A story of tailwinds and headwinds aggregate supply and macroeconomic stabilisation

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In the decades before the pandemic, tailwinds from geopolitics, technology, globalisation and demographics made aggregate supply highly responsive to aggregate demand. This delivered solid GDP growth and low inflation, even as stalling structural reforms weighed on productivity. Increasingly reliant on fiscal and monetary stimulus to sustain output, economies became fragile. The pandemic and the war in Ukraine painfully revealed the supply side fault lines, leading to decades-high inflation in much of the world. In the coming years, many of the disinflationary tailwinds are set to turn into headwinds. This calls for a more balanced approach to policymaking, recognising the limits of demand side policies, and a commitment to revitalising aggregate supply.