Models and their shortcomings

Debate about monetary policy, and about ultra-low – indeed, in some currencies, negative – interest rates in particular, is dominated by two schools of thought. In one camp there are the neo-Keynesians demanding "more of the same" (Krugman), i.e. a continuation of the monetary policy prosecuted by the central banks, using unconventional measures such as "quantitative easing" (QE) to put a stop to "secular stagnation". In the other we have those arguing from a more neo-classical, even monetarist, perspective who favour the speediest possible normalisation of monetary policy and issue dire warnings of looming inflation and other long-term economic ills associated with an oversupply of liquidity to the system. Both approaches, accommodative and restrictive alike, have the same Achilles heel, however – the effects they anticipate are failing to materialise: not only is there every indication that growth figures are still stuck in the doldrums, even after years and years of rock-bottom interest rates and aggressive bond purchase programmes, but the long-presaged rise in inflation still remains an obstinate no-show. The upshot is a stalemate of mindsets and models and a pervasive sense of helplessness.

These cyclical models of the world economy invite comparison with an alternative, structural approach. Three decisive structural breaks can be identified as effecting a sea change in economic and social conditions of such fundamental proportions that the results produced by cyclical paradigms can only be problematic. As such results ultimately include precisely the ultra-low interest rate policy pursued by the central banks, such criticism comes not a moment too soon in current debate. The first of the structural breaks we have mentioned concerns the dramatic reduction – indeed, elimination – of information and transaction costs by new business models based on cutting-edge data technology. The implications of this hundred-year storm for economic relationships and aggregates are an unopened Pandora's Box, but buzz-phrases such as "secular stagnation" and "deflation risk" seem misplaced when significantly greater amounts are being consumed thanks to significantly lower costs. The second structural break revealed in our analysis describes the blurring of the production function between service provider and consumer – the latter has put his shoulder to the wheel as a productive participant in an economy undergoing radical metamorphosis, and is set to become a participant of Stakhanovite output to boot, thanks to the use of efficiency-boosting applications. There can thus be no question of what traditional macro-economists have dismissed as "sluggish productivity growth" in the global economy. The third and final point is that we are witnessing a major expansion of the capital stock, as existing real and human capital can be exploited far more efficiently on the back of modern technologies; concrete examples we might mention here are Airbnb and Uber, which have become the world's leading providers in their respective sectors without having to foot the bill for as much as a single hotel building or a solitary car.

This new reality, so fundamentally transformed and difficult to capture in traditional aggregates like GDP figures or the inflation rate, will inevitably lead economic assessments – including those conducted by the central banks – up a blind alley. The prevailing view, of growth and inflation that are both "too low", and a consequential continuation of a largely fruitless ultra-low interest policy, is thus impossible to justify. The increasingly perilous side-effects of a policy that is ultimately undermining the banking system, derailing pension schemes and leading to widespread uncertainty can similarly not pass without mention.

In addition, the value of the data we surrender in a kind of barter exchange is almost entirely excluded from current models; have aggregated data become a kind of pseudo-currency? How valuable might this information actually be? What form will society and the economy take on when almost every last byte of data can be processed with such relentless efficiency, thanks to artificial intelligence, that the course of all future developments can be predicted and pre-empted, as it were? The consequences of reduced information and transaction costs have clearly yet to be fully thought through.

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