

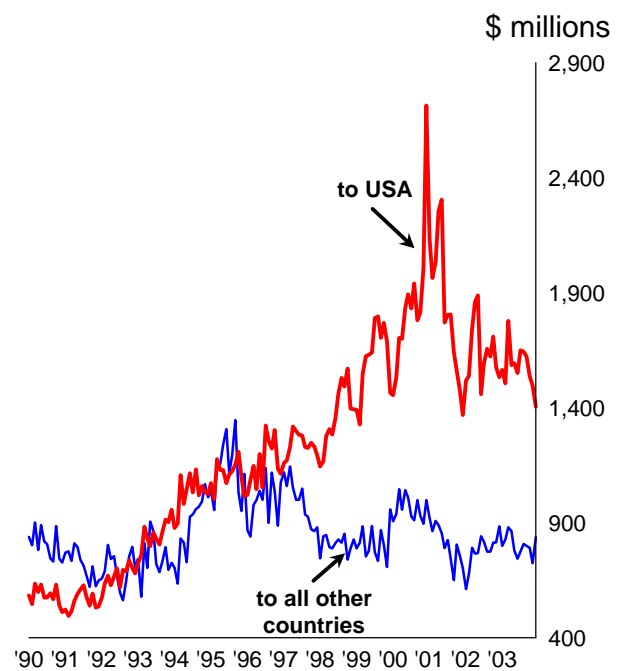
Exports ♦ December 2003

- For the third consecutive year, the value of total BC origin exports experienced a decline in 2003 (-1.6%), although the drop was only half that for Canadian exports as a whole (-3.2%). Strong growth in the value of energy product exports (+33.1%) helped partially offset the effects of the continuing dispute over softwood lumber, the impact of the “mad cow” crisis and the appreciating Canadian dollar, helping BC exports perform better than the national average.
- The most significant increase in the energy sector was in exports of natural gas, which soared 56.2% in 2003 compared to 2002. Most of this increase was due to price inflation, although volumes shipped were also higher. Exports of electricity also expanded in 2003, rising 24.9% over the value recorded in 2002, despite the fact that the quantity exported fell. The entire increase was due to higher prices for the commodity.
- The softwood lumber dispute with the United States helped drive down the value of lumber exports. Softwood lumber exports to the United States were 20.6% lower in 2003 compared to a year earlier, a drop in value of almost a billion dollars. Canada is continuing its legal battles through NAFTA and the WTO, but it will likely be at least autumn before the legal avenues have run their course. In the interim, it seems unlikely that a negotiated solu-

tion will be reached. This could indicate a rough ride for lumber exports through most of 2004 as well.

- Exports of motor vehicles and parts plunged 42.7% in 2003, likely due to the closure of the Western Star Trucks assembly plant in Kelowna in the fall of 2002.
- Exports to the United States dropped 3.9% in 2003, mostly due to reduced shipments of softwood lumber. Shipments to Japan also declined, falling 6.3%. Exports to China cracked the \$1 billion mark in 2003, a 29.2% increase over the previous year. Shipments to Western Europe rose a modest 1.6%.

Rising values of energy exports were not enough to offset declines in international shipments of forest products



Rising Commodity Prices Could Signal Turnaround for BC Exports

BC Exports Declined Once Again in 2003

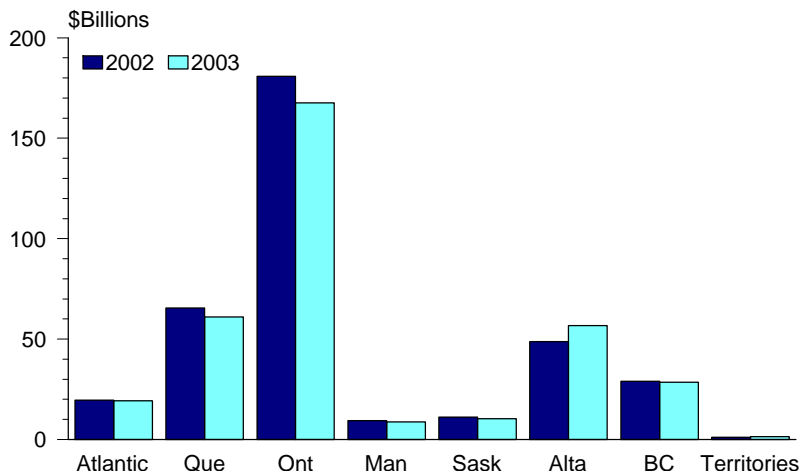
In 2003, the value of BC origin exports fell for the third consecutive year (-1.6%). The soaring price of natural gas and electricity and consequent rise in value of BC exports of those commodities was not enough to offset the poor performance in the forest sector. The effects of the softwood lumber dispute with the United States combined with low commodity prices for pulp and newsprint resulted in a 10.0% drop in exports of forest products.

Despite the substantial increase in the value of energy exports, total BC exports declined

The British Columbia forest industry's response to the substantial 27 per cent tariff on softwood lumber exports to the United States was to ramp up production and improve productivity, thereby driving down costs. This strategy worked for a while, but it resulted in oversupply in the marketplace, which in turn caused prices to drop. The combination of lower prices, crippling tariffs and a rising Canadian dollar has resulted in a 20.6% drop in the value of lumber exports to the United States, despite the fact that quantities shipped increased 3.4%.

The forest sector was not the only poor performer among BC exporters. The discovery of a cow in Alberta infected with bovine spongiform encephalopathy (BSE), more commonly known as "mad cow" disease, has had a significant effect on agricultural exports as many countries, including the United States, closed their borders to exports of live cattle and selected beef products. Another commodity that experienced a significant drop in exports was motor vehicles and parts. This was mainly due to the closure of the Western Star Trucks assembly plant in Kelowna in the fall of 2002.

Exports declined in many regions across the country in 2003

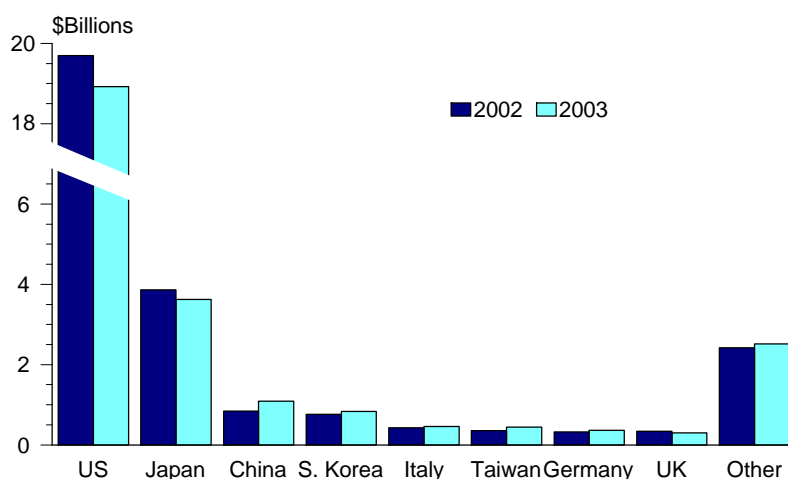


With the notable exception of Alberta, where exports grew on the strength of the energy sector, most areas of the country experienced declining exports in 2003

British Columbia was not alone with respect to declining exports. In fact, with the exception of Alberta, Nova Scotia and New Brunswick, which all benefited from the surge in prices for energy-related goods, all other provinces experienced a decline in the value of exports. However, the increases in Nova Scotia and New Brunswick were not enough to push total exports for the Atlantic region as a whole over the total recorded in 2002. The Territories, on the strength of increased exports of diamonds from the Northwest Territories, were the only other region to experience an increase in the value of exports.

Although the value of exports from BC to its top two major destinations, the United States and Japan, declined in 2003, international shipments to many other destinations experienced some growth. The distribution of exports was slightly more diversified in 2003 compared to the previous year. The United States' share of BC exports fell over one and a half percentage points to 66.3% (from 67.9%) and Japan's share also dropped, to 12.7% of BC exports (compared to 13.3% in 2002). China's share increased from 2.9% in 2002 to 3.8% in 2003. Several other countries ranked in the top ten destinations for BC exports also increased their share, albeit to a lesser degree.

The value of BC origin exports increased for many destinations outside the United States and Japan



The distribution of BC exports was slightly more diversified in 2003

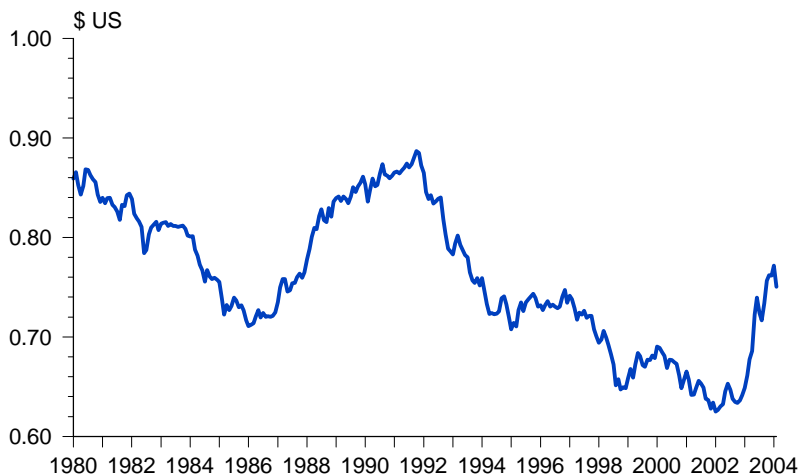
Rising Commodity Prices May Boost Exports in 2004

The outlook for BC origin exports in 2004 is looking more positive than what transpired in 2003. It is unlikely that there will be a fourth consecutive year of decline in the value of international shipments from BC, although part of the reason for that is the lower base from which measurement will start. In other words, the poor performance over the last few years means that even a

mediocre performance in 2004 will be an improvement. However, there are some indications that BC exports could bounce back for several commodity groups.

One of the most significant factors that impacted exports in 2003 was the rapid appreciation of the Canadian dollar. The dollar soared from US \$0.64 at the beginning of January to US \$0.77 by the end of December, an increase of 13 cents, or 22%. Although many economists were projecting a rise in the value of the Canadian dollar at the beginning of the year, none had anticipated this kind of expansion in this short a time. Most forecasts capped the growth of the dollar at somewhere around 69 or 70 cents. The speed of the appreciation caused problems for some exporters and likely had the effect of dampening exports of some key commodities.

The Canadian dollar appreciated rapidly through 2003 but is still well below levels seen in the early nineties



The Canadian loonie appreciated 22% relative to the American greenback in 2003

The consensus opinion for 2004 appears to be a continuation of the appreciation in the dollar, although at a much more moderate pace, finishing the year at between US \$0.77 and US \$0.80. This may be distressing for some exporters already feeling the bite of a “high” dollar, but it’s not as if this is new territory. It has been a decade since the dollar exceeded US \$0.78, but Canadian exporters were able to compete then and should still be able to compete. If anything, the higher dollar may be viewed as an opportunity by some exporters to make capital investments to improve efficiency and make themselves more competitive. With a significant amount of cutting-edge technology being developed in the United States, the low Canadian dollar may have made these investments too expensive in the past, but they may be more affordable now.

The consensus forecast is for the dollar to continue to rise, albeit at a much slower pace than last year

There are some indications that the outlook for a higher Canadian dollar may be overly optimistic (or pessimistic, depending on your viewpoint). The recent decision by the Bank of Canada to cut its trend-setting rate by 250 basis points and the indication given that further rate cuts may be on the horizon could signal depreciation for the loonie, particularly since the US Federal Reserve Board is giving indications that it will soon start increasing interest rates, which will shrink the gap between Canadian and American rates and make the Canadian dollar somewhat less attractive compared to its American counterpart. Also, the United States economy is forecast to grow faster than Canada's in 2004, which should also have a dampening effect on the loonie. Whether or not these factors will outweigh those that are driving the dollar up remains to be seen; however, it is likely that the forecasters are correct in saying that the pace of growth experienced in 2003 will not recur this year. If the dollar does appreciate, it should be at a far more moderate pace at which exporters should be able to adjust much more easily.

There are some factors that could dampen the dollar's growth

Regardless of whether the dollar appreciates or not, the prospect of rising commodity prices could prove to be the saving grace for many British Columbia exporters. Although there were some increases in prices for selected export commodities in 2003, the rapid appreciation of the Canadian dollar nullified much of the positive effect.

Prices are expected to rise for many key commodities, which should benefit BC exporters

The one area where commodity prices are expected to fall is for energy-related commodities, such as natural gas and electricity. Low inventories of natural gas combined with greater demand caused by extreme weather conditions (very cold winter, very hot summer) helped drive up prices in 2003. It is unlikely that these conditions will occur again, which should cause prices to ease back; however, there is still a significant demand for natural gas and there have not been many new discoveries that will increase supply, so prices should remain well above historical levels.

For electricity, the volume of exports will depend to a large extent on weather conditions. In 2003, low snow packs resulting from reduced precipitation in the winter, combined with the long dry spell in the summer, had a significant impact on electricity production and the supply of electrical power available for export. Volumes exported were well down from 2002, but due to significant price inflation, the value of exports increased substantially. It is likely that export volumes will increase in 2004, which means that unless prices fall significantly, the value of electricity exports may continue to rise.

Although exports of energy-related products have become very important to British Columbia, the forest sector is still the leading source of exported goods. The ongoing trade dispute with the United States regarding softwood lumber is probably the most significant issue affecting trade in the province. Attempts to come to a negotiated agreement have thus far been unsuccessful and Canada is continuing its challenges with both NAFTA and the WTO. The results of these challenges have so far been mixed, with both the United States and Canada claiming victory on most of the panel decisions, but the NAFTA panel findings on whether or not the Canadian industry caused injury to the American lumber industry were most certainly leaning in Canada's favour.

The panel remanded the issue back to the US International Trade Commission (ITC) with instructions to come up with a better methodology to support their argument. This is particularly important because if the panel finds there was no injury, the argument about whether or not Canada subsidized its lumber becomes moot. Without injury, the United States has no legal justification for implementing tariffs. Since the NAFTA panel's findings are binding, if in the end they do not find injury, the dispute will be over and Canada will have won. At this point, the ITC has rejected the panel's conclusions and maintains that their original calculations were correct. The NAFTA panel may once again reject the ITC's argument after which there may be yet another appeal; however, the likelihood is that this dispute should come to an end one way or another by the end of 2004. This will be good news for BC lumber producers, but in the meantime, they will still have to deal with the duties.

The softwood lumber dispute with the US continues to trouble BC lumber producers, but the dispute could be resolved by the end of the year

There is still a situation of oversupply in lumber, despite the record low interest rates that are driving up the number of housing starts on both sides of the border. If the US economy takes off sufficiently to induce the US Federal Reserve to boost interest rates, the demand for lumber could fall, further exacerbating the oversupply situation. There is also a potential supply increase coming online as companies try to salvage as much of the lumber burned in last summer's forest fires as possible, not to mention the continued effort to eradicate the pine beetle and salvage beetle-damaged timber. This does not bode well for significant price increases and with a stronger Canadian dollar and 27% duties to face, this puts BC lumber companies in a poor position. Unless the dispute with the US is resolved soon, it is unlikely that there will be significant growth in revenues from lumber exports.

On the positive side in the forest sector, 2004 may be the year that the fortunes of pulp and newsprint producers finally turn around. Pulp prices improved somewhat in 2003, but not as much as anticipated at the start of the year. The consensus forecast for 2004 is that pulp prices will rise, driven at least in part by demand from

China. Higher commodity prices should help boost the value of BC pulp exports. The outlook is even more positive for newsprint. As the US economy starts to take off, demand for newsprint should rise. Demand for newsprint and paperboard for containers is correlated with the business cycle, as advertising tends to rise when the economy is on a roll and an increase in goods shipped means that there is more demand for containers in which to ship them. The fact that this is an election year in both Canada and the United States will also increase advertising demand.

Demand for pulp and newsprint is up, which should lead to higher prices in 2004 and consequently, increased exports

Metals and mineral ores are another commodity group that should see a rebound this year. Prices for these goods are on the way up, once again driven by demand from China, particularly for copper and nickel. Metal prices have already been rising through the last half of 2003 and the expectation is for further price inflation through 2004. This should lead to an improvement in BC exports of these commodities and may even spur an increase in exploration, which could further increase exports in years to come.

The one mineral that may not see an increase in the value of exports is coal. With the closure of the Bullmoose mine in the northeast and the mergers occurring in the southeast, there has been a significant reduction in capacity, which means volumes of coal exported should fall; however, prices are expected to rise, which may lead to flat growth in revenues from coal exports.

The improving situation for metals may also help boost BC exports of machinery and equipment as demand for mining and energy-related equipment could rise. If housing starts continue to be strong, construction-related equipment should also be in high demand.

Higher commodity prices may also benefit the agricultural sector, but the BSE crisis will continue to be a drag on total agricultural exports. With the discovery of an infected cow in Washington State that was traced back to Alberta, the removal of trade barriers is unlikely. Although the cattle and beef industry represents a relatively small part of BC's total exports, it is significant for some regions of the province, and is certainly significant for other provinces, particularly Alberta.

The Outlook for Service Exports is Mixed

Rising commodity prices should offset any further appreciation of the Canadian dollar, but the higher dollar could still have a significant effect on exports of services. Data on exports of services, particularly with a provincial breakdown, is sparse; however, services are a significant BC export.

Tourism is one of the more high profile service exports from BC. Last year was a tough one for the BC tourism industry, as it had to deal with the effects of SARS, the war in Iraq and the spate of forest fires at the height of the summer tourist season. All this was compounded by the rapid appreciation of the Canadian dollar, which made it more expensive for Americans to visit Canada. While the rising Canadian dollar may not have been enough of a disincentive to dissuade the majority of American tourists, it probably did have an effect on the decisions of Canadians whether to take their vacations within Canada or travel south of the border. It is unlikely that the unfortunate confluence of disastrous events will be repeated in 2004, which alone should signal a better performance for tourism in BC. The improving American economy may also help boost tourism activity and the high profile given to Vancouver as forthcoming host of significant sporting events such as the 2010 Olympics and the 2006 World Junior Hockey Championship should make it a popular destination for tourists over the next several years.

With the problems that plagued the industry in 2003 out of the way, the BC tourism sector should see an improvement in 2004

Another high profile service export is the BC film industry. This is another industry that is possibly being harmed by the higher Canadian dollar, but on the positive side, many of the BC industry's competitors are also facing appreciation of their currency against the American dollar. Perhaps a greater impediment to the industry in BC is the proliferation of so-called "reality" television programs. These low-budget programs are affecting the production of made-for-TV movies and one-hour dramas, which have been a big part of the BC industry. However, feature film production has been steady in British Columbia. If the BC industry can continue to attract these big-budget feature films, they could offset the reduction in television production, but it is likely that there will not be substantial revenue growth in 2004.

A higher dollar and the effect that 'reality-TV' is having on other television production could cause problems for BC's film industry in 2004

One area that has been experiencing strong growth and likely will continue to do so in 2004 is exports of high technology services. The gross domestic product of high tech services reached its highest level ever in the third quarter of 2003.¹

Conclusion

The prospect of rising commodity prices and a more stable Canadian dollar should signal a turnaround for BC exports. Lower prices for energy may cool off that sector, but higher prices for pulp, newsprint and metals, combined with increased demand from the US and China should boost overall exports in 2004. If the softwood lumber dispute is settled soon, there could be significant growth, but more likely, growth will be modest.

¹ See: BC Stats, *High Tech Quarterly*, Third Quarter 2003.

**Recent Feature Articles in British Columbia Origin Exports Release
Listed By Statistical Reference Date of Issue**

03-12	<i>Rising Commodity Prices Could Signal Turnaround for BC Exports</i> (released February 2004)	02-09	<i>Canada Looking to Shed Light on Trade With the Dark Continent</i> (released November 2002)
03-11	<i>The Lows of High Tech Trade</i> (released January 2004)	02-08	<i>Canada's Share of US Softwood Lumber Market Slipping</i> (released October 2002)
03-10	<i>Is Global Free Trade Possible?</i> (released December 2003)	02-07	<i>FTAA: Free Trade for the Western Hemisphere?</i> (released September 2002)
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02-10	<i>Lumber Battle Takes an Unexpected Turn</i> (released December 2002)	01-07	<i>International Trade in High Technology Goods and Services</i> (released September 2001)

NOTES

Countries Included Within World**Regions:**

(1) Western Europe: United Kingdom, Ireland, Austria, Belgium, Denmark, Finland, France, Germany, Greece, Iceland, Italy, Luxembourg, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland.

(2) Eastern Europe: other Europe, including all of Russia, Georgia, Kazakhstan, Kyrgyzstan, Moldova, etc.

(3) South East Asia: Malaysia, Brunei Darussalam, Singapore, Myanmar, Kampuchea, Laos, Indonesia, Philippines, Thailand, Vietnam.

(4) Africa: continental Africa, excluding Ethiopia, Libya, Somalia, Sudan, Egypt.

(5) South America: continental South America from Colombia and Venezuela south to Chile and Argentina, including offshore islands, but not Caribbean.

(6) Central America and Caribbean: from Guatemala and Belize to Panama, plus Caribbean Islands.

(7) Pacific Rim (including Japan): Japan, Hong Kong, Malaysia, Brunei Darussalam, Singapore, Laos, Mongolia, China, Indonesia, North Korea, South Korea, Philippines, Macau, Taiwan, Thailand, Vietnam, Australia, Fiji, New Zealand.

(8) Pacific Rim: as above, but excluding Japan.

(9) Middle East: from Turkey and Iran south through the Arabian Peninsula. Excluding Afghanistan and Pakistan, but including Cyprus, Ethiopia, Egypt, Somalia, Sudan and Libya.

'Selected Value-added Wood Products'

category includes prefabricated houses, doors, windows, furniture, moulding, siding, etc. It does not include panel products, shakes, shingles or any pulp and paper products.

Revisions

Statistics Canada revises trade data for the previous three data years with release of the December data. The revision number is indicated in the footer of the tables (e.g., Rev 1 is the first annual revision, etc., and Prelim indicates it is the first release of data to December for that year). In addition to annual revisions, Statistics Canada revises the data for the previous data year every quarter (indicated in the footer by Rev Q1, etc).

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Dan Schrier - Trade Statistics**BC STATS**

P.O. Box 9410 Stn Prov Govt

Victoria, B.C.

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This service is provided through the Trade Research and Inquiry Package (TRIP) computer reporting system. TRIP offers user-defined tabulations of export or import statistics for British Columbia, Canada, the United States and other countries. Tabulations can include information on commodities, countries, U.S. states, years, months, mode of transport, etc.