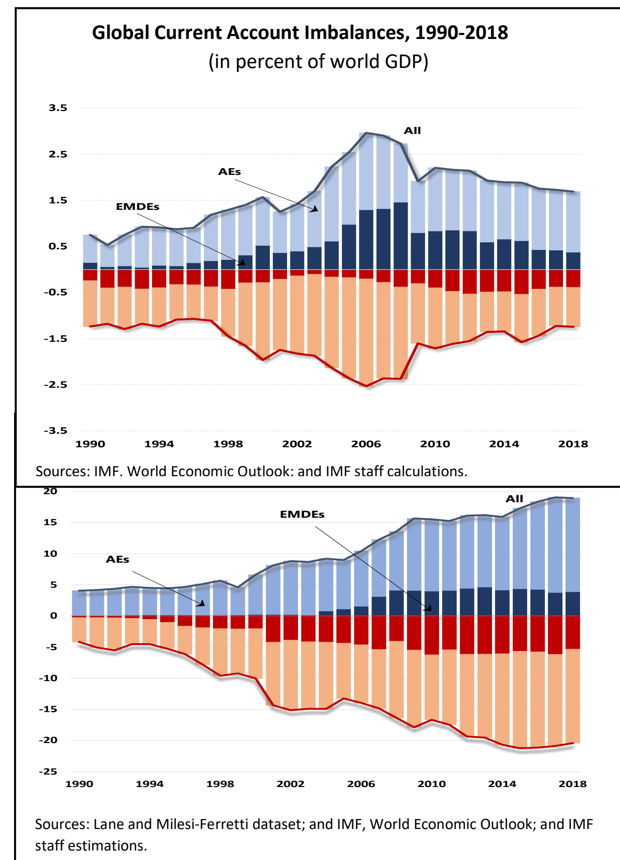
G20 FWG Summary Document on Global Imbalances[i]

While global current account imbalances narrowed in the aftermath of the global financial crisis, they remain large and persistent, and stock positions continue to diverge. While some imbalances may be appropriate, others may be excessive reflecting macroeconomic imbalances and structural challenges. It is important for G20 members to jointly address the underlying causes and mitigate the risks arising from excessive imbalances to achieving strong, sustainable, balanced and inclusive growth.

As we have discussed in the past decade as a core mandate of the FWG, reducing excessive imbalances in a growth-friendly manner requires a joint effort by G20 members. Addressing domestic macroeconomic imbalances and structural challenges remains of the essence to reducing external imbalances. Exchange rate flexibility, where feasible, will help support the necessary external adjustments. Further progress toward free, fair, and mutually beneficial goods and services trade will be critical. The joint G20/IMF Spring Meetings Seminar held in Washington D.C. offered a good opportunity for the G20 membership to broaden their perspectives and deepen their understanding of issues relating to global imbalances, while highlighting the need for additional analysis of the underlying drivers of global imbalances both in terms of flows and stocks, including the role of exchange rates in external adjustment, the drivers of corporate saving, and measurement challenges, among others.

Discussion of global imbalances and risks

Global current account deficits and surpluses, as measured against world GDP, have been reduced by over 40 percent from the high levels seen before the global financial crisis. However, they remain high compared to the early 1990s and persistent**.** Imbalances are increasingly concentrated in advanced economies (AEs), as emerging markets and developing economies (EMDEs) have experienced a narrowing in their surpluses or their deficits.



Sources: IMF. World Economic Outlook: and IMF staff calculations.

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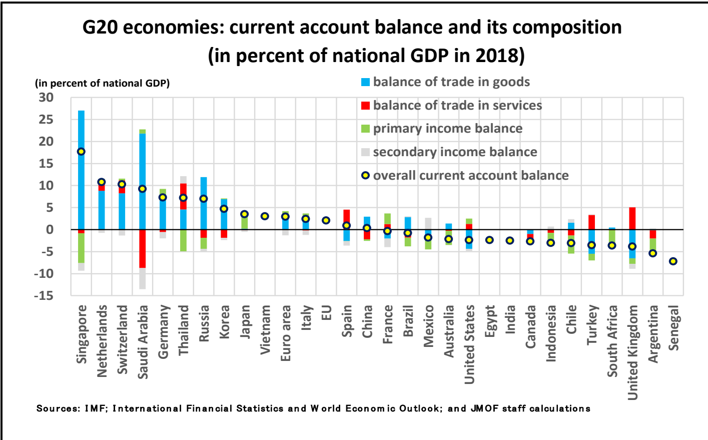
External stock positions have continued to diverge. According to the IMF, the sum of net creditor and net debtor positions is at a historical peak and four times larger than in the early 1990s. This divergence of stock positions took place against the backdrop of persistent flow imbalances, contributing to an increase in primary income earnings or payments from foreign assets or liabilities respectively. Movements in stock positions have also been influenced by valuation effects in the form of exchange rate and asset price movements. Also, some EMDEs have seen their secondary income strengthen significantly over the years, on the back of strong remittances from their overseas workers. All this, combined with the increasing prominence of the services trade balance in some countries, underscores the importance of monitoring all components of the current account (i.e., balances of trade in goods and services, and income balances), as well as the size and composition of international investment positions, including valuation effects.



Underlying drivers of global imbalances vary across countries, highlighting the need for nuanced and targeted policy recommendations. Global imbalances reflect a combination of cyclical factors, domestic policies and fundamentals, as well as spillover effects from abroad. Among AEs, the imbalances were generally driven by an asymmetry in demand strength, in part reflecting differences in fiscal policy stances. In addition, rising gross corporate saving also appear to have played a role in some AEs. In EMDEs, the IMF notes reserve accumulation has become a far less significant driver of current account dynamics since the crisis, with fiscal and credit policies playing a more important role. At the same time, fluctuations in commodity prices continue to have significant implications for current account balances in some countries. Meanwhile, the BIS notes that with growing global financial integration, the impact of exchange rates on the economy through financial channels may have become more important than through traditional trade channels, especially for EMDEs that borrow in foreign currencies. Progress is needed to strengthen external statistics, both in flows and stocks, to correctly assess external positions, especially given the growing role of multinational corporations and global value chains, where the boundaries between residents and non-residents can be blurred.[ii]

Excess global imbalances can fuel vulnerabilities and risks. FWG members generally agreed that current account surpluses or deficits may be appropriate and in line with economic circumstances—for example, when they reflect the need to accumulate savings to prepare for an increasing pool of retirees in economies with rapidly aging populations (resulting in current account surpluses) or foreign funds flowing to rapidly growing economies with ample investment opportunities (resulting in current account deficits). However, others may also reflect domestic policy settings that lead to macroeconomic and financial vulnerabilities and pose risks.[iii] Meanwhile the composition of funding sources of the external balance is also important when examining whether global imbalances pose financial stability risks. For example, FDI provides relatively more stable funding than others.

The FWG stressed the need to reduce short- and long-term risks from global imbalances. The increased concentration of deficits in advanced countries lowers near-term financing risks. However, a synchronized global slowdown or increasing policy uncertainties with knock-on effects on commodity prices and global risk aversion could affect the external debt service capacity of some EMDEs, especially those highly reliant on foreign demand and short-term financing denominated in foreign currencies. Over the medium term, a further widening of stock positions could also result in a disruptive adjustment in debtor economies that could spill over to creditor economies and have global and/or regional ramifications. In addition, excessive flow imbalances induced by, for example excessive credit growth and excessively high corporate or precautionary household savings, could put at risk the G20 goal of achieving strong, sustainable, balanced, and inclusive growth.

Joint policy actions

Carefully calibrated macroeconomic and structural policies tailored to specific country circumstances will continue to be important (see Annex). Countries with excessive deficits can help by conducting growth-friendly fiscal consolidation and, where credit is excessive, improving financial sector oversight (including

possibly by tightening macroprudential measures). On the other hand, countries with excessive surpluses can help by making use of available fiscal space to boost potential output, including increasing public investment, and avoiding overreliance on accommodative monetary policies. Well-tailored structural reforms are also critical. For excess deficit countries, reforms that increase competitiveness by enhancing labor market flexibility and strengthening the skill base of workers, while encouraging saving by adjusting pension schemes (including reducing pension generosity) and advancing financial deepening, will help mitigate risks. Many excess surplus countries have scope for reforms that address excessive corporate saving by encouraging investment and further liberalizing trade in goods and services (e.g. removing barriers) as well as reforms that discourage excessive precautionary household savings including by widening the coverage of the social safety net, reducing the labor tax wedge, and further encouraging elderly labor participation. Specific policy actions should be targeted at the identified drivers of imbalances in each country.

Exchange rate flexibility, where feasible, should continue to help support the external adjustment process, although its impacts are likely to vary across countries, especially given their different degree of integration into global value chains and varying compositions of the current account. Ongoing analysis by the IMF suggests that the extent of integration into global value chains and invoicing in dominant currencies may dampen some of the effects especially in the short run. On the other hand, the BIS notes that the role of exchange rates may have changed in an opposite direction from the traditional external adjustment role, especially in EMDEs, as funding availability in dominant currencies became crucial in global economic activities. The composition of funding sources also needs to be carefully monitored. Especially, currency and maturity mismatches may pose risks and limit exchange rate policy options, given the rapid rise in corporate indebtedness in many EMDEs, as suggested by recent BIS research.

Free, fair, and mutually beneficial goods and services trade will support efforts to reduce domestic imbalances, while supporting growth and helping to contain risks of trade policies that distort the level playing field. External imbalances primarily reflect macroeconomic imbalances and structural challenges. In this regard, lower trade costs can foster a more efficient allocation of resources and boost productivity. Therefore, the focus should be on removing barriers and pursuing pro-growth strategies. Promoting trade in services could generate substantial gains, but barriers remain high in certain economies.

The FWG welcomes the primary contributions from the IMF, in line with its mandate, as well as other IOs in analyzing global imbalances. It calls on the IMF to conduct further analysis to help members' understanding of the underlying drivers, including how exchange rates affect the adjustment of the current account and its components, the risks posed by diverging stock positions, and the role of corporate saving in explaining the evolution and persistence of imbalances. Another set of issues that warrants the attention of the FWG members is potential measurement challenges posed by the growth of multinationals and global value chains, and the need to strengthen external statistics to ensure the proper attribution of income from different sources. The analysis should be taken from a global perspective so as to get a consistent and complete picture of the root causes that give rise to excess global imbalances.

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[i] This document draws on the IMF's background paper on global imbalances, as well as G20 member discussions at 2019 meetings of the G20 Framework Working Group for Strong, Sustainable, Balanced and Inclusive Growth, and the joint G20/IMF Spring Meetings Seminar held in Washington, D.C.

[ii] The G20 Data Gaps Initiative helps fill in the gaps to some extent, but may not be able to fully address the challenges posed by the growing role of multinationals and global value chains given its specific nature.

[iii] The IMF estimates that in 2017 about 40 percent of global imbalances were excessive and partly a consequence of undesirable policy settings.

Annex: Overview of joint G20 policy actions to mitigate risks arising from excessive imbalances