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Macro Roundup Artcile

Headline: Pettis On Obstfeld

Article Link: https://x.com/michaelxpettis/status/1802214257657851993

Author(s)	Michael Pettis
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Tweet: Responding to Maurice Obstfeld, @michaelxpettis argues that a capital inflow tax won't raise US interest rates because capital inflows are "more likely to cause domestic savings to decline than to cause domestic investment to rise."

Summary: The balance of payments must still balance, and so this means that foreign inflows must either cause US investment to rise or US savings to decline. If the US were a developing economy in which businesses were eager to invest, but were constrained by scarce and expensive capital, these inflows would indeed probably cause interest rates to decline and investment to rise. In advanced economies, net foreign capital inflows are more likely to cause domestic savings to decline than to cause domestic investment to rise. That is why they don't reduce interest rates, and why taxing them won't raise interest rates. Many Americans find it shocking to think that foreigners can affect US savings rates, but this is how the balance of payments works: if one country increases its savings relative to its investment, other countries must either increase their investment or reduce their savings. And because the US absorbs nearly half of the excess savings of the world (and the UK, Canada and Australia, much of the rest), it is mainly US savings that must rise and fall to accommodate that of the rest of the world.

Related Articles: The Dangers of a US Capital Inflow Tax and Can Trade Intervention Lead to Freer Trade? and He Helped Trump Remake Global Trade. His Work Isn't Done

Primary Topic: Savings Glut/Trade Deficit

Topics: Database, GDP, Op-Ed/Blog Post, Savings Glut/Trade Deficit

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