

U.S. Trade Springs Back

Trade flows tend to be procyclical: A country's volume of imports and exports contracts during recessions and expands during recoveries. During the Great Recession of 2007-09, however, most advanced economies experienced an unprecedented collapse in trade that surprised almost everyone.¹ The United States was no exception. From 2007:Q4 to 2009:Q2, real gross domestic product (GDP) declined 4 percent, but U.S. imports and exports declined a staggering 25 percent and 14 percent, respectively. Since June 2009, however, the value of international trade (imports and exports) has remarkably rebounded to pre-crisis levels. What explains these dynamics?

Nearly 90 percent of international trade transactions rely on some form of credit or financing. Initial empirical work seemed to suggest that the near disappearance of trade finance, during what was indeed a *financial crisis*, was the likely cause of the large trade decline. During the crisis, countries with higher inter-bank rates (viewed as evidence of tighter credit markets) had greater declines in exports to the United States, with the largest declines in sectors that relied more heavily on financing.²

Although trade finance may have played a role in the decline in trade, its significance relative to other potential causes is disputed. Anecdotal evidence suggests that the lines of credit made available to exporters in advanced economies after the April 2009 G-20 meeting were underutilized.³

Moreover, two other facts suggest that trade finance is not the only explanation for the trade collapse and rebound. First, although some countries experienced milder or lagged financial stress, the behavior of trade flows is highly synchronized across countries. Second, capital goods, industrial supplies, and automotive vehicles constitute almost the entire decline in U.S. imports and exports from late 2008 to early 2009—a decline suspiciously similar to the downward adjustment in manufacturing output, which was predominantly concentrated in machinery, vehicles, and raw materials. Even at the simplest level of disaggregation (see chart), it is clear that service imports during the Great Recession contracted much less than goods imports, despite their tendency to track each other in earlier periods.

Although some goods industries may be particularly affected by the availability of trade finance, one explanation consistent with the observed patterns and emerging literature is that inventory adjustments in response to declining demand for durable goods caused

most of the trade collapse.⁴ Although durable goods represent a modest share of GDP (8.6 percent in 2008), they account for a much larger share of trade (45 percent in 2008). Therefore, when demand for durable goods declined and inventories grew, new international orders were temporarily suspended to allow excess inventory to clear. For example, reports indicate that slow sales in November 2008 prompted auto companies (e.g., Toyota) to lease space near U.S. ports to temporarily store newly imported cars.⁵ During the recent recession, inventories recovered after trade rebounded (see chart), a pattern consistent with the recovery from the 2001 recession. Together, the evidence suggests that the combination of a slowdown in trade finance and inventory adjustments likely explains the recent trade dynamics.

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¹ A similar collapse occurred in emerging economies—a common event for most of them.

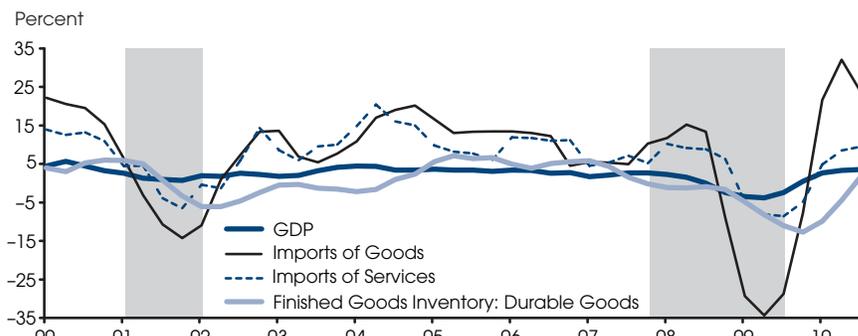
² Chor, Davin and Manova, Kalina. “Off the Cliff and Back? Credit Conditions and International Trade During the Global Financial Crisis.” VoxEU.org, February 15, 2010.

³ Korinek, Jane; Le Cocguic, Jean and Sourdin, Patricia. “The Availability and Cost of Short-Term Trade Finance and Its Impact on Trade.” Working Paper No. 98, OECD Trade Policy Working Papers, June 2010.

⁴ Alessandria, George; Kaboski, Joseph P. and Midrigan, Virgiliu. “The Great Trade Collapse of 2008-09: An Inventory Adjustment?” NBER Working Paper No. 16059, National Bureau of Economic Research, June 2010; Eaton, Jonathan; Kortum, Samuel S.; Neiman, Brent and Romalis, John. “Trade and the Global Recession.” NBER Working Paper No. 16666, National Bureau of Economic Research, January 2011.

⁵ See Richtel, Matt. “A Sea of Unwanted Auto Imports.” *New York Times*, November 19, 2008.

Year-to-Year Changes in U.S. GDP, Imports of Goods and Services, and Finished Goods Inventory



NOTE: Gray bars indicate recessions.

Views expressed do not necessarily reflect official positions of the Federal Reserve System.