Capital Flows in the United States

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Capital Flows – An Overview

• What are capital flows?
• How are they measured?
• How have capital flows evolved over time in the United States?
• Is being a net debtor sustainable?
• What is the relationship between public debt and fiscal deficits?
The Balance of Payments and its Different components
The Balance of Payments

- In the U.S., international transactions are recorded by the Bureau of Economic Analysis (BEA) in the balance of payments.

- The balance of payments has three components:
  - The financial account (change in international ownership of assets)
  - The capital account (any other financial transactions)
  - The current account
The Current Account

- **Current Account** = Trade Balance + Income Balance + Net Unilateral Transfers

- **Trade Balance** = Goods Balance + Services Balance

- Why is the current account important? It tells us if a country is a net debtor or net lender

- Has the U.S. been a net debtor or lender **historically**?
Deficits and Surpluses

• Who are the U.S.’s main trading partners?

• If the U.S. is running a large current account deficit, some other countries must be running current account surpluses. Why?

  \[ \text{Current Account (U.S.)} + \text{Current Account (Rest of the World)} = 0 \]

• So who is running big current account surpluses?

Source: International Macroeconomics Ch. 1: Global Imbalances, Schmitt-Grohé, Uribe, Woodford, 2018
Can a Country Run a Perpetual Current Account Deficit?

- In the absence of valuation changes, the change in the net international investment position (external financial assets minus liabilities $\text{NIIP}$) is the current account:
  \[
  \text{Current Account}_1 = \text{NIIP}_1 - \text{NIIP}_0
  \]

- Similarly, in period 2 we have:
  \[
  \text{Current Account}_2 = \text{NIIP}_2 - \text{NIIP}_1
  \]

- Assuming that $\text{NIIP}_2 = 0$, and combining the previous two expressions to eliminate $\text{NIIP}_1$, we obtain:
  \[
  \text{NIIP}_0 = -\text{Current Account}_1 - \text{Current Account}_2
  \]

- If $\text{NIIP}_0 > 0$ (initial positive asset position), the country can run current account deficits in both periods.
From the Current Account to Public Debt
U.S. Public Debt since 1952

Source: U.S. Treasury, BEA, Haver, author's calculation
From External Debt to Fiscal Deficits
The Fiscal Balance

• Fiscal Balance = Government Income - Government Expenditure

• Government debt: accumulation of fiscal deficits

• Government expenditure includes the service of the debt

• Is there a relationship between the fiscal and CA deficit?
U.S. Fiscal Balance since 1954

Percent of GDP

Sources: U.S. Treasury, BEA, Haver, author's calculations
U.S. Twin Deficits since 1960

Source: U.S. Treasury, BEA, Haver, author's calculations
Key Takeaways

• The U.S. current account deficit is sustainable

• From an economist’s perspective there is no need for trade wars

• No systematic correlation between current account and fiscal deficit
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U.S. Current Account since 1960

Percent of GDP

Sources: BEA, author's calculations

The Current Account
U.S. Trade Balance since 1950

The Current Account

Trade Balance = Goods Balance + Service Balance
Goods Balance = Exports of Goods − Imports of Goods
Service Balance = Exports of Services − Import of Services

Sources: BEA, author's calculations
Historical U.S. Goods Trade Balance

Percent of GDP

Sources: World Trade Historical Database, Measuring Worth, BEA, author's calculations

The Current Account
U.S. Trade Balance with China

Sources: Census, BEA, author's calculations

Deficits and Surpluses
Historical U.K. Goods Trade Balance

Sources: Correlates of War, World Trade Historical Database, Measuring Worth, OECD, author's calculations