



Metamorphosis into global lender far from completed

At present, the euro area owes the world roughly 10% of its GDP. In other words, foreigners own more European assets than European investors do abroad. In theory, persistent current account surpluses will eventually offset this debt and turn the Eurozone into a net creditor. Once a mature lender, Europe's assets abroad will yield stable investment income on the current account. Interest and dividends will either be reinvested or spent on imports from the borrowing economies, thus being neutral or even bullish for the euro. While current account surpluses would tend to expand foreign wealth indefinitely, offsetting currency appreciation means that NIIPs eventually stabilize.² This is the situation in which Japan found itself during the 1990s, when a conservative BoJ, a large current account surplus and a large Japanese net foreign asset position led to persistent JPY strength.

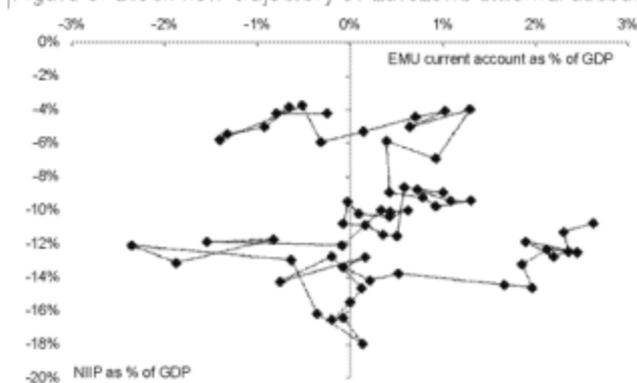
However, in contrast to Japan in the 1990s, the Eurozone is nowhere near the NIIP levels that would be consistent with its new equilibrium saving rate. It will take trillions of Euros worth of further investment outflows as well as significant depreciation over several years for the euro area to accumulate the net foreign wealth position associated with mature creditor economies.

Eurozone only just embarking on transition toward being a net creditor

Traditionally, the G10 universe has been divided into structural surplus and deficit economies. While Anglo-Saxon countries have tended to run current account deficits, Japan, Switzerland, Norway, and Sweden have generated consistent surpluses for decades. As a result of these highly persistent global imbalances, the two camps have accumulated large net international investment positions (NIIP), but with opposite signs.

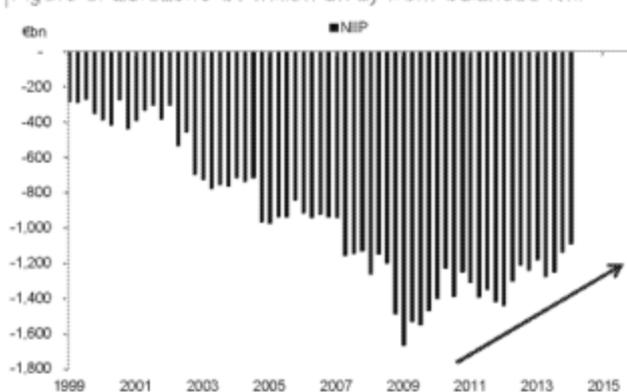
Upon its inception, the Eurozone joined the Anglo-Saxon cluster of net debtors, owing to the external debt positions of its member states. Its NIIP then quickly deteriorated as small and unstable current account surpluses were insufficient to offset negative valuation effects. The Lehman and most importantly the Eurozone crisis marked an inflection point, and the euro area has since run current account surpluses of a greater order of magnitude than during its first decade. Yet, coming from a low base level and still facing valuation headwind, the NIIP has improved only slowly and still stands at only -10% of GDP (Figure 5). Simple arithmetic suggests that this external debt ratio is not consistent with quarterly surpluses of

Figure 5: Stock-flow trajectory of Eurozone external account



Source: Deutsche Bank, ECB

Figure 6: Eurozone €1 trillion away from balanced NIIP



Source: Deutsche Bank, ECB

² In Switzerland, for instance, large and persistent current account surpluses since 1999 have failed to further expand the Swiss NIIP due to valuation losses. See Stoffels et al (2007), "Why Are Switzerland's Assets So Low? The Growing Financial Exposure of a Small Open Economy", Fed Staff Report 283. http://www.fednewyork.org/research/staff_reports/sr283.pdf