Fall 9-20-2019

Summary: Service Exports and the US Trade Deficit

Joao F. Gomes
University of Pennsylvania

Summary: Service Exports and the US Trade Deficit

Summary

A trade deficit is defined by the amount by which a country's imports exceeds the value of its exports. The US has consistently held a trade deficit since the 1970s; as of the end of 2016, the deficit had risen to $502 billion. This trade deficit has been a "political hot potato," particularly with respect to China, on the assumption that a sustained deficit weakens the overall economy. But is that accurate? In this B-School for Public Policy Seminar Summary, Professor Gomes takes a closer look at the economics of boosting service exports as a means of rebalancing the US trade deficit and, in the process, sheds new light on policy discussions regarding the future of America's trade agreements.

Keywords

trade, exports, deficit, service, industry

Disciplines

Finance | International Economics | Other Economics | Public Economics | Regional Economics

B★SCHOOL *for* PUBLIC POLICY

Better-informed policymaking through a deeper understanding of economics.

Summary: Service Exports and the U.S. Trade Deficit

Seminar by Professor Joao Gomes

A trade deficit is defined by the amount by which a country's imports exceeds the value of its exports. The US has consistently held a trade deficit since the 1970s; as of the end of 2016, the deficit had risen to $502 billion. This trade deficit has been a "political hot potato," particularly with respect to China, on the assumption that a sustained deficit weakens the overall economy. But is that accurate?

IS A TRADE DEFICIT A BAD THING?

What a deficit fundamentally means is that the US is able consume more goods than it produces. Or, to put it another way, the rest of the world is working really hard—year after year—to satisfy our consumption needs and wants. From the US point of view, that is not such a bad thing.

A TRADE DEFICIT SIGNALS CONFIDENCE

In fact, history depicts trade deficits positively: the Roman Empire, the Spanish and British Colonial Empires, and the Ottoman Empire were able to gain power by running large current account deficits. (One might also point out that these empires eventually fell—but that is because of forces much more complex than their trade deficits!)

The assumption that trade deficits are a sign of weakness and not strength rests on the fact that they translate into debt. When national spending is too high, the US must borrow from abroad. Importantly, however, the US borrows in its own currency: US dollars. For that reason, the deficit does not pose the same risks for the US as it would for developing countries with large debts. Moreover, foreign nations are willing to invest in or lend to the US specifically because they have the confidence in America's ability to repay its debts. They expect the US to realize continued future growth. If America's creditors are not especially worried, why should we be? So long as the US actually continues to achieve economic growth, the trade deficit need not be regarded as dangerous.

SERVICE EXPORTS

Although a trade deficit is not intrinsically a bad thing, there is one option for reducing the US trade deficit that is often overlooked: promoting exports of services. Already, the US is by far the world leader when it comes to trade in services. The US trade surplus in services currently exceeds $262 billion, with the largest surpluses occurring in travel services ($91.7 billion), intellectual property charges ($85.2 billion), and financial services ($77.3 billion).

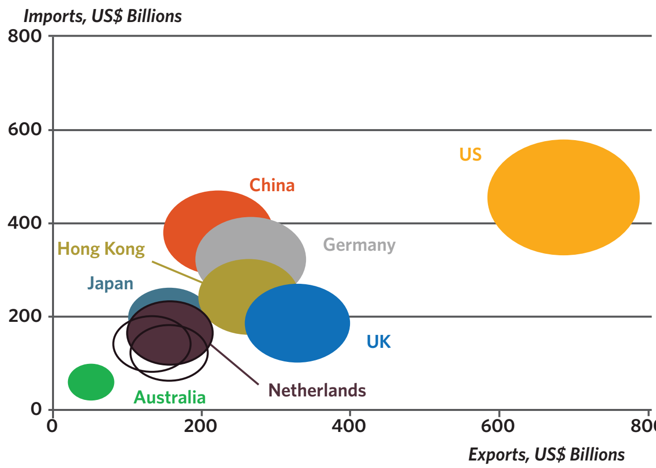

Figure 1: World Leaders in Trade Services
Data Source: World Trade Organization

PENN WHARTON
UNIVERSITY *of* PENNSYLVANIA

PUBLIC POLICY INITIATIVE

More on classes:
http://bit.ly/BSchoolPublicPolicy

Monthly
90-Minute Sessions
on Capitol Hill

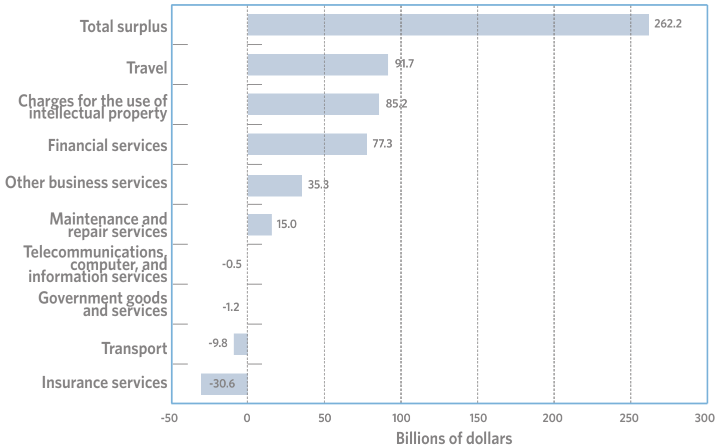

Figure 2: US Services Surplus by Industry
Data Source: Bureau of Economic Analysis

> "The rest of the world is working really hard to satisfy our consumption needs and wants."

SERVICE EXPORT GROWTH AREAS

While the majority of travel services come in the form of foreign residents visiting the US (or US citizens going abroad) for tourism or business purposes, there are two other key forms of travel-related consumption: foreign residents who come to the US for education and for medical treatment. The US is renowned across the globe for its system of higher education and for the quality of its medical care, but these two elements of travel-related consumption have been under-exploited. In 2015, the US exported over $204.5 million in travel services, but only around $35.7 million of that was from education and just $3.6 million was health-related. The US would do well to think more about education and health care as export sectors that have high growth potential.

The US also has the potential to export more technology-based services. These include the sale of software or brokerage services, or the dispensing of legal or consulting services to overseas clients, as well as universities offering distance learning courses to foreign students. Expanding such service exports will depend on investment in the development and enhancement of accessible and secure e-commerce platforms.

REGULATORY CONCERNS

Many of these same business and financial services can also be exported through the movement of US citizens abroad to conduct business. But this raises a major regulatory issue, as professional certifications must be accepted across national jurisdictions. Much more often, though, trade in these services is conducted not by US individuals going abroad, but by US multinational firms setting up branches overseas. Services provided by US multinationals are the largest component of international trade in services, but are not included in the official trade balance statistics of the US.

SERVICE EXPORTS AND JOB GROWTH

Importantly, the industries associated with service exports also promote the creation of well-paying American jobs. Statistics from 2011 indicate that average weekly earnings (in 2008 dollars) in export-intensive service industries were nearly 33% higher than the average in all other service industries. Professional service jobs within "tradable industries" not only offer, on average, higher pay, but demand a higher percentage of workers who have at least a bachelor's degree.

Manufacturing (NAICS 30s)		
	Non-tradable Industry	Tradable Industry
Number of Workers	2,235,432	12,994,490
Average Earnings	$44,014	$49,952
Share with B.A.	16%	24%
Share with Advanced Degree	3%	7%
Share with Tradable Occupations	26%	34%
Professional Services (NAICS 50s)		
	Non-tradable Industry	Tradable Industry
Number of Workers	8,038,246	18,430, 199
Average Earnings	$42,226	$66,454
Share with B.A.	29%	50%
Share with Advanced Degree	7%	17%
Share with Tradable Occupations	31%	60%

Figure 3: Worker Characteristics in Selected Industries
Bradford Jensen (2011) "Global Trade in Services: Fear, Facts, and Offshoring"

> "There is one option for reducing the US trade deficit that is often overlooked: promoting exports of services."

CONCLUSION

In sum, a trade deficit is not a bad thing so long as the US economy is able to grow relatively fast. But if the US wants to reduce or eliminate future trade deficits, focusing on the export of services makes a lot of sense, and amplifies the importance of considering, at a policy level, how these service sectors are regulated. The US has enormous advantages in education, health, finance, and technology, regulators should focus on policy that supports trade in these areas.