QNB Economics
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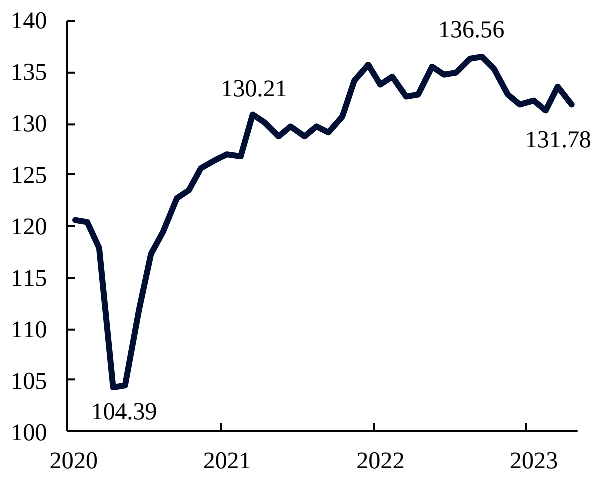
Global trade is set to recover in the coming months

International trade is a key indicator of the dynamism of the global economy. Trade data reflects, like few other indicators, the strength of economic conditions across different countries. In other words, trade reveals the appetite for final goods by consumers, as well as the need for intermediate and capital goods by firms, and their production capabilities. Thus, trade volumes fluctuate in line with the global cycles of economic expansion and contraction, and are therefore an informative gauge of macro conditions.

The latest data releases show that trade volumes have stabilized. According to the Central Planning Bureau of Netherlands for Economic Policy Analysis (CPB NEPA), global trade volumes have remained broadly unchanged since the end of last year, after falling from the peak registered in September 2022. This has been a reflection of economic resilience in front of significant headwinds, as we have discussed in a previous commentary.

Global Trade Volume
(index, 2010=100, seasonally adjusted)



Source: Haver, Netherlands BEPA, QNB Economics

However, these statistics provide a backward-looking picture of the dynamism in trade, rather than a forward-looking outlook. Data from CPB NEPA, for example, has a lag of 3 months, and is therefore of limited value to form a view of future trends. Thus, it is useful to make use of forward-looking, or leading indicators that help anticipate upcoming trends.

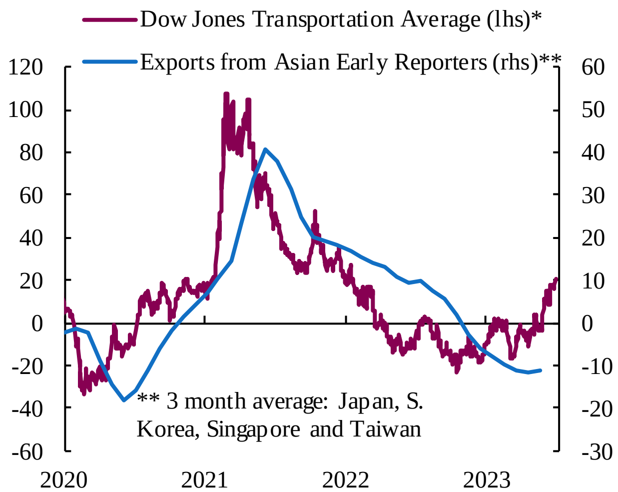
In our view, leading indicators suggest that global trade may have reached the bottom of its slump and is set to begin a phase of recovery. In this article, we discuss three main factors supporting our view.

First, foreign exchange movements are likely to provide support to international trade. Historically, global trade tends to be negatively correlated with the USD. As the dollar weakens, global trade expands on the back of cheaper imports outside the US. This is due to the fact that more than 50% of all trade transactions are denominated in USD. As the USD has depreciated by 10% since its peak in September 2022 against a basket of major currencies, global trade should be supported by expanding imports in countries other than the US. Such dynamics could be further boosted by additional USD depreciation, if the US Federal Reserve halts its tightening cycle ahead of the European Central Bank and the Bank of England.

Second, the global manufacturing cycle is likely reaching its bottom in major advanced economies. The manufacturing cycle in the US has typically lasted 3 years, equally divided into 18 months of contraction and 18 months of expansion. According to the Institute of Suppy Management survey tracking activity in the manufacturing sector, the current down-trend began in mid-2021. Since then, industrial activity has already stabilized. In the Euro Area, manufacturing has followed similar dynamics as in the US, and is expected to recover in the second half of the year on the back of improving real incomes, the receding energy crisis and lower natural gas prices, and the need to replenish inventory levels after a destocking phase that has weighed on activity. Global trade is expected to receive an additional boost as manufacturing seems to be bottoming out in the two major advanced economies.

Third, expectations of forward-looking investors suggest renewed optimism and anticipate an improvement in the international trade outlook. A useful indicator that embeds these expectations in stock markets is the Dow Jones Transportation Average, an equity index comprised of airlines, trucking, maritime transportation, railroad and delivery companies. The performance of this indicator tends to foresee global exports by at least 3 months. Since its bottom in April this year, it has recovered by 14%, suggesting that global trade should return to expansionary mode in the second half of 2023.

Global Trade Key Indicators
(%, year-over-year)



Source: Federal Reserve Bank of St. Louis, Haver, QNB Economics

All in all, global trade volumes seem to have bottomed out, and leading indicators suggest that they are entering a phase of recovery. Trade is a good reflection of macroeconomic conditions and provides another metric of the resilience of the global economy.

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