

Choppy waters in the global economy are holding Quebec's exports in check

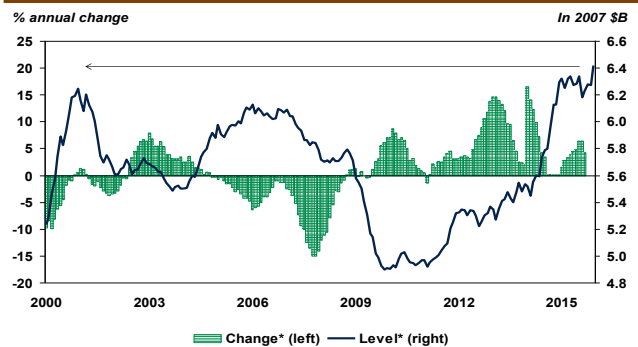
Quebec's international exports have made considerable progress in the past five years. Since touching bottom after the 2008–2009 recession, shipments abroad have recovered all the ground that was lost, and even hit a new peak in 2015 (graph 1). The province's international exports have now surpassed their former peak of the early 2000s, just before the bursting of the technology bubble and the U.S. recession of 2001, which together caused significant damage in Quebec. While shipments to the United States are maintaining their momentum (graph 2), those to the rest of the world are being affected by the economic slowdown in Asia and flagging demand from Europe. As a result, the increase in total shipments abroad has been stalling in the past several months. What is the outlook for 2016?

UNITED STATES: THE INCREASE IS NO LONGER ENOUGH

Our southern neighbour's economy has been gathering steam for two years now, with annual real GDP growth close to 2.5%. Imports by the United States even reached a growth rate of 5.0% last year. Naturally, this stimulated demand for Quebec products. For the second year in a row, the value of exports to the United States climbed by more than 10% in 2015 (graph 3).

The boom in exports to the United States has also coincided with the depreciation of the Canadian dollar (graph 4 on page 2). It stood in the neighbourhood of US\$0.90 in 2014, but its average value plunged to US\$0.78 last year. Since the beginning of 2016, the loonie has been hovering around

Graph 1 – Quebec's international exports peak at a high level



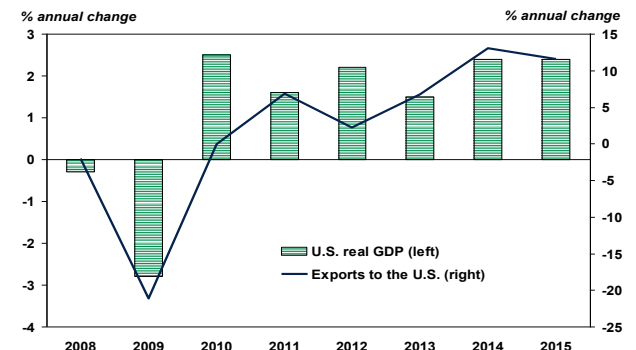
* Eight-month moving averages.
Sources: Institut de la statistique du Québec and Desjardins, Economic Studies

Graph 2 – Exports to the United States are still increasing, but those to the rest of the world are declining



* Eight-month moving averages.
Sources: Institut de la statistique du Québec and Desjardins, Economic Studies

Graph 3 – U.S. economic growth has been stimulating Quebec exports since 2010



Sources: Institut de la statistique du Québec, Datastream and Desjardins, Economic Studies

François Dupuis
Vice-President and Chief Economist

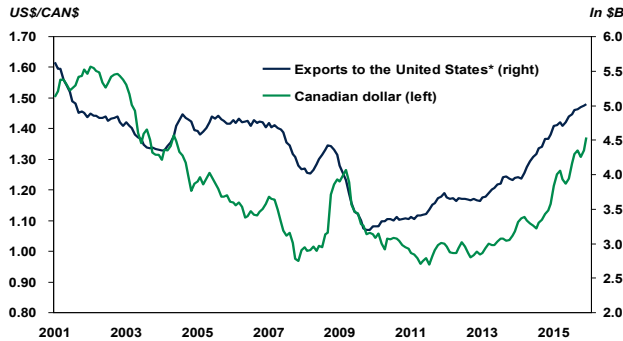
Hélène Bégin
Senior Economist

418-835-2450 or 1 866 835-8444, ext. 2450
E-mail: desjardins.economics@desjardins.com

NOTE TO READERS: The letters **K**, **M** and **B** are used in texts and tables to refer to thousands, millions and billions respectively.

IMPORTANT: This document is based on public information and may under no circumstances be used or construed as a commitment by Desjardins Group. While the information provided has been determined on the basis of data obtained from sources that are deemed to be reliable, Desjardins Group in no way warrants that the information is accurate or complete. The document is provided solely for information purposes and does not constitute an offer or solicitation for purchase or sale. Desjardins Group takes no responsibility for the consequences of any decision whatsoever made on the basis of the data contained herein and does not hereby undertake to provide any advice, notably in the area of investment services. The data on prices or margins are provided for information purposes and may be modified at any time, based on such factors as market conditions. The past performances and projections expressed herein are no guarantee of future performance. The opinions and forecasts contained herein are, unless otherwise indicated, those of the document's authors and do not represent the opinions of any other person or the official position of Desjardins Group. Copyright © 2016-, Desjardins Group. All rights reserved.

Graph 4 – The upturn in exports to the United States coincides with the depreciation of the loonie



* Eight-month moving average.
Sources: Institut de la statistique du Québec and Desjardins, Economic Studies

US\$0.70. The weakness of the Canadian dollar helps drive prices down; this can have a positive effect on our exports to the United States. However, most of the world’s major currencies also depreciated against the greenback in 2015. Consequently, Canadian and Quebec businesses have not necessarily managed to stand out from many competing countries as far as prices are concerned.

The effects of a weak currency seem to have reached their limit for supporting an increase in Quebec exports to the United States. Maintaining a weak loonie throughout 2016 will have less impact on international trade than last year’s collapse by the Canadian dollar. In any case, it is first and foremost the pace of the U.S. economy, rather than the value of the currency, that dictates the trend of Quebec’s exports to the United States. Given that U.S. real GDP growth is expected to hold steady at nearly 2.5% this year, shipments to that country should keep experiencing healthy growth.

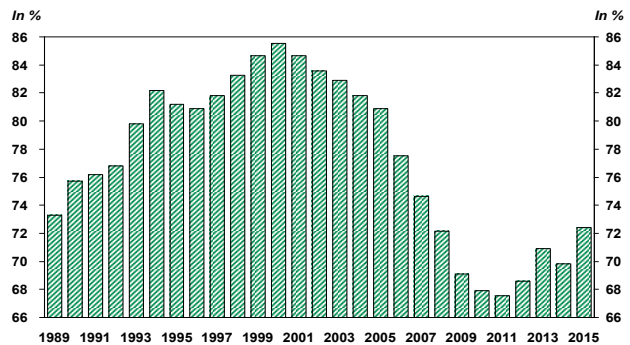
While the United States is still Quebec’s main customer, it now carries far less weight than it did 15 years ago. At the beginning of the 2000s, approximately 85% of shipments abroad were bound for the U.S. market. That share has gradually melted since then due to numerous situational and structural factors (table 1) that have undermined shipments of Quebec products. In the past few years, the United States share of Quebec’s exports has edged back up slightly (graph 5). But that share is as small as it was before the coming into force of the Canada–United States Free Trade Agreement in 1989. All of the gains recorded from the end of the 1980s onwards have rapidly dissipated, mainly due to fiercer competition from many countries with low production costs, such as China and Mexico. The data that are available for Canada clearly demonstrate this

Table 1 – Main causes of the decline in Quebec exports during the first 2000 decade

Factors	Situational	Structural
U.S. recession of 2001	x	
Bursting of the technology bubble of 2001		x
Rationalization of the forestry sector		x
Textile and clothing sector: elimination of import tariffs for many countries in 2002		x
Intensification of competition from Asia, especially China		x
U.S. recession of 2008–2009 and collapse of the residential real estate market	x	
Appreciation of the Canadian dollar from around US\$0.65 at the beginning of the 2000s	x	x

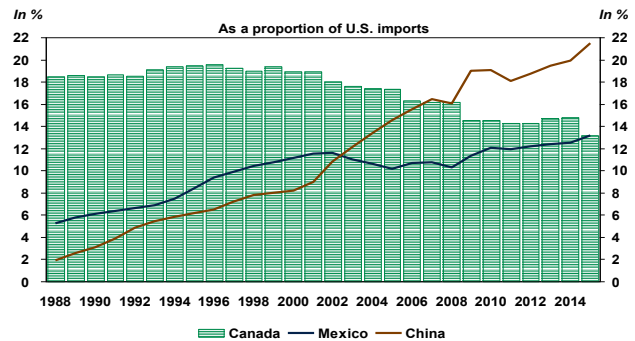
Source: Desjardins, Economic Studies

Graph 5 – The proportion of international exports bound for the U.S. is smaller than it was at the beginning of the 2000s



Sources: Institut de la statistique du Québec and Desjardins, Economic Studies

Graph 6 – The proportion of U.S. imports originating from Canada has never been so small



Sources: Bureau of Economic Analysis and Desjardins, Economic Studies

phenomenon,¹ which has also affected Quebec: the United States now has foreign suppliers larger than our local businesses (graph 6).

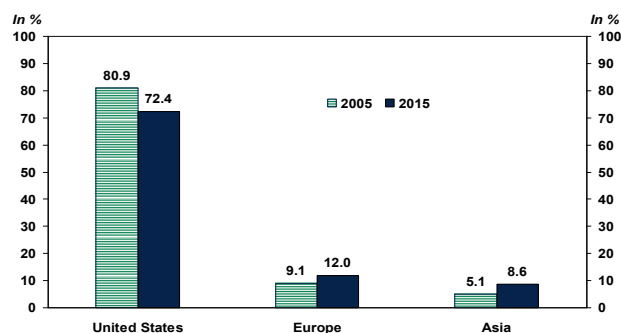
¹ Desjardins, Economic Studies, Economic News “Canada’s share in U.S. imports shrinks,” February 17, 2016.
<https://www.desjardins.com/ressources/pdf/nf160217-e.pdf>

WEAKNESS OVERSEAS

Europe and Asia have gained ground in Quebec's trade in recent years, thanks to efforts to diversify the province's export markets. Approximately 20% of Quebec's international exports are now headed for those two economies (graph 7). The value of shipments to Europe has increased of more than 3 billion dollars in the space of 10 years, while that of shipments to Asia has almost doubled during that period. The consequence of this is greater sensitivity to the economic well-being of those partners; this can be good news or bad, depending on the ups and downs of economic conditions. In 2015, the slowdown of the Asian economy, especially China, affected exports to that region. The sluggish conditions in many Old World economies led to a lack of growth in shipments to Europe last year.

It is far too early to hope for a boost from the signing of free-trade agreements. The agreement between many countries of America and many countries of Asia-Pacific region must first be ratified over the next two years. Canada will probably wait to see the outcome of the U.S. presidential elections in November 2016 before making a decision about the Trans-Pacific Partnership.² Therefore, this free trade zone will probably not come into force before 2017. Meanwhile, the Canada-European Union: Comprehensive Economic and Trade Agreement is still under discussion, delaying its signing. Canada's exporting firms will thus have to wait patiently to gain easier access to European and Asian markets. The other side of the coin is that our local firms will face stiffer competition in the domestic market, once the agreements with Asia and Europe come into force.

Graph 7 – Share of international exports held by the main trading partners



Sources: Institut de la statistique du Québec and Desjardins, Economic Studies

WHAT DOES 2016 HAVE IN STORE FOR US?

Given that U.S. real GDP growth will stay close to 2.5% this year, the value of shipments to that country should post similar growth in 2016, i.e. around 10%. Whether exports overseas will manage to rally this year is questionable. The Euro zone's real GDP should maintain a growth rate of 1.5%, while that of China will dip slightly to around 6.5%. A moderate increase in European demand combined with a slight growth in exports to Asia will, maybe, result in some improvement of shipments to those two trading blocks.

Generally speaking, the economic conditions of our main trading partners in 2016 will be fairly similar to those of last year. Even though considerable uncertainty currently exists in the global economy, the strong performance by the U.S. economy should enable exports to record growth. Let's hope that it will be enough to re-instate an upward trend in total shipments abroad over the course of 2016. Everything will depend on the European and Asian demand for our products.

Hélène Bégin
Senior Economist

² Colas, Moreira, Kazandjian, Zikovsky, "CMKZ International Trade Law Predictions for 2016," January 2016.
<http://cmkz.ca/en/cmhz-international-trade-law-predictions-for-2016/>