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German current account surplus Market Top Competitors Analysis Report

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The German current account surplus

SUMMARY

WiseGuyReports published new report, titled “The German current account surplus - Holding captive the German and global economies”

The size of Germany's current account surplus is an economic phenomenon as the forces behind it go beyond the simple competiveness of German exports. Indeed, the widening gap between domestic savings and investment is the determinant of this trade surplus, which is shaped by the actors of the German economy; namely firms, the government and households. Furthermore, the harmful impact of this trade surplus reaches across the domestic economy - where it is a source of rising inequality and limited social welfare - to the global stage, where it acts as a means of destabilizing the economies of countries that accumulate unsustainable debt through trade deficits.

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The vast trade surpluses of Germany have been a matter of dispute between the country and its trade partners over the legitimacy of these surpluses in free trade, which are a factor of imbalance for the global economy. For this reason, it is valuable to assess the forces behind these trade surpluses and their consequences for the global economy, including the German domestic economy.
An examination of the size of the German current account surplus, both in national and global terms, shows that it is not only vast for the country’s domestic economy, but that it also overshadows those of the largest country-exporters worldwide. As this trade surplus leads to an enormous current account surplus which is not justifiable on the premises of competiveness of German exports, understanding the forces behind this phenomenon is crucial.

An examination of the German current account surplus through a macroeconomic perspective reveals the gap between domestic savings and investment as a determining force. This in turn leads to the revelation of various interchanging dynamics between household, firms and the government that shape this gap. The intertemporal decisions of German households are the cause and at the same time the consequence of a large current account surplus. Particularly, the strong propensity of German households to opt for saving over consumption has shaped the subdued domestic consumption, urging the gigantic German firms to expand their marketplace through exports, hence increasing the trade surpluses of the economy. However, causality has also run inversely from the

impact of the German industrial relations model and the labor reforms of the previous decade to the German households, which have seen the growth of their income being depressed over that period. Still, the accumulation of capital by firms has not turned into domestic investment, putting a brake on domestic consumption. Similarly, the German government, which has prioritized the control of public finances since the beginning of the crisis in the Euro Area, has limited public spending and investments, which in turn has led to increased fiscal surpluses.
Since the amount of domestic investment has been diminishing, these savings have found their way out of the domestic economy in the form of the increasing ownership of foreign assets as shown through the country's balance of payments. This domestic trend that is propagated through international trade has a global impact.

Indeed, international trade expansion of Germany has been realized at the cost of the trade deficits of other countries. Moreover, the fact that this trade expansion has been based on economic distortions, namely the reliance of the German economy on an undervalued currency, means that the recycling of this growth model is not viable. In fact, the funding of countries with trade deficits through German savings cannot be reproduced forever since demand is certainly going to reach its upper limits in line with the
indebtedness of these countries.

As a result, this economic growth model of Germany based on trade surpluses is jeopardizing the growth prospects of its domestic and global economy. The impact of the self-destruction of this model by stretching its limits or by provoking the boomerang effect of protectionism might be obvious, but its inefficiency for the German economy is still not. In fact, there is evidence that this model of economic growth is the source of rising inequality and minimized welfare for the German population. Specifically, the accumulation of savings from the government and the firms for recycling these trade surpluses has meant and still means suppressed growth of income, limited government expenditure related to transfers for social protection and lack of public investment that prevent the stimulation of domestic consumption, eventually making the German economy vulnerable and captive of these trade surpluses.

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