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How the recession helped U.S. exporters

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Reduced net imports by value of fuels and lubricants contributed $9.7-billion of the $28.8-billion-per-month improvement in the U.S. trade position between 2007 and 2009.

A major challenge for the United States could be its seemingly permanent negative balance of trade. Warren Buffett -- among others -- has often warned about it. He wrote in Fortune magazine in 2003, "… our trade deficit has greatly worsened to the point that our country's 'net worth,' so to speak, is now being transferred abroad at an alarming rate." This was just after the annual deficit exceeded $400-billion for the first time. He added, "… the rest of the world owns a staggering $2.5-trillion more of the U.S. than we own of other countries." This was, he suggested, largely as a consequence of the need to fund the growing trade deficit.

As it turned out, the negative international investment position of the U.S. in 2002 was $2.0-trillion, not the stated $2.5-trillion. It rose to $3.3-trillion in 2008 and fell back to $2.5-trillion in 2009, remaining there in 2010. (All amounts here are in current dollars.) By 2011, the annual trade deficit -- for which data quickly become available -- had almost doubled to more than $700-billion.

Intuitively, a growing trade deficit and an increasingly negative international investment position should be bad news for the U.S. economy, just as the corresponding predicament would be for a household. This was what Warren Buffett suggested, although he has been saying less about these matters recently.

Not all economists and financiers would agree with Buffett. In his recent book, *Six myths that hold back America*, former Bankers Trust and Bank of America CEO Frank Newman seemed sanguine about both the investment position and the trade deficit. He wrote, "How did China become the owner of so much U.S. debt? It's because Walmart bought a few hundred million dollars of things from China and had to pay them for it. So Walmart calls JP Morgan and puts those dollars in a China bank account run by JP Morgan in New York. That money then gets invested in Treasury bonds. The money didn't disappear and go to China. The money is still in the U.S. economy."

A paradox of negative trade balances is that they can improve when the economy falters. This happened to the U.S. during 2009, the worse year of the recent recession, particularly during the middle third of that year. Comparing May-August 2009 with May-August 2007, the monthly trade deficit fell by 42 per cent from $68.0-billion to $39.2-billion. However, by the same months of 2011, it had risen back to $66.1-billion, almost regaining its mid-2007 level.

Figuring out what exactly changed between 2009 and 2009 and between 2009 and 2011 can be instructive. In both cases, the largest contributor to the changes was the trade category known as "fuels and lubricants" – i.e., mostly oil imports. Reduced net imports by value of fuels and lubricants contributed $9.7-billion of the $28.8-billion-per-month improvement in the trade position between 2007 and 2009. Increased net imports by value contributed $11.4-billion to the $26.9-billion-per-month worsening of the trade position between 2009 and 2011.

If consuming more than is produced is indeed as bad for the U.S. as it is for a household, oil dependence would seem to be a good thing to focus on. Barack Obama's administration has done this in an extraordinary and mostly unheralded manner. New model-year 2010 personal vehicles -- automobiles, SUVs, etc. -- were required on average to have hardly better fuel economy than those of MY1984 (actually 12 per cent better). However, compared with 2010, new MY2016 vehicles will have to be 51 per cent better. Almost approved are regulations for MY2025 personal vehicles, which will have to be 132 per cent better than MY2010 vehicles. As well, for the first time, fuel economy regulations for trucks and other heavy-duty road vehicles are close to approval.

Achieving agreement on all this, among manufacturers, unions, consumer groups, and state governments and agencies, may be the Obama administration's finest achievement to date -- more impressive, I believe, than passage of the heavily compromised health-care legislation.

After fuels and lubricants, the trade category contributing the most to the changes in the US trade balance between 2007 and 2011 was "Consumer goods except automotive." This was the category Frank Newman highlighted in the quotation above about Walmart.

As the U.S. economy faltered between mid-2007 and mid-2009, reduced net imports of these consumer goods contributed $4.6-billion a month to the improvement in the trade position between mid-2007 and mid-2009. However, during the following two years, the same category contributed $6.9-billion a month to the worsening of the trade balance. Consumers appear to have opened their pockets for the purchase of imported goods even more after the trough of the recession than before.

Pockets were opened in particular for goods from China, imports of which fell by 13 per cent between 2007 and 2009, but increased by 38 per cent between 2009 and 2011. The overall trade picture in consumer goods was not as bad as this suggests because between 2009 and 2011 the U.S. experienced a surge in exports, some to China and more elsewhere.

The next most important categories -- industrial supplies and automotive -- between them made the strongest contribution to the U.S. trade balance between 2007 and 2011: a net positive effect of $6.1-billion a month. Again, relative modest surges in exports in each case were contributing factors.

In brief, the convulsions in the U.S. economy during the last four years have raised more questions about the significance of the continuing U.S. trade deficit. Recession reduces the deficit, but the cure may be worse than the disease, if indeed the deficit is a disease. The convulsions have highlighted the importance of oil imports, and the remarkable steps being taken to reduce this aspect of the United States' economic vulnerability. Recession-induced reductions in imports appear to have been temporary, but there are hints that the economic downturn of 2008 and 2009 may have had a net stimulating effect on U.S. exports.

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