Assessment of Feldstein's 'Global Imbalance' [1]

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Abstract

This note is a systematic review of arguments provided by Feldstein (2008) on the necessity for global re-adjustments, both in the U.S. and in main trading partners. The purpose is to address the main arguments in the scientific and political debate on persistent To date, there has been no publication that challenged the opinions leading to totally wrong forecasts concerning the global imbalance. With a perspective of more than 10 years of post-2008-crisis developments, and together with empirical evidence one can easily see how erroneous were the arguments formulated in 2008. The tasks included a systematic review of all arguments formulated by Martin Feldstein in 2008, and casting them against empirical evidence. The U.S. current account (CA) deficit has continued for many years, since 1982, and has not changed, as foreseen by Feldstein. The primary method is a simple comparative analysis, supported by basic macroeconomic data. They allow to reveal multiple processes leading to further deterioration of the U.S. trade balance. Neither savings rate domestically nor abroad adjusted to give a basis for solving the global imbalance. In the same time, all traditional arguments presented on global imbalances seem undeniable. However, an alternative interpretation of the imbalance does not recognize the CA deficit as "a gift to the U.S. economy". This paper sheds new light on the "global imbalance", suggesting that increasing domestic absorption by China may be an important factor in resolving the U.S. problematic and persistent trade deficit. Disaster-scenarios may be not there in the U.S. to experience. Future developments may be far from those announced, and previously expected by Feldstein in his seminal paper. A careful reader may conclude that all coming changes and adjustments will be slow, gradual, and will not cause any major issues in the global economy. Such conclusions seem most justified by hard data and therefore encouraging. As the topic remains central to open economy empirical macroeconomics, continuation of studies on this issue seems natural. The U.S. and China will remain the biggest economies, and, as such, they are central to the global situation.

KEYWORDS: global imbalance, U.S., current account, foreign exchange reserves, the dollar.

Introduction

In the stabilization period after the global financial crisis) economists returned to 'global imbalances' (Obstfeld & Rogoff 2009, Whelan 2010), as a popular topic. There have been a few methods for assessing the imbalance (Bracke, et al. 2008). In general, the term refers to consequences of a specific consumption and saving pattern of American economy. The continuing (massive) deficit in the U.S. trade and current accounts calls for a new approach to its interpretation and analysis. In the traditional approach to balance of payments (BOP) and national accounts, these deficits have been indeed "the most striking features of the current global economy". Global and national institutions responsible for macroeconomic stability focused on the topic (King 2011). No wonder that also distinguished scholars (Feldstein 2008) expressed their deepest worries about the situation they observed, analyzed, and reported to the U.S. Presidents. There were also others, asking a similar question about nature and sustainability of the global imbalance (de Mello & Padoan 2010). It was the IMF explicitly expressing worries about the situation (Blanchard & Milesi-Ferretti 2011).

[1] I thank David Bywaters for very helpful comments. I thank Baktygali Salimgereyev for excellent research assistance. All remaining errors are my own.

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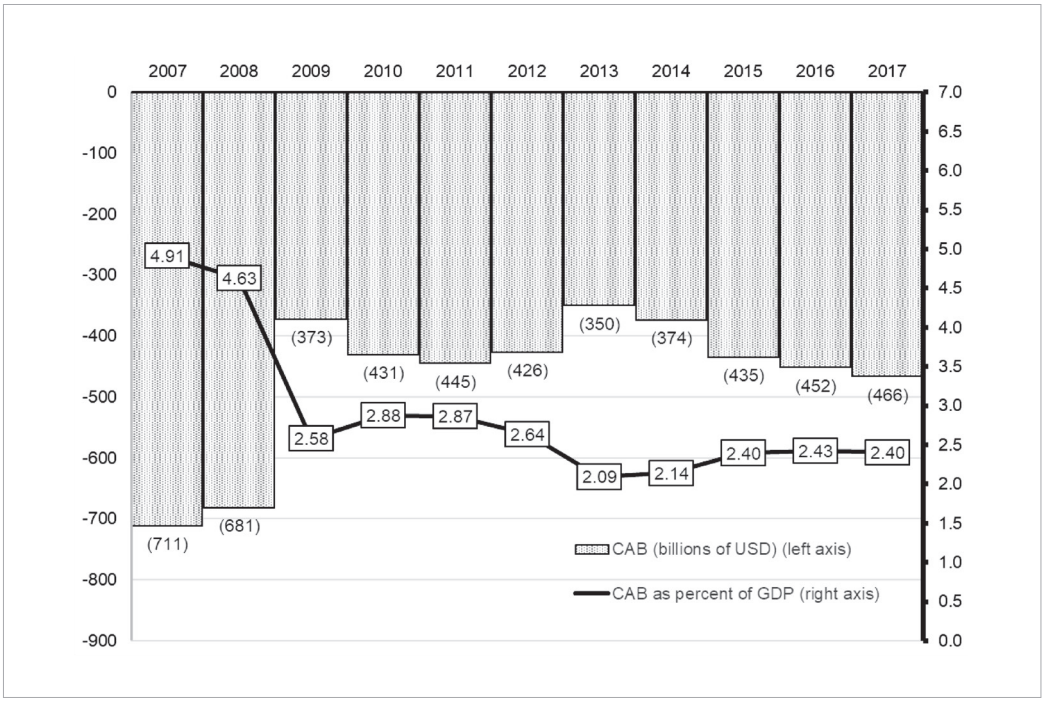
After year 2008, there has been a quite stable current account balance, remaining below 3% of the GDP (Figure 1). The most recent records show that in 2017 the situation remained unchanged.

Some observers claim that the U.S. economy can't continue to have trade deficits of such magnitude. M. Feldstein (2008) was right, forecasting significant decline in CA deficit in the coming years (i.e. after 2007). This paper discusses the reasons a) why the traditional interpretation of the U.S. current account deficit is not valid in these times of globalization, b) why the changes are not needed in the U.S. saving rate, and c) why the value of the dollar may not decline.

Figure 1

Current Account Balance: nominal and as percent of the GDP, 2007-2017 (Author, based on BEA statistics).



When evaluating traditional arguments on global imbalances, one may have an impression that they are all based on the Bretton Woods system still operating. Not only are the fixed exchange rates long gone for most developed countries, but new paradigms for the open economy are there. Nobody conducts devaluations anymore, and the Chinese exchange rate policy is far from the 'beggar-thy-neighbor' cases known from the past.

Liberalization (in the broad sense) has replaced institutional arrangements (i.e. Bretton Woods system, ERM) with market mechanism. For some (see Stiglitz), this situation calls for more active participation by national governments, and for protection, but that is not pursued in this paper. What matters is that the current global situation may have another interpretation. However, the traditional BOP analysis leads to consistent conclusions, based on erroneous assumptions. Previously, institutional arrangements guided international transactions and relationships, and the dollar was the global currency due to political decision. Since 1972 the dollar has served in the same capacity because of market participants' decision. This has had very different consequences for the U.S. economy. More on consequences for small open economy can be found in 'Dominant Currency Paradigm' by Casas, et al. (2017). An alternative interpretation pursued here is based on the diligent application of the fact, rather than institutions and economic policy, that there are market forces in play. Altogether, they invalidate many arguments provided so far on global imbalances and expected rebalancing schemes.

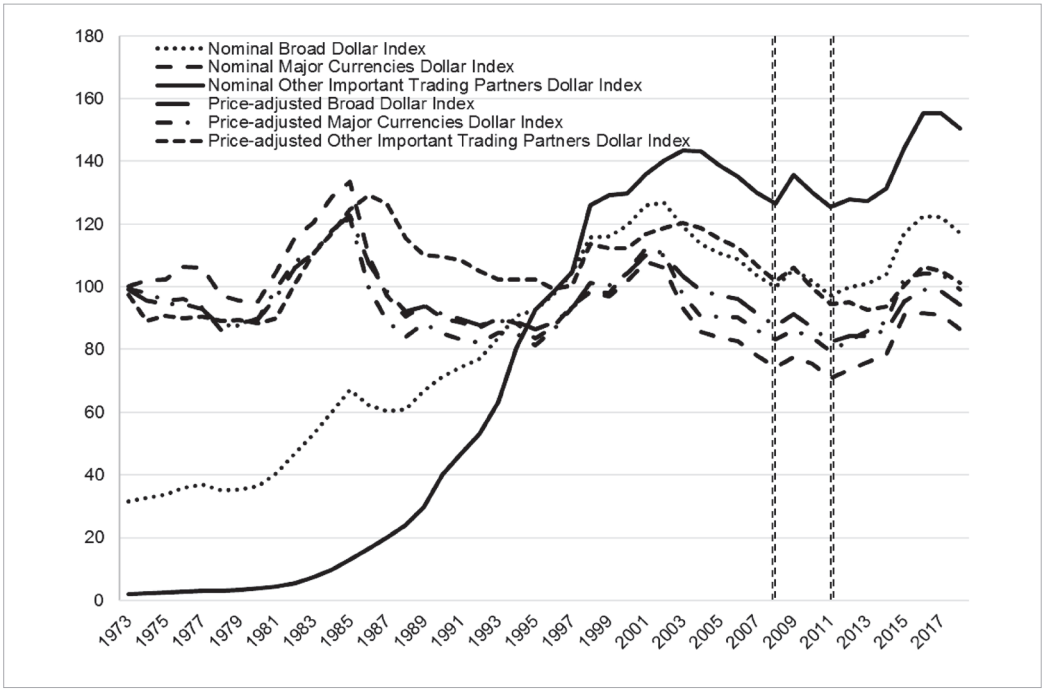


Figure 2
External value of the US dollar 1973-2017 (Author, based on The Federal Reserve, https://www.federalreserve.gov/releases/h10/summary/.).

The main rebalancing scheme expected by Feldstein (2008) was based on a significant decline in the external value of the dollar. Even though there has been significant decline in the U.S. current account deficit since 2008 (from almost 5% of the GDP to 2.75%), this cannot be attributed to the lower value of the dollar. Figure 2 offers a brief review of the external value of the U.S. currency since 1973. There has been a strong positive response to the U.S. political situation in December 2016. This particular factor will receive more attention later, as "making America great again" plays no small part in the sustainability of the otherwise unsustainable imbalance.

When compared with the decade ago (2008-first dotted vertical line), the value of the USD is higher in 2018 no matter which index is used. When compared with early 1990s, the value is basically the same (except for index "Other important trade partners"). Only when compared with its value in 1970s, the dollar does seem to be worth about 8% less. If really the global rebalancing will materialize through depreciation of the dollar, it has not started yet. Its value seems to be quite stable, suffering on average 2% depreciation per one decade over the last four decades. The observed decline in the current account deficit since 2008 has been driven therefore by some other factors and forces omitted by Feldstein (2008). After reaching its lowest value in 2011 (second dotted vertical line), the USD has climbed up, no matter which index is used to capture its external value (Figure 2).

Reductions in the U.S. current account deficit do not necessarily imply lower aggregate trade surpluses in the rest of the world. (Presumably they would, if world trade "balanced", but typically the data showed in 1980s the world had a big deficit with itself, while since 1990 it is about an exponentially growing global trade surplus.) The reason is in changes within the Chinese economy that imply expansion of domestic demand for imported products. Exporters seem to be switching the destination for their products already, supplying consumers in China, and maintaining their respective trade surpluses. At the same time, a reduction in any country's trade surplus does not necessarily reduce aggregated demand. Many, if not most, of 'trade surplus economies' have grown dynamically over the last two decades, or so, with exception for Japan and Germany. What follows is not only a change in consumption patterns, but also an expansion

of the domestic absorption, which develops independently from the U.S. trade policy. There may also be no negative response of employment to these adjustments. The decline of the U.S. deficit (and surplus) may not be so 'inevitable' as claimed by Feldstein (2008).

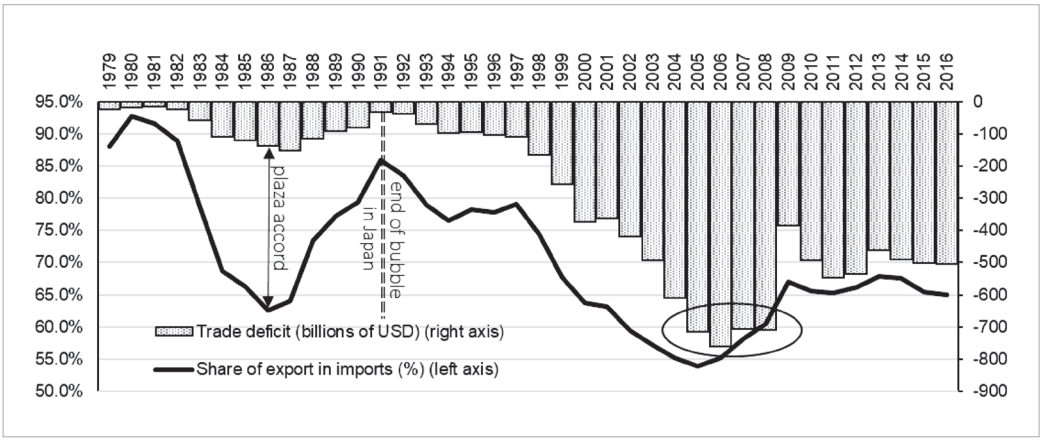
How Can the U.S. Current Account Imbalance Be Sustainable?

It is worth mentioning here that the traditional macroeconomic analysis assumes the level of current account deficit at 5% of GDP, as potentially problematic. de Mello and Padoan (2010) provided some post-crisis scenarios for sustainability using also 5% as a reference. This benchmark was developed on the basis of real life experience of (many) small open economies in the late 20th century. Such systems are, however, very different from the U.S. system with respect to 'sustainability' factors.

Sustainability of the U.S. current account deficit has been driven by several factors. Three of them seem to be crucial. The dollar has been the most important international currency for (1) trade, (2) reserves, and (3) investment. They were, however, neglected by M. Feldstein (2008). There is a recent contribution to this discussion concerned with the dominant currency paradigm by Casas et al. (2017). Studying merchandise trade from 1979, one can see (Figure 3) that U.S. exports have remained low, matching (i.e. financing) no more than 65% of imports in 2017.

Figure 3

U.S. nominal trade deficit, and share of merchandise imports financed by merchandise exports 1979-2017.



In 1980 U.S. exports financed 93% of merchandise imports. The Plaza Accord in mid-1980s seem to be responsible for the rebound, but the end of the bubble economy in Japan in 1991 reversed the trend again for the next 15 years, or so. The following years, until 2006 witnessed indeed a very special, and worrisome, situation with stable deficit oscillating around 700 billion USD in the period 2005-2008. No wonder it motivated many economists to issue warnings and call for rebalancing by the means of economic policy and facilitating market adjustments. Even though the global financial crisis has executed a pressure on the trade deficit, the merchandise trade imbalance since 2011 was back on the same track as in the pre-crisis period. There has also been a quite stable share of imports financed by exports in the most recent period (at 65%). No actual rebalancing can be observed, so far. This has been as if market participants have been not aware of the 'severity' of the global imbalance at hand. So how has the trade deficit been financed since 2008? Exports manage to finance only between 60% and 65% of merchandise imports. (NOTE: there is a difference between a current account balance, and a merchandise trade balance, which is particularly great for a country such as the US which is a successful exporter of services).

"A nation that buys more than it sells must finance the difference by borrowing from the rest of the world or by selling assets." The U.S. economy does it in both available manners, with the former slowly diminishing in significance, and the latter gaining momentum.

The U.S. remains the deepest and the most diversified financial market in the world. This unique feature allows it to finance part of the current account balance by selling financial assets. In particular, these have been equity, along with debt (corporate and public), that have attracted foreign savings. Sale of financial assets continues, as the rest of the world purchases claims on U.S. companies' profits, and becomes owner of entire businesses (prominent examples are: CIT Group, Blackstone, and Ingram Micro that have changed ownership since 2013). Private funds keep coming to the U.S. in a variety of ways, but the expected returns have not been the only reason for that, as observed already by Feldstein (2008). The situation changed dramatically in 2007, following the global financial crisis.

Since 2013 net portfolio investment seems to be significantly reduced, and foreign capital has been no longer provided to the U.S. economy at the previous scale. Since 2015, non-residents have contributed more long-term capital to the U.S. than the U.S. investors exported in the form of FDI, with 2017 witnessing a slight reversal towards the previously observed pattern. This change calls for additional elaboration, as it was unexpected, and unforeseen by M. Feldstein (2008).

There was a unique feature of the U.S. economy over many decades, until 2014. It served as a global financial intermediator. In the real terms, this intermediation utilized a straight scheme. Short-term foreign capital was flowing in (amounts in excess of the current account deficit), and long-term capital was exported from the U.S. Benefits materialized due to the difference in rates of return. Short-term (i.e. portfolio) investment in the U.S., as the more liquid one (i.e. less risky), paid lower rate of return to foreign investors taking long positions in dollar-denominated financial instruments. Net portfolio investment in the U.S. used to be positive (Figure 4). In the same time, the U.S. economy exported long-term capital, receiving a rate of return in excess of the rate paid on the short-term liabilities (positive net portfolio investment).

Flows of long-term capital (i.e. direct investment) used to be negative (Figure 4: until 2014). This indicated an outflow of long-term capital. Such a situation generated substantial benefits for the

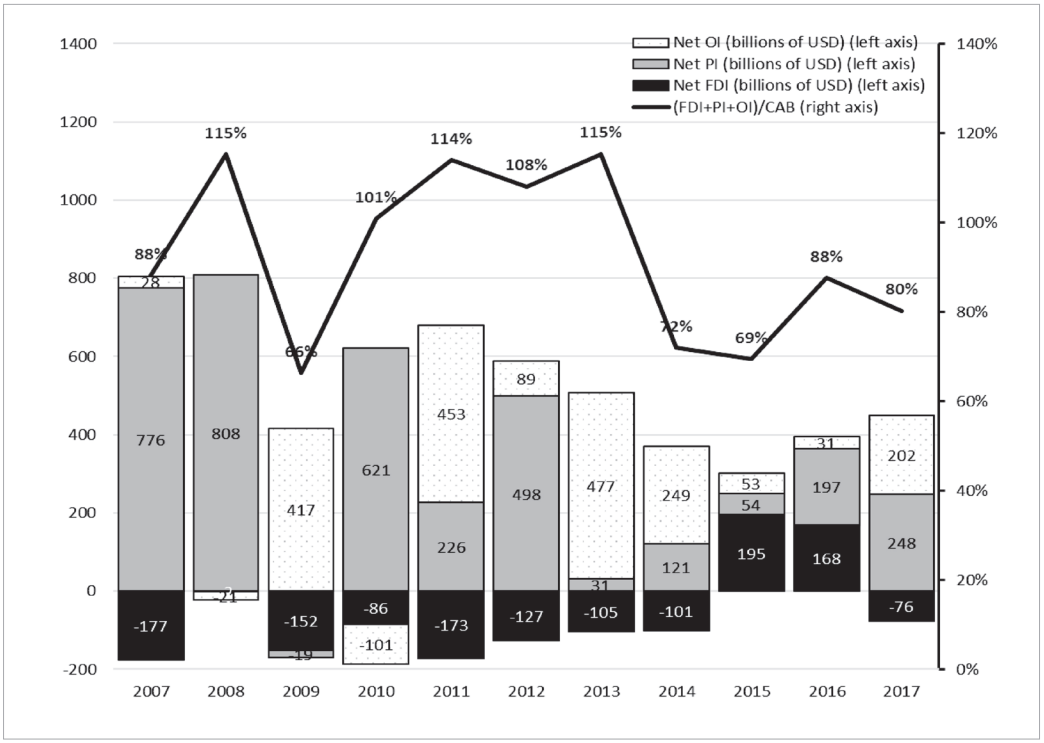


Figure 4

Capital flows: current account balance (CAB), net portfolio investment (PI), FDI, and other investment (OI) and their total as a share of the current account deficit, 2007-2017 (Author, based on the U.S. International Transactions Accounts Data from the BEA.).

U.S. economy due to financial intermediation. America benefited because the rate of return on long term capital invested outside U.S. was greater than the cost of short-term capital that was provided by other countries in the first place. Borrowing at a low rate (from other countries), and providing financing at a higher rate (to other countries), along with transformation of the nominal (from multiple small deposits to few big loans), and the term (from short to long-term financing) belong to the very nature of every banker.

There has been a similar scheme in the case of the UK, but not in any other country or region. For example, financial flows within the EU, and debtor-creditor positions are of a very different nature. They are also motivated by totally different considerations than in case of the U.S., as argued by Daugeliene and Młodkowski (2014).

The composition of portfolio investment (equity versus debt) may suggest the actual beneficiary of financial instruments purchased in the U.S. It was claimed by Feldstein (2008) that main U.S. trade partners' governments accumulate foreign exchange reserves to maintain competitiveness and "sustain [...] export surpluses". Such interpretation seems to fit perfectly in the environment, where 'beggar-thy-neighbor' policy is the everyday practice. However, the actual motivation for governments to buy and maintain large foreign exchange reserves denominated in the dollar may be much more complex (Eichengreen et al. 2017).

According to an investigation by Du, Im, and Schreger (2018) into changes in preferences of investors for U.S. Treasury bonds, there seems to be some empirical support for arguments formulated by Feldstein (2008). Traditionally, investors preferred U.S. T-bonds over instruments issued by other 'nearly default-free' governments. For decades, these preferences reduced borrowing costs for the U.S. federal government. Du, Im, and Schreger (2018) report disappearance of 'specialness' of medium- and long-term U.S. government bonds. This change occurred after the global financial crisis, and a new situation has continued since. It could be concluded that except for short-term T-bills, "investors, both public and private, [became] less willing to keep adding dollar bonds to their portfolios", as foreseen by Feldstein (2008). However, among reasons that may be responsible for this new situation Du, Im, and Schreger (2018) do not list portfolio adjustments resulting from the fear of loss resulting from a decline in the value of the U.S. dollar.

The situation presented in Figure 5 with negative net equity investment in the U.S. in 2013, 2015, and 2016 indicates a significant change in private investors' decisions. Following the 'foreign investors type recognition' method (by Feldstein 2008) one can conclude that foreign governments, which are supposed to invest in debt instruments, reduced then the pace of accumulating USD-denominated assets. Since 2013, private savings have been divested from the U.S., and foreign governments have been adding foreign exchange reserves in USD-denominated assets much more slowly. If these trends continue, the scenarios formulated by Feldstein may really materialize.

The most recent records of foreign exchange reserves holdings reveal a substantial expansion in all of them, except for Russia and China (Figure 6). There has, indeed, been a staggering surge in the total value of Chinese foreign exchange reserves from 2008 to 2014 but reserves maintained in 2018 are already below the 4 trillion reached in the preceding years. Russia and China reduced their holdings of foreign exchange reserves in the most recent period, which is reflected in a decline of net debt investment in the U.S (Figure 5). If other main reserve-holders follow the same path, then the depreciation of the dollar foreseen by Feldstein (2008) may indeed materialize. On top of that, changes in the level and composition of foreign exchange reserves holdings may also affect global interest rates, as discussed by Młodkowski (2011). The global economy seems to suffer from excessive liquidity. Alterations of demand for particular currencies, while portfolio composition is rearranged, may have local, or even regional, impact on the cost of capital for private and public sectors alike.

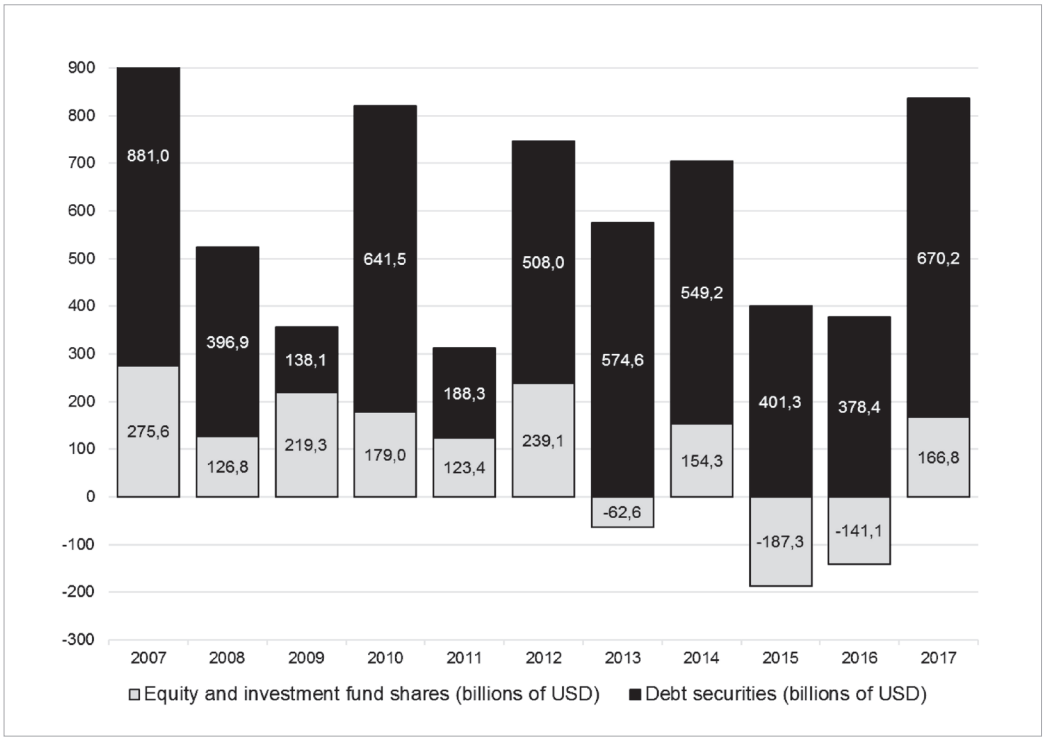


Figure 5

Composition of net portfolio investment in the USA, debt versus equity, 2007-2017 (Author, based on the U.S. International Transactions Accounts Data from the BEA.).

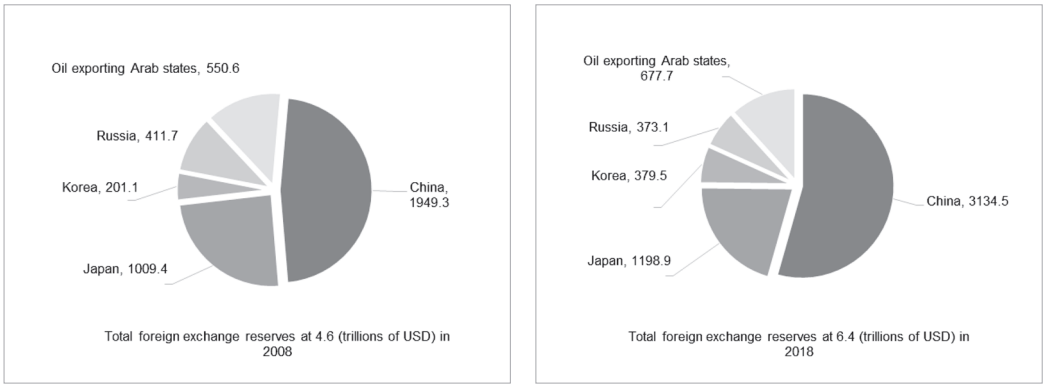


Figure 6

Foreign exchange reserves of China, Japan, Russia, South Korea, and oil-producing countries, in 2008 and 2018 (Author, based on COFER, by the IMF, World Bank.).

After accumulating sufficient foreign exchange reserves to discourage speculative attacks on currencies managed under hard pegs (conventional pegs in 2012: 43 and in 2017: 44, according to AREAER, by IMF 2018) may be a reason for the lower demand for the dollar. Empirical evidence available in 2018 undermines the 'satiation' argument formulated by Feldstein (2008, p. 118). Both South Korea, and Taiwan significantly increased their respective foreign exchange reserves holdings over the last decade, both in nominal and relative terms. South Korea moved from 201 to 379 billion – by 94%, while Taiwan from 189 to 314 billion – by 66%)[2]. Precautionary demand for USD, as the main reserve currency in 2008 seems to be understated by Feldstein (2008). Observing Japan increasing its foreign exchange reserve holdings by about 20% over the last decade indicates that it might be associated with "stimulating trade surplus". However, the recent

[2] South Korea: https://fred.stlouisfed.org/series/TRESEGKRM052N,
Taiwan: https://fred.stlouisfed.org/series/TRESEGTWM194N

substantial decline in Chinese foreign exchange reserves holdings from 4 to 3 trillion, does not fit with the "stimulating trade surplus" narrative. Indeed, the Chinese economy seems to have diverted from perpetual IOUs, and started managing its trade surplus in a new manner.

In summary, the large trade and current account deficits of the United States still continue, but at a significantly lower scale than around 2008. The U.S. economy no longer receives "a permanent gift". Instead, it provides real assets to foreign investors. Non-residents acquire ownership of U.S. enterprises and real estate. This is a process that causes U.S. citizens' property to shrink. The dollar will not fall, because private investors are willing to increase their holdings of U.S.-based property. According to the Research Division of National Association of Realtors (NAR 2017), foreigners increased their spending on real estate in the U.S. 2.5 times, between 2011 ($66.4 billion) and 2017 ($153.9 billion). The increased demand for ownership in the U.S. may trigger another asset-bubble in the financial and real estate markets. Therefore, one may claim that fall of the dollar has started already, but domestically, due to inflation.

Role of national savings

The national saving rate in the U.S. has been historically low (Table 1). When domestic absorption in relation to domestic production results in a small surplus only, it does not allow for investment in business equipment, housing, and other structures. It also makes exporting the surplus to other countries not an option. This is all about just another national accounting identity that implies that the difference between savings and investment be matched by trade balance. The permanent trade deficit means negative net domestic savings.

Table 1

Gross national saving rate in the US and China as % of GNI (GDP for China) 2007-2017.

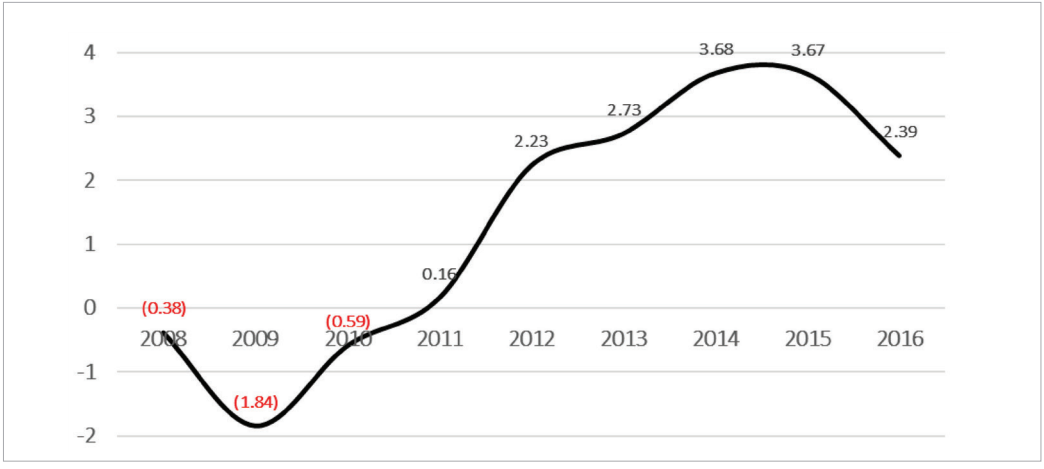
Source: Author, based on Economic Report of the President, 2017 (for U.S. data), and World Economic Outlook Database (for China).

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
USA		15.5%	14.4%	15.1%	15.6%	17.5%	18.1%	19.0%	18.9%	17.7%	
China	51%	52%	51%	52%	50%	50%	49%	49%	47%	46%	46%

Feldstein (2008, p. 118-119) claimed that low national saving is the "fundamental cause" of the global imbalance addressed here. National savings are the sum of three elements: (1) household savings, (2) retained earnings, and (3) government budget balance. Although the U.S. government deficit was not considered problematic at 1.5% of the GDP in 2008, it is its nominal, not relative (to GDP) size that matters for the global imbalance. It was Feldstein (2008) who had already foreseen two developments in regard to U.S. national saving. In general, he expected the saving rate to increase.

Figure 7

Net private savings rate in the U.S. as a percentage of the GNI, 2008-2016 (Author, based on World Development Indicators by the World Bank.).



This has already materialized since 2010 (Figure 7, and Table 1). The other correct expectation was "the government deficit (...) potentially heading for trouble in the next decade". Indeed, it was 2009, when the general government deficit hit almost 13% of the GDP, and continued as a double-digit for three years (Figure 8). However, the reasons seemed very different from what Feldstein (2008, p. 119) explained. Public savings, although still negative, seem to be under control, stable, at around 5% of GDP since 2013 (Figure 8). There will probably be a change after the recent US tax cuts. Straight return to double-digit percent of GDP deficit, may not be there, however, due to acclaimed 2018-economic recovery.

Why did private savings, after a 5-year period (2010-2014) of growth start to decline? The most recent developments in residential construction may shed some light on possible reasons. Data reported for 2017 (Table 2) indicate that the U.S. economy is on a similar track, as in the pre-2008 period.

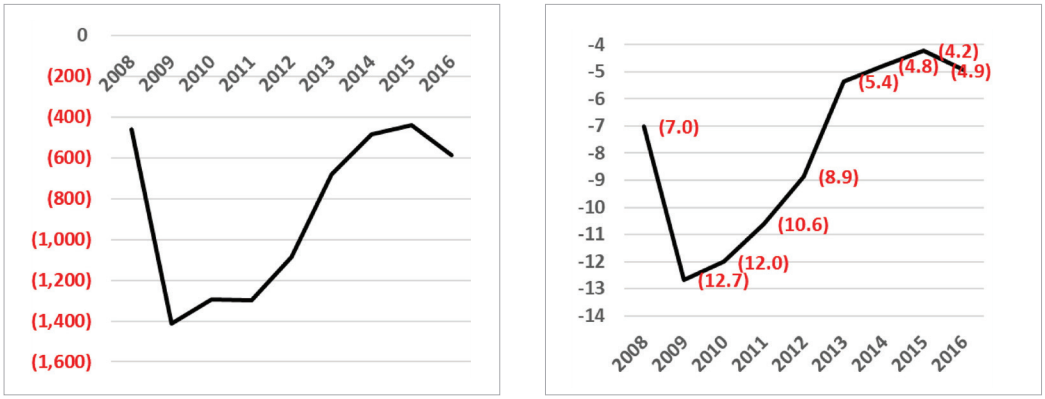


Figure 8

Nominal federal government deficit, and general government deficit, as % of GDP (Author, based on Federal Reserve Economic Data (left chart), OECD database (right chart).).

The new trend in construction industry (Table 2), after 2011's low, suggests that the trade deficit will receive no longer any support from lower residential investment domestically. Rising prices of real estate, reported in 2017 and 2018 (NAR, 2018) have led to another rapid rise in household wealth. One can already observe growing level of mortgage refinancing with equity withdrawal, after substantial reversal in this regard in the preceding decade.

Housing starts	1,202,100 units	Up 2.4% from a year earlier
Housing completions	1,152,300 units	Up 8.7% from a year earlier
Housing permits	1,263,400 units	Up 4.6% from a year earlier

Table 2

U.S. housing market statistics for 2017.

Source: Author, based on National Association of Realtors (NAR).

It seems that a poor-performance-decade is also over for stock markets. The stock prices are also likely to outperform earnings in the future, in the way that they had been doing so before 2008.

The reducing trade deficit has not been supported by higher spending on American-made goods and services, domestically and abroad (Table 3). There are many reasons for that. While Feldstein

	IBT	FAFH	EE	ER
Income before taxes (IBT)	1			
Food away from home (FAFH)	0.353	1		
Entertainment expenditure (EE)	0.55	-	1	
Exchange rate - annual average (ER)	-0.26	0.57	0.351	1

Table 3

Correlation coefficients between nominal exchange rate, income and domestic consumption spending categories 2006-2017.

Source: Author

(2008, p. 120) addressed only relative prices, one should also point out quality. This is another, even more important factor. There is much stronger environmental consciousness outside U.S. that drives consumer behavior. This is supported nowadays by strong tax-incentives for using fuel-efficient and eco-friendly solutions outside the US. EU and Japan are good examples here. The decline of the dollar relative to the euro, the yen, and other currencies (although not witnessed so far) does not seem to be sufficient for other countries to increase consumption of U.S. products. There are some American products that still compete in global markets with Japanese, and European. Even as the dollar declines, the U.S. products will not become really more attractive to buyers at home and abroad, due to other factors that drive consumer decisions these days. A good example could be the Persian Gulf region, where consumers prefer Japanese (personal vehicles), and European (heavy trucks: Renault, MAN, Mercedes) products over American ones. The reasons are in reliability and higher efficiency of the former two, and not the relative price.

One could find few of "making America great again" themes already in Feldstein's (2008) suggested rebalancing scheme. This is mainly about promoting a change in domestic consumer behavior. In particular, it was about switching consumption from imported products to made-in-U.S. After a decade, or so, one can conclude that this scenario has still not materialized, in spite of intensive propaganda, since 2016, and protectionist trade policy by the current administration in 2018.

According to the correlation coefficients reported in Table 3, American consumers respond positively to exchange rate appreciation, expanding their spending on domestically-produced goods & services. Appreciation of the dollar seems to have a much stronger positive impact on decisions to buy food away from home than in the case of entertainment spending. The response of the same categories of non-tradables to changes in income is somehow symmetrically reversed in terms of magnitude.

So if it has been not the declining dollar that led to reducing the trade imbalance, what has been the reason(s)? Feldstein (2008) saw his balancing scheme via the decline in the external value of the dollar, and kept repeating it like a mantra throughout his paper. Real life developments have led to adjustments in very different ways, while the dollar has appreciated, since 2011 (Figure 2).

Why has the dollar not declined relative to the euro, and why has it hardly declined at all relative to the Japanese yen, and the Chinese yuan? Feldstein (2008, p. 122) pointed out devaluation expectations, but did not address how these expectations are formed. Another argument dealt with the positive difference between interest rates on euro bonds and dollar-denominated bonds. Actually, the latter issue has disappeared for mid-term and long-term bonds, as reported by Du, Im, Schreger (2018). Even with these positive rate differentials disappearing, the fall of the dollar is nowhere to be seen. Forming expectations according to the misleading statements of the U.S. government, and international financial institutions, does not seem to be really the case in the world of efficient (foreign exchange) markets. Although the two biggest foreign exchange reserve owners (China and Japan) still maintain substantial dollar holdings, the last decade (2008-2018) witnessed a sharp appreciation (2008: 1 USD = 110 JPY and 2013: 1 USD = 78 JPY) and then depreciation (2015: 1 USD = 125 JPY and 2018: 1 USD = 110 JPY) of the yen that can hardly be attributed to observed developments in foreign exchange reserve holdings. Somehow, this has still not resulted in the foreseen decline of the dollar.

Resolving global imbalance

The actual rebalancing scheme has been observed in the latter half of the previous decade. It has been far from what Feldstein (2008) advised, and foresaw. He postulated a substantial reduction in the external value of the dollar. In such a scenario, all foreign holders of greenbacks would suffer a substantial loss. Benefits would be there only for the U.S. As fiat money is really debt, depreciation would mean that for many decades the debt was created in a strong currency, but

when it comes to repayment, the debtor calls for reducing the real value (i.e. purchasing power) of the liability to-be-repaid. Accumulation of trade-induced debt in strong currency allowed U.S to purchase cheaply from the rest of the world, with all its consequences, benefiting the domestic economy. However, when the time came to repay the debt, Feldstein (2008) postulated a scheme that would ease the pain of giving up equivalent in other assets, by a substantial reduction in the real value of the liability.

If it really comes to substantial decline of the dollar, it will result in wealth transfer at the global scale. Wealth transfer that is addressed here is both international, and intergenerational.

It should not be denied that there has been enormous effort invested in developing production by emerging economies. Their rapid growth came at a cost of sacrificing contemporary consumption for the purpose of accumulating capital. It has been motivated by expectations of improved living standards, and expanded consumption in the future. Hard and diligent work, along with saving a substantial fraction of income may, however, become the most disappointing virtues in the developing world. Such demoralizing scenario depends critically on the actual decline of the dollar, if it really materializes.

The global imbalance has been in fact an inter-temporal imbalance of consumption. The U.S. economy has already been consuming in excess of its contribution to the global GDP for about 40 years. Such a comfortable situation has been made possible only due to decision of the rest of the world to consume less 'today', and receive a promise to have higher consumption in the future. Pieces of empirical evidence presented here suggest that this 'future' is now. The U.S. economy has offered real and financial assets to foreigners at the unprecedented scale. The official foreign exchange reserves have greatly declined already in China, suggesting the nationality of most of the foreign homeowners in the U.S. This particular expansion of Chinese-owned property even caused the Chinese monetary authority to introduce semi-restrictions on foreign exchange available to citizens investing abroad.

The decline of the dollar is neither required nor necessary to solve the global imbalance. The rest of the world has claimed U.S.-based assets exchanging perpetual IOUs for real estate and firms. Foreigners have become, sole owners of underlying real U.S. assets (as owners of firms), and not only, as it was before, of shares in profits generated by U.S. corporations.

Dynamically growing demand has already pushed prices of both up. This inflow of purchasing power should be appreciated, as it fuels activity in the U.S. construction sector, and thus indirectly in all other sectors that supply materials and technologies to homebuilders.

U.S. economy enjoys win-win situation, while the global imbalance has been gradually resolved. Appreciation of the dollar makes imported inputs cheaper every year, since 2011. On the top of that, most welcome form of foreign investment – FDI – has become positive (net FDI) already in 2015 and 2016 for the first time in history. Most recently observed adjustments in savings in U.S. and the rest of the world (Figure 9, Figure 8, Figure 7, Table 1) make the situation much less dramatic than it was reported back in 2008. The U.S. economy has still provided a reasonable equivalent for its external debt accumulated over the past several decades. There seem to be no reasons to sound an alarm, and issue warnings on 'greater instability' coming, when increasingly large imbalances are resolved. The last decade witnessed substantial changes to income, domestic absorption, and production in all countries that effectively matter for the global imbalance. It seems that time has come for the U.S. to finally start settling its debts. This has been achieved without the international 'transfer' of wealth that would deprive many nations of the fruits of their hard work. It would be most inappropriate to induce the fall of the dollar to ease the pain of settling accumulated external debt. Such a scenario would make sacrifices of hun-

dreds of millions, due to postponed consumption for a few generations most void, pointless, and disappointing. The only potentially negative effect might be in a relative fall of living standards in the U.S. because of purchase of 'better' U.S. assets by the rest of the world. However, this does not seem to represent any real problem.

Empirical evidence available in mid-2018 suggests that claims on ways to solve global imbalance found in Feldstein (2008) were erroneous. In particular, (p. 124) it was not 'a more competitive dollar' that was the key to shrinking the trade deficit (after 2009), although this idea was supported by 'most professional economists'. This was, therefore rather about the approach pursued by the IMF, and G-7, and criticized by Feldstein that was much more appropriate. Slow and gradual adjustments in U.S., and in the rest of the world have led to stabilizing CA deficit at 2.5% of GDP for already an extensive period 2009-2017. The stability of the current situation, in spite of significant political developments, suggests that the world could be safe again.

The U.S. economy is a double (if not triple) winner. For decades it enjoyed paying for its excessive consumption with perpetual IOUs. Settlement of the accumulated debt is achieved, however, not by the foreseen reduction in consumption, as originally understood. The U.S. economy provides real assets to foreigners in the primary, and secondary, real estate market. Insights into the revealed intentions of foreign buyers (NAR, 2018) indicate that the U.S. economy will receive benefits from the surge in incoming skilled workforce in the future, as today's house owners move to the U.S. with their families. Until then, there will still be another issue to-be-handled by U.S. authorities. In the current situation there are large injections of high-power money. This special expansion in the money supply will not remain neutral for the price level.

Repatriation of substantial purchasing power to the U.S. has a great potential for fueling inflation, and not only in the real estate market. The provision of additional high-power money to settle transactions in any domestic market by foreigners delivers real cash for all other domestic transactions. The more inflated prices of the initial assets acquired, the more money supply expands. With the supply of other goods lagging behind, purchasing power of the dollar must adjust downwards. Mid-2018 reported a takeoff of the CPI, and the FED's response, seems to fit this narrative perfectly.

There has been more migration of purchasing power in the global economy than just the return to the U.S. Countries that accumulated dollar-denominated reserves expand in a variety of directions. The U.S. remains the main destination due to the biggest capacity to absorb this spending. However, further analysis seems most desirable with investigation into the nature of non-U.S. destinations of FDI originating from trade-surplus economies. The real issue concerns the effects that differential GDP growth rates, and their associated savings rates, have on trade and exchange rates.

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