Economic Indicator — January 5, 2023

U.S. Trade Deficit Narrows Sharply in November

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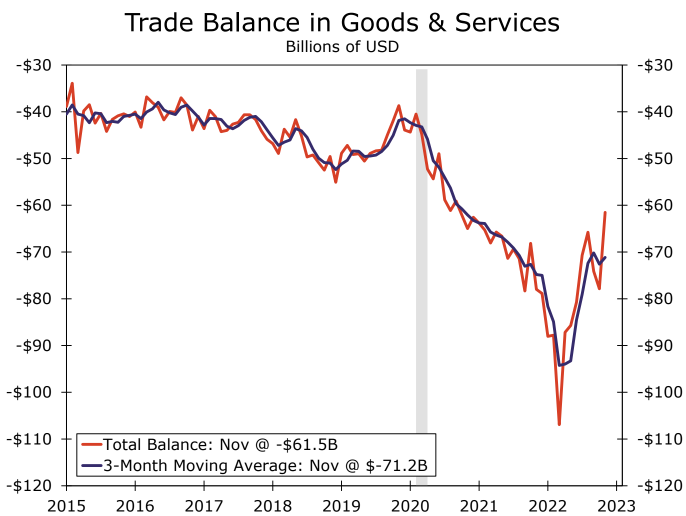
Summary

The U.S. international trade deficit narrowed sharply in November amid a collapse in imports. While this presents some upside risk to Q4 GDP growth, the details suggest economic weakness is also starting to show up in trade flows.



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

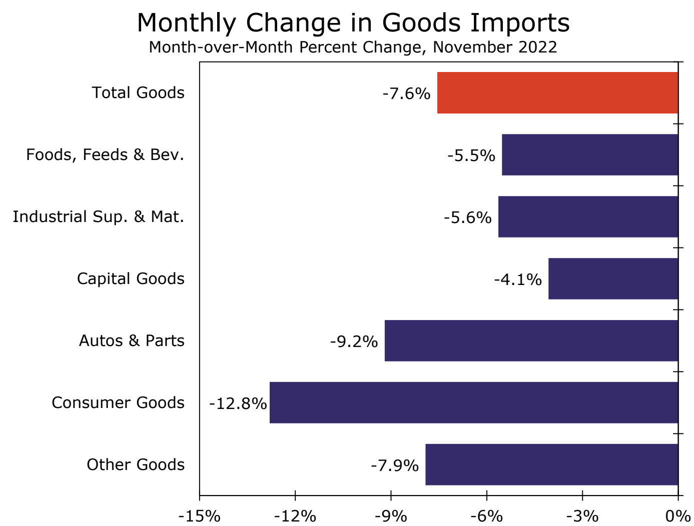
Trade Flows Essentially Collapsed in November

International trade flows continued their volatile path in November and caused the U.S. trade deficit to narrow to over a two-year low of $61.5 billion (chart). Specifically, U.S. imports from the rest of the world plunged by $21.5 billion during the month, which essentially puts the level of imports back to where they stood a year earlier (chart). While some volatile factors explain the sharp decline, broad weakness suggests the transition away from goods of domestic consumers may be starting to show up in import activity.

While all major categories declined (chart), the $8.8 million pullback in consumer goods led the drop. Weakness was broad based—consider that just five categories of end-use consumer goods imports rose during the month and that they are rather small representing less than 2% of year-to-date imports in consumer goods. That said, an unusually large $2.9 million decline in *pharmaceutical preparations* and another $2.7 million drop in *cell phones & other household goods* together were responsible for about 60% of the overall decline in consumer products. We thus conclude the transition away from goods and to services domestically is likely leading to some gradual weakness in consumer goods, but monthly volatility has made these figures appear a bit worse.

Volatility doesn't stop at consumer products either. A $1.7 million decline in *crude oil* imports, which is likely in part price driven, drove overall industrial supplies lower, and outsized declines in *computers* and *telecommunications equipment* were what weighed on capital goods in November.

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



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

Exports also slipped $5.1 billion, and while that pales in comparison to the decline in imports, it marks the largest monthly decline since the height of the COVID pandemic in April 2020. Prior to that you can only find a steeper monthly drop during the 2008/2009 global financial crisis. Trade flows essentially collapsed in November.

Factoring in the November data, and outsized import decline specifically, suggests less of a drag from net exports than we previously expected. For example, if the real trade balance in goods remains unchanged in December, net exports would shave only 0.2 percentage points off of fourth quarter growth, much less than the 1.5 percentage points we have in our current forecast, which suggests there is some upside risk to fourth quarter GDP growth from this morning's data.

Even so, our broader expectations of where trade is headed this year have not materially changed. We still anticipate weakness in exports to be more pronounced in the near-term amid economic deceleration abroad and a stronger U.S. dollar. Import growth, on the other hand, may hold up a bit better as supply and demand get back in line, but a gradual pullback in categories that saw a run up during the pandemic—like consumer goods—seems likely, and we expect weakness to more meaningfully take hold here as well around the second quarter as domestic demand begins to falter.

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