Trade Annex

The outlook for global trade

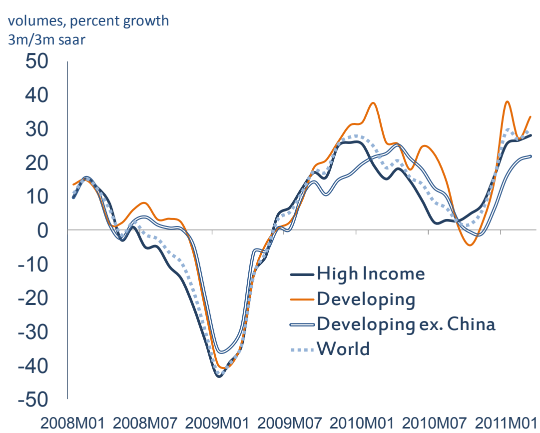
International trade has been volatile during the current recovery, reflecting the wider inventory cycle in global industrial production (see Main text and Industrial Production annex). The recovery in trade has been dominated by strong import demand from developing countries, which has accounted for more than half of the increase in global imports. As the recovery matures, support for trade is shifting from temporary factors (government stimulus and re-stocking of inventories) to more sustainable drivers, notably a rebound in private sector spending on capital goods and consumer durables. Looking forward, world trade is expected to continue expanding at close to 8 percent annual pace, above average in historical context.

Trade volumes are surging again. After a blistering pace of growth in the first half of 2010, global trade growth ground to a halt in the third quarter, only to pick-up again strongly in the fourth quarter. By March 2011 (latest data), global merchandise trade volumes were expanding at a 30 percent annualized rate (3m/3m, saar), the fastest pace in over a decade (figure Trade.1).

The rapid pace of trade growth partly reflects the depth of the decline observed during the recession. Despite faster growth rates, trade volumes regained pre-crisis peak levels 32 months after the crisis, something achieved in only 16 months following the previous major slump in world trade in 2001 (figure Trade.2). As of March 2011, global trade was 8.9 percent above its pre-crisis peak, compared with 10.6 percent higher at the same stage in the previous recovery. And in spite of recovery, global trade volumes remain below trend levels (the level of trade would have been if the crisis did not occur and trade grew at its pre-boom average), though developing countries have regained their trend levels.

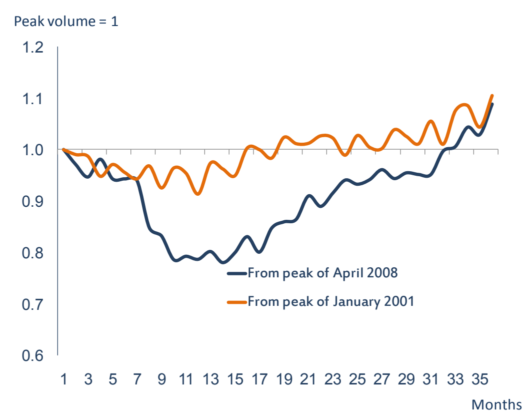
Developing country demand is at the heart of the recovery in global trade. Import demand from developing countries was responsible for more than half of the growth of global trade during the first half of 2010, and again during the fourth quarter of 2010 and the first quarter of 2011. Like other regions (with the exception of the United States) developing countries' support petered out in Q3-2010, but then rose strongly in the fourth quarter (while U.S. imports declined).

Figure Trade.1 After decelerating in Q3, the trade recovery has gathered pace again



Source: World Bank.

Figure Trade.2 Recovery in current crisis lags behind previous crisis



Source: World Bank.

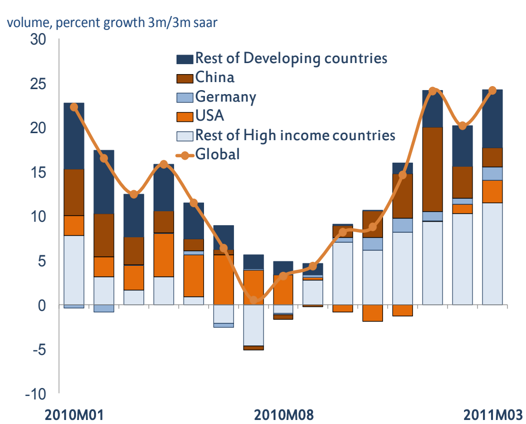
For the first quarter of 2011, developing countries accounted for nearly 50 percent (of which China's contribution alone was 25 percentage points) of the increase in global import demand (figure Trade.3).

Developing country export performance has shown considerable heterogeneity. Trade volume growth in Asia has been extremely rapid. Buoyed by strong growth in Pakistan and India, the annualized pace of export growth in South Asia reached a record 81.7 percent (3m/3m, saar) in February 2011 and moderated to 74.9 percent in March 2011 (figure Trade.4). Spurred by strong performance in China, export volumes in East Asia and the Pacific expanded at a 64.0 percent annualized pace in the 3 months to January 2011 and moderating to 45 percent in March 2011. Strong exports in Russia drove volume growth in Europe and Central Asia to an eight month peak of 15.5 percent (3m/3m saar) by March 2011. And reflecting exchange rate appreciation, export growth in the Latin America and Caribbean region lags other developing regions, having expanded at a 12.2 percent annualized rate in the three months ending March 2011.

The recovery in the dollar value of exports is less advanced than that of volumes. Notwithstanding the sharp rise in the price of commodities in recent months, the dollar value of exports has not recovered as far as volumes, because many prices remain below their pre-crisis peaks of 2008. As of January 2011, global exports were 6.3 percent above their pre-crisis peak in volume terms, but remained 5.7 percent below earlier highs in dollar terms. Nevertheless, price developments have favored commodity exporters, in particular oil. metals and mineral exporters. For example, the terms of trade improvement for oil exporters in Europe and Central Asia amounted to about 1.8 percent of GDP, compared with a deterioration of 1.1 percent for oil importers in the same region (figure Trade.5).

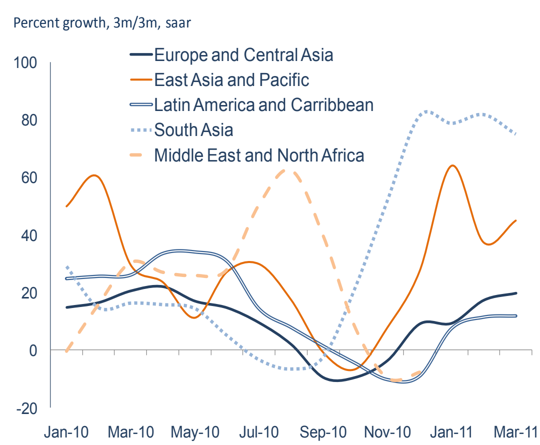
World trade growth is on more solid footing. Capital goods exports have continued to strengthen as the recovery matures, a sign of the increasingly self-sustaining nature of the recovery (figure Trade.6). During the recession, capital goods imports fell by more than imports of consumer durables and agricultural products (although less than oil imports), as falling demand and increasing uncertainty led businesses to cut investment and run down stocks. During the initial phases of the recovery, growth in capital goods imports was driven by massive government stimulus programs (most of which had a heavy infrastructure component) as well as a need for businesses to replenish their

Figure Trade.3 Contributions to global import demand from selected regions and countries



Source: World Bank.

Figure Trade.4 South Asia leads in second phase rebound in global trade

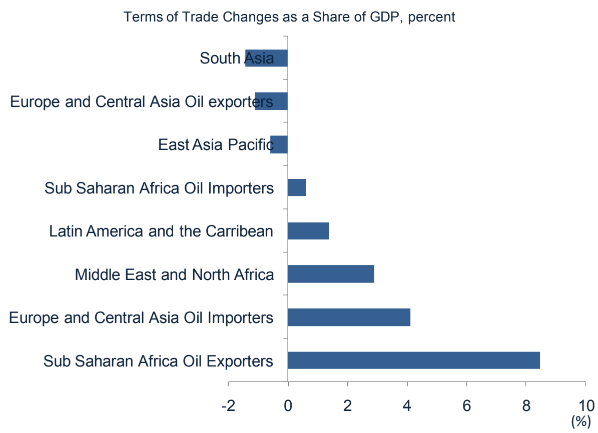


Source: World Bank.

stocks. Since that time, these temporary factors have waned, and imports of capital goods by businesses surged in the fourth quarter of 2010. In the United States, for example, business spending on equipment and software rose at a 7.7 percent annualized pace in the fourth quarter – although it eased to just 1.8 percent growth in the first quarter of 2011.

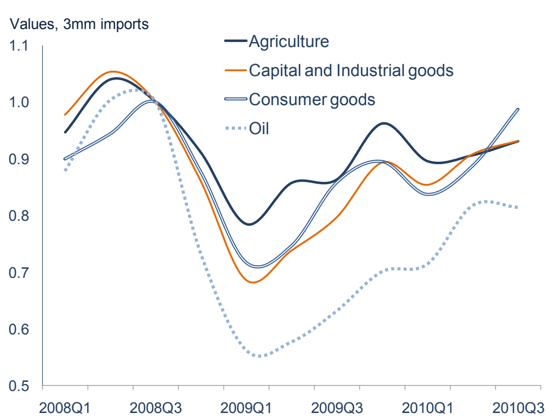
Recently, slowly improving labor market conditions in high income countries have boosted consumer goods imports, with trade in these goods exceeding that of capital goods. Consumer goods imports are now 4.6 percent higher than their pre-crisis peak levels, while capital goods imports remain 11.5 percent below pre-crisis peak levels, partly reflecting the much deeper trough they experienced (capital good demand declined 35 percent during the crisis).

Figure Trade.5 The Recovery in Prices has Favored Oil Exporters



Source: World Bank.

Figure Trade.6 Strong recovery in capital goods imports but still below pre-crisis levels



Source: World Bank.

The global recovery also is becoming more broadly based. High-income country exports are now growing rapidly, though, consistent with lower potential growth rates, not as quickly as among developing countries. By March 2011 export volumes for high-income countries were increasing at a 28.1 percent (3m/3m, saar) rate, up from the 2.7 percent (3m/3m, saar) in July 2010. In contrast, developing countries' export volumes advanced at 33.4 percent (3m/3m, saar) in March 2011, compared to a decline of 4.6 percent (3m/3m, saar) in September 2010.

Outlook and Risks

Global trade is expected to continue to grow as the recovery matures. Though a moderation of growth from the high first quarter figures is in order, the expansion in global trade is projected to remain above pre-crisis averages over the forecast period. Overall, global merchandise trade is anticipated to grow at about an average of 7.6 percent over the forecast horizon (2011-2013). Developing countries, which were at the forefront of the global trade revival, will continue to be important sources of demand. However, with improvements in high-income country labor markets, ongoing lax monetary policy, and a rise in business and consumer confidence, demand from high income countries is expected to provide increasing support to global trade growth.

Recent business surveys support the view that global trade will continue to expand, at least for the near term. Though the Global Purchasing Manager's Index, as reported by JP Morgan and Markit, has fallen from its peak level in March, it still remained in expansion territory in May, including the sub-index for new export orders. Moreover, the latest OECD Composite leading indicators survey, designed to anticipate turning points in economic activity relative to trend, continues to point to expansion in most OECD countries even if at a lower pace- this should inevitably provide support to further trade growth.

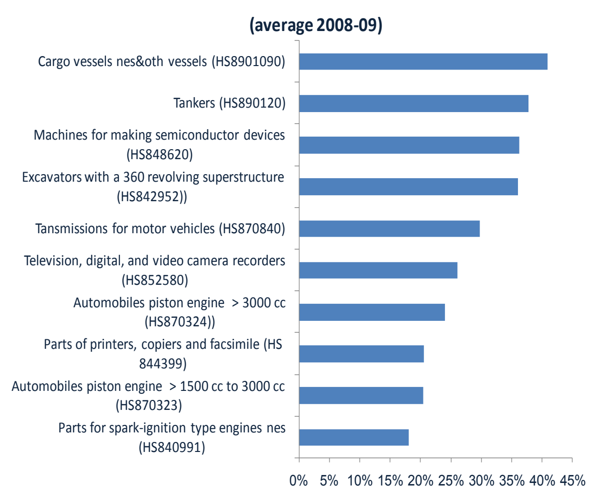
The risk of a faltering in global economic recovery. Nonetheless, significant risks to the continued expansion in global trade remain. The most significant risk is a faltering of the global economic recovery. As outlined in the main text, a key risk to the global recovery is the possibility of higher oil prices – either due to continued uncertainty in the Middle East, or because of a major disruption to supplies. Though this remains a "tail-probability" event, should it occur, it could derail the recovery, since higher oil prices would reduce incomes in oil-importing countries, cutting into consumer and business demand. A further $50/bbl increase in oil prices could shave global GDP by 0.3 percent in 2011 and 1.2 percent in 2012. These could in turn reduce global trade by 0.5-1.5 percent in 2011 and by between 1.9-6.0 percent in 2012. Other risks to the global recovery include a possible slowdown in growth from a tightening of monetary policy in some of the large fast growing developing economies and a resurgence in the euro area sovereign debt crisis (see main text).

Ramifications of the Japan earthquake on global trade. The recent disaster in Japan is another source of concern. Japan's share of global trade is less than 5 percent, so even a recession there is unlikely to derail global trade growth. However, individual countries could be significantly affected. Non-oil exporting countries whose exports to Japan account for a sizeable share of their total exports and GDP, for example Malaysia, Papua New Guinea, Vietnam, Singapore, Thailand and the Philippines, will be most affected. In addition, disruptions in the global supply chain due to the situation in Japan could affect trade in many products, which could have major implications for industry (especially where switching to other suppliers requires significant re-tooling). Against this backdrop, industries whose global supply chains are very much dependent on critical supply of parts from the North East part of Japan (Miyagi prefecture) are likely to be the hardest hit. These could include parts supplies in the semiconductor, auto, camera recorders and office equipment industries (figure Trade.7). Already in the U.S, recent industrial production figures released show that the total motor vehicles assembled dropped from an annual rate of 9.0 million units in March to 7.9 million units in April mainly on account of disruptions to part supplies resulting from the Japan earthquake.

While in the short-run Japanese industrial production and exports are likely to fall, in the medium term reconstruction will require a ramp up in demand for capital goods and for the industrial metals necessary to repair capital stock and build new infrastructure. This new demand from Japan could significantly boost exports from the high-income countries that dominate global exports of capital goods, as well as from developing country metals exporters.

Global Imbalances. The onset of the global crisis accelerated the narrowing of global imbalances that had already begun in 2006. Global imbalances (measured as the absolute value of national current account balances divided by global GDP) peaked at 5.6 percent of global GDP in 2005 and fell to 3.9 percent in 2009 and to an estimated 3.3 percent in 2010. The question is whether this is a short-run change or a structural change brought about by the crisis.

Figure Trade.7 Share of Japan's exports in World exports



Source: Comtrade

The future evolution of global imbalances depends on a constellation of real and financial forces, including exchange rate movements, the extent to which developing country domestic demand remains a major source of growth, and the extent to which high-income countries rein in government deficits and low interest rates as their economies recover. To the extent that surplus countries do not experience real effective appreciations of their exchange rates, and that recovering high-income countries maintain current levels of government dis-saving and low-interest rates, which encourage low private-sector savings rates, the global imbalances that characterized the early 2000s through 2007 could return.

Increased Protectionism. High unemployment rates, global imbalances, and perceptions of exchange rate undervaluation among trading partners puts pressure on governments to take a more protectionist stance on international trade, with the potential to slow the expansion of trade. These pressures have only heightened in the aftermath of the global recession. The WTO reports that between November 2009 and October 2010, new trade restrictive measures covering some 1.2 percent of global imports were introduced.[1] New trade restrictions introduced since the commencement of the crisis in 2008 have affected some 1.9 percent of total trade. Though some of the measures were meant to be temporary, so far only 15 percent of the measures introduced have been removed. Most of the measures that have been introduced affect trade in base metals and products, machinery and mechanical appliances, and transport equipment, all of which are important in helping to rebuild productive capacity to help sustain the recovery. Further, Bown and others (2010), find that increasingly such measures are being applied within the context of South-South trade.[2] They observe that protectionism has been imposed disproportionately by developing world importers on developing world exporters, notably China. Though the current application of such protectionist measures remains limited, the greater threat lies in the continued accumulation of new restrictions, without repealing earlier temporary ones, thereby leading to an increasing share of trade affected by restrictive measures.

Notes

1. WTO, 2010. Overview of Developments in the International Trading Environment. WT/TPR/OV/13, World Trade Organisation, Geneva.

2. Chad P.Bown and Hiau Looi Kee (2010) "Developing Countries, New Trade Barriers, and the Global Economic Crisis" in Mona Haddad and Ben Shepherd (eds), Managing Openness, The World Bank, Washington, D.C.