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“International Investors, the U.S. Current Account, and the Dollar”  
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Two main forces lie behind the large U.S. current account deficits: an increase in U.S. demand for foreign goods and an increase in foreign demand for U.S. assets. Both have contributed to steadily increasing current account deficits since the mid-1990s, accompanied by a real dollar appreciation until late 2001 and a real depreciation since, which accelerated in late 2004. This paper explores whether and how much more depreciation is to come, and against which currencies: the euro, the yen, or the renminbi. The paper develops a simple model of exchange rate and current account determination based on imperfect substitutability in both goods and asset markets and uses that model to interpret the past and explore alternative future scenarios. The paper concludes that substantially more depreciation is to come, surely against the yen and the renminbi, and probably against the euro.

JEL codes: F11, F32, F41