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FINANCE & ECONOMICS

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America's central bankers are too complacent about the current account

CENTRAL bankers are paid to worry. But top officials at America's Federal Reserve appear quite relaxed about the country's current-account deficit, just as it hits a new record. According to figures released on March 16th, the deficit widened to 6.3% of GDP in the fourth quarter of 2004. To sustain it for a year, America would have to borrow a net \$750 billion.

An odd moment, then, for the Fed to send sanguine signals. But that was the message from speeches by Alan Greenspan, its chairman, and Ben Bernanke, an influential governor, given only days before the latest figures were released. Mr Greenspan's thesis was not new. He has argued before that integrated global capital markets allow the world to transfer its savings to America with much less strain than in the past. But the tone was noticeably more upbeat this time. Rather than emphasising that foreigners might tire of buying American assets, he suggested there was little sign of that. And any eventual adjustment would bring only "modest risk of disruption". In other words, don't worry about a dollar crash.

As Mr Greenspan says, America has so far attracted the capital it needs with relative ease. Net foreign portfolio investment jumped to \$91.5 billion in January, far more than that month's trade gap. Economists at Goldman Sachs reckon that in 2004 America paid interest rates of just 3.25% on foreigners' hoards of Treasury and agency securities. But rates are rising, even as the stock of debt is increasing. Goldman Sachs reckons that servicing foreign-held Treasury, agency and corporate bonds will cost America up to 0.5 percentage points of growth in the coming years.

Mr Bernanke's opinion was bolder. Contrary to popular belief, he argued, the current-account deficit was not primarily "made in the USA". It had less to do with American actions—whether the big budget deficit or low household saving—than with a "global saving glut" created largely by emerging economies. In 1996, he points out, the developing world was a net borrower, running a joint current-account deficit of over \$87 billion. But after a string of financial crises, it became a big net lender. By 2003, the developing world was running a surplus of \$205 billion.

This glut of saving, he points out, must be offset by a dearth elsewhere. In other words, the poor



world's determination to live well within its means has forced America to live well beyond its own. America's current-account deficit, Mr Bernanke argues, is the "tail of the dog."

Innocent of causing the current-account deficit, America's policymakers can also do little to resolve it, Mr Bernanke suggests. He cited a recent Fed study, which reckons that cutting America's budget gap by a dollar would knock less than 20 cents off the trade gap.

This may play well in the White House (no small concern for Mr Bernanke, who is keen to succeed Mr Greenspan when the chairman retires next January). But it downplays America's responsibility for its fate. After all, the two biggest global policy shifts in recent years—the White House's move from budget surplus to deficit and the Federal Reserve's decision to slash short-term interest rates—were both emphatically made in America. Both helped prop up the global economy, but they also aggravated external imbalances.

Mr Bernanke insists that cutting the budget deficit is worth doing for its own sake. His boss, Mr Greenspan, preaches fiscal virtue at every opportunity. But by suggesting that budgetary restraint may not do much to help the current account, Mr Bernanke's logic risks undermining what little enthusiasm Washington's politicians now have for fiscal discipline. Central bankers are paid to worry. Perhaps America's need to worry a little more.

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