Trade balances (TBs) of US and, especially, Euro Area (EA) have improved after Global Financial Crisis.

Widely viewed as largely reflecting weak domestic demand & deleveraging.

This paper challenges conventional view.

Paper finds that commodity prices are key drivers of US and EA TBs.

Sharp post-2012 fall in commodity prices, and Euro depreciation explain bulk of EA TB surge.

Impact of EA domestic shocks on EA TB is much more modest.

Commodity markets also play key role for transmission of Emerging Markets (EM) shocks to the US and EA.

EM productivity growth has weak effect on EA GDP, when effect on commodity prices is taken into account.

Methodological contribution: Bayesian estimation of a three-region (EA, US, rest of world) DSGE model with trade in manufactured goods and in commodities. In model, world commodity price reflects global demand and supply conditions (market clearing).

Broader lessons: Emerging Markets and commodity prices are key drivers of advanced countries’ trade balances and terms of trade.

Historical decompositions (based on estimated model):

(a) Euro Area trade balance/GDP

(b) EA terms of trade (exports/imports price ratio)