

# United States and Euro Area External Adjustment:

## The Role of Commodity Prices and Emerging Market Shocks

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Massimo Giovannini<sup>1</sup>; Stefan Hohberger<sup>1</sup>; Robert Kollmann<sup>2,3</sup>; Marco Ratto<sup>1</sup>; Werner Roeger<sup>4</sup>; Lukas Vogel<sup>4</sup>

<sup>1</sup>European Commission, JRC; <sup>2</sup>Université Libre de Bruxelles; <sup>3</sup>CEPR; <sup>4</sup>European Commission, DG-ECFIN

Contact: [robert\\_kollmann@yahoo.com](mailto:robert_kollmann@yahoo.com), [www.robertkollmann.com](http://www.robertkollmann.com)

► **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.

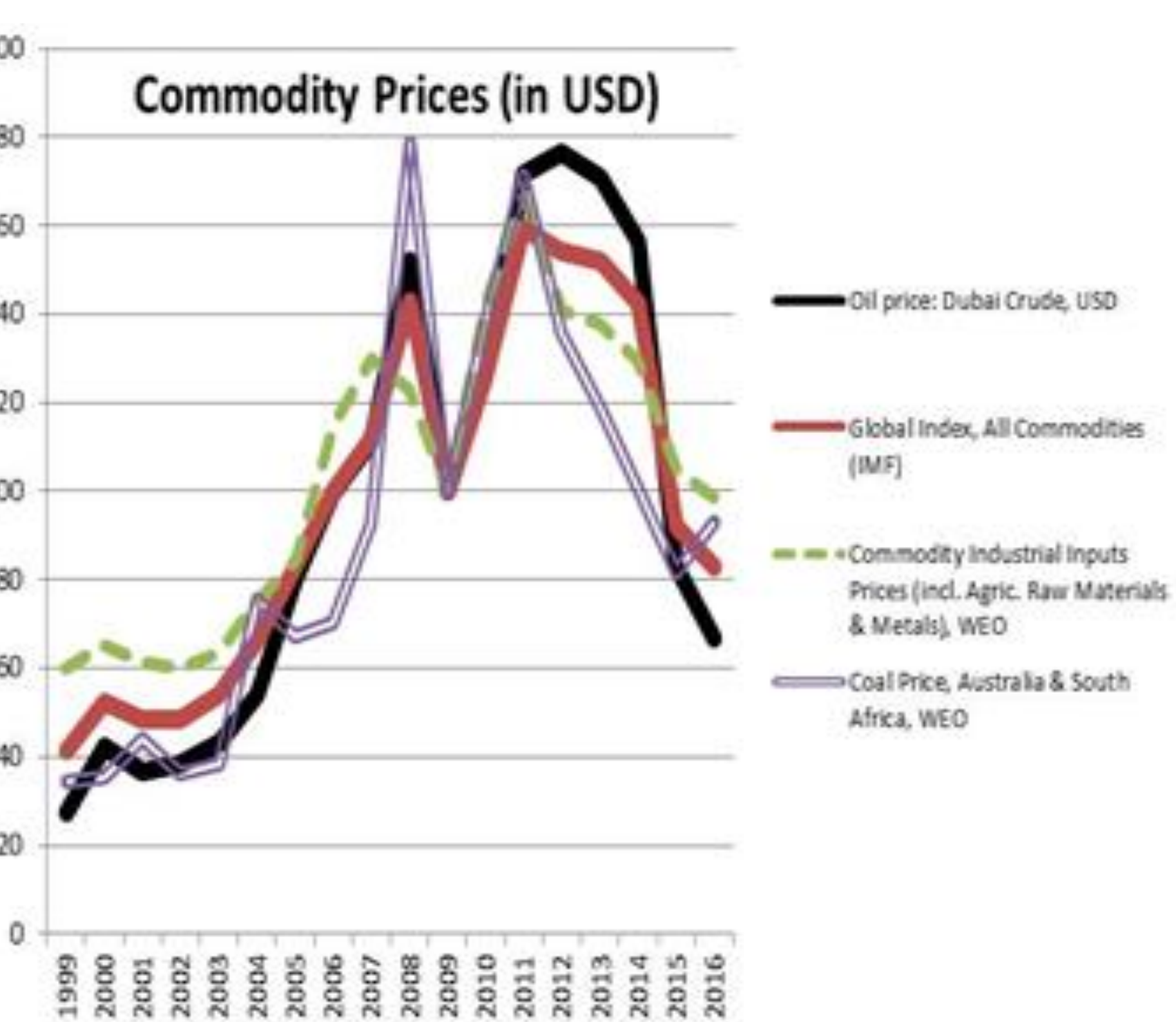
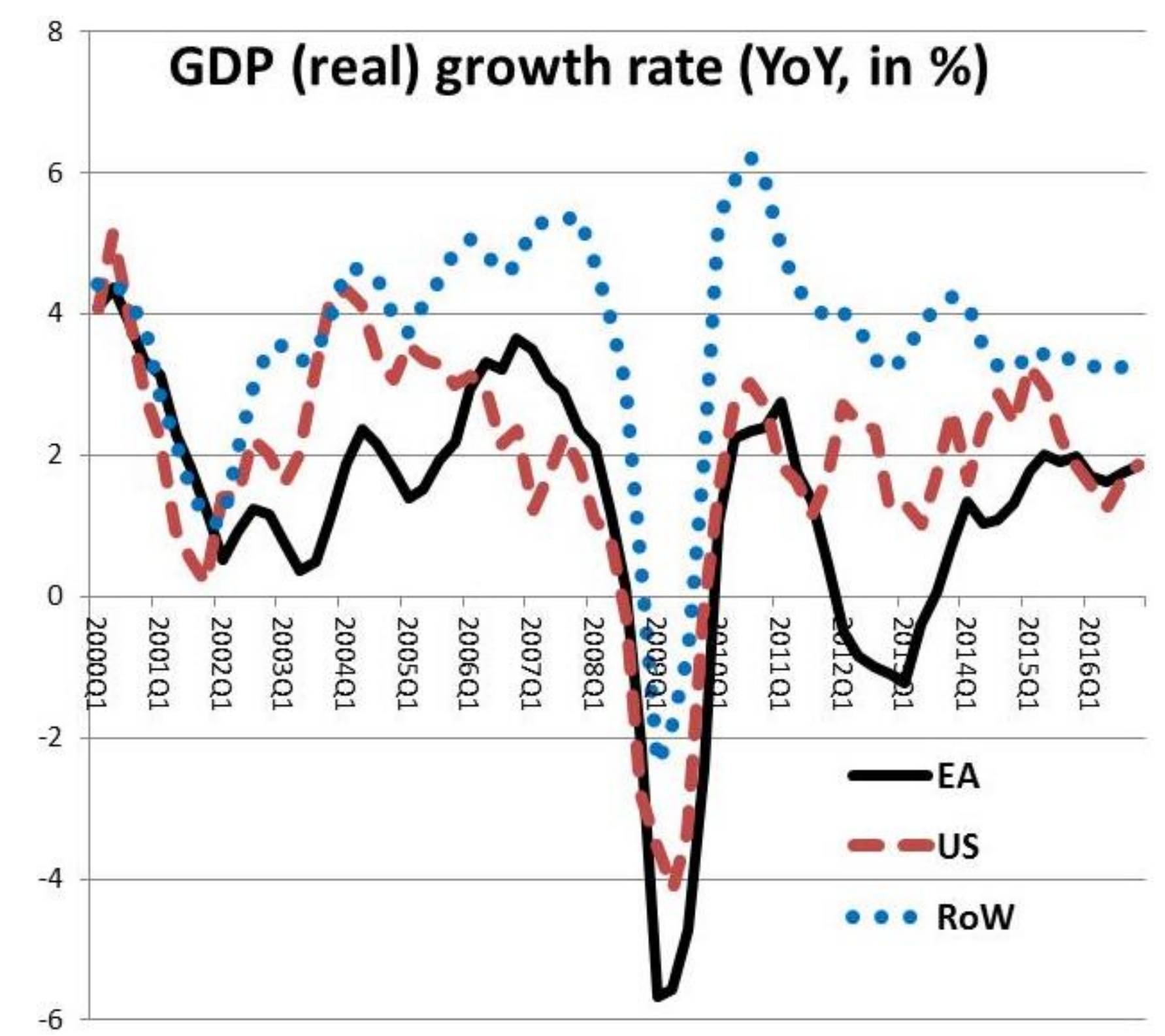
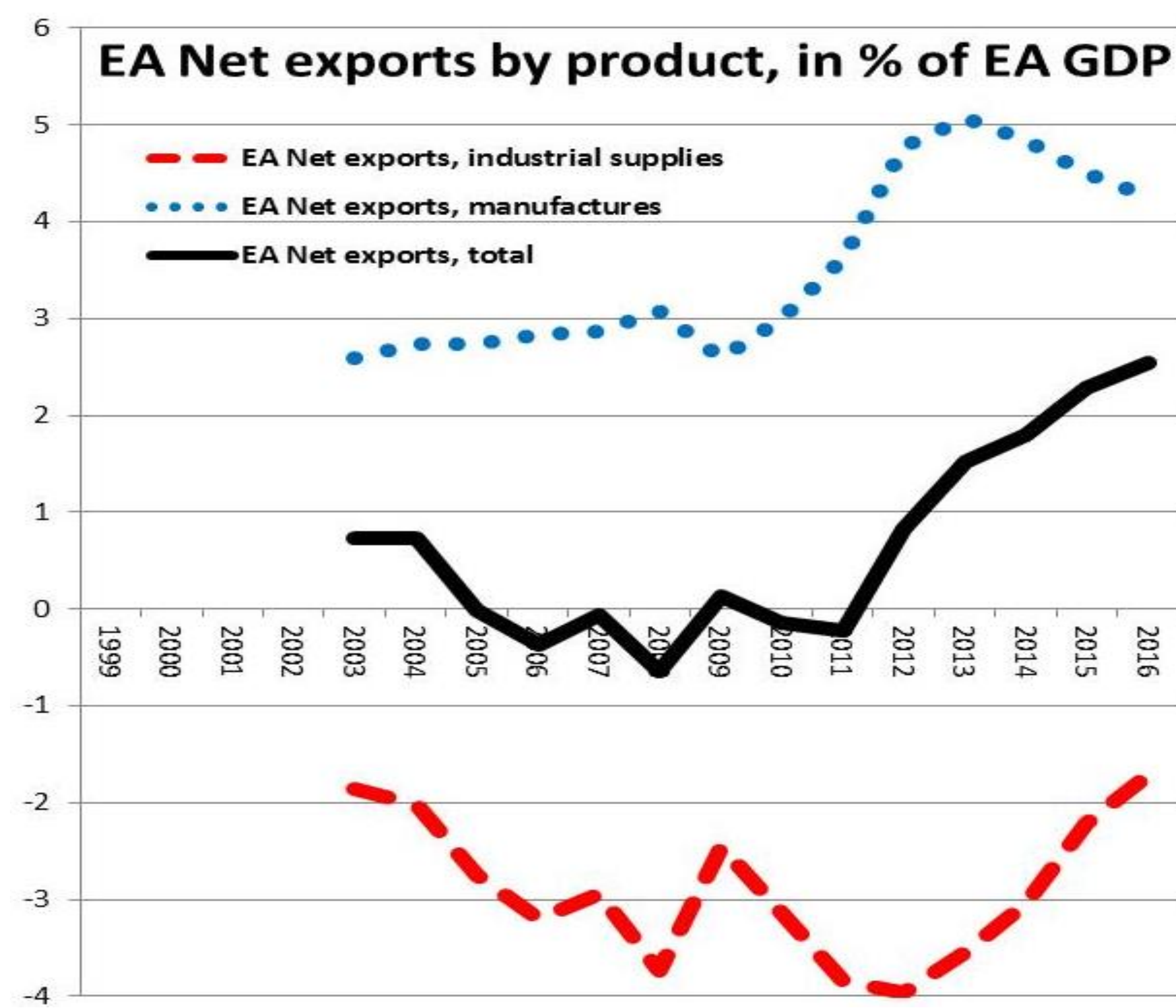
► Findings consistent with pre-crisis RoW saving glut (Bernanke) effect on US and EA TB

► 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

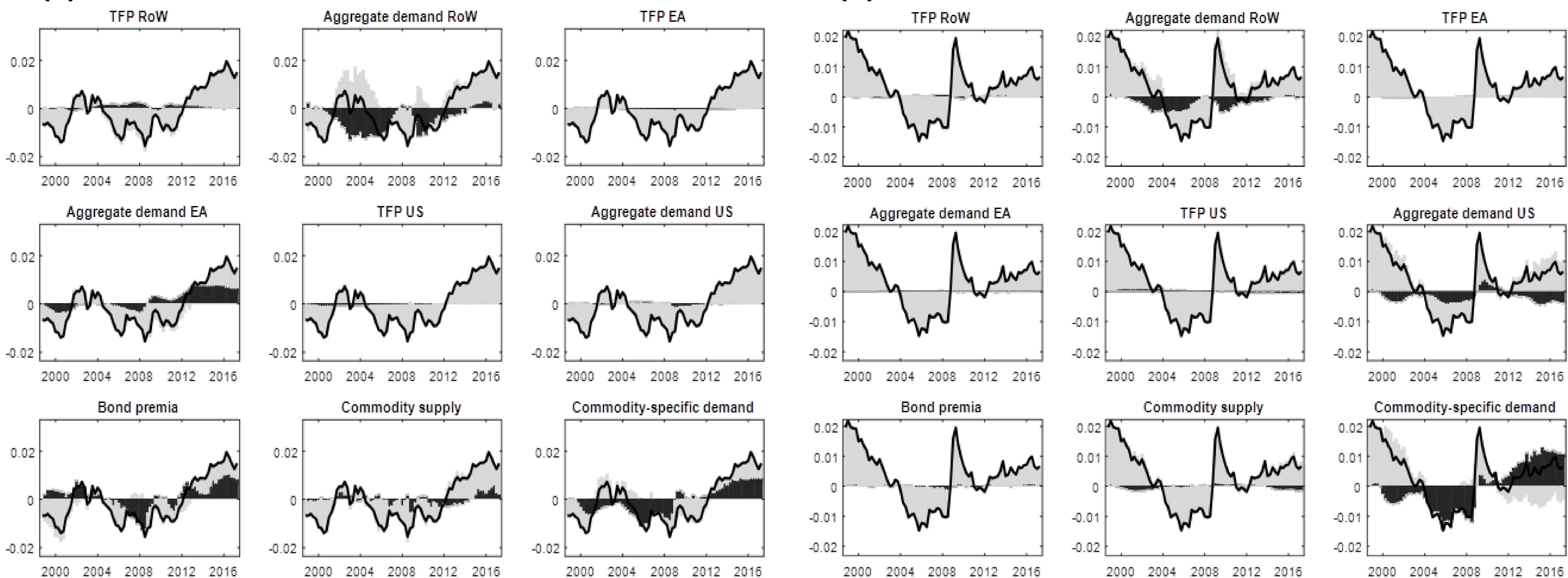
► **Methodological contribution:** Bayesian estimation of three-region (EA, US, RoW) DSGE model with trade in manufactured goods and commodities. Commodity price reflects global demand and supply conditions. Sample: 1999-2017. 66 structural shocks; 60 observables for estimation



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