

»» Momentum of external trade is steady

6 June 2016

Author: Dr Katrin Ullrich, +49 69 7431-9791, katrin.ullrich@kfw.dePress contact: Christine Volk, +49 69 7431-3867, christine.volk@kfw.de

- Momentum of external trade remains solid although stubbornly below long-term level
- Imports outperform exports again this year
- Export weakness should be overcome in the course of the year

External trade indicator



Forecast for 2nd quarter 2016 to 1st quarter 2017.

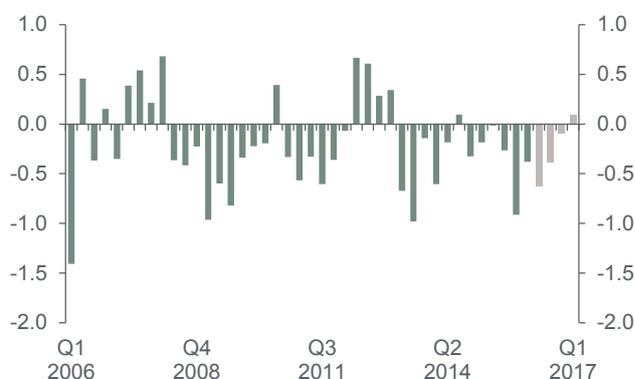
Source: KfW

The indicator of German external trade activity computed by KfW, the KfW External Trade Barometer, was at 99.7 points in the first quarter of 2016 – below its long-term average. The overall indicator does not show any major variations in foreign trade activity for the next four quarters either, as the momentum will continue roughly on this level. This also reflects the economic situation in Germany, which is virtually unchanged from last year.

The first quarter of 2016 was characterised by turmoil in the financial markets and concern over the global economy. The weakness of global trade was debated as a possible sign of a global recession. On the basis of previous patterns, however, foreign trade is not an early indicator of an economic downturn. Rather, an economic slump and a decline in foreign trade are usually parallel movements. And although significant risks to the global economy do exist, the growth rates of industrialised as well as developing and emerging market economies are likely to be similar to the previous year's level. Next year the developing and emerging market economies at least are expected to show stronger growth again.

Germany's exports also slowed down in the winter half year. Later in 2016, however, external demand is expected to

Balance of export and import momentum



increase and revive exports. Towards the end of the forecast period, the first quarter of 2017, the momentum of exports may have overcome its weakness and returned to its long-term level.

Imports outperform exports this year as well due to the robust German economy. But a repeat of the strong first quarter is unlikely, and even this strength has been insufficient to generate above-average momentum in import activity. Accordingly, the remainder of the year will probably be unspectacular as well, with average import momentum continuing on the long-term level.

In the first quarter of 2017, export activity is expected to exceed import activity for the first time since 2013, with the exception of the overhang in export momentum in the third quarter of 2014. But it is doubtful whether this can be maintained in the further course of 2017. For one thing, Germany is expected to experience a continuing economic upturn in the wake of which imports will also increase. For another, next year's economic impetus and, with it, increased demand, is expected to come primarily from the developing and emerging market economies, whereas Germany exports most of its goods to industrialised countries and so stands to benefit less from the global economic recovery. ■

Methodological appendix: Construction of indicators

The external trade indicator is the simple average of the export sub-indicator and the import sub-indicator. The value 100 marks the long-term average. Values above / below 100 represent above-average / below-average growth of imports and exports compared with the previous year.

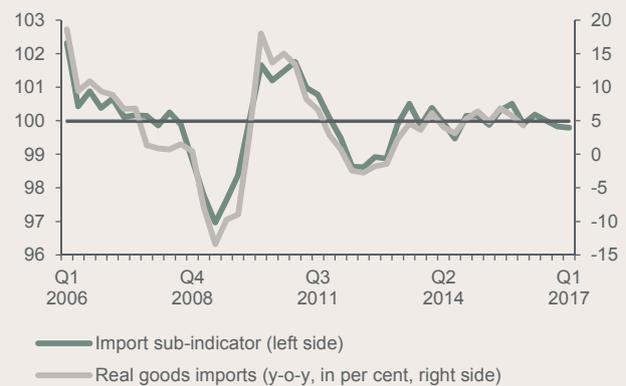
The indicator as the balance of export and import momentum is the difference between the export sub-indicator and the import sub-indicator. If the value is positive (negative), exports develop more strongly (less strongly) than imports, whereas both factors grow at the same rate when the value is zero.

The indicators and the underlying estimation models are based on quarterly figures. The forecast period comprises four quarters.

Export sub-indicator



Import sub-indicator



Source: KfW

The sub-indicators for imports and exports are obtained from the respective estimated values of an ordinary least squares estimation. All variables used in the estimation are computed as variations on the previous year's quarter and normalised to a mean value of zero and a standard deviation of one based on the period from Q1 1995 to the current margin. The import and export series of the balance of payments statistic are used as dependent variables and deflated with the export and import price index. The explanatory variables used in the export estimation equation are the non-domestic new orders in manufacturing, the Deutsche Bundesbank's indicator of price competitiveness vis-a-vis 56 trading partners and the export-weighted economic trend in the destination countries of German exports on the basis of IMF data and national statistics – where available.

The explanatory variables for imports are domestic use, the domestic new orders in manufacturing, the Baltic Exchange Dry Index as an indicator of international transport costs and a dummy variable. The latter assumes a value of 1 between Q2 2002 and Q1 2006 in order to take into account two structural breaks in the import equation.

Table: Description of variables applied

Description	Forecast	Source of the underlying data
Goods imports and exports based on the balance of payments statistics		Thomson Reuters Datastream: Deutsche Bundesbank
Economic situation of Germany's trading partners weighted with the value of exports	Forecasts based on the IMF's World Economic Outlook and internal economic forecasts; forecast export weights on average for the past four quarters	Thomson Reuters Datastream: IMF, national source.
Domestic use according to national accounts	Autoregressive model	Thomson Reuters Datastream: Federal Statistical Office
Non-domestic new orders in manufacturing	Autoregressive model	Thomson Reuters Datastream: Federal Statistical Office
Domestic new orders in manufacturing	Autoregressive model	Thomson Reuters Datastream: Federal Statistical Office
Indicator of Germany's price competitiveness against 56 trading partners	Autoregressive model	Thomson Reuters Datastream: Deutsche Bundesbank
Baltic Exchange Dry Index	Autoregressive model	Thomson Reuters Datastream: Baltic Exchange