CENTRE FOR EUROPEAN REFORM
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Macroeconomics in a time of pandemic and war

Ditchley Park, Oxfordshire
18-19 November 2022

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The Delegation of the European Union to the United Kingdom

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Policy-makers were caught off-guard by the surge in inflation after lockdowns were eased. Putin's invasion of Ukraine has made their dilemma even more acute. Tighter monetary policy will reduce inflation but could tip the European economy further into recession, and Italian debt yields might rise to unsustainable levels. Meanwhile, governments will be forced to raise investment in energy and defence, in a period of rising borrowing costs. The EU may have to expand the Recovery and Resilience Facility – or create a new facility along the same lines – to fund key European public goods: energy independence from Russia, climate change mitigation, and European security. The Russian threat will also strengthen Western governments' resolve to cut autocratic countries out of Western supply chains, especially in the tech and energy sectors, while lockdowns have shown that more services can be delivered remotely (and therefore across borders). The effects of the pandemic and war on labour markets are unclear: on the one hand, labour has been scarce as a result of the pandemic, but on the other, millions of Ukrainian refugees may permanently settle in other European countries. There will be winners and losers from these processes among European countries and regions.

Friday, 18 November 2022

13.30-15.00 Arrival of participants

15.00-15.15 Welcome and introduction

15.15-16.45 **Session 1: How should monetary policy respond to the shocks to supply?**

With very high headline inflation, and core inflation above target, the European Central Bank (ECB) is tightening monetary policy rapidly. The Federal Reserve and the Bank of England have been faster to raise interest rates, in part because there has been more rapid core inflation in the US and UK. The ECB must strike a delicate balance between anchoring expectations by tightening policy in the face of a negative consumption shock and guarding against financial instability, especially in highly indebted member-states. Italy's borrowing costs have not spiralled out of control, in part thanks to the ECB's Transmission Protection Instrument, but spreads have been increasing. The risks of a policy mistake are high: the eurozone may be entering a prolonged period of high inflation, potentially in combination with low growth, but it is also possible that the currency union will return to low inflation and low interest rates once the energy and supply shocks subside. Are we entering a new world of higher inflation and interest rates, or should we expect a return to the macroeconomics of the 2010s? What are the reasons for the differences in core inflation between continental Europe and the UK and US, and should their monetary policies also differ? How should central banks prevent quantitative tightening from leading to financial instability? Will the ECB ultimately be forced to choose between curbing inflation and compressing spreads, and is the Transmission Protection Instrument a recipe for moral hazard?

17.15-18.45

Session 2: Is more government activism the answer?

During the pandemic, European governments did not provide as much stimulus as the US, and the difference between core and headline inflation has been larger in the eurozone. However, both sides of the Atlantic protected household incomes through lockdowns, and experienced only short-lived rises in unemployment. Now many European governments are seeking to help households cope with higher inflation, through cash transfers and caps on energy prices. Meanwhile, state investment in energy infrastructure and defence must rise substantially thanks to Russian aggression and climate change, and spending on healthcare and pensions will be hard to contain. Countries with high debt ratios may find these pressures strengthen populism (if they try to solve them through higher taxes) or higher yields (if they borrow more). Does the 2020-2022 period herald a pivot towards a more activist state, with more redistribution, public investment and interventions in labour markets? Should governments do more to protect incomes during future recessions, as they did during the pandemic? How should governments fund the pressures for spending – through cuts to other spending lines, higher taxation or more borrowing? Is there a need for a permanent fiscal capacity at the EU level, and should it be focused on investment, or on more countercyclical forms of spending?

Saturday, 19 November 2022

09.00-10.30

Session 3: Are we moving from a labour glut to a labour shortage?

On the eve of the pandemic, unemployment had reached record lows in many European countries, while wage growth and inflation had been modest. Greater competition from low-wage countries, technology displacing manufacturing workers, labour market deregulation, declining trade union membership and higher migration flows may all have played a part in the flatter relationship between wages and unemployment.
Over the pandemic unemployment remained low, and job vacancies are rising, but so far wage settlements have lagged behind inflation. The EU has absorbed millions of Ukrainian refugees, migration both within the EU and from outside has resumed, and technology allows more services to be provided across borders. But there are reasons to think that, in the future, labour might be scarcer, and workers may have greater bargaining power: global trade integration has been stagnating; societies are ageing especially in many lower-wage competitors, including China; and reengineering the energy system, especially insulating buildings, is labour-intensive. Will labour be scarcer in the future? Might scarcer labour reduce income inequality and induce more productivity-enhancing investment? Or could it raise the risk of stagnation, especially in countries that attract fewer migrants? Might scarcer labour make Europeans more welcoming to immigrants?

11.00-12.30

Session 4: What are the economic consequences of energy independence from Russia?

Rapid economic recovery after lockdowns, together with bottlenecks in gas supply chains and a particularly hot summer, contributed to a gas price spike in autumn 2021. Russia's invasion of Ukraine has only increased energy prices, and the EU has vowed to do all it can to curb Russian fossil fuel imports as quickly as possible. For his part, Putin has been withholding gas supplies in order to damage Europe's economy. This will ensure that fossil fuel energy prices remain high during the phase-out, making it harder for politicians to press for tougher policies to reduce emissions (especially if these policies raise the energy costs for consumers). Has the EU made the right decision to phase out energy imports from Russia, rather than imposing a tariff or embargo? How can Europe avoid locking in 'temporary' solutions such as switching from gas to coal, or from piped to shipped gas? How long will high energy prices persist for, and what might be the consequences for inflation and interest rates? How should governments finance investment in clean energy? Should the EU exempt energy investment from its fiscal rules, or create more central funds to help accelerate the transition? How should governments protect citizens from high energy prices?

13.45-15.15 **Session 5: Is globalisation in retreat?**

The pandemic and the war in Ukraine have caused an upheaval in international trade flows. During the pandemic, international migration all but ceased, sharply reducing trade in services, but goods trade has been undergoing a boom since the end of the first lockdown, as consumers switched spending from services to goods. In the medium-term, Covid may accelerate the globalisation of services trade, by proving that more services could be delivered remotely. Covid-related export controls show that governments are increasingly prepared to ignore the import needs of other countries, while the war shows they might also exploit them. Governments have become more determined to insulate their own economies from the political risks of globalised supply chains – as seen in Europe's rapid efforts to end Russian gas imports. The EU is pursuing a trade agenda that seeks to penalise imports from countries that damage the environment, violate labour and human rights, or compete in ways the EU considers unfair. To what extent will democracies try to cut their dependence on autocratic rivals, and will they be successful? Will we see increased trade and economic (re)integration within the West? Will fraying globalisation – or even outright disintegration of the global economy – lead to higher inflation and falling real living standards, or might it create opportunities for 'left-behind' regions in Europe? Is the EU becoming more protectionist, or are its attempts to create a more level playing field globally justified? Will that have a material impact on its openness to the global economy?

List of participants

Charles Bean	Professor of Economics, London School of Economics & Political Science
Agnès Bénassy-Quéré	Chief Economist, French Treasury
Ashok Bhatia	Director, Offices in Europe & Senior Resident Representative to the EU, International Monetary Fund
Marco Buti	Chief of Staff to Commissioner Paolo Gentiloni, European Commission
David Claydon	Founder & Partner, Kaya Advisory
Benoît Cœuré	President, Autorité de la concurrence
Nick Collier	Managing Director, Brussels Office, City of London Corporation
Elisabetta Cornago	Senior Research Fellow, Centre for European Reform
Arnab Das	Global Macro Strategist, Invesco
Swati Dhingra	Associate Professor of Economics, London School of Economics & Political Science
Per Eckefeldt	Economic Counsellor, Delegation of the EU to the UK
Charles Goodhart	Professor Emeritus of Banking & Finance, London School of Economics & Political Science
Charles Grant	Director, Centre for European Reform
Megan Greene	Global Chief Economist, Kroll
Jonathan Haskel	Professor of Economics, Imperial College London
Gavin Kelly	Chief Executive, Resolution Trust
Stephen King	Senior Economic Adviser, HSBC Holdings plc
Matthew Klein	Founder, The Overshoot
Clare Lombardelli	Chief Economic Advisor, HM Treasury, UK
Eric Lonergan	Macro Fund Manager, M&G Investments
Selma Mahfouz	Finance General Inspector, Ministry of Economy, Finance & Industrial & Digital Sovereignty, France
Dalia Marin	Professor of Economics, TUM School of Management, Technical University of Munich
Zach Meyers	Senior Research Fellow, Centre for European Reform
Jan Mischke	Partner, McKinsey Global Institute
Soňa Muzikářová	Chief Advisor to Secretary of State, Ministry of Foreign & European Affairs, Slovakia
Christian Odendahl	European Economics Editor, *The Economist*
Jean Pisani-Ferry	Tommaso Padoa-Schioppa Chair, European University Institute & Senior Fellow, Bruegel
Richard Portes	Professor of Economics, London Business School
Lucrezia Reichlin	Professor of Economics, London Business School
Debora Revoltella	Director, Economics Department, European Investment Bank
Elina Ribakova	Deputy Chief Economist, Institute of International Finance
Martin Sandbu	European Economics Commentator, *Financial Times*

Yael Selfin	Chief Economist, UK, KPMG LLP
Brad Setser	Whitney Shepardson Senior Fellow, Council on Foreign Relations
John Springford	Deputy Director, Centre for European Reform
Simon Tilford	Director, The Oracle Partnership
Sander Tordoir	Senior Economist, Centre for European Reform
Ángel Ubide	Managing Director, Citadel
Shahin Vallée	Director of the Geoeconomics Programme, German Council on Foreign Relations (DGAP)
Karl Whelan	Professor of Economics, University College Dublin
Charles Wyplosz	Professor Emeritus of International Economics, Geneva Graduate Institute
Jeromin Zettelmeyer	Director, Bruegel

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