



# The Long View: Debt and Demographics

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## DOUG PEEBLES

I'm very excited to be here actually to discuss this, because we do oftentimes spend so much time talking about the short term. Since the financial crisis of 2008, we've also spent a lot of time talking about these longer-term, thematic trends that I find fascinating, and the key I think to helping our clients make money is, How do we create the narrative around all of those issues? But the first thing is the debt dynamics of the world. And again, post-financial crisis, we've had just an enormous amount of debt issued.

## ERIC WINOGRAD

And you're exactly right, Doug. It is true there's been a large amount of US sovereign debt in particular issued. But when we look at a country like China, for example, we see debt dynamics that are, if anything, even a bit more dramatic than what we've seen in the United States. And so the debt overhang, as we like to talk about it, is a global phenomenon, and it's one of the variables that we look at with a long-term time horizon. Because it has implications for long-term growth. Put simply, when you borrow money today, particularly as a sovereign, what you are doing is trying to boost growth in the short term at the expense of growth in the long term.

## DOUG PEEBLES

That's right.

## ERIC WINOGRAD

And so when we look into the distant future—into 10, 15, 20 years—one of the consequences of the debt overhang is that we think growth globally will be slower in the next few decades than it has been in the past few decades. The thing that really gets our attention is that it isn't only the debt dynamics that point in that direction. Just to take one example, demographics are pointing toward slower growth. And we know that in the developed world, the working-age population isn't gonna grow as fast as it has. And when you combine that with the debt dynamics, we're quite confident that growth will be slower going forward than it has been in the past.

## DOUG PEEBLES

Can you talk a little bit about what you think it will be from an inflation standpoint? Because I think across the world, commentators and writers have been talking about this build-up of inflationary expectations. And again, when we look at a country like Japan, those high, high debt dynamics, and those poor demographics, have actually resulted in a continuation of very low inflation, if not deflation.

## ERIC WINOGRAD

Yeah, certainly the population—the demographic trends in Japan have led to a preference for low inflation. As societies age you tend to have populations that are living on fixed incomes. For whom inflation is quite damaging. The debt dynamics unfortunately add to that. Because from a certain perspective, the best way to pay off debt is by inflation.

## DOUG PEEBLES

Inflation.

## ERIC WINOGRAD

Right? Because the amount you have to pay out is fixed, but if your income goes up because of inflation, you pay it off more easily. So the tug of war there can be quite damaging. And the slower growth that

higher debt dynamics tend to lead to can in fact make it more difficult to pay that debt back.

**DOUG PEEBLES**

Have we ever had a central bank in your study of central banking that has tried harder to get inflation in their economy than Japan has?

**ERIC WINOGRAD**

Not in the developed world, for sure.

**DOUG PEEBLES**

Not in the developed world.

**ERIC WINOGRAD**

The Bank of Japan has thrown everything but the kitchen sink at it. And [it] still hasn't been able to get inflation up, and I think the way that most economists—and myself included—would think about that is [that] inflation is in a large part a mystery. Right?

**DOUG PEEBLES**

Right.

**ERIC WINOGRAD**

We don't necessarily have a robust understanding of the dynamics that drive it. But one thing we do know is that inflation expectations matter a lot.

**DOUG PEEBLES**

Right.

**ERIC WINOGRAD**

What people expect prices to do tends to become self-fulfilling. If you expect prices to rise, you consume more today. If you consume more today, prices are more likely to go up today.

**DOUG PEEBLES**

Right.

**ERIC WINOGRAD**

Once a deflationary mind-set has entered into the economy, as is the case in Japan, it's very, very difficult to break. And Japan is the best example of that. I think that that example is a large part of the reason that our own Federal Reserve worked as hard as it did to prevent inflation from being too low.

**DOUG PEEBLES**

And hopefully they've accomplished at least a little bit of that.

**ERIC WINOGRAD**

Well, you know, look—our inflation expectations are still consistent with a 2% target over the medium term. And so I do think that the Fed has done a pretty good job of preventing a deflationary mind-set from setting in.

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