Escaping the trap: Secular stagnation, monetary policy and financial fragility

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1. Escaping the trap

Everything depends on everything else
Escaping the trap

1. The strange economic world
2. Explaining the strange world
3. Policy in the strange world
4. Uncertain end game
1. The strange economic world

BANK OF ENGLAND LENDING RATES SINCE 1694
1. The strange economic world

![Graph of YIELD ON 10-YEAR INDEX-LINKED GILTS](image)
1. The strange economic world

![Central Bank Intervention Rates Graph](image)

- Fed
- BoE
- Buba
- ECB
- BoJ
1. The strange economic world

![CORE CONSUMER PRICE INFLATION](chart)

- US
- Japan
- UK
- Eurozone
1. The strange economic world

DEBT OVER GDP OF MATURE ECONOMIES
(per cent)(IIF)
1. The strange economic world

DEBT OVER GDP IN MATURE ECONOMIES (IIF Database)
2. Explaining the strange world

CHINA INDEBTEDNESS (per cent of GDP)

Household  Non-financial corporate  Financial corporate  Government
4. Uncertain end game

- So how might this end?
- There are five broad possibilities:
  - Interest rates remain consistently below long-term nominal growth. Demand becomes structurally stronger. Exceptional monetary (and fiscal) policies are withdrawn. Economies grow out of indebtedness.
  - The *status quo* continues, with ultra-low interest rates, but also tolerable growth of nominal and real GDP.
  - There is an inflationary surprise. Central banks fail to respond quickly. So the real burden of debt is substantially reduced, as in the 1970s.
4. Uncertain end game

• Policy generates an inflationary surprise, central banks raise rates sharply. Debt liquidation (that is, mass bankruptcy and a deep recession) ensues, along with another financial crisis.

• There is an unexpectedly deep downturn, perhaps because of a policy shock, or perhaps for some other reason. Central banks are unable to respond. Again, there is debt liquidation and a deep recession.

• We are in a global policy trap. We need to find a way out of it.

• The requirements for this are sources of demand that do not depend on explosive expansions in arguably unsustainable debt.