

Macro Roundup Article

Headline: [Misconceptions About US Trade Deficits Muddy The Economic Policy Debate](#)

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Author(s)	Maurice Obstfeld
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Tweet: Maurice Obstfeld argues that “foreign capital did not push in during 2002–06, it was pulled in” by low US interest rates and easing of US financial conditions which drove an increase in home prices and consumption.

Summary: Over 2002–06, the US external deficit grew by 1.7pp of GDP as the dollar depreciated by 14%, inconsistent with the view that capital inflows from abroad induced a bigger US deficit by expanding the demand for US assets and strengthening the dollar. The mechanisms at work [are] that low US interest rates and especially the easing of other US financial conditions allowed a big increase in home prices as well as in equity prices and consumption spending, accompanied by a weaker dollar. Higher consumption spilled over into imports and nontraded US products, drawing resources from the manufacturing export sector and raising the net export deficit at the same time. A demand switch from import-competing goods toward cheaper Chinese imports helps explain the China shock—and this switch would have occurred even if the US trade deficit had been smaller.

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Primary Topic: Savings Glut/Trade Deficit

Topics: Database, Fiscal Deficits, Fiscal Policy, GDP, Op-Ed/Blog Post, Savings Glut/Trade Deficit, Trade (not deficits)

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