EXECUTIVE SUMMARY

After narrowing sharply in the aftermath of the global financial crisis, overall current account surpluses and deficits reached 3 percent of world GDP in 2018, declining marginally while rotating toward advanced economies in recent years. The IMF's multilateral approach suggests that about 35–45 percent of overall current account surpluses and deficits were deemed excessive in 2018. Higher-than-warranted balances remained centered in the euro area as a whole (driven by Germany and the Netherlands) and in other advanced economies (Korea, Singapore), while lower-than-warranted balances remained concentrated in the United Kingdom, the United States, and some emerging market economies (Argentina, Indonesia). China's external position was assessed to be in line with fundamentals and desirable policies, as its current account surplus narrowed further, although achieving a lasting external rebalancing will require gradual reining in expansionary macroeconomic policies and adopting further structural reforms.

Meanwhile, net creditor positions have continued to increase and, at about 20 percent of global GDP, are at a historical peak—four times the level prevailing in the early 1990s, with net debtor positions reaching a similar magnitude. Short-term financing risks from the current configuration of external imbalances are generally contained, as debtor positions are concentrated in reserve-currency-issuing advanced economies. An intensification of trade tensions or a disorderly Brexit outcome—with further repercussions for global growth and risk aversion—could, however, affect other economies that are highly dependent on foreign demand and external financing. Over the medium term, in absence of corrective policies, trade tensions could become entrenched, and further divergence of external stock positions could trigger costly disruptive adjustments in key debtor economies that could spill over to the rest of the world.

With output near potential in most systemic economies, a well-calibrated macroeconomic and structural policy mix is necessary to support rebalancing. Excess deficit countries (United Kingdom, United States) need to adopt or continue with growth-friendly fiscal consolidation, while excess surplus economies should deploy available fiscal space to boost potential growth and achieve rebalancing (Germany, Korea, Netherlands), including by boosting public infrastructure investment, and avoid overreliance on monetary policy where applicable. Structural policies remain central to tackle external imbalances, but they need to be carefully sequenced and tailored. In general, excess surplus countries should adopt reforms that encourage investment and discourage excessive saving, including by supporting innovation and deregulating certain sectors (Germany, Korea), widening the coverage of social safety nets (Korea, Malaysia, Thailand), and addressing rising and high corporate saving. Excess deficit countries should increase labor market flexibility and improve competitiveness, including by strengthening the skill base of workers (Canada, Indonesia, South Africa, Spain, United Kingdom, United States). In the euro area, where accommodative monetary conditions remain necessary to support the return of area-wide inflation to its objective, higher wage growth in key creditor economies is necessary for rebalancing. Even in some economies where external positions are assessed to be broadly in line with fundamentals, actions are necessary to tackle domestic imbalances and prevent a resurgence of external imbalances through targeted structural reforms, including by reducing barriers to investment and competition in certain sectors (China, Japan).

Exchange rate flexibility remains key to facilitate external adjustment, with limited evidence of this mechanism weakening over time. As highlighted in Chapter 2, varying features of international trade, including dominant currency invoicing and global value chain integration, can alter the mechanisms of external adjustment in the short term, while conventional exchange rate effects on trade flows remain at play in the medium term. Sluggish near-term export responses in some cases—in part reflecting these features of international trade—suggest that exchange rate flexibility may need to be supported with other policies in some cases, including to lessen capacity constraints through improved access to credit and transportation infrastructure, to facilitate external rebalancing. Other country-specific features, including reliance on foreign currency borrowing, need to be considered when designing the overall policy response.

It is imperative that all countries avoid policies that distort trade. Recent trade policy actions are weighing on global trade flows, investment and growth, including through confidence effects and the disruption of global supply chains, with no discernible impact on external imbalances thus far. Instead, surplus and deficit countries alike should work toward reviving liberalization efforts and strengthening the rules-based multilateral trading system that has served the global economy well over the past 75 years.