TOKYO CLUB: the “US external deficit” and its counterpart conundrums

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US external deficit:

- History of deficits between zero and 3-4% GDP based on mediocre savings rates, cyclical swings in competitiveness - but trade performance was more or less in line with demand drivers (exports-world trade and imports-domestic demand) - up to 1999

- The cycle adjusted current account deficit fairly stable up to 1999

- US savings rate has been trending down

- Dollar tends to be pro-cyclical - except 2001?
Cycles in US and world economy

Source: IMF
US cycle adjusted current account steady to 1999
US under-performs world trade from 1999
World trade loss fairly uniform in crisis - exception is Japan not US
US imports outperform domestic demand
US wealth losses in crisis were large, savings up, debt decreasing
US exits recession in Q3 - and imports rise
Thorough discussion of possible explanations for deepening external deficit:

• Don’t write off the possibility that wealthy consumers have an increasing propensity to consume and to consume imports - more choice and more demand for the categories of goods and services that are traded

• Poorer countries still buying staples - don’t start to buy holidays abroad or cars until they pass certain income thresholds

• Non-linearities & threshold effects may matter - ever greater US competitiveness needed to curb deficit?

• Right to investigate US savings rate - but also recall that the Rest of the World is the mirror image
Euro swings dominate US “exchange rate”?
Euro/dollar rate v US real effective rate
Trade balances for Japan, Germany and China ($m)
German trade dependency

- Private consumption
- Gross investment
- Gov't consumption
- Exports
- Imports

Shares of 2008 GDP

19.2% 18.1% 47.2% 41.0% 56.5%
Conundrums:

• US consumers spend more when they feel wealthier - but not Europeans in spite of much greater social benefits

• Persistently high savings rates (10-15%) in Euro area

• In comparison, China’s savings rate is more justifiably high -- but it is coming down

• And Japan’s savings rate too has dropped from Euro style to around 2-3% recently
Conclusions: some pot shot guesses?

- Want reasonably stable situation for acceptable external imbalances, eg US deficit 0-4% GDP

- US, European and Japanese savings rates should cluster closer to about 5%

- Developing world fast passing thresholds - spending more and will want more choice

- Try to curb excessive swings in major FX rates - euro, yen and also leading emergers

- Euro not at parity or 1.70 but 1.20-1.40, Yen 90-110 not 140 or 80, and continue trend to strengthening RMB