

Trade and Investment Highlights

Goods Exports Reach Their Lowest Level Since the End of 2001

Exports of Canadian goods and services declined 17.9% in the second quarter (Figure 1). Merchandise exports fell to their lowest level since the fourth quarter of 2001. Their 18.3% slide was accompanied by a 15.1% decline in services exports. Imports of goods and services fell 16.7%, reflecting a 17.6% decline in commodity imports and a 12.2% drop in services imports. Hit by falling energy prices, energy exports declined by more than 50% compared with the previous quarter, when energy prices were on the rise (Figure 2). Exports of agricultural products, hampered by the discovery of BSE in a single animal, declined 23.1%. Exports of automotive parts were at their lowest level since the first quarter of 2001, while exports of forestry products slumped to their lowest level in more than 10 years.

Reduced imports of aircraft and parts as well as of automotive products were the main contributing factors in the decline in merchandise imports. Merchandise exports to the United States fell by 18.5%, or \$17.5 billion, in the quarter. All major markets, with the exception of "other OECD countries" (other than the U.S., the EU and Japan), experienced a decline in goods exports. Merchandise imports from the U.S. also fell substantially, down 19.5% or \$13.3 billion. Commodity imports from all other major markets—with the exception of Japan—declined.

With goods exports declining faster than imports, the merchandise trade balance narrowed \$3.9 billion in the quarter to \$59.2 billion. A \$4.2 billion decline in the merchandise trade balance with the U.S. and a \$1.2 billion reduction in the balance with Japan were only partially offset by improvements in the goods trade balance with the EU and other OECD countries.

Both Exports and Imports of Services Decline

Services exports fell 15.1% in the second quarter, primarily due to declines in travel (down 46.8% or \$2.3 billion). A number of factors contributed to the reduction in travel and travel spending, including the war in Iraq and concerns about SARS (Figure 3). Exports of transport services were also down—by 24.0% or \$928 million—as a result of reduced levels of trade. The declines were limited by increased exports of commercial services (up 9.6% or \$684 million).

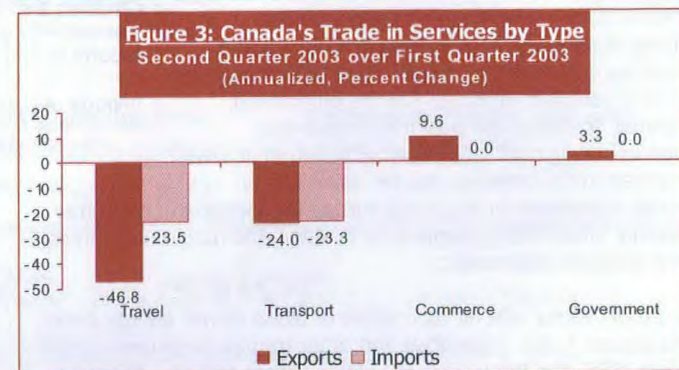
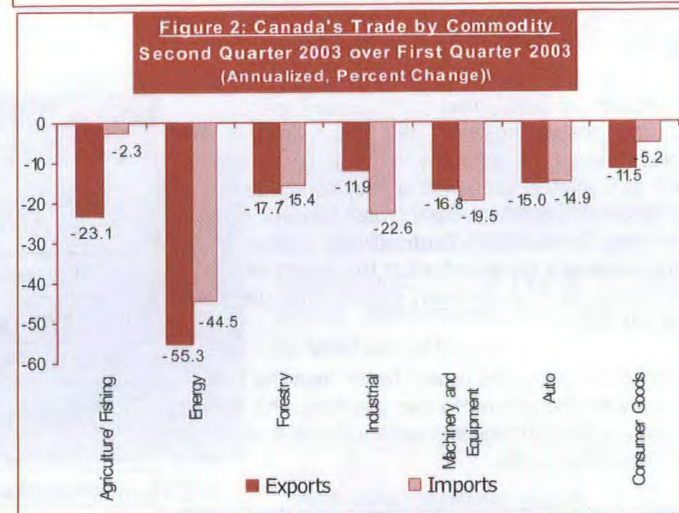
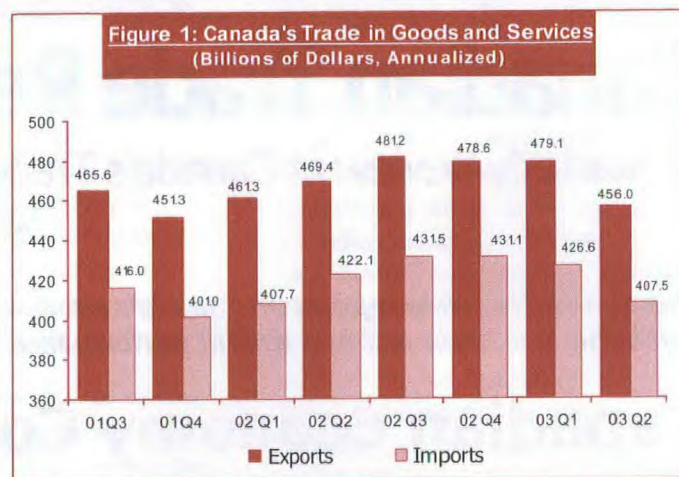
Services imports also fell in the second quarter. But at 12.2%, the decline in services imports was somewhat slower than the rate of decline in services exports. Like services exports, the declines in services imports were concentrated in travel services (down 23.5% or \$1.2 billion) and transport services (down 23.3% or \$928 million), whereas imports of commercial and government services remained at levels comparable to the previous quarter.

Because services exports declined at a somewhat more rapid rate than services imports, the services trade balance widened slightly to \$10.7 billion in the second quarter from \$10.6 billion in the previous quarter.

Inward Investment Flows Exceed Outward Flows

Canadian direct investment abroad (CDIA) was \$2.8 billion in the second quarter of 2003—down from the \$8.7 billion recorded in the second quarter in 2002. All sectors experienced a downturn in CDIA, with the exception of a small increase for the service & retail sector. Declines were particularly pronounced in the energy and finance & insurance sectors. Regionally, the declines were concentrated in the EU (down \$5.0 billion) and non-OECD countries (down \$0.7 billion). CDIA into the U.S. was down only marginally.

Foreign direct investment (FDI) flows into Canada amounted to \$5.1 billion in the second quarter of 2003—down from \$7.3 billion in the same quarter a year earlier. Most of the decrease in FDI flows occurred in the energy (down \$1.4 billion) and service & retail (down \$1.0 billion) sectors, while the machinery & transport sector registered a \$0.8 billion increase.



Source: Statistics Canada

The reductions stemmed primarily from declines in FDI from the EU (down \$1.4 billion), the U.S. (down \$0.4 billion) and Japan (down \$0.3 billion). Overall, inward flows exceeded outward flows by \$2.3 billion in the second quarter, a reversal of the situation in the same quarter the previous year when CDIA exceeded FDI by \$1.4 billion.

Canada Draws Down on Its Official International Reserves

Canada reduced its official reserves of assets in the second quarter of 2003 by \$0.2 billion, compared with a \$1.5 billion increase in the same quarter in 2002.

Economic Changes in U.S. Regions Between 1989 and 2001

Canada shares geographical proximity, a largely integrated production system and a comprehensive free trade agreement with the United States. These factors, coupled with strong U.S. demand for Canadian exports, have worked in favour of Canada selling relatively more and more of its output to the United States. However, U.S. demand for Canadian products differs from region to region and has been evolving over time. For example, an earlier feature article in the *Review* (Third Quarter, 2002) showed that increasing shares of Canadian exports were going to the U.S. West and South, at the expense of exports to the Northeast and Midwest. Regional and state disparities in economic growth and prosperity might be one explanation for these shifting trade patterns.

This special feature analyzes economic changes in U.S. regions between 1989 and 2001, the latest year for which data on gross state product (GSP) are available.¹ Table 1 provides an overview of the average annual growth rates in GSP, arranged by subregional and regional classifications. For the United States as a whole, GDP grew at an annual average rate of 3.0% over the period.

The data in Table 1 reveal considerable differences in growth rates over the past decade or so, even at the subregional level. For example, the state with the highest growth rate (6.0%) over 1989-2001 was Nevada, in the Far West subregion. Alaska, in the same subregion, experienced the lowest rate of growth. GSP in Alaska was actually shrinking by an average 1.1% over the period.

If we use a standard of ± 2 percentage points from the national average growth rate to designate well performing and poor performing states, then well performing states would include Nevada, Oregon, Arizona, Idaho, New Mexico,

Colorado and Utah, while poor performing states would be restricted to the District of Columbia, Hawaii and, of course, Alaska.

The remainder of this special feature will concentrate on the regional and subregional levels to complement the findings published in the earlier *Review* article.

Average Annual Growth by Region

Of the four principal, or macro, U.S. regions, real regional state product² was led by the South and the West, which at 3.6% and 3.4%, respectively, registered growth rates exceeding the national average (Table 1). On the other hand, the rates for

Table 1: Average Annual Growth in Real Gross State Product (chain index 1996=100), 1989-2001

	Average Annual Growth 1989-2001	Difference from National Average		Average Annual Growth 1989-2001	Difference from National Average
UNITED STATES of AMERICA	3.0%	N/A	SOUTH REGION	3.6%	0.6%
NORTHEAST REGION	2.3%	-0.7%	<i>Southeast Subregion</i>	3.2%	0.2%
<i>New England Subregion</i>	2.5%	-0.5%	Alabama (AL)	2.6%	-0.4%
Connecticut (CT)	2.2%	-0.8%	Arkansas (AR)	3.2%	0.2%
Maine (ME)	1.6%	-1.4%	Florida (FL)	3.4%	0.4%
Massachusetts (MA)	2.7%	-0.3%	Georgia (GA)	4.4%	1.4%
New Hampshire (NH)	3.9%	0.9%	Kentucky (KY)	3.0%	0.0%
Rhode Island (RI)	2.2%	-0.8%	Louisiana (LA)	1.5%	-1.5%
Vermont (VT)	2.5%	-0.5%	Mississippi (MS)	2.7%	-0.3%
<i>Mideast Subregion</i>	2.2%	-0.8%	North Carolina (NC)	3.5%	0.5%
Delaware (DE)	3.2%	0.2%	South Carolina (SC)	3.1%	0.1%
District of Columbia (DC)	0.9%	-2.1%	Tennessee (TN)	3.5%	0.5%
Maryland (MD)	2.1%	-0.9%	Virginia (VA)	2.8%	-0.2%
New Jersey (NJ)	2.3%	-0.7%	West Virginia (WV)	1.8%	-1.2%
New York (NY)	2.2%	-0.8%	<i>Southwest Subregion</i>	4.3%	1.3%
Pennsylvania (PA)	2.2%	-0.8%	Arizona (AZ)	5.8%	2.8%
MIDWEST REGION	2.8%	-0.2%	New Mexico (NM)	5.5%	2.5%
<i>Great Lakes Subregion</i>	2.7%	-0.3%	Oklahoma (OK)	2.3%	-0.7%
Illinois (IL)	2.9%	-0.1%	Texas (TX)	4.2%	1.2%
Indiana (IN)	2.9%	-0.1%	WEST REGION	3.4%	0.4%
Michigan (MI)	2.2%	-0.8%	<i>Rocky Mountain Subregion</i>	5.0%	2.0%
Ohio (OH)	2.4%	-0.6%	Colorado (CO)	5.4%	2.4%
Wisconsin (WI)	3.3%	0.3%	Idaho (ID)	5.5%	2.5%
<i>Plains Subregion</i>	3.0%	0.0%	Montana (MT)	2.6%	-0.4%
Iowa (IA)	2.9%	-0.1%	Utah (UT)	5.3%	2.3%
Kansas (KS)	2.7%	-0.3%	Wyoming (WY)	2.5%	-0.5%
Minnesota (MN)	3.5%	0.5%	<i>Far West Subregion</i>	3.1%	0.1%
Missouri (MO)	2.5%	-0.5%	Alaska (AK)	-1.1%	-4.1%
Nebraska (NE)	3.1%	0.1%	California (CA)	2.9%	-0.1%
North Dakota (ND)	2.8%	-0.2%	Hawaii (HI)	0.8%	-2.2%
South Dakota (SD)	4.0%	1.0%	Nevada (NV)	6.0%	3.0%
			Oregon (OR)	5.8%	2.8%
			Washington (WA)	3.9%	0.9%

Source: Real gross state product (GSP), Bureau of Economic Analysis, U.S. Department of Commerce, May 2003

1 All data are from the U.S. Bureau of Economic Analysis and refer to real GSP (i.e. nominal GSP deflated by a chained price index with 1996 = 100). Gross state product is similar to the concept of state gross domestic product on the income side except that it does not incorporate income and compensation paid to military and government personnel stationed outside the country.

2 The sum of individual real gross state products.