Economic Analysis

The U.S. Trade Balance: Then and Now

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- **Total U.S. trade accounts for nearly 30% of GDP as we remain a net importer of goods but a net exporter of services**
- **Nonpetroelum goods deficit has returned to the pre-crisis peak as global imbalances linger, yet we could see a petroleum goods surplus in the near future**
- **Current and pending free trade agreements have the potential to boost global growth and keep imbalances in check**

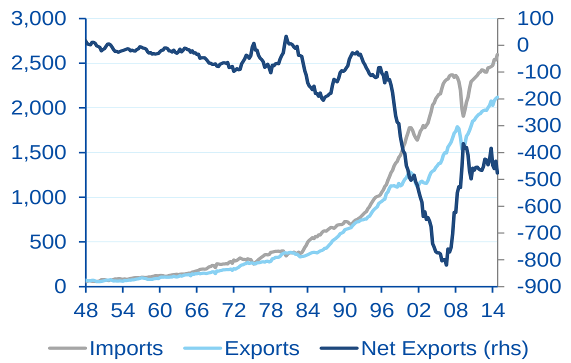
"The Nation's economic recovery and long-run growth prospects depend in large part on U.S. businesses being able to compete in an open, fair and growing world economy."

– Economic report of the President, transmitted to the Congress March 2013, together with the annual report of the Council of Economic Advisers (Washington, DC, U.S. Government Printing Office, 2013).

Acknowledging the importance of international trade is not a new phenomenon, yet the dynamic global environment has forced us to look at post-crisis trends in a different light. The 2008 recession was one of the worst on record for modern international trade, and conditions have been shaky ever since. Global imbalances that raised concerns prior to the financial collapse have come back to haunt us, emphasizing the cyclical and structural impacts lingering in the world economy. As the global economy expanded rapidly throughout the 2000s, the U.S. dealt with a large current account deficit while other countries built up large surpluses. Furthermore, concerns were growing over China's increasing holdings of foreign currency reserves. While all of this may not have directly caused the financial crisis in 2008, it has certainly played a role in the adjustment process throughout the recovery. Former Federal Reserve Chairman Ben Bernanke commented on this in 2005, noting the "global saving glut" that emerged throughout the prior decade. His sentiments still hold true today: "we probably have little choice except to be patient as we work to create the conditions in which a greater share of global saving can be redirected away from the United States and toward the rest of the world--particularly the developing nations."

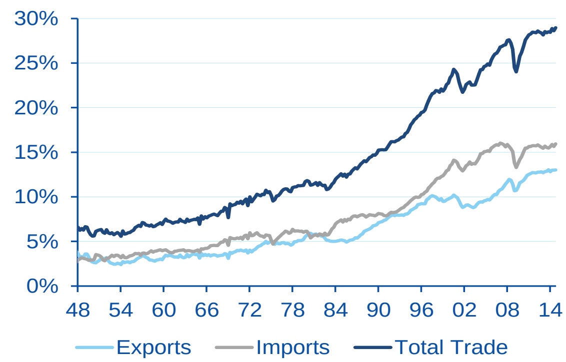
While there are certainly some similarities from the pre-crisis environment, other newer factors could pose challenging for the future of global trade. For example, increased monetary policy accommodation since the crisis has created a new environment, influencing demand in unfamiliar ways. Six years into the recovery and central bank actions have intensified, with the Federal Reserve slowly approaching normalization while others seem to be moving in the opposite direction. This can have a significant impact on foreign exchange rates, which have played an important role throughout the recovery as economies seek to maintain favorable currency values to support export-led growth, with competitive devaluation igniting potential currency wars. Now more than ever global trade is put under the microscope as the U.S. dollar appreciates and oil prices are expected to hold steady near crisis lows for a prolonged period, all while demand conditions remain vulnerable. This makes things particularly difficult for the U.S. as we strive to become a more export-oriented economy, and it is especially important for U.S. multinationals that derive nearly 50% of their revenues from sales abroad. A look back at international trade before and after the crisis will help pave the way for where we are headed in the coming years under a "new normal" set of assumptions for the global economy.

Chart 1
International Trade (SAAR, Bil.Chn.2009$)



Source: BEA & BBVA Research

Chart 2
Total U.S. Trade as a Share of Real GDP (%)

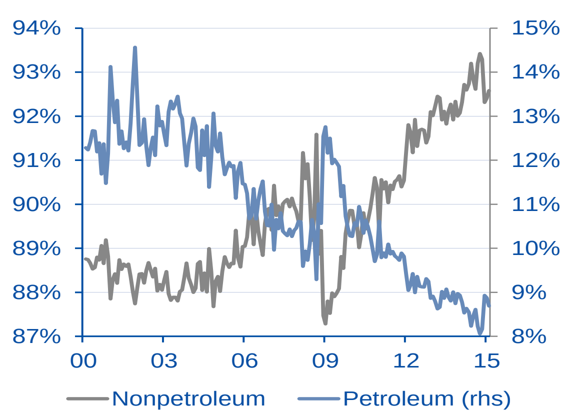


Source: BEA & BBVA Research

The U.S. Continues to Balance a Services Surplus with a Goods Deficit

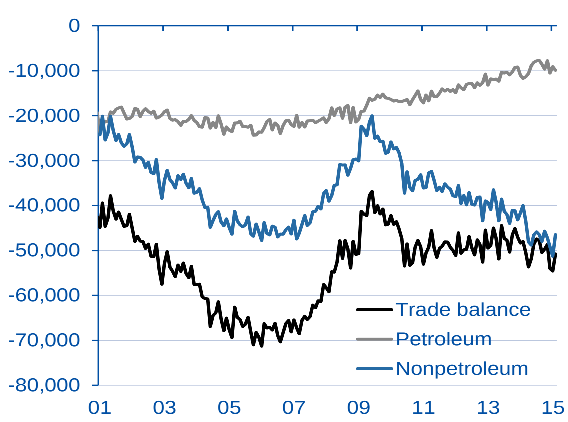
For the U.S., the total volume of trade shrank significantly throughout 2008 and 2009 but has been on the rebound ever since. Now, total U.S. trade accounts for a record high of almost 30% of GDP, though this is driven primarily by domestic demand as we remain a net-importer of goods. Specifically, trade in goods accounts for approximately 75% of total trade, down from a peak near 80% in the early 2000s. For the most part, the crisis did not have an impact on the composition of trade in goods for the U.S. By volume, industrial supplies and capital goods are the most heavily traded, though this has always been the case and was not a consequence of changing economic conditions after the recession. Not surprisingly, auto-related trade took the biggest hit in 2008 and 2009 but by 2013 both exports and imports had recovered fully. The U.S. had already moved away from manufacturing and labor-intensive goods production, so the impact of the crisis on the sector itself was more cyclical than structural.

Chart 3
Real Petroleum and Nonpetroleum Goods as a Share of Total Trade (%)



Source: U.S. Census & BBVA Research

Chart 4
Real Trade Balance, Petroleum vs Nonpetroleum Goods (SA, Mil.Chn.2009$)

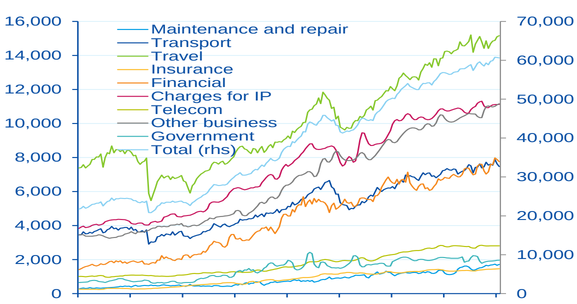


Source: U.S. Census & BBVA Research

It is interesting to look at the international trade balance when it comes to petroleum versus nonpetroleum goods, as the share of GDP is weighted heavily towards the latter. Currently, more than 90% of total trade in goods comes from the nonpetroleum component. Before 2005, the share of nonpetroleum goods trade (in real terms) was steady around 88% of total trade. During the few years prior to the crisis, this share skyrocketed to 92% before dropping sharply. Since then, the share has crawled back above the pre-crisis high. On the contrary, the share of petroleum goods to total trade has trended downward from a high of more than 18% in the mid-1990s to current historical lows near 9.0%. When it comes to the trade balance as a share of GDP, the nonpetroleum side takes the cake at approximately 80% in nominal terms (87% in real terms). The petroleum balance only accounts for 23% of GDP (17% real). With a growing focus on nonpetroleum goods trade, slow global growth, and (more recently) the appreciating USD, the nonpetroleum deficit has soared to the largest level of the recovery, right back to where we were before the crisis in 2007 (in both real and nominal terms). This highlights the fact that pre-crisis global imbalances have not disappeared and continue to be a serious concern, and it may be wise for the U.S. to move toward a more balanced share between petroleum and nonpetroleum-based trade. The IMF recently addressed this issue in their World Economic Outlook (September 2014), noting that “imbalances have narrowed substantially since their precrisis peak in 2006, and their configuration has changed markedly along the way.” Still, the IMF has acknowledged that “problems remain with respect to net external positions or stock imbalances.” The fact that the global economy has not significantly improved its imbalances makes it just as vulnerable to future shocks.

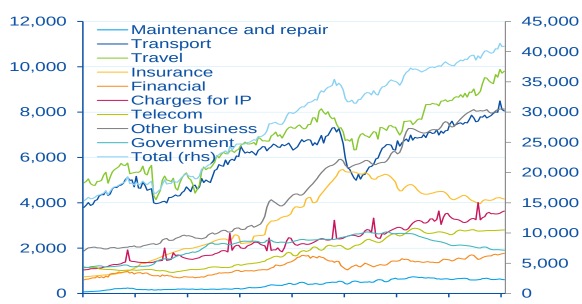
Unlike the nonpetroleum side, there has been an improvement in the petroleum balance since the crisis, with petroleum imports trending downward gradually and exports on the rise. It is important to note that the U.S. remains a net importer of petroleum products, specifically crude oil, but in the past few years has become a net exporter of other petroleum products for the first time since World War II. As a share of total exports, petroleum goods have trended upward more rapidly since the crisis and are on pace to overtake imports in the coming years. This would imply a petroleum goods trade surplus in the near future. However, various factors could prevent such a situation. For instance, the decline in oil prices and the resulting favorable price of gasoline lifted petroleum imports nearly 18% at the end of 2014. At the same time, the U.S. is not immune to trends in other oil-producing nations. The latest political plays by Saudi Arabia to keep prices low has proven that the U.S. still has a long way to go before it has control of the global energy market. Ultimately, this hurts the U.S.’s chances of becoming energy self-sufficient by 2020 and on track to be a net-exporter, as suggested by the International Energy Agency (IEA) a few years ago.

Chart 5
U.S. Services Exports (SA, Mil.$)



Source: U.S. Census & BBVA Research

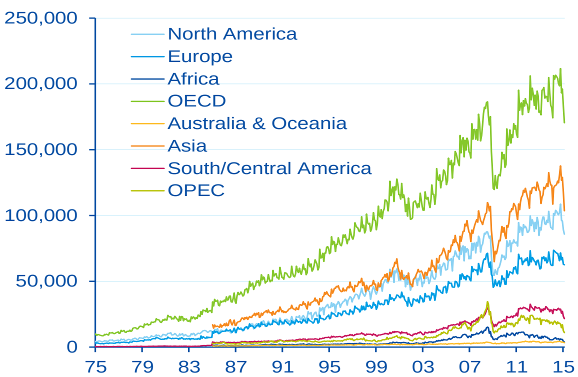
Chart 6
U.S. Services Imports (SA, Mil.$)



Source: U.S. Census & BBVA Research

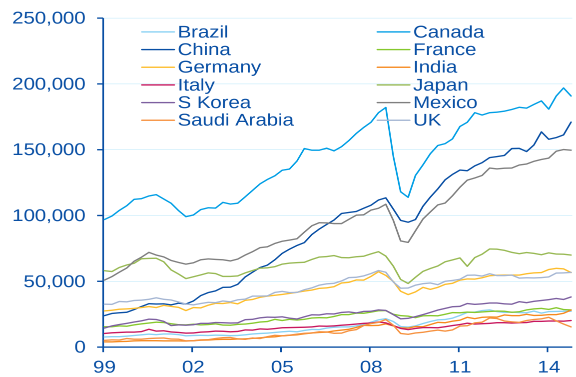
The U.S. could also benefit from a more balanced share between goods and services trade, considering that the U.S. has been running a healthy services surplus throughout the past few decades – one that began accelerating in the mid-2000s and has continued on an upward trend ever since the crisis. This plays into the role of the U.S. as a high-skilled center of trade, leaving behind the more industrialized labor-intensive goods production (i.e. manufacturing) for a greater focus on intellectual human capital. Similar to the patterns in goods trade, there wasn't much of a change pre- and post-crisis given that this services-based environment had already been established. However, there was clear downward shift in imports of insurance and government services after 2008, which makes sense given post-recession changes in financial and government regulations.

Chart 7
U.S. Total Trade by Region (NSA, Mil.$)



Source: U.S. Census & BBVA Research

Chart 8
U.S. Trade by Country (SA, Mil.$)



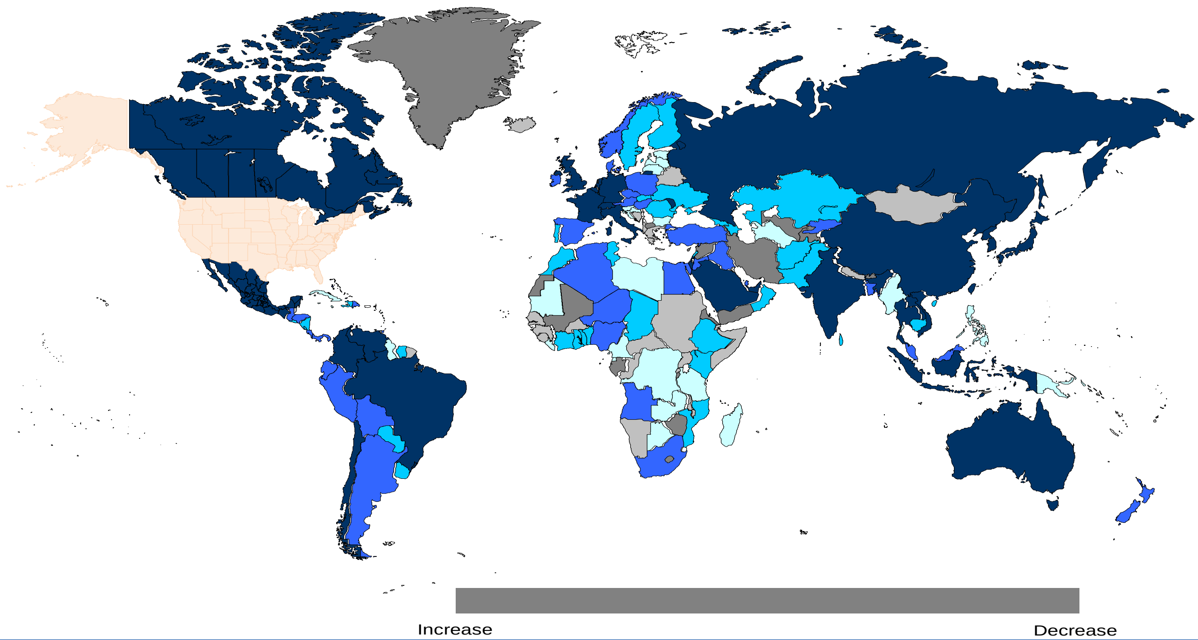
Source: U.S. Census & BBVA Research

Diversified Trade Helps Keep Global Imbalances in Check

On the whole, U.S. trade in both goods and services has been significantly influenced by trade agreements throughout the past few decades. Currently, the U.S. has 14 free trade agreements (FTA) with 20 countries, and policymakers are negotiating others including the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP) with the European Union. According to the International Trade Administration (ITA), almost 50% of U.S. goods are exported to these FTA nations and since 2009, merchandise exports to these trading partners have increased 64% (compared to 45% for the rest of the world). In 2014 alone, the U.S. surpassed record high trading volumes for many of these countries, including Canada, Mexico, Korea, Israel, Colombia, Oman, and the Dominican Republic. More surprisingly, the U.S. currently exports more nonpetroleum goods to these trading partners than it imports, with the machinery surplus leading all other sectors.

The FTA between the U.S. and Canada started it all in 1987, followed by the North American Free Trade Agreement (NAFTA) in 1994 that officially linked the U.S in a strong partnership with both Canada and Mexico. However, there has been an obvious shift toward China emerging since the early 2000s. In fact, there was a drastic increase in total trade worldwide when China opened up its economy by joining the WTO in December 2001. While this has obviously had a positive impact on the global environment, it also contributed to the aforementioned global imbalances that still remain today. From the U.S. perspective, a more diversified trading portfolio will help keep these imbalances in check. The potential for trade agreements is encouraging; current and future agreements (the TPP and TTIP, if implemented) will account for more than 70% of U.S. goods exports. Overall, the ITA expects that the international exchanges created by these agreements will account for more than 60% of global trade and 64% of global GDP (including the U.S.). The benefits are widespread, boosting potential growth among participants and allowing for a more stable trading environment that is less susceptible to geopolitical threats and currency wars. This is even more important in today's environment given that nominal trading volumes have declined sharply in the past few months.

Chart 9
Change in Total Trade Volume, 2002-2014



Source: U.S. Census & BBVA Research

Bottom Line: U.S. Slowly Moving toward a Healthier Trade Balance

The 2008 financial crisis caused significant structural damage throughout the global economy, yet trade patterns for the U.S. have seen mostly a cyclical impact. International trade is back at square one, yet there are glimpses of a stronger trading future ahead for the U.S. The idea that the U.S. could ever become a net exporter seems like a longshot, particularly when it comes to sectors where other economies have the competitive advantage of lower input costs of production. While the short- to mid-term outlook is for the U.S. to remain a net importer, particularly as the global economy lags behind stronger activity at home, we are likely to see further progress in the petroleum balance as well as continued strength in services. Free trade agreements have had (and will continue to have) a huge impact on U.S. trade, helping to create surpluses in nonpetroleum sectors such as machinery, plastics, aircraft and parts, and miscellaneous and organic chemicals. Moving forward, these trade partnerships will be the key to managing global imbalances and, ultimately, a healthier trade balance for the U.S. in the longer run.