Research Working Papers

Uninsurable Income Risk and the Welfare Effects of Reducing Global Imbalances

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Encouraging savings in debtor economies can help balance their current accounts while raising wages globally.

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We highlight the welfare effect of policies that balance global current accounts when households face uninsurable income risk and borrowing constraints. Subsidizing savings in debtor economies reduces current account imbalances and raises the welfare of almost all citizens by increasing world capital, raising wages, and improving insurance for low-wealth households. The same balancing of current accounts is achieved by taxing savings in lender economies; however, this policy hurts most households by reducing global capital. These results suggest that balancing global imbalances may be a positive byproduct of raising investment rates, especially in debtor countries.

JEL Classifications: E2, E44, F32, F36, F4

Article Citations

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Related Research

- Dávila, Julio, Jay H. Hong, Per Krusell, and José Víctor Ríos-Rull. 2012. "Constrained Efficiency in the Neoclassical Growth Model with Uninsurable Idiosyncratic Shocks." *Econometrica*, vol. 80, no. 6, pp. 2431–2467. Available at https://doi.org/10.3982/ECTA5989.

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