“The Saving Glut”

“... some of the key reasons for the large U.S. current account deficit are external to the United States, ... Providing assistance to developing countries in strengthening their financial institutions ... could ... increase both the willingness of those countries to accept capital inflows and the willingness of foreigners to invest there. ... Thus, we probably have little choice except to be patient as we work to create the conditions in which a greater share of global saving can be redirected away from the United States and toward the rest of the world - particularly the developing nations.”

Bernanke (2005)
Current Account Imbalances

Source: IMF, WEO, October 2013, Figure 1.14
Theories of the Current Account

• Determinants of national saving and investment (demographics, public sector)
• Intertemporal approach (expectations of growth)
• Mercantilism
• Global saving glut/financial development and Bretton Woods II
• Distorted financial markets
National Savings Approach

\[ CA \equiv (T - G) + (S - I) \]

- T-G is the budget balance
- S depends on demographics, income volatility, per capita income, financial development
- CA depends on trade, financial openness
- Treats each country as independent from each other
Intertemporal Approach

• Assume a future productivity shock
• Move from initial balance to deficit
• $CA = Y^*_{1} - C^*_{1} < 0$
Mercantilism: Exchange Rates

Log real value of currency (BIS), 2009M01=0

East Asian crisis
Lehman
Mercantilism: Intervention

[Graph showing trends in net official flows and current account for Developing Asia-Pacific from 1980 to 2010.]
Mercantilism: Intervention
Mechanics

\[ CA + (KA + ORT) \equiv 0 \]

- Up is depreciation
- Peg or target at \( E_{\text{peg}} \)
- Hence undervaluation
- Excess supply must be made up
Mercantilism: Counterexample
Saving Glut

- Financial market development determines where saving flows to.
- This means countries with low financial development will tend to have capital flow to countries with high financial development.
- Sometimes this is called a safe-asset shortage.
Market Distortion

- How does one measure financial development?
- A standard approach is private credit as ratio to GDP.
- But China has almost all lending from state-owned banks.
- Bond markets, stock markets, derivatives markets indicate US at the top
- How to explain 2008?