Session 2: GLOBAL IMBALANCES AND THEIR CONSEQUENCES: PAST, PRESENT AND FUTURE

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1. Proposition

• Examining global imbalances is fertile ground for economists and academics, but -

• It is difficult for a policy maker to win the domestic political debate in support of reforms on the basis that ‘it will help reduce global imbalances’

• And it can be a distraction.
2. Past Imbalances

1996-2000
- US CAD widens with strong increase in investment; Japan and East Asia in surplus

2001-2004
- US in deficit but rather than strong investment public saving falls

2005-2008
- US runs CAD, as does South and Central Europe, China rising surplus
3. Should we have worried more about external imbalances?

• ‘Good’ imbalances are where saving goes to where it can be most productively used: examples, aging population saves in anticipation of dissaving when workforce shrinks; investment opportunities beyond domestic saving.

• Examples of ‘bad’ imbalances- structural shortcomings lead to high saving, bubble driven asset boom, high public sector borrowing, export led growth strategy.
4. Did global imbalances cause the Global Financial Crisis?

• ‘Some commentators argue that external imbalances had little or nothing to do with the crisis.... (it) was the result of financial regulatory failures.’ Obstfeld and Rogoff.

• ‘Global imbalances helped fuel the crisis’. Mervyn King.

• ‘..it is impossible to understand this crisis without reference to the global imbalances in trade and capital flows that began in the latter half of the 1990s’ Bernanke
5. Did global imbalances cause the crisis?

• ‘External imbalances added to global vulnerabilities by exacerbating domestic asset bubbles/busts and the attendant spillovers to the real economy. As with earlier emerging market crises, external imbalances were a symptom rather than the major driver of the global crisis, whose main causes were loose financial supervision and monetary policies...’

IMF External Sector Report
6. Should more have been done about external imbalances prior to the crisis?

- In hindsight, clearly ‘yes’ – address underlying distortions.
- At the time, not so clear cut.
- IMF focused on risk of disorderly unwinding, not the link to systematic risks building up.
- Others said benign resolution more likely.
- 2007 multilateral consultations a failure – no commitment by countries involved.
7. G 20 focus on imbalances

Three phases of G20:

• 2008-2009 – ‘saving the world’
• 2010-2011 – ‘conceptually debatable and politically delicate issue: the so-called global imbalances.
• 2011-2012 – ‘responding to the threat imposed by the euro crisis’.
8. G 20’s indicative guidelines of persistently large imbalances

• Negotiated compromise to quantifiable targets for current account imbalances;

  ‘persistently large imbalances, assessed against indicative guidelines..., warrant an assessment of their nature and root causes of impediments to adjust as part of the MAP.....’

Seoul Summit
9. G 20 challenges in dealing with global imbalances

- No consensus of risks. Pattern of imbalances changed with reduction in Chinese surplus and rise of those of oil-producing countries.
- Previous attempts at global discussions on imbalances – 2007 multilateral consultations had failed.
- Participating countries not ready to change policy for a change in a partners’ policy
10. IMF’s Pilot External Sector Report

• Examines the drivers of external positions and assesses the extent to which they;
  1. Abate over the cycle.
  2. Reflect policy distortions and potential vulnerabilities.
  3. Are warranted by fundamentals
11. Bottom line

• In terms of winning the public policy debate in order to get measures accepted, the focus should be squarely presented on what is required to achieve sustained economic and jobs growth, and not in terms of reducing global imbalances.