Discussion of: Intertemporal Approach to the Financial Account

Pierre-Olivier Gourinchas and Hélène Rey

Fabrizio Perri
New York University

AEA Meetings, Boston 2006

The Question

- How does the external adjustment take place, or

The Question

- How does the external adjustment take place, or or how do countries repay their debts?

The background findings

Gourinchas and Rey (2005) find that when US is debt, on average:

- US net exports grow (direct repayment)
- Relative returns on US owned foreign assets increase, mostly through RER movements.

In a two periods setup

$$
\begin{aligned}
c &= y + A - A^* - \left(A' - A^{*'}\right) \\
c' &= y' + (1+r)A' - (1+r^*)A^{*'}
\end{aligned}
$$

A is US ownd foreign asts, A^* is foreign ownd US asts

$$A - A' = NFA = -nx - nx' - rA' + r^* A^{*'}$$

In a two periods setup

$$
\begin{aligned}
c &= y + A - A^* - \left(A' - A^{*'}\right) \\
c' &= y' + (1+r)A' - (1+r^*)A^{*'}
\end{aligned}
$$

A is US ownd foreign asts, A^* is foreign ownd US asts

$$A - A' = NFA = -nx - nx' - rA' + r^* A^{*'}$$

how does the repayment happens is intimately connected to the question of caused the imbalance in the first place..

The Objective of this paper

Understand these phenomena as equilibrium responses to primitive shocks

The Objective of this paper

Understand these phenomena as equilibrium responses to primitive shocks

Very helpful exercise...

- What kind of model?
- What type of shocks?

The model

GR use a two good GE endowment model with complete markets Positives:

- Everything endogenous and easy to characterize allocations

The model

GR use a two good GE endowment model with complete markets Positives:

- Everything endogenous and easy to characterize allocations

Negatives

- Misses investment dynamics which are important for NX dynamics (endowment)
- Harder to map wealth in the model to wealth in the data

The model

GR use a two good GE endowment model with complete markets Positives:

- Everything endogenous and easy to characterize allocations

Negatives

- Misses investment dynamics which are important for NX dynamics (endowment)
- Harder to map wealth in the model to wealth in the data

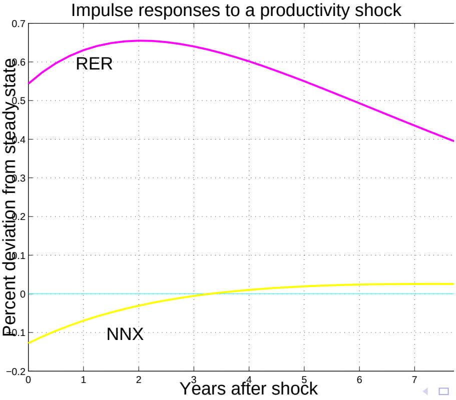
Needed?

- Additional shocks?

An alternative model

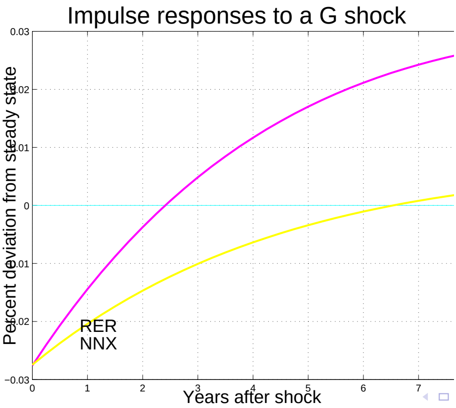
- Standard IRBC model with investment and IM
- Still easy to solve (linearization)
- Clear notion of NFA
- Can easily be used to check what type of shocks are needed to reproduce GR facts

An example



Impulse responses to a productivity shock
Percent deviation from steady state
Years after shock
RER
NNX
0.7
0.6
0.5
0.4
0.3
0.2
0.1
0
−0.1
−0.2
0
1
2
3
4
5
6
7

An example


Impulse responses to a G shock
Percent deviation from steady state
Years after shock
0.03
0.02
0.01
0
−0.01
−0.02
−0.03
0
1
2
3
4
5
6
7
RER
NNX

Summary

- GR uncovered some new findings on the dynamics of external adjustment
- This paper checks whether these findings can be rationalized by our existing models
- The use of these findings together with models can help us understand the forces that caused the external imbalance in the first place.