

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.