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Update & Redesign of the conference to the Collège de France

Olivier Klein

"INFLATION, INTEREST RATES AND DEBT"

I. INFLATION

- ❖ INFLATION RATE
- ❖ DIFFERENT TYPES OF INFLATION

II. MONETARY POLICY IS ESSENTIAL TO COMBAT INFLATION

- ❖ MONETARY POLICY MUST COMBAT INFLATION
- ❖ How?

III. BUT MONETARY POLICY CANNOT DO EVERYTHING - THE NEED FOR STRUCTURAL REFORMS

- ❖ GLOBAL DEBT HAS NEVER BEEN SO HIGH
- ❖ PUBLIC AND PRIVATE DEBT, SNOWBALL EFFECT AND SOLVENCY RISK (FRENCH EXAMPLE)
- ❖ STRUCTURAL REFORMS AND POLICIES ARE ESSENTIAL

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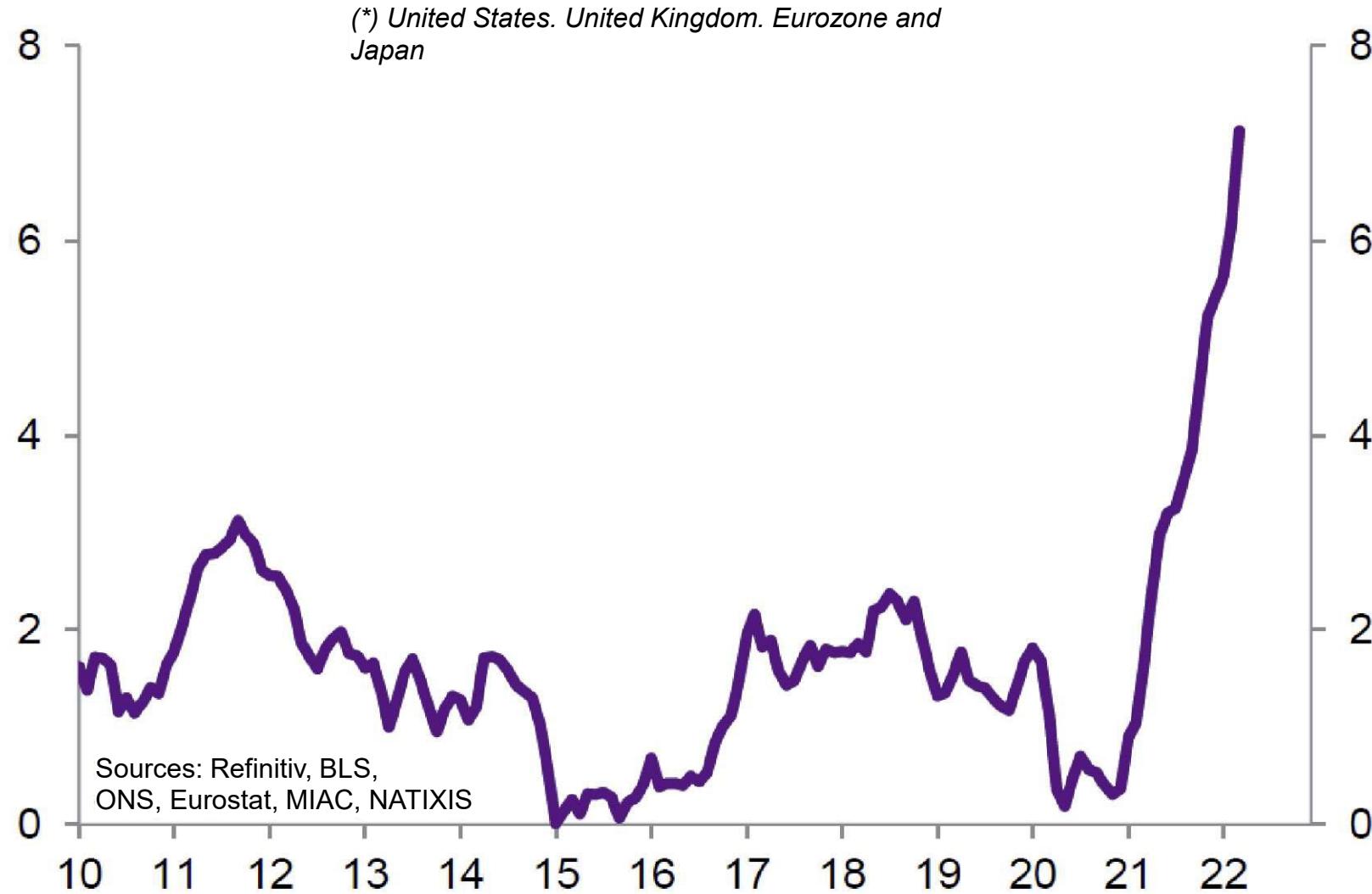
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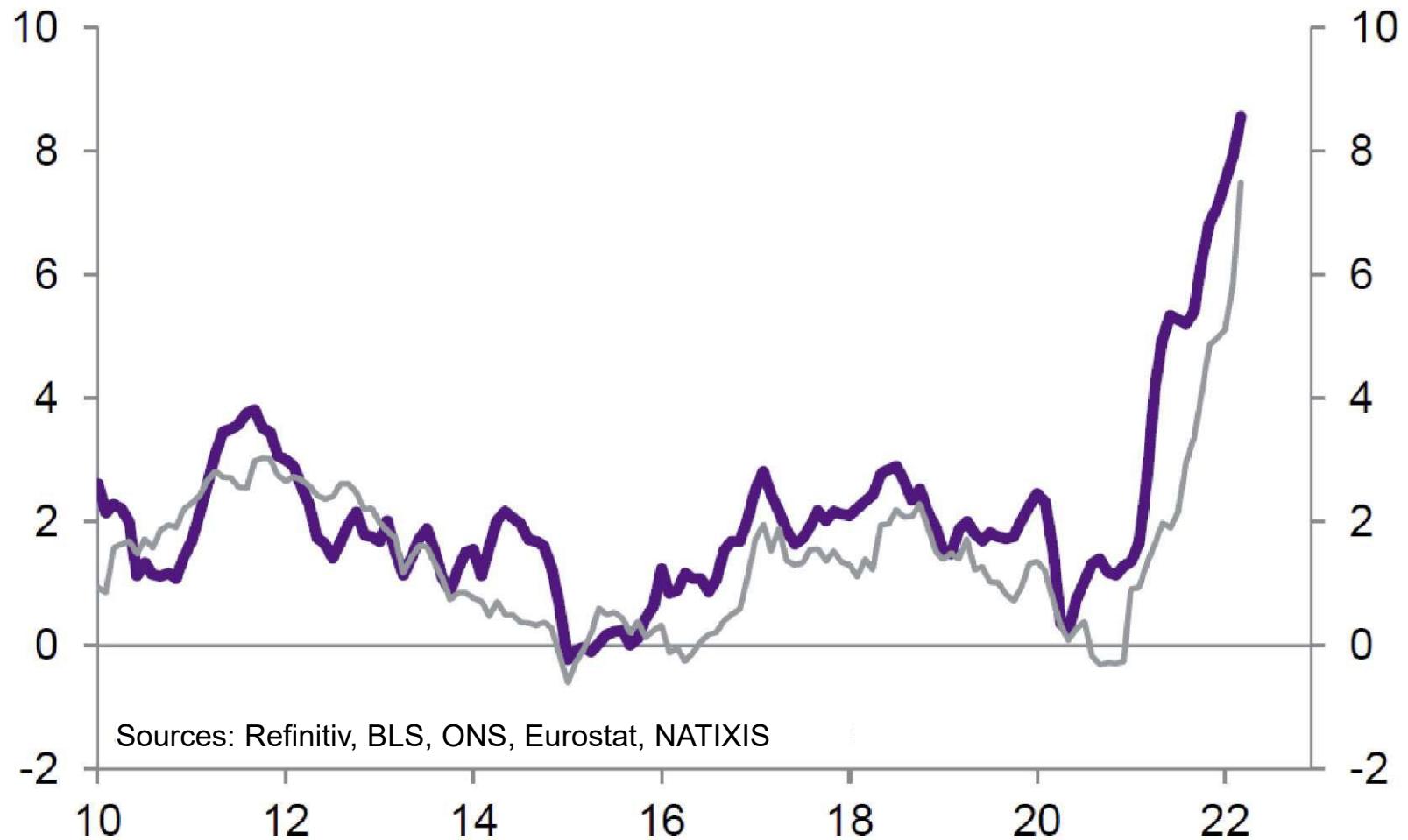
OECD*: INFLATION (CPI, YoY %)



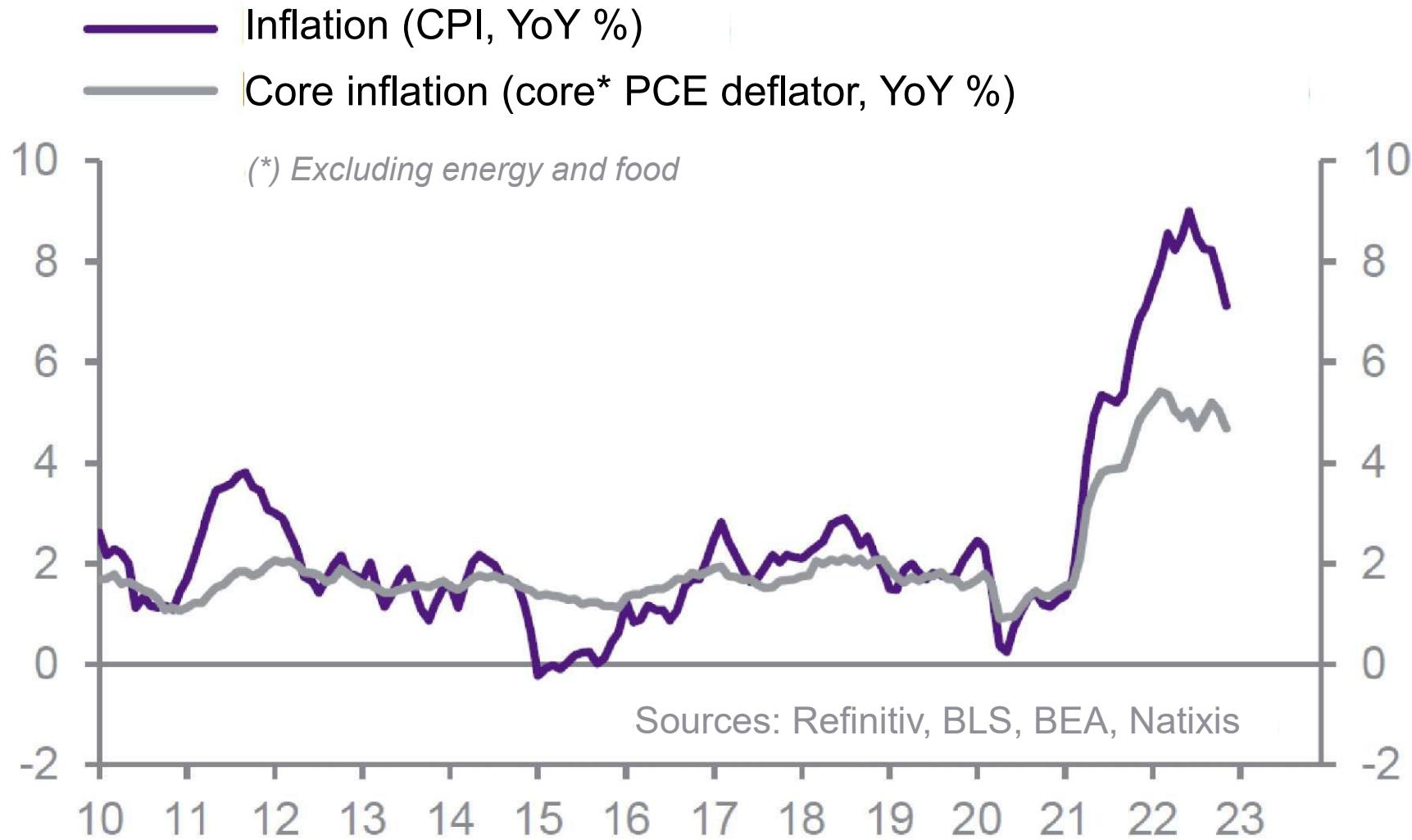
INFLATION (CPI, YoY %)

United States Eurozone

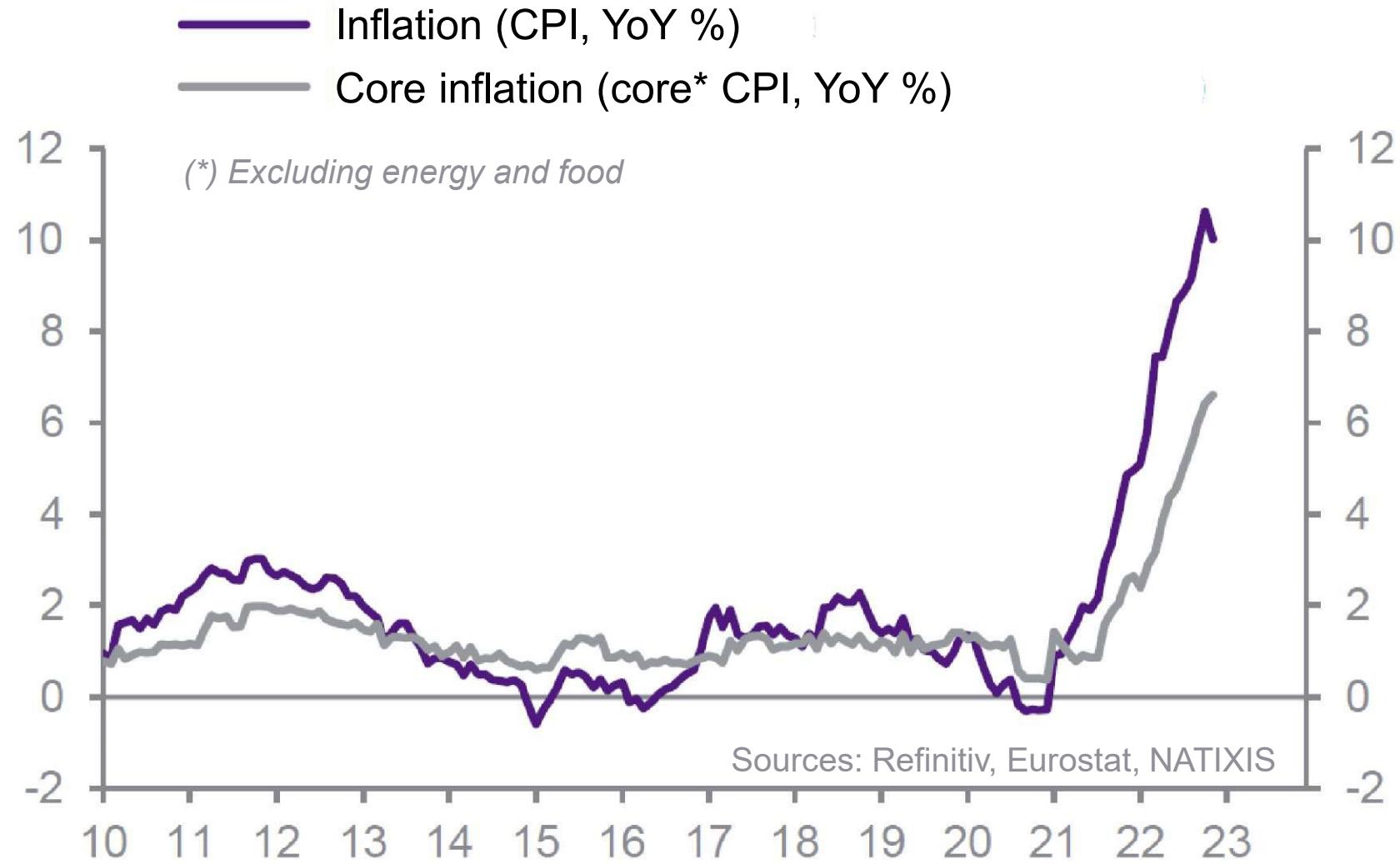
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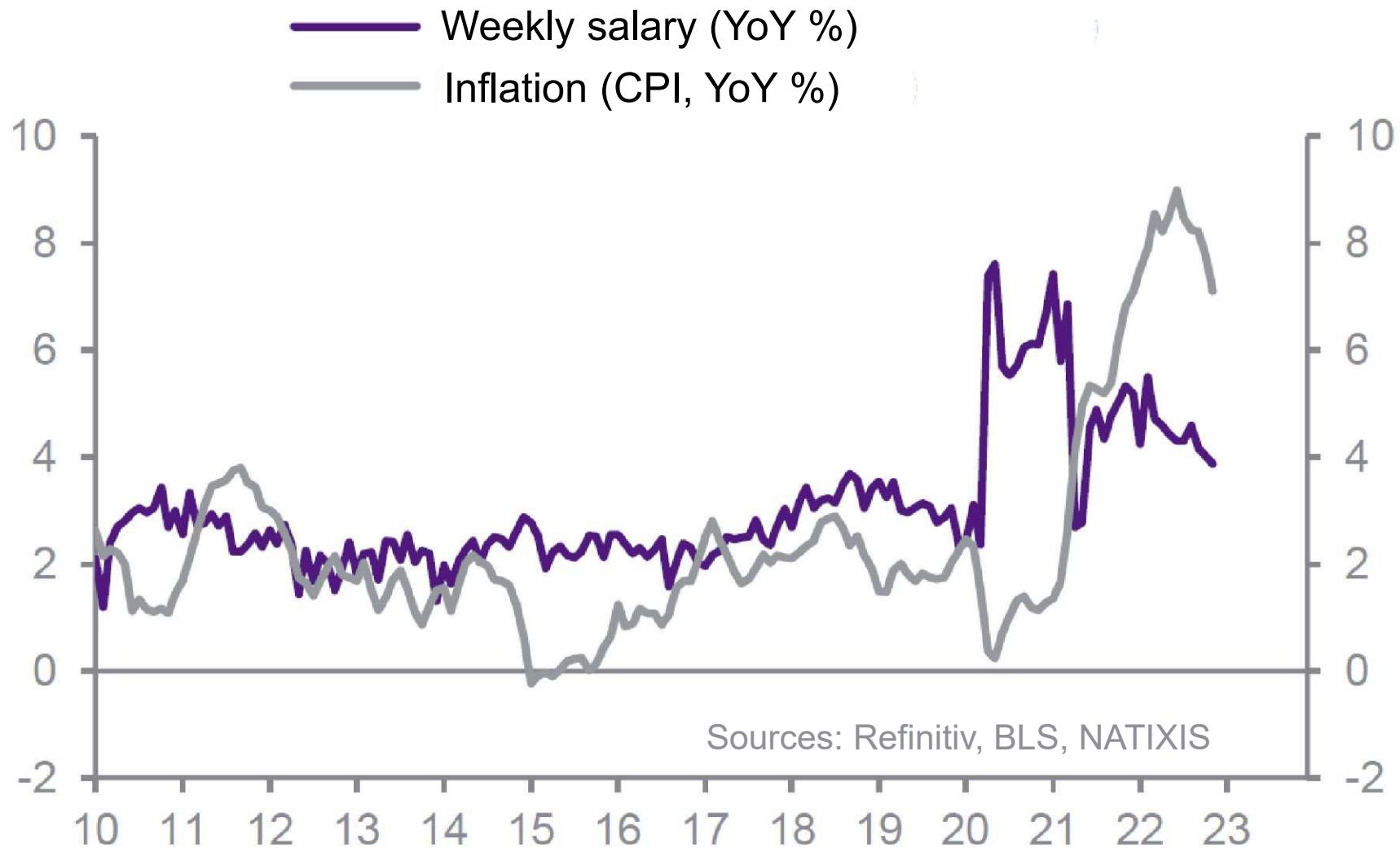
US: INFLATION AND CORE INFLATION



EUROZONE: INFLATION AND CORE INFLATION

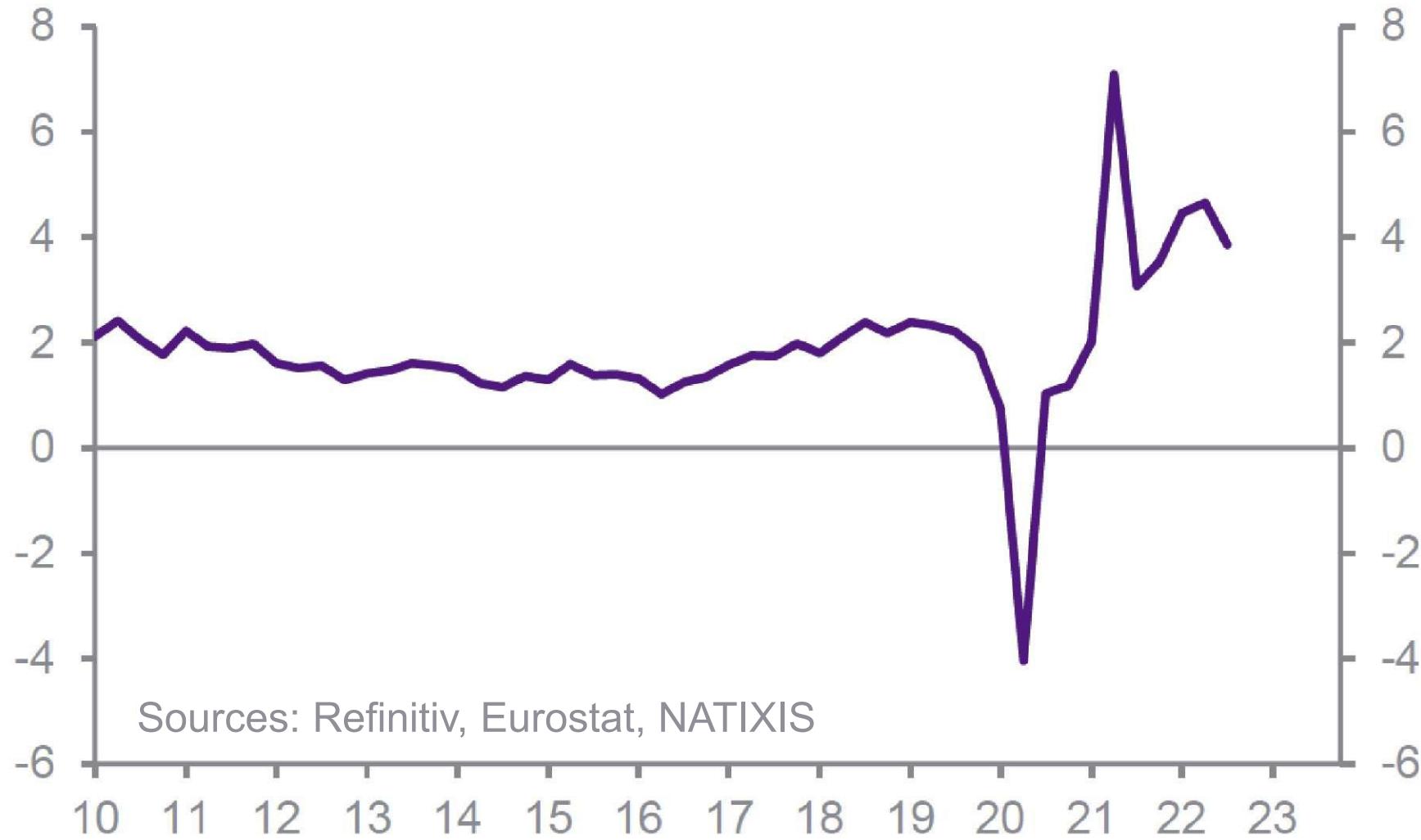


US: WEEKLY SALARY AND INFLATION



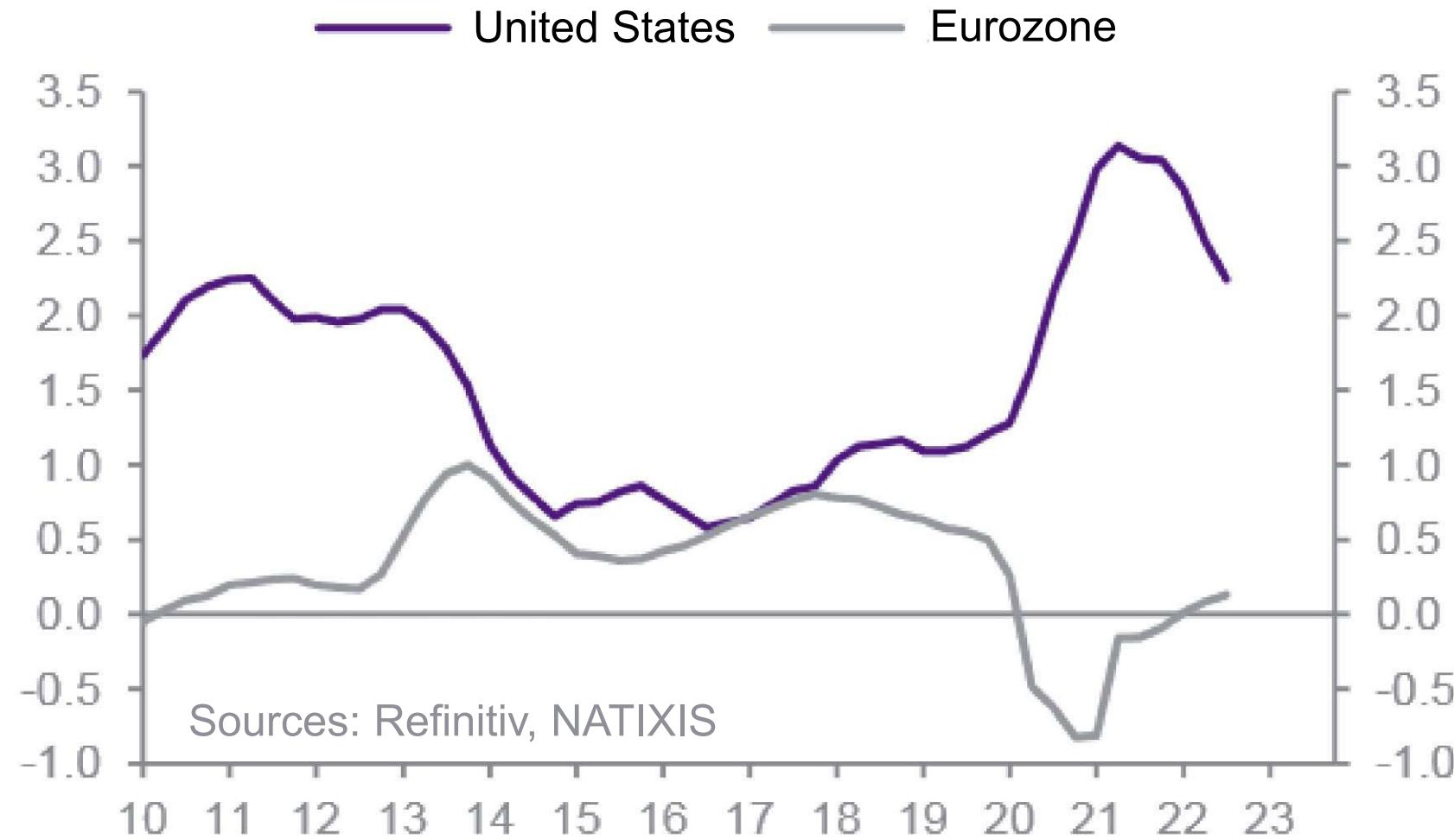
EUROZONE: NOMINAL WAGE PER CAPITA (YoY %)

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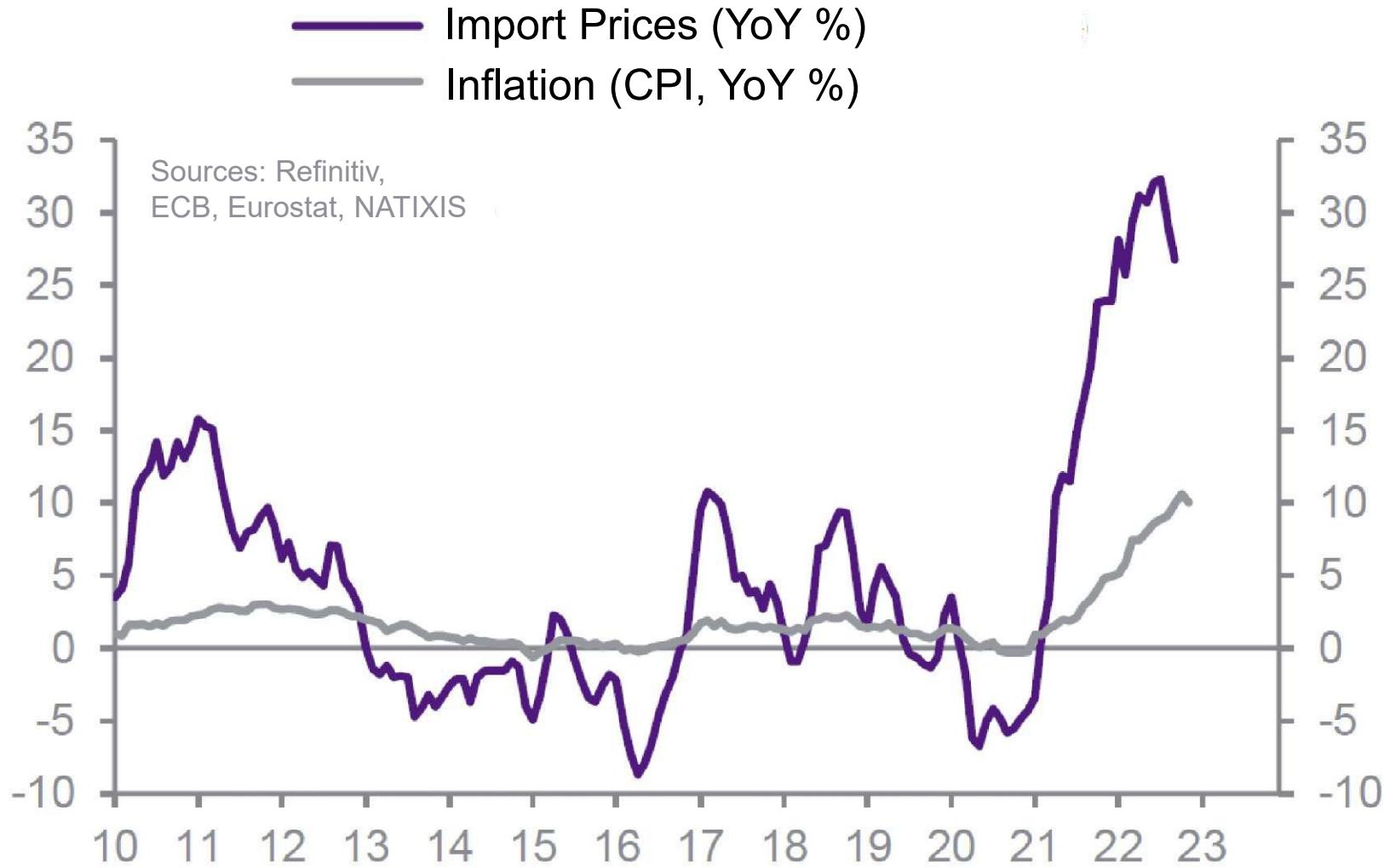


PRODUCTIVITY PER CAPITA (YoY, SMOOTHED OVER 4 YEARS)

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EUROZONE: IMPORT PRICES AND INFLATION



THE EFFECT OF THE REOPENING OF CHINA?

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- The two historical inflation regimes (low inflation regime and a high inflation regime): long cycles

The self-reinforcing nature of each of them

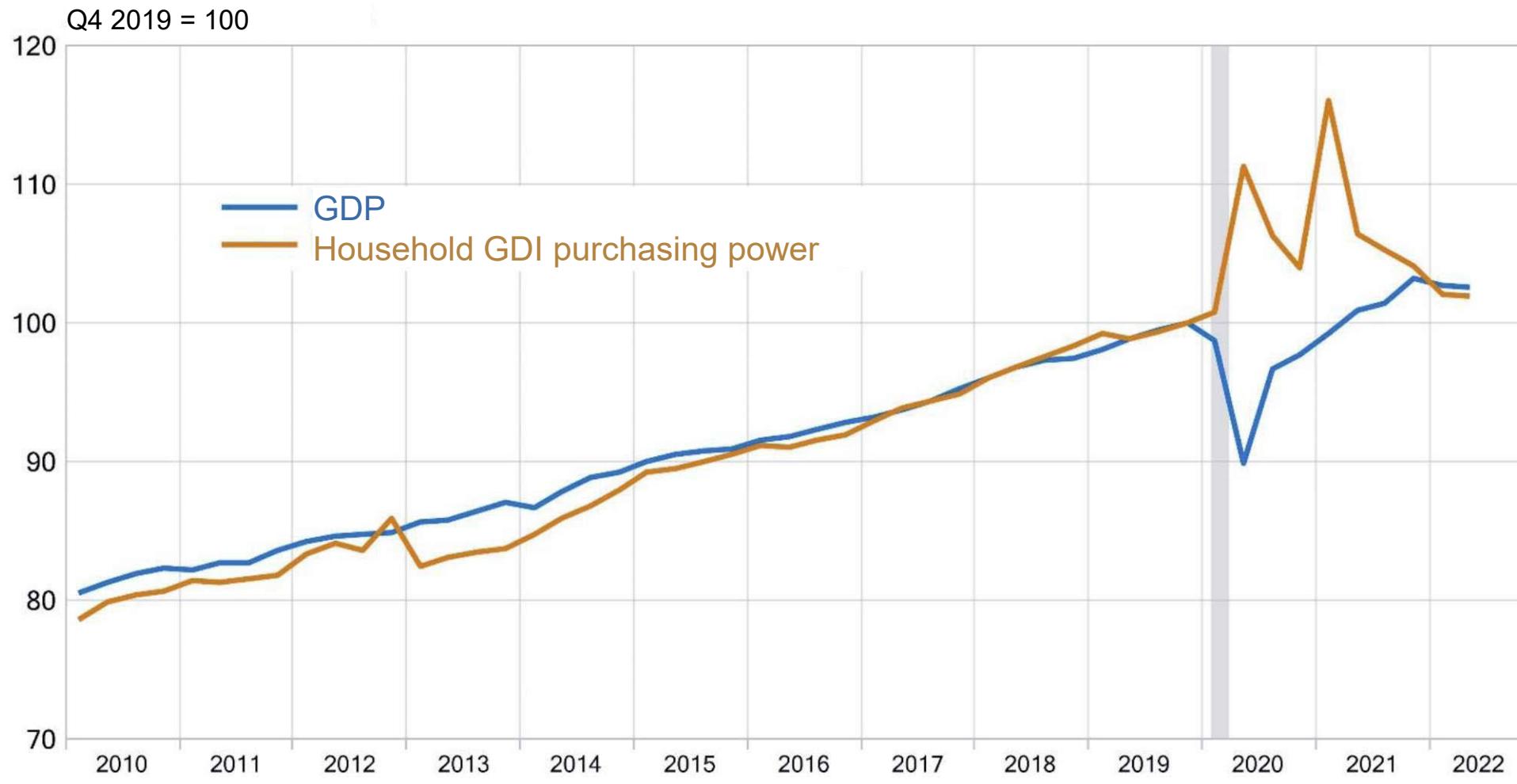
Today:

- Transitory inflation or change in inflation regime?
- Cyclical inflation or structural inflation?

- The transitory and cyclical component:
It is due to the supply/demand imbalance at the end of the pandemic
- The structural component (change in inflation regime):
Partial deglobalisation, cost of the energy transition, delay in training on economic and technological changes, change of cycle in the sharing of value added?

1. The transitory and cyclical component of inflation

UNITED STATES: GDP AND PURCHASING POWER OF HOUSEHOLD GROSS DISPOSABLE INCOME



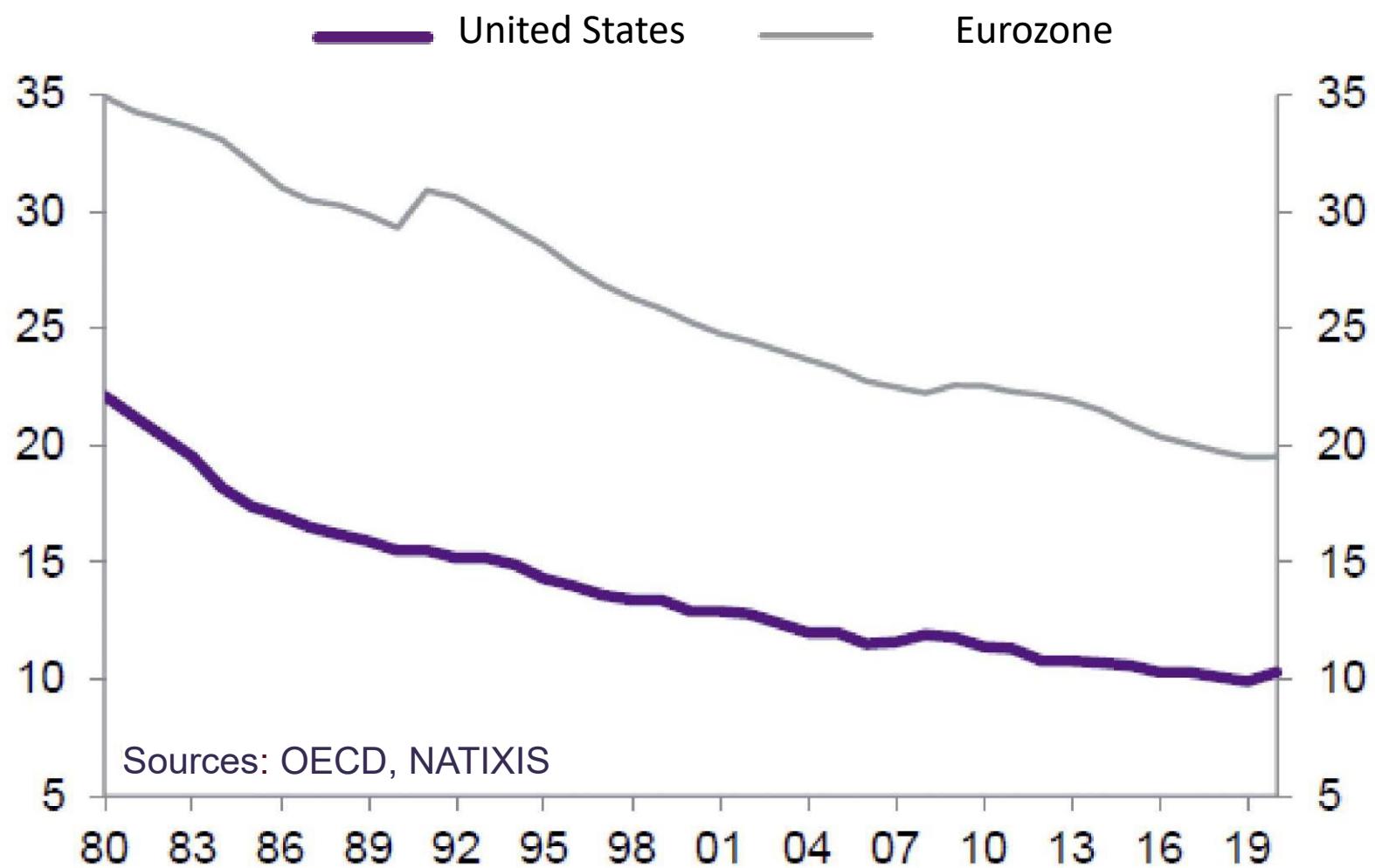
Sources: BEA

2. But a change in the long cycle is likely.

We are probably moving out of a 40-year low inflation cycle, caused by:

- globalisation
- the technological revolution
- sharing of value added to the detriment of work

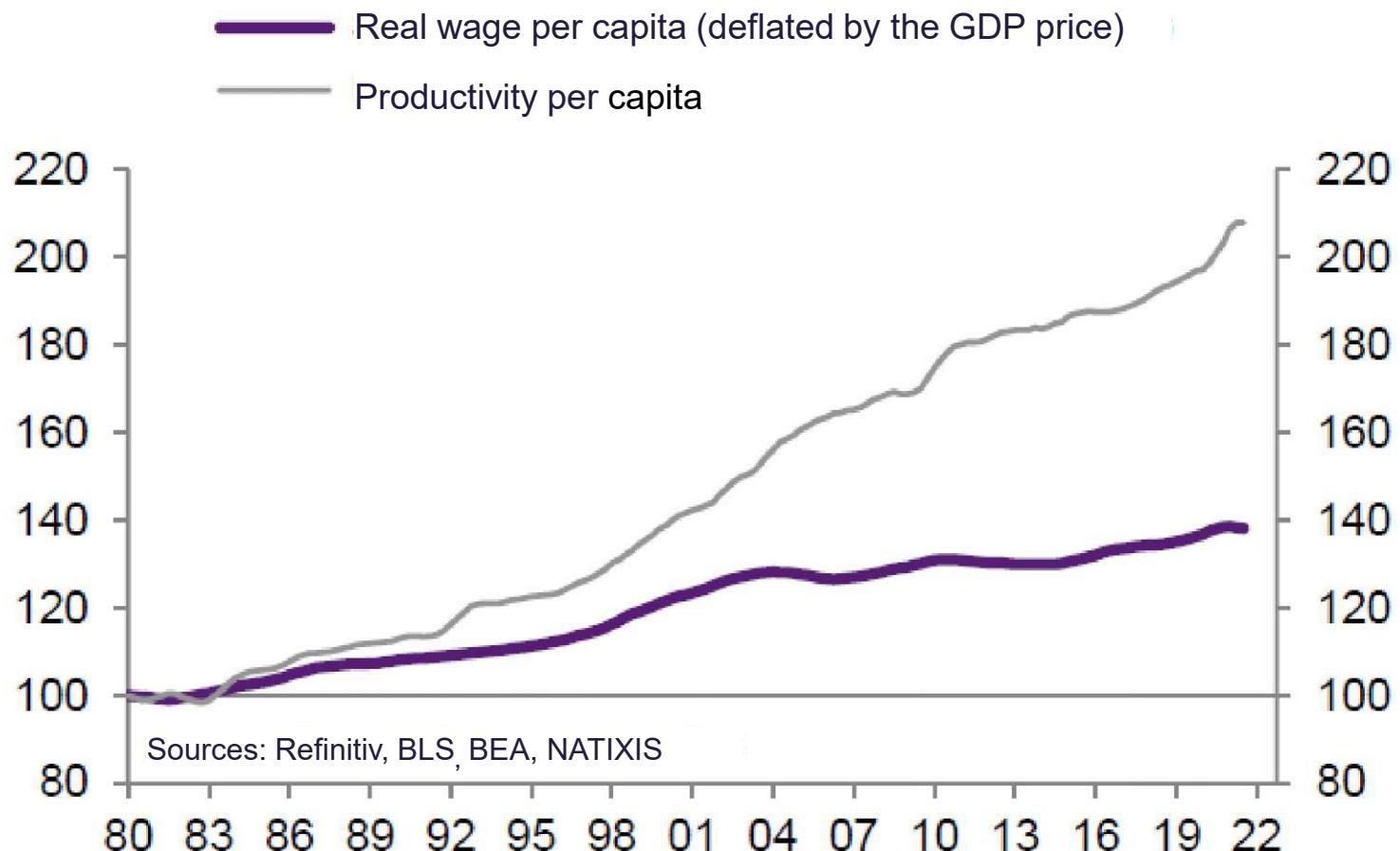
UNIONISATION RATE (AS A %)



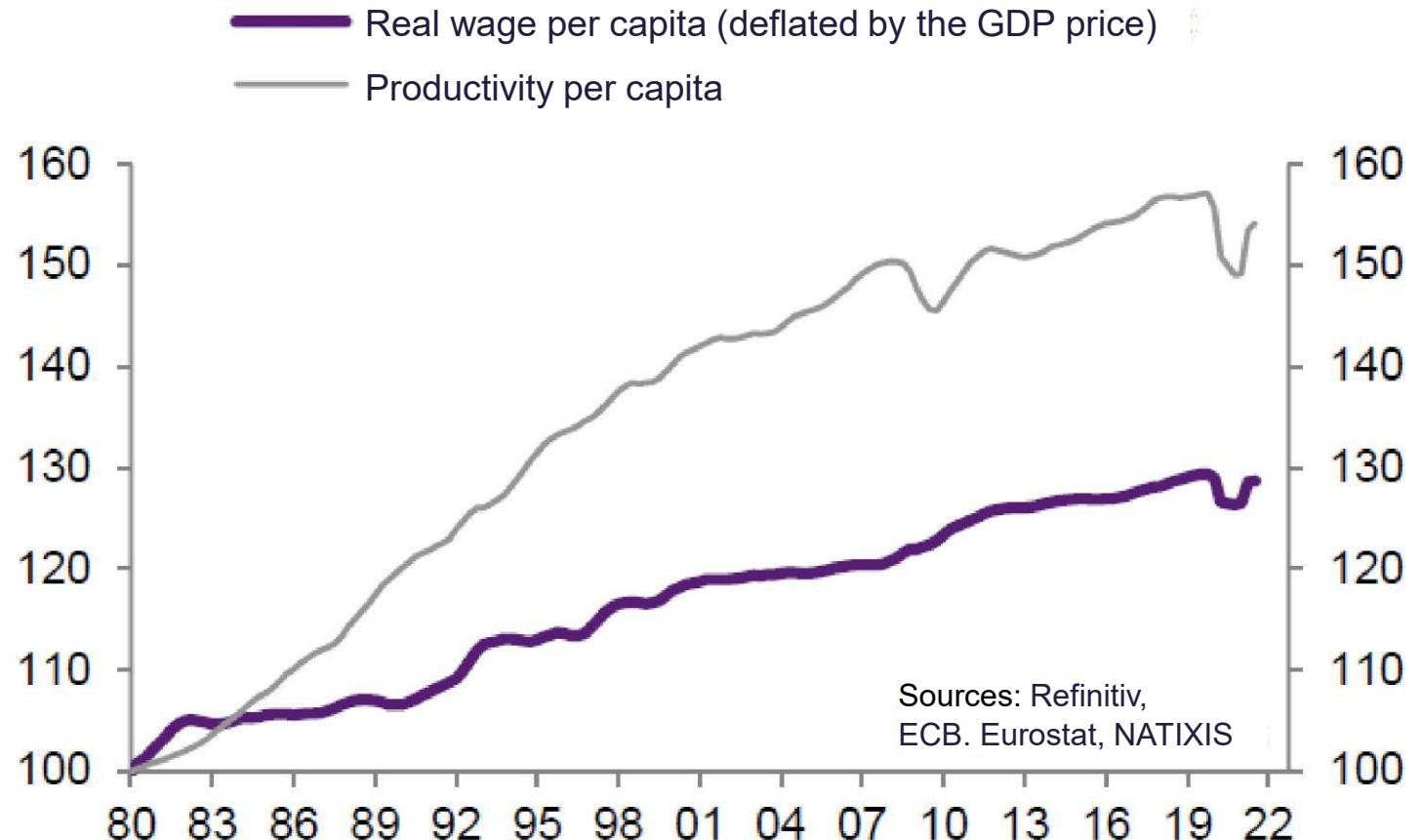
For 40 years, real wages have risen slower than productivity in the OECD on average

- Except in France

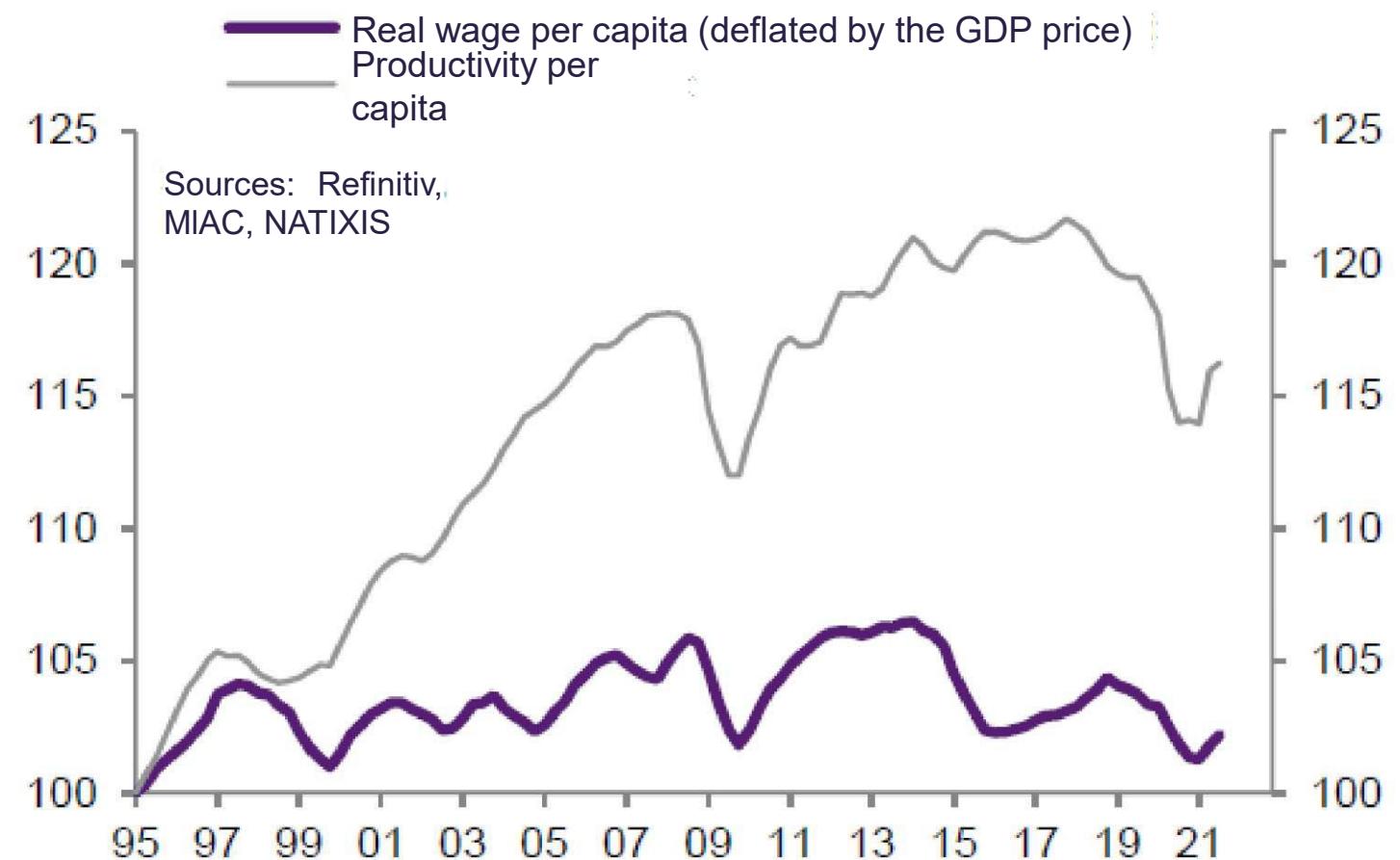
UNITED STATES: REAL WAGE AND PRODUCTIVITY PER CAPITA (100 IN 1980: 1)



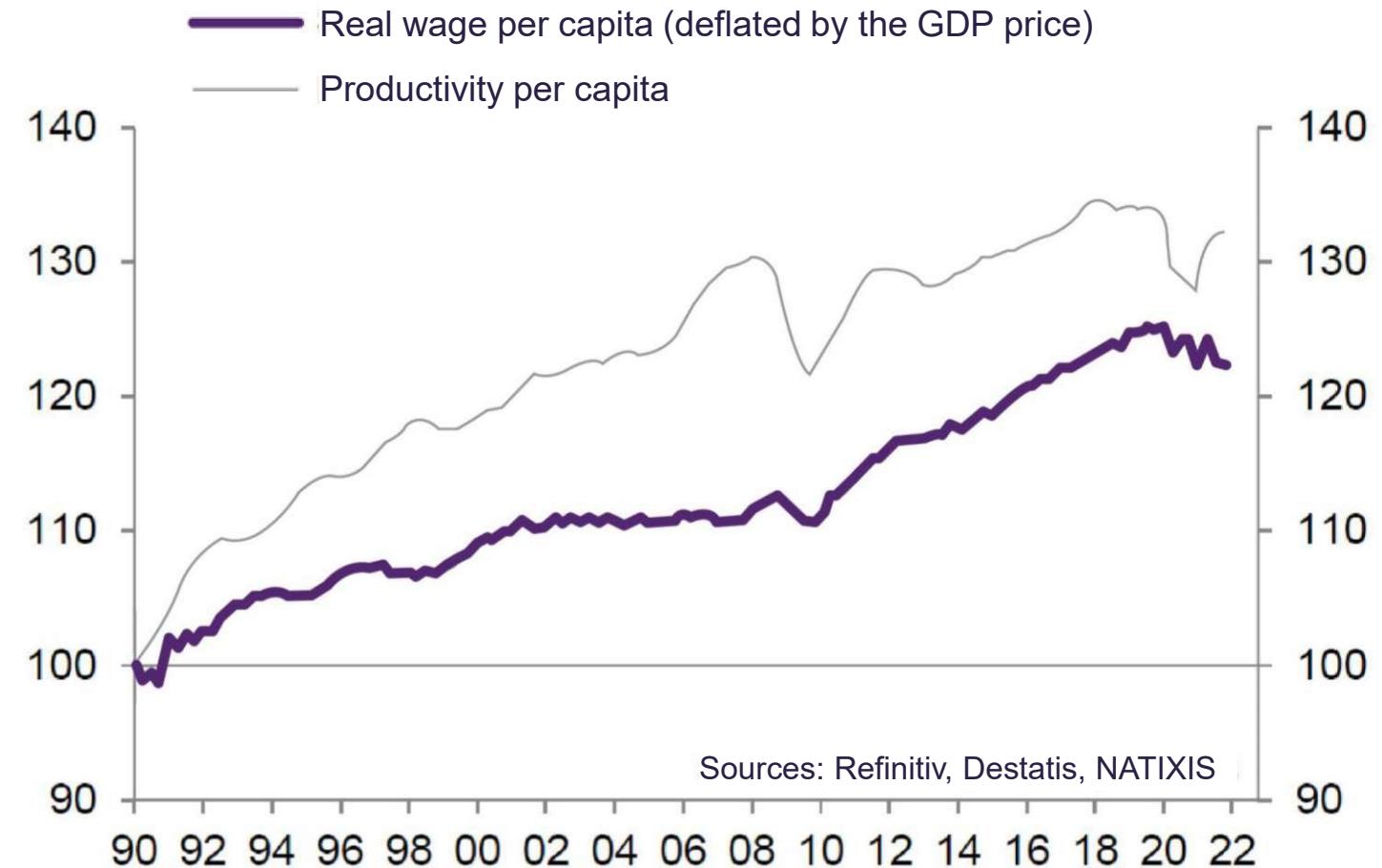
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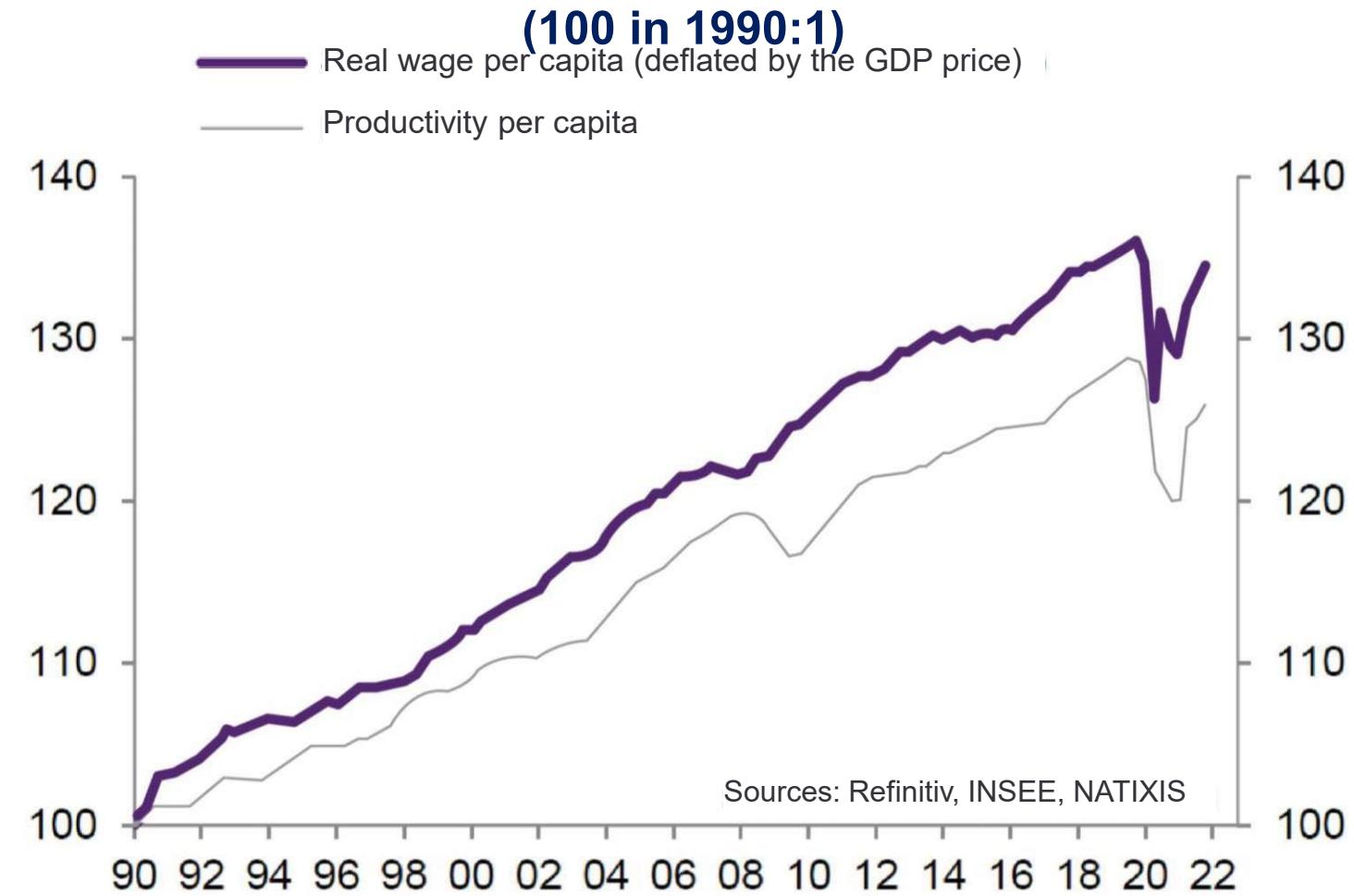
JAPAN: REAL WAGE AND PRODUCTIVITY PER CAPITA (100 IN 1995: 1)



GERMANY: PRODUCTIVITY PER CAPITA AND REAL WAGE PER CAPITA (100 IN 1990:1)



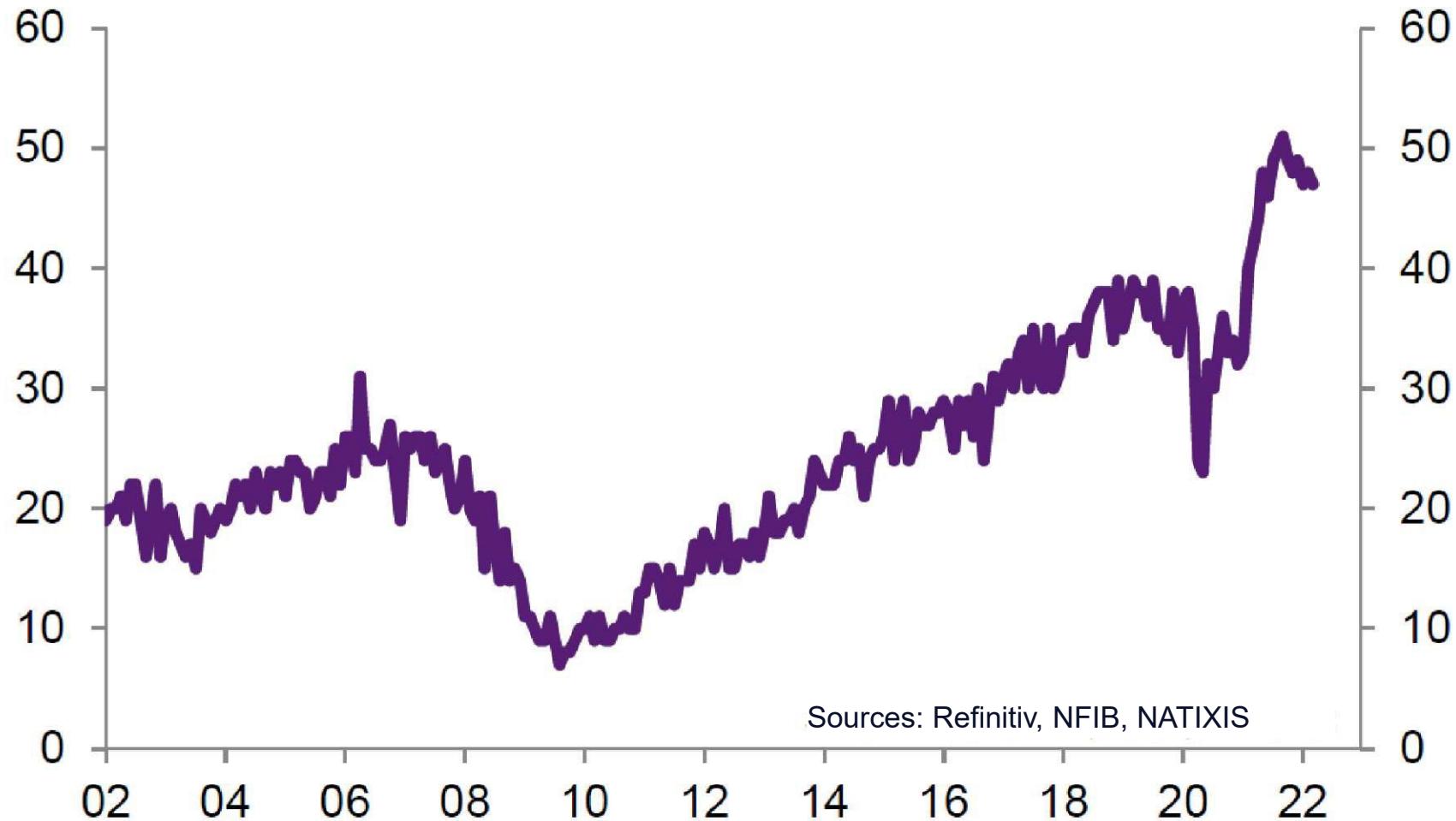
France: productivity per capita and real wage per capita



In an environment where labour shortages are found in many countries and in all sectors, those with high value added and those with low value added,

The resulting pressure increases the possibility of a change in cycle and provides support for wage inflation

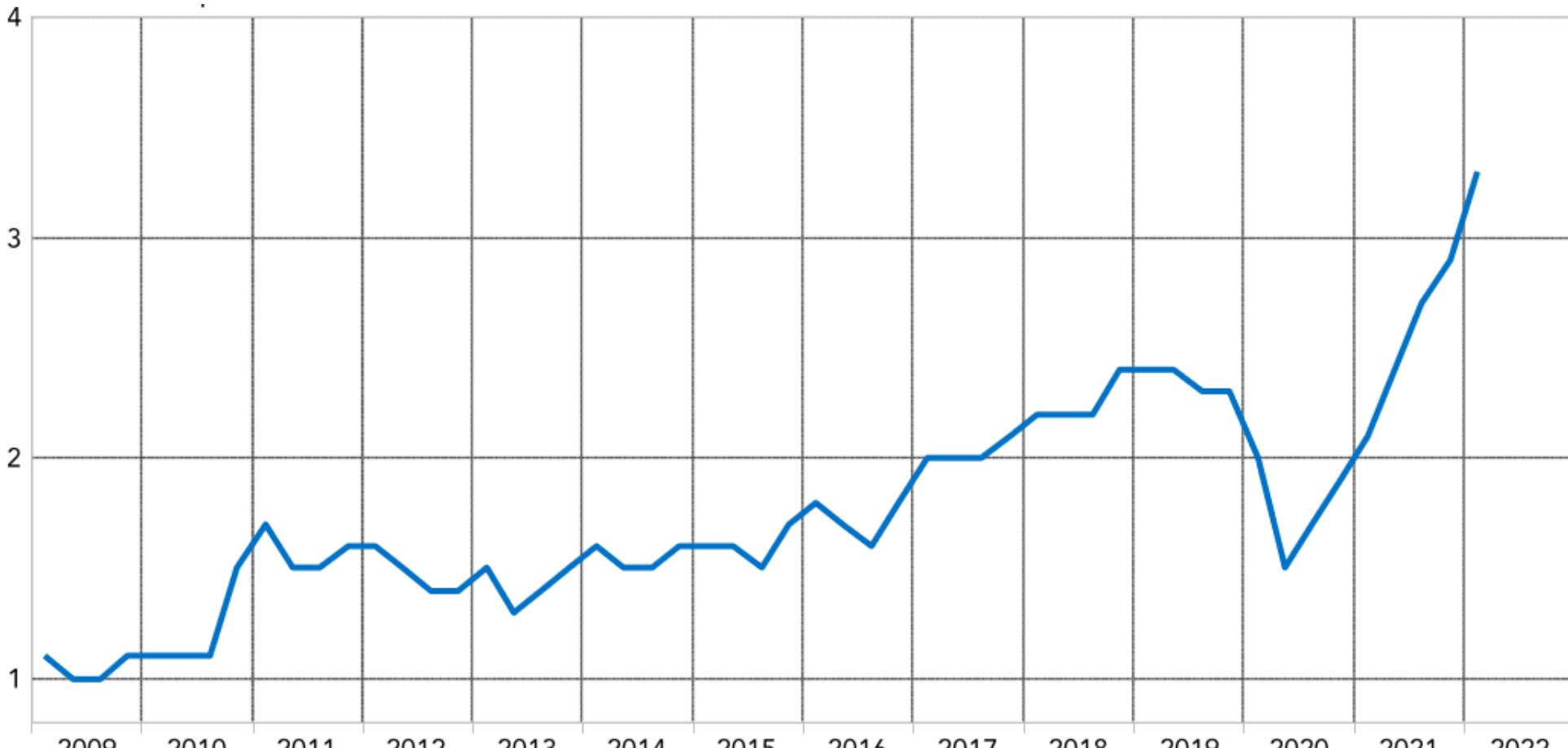
United States: proportion of companies having recruitment difficulties (as a %)



EUROZONE

JOB VACANCY RATE IN THE WHOLE ECONOMY

As a % of total employment



Source: Eurostat

An inflation regime change dynamic, due to:

- ✓ Gradual indexation of prices to prices, wages to prices and wages
- ✓ This regime change dynamic is not predictable by business models
- ✓ And when it is detectable in the figures, it is too late - partial deglobalisation

In addition, persistently high cost of the energy transition

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Monetary policy must combat inflation:

- The benefits of low (but not too low) and stable inflation versus the dangers of an inflationary regime
- Slowing demand (supply/demand)
- Not letting the “de-anchoring” of expectations (generalised indexation) take hold
- Therefore, at a minimum, leading monetary policy to neutrality, i.e. raising real interest rates to the level of the potential growth rate, by increasing short-term rates and by quantitative tightening
- Acting with determination and clarity

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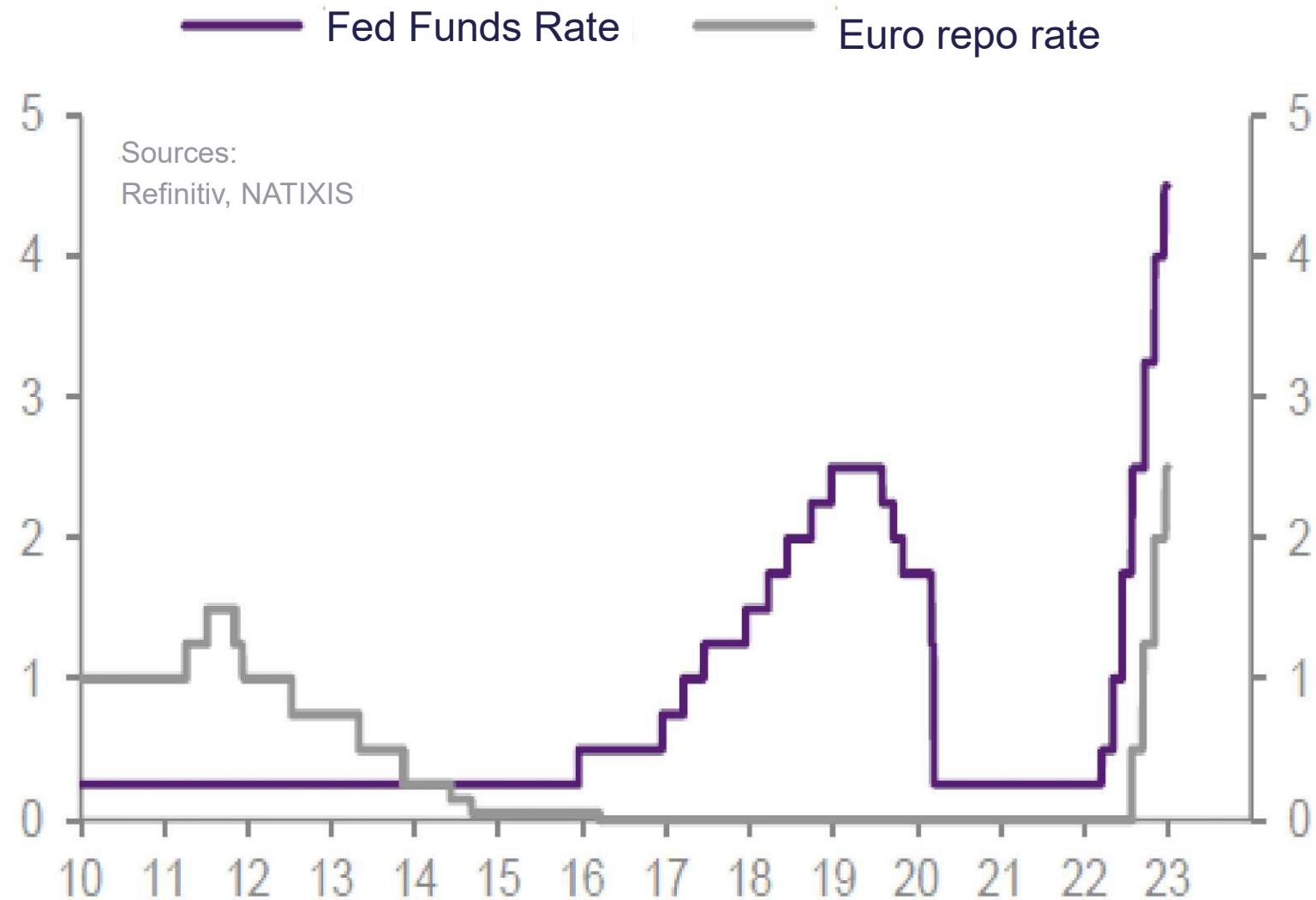
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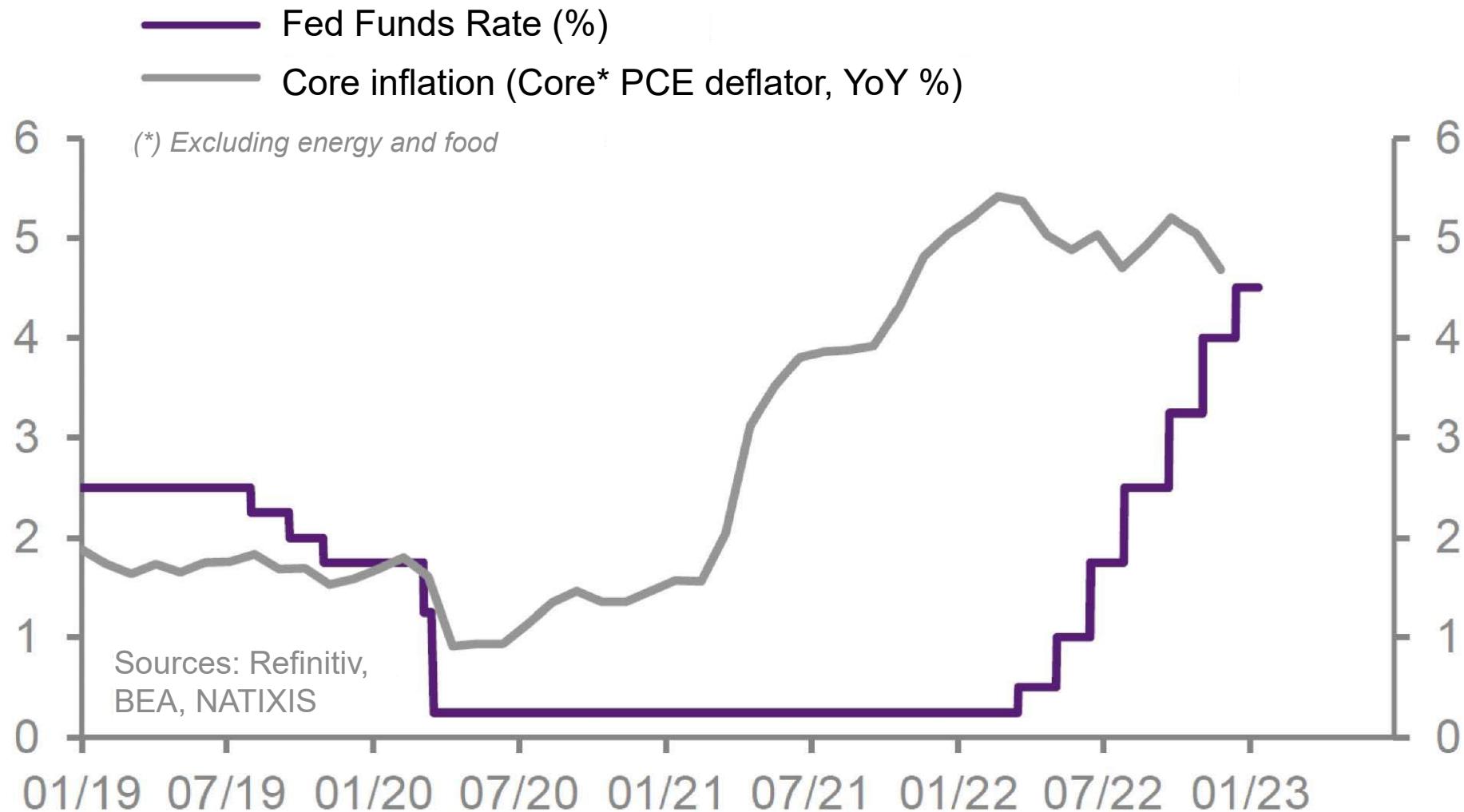
HOW?

- Implementation of quantitative tightening
- Rise in short-term interest rates and upward trend in long-term interest rates
- But in a potentially explosive situation of the dynamics between inflation, interest rates and debt

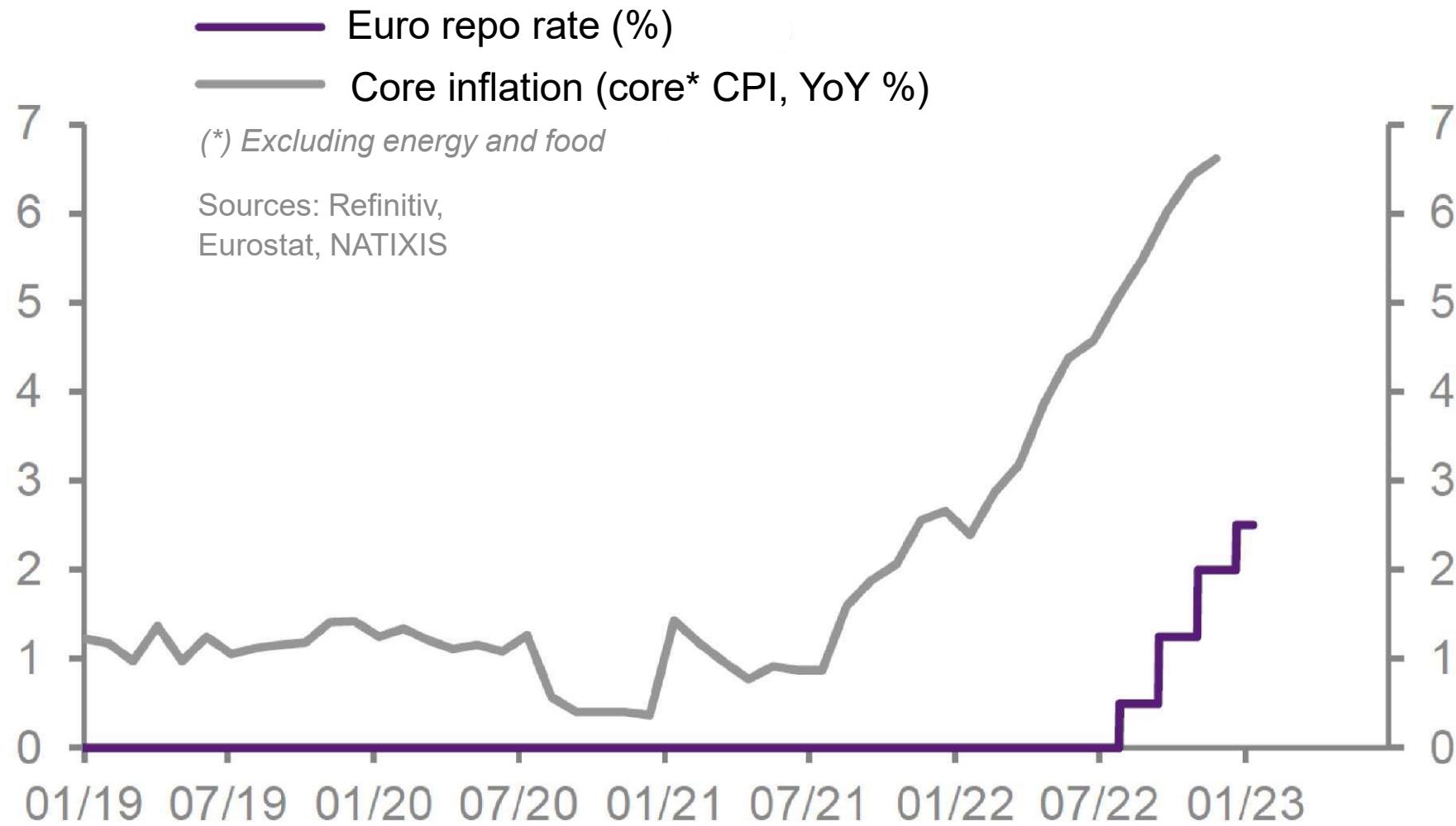
CENTRAL BANK INTERVENTION RATE (AS A %)



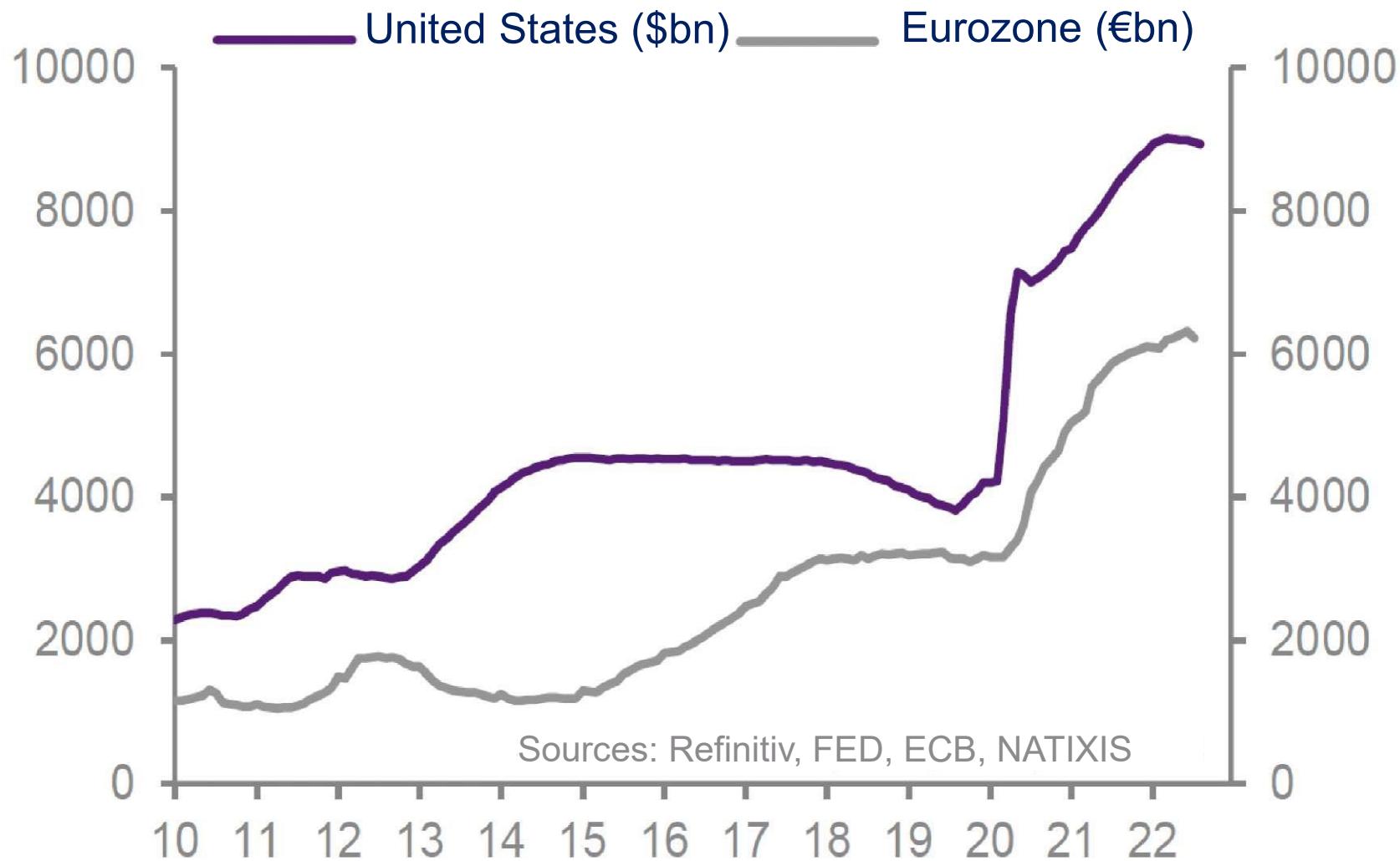
US: FED FUNDS RATE AND UNDERLYING INFLATION



EUROZONE: EURO REPO RATE AND CORE INFLATION

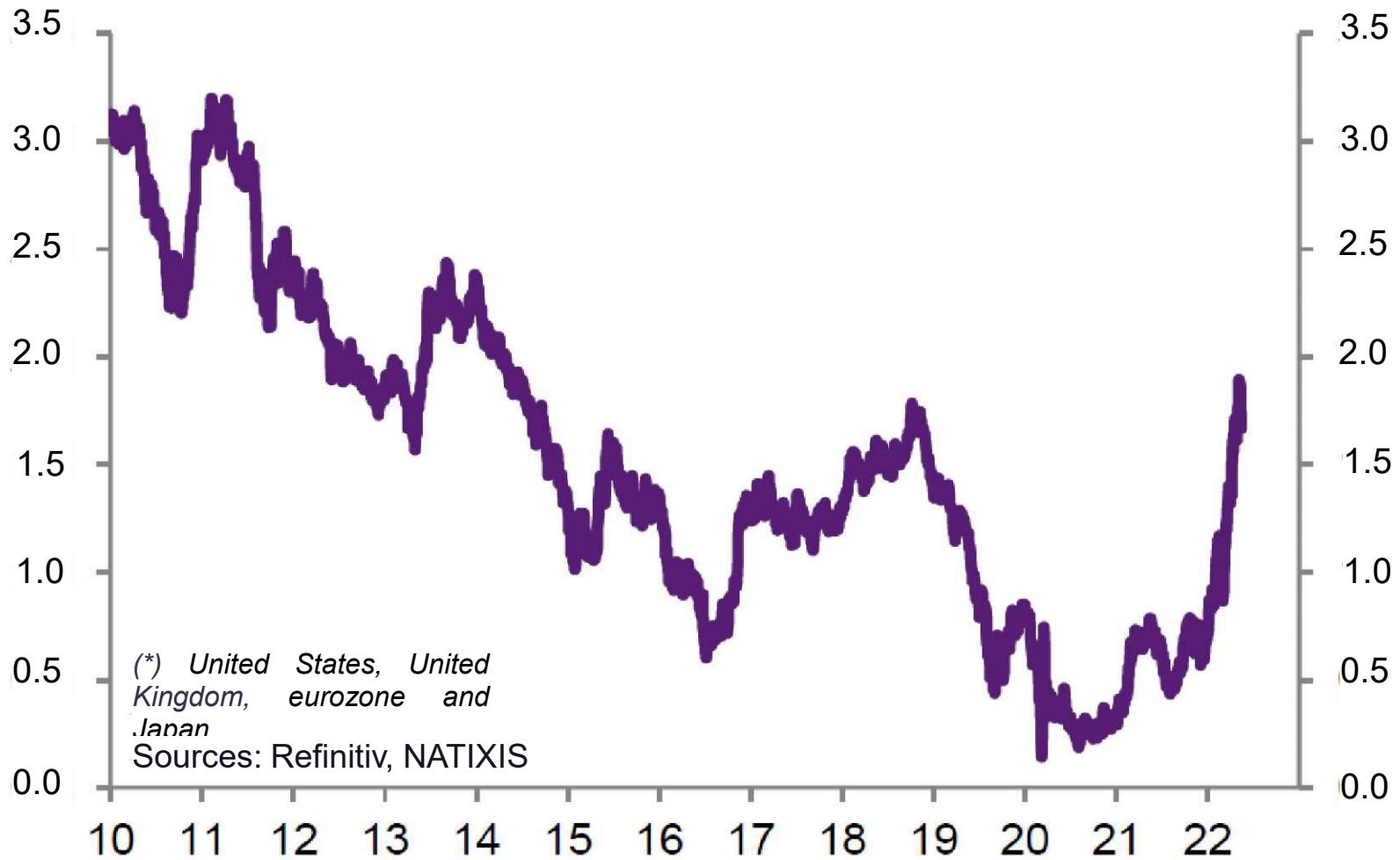


MONETARY BASE (LOCAL CURRENCY)



OECD*: 10-year interest rate on government
BONDS (AS A %)

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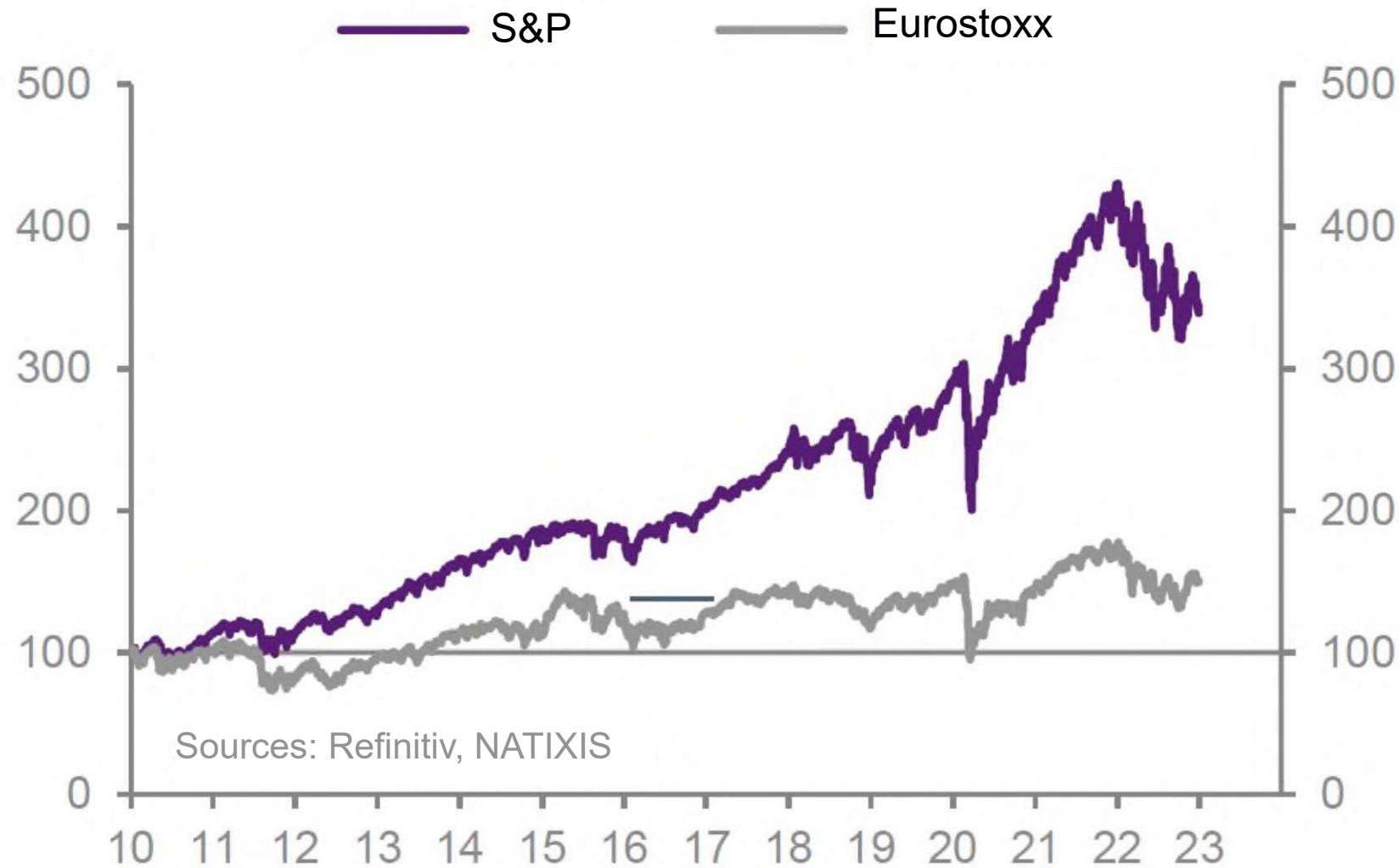
UNITED STATES: INTEREST RATE ON GOVERNMENT BONDS (AS A %)



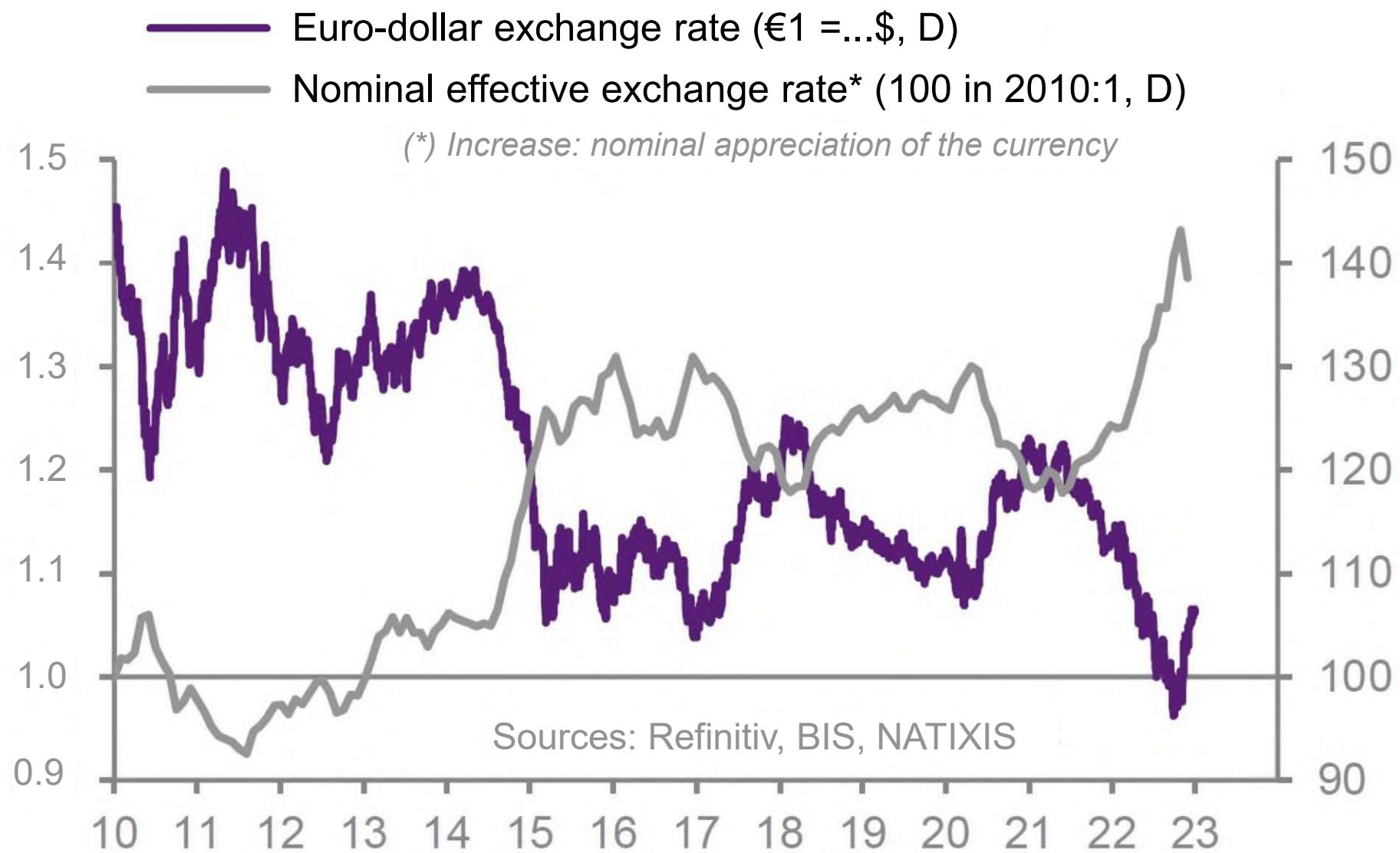
10-YEAR GOVERNMENT BOND YIELDS



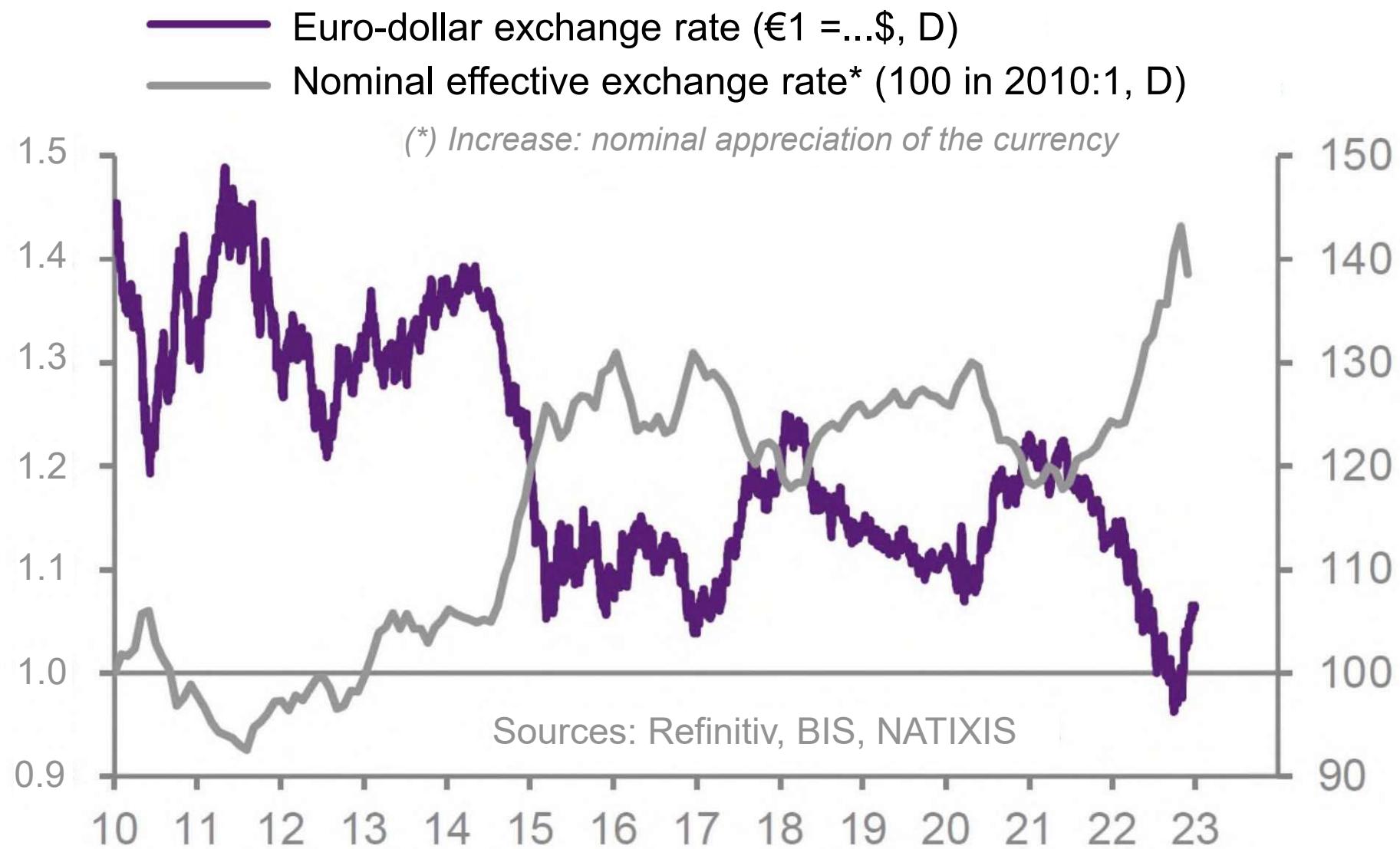
STOCK MARKET INDICES (100 IN 2010:1)



UNITED STATES: EXCHANGE RATE



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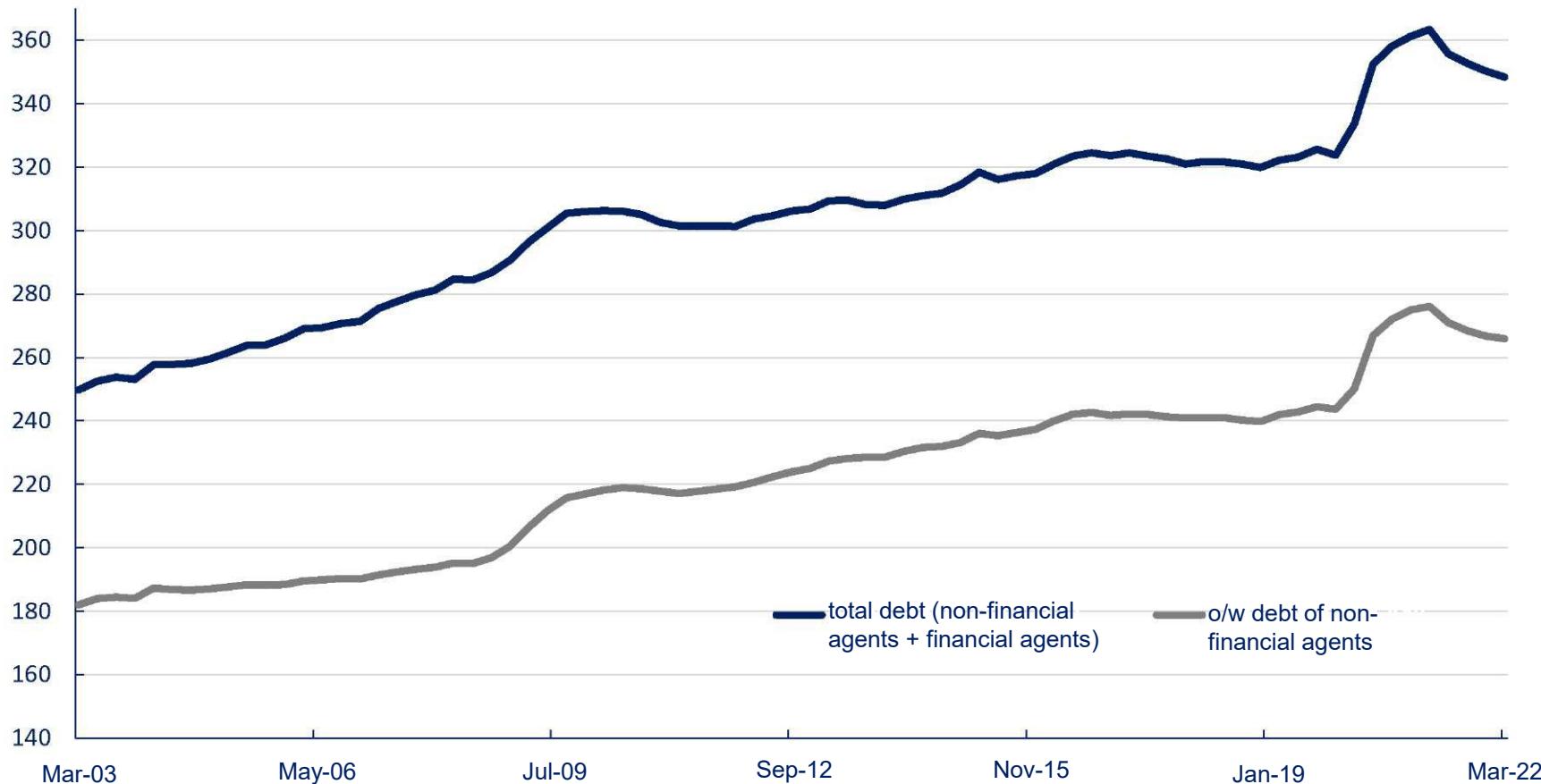
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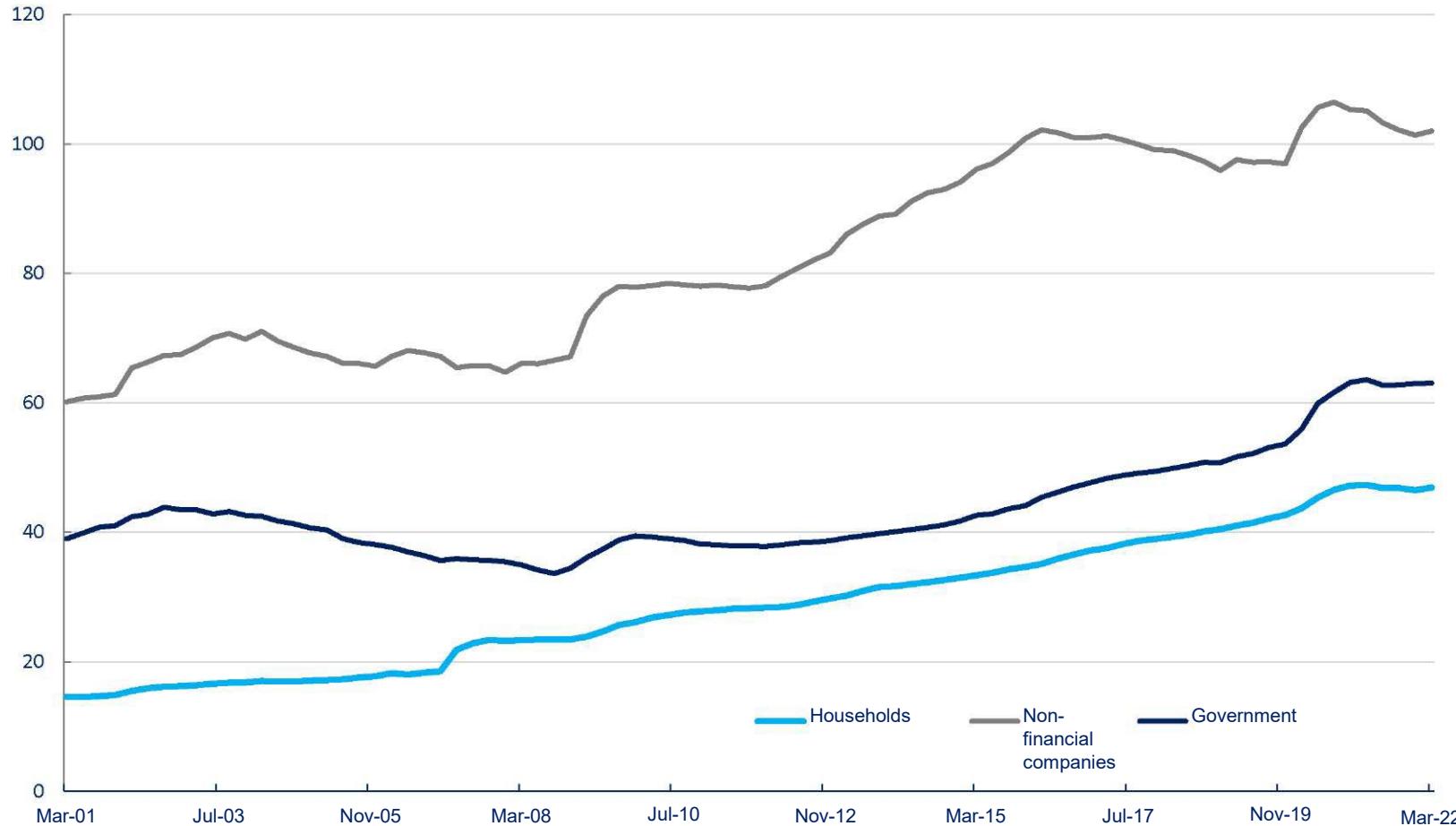
GLOBAL DEBT

(% OF GDP)



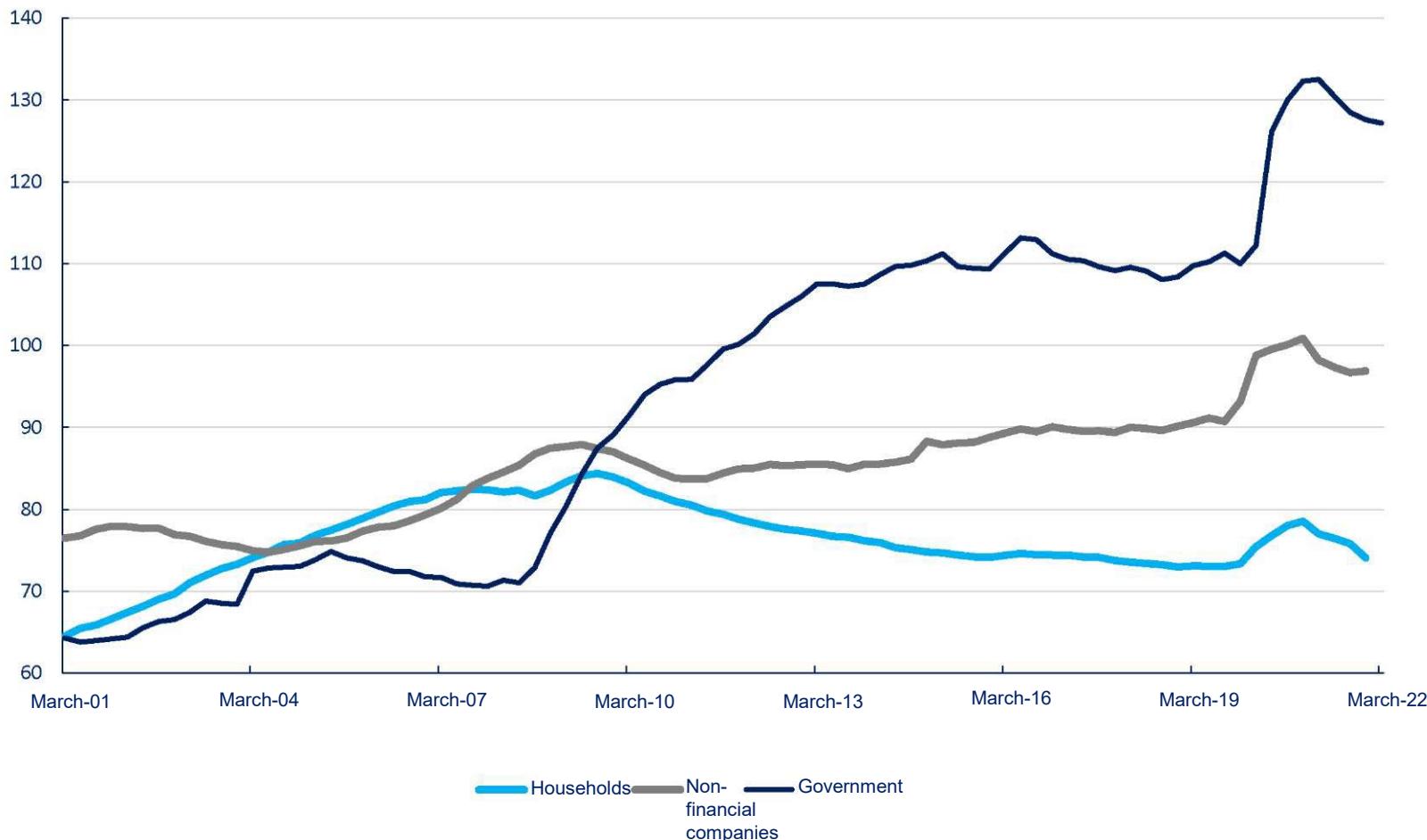
Sources: IIF

DEBT OF EMERGING COUNTRIES (% OF GDP)



Sources: IIF

DEBT OF ADVANCED COUNTRIES (% OF GDP)



Sources: IIF

CHANGE IN TOTAL NFA DEBT (% OF GDP)

total AIMF Debt (MGDP)	Dec-00	Dec-08	Dec-18	Dec-19	Dec-20	Dec-21	March-22
Advanced countries	210	239	264	274	321	289	281
EM	114	112	189	203	243	227	230
United States	187	240	251	255	296	281	275
Japan	308	313	372	381	423	422	425
Eurozone	198	229	258	258	289	279	273
Germany	201	199	186	186	205	204	199
France	200	237	316	325	374	358	353
Italy	192	224	252	258	299	282	276
Spain	181	256	265	264	310	295	284
United Kingdom	176	239	262	264	306	289	271
China	132	139	254	263	292	287	292

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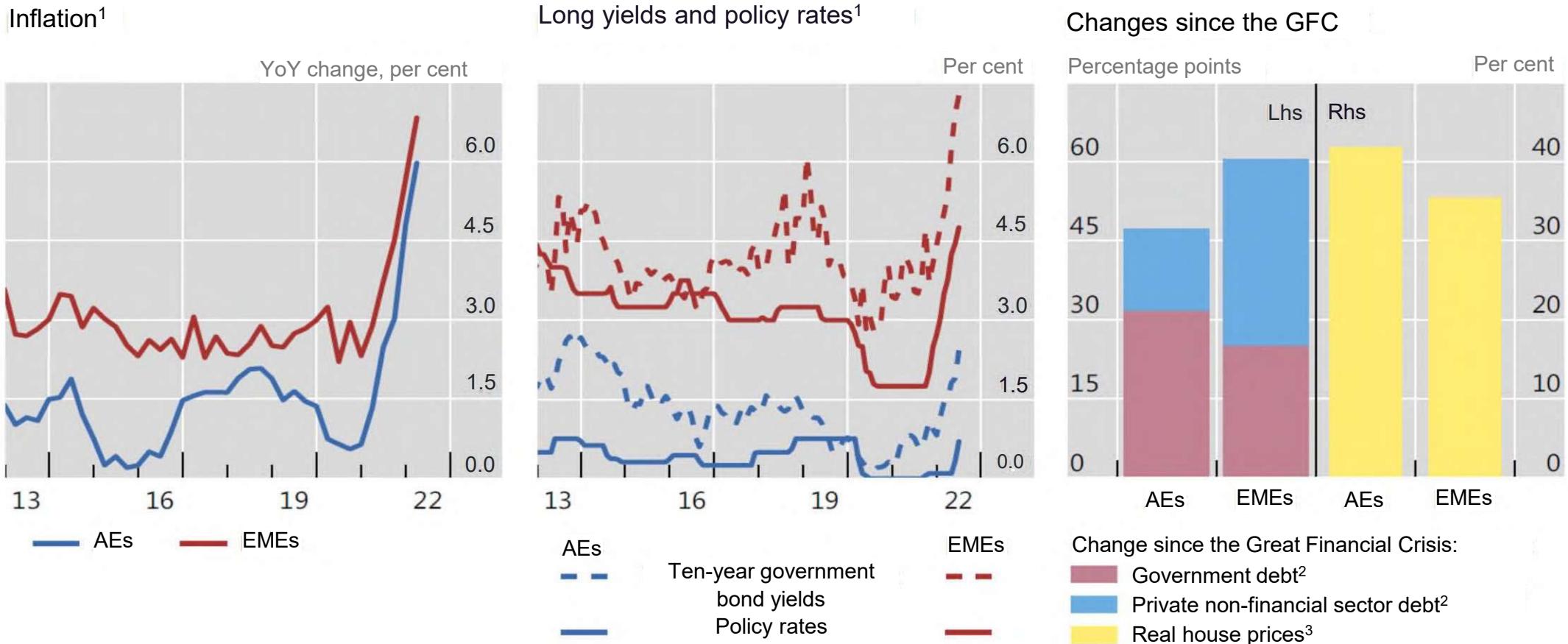
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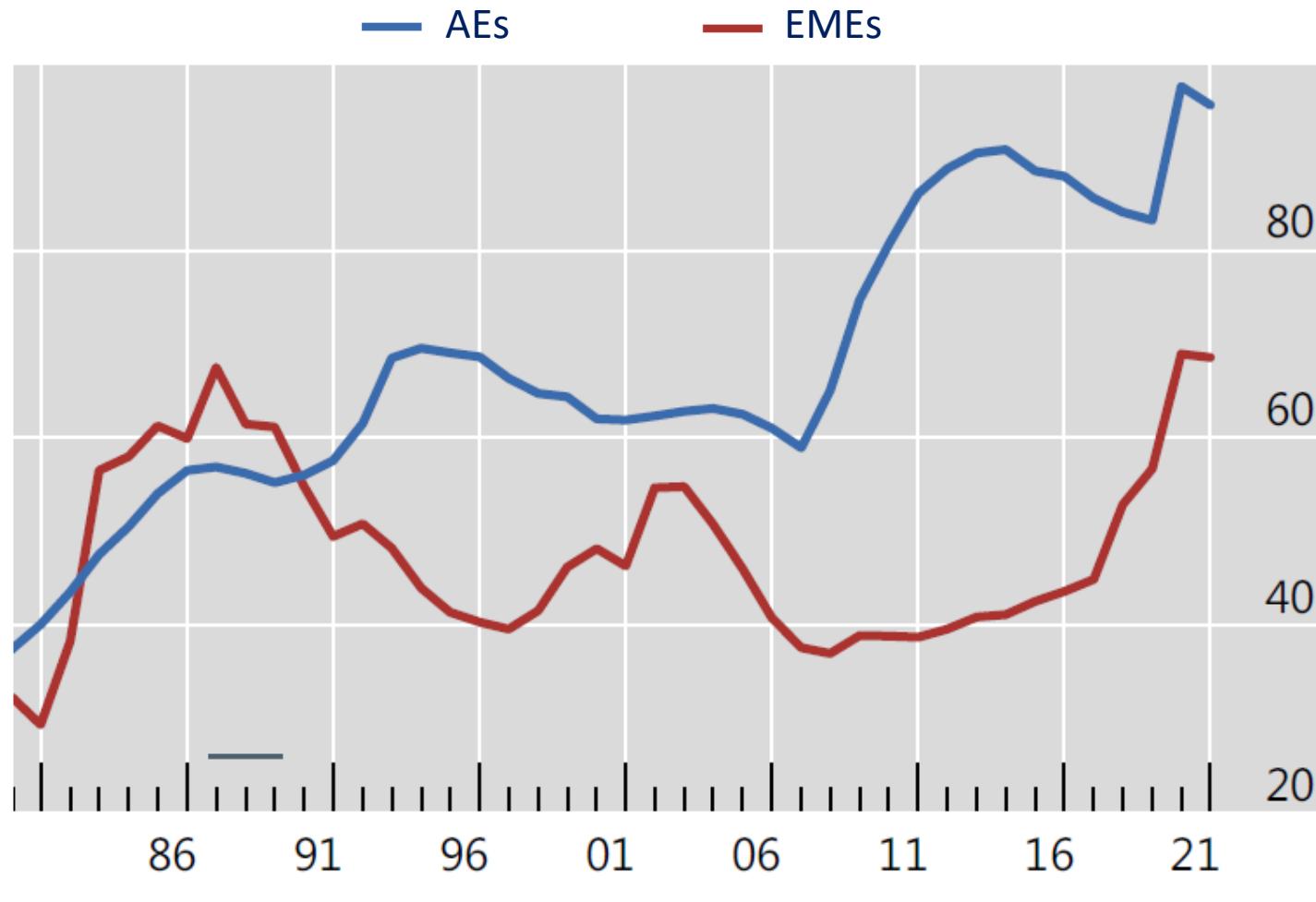
A PERFECT STORM BREWING?



¹ Median of 11 advanced economies (AEs) and 21 emerging market economies (EMEs). Q3 2008. ³ Median change in the debt-to-GDP ratio since Median change in real property prices since Q3 2008.

Sources: Bloomberg; national data; BIS; BIS calculations.

PUBLIC DEBT AS A PERCENTAGE OF GDP



Monetary policy is therefore very constrained and must follow a very narrow path of exiting with determination and with caution from its very accommodative stance:

- To avoid the danger of a sudden bursting of bubbles and an insolvency crisis due to high public and private debt rates
- And to avoid, as far as possible causing, by raising interest rates, a deep recession, by altering the demand trajectory too sharply
- In addition , in the supply/demand imbalance, monetary policy cannot increase the supply of imported products , it can only influence the level of domestic demand in the short term
- And fiscal policies are themselves already very constrained (levels of public deficits and public debt)

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Structural reforms and policies are essential:

- to increase supply (goods and services, but also work) in both the short and medium term
 - to raise the level of potential growth (to facilitate the resolution of the debt problem, as for public revenues)

THANK YOU FOR YOUR ATTENTION