



2016.7.15

Discussions in This Year's Bank Economist Meetings

**Koji Sakuma, General Manager and Chief Economist
Institute for International Monetary Affairs**

Last week, an international conference of bank economists was held in Tokyo and discussed many current global economic and financial issues. I would like to introduce here some of the outlines of what interested me specifically among them.

It is Growth Strategy That Determines the Successful Exit from Deflation

Monetary policies of the advanced countries were one of the major themes this year as well as before. No one thinks that the current accommodative monetary policies are harmless and can be continued forever but also knows they cannot be stopped immediately. What makes the key is the recovery of growth expectation of corporates and households.

The monetary policies taken so far prevented the collapse of the US and European economies after the financial crisis of 2008. In Japan they helped to raise the inflation rate from a negative level to a positive one. But it is the growth strategy that is fundamentally important to make the expectations of corporates and households more sustainable. A simple implementation of monetary policies may only bring a short-lived rise of expectations, if any, and in the global framework, it may run the risk to trigger a zero-sum game of competitive currency depreciation. As a result, it was the meeting's agreed conclusion that in any country the growth strategy was the best and final solution to exit from deflation and raise the bottom rate of growth.

Fiscal policy should be given more room for flexibility

Fiscal policy invited a hot discussion among the economic policies in Europe. Economists from Italy and the UK advocated for a need of more flexible framework of fiscal policy. Even the participants from Germany seemed to have understood how rare and imbalanced was the Germany's case of achieving fiscal surplus together with current account surplus up to 7~8% of GDP in the world economy that was suffering from low growth. Simultaneously, however, an optimal balance for the entire Euro zone is also needed to consider. What would become of Europe if Germany should join the group of soft fiscal policies? The response of the German participant revealed his difficult situation expressed with such a mixed feeling on these arguments.

Skepticism to helicopter money

Also discussed was the helicopter money which is ambiguous between fiscal policy and monetary policy. But the conclusion was there were no supporters of it among the participants of the meeting. Several past cases were presented as a reference such as an expansion of money following the gold rush in the watershed areas of the Yukon River, Alaska/Canada at the end of the 19th century, the fiscal policy taken by the then Finance Minister Korekiyo Takahashi in the 1930s in Japan, and vast purchase of government bonds by the US Fed during the wartime of the Second World War.

At the time of Yukon Gold Rush, Canada indeed achieved a higher real growth rate than the US, but it was not clearly identified whether the higher growth in Canada was brought by the expansion of money or brought by an increased demand in mining industries triggered by the gold rush. The fiscal expenditures by Takahashi were evaluated as that although it might succeed in taking the economy out of deflation, it did not succeed in making the society soft landing as a whole since the economy was followed by inflation, social unrests, 2.26 incident (failed attempt of a coup) and expansion of battlefield in China.

As regards the US economy at the time of the World War II, the quantitative accommodation by the US Fed ended in a persistent holding of government bonds without restructuring of its balance sheet. At the same time the economy had an enormous demand from war affairs and the reconstruction of the Europe that followed. So it was hardly said that the exit from deflation was successfully achieved only by the swelling money. As for the current accommodations by the central banks in the advanced countries, there are arguments that the monetary accommodations would be more effective to the exit from deflation if the central banks announce that their holdings of government bonds are perpetual. Purchasing of perpetual bonds by the Bank of Japan or helicopter money would be one of these options. But learning from the lessons of the past experiences in Japan and the US, the conference came to the conclusion that not only the amount of monetary accommodations, it is indispensable to also discuss such issues as what kinds of demand we can stimulate from the economy, and what kinds of new industries we can develop to boost potential demand and how they can be promoted by the deregulations and innovations.

Revival of Pessimism on Europe

The Brexit and refugee problems were the focal points among the regional topics for Europe. The leaving of the UK from the EU was mainly discussed from the perspective of what is the EU after all, rather than the point of what would become of the UK in the future. (It seemed to be a prevailing atmosphere that the UK would manage to find its way by themselves.)

One of the turning points of the EU was its enlargement to Eastern Europe in 2004. This led to the diversity of positions to each policy of the EU and brought about a difference in accuracy of policy management. Such divergent positions and difference in accuracy in policy management have now thrown the EU into chaos in addressing the terrorism and refugee

problems. For instance, sharing of information on potential terrorists is quite difficult to achieve in the EU, in contrast to sharing of information on wanted persons of the past incidents or crimes. It would be very hard to share information among the organizations and employees with different cultures and disciplines. Optimal solutions might be found as to refugee problems if the EU member countries cooperated step by step over time, but they are now facing the reality of increased inflow of refugees. They also face the possibility of accelerated influx of African refugees in following decades. In these circumstances, the discussion focused on how Europe should deal with the lowering capacity to solve the problems on the European Community levels, rather than the future of the UK after the Brexit decision in the referendum. Naturally there was no clear answer found and only in this session the meeting was clouded with a dismal atmosphere.

Expectations and Skepticism on FinTech

Expectations for FinTech are high especially in the areas of money transfer and asset management, and the existing financial institutions are eager to explore the ways how to incorporate innovations into their business through alliance and M&As. But cautious opinions prevailed on the utilization of the Fintech as a whole. The essence of such cautiousness was that financial business would cause confusion in the market if it was simply based on the business sense at micro-level that the financial business could be done by merely matching the demand and supply of money. Given the functions expected for credit creation and maturity transformation, the financial business should continue to perform a certain level of functions even at the downturn phase of credit cycles. Therefore many participants were skeptical about the ability of the FinTech companies whether they could play such a role by themselves single handedly.

New Rule Making for Global Competitions

The globalization of the economy has now hit the big wall. Since the early 1990s when the communist block collapsed, cross-border movements of capital and people rapidly increased. In such circumstances, it became a priority for individual countries that they would take policies to attract global money and human resources continuously by overcoming competition from other countries. And in every country the compensations for highly expertized jobs went up while the wages for general works were restrained.

As a result, the income redistribution function was weakened in the entire world and income disparity spread. Politically, the middle class fell, leading to a rise in populism in the US and Europe. Economically, consumption power of the voluminous middle class declined to cause a stagnation of domestic demand. After all, free competition among countries has resulted in a diversion from the optimum situation of the world as a whole.

Every year the ICCBE meetings invited guest speakers from financial circles in the host country, and this year one of the participants asked the one of the Japanese guest speakers the following question: Japan is always a frontrunner of the world in such issues as the burst of

bubbles, deflation, ageing society with less children, etc. Yet the society is kept stable. The social security system maintains a certain level of welfare with average life expectancy at one of the tops in the world. It seems that something that other countries don't have may be working. What would it be?

After a moment's thought, the speaker answered that it might be the narrower disparity of the income than other countries. Probably it was correct. When the income disparity spreads beyond a certain level, a sense of community of the members of a society apparently becomes less strong. And no one would try to contribute to solve the problem if someone noticed any problems at all. Or probably they would lose such a sense of noticing in a society of weak gravity. Such a hit of "the *Le Capital au XXI siècle*" by Thomas Piketty has made, substantial supports that a candidate who identified himself as a socialist gathered in the US election campaign, they all may represent a warning bell to the fact that the income disparity of the global society is approaching to a too dangerous level to continue to maintain the community of human beings.