

## **B. International Review and Outlook**

### **Introduction**

The global economy has been producing a series of bad economic news in recent weeks. The idea of decoupling, that is, the rest of the world economy will be O.K. even with faltering U.S. economy, once again succumbed to the reality that when the U.S. economy sneezes the rest of the world catches cold. There are growing signs that more advanced economies are teetering on the border of recession and even the emerging markets, which have sustained long periods of strong growth, are bracing for much tempered economic activities.

The global economy is generally expected to slow substantially this year and next. At the same time inflation is back with food and energy prices soaring. Once content with stable inflation environment the central banks will now have to try a balanced approach in two areas that require some trade-off: price stability and economic growth.

While there is wide variety of views on the prospects of the global economy, less optimistic forecasts cite a tough economic environment in which the global economy is stuck: continuous unraveling of financial sector, credit and liquidity crunch, the collapse of housing sector in many countries, struggling stock markets, high inflation, financially stretched consumers, and geopolitical tensions.

One bright spot in the global economy is trade. For many countries export sector has been a big engine of growth. U.S. exports, for example, increased 18.0 percent in the first six months from a year ago, totaling \$660.8 billion in current dollars. During the same period Oregon saw even more growth: Oregon's exports increased 23.7 percent to reach \$9.9 billion. Oregon's share in total U.S. exports remained at 1.5 percent. Weak U.S. dollar has provided tremendous support for U.S. exports. At the same time the U.S. exporters took advantage of robust demand from the global economy that stayed strong until very recently.

### **Recent Developments and Outlook for Oregon Export Markets**

A sudden deluge of bad economic news across the world caught most economists by surprise. We've seen trouble signs in the U.S. economy but the notion that the rest of the world can stay relatively insulated from the headwinds in the U.S. economy had dominated the minds of great many observers.

First, Japan reported that its economy shrank by 0.6 percent in the second quarter. It was Japan's worst quarterly economic performance in seven years. This news was followed by Eurozone's negative economic growth, the first contraction since the inception of the single currency in 1999. Three large economies in the Eurozone, Germany, France and Italy had seen a decline in economic activity.

It wasn't until recently when the economies in Europe and Japan started suddenly looking shaky. Financial instability is taking a toll and strong currencies are hurting Europe's export sector. Consumer and business sentiment have been deteriorating, reflecting the worsening economic

environment. High inflation has kept the European Central Bank from injecting stimulus into the economy.

U.K.'s economic growth was 0.0 percent in the second quarter, ending more than 15 years of continuous expansion. This is yet another indication that the U.K. economy may slip into a recession. British economy has been suffering from one of the worst collapses in housing market in 30 years, depressed consumer sentiment and high inflation rate.

Canada has not been spared from current economic scourge. Its total employment declined sharply in July, the worst decline since February 1991. At the same time, inflation rate has been accelerating. July's 3.4 percent increase year-over-year (Y/Y) marked the fastest pace since March 2003.

Perhaps the broadest indication of widespread economic slowdown in developed economies is in the latest report by the Organization for Economic Cooperation and Development (OECD) on 2<sup>nd</sup> quarter economic growth. OECD reported that its 30 member economy grew 0.2 percent from the 1<sup>st</sup> quarter of 2008, the lowest since the 3<sup>rd</sup> quarter of 2001 when its economy shrank 0.1 percent. This is a clear indication that ill effects from credit crunch and high commodity prices are taking a toll on economic activity.

A latest concern has developed that new economic slowdown in most developed countries may aggravate the conditions in global financial markets which are already under tremendous strain. Worsening financial market could lead to even tighter lending standards, thereby further constricting economic activity.

Another development that Oregon has to follow closely is the extent to which these slowing economies are going to hurt its important export markets, including China and the rest of Asian countries. More pessimistic views argue that China and other Asian countries will feel acute pain from reduced exports to U.S. and European markets. At the same time falling commodity prices will hit hard those developing countries that depend on exports of raw materials. It is highly likely that weaknesses in developed economies will spill over to the developing world, thus effectively ending the talk of decoupling.

It shouldn't come as a surprise then if economists put out a rather gloomy forecast for the next year and a half. In fact, consensus view predicts that slowing momentum in 2008 will be carried well into 2009.

Table I.1 shows global economic forecast by the Global Insight (GI) as of August 19, 2008. In its global forecast, GI cites some issue to watch to gauge future trend of the global economy, First, GI contends that further significant house-price corrections could undermine residential investment and consumer spending through a negative wealth effect. Second, GI thinks that continued strong demand for oil in the emerging world and restrained OPEC production mean

**Table I.1**

Projected Growth Rates of Real GDP (Percent)				
As of 8/19/2008	(Average)			
	2007	2008	2009	2010-13
United States	2.0	1.6	1.0	2.8
Canada	2.7	1.2	2.1	2.5
Japan	2.0	1.0	0.8	2.0
Eurozone	2.7	1.4	1.0	1.9
Mexico	3.2	2.5	2.9	3.8
South America	5.9	5.0	4.7	4.4
Asia except Japan	8.3	7.0	6.7	6.5
China	11.9	10.0	9.0	7.8
World	3.9	3.0	2.8	3.7

Source: Global Insight, August 2008

supply/demand conditions will remain tight and could bring a reversal of recent price declines. Third, GI has the view that recent commodity price declines are good news for purchasers if they are just taking froth out of overextended markets, but more troubling if they are an early warning of a global hard landing.

GI's August 2008 global forecast reflects decidedly subdued growth expectation. The Eurozone's real GDP growth is projected to slow from 2.7 percent last year to 1.4 percent in 2008. Real GDP has cooled faster than expected, contracting by 0.2 percent quarter-to-quarter (q/q) in the second quarter of 2008. The European Central Bank's reluctance to cut its key interest rate should ease as growth remains muted into 2009.

GI writes that China's real GDP growth reached a cyclical high of 11.9 percent in 2007, but is projected to slow to 10.0% this year and 9.0 percent in 2009. Exports will decelerate as global growth downshifts and the renminbi (Chinese currency) appreciates. GI believes that inflation is likely to ease in the coming months as food-supply constraints are alleviated. However, if nonfood prices continue to accelerate, monetary policy will tighten, cooling the investment boom.

GI projects Japan's economic growth to slow from 2.0 percent last year to 1.0 percent in 2008. In the past, deflation had discouraged consumer spending. Now, with high commodity prices importing inflation, producers may soon feel the effects on their profits, putting long-anticipated wage gains on hold again.

Table I.2 summarizes the Blue Chip Consensus forecast (August 2008) for Oregon's major export markets. It is consistent with the GI forecast shown in Table I.1.

**Table I.2**

**Projected Growth for Top U.S. Export Markets**

Ranked by \$ Value of U.S. Goods Exported	Oregon Exports 2007	Projected Change in Real GDP			
		Rank (\$ mil.)	2006	2007	2008
Canada	1 2,785	2.8	2.7	1.3	2.1
Mexico	6 954	4.8	3.3	2.6	3.2
Japan	2 1,477	2.4	2.1	1.3	1.3
United Kingdom	14 290	2.8	3.0	1.5	1.2
China	3 1,432	11.1	11.4	9.8	9.3
Germany	12 416	3.1	2.8	1.8	1.4
South Korea	4 1,332	5.1	5.0	4.4	4.6
Netherlands	15 288	3.0	3.5	2.5	1.7
Taiwan	7 939	4.7	5.7	4.4	4.8
France	16 284	2.4	2.1	1.5	1.4
Singapore	11 433	7.9	7.7	4.8	5.4
Belgium	24 101	2.9	2.8	1.7	1.7
Hong Kong	13 310	6.9	6.3	4.9	4.9
Australia	9 590	2.6	4.1	2.8	2.7
Brazil	17 189	3.7	5.3	4.7	4.0
Eurozone		2.9	2.6	1.6	1.4
U.S.		2.8	2.0	1.6	1.5

Source: Blue Chip Economic Indicators, August 2008

## Oregon Exports

While the domestic economy has been plagued by turmoil in housing sector, credit crunch, financially strapped consumers, uncertain business environment, and high inflation, the export sector of the U.S. economy has assumed a prominent role in boosting economic growth. With the support of global expansion and a favorable U.S. dollar, U.S. merchandise exports increased 17.2 percent in current value in the first quarter 2008 Y/Y.

During the same period Oregon saw even more growth: Oregon's exports increased 23.7 percent to reach \$9.9 billion. Oregon's share in total U.S. exports remained at 1.5 percent. Behind this increase is tremendous growth in exports of agricultural products and computer and electronics products. Graph I.1 illustrates Oregon's total exports. After a brief slowdown in the middle of 2007, the export growth has reaccelerated.

**Graph I.1**

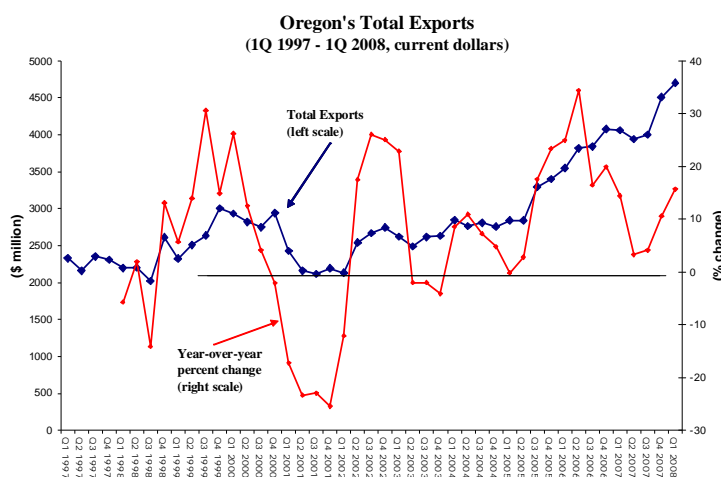


Table I.3 shows Oregon's exports and growth rates by industry through second quarter 2008 Y/Y. These are the top fifteen industries by export volume (in value). Global expansion, a business investment boom in Asia, and a weak U.S. dollar combined to promote exports of agricultural products, computer and electronics, chemicals, and other industry products.

The computer and electronics sector saw a strong rebound Y/Y

in exports to Asia after a short pause in the first part of 2007. The sector registered 24.8 percent increase Y/Y and now accounts for 39.4 percent of total Oregon exports.

Agricultural exports continue tremendous growth, now increasing 82.2 percent Y/Y. Undoubtedly some of this increase reflects highly elevated grain prices. Chemicals also saw a dramatic increase in exports, recording 47.6 percent growth Y/Y.

**Table I.3**

**Oregon Exports by Industry**  
(\$ millions, current prices)

	2Q 2007 YTD	2Q 2008 YTD	y/y % change	Share out of
<b>Total All Industries</b>	<b>8,005.3</b>	<b>9,901.2</b>	<b>23.7%</b>	<b>100.0%</b>
Computer And Electronic Products	3,124.2	3,898.5	24.8%	39.4%
Agricultural Products	911.1	1,660.3	82.2%	16.8%
Machinery, Except Electrical	892.6	897.4	0.5%	9.1%
Transportation Equipment	889.7	796.3	-10.5%	8.0%
Chemicals	334.4	493.5	47.6%	5.0%
Primary Metal Manufacturing	287.1	376.0	31.0%	3.8%
Waste And Scrap	183.6	315.0	71.6%	3.2%
Wood Products	200.1	247.6	23.8%	2.5%
Paper	229.5	197.8	-13.8%	2.0%
Food And Kindred Products	203.9	191.0	-6.3%	1.9%
Miscellaneous Manufactured Commodities	127.3	160.4	26.0%	1.6%
Fabricated Metal Products	149.2	143.6	-3.7%	1.5%
Electrical Equipment, Appliances, And Component	116.7	114.1	-2.2%	1.2%
Plastics And Rubber Products	86.4	84.1	-2.7%	0.8%
Nonmetallic Mineral Products	52.5	80.8	54.0%	0.8%

Source: WISER, August 2008

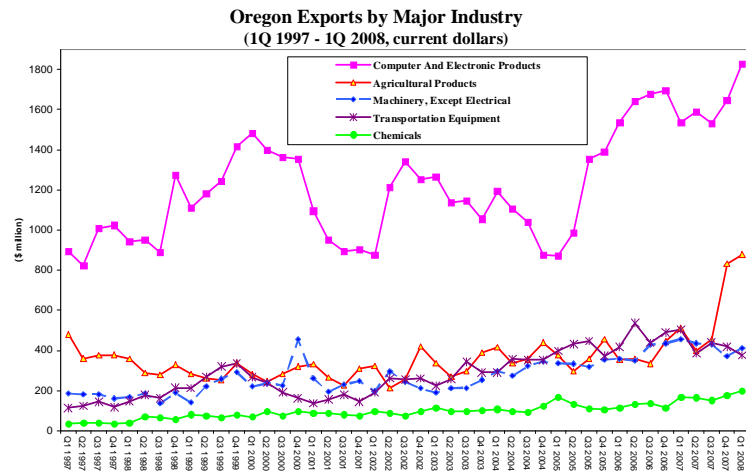
A disappointing development is the flat performance in exports of industrial machinery. And exports of transportation equipment, reflecting cautious business investment environment, declined 10.5 percent from a year ago.

Graph I.2 illustrates quarterly exports by major industry since 1997. The graph demonstrates a continued robust increase in computer and electronics since 2005. It reflects a major increase in exports to Malaysia, China, the Philippines, Costa Rica, and Taiwan. On the other hand, exports to South Korea declined substantially.

Agricultural exports have been a major beneficiary of recent high commodity prices. Exports to Japan, South Korea, and the Philippines more than doubled in value Y/Y. Exports to Taiwan and Canada also increase sharply.

Table I.4 charts exports of Oregon products to major destinations. Canada remains the biggest export destination for Oregon products thanks to that country's continued robust growth. Exports to Canada increased 8.0 percent Y/Y and now account for 15.3 percent of total Oregon exports. Exports to Japan, China, and Malaysia continue to increase sharply. Still favorable economic conditions in non-Japan Asia bode well for Oregon's export prospect, but the region will surely feel the impacts from rapidly worsening economic surroundings.

**Graph I.2**



**Table I.4**

**Oregon Exports to Major Trading Partners**  
(\$ millions, current prices)

	2Q 2007 YTD	2Q 2008 YTD	y/y % change	Share out of Total
Total All Countries	8,005.3	9,901.2	23.7%	100.0%
Canada	1,401.4	1,513.9	8.0%	15.3%
Japan	708.4	1,089.7	53.8%	11.0%
China (Mainland)	765.8	993.7	29.8%	10.0%
Malaysia	518.1	906.2	74.9%	9.2%
Korea, Republic Of	569.3	713.0	25.2%	7.2%
China (Taiwan)	453.2	574.5	26.8%	5.8%
Philippines	325.1	571.0	75.6%	5.8%
Mexico	517.6	399.8	-22.8%	4.0%
Costa Rica	249.1	357.7	43.6%	3.6%
Netherlands	115.0	213.2	85.4%	2.2%
Germany	222.0	202.8	-8.6%	2.0%
United Kingdom	147.6	196.6	33.2%	2.0%
Singapore	228.9	181.7	-20.7%	1.8%
Brazil	93.0	180.1	93.8%	1.8%
Hong Kong	155.5	170.2	9.5%	1.7%

Source: WISER, August 2008

Graph I.3 shows the quarterly export trend for Oregon's major markets since 1997. Exports to Canada continue to stay high. Exports to Japan is evident. However, deceleration in exports to Japan is expected as the economy fights to continue its expansion. Exports to Malaysia, China, South Korea, Taiwan, and the Philippines picked up very sharply.

Exports to regions other than Asia also remained strong. While conditions for further export growth remain favorable, uncertain economies in developed countries will be something to watch for Oregon exporters.

**Graph I.3**

