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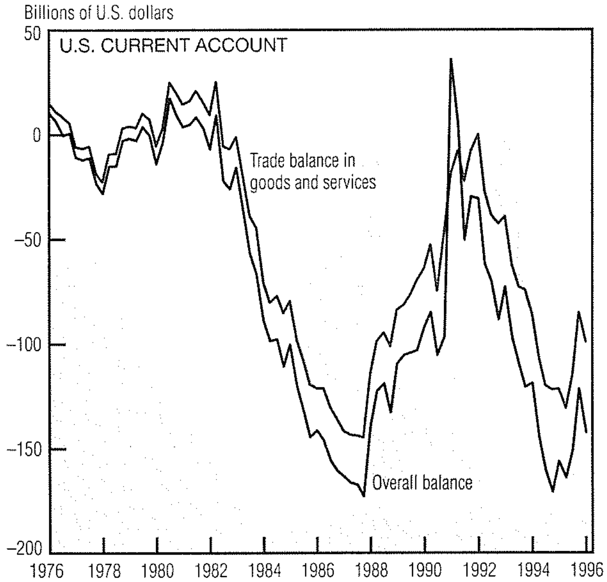
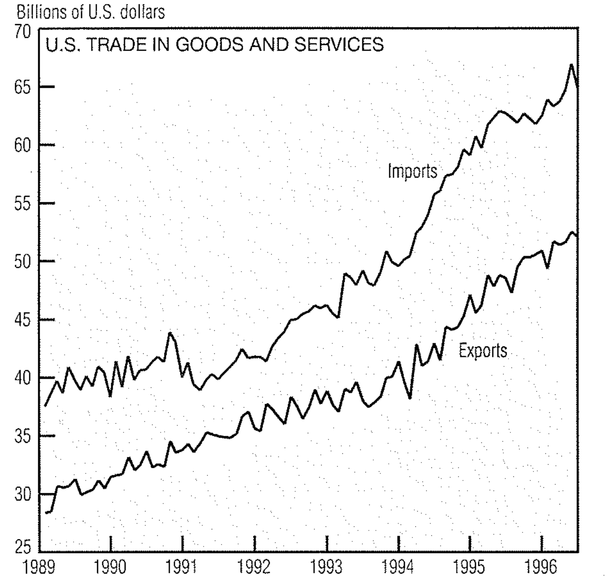
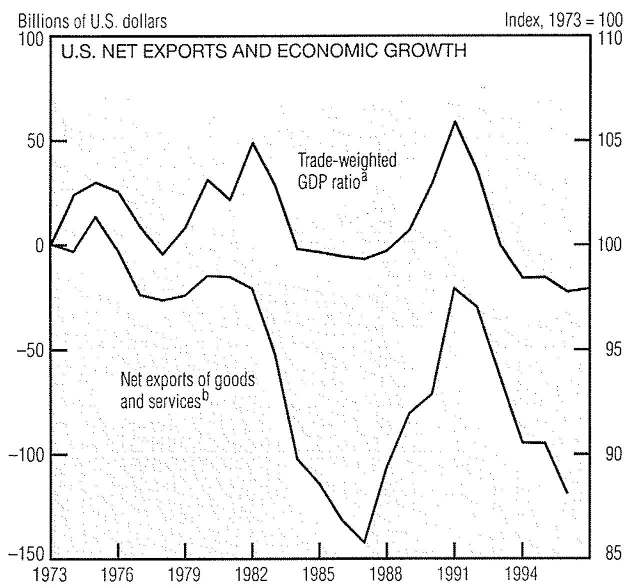
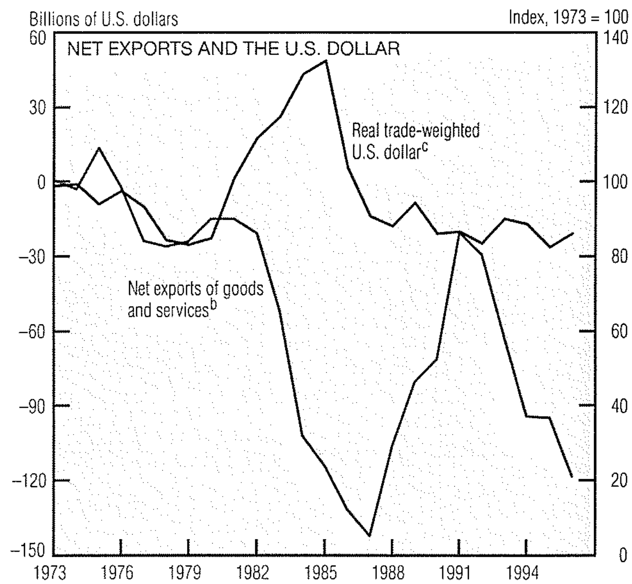
International Trade









a. Ratio of foreign real GDP or GNP to U.S. real GDP. Foreign countries and trade weights are those used to construct the Board of Governors' trade-weighted dollar index. 1996 and 1997 projections are from *The Economist,* August 10–16, 1996.
b. 1996 plot is an average of the first two quarters of the year.
c. 1996 plot is an average of the first seven months of the year.
SOURCES: U.S. Department of Commerce, Bureau of Economic Analysis; Board of Governors of the Federal Reserve System; International Monetary Fund, *Financial Statistics;* and *The Economist,* August 10–16, 1996.

The U.S. current account deficit grew by $20.6 billion (annual rate) in the first quarter, reaching $142.4 billion. A wider trade deficit and larger unilateral transfers offset a slight decline in net U.S. interest payments to foreigners. Monthly data on trade in goods and services suggest that the trade deficit, the largest component of the current account balance, will widen further in the second quarter.

The deterioration in U.S. net exports since the 1991–92 recession can be traced to substantially higher economic growth here than abroad. Foreign economies have been picking up, however, and with trade-weighted growth projected at 1.7% this year and 2.5% in 1997, the prospects for a further sharp decline in U.S. net exports seem remote.

The connection between relative growth and the trade deficit is indirect and therefore somewhat tenuous. The relationship ultimately depends on how growth influences decisions to save and invest. A deficit country, by definition, consumes and invests more than it produces and hence must borrow savings from abroad. The connection between movements in the real dollar exchange rate and net exports also runs through savings and investment decisions and seems even weaker than that between relative growth rates and net exports.