SUPPLEMENT CanadExport

Canadian Trade Review

A Quarterly Review of Canada's Trade Performance

Fourth Quarter 2002

This trade and investment quarterly review reports on Canada's economic activity in the fourth quarter of 2002, highlighting our trade and investment performance in key sectors and markets.

Consumer Spending and Residential Construction Strong, but External Trade Weakens

The Canadian economy continued to expand in the fourth quarter of 2002, with real gross domestic product (GDP) increasing by 1.6% on an annualized basis.[1] Although the Canadian rate was slightly ahead of the revised 1.4% rate registered in the U.S. in the same quarter, it fell short of the more robust 3.1% rate registered in the third quarter.

Table 1: Canada's Economic and Trade Indicators

Percent Change at Annual Rates Fourth Quarter 2002 over Third Quarter 2002	
Real GDP *(annualized)*	1.6
Employment *(quarterly increase, level)*	133,100
Rate of Unemployment *(quarterly average)*	7.0
Consumer Price Index *(January 2003, year-over-year percent change)*	
All Items	4.5
Core *(excludes food and energy)*	3.3
Canadian $ in U.S. funds *(average for 2002, level)*	0.6368
Exports of Goods and Services *(annualized, current dollars)*	-0.4
Imports of Goods and Services *(annualized, current dollars)*	0.2

Source: Statistics Canada

Expanded consumer spending, in particular for durable goods and autos, and continued strength in the residential housing market supported growth in the fourth quarter, while continued weakness in machinery and equipment investment limited economic expansion in the business sector. Exports of goods and services experienced a small decline of 0.4% during the quarter, mainly due to a reduction of auto sector shipments to the U.S. This decline in exports reversed the trend of export expansion experienced during the first three quarters of 2002. Canada's continuing economic expansion supported a 0.2% increase in imports for the quarter, as a slight decline in merchandise imports was offset by increased services imports. The current account deteriorated in the fourth quarter—primarily due to continued strong expansion of Canadian direct investment abroad combined with a reduction of inward foreign direct investment.

Job creation continued to be strong in the fourth quarter, with a net quarterly increase of 133,100 jobs—of which some 61% were full-time positions. The average unemployment rate fell to 7.0% in the fourth quarter, down from 7.6% in the third quarter.

The 12-month increase in the overall Consumer Price Index (CPI) was 4.5% in January 2003, up sharply from 1.3% in January 2002. Similarly, the CPI rate for core items (excluding food and energy) reached 3.3% in January 2003, up from 1.7% recorded in January 2002.

The average U.S. dollar value of the Canadian dollar in 2002 was US$0.6368, a 1.4% depreciation from US$0.6458 in 2001.

1 To make quarterly data comparable with annual data, the quarterly figures for trade in goods and services are adjusted for seasonality and expressed at annual rates by raising them four times. This process provides seasonally adjusted annual rates or s.a.a.r. All figures, with the exception of investment figures, are expressed on a s.a.a.r. basis, unless otherwise noted.

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Department of Foreign Affairs and International Trade

Ministère des Affaires étrangères et du Commerce international

Trade and Investment Highlights

A Small Export Contraction Accompanied by Limited Growth in Imports in the Fourth Quarter

Exports of Canadian goods and services fell by 0.4% in the fourth quarter (Figure 1). The $1.9 billion decline in merchandise exports was offset by a strong $1.4 billion expansion in services exports. Imports of goods and services increased by 0.2%—entirely due to growing services imports—as merchandise imports registered a 0.1% decline in the fourth quarter. The $1.9 billion or 1.8% decline in merchandise exports in the fourth quarter was characterized by mixed performance among the sectors (Figure 2). Strong gains in energy (up 91.5% or $9.0 billion) were offset by declines in the auto sector (down 31.8% or $9.4 billion), in agriculture and fishing and in industrial goods. On the imports side, a $1.0 billion (26.3%) increase in energy imports was offset by a $1.0 billion (4.7%) decline in auto imports, while a strong advance in consumer goods was sufficient to offset declines in the remaining sectors.

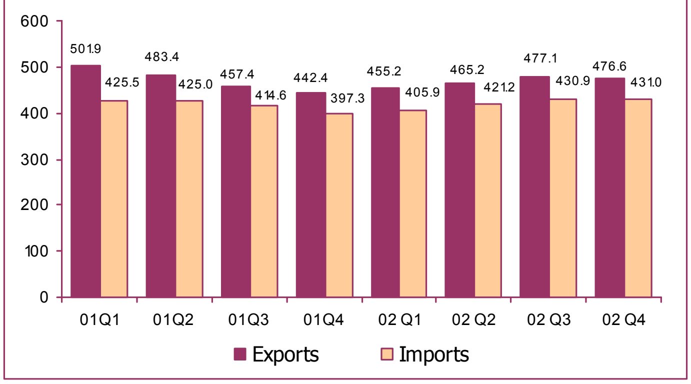
A decrease in merchandise exports to the U.S. (down 3.0% or $2.7 billion) was the major contributor to the decline in overall exports in the fourth quarter. Merchandise exports to non-OECD countries and the EU also declined, although this was almost entirely offset by increased shipments to Japan and other OECD countries. Similarly, merchandise imports from the U.S. experienced a substantial decline, down 5.0% or $3.3 billion. However, increased imports from all other major markets, in particular from non-OECD countries, limited the overall decline in imports.

Because of the decline in exports and the rise in imports of goods, the merchandise trade balance with non-OECD countries deteriorated rapidly in the fourth quarter. The merchandise trade balance with the EU also deteriorated, principally as a result of increased goods imports from and declining goods exports to the U.K. The improvement in the merchandise trade balances with all other major markets was not sufficient to offset the losses noted above. As a result, the merchandise trade balance fell by $1.8 billion in the fourth quarter.

Services Trade Deficit Continues to Decline

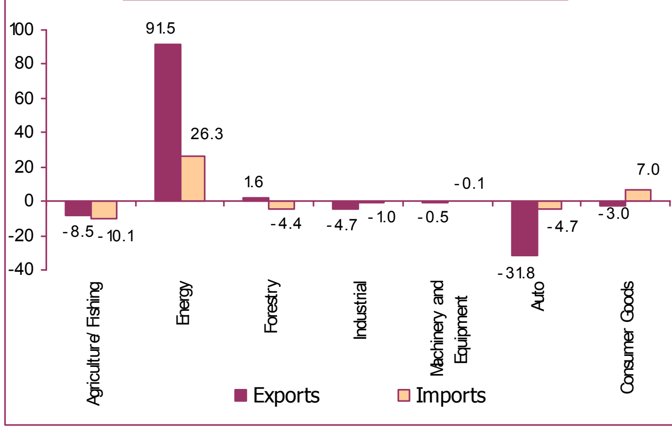
Canadian services exports increased by 10.0% in the fourth quarter. Exports increased for all types of services—led by travel and commercial services. With the exception of transport, services imports also rose, as overall services imports expanded by 1.4% (Figure 3). Because services exports increased more than services imports, the services trade balance narrowed to $7.1 billion in the fourth quarter—down from $8.3 billion in the previous quarter.

Figure 1: Canada's Trade in Goods and Services
(Billions of Dollars, Annualized)



Source: Statistics Canada

Figure 2: Canada's Trade by Commodity
Fourth Quarter 2002 over Third Quarter 2002
(Annualized, Percent Change)



Source: Statistics Canada

Figure 3: Canada's Trade in Services by Type
Fourth Quarter 2002 over Third Quarter 2002
(Annualized, Percent Change)

Source: Statistics Canada

Outward Foreign Direct Investment Flows Exceed Inward Flows

Canadian direct investment abroad (CDIA) was $16 billion in the fourth quarter of 2002—more than double the amount recorded in the last quarter of 2001. The increase in quarterly flows was particularly strong in the finance and insurance sector and in other industries, while CDIA in the services and retailing and energy sectors declined compared with the same quarter the previous year. Outward flows were predominantly directed to the U.S. and the EU (other than the U.K.), while non-OECD countries experienced a decline in CDIA flows in the fourth quarter.

Foreign direct investment (FDI) flows into Canada stood at $5.7 billion in the fourth quarter of 2002—about half the level recorded in the same quarter a year earlier. Most of the decrease in FDI flows occurred in energy, which experienced a drastic 90% reduction in FDI over the same quarter the previous year. The decline in FDI flows stemmed from a decline in FDI from the U.S., which decreased its flow of direct investment to $3.8 billion in the fourth quarter of 2002 from $15.6 billion in the same quarter the previous year. Partially offsetting this decline were increases in FDI from the EU (other than the U.K.) and non-OECD countries. Overall, outward flows exceeded inward flows in the fourth quarter by $10.3 billion, a reversal of the situation in the same quarter the previous year, when FDI exceeded CDIA by $4.1 billion.

Canada Draws Down on Its Official International Reserves

Canada reduced its official reserves of assets in the fourth quarter of 2002 by $559 million, compared with a $1.1 billion increase recorded in the same quarter in 2001.

Key Trade and Investment Highlights for 2002

Canada's two-way trade in 2002 increased to $2.44 billion per day, up from $2.43 billion in 2001. Two-way merchandise trade advanced marginally (0.2%), while two-way services trade expanded by a more robust 2.3%.

Lower Current Account Surplus

The current account surplus contracted from $30.0 billion in 2001 to $17.3 billion in 2002, led downwards by a reduced balance in goods and services, which declined by $9.3 billion. For the year as a whole, exports of goods and services were down by 0.6%, while imports expanded by 1.6%.

Merchandise Imports Expand while Exports Decline

Merchandise exports fell by 1.0% in 2002—led lower by reduced shipments to the U.S. On the other hand, merchandise imports expanded by 1.6%. Although merchandise imports from the U.K. and U.S. declined, increased imports from all other markets underpinned the expansion in imports. As a result, the overall merchandise trade balance decreased by $9.8 billion to $54.2 billion in 2002—down from a record high of $64.0 billion in 2001. Separately, the merchandise trade balance with the U.K. improved in 2002, while the trade balance with all other major markets declined.

Merchandise Imports and Exports to the U.S. Decline

Canada's annual merchandise exports to the U.S. declined by 0.8% and imports by 0.1% in 2002. Consequently, the record high bilateral merchandise trade surplus of 2001 declined in 2002—from $95.9 billion to $93.3 billion.

Bilateral Merchandise Trade with Japan, the EU, Mexico and China

In 2002, both merchandise exports and imports from Japan expanded over 2001. Exports to Japan were up by 2.4%—it was the only major export market to expand—while imports from Japan increased by 10.9%. As a result, the merchandise trade balance with Japan declined by $925 million in 2002. Merchandise exports to the EU fell by 4.9% in 2002, led by a 10.1% decrease in exports to the U.K. Imports from the EU increased by 3.0% as a 13.1% reduction in imports from the U.K. dragged down the 11.2% expansion in imports from the remaining EU countries. With fewer exports and more imports from the EU, the merchandise trade deficit with the EU worsened from $12.8 billion in 2001 to $14.9 billion in 2002. Shipments to Mexico declined by 13.1% over 2001, while imports from Mexico expanded by 4.8%. Exports to China fell by 5.2% in 2002, while merchandise imports from China grew rapidly, up 25.6%. In 2002, China moved ahead of Japan to rank as the second-largest source country for imports.

Merchandise Trade by Commodity Group

Merchandise exports experienced mixed developments in 2002, with declining exports in energy (down 8.5% over 2001), forestry (down 6.8%), machinery and equipment (down 5.0%) and agriculture (down 1.1%), and increased exports for consumer goods (up 8.6%), autos (up 4.5%) and industrial goods (up 3.9%).

Increased merchandise imports in 2002 reflected strong expansion in autos (up 12.3% over 2001), forestry (up 8.6%), consumer goods (up 8.1%) and agriculture (up 7.0%). At the same time, imports of energy fell by 7.3% and imports of machinery and equipment dropped by 5.9%. The deterioration of the merchandise trade balance in 2002 for autos (down $4.7 billion), energy (down $3.4 billion) and agriculture (down $1.8 billion) explains most of the decline in the overall merchandise trade balance in 2002. Gains and losses in the other sectors largely offset one another.

Reduction in the Services Trade Deficit

Growth in services exports outpaced growth in services imports (2.8% compared with 1.8%), resulting in a narrowing of the services trade deficit to $7.9 billion in 2002 from $8.4 billion a year earlier. Growth was led by commercial services trade—exports of commercial services in 2002 increased by 4.2% over 2001 and imports of commercial services expanded by 2.8%. On the export side, the expansion in commercial services was accompanied by a modest increase in transport services and a reduction in travel services.

Foreign Direct Investment

Both inward and outward FDI flows slowed in 2002, with each about 20% lower than their respective levels a year earlier. As in 2001, outward FDI flows in 2002 outpaced inward FDI flows. However, with inward FDI at $43.8 billion in 2002 and outward FDI at $33.6 billion, the difference narrowed to $10.3 billion compared with $12.4 billion in 2001. Reductions in outward FDI flows were predominantly in the wood and paper and the services and retail sectors, while the machinery and transport sector registered an increase. A drastic decline in inward FDI in the energy sector, coupled with a more modest decline in the wood and paper sector, explains most of the overall decline in inward FDI. On a regional note, the declines in FDI flows to and from the U.S. were the principal reasons for the reduced inward and outward FDI flows observed in 2002. Outward FDI flows to the U.S. fell from $33.7 billion to $15.5 billion, as the U.S. share of outward FDI plummeted to 35.2% from 61.4% a year earlier—predominantly in favour of outward FDI to the EU (other than the U.K.).

Inward FDI from the U.S. declined from $38.7 billion in 2001 to $25.0 billion in 2002, as the share of annual inward FDI flows originating from the U.S. declined from 91.0% in 2001 to 74.7% in 2002. Inward FDI flows from the U.K. saw a sharp decline from 2001 to 2002, while there was a substantial increase in inward investment from the non-U.K. EU countries. Overall, the EU maintained its position as the second-largest source of inward FDI in 2002, after the U.S.

Portfolio Investments

Canadian net investment in foreign securities (bonds and stocks) was $24.7 billion in 2002, down from $37.7 billion in 2001—large reductions in stock holdings (to about half of the 2001 levels) were only partially offset by modest increases in bond holdings. Similarly, foreign investments in Canadian securities declined from $30.1 billion in 2001 to $17.9 billion in 2002.

Official International Reserves Reduced

Canada reduced its holdings of official international reserves by $298 million in 2002. In contrast, $3.3 billion was added to the reserves in 2001.