United States and Euro Area External Adjustment: The Role of Commodity Prices and Emerging Market Shocks


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TRADE BALANCES (TB) of US and Euro Area (EA) improved after Global Financial Crisis
Widely viewed as reflecting weak domestic aggregate demand & deleveraging
This paper challenges conventional view
Paper highlights key role of post-crisis commodity price collapse for EA and US trade balance reversals
Aggregate demand shocks in Rest of World (RoW) too mattered for EA & US TB
Findings consistent with pre-crisis RoW saving glut (Bernanke) effect on US and EA TB
Broader lesson: Emerging Markets and commodity shocks are major drivers of Advanced Countries’ TBs & terms of trade
Model captures other key changes in world economy since 2000:
• Growth acceleration in Emerging Economies
• Boom-bust cycle in Euro Area (EA) & US
• Enormous fluctuations in commodity price


Historical shock decompositions (based on estimated model):
(a) Euro Area trade balance/GDP
(b) US trade balance/GDP

Continuous line: historical series (demeaned). Black areas show contributions of different shocks. Areas above (below) dashed horizontal line show positive (negative) contributions