I THE TRADE SITUATION IN 2007

A Introduction

Growth in world output and trade decelerated in 2007. Weaker demand in the developed economies reduced global economic growth to 3.4 per cent from 3.7 per cent, roughly the average rate recorded over the last decade. At some 7 per cent, growth in the developing regions was nearly three times the rate recorded in the developed regions and the contribution of the developing countries to global output growth in 2007 exceeded 40 per cent.[1] Economic expansion in the least-developed countries fully matched the growth rate recorded by developing countries as a group in 2007, sustaining a pattern that has been maintained since 2000.

Domestic demand weakened sharply in the United States, which reduced the external deficit and led to the weakest annual GDP growth rate (2.2 per cent) since 2002. A further widening of the external surplus contributed to more than one half of Japan's 2.1 per cent GDP growth rate in 2007. Europe recorded GDP growth of 2.8 per cent – a somewhat better performance than both Japan and the United States last year. Stimulated by sharply higher export earnings and rising investment, Russia's economic growth of 8 per cent was the strongest annual rate since 2000. In Central and South America, Africa, the Middle East and developing Asia, economic expansion rates showed no signs of deceleration in 2007. The most populous developing countries – China and India – continued to report outstandingly high economic growth.

The favourable investment climate maintained in developing regions and the Commonwealth of Independent States (CIS)[2] more than offset the adverse effects of financial market turbulence, especially that arising from the US sub-prime market crisis in the second half of 2007. Despite the adverse effects of scarce credit on the volume of mergers and acquisitions, global foreign direct investment (FDI) flows continued to rise. The UN Conference on Trade and Development (UNCTAD)[3] provisionally estimated that global FDI inflows rose by 18 per cent to US$1.54 trillion in 2007. Foreign direct investment flows to Latin America (eg, Brazil, Chile and Mexico) and Russia have been particularly strong (50 per cent and 70 per cent respectively). FDI flows to developing Asia and the new EU member states are estimated to have seen less dynamic growth in FDI inflows in 2007 than in the past.[4]

Variations in the exchange rates of major traders in 2007 did not always result in effective exchange rate developments conducive to a reduction in global imbalances. While the US real effective exchange rate depreciated and contributed to a smaller current account deficit relative to its GDP, the real effective exchange rate of a number of current account surplus economies in East Asia (such as Japan, Chinese Taipei, Hong Kong, China) also decreased, contributing to new peak levels in the ratios of their respective current account surpluses to GDP in 2007.[5] The real effective exchange rates of the Chinese and Singaporean currencies appreciated by 2 per cent and 7 per cent respectively in 2007, without arresting the rise in their respective current account surpluses.[6] The real appreciation of the euro had differing consequences for the export performances of euro-zone economies. Thanks to a 20 per cent increase in its exports, Germany remained the world's leading exporter of merchandise.

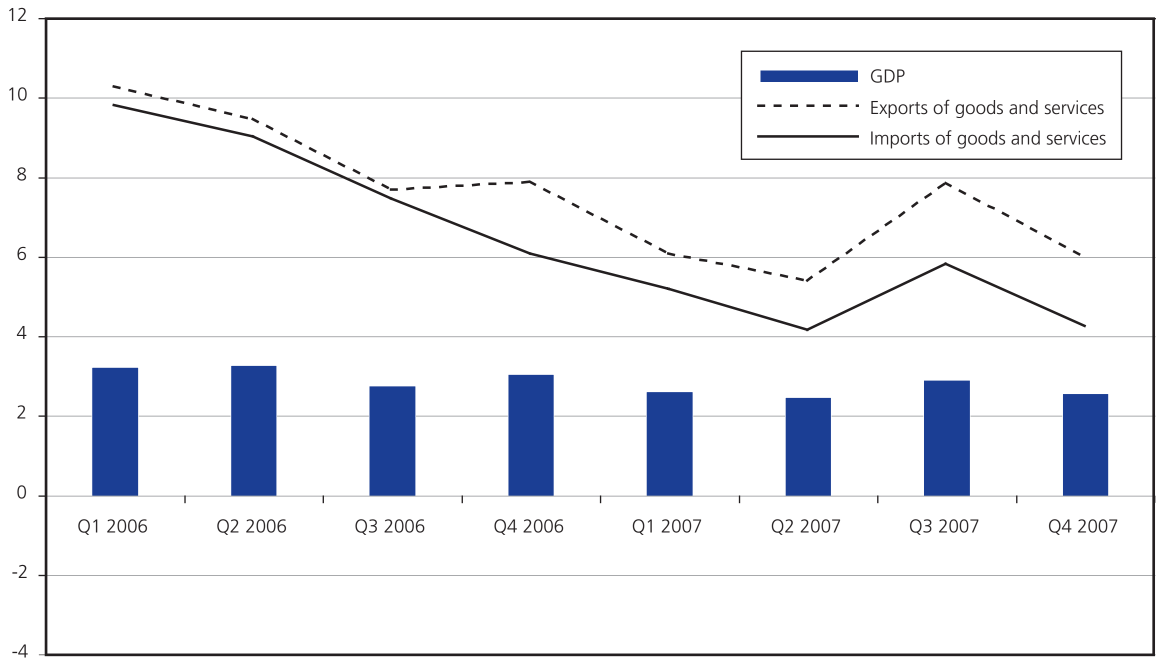
The length of the global upswing and the strength of economic activity outside the industrial regions contributed to a further rise in the price of fuels and pushed up domestic inflation rates. At the end of 2007, consumer prices in developed and developing economies were increasing faster than at the beginning of the year, by about 1 and 2 percentage points respectively.

Weaker demand in the developed countries provided a less favourable framework for the expansion of international trade in 2007 than in preceding years (See Chart 1). Consequently, world merchandise exports grew in real terms (that is, at constant prices) by only 5.5 per cent, compared to 8.5 per cent in 2006. Lower import growth than in the preceding year was observed in North America, Europe, Japan and the net oil importing developing countries in Asia. This downward trend outweighed the higher import growth observed in Central and South America, the CIS, Africa and the Middle East. It is estimated that the developing countries as a group accounted for more than one half of the increase in world merchandise imports in 2007.

Among the leading traders, China's (real) merchandise trade expansion remained outstandingly strong in 2007 as lower export growth to the US and Japanese markets was largely offset by higher export growth to Europe and a boom in shipments to the net-oil-exporting regions. Despite a vigourous domestic economy, weaker demand in some of China's major export markets and a moderate real effective appreciation of the yuan, import growth continued to lag behind export growth.

The strength of overall economic growth in the developing world should not blind observers to the sometimes large differences in the situation faced by individual countries within this grouping. While higher prices for minerals and various food products have improved the prospects of some developing country exporters, a large number of developing countries are net importers of fuels and food and have been adversely affected by the surge in the prices of these commodities. Surging food prices have become a cause of civil strife in some countries and the situation poses serious challenges for governments. The adverse consequences of turmoil on financial markets will not only affect US demand growth but also lead to further downward revisions in economic growth for Japan and Western Europe. As world trade responds strongly to variations in global economic activity a stronger than projected deceleration in world economic growth could cut trade growth much more sharply, to significantly less than the 4.5 per cent predicted above. (Income elasticity – how much trade responds to changes in income – has been between 1.5 and 2 over the last decade, indicating that trade reacts significantly.)

Chart 1
Real GDP and trade growth of OECD countries, 2006-07
(Percentage change on a year to year basis)



Source: OECD National Accounts.