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Opening Remarks

Ladies and gentlemen,
I am very pleased to welcome you to the 43rd Economics Conference of the Oesterreichische Nationalbank here in Vienna.

This year we are going to discuss the "Long-Term Perspectives for Economic Growth" – and I would like to invite all of you to take part in this important discussion. We have once again prepared a *highly interesting program* featuring distinguished speakers and discussants from different backgrounds in academia and policy-making. My particular welcome goes to State Secretary *Sonja Steßl*, who will address this year's conference as our first speaker. Thank you very much for joining us today. At this point, let me also take the opportunity to thank the OeNB staff in charge of organizing this event for their outstanding efforts and commitment.

I would like to start my introductory remarks today with a quote that very well captures the recent economic policy debate:

> *"We are suffering just now from a bad attack of economic pessimism. It is common to hear people say that the epoch of enormous economic progress […] is over; that the rapid improvement in the standard of life is now going to slow down. […]; that a decline in prosperity is more likely than an improvement in the decade which lies ahead of us."*

These lines are not taken from a recent editorial or contemporary blog post. They are the *beginning of a famous essay by John Maynard Keynes* on "The Economic Possibilities for our Grandchildren," written in 1930. It is quite telling that 85 years later, we – the grand- and great-grandchildren of Keynes' generation – seem to find ourselves in a situation similar to his. The ruptures of a great economic crisis have again prompted sometimes gloomy forecasts of our future growth prospects. At this year's Economics Conference, we will

discuss in more detail whether these pessimistic outlooks are justified – or whether "this interpretation is widely mistaken," as Keynes concluded almost a century ago.[1]

Economic growth is a spectacular phenomenon. While an annual real growth rate of 2% might at first sight seem modest and inconsequential, it generates tremendous energy if it reoccurs year after year. A look at historic

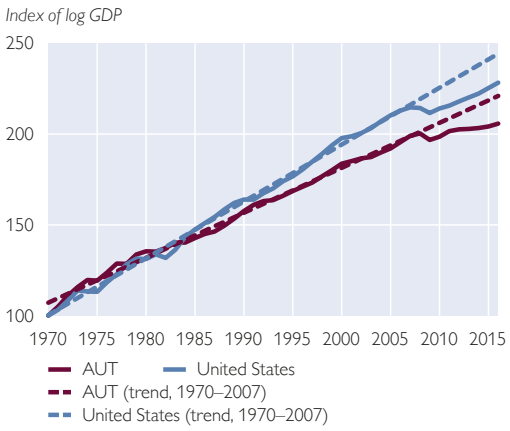
[1] *The entire quote is: "We are suffering just now from a bad attack of economic pessimism. It is common to hear people say that the epoch of enormous economic progress which characterised the nineteenth century is over; that the rapid improvement in the standard of life is now going to slow down – at any rate in Great Britain; that a decline in prosperity is more likely than an improvement in the decade which lies ahead of us. I believe that this is a wildly mistaken interpretation of what is happening to us. We are suffering, not from the rheumatics of old age, but from the growing-pains of over-rapid changes, from the painfulness of readjustment between one economic period and another. The increase of technical efficiency has been taking place faster than we can deal with the problem of labour absorption; the improvement in the standard of life has been a little too quick; the banking and monetary system of the world has been preventing the rate of interest from falling as fast as equilibrium requires." (John Maynard Keynes, Economic Possibilities for our Grandchildren, 1930).*

data reveals that *national per capita income*[2] in Western European countries has grown *by a factor of almost 15 since the onset of the industrial revolution*. This continuous growth in the last two centuries has fundamentally changed the economic environment: the range and quality of consumption goods, the means and possibilities of production, the available types of technology and the ways how people communicate, interact and conduct their lives.

For now, I would like to somewhat confine our view and look at no more than the past 45 years. In the chart you can see the real growth rates for Austria and (by comparison) for the United States for the period from 1970 to today. This chart contains three interesting messages. First, up to 2007 growth rates followed a *clear trend* in both countries: 2.7% in Austria and 3.1% in the U.S.A. Second, there are *considerable fluctuations* around these trend growth rates; the standard deviation in both countries is around 2%.

Chart 1

Real GDP development (1970–2016)



Source: OECD.

Third, it is extremely *difficult to disentangle* the two elements – *trend growth* and *fluctuations around the trend* – in real time. This is particularly relevant for the period after the onset of the Great Recession in 2007, when the strongest deviation from the trend path occurred.

There are two ways to interpret the developments following the Great Recession. The first one is to consider them a dramatic example of severe and persistent *underperformance*. Returning to the old trend path would require closing an output gap of almost 15% of GDP. This would still be possible within a number of years if growth rates were distinctly above the trend.

Unfortunately, our most recent forecasts do not indicate that such a catching-up process is already in the making, but rather suggest a slow recovery.

This gives some support to the second possible reading of the above chart. Under this interpretation, it would be overly optimistic to simply extrapolate the past growth trend into the future. On the contrary, we should consider the possibility that the Great Recession has marked the beginning of a *new era of lower trend growth rates*.

These are, in a nutshell, the two views that characterize the topic of this year's Economics Conference: the view that we are dealing with a persistent negative output gap and the view that we are confronted with a lower long-term growth rate.

The conference program includes sessions that are related to both perspectives and I am sure that we will be presented with evidence and arguments

[2] *This is based on the data provided in Angus Maddison. 2001. The World Economy. A Millennial Perspective, OECD, tables 1–2 and 1–3. The level of GDP per capita (measured in 1990 international dollars) increased from 1,232 to 17,921 (i.e. by a factor of 14.5) for Western European countries, while the figures for total GDP are even more impressive: an increase from 164 billion (measured in 1990 international dollars) to 6,961 billion (i.e. by a factor of 42.5).*

for both sides. In the following, I would like to briefly talk about some aspects that I consider particularly relevant and important. I will first focus on the long-term perspective, then comment on some demand-side aspects before concluding with remarks on policy implications.

Long-run economic development is influenced by many factors, ranging from technology, demography, political and social institutions to more recent phenomena like globalization and climate change. Making predictions about the next 50 or 100 years is highly speculative, but interesting nonetheless. A look at the standard growth model is probably a good starting point for organizing thoughts along these lines. In the standard growth model, the determinants of long-run GDP growth are population growth on the one hand and productivity growth on the other hand.

Demographic developments are expected to have a considerable impact on the future macroeconomic outlook. Decreasing fertility rates will have a direct negative impact on the growth rate of total GDP as long as they are not counteracted by increasing rates of net migration. Population aging, on the other hand, might lead to higher savings and thus – ceteris paribus – to a downward pressure on real interest rates. This reaction is sometimes presented as a direct and necessary consequence of the rise in life expectancy. It is important, however, to emphasize that the strength of this channel will depend on the reaction of retirement behavior, i.e. on people's incentives, willingness and ability to work longer. While demographic developments can be forecast quite accurately for the next 20 to 30 years, the development of retirement age is much less certain, as it will depend on the design of public and private pension systems, on the economic environment and on the progress of medical science.

This brings me to the second main driver of long-term economic growth: the *development of productivity*. A number of observers have argued that the

technological frontier is no longer expanding at the previous speed, that the "low-hanging fruits" have already been picked and that the wider consequences of the computer/internet revolution are more modest than those of the introduction of equivalent general purpose technologies like the steam engine or electricity.

Opposed to this pessimistic view of the future of innovation there is, however, a second camp of thought that has a much rosier, almost enthusiastic view of the technological possibilities that lie ahead. The subtitle of a famous book captures this perspective in a compact form: "How the Digital Revolution is Accelerating Innovation, Driving Productivity, and Irreversibly Transforming Employment and the Economy".[3] This camp of technological optimists refers to scientific breakthroughs that one might expect (or rather: not even expect) over the next decades, especially in the realm of life sciences. These discussions are thrilling and

there are many aspects that deserve thorough and sometimes speculative thinking. The second conference day is almost exclusively dedicated to these long-term topics.

Long-term forces are not the only possible cause for the modest growth performance recorded over the past few years. The recent debate has provided many more potential explanations for the weak economic recovery, and these, too, will be discussed later today and tomorrow.

Of particular prominence is the *secular stagnation* hypothesis dating back to Harvard economist Alvin Hansen. He viewed the weak recovery in the aftermath of the Great Depression as being caused by excess savings and a real interest rate that could not fall sufficiently such as to equate supply and demand at full employment. Today's

proponents of Hansen's hypothesis, for example Harvard economist Larry Summers, consider this mechanism to be the main driving force behind a *secular deficiency in aggregate demand* in the aftermath of the Great Recession. According to this view, long-term factors can be considerably amplified by a number of specific characteristics of a post-crisis recovery process.

The first characteristic is the zero-lower-bound on nominal interest rates. If inflation expectations are well anchored at the same time, the real interest rate will be stuck at an excessive level. As a consequence, we will see low investment and high unemployment.

A second characteristic of the current recovery process is the phenomenon of *debt overhang*, including household, corporate and public debt. A number of observers have identified this debt overhang as also having an aggravating influence on the drag on growth. They consider painful and long-lasting deleveraging both in the private and the public sector as a necessary prerequisite for economic recovery.

Finally, there is also the view that weak recovery is at least in part due to the increased degree of *uncertainty* surrounding future economic developments. This uncertainty leads households to increase their precautionary savings and firms to postpone their investments, further enhancing excess savings and thus exacerbating the deficiency in aggregate demand.

Let me conclude by discussing the *policy implications* – in particular the implications for monetary policy – of the recent debate. What can and should central banks do to sustain long-run growth and support economic recovery?

Monetary policy plays a vital role in managing demand fluctuations, in stabilizing prices, output and unemployment. The recent episode has shown that this is also true at the zero lower bound. Quantitative easing policies have contributed significantly to economic

[3] *This refers to Erik Brynjolfsson and Andrew McAfee. 2011. Race Against The Machine: How the Digital Revolution is Accelerating Innovation, Driving Productivity, and Irreversibly Transforming Employment and the Economy.*

recovery in the United States, and there are first signs of success of these policies also in the European Union. The recent spring forecast of the European Commission predicts a cyclical upswing across basically all EU Member States, and it attributes this upswing partly to the stronger-than-expected effect of the ECB's quantitative easing policy.

On the other hand, monetary policy is less effective when it comes to improving a country's long-term growth potential. Structural policies, institutions, research and development play more important roles in this context. But this is not to say that monetary policy is irrelevant for long-term growth. In fact, economic performance requires a growth-friendly environment. Monetary policy contributes to such an environment by ensuring a reliable policy framework, a sound financial system, a well-functioning banking system, and macroprudential policies that prevent excessive price fluctuations.

Finally, I do dare to confront this meeting of economists with a rather philosophical question – a question, however, that has already been asked by J. M. Keynes and which is today being frequently repeated especially among young people: What about the connection between economic growth and human well-being? Is there not an increasing need to look not only at the quantity but also at the quality of economic growth? This is a very broad field indeed, but questions like these may point to some aspects that also central bankers may have to take into immediate consideration. At the recent, highly interesting ECB Forum on Central Banking in Sintra, there was a discussion on structural reforms – which, as you know, is a mantra in all ECB statements. One of the eminent economists attending the conference asked what may be the human costs of certain forms of structural reform. So e.g. what forms of increased flexibility in the labor markets are really welfare improving and what forms of increased insecurity, involuntary mobility, reduced chances for family life may have long-lasting negative welfare – and maybe also outright growth – effects? And I may add: Would such a perspective lead to different priorities for policies that are intended to reduce unemployment? What does this mean for our standard concepts of potential output and a natural rate of unemployment, which the ECB by the way sees at 10 %, compared to 5 % in the U.S.A.? You may know the famous remark by George Bernard Shaw: "Economists know everything about prices and nothing about values." I trust that this will not be the motto of our meeting!

This brings me to the end of my introductory remarks. To conclude, I look forward to having a day and a half with you to discuss these important issues of economic policy from a multitude of perspectives. I hope you will find our Economics Conference a useful and an insightful event.