# Challenging times: Higher-for-longer, the financial system, and the economy

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*Disclaimer: the views expressed here are those of the presenter and not necessarily reflect those of the BIS.*

# A very quick summary of the past three years in the global economy

# Inflation makes a comeback in 2021 as supply and demand clash

## Supply chain disruptions erupt…

Global Supply Chain Pressure Index (lhs)

Container shipping price from China to (rhs):
US West Coast
Europe

## …spending rotates from services to goods…

Goods share of nominal consumption:
US
JP
EA
Other AEs

## …commodity prices rise from lockdown lows

Bloomberg Commodity Index
Brent oil

Source: *BIS Annual Economic Report, 2023*

# A second blow from the war in 2022

## Commodity prices hit record-highs…

## …supply chain disruptions linger…

## …spending rotation proves persistent

Source: *BIS Annual Economic Report, 2023*

# Headline inflation abates while core inflation proves sticky

## Contribution to year-on-year inflation

Source: *BIS Annual Economic Report, 2023*

# Factors that triggered the initial inflation surge weaken

## Commodity prices retreat (yet recent tick is concerning)…

Bloomberg Commodity Index
Brent oil

## …supply chain disruptions ease…

Global Supply Chain Pressure Index (lhs)

Container shipping price from China to (rhs):
US West Coast
Europe

## …spending rotation starts to revert

Goods share of nominal consumption:
US
JP
EA
Other AEs

Source: *BIS Annual Economic Report, 2023*

# Directionally the same, notable differences in terms of distance to target

## Inflation

Sources: *Datastream; Macrobond; national data; BIS.*

# Disinflation takes time

## Past disinflation episodes

Core: Median, Interquartile range
Headline: Median, Interquartile range

## Services price growth

Historical: Median, Interquartile range
2022–23: Median, Interquartile range

## Headline inflation: 1970s vs now

1970: Median, Interquartile range

## Real interest rate: 1970s vs now

2022–23:

Source: *BIS Annual Economic Report, 2023*

# Larger contribution from services may imply more persistent inflation

## Services prices continue to rise at an increasing pace

Goods: Services:

Price, yoy change (lhs): AEs, EMEs

Coefficient of variation (rhs): AEs, EMEs

## Share of labour costs is higher in services

AEs EMEs

## Common global factor explains less of changes in services prices

Goods: Services:

AEs

EMEs

Source: *BIS Annual Economic Report, 2023*

# Wage- and price-setting could easily change, with implications for inflation

## Purchasing power of households has been eroded

## Real wages have fallen behind more than they did in the past

## Firm profits have grown at a solid pace

Annual wage growth:

Nominal: 2020–22; 2008–19

Real: 2020–22; 2008–19

Historical: Median; Interquartile range

2022–23:

Source: *BIS Annual Economic Report, 2023*

# Adjustment to higher interest rates

# The first link in the transmission is in operation

Financial conditions tighten in lock step with rate hikes…

…unusual in advanced economies but not emerging markets…

…and may tighten even after rate hikes end

Source: *Monetary policy, financial conditions and real activity: is this time different?* Forthcoming BIS Bulletin

# An activity gap has emerged between advanced economies and emerging markets

Growth in advanced economies more resilient than expected…

…but not as much in emerging markets…

…as strong dollar and weak trade act as a drag

Source: *Monetary policy, financial conditions and real activity: is this time different?* Forthcoming BIS Bulletin

# Boxes are ticked for financial stress during monetary tightening

Stress more likely when private credit-to-GDP is high…

…when the surge in inflation is strong…

…when house prices grow rapidly

In the month of the first hike, the variable in the panel heading is in:

First quartile — Fourth quartile

Source: *BIS Annual Economic Report, 2023*

# The long shadow of low-for-long: rising interest rates test resilience

## Losses on debt securities accumulate, authorities intervene

AFS
HTM
Bank Term Funding Program
Loans to domestic banks through the discount window

## Recognition of unrealised losses would weigh on capital ratios

CET1 capital ratio:
SVB
Other banks

Adjusted for unrealised losses:

## Equity investors differentiate across banks

AE banks:
Low PBR
High PBR

EME banks:

Source: *BIS Annual Economic Report, 2023*

BIS

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