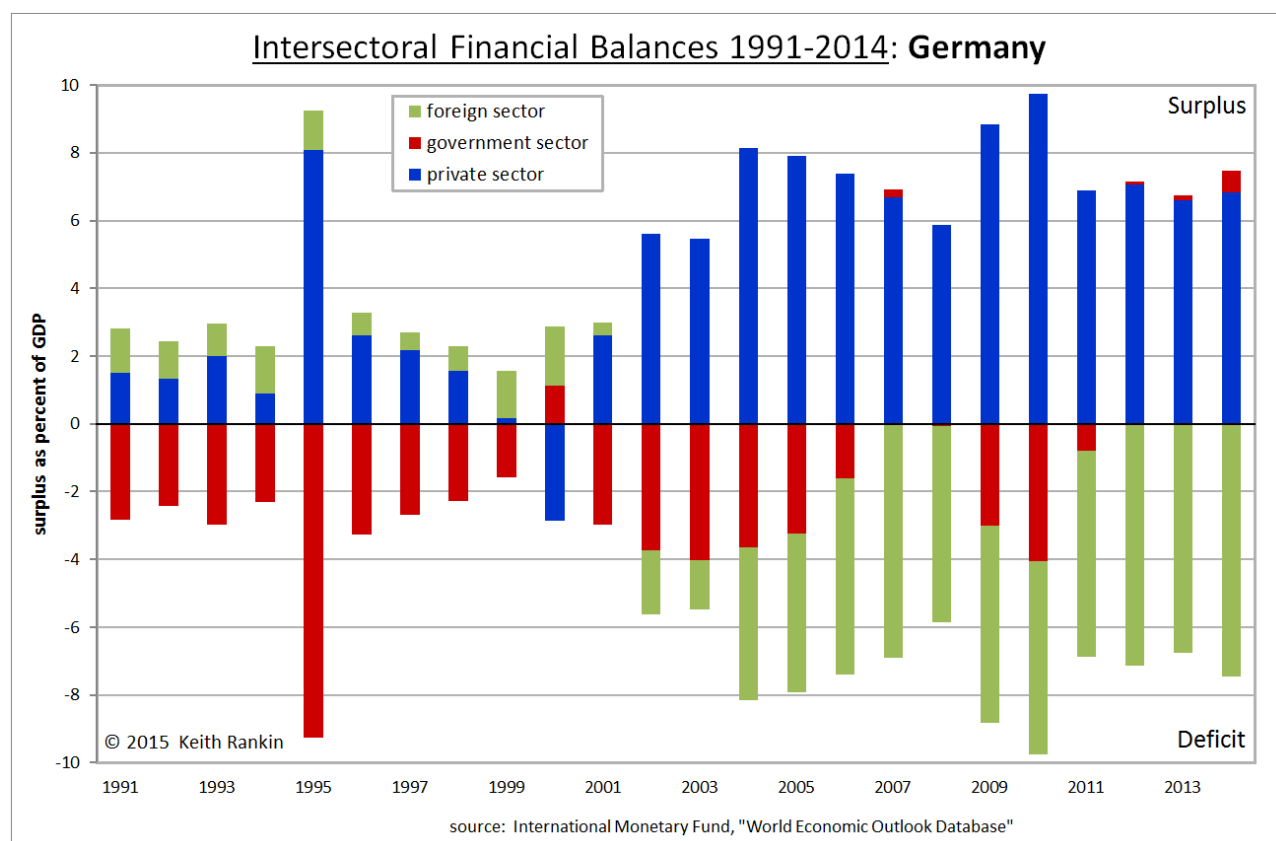


Chart for this Week: Financial Balances of Germany 1991-2014

Keith Rankin, 12 August 2015



[Germany's current account time bomb](#)

[Last week's chart](#) showed advanced country financial balances from 1991 to 2014. My commentary probably understated its significance. The private sector financial balances (in blue) since 2008 represent the single biggest threat to the global economy since the emergence of similar global imbalances in the 1920s. And what that chart shows is only the tip of the iceberg. If we divided the advanced country economies (especially the USA) into rich businesses and households and the rest, then the unspent balances of the rich (recycled to be spent by the poor as debt) would be several multiples larger.

Germany is a big part of this problem, as British author and political economist Philippe Legrain has written about in two July 2015 articles ([Europe needs Britain in the EU to curb German dominance](#) for CapX; [The Eurozone's German Problem](#) for Project Syndicate). The name of the problem is 'mercantilism', which essentially means running persistent current account surpluses for their own sake. From a short term perspective it means making lots of money, especially through foreign trade. From a long term (multi-decade) perspective it means producing lots of exports which, through requisite debt write-offs, amount to giving stuff away (lots of stuff!) and ruining other economies in the process.

Germany in the 1990s was in an unusual situation, on account of the post-cold-war reunification of East and West. This week's chart shows that, in the 1990s, small German private surpluses were matched by small government deficits. (Something went awry in 1995, causing Germans to slash their private spending; the federal and state governments accommodated this through a very large general government deficit.)

From 2002 Germany began reverting to pre-WW1 type (see [The Return of the Ugly German](#), by Joschka Fisher), and the formation of the Eurozone made this economic behaviour very easy. For Germany, the Euro is undervalued compared with what a free floating Deutschmark would have been. This currency undervaluation, reinforced through ruthless cost management, has enabled Germany to become extremely 'competitive', initially with respect to its Eurozone partners and subsequently with respect to the rest of the whole world.

After the formation of the Eurozone at the turn of the millennium, and the effective completion of the reunification project, we see the accommodation of these huge private surpluses switching from the government account (red) to the current account of the balance of payments (green). From 2002 to 2010, this was Germans lending especially to Greeks, Spanish, Portuguese, and Irish (once called PIGS), with the effect that those countries' people could (and did) buy swathes of German exports. This decade Germany's private and government surpluses together have become the current account surplus of the whole Eurozone with the rest of the world. The whole Anglo-Latin world is becoming the next set of PIGS.

This monetary outflow from Germany in 2002 to 2008 was not investment in Greece and Spain, just as foreign-sourced money coming into New Zealand to buy existing houses is not investment either. If this money had been effective investment, Greece and Spain would have become competitive and would now be exporting swathes of goods to Germany. Rather that surplus money was 'investment' in keeping Greece and Spain economically dependent on German credit, much as loan sharks invest in their clients. The strategy worked.

Legrain sees these huge and growing German current account surpluses (in green) as the single biggest threat to the world economy. I agree, though I would argue that the problem is bigger than German mercantilism. As I showed last week, the other part of the same problem is the huge monetary stockpiles of the global rich – corporations and households. Substitute 'Apple' for 'Germany'. The world economy ticks over nicely so long as the governments and the poor accommodate these cash stockpiles through indebted spending. The crunch comes when governments resist further indebtedness and private debtors default *en masse*. The governments are resisting.
