



The effects of global liquidity on global imbalances



Marie-Louise DJIGBENOU-KRE^{a,b}, Hail Park^{c,*}

^a Banque de France, Laon, France

^b University Montesquieu Bordeaux IV, France

^c Department of International Business and Trade, Kyung Hee University, 26, Kyunghedae-ro, Dongdaemun-gu, Seoul, 02447, Republic of Korea

ARTICLE INFO

Article history:

Received 17 February 2015

Received in revised form 15 October 2015

Accepted 15 October 2015

Available online 23 October 2015

JEL classification:

E51

F30

F33

Keywords:

Global liquidity

Global imbalances

Panel-VARX

US monetary shock

Spillover effect

ABSTRACT

This paper examines whether global liquidity has effects on global imbalances. To this end, we estimate Panel-VARX models using data from the G5 (United States, United Kingdom, Euro area, Japan, and Canada) and 20 emerging countries. The empirical results show that the effects on global imbalances of global liquidity, especially the US monetary aggregate, are significant. The foreign exchange reserves of emerging economies are also found to play a significant role related to global imbalances.

© 2015 Elsevier Inc. All rights reserved.

1. Introduction

Global liquidity in monetary terms has increased significantly in recent years. Private agents, economists, and researchers as well as central banks and international institutions are becoming increasingly interested in this phenomenon. This increased interest in global liquidity has been driven first of all by the period of excess liquidity prior to the outbreak of the global financial crisis. Moreover, this excess liquidity has come both from the liquidity provided by official authorities and the liquidity from financial institutions and markets. More recently, the interest has been motivated in essence by the accommodative policies adopted by monetary authorities with their expanded use of unconventional measures. At the same time, the liquidity issued by banks and some markets has continued to slow. This dynamic of global liquidity continues to intrigue us, especially because its impacts on the international economy and financial system are not well known.

In this regard, the IMF (2013) has tried to conduct surveillance of the dynamics. The BIS also shares this logic and is already providing some indicators. One main indicator highlighted by both institutions to this end is interbank flows, as this is a channel used by financial agents to transfer liquidity from the monetary to other areas. However, this liquidity and the management of the funds are highly dependent on the monetary policy implemented by the local monetary authorities. Looking for instance at the key policy interest rates of central banks, a global downward trend has been observed since the global financial crisis. These policy rate decisions are without doubt justified by the objectives of the monetary authorities. According to Djigbenou (2013), global

* Corresponding author. Tel.: +82 2 961 2170; fax: +82 2 961 0622.

E-mail addresses: marielouise.djigbenou@gmail.com (M.-L. DJIGBENOU-KRE), hailpark@khu.ac.kr (H. Park).

liquidity is essentially guided by the real economic situation and financial stability. In addition, the recent experiences with implementation of the US Federal Reserve's quantitative easing (QE) policy illustrate these purposes. The low key policy rate of the European Central Bank, in a context of deflation risk, could also be explained by these economic motivations. However, even if they are justified, accommodative domestic policies in advanced economies (AEs) could also significantly affect the dynamics of liquidity in the world as a whole.

In this paper, we focus essentially on a monetary definition of global liquidity, especially on that issued by monetary authorities. Basically, global liquidity can be considered as the monetary aggregates provided by domestic agents (in this case, mainly monetary authorities), which can be used outside their own monetary areas for buying goods, services or assets. Accordingly, the dynamics of global liquidity are strongly linked to the monetary liquidity provided by advanced countries. The monetary liquidity issued by the US Federal Reserve, the European Central Bank, the Bank of England, the Bank of Japan, and the Bank of Canada can be directly used outside their own monetary areas in the international trade and financial markets. Therefore, they contribute directly to the growth or decline of global liquidity, particularly by reallocations of their domestic liquidity throughout the world thus increasing liquidity in different economies and markets. The monetary policies adopted by these advanced country central banks during the recent crisis have been favorable to increased global liquidity. In the meantime, the global liquidity dynamics are not based solely on the liquidity provided by advanced countries but may also be affected by liquidity from emerging market economies (EMEs). For instance, some regional trades in Latin America or in Asia are in local currencies. However, the currencies of the main advanced countries remain the most used and the most liquid.

In general, each monetary authority defines its own monetary policy in accordance with its objectives and its economic situation. Considering the evolution of interest rates, the dynamics of global liquidity seem to have followed a self-sustaining process. For example, the monetary policy tightening adopted by the US Federal Reserve in 2004 by itself slowed overall global liquidity growth. A few quarters later, other central banks adopted monetary tightening policies, which in their turn also contributed to the slowdown of global liquidity growth. A similar mechanism can be observed as well in an accommodative framework. As in the previous case, the accommodative policy of the US Fed was followed by accommodative policies of other central banks. This strong correlation between the liquidity issued by the Fed and that by other central banks could lead to questions about the spillover effects of a domestic liquidity policy to the global liquidity dynamics, especially after a modification of US monetary policy. What are the spillover effects of such a change in US monetary policy on global liquidity?

In this context, the global liquidity dynamics and global imbalances seem to be mutually related. It is obvious that periods of slowdown in global liquidity growth are followed by decreases in global imbalances. According to Fig. 1, advanced economies have in the past 15 years shown large deficits in their current accounts, whereas emerging market economies have recorded substantial current accounts surpluses. Obviously, AEs' current account deficits have been offset by surpluses in their capital and financial accounts, since EMEs have invested their funds in AEs (Chung, Kim, Park, Choi, & Shin, 2014). Moreover, the rise in global liquidity in the run-up to the global financial crisis of 2008 appears to have been associated with the increase in global

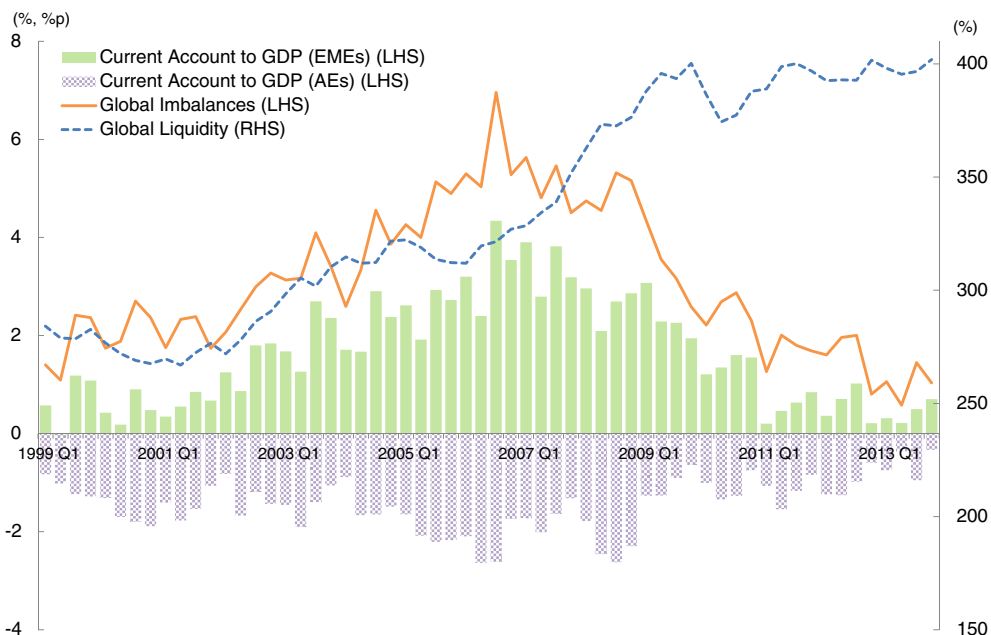


Fig. 1. Global liquidity and global imbalances.

Source: IMF International Financial Statistics. Notes: Global Liquidity is defined as the M2-to-GDP ratio in AEs. In the case of the UK, M4 is used instead of M2. Global imbalances are calculated as the sum of the absolute values of the aggregate current account-to-GDP ratios of EMEs and of AEs. AEs (5): United States, United Kingdom, Euro Area, Japan, Canada. EMEs (20): Argentina, Brazil, Chile, Mexico, Peru, Czech Republic, Hungary, Poland, Russia Federation, Turkey, China, India, Indonesia, South Korea, Malaysia, Philippines, Singapore, Thailand, Israel, South Africa.

Download English Version:

<https://daneshyari.com/en/article/5083132>

Download Persian Version:

<https://daneshyari.com/article/5083132>

[Daneshyari.com](https://daneshyari.com)