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\*The views expressed belong only to the author and are not necessarily shared by the ECB. With thanks to S. Arrighi, M. Ca'Zorzi, M. Fidora, G. Georgiadis and M. Rau-Göhring for their input.

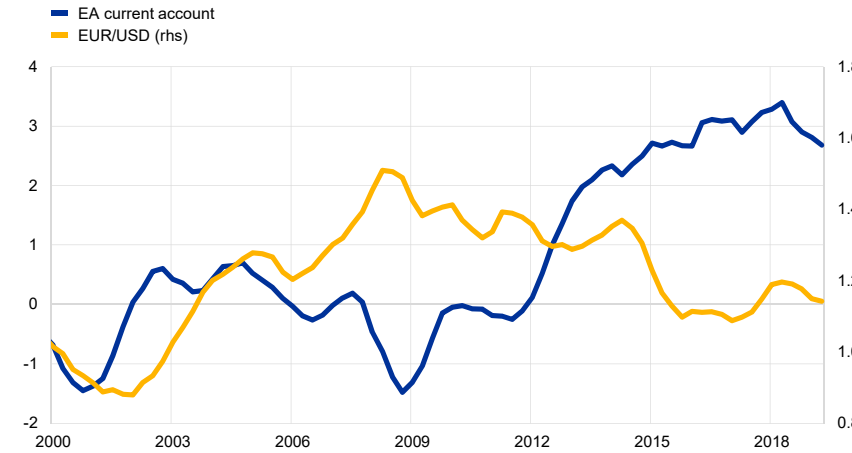
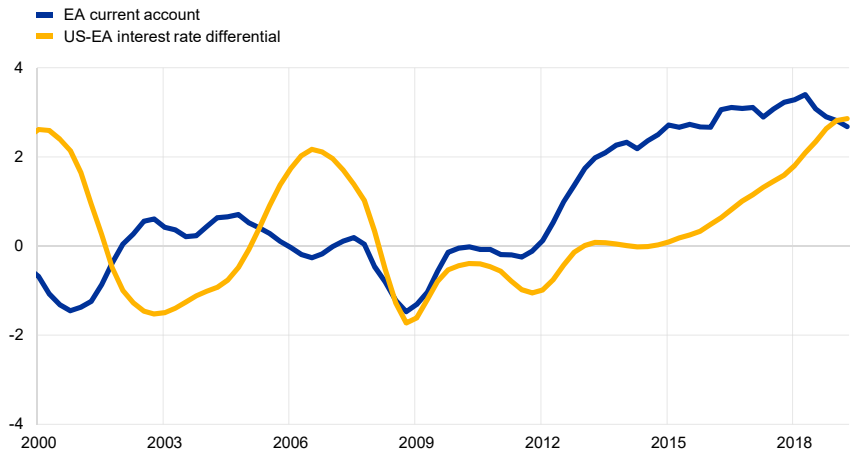
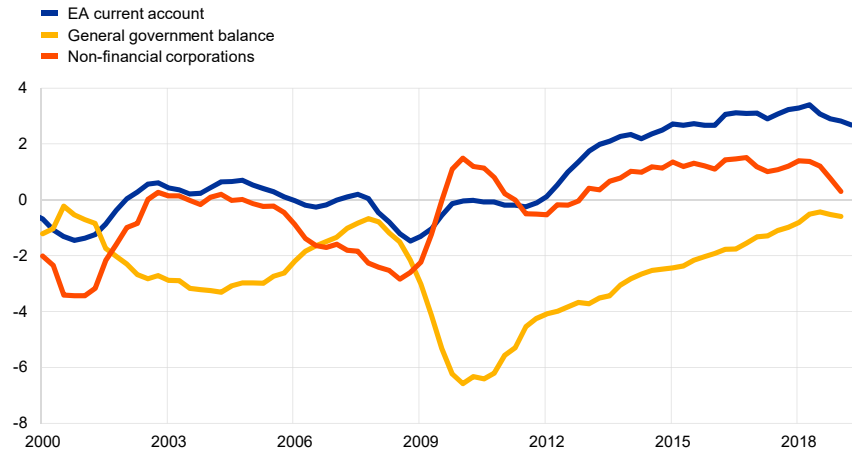
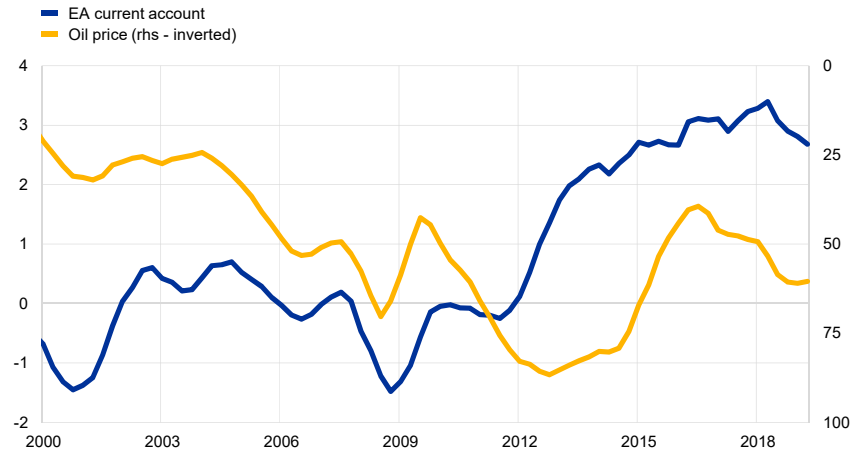
# Current account adjustment: Some evidence from the euro area

Banco de España and Reinventing Bretton Woods Committee Conference

*Global Imbalances and Capital Flows in the Era of New Technologies*

Madrid, 10 September 2019

# What is driving the euro area current account?

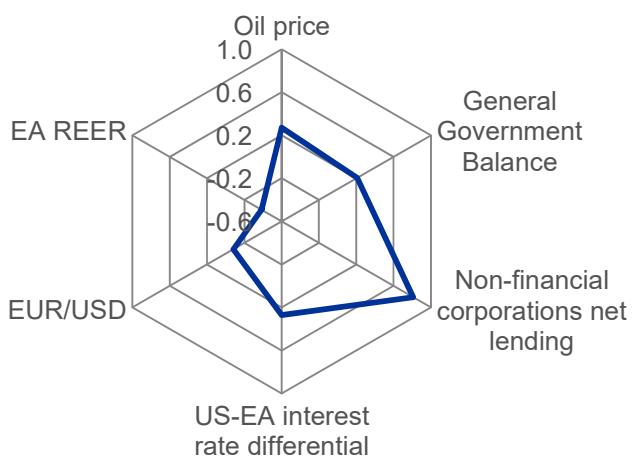


Source: National Central Banks/National Statistical Offices, ECB, Eurostat, and Haver Analytics.

Notes: Data are 4-quarters moving averages. The interest rate differential is based on 3-months short-term interest rates, the oil price is Brent.

# What is driving the euro area current account?

Correlations with EA Current Account	
Oil Price	26.9%
General government balance	21.1%
Non-financial corporations net lending	81.1%
US-EA interest rate differential	27.0%
EUR/USD	-8.2%
EA REER	-38.4%



Source: National Central Banks/National Statistical Offices, ECB, Eurostat, BIS, and Haver Analytics.

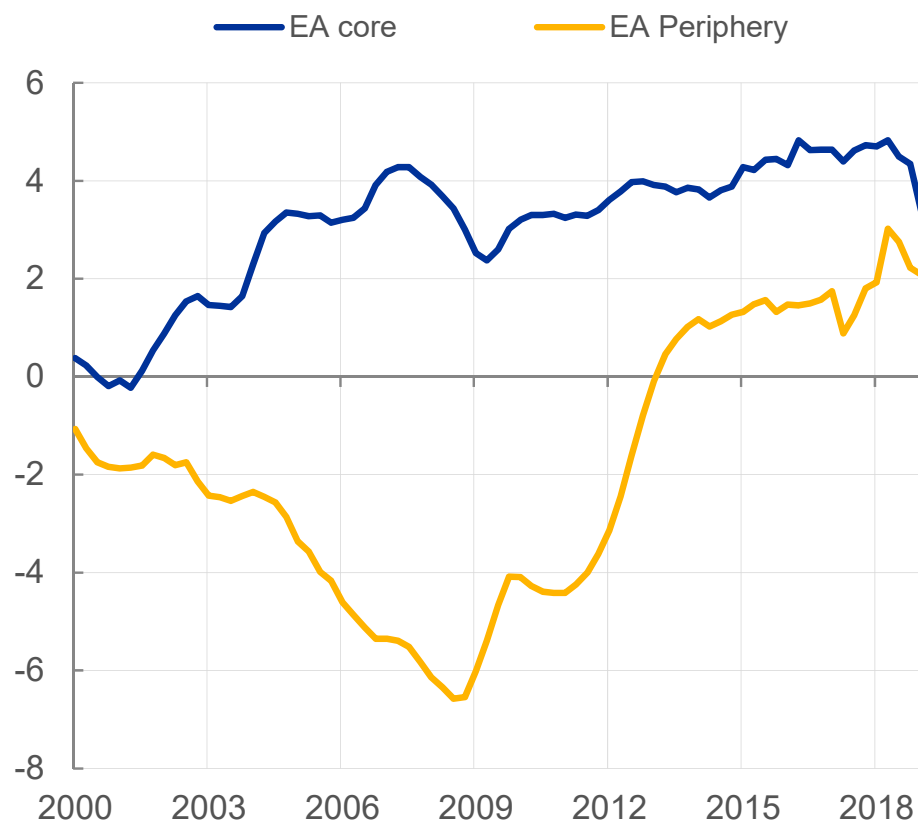
Notes: Quarterly data.

# Asymmetric adjustment once again?

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Current account balance (in % of GDP) - quarterly



- Germany: An issuer of a safe asset in surplus (Landau, 2017)
- However, important to take a euro area perspective

Source: National Central Banks/National Statistical Offices, ECB and Eurostat.

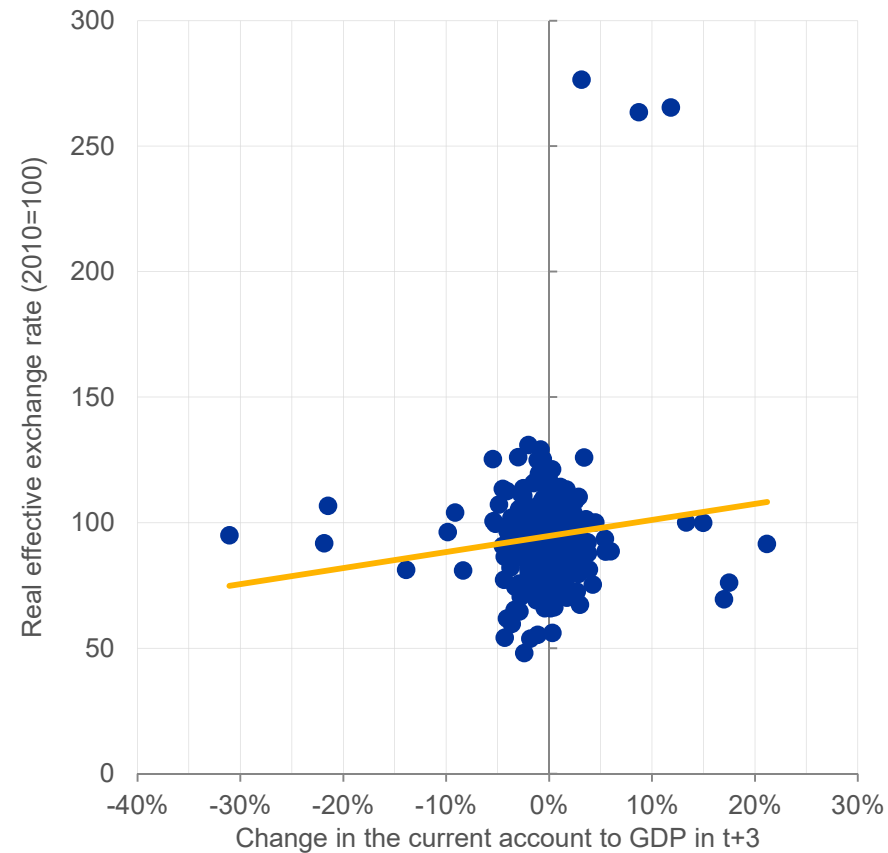
Notes: Data are 4-quarters moving averages.

# The FX adjustment channel is weak

- **Why?**
- **Two potential explanations:**
  - Weak link between FX movements and terms of trade
    - Several possible reasons: GVC, strategic complementarities, DCP (at least temporarily, if prices are sticky)
  - Weak link between terms of trade and the trade balance (current account)
    - Low trade elasticities? (may be higher in the medium term once technology has adjusted)

# Wrong sign for floating countries

## Floating currencies (G20 ex China), 1999-2018

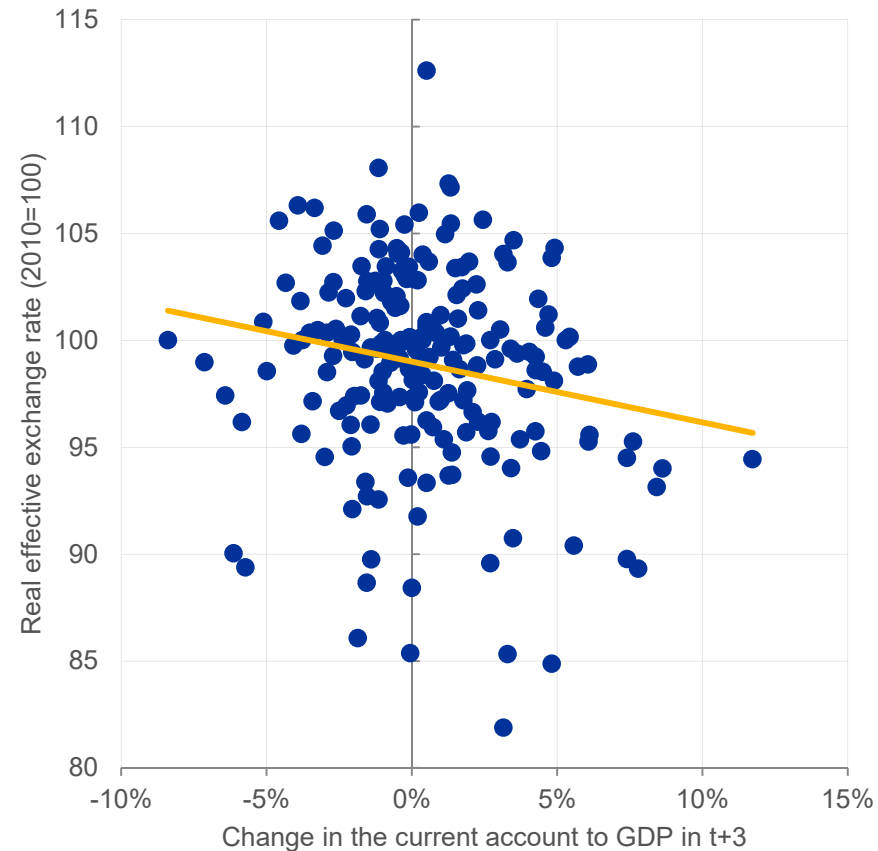


Source: National Central Banks/National Statistical Offices, ECB staff calculations, BIS and Eurostat.

Notes: The euro area enters as an aggregate.

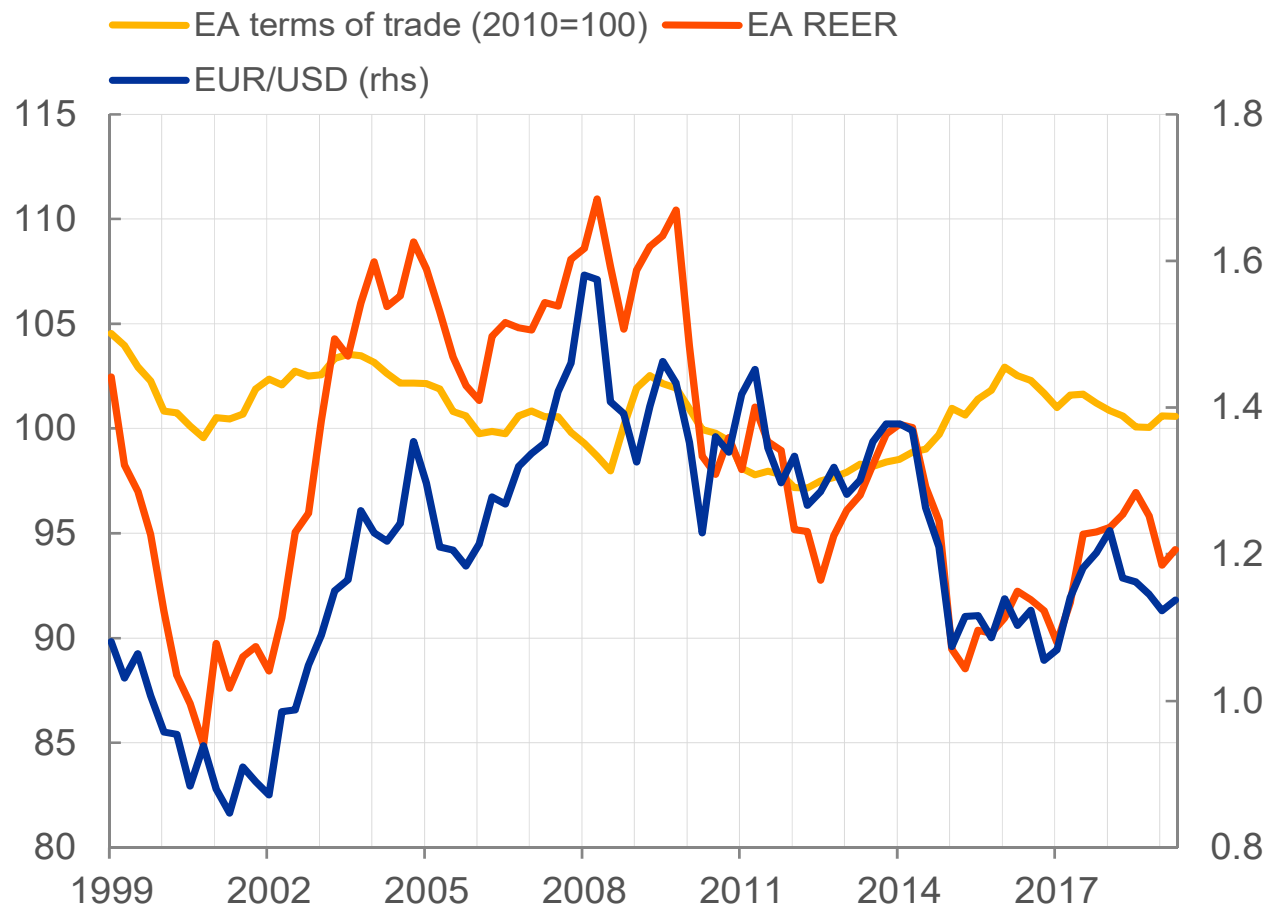
# At least the sign is right for the euro area countries

EA countries in 1999 plus Greece, 1999-2018



Source: National Central Banks/National Statistical Offices, ECB staff calculations, BIS and Eurostat.

# Unstable link between EUR/USD and terms of trade in the EA



Source: National Central Banks/National Statistical Offices, ECB, Eurostat, BIS, and Haver Analytics.



## Selected recent ECB work on global imbalances

- **Impact of service trade liberalisation**
  - Georgiadis and Mijakovic (2019) show that liberalising service trade would reduce CA deficits in some debtor countries but at the same time increase CA positions of surplus countries.
  - Overall, ECB results show that global imbalances would increase further.
- **GVC participation, CA imbalances, and exchange rate pass-through to export/import prices**
  - Georgiadis, Gräb et al (2019) show that GVC participation has effect on CA: Countries with greater GVC participation have larger CA surpluses.
  - The existence of cross-country production linkages may amplify exchange rate pass-through to export prices but thereby dampen exchange rate pass-through to import prices.
- **Impact of dominant currency pricing (DCP)**
  - Georgiadis and Schumann (2019) show that the response of net exports to USD appreciation is inversely related to the export-import DCP invoicing share differential
  - Heterogeneity in DCP invoicing share differentials therefore implies differences in countries' CA adjustments following USD exchange rate variation