



I. MERCHANDISE TRADE

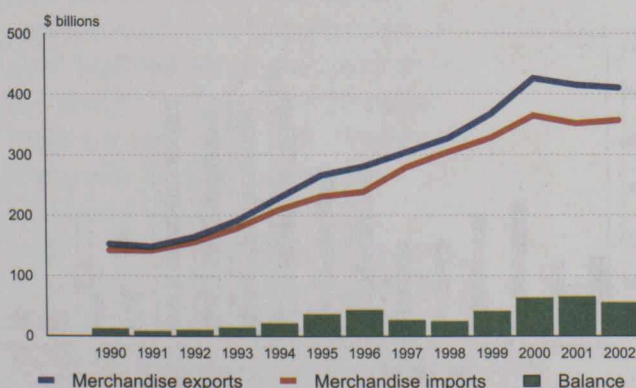
Merchandise trade is one, and in Canada's case, an overwhelmingly important component of the balance of payments, which also includes trade in services as well as direct and portfolio investment.

Overview

Over the first half of 2002, weaknesses in global financial markets and heightened uncertainty related to problems in corporate reporting and governance, particularly in the United States, fostered a softening in aggregate demand and raised uncertainties about the ability of the major developed economies to sustain their rates of economic expansion. Into the second half of the year, the threat of war in the Middle East helped raise oil price premiums; other aspects of geopolitical risks further prolonged the anaemic global recovery. The unfavourable external climate had an impact on Canada's merchandise exports as they fell for the second consecutive year, declining 1.0 per cent (\$4.3 billion) to \$410.3 billion. The declines were geographically widespread, led by declines to the U.S. (down 0.8 per cent, or \$2.9 billion), the European Union (down 4.9 per cent, or \$1.1 billion), and all other countries (down 1.8 per cent, or \$562 million). Only Canadian exports to Japan managed to increase last year (up 2.4 per cent, or \$226 million); the increase was not enough to offset the declines elsewhere.

Figure 1-1

Merchandise trade, 1990-2002

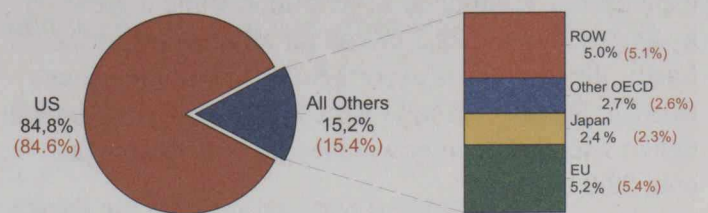


Notwithstanding the decline in exports to the U.S., that country remained Canada's principal export destination, accounting for some 84.8 per cent of Canada's merchandise exports. In fact, the share rose two-tenths of a percentage point last year. The EU (at 5.2 per cent) and Japan (at 2.4 per cent) together made up half of the remaining 15.2 per cent of Canadian exports, leaving the final 7.6 per cent to all other destinations.

The strong economic performance of Canada relative to the other developed countries during 2002 was reflected particularly in Canada's merchandise imports, which generated a 1.6 per cent (or \$5.5 billion) increase. With the exception of the United States, all other major regions posted gains; in particular, imports from all other countries jumped 7.3 per cent (or \$3.6 billion), those from Japan shot up 10.9 per cent (or \$1.2 billion), and imports from the EU rose 3.0 per cent (or \$1.1 billion). Merchandise imports from the U.S. edged down \$340 million to \$254.7 billion, a 0.1 per cent decline.

Figure 1-2

Merchandise export shares by region, 2001 and 2002



Black ink: 2002 shares
Red ink: 2001 shares

While the U.S. remains by far the principal supplier of merchandise imports into Canada, last year's combination of lower imports from the U.S. coupled with higher imports from all other sources led to the U.S. share in total Canadian merchandise imports falling — from 72.7 per cent in 2001 to 71.5 per cent in 2002. The EU share in total merchandise imports increased 0.1 per cent to 10.1 per cent while Japan's share reached 3.3 per cent, up from 3.0 per cent a year earlier. The share for the rest of the world jumped to 15.0 per cent last year from 14.2 per cent a year earlier.