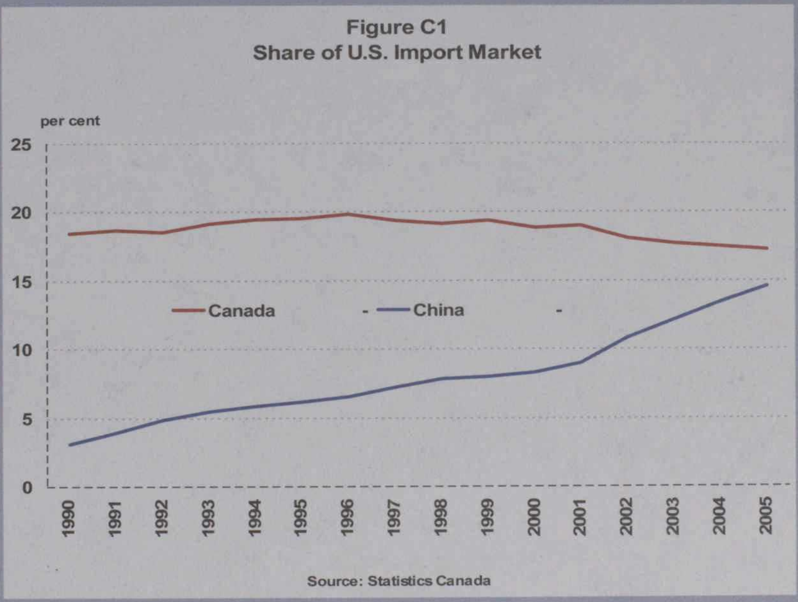
BOX C: CHINA–CANADA COMPETITION IN THE U.S. MARKET

Over the past few years, China has been growing at a very impressive rate. Since 1990, GDP has grown at an average annual rate of 9.4 per cent.[1] China's exports have been growing even faster, at an annual average growth of 18.1 per cent, over the same period. The emergence of China clearly offers many opportunities for Canada; exports to China have more than doubled over the past decade, from $3.4 billion in 1995 to $7.1 billion in 2005. Nevertheless, in addition to the expanding opportunities that China might offer, it can also pose challenges for Canada. With its dramatic growth in exports, particularly to the U.S., the question arises: is China a threat to Canadian exports?



Although China might offer competition to Canada in many of our export markets, of particular interest is the likely impact of the growth of China's exports to the United States. As most Canadians are aware, the U.S. consumes the majority of Canada's merchandise exports, just under 84 per cent in 2005. Canada has the great advantage of being next door to the largest consumer market in the world, and with NAFTA Canada has unparalleled access to this large dynamic and growing economy. Canada has been the largest trading partner of the U.S. for the past several decades, but this is likely to change. China's exports to the U.S. are surging, its share of the U.S. import market has sharply increased from 3.1 per cent in 1990 to 14.6 per cent in 2005, not far behind Canada's 17.2 per cent share (See Figure C1). Over the same period, Canada's share increased from 18.5 per cent in 1990 to 19.8 per cent in 1996, but then started a steady decline to 17.2 per cent in 2005. As a possible sign of things to come, for the first time ever in July of 2005 China surpassed Canada to be the largest supplier of U.S. imports for the month. Canada has since regained its lead, but this might not last.

Although China's market share in the U.S. has increased while Canada's has decreased, this does not necessarily mean China's gain came at Canada's expense. Trade is not a zero sum game; although Canada's share has been dropping, the total value of Canadian exports to the U.S. is continuing to increase, i.e. Canada has a smaller share of a larger pie. One question is whether Canada's exports would have increased at a greater rate without competition from China? In other words, the surge of Chinese exports to the U.S. squeezing out Canadian exports? A closer look needs to be taken to evaluate the threat of China's rising share of the U.S. market.

One of the basic economic theories explaining why countries trade is the theory of comparative advantage. Simply put, a country will export goods and services in which it has a lower opportunity cost in producing, or put another way, goods it is more efficient at producing than is the case for other countries. On the other hand, a country will import goods and services it has a relative disadvantage in, since it will cost less to import than to produce itself. Therefore China and Canada should export goods and services to the U.S. in

[1] There has been some debate over the accuracy of China's GDP figures. Critics have argued that over some periods the growth in China's GDP has been over or underestimated by official Chinese Statistics. See Rawski (2001), "What's Happening to China's GDP Statistics?" China Economic Review, Vol 12.4.