Trade and Investment Highlights

Both Exports and Imports Expand in the First Quarter

Exports of Canadian goods and services increased by 12.1% in the first quarter, with merchandise exports expanding by 12.9% (see Figure 1 for levels). Imports of goods and services increased at a rate of 8.4%, with merchandise imports growing at a slightly faster pace of 8.8%.

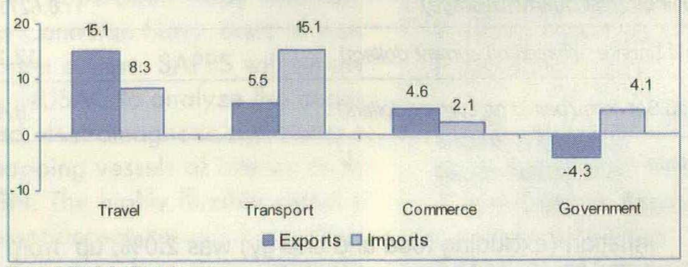
As is evident from Figure 2, shipments of energy and consumer goods experienced strong growth, while imports of forestry products, automotives and industrial products also expanded substantially.

Exports to the U.S. and to the EU—in particular to the U.K.—expanded, while shipments to all other destinations declined. Imports from the EU and Japan declined, while imports from the U.S. and other countries increased. As a result of exports expanding at a more rapid rate than imports, the trade balance improved in the first quarter—in particular with the U.S. and the EU.

Services Trade Deficit Expands

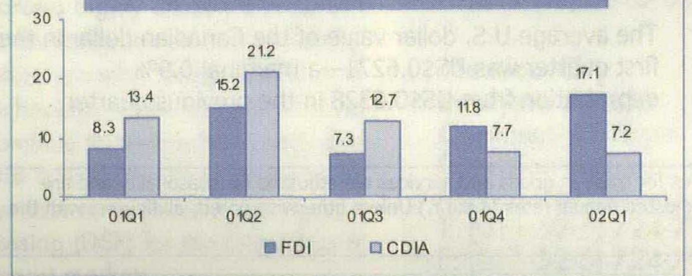
In the first quarter, a 6.2% increase in overall services exports led by travel was more than offset by a 6.3% increase in services imports (notably in travel and transport services). The net effect was a widening in the services deficit by $108 million to $6.0 billion. For details by type of services, see Figure 3.

Figure 3: Canada's Trade in Services by Type
First Quarter 2002 over Fourth Quarter 2001
(Annualized, Percent Change)



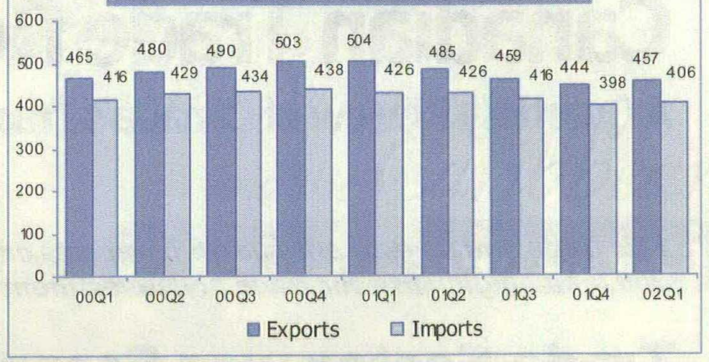
Source: Statistics Canada.

Figure 4: Foreign Direct Investment in Canada (FDI) and Canadian Direct Investment Abroad (CDIA)
(Billions of Dollars)



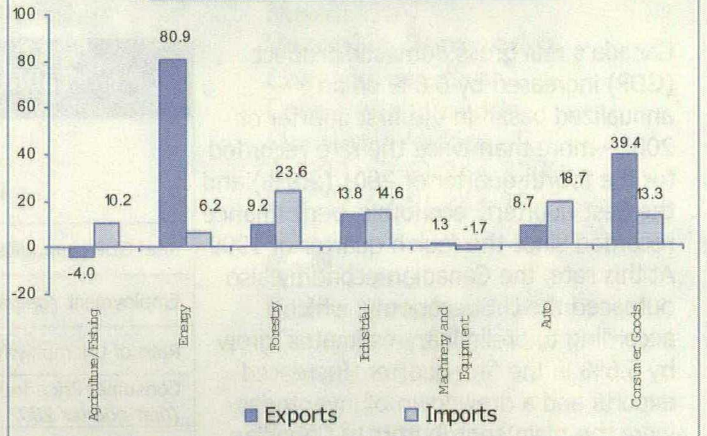
Source: Statistics Canada.

Figure 1: Canada's Trade in Goods and Services
(Billions of Dollars, Annualized)



Source: Statistics Canada.

Figure 2: Canada's Trade by Commodity
First Quarter 2002 over Fourth Quarter 2001
(Annualized, Percent Change)



Source: Statistics Canada.

Canada Attracts Inward Foreign Direct Investment

In comparison with the same quarter in 2001, the first quarter of 2002 recorded a doubling of inward foreign direct investment (FDI), which was heavily concentrated in the energy and minerals sector. The U.S. was the primary source country for this expansion, accompanied by the EU. Although outward FDI in the energy and minerals sector grew substantially, declines in all other sectors combined to reduce the level of outward FDI by half compared with the first quarter a year earlier. Outward FDI declined to all destination countries and regions.

Canada Adds to Its Official International Reserves

Canada added $0.7 billion to its official reserve assets in the first quarter of 2002, compared to $2.5 billion added in the same quarter in 2001.

CANADIAN TRADE REVIEW—FIRST QUARTER 2002

The Role of Imports in Canada's Economy

Overview

In today's world, the globalization of business, underpinned by increased international trade and investment, has compelled Canadian companies to embark on a wide-ranging effort at organizational and operational restructuring. Many, albeit not all, trade and investment barriers are gradually being dismantled, and the labour, capital and other advantages of one country or region are being combined with the technical and other strengths of another. The outcome is the creation of many new economic realities that, for the first time ever, are truly global in conception, administration and delivery. As part of this ongoing process of restructuring, businesses are often relying on imports to replace less efficient domestic suppliers and/or to increase intra-firm trade flows.

This special feature reviews the role of imports in the contemporary Canadian economy, with a particular focus on the role of imports as intermediate goods in Canada's exports.

At the most basic level, imports not only benefit the exporting country, they also provide benefits to the importing economy. For the Canadian consumer, for example, imports provide a greater variety of choice of products at more competitive prices. Canadian producers also benefit—from the use of imported parts or services as well as from the use of foreign machinery and equipment, which enables them to lower their costs. Thus, domestic producers are able to offer their products (final as well as intermediate goods) for sale more cost-effectively in the Canadian market or enhance their competitive position in international export markets.

Imports enrich the lives of Canadians and improve Canadian competitiveness in several ways. First, a major share of imports consist of final goods sold and consumed in the Canadian domestic market. For example, the demand for fresh fruits and vegetables by Canadian consumers over the winter months is largely met by imports.

Second, a large portion of imports consist of intermediate goods used as inputs in the processing and manufacture of goods and services in Canada. Goods and services generated in Canada encompass both final products and services intended for the consumer market and those intended as inputs for further processing. The two types of goods and services can in turn be destined for either the Canadian domestic market or export markets.

Third, certain imports consist of machinery and equipment, which are used by Canadian industry in the provision of final goods or services.

Imports thus are of significant benefit to our economy. Moreover, their role in Canadian economic activity has been on the rise for some time, as evidenced below:

- The ratio of imports of goods and services to GDP has increased from 18.0% in 1961 to 38.1% in the year 2001.
- The share of imports in the "apparent Canadian market" (i.e. net domestic shipments plus imports) has been on the rise over time and increases with the degree of processing.
- The share of imports in the "apparent market" for primary goods increased from 16.8% to 20.6% between 1965 and 1996. Primary goods are defined as agricultural, fishing, trapping, forestry, mining, crude oil and natural gas, and quarried products.
- The share of imports in the "apparent market" for manufactured goods jumped from 20.0% to 44.1% over 1965-1996.
- The share of imported inputs in the gross output of primary goods rose from 2.7% to 6.2% over 1965-1996, while for manufactured goods it increased from 10.0% to 23.1% over the same period.

What factors explain the ever larger role of imports in the Canadian economy? One contributing factor, as alluded to above, is the increasing sophistication of the Canadian consumer—both individual and industrial. Another factor is the decline in trade barriers, as epitomized by the outcome of various trade agreements, such as the Uruguay Round and the NAFTA. Yet another explanation might be the increased specialization, or fragmentation, of the production process across countries and regions. We examine this last explanatory factor in further detail below.

Vertical Specialization and the Import Content in Canadian Exports

Vertical specialization refers to the degree of specialization through the various stages of the production process as a good moves towards completion as a final product. For example, it takes many different manufacturers to produce the inputs needed for the assembly of an automobile—tires, chassis, seats, steering wheels and mirrors, to name a few. As mentioned above, the labour and other advantages of one country or region can be combined with the technical strengths of another to create new and different economic opportunities and modes of