

# What's Behind the Surge in America's Imports?

■ **Joseph G. Carson**  
 US Economist and Director—Global Economic Research

US imports posted a record surge during the second quarter, creating a new headwind to the economic recovery. With the US economy growing at a slower pace than the global average, a reversal of the import drag during the second half of 2010 would provide important support for GDP growth.

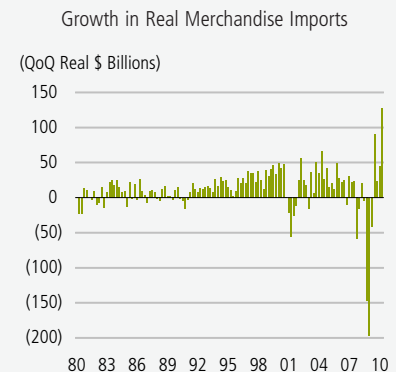
The US economy faced an unexpected headwind in the second quarter, as a surge in imports raised concerns of a new challenge to the recovery. During the second quarter, US imports rose by an annualized \$126.8 billion (**Display 1**), subtracting four percentage points from real GDP. In real dollar terms, it was the biggest quarterly leap in imports of the postwar period, and the subsequent damage to economic growth was unprecedented (**Display 2**).

This puzzling development appears to contradict our *new mix* thesis for the US economy, which expects economic growth to be fueled by continued strength in exports. It also raises some big questions about the future trajectory of the recovery: First, why did US imports post a record surge amid modest domestic consumer demand, which is usually the main catalyst for rising imports? Second, was the spurt in imports a one-off aberration or should we expect a continuation of import growth that could undermine momentum for GDP expansion?

Our research shows that strong US exports are being driven primarily by a competitive manufacturing sector and robust growth in emerging markets, which in turn should deliver positive spillover effects on domestic capital spending. So far, this new mix of growth drivers has played out according to our expectations in the early stages of the US economic recovery that began in mid-2009. Contributions from exports and capital spending accounted for more than the overall gain in real GDP over the past year—the first time this has ever happened in the postwar period.

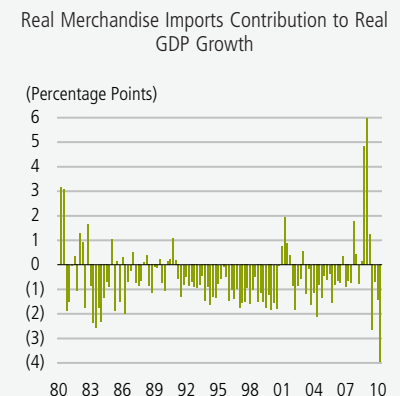
**Import Growth Pace Exceeds Exports**  
 Yet, the trend in imports does not fit. In an export-driven economy, against a backdrop of moderate domestic demand growth, the pace of import growth should be much slower than export growth. But in the second quarter, the initial GDP report showed imports advancing at an extremely rapid pace of 35.4% annualized—more than five times faster than exports. To make matters worse, the growth rate in imports will probably be revised even

Display 1  
Imports Post Record Increase...



As of June 2010  
Source: Bureau of Economic Analysis and Haver Analytics

Display 2  
...Inflicting Huge Damage to GDP



As of June 2010  
Source: Bureau of Economic Analysis and Haver Analytics

higher following the release of June trade data last week.

The surge in imports from April to June was the largest quarterly gain since the second and third quarters of 1983, when imports increased by 36% and 39% respectively. Yet despite the similar pace of import growth, the surrounding environment is markedly different. In particular, during the middle quarters of 1983, consumer spending growth exceeded 10% on an annualized basis, while in the second quarter of this year, consumer spending on goods advanced by just 3%.

### Domestic Demand Remains Weak

Import growth trends typically echo movements in domestic demand. Strong growth in domestic sales—especially consumer sales—tends to trigger a solid rise in imports. In contrast, weak or modest domestic demand growth is usually accompanied by small gains in imports, and occasionally even a decline.

According to the GDP data, about 37% of the record gain in real imports during the second quarter was concentrated in consumer durable and nondurable goods (**Display 3**). Half of the increase came from the motor vehicle sector as US firms began to rebuild inventory positions by importing products from their manufacturing plants in Canada and Mexico. Much of the remaining consumer good imports were nondurables, with pharmaceuticals accounting for about a third of the gains.

Real capital goods imports accounted for about 37% of the second-quarter gain, with technology products contributing about a third of the increase. Trade flows of technology products are a double-edged sword for the US economy.

Although many ideas and designs behind some of the most popular technology products originate in the US, almost all US technology companies produce these items abroad. In these cases, the transfer

of the idea, design or blueprint is not counted as a US export, while the final assembled product that returns to the US for sale is counted as an import.

Of course, the US economy and real GDP growth reap great benefits from innovation and new products, as the value added to the economy is roughly five to six times larger than the price of the imported product. However, as long as US companies rely upon foreign affiliates or alliances to produce most of their technology products, any technology-driven capital spending cycle will be accompanied by a strong gain in imports. The benefit to the US comes from strong job creation in computer design and technical services as well as through large profits to those firms that invent innovative products.

Most of the rest (22%) of the import surge was concentrated in petroleum and related products. The \$28.4 billion increase in real petroleum products followed declines in five of the last six quarters, so the rise in the second quarter reflected a normal restocking phase that is common in the early stages of economic recovery. Total product inventories are now back to near record highs, meaning a modest reversal in petroleum imports is likely over the near term, which may help reverse the import boom from the second quarter that hurt economic growth.

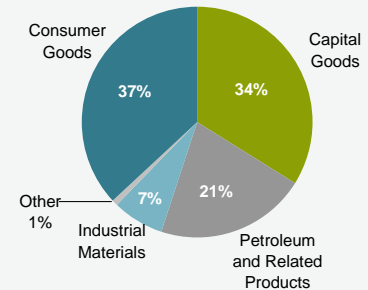
### Challenge to New Mix?

Clearly, the import data for the second quarter pose a significant challenge to our forecast and to our *new mix* macroeconomic theme for the US economy. That's because further import growth would suggest that non-US production may be squeezing out domestic production, further weakening the domestic labor market in the process.

However, we're not convinced that the recent import gains will persist. Without the fundamental support of strong consumer demand growth, imports lack a

### Display 3 Increase in Imports Was Broad Based

Composition of Real Merchandise Import Growth in 2Q:2010



As of June 2010

Source: Bureau of Economic Analysis and Haver Analytics

crucial magnet and the recent pace of growth is unlikely to be sustained. Indeed, during the second quarter, the dollar increase in real consumer goods imports was double the dollar increase in consumer spending on goods, indicating that many recent imports are still sitting on retailer shelves or in dealer inventories.

Moreover, we expect consumer spending to increase by a modest 2% to 2.25% in the second half, which implies the growth in imports of consumer goods is likely to slow dramatically from the pace in the second quarter. Away from the consumer sector, the volume of petroleum imports has already started to trend lower following the surge in the second quarter to a near record level of oil inventories.

On the other hand, as manufacturing production continued to enjoy a strong and broad-based rebound in July, export demand still looks firm. This trend is supported by ongoing strength in export orders in the ISM manufacturing survey. On balance, the strong export trend appears much more durable than the recent swell in imports, and we view the poor trade data in the second quarter as a hiccup rather than a reversal in the US economy's growth trend. ■

---

The information contained here reflects the views of AllianceBernstein L.P. or its affiliates and sources it believes are reliable as of the date of this publication. AllianceBernstein L.P. makes no representations or warranties concerning the accuracy of any data. There is no guarantee that any projection, forecast or opinion in this material will be realized. Past performance does not guarantee future results. The views expressed here may change at any time after the date of this publication. This document is for informational purposes only and does not constitute investment advice. AllianceBernstein L.P. does not provide tax, legal or accounting advice. It does not take an investor's personal investment objectives or financial situation into account; investors should discuss their individual circumstances with appropriate professionals before making any decisions. This information should not be construed as sales or marketing material or an offer of solicitation for the purchase or sale of, any financial instrument, product or service sponsored by AllianceBernstein or its affiliates.

**Note to Canadian Readers:** AllianceBernstein provides its investment management services in Canada through its affiliates Sanford C. Bernstein & Co., LLC and AllianceBernstein Canada, Inc.

**Note to UK Readers:** UK readers should note that this document has been issued by AllianceBernstein Limited, which is authorised and regulated in the UK by the Financial Services Authority. The registered office of the firm is: Devonshire House, One Mayfair Place, London W1J 8AJ.

**Note to Australian and New Zealand Readers:** This document has been issued by AllianceBernstein Australia Limited (ABN 53 095 022 718 and AFSL 230698). Information in this document is intended for wholesale investors only, and is not to be construed as advice.

**Note to Readers in Vietnam, the Philippines, Brunei, Thailand, Indonesia and India:** This document is provided solely for the informational purposes of institutional investors and is not investment advice, nor is it intended to be an offer or solicitation, and does not pertain to the specific investment objectives, financial situation or particular needs of any person to whom it is sent. This document is not an advertisement and is not intended for public use or additional distribution. AllianceBernstein is not licensed to, and does not purport to, conduct any business or offer any services in any of the above countries.

**Note to Readers in Malaysia:** Nothing in this document should be construed as an invitation or offer to subscribe to or purchase any securities, nor is it an offering of fund management services, advice, analysis or a report concerning securities. AllianceBernstein is not licensed to, and does not purport to, conduct any business or offer any services in Malaysia. Without prejudice to the generality of the foregoing, AllianceBernstein does not hold a capital markets services license under the Capital Markets & Services Act 2007 of Malaysia, and does not, nor does it purport to, deal in securities, trade in futures contracts, manage funds, offer corporate finance or investment advice, or provide financial planning services in Malaysia.

**Note to Singapore Readers:** This document has been issued by AllianceBernstein (Singapore) Ltd. (Company Registration No. 199703364C). The Company is a holder of a Capital Markets Services Licence issued by the Monetary Authority of Singapore to conduct regulated activity in fund management.

**Note to Taiwan Readers:** This information is provided by AllianceBernstein funds Taiwan Master Agent, AllianceBernstein Taiwan Limited. SFB operating license No.: (97) FSC SICE no. 049. Address: 57F-1, 7 Xin Yi Road, Sec. 5, Taipei 110, Taiwan R.O.C. Telephone: 02-8758-3888. AllianceBernstein Taiwan Limited is a separate entity an independently operated business.

**Note to Hong Kong Readers:** The document has not been reviewed by the Hong Kong Securities and Futures Commission. The issuer of this document is AllianceBernstein Hong Kong Limited.