and Remedies**

October 2016

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What has changed?

The view from the Bank of England

“Long-term interest rates have risen globally (Chart 1.1)”

“Survey indicators of global growth have picked up (Chart 1.2)”

“Inflation in advanced economies has picked up (Table 1.B)”

“Market-implied paths for short-term interest rates have risen internationally (Chart 1.3)”

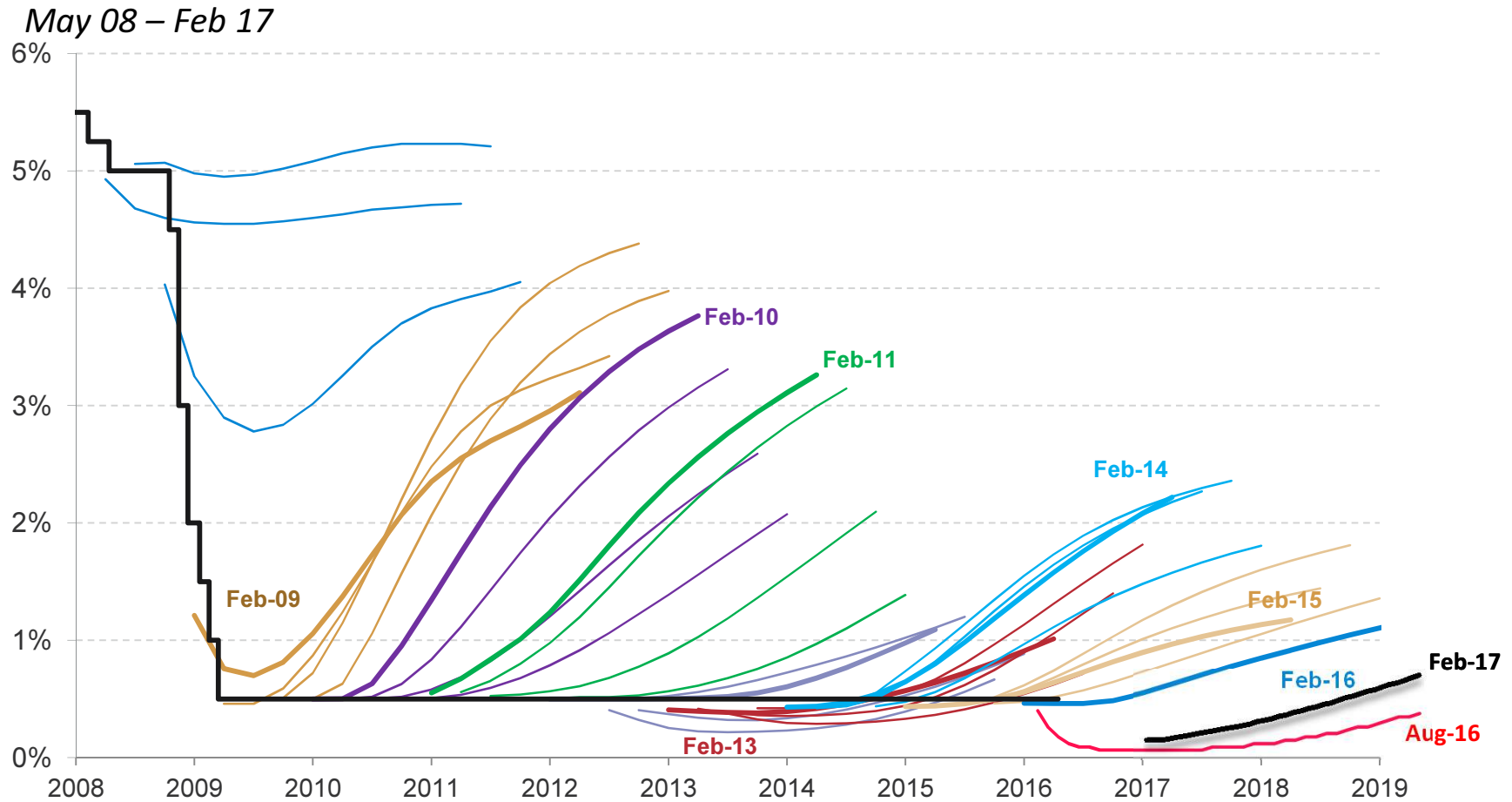
“Equity prices in advanced economies have risen (Chart 1.5)”

“Long-term implied future inflation rates have picked up in the United States and Germany (Chart 1.7)”

“Measures of confidence have increased sharply in the euro area and United States (Chart 1.8)”

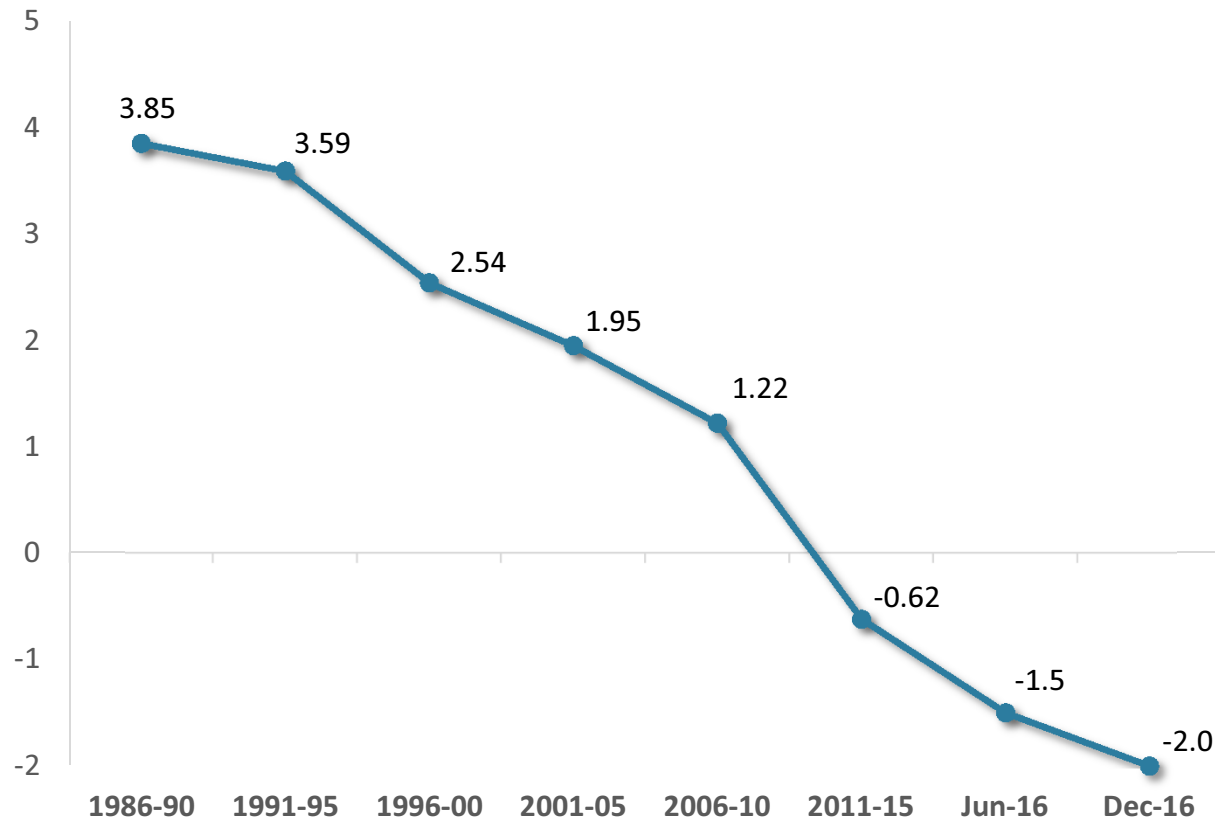
Source: Bank of England Inflation Report February 2017, Section 1, Financial Markets and Global Economic Developments

Successive market forecasts of BofE interest rates



Source: Resolution Foundation and Bank of England Inflation Report, August 2016

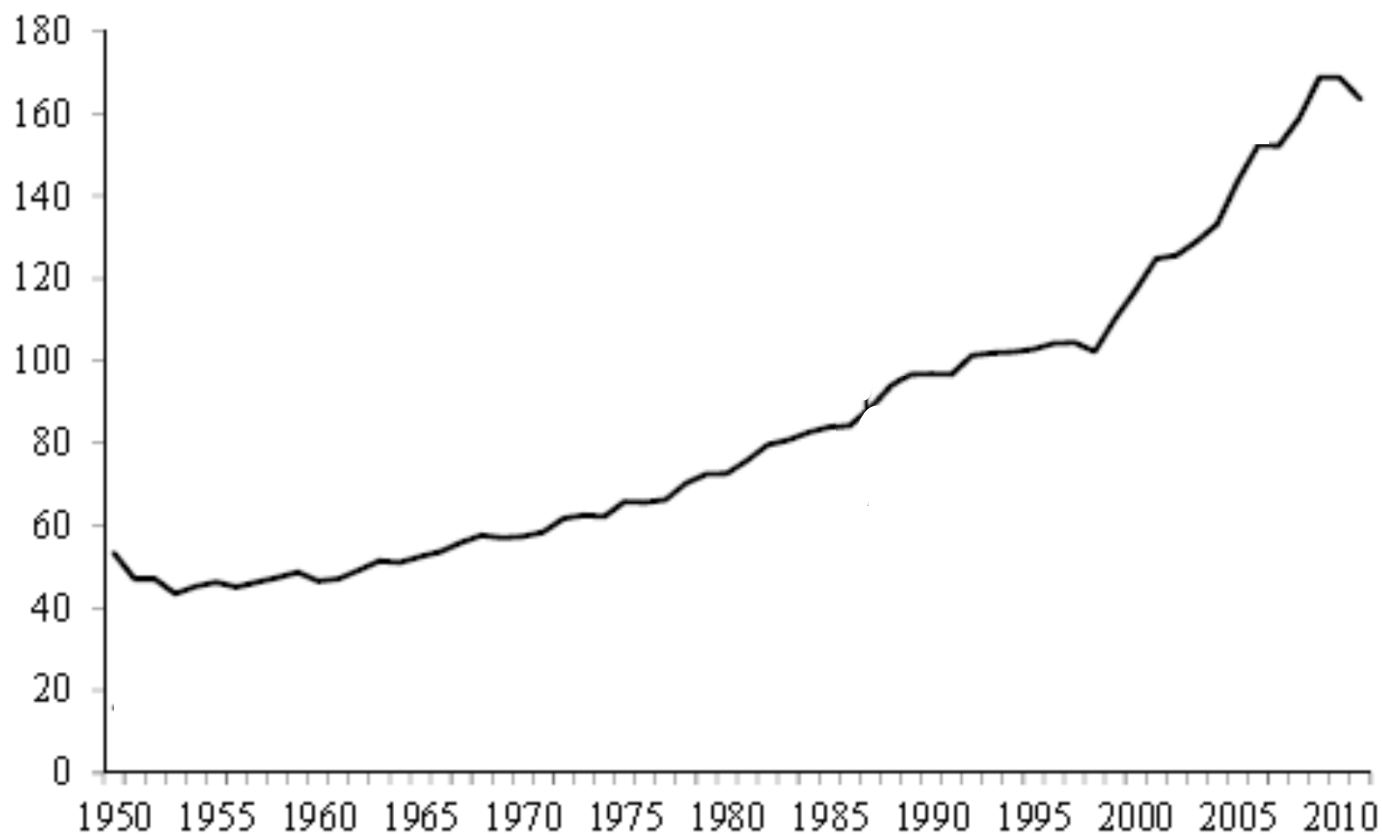
What has not changed : Sterling 10 year index-linked gilt: YTM 1985 – 2016



Source: Bank of England Statistics

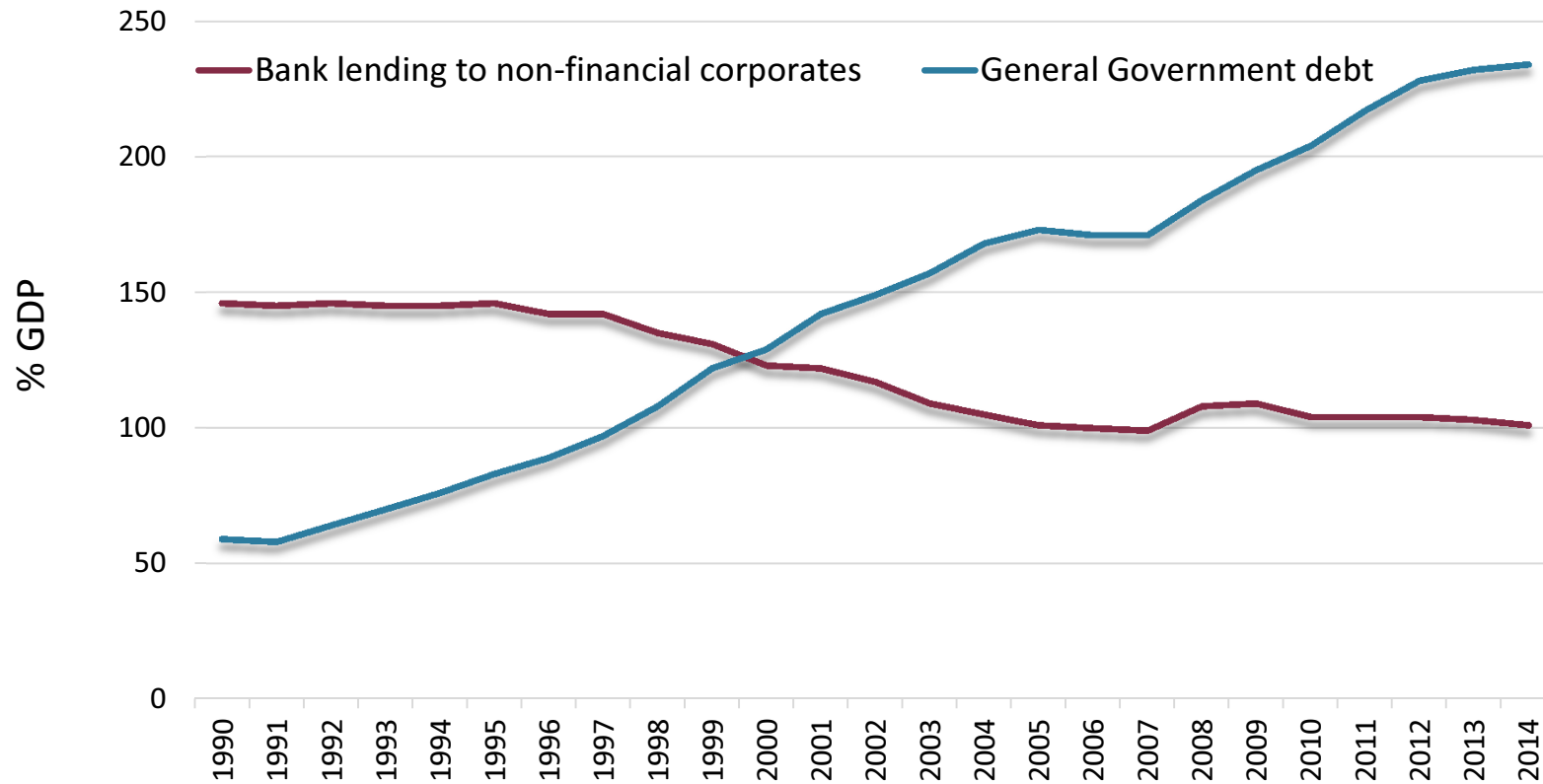
- ❖ Debt overhang
- ❖ Secular Stagnation
- ❖ What will happen now?

Private domestic credit as a % of GDP: Advanced economies 1950 – 2011



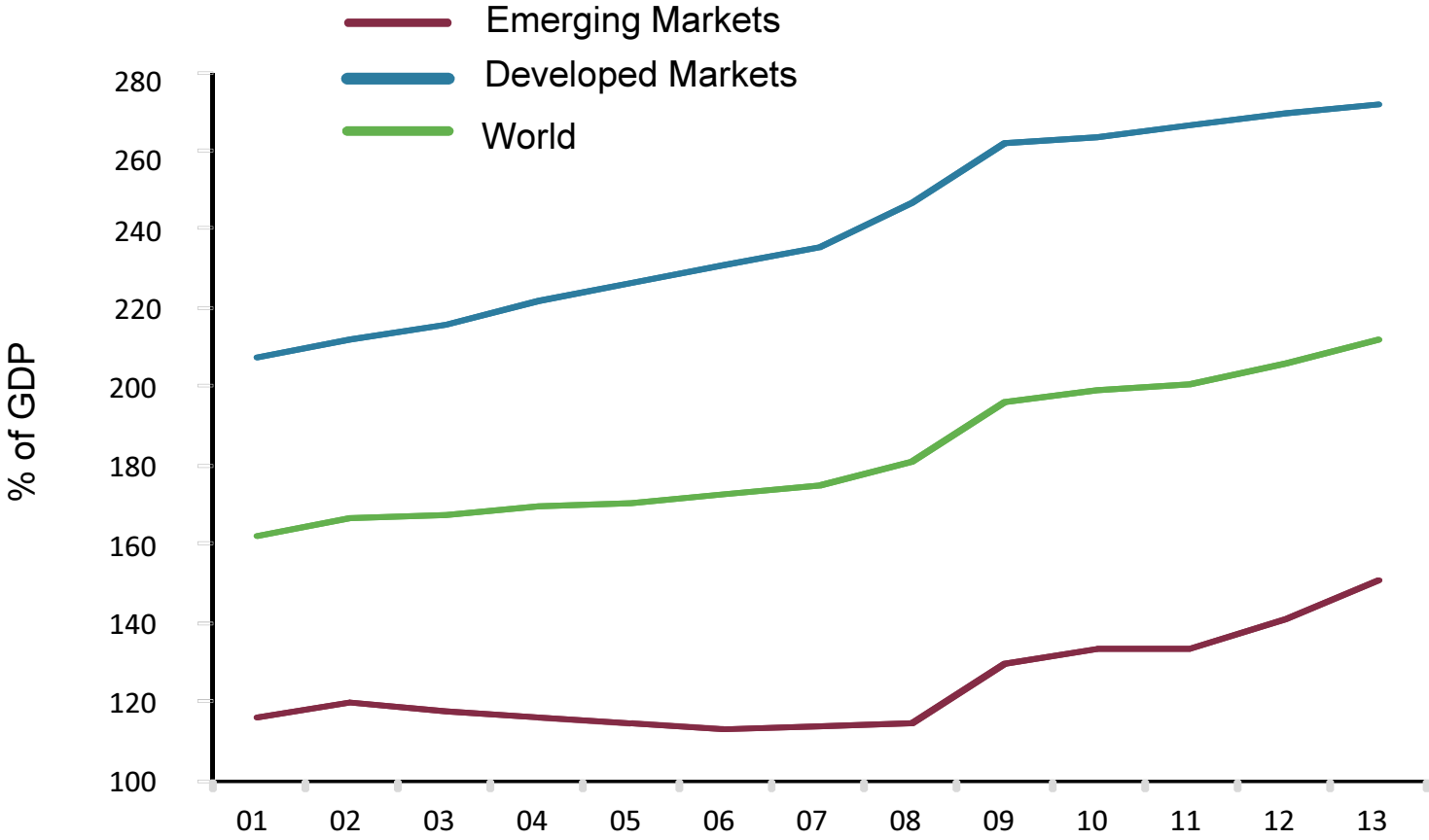
Source: *Financial and Sovereign Debt Crises: Some Lessons Learned and Those Forgotten*, C. Reinhart & K. Rogoff, 2013

Japanese government and corporate debt: 1990 – 2010



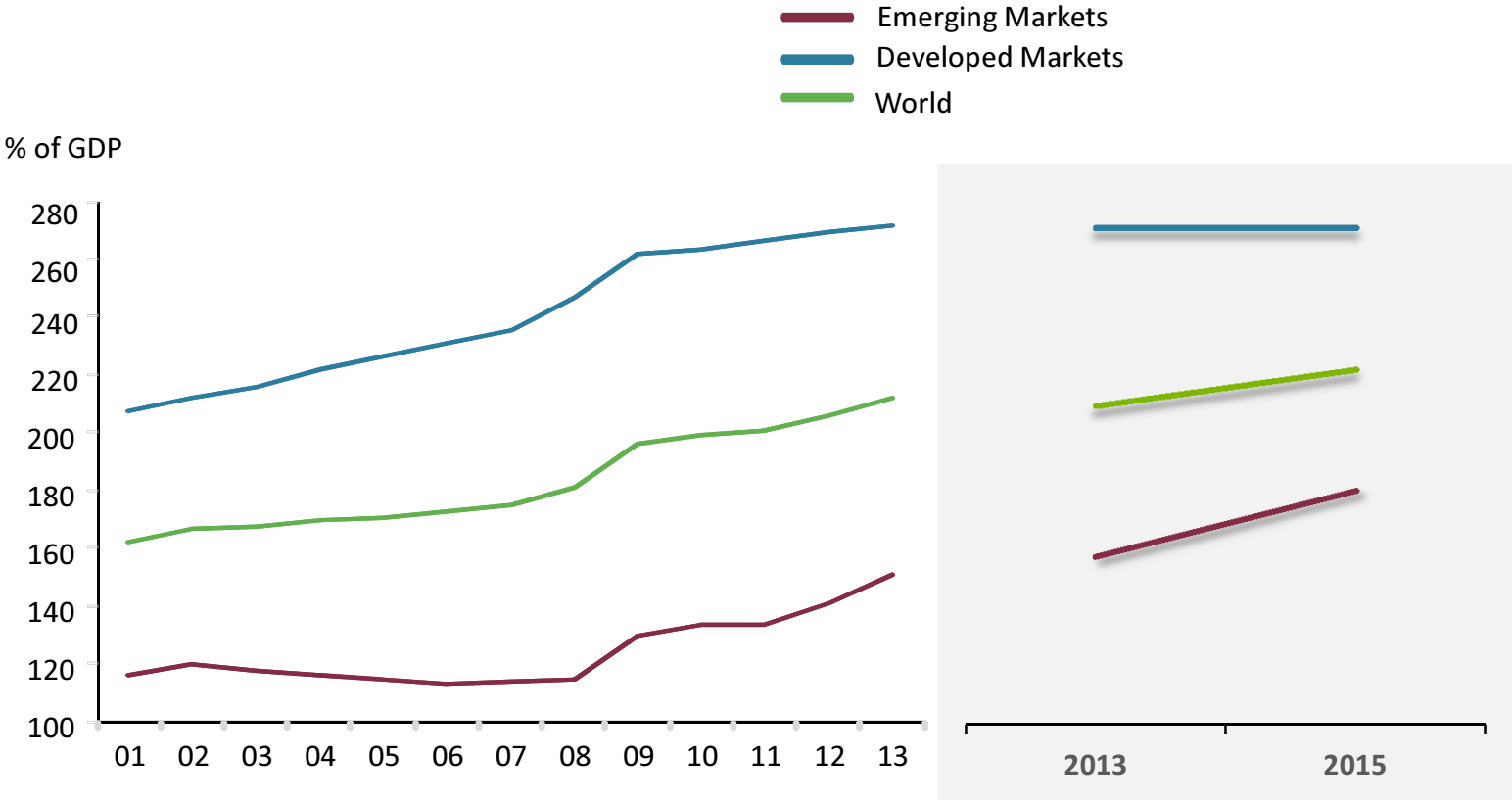
Source: BoJ Flow of Funds Accounts, IMF WEO database (April 2011), FSA calculations

Global debt excluding financials



Source: Geneva Report No 16 *Deleveraging, What Deleveraging?* ICMB / CEPR September 2014

Global debt excluding financials



Source: Geneva Report No 16 *Deleveraging, What Deleveraging?* ICMB / CEPR September 2014 for years 2001 to 2013

Source: BIS for years 2013 and 2015

Traditional policy levers blocked

Debt-financed fiscal deficits

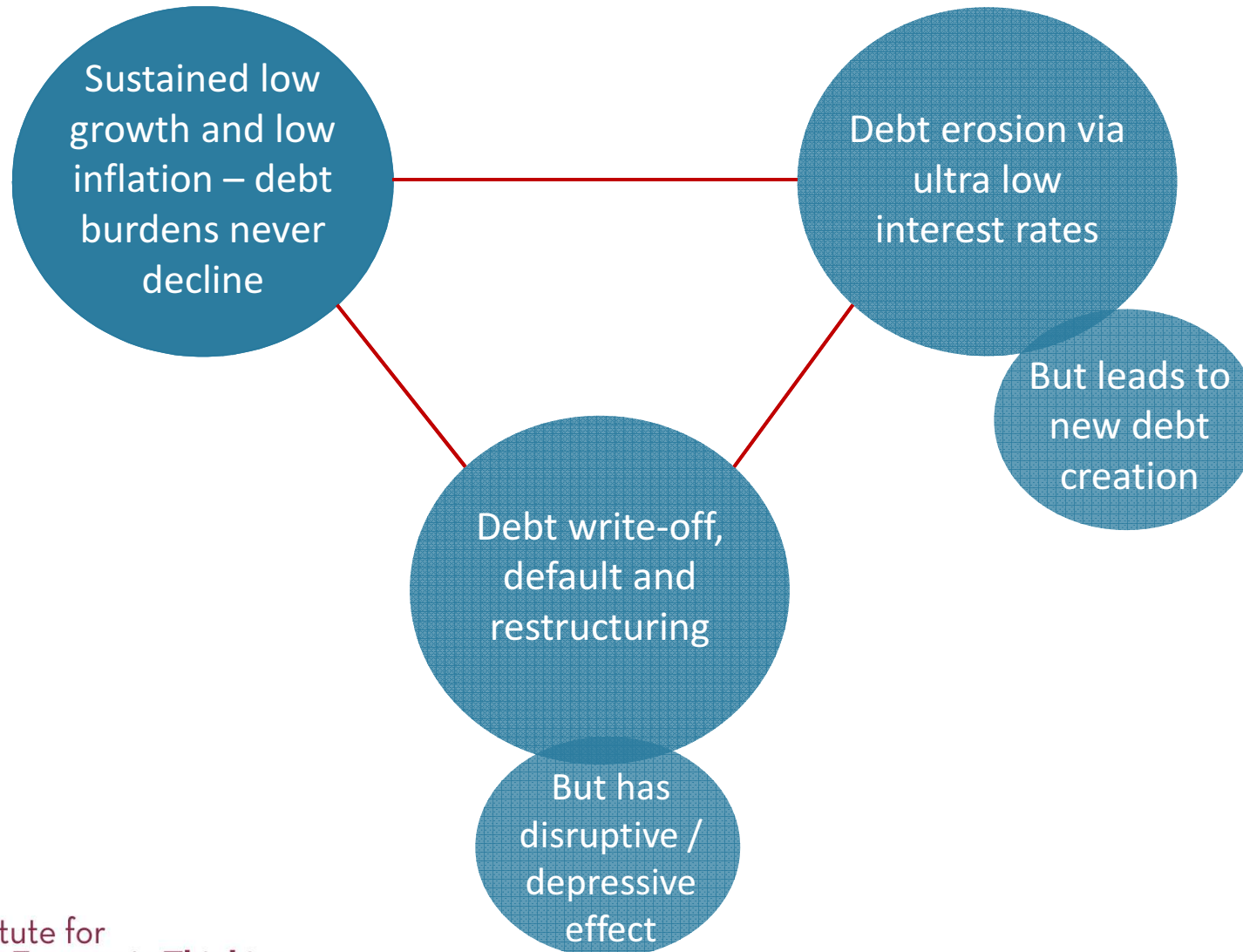
- First round stimulative effect
- But concerns about long-term debt sustainability

Ultra loose monetary policy

- Interest rate at zero bound
- QE

- Imperfect transmission to real economy investment and consumption
- Asset prices → inequality
- Currency devaluation channel is zero sum game
- Only works by re-stimulating growth of private credit

Debt overhang : the unavoidable choice?

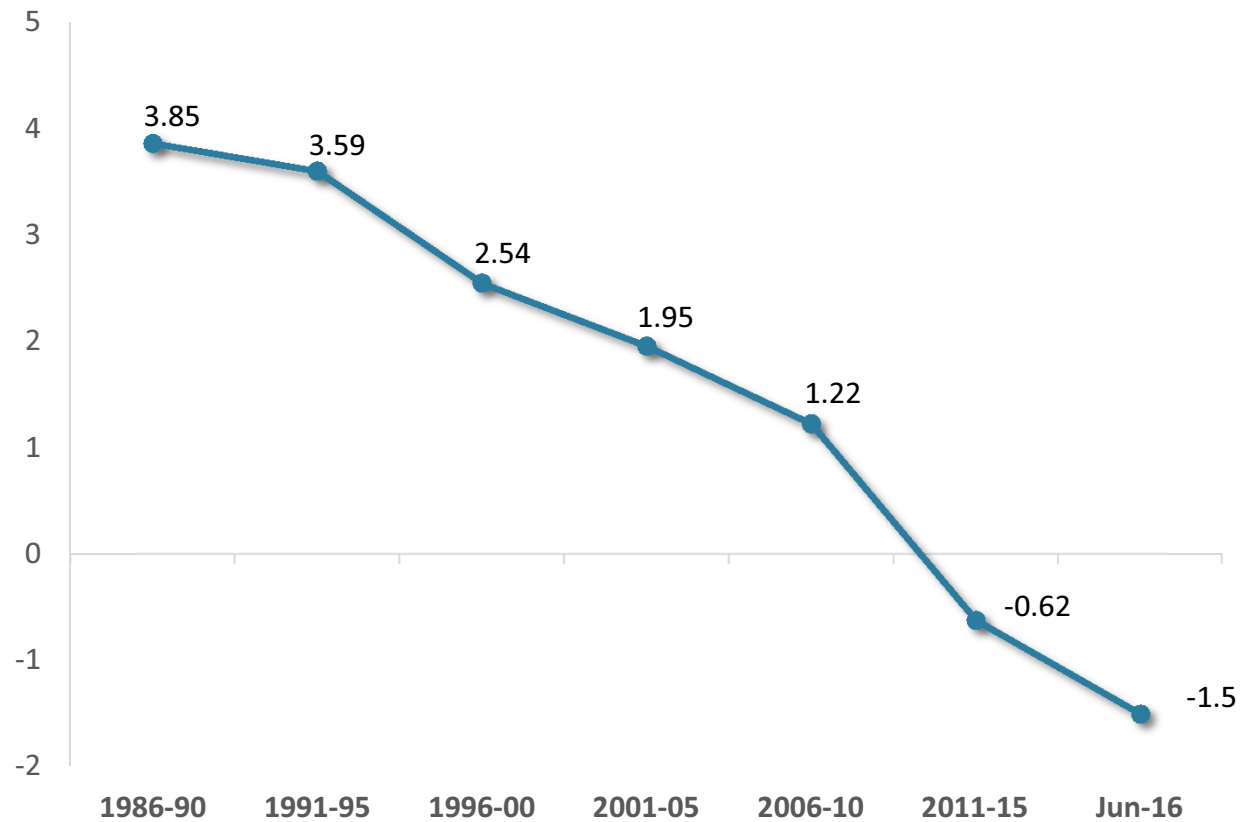


❖ Debt overhang

❖ **Secular Stagnation**

❖ What will happen now ?

Sterling 10 year index-linked gilt: YTM 1985 – 2016



Source: Bank of England Statistics

Why did real rates fall so much even before the crisis?

Ex-ante savings

Global imbalances?

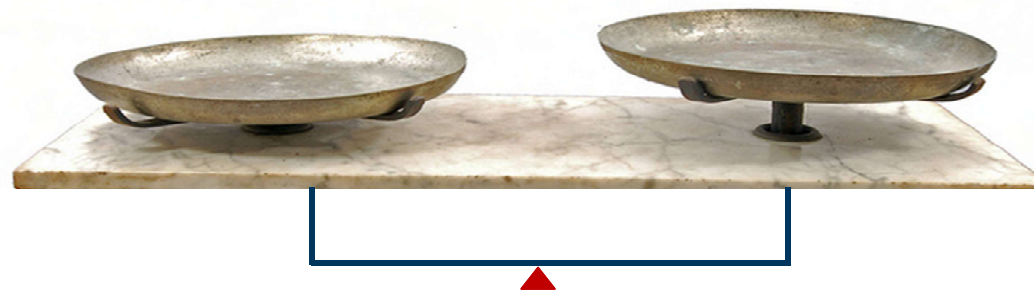
Inequality?

Demographic effects?

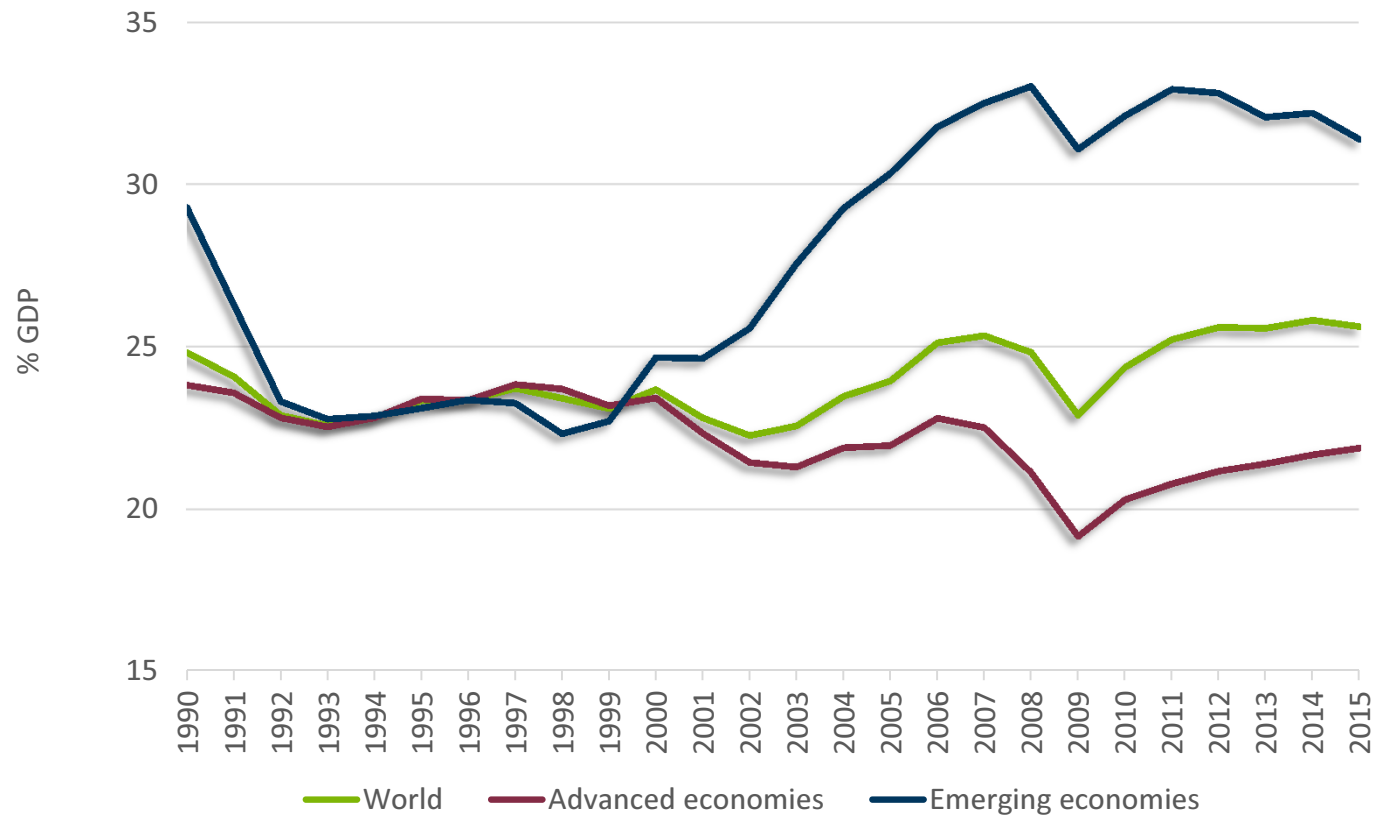
Ex-ante investment

Reduced investment needs?

- In plant and machinery?
- In advanced economy property and infrastructure?











Global saving rates: 1990 – 2015



Source: International Monetary Fund, World Economic Outlook Database, April 2016

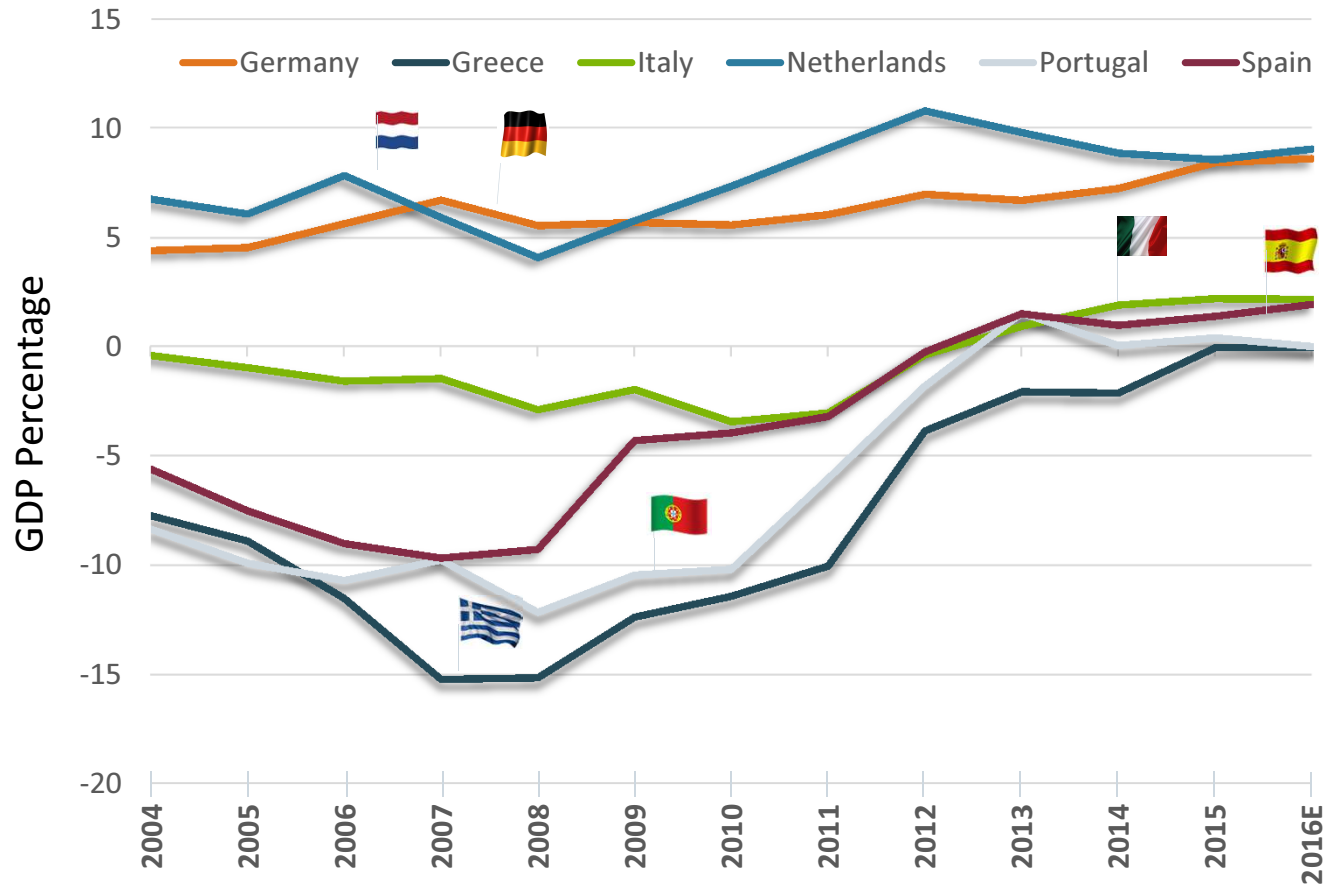
Global imbalances: current account surpluses/deficit as % of GDP

Advanced Economies			
		2007	2016
Germany		+6.7	+8.6
Japan		+4.9	+3.7
Korea		+1.1	+7.2
Netherlands		+6.0	+9.1
Switzerland		+10.1	+9.2
Taiwan		+8.6	+15.0
UK		-2.5	-5.9
US		-5.0	-2.5

Developing Economies			
		2007	2016
China		+9.9	+2.4
Brazil		+0.3	-0.8
Egypt		0.0	-5.8
India		-1.3	-1.4
Indonesia		-1.4	-2.3
Mexico		-1.4	-2.7
South Africa		-5.4	-3.3
Turkey		-5.9	-4.4

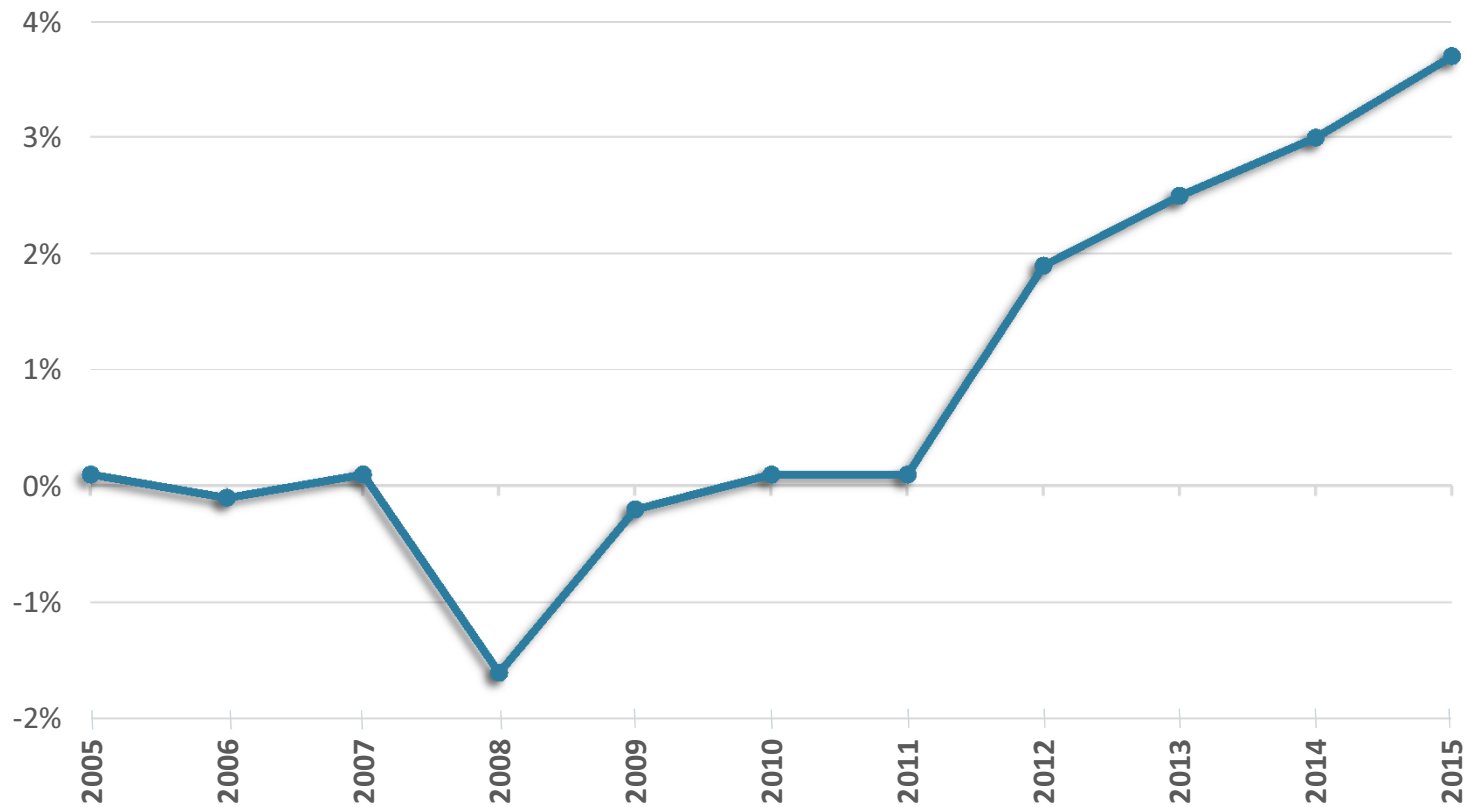
Source: IMF World Economic Outlook Database, October 2016

Current account balances of Eurozone countries



Source: International Monetary Fund, World Economic Outlook Database, October 2016

Eurozone current account as % GDP : 2005-15



Source: International Monetary Fund, World Economic Outlook Database, October 2016

China current account surplus

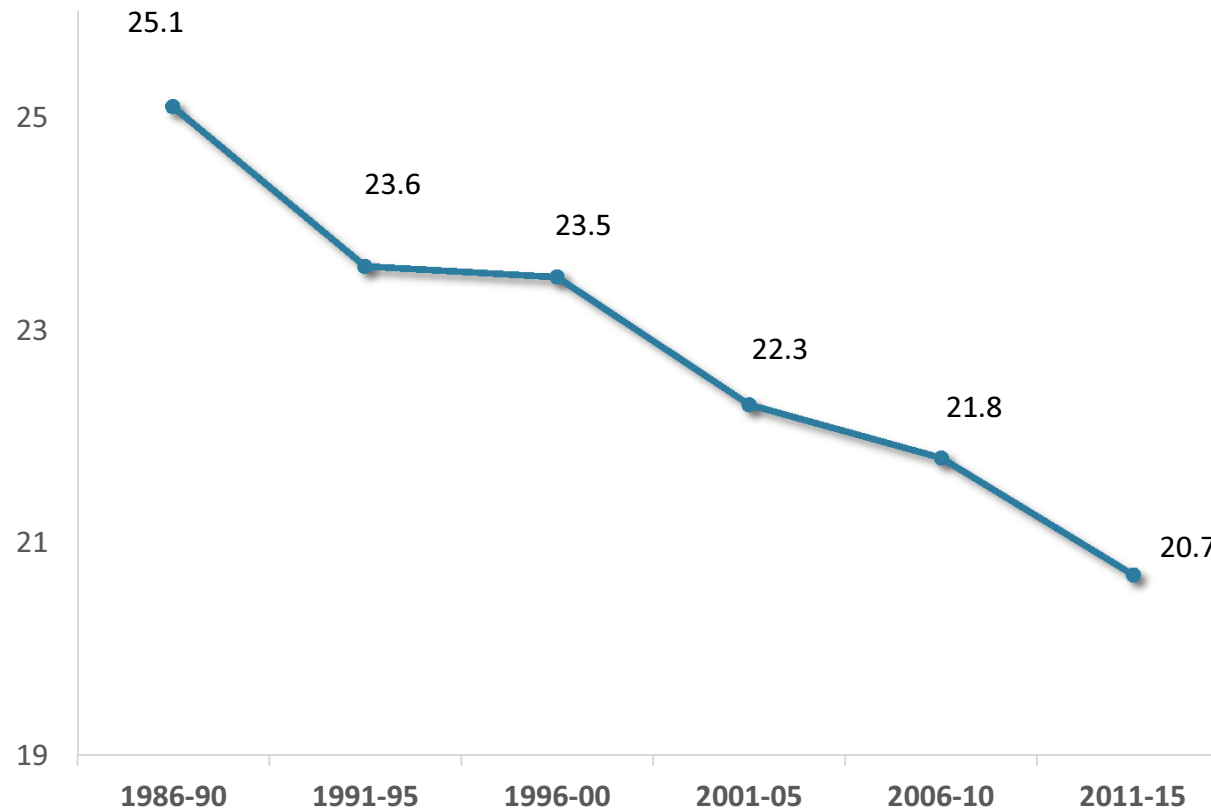


Source: IMF World Economic Outlook Database, October 2016








Source: IMF World Economic Outlook Database, October 2016

Advanced economy investment as % of GDP: 1986 – 2015 five-year averages



Source: IMF World Economic Outlook Database, April 2016

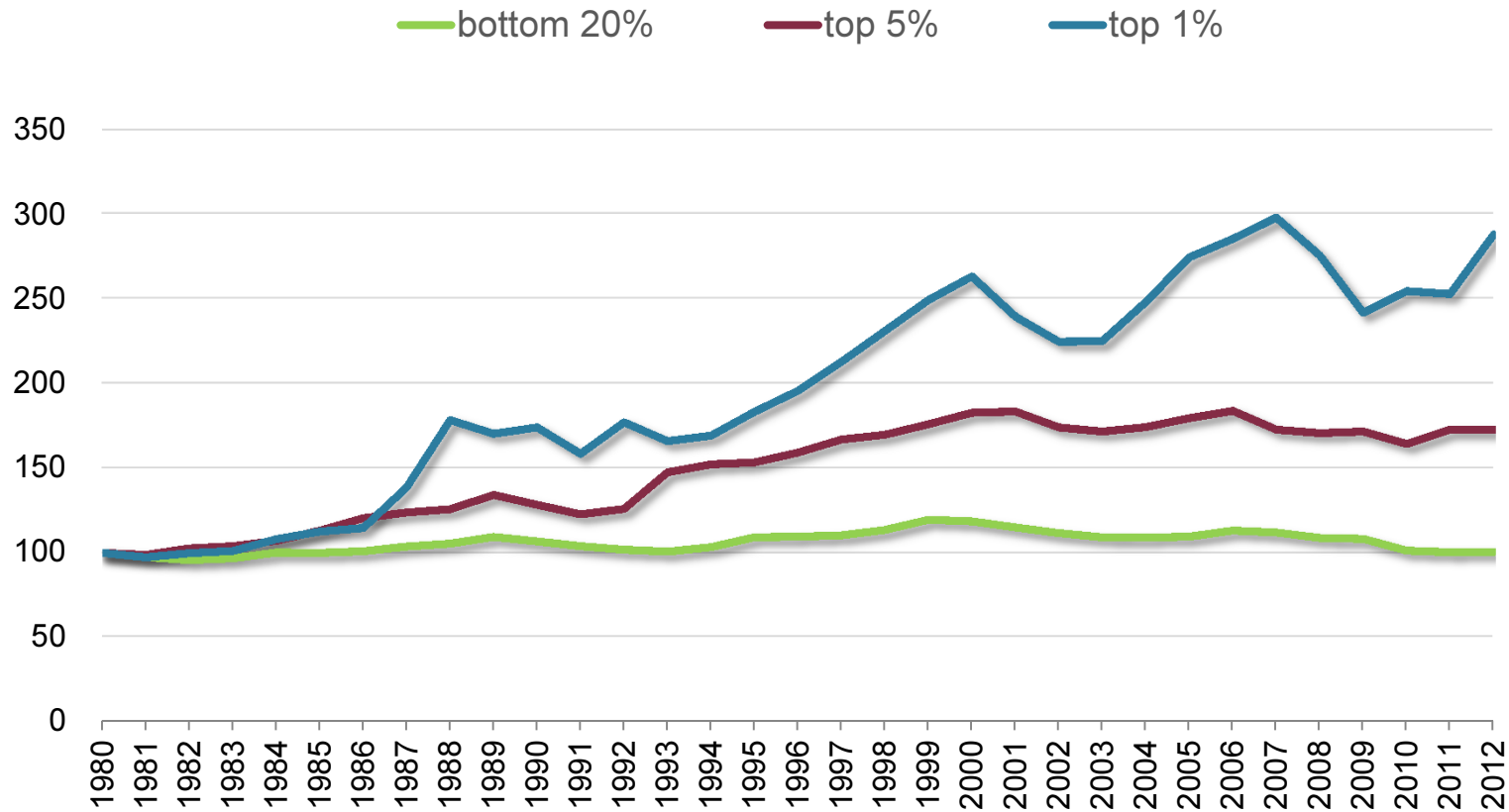
Wealth and employment in ICT businesses

	Market Value (\$bn)	Employees (000s)
	447 (Sep 2016)	~ 114,000 (Sep 2010)
	555	~ 67,000
	374	~ 14,500
 Instagram	1*	~ 12
	19* * Paid by Facebook	55

We have over 1 million users per engineer and this number has been steadily increasing

With only 32 engineers, one WhatsApp developer supports 14 million active users

Average income increases US (1980=100)

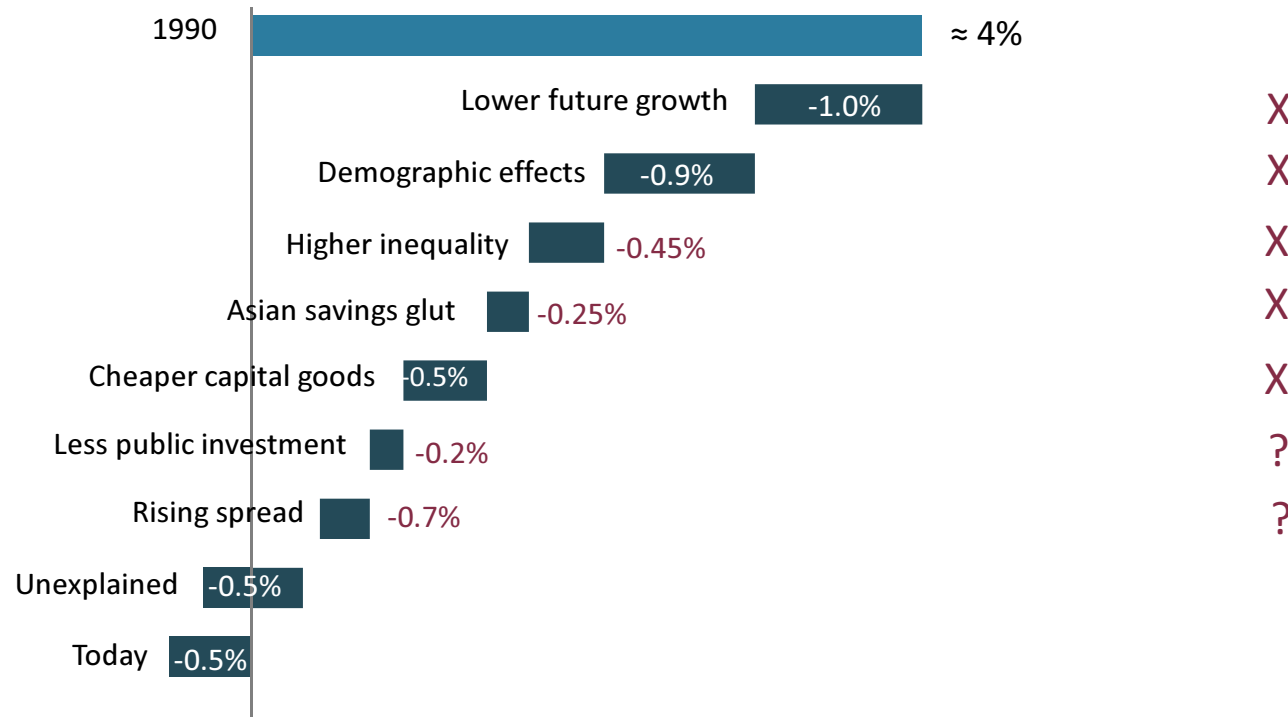


Source: US Census Bureau; World Top Incomes Database

Drivers of a falling neutral real rate?

Developed economies

Likely reversal



Source: Lukasz Rachel and Thomas Smith, *Secular Drivers of the Global Real Interest Rate*, Bank of England Working Paper No. 571, December 2015

❖ Debt overhang

❖ Secular Stagnation

❖ **What will happen now?**

What has changed ?



China



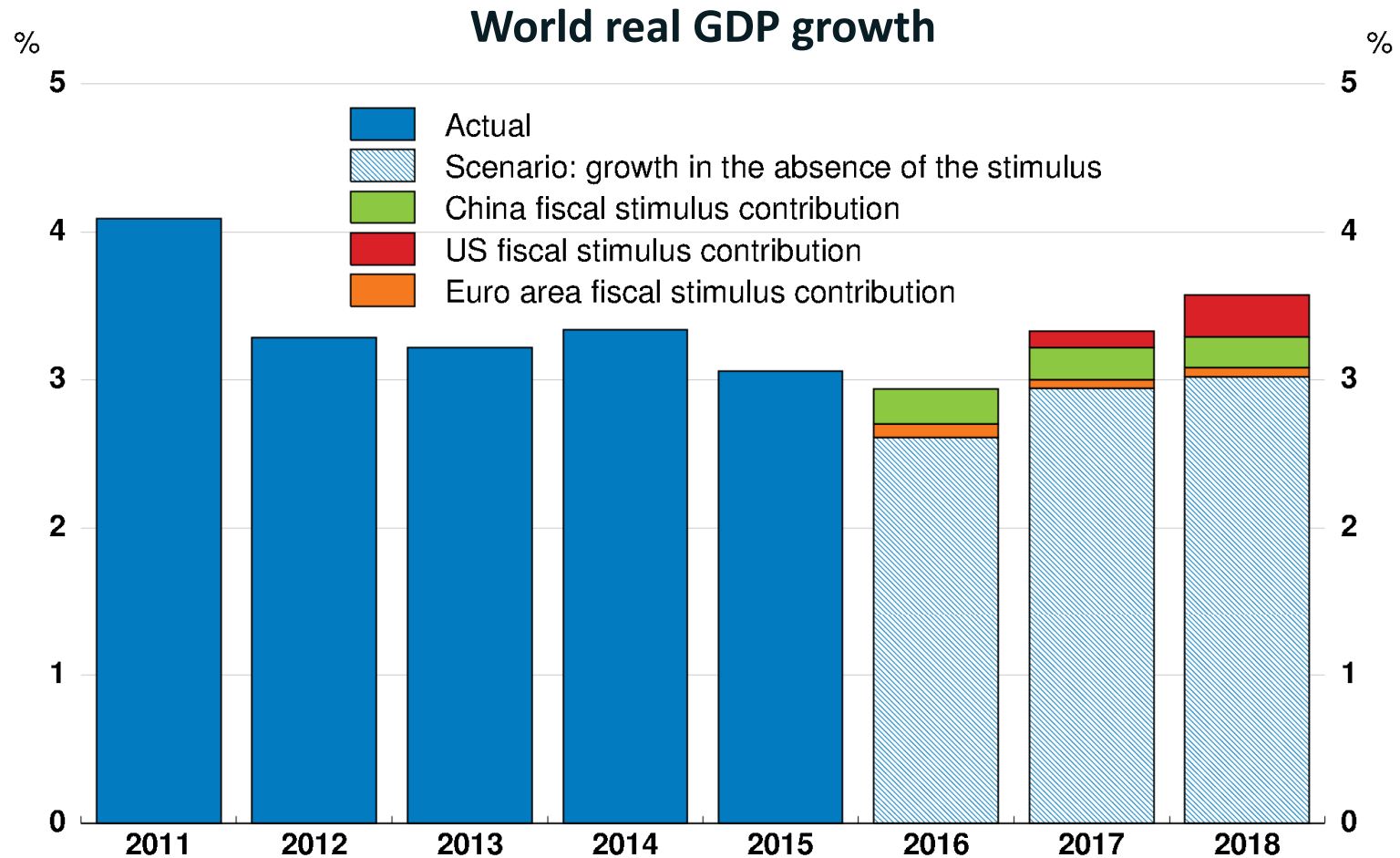
Trump



“The projections in this Economic Outlook offer the prospect that fiscal initiatives could catalyse private economic activity and push the global economy to the modestly higher growth rate of around 3½ per cent by 2018”

(OECD Global Economic Outlook,
November 2016)

OECD scenario for increased global growth

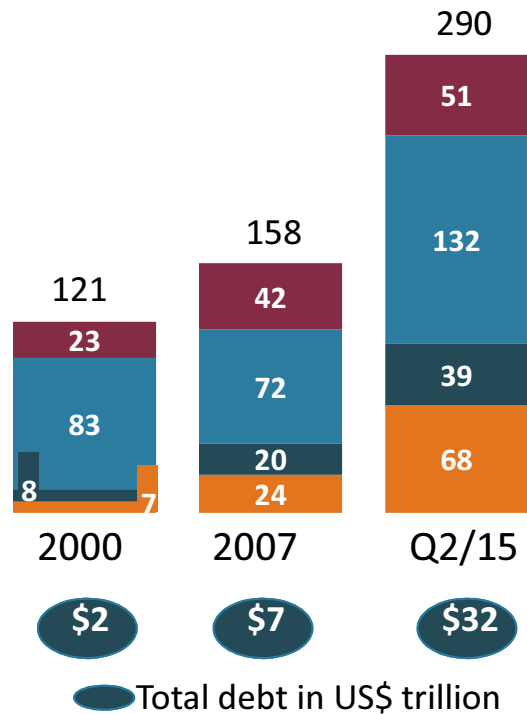


Source: OECD November 2016 Global Economic Outlook

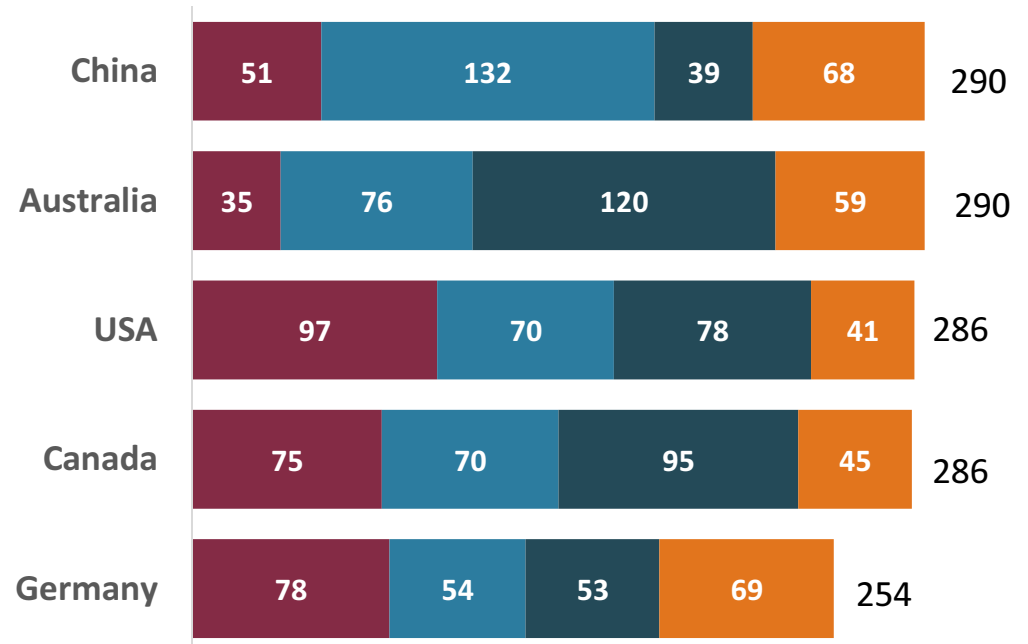
China Debt to GDP Ratio

■ Government
 ■ Non-financial Corporate
 ■ Households
 ■ Financial Institutions

China



By country, 2015



Source: Group of Thirty Report , “Shadow Banking and Capital Markets: Risks and Opportunities”, November 2016

China in 2016

Expectation

- Credit discipline imposed
- Controlled growth slowdown
- Shift to more sustainable model

Reality

- Continued rapid credit growth
- Rising potential bad debts
- Quasi-fiscal stimulus via banks, policy banks and PBOC direct lending
- Dramatic growth of shadow banking
- Rising deposits and other bank liabilities as % GDP

Result

- Investment and growth maintained
- Increasing vulnerability to capital outflow

The Trump effect

- ❖ **Fiscal stimulus and financial deregulation**
 - Demand no longer “subdued”
 - short term boost but long term risks

- ❖ **Tax cuts, ACA repeal and labour market deregulation**
 - Will boost inequality

- ❖ **Protectionism via tariffs or corporate tax reform**
 - Cannot offset technological change
 - Major global risks

What will happen



De facto monetisation – should we care ?



Slowdown and restructure continually delayed
– but must happen sometime



Still playing with social and political fire



OK for now – but unbalanced



Trump sugar rush – but big medium term risks