POLICY NOTE

GLOBAL IMBALANCES RECONSIDERED: TOWARD FINANCIAL STABILITY AND INCLUSIVE GROWTH

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Global Imbalances Reconsidered: Toward Financial Stability and Inclusive Growth

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Abstract

Global imbalances are back at the centre of multilateral debate at the G20. While global imbalances warrant consideration and action, the current discussions remain analytically incomplete, and thus the policy guidance currently under consideration will do little to address the imbalances in the global economy. The current debate is overly focused on the trade or current account aspect of global balance sheets. The renewed debate lacks important analysis of stock imbalances, financial adjustment mechanisms, and cross-border spillovers. Capital account and related financial stability issues remain largely outside the scope of the current policy discussions. These include maturity and currency mismatches within international balance sheets, the transmission of valuation shocks through global portfolio rebalancing, and the vulnerability of Global South countries facing spillovers from disorderly adjustments in net international investment positions.

A genuinely multilateral response requires action across four areas: embedding financial stability in the rebalancing agenda; strengthening the global financial safety net through a larger, better-governed International Monetary Fund (IMF) and expanded regional arrangements; widening the supply of safe assets through Special Drawing Rights (SDRs), local-currency bond markets and Multilateral Development Banks (MDBs) instruments; and linking rebalancing explicitly to development through productive Foreign Direct Investment (FDI), improved market access, and expanded MDB lending.

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For the G20 specifically, two priorities should anchor discussions in 2026 and 2027 on this matter: strengthening the global financial safety net (GFSN) and accelerating MDB reform—making these systems not just bigger, but better. On the GFSN, this means expanding precautionary financing and reducing conditionality, alongside a larger IMF quota base, deeper embrace of capital flow management measures, and a shift toward supporting expansionary recoveries rather than forced contractionary adjustment. On MDB reform, this means further implementing the Capital Adequacy Framework recommendations, greater balance-sheet use, and capital increases, but also expanding MDB financing for structural transformation—including improving a country's balance-of-payments position. Both require a new analytical angle capturing financial spillovers, and deeper collaboration across members, so adjustment strengthens stability without compressing developing countries' growth prospects.

1. Problem Statement and Analysis

Global imbalances are once again at the center of multilateral discussion at the G20. Not since the Global Financial Crisis have imbalances received comparable attention. Following the 2009 Pittsburgh Summit, the G20 established the Mutual Assessment Process (MAP) to coordinate policies and address persistent global imbalances. Yet this framework did not deliver a sustained reduction in the major imbalances, and since 2013, the IMF has continued to flag widening current-account divergences among major economies.[1]

In 2026, the issue has moved decisively to the fore. Under the US presidency of the G20, "better understanding excessive global imbalances" has been designated as a priority area within the Growth and Deregulation Working Group. Complementing this, a Global Imbalances Study Group co-chaired by Australia and South Korea has been established, with the IMF and OECD serving as key international institutional participants.

The debate on global imbalances remains centered on the United States, China and the euro area. A genuinely multilateral response, however, must address three shortcomings in the current approach: the prevailing framework is analytically incomplete, existing policy responses are narrowly focused on trade, and the implications for developing economies are largely absent from the discussion.

1.1 The Dominant Narrative: Trade and Macroeconomic Accounting

The prevailing analytical framework treats global imbalances primarily as a problem of excessive current account surpluses and deficits. Both the IMF and OECD review these imbalances through two complementary lenses: flow imbalances—reflected in current account and closely linked to trade dynamics—and stock imbalances, captured by Net International

[1] Gustavo Adler and Luis Cubeddu, "Global Imbalances: Avoiding a Tragedy of the Commons," https://www.imf.org/en/blogs/articles/2017/07/28/global-imbalances-avoiding-a-tragedy-of-the-commons.

Investment Positions (NIIPs) and associated financial valuations and cross-border asset-liability structures. However, their subsequent policy recommendations focus on the flow imbalances. The IMF provides a conceptual framework explaining how macroeconomic, trade, and industrial policies influence current account outcomes by altering domestic saving and investment decisions, treating the saving–investment framework as the primary analytical anchor.[2] The OECD proposes that rebalancing could benefit from domestically grounded reforms, including fiscal adjustment in deficit countries and structural measures to reduce excess savings and industrial policies that may influence trade flows and alter current account compositions.[3]

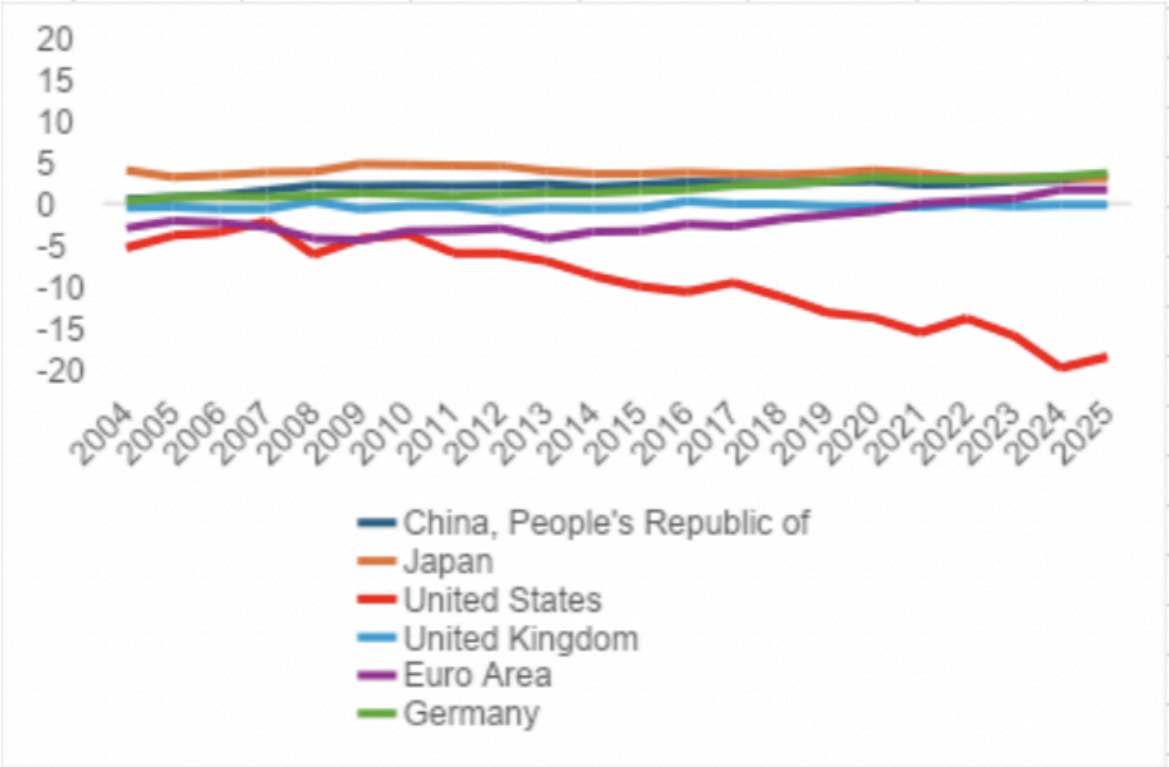
The current discussion lacks extensive analysis of the broader implications of stock imbalances, financial adjustment mechanisms, or cross-border spillovers. Financial stability issues, including the maturity and currency mismatches within international balance sheets, the transmission of valuation shocks through global portfolio rebalancing, and the vulnerability of Global South countries facing spillovers from disorderly adjustments in NIIPs, remain largely outside the scope of the current policy discussions.

1.2 The Missing Financial and Development Dimensions

Large and persistent current account deficits or surpluses are indeed generally unhealthy for the world economy. While global imbalances measured by the current account as a percentage of GDP remain below their peak before the Global Financial Crisis (GFC) in 2007, financial imbalances are now at their most acute levels. IMF NIIP data shows (Figure 1) that the US NIIP was roughly minus 19 percent of world GDP in 2025. Meanwhile, the major surplus countries, including Germany, China and Japan, each held net foreign assets equivalent to 3-3.7 percent of global GDP. As the Paris Report (aimed at the French G7 presidency discussions) emphasizes, the sharp increase in US net liabilities has become the major concern of this round of global imbalances (Rey et al., 2026).[4] Given the profound impact of financial imbalances on exchange rate dynamics and macroeconomic stability, any serious debate regarding the causes and remedies of global imbalances must focus more on those structural imbalances endogenous to the current international financial architecture (IFA).

[2] International Monetary Fund (IMF), "Understanding Global Imbalances."
[3] Frohm et al., *Current Account Imbalances, Facts, Drivers, and Policy Challenges*.
[4] Rey et al., *The New Global Imbalances*.

Figure 1. Net International Investment Position (NIIP) as share of global nominal GDP[5]



There are increasing concerns about sovereign bond market vulnerabilities and their cross-border financing spillovers. The BIS Annual Report notes that foreign private lenders, predominantly non-bank financial institutions, have become the principal marginal buyers of bonds, while the mutual holdings of bonds between developed economies are most notable. This growing interconnectedness is further amplified by the foreign exchange (FX) swap market.[6]

A newer and equally significant concern arises from the short-term capital flows. A noticeable change is the increasing foreign holdings of equities in the major financial markets, driven largely by the technology and AI revolution.[7] Those flows are pro-cyclical and risk-driven, resulting in excessive capital movements and market turmoil. The spillover effects are extremely negative for countries that are financially vulnerable with limited tools to prevent crises.

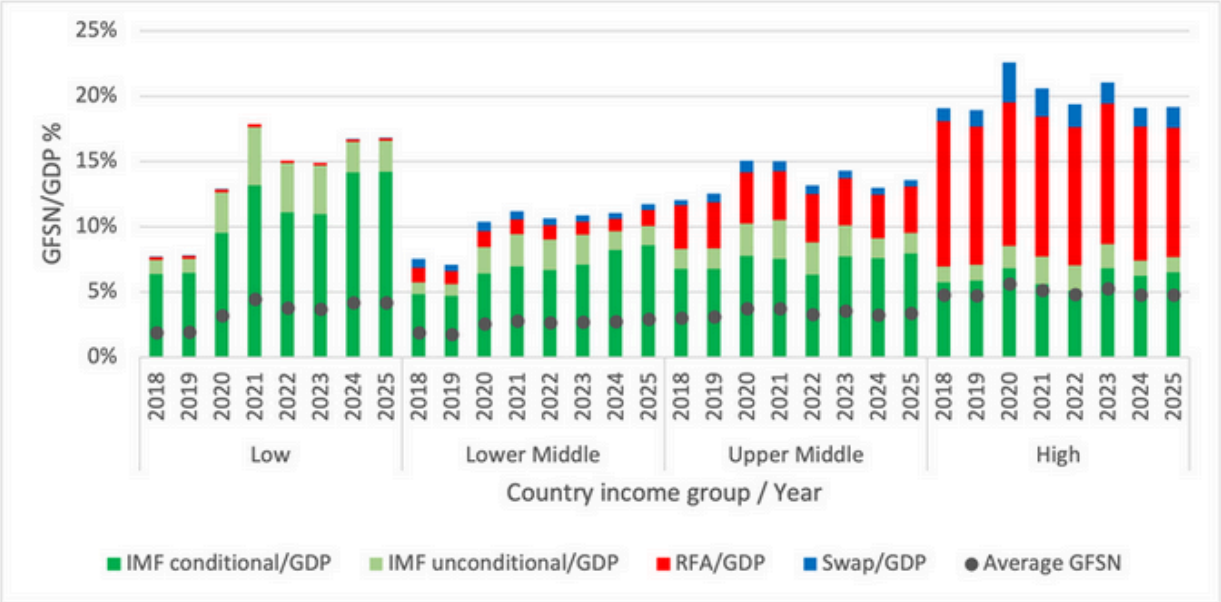
A disorderly unwinding of global imbalances can transmit shocks far beyond advanced economies, while developing countries operate within an inadequate global financial safety net

[5] IMF Balance of Payments and International Investment Position Statistics (BOP/IIP) database
[6] Bank for International Settlements (BIS), "Financial Conditions in a Changing Global Financial System."
[7] Xu and Yang, "How AI and Geopolitical Rivalry" https://www.scmp.com/opinion/world-opinion/article/3349158/how-ai-and-geopolitical-rivalry-are-breaking-economic-orthodoxy.

(GFSN).[8] As Figure 2 shows, lower-income countries not only have less access to the GFSN as a share of their GDP, but less access to unconditional sources of finance. In such contexts, sudden stops or reversals of capital flows can trigger sharp currency depreciations, raising the local currency burden of external debt and imports and compressing already limited fiscal space. This risk is compounded by the high cost of financing in the inflationary period: as central banks raise rates to contain inflation, emerging and developing economies—largely "policy takers" in the international system—face a double burden, with interest payments on new and rolled-over debt rising even as currency depreciation inflates the local-currency value of outstanding debt.[9] Countries perceived as vulnerable may then face capital flight, widening sovereign spreads, credit-rating downgrades, and even loss of market access.

To mitigate these GFSN gaps, and because of open capital accounts, Global South countries often self-insure by holding reserves well beyond standard adequacy benchmarks. With global official foreign exchange reserves reaching $13.1 trillion in the first quarter of 2026, 57.13 percent of which remain denominated in the US dollar, this systemic reliance on self-insurance exposes structural flaws within the GFA and exacerbates global imbalances. Further, this strategy carries high social and developmental costs. Earlier studies, when the stock of reserves was below current levels, indicated a social cost of at least 1.8 percent of developing countries' GDP.[10]

Figure 2. Access to the GFSN by Income Group, as Share of GDP (%), 2018-2025[11]



[8] Gallagher et al., *Resetting the Global Financial Safety Net for the COVID-19 Recovery*.
[9] Ocampo, José Antonio. *International Asymmetries and the Design of the International Financial System*.
[10] Gallagher, Kevin P., and Elen Shrestha. "The Social Cost of Self-Insurance: Financial Crisis, Reserve Accumulation, and Developing Countries."
[11] Mühlich, Laurissa, Marina Zucker-Marques, and Barbara Fritz. "Geopolitics on the Rise, IMF on the Decline"

Beyond the financial dimension, rebalancing policies in advanced economies generate significant uncertainties, disrupt supply chains, and create trade diversion, which may constrain the development prospects of emerging and developing countries. US tariffs – a unilateral measure aimed at increasing the American trade surplus – for instance, can directly limit developing countries' access to key export markets. They can also produce indirect effects through trade diversion, as surplus exports from major economies are redirected toward third markets. This can make access to key products more accessible, but also intensifies competitive pressures on domestic firms and potentially worsens external balances. These effects are especially harmful where countries lack long-term development finance to expand productive capacity, raise productivity, and strengthen competitiveness.

2. Policy Recommendations

Policy action is needed across **four connected areas:**

First, financial stability should be placed as a key pillar on the rebalancing agenda. The IMF's current External Balance Assessment (EBA) framework for measuring global imbalances should be improved by adding financial parameters, such as currency effects and capital flows, so that the assessment identifies root causes for imbalances and captures financial spillover effects alongside current account flows. The G20 Global Imbalances Study Group, at present supported mainly by the IMF and the OECD, should play a pivotal role in building shared understanding among member countries, and take steps to include financial stability in policy actions to achieve G20's objectives of strong, sustainable, balanced, and inclusive growth.

In a deteriorating market environment, the G20 should strengthen coordination and encourage multilateral and bilateral cooperation to prevent financial crises. Joint monitoring of cross-border capital flows and their spillovers is necessary within the global imbalances agenda, with findings feeding directly into G20 policy discussions. For emerging markets and developing economies, exchange-rate flexibility alone cannot always prevent abrupt inflows or outflows from amplifying domestic financial fragility. Capital flow management is therefore a complement to underlying macroeconomic adjustment.

Second, a stronger global financial safety net (GFSN) can be an important instrument of imbalance reduction, not merely of crisis preparedness. An effective GFSN lowers the need for precautionary reserve accumulation, reduces one of the driving forces for financial imbalances and the probability that capital-flow reversals become liquidity or debt crises, and gives countries room to rebalance without abrupt demand compression.

Three actions are priorities. First, the IMF should remain the anchor of the system, but requires a larger quota-based resource base and governance that better reflects emerging markets and developing economies. Advancing quota realignment and reducing reliance on temporary borrowed resources would strengthen both legitimacy and capacity.[12] Second, the Fund's lending

[12] Kring et al., *Towards a Balanced Quota Reform at the IMF*.

toolkit should be more countercyclical, such as expanded precautionary facilities and faster access to emergency liquidity.[13] Third, regional and bilateral financial supports, including central banks' swap arrangements, should play bigger roles in financial stability through broader coverage and enhanced funding capacity. They are a supplement to the IMF's financial assistance.

Third, deeper reforms are needed in the international monetary system to widen the supply of safe and liquid assets and to reduce the negative spillovers. Three complementary directions stand out. First, the role of Special Drawing Rights (SDRs) should be expanded. This includes considering allocations that better reflect countries' actual demand for reserves, particularly in periods of global stress, as well as the wider use of SDRs in crisis lending and development finance. Rechanneling SDRs from advanced economies toward vulnerable countries would strengthen the global financial safety net at limited fiscal cost. Current rechanneling efforts through the IMF's RST and PRGT not only face funding constraints but yield limited impact due to unremarkable disbursement rates; by 2026, for instance, just about 20 percent of RST resources had been distributed.[14] Consequently, innovative rechanneling and redeployment mechanisms are required to supplement existing schemes and reinforce the GFSN. Second, establishing deeper local-currency bond markets, supported by credible macroeconomic frameworks and sound market infrastructure. This would reduce currency and maturity mismatches on national balance sheets while expanding the overall supply of safe assets. Third, highly rated multilateral development bank bonds and other supranational instruments can provide additional globally diversified reserve assets on a larger scale. Although these instruments are increasingly categorized as reserve assets, their share as an asset class remains marginal. Limited disclosures from central banks, such as the Swiss National Bank and Banco Central do Brasil, indicate substantial headroom for expanding the integration of MDB securities into official reserves, a shift that would help enhance the resilience of the international monetary system.[15,16]

Fourth, the discussion on rebalancing should include the support of productive investment in the Global South. International policy should therefore encourage FDI that expands productive capacity, transfers technology, develops local capabilities, and supports structural transformation. This requires shifting incentives toward long-term, green, and productivity-enhancing investment. However, FDI should be accompanied by greater trade to ensure that new productive capacity translates into higher exports, employment, and domestic demand. Once trade and investment policies are thought through jointly, it is possible to turn

[13] Gallagher et al., *Resetting the Global Financial Safety Net for the COVID-19 Recovery*.
[14] Data from IMF Finances https://www.imf.org/en/data/imf-finances
[15] Swiss National Bank, Foreign Exchange Reserves. https://www.snb.ch/en/the-snb/mandates-goals/investment-assets/reserves-bonds - indicates 11 percent of foreign reserves are allocated in "other"assets including: Government bonds in foreign currency, covered bonds, bonds issued by foreign local authorities, supranational organisations, corporate bonds, etc.
[16] Banco Central do Brasil, *International Reserves Management Report*, Volume 17, July 2025 indicates less than 2 percent of foreign reserves allocated in supra-national bonds.

global rebalancing into a source of structural transformation rather than a costly adjustment pressure.

MDBs play a key role in supporting structural transformation while preserving policy space in the Global South. In a context of high global interest rates, declining official development assistance, and tighter external financing conditions, multilateral development banks (MDBs) must significantly expand their lending capacity (Gallagher et al. 2024). This requires greater use of their balance sheets, alongside scaled-up concessional and non-concessional financing. MDBs should prioritize green and productivity-enhancing investments, including climate-aligned infrastructure and industrial upgrading. Moreover, by providing more stable and predictable financing through MDBs, countries could reduce their reliance on volatile private capital flows and reduce costly reserve accumulation. So MDBs financing has a direct effect on structural transformation and an indirect stabilizing effect.

Next Steps by the G20

In terms of policy change, two priorities should guide action in 2026: strengthening the global financial safety net (GFSN) and accelerating multilateral development bank (MDB) reform — making these systems not only big, but better equipped to deal with current challenges.

First, the G20 should call for strengthening the GFSN. This should be accomplished by increasing IMF quotas, volume, and accessibility of precautionary financing, reducing counterproductive conditionality, and instead supporting expansionary recoveries. Support regional financing arrangements. Such reforms should be accompanied by more voice and representation of EMDE at the IMF.

Second, the G20 should accelerate MDB reform. This includes implementation of the Capital Adequacy Framework (CAF) recommendations and reviews of MDB capital and lending capacity. Greater use of MDB balance sheets, alongside additional capital and expanded concessional and non-concessional financing, is essential to mobilize investment for structural transformation in developing economies. Moreover, MDBs should more broadly finance the structural change of developing countries, especially by supporting domestic investments that reduce the structural balance of payments deficits that many developing countries face.

These measures provide a feasible 2026 agenda while laying the groundwork for longer-term reform of the international monetary and financial system. The objective should not simply be to reduce measured imbalances, but to ensure that adjustment strengthens financial stability while preserving developing countries' capacity to pursue inclusive and sustainable growth.

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