

forms to its banking system were sufficiently advanced, the timing of which remained uncertain.⁴

As regards the US domestic savings-investment imbalance which has been exacerbated by the expansion of the US fiscal deficit and which has increasingly come to be seen as to blame for the external imbalance, it was noted that there is a general expectation of some improvement with robust global economic growth reducing the cyclical component in the near term and the Administration having announced a program of fiscal consolidation to reduce the structural component in the medium term.

However, it was suggested, the so-called "twin deficit" issue has not generated a sense of urgency in Washington.⁵ In part, this reflects consideration of the context in which the US current account deficit originated: some two-thirds of the external deficit was built up during the late 1990s at a time when the US was going into fiscal surplus. This was a period of high growth in US productivity and of the US economy overall, while slow growth in continental Europe and Japan weakened external demand for US exports. This suggested that cyclical factors were primarily responsible. And since the expansion of the external and fiscal deficits has *not* led to rising longer-term interest rates, typically a symptom of investor unease, the more compelling case to some analysts is that the external deficit reflects the attractiveness of the United States to foreign capital—in other words, the US capital account surplus is driving the current account deficit. Moreover, insofar as there *is* a real fiscal problem in the United States, it was thought to lie in the longer term as

⁴ Editors' note: On 21 July, 2005, China announced that its currency, the renminbi (RMB), would no longer be pegged to the US dollar, but would float against a basket of currencies. The initial revaluation of the RMB by 2.1 percent from 8.28 to 8.11 was not however followed by further significant changes in its parity; the RMB traded at 8.09 to the US dollar in mid-October.

⁵ In fiscal year 2004, the US federal government deficit, inclusive of social security, amounted to US\$412.1 billion or 3.5 percent of 2004 US GDP of US\$11,733.5 billion; the current account deficit in calendar year 2004 amounted to US\$665.9 billion or 5.7 percent of GDP. Source: Congressional Budget Office and US Bureau of Economic Analysis.