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Demystifying the decline in world trade growth

Summary

There has been a growing concern that global trade has slowed down more than warranted by the overall slowdown in global growth.There is the added concern that even when the G3 (G4 adding China) have clearly bottomed, trade will not recover with severe consequences for the "trade dependent" EMKs. We show that the evidence is not unequivocal and that, in any case, not all countries are exports driven, especially China. However the current decline in exports growth (and its mirror image imports, something permanently forgotten in commentaries) does have macro and country/sector implications, especially for commodities producers, including oil, and for shipping.

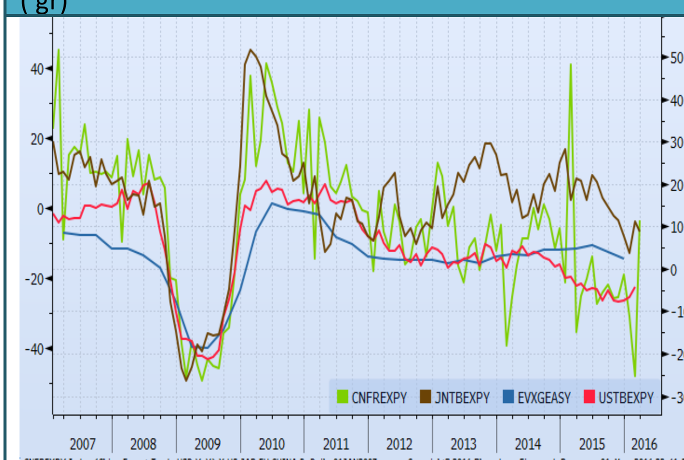
Investment Conclusions

As it is difficult to prove that the deceleration in trade growth is not structural but only cyclical, the best that can be done is to take a rolling one-year view rather than the apocalyptic "we are all going to die". The macro outlook for commodities exporters stays negative, with oil prices likely to stay range bound while supply is not under control. China' bottoming will not be trade driven as will also be the case with the US and EU, while Japan's case is more complex in the absence of domestic growth drivers. Most commodities will stay under pressure but some sectors in shipping will continue to benefit from firm freight rates.

The facts, such as they are not !

The WTO has forecast a 2.8% growth of world trade for 2016 the same for 2015.In comparison, in 2011 trade grew nearly double that rate, while during the pre -2008 crisis period the average growth was around the 6.0% mark. Hence world trade growth has declined very significantly. Fig 1 shows the exports growth rate for the G4 countries with all of them on a broadly decelerating trend since the sharp rise in 2010, the latter being the result of a low base effect. Exports from the US may, just, have bottomed, while China's sharp spikes could be concealing the start of a bottoming trend as well. The same may not be true for Japan, while exports from the Eurozone continue to decelerate. The data in Fig.2 shows growth of imports for the G4 all of whom looking as if they are bottoming. In interpreting these data (all in value terms) it is important to keep several points in mind and specifically volumes, values and exchange rates. Volume and value of trade can play havoc with this picture. During this period of falling commodity prices for some goods, such as oil, some prices have been down but volumes up. Actually, according to data from the CPB World Trade Monitor, the volume of trade has been continuously rising registering a 40% overall growth between 2009-2015. Value, however ,is now at the same level as in 2009, having fallen almost continuously since 2011.One is tempted instinctively to go for value rather than volume, but this could be misleading.Taking as example,the price of oil,it has fallen ,while volumes of oil traded has risen, potentially giving an overall falling value of oil traded. For an economy such as Venezuela or Russia with depreciated currencies, the declining overall USD value could represent rising value in local currency terms. This has been partially true for Argentina's wheat exports.Hence declining volumes and even values may have different impact for different economies.

Fig.1: Exp. Yoy%, US(red), EU (blue), Jap (Brown),PRC (gr)



Source: Bloomberg

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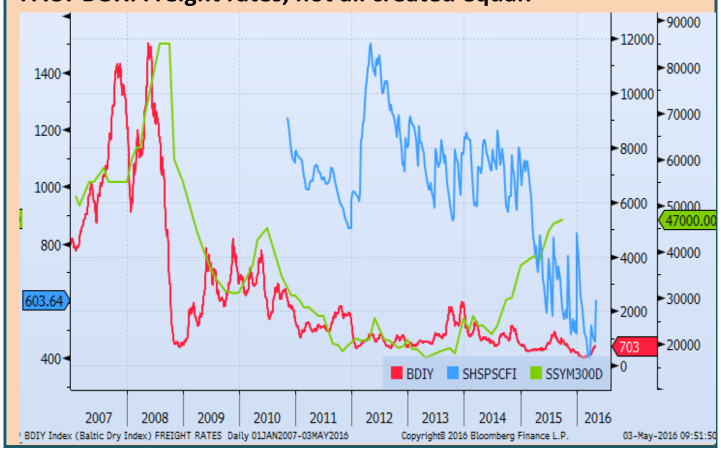
Freight becomes fright , but don't blame China !

For a long time now the parlous state of the Baltic Dry Index (red in the Box) had been the proxy of the poor state not only of the shipping industry but also of the world trade in general.

But even here, the dangers of expostulating about "shipping" without specifying individual sectors can be misleading.Dry cargo, such as grains, ores, coal etc, have been hit by the slowdown, as have containers (blue in the box). The latter have also been squeezed by oversupply of capacity. At this point, it is important to point out the circularity of the"overcapacity" argument. If demand drops, even if not one ton of extra shipping had been added to the global fleet, there will be "overcapacity"! As ordering and building ships take time,entrance of new capacity can be unfortunately timed. Equally surges in demand can hit limited capacity.However not all is bad as the data in the Fact Box show.

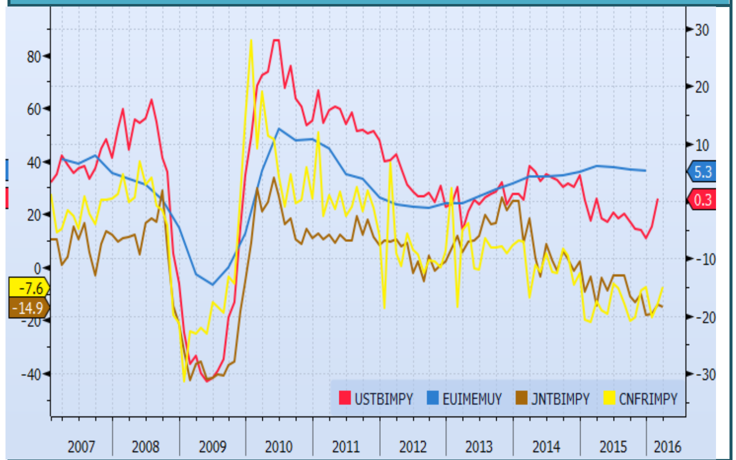
FACT BOX: Freight rates, not all created equal!



Source: Bloomberg

As the green line shows, freight rates for Very Large Crude Carriers (VLCC) have boomed reflecting the low oil prices which have maintained demand for oil, the rise in supply as Saudi Arabia refused to lead supply control while Iran, Iraq and possibly Libya will be adding to oil flows, and US shale also contributing. Congestion in ports and refineries led to VLCC being used as floating storage tanks! Whether this boon to a section of shipping will last for the rest of 2016 will depend on the price of oil staying low thus maintaining this cycle of events, and this is quite likely. The charts in the Box point to the likelihood that the drop in most freight rates may be bottoming, in line with the evidence presented in Figs 1& 2. World trade trends are pointing to a very modest bottoming out, more cyclical than structural.

Fig 2: Imp. Yoy%, US (red), EU (bl), Jap (Br) PRC (yel)



Source : Bloomberg

Altogether now

We have left the analysis of the role of China in all this last. Some aspects of the deceleration of global trade can be attributed to China's slowdown, especially in its imports of iron ore, but not on its imports of oil, for example. We have explored this and related issues in detail in past issues of Econotes (Nos 40,46) why the Chinese economy is not exports driven, as indeed is also the case with those of the US, EU and partially Japan.Hence the slowdown in the global trade growth can not be "accused" simultaneoulsy of causing the global slowdown and being the conseuence of ! The likelihood is that the long- drawn prorcess of recovery since 2007-8 has taken an equally long- drawn out toll on trade. Last but not least, the usual accusation that China has kept the CNY undervalued to support its exports during this tought period, always leaves out an important point.If that was true, then China deliberately kept the prices of its imports high thus partially negating the putative advantage of the "cheap" CNY given the very substatial component of imports in China's exports ! One can never win !

Andrew Freris (writing completed on 4/5/2016)