

ECONOMIC VIEWPOINT



The Diversification of Quebec's Exports Does Not Prevent Them from Slowing Down

Quebec benefited from the expansion period of its main trading partners in recent years. Shipments to the United States, the rest of Canada, Europe and Asia recorded solid growth. However, the recent economic difficulties in the country and the weakness of the European economy have already caused exports from Quebec to these two markets to slow in 2018. The slower rate of global real GDP will slow down Quebec's exports even more this year. Quebec has the advantage of being the most diversified among the Canadian provinces in terms of types of exports; this situation has generally softened the impact of any upheaval. Despite having the broadest geographic diversification in shipments abroad in recent years, Quebec remains vulnerable to changes in the economic situation of its main customers. Even if two major trade agreements came into effect lately, i.e., one between Canada and Europe, and another one between Canada and roughly ten Asia-Pacific countries, the impact is difficult to assess at this time. What is certain is that these two agreements will help increase Quebec's exports overseas in the coming years, resulting in even greater geographic diversification.

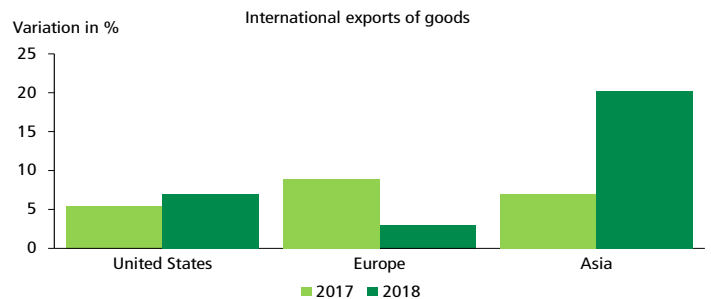
From Rapid Growth to a Loss of Speed

The favourable economic period in the major regions of the world has sustained Quebec's growth in international exports for the last two years. The value of shipments of goods to the major trade blocs increased, especially those to Asia, which jumped 20.2% in 2018 (graph 1). Growth in U.S. real GDP, which rose from 2.3% in 2017 to 2.9% in 2018, is reflected in the exports of goods to the United States. Exports to Europe lost some strength in 2018, as several economic difficulties affected the euro zone.¹ As a result, growth in exports to Europe slowed down from 8.9% in 2017 to 3.0% last year. Shipments to other destinations, i.e., elsewhere within the three main geographic areas, were also up in the last two years.

Still, the monthly change in exports makes it possible to better identify recent trends. The rapid growth in the global economy until mid-2018 led to the sustained rise in Quebec's international exports to the United States and elsewhere in the world. The situation changed quickly in the second half of 2018, as the shipments of goods from Quebec to foreign markets began to stabilize (graph 2 on page 2).

GRAPH 1

Value of Quebec exports according to main geographic areas



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

Quebec was not spared from the general slowdown in global trade, in part because of the U.S. tariffs imposed on specific products from more than ten countries, in particular China and Canada, as well as the European Union. Later, the retaliatory measures also weakened real GDP growth around the world. Quebec's international exports were not able to avoid this widespread slowdown. Although the shipments of goods to the United States and Europe have been flat over the last

¹ *Euro Zone: An Alarming Slowdown*, Desjardins, Economic Studies, *Economic Viewpoint*, March 28, 2019, 5 p.

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GRAPH 2
Exports from Quebec to the United States and elsewhere in the world have stabilized in recent months



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

GRAPH 3
Exports from Quebec to Europe are fairly stable, but those to Asia are rising rapidly



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

few months, those to Asia have been booming since last year (graph 3).

Exports to China rose sharply in 2018, growing 27.5%. The trade tensions between China and the United States, which led to tariffs being imposed on a number of products between the two countries, helped sourcing from Canada. For example, the value of soybean shipments from Quebec to China more than tripled in the space of a year. Still, this boom could prove to be short-lived if the tariffs are abolished as the result of a possible trade agreement.

Overseas Exports Are Gaining Ground

Even if Quebec’s exports to Europe have slowed in recent months, they are taking up a greater share of shipments abroad. The upward trend started well before the Comprehensive Economic and Trade Agreement (CETA) between Canada and Europe came into effect on September 21st, 2017.² The positive effects on Quebec exports have yet to be felt, as the economic slowdown in Europe has created some confusion. In any case,

² *Canada–European Union Comprehensive Economic and Trade Agreement: An overview of the agreement, trade and advantages*, Desjardins, Economic Studies, *Economic Viewpoint*, April 22, 2015, 20 p.

the impact of a new trade agreement is rarely immediate. The benefits should be felt more in the coming years, given the time it will take for exporters to target new customers and link up with European distribution chains.

Asia also carries more weight now than it did few years ago, since the increase in exports is clearly higher than the increase in exports to Europe (graph 4). Considering the rapid economic growth of many countries in Asia that are continuing to develop, the number of business opportunities appears to be higher in this part of the world. In addition, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) between Canada and roughly ten countries in Asia and South America offers new export opportunities for Quebec since coming into effect in the spring of 2018³. The member countries account for nearly 15% of global GDP, which is huge considering China is not a part of this free-trade zone. It is difficult to assess the impact one year later, since the rapid rise in exports from Quebec to Asia since 2018 is largely due to China. The withdrawal of the United States from CPTPP prior to it coming into effect gave Canadian exporters a leg up due to the lack of tariffs between the signatories.

GRAPH 4
Share of shipments from Quebec to Europe and Asia



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

The U.S. Market Is Less Dominant

The geographic diversification of Quebec’s exports among the major economic blocs has increased in recent years. Over the last five years, the value of the goods exported to Europe and Asia has risen approximately 50%, i.e., at a rate far greater than that of exports to the United States (table 1 on page 3). The market share of each of these two areas—currently at around 10% (graph 5 on page 3)—has increased to the detriment of our neighbours to the south. The proportion of international exports from Quebec to the United States has dropped below 70% after peaking at roughly 85% in the early 2000s (graph 6 on page 3).

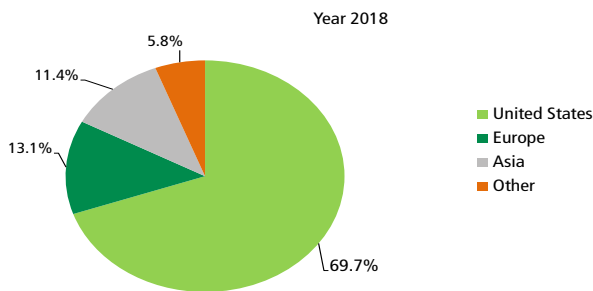
³ *The New Trans-Pacific Partnership: Smaller, but Just as Ambitious*, Desjardins, Economic Studies, *Economic Viewpoint*, March 16, 2018, 4 p.

TABLE 1
Exports from Quebec to Europe and Asia are growing faster than those to the United States

International exports of goods			
	UNITED STATES	EUROPE	ASIA
Level in \$B			
2013	46.9	7.9	7.1
2018	64.3	12.1	10.5
Variation in %			
2013-2018	37.3	53.3	48.6

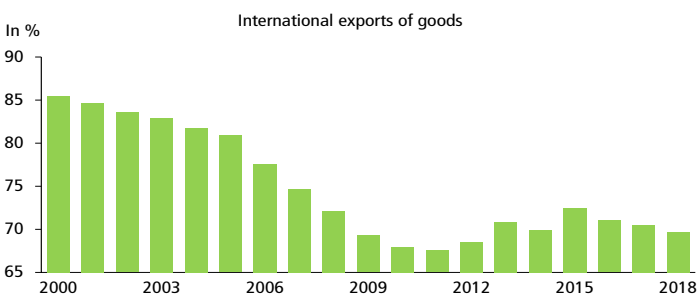
Sources: Institut de la statistique du Québec and Desjardins, Economic Studies

GRAPH 5
Share of international exports from Quebec according to destination



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

GRAPH 6
Share of shipments from Quebec to the United States



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

For now, China is the second most important country in terms of Quebec's international exports after the United States. And then there are Mexico, France and Germany (table 2). Besides the U.S. market, shipments abroad from Quebec are fairly well diversified among different countries.

TABLE 2
Exports of goods from Quebec to the ten main countries

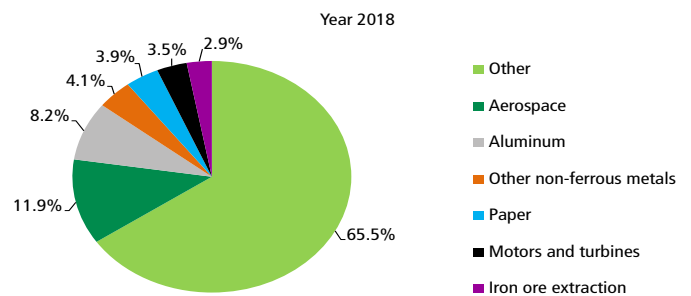
COUNTRY	\$B	2018	
		Total % of all countries	Annual variation in %
1. United States	64.3	69.7	7.0
2. China	3.6	3.9	27.5
3. Mexico	2.1	2.3	19.1
4. France	1.6	1.8	-3.1
5. Germany	1.6	1.7	20.5
6. Japan	1.6	1.7	16.5
7. Netherlands	1.5	1.6	40.2
8. United Kingdom	1.2	1.3	-9.4
9. South Korea	1.2	1.3	32.8
10. Switzerland	1.2	1.2	5.9

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

Aerospace at the Forefront

From a sectoral point of view, exports are distributed among many industries, thereby reflecting a highly diversified economy. Furthermore, Quebec is the most diversified of all of the Canadian provinces.⁴ Nonetheless, it is the aerospace sector that weighs heaviest at 11.9% of the total value of international exports in 2018 (graph 7). Many businesses of all sizes in Quebec supply parts to such major buyers as Bombardier, Boeing and Airbus. They are part of the global supply chain, which is crucial to ensuring the growth of this kind of industry. However, the fact that the C Series now lies in the hands of Airbus, which renamed the aircraft, may, over time, jeopardize the link of some parts manufacturers in Quebec in the chain.

GRAPH 7
Share of international export of goods from Quebec according to the main industries

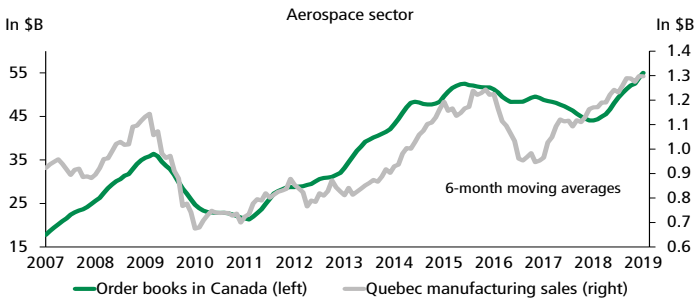


Sources: Institut de la statistique du Québec and Desjardins, Economic Studies

The aerospace industry, which has been posting strong growth since 2017, has benefited from the global expansion cycle. The economic slowdown currently underway will probably not spare Quebec's number one exporting industry, but a drop in deliveries like the one seen during the 2008–2009 recession is unlikely. For

⁴ *Canada's International Trade Facing Numerous Challenges*, Desjardins, Economic Studies, *Economic Viewpoint*, May 3rd, 2019, 4 p.

GRAPH 8
The aerospace sector sends positive signals for Quebec exporters



Sources: Statistics Canada and Desjardins, Economic Studies

now, deliveries of aerospace manufacturers in Quebec are on the upswing, and order books across Canada are full (graph 8).

Aluminum Ranks Second

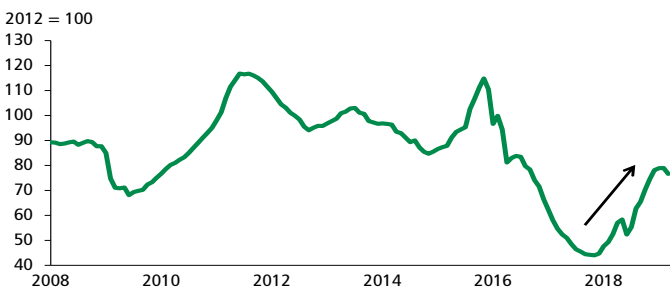
Aluminum is also an important part of Quebec’s industrial fabric. This sector ranks second with 8.2% of the total value of international exports in 2018. Shipments of aluminum grew rapidly in 2017, but several pitfalls have since caused them to stagnate. The imposition of U.S. tariffs and the lockout triggered by a major aluminum plant in Quebec complicated things last year.

Beginning in May 2018, the United States imposed a 10% tariff on Canadian aluminum products and 25% on steel products. Canada retaliated in July 2018 by imposing similar tariffs, yet the United States remain our main export market. Prior to the tariffs being implemented, more than 90% of Quebec’s aluminum exports headed to the U.S. market compared to 60% for steel.

Consequences of the U.S. Tariffs

The imposition of tariffs on aluminum from Quebec artificially allowed U.S. factories to become more competitive. While production in the United States has been in free fall since 2016, it has gone up a little since the tariffs were introduced (graph 9).

GRAPH 9
United States: primary aluminum production on the upswing



Sources: Datastream and Desjardins, Economic Studies

As long as these remain in place, U.S. factories can produce more to encourage buying locally while lowering the prospects somewhat for factories in Quebec. The value of aluminum exports to the United States fell 5% last year. Aside from the tariffs, the lockout triggered at ABI in January 2018 also contributed to reducing production in the province and, as a result, exports. It is difficult to isolate the negative impact of the tariffs under these circumstances.

However, exports of aluminum to the rest of the world (anywhere but the United States) rose sharply in 2018, a sign that Quebec was able to direct its output to other markets. All in all, aluminum exports to all countries remained stable in 2018, (table 3), and the outlook remains uncertain. As long as the U.S. tariffs remain in place, access to our main export market will be limited. If global demand slows too much, it will certainly not help the return to growth. Despite the 25% tariffs on steel products, exports to the United States and other countries increased at a similar rate in 2018. Still, this sector is far less important than the aluminum sector in terms of the value of shipments abroad.

TABLE 3
Value of international aluminum exports to the United States down in 2018, but up for steel

QUEBEC	PRODUCTION AND PROCESSING OF ALUMINUM* VARIATION IN %		STEEL INDUSTRY VARIATION IN %
	2017	2018	2018
United States	24.8	-5.0	7.8
Rest of world	-6.2	74.5	8.3
TOTAL	22.0	0.6	8.0

* Start of the ABI aluminum plant lockout on January 11, 2018.
Source: Statistics Canada, Institut de la statistique du Québec and Desjardins, Economic Studies

CUSMA or NAFTA?

The new trade agreement between Canada, the United States and Mexico (CUSMA) has yet to be ratified after the initial signing last fall. The elimination of the tariffs on steel and aluminum, which are not part of CUSMA, could compromise the agreement coming into effect. Behind the scenes, Canada and Mexico are aiming to have this obstacle to trade removed before the new agreement can be ratified. The federal elections held in the fall of 2019 may also delay things as the approval of the U.S. Congress is not a given.

Of course, the North American Free Trade Agreement (NAFTA) is still in effect, and the free trade of almost all products continues. Remember that President Donald Trump described NAFTA “as perhaps the worst trade deal ever made.” If ratification of CUSMA is delayed, it is possible that tariffs would be applied to other Canadian products, and Quebec exporters would be

penalized. The more time goes by, the greater the risk. Therefore, the outlook for shipments to the United States remains uncertain. Nonetheless, we are still assuming that CUSMA will be ratified and that new tariffs will not be introduced. Aside from this issue, the slower pace of the U.S. economy expected this year, like that of the global economy as a whole, will put the brakes on Quebec's international exports.

Exports to the Rest of Canada

Even if exports abroad tend to be in the spotlight, exports from Quebec to the other provinces are also important. In 2018, approximately 40% of the goods and services exported were directed at the rest of Canada (graph 10). This figure has been growing steadily over the last few years. Even if the details for each province and each product are not available, a few observations can be made.

GRAPH 10
Exports from Quebec to the rest of Canada are significant



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

Exports of goods and services to the other provinces grew 2.2% in real terms in 2018, down from the 6.0% recorded in 2017 (graph 11). The economic slowdown of the country, mostly due to weak domestic demand, affected Quebec exports.

Not as Strong in the Short Term, but No Drop in Sight

Quebec enjoys closer trade ties with Ontario, which shares a similar industrial structure. Approximately 60%⁵ of Quebec's exports to the rest of the country are aimed at this province. Given that the Canadian and Ontario economies will continue to slow, exports from Quebec to the other provinces will rise more slowly this year, i.e., by 1.7% in real terms.

Roughly 60% of Quebec's exports in goods and services were directed at other countries. Their volume was up 3.7% in 2018. The pace is expected to slow to 3.1% in 2019 due to the slower growth of the global economy, especially among Quebec's main trading partners, i.e., the United States, Europe and Asia. Quebec's exports are already losing steam despite the greater geographic diversification from a few years ago. When

⁵ According to the most recent estimate available (2015).

GRAPH 11
Exports from Quebec to the other provinces: a more modest hike in 2018 than in the previous year



* In 2012 \$B.
Sources: Institut de la statistique du Québec, Statistique Canada and Desjardins, Economic Studies

the economic cycles of the main areas around the globe are synchronized and a slowdown occurs, exports inevitably suffer the repercussions.

Canada's free trade agreements with Europe and some of the Asia-Pacific countries will have an impact over time and make Quebec's exports even less vulnerable to the U.S. market. Failing ratification of CUSMA any time soon, exporters risk going through a period of upheaval, even if NAFTA remains in effect. Everything will depend on the mood of our neighbour to the south. Still, increased geographic diversification of export markets and distribution based on products—which is already greater than in the rest of the country—represent major assets for Quebec.

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