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GRISWOLD: Are rising imports a boon or bane to the economy?

By Daniel Griswold

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ANALYSIS/OPINION:

It has become conventional wisdom in reporting on the economy that rising imports and a growing trade deficit ar bad signs for growth. As recent headlines warn us, "Economic growth slowed by trade gap" (Washington Post) an "Wider Trade Gap Signals Weak Growth" (Wall Street Journal).

Such reporting flows unavoidably from Keynesian logic. If we import a million shoes to satisfy domestic demand, that's a million shoes we no longer need to make ourselves. When demand "leaks" abroad, the economy grows mo slowly and it creates fewer jobs.

Or so we are told.

Those journalists and the experts they quote who tout this theory should get their heads out of the theoretical clouc and look at what really goes on in the economy. All the evidence points to the fact that rising imports and a growi trade gap, far from being drags on growth, are among the surest signs that the economy is expanding.

A major flaw of the Keynesian view is that it neglects the supply-side role of imports. More than half of what we import consists of goods consumed by producers — capital machinery, raw materials, parts and other intermediate inputs. Those imports help us produce more, not less. This is one reason why, over the past year, imports of manufactured goods have been rising along with domestic manufacturing output.

In the long run, imports spur growth by forcing domestic producers to be more efficient and productive. Like competition generally, imports weed out the less-productive domestic producers, leaving the market to more-competitive U.S. companies. Those companies are better able to expand their share in global markets and create sustainable jobs with higher pay.

Obsession with the trade deficit also ignores the fact that the dollars we spend on imports quickly return to the United States. If they are not used to buy our goods and services, they are spent on assets, such as real estate, stock and Treasury bonds. This inflow of capital also helps to fuel growth by keeping interest rates down and providing capital to build factories and expand output.

If the Keynesian worry about imports were justified, we should expect to see a negative correlation over time between the growth in imports and the growth of GDP. Rising imports would tend to be associated with weaker growth, and more slowly growing or falling imports with stronger growth.

In reality, rising imports are one of the surest indicators of stronger economic growth. After examining quarterly economic data from the U.S. Bureau of Economic Analysis going back to 1980, I found a strong positive correlati between the change in real imports to the United States and the change in real gross domestic product (GDP). Compared with a perfectly proportional correlation of 100 percent, the correlation between imports and GDP is a strongly positive 62 percent.

Politicians myopically focus on exports, but the correlation between rising exports and rising GDP is actually weaker, at 45 percent, than the connection between imports and GDP. If President Obama wants to promote more robust economic growth through trade, he should consider complementing his National Export Initiative with a companion National Import Initiative. The only other major categories of economic activity that correlated more strongly to GDP growth than imports were personal consumption expenditures, at 66 percent, and gross private domestic investment, at 80 percent.

You don't need to analyze a spreadsheet to see the positive connection between imports and economic growth. Think back to the 1990s, the "Goldilocks economy" from 1992 to 2000, when growth was strong, jobs plentiful an inflation low. That was also a time of surging imports and rising trade deficits. Again, in the middle of the George W. Bush presidency, imports resumed their robust growth and the trade gap grew for five straight years. During th same period, 2002-2007, the economy expanded and the unemployment rate fell from 5.7 to 4.4 percent.

In contrast, imports slow and the trade deficit invariably shrinks during periods of recession. From 2007 to 2009, during the "great recession," the trade deficit fell by half as domestic demand and imports plunged, while unemployment soared. Indeed, 2009 was one of only half a dozen years in the past half century in which the value of imports actually decreased from the previous year. The others were 1961, 1975, 1982, 1991, and 2001. According to our Keynesian friends, those should have been robust years for economic growth and job creation. In fact, each of those years was marked by recession.

The Keynesian believers among us may be wishing for a decline in imports, but for millions of Americans struggling in the real economy such a decline would be a curse.

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