

Bank of Italy – The Global Foundation

Rome Roundtable 2018

Rome, 15 June 2018

Dinner address of the Governor of the Bank of Italy

Ignazio Visco

Your Excellences, Ladies and Gentlemen, it is a pleasure to welcome you to the Bank of Italy. I would like to thank Steve Howard, Secretary General of The Global Foundation, for bringing together so many distinguished guests to discuss the state of the world and how it might be improved. I also thank Jock Murray, Chairman of The Global Foundation, for his kind introduction. I am honoured to set the stage for the keynote address by His Eminence Cardinal Pietro Parolin.

Unfortunately, I could not attend the sessions of the first day of this meeting. I regret it very much because you have been addressing themes of fundamental importance for the global economy. These themes appear remote from the main tasks of central bankers, preserving price and financial stability, but at a deeper level all the issues are connected and we should not lose sight of the major changes that affect our societies and economies.

In January 2017, Pope Francis' address to The Global Foundation inspired the main theme of today's and tomorrow's discussion. He stigmatized "an ideology of capitalism" that shows "little or no interest for the realities of marginalization, exploitation and human alienation, a lack of concern for the great numbers of people still living in conditions of grave material and moral poverty, and a blind faith in the unbridled development of market forces alone" and invited us "to discern just ways of attaining a globalization that is 'cooperative', and thus positive, as opposed to the globalization of indifference".

Obviously, I do not have a clear and short answer to the questions posed by Pope Francis, but I do believe that the issue of labour is central. It relates to social integration and personal identity. At the economic level, it should not be seen solely as a cyclical problem: the economy's growth depends on the quantity and quality of the labour force and on the capacity to provide adequate jobs in these ever-changing times.

Therefore, in my remarks tonight I will first consider the main forces shaping our future and the challenges they pose; then I will hint at the traps that – as policy makers – we

should avoid in order to move towards the “cooperative globalization” that we are invited to realize.

Over the last decades, four overarching forces have been shaping the world economy: globalization, technological progress, demographic transition and climate change.

For the most part, globalization and technological progress have been positive and powerful engines of economic progress and social change. But given their heterogeneous, pervasive and differentiated effects, they have also been the object of fierce critiques and deep-seated fears, which policy makers should not neglect.

Globalization is a complex, multidimensional phenomenon, consisting not only of the deeper integration of goods, services and capital markets, but also of the greatly increased mobility of people, information and ideas. The globalization we have experienced over the last quarter of a century could not have been achieved without the technological revolution that today is symbolized by the wide diffusion of computers, the internet, smartphones and robots.

This technological revolution is inexorably permeating all aspects of economic and social life. It is radically changing people’s habits and firms’ activities, as well as our way of working, producing, consuming, exchanging information and interacting socially. Statistics concerning the digitalization of the economy tell a clear story: in 2016, about 95 per cent of businesses in the OECD countries had a broadband Internet connection; more than 75 per cent had a web presence; half of the adult population had purchased goods or services online, compared with 36 per cent in 2010. These numbers suggest that, in this digital era, financial, economic and even social inclusion are closely related to technological inclusion.

The formidable achievements of globalization and technological progress are too often forgotten as the discussion turns to their shortcomings and risks:

- The world economy is today six times larger than 50 years ago, while the total population has increased little more than two-fold, so that average per capita GDP has more than doubled.
- Over the last 25 years or so more than 1 billion people have escaped extreme poverty (defined as an income below 1.9 dollars per day) while 2.2 billion have been added to the world population. Therefore, about 3.5 billion people have never entered or have escaped this condition. The target of halving the share of people living in extreme poverty has thus been achieved five years earlier than was established within the *Millennium Development Goals* agreed in 2000 by the United Nations, notwithstanding the exceptional increase in the world population.
- The so-called emerging economies – once excluded from the global economy and hosts for the largest share of the poor – have substantially narrowed the gap with advanced countries and are today the main contributors to world growth.

- The mortality rate for children under the age of 5 was halved globally between 1990 and 2015.
- Thanks to greater labour mobility, today about 260 million people live in a foreign country, up from less than 80 million in 1970, and flows among developing countries now exceed those towards advanced economies.

However, not everybody has benefited in the same way from the economic expansion provided by trade and innovation. Economic backwardness, poverty and high mortality rates are still dramatic problems in many developing countries, especially in Sub-Saharan Africa.

Even in the more prosperous countries, many have been left behind. Inequality in the distribution of income has declined dramatically over the last three decades at a global level, mainly as a result of the fast growth of China and other emerging markets that has reduced their distance from the richer parts of the world. However, within most countries differences in income and wealth have risen to historically high levels.

Finally, the rapid pace of technological progress and its unprecedented nature make it possible not only to replace physical labour but even to displace intellectual contributions in a variety of tasks once believed to be a prerogative of humans. This has raised fears of a new form of technological unemployment, to which the medium-skilled population is also vulnerable, and has helped to spread a sense of insecurity, raising the demand for protection.

The two other factors shaping our present and future conditions – demographic transition and climate change – are not independent from, and have actually been reinforced by, global economic integration and technological progress.

Higher living standards and wider access to better healthcare have increased life expectancy across the globe. For the first time in our history, the world faces not only a growing population – estimated to reach almost 10 billion in 2050, up from 7.5 billion today (and 2.5 billion in 1950) – but also an ageing one: there are almost 1 billion people aged 60 or over in the world (13 per cent of the global population) and this age group is growing faster (at 3 per cent per year) than younger age groups.

In most advanced countries, as well as in China, declining birth rates, with increased life expectancy, are pushing up the so-called old-age dependency ratio, the population over 64 relative to the working-age population (aged 15 to 64). In Europe, ageing is progressing at a very fast rate: in Italy, the old age dependency ratio has risen from 12 per cent in 1950 to more than 35 today; in Germany, from 14 to 32 per cent. Demographic transition, however, is a global phenomenon: Japan has the oldest population in the world, while in China the dependency ratio has doubled since 1950 and is expected to reach 44 per cent by 2050, up from 13 today.

This demographic transition will have a deep and long-lasting economic impact. However, the argument that this impact is inevitably negative rests on the assumption that

old people are only unproductive consumers of government benefits. This is not necessarily the case:

- Ageing does not automatically imply being unproductive or sick. A 70 year old today is in many respects much “younger” than a person of the same age 50 years ago and we now have the means to avoid the marginalization of the elderly and to keep them an integral and productive part of society for longer.
- While in relative terms the old are outgrowing the young, the number of young people in the world is the largest in history in absolute terms, but it is not distributed evenly around the globe. Of the 2.2 billion people added to the world population since 1990, less than 1 in 10 live in advanced countries. Africa, which hosts some of the poorest countries in the world, is expected to have the fastest population increase over this century, reaching Asia in absolute terms. Only an integrated world economy and wise policies can help to spread the benefits of progress more evenly. This also requires that the flows of migration be properly managed.

Climate change is linked to what we have been saying so far. The post-war exponential demographic acceleration – the “population explosion” – prompted discussion of the “limits to growth”. At the start of the 1970s, the Report of the *Club of Rome*, which centred on the predicted depletion of natural resources, raised alarm about the survival of the earth’s ecosystem and of the human race. These projections received great attention from the media, but they were greeted sceptically by many eminent economists of the time. With some reason, the critics noted that the Report failed to account for two major stabilizing mechanisms: the ability of relative prices to rebalance supply and demand and the endogenous response of technology.

Notwithstanding the power of these two mechanisms, which makes any long-term projection hazardous, the concern has not abated. The debate on sustainable development – i.e. development that can “meet the needs of the present without compromising the ability of future generations to meet their own needs” – suggests that today it is impossible to ignore the environmental balance of the planet and the reciprocal compatibility, or trade-offs, between economic, social and ecological objectives.

Climate change is no longer a scientific curiosity, it is a fundamental theme of today’s public debate. A series of important international agreements (the Kyoto Treaty of 1997 and the Paris Climate Agreement of 2016) have made it clear that two aspects are of special importance: 1) tackling the challenge of climate change at a global level, with the cooperation of all the parties involved; and 2) devising incentives for the invention and use of new technologies to drastically curtail emissions of carbon dioxide and other greenhouse gases.

Globalization, technological progress, demographic transition and climate change present us with formidable challenges. But economic integration, scientific progress and improvements in education and health conditions provide great opportunities for forging a

more prosperous, more equitable and more sustainable world economy. However, it must be clearly understood that attaining a “cooperative” globalization entails governing the world economy, as it would be illusory to rely solely upon unfettered market forces. As the global financial crisis has clearly demonstrated, effective regulation, adequately funded international financial institutions and strong cooperation among nations are necessary to mitigate risk, grant stability and correct market excesses.

Unfortunately, we live in unprecedented bad times for international relations. A retrenchment of policies towards narrowly defined national interests and short-termism in the definition of policy objectives, partly dictated by the continuous monitoring of popular approval and facilitated by the new digital technologies, are the most significant risks today. The US decision to back out of the Paris Climate Agreement and the recent failure to sign a shared Communiqué at the G7 Summit in Charlevoix are clear signs of the dangers to the liberal world order and global cooperation.

The trade dispute is revelatory of the difficulties we encounter on the road to cooperation. As is well known, the basic economic teaching on trade policy is that free trade is by far the best option as it grants full exploitation of comparative advantages to all parties involved. Indeed, the current trade system based on multilateral agreements underpinned economic development for decades. Obviously we should not ignore the potential complications arising from different levels of industrialization across nations and the risk of specializing in products that might lock in a country at a pre-industrial stage, as may have been the case for much of North-South trade during the colonial period. But we must consider that, in trade deals, the interests of producers and consumers are seldom aligned. Often the benefits of a given tariff or import quota are concentrated in the hands of few well-organized producers, while their costs, no matter how great in absolute terms, are spread among a large number of unaware and unorganized consumers. A similar conflict between concentrated and diffuse interests also arises in the case of climate change, where a further tension is added, the one between current and future generations.

A final example of the difficulties we encounter on the road to cooperation is the reaction to migration. Of course, there are many reasons why migration is met with some resistance by receiving communities. While the concerns of the more vulnerable parts of the population must be addressed, we should recognize that international mobility is a positive force for economic and social development: if properly handled, it could help poor countries to grow by alleviating the pressure on their labour markets, and it could ease the consequences of ageing in richer economies, which need a young labour force to balance falling birth rates.

But we should not ignore the conflicts that migration may generate. A first one is between the citizens of rich countries, who enjoy a “citizenship rent” they have received without meriting it, and the citizens of poor countries, who try to escape a poverty for which they have no responsibility. A second one is between young people today, who feel their

jobs are threatened by migrants, and the same people tomorrow, as a young labour force is needed now to support their living standards in the future.

These are formidable problems that cannot be tackled by policies constrained by geographical borders. The wide-ranging integration of the global economy has brought a corresponding integration of global problems. It would be short-sighted – actually counterproductive – to think that effective solutions can be found exclusively within one’s own territory, following “me first” national strategies. But this is the reality we face.

By the same token, an effective solution to these problems requires a longer-term view, a political agenda that is not enslaved by short-termism, since the needed reforms and policies have effects that are not immediate, but are distributed over a long-time horizon.

We need to prepare the polity for this kind of intervention, which is now opposed by so many. To shape public opinion, education and information are key. We need to communicate in clear, accessible terms the long-term benefits of openness to trade, to new ideas and to managed migration, while addressing the needs and fears of the most vulnerable parts of the population in advanced economies and in the world at large.