# DANIEL DAIANU

## Member of the Board of the Central Bank of Romania; former Finance Minister of Romania

I will say a few words on the workshop on economy and finance which was chaired by Jean-Claude Trichet, the former President of the ECB. I will mention the members of the panel: Marek Belka, the President of the National Bank of Poland; Korn Chatikavanij, former Finance Minister of Thailand; myself, as a member of the board of the Romanian Central Bank; Bozidar Djelic, former Deputy Prime Minister of Serbia and currently Managing Director and Head of Central and Eastern Europe for Lazard; Horii Akinari, former Deputy Governor of the Bank of Japan and currently a Special Advisor to the Canon Institute for Global Studies; John Lipsky, Senior Fellow of the Foreign Policy Institute at Johns Hopkins University, and former First Deputy Managing Director of the IMF; and Jean-Pierre Roth, Chairman of the Cantonal Bank of Geneva.

The workshop had three chapters. The first one was the state of the global economy and global economic dynamics. The second chapter, which was not initially envisaged but occupied a substantial chunk of our time, was about monetary policy idiosyncrasies, and finally, we had the state of financial reform. When it comes to the state of the global economy, and I am trying to escape my intellectual prejudices to be as balanced as possible, what was in a way a signal that things were not so bad was that the numbers do not so bad if longer-term trends are considered. However, at the same time one has to accept the reality that the forecasts, which have been invalidated for years by dynamics, show that there will be lower economic growth rates in the immediate period to come.

What does this indicate? There is still much that gives us food for thought, and one has to link it with what some people have called secular stagnation and the lack of investment. The investment deficit is quite a worry for all of us. Investment rates have plummeted all across the industrial world, and these are numbers that were not necessarily mentioned yesterday, but the OECD's analysis of what the economic commission, the IMF and the World Bank do showed that investment ratios have come down quite dramatically in the industrialised world. It is happening in other parts of the world.

The big question here, which was both explicit and implicit, was whether this is linked with getting back to normal rates, because there has been tremendous resource misallocation over the past 20 years, so if we continue along the same lines with investment, it will not be very fruitful. Several participants emphasised, on the other hand, that if we do not invest sufficiently, we cannot have high economic growth rates and may continue economic slowdown. We will not, on the other hand, be able to capitalise on the new technologies, although it may also be the case that investing in the new technologies may not demand as much investment per se as used to be the case when investing in infrastructure, for example.

Then there is clear evidence that there are major differences among the regions. There is an economic rebound in the US; and one could even say that US economic growth rates are above the potential growth rates, and the American economy has narrowed the output gap significantly. This is not the case in Europe, and I remember people from the Commission saying that the output gap in Europe is between 4% and 5%, so there is a lack of aggregate demand in Europe, which is substantiated also by the relatively large current account surplus run by the Euro area.

Therefore, the obvious question is what to do about it, especially in Europe, if this is the case. When it comes to Asia, Japan is muddling through; it is the old story. What is quite a novelty, and this is something of recent vintage, is that China is apparently trying to move to a different growth model, and this is not easy to do. It is not easy for China as a growing economy in the global space, but there are also implications for the global economy in this change of the growth model. There are regional implications in terms of the impact on other economies in Asia.

Another policy dilemma of major concern in the emerging economies of Asia is whether we need to go to another growth model. This is also a big question. What was not said yesterday, but was easy to detect from our friend from Thailand, was whether we are threatened by the middle-income trap, because if we do not continue to grow as we used to, then we have a problem, as it will be very hard to catch up. Secondly, there are worsening conditions in the global economy, and if we do not grow we will have a very hard time explaining to a very restive population why the economic growth rates are not continuing.

Another big issue in our debate was secular stagnation and whether there is such a syndrome. This is a very topical issue; it is intensely researched and there is much debate about it. There were several lines of reasoning yesterday; one was linked with our colleague and friend from Japan, who alluded to the economic reconstruction after the Second World War. There was another argument which brought forward the demographic issue, and demography is a huge challenge in the industrialised world, but in emerging economies there is also declining productivity. However, declining productivity is not something recent, and if one looks at a long-term series, there has been declining productivity, both in terms of total factor and labour productivity.

There are structural trends at work, and this is also linked with technology. One could ask how this is coming, and some people talk about an industrial revolution. How can you think about technology as something which may foster secular stagnation? We have not touched upon this sufficiently, because this is a hugely interesting issue. There are people in leading economies who are now saying that the new technologies are not going to usher in a new industrial revolution, and that the digital world is not going to change. Bob Gordon is one of those, but there are others.

Therefore, thinking about that overhang, Ben Rogoff is one of the proponents of this thesis combined with the balance sheet effect, which is also something that has to be considered given the size of public and private debt, it is having an impact on the propensity to save and also to invest. One can figure out explanations of what drives economic growth and economic slowdown, which might not necessarily be bad if we think about climate change. This is something we also have to consider. We might be addicted to very high economic growth rates.

Finally, I would mention a few symptoms of big difficulties, not to say crises, in our economies. We still rely on unconventional methods in policymaking, and it is very unusual to rely for so many years on unconventional measures. It is not clear to us what the unintended consequences might be. For example, the experts keep warning us about bubbles in the making and that the prices of financial assets are going skyward, and we continue resource misallocation by investing in some of these. Regarding resource misallocation, one of the participants said that companies, unfortunately, are staying on this path, but there is not much investment, and this is a worry. It shows enormous risk aversion and fear about the future. There is no confidence, and this was also linked with the issue of trust, but trust is multidimensional. I am talking about the relationship between governments and people and the lack of trust in the future. We also have strange societies against the background of rising income inequality, and we also have rapidly growing populism and demagoguery; this is also an issue, and we know about it in Europe, with a rapidly-changing political landscape, which should worry us.

The second chunk of our discussion was on monetary policy issues, and here I refrain from mentioning names, but I still want to point out what Marek Belka programmes. The QE programmes, and this is a view I share, have helped to rescue the financial sectors, but they have amplified the power of finance over the real economy, and this is what we have to think deeply about over the period to come. However, this is probably inevitable, as policymakers face trade-offs and very difficult policy dilemmas. Central banks have clearly rescued financial sectors, but they have turned into a factotum. There is so much people are asking central banks to do, and there has been a sort of fiscal dominance, because they have taken over much more than the mandates they were given. There is a financial dominance because they need to rescue banking sectors.

Central banks have a very hard time in reaching inflation targets; this is also something which is mind-boggling for central banks because such huge quantities of liquidity have been introduced into the system. Therefore, Keynes' concept of the liquidity trap is still operating very clearly and powerfully. There is divergence between what the Fed is planning to do and what the ECB is planning, and there continue to be big policy dilemmas for central banks. When it comes to finance, and we probably did not have enough time to talk about reform, but there is reform of the regulation and supervision of finance. It was strongly emphasised by Mr Trichet that one should not underestimate the fact that a substantial amount of policy coordination is being done in the framework of the G20 and the Financial Stability Board. The total loss-absorptive capacity, not only as a concept but as one which will be operationalised, is a fruit of this sort of policy coordination.

The concept itself poses questions. It is clear that it will not be the saviour, in terms of an effective measure to deal with too-big-to-fail. It might be that, because of the size of major actors in the global economy, a lender of last resort will continue to be needed in spite of rising gaps in liquidity requirements. There was also mention of something which is sometimes underestimated when trying to judge why the US was more capable of cleaning up the slate than Europe. We should not forget that capital markets play a much bigger role in the American economy as against Europe, where we rely on banks for 80% of our funding, which is why it has been so hard to clean it up. The Glass-Steagall Act was also mentioned, and there is a problem with universal banking. It is hard to manage complexity and very large entities, and there are trends in terms of what is happening in Switzerland, the UK and most recently with Deutsche Bank, which shows that people are thinking about it and trying to adapt.

Finally, there is a culture issue. Banking has to change, and it has to change both physiologically and culturally. There is an ethical issue in terms of how banking treats the rest of the economy and citizens at large.