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OPENING REMARKS

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Check against delivery!

The return of inflation!

Opening remarks for the 49th OeNB Economic Conference on 23 May 2022

Ladies and Gentlemen!

It is my great pleasure to welcome you to this year's OeNB Economic Conference and SUERF Colloquium.

Let me start by thanking you all for joining us, both virtually and in person. I would also like to extend my very heartfelt gratitude to the distinguished speakers, panelists, and researchers who have agreed to join us and contribute to this event. A big “thank you” also goes to SUERF. This joint conference is yet another step in the long-standing close and fruitful cooperation which we have successfully pursued for more than two decades. [PAUSE]

It has almost become standard to open a conference by emphasizing that its main topic “could not be timelier”. Let me try and convince you that these are not just empty words when it comes to the 49th OeNB Economic Conference and 35th SUERF Colloquium. When we started out organizing this event half a year ago, we still had a question mark featuring in the conference title. Back then, for many the “return of inflation” still seemed a remote, albeit not impossible, scenario. Since then, inflation rates have surged in Europe and elsewhere to levels we have not seen for more than four decades. According to the Eurobarometer survey, inflation already represented the second most important concern of Europeans in early 2022, even before the start of the war in Ukraine.¹

¹ c.f. Standard Eurobarometer 96, Winter 2021-2022. The survey was conducted between 18 January and 14 February 2022. Inflation was mentioned as the most important concern by 24% of all respondents. The most important concern of Europeans was the environment and climate change (26% of respondents).

As dutiful central bankers, we have reacted forcefully and in a swift manner to these dramatic developments: namely, by dropping the question mark from our conference title. Yet, I admit, to my taste, we could have probably done much more than that - for example, by adding an exclamation mark.

On a more serious note, the underlying question why so few people saw inflation coming is indeed both challenging and stimulating. It guided our selection of contributions to this conference.

Part of the engrained disbelief in the return of inflation may be explained by the recent sequence of large adverse shocks and their relative absence over the last decades.² But there is only a fine line between unexpected events, on the one hand, and missing creativity in interpreting the data, limited foresight, and too narrow scenarios, on the other. Did central banks underestimate inflation dynamics in Europe and the US, and if yes, why so? Should we have invested more efforts in forecasting energy prices and to better understand the implications of (geo)political events for economic and inflation developments? Have our modelling efforts been too narrow when it comes to capturing large global trends and supply shortages, for example, related to the “green transition”?

In the very first session of this conference, Manoj Pradhan will shed new light on these questions by discussing secular drivers of inflation in the 2020s. As a nice complement, an academic session tomorrow will be fully dedicated to current challenges in inflation forecasting and modelling.

As Isabel Schnabel recently pointed out (from this very physical position), the current high inflation rates are driven to a significant extent by the interplay of global forces.³ Large global excess savings, high global demand and the strong integration of international value chains are part of the reason why inflation rates have risen worldwide. However, this synchronization of inflation due to global shocks and the spillovers of large idiosyncratic or regional shocks is not a new phenomenon. For this reason, I am particularly happy that Harold James agreed to share his longer-term perspective on the interplay between inflation and globalization in this year’s SUERF Marjolin Lecture tomorrow afternoon.

Yet, purely macroeconomic and econometric considerations can only deliver an incomplete picture of the multifaceted phenomenon of inflation. In fact, behavioral factors may also be to blame for our limited capacity to anticipate the return of inflation. Research based on adaptive learning models suggests that personal experiences have an important influence on the formation of inflation expectations, including the individual forecasts of policy-makers.⁴ According to these

² For example, c.f. Jón Steinsson’s intervention on the AEA/PIIE policy panel in January 2022 (Annual Allied Social Science Associations Conference).

³ c.f. Schnabel (2022a).

⁴ c.f. Malmendier and Nagel (2016) and Malmendier et al. (2021) for seminal papers on these behavioral factors.

findings, how individuals react to inflation surprises depends to a considerable extent on the “data series” of inflation experiences they have accumulated during their lifetime.

Translating these results into the context of the current episode of surging prices can provide some thought-provoking insights. For example, whereas the inflation experiences of younger cohorts of policymakers would seem to be particularly dominated by persistently low inflation, the more senior colleagues among us are more likely to remember the high and volatile inflation periods of the 1970s and 1980s.

According to my calculations, the mean age of the current members of the ECB Governing Council is 58 years.⁵ In other words, the average central bank governor in the euro area may be too young to have a memory of the prelude to the Volcker shocks. So, my little thought experiment yields an unambiguous policy implication: we clearly need a minimum age mandate for monetary policy committees to better foresee future inflation surges.

In - the unlikely - case that you are skeptical about the unbiasedness of my scientifically grounded recommendations on this topic, I would strongly advise you to attend today’s Session 2 and tomorrow’s first academic session, both on inflation expectations and perceptions. Furthermore, tomorrow’s final Session 4 will also teach us more on how we can make use of the wealth of micro data out there to better grasp real-time and past developments of the inflation process.

Sometimes we need to take a step back in order to find the right words to accurately describe the way forward. In his famous memoirs, “The World of Yesterday”, Austrian author Stefan Zweig painted a rosy picture of pre-1914 Europe as a “world of security”.⁶ To Zweig, World War I represented a watershed moment from which the continent never fully recovered during his lifetime, and which would shape the political, economic and social arena for years and decades to come.

For Europeans, Russia’s invasion of Ukraine in late February 2022 will likely mark a similar turning point in history. Once again, a hitherto unthinkable war brought the European dream of a “world of security” to an abrupt end. First and foremost - and this point needs to be stated outright - this war causes unimaginable and unnecessary human suffering and destruction in Ukraine.

From the perspective of monetary policy, this war also puts a fresh spotlight on two drivers of inflationary pressures we have either tended to neglect in the recent past or, even worse, refused to acknowledge at all.

⁵ According to available public sources, the mean age of all ECB Governing Council members is 57.8 years. The median age of all ECB Governing Council members amounts to 55.1 years.

⁶ c.f. Chapter 1 (“The World of Security”, ger. “Die Welt der Sicherheit”) in Zweig (1942).

On the one hand, the aggression against Ukraine pushed geopolitics and war back to the top of the European policy agenda. Here, I could not imagine a more suitable forum to discuss the economic implications of these radical changes in a post-pandemic world than our high-level policy panel. I am proud and very happy to welcome Tobias Adrian, Andrew Bailey, Claudio Borio and Joachim Nagel this afternoon.

On the other hand, Russia's invasion also serves as a painful reminder of how vulnerable our dependency on fossil energy sources makes us to sudden commodity price increases and their wider economic consequences. This wake-up call can serve as a unique opportunity to accelerate an anyway necessary transition to a greener *modus operandi*. However, forceful action against climate change can also imply trade-offs in terms of price stability.⁷ Session 4 tomorrow afternoon will therefore provide the important platform for an in-depth discussion of the opportunities and risks deriving from the impact of climate change and climate protection on inflation.

Let me conclude. The last chapter of Zweig's memoirs is called "The Agony of Peace".⁸ It describes an interwar period that had in fact managed to achieve a shaky peace, but only at the price of constantly rising political antagonism, uncertainty, and economic hardship. This gloomy outlook simply must not be our benchmark.

When thinking about where to begin addressing the challenges ahead of us, we would be well advised to listen to those whose lives will be most affected by our decisions today: the younger generations. According to a Flash-Eurobarometer survey conducted in spring 2022, young Europeans speak with a clear voice. Their top priority expectation from the EU is to guarantee the "preservation of peace, the reinforcement of international security and the promotion of international cooperation".⁹

There can be no doubt that, as monetary policy makers, the best contribution to social peace we can make to fulfill young Europeans' expectations is to abide by our price stability mandate. I sincerely hope that this conference will pave our way back to this target and help us to better forecast - and thus to prevent - future "returns of inflation".

Thank you very much for your attention.

I would like now to invite Jacob de Han of SUERF for his welcome statement

⁷ For example, c.f. Schnabel (2022b).

⁸ c.f. Chapter 16 ("The Agony of Peace", ger. "Die Agonie des Friedens") in Zweig (1942).

⁹ c.f. Flash-Eurobarometer 502, May 2022. This survey was conducted between 22 February and 4 March 2022. 37% of all respondents mentioned the "preservation of peace, the reinforcement of international security and the promotion of international cooperation" as their most important expectation.

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