SECULAR STAGNATION II-
WHY IS GLOBAL GROWTH A SHORT STORY?

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Reasons why the global economy is slowing

Declining labor force • Rising inequality and wealth gap• Shrinking middle class • Declining trend in labor productivity • Increasing wedge between productivity and compensation • Risk aversion and weak business investment • Hyperfinance

1. Long-term structural decline of global trade on top of short-term causes

(EU crisis, Brexit, oil prices, deflation, geopolitical volatility…)

- Between1950s-late 1990s: **high import elasticity to global GDP**

1. 1990s: global fragmentation of the supply value chain: 1% increase in GDP leads to 2,2% trade rise
2. Since 2000, 1% increase in global GDP leads to only 1,2% in trade

- WHY? 1990s: China's imports of spare parts and components = 60% of total exports. Since 2000, decline to only 35%
- Global supply sources are scattered across many countries : bad news for South Korea and Asean countries
- Mounting protectionism

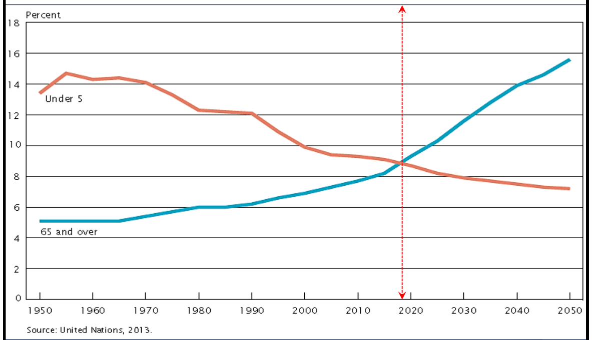
2. The **demographic tax** of unprecedented pace of aging

- Aging will reduce aggregate annual economic growth by 0.4 percentage point in 2015-20 and by a much larger 0.9 percentage point in 2020-25 in both OECD and EMCs, due to shrinking labor force, decline in household savings rates, and falling fertility rates

1. By 2030, 34 countries will be ***super-aged*** (populations with > 20% elderly> 65 year): Russia, Thailand, Chile, China, Italy, Germany, Japan…
2. **Policy reforms** to improve labor participations rates, streamline migration, and improve financial flows, can partially mitigate the impact of aging on economic growth.
3. In the long term, innovation and technological progress that improve **productivity** could reduce the impact of the rapid demographic changes

https://www.moodys.com/research/Moodys-Aging-will-reduce-economic-growth-worldwide-in-the-next--PR_305951?WT.mc_id=NLTITLE_YYYYMMDD_PR_305951

Evolution of the age gap in % of global population
1950-2050: « becoming old before getting rich »?



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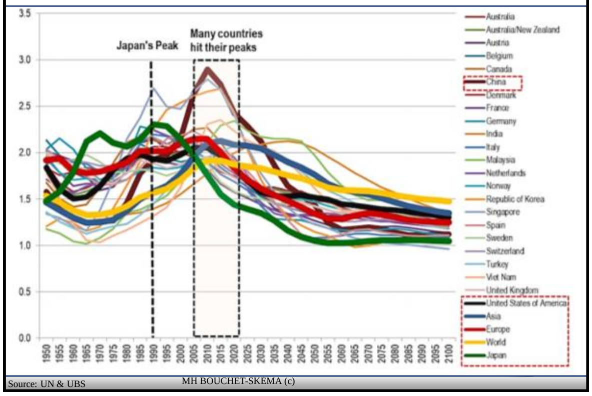
The 'Japanization' of the global economy marked by transition to low growth and low inflation:
Ratio of working-age population/dependent population



Source: UN & UBS
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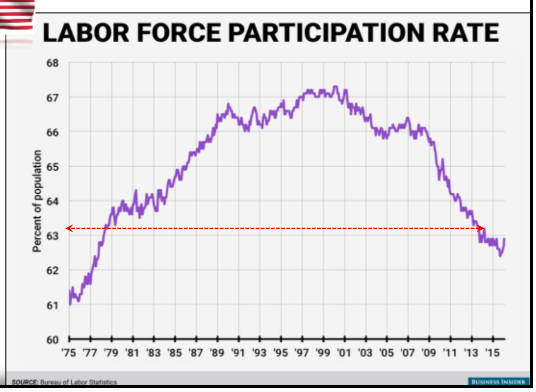
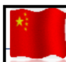
US: Combination of negative demographic trends and automation leads to shrinking working population





China: sharp decline in working age population (15-59)

Source: UN WPP 2015
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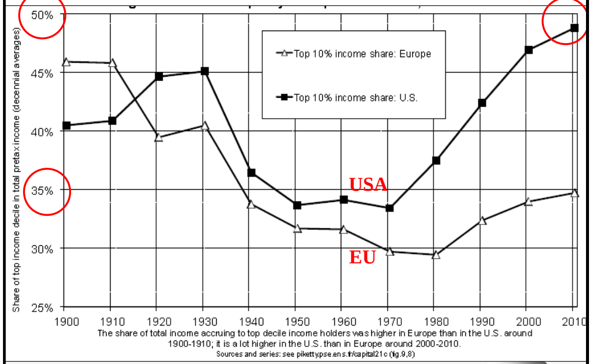
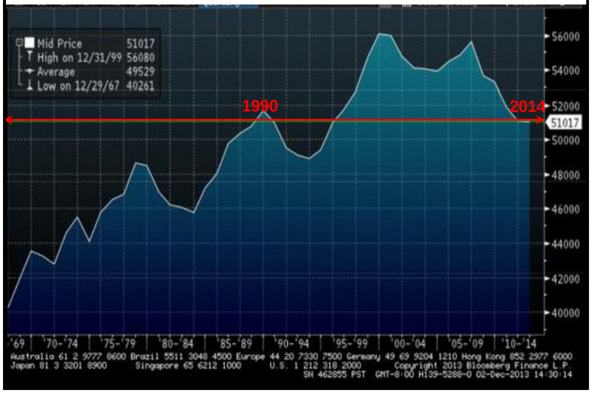
3. Income and wealth concentration since the 1970s

THE WINNER-TAKES-ALL



Declining US « median » income since 1965



Decline in labour share and wage stagnation are holding back the **global recovery (**and threatening social stability?**)**

- In most OECD countries, the labor share in GDP has dropped from >66% in 1990 to 61% today

What explains the declining labor share?

1. Increased productivity and capital-deepening
2. NTICs and automation
3. Increased domestic and international competition
4. Reduction of workers' bargaining power

- Decrease in wage share leads to lower consumption (despite cheap credit) and to lower growth

4. The role of **information technology** in holding back global GDP growth

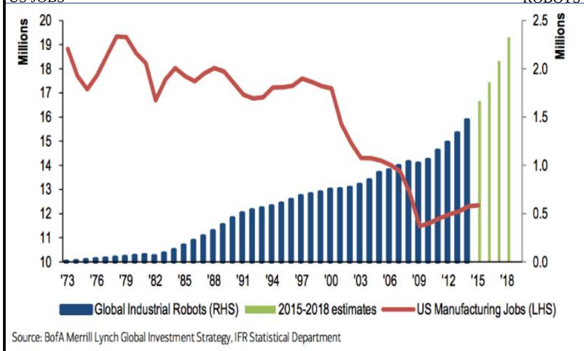
- **Information technology** makes the most dynamic force in modern "cognitive capitalism" **abundant and almost free**!
- Information goods are freely replicable. Once a thing is made, it can be copied/pasted infinitely. Its cost of reproduction falls towards zero.
- The NTIC revolution wave does not demand the creation of higher-consumer spending, or the re-employment of the old workforce in new jobs.
- Collaborative production, using network technology to produce goods and services, is a revolutionary process that cuts prices and slashes the work time needed to support life on the planet

Bad news for wage earners and for old style capitalism!

Source: Paul Mason, The Guardian. July 2015

Long robots, short humans?

US JOBS ROBOTS



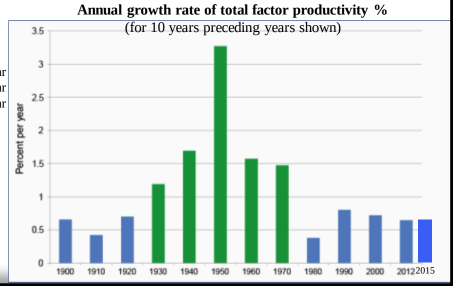
5. Declining trend in **labor productivity** since the 1990s

- Instead of wondering why there was a productivity growth slowdown after 1970, we should ask: can we explain the productivity miracle that occurred in the US economy in 1900-1970?

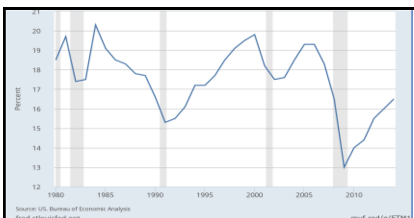
1. LT decline in public and private investment (budget tightening, risk aversion, share buyback)
2. R&D tends to stabilize, not to grow any longer
3. The shift from manufacturing to services also reduces productivity growth

Annual growth rate of total factor productivity %
(for 10 years preceding years shown)

- 1890-1920: 0,5%/year
- 1920-1970: 2,5%/year
- 1970-2015: 0,5%/year

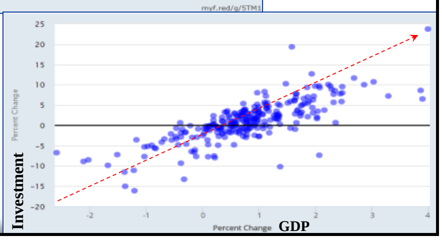


Conference Board 2015



Decline of domestic private capital formation (investment/GDP %) in the US since the 1980s

1947-2015
Co-movement of investment and GDP in the US economy



St Louis FED-2016

New IT generation growth?
The jury is still out

Where is the beef?

- Stiglitz, Krugman, Summers, Martin Wolf…
- Global transformation of value chain and consumer well-being but **no** substantial and lasting impact on GDP
- Temporary and short-lived productivity increase = secular stagnation!

The digital revolution just started!

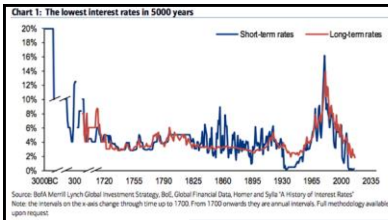
- J Rifkin, Erik Brynjolfsson, Andrew McAfee (MIT), R. Lucas
- Collapse in the price of information = **knowledge** is a prime determinant of LT growth
- **New IT revolution + business innovation**: driverless cars, 3D printing from mass production to production by masses, solar energy, connected objects and connected machines + Big data = gold mine
- Productivity increase potential with positive growth impact!

6. Rising public and private debt tends to create headwinds on growth

Economic Growth Hasn't Kept Pace With Debt

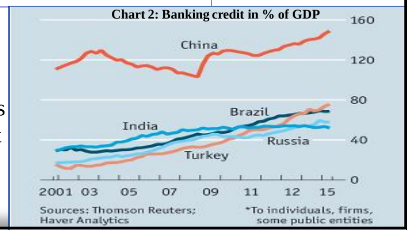
	2007	2014
Global Debt*	$142 T	$199 T
Global Debt/GDP	269%	286%

*47 nations, including 22 developed and 25 developing countries
Source: McKinsey Global Institute, as of 06/30/14



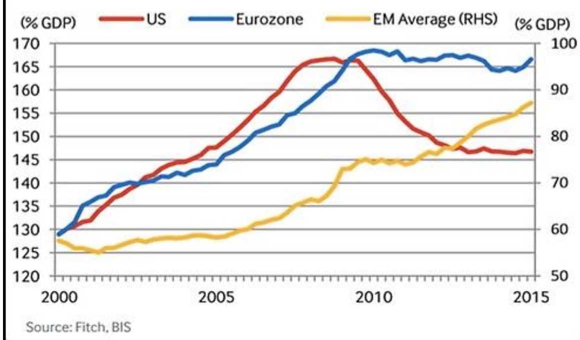
Interest rates have never been as low as … today!

Central banks' accomodative monetary policy is a recipe for credit bubbles



Deleveraging? What deleveraging?

Continued rise in private debt in the EU and EMCs



Conclusion: Corporate short-termism vs sustainable capitalism: Tradeoff between short-run profits and long-run investment

- Since the global crisis, Western companies have cut capital expenditures and even increased debt **to boost dividends and increase share buybacks**, hence hampering global economic growth
- Pressure to meet quarterly earnings targets may be reducing R&D spending, investment and growth
- Global growth remains weak due to companies returning money to shareholders rather than financing new projects: while in the 1970s only 10% of company profits were returned to shareholders, that has now climbed up to 70%
- Financial rewards should be reserved for managers who deliver long-term value, not just a quick pop in the stock!

Standford University, D. Barton at McKinsey

Headwinds to global sustainable grow

1. XX° century:

Mix of well-paying manufacturing jobs, higher education, rise of middle class

- **EMCs**: End of "high growth success stories"
- **OECD**: shrinking productivity and declining employment + de-skilling process

2. The great "**age of industrialization**" is over: In search of new growth engines!

- Pushing the **technological frontier** with robotics shrinks labor =
- Structural unemployment, wage stagnation + declining purchasing power

3. Creating value?

The tyranny of short-term profits!

- Creating value for shareholders does **not make capitalism sustainable**
- Economic gaps within and between nations with emergence of **development enclaves : Forget GDP**!

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