Comments on

The US Current Account

and the Dollar

by Blanchard, Giavazzi, and Sa

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UC Berkeley, CEPR and NBER
A fine paper!

- Good topic

- Nice model
  
  - Especially inclusion of valuation effects

- Reasonable assumptions

- Appropriate caveats
Bottom line eminently plausible

• Bearish on dollar

• Fiscal adjustment AND depreciation needed

• Going to the dentist sooner is easier than later
Of course …

- Ambitiousness necessarily implies vulnerability

Still,

- Most questions are small/technical/unimportant
Comments in Passing

- A paper seemingly written for/by US macroeconomists?
  - (exchange rate is not price of foreign exchange)
Is it Possible to Discuss these issues sensibly without Addressing Mystery #1?

- Why is long American interest rate so low and falling?
Doubts about Imperfect Asset Substitutability

- Good: Model works well in quantities
  - Home bias

- Bad: Model works poorly in prices
  - UIP deviations not linked empirically to shares/debt
  - A long history of failure, e.g., Frankel (1982)
  - Profession gave up on this in part because of evidence
Asset Preferences and Expected Long Run Depreciation

• Plausible to argue that asset preferences aren’t more affected by expected paths and history?

• Will foreign investors take slow, steady depreciation of their $ assets?

  o 56% (p 23) is a large number and exchange rates often move too much in short-run (for unknown reasons)

  o p13: key that American liabilities in $
Perhaps Not an Issue

- In practice, almost all movements to floating exchange rates unexpected

- Deterministic trends swamped in practice

- Includes big movements, which are sharp and usually unexpected (Figure 4)

- So trend may be there but very hard to detect
Bilateral Current Account Balances and Wealth

Reallocations

• Unusual to see bilateral accounts in macroeconomics

  o Usually only multilateral accounts matter

    ▪ Solow’s barber

  o Financial intermediation through third countries

  irrelevant?
US Trade Deficit 2004

• BGS: $652 bn
  
  o half China ($160 bn)

  o one-quarter each: Euro area ($71bn), Japan ($75bn)

  o ignore half the deficit! ($346 bn)!
• **Data** (ERP Table 105):
  
  - $641 billion total
    - China $153 bn
    - Euro $84 bn
    - Japan $76 bn
But also

- Canada $69 bn
- Mexico $46bn
  - Anti-North American bias!
More seriously, ignoring RoW means ignoring:

- “Fear of Floating”
- Countries with strong $ preferences
  - Latin America, E Asia all historically resist $ depreciation actively
  - Yen also actively managed from time to time (Ito)
  - More adjustment possible in $/Euro?
Dooley-Garber on Future

- India, Indonesia, etc. lining up if China’s “development through undervaluation” is successful
Bottom Line

• Thorough, reasonable paper HIGHLY worth reading

• Agree with major conclusions

• Especially conclusion that large $ depreciation not a catastrophe

  o Ditto loss of $ as anchor/reserve currency

  • Unlikely even in long run,

  • Not critical anyway (seigniorage small)