

In terms of whether trade diversion exists, it is extremely difficult to isolate this particular economic effect, as in theory it assumes *ceteris paribus* conditions are met for variables such as exchange rates, growth rate differentials, inflation differentials, as well as micro considerations such as the extent of variety and the scale of production. In more recent work, Winters (1997) has suggested that neighbouring countries linked tightly to the EU economy could lose significantly from the latter's integration, but that for other countries the losses are likely to be very small.

Second, it is apparent that there was a long term decline in exports to the EU as a percentage of total exports over the period, with a over a 60 percent reduction in the proportion of exports to the EU as a proportion of the total value of exports. This secular decline appears to have largely occurred in the early 1980s and 1990s. On the import side, the trend is very different, with a growth in EU imports as a proportion of total Canadian imports to 1988, followed by a decline in EU import proportion to the early 1990s, and then little trend in the figures from 1992 to date. In other words, the total percentage of Canadian imports from the EU as a proportion of total imports has remained fairly constant over the period, but the proportion of Canadian exports to the EU to total exports has been in long-term decline.

Third, these trends are borne out by the export to GDP and the import to GDP ratios. Exports to the EU have declined over the period, with some rebound in 1995, but imports from the EU have remained roughly steady as a proportion of GDP. Clearly, imports from the EU are still an important component of foreign trade, but exports to the EU have been of declining importance. This must give some rise for concern, as there appears to have been little improvement in the trade imbalance with the EU, even with the Canadian currency at very competitive levels in world markets, and structural adjustments in response to the establishment of the NAFTA being supposedly completed since the recession of the early 1990s.

Table 2.2 shows nominal Canadian dollar trade values for exports from Canada to the EU, split down by product group, while table 2.3 shows nominal Canadian dollar trade values for imports from the EU to Canada, using the same format. Canadian exports and imports are recorded on a customs basis, but for exports the standard commodity classification is used, and for imports the harmonised commodity classification is used. Canadian exports appear to be concentrated in the areas of fabricated materials, inedible crude materials, food, feed, beverages and tobacco and most recently in aircraft and other equipment and tools. This reflects the widely reported export successes of the large Canadian beverage companies, telephone equipment companies and transportation manufacturers.

In table 2.3, EU imports appear to be less concentrated in specific areas, but the highest import categories by value are in the areas of fabricated materials, machinery, other equipment and tools and inedible crude materials. It is immediately apparent that imports from the EU are much more diversified among the classifications presented in the tables than are exports. One reason for this might be that the specialisation required to compete in the NAFTA bloc has caused Canada to orient its export production so as to concentrate in specific areas for the US market, but these areas, due to economies of scale, then become Canada's main areas of exports to the rest of the world. To shed some light on this, tables 2.4 and table 2.5 show the proportion of exports to the EU and imports from the EU in each category as a percentage of the total EU exports and imports.

In table 2.4 the export proportions for each product category show that the larger categories have declined in importance, whereas several smaller categories have shown significant growth. These categories are aircraft, other equipment and tools and to a lesser extent, communications and related equipment. This points to an emerging trend to export goods with a higher technical component to the EU.