Global capital flows and imbalances

VANESSA ROSSI
Director International Economics, Oxford Economic Forecasting and Associate Fellow, Chatham House
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www.oef.com and vrossi@oef.co.uk
Tel: (44) 1865 268900 and 268903
The “simultaneous” world

• Reminder that the world economy is complex - no one magic bullet for imbalances – well *not one we would like*

• Hope to “persuade” global imbalances to gradually unwind – every little helps – but “*must try harder*”

• Counterparts to US problem – China trade surplus – Europe’s capacity gap and high unemployment – oil market …
Savings rates* & unemployment

Personal Savings rate 2003 %

*National definitions

Unemployment rate 2003 %

Source: OEF
Oil producers: Current account balances

"OPEC 7" = Saudi Arabia, Iran, UAE, Algeria, Venezuela, Indonesia & Nigeria

"OPEC 7" + Russia + Mexico + Malaysia

Forecast

Source: OEF
Exports to UAE (in US$bn)

$bn

12 month running total

Source: OEF / Datastream

GLOBAL 8 Oxford Economic Forecasting
Saudi Arabia: Trade surplus indicator

12 month running total

Aggregate of exports to 8 leading trading partners - imports from 8 leading trading partners

Source: OEF / Datastream
Are we heading for a crisis?

• Yes - according to those who see the US trade deficit as “unsustainable”

• But it has been “sustained” so far – so at what point is it “unsustainable”?

• Demand for dollars is high – trade finance largely in $, rising FX reserves but also strong private investor demand

• What proportion of US assets do investors want in their total wealth?
## US current account $bn

<table>
<thead>
<tr>
<th></th>
<th>2003</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exports of goods</td>
<td>713</td>
<td>808</td>
</tr>
<tr>
<td>Exports of services</td>
<td>309</td>
<td>344</td>
</tr>
<tr>
<td>Income receipts</td>
<td>310</td>
<td>380</td>
</tr>
<tr>
<td>Total</td>
<td>1332</td>
<td>1531</td>
</tr>
<tr>
<td>Imports of goods</td>
<td>1517</td>
<td>1769</td>
</tr>
<tr>
<td>Imports of services</td>
<td>257</td>
<td>296</td>
</tr>
<tr>
<td>Income payments</td>
<td>264</td>
<td>349</td>
</tr>
<tr>
<td>Total</td>
<td>1781</td>
<td>2118</td>
</tr>
<tr>
<td>Net current transfers</td>
<td>-71</td>
<td>-81</td>
</tr>
<tr>
<td>Current account</td>
<td>-520</td>
<td>-668</td>
</tr>
</tbody>
</table>

Source: US Bureau of Economic Analysis
## US financial account in 2004 (US$bn)

<table>
<thead>
<tr>
<th></th>
<th>2003</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>US assets abroad</strong></td>
<td>-328</td>
<td>-856</td>
</tr>
<tr>
<td><strong>US private assets</strong></td>
<td>-330</td>
<td>-860</td>
</tr>
<tr>
<td>Direct investment</td>
<td>-141</td>
<td>-252</td>
</tr>
<tr>
<td>Foreign securities</td>
<td>-156</td>
<td>-102</td>
</tr>
<tr>
<td>US claims reported by non bank</td>
<td>-24</td>
<td>-149</td>
</tr>
<tr>
<td>US claims reported by US banks</td>
<td>-10</td>
<td>-356</td>
</tr>
<tr>
<td><strong>Foreign assets in US</strong></td>
<td>889</td>
<td>1440</td>
</tr>
<tr>
<td>Official assets</td>
<td>278</td>
<td>395</td>
</tr>
<tr>
<td>Direct investment</td>
<td>67</td>
<td>107</td>
</tr>
<tr>
<td>US treasury securities</td>
<td>104</td>
<td>107</td>
</tr>
<tr>
<td>US securities other than treasury</td>
<td>226</td>
<td>370</td>
</tr>
<tr>
<td>US liabilities reported by US banks</td>
<td>97</td>
<td>323</td>
</tr>
</tbody>
</table>

Source: US Bureau of Economic Analysis
US$ trillion

- US Corporate Bonds $1.8tr
- US Corporate equities $1.9tr
- Private holdings of gov. securities $1.2tr
- FDI $1.7tr
- Official holdings of gov. securities $1.4tr
- Other $1.3tr

Total assets = US$9.3 tr
Total liabilities = US$4.3 tr

Source: Flow of Funds Accounts
Non-US private holdings of US Assets

% of households' financial assets

Source: OEF calculations

Projections based on different forecasts for the US current account deficit

3% of GDP

7%

6%

5%

4%

% of households' financial assets

2003 2004 2005 2006 2007 2008 2009 2010

Source: OEF calculations
threat of discontinuities

- We must understand the case for “sustaining the unsustainable”

- Then it’s important to recall that small continuous changes can lead to major dislocations – financial markets fickle

- Investors could back out of dollars

- But the system can be stabilised – cut deficits and/or act to stabilise global interest rates in event of turbulence