

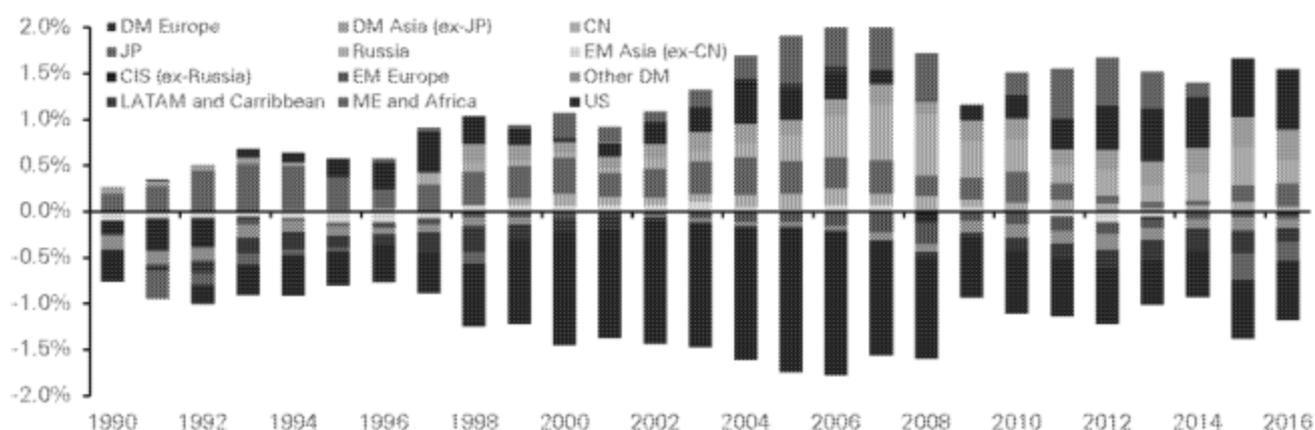


allowed to build which gave policy makers more short-term flexibility but arguably left them more vulnerable to the whims of international capital flows over the medium to longer term.

As we discussed in the main section, the EM crises of the late 1990s seemed to take global current account imbalances to the next level as those who suffered most in this period vowed to ensure they operated with surpluses from that point on to protect themselves from a repeat of the extreme stresses of the period. As such Figure 52 and Figure 53 show that the last 20 years have seen these imbalances hit extreme levels. China's huge current account surplus (c.10% in 2007) was perhaps a contributor to the GFC (alongside all the other surplus countries) as their excess savings were largely channeled into safe US assets like US treasuries thus lowering global interest rates and leading to a huge global credit expansion. At the time, China didn't allow its currency to appreciate to correct the imbalances thus encouraging these excesses to continue for longer than they should have done.

Although China's surplus has dramatically reduced post the GFC, it's not obvious from Figure 52 that overall global imbalances have reduced much since the crisis. Figure 54 shows the entirety of the globe's current account imbalances cumulatively (stacked) by groupings as a percentage of global GDP and shows that although the imbalances are off their 2006/2007 peaks, they remain elevated. So if current account imbalances were a contributor to unstable markets leading up to the GFC and the Euro Sovereign crisis in 2010-2012 then they equally could be a cause today given that the overall numbers are similar.

Figure 54: Global imbalances – Current account balances (% of global GDP) – Legend ordered from largest surplus (DM Europe) to largest deficit (US) as of 2016



Source: Deutsche Bank, Haver (IMF data)

It's clear from Figure 52 - Figure 54 that we live in a world where huge cross border flows are essential to fund the status quo. As such this surely makes the financial system more crisis prone as domestic policy makers have less control of their own economy. If sentiment changes in the global financial system, flows can reverse at the touch of a button and the current global landscape makes this more possible.

Figure 55 shows today's current account position for all G20 countries (including EU27 countries) in our sample.