

# GLOBAL REBALANCING

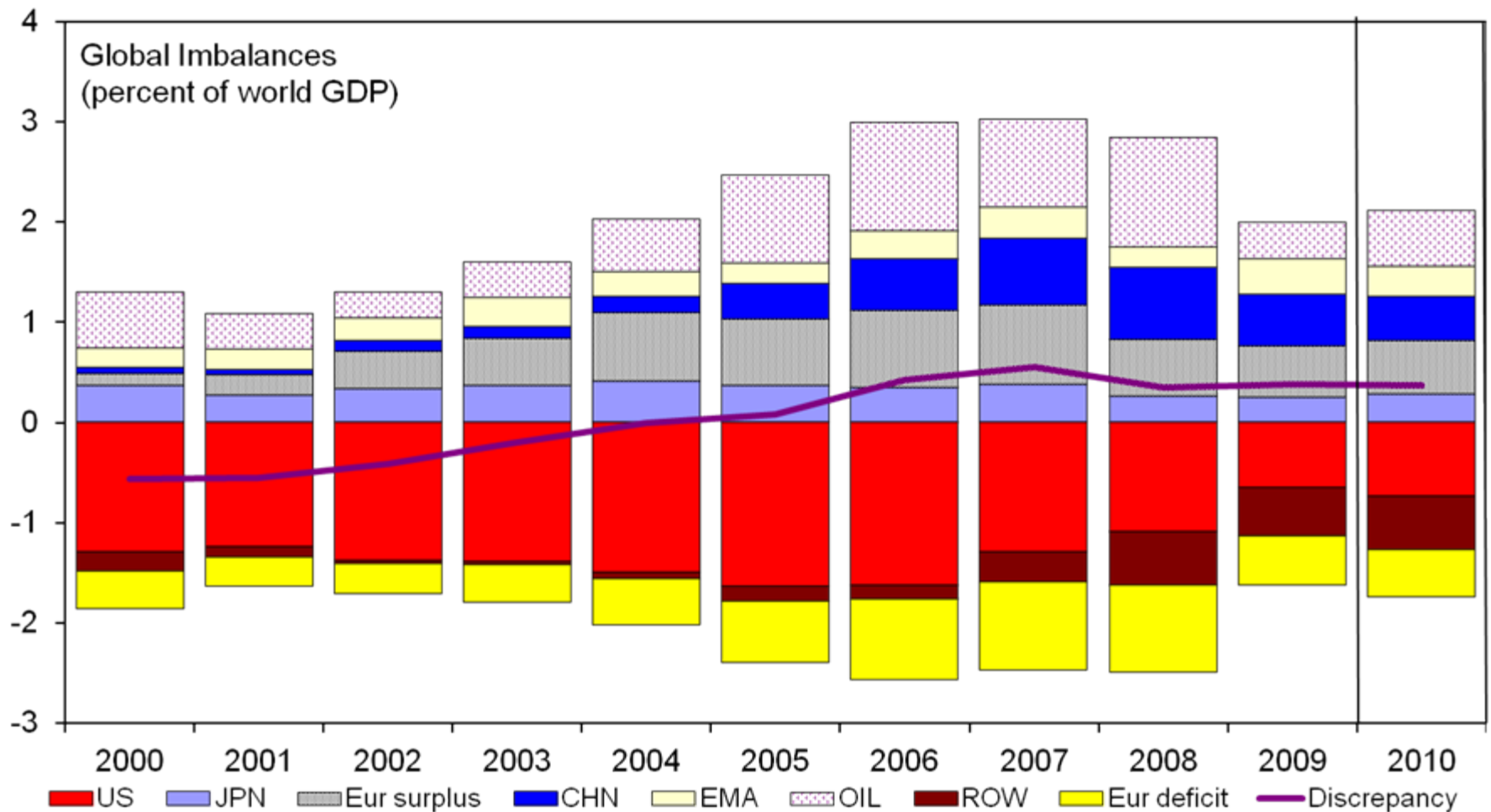
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Views expressed are mine and do not necessarily represent those of the IMF or IMF policy

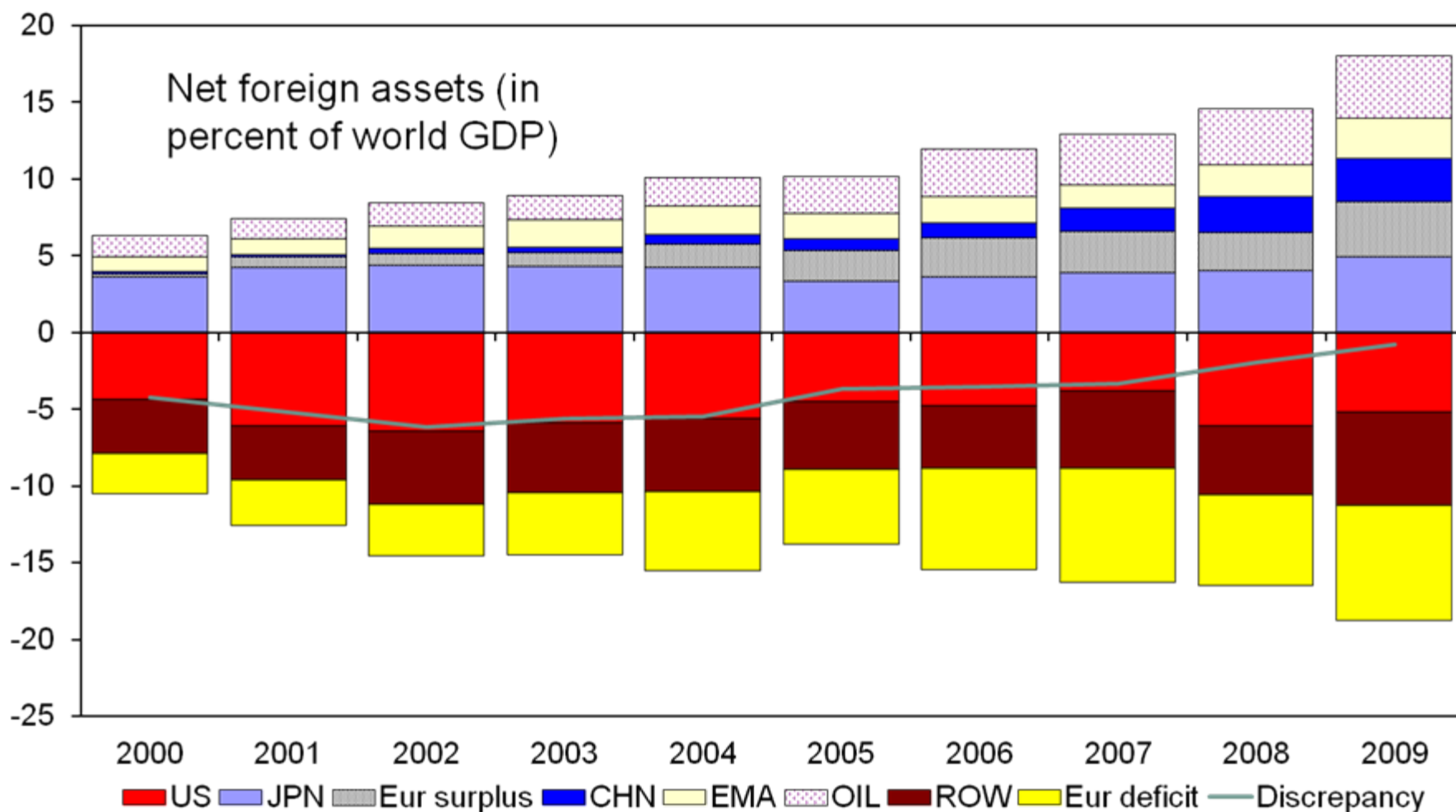
# Global Imbalances: a look ahead

- Much debate about role of imbalances in crisis...
- ...but theme of this presentation is forward-looking
- Should we still worry about imbalances?
- If yes, what should we do about it?

# Where do we stand on current account imbalances?



# External positions have widened as well (but not always in synch with CA)

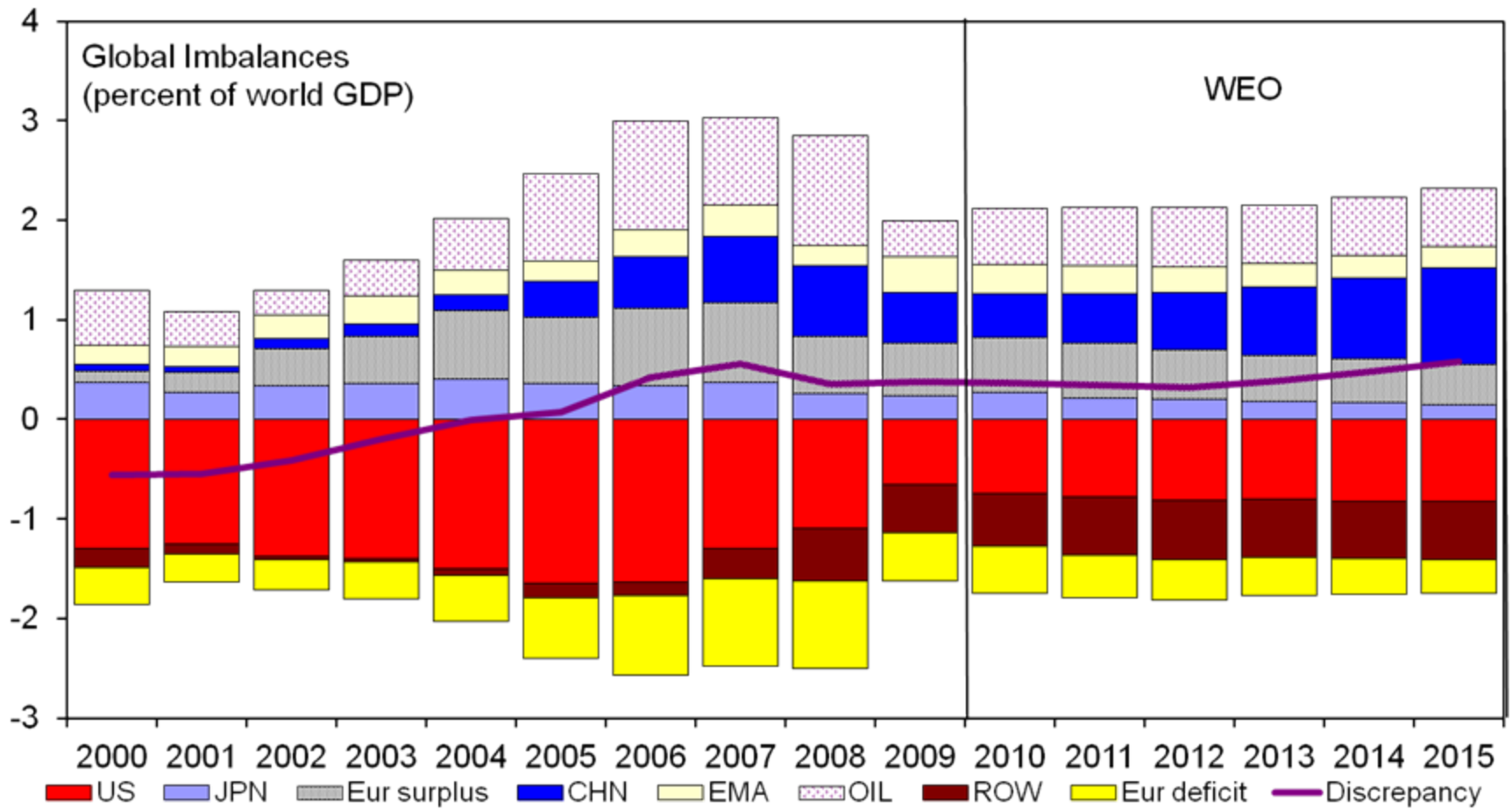


# Why should we worry about imbalances?

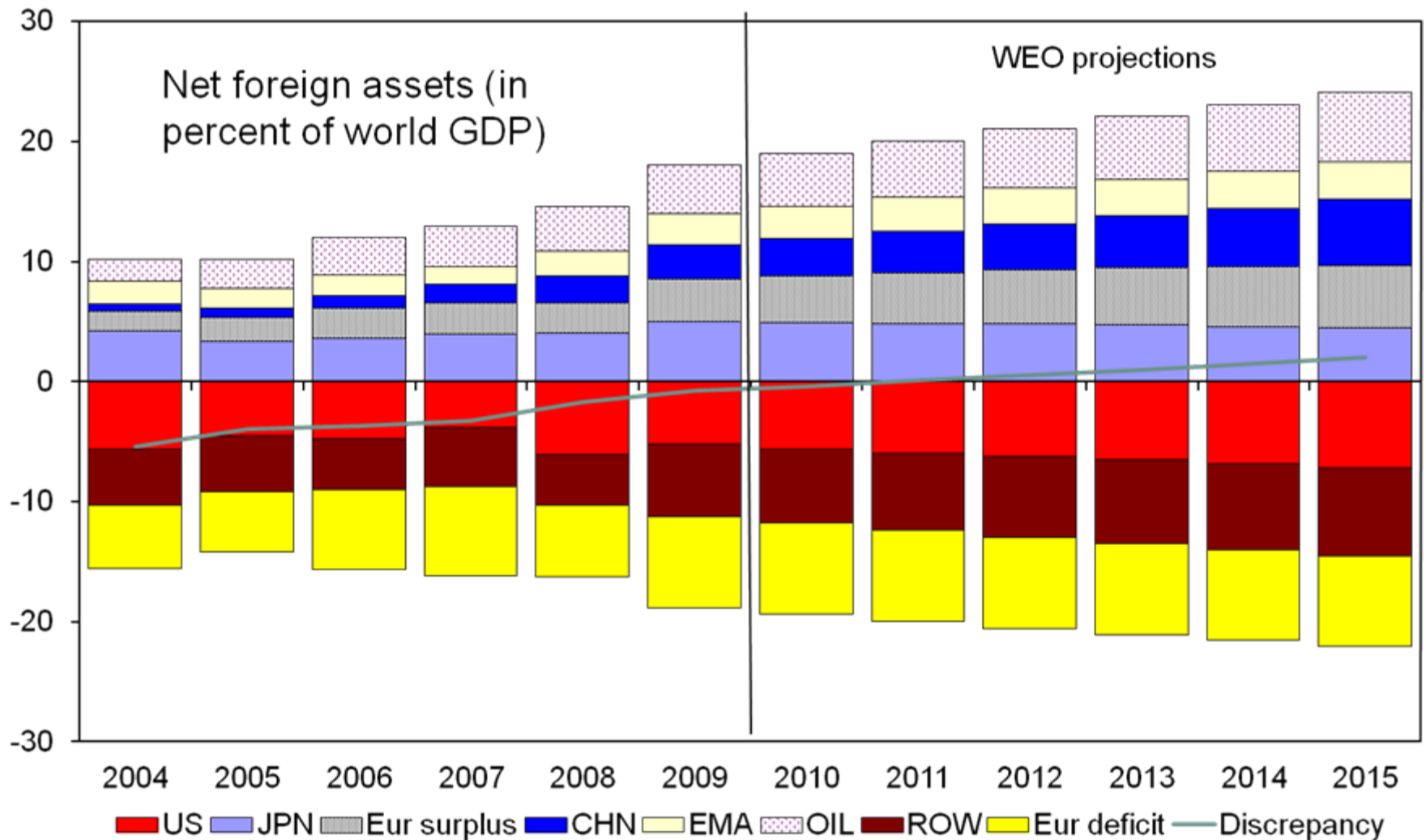


- They are a threat to the world recovery
- Divergent asset and liability positions are ultimately unsustainable, and can be a source of instability

At current exchange rates and current policies, current account imbalances would widen again...



# .. And net creditor and debtor positions would continue to diverge



# Imbalances and the world recovery

- Two rebalancing acts needed for sustained world recovery:
  - ▣ From public sector to private sector demand in advanced economies (AE) as stimulus spending fades and fiscal adjustment starts
  - ▣ From external demand to domestic demand in several emerging markets (EMs) and from domestic to external demand in (mostly) AE with large CA deficits



# If this does not happen....

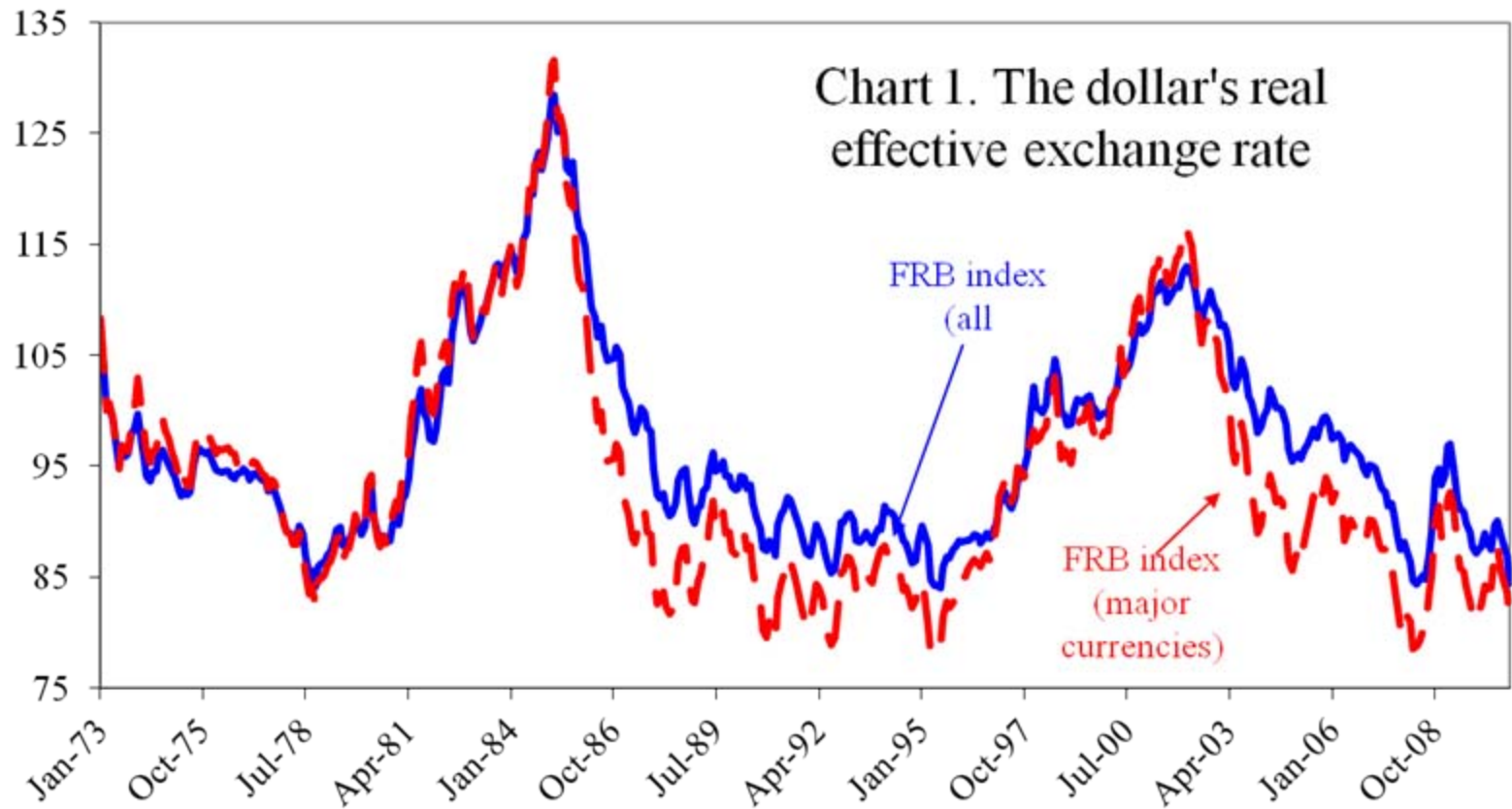
- Increased risk of stalled recovery in the US and some other advanced economies
  - ▣ *Consumption weak because of households balance sheet repair*
  - ▣ *Investment weak because of construction, prospects of weak demand, and incomplete process of financial system repair*
- Stronger protectionist pressures amidst lack of international coordination of policies

# Policy actions needed

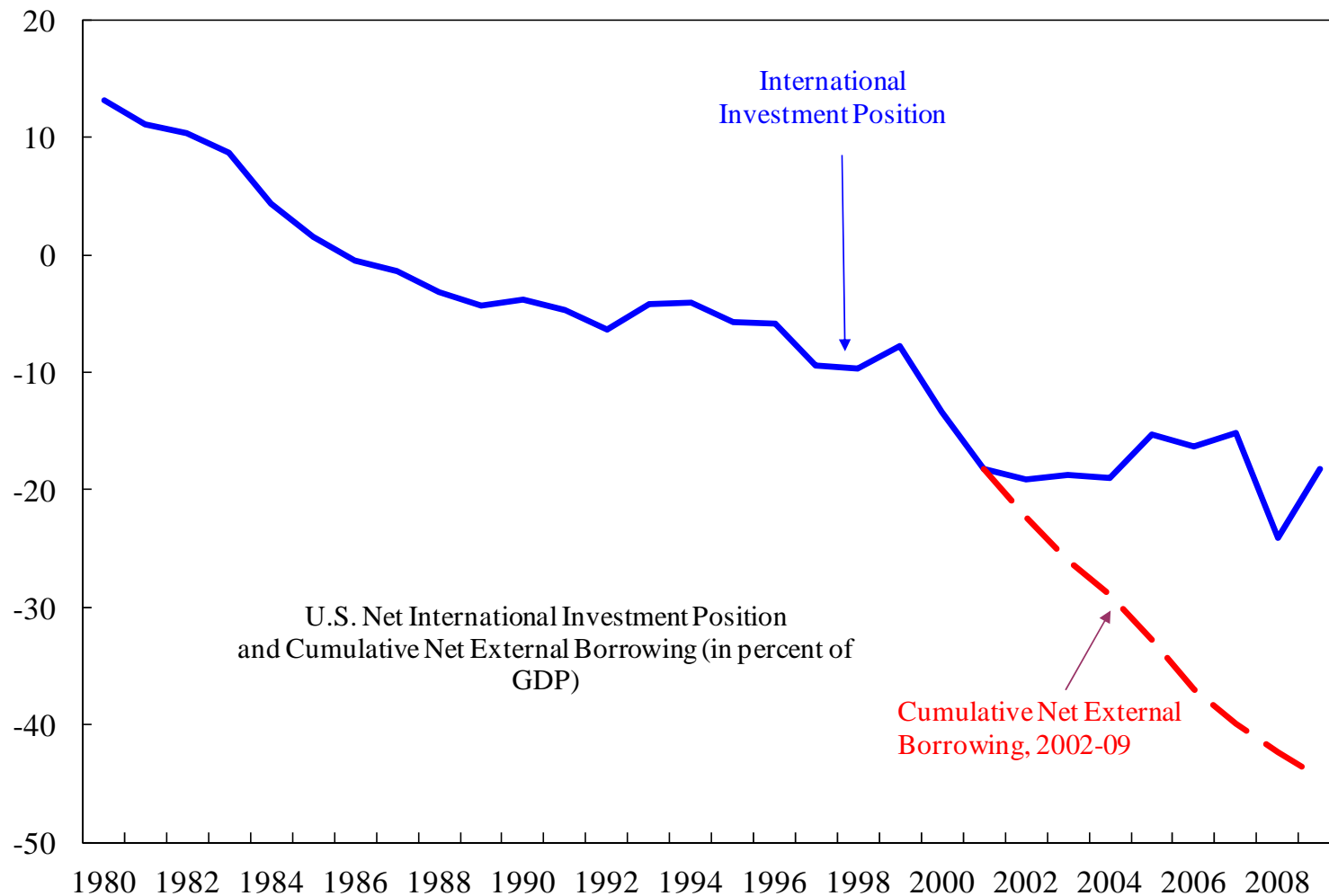
- Expenditure-switching: adjustment in exchange rates
  - ▣ *Appreciation in China and some other EMs, esp. in Asia*
  - ▣ *Some further weakening of the USD [possibly euro?]*
  
- Policies to sustain domestic demand in surplus countries. For example, address distortions that keep private consumption low (China) or stifle investment (other countries in emg Asia)
  
- In deficit countries,
  - ▣ Policies to address M-T fiscal challenges
  - ▣ Financial sector reform
  - ▣ Other structural reforms to sustain L-R growth

# The puzzles: (I) US

- CA balance projections suggest future weakening of the USD
- ...but USD is close to a post-BW-minimum in real terms

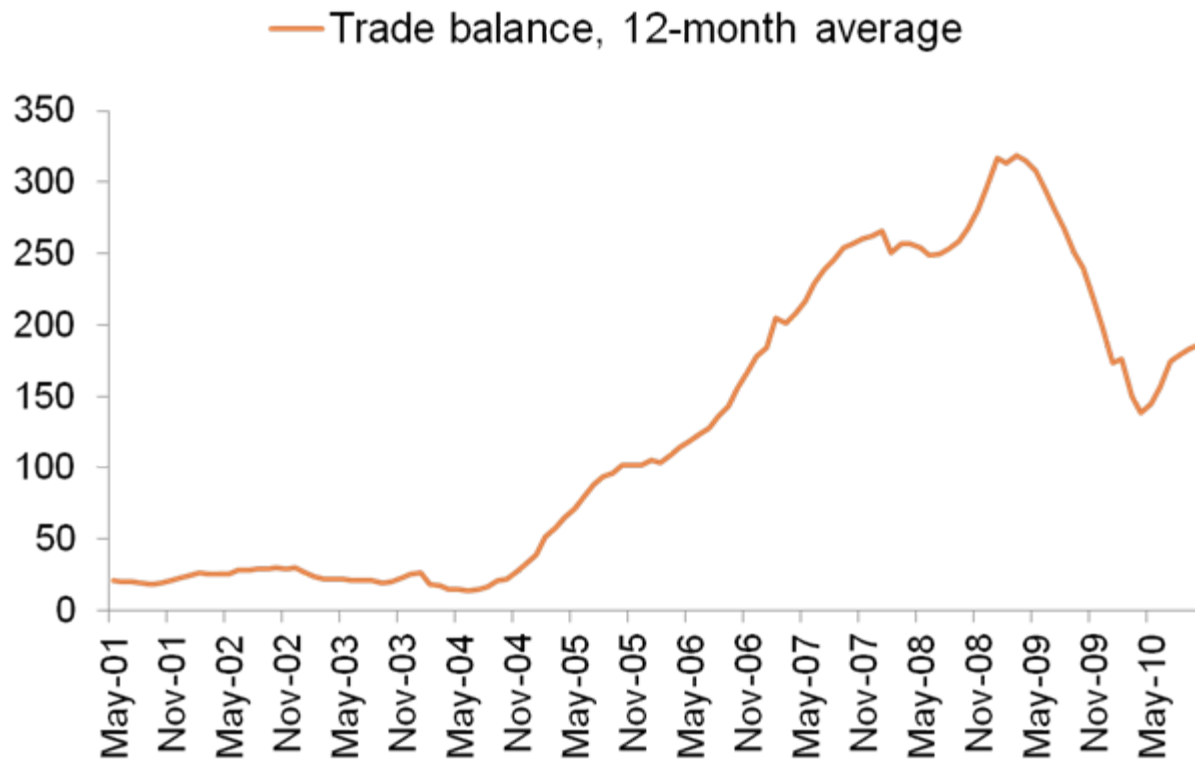


Based on CA deficits since 2001, US NFA should approach -50% of GDP. It is instead -20%



# The puzzles: (II) China and emerging Asia

- What is the extent of global rebalancing underway?
- China is not a “small open economy”...
- ...but hard to assess the length of transition



# The puzzles (III)

## Imbalances in Europe

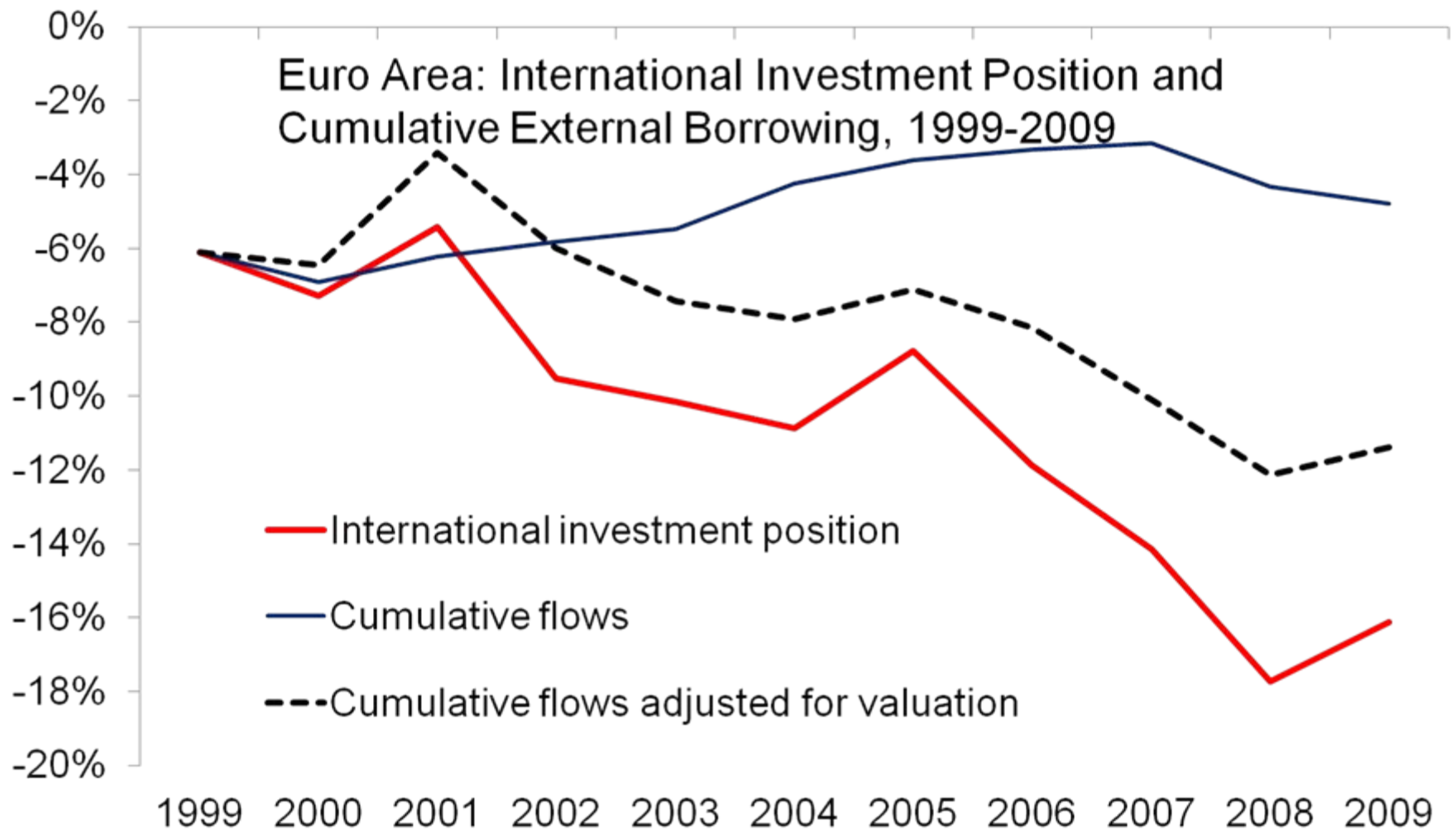
- Issue mostly neglected prior to crisis
- Real appreciation: inflation differentials vs euro appreciation
- Differential impact of external shocks on “North” vs “South”
  - China
  - Oil and commodity exporters
  - Emerging Europe
- Trade versus finance
  - Significant trade with countries outside euro area
  - Financing of “peripheral deficits” mostly internal to the euro area

# The puzzles (III)

## Imbalances in Europe

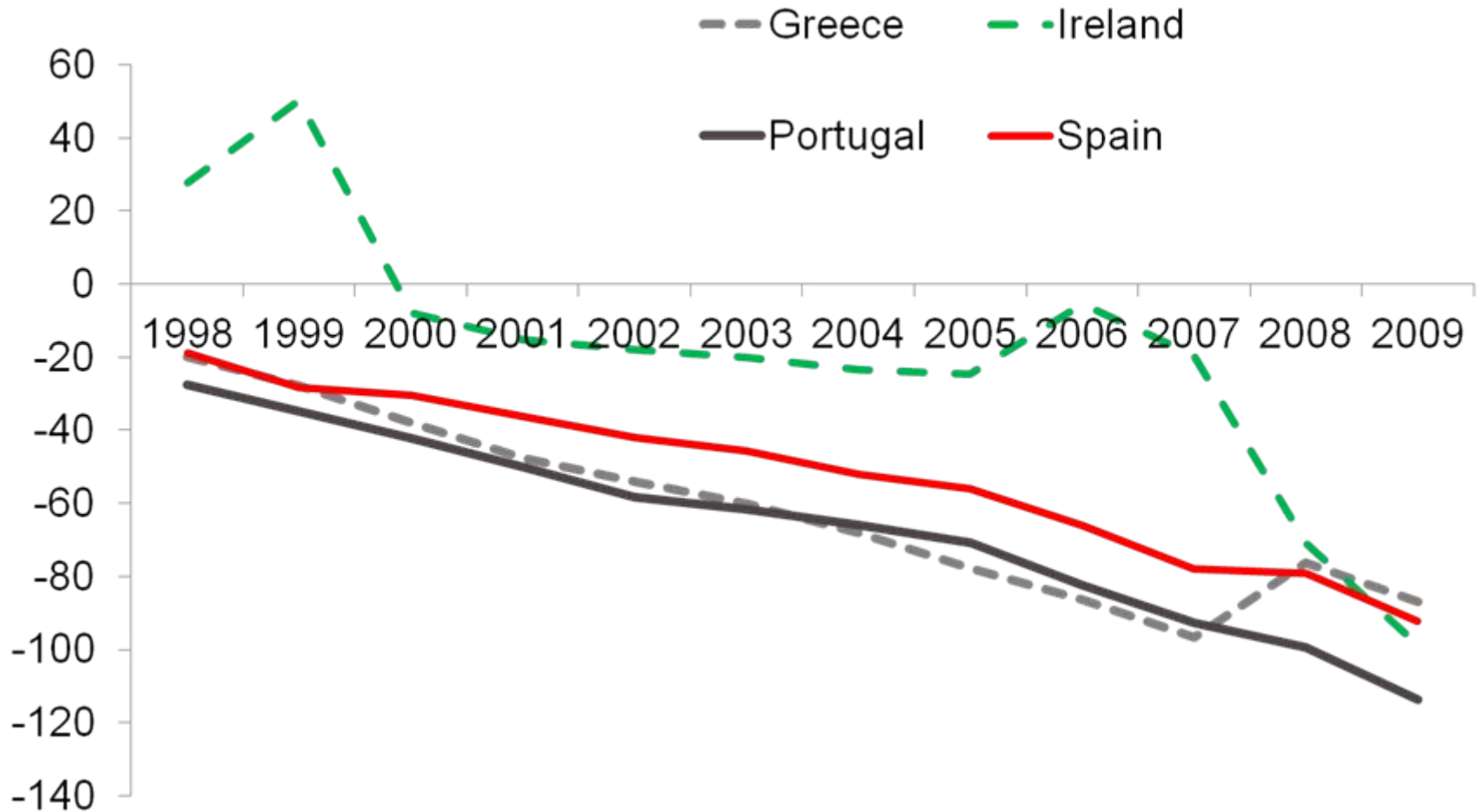
- How can adjustment work?
  - ▣ Compression of domestic demand in debtor countries
  - ▣ Costs of a strong euro?
  - ▣ What about the “North” in the euro area?
    - Emerging market demand for goods strong
    - ...but some impact of weaker demand within the euro area
    - Portfolio effects? Bilateral financing of “South” comes mainly from “North”
    - Tension between “safe haven” role of North and worries about debtor countries

# The external position of the euro area

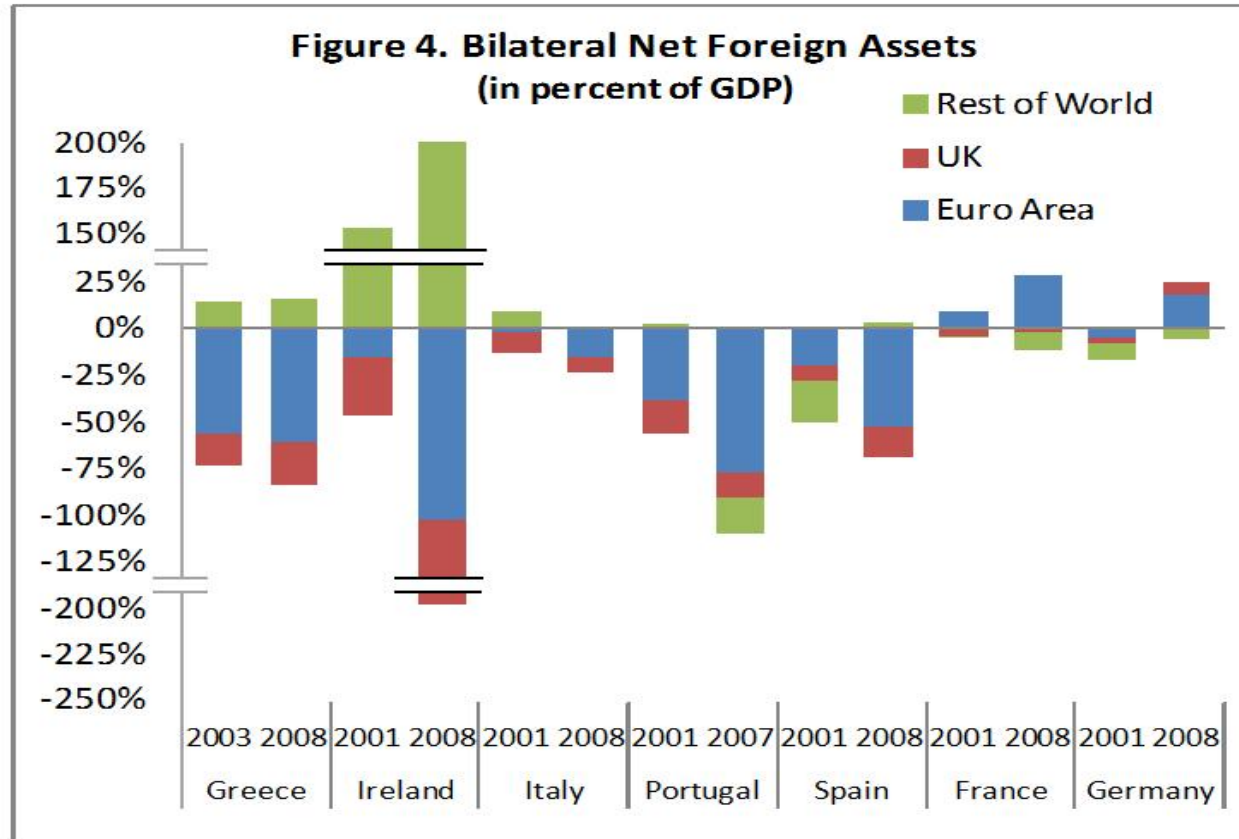




# Debtor positions have increased...



...financed primarily by the rest of the euro area



Sources: IMF Staff calculations based on OECD, BIS, and CPIS data

Portugal FDI data only available through 2007.

Greece Other Investment data only available from 2003.

Thank you!

