# VINCENT KOEN

## Deputy Director of Country Studies at the OECD

**Jean-Claude Trichet, former President of the European Central Bank, Honorary Governor of the Banque de France**

Thank you very much, Gabriel. The introductory remarks are limited to six minutes but after that we will have a discussion and respond to questions from the audience. You have the floor for six minutes, Vincent.

**Vincent Koen, Deputy Director of Country Studies at the OECD**

Thank you very much, Chairman, and thank you very much to Mr. de Montbrial and IFRI for inviting me back again to this wonderful event. I am very honored to be part of this panel chaired by central bank and civil service legend, President Trichet, this is really a treat. I will try to give you a tour of the world economic outlook as we see it at the OECD.

Let me start on a positive note. Global growth has held up fairly well over the past three years following the bounceback from Covid and despite the enormous adverse supply shock imparted by Russia's invasion of Ukraine. Of course, this global average masks sharp contrasts across countries. For example, compare the buoyant US performance to the stagnation endured by Germany, or India's dynamism to China's struggle to approach the 5% mark.

Turning to inflation, central banks tightened policies substantially in 2022 and the supply shock that hit at that time has largely faded so inflation is back to more comfortable levels, although service price inflation remains sticky in many countries. Remarkably, unlike in earlier tightening episodes, labor markets have continued to perform quite well overall. The EU area unemployment rate, at 6.3%, is at an historic low as we speak and the US unemployment rate, at 4.2%, is still relatively low as well. In that sense, central banks have achieved something like immaculate disinflation.

However, even if inflation has come down and unemployment is not high in most countries, there is a feel-bad sense among consumers, and consumer confidence has languished in both emerging markets and developing economies. To a large extent, this is the result of the price jump that occurred post-Covid and post-Ukraine invasion with consumers feeling that the most visible prices, the everyday prices you see at the pump and in the supermarket have risen so much more than income in most countries. The lingering sticker shock experienced at the supermarket leads to the perception that prices are still rising fast because the price level is so much higher than before even if inflation has actually come down significantly.

While consumer confidence has languished, business sentiment has held up somewhat better, especially in services, and this tends to convey a more accurate sense of what economic momentum there is at the moment. Against this backdrop, for the G20 countries the OECD forecasts, fairly reassuringly, that growth will continue at the global level to cruise around the 3% mark, which is also true for the OECD average. However, again, performance is highly variable across countries. Our inflation forecasts are also reasonably reassuring even though inflation remains very high in some emerging market countries and uncomfortably low in China, where it flirts with deflation.

Turning to the risks following this seemingly benign baseline forecast, one risk relates to energy prices which could very well spike again, notably if geopolitics take a turn for the worse. Second, uncertainty surrounding trade policy has soared over the past few weeks. Many outfits have cranked out trade wars scenarios with various assumptions about how sweeping and how high tariffs may be, how fast they might come into place, for how long, for whom and with various assumptions about how exchange rates would react in this context and trade diversion, notably from China to Europe. However, at the OECD we have refrained from speculation about what we cannot yet calibrate in our models. Of course, we do worry that a more fragmented, protectionist trading environment and inward-looking policies would hurt supply chains, raise prices and reduce competitive pressures that deliver productivity gains. This is very much in line with the theme of this year’s WPC, and I trust that Jean-Marie will have a lot more to say about this.

Another risk pertains to public finances, which in most countries are in poor shape. One factor that supported growth in many economies during and after Covid is fiscal support in various guises, but some of that support turns out to be hard to unwind. For example, Japan and Korea repeatedly extend energy subsidies contradicting their commitments on climate change and even though energy prices have come down. Public debt ratios have reached new highs in advanced countries, in EMEs and low-income countries. At the same time, spending pressures associated with aging populations, climate action and defense priorities – and this week the NATO countries are discussing how to bring defense spending up from 2% to 3% this year – all these pressures are building up on the fiscal side and interest rates are unlikely to go back to the near zero era we experienced before Covid. The BIS also echoed this concern just two days ago in their quarterly report.

Turning to policies, we see central banks continuing to ratchet interest rates down somewhat; the ECB cut by 25 basis points again yesterday, the Swiss National Bank by 50, the Bank of Canada by 50, and the Fed may also cut again next week. The only outlier here is Japan, which continues to normalize monetary policy.

Lastly, as to governments, not only are the debt ratios far above any comfort zone but in flow terms, looking at the deficit numbers, far greater efforts are called for to restore fiscal space and fiscal sustainability.

Our main messages are quite nicely captured by the *Bloomberg, Financial Times* and *Wall Street Journal* headlines.

**Jean-Claude Trichet, former President of the European Central Bank, Honorary Governor of the Banque de France**

Thank you very much, Vincent. I noted in Gabriel's exposition our vulnerability to deglobalization or friendshoring or reshoring, particularly the Europeans and your figures were very striking. The idea that the danger of trade disruption could be considerable is something that is on the horizon of everything we say. I was also very interested in the figures on debt because when I look at outstanding private and public debt today in the global economy and compare that with the same debt as a proportion of GDP immediately before Lehman Brothers, I can see that if this is an important indicator we are more vulnerable than we were before the great financial crisis. For me that means that we have to be very cautious in this respect.