

ECONOMICS: US PERSPECTIVES—APRIL 9, 2010

Rapid Rise in US Export Orders Supports “New Mix” Prognosis for Economic Recovery

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Exports are poised to play a much bigger role than ever before in fueling the US economic recovery. With a wide range of US manufacturing industries generating more revenue and profit from overseas markets, we expect exports to imprint lasting changes on the US economic and business landscape.

US exports continue to grow at a brisk pace and are poised to play an increasingly important role in the nascent economic recovery. In March, the Institute of Supply Management’s (ISM) export orders index surged over five percentage points to 61.2—the highest reading since 1988. It marked the ninth consecutive month in which the index, taken from the ISM monthly survey of manufacturing firms, exceeded the 50% threshold signaling export growth.

The indicator is an important barometer for exports even though it is not part of the overall composite manufacturing index, which relies upon data such as total new orders, production, employment and inventories. Since its inception in the late 1980s, the ISM export orders index has provided valuable insight into the flow of business stemming from overseas customers, and is a reliable and leading indicator for overall export growth.

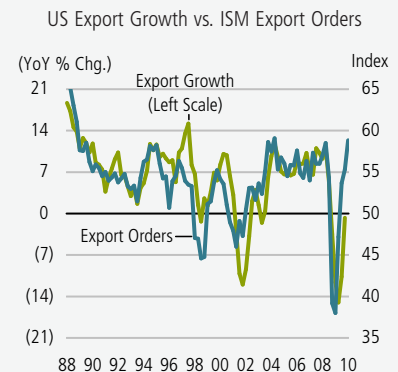
Historically the export orders series has tended to trough and peak before actual

exports. Moreover, the level of export orders is highly correlated with actual growth in overall exports. As a diffusion index, the level and change in the export orders index provides important information: a reading above 50 means orders are rising, while five-point gains—as seen in March—indicate orders are increasing at an accelerating rate. Based on the current reading for the first quarter, the exports order index is predicting double-digit US export growth in 2010 (**Display 1**), which is in line with our forecast of 11% growth in real exports for the year.

Many Industries Report Export Gains

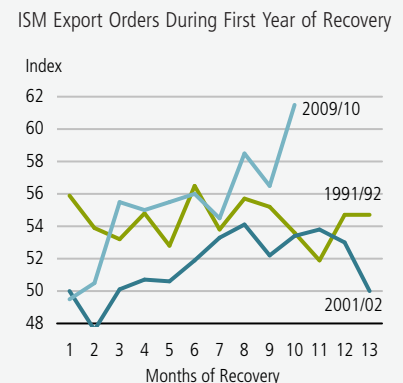
Overseas orders are rising across a wide range of industries, according to the recent survey. These include transportation (commercial aircraft and autos); chemicals; electrical equipment; appliances and components; and computers and electronic products. Strong export orders were also reported in consumer-related industries such as apparel, food, beverages and tobacco products.

Display 1
Order Trends Predict Strong Export Growth



Source: Bureau of Economic Analysis, Haver Analytics and Institute for Supply Management

Display 2
Bigger Role for Exports in 2010 Recovery



Source: Haver Analytics and Institute for Supply Management

Exports have contributed to US economic recoveries in the past, but the role of overseas sales was relatively muted for two reasons. First, domestic demand growth in the US was traditionally the most powerful driver of overall global recovery. Second, export business was typically not a significant part of overall US manufacturing sales.

Why Are Exports Gaining Traction?

However, a dramatic change is unfolding today in the leadership of the global economic cycle, as demand growth in emerging markets powers the recovery. Simultaneously, US manufacturing has become leaner and more competitive, with exports accounting for more than a quarter of overall sales. The result is a “new mix” of GDP growth for the US, in which exports play a much more significant role than domestic factors such as consumer spending or housing.

In our view, these changes will make a profound difference in the shape of US economic growth. In each of the two previous economic recoveries, overall exports contributed 0.6 percentage points

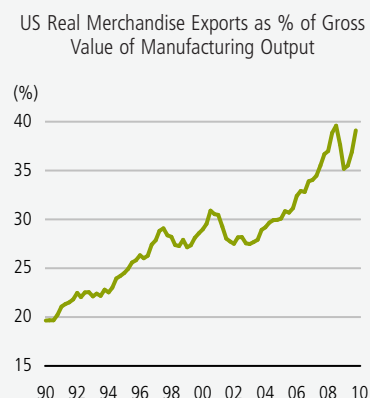
on average to real GDP growth in the initial year of the rebound. The US economy has just entered its fourth quarter of growth following recession, but the contribution from exports is already more than three times greater than during the upturns of 1991/92 and 2002 (Display 2, previous page). Based on our analysis of the orders data, we believe the contribution from export growth in the initial year of recovery will be greater than at any other time in the postwar period.

Big Shift in US Business Trends

As the “new mix” develops, some US companies may generate more than half of their sales—and most of their growth—from overseas markets (Display 3). Investors should therefore be wary of focusing too closely on strict geographic factors such as relative growth rates of developed and emerging economies, since many US companies will be beneficiaries of fast-growing markets.

For these companies, sales and profit improvements will mirror previous US economic recoveries, but the key differ-

Display 3
US Industry Relies Heavily on Exports



Source: Bureau of Economic Analysis and Haver Analytics

ence this time is that incremental growth will be driven by overseas business and not the domestic market. In our view, the growing importance of exports will have significant implications for the macroeconomic landscape as well as for companies and investors, and could prove to be the biggest shift in US business trends for many years to come. ■

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