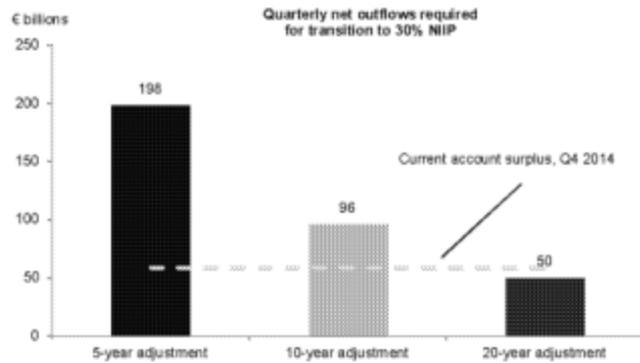


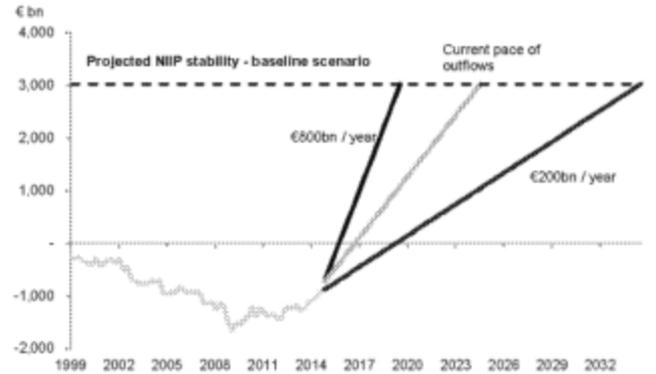


Figure 11: Pace of outflows determines how long adjustment will take



Source: Deutsche Bank

Figure 12: NIIP will not stabilize for years depending on size of Euroglut



Source: Deutsche Bank

these outflows due to its sheer magnitude. Even the speculative FX market would be too small to price this immense shift in Europe's economy ex ante even if participants fully understood the massive implications of Euroglut.

Ultimately, portfolio outflows are likely to exceed the euro area's current account surplus even under extremely conservative assumptions as to the pace of NIIP adjustment. The current pace of portfolio outflows is double the current account surplus, explaining the recent weakness of the Euro. Even if one assumes that the pace of adjustment slows and that it would take a decade for the new NIIP equilibrium to be reached, portfolio outflows would still exceed the current account surplus, maintaining downward pressure on EUR.

## Case Studies of Other Mature Creditor Transitions

### The recent Japanization of South Korea

South Korea provides a particularly relevant and timely precedent for assessing the speed with which Europe will transition towards a 21st-century Japan from a NIIP perspective. The Korean NIIP turned positive only last autumn, for the first time since the data began to be collected in 1994. This coincided with a surge in capital outflows and depreciation resulting from the Bank of Korea's decision to react to Japanese quantitative easing. This was certainly the final push the NIIP required to slide into positive territory (Figure 12). The episode illustrates how responsive capital flows, exchange rates, and ultimately NIIPs are to the Japanization of monetary policy. South Korean outflows over the past six months certainly mirror and anticipate Euroglut.

That said, structural breaks in monetary policy rarely turn perennial debtors into creditor economies overnight. On closer inspection, Korea's transition to a positive NIIP was a structural adjustment spanning almost twenty years (Figure 13). During the Asian financial crisis of 1997, the Korean economy experienced a sudden current account reversal. At the time, Korea's NIIP stood at roughly 10% of GDP, similar to the euro area today. Since then, quarterly current account surpluses have averaged at 3% of GDP. However, despite running persistent surpluses and starting from a moderate level of external debt, it took Korea two decades to become a creditor nation. Moreover, it is far from being a mature creditor economy yet: surpluses are predominantly earned through net exports rather than investment income from foreign assets.