

Slawomir I. Bukowski*

GERMANY, JAPAN AND INTERNATIONAL PAYMENT IMBALANCES

Abstract

International payment imbalances are usually discussed in the context of the U.S. – China relations. However, it is worth noticing that apart from China also Germany and Japan and many other countries (mainly raw-material exporters, such as Russia, Saudi Arabia, etc.) belong to surplus countries. Germany and Japan are characterized by specific features among which high international competitiveness in comparison to other countries prevails. It is their competitiveness that accounts for their success and their vital role in international payment imbalances both in the EU and globally.

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Introduction

International payment imbalances are one of the crucial problems in modern global economy.

K. Lutkowski writes about payment imbalances in the USA – East Asia – Europe triangle. According to him it is „a kind of triangle whose sides stand for the directions of the largest capital and trade flows in the world” (Lutkowski 2006, p. 425). Usually this phenomenon is discussed in the context of relationships between the United States and China. It must be noted, however, that payment imbalances appear also in the relationships between Germany and the United States, and Germany and the majority of the EU countries (including the euro area), as well as between Japan and the United States, and Japan and the EU countries.

* Prof., Ph.D., The Department of International Business & Finance, Kazimierz Pulaski University of Technology and Humanities in Radom, s.bukowski@pr.radom.pl

In view of the above said a question can be posed about the causes of international payment imbalances in the relationships between Germany and Japan on the one hand and the United States and the majority of the EU countries on the other.

Concept and causes of international payment imbalances

International payment imbalance indicates a long-term current account imbalance and possibly the balance of payments imbalance (the positive balance of official reserves) between a given country (region) and other countries (regions).

The literature on the subject offers numerous hypotheses accounting for the causes and mechanism of international payment imbalances in the relationships between the United States – Asian countries – EU countries. The ones which deserve a mention are: the „Bretton Woods II” hypothesis, the global savings glut hypothesis, the global investment drought hypothesis, the negative US savings rate hypothesis, the Asian 1990s crisis effect hypothesis, the hypothesis of shocks affecting relative investment attractiveness of economic areas, the hypothesis of the optimal level of the current account deficit in the intertemporal approach, the hypothesis of changes in the asset and liability valuations and differences in return rates, and theories questioning correctness of imbalance measurements. A paper by K. Rybiński contains a very good overview of these hypotheses and theories and their critical analysis (Rybiński 2006). Discussing them here does not seem justified as this has already been done by the quoted author. The critical analysis of the international payment imbalance hypotheses and theories can also be found in K. Lutkowski’s paper (Lutkowski, 2006, p. 448).

Among the causes of international payment imbalances the following are listed: on the one hand – low savings and high levels of consumption in the United States; on the other hand – low domestic absorption and low consumption levels at growing savings in China and other East Asian countries as well as poorly developed financial markets in the latter making investment of amassed savings difficult. Consequently, on the one hand we deal with growing US current account deficit, on the other hand – with the inflow of capital in the form of portfolio investments (mainly in American treasury bonds, but also in shares of American companies) and direct investments in the United States. In the literature on the subject one can easily find opinions that „Capital does not flow to the United States because it is „sucked in” there by some kind of lack of savings (because to put the record straight, there is no such lack), but it is directed there because it is attracted by the advantages of that place” (Lutkowski 2006, p. 449). American economy is particularly attractive for investors from Asian and oil countries and partly for some European countries on account of its specific qualities: high competitiveness, economic freedom, spirit of entrepreneurship, protection of the right of ownership,

high development of technology, labor mobility, market flexibility and relatively dynamic economic growth as for a highly developed country. All these account also for the credibility of the American dollar despite its exchange rate fluctuations in the last decade. It is also important that the American debt is entirely denominated in dollars. Approximately 80% of official foreign exchange reserves of central banks worldwide are also kept in dollars (Lutkowski 2006, p. 425).

On the other hand, in the European Union we deal with the division into countries indicating a current account surplus and those indicating a current account deficit. The main surplus country is Germany, a country where the current account surplus in transactions with the rest of the world, including also the EU countries, has been maintained with some short intervals since the so called „economic miracle” of the 1960s. It seems that the key to the explanation of this phenomenon is a relatively high rate of domestic savings in comparison to other highly developed countries as well as high international competitiveness of German economy. A relatively high fiscal discipline should be added to all the previously mentioned factors.

The high level of international competitiveness appears to be one of the crucial factors in achieving a long-term surplus in the current account by Japan. Another crucial factor is also a tendency for saving and a relatively lower than in other countries consumption and demand for imports.

Position of Germany and Japan, as surplus countries, in world economy

For many years, Germany has indicated a current account surplus in transactions with the rest of the world and EU-27 countries. A similar situation has been noted in Japan (see: Table 1, Fig. 1).

Within the framework of the European Union Germany holds a position of a surplus country, like Austria, the Netherlands, Finland and Sweden. The main reason for this is the high international competitiveness of these countries' economies and their exports. This refers in particular to Germany. In the Global Competitiveness Report 2010-2011, Germany is ranked 5th for its international competitiveness, just behind Switzerland, Sweden, Singapore and the United States and ahead of such countries as Finland, the Netherlands, Denmark and Austria (the latter is ranked 18th)¹. The factors that contribute to this are a relatively high position in economic freedom ratings (at 23rd position)², relatively stable economy and economic policy and, in particular, a relatively high level of fiscal discipline.

¹ See: Global Competitiveness Report 2010-2011, Klaus Schwab, World Economic Forum, Geneva Switzerland 2010.

² See: www.heritage.org/index/ranking.

Table 1. Balance of the EU, US and Japan's current account with the rest of the world in the years 1999-2009 (millions, EUR)

Country/year	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Belgium	:	:	:	12430	19670	19059	7854	6318	5427	-6539	2858
Bulgaria	-619	-757	-1106	-928	-1504	-1310	-2705	-4647	-7756	-8191	-3477
Czech Republic	-1378	-2961	-3654	-4442	-5028	-4650	-1345	-2745	-4090	-962	-1465
Denmark	3123	2443	5609	4590	6500	5939	9008	6515	3093	6194	7929
Germany	-25176	-35235	425	42972	40918	102832	114630	150106	185137	166963	117263
Estonia	-230	-325	-376	-760	-986	-1095	-1115	-2053	-2721	-1568	628
Ireland	573	52	-756	-1295	-2	-867	-5690	-6304	-10124	-10169	-4853
Greece	-4801	-10624	-10580	-10201	-11266	-10718	-14744	-23748	-32577	-34798	-25814
Spain	-16965	-24948	-26823	-23765	-27476	-44164	-66861	-88313	-105267	-105973	-58298
France	35309	17702	25702	15353	7013	8940	-8325	-10345	-18913	-37117	-36790
Italy	7694	-6345	-713	-10041	-17337	-13036	-23639	-38336	-37713	-46001	-31678
Cyprus	-159	-535	-351	-418	-266	-635	-800	-1006	-1865	-2974	-1279
Latvia	-608	-412	-707	-653	-814	-1439	-1626	-3603	-4710	-3014	1598
Lithuania	-1127	-738	-640	-772	-1116	-1393	-1482	-2551	-4149	-4227	1128
Luxembourg	:	:	:	2526	2103	3255	3495	3516	3784	2087	2549
Hungary	-3532	-4353	-3568	-4923	-5936	-6832	-6378	-6829	-6965	-7747	-404
Malta	-118	-533	-165	108	-138	-269	-421	-472	-304	-328	-399
Netherlands	14664	7844	10911	11582	26153	36917	37275	50436	38427	25371	26156
Austria	-3325	-1530	-1754	5871	3776	4842	4916	7105	9619	13757	7976
Poland	-14334	-11189	-6642	-5919	-4880	-8165	-3020	-7443	-14701	-17399	-6752
Portugal	-9665	-13167	-13879	-11574	-9230	-12432	-15924	-17186	-17075	-21699	-17261
Romania	-1352	-1497	-2491	-1618	-2877	-5102	-6876	-10220	-16758	-16178	-4933
Slovenia	-661	-579	38	250	-195	-717	-498	-772	-1646	-2490	-526
Slovakia	-1084	-763	-1951	-2052	-249	-1156	-3242	-3636	-2912	-4279	-2023
Finland	7638	10723	11983	12692	7511	9969	5697	7553	7650	5375	4696
Sweden	10054	10719	10826	13140	19801	21091	20430	26478	28859	29361	21848
UK	-33099	-42399	-34065	-29667	-26162	-36941	-48017	-64350	-55276	-27219	-26944
Belgium-Luxembourg	18142	18341	16939	:	:	:	:	:	:	:	:
United States	-283817	-453949	-443885	-483253	-460791	-507011	-603703	-638720	-525462	-454811	-270599
Japan	107591	129222	97842	119978	120335	138546	133259	136007	154040	105120	101560
All countries of the world	-94133	-165107	-168349	-104216	-19010	41745	69390	189738	271022	210276	224507

Source: compiled by the author on the basis of the EUROSTAT data

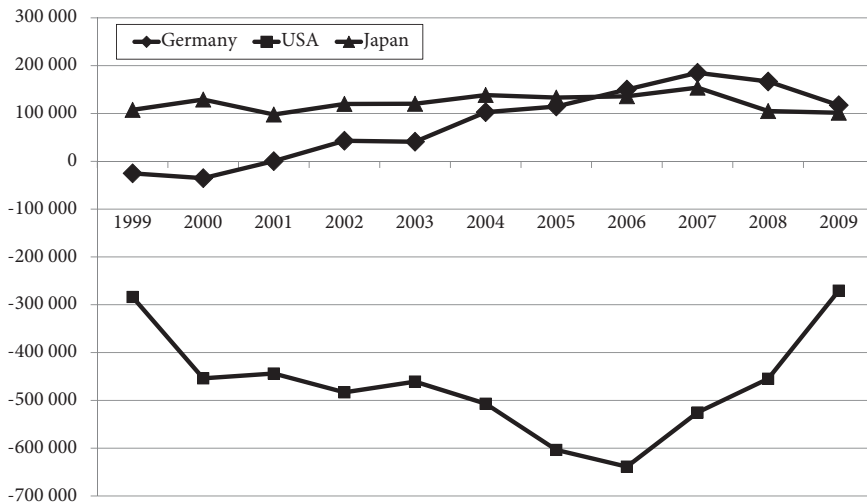


Fig. 1. Current account balance for Germany, US and Japan with the rest of the world in the years 1999-2009 (millions, EUR)

Source: compiled by the author on the basis of data included in Table 1.

German economy is also characterized by a high level of innovation, which is reflected in the share of high-tech goods in exports (See: Table 2).

Table 2. Exports of high – tech products in EU countries and top EU trade partners – share of global high-tech product exports in the years 2007-2008 (SITC, including exports within the EU) (%)

Country/year	2007	2008
Belgium	1.406	1.549
Bulgaria	0.032	0.039
Czech Republic	0.852	1.003
Denmark	0.593	0.605
Germany	8.445	8.689
Estonia	0.042	0.045
Ireland	1.539	1.475
Greece	0.055	0.072
Spain	0.528	0.566
France	4.229	4.753
Italy	1.476	1.546
Cyprus	0.010	0.015
Latvia	0.019	0.023

Table 2. Cont'd

Country/year	2007	2008
Lithuania	0.062	0.074
Luxembourg	0.357	0.431
Italy	1.003	1.061
Malta	0.072	0.063
Netherlands	4.954	4.980
Austria	0.895	0.949
Poland	0.210	0.352
Portugal	0.165	0.165
Romania	0.070	0.129
Slovenia	0.068	0.086
Slovakia	0.144	0.166
Finland	0.776	0.807
Sweden	1.151	1.199
UK	3.495	3.356
Norway	0.220	0.282
Switzerland	1.706	2.012
Russia	0.213	0.264
Canada	1.547	1.463
United States	11.640	12.047
Mexico	1.627	2.082
Brazil	0.468	0.256
China (excluding Hong Kong)	16.859	18.367
Hong Kong	6.067	6.914
Japan	6.315	6.136
Indonesia	0.248	0.263
South Korea	5.146	:
Malaysia	2.270	2.055
Philippines	1.275	1.166
Singapore	5.430	5.957
Thailand	1.598	1.569
India	0.295	0.370
Israel	0.154	0.463
Other Asian countries	2.900	2.897
Australia	0.182	0.210

Source: compiled by the author on the basis of the EUROSTAT data.

Japan, like Germany, has a status of a surplus country in the world economy (see: Table 1 and Fig. 2). Again the main factor contributing to this status is the high international competitiveness of Japanese economy in comparison to the

rest of the world (6 position in the Global Competitiveness Report 2010-2011 ranking³) despite economic stagnation observed since the beginning of the 21st century and during the 2008-2009 recession.

Japan also belongs to economies characterized by considerable innovation and a high share of high-tech products in global exports of high-tech products. It is also noteworthy that high-tech exports constitute a significant share in total exports of Germany and Japan (see: Table 3).

Table 3. Exports of high-tech products as a share of total exports of EU-27 and selected countries in the world in the years 2007-2008 (%)

Country/year	2007	2008
European Union - 27	15.965	15.363
Belgium	6.627	6.796
Bulgaria	3.49	3.573
Czech Republic	14.128	14.142
Denmark	11.689	10.752
Germany	12.988	12.439
Estonia	7.812	7.491
Ireland	25.732	24.282
Greece	4.737	5.878
Spain	4.238	4.162
France	15.569	16.365
Italy	6.002	5.95
Cyprus	14.64	19.089
Latvia	4.617	4.632
Lithuania	7.338	6.518
Luxembourg	32.403	35.211
Hungary	21.358	20.238
Malta	47.825	44.993
Netherlands	18.278	16.16
Austria	11.112	10.838
Poland	3.04	4.271
Portugal	6.523	6.127
Romania	3.504	5.402
Slovenia	4.621	5.192
Slovakia	4.997	4.831
Finland	17.519	17.331

³ See: Global Competitiveness Report 2010-2011, Klaus Schwab, World Economic Forum, Geneva Switzerland 2010.

Table 3. Cont'd

Country/year	2007	2008
Sweden	13.844	13.535
UK	16.173	15.113
Iceland	1.644	1.634
Norway	3.276	3.284
Switzerland	20.148	20.766
Russia	1.226	1.168
Canada	7.479	6.647
United States	20.344	19.185
Mexico	:	14.776
Brazil	5.914	2.674
China, excluding Hong Kong	28.13	26.614
Hong Kong	35.285	38.657
Japan	17.963	16.255
South Korea	28.15	:
Singapore	36.865	36.47
Thailand	21.147	18.462
Israel	5.771	15.611
Australia	2.661	2.327

Source: compiled by the author on the basis of the EUROSTAT data.

The positive current account balance of Germany and Japan in transactions with the rest of the world is accompanied by the negative financial account balance (see: Table 4 and Fig. 2).

It is connected with considerable foreign direct investments and portfolio investments of both countries. One of the areas of large direct investments for both countries is the United States. Direct investment balances for both countries in transactions with the United States are positive and fairly high (see: Figure 3). During the 2007-2009 recession, the positive balance of German direct investments in relationships with the United States was maintained at an almost unchanged level, whereas in the case of Japan it increased significantly.

Japan and Germany are also among the main holders of the US government's treasury securities. It must be mentioned that as far as the value of the owned treasury securities is concerned, Japan holds the second position, just behind China, whereas Germany is the fourteenth (see: Table 5).

Table 4. Financial account balance for the EU countries, US and Japan in transactions with the rest of the world in the years 1999-2009 (millions, EUR)

Country/year	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Belgium	:	:	:	:	:	-8006	-7304	-5988	-5829	9562	-3896
Bulgaria	635	827	330	1129	967	883	3409	5298	10512	10735	2844
Czech Republic	1349	3294	3103	4244	4515	5421	2092	3206	3967	878	1427
Denmark	-374	3429	-9437	-2079	-6288	-13949	-7220	-2090	-2997	-403	-5284
Germany	-10395	34186	-11794	-38448	-61758	-122985	-129634	-175473	-219502	-197330	-129649
Estonia	377	302	352	735	976	1161	915	1910	2398	1261	-911
Ireland	:	:	-319	1068	-1371	3801	-487	4770	12051	16132	-3315
Greece	4730	8907	6933	10303	9885	8100	12611	20453	27570	29914	24396
Spain	11328	19476	21702	15381	17825	34851	60817	85625	101005	101976	57580
France	-36900	-31098	-33100	-20603	9710	-7837	-1589	25958	30296	26630	59444
Italy	-8817	4233	-3421	8512	17319	9025	20901	25404	26212	29733	24447
Cyprus	:	:	257	468	216	416	592	987	1902	2936	1365
Latvia	622	455	660	704	752	1302	1700	3311	4468	3083	-2191
Lithuania	1163	602	462	550	914	1018	1257	2499	3678	3674	-2036
Luxembourg	:	:	:	-2668	-1961	-2808	-4365	-3191	-3519	-1825	-2271
Hungary	3857	4243	3180	4564	5763	7942	7485	7880	6537	9286	-590
Malta	152	492	-127	-49	96	133	300	313	306	348	130
Netherlands	-4959	-13096	1230	6180	-20728	-36347	-30307	-53471	-25109	-7327	-36995
Austria	6590	4647	4154	-2665	-527	-643	-240	-7944	-11503	-14966	-4678
Poland	:	10389	4039	6971	6590	5985	5745	8429	18816	28535	15309
Portugal	8328	11765	12264	9390	6327	10073	14004	15301	14423	19121	15423
Romania	402	1371	1565	2403	2983	3706	5977	9403	16781	17662	5581
Slovenia	623	533	-143	164	208	794	1084	1223	1972	2572	229
Slovakia	929	635	1674	1621	209	1070	2778	3018	2425	5107	3525
Finland	-4891	-9897	-12758	-7476	-7626	-8318	-2781	-6383	98	9135	11011
Sweden	:	:	:	:	:	-22927	-23723	-25143	-6636	15008	-8180
UK	44957	37946	44213	38277	31713	43605	42776	55972	46301	18372	34653
Belgium-Luxembourg	:	:	:	:	:	:	:	:	:	:	:
United States	226618	527254	447063	523183	470604	427515	573082	642147	469148	393342	148519
Japan	-107704	-136666	-99299	-117655	-102318	-112032	-116144	-107489	-164001	-138904	-114541
All countries of the world	61446	270427	211828	196151	48174	-129024	-88478	-163442	-242304	-182274	-171382

Source: compiled by the author on the basis of the EUROSTAT data.

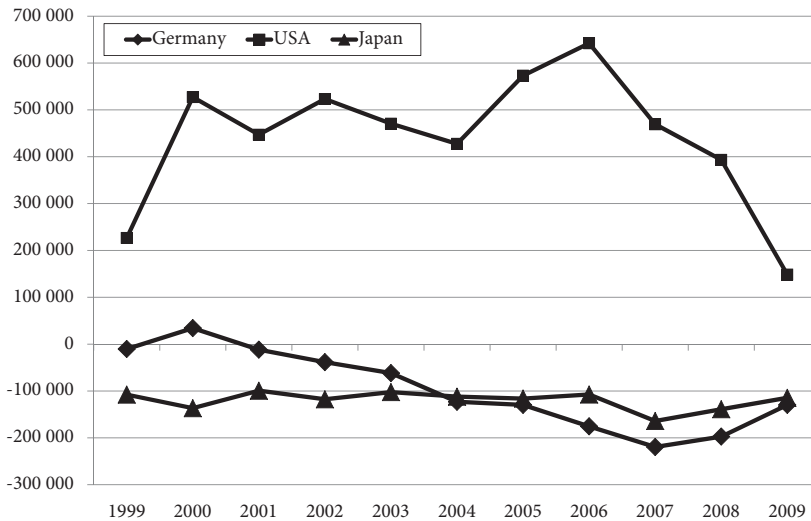


Fig. 2. Financial account balance for Germany, United States and Japan in transactions with the rest of the world in the years 1999-2009 (millions, EUR)

Source: compiled by the author on the basis of data included in Table 2.

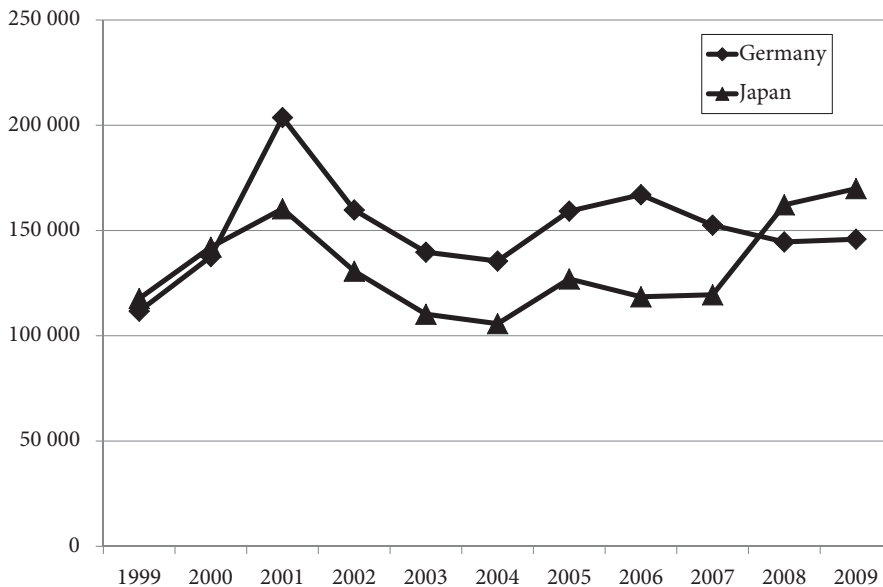


Fig. 3. Balance of direct investment account for Germany and Japan in transactions with the United States in the years 1999-2009 (millions, EUR)

Source: compiled by the author on the basis of the EUROSTAT data.

Table 5. Major foreign holders of US government's treasury securities in the years 2009-2010 (as of end of the month)

Country/year	2009 November bn USD	Share %	2010 November bn USD	Share %
China	929.0	25.3	895.6	20.6
Japan	754.3	20.6	877.2	20.2
UK	155.5	4.2	511.8	11.8
OPEC countries	202.6	5.5	210.4	4.8
Brazil	165.8	4.5	184.4	4.2
Caribbean bank centers	123.2	3.4	146.3	3.4
Hong Kong	142.1	3.9	138.9	3.2
Canada	50.7	1.4	134.7	3.1
Taiwan	115.4	3.1	131.1	3.0
Russia	151.4	4.1	122.5	2.8
Switzerland	89.6	2.4	100.6	2.3
Luxembourg	80.2	2.2	81.0	1.9
Thailand	29.6	0.8	65.7	1.5
Germany	48.7	1.3	60.4	1.4
Singapore	37.5	1.0	59.4	1.4
Ireland	43.1	1.2	42.1	1.0
South Korea	40.2	1.1	41.5	1.0
India	34.5	0.9	40.7	0.9
Total value of treasury securities owned by foreign investors	3669.0	1.0	4348.8	1.0

Source: compiled by the author on the basis of the data of the U.S. Bureau of Economic Analysis.

When compared to the United States, both countries are characterized by a higher share of gross domestic savings in GDP (see: Fig. 4). A drop in the share of gross domestic investments in German and Japanese GDP in the last decade accompanied by a growing share of savings in GDP must have been related to increased foreign direct investments in the US economy and portfolio investments of financial institutions the object of which were, among others, American treasury bonds (see: Fig. 5).

Germany and Japan are characterized by a gross public debt to GDP ratio higher than 60%. In the case of Japan this indicator considerably exceeds 100% (see: Table 6).

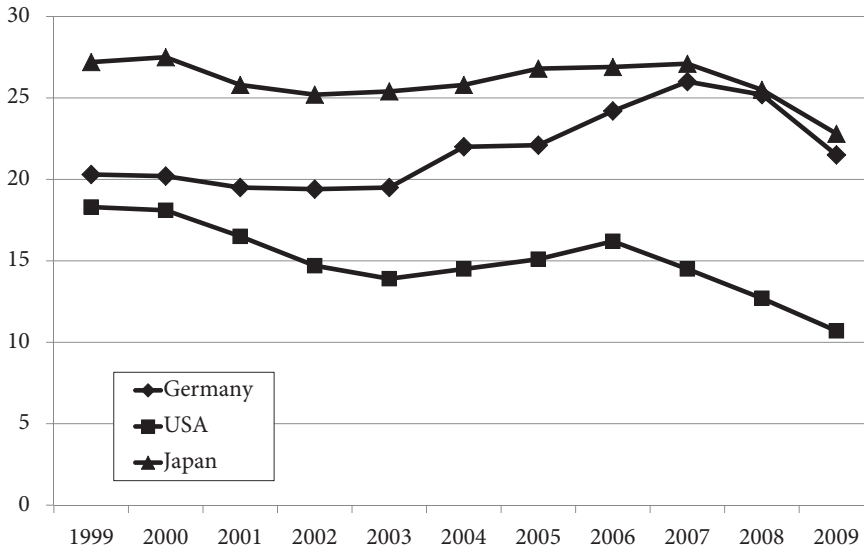


Fig. 4. Gross domestic savings as a percentage of GDP - Germany, Japan and the US in the years 1999-2009 (%)

Source: compiled by the author on the basis of the EUROSTAT data

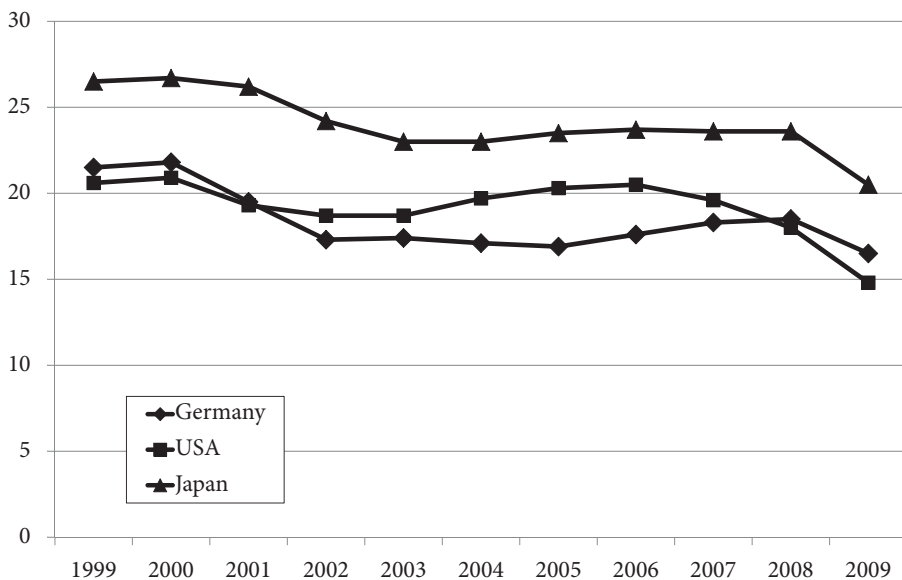


Fig. 5. Gross investments as a percentage of GDP - Germany, United States and Japan in the years 1999-2009

Source: compiled by the author on the basis of the EUROSTAT data

Table 6. Consolidated public sector balance sheet, public debt, the current account surplus/deficit as a percentage of GDP (%)

Country/Year	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Germany											
Public sector balance sheet	-1.7	1.3	-2.8	-3.7	-4.0	-3.8	-3.3	-1.6	0.2	0.0	-3.1
Public debt	60.9	59.7	58.8	60.4	63.9	65.7	68.0	67.6	64.9	66.3	73.5
Current account balance	-1.3	-1.7	0.0	2.0	1.9	4.7	5.1	6.5	7.6	6.7	4.9
Japan											
Public sector balance sheet	-7.4	-7.6	-6.3	-8.0	-8.0	-6.2	-4.8	-4.0	-2.4	-4.1	-10.2
Public debt	133.8	142.1	151.7	160.9	167.2	178.1	191.6	191.3	187.7	194.7	217.6
Current account balance	2.6	2.6	2.1	2.9	3.2	3.7	3.6	3.9	4.8	3.2	2.8
United States											
Public sector balance sheet	:	:	-0.3	-3.9	-4.9	-4.4	-3.2	-2.0	-2.7	-6.7	-12.9
Public debt	60.8	54.8	54.7	57.1	60.4	61.4	61.6	61.1	62.1	71.1	84.3
Current account balance	-3.2	-4.2	-3.9	-4.3	-4.7	-5.3	-5.9	-6.0	-5.1	-4.7	-2.7

Source: OECD data

Despite this, the economies of Germany and Japan are regarded as credible by investors who willingly invest in treasury bonds issued there. Both their economies and treasury bonds of these countries are assessed very well in S&P ratings (see: Table 7).

Table 7. Standard & Poors rating– Germany, Japan, United States and China in January 2011

Country	Domestic rating	Foreign rating	T&C Assessment
Germany	AAA	AAA	AAA
Japan	AA-	AA-	AAA
United States	AAA	AAA	AAA
China	AA-	AA-	AA-

Source: www.standardandpoors.com/ratings/sovereigns/ratingslist/en/us/?sectorName=Governments&subSectorCode=39&start=0&range=50

In spite of the fact that in the last decade in both countries public debt has increased in relation to GDP, they do not have problems with placement of new

bond issues in financial markets and German bonds are still treated as benchmark reference and are used for international comparisons.

As a result, when combined with considerable financial reserves, the position of the two countries in global economy, both in the sphere of real flows as well as financial ones, is unshakeable.

Conclusions

The preliminary analysis conducted in this work seems to confirm some research hypotheses.

Maintaining the current account surpluses by Germany and Japan in transactions with the rest of the world including the United States is a result of a high level of international competitiveness of both economies, including exports.

American economy is attractive for investors from both countries which is connected with a relatively high balance of foreign direct investments in transactions with the United States.

It seems unlikely for the situation of payment imbalances between Germany and Japan on the one hand and the rest of the world on the other to be dangerous either for the two countries in question or global economy. A payment imbalance between Germany and other EU countries has been noted for years. A similar situation has also been observed in the relationships between the Netherlands, Austria, Denmark and France (in some years) – and the remaining EU countries. Such a situation can be accounted for by differences in the international competitiveness levels among economies of the above mentioned countries and the remaining member countries, different stages of their economic advancement and differences in economic policy stability.

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