Ideas, Interests, and the Balance of Payments

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Abstract: Financial activity, particularly the lending of money and taking on debt, have long been subject to cultural taboos. This paper argues that we should anticipate greater willingness to borrow where this taboo has eroded more completely; conversely, we should expect higher savings and less borrowing where the legacy of finance-critical and anti-debt norms remain stronger. The differential erosion of the debt taboo should therefore be expected to exacerbate macroeconomic imbalances, with serious consequences for international political-economic relations. This constitutes a mechanism by which ideas – in addition to conventional accounts of materially self-interested behavior – can exert influence over significant political economic outcomes.

Keywords: International Political Economy, Debt, Financial Markets, Ideas, Macroeconomics

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Divergent economic ideas are crucial to explaining cross-national differences in economic preferences and outcomes. These ideas can concern how an economy functions: someone who accepts the inflation-unemployment trade-off will likely arrive at different policy conclusions than someone who rejects it. They can also concern norms, with certain actions morally proscribed for some but not for others. They can also concern interpretations of national interests: a mercantilist understanding of the national interest might prioritize exports while a more financialized understanding of national interests would focus more on bank-friendly regulation.

This paper is focused on ideas surrounding *debt* – how it works, whether it is regarded as shameful, and what role it plays in serving 'the national interest.' Debt sits at the center of domestic and international politics, feeding into fundamental debates over spending, investment, and the negotiation of financial crises. More than that, divergent ideas on the topic of debt help to explain the emergence of persistent imbalances in states' Balance of Payments (BoP). Such an explanation is both practically and theoretically important: such imbalances have become increasingly politicized, even as they run contrary to the mainstream economic expectation that BoP imbalances should generally resolve themselves.

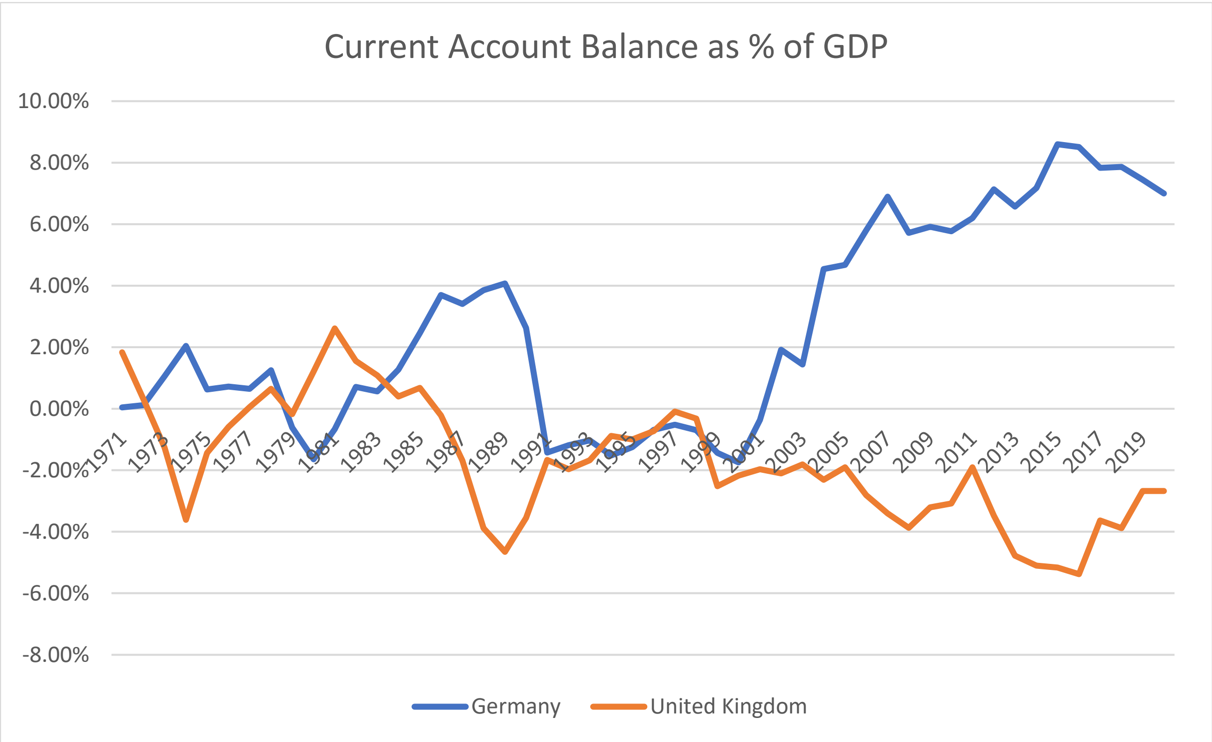

Figure 1: World Bank WDI Database

In short, this paper argues that ideas about debt – especially as captured in debates over 'good' versus 'bad' economic policy – generate larger and more persistent macroeconomic imbalances like the one seen in figure one above.

In order to make this argument, several steps are necessary: First, we need to address the debate within International Relations (IR) – and specifically International Political Economy (IPE) – over whether ideas can exert causal force over economic policy outcomes. Second, we must establish the theory supporting the notion that ideas surrounding debt should specifically be expected to exert influence over BoP outcomes. The paper addresses these steps in the two following sections, with the third assessing evidence that such a theoretical mechanism is actually at work in the real world. The final section concludes.

I: Ideas as Causes

The notion that ideas exert influence over behaviors and outcomes is uncontroversial in most social sciences. Even in economics, home of the perfectly rational and materially motivated *homo economicus*¸ the understanding of human decision-making has been substantially revised to account for insights from cognitive psychology. However, despite the tradition of political scientists following economists' methodological lead, a hard core of holdouts still arguably dominates American IPE. These scholars assert that a disciplinary consensus exists on "theories, methods, analytical frameworks, and important questions" which leaves little room for norms, identity, and ideas (Frieden and Martin 2003, 118). The outsized influence of the US in academia amplifies this group's power. Consequently, much of the early-21st century ideas-driven IPE scholarship has felt the need to justify itself against the hegemony of materialist theories and approaches (Berman 2001; Parsons 2002; Abdelal, Blyth, and Parsons 2010) – though this has arguably changed in the past decade (Parsons 2016).

It is important to distinguish between what I will call "strong" and "weak" forms of ideational importance. The strong form – often described as interpretivism – asserts that ideas effectively define subjective reality, making it impossible to appeal to any objective reality untainted by human interpretation. From this perspective, human action cannot be understood without examining how we interpret the world around us and cast ourselves into roles in relation to others. Even the scholar is not immune, meaning that academics are engaged in interpreting how others interpret the world around them. I call this a "strong" expression of ideational importance because it rejects the need to establish causality altogether, instead focusing more on understanding how intersubjective interpretation imbues the world with the appearance of order. The "weak" account of ideational importance – heavily influenced in IPE by the work of Peter Hall (1993) and Craig Parsons (2002) – diverges less from conventional IPE. This approach still seeks to explain the causal effect between independent and dependent variables; however, it argues that ideas, norms, and identity are often very important variables indeed. In other words, weak-form ideational accounts are still broadly positivist in orientation.

Despite being sympathetic to strong-form ideational arguments, this paper sticks closer to the weak form of ideational scholarship. Following Sheri Berman (2001), it is focused on the task of explaining how particular ideas have become politically significant, become embedded in national institutions, and driven political-economic outcomes. Parsons (2016) identifies four key mechanisms by which ideas can gain this sort of power: (1) through motivating powerful individuals to take a course of action, (2) by generating new choices that clearly contrast with prescriptions generated by existing ideas, (3) by generating new political coalitions from previously disparate actors, or (4) by defining the nature and purpose of institutions.

Hall's (1993) examination of paradigmatic change in economic policy is a seminal early account of how ideas, rather than material interests or pluralistic bargaining, best account for Britain's shift from Keynesian to monetarist policymaking. Johannes Lindvall (2006) followed two decades later with a similar account of why Keynesianism survived longer in Sweden. Parsons' own (2002) work articulates how the emergence of the European Economic Community was neither a function of path dependence nor an inevitable result of material interest calculations, but a function of a new "ideology of integration" that took precedence over other possible approaches to European cooperation. Jeffrey Chwieroth (2007a; 2007b; 2008; 2015) runs a veritable cottage industry examining the role of ideology within the International Monetary Fund, particularly concerning capital controls – as well as arguing that the late-20th century burst of international financial liberalization in emerging markets was driven by an ideologically coherent group of American-trained neoliberal economists. It is also worth noting that some scholars operating in the more classical and holistic tradition of IPE accept the causal force of ideas without ever making that position explicit or linking it to a systemic methodology (consider, for instance, the idea of false consciousness).

Particularly useful for the purposes of this paper are Rawi Abdelal, Mark Blyth, and Parsons (2010) notion of different ideational "logics" or "paths" behind the construction of the global economy. Ideas surrounding debt follow the "path of meaning" by shaping our shared understanding of how debt works and what actions with respect to debt are legitimate; they follow the "path of cognition" by functioning as heuristic cognitive short-cuts reducing pressure to critically examine conventional wisdom; they follow the "path of uncertainty" when they drive responses to financial crises; and they follow the "path of subjectivity" by defining the social identities of debtors and creditors. These statements are currently vague. However, having established how ideas have generally been integrated into causal accounts within IPE, we can now turn to more concrete identification of how ideas surrounding debt follow these "paths" in shaping global economic outcomes.

II: Debt and Macroeconomic Imbalances

Most IPE approaches to debt that already take ideas seriously are domestic in orientation. The most noteworthy of these is arguably Blyth's (2013) *Austerity: The History of a Dangerous Idea.* In it, Blyth argues that much of the conventional wisdom on sovereign debt – namely, that government over-borrowing is economically ruinous and should be unwound through fiscal retrenchment – is less objectively true than it is the product of normative hostility toward government debt fostered by influential economic narratives. Puzzlingly, however, appeals to austerity are also popular among those who stand to suffer most from such policies (Stanley 2014) – a topic we will return to in the next section. In contrast to these works focused on domestic outcomes, we are particularly interested here in how ideas about debt affect a state's *international* economic situation, as captured in the BoP.

The BoP is effectively a record of all payments into and out of an economic system. Using a very simple BoP model, in which the current account is reducible to the trade balance and the financial account reducible to savings and investment, the two accounts are related as follows:

$$\textit{Savings} - \textit{Investment} = \textit{Exports} - \textit{Imports}$$

Here, "investment" is a somewhat confusing term: it does not mean financial investment (e.g., buying stocks, bonds, and other financial products). In fact, those activities are actually considered *savings* in macroeconomic parlance. Rather, investment refers to spending on capital (e.g., building new factories, technological improvements, etc). Reflecting longstanding assumptions within mainstream macroeconomics that borrowing exists almost exclusively for the purpose of creating new productive capital (Schumpeter 1983; King and Levine 1993), investment is operationalized in a way that makes it impossible to disentangle from *borrowing*. Replacing investment with borrowing in the identity, the model still holds – and is arguably more reflective of the real world of the early 21st century. For instance, household borrowing in support of consumption is not investment; however, it must be included as a negative on the left-hand side of the identity for it to balance.

Some of the implications of this identity are more intuitive than others. The most intuitive case concerns situations where imports are greater than exports (i.e., a trade deficit). This makes the right side of the identity negative; necessitating a negative on the left side as well. Put in language, when spending on foreign goods is higher than sales to foreign buyers, the country in question will experience a shortfall of foreign exchange. The only way to maintain such an imbalance is to borrow the foreign exchange needed to cover the trade deficit. This describes the increasingly typical situation in the United Kingdom, as well as Europe's crisis-stricken debtors during the eurozone crisis. It is important to note, however, that this definition of the situation implicitly starts on the current account side, with the financial account forced to adjust (i.e., the current account clears "first") However, a negative on the left-hand side of the identity can also force an adjustment: sudden surges of capital inflows can drive down interest rates and encourage spending booms, driving up imports relative to exports. As before, both sides of the identity remain negative – the difference is that the financial (left) side of the identity conceptually moves first (Fuller 2018).

What about the opposite case, where exports exceed imports and savings are higher than investment? That is the situation faced by so-called "surplus" countries like Germany, the Netherlands, or Japan. In these cases, both sides of the identity are positive. As with a deficit, explanations of surplus situations can start on either the goods or financial side: for countries that export much more than they import, they will have excess savings to place in financial markets. Alternatively, starting on the financial side of the equation, economies that save more than they borrow will have relatively low demand for imports relative to exports. In both cases, a positive for one account pushes the other toward positive as well.

A common mistake when discussing the BoP is to assume that it reflects the actions of national governments. In fact, the BoP encompasses *all* transactions crossing a recognized international border – albeit with serious caveats about the data's accuracy (Linsi and Mügge 2019). While a government deficit can often encourage a current account deficit (so-called "twin deficits), they are not the same thing. And, indeed, it is possible for a government in deficit to run a BoP surplus due to actions in the private sector (as is currently the case in the Netherlands and Germany).

In mainstream economic theory, there is a longstanding assumption that economic systems tend to alternate between surpluses and deficits: a country that borrows foreign exchange in time period t should invest their borrowed funds in ways that allow them to accumulate more foreign exchange in time period $t+1$. This view of the BoP is built on the notion of intertemporal trade: a current account surplus indicates that a country is consuming less now (in period t) so that it can consume more in the future. Conversely, a current account deficit indicates that a country is consuming more in period t – at the cost of paying back debts and consuming less at $t+1$ (Krugman and Obstfeld 2006). The notion of an automatically rebalancing BoP goes back further, to David Hume's (1742) *specie-flow* mechanism, which illustrated the impossibility of a country maintaining a permanent trade surplus.

Hume's intervention remains relevant because the target of his critique has not actually disappeared. Hume was motivated to reject the central policy goal of mercantilism – the accumulation of precious metals through exporting more than one imported – as ultimately self-defeating. While international trade and financial relations have changed a great deal since the 18th century, the notion that current account surpluses are superior to current account deficits remains deeply entrenched in many legislatures and state houses. An economic system where actors value savings and are suspicious of borrowing should be biased surpluses – both of exports over imports and savings over borrowing. This is arguably clearest in the case of Germany, which has pushed the normative virtues of current account surpluses to a "wacky" extent that seemingly misunderstands that surpluses cannot exist without matching deficits (Wolf 2013; Münchau 2014; Jacoby 2020). This neo-mercantilist approach to the BoP contrasts with a more financialized perspective based on the notion that innovative and deep financial markets are desirable – a relatively recent innovation in economic thinking. In short: divergent policy approaches to debt and borrowing – rooted in different concepts of appropriate economic policy – inevitably affect the balance of payments. More than that, sustained differences between national approaches to borrowing will make BoP imbalances stickier.

This dynamic has appeared in several IPE debates. Most noteworthy of these is the early-21st century analyses of the growing interdependence between the United States and China – sometimes known as "Chimerica," whereby Chinese export revenues were saved in the United States, further fueling American imports of Chinese goods (Ferguson and Schularick 2007) Richard Cooper's (2008) explanation for this interdependence effectively focused on the identity presented above, explaining the Chimerica dynamic by pointing to (a) the Chinese desire to save their export revenues in more attractive American markets and, and (b) the relatively large American appetite for taking on new liabilities. Rather than US trade deficits (solely) reflecting poor export performance or dependence on cheap Chinese goods, they were also generated by the glittering appeal of American financial markets to Chinese savers.

This relatively benign view of the two countries' growing interdependence was at the heart of a number of debates. A big question was whether the growing polarization between American trade deficits (and capital inflows) and Chinese trade surpluses (and capital outflows) were natural and desirable, or indicative of policy mistakes. For Cooper, it was more the former. Maurice Obstfeld and Kenneth Rogoff (2009) supported the latter viewpoint. In sum, the Chimerica situation was an early instance of the central problem under examination here: the emergence of large and persistent BoP imbalances.

However, where observers like Cooper were willing to point to net savings (i.e., savings minus borrowing) behaviors as a major driver of those imbalance, there was substantially less examination of what generated those behaviors in the first place. This is partly because the material drivers of divergent Sino-American views on borrowing were fairly self-evident: China's poorly developed welfare state encouraged high savings and its growth model relied on exports; the US embraced cheaper Chinese imports and provided those exporters with the financial services and products to store their gains. At least in the short-term, the Chimerica construction very plausibly served the interest of both parties. From the vantage point of 2022, however – and particularly looking back on years of financial crisis and associated discord in Europe – the notion that increasingly sticky and large BoP imbalances serve national interests is more questionable.

III: A Plausible Ideas-Driven Account

It seems difficult to dispute that societal willingness to borrow should affect a state's BoP. Moreover, *divergent* approaches to debt can result in larger, more persistent imbalances between economic systems. The rest of the paper addresses a hypothesis concerning these observations:

While material interests do play a role in the determination of macroeconomic imbalances, divergent ideas on the appropriate ends of national economic policy (i.e., the discursive construction of "national interests"), specifically on the role of indebtedness in pursuing those ends, must be included in any account of the growth and increased stickiness of global macroeconomic imbalances.

I do not pretend that it is possible to definitively assess this hypothesis here. We will discuss the key data that would be helpful in making such an assessment; however, the immediate goal is to offer an initial assessment of whether the hypothesis holds promise – and to identify what we need in order to provide a clearer assessment.

The Debt Taboo

Debt, in many cultures and over many time periods, has been seen as ethically suspect. This idea is and has been deeply embedded in a wide variety of cultural and intellectual traditions. The oldest continuously held attitudes toward debt are rooted in religion. This antipathy toward financial activity is arguably strongest - and particularly problematic - in the Judeo-Christian tradition. In the Old Testament, interest is forbidden on loans between Jewish people (Exodus 22:24), while, in the New Testament, Jesus famously evicts moneylenders from the temple, pointedly describing them as "thieves" (Matthew 21:13). In Christianity, these attitudes persisted through the early capitalist era, with injunctions against usury - either the charging of interest or the charging of unreasonable interest - routinely reinforced by papal encyclicals and ecumenical councils. In Islam, the rejection of usury (*Riba*) has persisted more strongly into the present day, with contemporary Islamic finance still built around normative skepticism toward the charging of interest.

The evolution of the Jewish community's involvement in finance is more tragic. Historically excluded from mainstream European society, Jewish communities were forced to specialize in relatively marginalized professions - including the ostensibly tawdry business of moneylending. As the economic importance of finance grew with economic changes, the normative hostility toward finance combined with the social exclusion of Jewish communities fostered a virulent strain of antisemitism (D'Acunto, Prokopczuk, and Weber 2019; Max and Uhl 2021). Many of the tropes that resulted - the depiction of Jews as possessing secret behind-the-scenes power, often concentrated in banking groups such as the Rothschilds - remain politically active to this day. If it is taken as given that financial activities are sinful, then it would seem wise to avoid becoming indebted to those who engage in the lending business.

The picture in other religions is somewhat more mixed. Confucianism is similarly hostile to debt, though its stance is directed more toward debtors than creditors, emerging from a strong normative emphasis on thrift (Zhao 2013). On the other hand, Buddhism tends toward a friendlier stance, since merchants and financiers generally funded the monastic orders (Caring-Lobel 2015).

Especially within the western tradition, this thick vein of suspicion toward finance persists. This persistence can take symbolic forms that usually pass beneath conscious awareness: the etymology of the word "debt" in Germanic languages is very similar to words related to guilt. However, much of the antipathy toward debt remains explicit and, surprisingly, commonly held across much of the ideational spectrum. Anarchist and Anthropologist David Graeber (2012) and Nobel Laureate in Economics James M. Buchanan (1985) presumably would not have agreed on much. But one thing they did agree on was that debt is normatively undesirable. Graeber referred to debt as slavery, while Buchanan's views are arguably more surprising and interesting. In his essay on the *Moral Dimension of Debt*, Buchanan lays out a norm-based worldview that could easily come from contemporary ideational political economy. He describes rising levels of indebtedness during the 20th century as resulting from “an erosion of previously-existing moral constraints” championed by the “revolutionary” John Maynard Keynes, who pursued “the destruction of fiscal morality.” The moral dimension of debt is arguably most on display in the construction of bankruptcy regimes, in which insufficiently punishing debt resolution systems are considered a “moral hazard.”

Diverging Ideas on Debt

Without opining on the specific moral attitude presented by Buchanan, his contention that culturally embedded ideas concerning borrowing manifestly affect policy attitudes on debt is sustained by empirical work. The idea that financial activity operates on questionable ethical norms – and that excessive reliance on debt constitutes a moral failing (or ‘moral hazard’) – sits at the heart of the paradoxical appeal of austerity measures.

Even those who do not benefit from austerity tend to recognize the ‘common sense’ logic of austerity and are willing to support it politically. This appears based on the position that, if someone has borrowed too much, they must promptly pay back what they owe (Stanley 2014; Hopkin and Rosamond 2018). On both the creditor and debtor sides of the 2010s eurozone crisis, media tended to present a common narrative of overborrowing and the need for fiscal retrenchment (Kaiser and Kleinen-von Königslöw 2017). Similarly, religiosity and adherence to religious norms has been revealed to affect corporate financing decisions (Cai and Shi 2019) while normative viewpoints on debt appear to correlate with actual levels of indebtedness within Sweden (Almenberg et al. 2021). Perhaps most disturbingly, households in countries with higher levels of historical antisemitism continue to shun borrowing and save (especially outside the financial system) at higher rates than households where historical antisemitism was weaker (D’Acunto, Prokopczuk, and Weber 2019). All of these arguments agree on one point: ideas about the appropriacy of debt matter in determining debt-related behavior.

If that is true, different ideas should be expected to generate different behavioral outcomes – which brings us back to the balance of payments. We should anticipate greater willingness to borrow where Buchanan’s “fiscal morality” has eroded more completely, pushing economies toward current account deficit / net borrower positions on the BoP. Conversely, we should expect higher savings and less borrowing where the legacy of finance-critical and anti-debt norms remain stronger.

Anecdotally, this divergence is most readily apparent between English-speaking Anglo-American economies and German-speaking continental economies. While Buchanan might point the finger at Keynes as the harbinger of moral destruction on the issue of debt, another potential candidate would be Alan Greenspan. Greenspan, in his role as the avatar of late-20th century financial innovation, saw innovative financial markets as a mechanism for eliminating a range of socio-economic ills, including the business cycle. This faith in smarter borrowing – in the form of derivative tools such as mortgage-backed securities – posited that the moral problems associated with debt could be transcended through financial engineering (Greenspan 2000). This contrasts sharply with the explicit political appeals to the wisdom of savings, such as former German Chancellor Angela Merkel's repeated appeals to the positive example of the frugal "Swabian housewife" (Kollewe 2012). As an archetype, the Swabian housewife demonstrates her goodness by saving rather than spending, which is then taken as the appropriate behavior for a state as well as an individual.

A national system operating on a Greenspan-ian understanding of finance and another operating on the long-entrenched cultural assumption that fiscal restraint is desirable will exert strong pressure on one another to expand their BoP imbalances. The big savers need places to put their funds abroad; the big borrowers borrow to generate the assets sold to the savers. So how do countries end up on team Greenspan versus team Swabia? Here, grounds for serious disagreement remain.

The "How Much" Problem and the National Interest

We possess a puzzle: the emergence of growing and increasingly persistent BoP imbalances. We also possess multiple theoretically plausible explanations for those imbalances. The key question – and one we cannot directly address here – is whether the divergence between economic postures emanates from ideas versus ostensibly rational self-interest. This is the "how much" question: it seems impossible to argue that ideas concerning the appropriacy of debt do not play a role in debt-related behavior. But it is equally implausible to maintain that that material interests play no role at all.

Comparative Political Economy, building off heuristics such as the *Varieties of Capitalism*, can easily argue that Germany's older demographics – combined with its institutional comparative advantage in macroeconomic coordination – *should* bias the country towards being net savers and exporters (c.f. Bonatti and Fracasso 2013; Donnelly 2014; Hall 2014; Iversen, Soskice, and Hope 2016; Frieden and Walter 2017; Dooley 2019; Dold and Krieger 2019). At the same time, the inability of Anglo-American liberal systems to coordinate in the same way gives them an advantage in the production of liquid and lightly regulated financial markets. Again, this should theoretically bias such liberal systems towards the sale of financial products (i.e., borrowing) and higher levels of consumption from abroad.

The problem with such a simple materialist argument is that it breaks down at different levels of analysis. While it may be that a policy of pursuing real exchange rate compression benefits large parts of the German economy, for instance, it is much harder to argue that such a policy benefits all Germans (let alone benefits them to an equal extent). Even in countries like the UK, where the debt taboo has eroded more, it can be politically advantageous to appeal to austerity – *even among communities who most directly suffer from austerity measures*. Rather than simply supporting economic policies that benefit them, people seem to respond to economic policies that are framed as being in 'the national interest.'

It is difficult to discuss IR's approach to national interests without engaging in taxonomic exercises that outline how different types of scholars understand the concept in divergent and often mutually exclusive ways (Frankel 1970; Burchill 2005). Even very general formulations are problematic: Joseph Nye (1999, 23) attempted to define the national interest as "shared priorities regarding relations with the rest of the world," whether regarding national security, human rights, or economic interests. Yet this still assumes that such priorities are shared in the first place.

So why engage with the concept of the national interest at all? As we have seen in debates over savings, rhetorically framing a set of behaviors as supporting (or opposing) the national interest can be a powerful political tool. Indeed, the very idea of national interests emerged alongside the nation-state as a form of political organization, with the latter charged with protecting the former (Beard 1934). Declaring an outcome or course of action to be in the national interest functions like claiming the approval of "science" (or God): it delineates between good/appropriate and bad/inappropriate (Jackson 2016). Explicit appeals to the national interest – such as Donald Trump's "America First" campaign slogan – ennoble those who agree while implying that anyone who disagrees is *opposed* to the national interest.

While we may not be able to arrive at any consensus on what a nation's interests are – nor whether they exist as a fact beyond human interpretation – it should be possible to agree that rhetorically appealing to the national interest can mobilize political support. Promoting a specific ideational formulation of national interests acts as an easily digestible heuristic device, sorting preferences and goals into normative categories. As Winfried Kretschmann, the Green premier of Baden-Württemberg, described the Swabian housewife: "she is a cliché, but much more than a cliché… the Swabian housewife represents the starting point" of German economic thinking (The Economist 2014, para. 2) (The Economist 2014, para. 2). The construction of collective interests – the imperative to prioritize frugality and avoid indebtedness – essentially trumps individual self-interest.

NB: For EUSA (and RUG) readers: this is where I am not clear myself on what sort of additional evidence should be presented. The practical issue is discussed below.

IV: Conclusion

The largest problem isolating ideational effects in the determination of macroeconomic imbalances is the lack of data. At best, we need is extensive survey data that probes individual attitudes toward debt and how they are subjectively justified. A wide cross-section, encompassing significant numbers of individuals within different economies *for* several economies is necessary. Such data is not routinely collected, necessitating a specific effort.

However, even with this hypothetical survey data in hand, we still have a fundamental question: do ideas about the appropriacy of economic behavior shape the definition of material self-interest? Or do people reverse-engineer their norms from what they consider in their material self-interest? In reality, the answer is overwhelmingly likely to be “both” – and in ways that are highly sensitive to idiosyncratic forces. In other words, some political actors may be better than others at convincing individuals that a policy stance which works against an individual’s self-interest in the short run will serve their interests over the long haul. One consequence of this limitation means that any data collected must be forward-looking – asking about how people viewed debt in the past is likely to be colored by how their attitudes played out. Even so, we must also be able to interrogate the *reasons* behind expressed preferences, rather than simply the preferences themselves.

While such a project would certainly be challenging, one of the motivating factors behind this paper is to argue that is nevertheless necessary. This is because (a) it seems highly implausible that ideational factors do not contribute to macroeconomic imbalances, and (b) those imbalances are profoundly *important.*

The Balance of Payments is one of the most important constraints on state action. If an economic system does not produce something on its own, it must be able to buy those things from abroad. Being able to buy anything abroad in this way necessitates access to payment inflows that are equivalent to payment outflows. If a state has no access to foreign exchange, it simply cannot buy what it wants to buy. Where imports are necessary to maintain the fundamental material needs of a populace, simply going without may not be possible – at least not without taking a North Korean-style path to famine. This hard constraint is why states generally end up accepting strings-attached assistance from bodies like the IMF or European Stability Mechanism.

This vulnerability means that it is exceedingly important for states to avoid crisis-driven “hard landing” BoP adjustments. Such adjustments are not only dangerous for deficit states (for instance, Greece) – they are also costly and politically dangerous to surplus states (such as Germany). Moreover, a hard landing in one part of an integrated political space can force adjustments in partner states, as financial market participants look to avoid being exposed to the next site of crisis. Indeed, the eurozone is arguably the area where these issues are most important. While the United States’ monetary system includes permanently unbalanced internal BoPs, they are never subject to political activation and are unlikely to require settlement (short of a national disintegration). Conversely, the eurozone still operates on the expectation that extant imbalances will be settled. And those settlements have profound distributional implications, it becomes more important to understand where the underlying imbalances come from in the first place.

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