ABSTRACT

THE U.S. TRADE DEFICIT, THE U.S. FISCAL DEFICIT, AND THE FOREIGN EXCHANGE VALUE OF THE U.S. DOLLAR

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The period since the breakdown of the Bretton Woods System of pegged exchange rates has been the most tumultuous in monetary history. More than forty national banking systems have collapsed. There have been four major asset price bubbles. The scope of overshooting and undershooting of national currencies has been much greater than in any previous period. One feature of this period is that countries have experienced extended inflows of foreign funds that have led to the real appreciation of their currencies and the increase in asset prices. Another feature of this period is that the U.S. international investment position evolved from the world's largest creditor to the world's largest debtor—and U.S. international indebtedness is increasing at the rate of more than fifteen percent a year. The development of the U.S. trade deficit reflects that the United States in the Nth country; the components of the U.S. external payments accounts change to provide consistency for the balance of payments accounts of all other countries as a group. The United States is now on a time-inconsistent trajectory; U.S. international indebtedness is increasing too rapidly relative to U.S. GDP. The likelihood that there is market solution to this problem is low.