Macroeconomic and Financial Imbalances in the World Economy

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Globalization = Imbalances

1. Presence of chronic imbalances over last 30 years -> do not get corrected by market forces or policy-mix adjustments, only by crisis-induced breaks in pattern.

2. Imbalances are systemic -> meta-economic view, as the whole of world economy is more than the sum of its parts => identify global growth dynamic within IMS.

3. Imbalances are mobilized by global finance -> meso-economic view of finance as a system, since ongoing transformation of financial system has changed capitalism itself (“finance-led capitalism”).
Origins of Global Finance


2. Crucial Role of Financial Innovations:
   • Eurocurrency Markets (1960s) -> global private banking network beyond reach of national regulators.
   • Wholesale Funding (1970s) -> money markets -> asset management -> more aggressive bank expansion.
   • Expansion of Bond Markets (1980s) -> junk bonds, emerging-market bonds.
Universal Banks = Pillars of GF

Universal Banks:
1) integration of indirect, market, and network finance;
2) scale + scope + network economies;
3) cartel-like extraction of monopoly rents;
4) organization of worldwide correspondent system and inter-bank markets;
5) privileged access to governments as TBTF institutions (SIFIs).
Contradictory Tendencies of GF

1) **Financial Concentration**: corporate accumulation of financial assets; preference for external growth via mergers and acquisitions; workers’ forced savings.
2) **Financial Centralization**: rapid growth of finance sector; income redistribution toward financial income.
3) **Monetary Fragmentation** (within IMS): From US-$ dominance to multi-currency system; variety of exchange-rate regimes; post-crisis home bias; uneven implementation of regulatory reforms.
4) **Centripetal vs centrifugal** forces within IMS.
Centripetal and Centrifugal Global Growth Dynamic (Meta-Economic Analysis)

- 1970s: Exporting of US stagflation and Petro-dollar recycling;
- 1980s: US stock-market bubble (as vehicle of post-stagflation industrial restructuring) and LDC debt crisis (Brady bonds);
- 1990s: US internet bubble and “Asian” Crisis;
Strategic Role of Exchange Rate

1) Carry Trade: excess appreciation, ER-volatility
2) Internationalization of “resource currencies”
3) Policy Responses and Challenges:
   • Capital Controls: how effective are they? what are their long-term effects?
   • ER-regime: neither peg nor float; what hybrid?
   • ER-level: inter-sectoral adjustment arbitrage between different sectors of large-EME economy.
Other Policy Challenges

1. Inflationary Pressures: low currency price -> more inflation; overheating risk; need to raise productivity growth, but that’s difficult.
2. Mixed Finance: kinked (or negatively sloped) yield curve -> ST bias; role of public FIs.