

Economic Indicator — November 7, 2023

Larger Trade Gap Shows Downside of Robust Domestic Demand

Summary

The September trade report makes sense of the initial GDP estimate which revealed a drag from trade in Q3 when most anticipated a slight boost amid a trend narrowing in the trade gap. Exports grew in September, but imports grew even faster amid resilient domestic demand.

Economist(s)

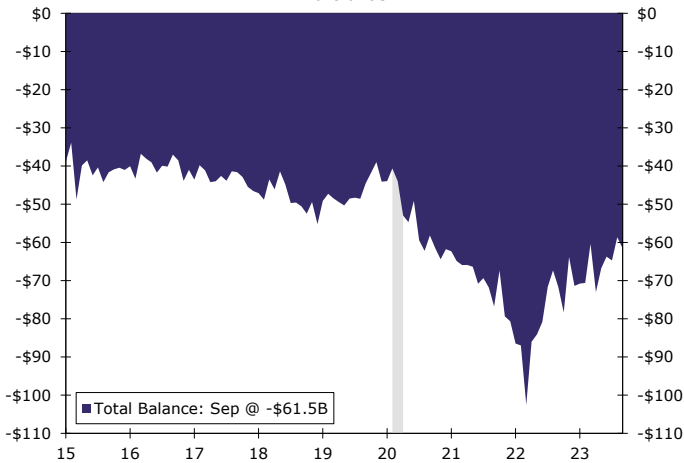
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Trade Balance in Goods & Services
Billions of USD



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

Bridging the Gap Wasn't Going to Be Easy

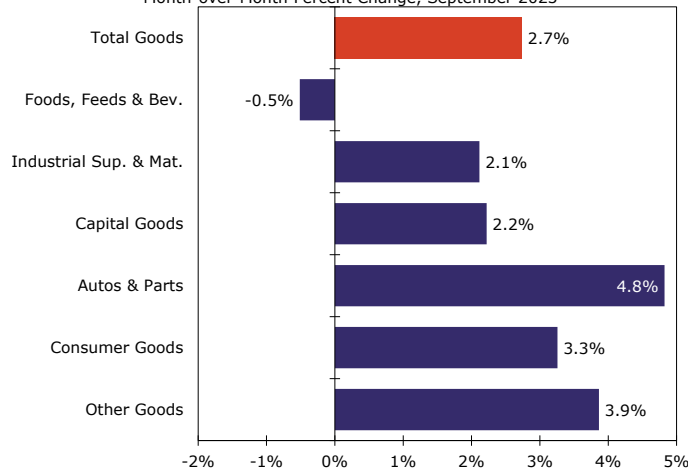
With a trend normalization toward pre-pandemic norms underway, it did not immediately make intuitive sense to see trade *subtracting* from third quarter growth in the first estimate of that quarter's GDP. It is a reminder that trade flows can be volatile on a month-to-month basis. The trade deficit widened to \$61.5B in September, undoing about half of the trade gap's narrowing in the prior month ([chart](#)). Imports increased 2.7% outpacing exports which rose 2.2%. The outturn, along with a slight downward revision to August's balance, makes sense of the advance Q3 GDP report.

Still, over the past year, the trade deficit has narrowed back toward its pre-pandemic norm. Exports and imports have downshifted on trend, as global growth has plateaued and domestic demand has slowly moderated.

Sometimes strong domestic demand can result in a larger trade gap, especially if demand is less robust in other economies. A pickup in consumer goods and auto & parts imports contributed to the deficit widening in September ([chart](#)). That was certainly the case this month as consumer spending on durables goods was robust in September. The strength in durables spending was at odds with widespread expectations for a slowdown in durables spending amid elevated prices and borrowing costs. The consumer's underlying resilience has supported autos, where trade has been particularly bouncy as the industry is still recovering from pandemic-related disruptions and strike activity more recently.

Monthly Change in Goods Imports

Month-over-Month Percent Change, September 2023



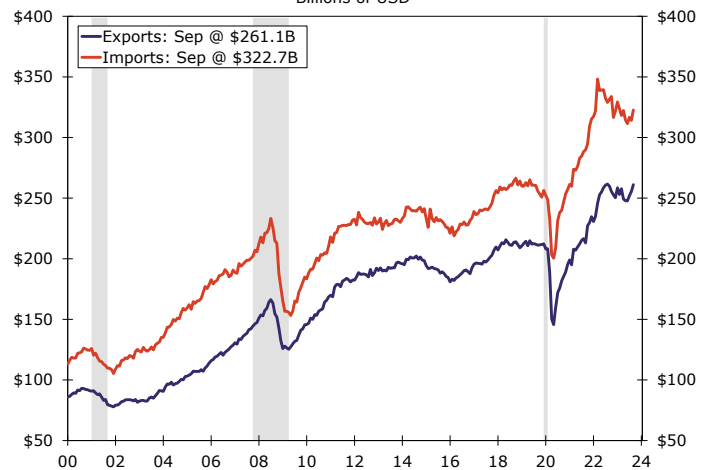
Source: U.S. Department of Commerce and Wells Fargo Economics

Exports were strong across the board. The monthly gain was enough to pull the year-over-year change above zero for the first time in five months ([chart](#)). While exports ended the summer on strong note, the recent strengthening of the U.S. dollar makes U.S. goods more expensive to foreigners which we expect could restrain export growth in the coming months.

At the same time, higher financing costs will eventually catch up to even the intrepid U.S. consumer. The business activity component of the ISM services index shed 4.7 points to come in at a five-month low of 54.1. Slowing domestic demand should lead imports lower, which in turn will lead net exports to be a mostly neutral factor on headline growth in the coming quarters.

U.S. Exports & Imports

Billions of USD



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

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