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Global trade fast out of the gates but supply chain issues continue to bite

World trade has proved resilient in the pandemic, rising strongly after an 18% fall in May. After the boost from initial rebound effects, further recovery will be harder, with new lockdowns, a downturn in investment and capacity issues along supply chains as the biggest risks to trade growth

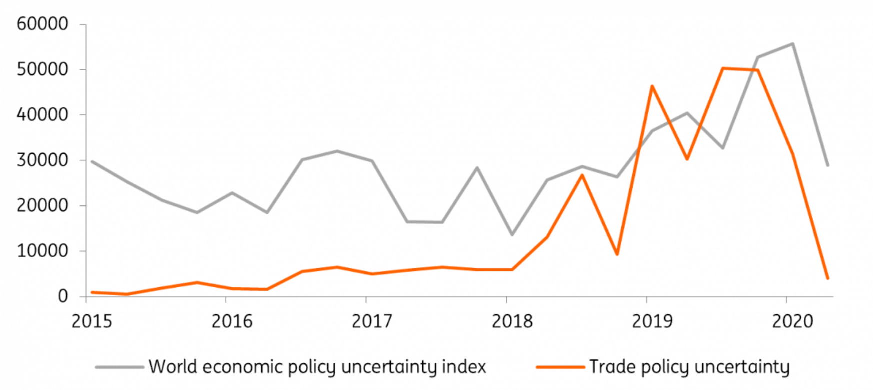
Source: Shutterstock

Not now, trade policy

In 2018 and 2019, global trade developments dominated the discussion about global growth. Trade war concerns and Brexit developments were important drivers of the slowdown of GDP growth and industrial downturn in advanced economies over the past two years.

While US-China relations and Brexit are far from resolved, trade policy uncertainty has fallen back. Businesses are now, of course, dealing with uncertainty on many other fronts, including falling demand and economic policy as governments respond to Covid-19 (**Chart 1**).

Chart 1: Trade policy uncertainty has improved in 2020

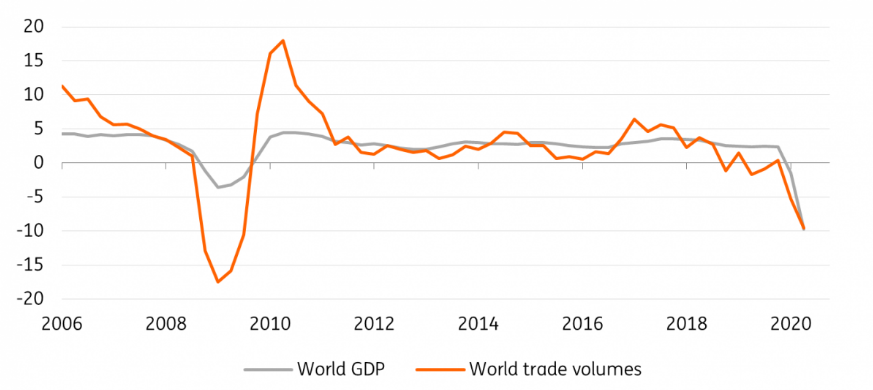


Source: Macrobond

A different type of crisis

At first, Covid-19 affected markets in Europe and the US through disrupted supply chains, but then economies worldwide quickly saw huge falls in demand as they went into lockdown. World trade has contracted alongside world GDP, with both falling around 10% in the first two quarters of 2020. The similar falls are in contrast to the Global Financial Crisis (GFC), when world trade fell six times as much as GDP (**Chart 2**).

Chart 2: World trade and GDP are sticking close together, so far

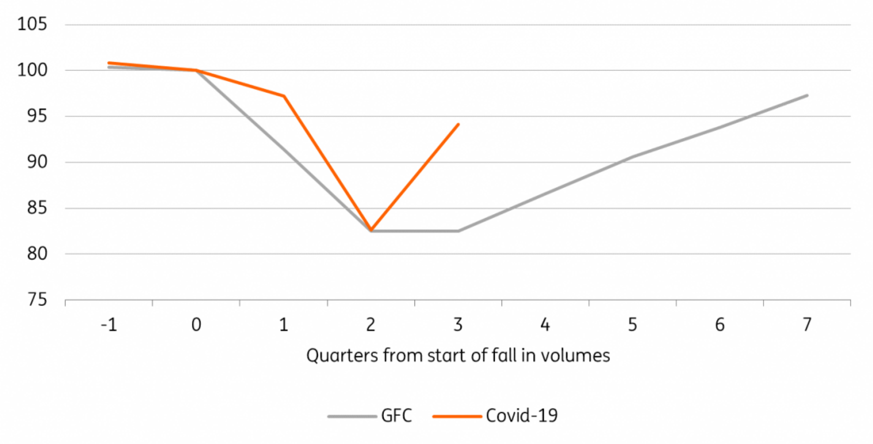


Source: World Bank and CPB

A number of reasons have been put forward for the huge decline in world trade in 2008-09, the dominant one being the disproportionate decline in demand for investment which is more import-intensive than other parts of the economy. In 2020, the falls in private consumption and investment have been similar, making the declines in global trade and world GDP much more synchronised.

As the decline in GDP has been largely due to the locked down economies across the globe in 1Q and 2Q, a large jump in GDP has followed mechanically from economies reopening. World trade volumes resumed growth in June, and by July had recovered two-thirds of their pre-pandemic level, a much faster path of recovery than seen in the aftermath of the GFC (**Chart 3**).

Chart 3: World trade has bounced back faster than in the GFC

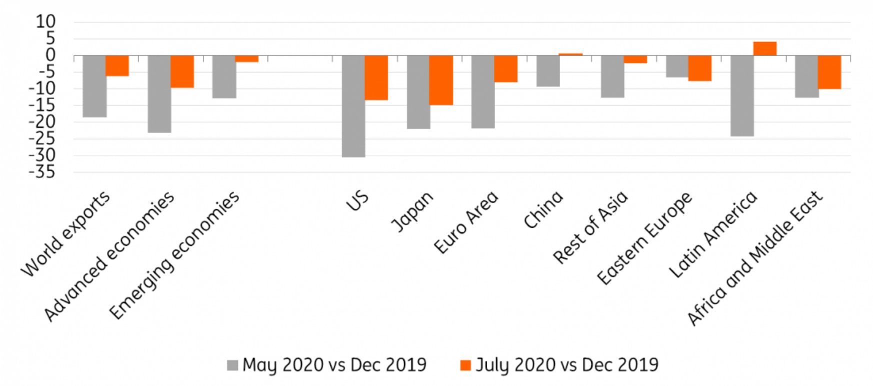


Source: CPB, ING calculations

Not all countries have suffered alike

In July, export volumes were back at -6.2% below their December 2019 levels, having bottomed out at -18.5% in May. Some regions have already recovered to pre-pandemic levels of exports, and the relatively quick domestic recovery in China has helped some markets more dependent on Chinese demand. Among advanced economies, the US is lagging behind Japan and the EU in terms of recovering its export flows (**Chart 4**).

Chart 4: The uneven global exports recovery



Source: CPB, ING calculations

Much of the US's export weakness reflects the stringency of Covid-19 measures still in place in its major trading partners. Exports to China continue to be significantly affected by the trade war tariffs. The tariff hikes caused exports to drop in 2019, and flows remain depressed in 2020 despite the 'phase one' deal struck between the two countries (**Table 1**). Of course, extraordinary circumstances have arisen since the deal was struck in January, but China's imports from the US are currently falling some $100bn short of the deal, which would have been a much-needed boost to US exports.

Table 1: US exports are still sharply down, in spite of the 'phase one' deal with China

Annual difference in trade flows, year to July (%)	
EU imports from US	-31.3
EU exports to US	-22.6
China imports from US	-3.4
China exports to US	-14.7
EU imports from China	-1.5
EU exports to China	-0.3

Source: Eurostat, US Bureau of Economic Analysis

Covid-19 goods are in demand worldwide

After the rapid return of domestic demand and global trade, the coming months are likely to see a slowdown of global trade in tandem with the global economy. Of course, second wave effects could cause another downturn if restrictive measures were to become more far-reaching and national than they are at the moment, which is not our base case but also not unlikely.

Focusing more on specific trade effects, we see that the recovery of trade has not involved a significant shift in the mix of traded goods so far. Retail sales have been strong as economies have reopened, but that is not yet reflected in more trade in consumer goods, as capital goods have remained close to half of all traded products by value (**Chart 5**).

Chart 5: Exports of capital goods have continued throughout the pandemic

Source: UN Comtrade, ING calculations

In terms of specific products performing well, we do note a surge in Covid-19 related goods, including test kits, face masks, disinfectants, and ventilators. Accounting for about 5% of imports before the pandemic started, these goods have increased their share of world trade to 11%. This increase may partly reflect price rises, but is also clearly due to increased demand for these goods from around the world, which can be expected to continue supporting world trade flows into next year.

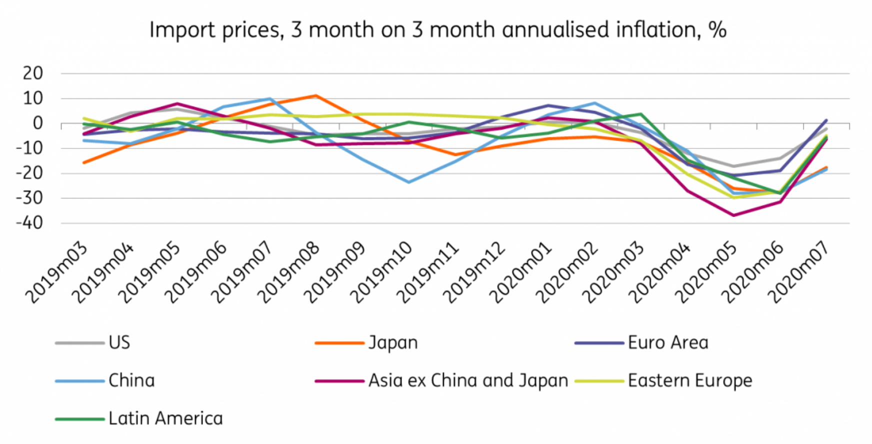
Supply chain distortions can still put the brakes on the recovery

While supply chain problems played a marginal role compared to the drop in demand in the initial decline and subsequent recovery of global trade, they may become more of a constraining factor in the next stage of the recovery. In part because some countries may face more severe restrictions again over the winter months, but also because of capacity problems along supply chains.

While the quick reopening of Chinese industry has solved some of the supply chain problems facing the global economy at the start of the coronavirus crisis, the increase in blank sailings (container ship cancellations) has led to ongoing container shortages around the world, and port restrictions are delaying container handling. Travel restrictions are limiting air freight capacity.

As new orders for export goods have started to recover, deliveries of inputs continue to be significantly delayed, according to manufacturers. This has caused businesses to run down inventories to make sure that recovering demand can continue to be met. Air and sea freight prices have also begun to rise again, which in turn is putting upward pressure on import prices (**Chart 6**).

Chart 6: Import price inflation is on its way back



Source: CPB

While restrictions persist, they will continue to weigh on trade volumes and make the recovery after the initial rebound phase harder to achieve.

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