A Macroeconomic History of the U.S., Japan, and Germany

Intermediate Macroeconomics - UCLA - Econ 102

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UCLA

December 7, 2020

Section 1

Introduction

Links

There are several versions of these slides:

- Slides. html / pdf / zip
- Handouts. html / zip

If you want to know more, there also exists a more advanced version of these slides (Ph.D. Level) - this is absolutely not exam material:

- Slides. html / pdf / zip
- Handouts. html / zip

Plan of the course

We'll illustrate some macroeconomic history in:

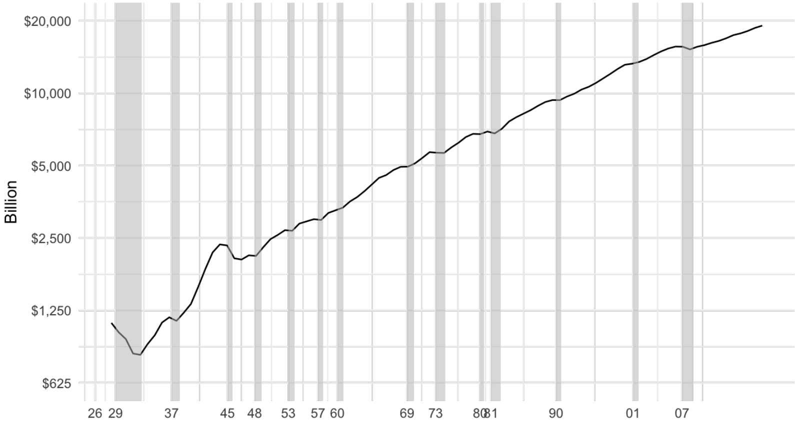
- United States
- Japan
- Europe
- Germany

Section 2

United States

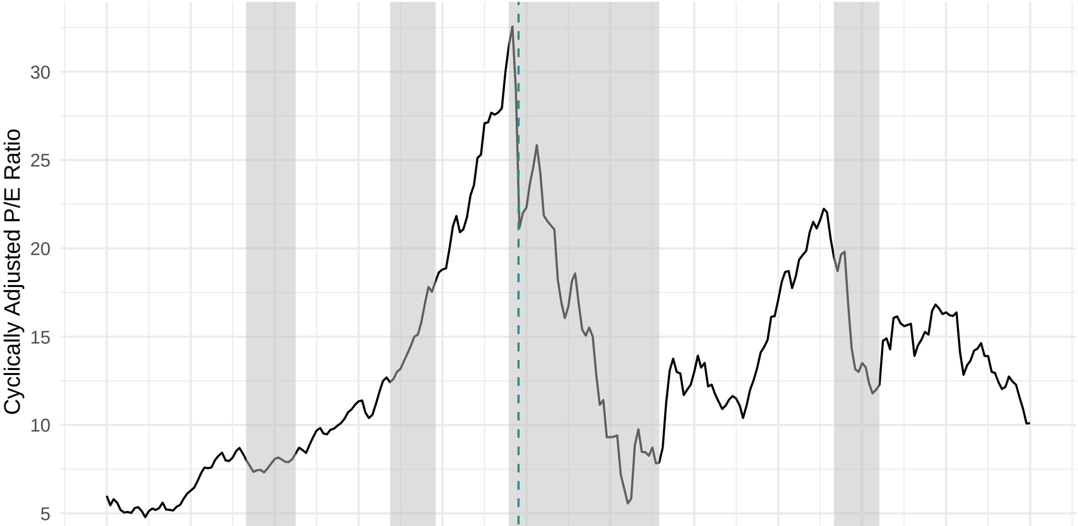
U.S. Real GDP

- Shaded areas: NBER recessions.
- World War II: large government purchases, loans to Europe (external demand).

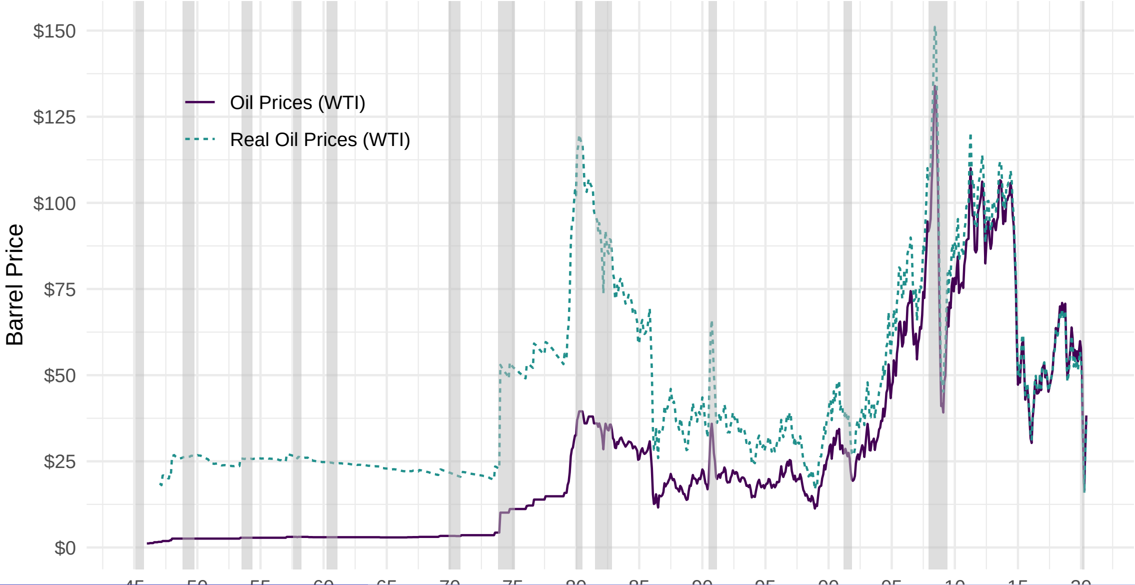


1929: The Big Crash

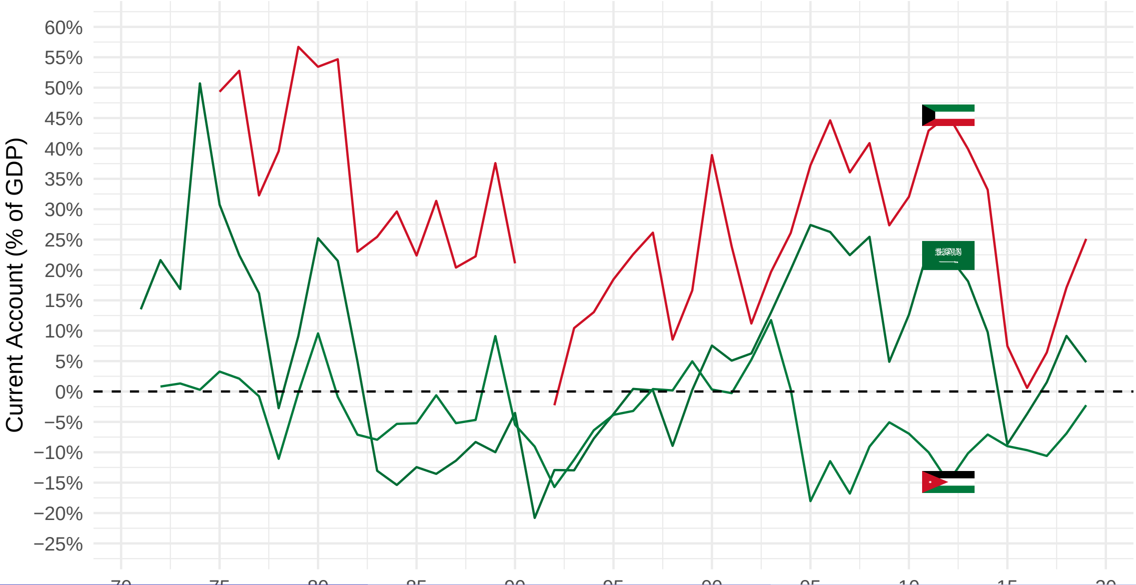
End October 1929: The Big Crash



1973 Oil Shock



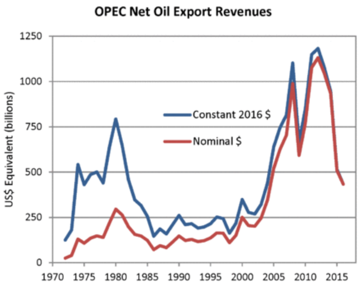
Effect on Oil Exporting Countries' CA



Petrodollar recycling (Wikipedia entry)

Petrodollar recycling

Petrodollar recycling is the international spending or investment of a country's revenues from petroleum exports ("**petrodollars**").[3] It generally refers to the phenomenon of major petroleum-exporting states, mainly the OPEC members plus Russia and Norway, earning more money from the export of crude oil than they could efficiently invest in their own economies.[4] The resulting global interdependencies and financial flows, from oil producers back to oil consumers, can reach a scale of hundreds of billions of US dollars per year – including a wide range of transactions in a variety of currencies, some pegged to the US dollar and some not. These flows are heavily influenced by government-level decisions regarding international investment and aid, with important consequences for both global finance and petroleum politics.[5] The phenomenon is most pronounced during periods when the price of oil is historically high.[6]



Fluctuations of OPEC net oil export revenues since 1972, showing elevated inflation-adjusted levels during 1974–1981 and 2005–2014[1][2]

Petrodollar recycling - Graeber (2011)

background, explaining how, during the '70s oil crisis, OPEC countries ended up pouring so much of their newfound riches into Western banks that the banks couldn't figure out where to invest the money; how Citibank and Chase therefore began sending agents around the world trying to convince Third World dictators and politicians to take out loans (at the time, this was called "go-go banking"); how they started out at extremely low rates of interest that almost immediately skyrocketed to 20 percent or so due to tight U.S. money policies in the early '80s; how, during the '80s and '90s, this led to the Third World debt crisis; how the IMF then stepped in to insist that, in order to

Petrodollar problem (IMF)

Petrodollar Problem

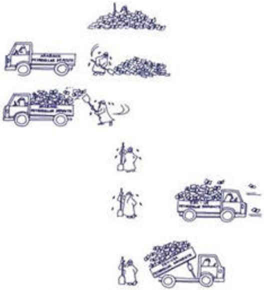
<--Previous

Next-->

While oil importers accumulated huge bills they could not pay, oil exporters accumulated large amounts of U.S. dollars - more than they knew how to use. These dollars were known as "petrodollars."

How will they pay?
Meanwhile, oil importing countries needed to borrow money to pay their huge oil bills. If they could not borrow the money, they would be forced to import less, causing their trading partners' exports to shrink. This could lead to a global contractionary spiral.

credits



Is there such a thing as TOO MUCH money?

Oil-exporting countries found themselves with so much money, they could not spend it fast enough. Some had small populations; many were still at early stages of industrialization. They could not import enough from the countries that bought their oil to keep from piling up enormous dollar surpluses.

Go-go banking - Borrowers' market (IMF)

Recycling Petrodollars

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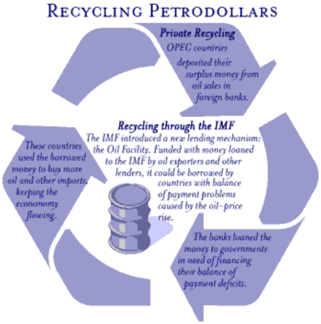
Borrowers' Market

The solution to one problem created another. Recycling petrodollars through the banking system slowed economic contraction, but did not alleviate massive payment imbalances. As a result the debts of oil-importing countries - especially developing countries - continued to pile up:

- The foreign debts of 100 developing countries (excluding oil exporters) increased 150% between 1973 and 1977.

Could the economies of the debtors withstand the inflationary pressure of the sudden, enormous oil-price increase?

Without the discipline of a fixed standard, could the new floating-rate system cope with such massive trade and monetary imbalances?



credits

China - U.S. Trade Tensions - Link between tariffs and devaluation

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# [1] "Link to the video:"
# [1] "https://fgeerolf.com/econ102/macro-history.html"
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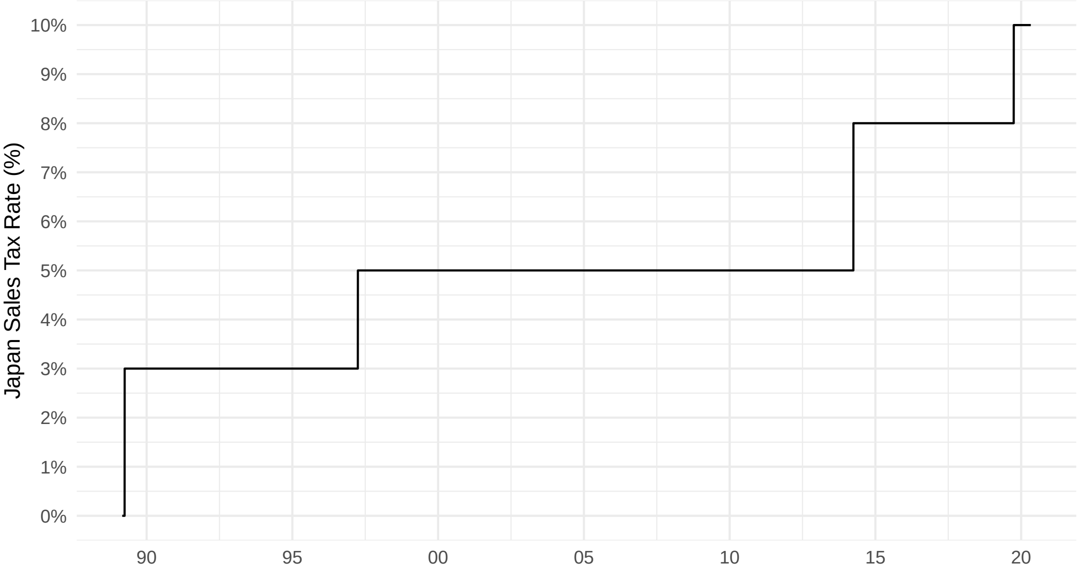
Section 3

Japan

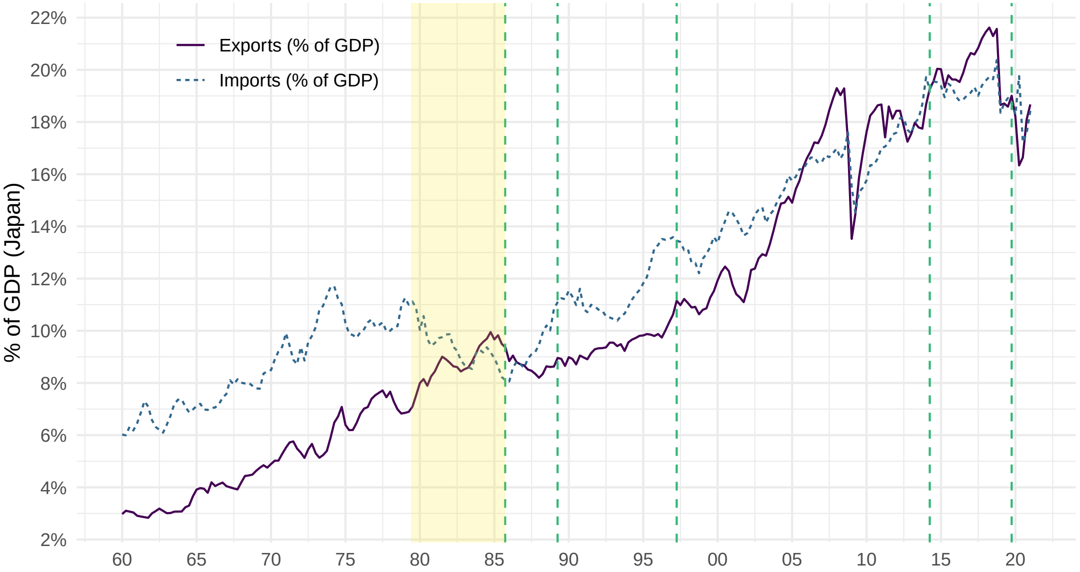
Sales Tax Increase: Abenomics

- April 2014: When the government raised the tax to 8% from 5% in April 2014, a last-minute buying spree.
- Subsequent pullback in demand caused a big downward swing in consumer spending.

Japan's Sales Tax Increases



Japan: X and M (% of GDP)



What is Abenomics ?

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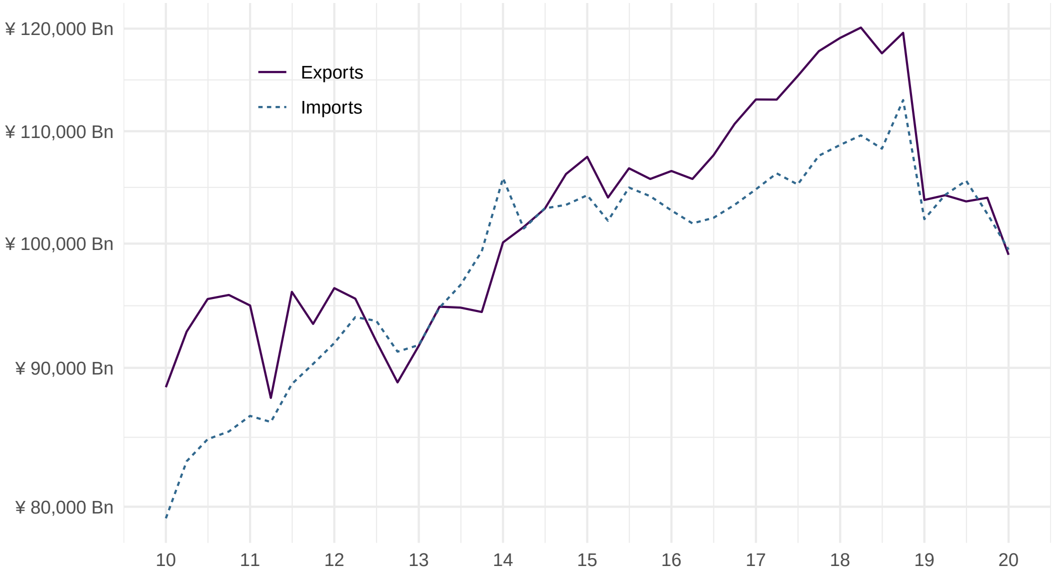
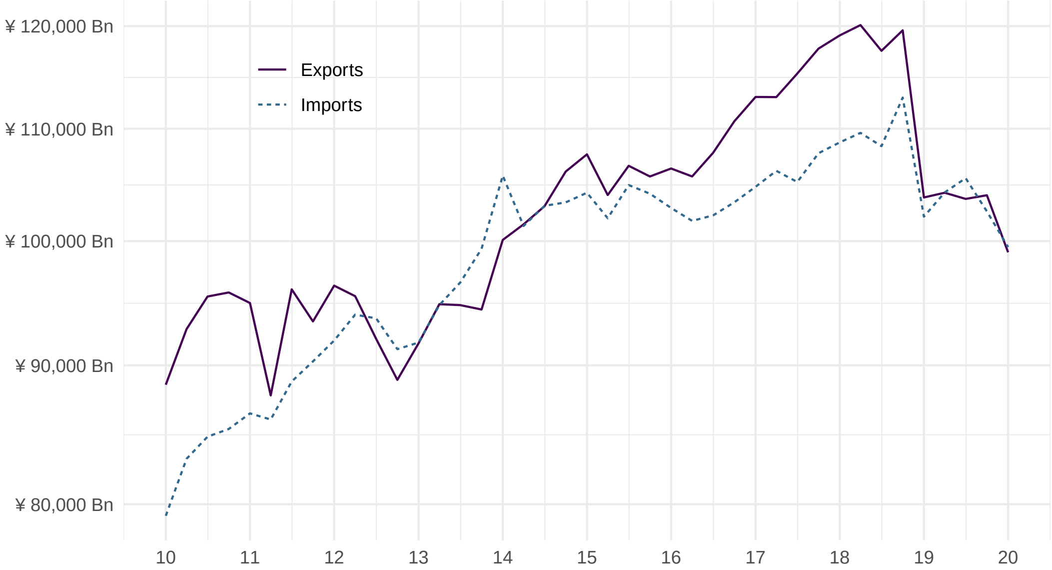
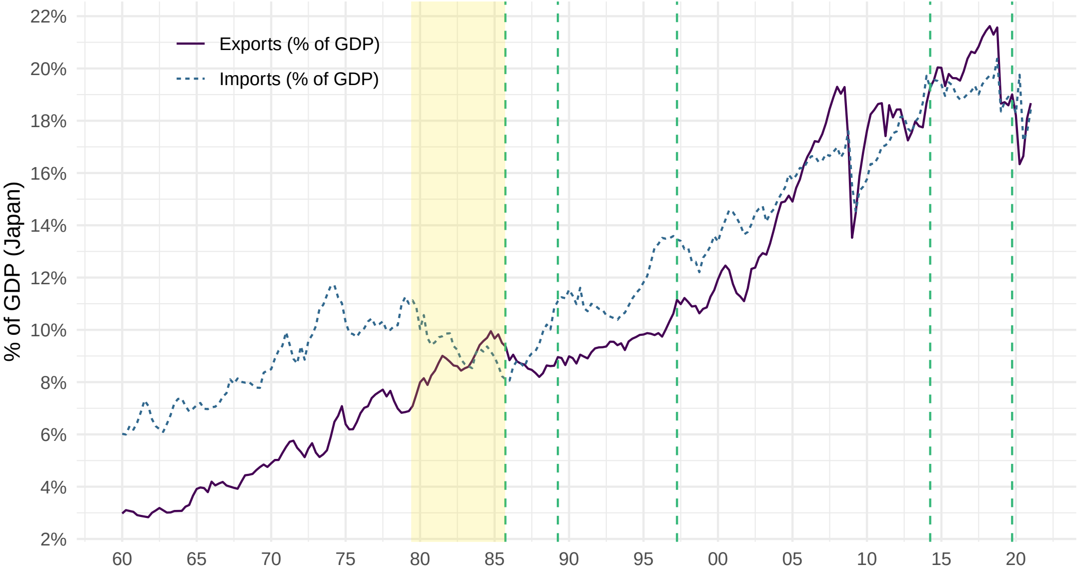
Japan: 2010-2020



Japan Exchange Rates



Japan: Abenomics



Section 4

European Debt Crisis: 2011-13 Mistake

Trichet defends ECB rate increase

George Osborne + Add to myFT

Trichet defends ECB rate increase

FT reporters APRIL 7, 2011

The European Central Bank president has defended a rise in official interest rates as good for the whole eurozone even as preparations began for a bail-out of Portugal, the latest victim of the region's debt crisis.

Trichet defends impeccable ECB record

European banks

Trichet defends 'impeccable' ECB record

Ralph Atkins in Frankfurt SEPTEMBER 8 2011

Trichet defends impeccable ECB record

Jean-Claude Trichet has vented his anger at German critics of the European Central Bank's handling of the eurozone debt crisis, saying governments had failed to shoulder their own responsibilities and his bank deserved more praise for combating inflation.

The soon-to-depart ECB president said in a speech in Frankfurt that the bank had a better record on containing inflation in Germany than the country's revered Bundesbank. "We have delivered price stability over the first 12 years of the euro – impeccably! Impeccably!"

"I would very much like to hear congratulations for an institution which has delivered price stability in Germany over almost 13 years at 1.55 per cent approximately …which is better than has been obtained in this country over the last 50 years."

An amazing mea culpa from the IMF on austerity

The Washington Post

An amazing mea culpa from the IMF's chief economist on austerity

By Howard Schneider

January 3, 2013

An amazing mea culpa from the IMF on austerity

Consider it a mea culpa submerged in a deep pool of calculus and regression analysis: The International Monetary Fund's top economist today acknowledged that the fund blew its forecasts for Greece and other European economies because it did not fully understand how government austerity efforts would undermine economic growth.

The new and highly technical paper looks again at the issue of fiscal multipliers – the impact that a rise or fall in government spending or tax collection has on a country's economic output.

That it comes under the byline of fund economic counselor and research director Olivier Blanchard is significant. Fund research is always published with the caveat that it represents the views of the researcher, not the institution itself. But this paper comes from the top, and attempts to put to rest an issue that has been at the center of debate about how fast countries should move in their efforts to tame large debts and deficits.

Independent Evaluator appointed by the ESM Board of Governors

Lessons from Financial Assistance to Greece

INDEPENDENT EVALUATION REPORT

Varoufakis and Schäuble

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# [1] "Link to the video:"
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Varoufakis' diagnosis in April 2015

- 7-year old winter of discontent
- Design faults of the eurozone. Greek's nation failings. $\Rightarrow$ monster of a crisis.
- Greece went to a period of Ponzi growth to a period of Ponzi austerity.
- A glut of savings, generalized austerity leads the EU to export its crisis to the rest of the world.

Schäuble's diagnosis

- In Europe we have good reason not to provide financial assistance without demanding something in return.
- A lot of people underestimate the problem of moral hazard.
- Debt relief would not solve any structural problem. It would only weaken the incentives to carry out reform.
- Any democratic system tends to take the more comfortable decision if you have the alternative to do so.
- Wolfgang Schäuble: the Eurozone economy is expected to post positive growth.

Tsipras VS Merkel

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# [1] "Link to the video:"
# [1] "https://www.youtube.com/watch?v=dnZsqI_Q0NQ"
# [1] "https://fgeerolf.com/econ102/handouts/macro-history.html"
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Independent Evaluator appointed by the ESM Board of Governors

Lessons from Financial Assistance to Greece

INDEPENDENT EVALUATION REPORT

Section 5

Germany

Schröder (center-left) wins over Lafontaine (left)

Context: Tony Blair elected in 1997 in the U.K.

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# [1] "Link to the video:"
# [1] "https://www.youtube.com/watch?v=cJpyks_lPhQ"
# [1] "https://fgeerolf.com/econ102/handouts/macro-history.html"
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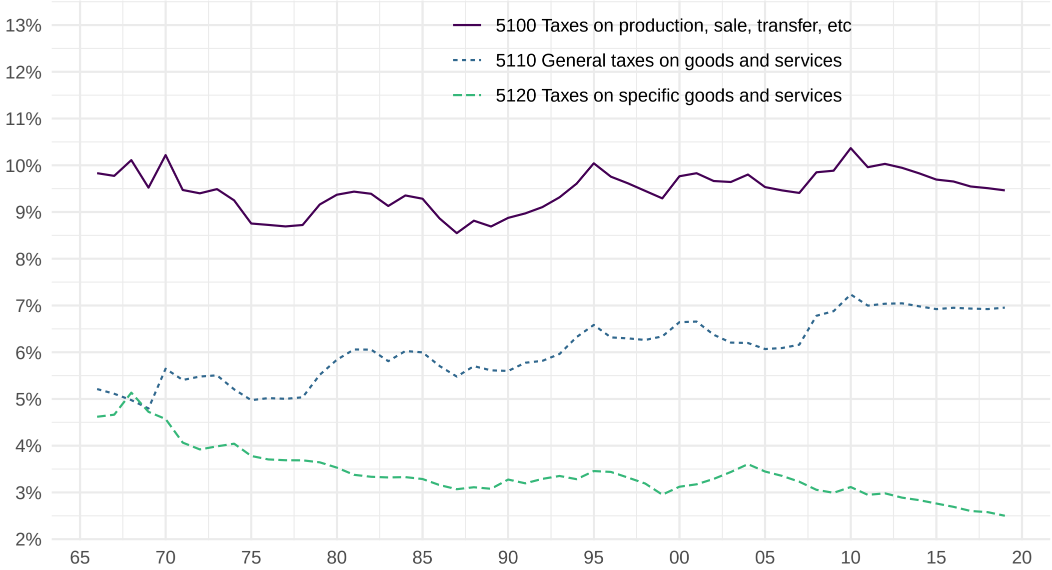
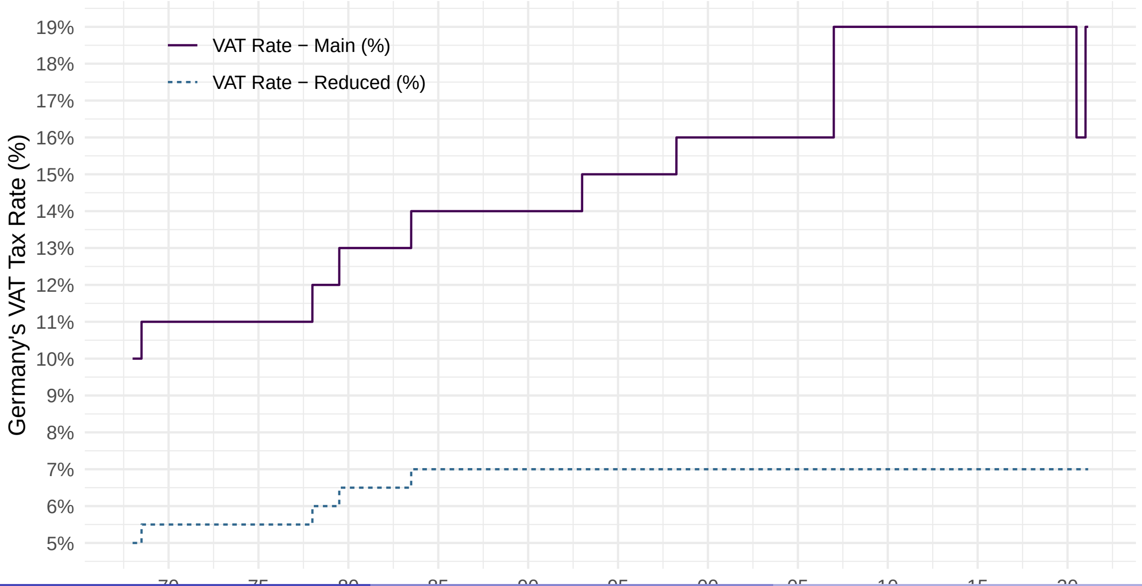
VAT Tax Increases in Germany



VAT Tax Rates in Germany

Germany		
01-01-1968	5	10
01-07-1968	5.5	11
01-01-1978	6	12
01-07-1979	6.5	13
01-07-1983	7	14
01-01-1993	7	15
01-04-1998	7	16
01-01-2007	7	19

Germany's VAT Tax Increases



Compressing Internal Demand (1998-2003)

Special

Jun 3rd 1999 edition ›

The sick man of the euro

The biggest economy in the euro area, Germany's, is in a bad way. And its ills are a main cause of the euro's own weakness

Europe

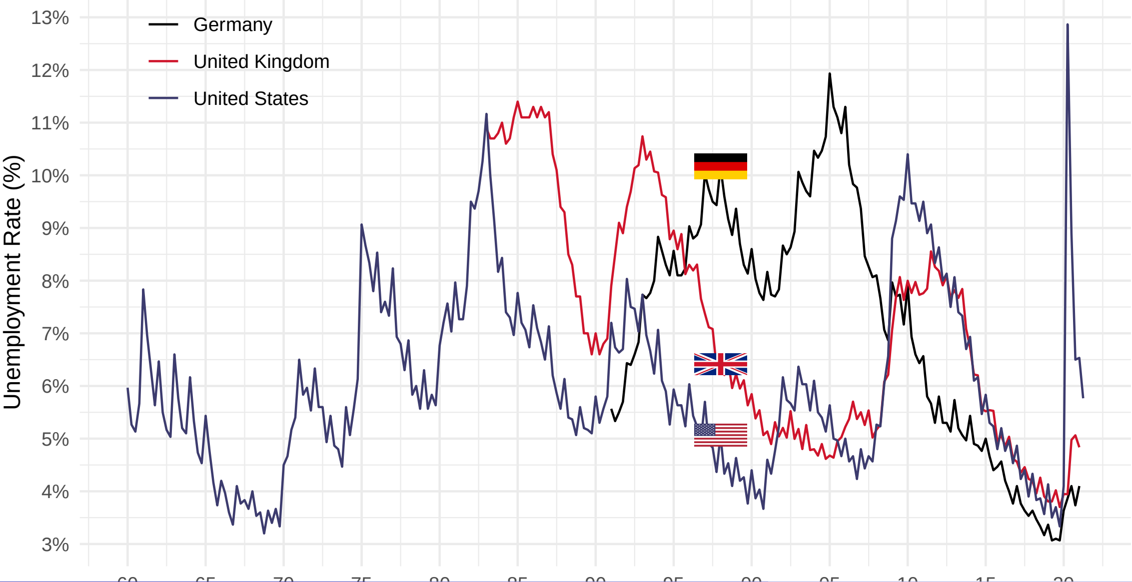
Aug 30th 2001 edition ›

Germany

Will the economy—and Gerhard Schröder—bounce back?

Germany's ebullient chancellor is still hoping that his country will avoid a

Unemployment in Germany VS UK, US



2005 VAT Tax Increase Found Puzzling

German move to raise VAT found puzzling

By Mark Landler

Nov. 15, 2005

FRANKFURT — Germany, saddled with some of the highest taxes and lowest-spending consumers in Europe, has come up with a novel approach to whip its economy into shape: increase the tax on consumption.

The new German coalition government, which will take power next week, intends to increase the value-added tax to 19 percent in 2007 from 16 percent now. The move will raise an estimated Â27 billion, or $31 billion, which the government plans to use primarily to whittle down its huge budget deficit.

2010 - G20

WORLD

Merkel wins trade surplus duel with Obama at G20

Exporters like Germany and China have won through in a battle of wills with President Barack Obama. The cap on trade surpluses and deficits desired by the US will not be imposed at Seoul's G20 summit, Merkel has said.

Hands off our trade surplus

Hands off our trade surplus, 'stingy' Germans tell US

By Stephen Evans
BBC News, Berlin

9 November 2010

2017 - The German Problem

The Economist

Hard truths about North Korea

The sad decline of the summer job

What comes after Mosul falls?

A special report on the young old

JULY 8TH–14TH 2017

The German problem

Why its surplus is damaging the world economy

2017 - The German Problem

Leaders

The Economist July 8th 2017 9

The German problem

Why Germany's current-account surplus is bad for the world economy

THE battle-lines are drawn. When the world's big trading nations convene this week at a G20 summit in Hamburg, the stage is set for a clash between a protectionist America and a free-trading Germany.

President Donald Trump has already pulled out of one trade pact, the Trans-Pacific Partnership, and demanded the renegotiation of another, the North American Free-Trade Agreement. He is weighing whether to impose tariffs on steel imports into America, a move that poused by Mr Trump. Germany has not entirely escaped this, but it has held on to more of the sorts of blue-collar jobs that America grieves for. This is one reason why the populist AfD party remains on the fringes of German politics.

But the adverse side-effects of the model are increasingly evident. It has left the German economy and global trade perilously unbalanced. Pay restraint means less domestic spending and fewer imports. Consumer spending has dropped to just 54% of GDP, compared with 69% in America and 65% in Britain. Exporters do not invest their windfall profits at home. And Germany is not alone; Sweden, Switzerland, Denmark and the Netherlands have been piling up big surpluses, too.

Germany's trade surplus is a problem

Tilford (2019): Germany is an economic masochist

Germany Is an Economic Masochist

Europe's biggest economy could easily stop its own slide into long-term stagnation—but it would prefer not to.

By **Simon Tilford**

AUGUST 21, 2019, 5:31 AM

An economic miracle ?

For much of the last 10 years, Germany has been lauded for its successful adjustment to globalization, its sound management of public finances, and its political stability. Some have even breathlessly talked of a new *Wirtschaftswunder* (economic miracle). Now fears are mounting that worsening global trade tensions and China's slowdown spell serious trouble for the country's export-dependent economy threatening to return the country to the "sick man of Europe" status it held in the early 2000s.

The situation is less dramatic. German's economic performance has not been as good over the last 10 years as is often claimed, but the German government could now easily take steps to boost the economy should it choose to do so. There is little to indicate that it will do enough, however, thanks to a deep-seated belief in Germany—spanning the political spectrum—that deficit spending would be counterproductive economically and unpopular politically.

Germany's export surplus

Seen over the last 10 years, the German economy has performed relatively well in comparison with similar European economies such as France and the United Kingdom, but it has done no better than the United States. Moreover, over the last 20 years, Germany has grown largely in line with other large European economies (bar Italy, which has done terribly) and on many measures less well than the United States. There has certainly been no Wirtschaftswunder.

Moreover, the German economy has become strikingly dependent on exports over this period. Germany has long tended to run a trade surplus, but never of the present magnitude. The country has averaged trade surpluses of close to 8 percent of GDP since 2005 and 6.5 percent since 2004. At close to $300 billion in 2018, the German trade surplus is easily the largest in the world. The heavily trade-orientated focus of the German economy helps explain why Germany bounced back more rapidly following the financial crisis than comparable European economies, but it also explains why Germany's prospects have turned down particularly sharply over the last 12 months as the external environment has worsened rapidly.

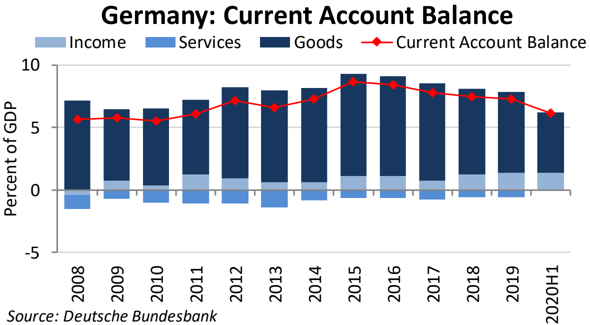
“The U.S. need to build better cars”

There is a tendency in Germany and elsewhere to talk about trade balances in terms of competitiveness, with countries with surpluses being “competitive” and those with deficits being “uncompetitive.” Indeed, in response to U.S. President Donald Trump’s criticism in 2017 of the scale of Germany’s surplus, the country’s then-Economic Minister Sigmar Gabriel—a social democrat—joked that the United States simply needed to build better cars. German economists and representatives of the economy and finance ministries also tend to throw their arms in the air and argue that Germany’s trade surplus is simply the product of private-sector decisions over which the German government has no influence. Both claims are at best misleading.

U.S. Treasury agrees with Tilford

Germany's CA Balance

Germany's large current account surplus has narrowed somewhat in 2020 as the shock to global trade has weighed on exports. The current account surplus stood at 6.8% of GDP over the four quarters through June 2020 (down from 7.2% of GDP in 2019). Nonetheless, Germany's current account surplus remains the largest in the world in nominal terms (at $253 billion over the four quarters through June 2020). While German domestic demand contributed substantially to growth from 2015-2019, helping gradually narrow the current account surplus, it was not sufficient to reduce appreciably external imbalances. There are signs, however, that the current crisis is accelerating the shift of Germany's growth composition toward domestic demand, which has held up well in recent months amid fiscal stimulus measures, compared to the precipitous drop in exports. For this shift to take hold beyond the current crisis, Germany will need to implement economic policies to address the structural factors that contribute to high domestic saving



Source: Deutsche Bundesbank

Germany's economic policies

Germany's economic policies — notably excessively tight fiscal policy emanating from high tax levels — have for many years restrained domestic consumption and investment. The measures announced in response to COVID-19, including the VAT cut and the suspension of the national fiscal rules to allow for new debt issuance, are steps in the right direction but are temporary in nature. These measures fail to address the overly conservative budget processes which have played a role in Germany's excessively tight fiscal stance. Since 2014, Germany's approved budgets have called for fiscal balance, but stronger-than-forecast revenues and under-execution of spending plans have meant that in fact fiscal surpluses have averaged 1.2% of GDP over this time period, while reaching historic records of 1.9% of GDP in 2018 before declining modestly to 1.4% of GDP last year. As the public health crisis is overcome and recovery takes hold, Germany's substantial fiscal space should be deployed through structural fiscal measures that will bolster current activity, reduce the burden of taxation — particularly through tax cuts that would lower the labor tax wedge — and reinvigorate investment, which would help external rebalancing proceed at a reasonable pace.

Trump and tarriffs

Germany's economic policies — notably excessively tight fiscal policy emanating from high tax levels — have for many years restrained domestic consumption and investment. The measures announced in response to COVID-19, including the VAT cut and the suspension of the national fiscal rules to allow for new debt issuance, are steps in the right direction but are temporary in nature. These measures fail to address the overly conservative budget processes which have played a role in Germany's excessively tight fiscal stance. Since 2014, Germany's approved budgets have called for fiscal balance, but stronger-than-forecast revenues and under-execution of spending plans have meant that in fact fiscal surpluses have averaged 1.2% of GDP over this time period, while reaching historic records of 1.9% of GDP in 2018 before declining modestly to 1.4% of GDP last year. As the public health crisis is overcome and recovery takes hold, Germany's substantial fiscal space should be deployed through structural fiscal measures that will bolster current activity, reduce the burden of taxation — particularly through tax cuts that would lower the labor tax wedge — and reinvigorate investment, which would help external rebalancing proceed at a reasonable pace.