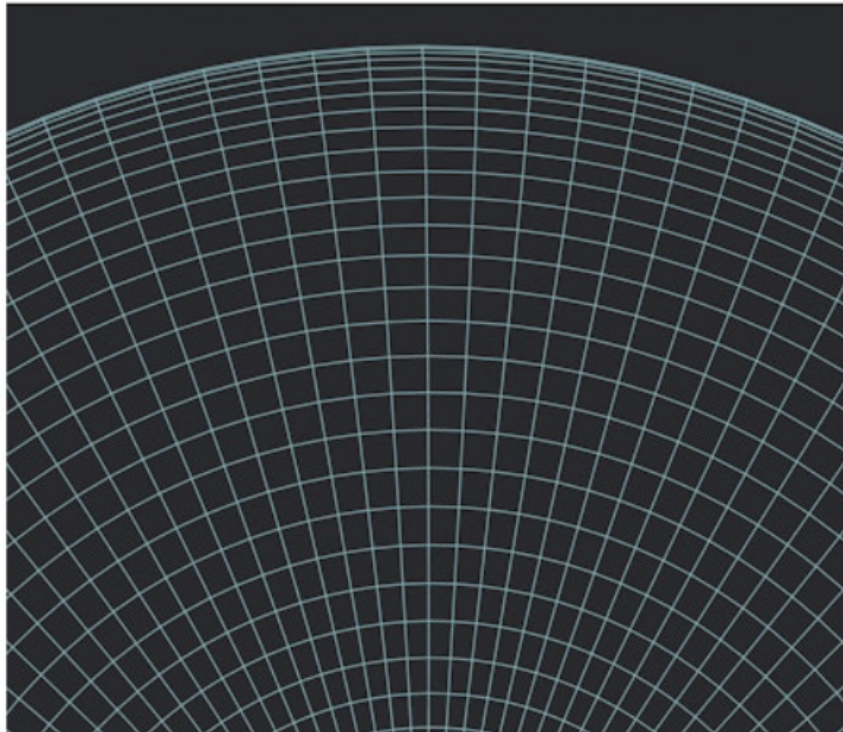

INTERNATIONAL MACROECONOMICS

A MODERN APPROACH

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Slides EC201

Chapter 1 Summary

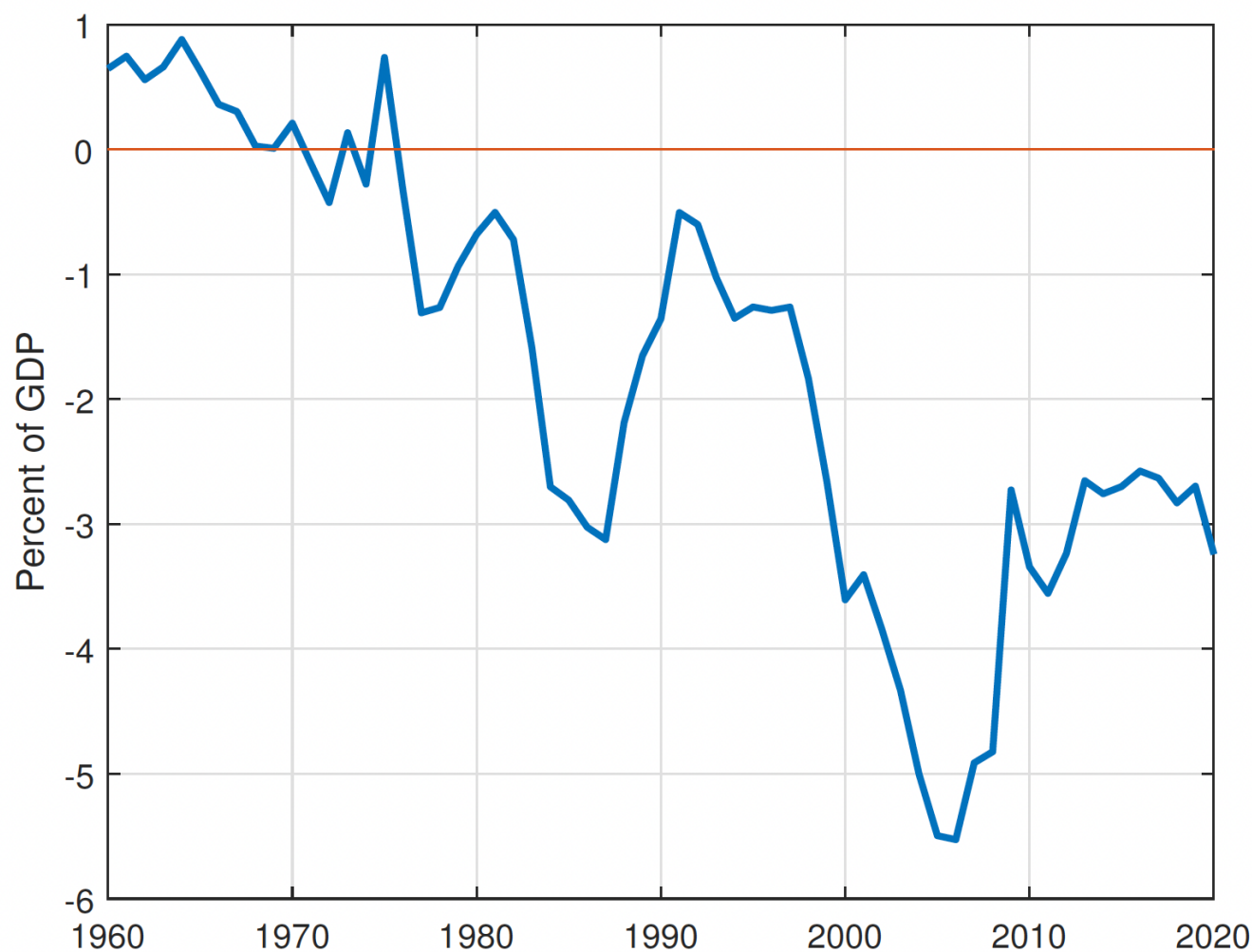
Global Imbalances

Balance of Payments = Current Account + Financial Account + Capital Account

Current Account:

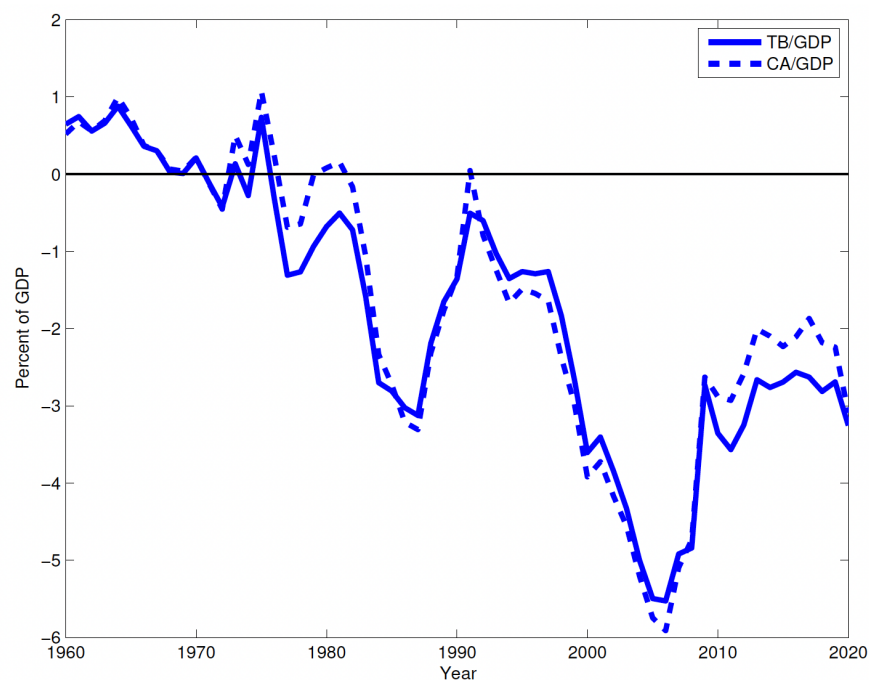
- Trade Balance = Exports - Imports (goods & services)
- Income Balance = Net Investment Income + Net Compensation to Employees
- Net Unilateral Transfers = Gifts received - given (large part are remittances)

The U.S. Trade Balance as a Share of GDP: 1960-2020



Data Source: BEA, bea.gov. TB data: ITA Table 1.1. GDP data: NIPA Table 1.1.5.

The U.S. Trade Balance and Current Account as Percentages of GDP, 1960–2020



Notes. *TB* and *CA* stand for trade balance and current account, respectively. Authors' calculations based on data from ITA Table 1.1 and NIPA Table 1.1.5 of the BEA.

Current Account vs. Net International Investment Position (NIIP) Flows vs. Stocks

Current Account (Flow):

- Annual borrowing/lending with rest of world

Net International Investment Position - NIIP (Stock):

- $NIIP = \text{Foreign Assets} - \text{Foreign Liabilities}$
- Accumulated wealth position

Relationship:

- Current Account Deficit \rightarrow NIIP falls
- Current Account Surplus \rightarrow NIIP rises

Why NIIP \neq Accumulated Current Accounts

Market valuations matter

NIIP changes from two sources:

1. Current Account flows (borrowing/lending)
2. Valuation changes (market price movements)

Valuation changes caused by:

- Stock price movements
- Bond price changes
- Exchange rate fluctuations

US Example (2002-2007):

- Ran \$3.9 trillion in current account deficits
- But NIIP improved by \$80 billion!
- Reason: \$4 trillion in positive valuation changes

Global Imbalances: Who Owes Whom? The world's creditors and debtors

Major External Debtors:

- United States (world's largest debtor)
- United Kingdom
- Australia, Spain

Major External Creditors:

- Japan, China, Germany
- Switzerland, Netherlands
- Norway, Saudi Arabia

Key Pattern:

- Advanced economies often run deficits
- Export-oriented economies often run surpluses
- Global constraint: $\sum \text{Current Accounts} \approx 0$

The NIIP-NII Paradox How can the US be a debtor but earn positive investment income?

The Paradox:

- US has negative NIIP (net debtor: -\$14.1 trillion in 2020)
- But positive net investment income (+\$191 billion in 2020)
- Imagine earning money on your credit card balance! Does this make sense?

Two Explanations:

1. "Dark Matter" Hypothesis:

- Unmeasured intangible assets (brands, know-how)
- True NIIP might actually be positive

2. "Return Differential" Hypothesis:

- US invests in high-return foreign assets (stocks, FDI)
- Foreigners invest in low-return US assets (Treasury bonds)
- "Exorbitant privilege" of reserve currency status