GLOBAL CAPITAL COMPETITION

I- The push-pull forces of global capital flows

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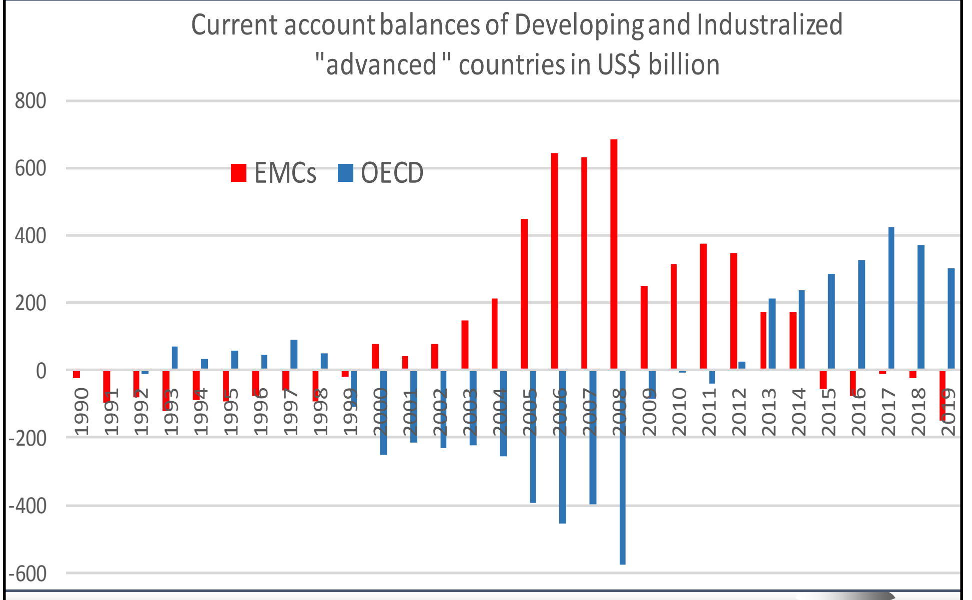
MYTH 1: CAPITAL FLOWS FROM RICH TO POOR COUNTRIES

Emerging market countries have < capital and offer > returns. By borrowing abroad, EMCs should be able to boost investment and growth rates!

- **Fact 1**: : Most « rich and developed » countries live « beyond their means » and must import capital
- **Fact 2:** EMCs' dynamic growth boosts savings, hence a current account surplus (Asia!).
- **Fact 3**: Capital is flowing « uphill » and the US twin deficit is financed by foreign countries' purchase of US Treasury securities.

WHO FINANCES WHOM?
CURRENT ACCOUNT BALANCES OF OECD (36) AND EMCS (160)

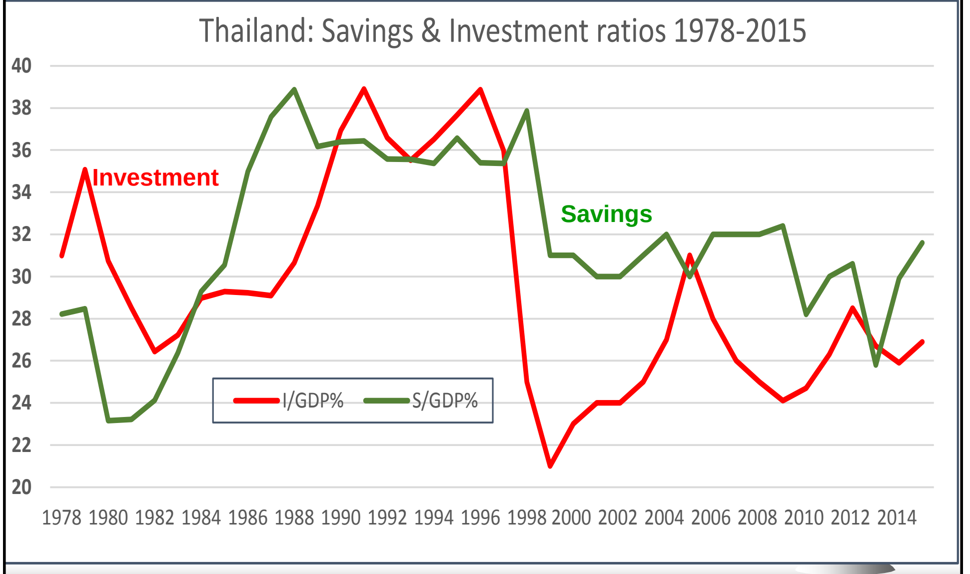


Source: IMF-WEO 2019

Why did most EMCS hold such large FX reserves and current account surplus… until the global financial crisis?

1. 1982 debt crisis + 1994 Tequila crisis + 1997 Asian crisis + 1998 Russian crisis + 2001 Argentina crisis + global crisis 2008-16 =
2. Strong IMF-monitored adjustment + economic and trade liberalization = FDI
3. Surge in raw material and oil prices until 2014
4. Devaluation + Boost in investment ratio= Current account surplus + reserve increase
5. Improvement in debt indicators
6. Since 2010, low interest rates and investors' search for yield finance growing CA deficits

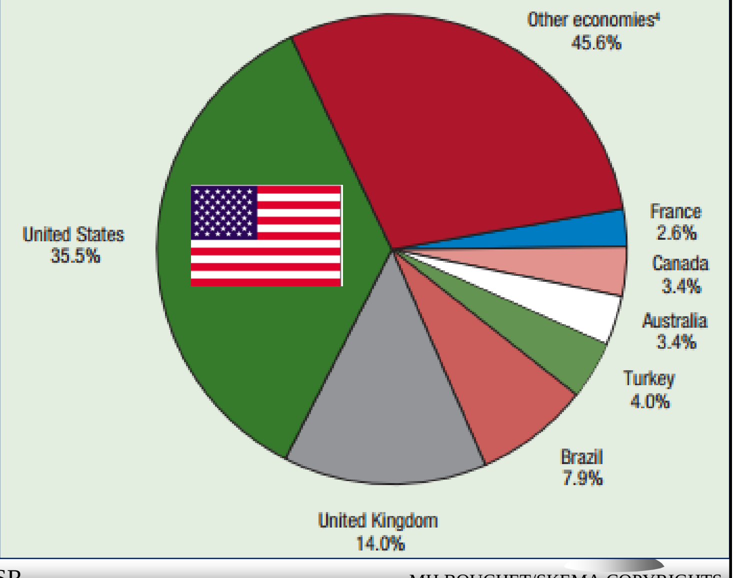
The long-term dynamics of investment and national savings



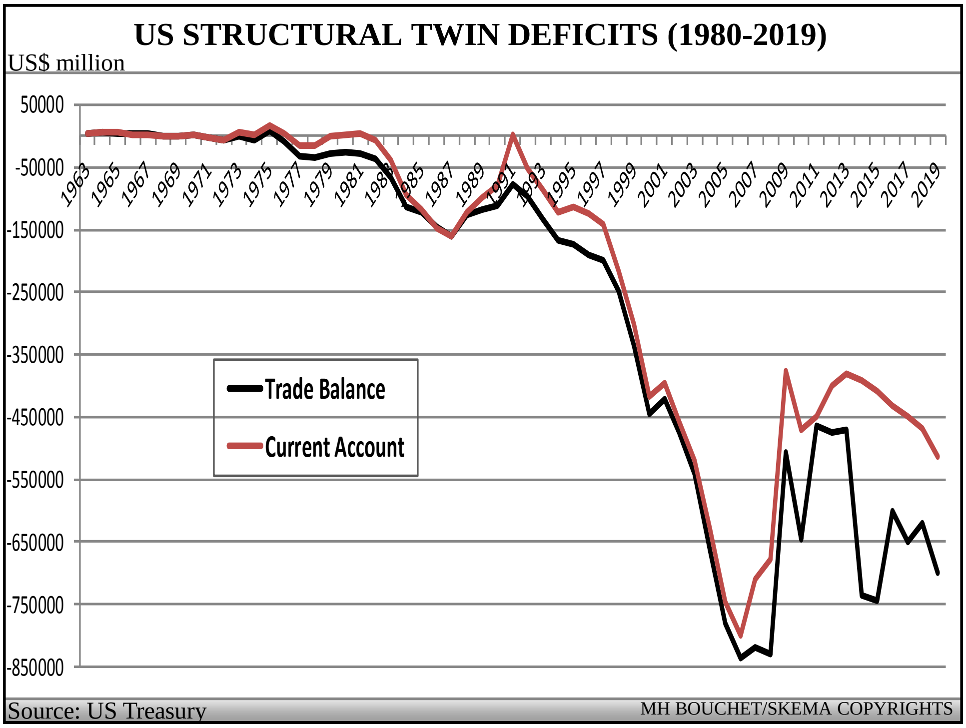
Source: WB and IMF 2015

LIVING BEYOND ITS MEANS:
MAJOR NET IMPORTERS OF CAPITAL

> 60% of economies that import capital flows are in the OECD



Source: IMF 2015 GFSR


US STRUCTURAL TWIN DEFICITS (1980-2019)
US$ million
50000
-50000
-150000
-250000
-350000
-450000
-550000
-650000
-750000
-850000
1963
1965
1967
1969
1971
1973
1975
1977
1979
1981
1983
1985
1987
1989
1991
1993
1995
1997
1999
2001
2003
2005
2007
2009
2011
2013
2015
2017
2019
Trade Balance
Current Account
Source: US Treasury
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GLOBAL COMPETITION IN FINANCIAL MARKETS
DEFICIT
-$500 billion
= $1,4 billion/day
SURPLUS
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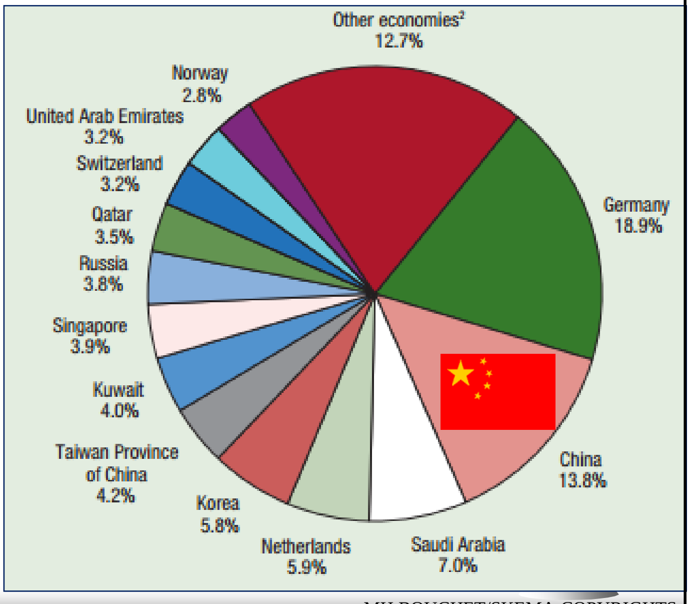
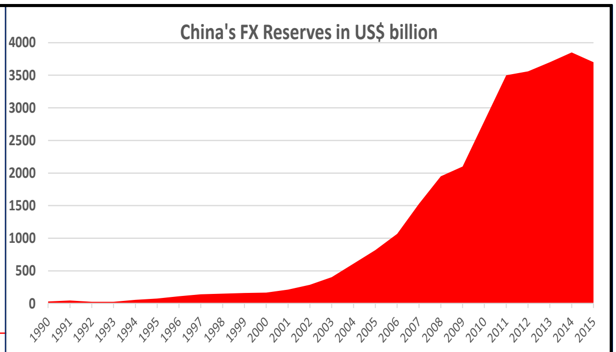
Major economies that export capital

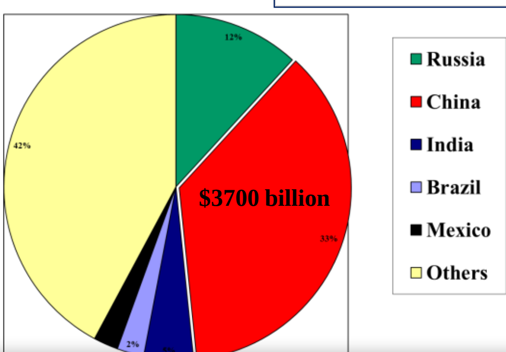
> 50% of global capital stems from emerging market countries that enjoy balance of paiements **surplus**



Source: IMF 2015 GFSR

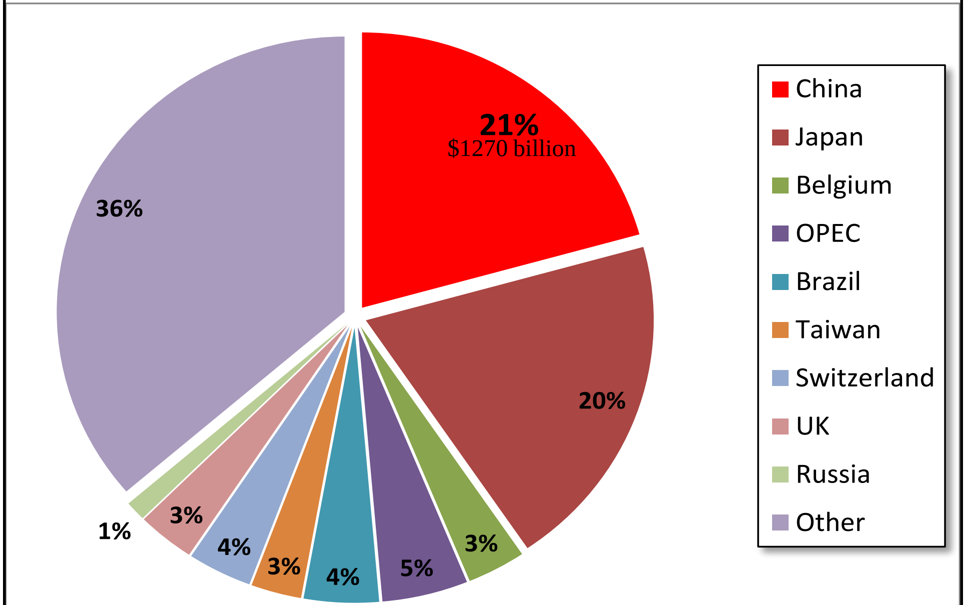
The rise (and decline) in China's hard currency reserves





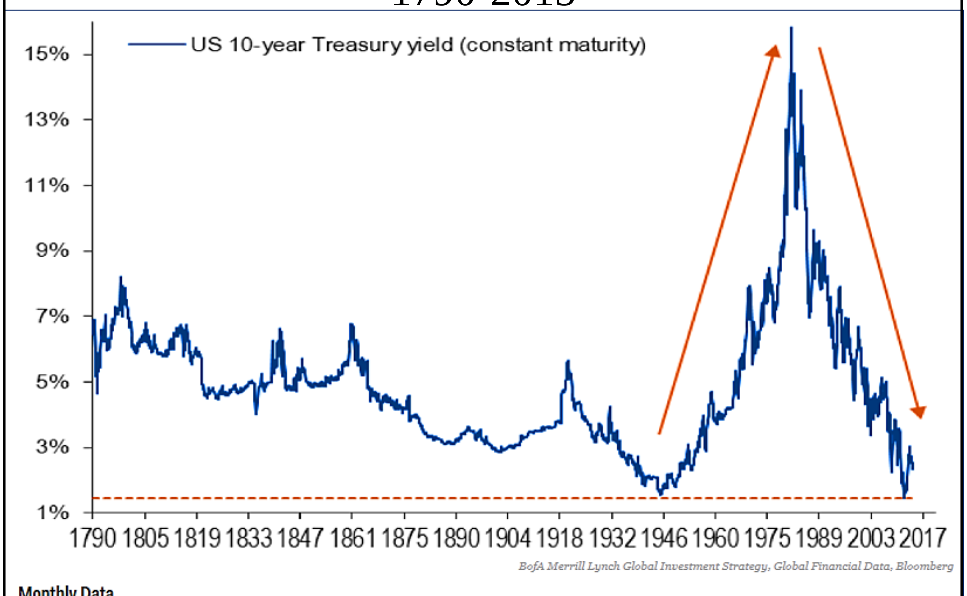
Σ world reserves = $11,500 billion

CHINA = > 1/5 OF FOREIGN HOLDING OF US DEBT



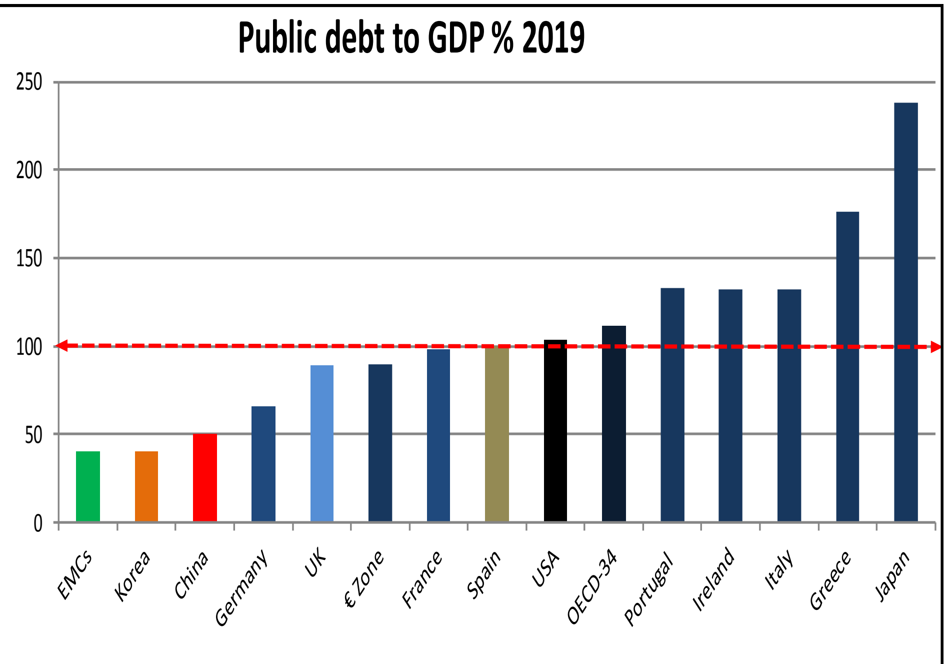
US Treasury 08/2015

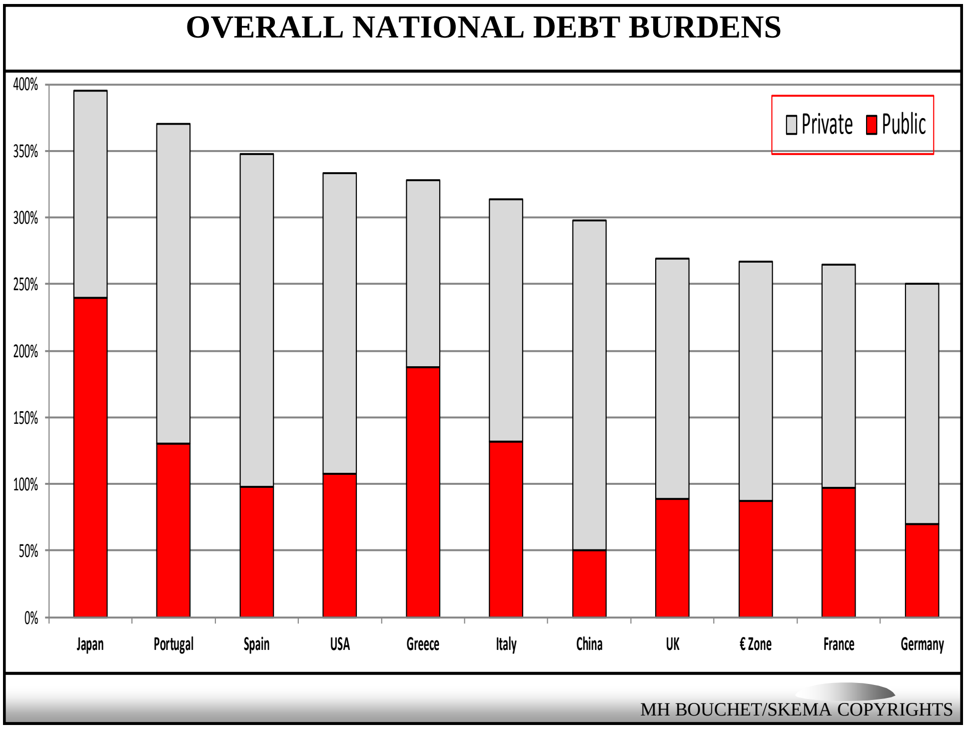
The rise and fall of US 10-year Treasury yields 1790-2015



MYTH 2. DEBT OVERHANG IS A SALIANT FEATURE OF EMCS

1. Capital flows finance countries with balance of payments deficits, those that consume more than they save
2. EMCs have much lower solvency ratios (Debt/GDP) than most OECD countries




OVERALL NATIONAL DEBT BURDENS
Private
Public
400%
350%
300%
250%
200%
150%
100%
50%
0%
Japan
Portugal
Spain
USA
Greece
Italy
China
UK
€ Zone
France
Germany
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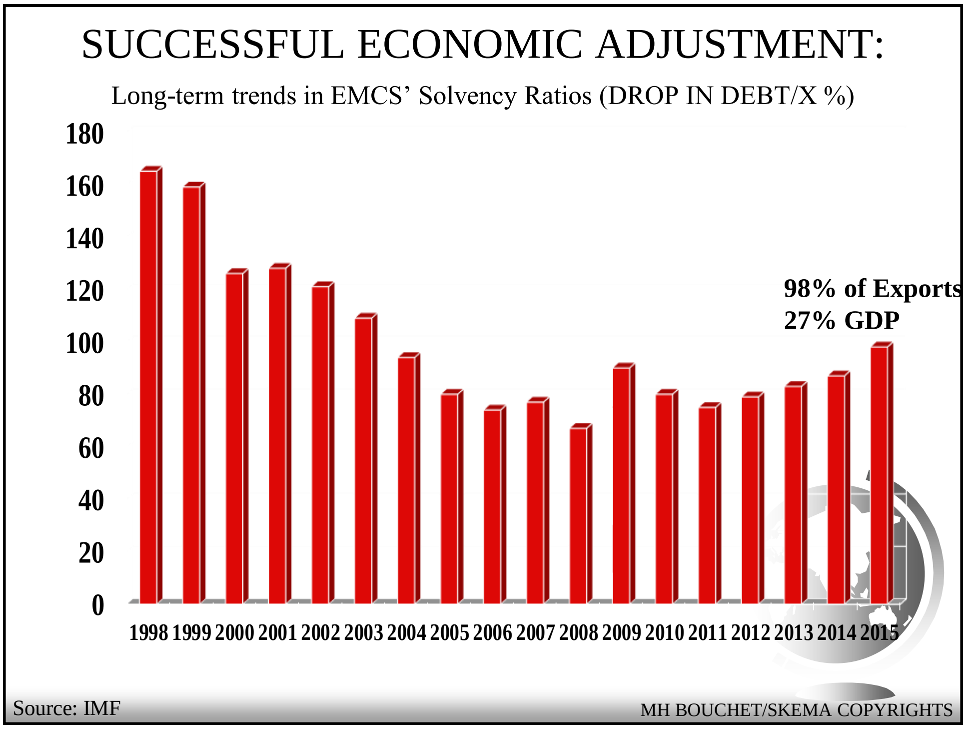
SUCCESSFUL ECONOMIC ADJUSTMENT:
Long-term trends in EMCS' Solvency Ratios (DROP IN DEBT/X %)
180
160
140
120
100
80
60
40
20
0
98% of Exports
27% GDP
1998 1999 2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 2015
Source: IMF
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