

Doris Ritzberger-Grünwald
Director of the Economic Analysis Department



The threat of secular stagnation and how to avoid it

The annual growth rates of Austria, but also of many other (mainly EU) countries have disappointed rather often in recent years. Contrary to the U.S.A., where the recovery started right after the Financial Crisis in 2009 and continued steadily thereafter, the level of euro area GDP stagnated (chart 1). The many downward revisions of forecasts which went along with this development have not only destroyed hopes for a pronounced upswing, more jobs and lower unemployment rates. This development has also triggered an intensive debate on growth in general and the multitude of factors and influences in particular. The debate is about sources of growth, about long-run and short-run determinants, about the fluctuations of growth over time and across countries, about its interactions with various other variables and also about the limits of growth. So far the conference has dealt with a large number of these possible perspectives, growth accelerators and

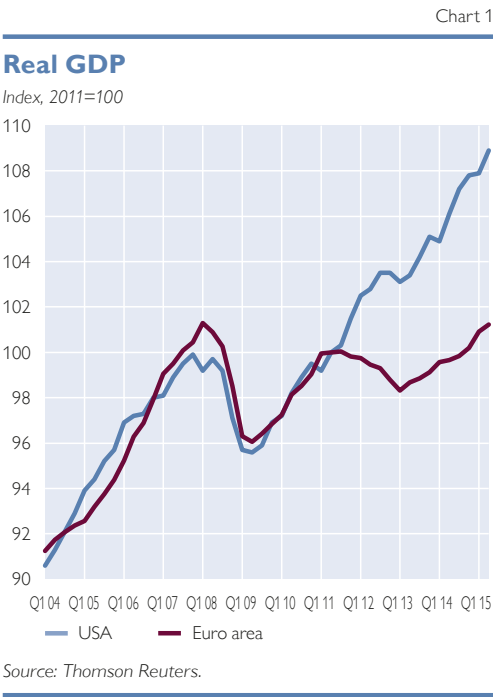
growth constraints, in particular in relation to our current difficult situation after the Great Financial Crisis. The last session of this conference looks at the future, looks at the “secular” trends, as the title of this session suggests.

To be precise, the title is not “secular trends” but rather “secular stagnation,” which sounds a little bit gloomier. This notion was popularized by



Larry Summers in late 2013 (Summers, 2013), while the expression itself goes back to Alvin Hansen, who coined it in 1938 (Hansen, 1939). The secular stagnation hypothesis usually refers to a situation in which people’s propensity to save is high while demand for investment is limited. If these two magnitudes can only be brought into equilibrium at a low or even negative real interest rate, then the economy might become stuck at a suboptimal point due to the zero lower bound on nominal interest rates.

Recently, we have seen many discussions on the topic of secular stagnation. Secular stagnation made headlines in internet fora, and was discussed intensively at academic conferences as well as at meetings of policymakers. In fact, the discussion has been so intense that the phenomenon even gained a



nickname and it is sometimes simply referred to as “secstag.” Some people have argued that “secular stagnation” is a clear and present danger for developed economies around the globe. Others have countered that it constitutes a rather theoretical possibility that can only happen in stylized models but not in the real economy, in particular since real interest rates cannot stay negative for a prolonged period of time. Yet another group has taken a middle ground arguing that the stag-



nation scenario sketched by Larry Summers might not turn out to be of a true secular nature but nonetheless be a major obstacle for the recovery process.

For some of us this debate is déjà vu, as we have had one or the other gloomy debate on economies suffering from no or very low growth rates before. Especially in the 1980s and 1990s, several economists claimed that technological progress was going to reduce the number of working places significantly. Growth would vanish also when households having essentially satisfied their needs would stop spending on additional consumption. Another obstacle for growth was detected in increased environmental standards. Time has proven that the opposite is true. Technological progress has not de-

stroyed the economies. Quite in the contrary, it has increased the affordability of many consumer and investment goods. Innovation has brought us new products, thus creating new needs and therefore additional demand. Even globalization has increased growth, at least in total. The question is if this optimistic view is still the right one, or whether things have changed fundamentally with the Great Financial Crisis. For instance, “trust” seems to have gained a more important role compared to the past, and the same holds true for “expectations.” But is this really the case, or are these two terms only the outcome of a new design of economics, which enables us – more or less – to model these things?

In this last session, two outstanding experts will offer their opinions on the presence and the danger of secular stagnation. Professor Carl Christian von Weizsäcker might be one of the few people who were not particularly taken by surprise when Larry Summers turned the attention to the phenomenon of secular stagnation at the end of 2013. In fact, Professor Weizsäcker pre-empted Summers by writing (Weizsäcker, 2011) about an economic situation that very much resembles a secular stagnation, if not by name then by concept. In his explanation he refers to two elements that have a close connection to the location of this conference. First, he relates the size of total savings to the design of the pension system and the prevalence of early retirement, a phenomenon that is not unknown in Austria. And second, he uses concepts from the Austrian capital theory, like roundaboutness, to explain the decrease in investment activity. Professor Nicholas Crafts, on the other hand, warned in a well-received article (Crafts, 2014) that the danger of secular stagnation might well be more rele-

vant for Europe than for the U.S.A. and even more so for the euro area. He offered a number of reasons for this prediction, ranging from demographics to monetary policy. Thus, the next two contributions will give a lot of insight into the ongoing debate and add to our understanding.

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