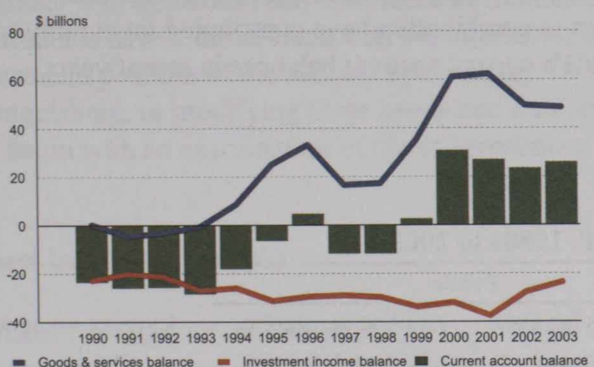
III. CURRENT ACCOUNT

The current account is one of the two major accounts that make up the balance of payments: the other is the capital account. The current account records the flow of goods and services between Canada and countries abroad. The capital and financial account, on the other hand, measures the short- and long-term capital flows between Canada and the rest of the world. Since the balance of payments must balance out at zero, the size of the surplus (deficit) in the current account is mirrored as a deficit (surplus) in the capital and financial account.

Canada recorded its fifth straight current account surplus in 2003, as the balance expanded $2.4 billion to $25.8 billion (Figure 3-1). The goods surplus rose $2.4 billion on the basis of imports falling faster than exports, while the services deficit widened $3.2 billion, as exports of services fell and imports rose. The deficit on investment income also narrowed by some $4.0 billion from a year earlier. Finally, rounding out the balances, the balance on current transfers fell $0.8 billion.

Figure 3-1

Current account balance and key components, 1990-2003



Regional analysis

The United States

Canada continues to run a surplus in its current account balance with the United States; this balance widened by $3.8 billion to $63.9 billion in 2003. A $5.6 billion narrowing of the bilateral investment income deficit was the principal reason for the advance. Profits accruing to Canadian direct investors in the U.S. shot up $3.7 billion while those accruing to U.S. holders of direct investment in Canada fell $0.4 billion to account for the bulk of the gains. The stronger Canadian dollar also likely contributed to a reduction in the deficit in portfolio investment income. This is because a large part of the Canadian securities owned by foreign portfolio investors are issued in US dollars, as is the interest paid on these securities (see Box B on the impact of the rising dollar, particularly the section dealing with debt holdings). In total, the deficit in portfolio investment income improved $0.9 billion as payments to U.S. investors fell $0.8 billion while remittances to Canadian portfolio investors were up by $0.1 billion.

The goods balance also contributed marginally to the improvement in the current account balance with the U.S. — a $15.6 billion decline in exports was slightly more than offset by a $15.7 billion decline in imports, resulting in a net contribution of $0.1 billion to the bilateral balance. However, the services deficit expanded by $1.6 billion as the travel deficit declined by $1.1 billion and the transportation balance fell $0.5 billion (and moved from a small surplus to a deficit position). These sectors were most likely negatively affected by the SARS outbreak in the Spring of 2003 and by the rising value of the Canadian dollar vis-à-vis the US dollar throughout the year. In fact, about 70 per cent of the decline in the travel deficit occurred in the second half of the year, when the dollar averaged nearly US 74.2¢ over July-December compared to a US 63.6¢ average for all of 2002.

The European Union

The current account with the European Union was relatively unchanged in 2003 from 2002, as the deficit narrowed $125 million to $15.1 billion. The goods deficit narrowed by $2.7 billion on the strength of a $1.3 billion increase in exports to the U.K., coupled with a $1.4 billion decrease in imports from the U.K. The goods trade balance with the rest of the EU edged down $75 million. However, offsetting the improvement to the goods balance were further deterioration to the services trade deficit (down $0.3 billion) and to the investment income deficit (down $2.4 billion).

Japan

The deficit in Canada's current account with Japan narrowed by $1.5 billion to $3.0 billion in 2003. The goods deficit contracted $0.7 billion to about three-quarters-of-a-billion dollars last year. Both exports to and imports from Japan were down — the former by $0.4 billion and the latter by $1.1 billion.

Similarly, the investment income deficit narrowed by $0.9 billion as income receipts were off by $0.1 billion and income payments were down by $1.0 billion. The reduction in payments is likely related to the stronger international value of the Canadian dollar, with Japanese investors likely holding Canadian securities issued in US dollars (see Box B on the impact of the rising dollar, particularly the section dealing with debt holdings).

Finally, the services deficit edged down $24 million to $491 million.