

Economic Indicator — July 2, 2021

May Trade Report: Net Exports Set to Be Neutral Force on Q2 GDP Growth

Summary

- The U.S. trade balance widened to a deficit of \$71.2 billion in May, as imports (+1.3%) outpaced exports (+0.6%).
- Export growth was constrained by a 4.6% decline in auto exports and a 1.0% drop in capital goods exports. But, consumer goods exports rose a strong 5.8% during the month, reflecting a pickup in demand amid America's international counterparts.
- Imports were boosted by a 5.2% gain in industrial supplies. Consumer goods imports also held up despite more recent weakness reflected in the U.S. personal spending data.
- Services trade continued to slowly recover with exports rising 1.5% and imports up 1.8% during the month.
- May's trade report does not materially change our expectations for net exports in the second quarter.

Economist(s)

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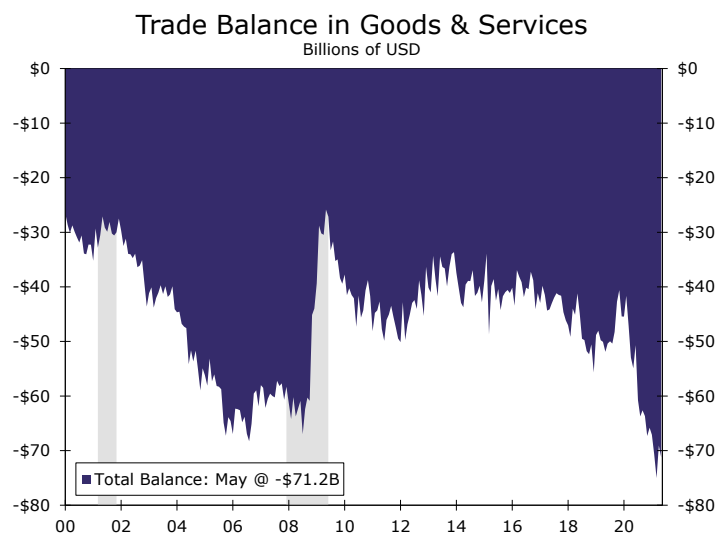
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U.S. Trade Balance Widened to Second Largest on Record

The U.S. trade balance widened to a deficit of \$71.2 billion in May from \$69.1 billion in April. This is just short of the record \$75.0 billion deficit reached in March. Both exports (+\$1.3 billion) and imports (+\$3.5 billion) advanced during the month. Today's trade report doesn't materially change our expectations for net exports in the second quarter, and we look for trade to be a pretty neutral force on growth for the quarter.



Source: U.S. Department of Commerce and Wells Fargo Securities

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Goods Trade Advances but Details Mixed

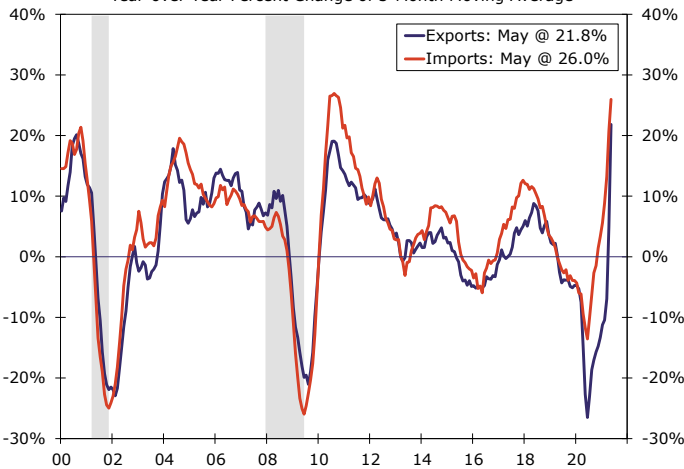
Trade flows continued to recover in May but the underlying categories remain volatile. The U.S. deficit in goods trade increased \$2.3 billion to \$89.2 billion. Exports of goods advanced 0.3%, but growth could have been even stronger if it were not for a 4.6% decline in auto exports. Capital goods exports also moved lower during the month due to a large \$1.4 billion decline in exports of civilian aircraft. Despite renewed interest in travel, the recovery in aircraft orders continues to stumble amid the relatively recent resumption of Boeing's 737 MAX deliveries. Industrial supplies and materials eked out a modest 0.3% gain, while consumer goods exports surged 5.8%, the second largest monthly gain since coming out of lockdowns last year. With economies recovering overseas, demand is increasing for a range of U.S. consumer products. There was a notably strong gain in pharmaceutical preparations last month.

Goods imports rose 1.2% in May. Imports continued to help supplement some of the weak output seen domestically. Industrial supplies and materials rose 5.2%, reflecting large gains in crude and fuel oil as well as some other key inputs (lumber, iron and chemicals). But, capital goods orders slipped 1.8% due to a sizable, \$1.3-billion pullback in computer imports and a \$578 million decline in telecommunications equipment. Our best read is that this reflects some payback after demand was pulled forward in these two categories last year to help facilitate work-from-home throughout the pandemic.

Auto imports were also weak, declining 0.6%. While weakness here likely continues to reflect ongoing supply constraints in the sector, demand has wobbled recently as auto sales declined by the most since lockdowns in May, and slipped again in June. Consumer goods imports overall rose a modest 0.4% and given the recent weakness in domestic spending on goods, likely reflects the inventory dynamics we've been communicating in recent months. As personal spending in the U.S. transitions back to the much larger services sector, consumer goods imports may hold up given the need to replenish exceptionally lean retail inventories.

Capital Goods Trade Ex. Autos

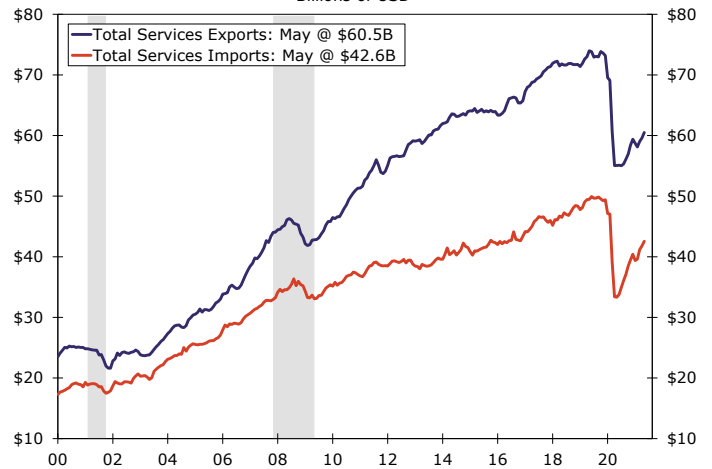
Year-over-Year Percent Change of 3-Month Moving Average



Source: U.S. Department of Commerce and Wells Fargo Securities

Total Exports & Imports of Services

Billions of USD



Source: U.S. Department of Commerce and Wells Fargo Securities

Slow but Steady Recovery in Services Trade

The real strength from today's report came from the services side of trade where the trade surplus rose to \$17.9 billion in May from \$17.8 billion in April. Exports rose 1.5% and imports advanced 1.8% during the month. Services trade continues to exhibit a slow but relatively steady recovery. Exports have risen in nine of the past 12 months, while imports have risen in all but one (Jan-2021) of the past 12 months. Both sides of services trade remain constrained by travel and transportation services specifically, which we expect to meaningfully pick up this year now that international travel restrictions have been relaxed and most indications of travel demand are rapidly improving.

Today's report for May doesn't materially change our expectations for net exports in the second quarter. Real exports slipped 2% while imports were flat. With real exports coming in a touch weaker than previously expected, the boost may be a bit softer than the 0.3 percentage point boost we're currently forecasting. Nonetheless, trade should generally be a neutral force for the quarter.

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