

G20 Global Financial Stability Conference

“Why is inflation back? Reflexions on other global economic and financial risks.”

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How to explain the very low inflation of years 2012-2021?

5 causes amongst others:

1. After the Great Financial Crisis (GFC) post Lehman Brothers, the scars of the crisis pushed real growth down and foster negative output gaps in many economies.
2. The acceleration of globalization was particularly important after the GFC, paving the way for lower production costs, due to optimized global value chain.
3. The additional weakening of the bargaining power of labor in many advanced and emerging economies, pushing down unit labor cost.
4. The post crisis confirmation of a « global savings glut » pushing simultaneously down global inflation and real interest rates.
5. Last but not least, COVID crisis amplified the trend towards very low inflation with a permanent threat of synchronized shrinking of economies the world over.

Why is inflation back since mid-2021?

8 causes amongst others:

1. The post COVID recovery triggered a sharp acceleration of the demand side whilst the scars of the crisis were still deeply weakening the supply side.
2. The governments, the private sector and Central banks were generally late in assessing the gravity of the inflationary threat, particularly in the advanced economies.
3. The legacy of 10 years of very accommodating fiscal policies.
4. The legacy of equally very accommodating monetary policies during the same period.
5. The post COVID structural inflexion point as regards globalization, with a new trend towards “deglobalization” or “slow globalization”.
6. The major inflexion point as regards the political perception of inequalities and unfairness as regards labor and particularly, low skilled workers.
7. The green transition has a necessary and very important cost, which is likely to push inflation and real interest rate up at a global level.
8. Last but not least, “War in Europe” dramatically increased the price of energy and food, particularly for the European countries and for all the global economies that are significantly depending on imports in these fields.

Why I remain reasonably optimistic as regards regaining control of inflation in the medium term?

3 main reasons to think price stability could be regained in the medium run:

1. Central banks of the emerging countries proved generally highly responsible in countering inflation. Central banks of advanced economies, after initial hesitation, demonstrated also appropriate determination to regain control of inflation.
2. Particularly as regards Central banks of the advanced economies, as well as the Central banks issuing currencies that are in the basket of the Special Drawing Rights (SDR), the confirmation that their 2% goal anchor definition of price stability in the medium term was indeed important. This confirmation, even in difficult times, and the unanimity of the banks concerned gave significantly more credibility for anchoring inflation expectations around 2% in the medium run.

To be noted that the People's Bank of China, issuing the 5th currency of the SDR basket, is also *de facto* credible to deliver 2% inflation.

3. Despite the inflationary surge since 2021, we have not observed a destabilization of the inflation expectations in a medium term (3 to 4 years) basis. This is reassuring, even if the game is not over...

Main global economic and financial risks

1. Threats stemming, at a global level, from the stress of higher nominal and real interest rates combined with a historic high level of public and private debt outstanding.
2. Risks associated with the high level of “Non Banks” Financial Intermediaries (NBFIs) and their interconnections, amplifying the vulnerabilities of the financial system.
3. Vulnerabilities of the developing and the poorest economies, and of many financial market segments – high leveraged in general and real estate, in particular.
4. Systemic vulnerabilities of some emerging countries. China, with its concerns over the debt sustainability of local government financial vehicles, is not alone in this respect amongst the emerging constituency.
5. War in Europe, its additional impact on energy and food prices, the possibility of a further deepening of these geopolitical tensions, not only in Europe, is aggravating considerably overall risks.

Longer term global economic and financial risks

- In a medium and longer term perspective, one cannot exclude the grave geostrategic risks already mentioned as part of the shorter term threats.
- To preserve stability and prosperity in the long term, the international community must win each of the following 3 important battles:
 1. The fight to pave the way to avoid dramatic climate change
 2. The fight to deliver an appropriate level of social cohesion in all economies and societies
 3. The fight to avoid a dramatic fragmentation of the global economy with disruption on global trade and on the “global value chains”
- These battles are all systemically important. A defeat of the international community in any of them would be paid at a high price by all economies in terms of prosperity and stability.

Urgent action is necessary

1. Taking into account the many dimensions of economic and financial risks, both short term and longer term, and challenges for the global economy, the likelihood of the materialization of these risks over the medium term is obviously elevated.
2. In those circumstances, preventing these risks and mitigating their consequences, if they occur, is necessary for the international community. In particular, but not exclusively, a significantly improved Global Safety Net is of the essence.
3. To that end, I share entirely the recommendations presented by the Independent Expert Group, co-chaired by Larry Summers and Nand Kishore Singh, commissioned by the Indian Presidency of the G20.

I will stress the financing recommendations of the Group in the next slide.

As a reminder: financial targets recommended by the Expert Group

1. Additional spending of some \$3 trillion per year is needed by 2030, of which \$1.8 trillion represents additional investments in climate action (a four-fold increase in adaptation, resilience and mitigation compared to 2019), mostly in sustainable infrastructure, and \$1.2 trillion in additional spending.
2. The international development finance system should be designed to support this spending by providing \$500 billion in additional annual official external financing by 2030, of which one-third in concessional funds and two-thirds in the form of non-concessional official lending. It should also catalyze an equivalent amount of private capital, implying a total additional external financing package of \$1 trillion.
3. MDBs should provide an incremental \$260 billion of the additional annual official financing, of which \$200 billion in non-concessional lending, and help mobilise and catalyse most of the associated private finance.

Thank you.

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