Journal of Banking & Finance 37 (2013) 5357–5372

Contents lists available at SciVerse ScienceDirect

Journal of Banking & Finance

journal homepage: www.elsevier.com/locate/jbf

Global imbalances and the intertemporal external budget constraint: A multicointegration approach

Mariam Camarero [a], Josep Lluís Carrion-i-Silvestre [b,*], Cecilio Tamarit [c]

[a] Department of Economics, Jaume I University, Spain
[b] Department of Econometrics, Statistics and Spanish Economy, University of Barcelona, Spain
[c] Department of Applied Economics II, University of Valencia, Spain

A R T I C L E I N F O

Article history:
Available online 13 February 2013

JEL classification:
F32
F36
F37
C22

Keywords:
Current account
Net foreign assets
Multicointegration
Structural breaks

A B S T R A C T

This paper analyzes the external solvency of a group of 23 OECD countries for the period 1970–2012. The empirical strategy adopted underlines the increasing importance of the financial channel for the external adjustment as proposed in Gourinchas and Rey (2007). We unify the traditional approaches to testing for external sustainability considering the stock-flow system created by the variables representing the external relationships of an open economy. External sustainability is tested using several types of cointegration and multicointegration tests. The results obtained point to weak sustainability in the flows analysis, whereas some degree of strong sustainability is found for up to six countries in the stock-flow approach. Among these countries we find both non-European economies, such as Japan and New Zealand, and Euro-area members, especially those with more restricted access to financing in the international markets.
© 2013 Elsevier B.V. All rights reserved.

1. Introduction

Since the beginning of the 1990s, current account (CA) imbalances have been widening considerably in the world economy. Economic globalization has meant an increase in international trade and capital mobility facilitating the financing of larger and more persistent current account imbalances. However, the size of the imbalances has raised the key question of their sustainability and the nature of the adjustment process. Moreover, Obstfeld and Rogoff (2009) have recently related the problem of global external disequilibria. to the current international financial crisis.

Fig. 1 shows the current account balance as a percentage of GDP for the Euro area countries, the UK, the US and Japan.[1] The visual inspection shows the existence of a diverting trend between countries like the US – depicting increasing deficits – and Japan – showing persistent surpluses measured as a percentage of the Current Account (CA) position over their GDPs. Moreover, even in the case of the euro area, although the zone seems to be balanced as a whole there are important differences among member countries – see Fig. 1. Fig. 2 on the left graph shows that the peripheral Southern European countries have experienced significant deficits. According to Lane and Milesi-Ferretti (2007), the exposures across Europe are very heterogeneous (differences in trade patterns, financial exposures, and net external positions) so that the process of adjustment may constitute an asymmetric shock. This implies bilateral real exchange rate adjustments between creditor and debtor countries as members of the euro area. The same picture appears when we assess the nature and dimension of external imbalances by looking at the net foreign assets (NFAs) position of the same group of countries. The negative values of the NFA position reflect the cumulated effect of persistent current account deficits, and therefore, the imbalance between foreign assets and liabilities. Fig. 3 shows quite clearly another stylized fact: the preeminence and persistence of the net debtor positions among the developed countries. The only exceptions have been Japan, Norway (the only oil exporter country in the sample), and a group of core EMU members (Germany, France and Belgium).

While temporary current account deficits may simply reflect the reallocation of capital to countries where capital is more productive, persistent deficits may be regarded as a more serious

* Corresponding author. Address: AQR-IREA Research Group, Department of Econometrics, Statistics and Spanish Economy, University of Barcelona, Av. Diagonal, 690, 08034 Barcelona, Spain. Tel.: +34 934024598.

E-mail address: carrion@ub.edu (J.L. Carrion-i-Silvestre).

[1] Caballero et al. (2008) divide the world into four groups: the United States (and "similar" economies such as Australia and the United Kingdom), the Euro Zone, Japan and the rest of the world. This classification also emerges from our stylized facts analysis.

0378-4266/$ - see front matter © 2013 Elsevier B.V. All rights reserved.
http://dx.doi.org/10.1016/j.jbankfin.2013.01.008

issue. Deficits may lead to increased domestic interest rates to attract foreign capital. However, the accumulation of external debt due to persistent deficits may imply increasing interest payments that impose an excess burden on future generations.

Country-specific macroeconomic imbalances that before the crisis were underestimated by policy-makers and financial market participants alike have now come to light as destabilizing factors. Of special importance have been the growing external imbalances led by the convergence of interest rates that occurred in the eurozone from 1995 to 1997 on the verge of the launching of the euro. According to Sinn and Wollmershauser (2011), the low interest rates unleashed a credit-financed boom in the countries of Europe's periphery, which initially was very positive for these countries as it fuelled their growth; however it generated an increasing external imbalance and also increasingly large amounts of capital flowed into these countries to finance the current account deficit. The situation for the peripheral countries changed dramatically when the US financial crisis spilled over into Europe. This gave rise to a credit crunch in the area, which hit the peripheral countries particularly hard. Then, private capital was no longer willing to finance these countries' accumulating trade deficits. Therefore, countries that had experienced a boom on capital imports have remained since then stuck in a crisis of which they have yet to emerge. Globally, these include the US, the UK and the peripheral countries of the eurozone, and, to a lesser extent, also France and Italy. Only very recently academics and policy makers have expressed the need to reinforce a system of explicit surveillance for these macro imbalances where the external ones are especially relevant – European Commission (2009) and Camarero et al. (2011).

The result of the process has been the need to implement financial assistance to Greece, Ireland and Portugal in the context of EU/IMF programmes as well as increasingly important (and dubious)

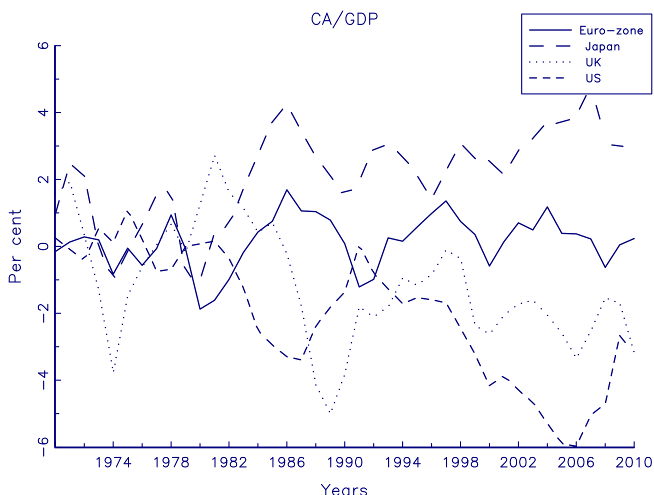
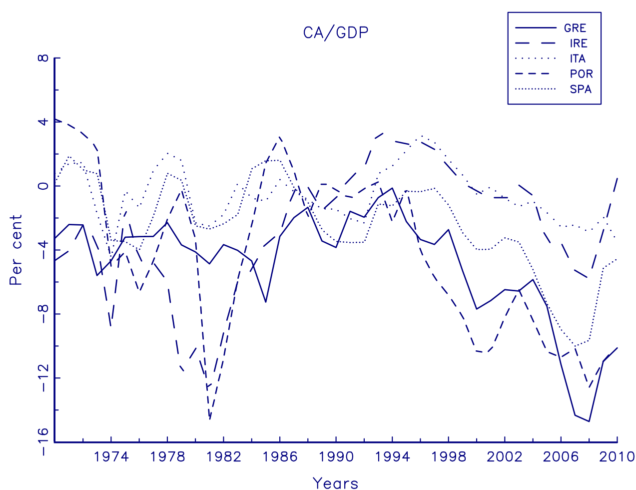
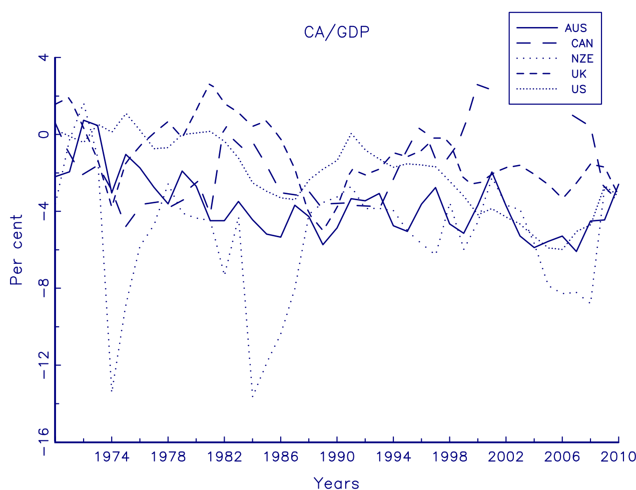
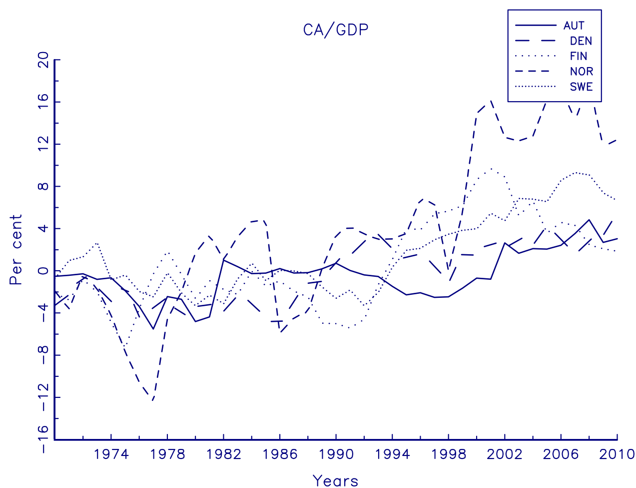


Fig. 1. Current account over GDP ratio for the euro-zone.







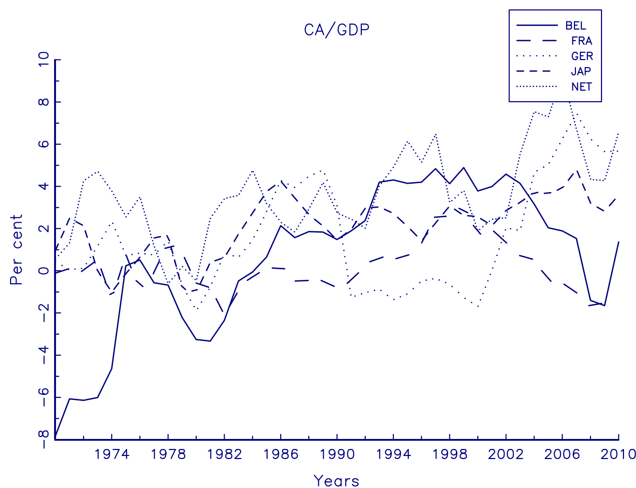


Fig. 2. Current account over GDP ratio.

Download English Version:

https://daneshyari.com/en/article/5089368

Download Persian Version:

https://daneshyari.com/article/5089368

Daneshyari.com