

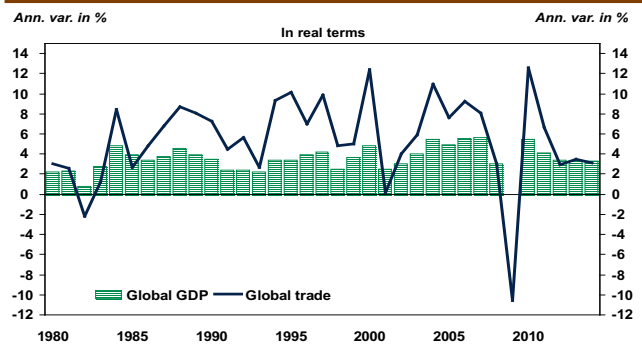
Why has growth flagged in international trade? A lot of hope rests on liberalizing trade

The 2008–2009 crisis had consequences that harmed the growth of global trade. Like the economy as a whole, trade rebounded but, there too, we are seeing rather disappointing growth compared with the period prior to the crisis. Where is this relative weakness coming from? Could growth in trade accelerate soon?

The evolution of global trade in goods and services has been transformed since the 2008–2009 crisis. To begin with, the Great Recession was especially painful for global trade. According to annual data from the International Monetary Fund (IMF), the trade in goods and services (in real terms) fell 10.6% in 2009, while global real GDP only stagnated (graph 1). Using the monthly data from the Dutch organization CPB Netherlands Bureau for Economic Policy Analysis, the contraction in the global merchandise trade was even more dramatic: it dropped 19.9% from the top of the cycle in April 2008 and the low in May 2009 (graph 2). During this time, global industrial output fell 13.9%, which is still not as much as the tumble in trade.

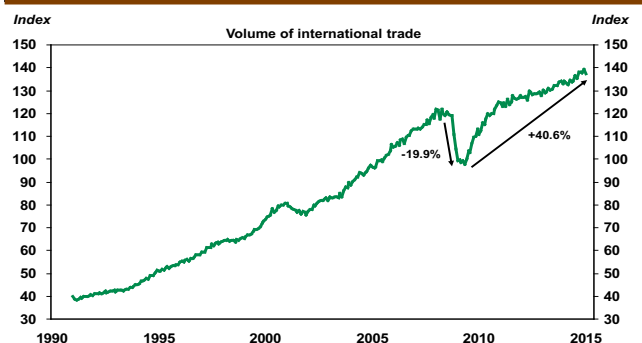
Various factors can explain why trade suffered more than the overall economy. Except perhaps for financial services, the service industry was not as sensitive to the vagaries of the situation. Thus, real GDP, which is more global, fell less than industrial output, while the trade in services did not retreat as much as merchandise trade. Secondly, some industrial sectors were especially hard hit, such as the auto sector, which underwent substantial restructuring, particularly in the United States. The auto industry's supply chains are highly internationalized and the trade in finished products, materials and parts was hit by the backlash. This is true for other industries as well, such as aviation. Thirdly, the financial difficulties that stemmed from the crisis generated financing problems for exporters and importers. The risks of bank failures sapped confidence in letters of credit that make short-term financing of trade possible. According to a British survey, financing difficulties were one of the primary curbs on exports (graph 3 on page 2).

Graph 1 – The tumble by international trade was especially serious during the crisis



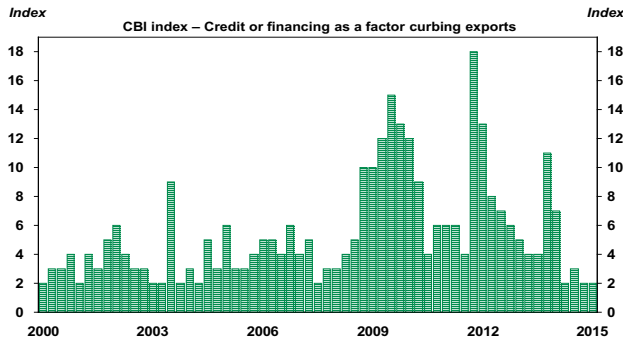
Sources: International Monetary Fund and Desjardins, Economic Studies

Graph 2 – The monthly data on merchandise trade shows an even greater contraction



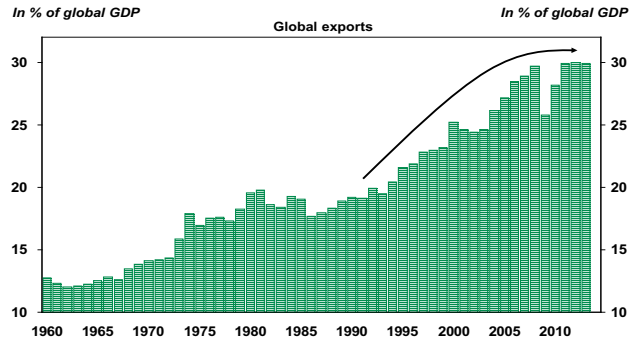
Sources: CPB Netherlands Bureau for Economic Policy Analysis and Desjardins, Economic Studies

Graph 3 – Financing difficulties were a curb on global trade during the recession and European crisis



Sources: Confederation of British Industry and Desjardins, Economic Studies

Graph 5 – The share of exports in global GDP has been stagnant for several years



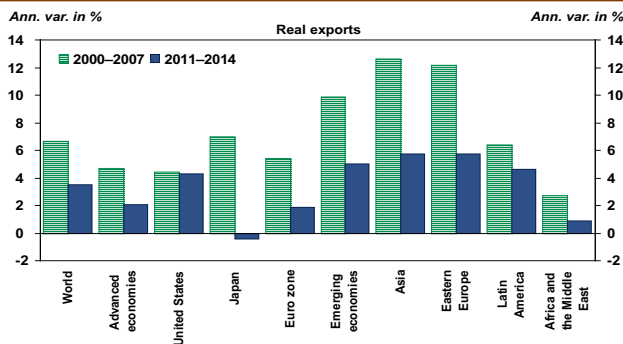
Sources: World Bank and Desjardins, Economic Studies

DISAPPOINTING RECOVERY

After the carnage of 2008 and 2009, trade began to rebound. Growth by the real trade in goods and services hit 12.6% in 2010, the strongest annual gain since data first became available in 1980. Merchandise took off even more strongly: in the 12 months following the May 2009 low, the volume of trade climbed 20.4%.

However, subsequent to the rebound effect, trade growth was fairly disappointing. Although it had previously tended to grow a lot faster than global real GDP, international trade instead advanced at the same pace, at about 3% since 2012. This fairly steady cruising speed is well below the average of 7% established in the 20 years that preceded the Great Recession. The trend can be seen in all of the major economic blocks (graph 4).

Graph 4 – Trade growth has slowed across the board compared with the pre-crisis period

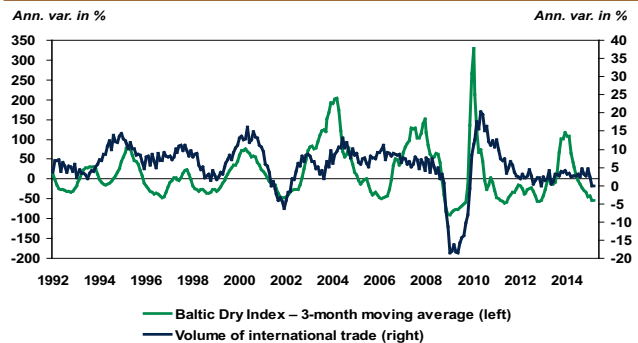


Sources: CPB Netherlands Bureau for Economic Policy Analysis and Desjardins, Economic Studies

Global GDP began to diverge from the trend during and after the recession, but that divergence is even wider in trade. The World Bank estimates that if the growth seen prior to the crisis had persisted, international trade would be 20% more than it was in 2014.

Other indicators attest to the current weakness in global trade. Historically, the Baltic Dry Index, which monitors the cost of moving merchandise by sea, tracks the change in global trade fairly well. Its annual change is currently heading down, suggesting that global exports will slow further (graph 6). However, the fluctuations in the Baltic Dry Index are also subject to the microeconomic factors affecting the maritime industry, sometimes violently. In other words, an excess supply of ships resulting from overly high orders may affect transportation costs, without involving demand. As the Baltic Dry Index recently hit a 30-year low (graph 7 on page 3), such factors could well have a major influence at this point.

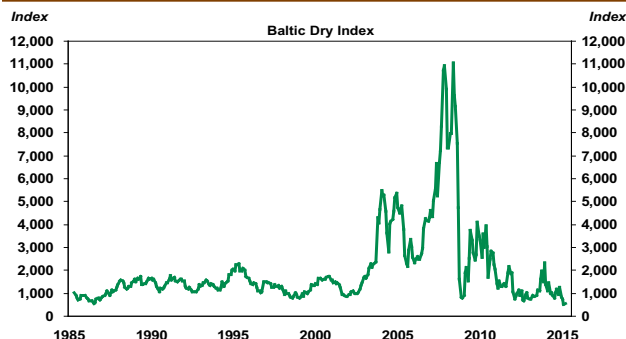
Graph 6 – The Baltic Dry Index points to ongoing weakness in global trade



Sources: Datastream, CPB Netherlands Bureau for Economic Policy Analysis and Desjardins, Economic Studies

Note also that exports as a % of global GDP have stopped improving. They went from 19% to 30% between 1990 and 2008. The ratio has been stagnating since: it was 30% in 2013 (graph 5).

Graph 7 – The Baltic Dry Index is at a historic low, likely because of an oversupply of ships



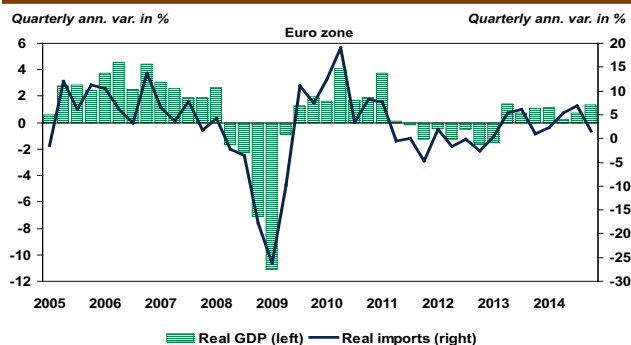
Sources: Datastream and Desjardins, Economic Studies

Nonetheless, trade has shown some weakness since the recession. Several factors may be responsible for it. Some factors are cyclical, while others are more structural.

CYCLICAL FACTORS

Weak growth in advanced economies: The post-2009 recovery was characterized by two very important factors for the global economy. The first is the **U.S. economy’s disappointing growth**. The U.S. economy was slow to return to an acceptable pace, with several factors sapping household and business capacity and confidence for picking up their contribution to growth. The various political crises between Democrats and Republicans undermined the climate for investment and consumption by creating artificial uncertainty. Households and financial institutions also had to keep repairing their balance sheets, delaying recovery by the real estate market and credit in general, despite the Federal Reserve’s unprecedented efforts. It was only as of mid-2013 that the U.S. economy and the job market started to show more satisfactory results. There again, the situation was hampered by abnormally harsh weather at the start of 2014 and 2015. Secondly, the sovereign debt crisis pushed **Europe back into recession** as of 2011, where it stayed until the spring of 2013 (graph 8). This substantially

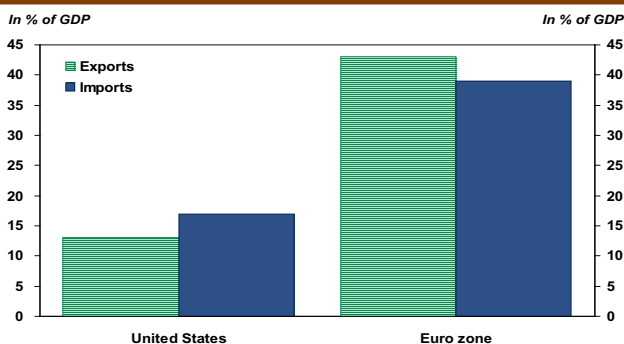
Graph 8 – The euro zone’s economic troubles lessened demand for imported goods



Sources: Eurostat and Desjardins, Economic Studies

lowered Euroland demand for imported products. In addition, the euro was weakened by financial and economic problems as well as by tardy action by the European Central Bank, trimming away some of the benefits of the European economy’s modest upswing. Although Euroland’s economy does not have as big a weight in global GDP as the U.S. economy does, the impact of European weakness on trade is more serious, because the volume of international trade there is more important in relation to the economy (graph 9).

Graph 9 – Trade in the euro zone is relatively much more important than in the United States



Sources: World Bank and Desjardins, Economic Studies

Slowdown in emerging nations: Most emerging nations were less plagued by difficulties during the 2008–2009 crisis. They did see substantial slowing but, in general, it was not as steep as it was in more advanced nations. Output by emerging nations rebounded in 2010; since then, however, a loss of momentum is becoming increasingly evident. Firstly, China is not growing as quickly as we had gotten used to. In the mid-2000s, China’s annual real GDP growth was consistently above 10%; now, the Chinese government is aiming for increases of 7%. For emerging nations as a whole, real GDP growth was under 5% in 2013, compared with nearly 9% in 2007. Most of the geographic zones are seeing a slowdown (graph 10).

Graph 10 – Emerging economies growth has slowed sharply



Sources: World Bank, Datastream and Desjardins, Economic Studies



STRUCTURAL FACTORS

Change in China's economic structure: China's economy is undergoing reform and its industrial structure is changing. Its output of finished goods requires fewer intermediary goods that are made elsewhere than it did before. According to the World Bank, the share of Chinese imports of parts and components compared with its total exports went from a peak of 60% in the mid-1990s to about 35% in 2012. China is exporting the same amount of manufactured goods, but it does not need to import as much to do so. Also, the emergence of a larger Chinese middle class triggers greater economic diversification toward the service industry, which generally requires less international trade.

U.S. oil boom: Since the end of the 2008–2009 recession, the United States has seen a real oil boom, made possible by extraction technologies from fracking. Oil output is up 49.2% since the end of 2009. Simultaneously, imports of petroleum products are down 14.3%. U.S. exports of processed petroleum products lessen the impact on trade. All in all, however, the trade in oil and petroleum products only rose 3.1% since the fall of 2009, while real GDP advanced 12.1%.

Services have a greater weight: The weight of services in global demand is one factor explaining the slower growth by exports and imports. Services account for 67% of global GDP, but only 12% of trade.

Surge in protectionism: The 1980s and 1990s saw a drive toward bringing down tariff trade barriers with the institution of multiple multilateral and bilateral agreements. However, the recent economic crisis brought protectionism back into fashion, where it remained. According to the World Bank and the World Trade Organization (WTO), G-20 members have instituted 1,185 new measures to restrict imports since October 2008.

Financial regulation: Financing for international trade was hard hit during the crisis. The situation has since recovered and the risks associated with letter of credit financing have largely dissipated. However, the more stringent financial regulatory environment since the crisis and calls for deleveraging and greater capitalization for financial institutions have prompted weaker growth by credit in general and trade finance in particular.

MORE ROBUST GROWTH IN THE HORIZON

The main pillar for trade growth remains more lively global economic growth. Here, the situation is looking more promising. Outside of unforeseen events like harsh weather or the labour dispute at West Coast ports, the United States is seeing faster growth. The U.S. dollar's rise makes it even

easier to export to the world's largest economy, which can only help global trade. The net impact of the drop in oil prices is more ambiguous.

The situation is also looking up in the euro zone, where the risks of a triple recession seem to have been dispelled and some indicators, particularly those pertaining to confidence and credit, are posting good results. For the euro zone, the better outlook is dependent on improvement to the trade balance, which is supported by the euro's slide. The global economy will primarily benefit from faster euro zone growth when it is also fuelled by more robust domestic demand. Stabilization in the emerging economies would also provide major support to global trade.

However, it will take structural changes that will make it possible to reverse the trend to deceleration noted since the crisis to see true acceleration by global trade and a return to a pace faster than real GDP growth. More robust business investment, where the demand for imported goods is often more intense, would be an important prerequisite. Greater hope also rests on a new drive toward liberalizing trade. Major bilateral and multilateral agreements are currently being negotiated. If the talks bear fruit, the protectionist trends recently observed would be largely reversed. Two bargaining tables seem especially promising, if only because of the importance of the players involved. The first is the Trans-Pacific Partnership which includes 12 countries, including the United States, Japan, Australia, Canada and Mexico. The European Union and the United States are negotiating the Transatlantic Trade and Investment Partnership. This type of agreement (and others, such as the one recently concluded, but not yet ratified, between Canada and the European Union) could be the spark that sets off more lively global trade growth.

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