Trade Update 2001

Second Annual Report on
Canada's State of Trade

May 2001

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ABOUT THIS DOCUMENT

In A PERIOD OF ONGOING ECONOMIC INTEGRATION both in the Americas and globally, trade and investment have a growing impact on the lives of all Canadians. As the markets for Canada's production of goods and services are increasingly found beyond our borders, and as Canadians continue to depend on goods and services produced abroad, whether for consumption or as inputs to raise domestic production, economic developments abroad are becoming more important.

Accordingly, Canadians are becoming more interested in issues in the international economic domain. This positive development has brought an increased demand for comprehensive information and analysis on Canada's trade and investment performance in a global context. This document is intended to help fill this demand. It reviews and analyses the major developments in Canada's international trade and investment in 2000 against the background of economic trends and performance at home and abroad.

The Economic and Trade Analysis Division (EET) of the Department of Foreign Affairs and International Trade prepared this report under the direction of John M. Curtis, Senior Economic Advisor and Co-ordinator. Hung-Hay Lau, Deputy Director and Senior Research Co-ordinator, wrote the report, with contributions from Suzanne Desjardins, Clea Coronel, Samad Uddin, Ming-Tao Chen and Sylvain Leger.

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A Message from the Honourable Pierre S. Pettigrew, Minister for International Trade

CANADA'S ECONOMY IN 2000 reached a number of significant milestones — the highest growth rate in 12 years, the ninth consecutive year of growth, the longest period of uninterrupted growth in more than 30 years, our best employment record in nearly a quarter of a century, and the best job creation record of any of the leading industrial countries. Simply put, in 2000, Canadians had more jobs, better opportunities, and more income. It was trade that drove our growth, providing the means for the Government of Canada to re-invest in education and innovation, in our universal health care system, and in our youth.

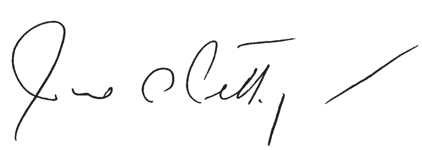
Trade Update 2001, the second annual report on Canada's State of Trade, documents new records in Canada's trade and investment performance. Our exports increased by nearly 15 percent, and are now equivalent to 45.6 percent — nearly half — of our gross domestic product. Overall, Canada traded close to $2.5 billion per day, on average, with the rest of the world, every day of the year. Our net external indebtedness fell to the lowest level in 50 years. We attracted a record $93.2 billion in new foreign direct investment, a massive vote of confidence in the future of Canada's economy. And Canadians looked confidently abroad for new business opportunities, investing nearly $62 billion to expand our global business presence.

Success in global markets is at the heart of Canada's continued technology orientation, fuelling innovation and financing Canada's evolution from a reliance on primary resources to a more knowledge-intensive economy. High technology exports rose 30 percent in 2000, nearly twice the rate of our overall exports. Similarly, our exports of knowledge-intensive services are the fastest growing segment of our services trade and now represent more than 50 percent of our services exports. In fact, since 1993, Canada has enjoyed annual double-digit growth in important knowledge-intensive service exports like R&D services, financial services, royalties and fees, and engineering. This success translates into high-quality jobs and a greater range of opportunity than ever for Canadians, particularly our young people embarking on careers in these dynamic new sectors of the economy.

In addition to providing better jobs and more opportunities for Canadians, trade finances the social system that Canadians cherish and which reflects our values of fairness, inclusion and equality. All Canadians, in all regions, have a stake in our continued trade success. So, even as we note our record of trade and investment achievement, we recognize and prepare to meet the challenges — such as a slowing U.S. economy — that lie before us. Past trade performance is no guarantee of future success.

In the hemisphere, with bilateral trade partners, and in the wider arena of the World Trade Organization, we must redouble our pursuit of freer trade that is governed by clear and equitable rules. Canadians can compete anywhere in the world, as long as there is a level playing field. The Government of Canada, through our network of Trade Commissioners and our trade development efforts like Team Canada, will continue to open doors for Canadian exporters in important markets.

Finally, we must remind ourselves that these record-breaking trade numbers represent the contributions of individual Canadians, including your neighbours and other people in your community. I want to congratulate the millions of Canadians — workers, entrepreneurs, business owners and exporters large and small — who have met the challenge of global competition. Your success has been shared with all Canadians.



HIGHLIGHTS OF CANADA'S TRADE AND ECONOMIC PERFORMANCE

For Canada, 2000 marked the ninth consecutive year of economic growth, the longest and most stable expansions since the 1960s.

2000 Economic Highlights and Prospects[1]

- *Gross domestic product* at current prices, reached the one trillion dollar mark ($1,039 billion) for the first time in history, or $33,727 per capita.
- *Real growth* (adjusted for inflation) in GDP accelerated to 4.7 percent from 4.5 percent in 1999. This was the highest growth rate in the last decade. In the context of a slowdown in economic growth in the United States, most analysts are expecting Canada's real GDP to increase at a more moderate rate of between 2.5 percent and 3 percent this year. This projected growth is of the same order of magnitude as that of 2.5 percent recorded over 1989 and 2000.
- *Consumer price inflation* rose to 2.7 percent in 2000, from 1.7 percent in 1999, with all of the acceleration accounted for by the increase in energy prices. Nevertheless, it remained within the Bank of Canada's 1 percent to 3 percent target band. Excluding energy, the all-item index rose by 1.5 percent in 2000, the same as increases seen since 1996. Core inflation, which excludes food and energy, was 1.4 percent in 2000, about the same as the 1.5 percent recorded in 1999.
- *Job growth* in 2000 was 2.2 percent (319,000), with all of the increase occurring in full-time employment.
- *The unemployment rate* fell from an average of 7.6 percent in 1999 to 6.8 percent in 2000, the lowest since 1974.
- *The Canadian dollar* closed the year 2000 at US$0.667, down from US$0.693 at the close of 1999. For 2000 as a whole, it averaged US$0.6733, virtually unchanged from its annual averages in both 1998 and 1999. Against the European common currency, however, the average value of the Canadian dollar strengthened by 11.5 percent to 0.73 euro in 2000. It appreciated against the pound sterling by 6.8 percent.

International trade played an important role in sustaining Canada's economic growth in 2000.

- Exports of goods and services increased 14.9 percent to reach $473.9 billion, equivalent to 45.6 percent of GDP, up from 25 percent in 1991.
- Imports of goods and services increased 10.8 percent to reach $426.0 billion, equivalent to 41 percent of GDP.
- Canada's rising outward-orientation is also evident in indicators such as tariff rates and duty-free imports entering Canada. Average Canadian tariff rates have come down substantially during the last decade, from 3.7 percent in 1989 to 0.9 percent by 1999. At the same time, imports entering Canada duty free rose from 65.7 percent of total imports in 1989 to 90.6 percent by 1999.
- The current account balance swung from a deficit of $3.4 billion or 0.4 percent of GDP in 1999 to a surplus of $18.9 billion or 1.8 percent of GDP in 2000 reflecting an increase in the merchandise trade surplus to $54.4 billion from $33.8 billion in 1999.

[1] All monetary amounts are expressed in Canadian dollars, unless otherwise indicated.

The direction of Canada's exports in 2000 was significantly affected by the dichotomy in global economic performance.

- Exports of goods and services to the United States grew much more strongly than did overall trade, as the U.S. economy advanced at a robust rate of 5 percent in 2000 up from 4.2 percent in 1999 the tenth year of economic expansion. The share of the U.S. in Canada's exports of goods and services rose to a record high of 82.9 percent, up from 82.6 percent in 1999. In particular, the U.S. share of Canada's merchandise exports rose to 86.1 percent in 2000 up from 85.8 percent a year earlier.

- The bulk of Canada-U.S. trade is concentrated in a limited number of regions, reflecting geographical proximity and complementarity in the mix of production (Box A). In recent years, Ontario accounted for about 60 percent of Canada's exports to the United States and three quarters of Canada's imports from the United States.

- Exports of goods and services to Japan posted an increase of 7.4 percent in 2000 a reversal of the steady decline observed between 1995 and 1999.

- Sales to the European Union picked up momentum in 2000 as growth in major Western European economies such as Germany and the U.K. firmed.

- Exports to most other major markets were, for the most part, up sharply on the year as well:

  - The strong economic rebound in Southeast Asia in 2000 was reflected in a general recovery in Canada's exports to the region. In particular, double-digit rates of increases were recorded in merchandise exports to the Peoples' Republic of China (up 39.3 percent), the Philippines (up 30.7 percent), Thailand (up 22.7 percent), and South Korea (up 12.3 percent).
  - Merchandise exports to most major Latin American destinations recovered smartly in 2000, reflecting an improvement in general economic conditions in the region. Exports to Canada's free trade partners in the region staged impressive gains, with Mexico up 26.5 percent, Costa Rica up 25.2 percent and Chile up 23.6 percent.
  - Canada's merchandise trade with member countries of the FTAA (Free Trade Agreement of the Americas) is dominated by trade with the United States, which accounted for 98.4 of exports and 92.7 percent of imports in 2000. This leaves 1.6 percent and 7.3 percent for exports and imports, respectively, for countries outside of the United States (Box C).

The product mix of Canada's exports experienced significant shifts in 2000.

- The highlight of 2000 was the spectacular growth in energy exports such as crude petroleum, natural gas, electricity and petroleum products. The gains in the export volume of energy and energy products were magnified by steep increases in the price of energy in world markets. As a net exporter of energy, Canada has benefited substantially from the escalation in the world price of energy, even if the high cost of energy adversely affects both manufacturing activity in Canada and consumers across the country. Canada's surplus in energy trade rose to $34.8 billion in 2000, up from $19 billion in 1999.

- Exports of machinery and equipment (M&E) increased sharply through 2000 to regain the position as the most important among all major sectors in Canada's export sales. The 22.8 percent increase in the value of M&E exports was led by exports of high-tech products such as telecommunications equipment, which shot up by 59.1 percent in the year. In 2000, exports of M&E represented 25.3 percent of goods exports, somewhat higher than the automotive sector's share of 23.1 percent.

- The value of Canada's merchandise exports and imports of high-tech products rose at a very rapid pace in recent years (Box B). In 2000, Canada's high-tech exports increased by 30 percent and imports by 26.2 percent, as measured in constant dollars, substantially outpacing growth in the remaining merchandise trade categories.
- Exports of metals, chemicals and other industrial goods also increased at double-digit rates in 2000, reflecting gains in both prices and volumes.
- Exports of services rose by 8.6 percent in 2000 led by transportation (in support of Canada's growth in merchandise trade) and knowledge-based activity such as commercial services. The overall rate of increase in services exports was smaller than that of exports of merchandise.

Two-way direct investment flows with the world continued at historically high levels, and Canada's net external indebtedness as a percent of GDP declined to the lowest point since the early 1950s.

- FDI flows, whether inward or outward, are beneficial to economic development in Canada (Box D). The flow of FDI into Canada reached a new record in 2000.
- Meanwhile, the flow of Canadian direct investment abroad (CDIA) also established a new record, following an easing in 1999.
- As in 1999, FDI into Canada continued to exceed CDIA in 2000, a reversal of the pattern observed earlier in the 1990s.
- As in recent years, mergers and acquisitions activity accounted for much of the direct investment flows in 2000.
- Canada's net external indebtedness, which had been declining since 1976 as a share of GDP, also declined in terms of absolute value in 2000 for the second year in a row.

Trends

- Trade performance in 2000 capped a decade of exceptional growth, continuing its trend as the principal driver of the Canada's economic growth. Over the period 1990-2000 during which real (inflation-adjusted) GDP grew by 2.5 percent at a compound annual rate, growth was 8.2 percent for real exports of goods and services and 7.4 percent for imports of goods and services.
- The sustained high rate of expansion of trade relative to GDP is indicative of the reorientation of Canada's industrial structure toward sectors of particular strength in the global economy. This reorientation and associated changes are in response to the new opportunities and competitive pressures created by the Canada-U.S. Free Trade Agreement (FTA) and its successor the North American Free Trade Agreement (NAFTA), along with the multilateral reduction of trade barriers pursuant to the agreements reached in the 1986-1994 Uruguay Round of trade negotiations.
- The higher rate of growth of exports over imports during the last decade reflected a combination of the more robust growth in the U.S. economy, the relatively tighter supply situation in the United States, as well as the effects of the decline in the Canada-U.S. bilateral exchange rate over the course of the decade.

Table 1: Trade as a percent of GDP, 1989-2000

	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Total exports	25.6	25.7	25.0	27.0	30.1	34.0	37.3	38.4	39.1	41.2	43.1	45.6
Goods	22.4	22.4	21.6	23.4	26.2	29.7	32.9	33.6	34.3	35.8	37.6	40.2
Services	3.2	3.3	3.4	3.6	3.9	4.3	4.4	4.8	4.8	5.4	5.4	5.4
Total imports	25.6	25.7	25.7	27.4	30.2	32.9	34.3	34.4	37.5	39.8	40.2	41.0
Goods	21.2	20.8	20.6	22.1	24.4	27.1	28.5	28.6	31.6	33.6	34.1	35.0
Services	4.4	4.9	5.1	5.3	5.8	5.8	5.7	5.8	5.8	6.2	6.0	6.0

Source: Statistics Canada, *National Income and Expenditure Accounts,* Catalogue no. 13-001-PPB, Fourth Quarter 2000. Statistics Canada, *Canada's Balance of International Payments*, Catalogue no. 67-001-XPB, Fourth Quarter 2000.

The long-standing economic relationship with the United States continued to be the dominant factor in Canada's trade and investment performance.

- In 2000 two-way trade in goods and services with the U.S. grew by 11.7 percent, with goods trade up 12.3 percent and services up 7 percent. The reduction/removal of trade barriers through trade agreements has encouraged consolidation and mass production of specific goods and services on one side of the border to take advantage of efficiency gains. As considerations based on comparative advantage alter the pattern of production, international trade has expanded rapidly.
- Two-way trade in goods and services jumped from $626.7 billion in 1999 to 700 billion in 2000, representing more than $1.9 billion of business per day. For the last decade as a whole, two-way trade grew at an average annual pace of 11.4 percent.
- With this performance, Canada turned a small but persistent deficit on the bilateral current account over the period 1988 through 1993 into a rapidly growing surplus in the years since. This reflected both an expansion of the traditional bilateral surplus in merchandise trade, as well as a substantial reduction in the long-standing deficit in services trade.
- Canada's current account surplus with the U.S. increased to an all-time high of $63.5 billion in 2000 from $32.4 billion in 1999.
- From a Canadian perspective, the trading relationship with the U.S. dominates the statistics: the U.S. accounts for 82.9 percent of Canada's exports of goods and services and 72.1 percent of our imports.
- However, data on Canada's exports to the United States include shipments to third countries via the United States, and this understates the share going to countries outside of the United States. For instance, our trading partners' import data reveal that Canada's exports to these countries are invariably higher than are indicated by our own export statistics. Ongoing work on data reconciliation with Canada's major trading partners such as Japan, the EU, Mexico, China and Korea will improve our knowledge of the distribution of Canadian exports.[2]

[2] "The Impact of Transhipments on Canada's International Trade Statistics," *Canadian Trade Review*, Department of Foreign Affairs and International Trade, Third Quarter 2000.

Table 2: Two-way Trade, Canada and the United States, 1990-2000

	Value (millions of current dollars)			Annual growth (percent)		
	Goods	Services	Goods & Services	Goods	Services	Goods & Services
1990-2000	366,204	49,140	415,343	11.6	9.9	11.4
1997	454 140	57 923	512 063	12.8	8.0	12.3
1998	503 293	63 248	566 541	10.8	9.2	10.6
1999	558 722	67 982	626 704	11.0	7.5	10.6
2000	627,208	72,762	699,970	12.3	7.0	11.7

Source: Statistics Canada, *Canada's Balance of International Payments*, Catalogue no. 67-001-XPB, Fourth Quarter 2000.

- From a U.S. perspective, Canada is the United States' largest trading partner, in terms of both exports and imports (Table 3). Canada carries a trade weight in the U.S. market that is substantially greater than our economic weight in the global economy. As a percent of U.S. merchandise imports, nevertheless, Canada's market presence in the United States declined from 19.3 percent in 1999 to 18.8 percent in 2000 as U.S. imports from countries outside of Canada grew at a more rapid pace.

Table 3: Shares of U.S. Goods Imports From, and Exports To, Five Main Trading Partners

	As percent of total U.S. imports					As percent of total U.S. exports				
	1994-1996	**1997**	**1998**	**1999**	**2000**	**1994-1996**	**1997**	**1998**	**1999**	**2000**
Canada	19.5	19.2	19.0	19.3	18.8	23.4	22.0	23.0	23.9	22.9
EU	17.9	18.1	19.3	19.1	18.1	21.4	20.4	21.8	21.8	21.1
Mexico	8.4	9.9	10.4	10.7	11.2	13.4	10.4	11.5	12.5	14.3
Japan	16.2	14.0	13.4	12.8	12.0	8.3	9.5	8.5	8.3	8.3
China	6.2	7.2	7.8	8.0	8.2	2.0	1.9	2.1	1.9	2.1

Source: U.S. Census Bureau, *International Trade Statistics*. Note: Data are on a customs basis.

Prospects for trade contingent on economic developments in the United States and abroad.

- Canada has benefited from its long-standing reliance on trade with other countries, particularly with the United States, the world's largest market. Naturally, these close trade ties with the United States also expose Canada to any economic uncertainty in the U.S. economy. At present, the consensus calls for a slowdown in U.S. economic growth this year, particularly in the first half. Indeed, real GDP in the United States grew at an annual rate of 1 percent in the fourth quarter of 2000, and appears to remain sluggish in the first quarter of this year. Even with an expected rapid pickup in the rate of economic growth during the second half of this year, U.S. GDP growth is likely to come down from 5 percent in 2000 to around 2 percent in 2001, with consequent impact on U.S. demand for Canadian goods and services.

- While Canada's exports will not escape unscathed from the slowdown in U.S. economic growth, the impact will be cushioned by Canada's competitive exchange rate. In 2000, fully 100 percent of Canada's $51 billion worth of exports of crude petroleum, natural gas and electricity was shipped to the United States, representing more than 14 percent of Canada's merchandise exports to the United States. With the energy shortage in the United States, the high demand for Canada's energy exports will most likely be sustained, particularly in an environment of increased production and pipeline capacities in Canada.

- The forceful actions taken by the U.S. monetary and fiscal authorities to revitalize the economic expansion, now in its 10th year, will over the course of the year bolster the housing sector and big-ticket consumer purchases via reduced mortgage payments, lower financing costs, and higher after-tax income. These interest-rate sensitive sectors figure prominently in Canada's exports. In effect, 50 percent of Canada's merchandise exports, taken up in the form of energy, forest products as well as autos and other consumer goods, can be expected to remain strong over the next year or two. In addition, information technology, and the machinery and equipment that accompany it, will most likely recover quickly in this dynamic international economy.

- Historically, the weakness in the U.S. economy is quickly propagated through the economies of Canada's major trading partners. Most forecasters are thus expecting a slowdown in economic growth in the European economy to around 2.5 percent in 2001, from about 3.5 percent in 2000. As well, economic prospects in Japan remain uncertain. In effect, the propagation of the weakness in the U.S. economy would, in turn, have an impact on Canada's exports of goods and services to the EU and to Japan, the destinations of 6.3 percent and 2.4 percent, respectively, of Canada's exports in 2000. This situation makes it clear that, even with greater emphasis on these markets, Canada would not be shielded from the impact of a downturn in economic growth in the United States.

I. MERCHANDISE TRADE

The economic environment was generally favourable for Canadian exporters in 2000: economic growth improved globally, and the prices for key commodity exports, such as energy, food and industrial materials (including metals and chemicals), improved markedly. In addition, the exchange rate remained at levels well below most measures of its purchasing power parity.[3] In 2000, the value of Canada's merchandise exports rose to $417.7 billion, up 15.8 percent from $360.6 billion in 1999. Meanwhile, the acceleration of real growth in Canada to 4.7 percent fed strong import demand. Canada imported goods worth $363.2 billion, up 11.1 percent from $326.8 billion in 1999. This resulted in a record merchandise trade surplus of $54.5 billion or 5.2 percent of nominal GDP in 2000, compared to $33.8 billion or 3.5 percent of GDP in 1999.

THE DIRECTION OF TRADE IN 2000

The share of Canada's exports in the United States has risen over the years. In the 1970s and 1980s, the rise in the U.S. share was reflected principally in a lower share of exports being shipped to Europe. In the 1990s, the rise in the U.S. share was mirrored in a diminution of shares of all regions of the world outside of the United States.

Table 4: Shares of Canada's Merchandise Exports (percent), 1970-2000

	1970-1979	1980-1989	1990-2000	1997	1998	1999	2000
U.S.	68.6	73.5	80.8	80.8	83.7	85.8	86.1
EU	11.3	8.0	6.1	5.5	5.5	5.1	5.0
Japan	5.9	5.5	3.9	4.0	3.0	2.6	2.4
ROW (rest of the world)	14.1	13.0	9.2	9.6	7.8	6.6	6.5

Source: Statistics Canada, CANSIM. Matrix no. 3685: *Merchandise Exports on a Balance of Payments Basis by 64 Major Groups and by 6 Principal Trading Areas based on the Standard Commodity Classification.*

Review of export performance by major partner economies and regions in 2000

The United States

Market conditions in the United States, which by 2000 was experiencing its longest peacetime economic expansion, were extremely favourable for Canada's exporters in 2000. U.S. GDP grew 5 percent in real terms (the fifth consecutive year of growth exceeding 4 percent), with even stronger growth in consumer spending and business investment in plants and equipment.

- U.S. consumer expenditure increased 5.3 percent in 2000 as demand was bolstered by increases in employment and a decrease in the savings rate. Spending on durable goods rose 9.6 percent in 2000 (following 12.4 percent in 1999).
- Business investment rose 12.6 percent in 2000, led by spending on M&E, extending by another year the long run of rapid growth in investment outlays.

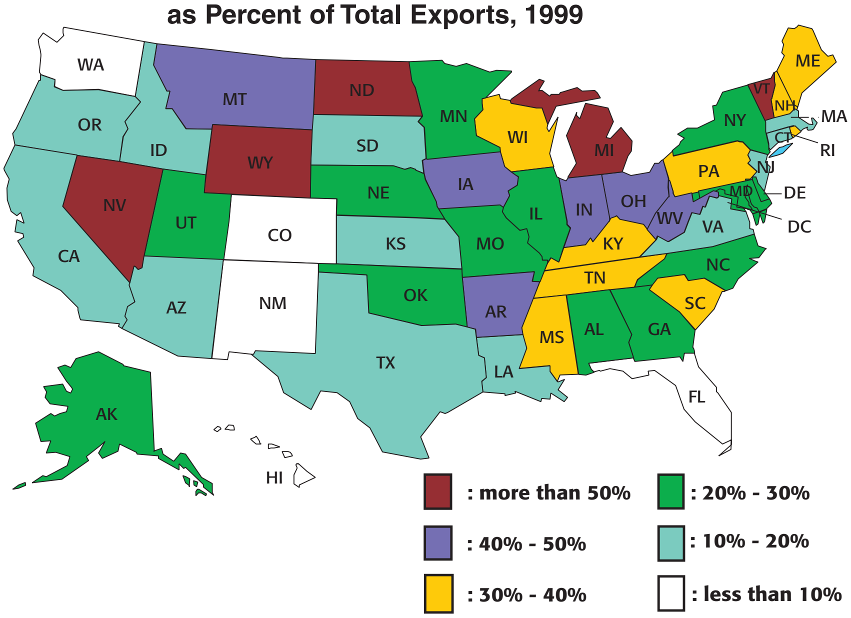
The strong U.S. domestic demand growth boosted Canada's exports of goods and services to the U.S. by 15.4 percent in 2000. With exports to Canada's other major markets expanding less strongly, the U.S. share of Canada's exports of goods and services edged up to 82.9 percent from 82.6 percent in 1999. In the case of merchandise, exports to the United States represented 86.1 percent of the goods total in 2000, up from 85.8 percent in 1999.

[3] The average value of the Canadian dollar versus the U.S. dollar was virtually unchanged in 2000. Although the average value of the Canadian dollar was up sharply against the euro and the U.K. pound, it lost value over the year versus the Japanese yen by about 5 percent.

Box A: Regional Merchandise Trade between Canada's Provinces and U.S. States [4]

Although the Canadian economy is small relative to those of the major industrialized countries, Canada is the most important trading partner of the United States both in terms of the market for U.S. exports and the source of U.S. imports. However, the pattern of trade varies considerably among the major regions in the two countries as a result of product complementarities and distance. For a number of U.S. states, trade with Canada is even more remarkable than national figures suggest. For instance, trade with Canada accounted for more than 50 percent of exports by Vermont, Wyoming, North Dakota, Michigan and Nevada (Figure A1). Vermont's dependence on trade with Canada is the highest among the states, with about 88 percent of the exports destined for Canada. By region, the U.S. Midwest is the most dependent on Canada for its exports.

Figure A1: U.S. States Exports to Canada as Percent of Total Exports, 1999



Source: Author's tabulation based on data from U.S. Department of Commerce.

Distribution of Trade by Region

As the bulk of Canada-U.S. trade is concentrated in certain regions, the national volume of trade is, by and large, affected by economic developments in these particular regions. For this reason, it is important to assess the pattern of interregional trade between the two countries. The regional distributions of Canada-U.S. two-way merchandise trade are shown in Figures A2 and A3. Canada's trade with the U.S. is mainly dominated by the central region, which consists of Ontario and Quebec.[5] The national share of Western Canada (British Columbia and the Prairies) was higher than that of Quebec, with 21 percent in southbound and 14 percent in northbound trade (Figure A2). The Atlantic provinces accounted for less than 3 percent of total Canada-U.S. two-way trade.

[4] For cost considerations, we use Statistic Canada data over 1995-1999 to illustrate the pattern of trade. Data for trade in goods and services by province for 2000 will be available in October 2001. The Web site version of this report will be updated in October 2001 to incorporate this information.

[5] Ontario represented 57 percent of Canada's exports to the U.S. and 75 percent of Canada's imports from the U.S., whereas Quebec accounted for 18 percent and 10 percent in exports and imports, respectively.

The U.S. Midwest is the most important regional market for Canada, accounting for 41 percent of Canada's exports to the U.S. in 1999, while the Northeast was the second most important destination, with 26 percent of southbound flow (Figure A3). The distribution of Canada's imports from U.S. regional markets is rather different from that of exports: while the Midwest (44 percent) remained the most important trade partner, the South (23 percent) replaced the Northeast (20 percent) to become Canada's second most important U.S. regional supplier of merchandise imports.

In Figure A4, the four U.S. regions are broken down into eight zones. It can be seen that Canada's trade with the eight U.S. zones is dominated by Great Lakes states, which accounted for 35 percent of Canada's exports and 38 percent of Canada's imports in 1999. The U.S. Mideast and Far West were the second and third most important markets for Canada's exports.[6] The U.S. Southeast and Mideast were the second and third most important sources of Canada's imports.

Figure A2: Distribution of Canada's Trade with the U.S. by Region (percent), 1999

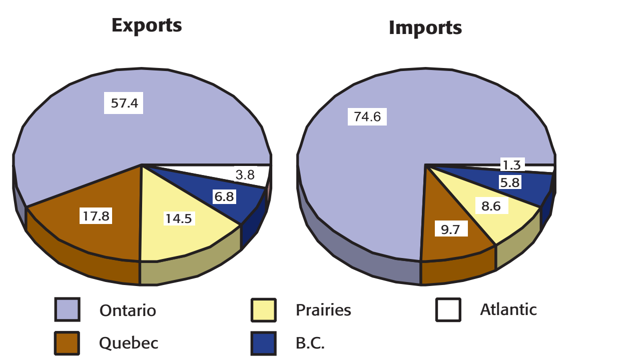
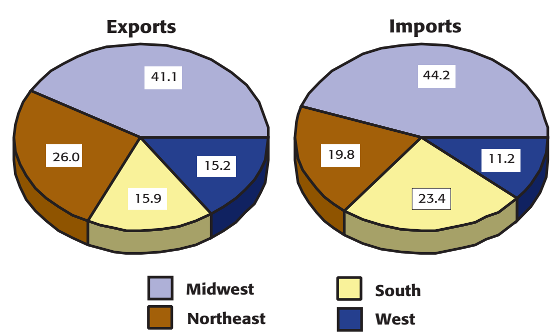


Figure A3: Distribution of U.S. Trade with Canada by Region (percent), 1999



Source: Statistics Canada

Interregional Trade Flows

At a more disaggregated level, it can be seen that Canada-U.S. trade is dominated by a limited number of regional flows. Among the cross-border flows between the five regions in Canada and the eight regions in the U.S., only 14 were worth more than $10 billion, together accounting for four fifths of Canada-U.S. cross-border trade. Ontario's trade with each of the eight U.S. regions exceeded $10 billion, totalling 65 percent of Canada's overall transborder two-way trade. The largest two flows were Ontario-Great Lakes (30 percent) and Ontario-Mideast (11 percent). Quebec's close U.S. trading partners were the Mideast (3.5 percent) and New England (2.9 percent). Border effects are also important in the Pacific and Atlantic regions: B.C.'s trade ties with Pacific states (3.1 percent) symbolized the role of the Interstate 5 corridor; the Prairies' two key trading regions were the Great Lakes (2.8 percent) and the Plains States (2.5 percent). Although the Rocky Mountain region also borders the Prairies, two-way trade between these two regions was insignificant since the primary economic activity of these U.S. states is agriculture, a sector that is not complementary to

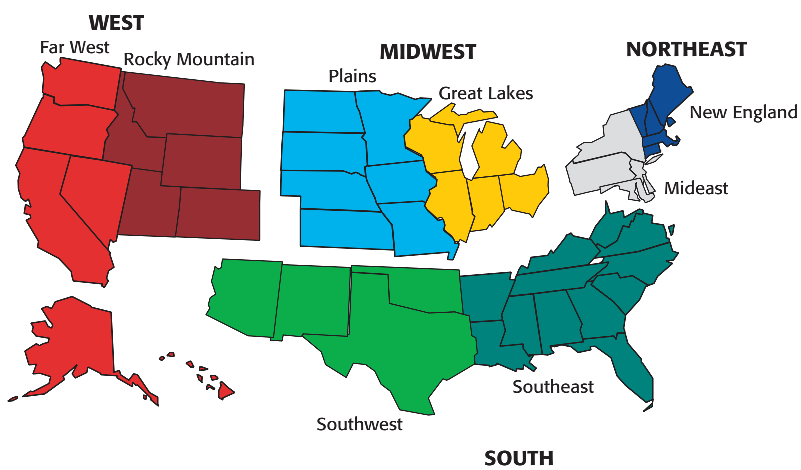
[6] The Mideast region covers New York, New Jersey, Pennsylvania, Delaware, Maryland and the District of Columbia.

activity in the Prairies. Finally, Atlantic Canada accounted for a very small portion of Canada-U.S. trade. Its two neighbouring U.S. regions, New England (0.5 percent) and Mideast (0.2 percent), were Atlantic Canada's most important trading partners.

Major Partner of U.S. Trade by States

The border plays an important role in U.S. state trade with Canada. Most of the key importing states, except for California and Texas, are located along the border (Table A1). Michigan occupied almost one quarter of total U.S. imports from Canada, while the Great Lakes (including Illinois and Ohio), Mideast (New York and Pennsylvania) and Pacific states (California and Washington) were the other main importing regions. In particular, the Ontario-Michigan trade flow was the most important among all province-state trade between the two countries (accounting for about 18 percent of total two-way trade), followed by Ontario-New York (6.7 percent), and Ontario-Ohio (5.5 percent). Three quarters of Ontario's exports to Michigan were concentrated in transportation equipment such as automotive products. As for Ontario's southbound trade with New York, the second most important state for Canada's exports, automotive products were also important, representing 40 percent of Ontario's exports to New York. The fast-growing importing states, on the contrary, were those importing less than 1 percent of Canada's exports to the U.S. during the second half of the 1990s, with the exception of California and New York (Table A1). It is worth noting that negative import growth for the past five years was recorded only in Rhode Island (-0.9 percent) and Wisconsin (-0.3 percent).

Figure A4: U.S. DOC Regions



Source: U.S. Department of Commerce

Canada's imports from the U.S. were more diversified among U.S. states than is the case of Canada's exports to the U.S., even though Canada was the top destination for exports of 35 U.S. states in 1999 (Table A2). For example, exports to the top five states from Canada represented roughly 50 percent of total Canadian exports to the U.S. over the past five years, compared with 44 percent for their imports. As in the case of Canada's exports, Canada's imports from the U.S. were heavily concentrated in Great Lakes and Mideast regions. Again, the growth in Canada's imports from U.S. states was the highest among states that account for a small share of Canada's overall imports from the United States. The only two states that experienced declines in exports to Canada during 1995-1999 were Idaho (-3.5 percent) and Maryland (-3.2 percent).

Overall, Canada's exports to the U.S. were dominated by trade with eight states plus the District of Columbia (Table A3). Canada's exports to each of these states exceeded Canada's exports to Japan, Canada's second most important export partner. The value of exports to 32 of the various states in the U.S. was so significant that each one could be ranked among Canada's top 10 trading partner countries.

Table A1: Distribution of Canada's Exports to U.S. States (percent), 1995-1999

	Share			Growth	
Ranking	State	Average	Ranking	State	Average
1	Michigan	23.9	1	Hawaii	227.6
2	New York	10.9	2	Wyoming	122.4
3	Illinois	5.4	3	New Mexico	61.7
4	California	5.3	4	Arizona	30.5
5	Ohio	4.7	5	Oklahoma	27.1
6	Washington	3.8	6	Nevada	26.9
7	Texas	3.7	7	Montana	25.8
8	Pennsylvania	3.3	8	Kansas	22.1
9	Minnesota	2.9	9	California	21.5
10	Massachusetts	2.7	10	New York	21.3

Table A2: Distribution of Canada's Imports from U.S. States (percent), 1995-1999

	Share			Growth	
Ranking	State	Average	Ranking	State	Average
1	Michigan	13.9	1	Wyoming	41.9
2	Ohio	9.3	2	Missouri	21.4
3	New York	7.5	3	Nevada	21.3
4	Illinois	6.4	4	Kentucky	17.7
5	California	6.4	5	Oklahoma	17.7
6	Texas	5.2	6	Georgia	17.5
7	Indiana	4.7	7	Montana	16.9
8	Pennsylvania	4.2	8	District of Columbia	16.7
9	North Carolina	2.9	9	New Mexico	15.8
10	Wisconsin	2.8	10	Virginia	15.7

Source: Statistics Canada

Table A3: Distribution of Canada's Exports to U.S. States (percent), 1999

1999 U.S. Ranking	States	1999 Imports from Canada (C$ millions)	Share of total U.S. Imports from Canada	1999 Equivalent World Ranking	Share of Total Canada's Exports to the World
1	Michigan	67,497.5	21.9	1	19.0
2	New York	38,297.5	12.4	1	10.8
3	California	21,027.1	6.8	1	5.9
4	Illinois	15,374.6	5.0	1	4.3
5	Ohio	13,763.7	4.5	1	3.9
6	Washington	12,595.7	4.1	1	3.6
7	Pennsylvania	10,211.6	3.3	1	2.9
8	Texas	9,781.7	3.2	1	2.8
9	Minnesota	7,903.2	2.6	3	2.2
10	New Jersey	7,609.5	2.5	3	2.1
11	Massachusetts	7,439.3	2.4	3	2.1
12	Vermont	6,177.3	2.0	3	1.7
13	Wisconsin	5,576.1	1.8	3	1.6
14	Georgia	5,557.8	1.8	3	1.6
15	Indiana	5,494.8	1.8	3	1.6
16	Tennessee	5,256.4	1.7	3	1.5
17	Kentucky	4,875.9	1.6	4	1.4
18	Oregon	4,278.9	1.4	4	1.2
19	North Carolina	4,192.2	1.4	4	1.2
20	Florida	4,164.9	1.4	4	1.2
21	Virginia	3,911.2	1.3	4	1.1
22	Missouri	3,753.5	1.2	4	1.1
23	Maine	2,878.3	0.9	4	0.8
24	South Carolina	2,592.3	0.8	5	0.7
25	Iowa	2,271.9	0.7	6	0.6
26	Connecticut	2,247.9	0.7	6	0.6
27	Maryland	2,229.1	0.7	6	0.6
28	Kansas	2,169.8	0.7	6	0.6
29	Montana	2,117.9	0.7	6	0.6
30	Arizona	2,008.1	0.7	6	0.6
31	Colorado	1,648.2	0.5	9	0.5
32	North Dakota	1,579.7	0.5	10	0.5
33	Alabama	1,549.1	0.5	11	0.4
34	New Hampshire	1,406.3	0.5	12	0.4
35	Oklahoma	1,243.7	0.4	12	0.4
36	Wyoming	1,128.6	0.4	13	0.3
37	Utah	1,056.5	0.3	14	0.3
38	Hawaii	1,025.2	0.3	15	0.3
39	Nevada	963.2	0.3	15	0.3
40	West Virginia	959.7	0.3	16	0.3
41	Arkansas	909.7	0.3	16	0.3
42	Louisiana	866.4	0.3	16	0.2
43	Delaware	778.9	0.3	16	0.2
44	Idaho	776.6	0.3	16	0.2
45	Nebraska	771.5	0.3	16	0.2
46	Mississippi	683.4	0.2	17	0.2
47	Rhode Island	653.5	0.2	17	0.2
48	New Mexico	526.9	0.2	20	0.2
49	South Dakota	409.4	0.1	26	0.1
50	Alaska	248.7	0.1	38	0.1
51	District of Columbia	100.8	0.03	54	0.03

Source: Statistics Canada

The European Union

In Western Europe, economic growth improved throughout 2000. In the Euro-15 area, real GDP growth picked up substantially, averaging 3.4 percent for the year as a whole. Growth in the U.K. also accelerated by 3 percent. Largely as a result of this income growth, Canada's exports of goods and services to the EU increased by 13.8 percent in 2000, led by the growth in merchandise exports, even though the average value of the euro weakened by 13.5 percent in 2000, relative to the Canadian dollar, to $1.37 per euro.

In the case of merchandise (for which country information is available), Canada's exports to key EU countries have increased over the last decade in all cases (Table 5A). However, these increases were smaller than the growth in Canada's overall exports. As a result, the EU's share of Canada's merchandise exports fell from 8.3 percent between 1989 and 1992 to 4.6 percent in 2000. This decline in export share is widespread among all principal EU members.

Table 5A: Canada's Merchandise Exports to the EU Economies, 1989-2000

Economies	Average 1989-1992	Average 1993-1996	1997	1998	1999	2000
Level in $ billions						
Germany	2.2	2.9	2.7	2.7	2.4	3.1
France	1.4	1.6	1.7	1.7	1.9	1.9
United Kingdom	3.3	3.6	3.9	4.4	4.8	5.7
Italy	1.1	1.4	1.5	1.5	1.4	1.7
Other EU	4.4	4.7	5.6	5.9	6.0	6.4
EU-15	12.4	14.1	15.4	16.2	16.5	18.9
As percent of total exports						
Germany	1.5	1.2	0.9	0.9	0.7	0.8
France	0.9	0.7	0.6	0.5	0.5	0.5
United Kingdom	2.2	1.5	1.3	1.4	1.4	1.4
Italy	0.8	0.6	0.5	0.5	0.4	0.4
Other EU	2.9	2.0	1.9	1.8	1.7	1.6
EU-15	8.3	5.9	5.2	5.1	4.7	4.6

Source: Statistics Canada, *Canadian International Merchandise Trade 2000.* Catalogue no. 65-001-XPB, December 2000.

Given regional developments in both Europe and North America in the past decade or so, which have favoured intensified intra-regional trade at the expense of trade with the rest of the world, it is interesting to consider the evolution of Canada's market share in Europe. Table 5B provides an overview of the share of imports of the 15-member European Union obtained from each other (intra-EU) and from the rest of the world.

Table 5B: Intra-EU Merchandise Trade and Imports from Selected Trading Partners, 1989-1999

	1989-1990	1993-1994	1998-1999
Share of EU-15 Imports from major trading partners (percent)			
Intra-EU	62.9	59.8	60.2
EU - ROW	37.1	40.2	39.8
Percentage breakdown of EU-15 imports from ROW			
Total	**100.0**	**100.0**	**100.0**
Canada	2.4	1.8	1.8
U.S.	20.2	19.4	20.3
Japan	12.1	11.3	9.2
China	2.2	4.3	5.4
Switzerland	8.1	7.7	6.6
Other countries	55.0	55.5	56.7

Source: International Monetary Fund, *Direction of Trade Statistics*, various issues.

As can be seen, intra-EU trade only edged up to 60.2 percent of the EU's total imports between 1998 and 1999 from 59.8 percent over 1993-1994. However, Canada's share in total EU imports from non-member countries fell to 1.8 percent in the post-1992 period, from 2.4 percent in 1989-1990. The market share of the United States, the EU's largest supplier, recovered during 1998-1999. China's market presence continued to expand rapidly. By contrast, Japan's market share dropped sharply in the 1990s. The commodity and product structure of trade and the fluctuations in exchange rates played an important role in shaping this observed geographical distribution of trade.

East Asian Economies

Exports to Canada's major markets in East Asia have staged a marked recovery from the financial and economic crisis that hit the region in 1997-1998. Over the course of 2000, all crisis-affected economies returned to positive growth rates as economic conditions progressively improved, even though there was renewed weakness in the Japanese economy during the second half of 2000. Note that trade with East Asian countries is very sensitive to prices of exporters and competitors, and is also very responsive to competitive exchange rate depreciation as well as economic growth. Table 6 summarizes the consequences of these developments for Canada's merchandise exports.

Table 6: Canada's Merchandise Exports to East Asian Economies ($ billions), 1989-2000

Economies	1989-1992	1993-1996	1997	1998	1999	2000
Japan	7.93	10.38	11.17	8.64	8.42	9.01
South Korea	1.63	2.38	3.03	1.82	1.99	2.23
People's Republic of China	1.78	2.62	2.41	2.50	2.66	3.71
Hong Kong	0.85	1.25	1.75	1.43	1.12	1.31
Taiwan	0.95	1.35	1.62	1.18	1.14	1.15
Indonesia	0.35	0.64	0.80	0.55	0.55	0.71
Malaysia	0.25	0.41	0.70	0.48	0.42	0.41
Philippines	0.21	0.25	0.43	0.26	0.30	0.39
Singapore	0.35	0.45	0.55	0.42	0.38	0.37
Thailand	0.39	0.48	0.47	0.30	0.30	0.37
Nine Major East Asian economies	6.76	9.83	11.76	8.95	8.85	10.64
Total East Asia	**14.70**	**20.21**	**22.92**	**17.58**	**17.27**	**19.64**

Source: Statistics Canada, *Canadian International Merchandise Trade* 2000. Catalogue no. 65-001-XPB, December 2000. Customs basis.

In virtually all cases, Canada's merchandise exports to East Asian economies increased in 2000. Exports to Japan recovered by 7.6 percent in 2000, reflecting in part the 5 percent depreciation in the value of the Canadian dollar versus the yen. Canada's exports to the nine other major East Asian economies gained 20 percent in value, reaching $10.64 billion in 2000. As a result, the share of these nine East Asian economies in Canada's exports recovered somewhat (Table 7).

Table 7: East Asian Economies' Share of Canada's Merchandise Exports (percent), 1989-2000

Economies	Average 1989-1992	Average 1993-1996	1997	1998	1999	2000
Japan	5.32	4.38	3.75	2.71	2.37	2.19
South Korea	1.10	0.99	1.02	0.57	0.56	0.54
People's Republic of China	1.18	1.08	0.81	0.78	0.75	0.90
Hong Kong	0.58	0.52	0.59	0.45	0.31	0.32
Taiwan	0.64	0.56	0.54	0.37	0.32	0.28
Indonesia	0.24	0.26	0.27	0.17	0.15	0.17
Malaysia	0.17	0.17	0.23	0.15	0.12	0.10
Philippines	0.14	0.11	0.14	0.08	0.08	0.09
Singapore	0.23	0.19	0.18	0.13	0.11	0.09
Thailand	0.26	0.20	0.16	0.10	0.08	0.09
Nine East Asian economies	4.54	4.09	3.94	2.81	2.49	2.58
Total East Asia	**9.89**	**8.46**	**7.69**	**5.52**	**4.86**	**4.77**

Source: Statistics Canada, *Canadian International Merchandise Trade 2000*. Catalogue no. 65-001-XPB, December 2000.

The significant positive bounce-back in merchandise exports to key East Asian economies in 2000 is consistent with the economic recovery in East Asia as well as movements in the exchange rates.

Exports to China increased sharply by about 40 percent to a record high in 2000, while exports to Hong Kong and Taiwan posted smaller gains of 17 percent and 4 percent, respectively.

Conditions in Asian economies were generally favourable to trade in 2000, although they varied considerably. South Korea's economic growth was more robust, and the Korean exchange rate remained comparatively low vis-à-vis the dollar, despite a 5.2 percent appreciation in 2000 against the dollar. In this context, Canada's exports to South Korea recovered further in 2000, growing 12 percent, albeit to a level that is still lower than that seen in 1998.

Total merchandise exports to the Philippines, Indonesia and Thailand increased at rates of between 23 percent and 31 percent in 2000, while exports to Malaysia and Singapore edged down somewhat.

- The Philippines (30.7 percent in 2000 after +12.4 percent in 1999);
- Indonesia (29.4 percent in 2000 after –0.2 percent in 1999);
- Thailand (22.7 percent in 2000 after –0.7 percent in 1999);
- Singapore (-2.5 percent in 2000 after –11.0 percent in 1999); and
- Malaysia (-3.5 percent in 2000 after –12.7 percent in 1999).

Table 8: Intra-Asia Trade and Imports from Selected Trading Partners, 1989-1999

	1989	1999
Share of Asia's imports from major trading partners (percent)		
Intra-Asia	44.0	53.9
ROW	56.0	46.1
Percentage breakdown of Asia's imports from ROW		
Total	100.0	100.0
Canada	4.2	2.8
U.S.	32.6	33.3
Australia	6.6	6.0
France	3.9	4.2
Germany	7.7	7.7
U.K.	4.4	4.4

Source: International Monetary Fund, *The Direction of Trade Statistics.*

Canada's market penetration measured in terms of Canada's share in total Asian countries' data on merchandise imports was 2.8 percent in 1999, down from 4.2 percent in 1989 (Table 8). Similarly, Australia experienced a decline in market presence in Asia, reflecting the impact of weak commodity prices and intensified intra-Asian trade. In contrast, the market shares of the U.S. and France edged up, while those of the United Kingdom and Germany were unchanged between 1989 and 1999.

Latin America

The widespread recovery in economic activity in Latin America through 2000 from the 1998 financial and economic turmoil in the region resulted in substantial gains in Canada's exports to most major countries in this region. Canada's merchandise exports to Central and South America increased in 2000, by 8.7 percent and 12.3 percent, respectively. Exports to free trade partners Mexico, Costa Rica and Chile rose by 26.5 percent, 25.2 percent and 23.6 percent respectively. Overall, the major Latin American economies (including Mexico) absorbed 1.15 percent of Canada's merchandise exports in 2000, an improvement from 1.13 percent in 1999, but still substantially below that of 1.7 percent in 1997.

Table 9: Canada's Merchandise Exports to Key Latin American Economies, 1989-2000

	1989-1992	1993-1996	1997	1998	1999	2000
Exports ($ millions)						
Mexico	673	1,082	1,277	1,467	1,612	2,040
Argentina	67	198	409	343	211	239
Brazil	575	1,123	1,693	1,382	1,043	1,068
Chile	155	333	392	340	360	446
Colombia	204	401	473	471	255	305
Venezuela	356	656	954	705	524	635
Total	**2,029**	**3,792**	**5,198**	**4,708**	**4,006**	**4,732**
Share in Canada's total exports to the world (percent)						
Mexico	0.45	0.46	0.43	0.46	0.45	0.50
Argentina	0.04	0.08	0.14	0.11	0.06	0.06
Brazil	0.39	0.47	0.57	0.43	0.29	0.26
Chile	0.10	0.14	0.13	0.11	0.10	0.11
Colombia	0.14	0.17	0.16	0.15	0.07	0.07
Venezuela	0.24	0.28	0.32	0.22	0.15	0.15
Total	**1.36**	**1.59**	**1.74**	**1.48**	**1.13**	**1.15**

Source: Statistics Canada, *Exports by Country*, Catalogue no. 65-003-XPB.

Sources of Canada's Merchandise Imports

As in the case of exports, the growth in imports of 11.1 percent in 2000 was broadly distributed among Canada's trading partners. In general, Canada's imports from major regions outside of the United States grew much more strongly than imports from the United States. Imports from the U.S. increased by 7.3 percent, substantially less robust than the import growth of 10.6 percent for Japan and 18.1 percent for the EU. Imports also rose rapidly from Asia (12 percent), and from Latin America (11 percent). As a result, the U.S. share of Canada's total imports decreased to 73.7 percent in 2000 from 76.3 percent in 1999 (Table 10). While the share of imports from the EU fell in the 1990s, some recovery occurred in 1999 and in 2000.

Table 10: Canada's Merchandise Imports, 1950-2000

	1950-1959	1960-1969	1970-1979	1980-1989	1990-2000	1998	1999	2000
Share (percent)								
U.S.	71.6	70.8	70.1	70.4	74.5	77.0	76.3	73.7
ROW	28.4	29.2	29.9	29.6	25.5	23.0	23.7	26.3
• EU	n.a.	n.a.	9.5	10.0	8.9	8.3	8.7	9.2
• Japan	n.a.	n.a.	4.2	5.8	3.9	3.2	3.2	3.2
Annual Growth (percent)								
U.S.		10.4	16.1	7.5	9.6	10.6	6.7	7.3
ROW		8.1	15.4	7.4	7.8	5.1	11.3	23.3
• EU		n. a.	n. a.	11.5	7.8	4.2	12.5	18.1
• Japan		n. a.	n. a.	6.6	3.1	10.9	9.7	10.6

Source: Statistics Canada, CANSIM, Matrix no. 3651: *Merchandise Imports on a Balance of Payments Basis by 63 Major Groups and by 6 Principal Trading Areas Based on the Standard Commodity Classification.* n.a. = not available.

Merchandise Trade by Sector

The salient features in the composition of Canada's exports by sector in 2000 included:

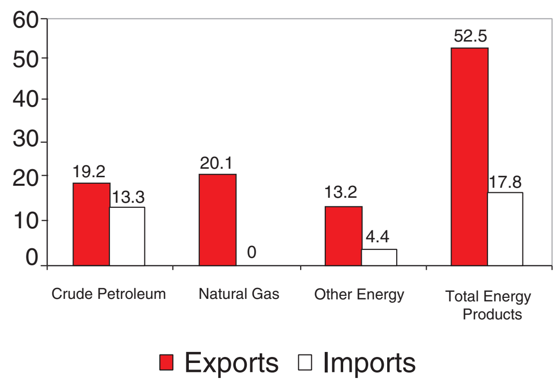
- a sharp rise in the value of energy trade, driven both by an escalation in energy prices and an increase in energy demand;
- widespread increases in exports and imports;
- stellar growth in trade in communications equipment among the various major M&E subsectors;
- a surge in exports of M&E to restore this sector's position as Canada's leading export sector, displacing the role played by exports of automotive products over most of the past quarter century; and
- a continuation in the decline of trade in resources as a percent of the volume of exports and imports.

Energy Products:

- High prices and solid demand led to a 77 percent jump in energy exports in 2000. While imports also increased sharply, Canada's surplus on energy trade rose to $34.8 billion, which accounted for 64 percent of the overall merchandise trade surplus of $54.5 billion in 2000. In response to strong demand from the United States, exports of electricity shot up by 110 percent in the year, while exports of natural gas and crude petroleum rose at robust rates of 84 percent and 74 percent, respectively. In all cases, export volume grew strongly in 2000.

❑ Energy imports also rose strongly, by 65.8 percent in 2000, led by an 86.2 percent increase in imports of crude petroleum. While Canada is a net energy exporter, most parts of Eastern Canada are net importers. Hence, the trade gain from the rebound in energy prices that was beneficial to Canada as a whole worked to the disadvantage of the non-energy-producing parts of Canada, as well as to all Canadian consumers.

Figure 1: Trade in Energy Products - 2000 Value in $ Billion



Agriculture and fishing and forestry products:

❑ In 2000, exports of agriculture (plus fishing) and forestry products rose by 7.9 percent and 5.8 percent, respectively. Imports of these two categories also increased, by 5.2 percent and 11.8 percent.

❑ The combined surplus in trade in these two sectors reached $47.3 billion in 2000, up from $44.3 billion in 1999.

Industrial goods and materials:

❑ Exports of industrial goods (including intermediate inputs such as metals, chemicals, plastics and fertilizers) rose by 12.5 percent to $64.6 billion in 2000, reflecting both volume gains and widespread price increases.

❑ Imports of these products increased at an even more rapid pace of 13.4 percent to $70.5 billion, reflecting the strength of the Canadian economy.

Machinery and equipment:

❑ In 2000, M&E exports rose by 22.8 percent, the strongest rate among all major non-energy exports, attaining a level of $105.6 billion.

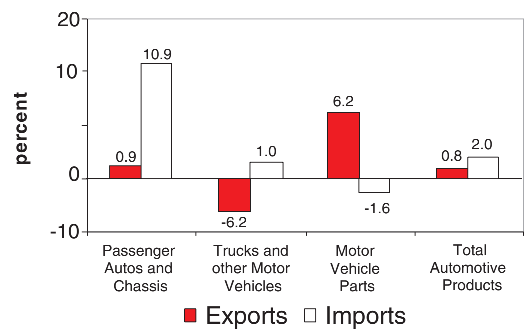
❑ Within this category, exports of "other machinery," which includes telecommunications equipment, computers and other office machines, rose by 30.6 percent, led by a 59 percent surge in exports of telecommunications equipment.

❑ M&E imports also increased sharply, by 13.5 percent, to $122.7 billion. Imports of communications equipment rose most strongly among the various M&E subcategories, by 29.4 percent.

Automotive products:

- ❑ Following a stellar performance in 1999, exports of automotive products edged up by 0.8 percent in 2000, reflecting falling demand from the United States as the year progressed. Exports of light trucks declined, offsetting a 6.2 percent gain in exports of motor vehicle parts.
- ❑ Imports of automotive products rose 2 percent, reflecting a 10.9 percent gain in imports of passenger cars. Sales of motor vehicles in Canada reached a record high of 1.59 million units in 2000, on the strength of sales of passenger cars.
- ❑ Canada's surplus on automotive trade eased to $18.9 billion in 2000, from $19.6 billion in 1999.

Figure 2: Trade in Automotive Products, Growth in 2000 over 1999, by Categories



Consumer goods other than motor vehicles[7]*:*

- ❑ Exports of consumer products grew by 8.9 percent in 2000, following a decade of exceptional growth, albeit from a relatively small base.
- ❑ Imports of consumer goods rose 8.5 percent, reflecting buoyant consumer spending in Canada.
- ❑ Canada typically runs a deficit in consumer goods trade; in 2000, the deficit widened further to $25.4 billion.

Resources:

- ❑ The notion that Canada's exports are based largely on resource and commodity production is outdated. Canada's dependence on trade in commodities and other resources has declined sharply over the last decade. Commodity exports have fallen from almost 60 percent of total merchandise export volume in 1980 to 34 percent in 2000.[8] Factors behind this decline include the greater use of raw materials for processing in Canada to enhance higher value-added exports as well as the rapid expansion of trade in high-tech and other non-resource products. In Canada's mix of exports, knowledge-based and other high-tech products have been among the fastest-growing areas. As a result, high-tech exports rose from 14 percent of overall merchandise export volume in 1992 to almost 29 percent in 2000.
- ❑ As in the case of exports, imports of resource products also play an important, albeit declining, role in Canada's foreign trade. In 2000, resource imports represented 25.1 percent of total merchandise import volume, somewhat lower than the 1990 figure of 30.8 percent.

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[7] Consumer goods include furniture and other household goods, apparel, footwear, photographic goods, medicinal and pharmaceutical products and other personal items.

[8] Resources include energy such as crude petroleum, natural gas, electricity, coal and other energy products; agricultural products such as wheat and other farm and fish products; forest products such as lumber, pulp and paper; and industrial materials such as metals, minerals, chemicals and fertilizers.

Box B: Canada's Position in Global High-tech Trade

Over the last decade, Canada's trade in high-tech products has been a key driver of growth in international trade, with Ontario and Quebec in the lead.[9] Canada has successfully positioned itself in supplying high-tech products to the U.S. market, but has remained a small player in the broader global market.

The value of Canada's merchandise exports and imports of high-tech products rose very rapidly in recent years (Figure B1). In 2000, Canada's high-tech exports increased by 30 percent and imports by 26.2 percent as measured in constant dollars, substantially outpacing growth in the remaining merchandise trade categories. Measured in current dollars, high-tech exports also posted strong gains, despite the continued decline in the prices of computers and computer-related products. The ratio of Canada's exports of high-tech products to total merchandise exports (in constant dollars) also might be used as an additional high-tech growth indicator: high-tech products represented 28.9 percent of total merchandise exports in 2000, more than double the 14 percent in 1992 (Figure B2). The corresponding import ratio was up from 22 percent to 37 percent over the same period.

Figure B1: Canada's Trade of High-tech Products

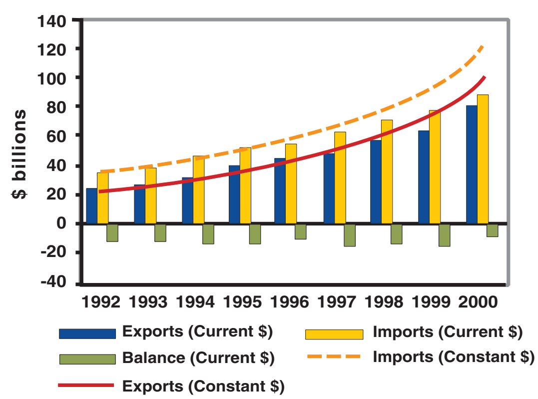
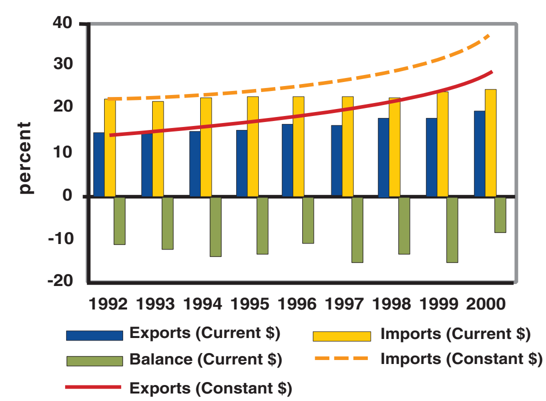


Figure B2: Ratio of High-tech Products to Canada's Goods Trade



Between 1992 and 2000, Canada's exports of high-tech products surged at a faster pace than like-product imports. Imports of high-tech products reached new heights over the year due to persistent high demand for investment in new technologies to enhance productivity, and the export capability of various sectors of the Canadian economy. As the value of imports is typically higher than that of exports, the surge in imports has widened Canada's deficit in high-tech trade, which reached $8.3 billion in current dollars in 2000. Among high-tech products, the category of office machines and equipment, which includes computers, has largely contributed to this development, in both current and constant dollars. Since 1994, office machines and equipment have also become the largest component of high-tech exports, as their share (in constant dollars) doubled from 20 percent in 1992 to 41 percent in 2000, while their counterpart import share rose from 23.2 percent to a peak of 51.5 percent during the same period (Figures B3 and B4).

[9] High-tech products include aircraft, engines and parts; office machines and equipment; television, telecommunications and related equipment; and other miscellaneous products based on Statistics Canada's publication entitled *Canadian International Merchandise Trade*. Balance of Payments data, available in both current and constant dollars, are used in this special report.

Figure B3: Composition of Canada's High-tech Exports

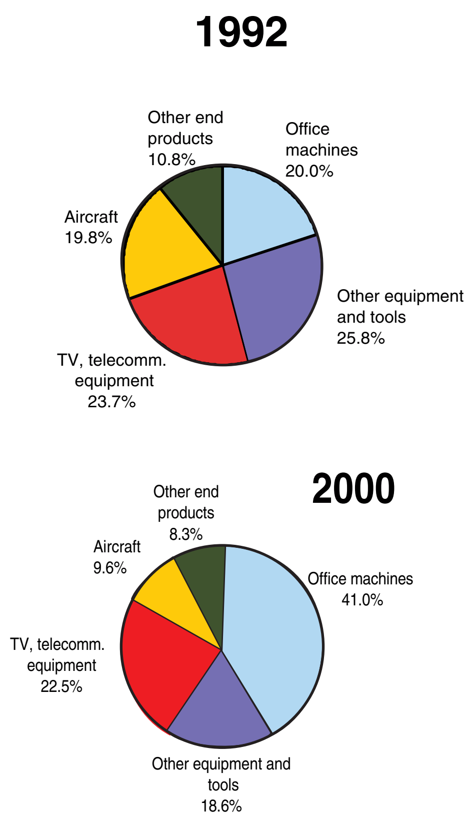
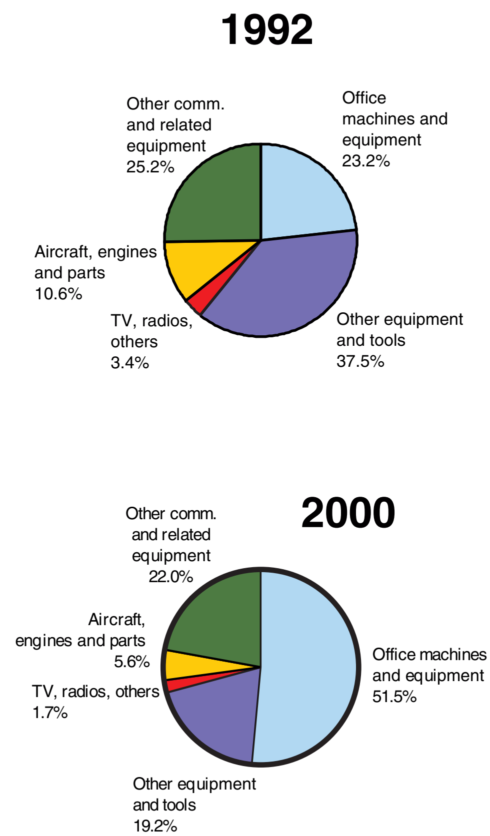


Figure B4: Composition of Canada's High-tech Imports



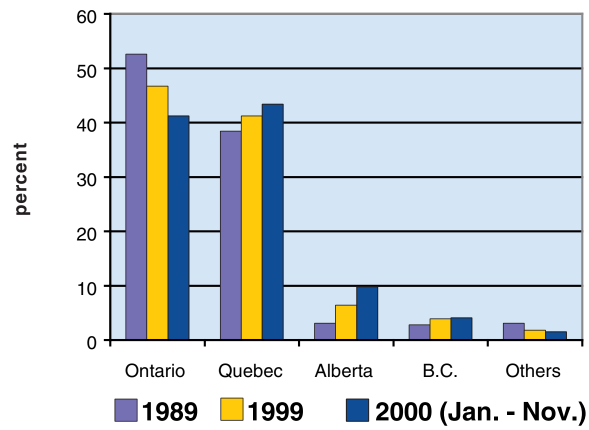
Within Canada, high-tech trade expansion is shared among the provinces, with Ontario as the largest exporter of high-tech products through 1999.[10] Ontario's major high-tech exports are office and business machines, and pharmaceutical and medicinal products. Quebec, which used to track Ontario's performance, appears to have become Canada's largest provincial exporter of high-tech products in 2000.[11] In 2000, Quebec accounted for 43.4 percent of Canada's total exports of high-tech products, just more than 41.2 percent for Ontario (Figure B5). Next to Ontario, Alberta ranked third, as its share of Canada's total high-tech exports tripled from 3.1 percent in 1989 to 9.8 percent for January to November 2000, while British Columbia's export share also gained during the same period. Apparently, Quebec also has the biggest high-tech component, representing about 30 percent of its current dollar export bundle, with aircraft, aircraft engines and parts, communications and related equipment as key items (Figure B6). On the import

[10] High-tech trade data by Canadian provinces were sourced from Statistics Canada's International Trade Division. The data measured on customs basis includes medicinal and pharmaceutical products; office machines and equipment; aircraft and associated parts; communications and related equipment; electrical lighting and distribution; navigation equipment; other measuring/controlling laboratory medical and optical equipment; and medical, ophthalmic and orthopaedic supplies. These data are available only in current dollars.

[11] For practical purposes, data for 2000 are based on monthly information up to November.

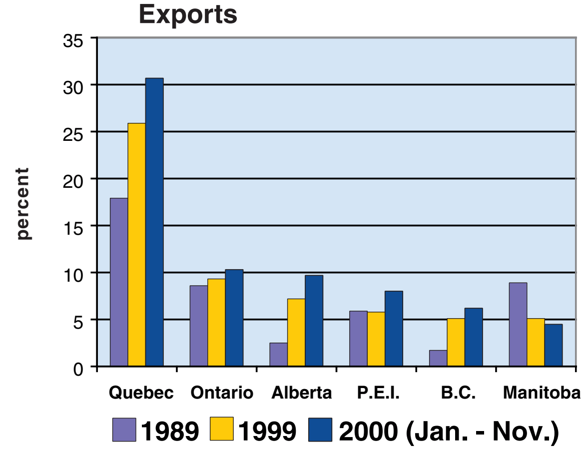
side, Ontario accounted for the largest share, at 58 percent of Canada's total high-tech purchases in 1999, while Quebec, British Columbia and Alberta ranked second, third and fourth, with shares of 28 percent, 7 percent and 5 percent respectively.

Figure B5: Canada's Composition of High-tech Exports by Selected Provinces



Canada's strength in high-tech exports is also reflected in its ability to penetrate and succeed in selected products in the U.S., the world's largest high-tech market. Canada's export sales of high-tech products[12] to the U.S. were brisk, growing at a compound annual growth rate of 15 percent between 1989 and 1999. Canada also has the ability to market high-tech products to some individual countries outside the U.S. For example, Canada's exports of high-tech products to the EU grew at 7.7 percent, to Japan at 8.1 percent, and to Mexico at 5 percent between 1989 and 1999, all at a compound annual growth rate.

Figure B6: High-tech Share of Provincial Goods Exports



On a product-specific basis, Canada supplied 25 percent and 10 percent, respectively, of U.S. imports of aircraft and telecommunications apparatus in 1999 (Table B1). In the case of office machines and data processing equipment, however, Canada had lost significant market share in the U.S., from 15 percent in 1980 to 4 percent in 1999. As a consequence, Canada's overall share in the U.S. high-tech market fell slightly from 9.3 percent in 1980 to 7.3 percent in 1999, although it remained substantially higher than countries such as Germany, France and the U.K. Japan's market penetration in the U.S. high-tech market is traditionally greater than Canada's. Since 1987, Mexico has overtaken Canada in the U.S. market for high-tech products.

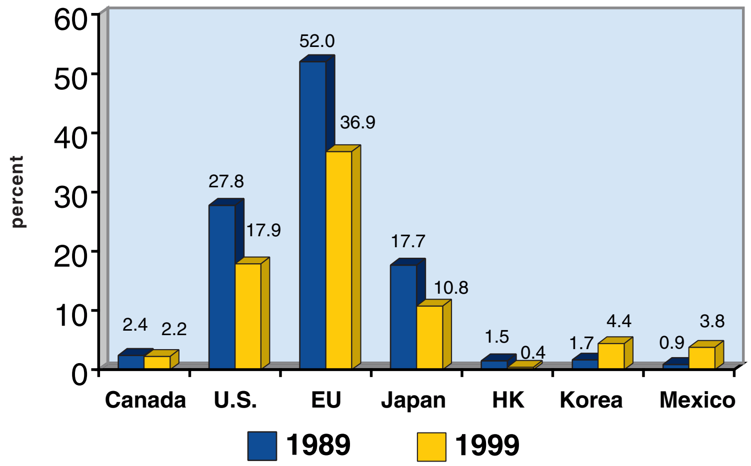
[12] Canada's high-tech trade data vis-à-vis other countries sourced from the UN Commtrade database includes medicinal and pharmaceutical products; office machines and automatic data processing equipment; electrical appliances; telecommunications and sound-recording apparatus; electric power machinery and parts; equipment for distributing electricity; electric apparatus for medical purposes; thermionic cold and photo-cathode valves/tubes/parts; and aircraft and associated parts. These sets of data are available only in current dollars.

In the context of the phenomenal rise in the demand for high-tech products worldwide, Canada's presence in the global market remained modest as global trade in high-tech products rose even more strongly than Canada's trade in these areas. On the basis of global market share and the ratio of high-tech exports to total exports, Canada is still positioned as a relatively small global player. Data in current dollars sourced from the UN Commtrade database for 1999 showed that Canada supplied 2.2 percent of the global demand for high-tech products in 1999, compared with 36.9 percent for the EU, 17.9 percent for the United States, 10.9 percent for Japan, 4.4 percent for South Korea and 3.8 percent for Mexico (Figure B7). With respect to high-tech exports as a percent of total exports during 1980 and 1999, Canada's performance was consistently behind the U.S., EU Japan, Hong Kong, Korea and Mexico.

Table B1: Distribution of U.S. High-tech by Country (percent)

	CANADA	MEXICO	JAPAN	U.K.	FRANCE	GERMANY
Aircraft and associated equipment and parts						
1980	**26.2**	0.0	7.5	15.4	20.5	0.0
1999	**25.3**	0.5	9.1	9.1	24.2	11.4
Compound annual growth (percent)	**-0.2**	13.3	1.1	-2.7	0.9	—-
Telecommunications and sound-recording apparatus						
1980	4.7	10.9	46.4	0.1	0.3	0.0
1999	**10.0**	23.3	19.4	1.3	0.6	0.8
Compound annual growth (percent)	**4.0**	4.1	-4.5	12.0	3.7	—-
Medicinal and pharmaceutical products						
1980	**3.3**	1.6	12.2	14.6	4.4	1.5
1999	**5.2**	0.6	9.6	15.7	5.0	23.9
Compound annual growth (percent)	**2.4**	-5.5	-1.2	0.4	0.7	—-
Office machines and automatic data-processing equipment						
1980	**15.1**	3.1	40.2	0.0	3.9	0.0
1999	**3.8**	8.4	18.6	2.3	0.4	1.1
Compound annual growth (percent)	**-7.0**	5.4	-4.0	—-	-10.9	—-
Electric apparatus for medical purposes						
1980	**6.7**	1.1	14.9	0.0	5.9	0.0
1999	**3.6**	5.1	28.1	4.5	5.8	28.7
Compound annual growth (percent)	**-3.3**	8.2	3.4	—-	-0.1	—-
Thermionic, cold and photo-cathode valves, tubes, parts						
1980	**3.8**	3.9	14.4	0.0	1.6	0.0
1999	**5.1**	3.5	18.2	1.3	1.6	1.8
Compound annual growth (percent)	**1.5**	0.6	1.2	—-	-0.2	—-
Equipment for distributing electricity						
1980	**17.1**	33.7	10.3	1.4	1.6	0.3
1999	**7.4**	62.9	3.3	0.8	0.8	1.7
Compound annual growth (percent)	**-4.4**	3.3	-5.8	-3.2	-3.4	9.1
Electrical appliances (switches, relays, etc.)						
1980	**10.9**	16.1	24.9	0.0	4.4	0.0
1999	**8.5**	23.8	18.4	3.1	2.3	7.1
Compound annual growth (percent)	**-1.3**	2.1	-1.6	—-	-3.3	—-
Electric power machinery and parts thereof						
1980	**17.7**	22.3	15.3	2.4	2.1	0.0
1999	**7.2**	25.0	7.4	1.9	1.1	3.6
Compound annual growth (percent)	**-4.7**	0.6	-3.7	-3.4	-3.4	—-
All high-tech						
1980	**9.7**	**7.6**	**29.8**	**2.6**	**4.2**	**0.1**
1999	**7.3**	**13.1**	**16.8**	**3.1**	**2.7**	**3.8**
Compound annual growth (percent)	**-1.5**	**2.9**	**-3.0**	**1.0**	**-2.3**	**23.35**

Figure B7: Distribution of Global Exports of High-tech products



Structural developments in import growth

In volume terms, merchandise import growth accelerated to 12.9 percent in 2000, consistent with the acceleration in Canada's output growth to 4.7 percent in 2000 (Table 11). The growth in the value of Canada's imports of goods in 2000 was somewhat smaller, at 11.1 percent, reflecting the impact of steady declines in the price of computers and other M&E.

Table 11: Canada's Merchandise Imports by Sector - Growth (percent) in 2000

Products	Value of imports ($ billions)	Growth in current dollars	Real growth in 1992 constant dollars
Agriculture and fishing	18.6	5.2	5.9
Energy	17.8	65.8	14.1
Forestry	3.1	11.8	2.7
Industrial goods and materials	70.5	13.4	10.1
Machinery and equipment	122.7	13.5	22.7
Automotive products	77.4	2.0	1.8
Other consumer goods	40.1	8.5	7.6
Total	**363.2**	**11.1**	**12.9**

Source: Statistics Canada, *Canadian International Merchandise Trade 2000*. Catalogue no. 65-001-XPB, December 2000.

The rapid growth of M&E import volume was particularly important for Canada in 2000, as it enabled businesses to expand and upgrade their production capacity at a time when the economy was operating at very high rates of capacity use. It also helped businesses to re-engineer the structure of their production facilities.

Table 12: Value, Share and Growth of Canada's Goods Trade (Balance of Payments Basis)

Industry	Level ($ billions)			Share of Total in percent			Cumulative percent Growth	Growth percent
	1989	1999	2000	1989	1999	2000	1989-2000	1999-2000
Exports								
Total	147.0.	360.6	417.7	100.0	100.0	100.0	184.1	15.8
Agricultural and fishing	11.6	25.6	27.6	7.9	7.1	6.6	137.9	7.8
Energy	13.7	29.7	52.5	9.3	8.2	12.6	283.2	76.8
Forestry	21.5	39.1	41.4	14.6	10.8	9.9	92.6	5.9
Industrial	32.3	57.4	64.6	22.0	15.9	15.5	100.0	12.5
M&E	24.0	86.0	105.6	16.3	23.8	25.3	340.0	22.8
Automotive	34.0	95.5	96.3	23.1	26.5	23.1	183.2	0.8
Consumer goods	2.6	13.5	14.7	1.8	3.7	3.5	465.4	8.9
Imports								
Total	139.2	326.8	363.2	100.0	100.0	100.0	160.9	11.1
Agricultural and fishing	8.3	17.6	18.6	6.0	5.4	5.1	124.1	5.7
Energy	6.2	10.7	17.8	4.5	3.3	4.9	187.1	66.4
Forestry	1.4	2.7	3.1	1.0	0.8	0.9	121.4	14.8
Industrial	26.9	62.1	70.5	19.3	19.0	19.4	162.1	13.5
M&E	43.3	108.2	122.7	31.1	33.1	33.8	183.4	13.4
Automotive	31.9	75.9	77.4	22.9	23.2	21.3	142.6	2.0
Consumer goods	15.0	37.0	40.1	10.8	11.3	11.0	167.3	8.4
Balance								
Total	7.7	33.8	54.5					
Agricultural and fishing	3.3	8.0	9.0					
Energy	7.5	19.0	34.7					
Forestry	20.1	36.4	38.3					
Industrial	5.3	-4.7	-5.9					
M&E	-19.3	-22.2	-17.1					
Automotive	2.0	19.6	18.9					
Consumer goods	-12.4	-23.5	-25.4					

Source: Statistics Canada, *Canadian International Merchandise Trade 2000*. Catalogue no. 65-001-XPB, December 2000. Note: Sums may not add up to 100 because special transactions, inland freight and other balance of payments adjustments figures, which are part of the merchandise trade account, are not included.

Merchandise Trade Balance

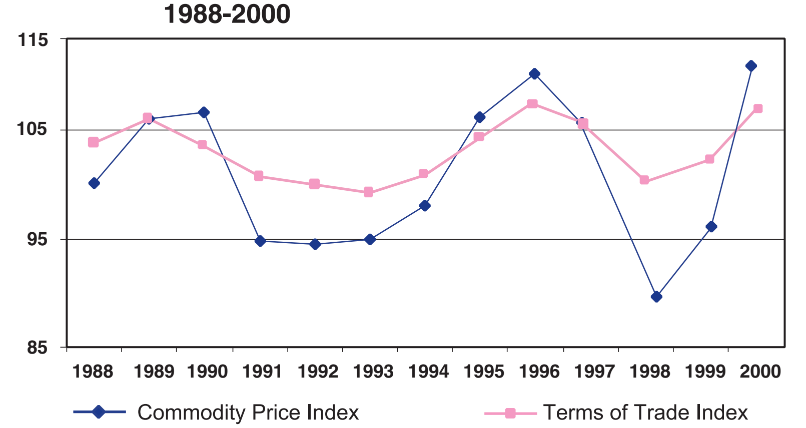
In 2000, the merchandise trade surplus increased to a record high of $54.5 billion from $33.8 billion in 1999 (Table 12). The overall surplus in trade in agriculture and fishing, energy, forestry, and automotive products rose sharply, while the deficit in trade in industrial products, M&E and consumer goods fell by $2 billion. The energy sector accounted for 76 percent of the $20.7 billion increase in the overall merchandise trade surplus in 2000.

In terms of trading partners, the merchandise trade surplus with the U.S. grew to a record $92.1 billion in 2000, up from $60.1 billion the previous year. Elsewhere, the deficit in merchandise trade widened, to $12.6 billion with the EU in 2000 (from $10.2 billion in 1999); to $1.8 billion with Japan (from $1.4 billion in 1999); and to $23.2 billion with countries other than the U.S., the EU and Japan (from $14.7 billion).

Developments with respect to the Terms of Trade[13]

Canada is a net exporter in commodity trade: in 2000, exports of food, energy, forestry products and industrial materials totalled $186.1 billion, while imports amounted to $109.8 billion, generating a surplus of $76.3 billion. The further rise in commodity prices in 2000[14] contributed to an 8.9 percent increase in Canada's merchandise export prices. At the same time, merchandise import prices rose by 2.5 percent. This resulted in the terms of trade increasing by 6.4 percent, accounting for much of the improvement in the trade surplus in 2000. Although Canada's dependence on commodity trade has been declining steadily, commodity prices continued to significantly affect Canada's terms of trade. The direction of movement in the terms of trade closely followed the movement of commodity prices (Figure 3). In general, fluctuations in the terms of trade are smaller than those in commodity prices, since the prices of non-commodity products such as automotive products, M&E and consumer goods do not fluctuate sharply over time.

Figure 3: Canada's Commodity Price Index and Merchandise Laspeyres Terms of Trade, 1988-2000



Source: Bank of Canada, *Banking and Financial Statistics*

[13] Movements in the price of exports relative to the price of imports are referred to as changes in a country's terms of trade. An improvement in the terms of trade (i.e. a rise in export prices relative to import prices) means that a country's purchasing power has increased. In other words, the earnings from a given quantity of exports purchase a greater quantity of imports. Conversely, a decline in the terms of trade requires a country to export more to pay for a given quantity of imports. The terms of trade are commonly measured as the index of average export prices, divided by the index of average import prices. This measure of the terms of trade is influenced by many factors, including commodity price changes, exchange rate movements, domestic and international supply and demand conditions, changes in the mix of products exported and imported, and domestic cost and productivity trends; accordingly, care must be exercised in interpreting changes in this indicator. In this analysis, the Laspeyres counterpart series are used, as they are more indicative of pure price movements because they exclude the price effect associated with changes in the product mix of exports and imports.

[14] The Bank of Canada's US$ energy price index (1982-1990=100) almost doubled from a low of 64.6 in 1998 to average 120.8 in 2000. The corresponding price index for industrial materials (which includes metals, minerals, forest products and other non-energy raw materials) rose from 108.0 in 1998 to 115.0 in 2000.

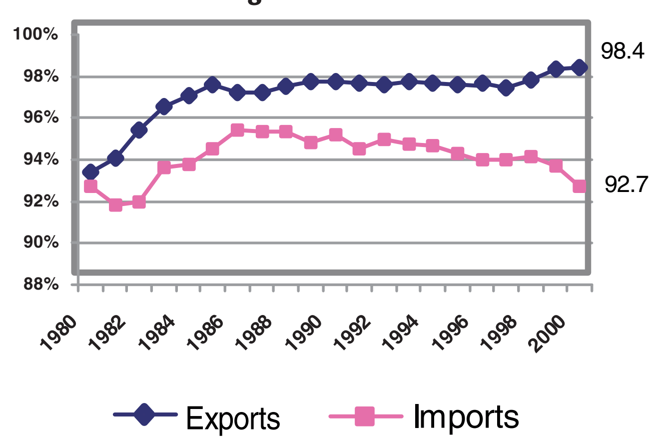
Box C: Trade and Investment with FTAA Member Countries

Introduction

Canada is currently negotiating with 33 other democratic countries in the hemisphere toward a Free Trade Area of the Americas (FTAA), which is to be concluded by 2005. The process was initiated by a Summit in December 1994 in Miami, hosted by U.S. President Clinton. A second Summit officially launched the negotiations in Santiago, Chile, in April 1998. Canada chaired the initial 18-month start-up phase of the trade negotiations from spring 1998 until November 1999, concluding with hosting of the Fifth FTAA Trade Ministers Meeting in Toronto on November 3-4, 1999. Canada hosted the Summit of the Americas in Quebec City in April, at which the FTAA was a key component.

The successful completion of the FTAA negotiations would create the world's largest free trade area, with 794 million people (1999 data) and a combined gross domestic product (GDP) of more than US$11 trillion (1999 estimate). The FTAA would build on Canada's free trade ties with the United States and Mexico, and separately with Chile and its expanding links elsewhere in the hemisphere, allowing Canada to take full advantage of emerging hemispheric markets. Even excluding Canada's NAFTA partners, the region was a $3.8 billion export market for Canadian goods in 2000 (about 7.5 percent of Canada's total merchandise exports to countries outside of U.S. and Mexico).

Figure C1: U.S. Share of Canada's Trade with the FTAA Region



Trade with FTAA Countries 1980-2000

As the United States is Canada's most important trade partner, much of Canada's trade with the FTAA "region" is with the United States. In 2000, the U.S. share in Canada's total FTAA trade was 98.4 percent in exports and 92.7 percent in imports, leaving only 1.6 percent and 7.3 percent for trade with the other 32 countries (henceforth referred to as $FTAA_{32}$). The following section discusses Canada's export and import performance with $FTAA_{32}$ countries in greater detail. It is important to stress at the outset that Canada's export and import trade with most of the $FTAA_{32}$ countries has not yet reached a significant order of magnitude, with the exception of Mexico, Brazil and Chile. In 2000, for instance, Canada's exports to each of nine of the prospective FTAA partners amounted to less than 1 percent of sales to the $FTAA_{32}$ countries. In the case of imports, the corresponding number of countries was somewhat larger, at 14. For this reason, it is sufficient to discuss in greater detail Canada's trade performance with respect to a limited number of countries.

Trade Balance

Historically, Canada has recorded a growing deficit in trade with the $FTAA_{32}$ countries. The deficit shot up from just below $300 million in 1980 to $12.2 billion by 2000. The gap between exports and imports grew rapidly in the 1990s, especially since 1997. Imports increased dramatically while exports declined noticeably in the wake of the financial crisis that adversely affected economic growth in these countries.

Much of the growth in the deficit originated in trade with Mexico, reflecting the growth in imports from Mexico since the Free Trade Agreement (FTA) came into effect in 1989. Mexico made up for 82.6 percent of the deficit in the FTAA$_{32}$ trade balance in 2000, totalling $10 billion.

Excluding U.S. and Mexico, Canada's trade balance with FTAA$_{32}$ countries has fluctuated greatly for much of the past two decades. Canada experienced a trade deficit ranging from $0.2 billion in 1986 to $2.1 billion in 2000. In contrast, Canada had a small surplus for much of the mid-1990s, reaching a high of $0.4 billion in 1997 with most of the FTAA nations other than the U.S. and Mexico. Although two-way-trade grew from $6.3 billion in 1980 to $9.7 billion in 2000 at a compounded annual rate of 2.2 percent, much of the increase came from imports.

Figure C2: Canada's Exports, Imports and Trade Balance with FTAA Countries (excluding the U.S.)

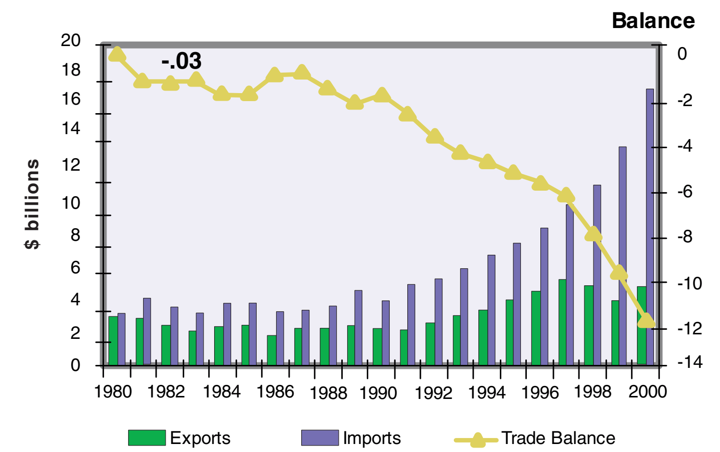
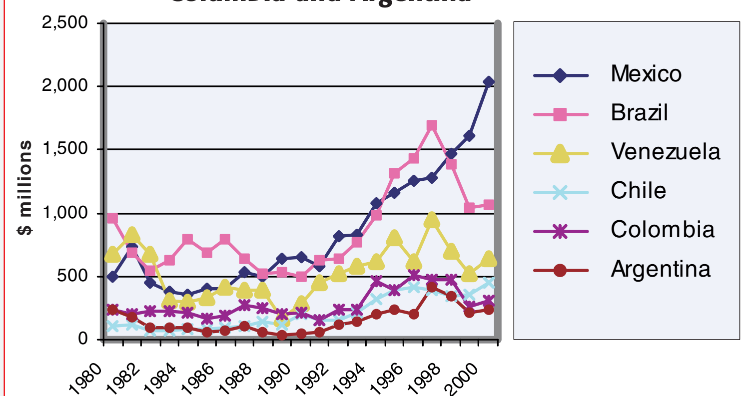


Figure C3: Export to Mexico, Brazil, Venezuela, Chile, Columbia and Argentina



Merchandise Exports

By country of destination, most of Canada's exports to the FTAA$_{32}$ countries are shipped to Mexico, Brazil, Venezuela, Chile, Colombia and Argentina. In 2000, these six countries represented 81 percent of Canada's total exports to the FTAA$_{32}$ region, up from around 75 percent in the 1980s.

- The top commodities that make up majority of exports to the FTAA$_{32}$ countries are vegetables; machinery/mechanical appliances; vehicles/aircraft; wood pulp; and chemicals.

Merchandise Imports

In the case of imports, Mexico, Brazil, Venezuela, Chile, Colombia and Argentina are also Canada's more important trading partners. In 2000, imports from these countries represented 90.2 percent of Canada's overall imports from FTAA$_{32}$, up from about 86 percent in the early 1980s. Almost all of the gains in market share can be attributed to Mexico.

- The top imports from FTAA$_{32}$ countries are machinery/mechanical appliances; vehicles/aircraft; minerals; vegetables; and foodstuffs.

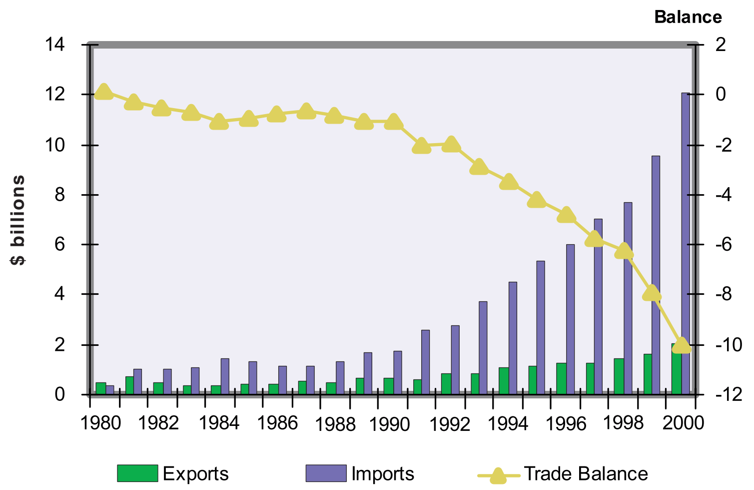
Two-way Trade - By Country

Mexico

Canada's exports to Mexico have increased considerably since the 1989 implementation of the FTA — even before the North American Free Trade Agreement (NAFTA) came into effect in 1994. Over the 11-year period between 1989 and 2000, exports to Mexico grew at a compound annual rate of 11.1 percent. However, growth in exports over this period was erratic, marked by an 11 percent decline in 1991 and increases of 40 percent in 1992 and 31 percent in 1994. Since the NAFTA came into effect, exports to Mexico increased strongly at a compound annual rate of 13.8 percent, despite the depreciation in Mexico's new peso from a high of $0.4315 in February 1994 to a low of $0.1490 in September 1998. In 1993, exports to Mexico made up for 23.8 percent ($0.83 billion) of the total FTAA_{32} share in exports and by 2000, they shot up to 34.9 percent ($2 billion).

❑ The top exports to Mexico are vehicles/aircraft/vessels; vegetables; machinery/mechanical appliances; live animals; and wood pulp.

Figure C4: Canada's Trade with Mexico



During the period 1993-2000, imports from Mexico increased steadily at a compound annual rate of 18.3 percent, substantially higher than the growth in exports. This reflects, in part, an increase in the import price of crude petroleum. This served to increase Mexico's share in Canada's imports from the FTAA_{32} countries, from 59 percent in 1993 to 67 percent by 2000. Imports went up from $3.7 billion in 1993 to $12.1 billion by 2000, an increase of more than 200 percent. Canada has become Mexico's second-largest export destination. As a result of this dramatic increase in Canada's imports from Mexico, the deficit in trade with Mexico increased from $2.9 billion in 1993 to $10 billion in 2000.

❑ The top commodities imported from Mexico are machinery/mechanical appliances; vehicles/aircraft/vessels and associated transport equipment; miscellaneous manufactured articles; base metals; and mineral products including crude petroleum.

Brazil

Brazil is the most important destination for Canadian exports in Latin America and the Caribbean (excluding Mexico). In the period 1989-2000, Brazil made up 22.7 percent of Canada's exports to FTAA_{32} countries. However, due to the financial crisis and the accompanying economic slowdown in that country, exports to Brazil were down 25 percent in 1999, from $1.4 billion in 1998 to $1 billion in 1999 recovering slightly to $1.1 billion in 2000.

❑ The top categories of exports to Brazil are vehicles; aircraft, vessels and associated transport equipment; mineral products; chemicals; machinery and mechanical appliances; electronic equipment; sound and television recorders/reproducers; wood pulp; and paper products.

Canada's imports from Brazil have trended up over the last 20 years, except in 1990-1991 when Canada was in a recession. On average, Brazil made up 13.1 percent of Canada's imports from the FTAA_{32} countries over the period of 1989-2000. Imports from Brazil increased at a compound annual rate of 2.6 percent over the same period. The trade balance with Brazil worsened from a $373 million surplus in 1997 to a deficit of $432 million in 2000.

❑ The major commodities imported from Brazil are foodstuffs; beverages; spirits and vinegar; tobacco; machinery/mechanical appliances; electronic equipment and parts; vegetables; metals; and minerals.

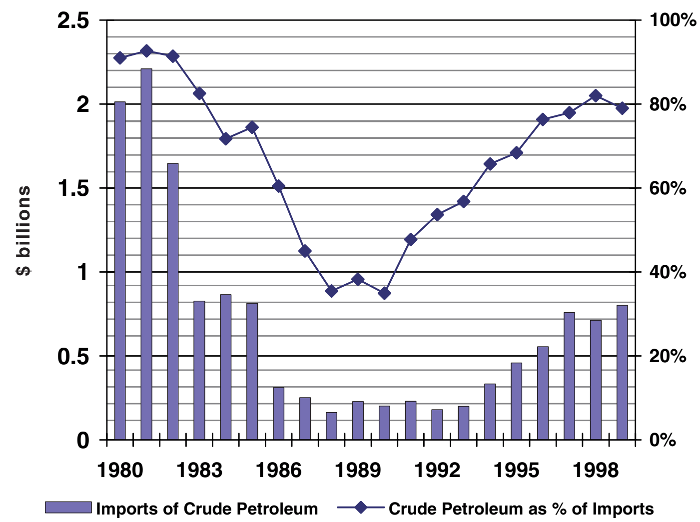
Venezuela

Canada's exports to Venezuela trended down over the last 20 years from more than 20 percent of $FTAA_{32}$ exports in the early 1980s to 10 percent in 2000. The absolute value of Canada's exports to that country also declined over this period, reflecting economic uncertainty in Venezuela and the associated weakness in demand.

- Major Canadian exports to Venezuela are vegetables; vehicles/aircraft/vessels; wood pulp; paper products; machinery/mechanical appliances; electronic equipment and parts; and metals.

From a high level in the early 1980s, Canada's imports from Venezuela declined substantially over time until the end of 2000. As a share of $FTAA_{32}$ trade, imports from Venezuela dropped precipitously from about 59.8 percent in 1980 to 7.8 percent in 1999 and 2000. This decrease in imports can be attributed primarily to the decrease in imports of crude petroleum. In the past two decades, crude petroleum averaged 66 percent of Venezuela's exports to Canada, with a high of 93 percent in 1981. Canada's imports of crude petroleum from Venezuela declined from a high of $2.2 billion in 1981 to $1.1 billion in 2000. As a result, the trade deficit narrowed from $1.6 billion in 1981 to $776 million in 2000.

Figure C5: Canada's Imports of Crude Petroleum from Venezuela



- The top imports from Venezuela are crude petroleum and mineral products; base metals; pearls; precious stones and imitation jewellery; coins; vehicles/aircraft/vessels; machinery/mechanical appliances; and electronic equipment and parts.

Chile

Canada's exports to Chile have been on an upward trend for the last two decades. Chile's share of Canada's exports to $FTAA_{32}$ grew from 3.3 percent in 1980 to 7.6 percent in 2000. Much of the increase in exports can be attributed to the 1997 Canada-Chile Free Trade Agreement (CCFTA), which provided immediate elimination of the 11 percent Chilean duty for the vast majority of Canada's industrial and resource-based exports.

- The top exports to Chile from Canada are machinery/mechanical appliances; electronic equipment and parts; vegetables; minerals; chemicals; wood pulp; and paper products.

Following increased market access provided by CCFTA, Canada's imports from Chile increased from $96 million in 1980 to $555 million by 2000. However, imports from Chile remained low in dollar terms in 2000, at around 3 percent of Canada's total imports from the $FTAA_{32}$ region.

- The major imports to Chile include vegetable products; mineral products; foodstuffs; beverages; spirits and vinegar; tobacco; base metals; and live animals and animal products.

Colombia

Colombia's economic slowdown, which started in the second half of 1998, caused a dramatic decrease in Canada's exports to that country. The share of exports to Colombia hovered at around 6 percent to 10 percent of Canada's $FTAA_{32}$ exports for much of the 1990s until the economic crisis began. Colombia's export share then fell from 9.5 percent in 1996 to 5.2 percent in 2000. The absolute value of exports also went down during the same period, from $513 million to $305 million.

- The top exports to Colombia are vegetable products; wood pulp; paper and paper products; machinery/mechanical appliances; electronic equipment and parts; plastics; rubber; and chemicals.

Canada's imports from Colombia have trended upward over time, except during Canada's 1981-1982 and 1990-1991 recessions. The value of imports ranged from a low of $83 million in 1981 to a peak of $372 million in 1995 over the two decades. Imports have been lower than exports over the last 20 years, with the exception of 1999 and 2000.

- Major imports from Colombia to Canada are vegetable products; minerals; textiles; chemicals; foodstuffs; beverages; spirits and vinegar; and tobacco.

Argentina

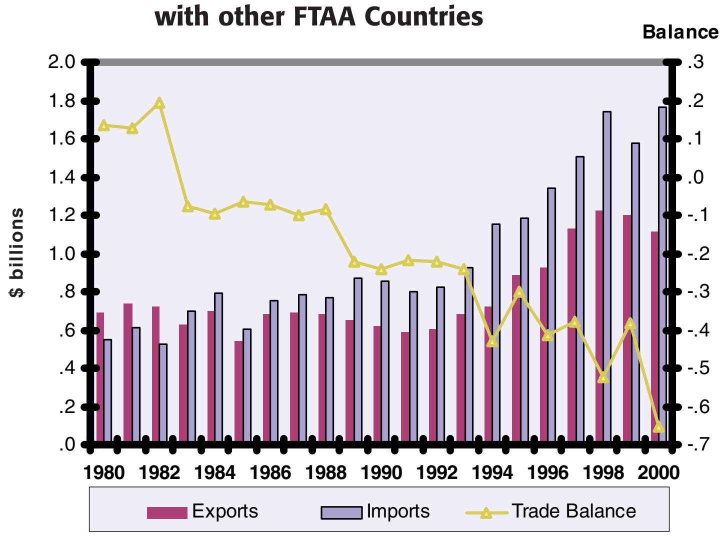
Canada's exports to Argentina declined in the early 1980s, stabilized for the rest of the decade, then increased sharply in the early 1990s, reaching an all-time-high of $409 million in 1997. This momentum came to a halt in 1998-1999 when the Argentine economy lapsed into a recession, resulting in a decline in exports to $211 million in 1999. In 2000, exports to Argentina recovered to $239 million.

- The top exports to Argentina are machinery/mechanical appliances; electronic equipment and parts; wood pulp; paper; plastic; rubber; chemicals; and transportation equipment.

Imports from Argentina increased eightfold over the last two decades, from $40.8 million to more than $357 million in 2000. As a result, Argentina's share in Canada's imports from $FTAA_{32}$ doubled to 2 percent between 1980 and 2000.

- The leading imports to Argentina are vegetables; minerals; live animals and animal products; foodstuffs; beverages; spirits and vinegar; tobacco; raw hides; leather and leather products; and travel goods.

Figure C6: Exports, Imports and Trade Balance with other FTAA Countries



Highlights of Other FTAA Countries

The remaining FTAA countries (i.e. $FTAA_{26}$, excluding Mexico, Brazil, Venezuela, Chile, Colombia and Argentina) made up 17.2 percent of Canada's exports to $FTAA_{32}$ over the past two decades. In the case of imports, the corresponding figure is 13.3 percent. Although the share is lower in imports than in exports, the value of imports is higher, implying trade deficits with most of the $FTAA_{26}$ countries.

Among these $FTAA_{26}$ countries, those standing out in volume of trade are Peru, Jamaica, Guatemala, Costa Rica, Ecuador, Trinidad-Tobago, Dominican Republic, and Guyana. Canada's imports from $FTAA_{26}$ trended upward through most of 1980-2000. In 2000, most imports came from Jamaica, Guyana, Costa Rica, Peru, Ecuador, Guatemala and Dominican Republic.

TRADE IN SERVICES WITH FTAA COUNTRIES

In 1998, the latest year for which official information is available, Canada's services trade with $FTAA_{11}$ countries represented 3.5 percent of total services exports to the world, and 4.4 percent of total services imports.[15] Two-way trade in services with $FTAA_{11}$ countries grew from $2 billion in 1991 to $4.2 billion in 1998, an increase of 108 percent during that period.

Exports

- In 1998, commercial services exports grew by 10.3 percent to reach $1.1 billion or 4.5 percent of Canada's total commercial services exports.
- Travel exports grew 15.7 percent to reach $398 million, representing 2.9 percent of total travel exports. The comparatively rapid growth of travel services reflected the increase of inbound tourism to Canada.
- Transportation and government services to $FTAA_{11}$ expanded by 13.6 percent to reach $200 million or 2 percent of total transportation and government services exports.

With respect to services imports:

- In 1998, commercial services imports grew by 12.6 percent to reach $1.3 billion or 4.7 percent of total commercial services imports.
- Travel imports grew by 7.2 percent to reach $922 million, which represented 5.8 percent of total travel imports.
- Transportation and government services imports expanded by 6.8 percent to reach $250 million or 2 percent of total transportation and government services imports.

In the 1990s, Canada was a net importer of services from $FTAA_{11}$ countries. The deficit during the 1990s was mostly in travel, followed by commercial services and government services/transportation. The overall deficit on services rose sharply in 1997 and 1998. In 1998, the deficit in overall services trade increased to $737 million from $563 million in 1991.

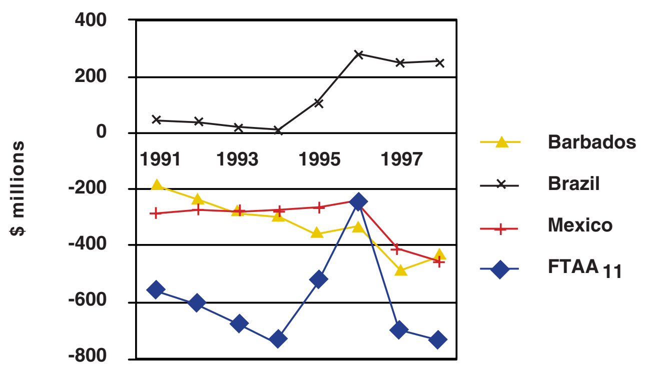
Mexico and Barbados are the major contributors to the deficit in Canada's services trade with $FTAA_{11}$ countries. In 1998, the services trade deficit was $458 million with Mexico and $426 million with Barbados. The comparatively high deficit in services with Mexico is reflected mainly in the travel sector, where outbound tourism from Canada to Mexico increased by 13.4 percent in 1998, to reach $558 million. In the case of Barbados, most of the deficit is accounted for by imports of commercial services, which in 1998 increased by 16.9 percent to $1 billion. In

[15] Services data for FTAA countries are published with a lag, as data for 1999 will be available in June 2001. Data on services are available from Statistics Canada for 11 of $FTAA_{32}$ countries, namely, Argentina, Bahamas, Barbados, Brazil, Chile, Jamaica, Mexico, Trinidad and Tobago, Venezuela, Colombia and Costa Rica. This group of countries is referred to as $FTAA_{11}$.

contrast, Canada had a persistent surplus in services trade with Brazil. Commercial services and travel exports to Brazil contributed to the surplus of $251 million in 1998.

Services trade with FTAA_{11} countries varied dramatically by country. Although most of the transactions in services trade came from commercial services trade, the share of travel is comparatively higher than that of countries outside of the FTAA. This feature reflects the importance of tourism, as the majority of Canadian travellers choose Latin American countries as their winter travel destinations.

Figure C7: Balance in Total Services Trade with FTAA_{11}, Barbados, Brazil and Mexico

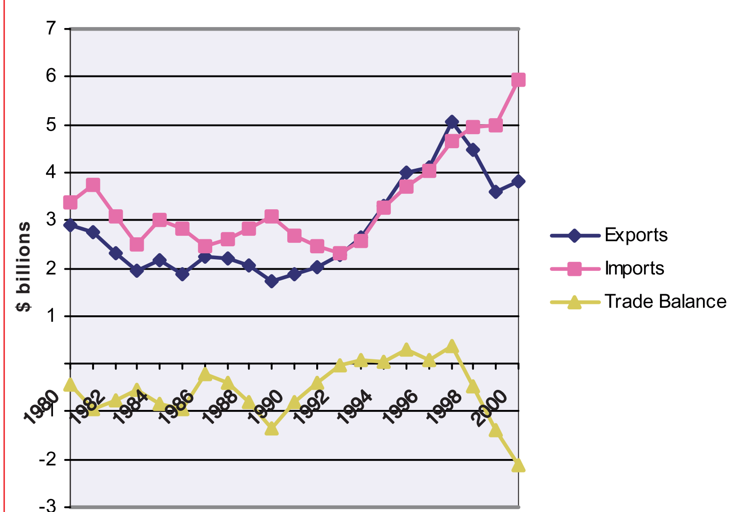


Direct Investment[16]

The stock of FTAA_{32} FDI into Canada is typically small. In 2000, it recovered by 11.4 percent to $1.106 billion, representing 0.4 percent of Canada's total FDI in the same year. Barbados, Brazil, Bahamas and Mexico were the largest source of FDI for Canada among the FTAA_{32} countries, together contributing 97.7 percent to the total FTAA_{32} flows in 2000.

The stock of Canada's outflow of CDIA to FTAA_{32} is substantially larger than that of inflows. In 2000, it amounted to $46.9 billion, or 15.6 percent of Canada's total CDIA, after rising by 7.1 percent from $43.7 billion the previous year. The record investment outflow resulted mainly from Canada's acquisition of production facilities in the FTAA_{32} countries. In order of significance, Barbados, Chile, Bahamas, Brazil, Argentina, Mexico and Peru were the main destinations of CDIA, accounting for 92.9 percent of total outflows to FTAA_{32}. In 2000, CDIA to Barbados increased sharply to $19.6 billion, from $18 billion in 1999. In contrast, Canadian investors reduced direct investments in Peru, Colombia, Jamaica, Honduras and Costa Rica in 2000.

Figure C8: Export, Import and Trade Balance with FTAA other than U.S. and Mexico



Conclusion

Two-way merchandise trade between Canada and the FTAA_{32} countries rose steadily, from $7.1 billion in 1980 to $23.8 billion in 2000. Most of the increases in two-way trade came from Mexico. Excluding Mexico, two-way trade with FTAA_{32} countries went from $6.3 billion in 1980 to $9.7 billion in 2000. Because the increase in two-way trade came from imports, Canada's deficits have worsened over time. Imports from FTAA_{32} totalled $18 billion in 2000, substantially higher than the $5.8 billion value of exports the same year.

In the case of services, much of Canada's exports are in the form of commercial services. For imports, both travel and commercial services are important. Canada's direct investment in FTAA_{32} is substantially higher than foreign investment in Canada. As well, Canada's outflow increased more than fivefold between 1989 and 2000, a more rapid rate than the threefold increase in inflows.

[16] Our thanks to the staff of Statistics Canada's Balance of Payments Division for compiling this new information.

II. TRADE IN SERVICES

In 2000, exports of services reached $56.3 billion, which accounted for 11.9 percent of total exports of goods and services and represented an increase of 8.6 percent over the 1999 figure of $51.8 billion. The growth rate in 2000 was higher than the 6 percent achieved in 1999. At the same time, imports amounted to $62.8 billion, which accounted for 14.7 percent of total imports of goods and services and represented an increase of 8.6 percent from $57.8 billion in 1999.

Services trade is classified into four categories: travel services; transportation services; commercial services (including accounting, legal, insurance, architecture, engineering, and management consulting); and a small component to cover government services.

With regard to services exports in 2000:

- Commercial service exports grew by 9.7 percent to $28.8 billion or 51.2 percent of total services.
- Travel receipts grew 4.2 percent to $15.7 billion, representing 28 percent of total service exports.
- Transportation services expanded by 13.8 percent to $10.7 billion or 19 percent of total service exports.
- Government services declined by 0.4 percent to $1.03 billion, accounting for 1.8 percent of total services exports.

With regard to services imports in 2000:

- Commercial service imports grew by 7.6 percent to $30.4 billion or 48.3 percent of total services imports.
- Travel payments grew 6.7 percent to a record $18 billion, as overseas spending by Canadians rose by 10.1 percent. The appreciation of the Canadian dollar against the euro contributed to this increased travel to European destinations. In 2000, travel payments represented 28.6 percent of total services imports.
- Transportation services expanded by 14.4 percent to $13.8 billion or 22 percent of total services imports. This growth reflected the sharp increase in two-way trade in merchandise.
- Government services imports declined by 2.4 percent to $0.66 billion, accounting for only 1 percent of total service imports.

Canada has traditionally been a net importer of services, overall and in all of the individual services categories except government services, which accounted for 1.4 percent of two-way service trade in 2000. The largest deficit has traditionally been in the travel and transportation sectors, followed by commercial services. In recent years, however, the overall deficit has been progressively reduced. In 2000, the deficit in overall services trade was $6.6 billion (0.6 percent of GDP); down from $13.6 billion (or 1.9 percent of GDP) in 1993, though up slightly from $6.1 billion in 1999 (0.6 percent of GDP). The reduction over the years was due in large part to improvements in the commercial services and travel balances. In 2000, however, Canada's deficit on the travel account rose for the first time since 1997.

With regard to the direction of Canada's trade in services, the U.S. remains Canada's principal trading partner. However, the share of the U.S. in Canada's two-way trade is smaller for services (61.1 percent) than for merchandise (80.3 percent). Here as well, however, the U.S. is becoming an increasingly important market, accounting for 59.3 percent of Canada's service exports in 2000 compared to 56.8 percent in 1989.

Turning to imports, the share of the U.S. edged up from 62.5 percent in 1989 to 62.8 percent in 2000. The share of the EU declined, both as a source and as a destination of services trade. The share of exports to Japan dropped sharply over the 1989-2000 period, but Japan's share in Canada's services imports was slightly higher in 2000 than in 1989. The relative shares of other countries increased over 1989-2000 for both exports and imports.

Figure 4: Service Exports to Selected Economies, 1989

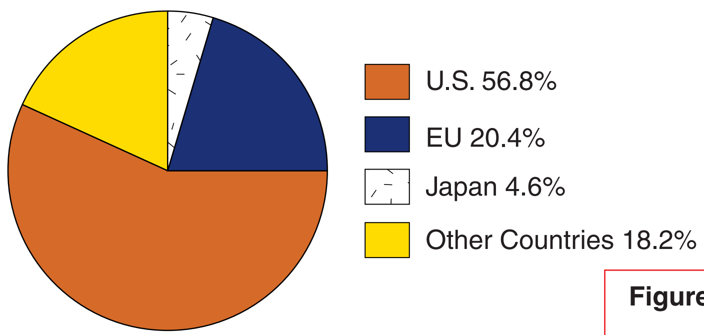


Figure 5: Service Exports to Selected Economies, 2000

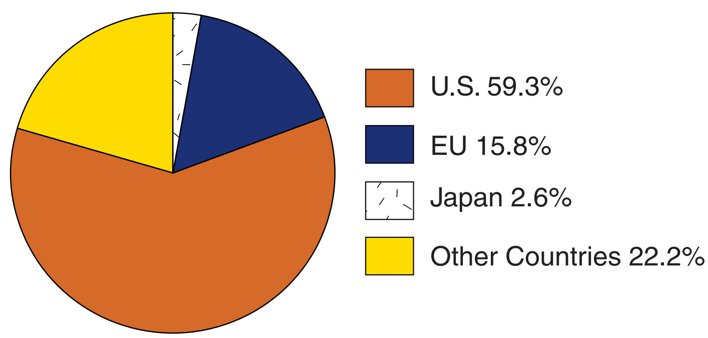


Figure 6: Service Imports from Selected Economies, 1989

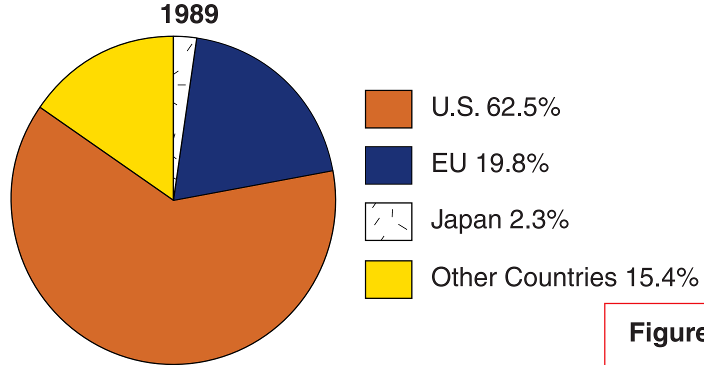
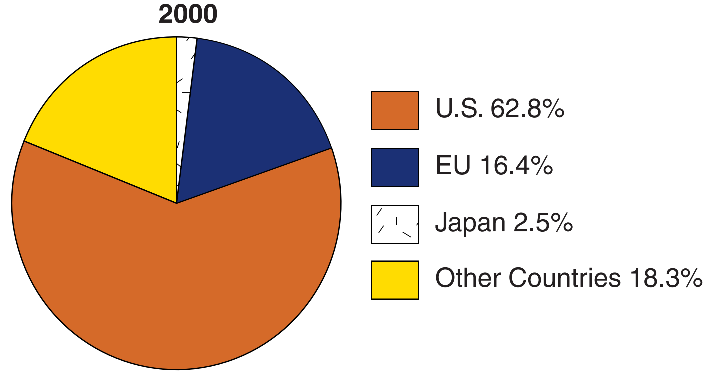


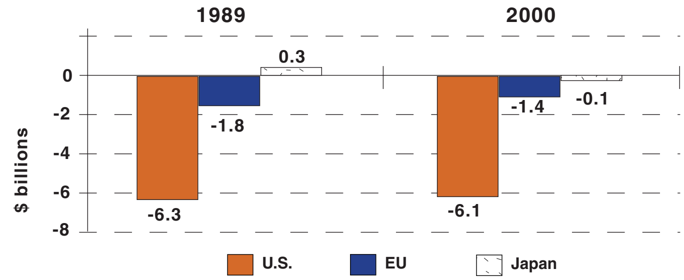
Figure 7: Service Imports from Selected Economies, 2000



Source: Statistics Canada, *Canada's Balance of International Payments*, Catalogue no. 67-001-XPB, Fourth Quarter 2000.

With these developments, Canada's deficit in service trade with the U.S. and the EU fell, while the small surplus with Japan in 1989 turned into a small deficit in 2000.

Figure 8: Canada's Services Trade Balance with Selected Economies, 1989 and 2000



Source: Statistics Canada *Canada's Balance of International Payments*, Catalogue no. 67-001-XPB, Fourth Quarter 2000.

Developments in Canada's Services Trade

Canada's exports and imports of services have risen at a steady pace over the last two decades. As a share of GDP, Canada's services exports rose to 5.4 percent in 2000, from 3.4 percent in 1989-1992 and 4.4 percent in 1993-1996. Services imports have also expanded faster than GDP; in this case, however, the expansion has been more moderate — from 4.9 percent in 1989-1992 to 5.8 percent in 1993-1996 and to 6 percent in 2000.

Compared to merchandise trade, the pace of growth of services trade has lagged over the last decade despite the rising importance of trade in commercial services. Accordingly, the share of services in Canada's goods and services trade fell further to 11.9 percent in 2000 for exports, and to 14.7 percent for imports, continuing the downward movement from the 1991 peak of 13.6 percent, and 19.8 percent, respectively.

Table 13: Average Annual Trade in Services, 1960-2000

	1960-1969	1970-1979	1980-1989	1990-2000	1998	1999	2000
$ millions							
Total exports of services	1,543	4,381	13,867	37,074	48,848	51,755	56,229
Total imports of services	1,984	6,588	19,284	46,859	55,809	57,824	62,814
percent							
Share of services in total exports	13.8	10.9	10.9	12.6	13.2	12.6	11.9
Share of services in total imports	18.0	16.6	16.1	16.8	15.5	15.0	14.7

Source: Statistics Canada *Canada's Balance of International Payments*, Catalogue no. 67-001-XPB, Fourth Quarter 2000.

Knowledge-based Sectors Drive Commercial Services Trade

The commercial services sector has established by far the largest share and the fastest-growth record in Canada's trade in services. In 2000, commercial services accounted for 51.2 percent of exports of services and 48.4 percent of imports, up from corresponding figures of 40.8 percent and 41.5 percent in 1989.

Commercial services include many of the sectors in which knowledge-based activities predominate. Accordingly, success in this sector is important to Canada's continued evolution as a knowledge-based economy. As shown in Table 14, the fastest growth has been recorded in the knowledge-intensive subsectors of commercial services, particularly in royalties and licence fees, research and development, and architectural, engineering and other technical services.

Table 14: Components of Commercial Services Exports, 1993-2000

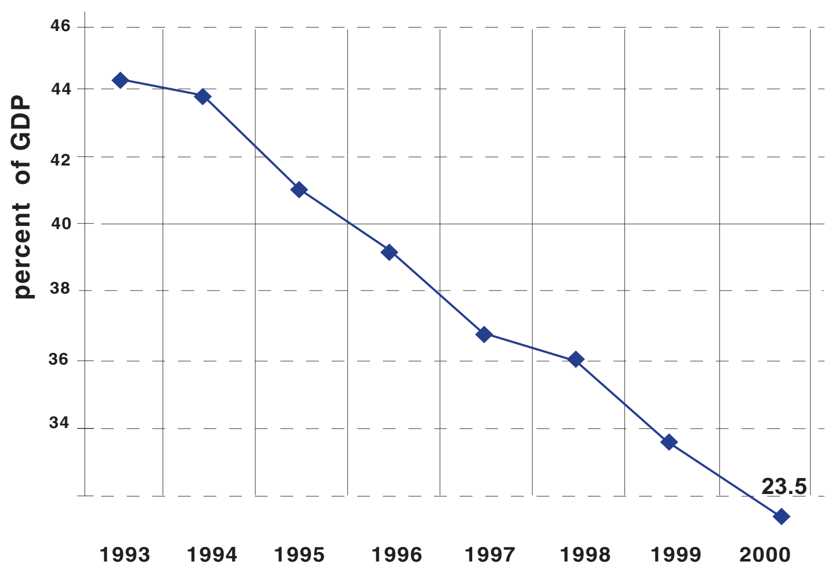
Components of commercial services	Value ($ millions)		Annual percent growth
	1993	2000	1994-2000
Communications services	1,417	1,926	4.5
Construction services	88	272	17.5
Insurance services	2,810	3,992	5.1
Other financial services	850	1,815	11.4
Computer and information services	1,043	1,743	7.6
Royalties and licence fees	308	2,097	31.5
Non-financial commissions	383	1,010	14.9
Equipment rentals	204	277	4.5
Management services	1,120	2,602	12.8
Advertising and related services	160	403	14.1
Research and development	997	3,288	18.6
Architectural, engineering, and other technical services	1,398	3,653	14.7
Miscellaneous services to business	1,603	4,167	14.6
Audio-visual services	599	1,526	14.3
Total	**13,113**	**28,770**	**11.9**

Source: Statistics Canada, *Canada's Balance of International Payments*, Catalogue no. 67-001-XPB, Fourth Quarter 2000.

III. INVESTMENT INCOME

Canada has historically run a deficit on its net investment income account, as money earned by non-residents on their Canadian investments has substantially exceeded the earnings of Canadians on their investments abroad.[17] This reflects the fact that, for the most part, Canada has been a net capital importing country for much of its history because of its over-abundance of investment opportunity. Accordingly, the stock of Canada's external liabilities (on which foreigners earn investment income), which stood at $1,023 billion at the end of 2000, was substantially greater than the stock of Canadian assets abroad (on which Canadians earn investment income), which was $779.3 billion. As a result, Canada had a net international investment position of $243.7 billion or about 23.5 percent of GDP. This share has been in decline in recent years (see Figure 9), with a particularly sharp drop in 2000 as the level of net external debt fell by 10 percent while GDP rose strongly. The decline in net external indebtedness in 2000 is particularly noteworthy, since it was the fifth such decline in the last six years.

Figure 9: Net Foreign Liabilities as a Share of GDP, 1993-2000



Sources: Statistics Canada, *National Income and Expenditure Accounts,* Catalogue no. 13-001-PPB, Fourth Quarter 2000. *Canada's International Investment Position*, Catalogue no. 67-202-XIB, 2000.

For 2000:

- ❑ Investment income earned by Canadian residents on investments abroad totalled $37.8 billion. Of this, 50 percent was on direct investment, 11.7 percent on portfolio investment and the remaining 38.3 percent on other investment (which includes loans, deposits, reserves and other assets).
- ❑ Income earned by foreign residents on investments in Canada totalled $68.1 billion. Of this, about 35.1 percent was on FDI, 43.2 percent on portfolio investment, and the remaining 21.7 percent on other investment.
- ❑ Canada had a deficit of $30.2 billion on the investment income account, a decline of $2 billion from the previous year. About 83 percent of this deficit was contributed by the deficit in portfolio investment earnings.
- ❑ The deficit on investment income was 55 percent as large as Canada's record merchandise trade surplus of $54.5 billion.

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[17] Investment income consists of income earned as interest, dividends and reinvested earnings on investments (direct, portfolio and other categories) by Canadians abroad and by foreigners in Canada.

IV. CURRENT ACCOUNT

Through most of the period since the early 1970s, Canada has run deficits on the current account, coinciding with the emergence of a structural deficit in public-sector finances.[18] At the same time, however, the share of private savings in Canadian GDP has fallen continuously, to 16.3 percent in 1998 from 22.2 percent in the first half of the 1980s. As a result, Canada has consistently required net borrowing from abroad to finance domestic investment through much of the last three decades. In the 1990s, Canada brought the public sector deficit down, and has turned the balance into a surplus since 1997. The improvement in the budget surpluses has contributed favourably to Canada's current account balances in recent years.

Table 15: Domestic Savings and Investment, as Share of GDP, 1981-2000

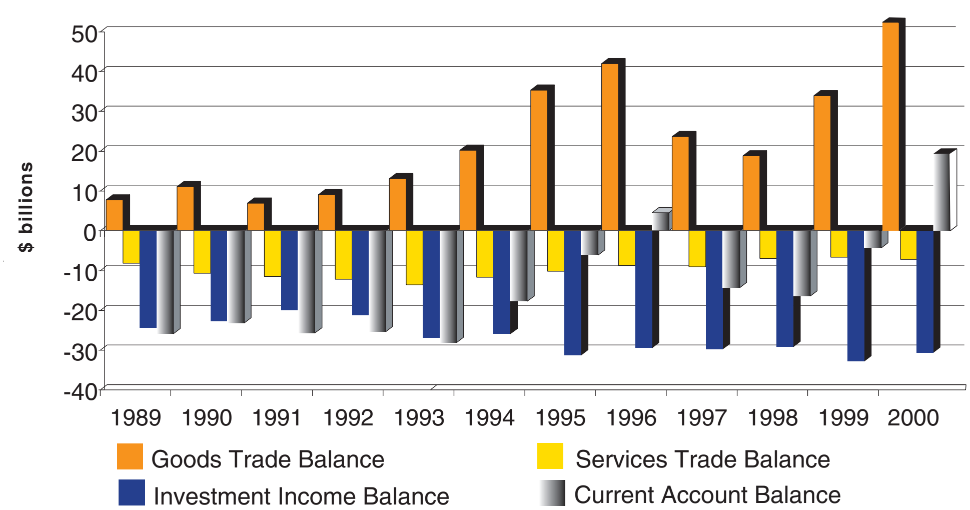
	Private			Public	
	Saving (percent)	Investment (percent)	Excess saving over investment	Budget surplus (+) Budget deficit (-)	Current account balance
1981-1985	23.2	17.8	5.5	-5.1	-1.2
1986-1990	20.8	18.9	1.8	-4.0	-3.3
1991-1995	19.5	15.2	4.3	-6.8	-2.8
1996	18.7	15.2	3.4	-2.5	0.6
1997	17.0	18.2	-1.2	0.1	-1.6
1998	16.3	17.9	-1.6	0.0	-1.8
1999	16.4	17.8	-1.4	1.8	-0.4
2000	17.1	17.8	-0.7	3.5	1.8

Source: Statistics Canada, *National Income and Expenditure Accounts,* Catalogue no. 13-001-PPB, Fourth Quarter 2000. Note: Due to the statistical discrepancy in the national accounts, the sum of the shares of excess private saving over private investment and budget surplus or deficit in GDP may not add to the share of current account deficit in GDP.

For 2000, Canada had a surplus on the current account of $18.9 billion, representing 1.8 percent of GDP (Figure 10). The improvement in the current account in 2000 was largely driven by an increase in the merchandise surplus with the United States.

[18] The current account balance is the sum of the balances on trade (in merchandise and services), investment income and transfers. A surplus on the current account indicates that a country has earned (or obtained via transfers) more money abroad than it has paid out, and is thus a net saver internationally. This surplus, which is mirrored in a deficit on the capital and financial accounts, requires a net outflow of capital. By the same token, a current account deficit means that a country is a net borrower internationally (as reflected in a net inflow of capital and thus a surplus on the capital and financial accounts). In an accounting sense, a current account deficit reflects a shortage of domestic savings relative to domestic investment.

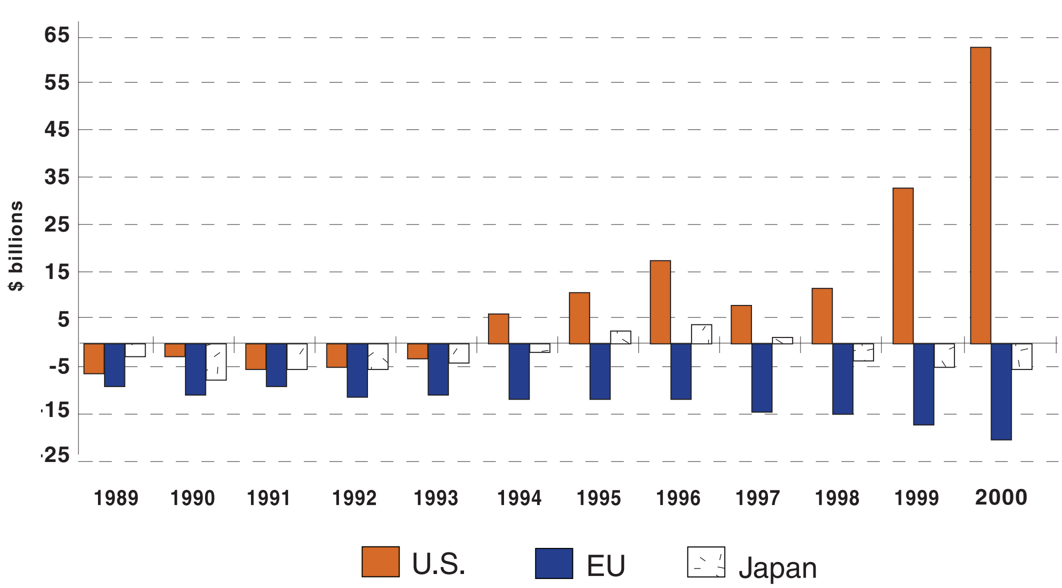
Figure 10: Structure of Canada's Current Account, 1989-2000



Source: Statistics Canada, *Canada's Balance of International Payments*, Catalogue no. 67-001-XPB, Fourth Quarter 2000

During 1994-2000 Canada's growing current account surplus with the U.S was partly offset by a rising deficit with the EU. The balance with Japan has tended to be small, with some cyclical variation (see Figure 11). Canada's current account surplus with the U.S. — $63.5 billion in 2000 — was the largest ever on this account. Canada's current account deficit with the EU widened to $19.9 billion in 2000 from $18.3 billion in 1999. With respect to Japan, Canada had a brief period of current account surpluses during the period 1995-1997, but these turned into deficits of $3.4 billion in 1998, widening to $4.2 billion in 1999 and to $4.5 billion in 2000.

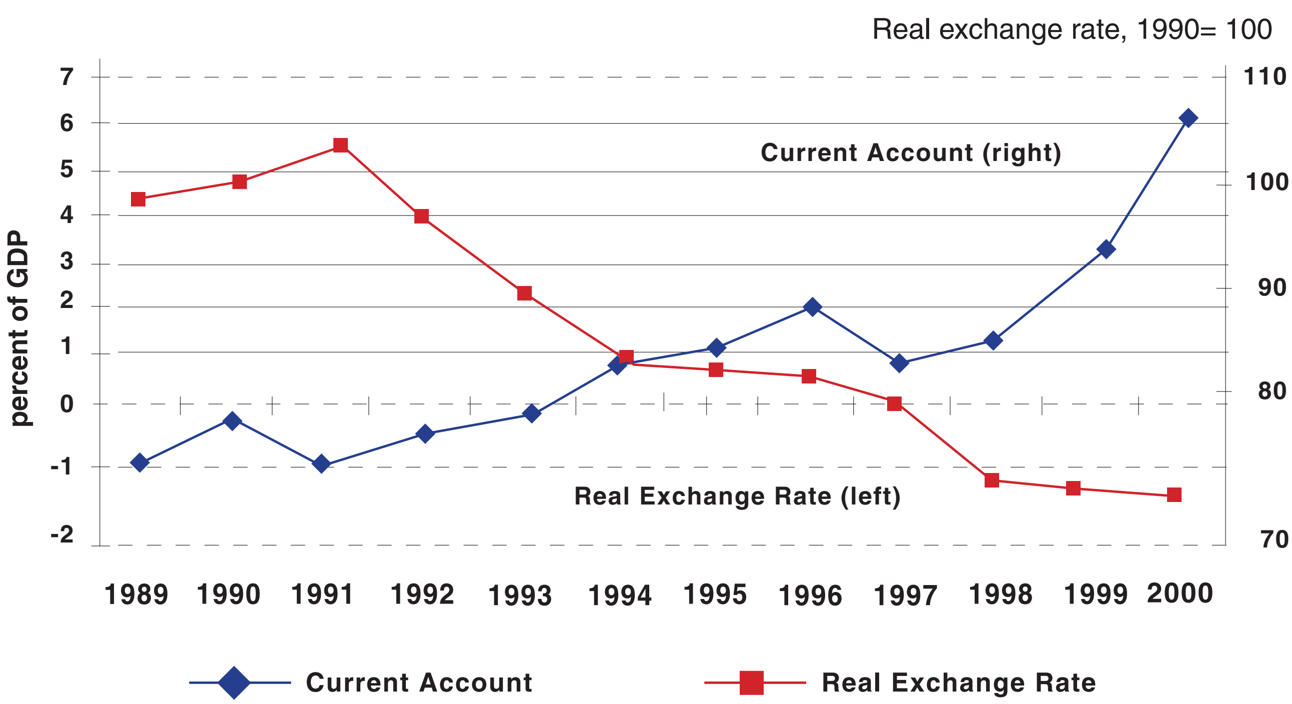
Figure 11: Current Account Balance with Major Trading Partners, 1989-2000



Source: Statistics Canada, *Canada's Balance of International Payments*, Catalogue no. 67-001-XPB, Fourth Quarter 2000.

As can be seen from Figure 12, the improvement in Canada's bilateral balance with the U.S. from deficit to surplus since 1994 was associated with the depreciation of the Canadian dollar in real terms over this period;[19] other factors, such as the stronger economic expansion in the U.S. and the FTA, were also important.

Figure 12: Canada's Real Exchange Rate vis-à-vis U.S. Dollar and Current Account Balance with the U.S., 1989-2000



Sources: Statistics Canada, *Canada's Balance of International Payments,* Catalogue no. 67-001-XPB, Fourth Quarter 2000.
Bank of Canada, *Banking and Financial Statistics*.

[19] In Figure 12, Canada's real exchange rate vis-à-vis the U.S. is calculated as the price of Canadian goods (measured in U.S. dollars) in terms of the price of U.S. goods (as the term "real" implies). This calculation, based on the consumer price index, shows that in 2000, the real price of a bundle of Canadian goods in terms of that of the U.S. has come down to 73 percent as much as that in 1990.

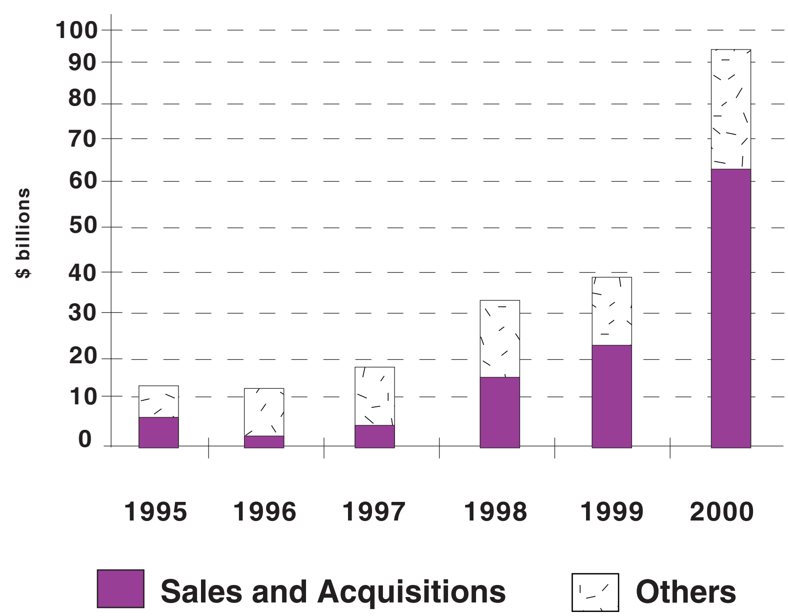
V. CAPITAL AND FINANCIAL ACCOUNTS

The capital and financial accounts consist of transactions in financial assets and liabilities. The capital account includes capital transfer such as migrants' assets and inheritances, and federal government superannuation. The financial account covers inflows and outflows of direct investment, portfolio investment and other investment.[20]

Direct Investment

Foreign direct investment into Canada in 2000 rose 150.4 percent, to a record $93.2 billion. This is up from $37.2 billion in 1999, despite a 55.5 percent decline in inflows from the U.S. to $17.1 billion, from $38.4 billion in 1999. Inflows from the EU shot up from $2.4 billion in 1999 to $72.2 billion in 2000, an unusually large 29-fold increase, mainly as a result of acquisitions of Canadian firms (see Figure 13). Prominent among these acquisitions were the takeovers of Seagram Co. by Viendi SA of France, and of Newbridge Networks Corporation by Alcatel SA of France. This surge in acquisitions by the EU occurred at a time when the euro has lost 11.4 percent against the value of the Canadian dollar, suggesting that exchange rates are not the primary considerations behind takeover activity.

Figure 13: FDI in Canada: Sales, Acquisitions and other Flows, 1995-2000



Source: Statistics Canada, *Canada's Balance of International Payments*, Catalogue no. 67-001-XPB, Fourth Quarter 2000.

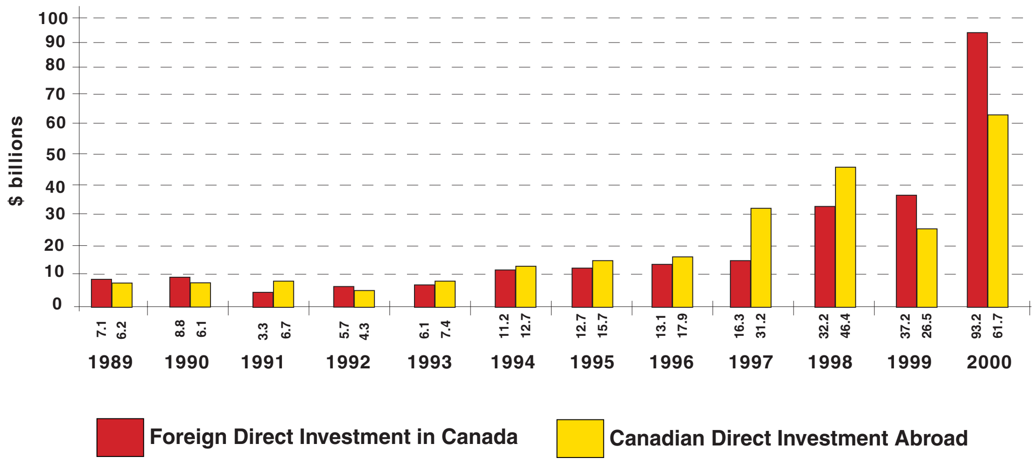
Much of the FDI inflows in 2000 went to the food, beverage and tobacco sector, as well as the fast-growing machinery and transportation equipment, and energy industries.

The outflow of CDIA more than doubled in 2000, to a record high of $61.7 billion, from $26.5 billion in1999. The increase in investment outflow was widespread across countries, but was concentrated in the U.S. market: CDIA into the U.S. more than doubled to $38.4 billion in 2000 from 17.4 billion in 1999, representing 62.3 percent of total outflows. CDIA into the EU jumped from $0.9 billion in 1999 to $9.4 billion in 2000. The movement in CDIA resulted from acquisitions of foreign companies in the United State and Europe, and were concentrated in the computer industry. Outflows to traditional sectors such as energy and metallic industries also increased strongly.

[20] Direct investment refers to investment that allows investors a significant influence in the management of an enterprise. For practical purposes, direct investment pertains to transactions in which the investor has ownership of at least 10 percent of an enterprise's voting equity. Portfolio investment includes transactions between non-residents and Canadian residents in stocks, bonds and Canadian money market papers, which are debt instruments with original maturities of one year or less. Other investment includes loans, deposits, official international reserves, and assets such as trade credits, deferred immigrants' funds and progress payments.

Over the period 1993-1998, CDIA consistently exceeded FDI. In 1999 and 2000, however, the flow of FDI exceeded CDIA by $10.8 billion and $31.5 billion, respectively (Figure 14). The high level of two-way flows suggests that the main driving forces have been shifts in the underlying structure of industry and trade in response to globalization pressures, rather than transient factors such as exchange rate movements or cyclical fluctuations.

Figure 14: Flows of FDI and CDI, 1989-2000



Source: Statistics Canada, *Canada's Balance of International Payments*, Catalogue no. 67-001-XPB, Fourth Quarter 2000.

With these developments, the stock of FDI rose to $301.4 billion at year end 2000, while CDIA reached $291.5 billion. These figures include capital gains/losses on existing assets, reinvested earnings and exchange rate revaluations, in addition to the stream of investment flows in previous years. As shown in Table 16, finance and insurance had the highest shares in the CDIA stocks in 2000 among the various sectors of the Canadian economy. In the case of FDI, the most important is the energy and metals sector.

Table 16: Stocks of CDIA and FDI by Sector, Year End 2000

	CDIA		FDI	
Industry Group	**$ billions**	**% of total**	**$ billions**	**% of total**
Wood and paper	7.8	2.6	15.3	5.3
Energy and metallic minerals	63.9	21.2	50.6	17.4
Machinery and transportation equipment	16.3	5.4	42.8	14.7
Finance and insurance	103.8	34.4	49.7	17.0
Services and retailing	32.7	10.8	24.3	8.4
Other industries	77.0	25.6	108.8	37.3
Total	**301.4**	**100.0**	**291.5**	**100.0**

Source: Statistics Canada, *Canada's International Investment Position*, Catalogue no. 67-202-XIB, 2000.

With respect to the country of source, the U.S. accounted for 63.9 percent of the total FDI stock in Canada in 2000, followed by France, at about 10 percent. Takeover activity raised the EU's share to 27 percent in 2000 from 20 percent in 1999. As for the stock of CDIA, the U.S. accounted for 51.1 percent, followed by the United Kingdom, at 8.4 percent. The EU accounted for 18.8 percent in 2000, down from 19.4 percent in 1999.

Box D: International Direct Investment and Canada's Position in the NAFTA

Direct Investment Flows

FDI decisions are governed by firms' actions to locate production and related activities in plants that are most cost-effective. These decisions consider the advantages associated with labour costs, government incentives, liberalization of cross-border investment, potential economies of scale or scope, rationalization of plant facilities through cross-border mergers and acquisitions, and access to foreign markets by bypassing trade barriers.

FDI flows, whether inward or outward, are beneficial in a number of ways. Firstly, such investment flows tend to strengthen commercial links between the host and recipient countries, and raise the overall level of trade (and economic exchange more generally) between the two countries. Recent empirical work has confirmed that FDI plays an important role in fostering international spillovers of technological information for both developing and advanced economies.[21] FDI provides a mechanism for transferring technology that cannot be achieved through trade in goods and services and financial investments. FDI increases the flow of knowledge spillovers, both from and to the investing multinationals, and benefits both countries through gains in employee training and enhanced opportunities to exploit economies of scale in R&D and production. Growth theorists have introduced knowledge spillovers resulting from trade in goods and FDI, and the ability to imitate the products of foreign producers as engines of endogenous growth. In the host country, inward FDI tends to raise imports in the short-term and stimulate exports in the longer run, as exports will rise when new production facilities associated with the FDI come on line. International flows of capital can also reduce the risk of investment by providing regional diversification of portfolio. Another benefit of FDI flows is that they tend to reduce both the risk and magnitude of potential international financial crises, as such long-term flows cannot and tend not to be quickly reversed, unlike short-term capital flows.

Table D1: World FDI Inflows in US$ millions

	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
World	200,612	203,812	157,773	175,841	219,421	255,988	331,844	377,516	473,052	680,082	865,487
NAFTA	75,928	58,322	29,502	28,055	54,998	64,275	77,555	103,277	130,080	218,259	311,827
Canada	5,018	7,855	2,740	4,777	4,749	8,207	9,257	9,636	11,761	21,705	25,061
United States	67,736	47,918	22,020	18,885	43,534	45,095	58,772	84,455	105,488	186,316	275,533
Mexico	3,174	2,549	4,742	4,393	6,715	10,973	9,526	9,186	12,831	10,238	11,233
Distribution of NAFTA FDI Inflows (percent)											
Canada	6.6	13.5	9.3	17.0	8.6	12.8	11.9	9.3	9.0	9.9	8.0
United States	89.2	82.2	74.6	67.3	79.2	70.2	75.8	81.8	81.1	85.4	88.4
Mexico	4.2	4.4	16.1	15.7	12.2	17.1	12.3	8.9	9.9	4.7	3.6

Source: UNCTAD World Investment Report, Annex Table B.1

[21] Lee Branstetter, Is Foreign Direct Investment a Channel of Knowledge Spillovers? Evidence from Japan's FDI in the United States, NBER Working Paper no. W8015, November 2000.

The data show that the sums borrowed and lent across Canada's borders are vast, as a result of the optimal international diversification of equity investment, even though the net flow in capital is much smaller. In the context of FDI in NAFTA countries, Canada's share of inward FDI flow was 8 percent in 1999, up somewhat from 6.6 percent in 1989. Canada's share shot up to a high of 17 percent in 1992 before trending down thereafter. The volatility in direct investment flows reflects mergers, acquisitions and outright purchases of existing firms, activities that are often associated with sizeable transfers of funds.[22] The rise in Canada's share between

Table D2: World FDI Outflows in US$ millions

	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
World	217,874	240,253	210,821	200,800	247,425	282,902	357,537	390,776	471,906	687,111	799,928
NAFTA	30,369	32,124	39,278	43,180	80,438	83,606	103,275	97,562	123,140	178,701	169,517
Canada	4,584	4,725	5,655	3,547	5,711	9,296	11,464	13,098	22,515	31,286	17,816
United States	25,678	27,175	33,456	38,978	74,837	73,252	92,074	84,426	99,517	146,052	150,901
Mexico	107	224	167	655	-110	1058	-263	38	1108	1363	800
Distribution of NAFTA FDI Outflows (percent)											
Canada	15.1	14.7	14.4	8.2	7.1	11.1	11.1	13.4	18.3	17.5	10.5
United States	84.6	84.6	85.2	90.3	93.0	87.6	89.2	86.5	80.8	81.7	89.0
Mexico	0.4	0.7	0.4	1.5	-0.1	1.3	-0.3	0.0	0.9	0.8	0.5

Source: UNCTAD World Investment Report, Annex Table B.2

1989 and 1999 occurred at the expense of both the United States and Mexico. Mexico's share of NAFTA inward flows eased from 4.2 percent in 1989 to 3.6 percent in 1999, after peaking at 17.1 percent in 1994. The share for the United States fell from 89.2 percent in 1989 to a trough of 67.3 percent in 1992, and recovered to 88.4 percent by 1999, reflecting flows associated with merger and acquisition activity by the EU. FDI has played a rising role in Canada's investment performance. The inflow of FDI in 1999 represented 31.8 percent of Canada's total business investment in non-residential structures and in machinery and equipment, up from 8.8 percent in 1989.

Typically, outward FDI is associated with significant growth in exports of the originating country in the form of intermediate and complementary supply of finished goods. Even though FDI outflow may have a substitution effect on exports of finished goods, an "analysis of 14 countries demonstrated that each dollar of outward FDI produces about two dollars' worth of additional exports."[23] This evidence refutes the popular myth that outward FDI reduces exports and employment by transferring production facilities and jobs to foreign locations. In the case of outward FDI flows, Canada's share in North America was down from 15.1 percent in 1989 to 10.5 percent in 1999, although this series has been very volatile, falling to a low of 7.1 percent in 1993 and rebounding to a high of 18.3 percent in 1997. Because Mexico's direct investment outflow is insignificant, developments in the United States mirror those in Canada.

[22] According to Crosbie and Co., a Canadian investment banking service company, foreign corporations bought up 222 Canadian companies in 2000 to the tune of $102 billion. The weak U.S. dollar value of the Canadian dollar did not appear to be a factor, as a number of the takeovers were by European corporations at a time when the Canadian dollar had risen sharply against the euro. Some of the more prominent acquisitions include the $49.5 billion takeover of Seagram Co. by Vivendi SA of France, and the $10.8 billion takeover of Newbridge Networks Corporation by Alcatel SA of France. Canadian corporations also acquired 318 foreign corporations for a total amount of $56.5 billion in 2000.

[23] Lionel Fontagne, "Foreign Direct Investment and International Trade: Complements or Substitutes?" Working paper 1999(3), OECD Directorate for Science, Technology and Industry, October 14, 1999.

Direct Investment Stocks

Outward and inward FDI flow data represent the bulk of the additions to Canada's external assets and liabilities, respectively. The accumulated stock of FDI flows over the years reveals the extent to which Canada has been both a supplier and a receiver of direct investment funds. According to the UNCTAD World Investment Report, the U.S. dollar stock of global FDI into Canada was up by 47.4 percent between 1990 and 1999. However, this growth compares poorly with the 175 percent increase of FDI into the United States over the corresponding period. As a result, the distribution of investment share dropped sharply for Canada, from 21.3 percent in 1990 to 12.5 percent in 1999, while the U.S. share rose steadily from 74.5 percent in 1990 to 82 percent in 1999. This development occurred as investors worldwide shifted their funds to the United States, whose economic expansion in the 1990s was the strongest and most prolonged among the G-7 countries. As well, the financial/exchange rate crises in Asia, Russia and Brazil from mid-1997 through early 1999 contributed to a substantial inflow of foreign investment into U.S. markets in search of a "safe haven."

Table D3: World FDI Inward Stocks in US$ millions

	1985	1990	1993	1994	1995	1996	1997	1998	1999
World	763,357	1,761,198	2,079,538	2,342,182	2,743,391	3,065,299	3,436,651	4,015,258	4,771,981
NAFTA	251,233	530,207	593,137	664,345	699,864	833,647	869,854	1,015,773	1,325,571
Canada	64,634	112,872	105,957	105,606	123,181	128,867	137,658	143,234	166,266
United States	184,615	394,911	445,268	504,401	535,553	630,045	681,651	811,756	1,087,289
Mexico	1,984	22,424	41,912	54,338	41,130	74,735	50,545	60,783	72,016
Distribution of NAFTA FDI Inward Stocks (percent)									
NAFTA	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Canada	25.7	21.3	17.9	15.9	17.6	15.5	15.8	14.1	12.5
United States	73.5	74.5	75.1	75.9	76.5	75.6	78.4	79.9	82.0
Mexico	0.8	4.2	7.1	8.2	5.9	9.0	5.8	6.0	5.4

Source: UNCTAD World Investment Report, Annex Table B.3

Table D4: World FDI Outward Stocks in US$ millions

	1985	1990	1993	1994	1995	1996	1997	1998	1999
World	707,133	1,716,364	2,134,619	2,412,249	2,870,624	3,115,870	3,423,433	4,065,798	4,759,333
NAFTA	294,694	515,925	646,020	717,751	821,252	919,946	1,009,949	1,147,326	1,316,438
Canada	43,127	84,829	86,310	105,606	118,105	124,741	143,948	160,936	178,347
United States	251,034	430,521	559,688	610,061	699,015	792,960	860,723	980,565	1,131,466
Mexico	533	575	22	2,084	4,132	2,245	5,278	5,825	6,625
Distribution of NAFTA FDI Outward Stocks (percent)									
NAFTA	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Canada	14.6	16.4	13.4	14.7	14.4	13.6	14.3	14.0	13.5
United States	85.2	83.4	86.6	85.0	85.1	86.2	85.2	85.5	85.9
Mexico	0.2	0.1	0.0	0.3	0.5	0.2	0.5	0.5	0.5

Source: UNCTAD World Investment Report, Annex Table B.4

While inward FDI grew rapidly in Mexico during the 1990s, its overall U.S. dollar value was still less than half of what Canada received in 1999. Mexico's share in 1999 was 5.4 percent, up from 4.2 percent in 1990, reflecting in part the impact of the relaxation of FDI controls and restrictions.

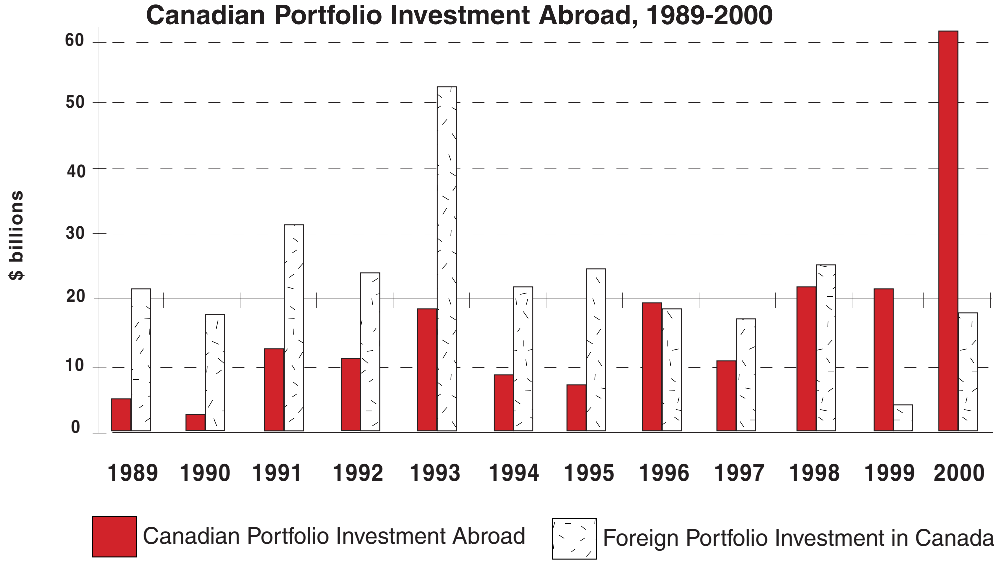
For NAFTA countries as a whole, the increase in the stock of inward FDI in the 1990s occurred at a time when the stock of outward FDI also increased rapidly as a result of globalization forces. Over the 1990s, Canada's share of NAFTA stock of outward FDI was rather stable at around 15 percent. The United States accounted for the remainder, since Mexico's FDI outflow is marginal.

Portfolio Investment

Portfolio investment has fluctuated sharply historically; reflecting perceived projected financial returns in the respective host countries. Inflows, which include investments in Canadian bonds, stocks and money markets, rebounded from a record low of $5.3 billion 1999 to $18.8 billion in 2000. Foreign investors acquired a record $35.2 billion of Canadian stocks in 2000, up from $14 billion in 1999.

Canadian portfolio investment abroad increased from $22.9 billion in 1999 to $62.9 billion in 2000. The composition of Canadian portfolio investment outflows changed significantly, as higher foreign content limits for tax-sheltered Canadian investment funds contributed to record-high purchases of foreign stocks. Canadian investment in foreign stocks rose to $58.9 billion in 2000, from $20.5 billion in 1999.

Figure 15: Foreign Portfolio Investment in Canada and Canadian Portfolio Investment Abroad, 1989-2000



Source: Statistics Canada, *Canada's Balance of International Payments,* Catalogue no. 67-001-XPB, Fourth Quarter 2000.

The year 2000 marked the third time since 1956 that Canadian portfolio investment abroad exceeded foreign portfolio investment in Canada. The other years were 1996 and 1999, when outflow exceeded inflows by $0.6 billion and $17.6 billion, respectively. In 2000 Canada's portfolio investment abroad exceeded foreigners' corresponding investment in Canada by $44 billion (Figure 15).

With the developments in 2000, the stock of portfolio investment abroad by Canadians reached $212.1 billion, whereas the stock of foreign portfolio investment in Canada edged up to $496.7 billion.

International Investment Position

In summary, Canada relies heavily on inflows of foreign capital to finance domestic investment activity and to finance imports of technology from abroad. As a result, Canada's foreign accumulated debt has traditionally exceeded its corresponding assets. However, Canada's foreign indebtedness fell from 44.7 percent in 1993 to 23.5 percent in 2000. This reflects a marked improvement in the FDI account from the traditional debtor position to that of a creditor since 1996, as well as the surge in investment in foreign stocks, in response to the higher foreign content limits for tax-sheltered Canadian investment funds. Falling government debt, much of which was held by foreigners, also contributed to this turnaround.

VI. SUMMARY OF BALANCE OF PAYMENTS

Table 17 summarizes Canada's overall balance of payments picture in 2000. By standard accounting practices, a country's balance of payments account is always balanced. In 2000, Canada registered a current account surplus of $18.9 billion, more than four times the previous surplus of $4.6 billion posted in 1996. Statistically, this surplus is offset exactly by a deficit in the capital and financial accounts.

Of particular note, the Canadian official settlement balance was a positive $5.5 billion (the table shows negative in the same way as direct investment abroad). This indicates that the Bank of Canada added that much to its foreign exchange reserve (particularly in the form of U.S. dollar and other foreign currencies). This is a positive development in what was a highly successful year for Canada in terms of its international economic activity.

The statistical discrepancy refers to the net position on transactions with non-residents not adequately captured in the balance of payments entries. In 2000 this discrepancy was negative, indicating net outflows of funds from Canada to the rest of the world.

Table 17: Canada's 2000 Balance of International Payments Accounts ($ millions)

Current Account				
• Exports of goods and services	$473,886			
• Imports of goods and services	$425,977			
a. Trade balance		$47,909		
• Investment income abroad	$37,844			
• Investment income of foreigners	$68,058			
b. Net investment income		-$30,214		
c. Net current transfer		$1,249		
1. Current account balance (a + b + c)				**-$18,944**
Financial Account				
• Canadian direct investment abroad	-$61,739			
• FDI in Canada	$93,227			
d. Net FDI		$31,488		
• Portfolio investment abroad	-$62,857			
• Portfolio investment in Canada	$18,846			
e. Net portfolio investment		-$44,011		
f. Other net investment		-$9,117		
2. Financial account balance (d + e + f)				**-$21,640**
Of which:				
- official international reserve			- $5,490	
- non-reserve financial account			-$16,150	
3. Capital account balance				**$4,994**
4. Statistical discrepancy				**-$2,298**
Balance of payments (1 + 2 + 3 + 4)				**$0**

*A negative sign denotes an outflow of capital associated with an increase in assets or a decrease in liabilities.

Source: Statistics Canada, *Canada's Balance of International Payments*, Catalogue no. 67-001-XPB, Fourth Quarter 2000.

STATISTICAL ANNEX

Section 7 - Direct Investment Stocks

Section 8 - Total Investment Stocks

Note: for updates to the Annex tables visit:

http://www.dfait-maeci.gc.ca/eet/stats-e.asp