



PIIE PETERSON INSTITUTE FOR
INTERNATIONAL ECONOMICS

Global Imbalances and the Trade Slowdown: Implications for Asia

Caroline Freund

Senior Fellow, PIIE

Seoul, South Korea



Motivation

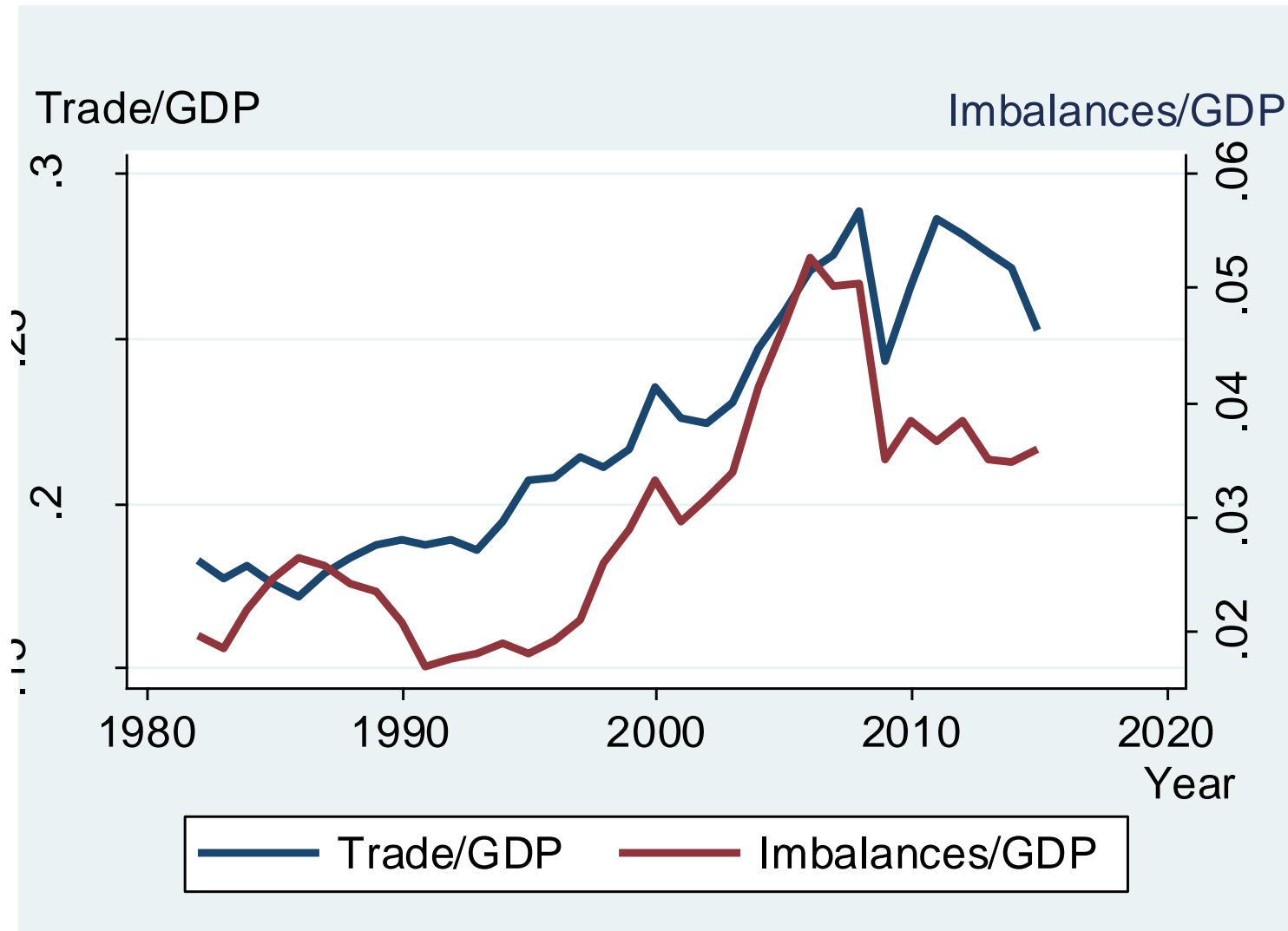
- Do sharp movements in global imbalances affect trade growth?
 - Extensive borrowing by deficit countries could boost global trade growth because demand is unconstrained.
 - Shifts consumption (and trade) from the future to the present, leading to a boom-bust trade cycle.
- Implications for the responsiveness of trade growth to income growth and for export-led growth model in Asia.



Trade Slowdown Literature

- Demand/Investment (Bussiere et.al. 2013, Freund 2016, IMF 2016)
- Global Supply Chains (Constantinescu et.al. 2015)
- China (Constantinescu et.al. 2015, Gaulier 2015)
- Protection (Hufbauer 2016)
- Global imbalances magnify demand effects.

Imbalances and Trade Move Together

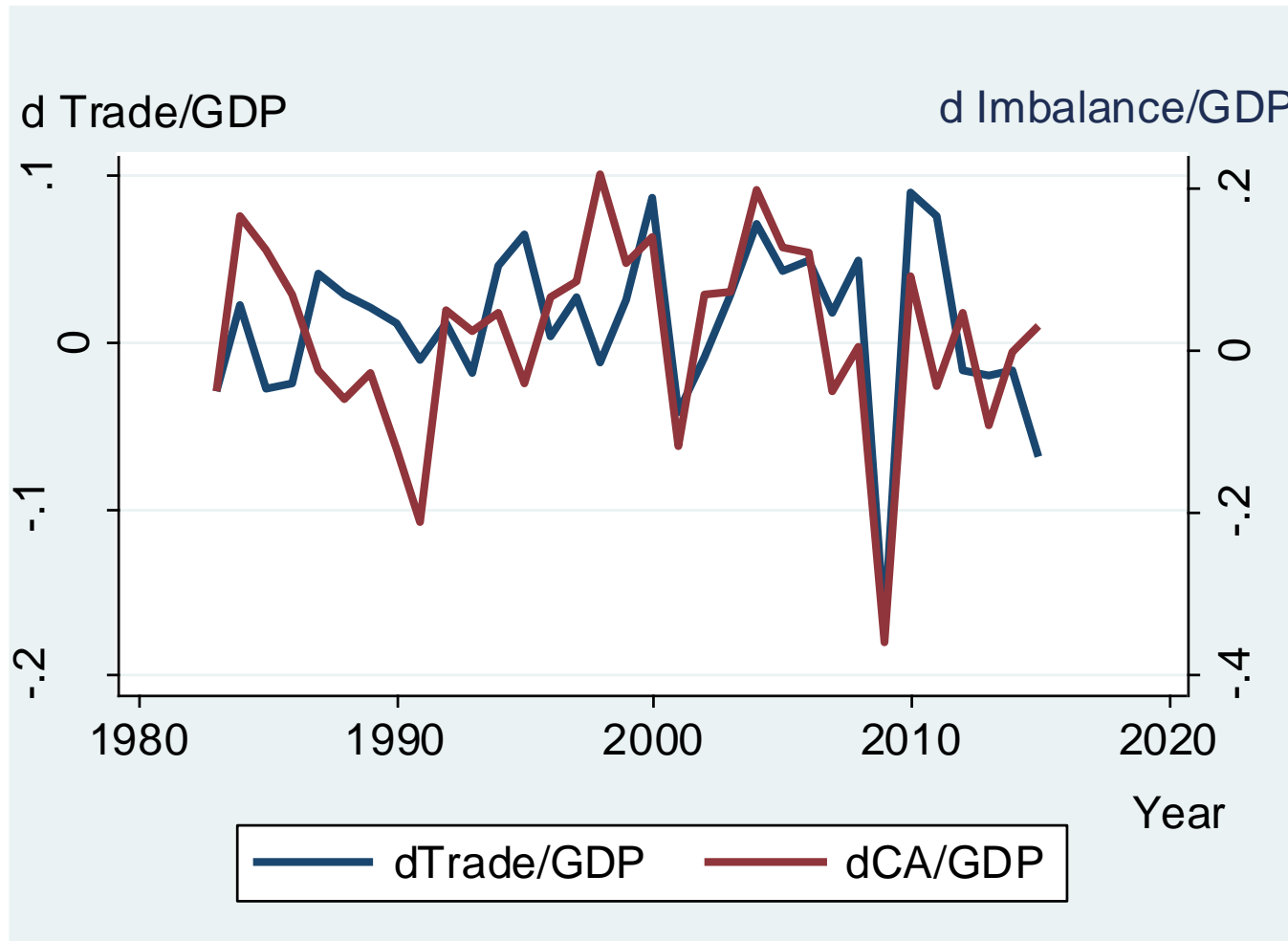


Correlation before 1995 = 0.80

Correlation after 1995 = -0.61



Correlation Started in Late 1990s



Correlation before 1995 = 0

Correlation after 1995 = 0.66



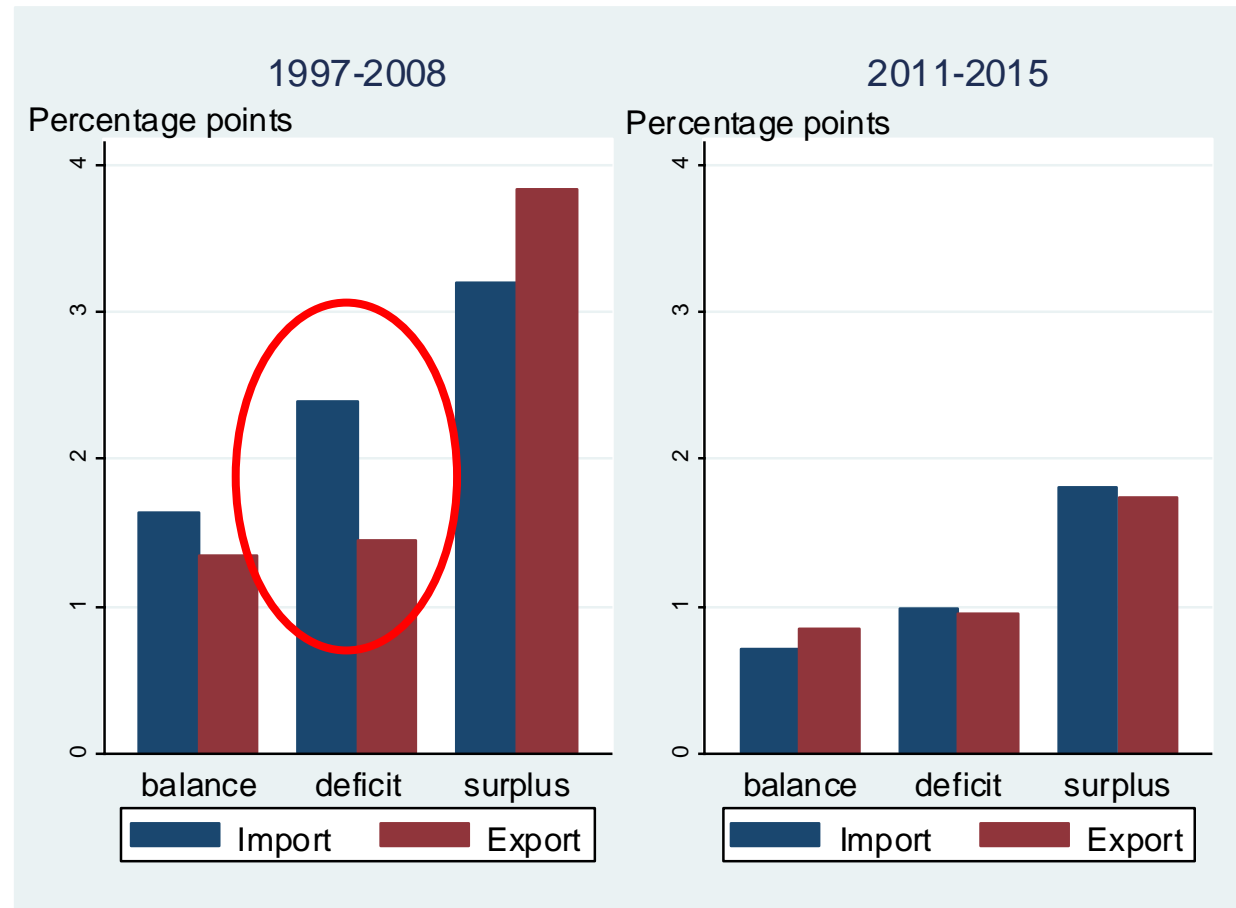
Why Do Trade & Imbalances Move Together?

- Trade growth drives imbalances
 - Imbalance/trade should be constant
- Demand drives trade growth, removal of trade balance constraint magnifies this effect
 - Trade growth should be driven by imports of deficit countries and exports of surplus countries
- Both respond to other factors
 - Eg. Oil prices lead to higher value of trade and higher value of imbalances
 - Real values should be stable



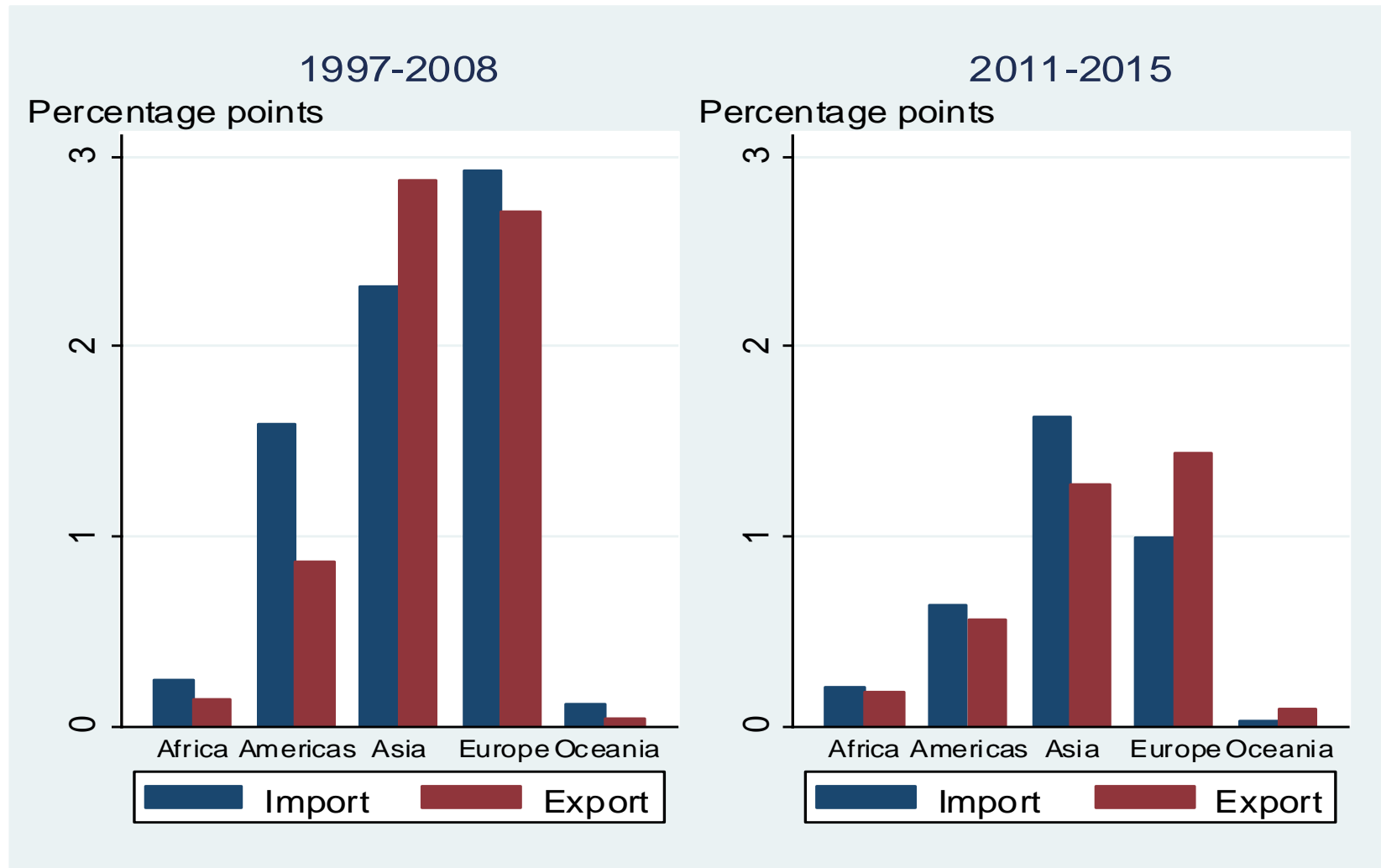
Imbalances Drove Trade Growth

Contribution to Global Real Trade Growth, by Group



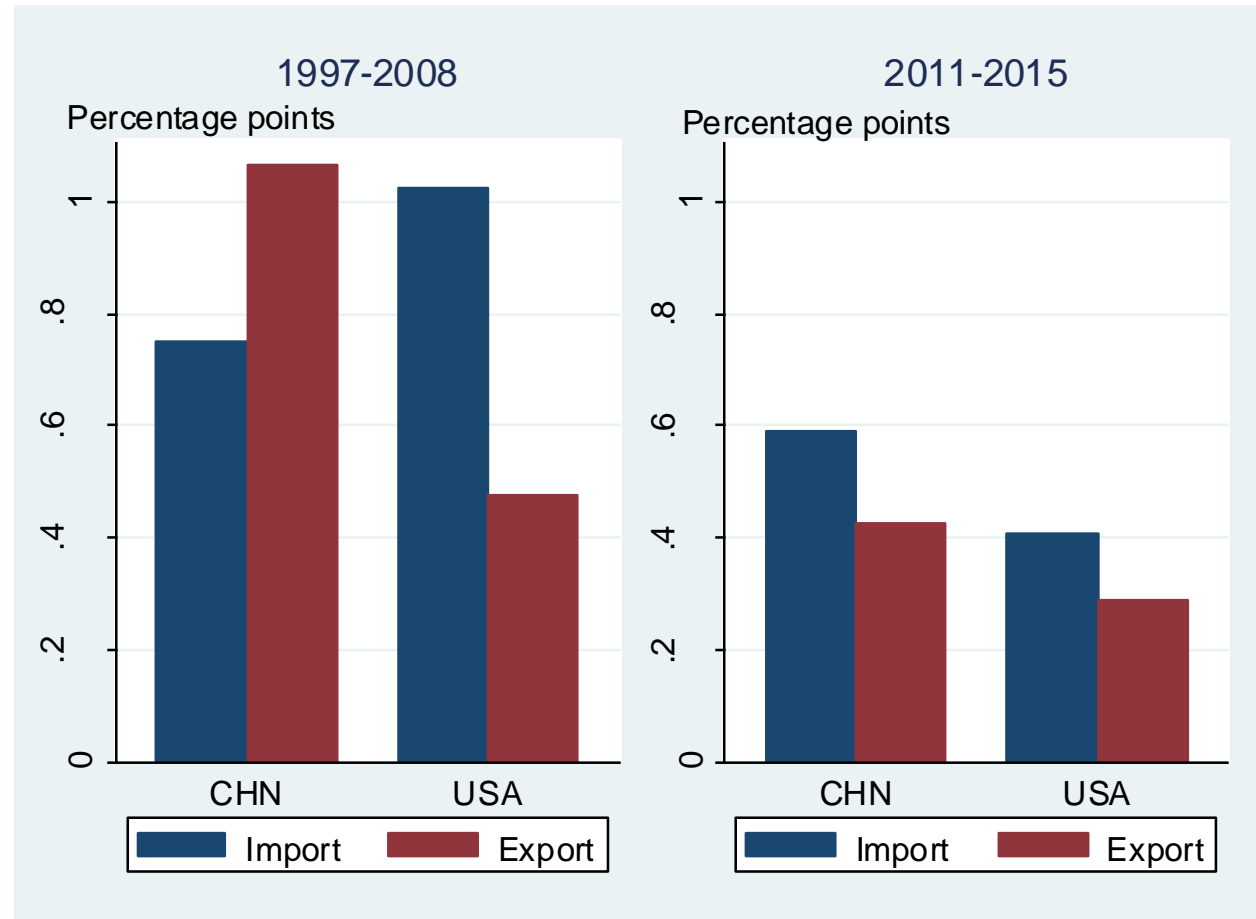


Imbalances Driven by Asia and US



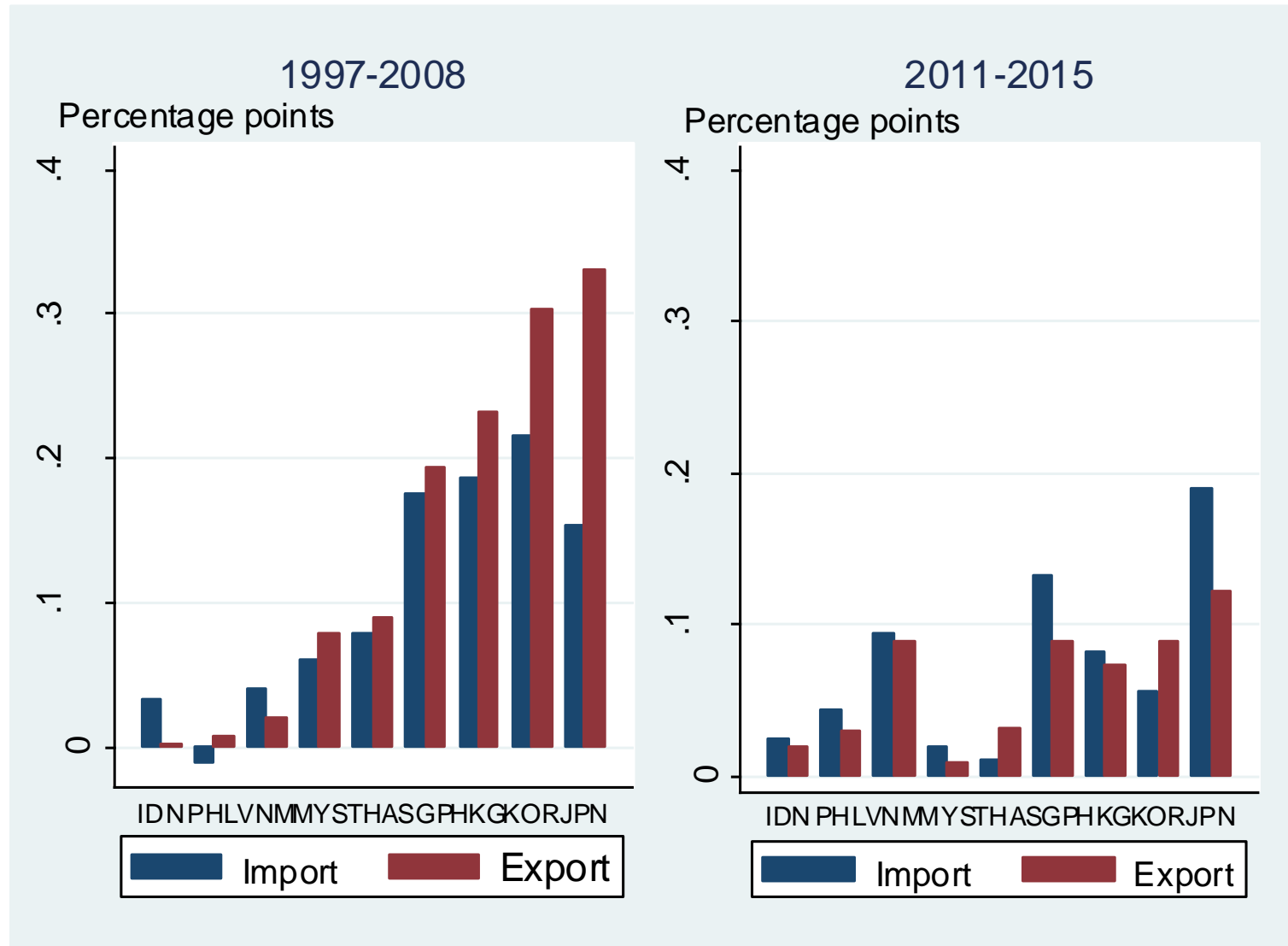


China and US: Strong Unbalanced Growth





Japan and Korea Similar to China





Trade/GDP without Imbalances

Force trade to be balanced—deficit countries cannot import more than they export

Force deficits to be constrained

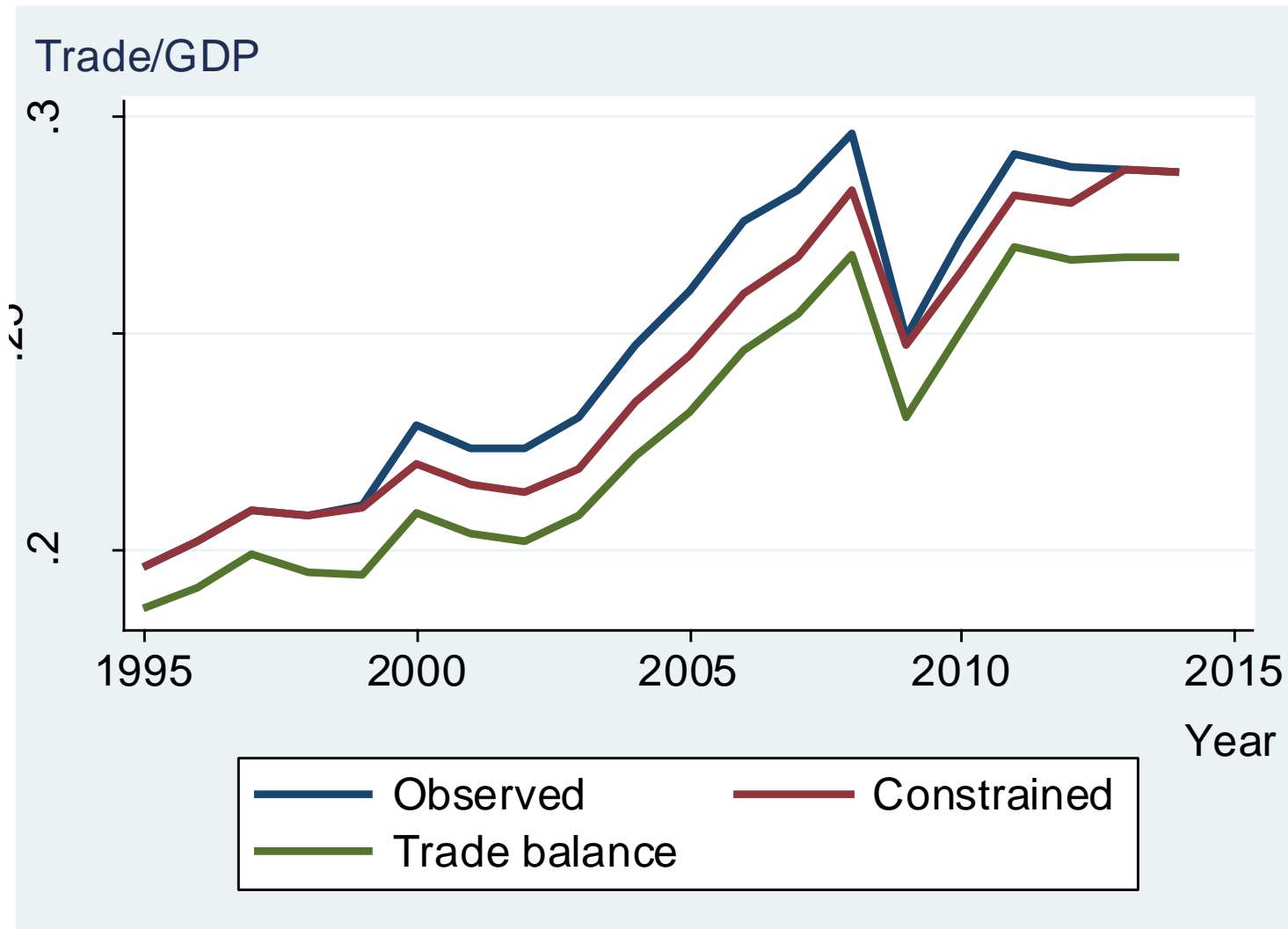
- Can't exceed 2.5 percent of GDP & historical average + 2 SD
- If hit limit return deficit to historical average or 0, whichever is smaller
- Keeps average imbalance at 2.5 percent of global GDP.

Feedback effects to surplus countries

- Excess exports reduced to match reduction in excess imports
- Imports of surplus countries reduced by import share of exports (OECD)



Trade/GDP without Large Imbalances





Imbalances Help Explain Surge and Slow Trade Growth

Period	Trade growth			Elasticity		
	Actual	Balanced	Restricted	Actual	Balanced	Restricted
1995-2007	8.1%	7.6%	7.6%	1.61	1.51	1.51
2010-2014	2.2%	2.3%	2.7%	0.98	1.03	1.21
Share of decline explained by imbalances					23%	52%



Conclusions

- Widening imbalances magnified trade surge and narrowing imbalances exacerbated trade slowdown
- Ability to run large deficits implies more volatile trade growth
- Export-led growth less feasible going forward
 - Structural reforms and domestic demand will be important in East Asia



US and Surplus Asia Trade Synchronization

<i>Dependent variable: Import growth</i>													
	Deficit		Balance			Surplus							
	LAO	KHM	VNM	IDN	PHL	JPN	KOR	CHN	THA	HKG	TWN	MYS	SGP
US import growth	0.0223 [0.414]	0.66 [0.489]	-0.186 [0.418]	0.505 [0.523]	0.0767 [0.375]	0.636*** [0.174]	0.695 [0.4]	0.596* [0.282]	1.110** [0.417]	0.625** [0.234]	1.237*** [0.206]	1.173*** [0.323]	0.825*** [0.269]
Observations	18	18	18	18	18	18	18	18	18	18	18	18	18
R-squared	0.00	0.10	0.01	0.06	0.00	0.46	0.16	0.22	0.31	0.31	0.69	0.45	0.37
Average CA/GDP	-16.26	-5.82	-1.14	1.12	1.83	2.72	3.28	3.84	3.86	7.22	7.66	10.28	18.89
<i>Dependent variable: Export growth</i>													
	Deficit		Balance			Surplus							
	LAO	KHM	VNM	IDN	PHL	JPN	KOR	CHN	THA	HKG	TWN	MYS	SGP
US import growth	0.275 [0.343]	0.783* [0.381]	-0.108 [0.238]	0.133 [0.371]	0.434 [0.464]	1.189*** [0.241]	0.718*** [0.177]	1.051** [0.364]	0.931*** [0.131]	0.720*** [0.222]	1.013*** [0.206]	0.918*** [0.206]	0.740*** [0.212]
Observations	18	18	18	18	18	18	18	18	18	18	18	18	18
R-squared	0.039	0.209	0.013	0.008	0.052	0.603	0.508	0.342	0.761	0.397	0.602	0.553	0.432
Average CA/GDP	-16.26	-5.82	-1.14	1.12	1.83	2.72	3.28	3.84	3.86	7.22	7.66	10.28	18.89