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**TRADING WITH CANADA:
THE IMPACT OF THE U.S./CANADA FREE TRADE AGREEMENT
ON NORTH AMERICAN AGRICULTURE**

by

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TRADING WITH CANADA:
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ON NORTH AMERICAN AGRICULTURE*

C. Ford Runge**

This paper provides a brief overview of the U.S./Canada Free Trade Agreement (FTA) and its relationship to North American agriculture. It first outlines the agreement, and discusses its linkages to the continuing resolution of the Uruguay Round of negotiations under the General Agreement on Tariffs and Trade (GATT). It then considers the relative competitiveness of several selected food processing industries which are heavily dependent on Canadian marketing boards. It concludes with responses to a variety of questions concerning specific implications for various agricultural producers and processors.

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Key Agricultural Provisions of the FTA

The FTA took effect on January 1, 1989. It calls for the elimination over 10 years, or by January 1, 1998, of all import tariffs. Some agricultural tariffs were eliminated effective immediately, while others are scheduled for phase-out over 5 and most over 10 years. An annual review by the U.S. and Canada is scheduled to see if those tariffs scheduled for 5- or 10-year phase out might be accelerated. This tariff acceleration led to speeded-up elimination of \$200 million worth of tariffs on 27 agricultural items on April 1, 1990.

Canada's import-licencing requirement for wheat, barley and related products are to be eliminated whenever, for each grain, U.S. support levels are at parity with Canadian support levels, based on the producer subsidy equivalent (PSE) measure. A "safeguard" provision allows either country to impose or reimpose import restrictions. In 1989, oats support levels came into alignment, and import licensing for oats and oat products was eliminated. Recent Canadian calculations of the wheat levels of support suggest that import licenses might also be eliminated for wheat sometime during 1991. In the grains area, Canada has ended the so-called "Crows Nest" transportation subsidy for farm products shipped to the U.S. through Western ports. This move primarily effects millfeeds and canola seed.

Both countries agree under the FTA not to use export subsidies for agricultural products exported to one another, or to sell through public entities at below cost. Both are to consider the "export interests" of the other when subsidizing exports to third countries.

Under the FTA, Canada raised its global import quota for poultry, eggs

and egg products.¹ Both countries have exempted each other from quantitative meat import restrictions. A "snapback" provision to remain in effect for 20 years from 1989 allows either country to increase tariffs on selected fruits and vegetables if the market undergoes specific changes. Nine technical working groups were established to harmonize regulations and standards in animal and plant health, food safety, seeds, fertilizers, pesticides, and packaging and labeling.

Perhaps one of the most important provisions of the FTA was to establish a bilateral dispute resolution mechanism -- panels that can arbitrate disputes according to the relevant GATT articles. However, both countries are allowed to retain countervailing duties and antidumping laws, which are permissible under GATT. A final detail is that the U.S. does not restrict imports from Canada of goods containing 10 percent or less sugar by dry weight.

The FTA and GATT

Perhaps the most notable aspect of the FTA is the extent to which it relies on the larger structure of the GATT to fully deal with agricultural issues. The Uruguay Round of multilateral trade negotiations, begun in 1986, was to have concluded in December 1990. However, the talks broke down when the European Community, together with South Korea and Japan, rejected a final compromise proposal for agriculture. This proposal, the so-called "Hellstrom compromise," was named after the Swedish minister of agriculture and head of the agricultural negotiating group. It called for

¹The new quotas as a percentage of domestic production are 7.5 percent for chicken/chicken products, 3.5 percent for turkey/turkey products, 1.647 percent for shell eggs, 0.714 percent for frozen, liquid and further processed eggs, and 0.627 percent for powdered eggs.

30 percent reductions in the level of export subsidies, 30 percent increases in market access through reductions in quotas and/or tariffs, and 30 percent reductions in internal price and income supports. This "30-30-30" deal was proposed to occur over 5 years on a 1990 base, rather than the 1986-88 base put forward by the United States.

When the compromise was rejected in early December, the GATT talks were adjourned, pending the submission of new or revised proposals, specifically from the EC. In the last two months, the EC has struggled internally to produce a new proposal, built around "decoupled" payments to smaller farmers, and linked to environmental set-asides. However, the U.S. authority to conduct negotiations under so-called "fast track authority" runs out March 1, 1991. It is doubtful that any agreement can be reached before then. Therefore, a two-year extension in negotiating authority must be requested by the President, which either house of Congress may deny by majority vote. In light of the Middle East conflict, however, it is likely that Congressional opposition to extension of fast-track authority will be somewhat subdued.

The outcome of the GATT negotiations, in my view, will either be something close to the 30-30-30 proposal (with more than 30 percent cuts in export subsidies possible) or no deal at all. The "no deal" outcome could be very risky for U.S. agriculture, because of the possibility of agricultural trade retaliation. Since neither the U.S. nor EC have the money to substantially increase export subsidies or internal supports (notwithstanding the "snapback" provisions of the 1990 farm bill), a trade war would more likely take the form of closed market access. The special threat of a trade war to the feed grains sector comes from a possible EC

decision to "close the CAP" by eliminating the zero-duty-binding on corn gluten feed, oilseeds, and meal, or other feed ingredients. A "no deal" outcome would hurt both U.S. and Canadian producers, and could not be compensated for by expanding U.S./Canadian trade. A compromise GATT outcome, however, would reinforce the logic of the FTA.

Some Specific Examples

What are some specific examples of food processing sectors likely to do well or poorly under the FTA? The range of commodities potentially affected is large, and I will confine myself to a few examples in poultry, dairy, tomatoes and flour, which together are protected by an approximate 15 percent tariff wall. I will focus primarily on Ontario, which accounts for over 40 percent of Canada's food processing capacity.² The first and most important fact that must be grasped is the role of Canadian marketing boards in its food processing industry.

Table 1 (van Duren and Martin, p. 3) shows the products in Ontario affected by marketing boards and marketing board powers. In general, these boards have shielded Canadian producers and processors from both the effects of competition, and the process of competitive pricing. As the FTA unfolds, it will have impacts both on prices and process, forcing Canadian producers to reacquaint themselves with the rigors of competition.

²This section is based on two recent papers: Erna van Duren and Larry Martin, "Assessing the Impact of the Canada-U.S. Trade Agreement on Food Processing in Canada: An Analytical Framework and Preliminary Results for Poultry, Dairy and Tomatoes," Department of Agricultural Economics and Business, University of Guelph, December 1990; Larry Martin, C. Ford Runge and Erna van Duren, "Canada and the U.S.: Relative Competitiveness of Selected Agrifood Industries," Invited Paper for the Canadian Agricultural Economics and Farm Management Society Meetings. Vancouver, B.C., August 6, 1990.

Table 1: Trade orientation and Summary of Marketing Boards

Products	Self-Sufficiency Ratio, 1987		Producer- Processor Market Interface	
	Raw	Processed	Marketing Boards	Marketing Board Powers
Cattle/Several Types of Beef	107	95	None	None
Hogs/Several Types of Pork	103	131	Ontario Pork Producers Marketing Board	Allocation to auctions and price pooling
Soybeans/Oil	96	100	Ontario Soybean Growers Marketing Board	Negotiates prices and terms of exchange
Soft White Winter Wheat/Flour	104	121	Canadian Wheat Board and Ontario Wheat Producers Marketing Board	Import controls on wheat and flour, different price for domestic and export market, must buy and sell all Ontario wheat, price pooling.
Fruits/Several Processed Forms	49	0 - 80	Ontario Tender Fruit Producers Marketing Board	Negotiates prices and terms of exchange
Potatoes/Several Processed Forms	105	112	Ontario Potato Growers Marketing Board	Negotiates prices and terms of exchange
Vegetables/Several Processed Forms	68	90 - 106	Ontario Vegetable Growers Marketing Board	Negotiates prices and terms of exchange
Tomatoes/Several Processed Forms	80	64 - 103	Ontario Vegetable Growers Marketing Board	Negotiates prices and terms of exchange
Chicken/Several Processed Forms	< 100	95	Ontario Chicken Producers Marketing Board and Canadian Chicken Marketing Agency	Prices, production and allocation processors controlled by Board. One price class.
Turkey/Several Processed Forms	< 100	101	Ontario Turkey Producers Marketing Board and Canadian Marketing Agency	Prices, production and allocation processors controlled by Board. One price class.
Eggs/Several Processed Forms	97	100	Ontario Egg Producers Marketing Board and Canadian Egg Marketing Agency	Prices, production and allocation processors controlled by Board. Different prices for table and eggs for processing, which are priced for export or domestic markets.
Milk/Cheddar /Butter	100 100	106 94	Canadian Dairy Commission and Ontario Milk Marketing Board	Prices, production and allocation to processors controlled by Board Prices and allocation policy set by class of milk

Source: van Duren and Martin, 1990, p. 3

Opportunities for U.S. producers and processors will be substantial. Table 1 shows that if the self-sufficiency ratio is greater than 100, Canada is a net exporter, while if less than 100, Canada is a net importer.

The relationship between the FTA and various food sectors involves a complex set of issues including tariffs, subsidies, market access, technical regulations, dispute settlement procedures, and the relevant GATT articles. These are summarized in Table 2, drawn from van Duren and Martin (1990). (These authors prefer to call the FTA the CUSTA, or Canadian/U.S. Trade Agreement).

The bottom line is that the protection afforded Canadian producers and processors through supply management has made many Canadian industries less competitive if forced into the less protective environment of the FTA. Consider the following examples.

Poultry

Ontario's poultry producers, including chicken, turkey, and eggs, market their products through provincial supply management boards. In eggs, the Canadian Egg Marketing Agency (CEMA) allocates production quotas to each province and sets prices based on national cost of production formulas. This quantity and price fixing arrangement is then administered by the Ontario Egg Marketing Board. Table eggs are distinguished from breaker eggs, which are sold as surplus above the national quota and priced by adding transport and handling costs, plus a tariff and processor levy to a price in the U.S. If exported, breaker eggs are priced on tender. As a result of this complicated scheme, imports are restricted to hold up domestic prices, but Canada is still a net importer of both table and breaker eggs from the U.S.

Table 2: Provisions of CUSTA Relevant to Canada's Agrifood Sector

Product	Tariffs	Subsidies	Market Access	Technical Regulations	GATT Rights and Obligations	Disputes and Settlement
CUSTA, Article	(401,402,702)	(701)	(703,704,705)	(708)	(710)	(Chapters 18,19)
Beef	Phased out Most over 10 years	Rules on export subsidies Cooperation on domestic subsidies	Mutual exemption from meat import laws	Aim to harmonize to ensure fair trade. Working groups on animal health, meat inspection, drugs, additives, packaging	Nothing specific	Border inspection dispute settled
Pork	Phased out Most over 10 years	Rules on export subsidies Cooperation on domestic subsidies	General commitment to improve	Aim to harmonize to ensure fair trade. Working groups on animal health, meat inspection, drugs, additives, packaging	Subsidies and Countervail Code	U.S. countervailing duties on Canadian hogs and pork being challenged in several fora
Soybeans	Phased out Most over 10 years	Rules on export subsidies Cooperation on domestic subsidies	General commitment to improve	Aim to harmonize to ensure fair trade. Working groups on plant health, seeds, fertilizer, pesticides, additives, packaging	Nothing specific	No disputes
Grains/Wheat	Phased out Most over 10 years	Rules on export subsidies Cooperation on domestic subsidies Public entities not to price below cost Special rates on grain shipped to U.S. by western Canadian ports prohibited	Canada to eliminate import licensing when government support equalized	Aims to harmonize to ensure fair trade Working groups on plant health, seeds, fertilizers, pesticides, additives, packaging	Nothing specific	U.S. conducting investigation into position of durum wheat from Canada in U.S. markets
Fruits and Vegetables	Phased out Most over 10 years Snapback for 20 years	Rules on export subsidies Cooperation on domestic subsidies Public entities not to price below cost	General commitment to improve	Aim to harmonize to ensure fair trade. Working groups on plant health, seeds, fertilizers, pesticides, additives, packaging, inspection	Subsidies and Countervail Code, Anti-dumping code	Several countervail and anti-dumping orders in effect in U.S. and Canada
Chicken, Turkey and Eggs	Phased out on further processed products Most over 10 years	Public entities not to price below cost	Canadian increase in global import quota	Aim to harmonize to ensure fair trade. Working groups on animal health, meat inspection, drugs, additives, packaging	Nothing specific	No disputes
Dairy	Phased out on further processed products Most over 10 years	Public entities not to price below cost	General commitment to improve	Aims to harmonize to ensure fair trade. Working groups on animal health inspection, drugs, additives, packaging	GATT Art II(2)(c) applies to Canada placing yogurt and ice cream under import controls U.S. has waiver from GATT	U.S. asked GATT panel to rule on Canada's import controls decision

Source: van Duren and Martin, 1990, p. 8.

Like eggs, chicken and turkey producers are given a provincial quota by the Canadian Chicken Marketing Agency. Imports are restricted through import quotas. The Ontario Chicken Marketing Board then allocates raw product to various classes of buyers. These include fast-food chains, processors, and the retail trade which together with the Hotel, Restaurant and Institutional (HRI) sector claims the amount left over. Turkey is handled in much the same way, but much more goes to retail and HRI trade. Overall, Canada maintains chicken and turkey import quotas to protect its system of supply management, but is still a net importer of chicken, chicken products, and raw turkey products, although occasionally exports processed turkey.

What will the FTA do to Canada's poultry industry? Based on quarterly data from 1985-87, van Duren and Martin concluded that the increase of global import quotas for chicken and primary processed products (which under Article 706 of the FTA rise to 7.5 percent of the previous years production, based on actual imports in the three years before the FTA was concluded), together with tariff phase outs over 10 years for further processed products will likely force changes in the current marketing board system. The data shown in Table 3-A and 3-B of their study indicate that with or without tariffs, Ontario chicken prices are above those in the U.S., and higher than the landed cost of U.S. product. Gross margins (value of processed product less value of raw product) for primary processing are almost twice as high in Canada as in the U.S. Net margins (value of processed product minus total costs of production) would become negative if U.S. product was landed in Ontario, with or without tariffs. The bottom line: "at 1985-87 processing costs, Ontario chicken processors

Table 3A: Estimated Impact of the FTA on Raw and Processed Chicken Prices in Ontario

Raw Product Price	Actual cents/kg	Indexed Ontario=1
Ontario (pre-FTA)	107.5	1.00
U.S.	93.2	0.87
Landed Cost of U.S. Product		
- with tariffs	104.4	0.97
- without tariffs	98.8	0.93
Ontario price if import quota is administered in the same manner as before the FTA	103.4	0.96
Competitive price, based on land cost of processed product (without tariffs)	68.8 to 73.1	0.64 to 0.68

Processed Product Price	<u>Primary Processed Chicken</u>		<u>Chicken Dinner</u>	
	Actual cents/kg	Indexed Ontario=1	Actual cents/dinner	Indexed Ontario=1
Ontario (pre-FTA)	209.8	1.00	272.9	1.00
U.S.	155.1	0.74	221.2	0.81
Landed Cost of U.S. product				
- with tariff	182.4	0.87	272.9	1.00
- without tariff	163.3	0.78	234.2	0.86
Ontario price (import quota, as described above)	201.3	0.96	NA	NA

Source: van Duren and Martin, 1990, p. 18.

Table 3B: Estimated Impact on the FTA on Gross and Net Margins in the Chicken Processing Industry in Ontario

	Primary Processed Chicken (cents/kg)	
	Gross Margin	Net Margin
Base (pre-FTA)	64.7	8.7
Raw and processed product	NA	
- at U.S. prices		
- at landed cost with tariff	41.4	-14.5
- at landed cost without tariff	28.6	-27.4
- at Ontario price (with import quotas as described above in Table 3A)	61.7	5.7

Source: van Duren and Martin, 1990, p. 19.

would experience net economic losses if they were to compete in a completely free trade environment, or one in which trade was distorted only by tariffs" (p. 17). Looked at from the U.S. side, export opportunities in the poultry sector are likely to continue to expand under the FTA.

Dairy

Canadian dairy has producer marketing boards that control supply through national policy, together with provincial milk marketing boards. The Ontario Milk Marketing Board (OMMB) controls production of fluid milk to maintain selling prices at the levels of demand, and restricts imports through quotas under Article 11(2)(C) of the GATT. Industrial milk is priced on national self-sufficiency for butterfat, in which the Canadian government purchases butter, and provincial boards fix prices based on the end use of milk. Ontario is allocated a share of national production for four classes of industrial milk and two classes of fluid milk. Processors are also subject to plant supply quotas, including those for cheese and butter. Exports are limited to skim milk powder and butter, and are sold at subsidy. Imports are again restricted through quotas.

The FTA says nothing specifically about this sector, but it is affected by the general application of GATT rules. For example, when Canada added yogurt and ice cream to its list of import-controlled products, a GATT panel ruled against these additions. If Canada is forced to grant greater market access under the terms of a larger GATT deal, the effects are likely to be analogous to poultry. In the same study cited above, van Duren and Martin considered the effect of increased import quotas at five percent of the production of the previous year, and the phase out of tariffs. Their Tables 4-A and 4-B, reproduced below, show

Table 4A: Estimated Impact of the FTA on Raw and Processed Dairy Product Prices in Ontario

Raw Product Price	Fluid Milk		Industrial Milk (Cheddar)		Industrial Milk (Butter)	
	Actual (\$/HL)	Indexed Ont.=1	Actual (\$/hl)	Indexed Ont.=1	Actual (\$/hl)	Indexed Ont.=1
Ontario (Pre-FTA)	52.5	1.00	39.0	1.00	39.6	1.00
U.S.	38.9	0.74	35.7	0.89	35.7	0.90
Landed Cost of U.S. product						
- with tariffs	47.3	0.90	43.6	1.09	43.6	1.10
- without tariffs	40.5	0.77	37.4	0.94	37.4	0.94
Ontario price if imports increase to 5 percent of production	41.5	0.79	37.3	0.93	37.4	0.94
Competitive price (based on landed cost of processed product without tariffs)	35.6	0.68	27.8	0.70	37.3	0.94

Processed Product Price	Fluid Milk		Cheddar Cheese		Butter	
	Actual (\$/HL)	Indexed Ont.=1	Actual (\$/hl)	Indexed Ont.=1	Actual (\$/hl)	Indexed Ont.=1
Ontario (pre-FTA)	69.9	1.00	5.74	1.00	5.22	1.00
U.S.	50.6	0.72	3.78	0.66	4.26	0.82
Landed cost of U.S. product						
- with tariff	59.1	0.85	4.63	0.80	5.30	1.02
- without tariff	52.3	0.75	4.56	0.79	5.04	0.97
Ontario price (import quota, as described above)	54.8	0.78	5.36	0.93	4.94	0.95

Source: van Duren and Martin, 1990, p. 22.

Table 4B: Estimated Impact of the FTA on Gross and Net Margin in the Dairy Processing Industry in Ontario

Gross Margins	<u>Fluid Milk (\$/HL)</u>	<u>Cheddar Cheese (\$/KG)</u>	<u>Butter (\$/KG)</u>
Base (pre-FTA)	16.68	1.86	2.07
Raw and Processed:			
- at U.S. Prices			
- at landed cost with tariff	11.70	0.40	1.82
- at landed cost without tariff	11.70	0.93	2.06
- at Ontario price (with import quotas as described in Table 4A)	-5.50	1.06	1.59

Net Margins	<u>Fluid Milk</u>	<u>Cheddar Cheese</u>	<u>Butter</u>
Base (pre-FTA)	6.04	1.43	1.87
Raw and Processed Product			
- at U.S. Prices	N.A.	N.A.	N.A.
- at landed cost with tariff	1.13	-0.04	1.62
- at landed cost without tariff	1.13	0.50	1.86
- at Ontario price (with import quotas as described in Table 4A)	-5.50	1.06	1.59

Source: van Duren and Martin, 1990, p. 23.

fluid and processed milk, cheddar cheese and butter higher than U.S. prices, although the effect with and without tariffs is complicated. When tariffs are eliminated, the landed cost of U.S. product is below the Ontario price for both new and industrial milk. For processed milk, landed U.S. product cost is below the Ontario price with or without tariffs except for butter.

Allowing five percent increases in imports leads to fluid milk price declines to 79 percent of the pre-FTA price, and industrial milk price declines to 93-94 percent of the pre-FTA price. In Table 4-B, both gross and net margins are shown to decline under increased market access and tariff removal for fluid milk, cheddar cheese and butter. In sum, the FTA and its links to GATT may lead the Canadian dairy sector to downsize, creating additional opportunities for U.S. producers, if access to the Canadian market is increased.

Tomatoes

Like other Canadian fruits and vegetables, tomatoes are marketed through boards which negotiate prices growers receive from processors, such as the Ontario Vegetable Grower's Marketing Board. Tomatoes are the most important horticultural crop in Ontario. Before the FTA, Canada maintained tariffs on processed tomatoes as well as other import regulations, and tariffs on raw tomatoes. As these tariffs are phased out over ten years, prices will decline. If priced according to the landed price of paste without tariffs, van Duren and Martin show in Tables 5-A and 5-B a price decline to 68 percent of the pre-FTA level. The very substantial level of pre-FTA margins (15.7 percent) however, suggests that the tomato processing industry will be able to adjust more readily to competition.

Table 5A: Estimated Impact of the FTA on Raw and Processed Tomato Prices in Ontario

Raw Product Price	Actual (\$/KG)	Indexed Ontario = 1
Ontario (pre-FTA)	11.43	1.00
U.S.	10.18	0.89
Landed cost of U.S. Product		
- with tariffs	13.83	1.21
- without tariffs	11.65	1.02
Competitive price based on: the processed product at the		
- Ontario (pre-FTA) price	11.43	1.00
- landed cost with tariff	9.94	0.87
- landed cost without tariff	7.77	0.68
Tomato Paste Price	Actual (\$/KG)	Indexed Ontario = 1
Ontario (pre-FTA)	130.00	1.00
U.S.	91.00	0.70
Landed cost of U.S. Product		
- with tariffs	120.00	0.93
- without tariffs	109.20	0.84

Table 5B: Estimated Impact of the FTA on Gross and Net Tomato Paste Processing Margins in Ontario

	Gross Margin \$/kg	Net Margin
Base (pre-FTA)	64.28	20.41
Raw and processed product:		
- at U.S. prices	33.29	N.A.
- at landed cost with tariff	41.79	-2.07
With raw product at competitive price and processed product at landed cost minus tariff		
- at pre-FTA processing margin	64.28	20.41
- at processing margin	43.87	0

Source: van Duren and Martin, 1990, p. 25.

From the U.S. perspective, fewer opportunities for exports in this sector are likely to arise.

Wheat and Flour

In the wheat and flour sector, the Canadian Wheat Board pools prices and sets marketing quotas together with a system of import licensing to regulate delivery of wheat and flour. In Ontario, the Ontario Wheat Producers' Marketing Board controls all purchases and sales, although production is not controlled. Recently, almost all Ontario production has been bought by domestic processors, although 40 percent of milled flour is exported. As noted above, if U.S. and Canada wheat support levels achieve parity as measured by the PSE during 1991, the FTA calls for the elimination of the import license barrier. However, imported U.S. wheat would still need to be accompanied by end-use certificates, and will probably have to move in sealed wagons.

The estimates of the impacts of the FTA in the wheat market are likely to be similar to the poultry, dairy and tomato cases, although the data do not allow as precise an estimate of the likely effects. On balance, the Canadian wheat and flour milling industry will also face substantial adjustments, leading to expanded opportunities for U.S. producers and processors.

Anxiety and Questions

Given these results, it is understandable that considerable anxiety exists over the impacts of the FTA on agriculture, especially in Canada. How, where and how much trade liberalization will benefit Canada and the U.S. will depend on the willingness of various industries to adjust,

foregoing government shelter for market expansion opportunities. Only complex and specific market level analysis can capture the subtle effects and process of increased competition. Even then, "competitiveness" is a moving and elusive target.

The following are some frequently asked questions.

(1) What are the specific prospects for feed manufacturing and feed ingredient industries under the FTA?

Somewhat in contrast to dairy, flour, and poultry industries, the Canadian feed manufacturing and ingredient industry is relatively well structured, with plants in advantageous locations to serve an expanded market. Oilseed crushers, in particular, are very optimistic about their prospects, and would like to put tariff reduction on the fast track. It is worth emphasis that this enthusiasm persists in the face of an .86 cent Canadian dollar. The general expectation is that soybeans and their products will flow North at expanded levels, while canola and its oil flows South.

(2) Will the supply controlled commodities continue to be protected under FTA?

As I have emphasized, the effect of the Canadian supply control policies has been to weaken the competitiveness of these products as protection falls under the FTA. The marketing board structure will be stressed and forced to change by the FTA and the GATT process (via panel rulings such as that on yogurt and ice cream) but will not disappear. A "new generation" of boards is likely to emerge.

- (3) Many Canadians feel that the FTA will simply lead the U.S. to "mine" Canada's raw materials, with most of the value added coming from the U.S. side. Is it accurate to characterize the FTA as a one-sided deal under which Canadians will remain "hewers of wood and drawers of water"?

These concerns are real, and represent a widespread fear in many sectors in Canada. Whether these fears will prove justified depends on whether (a) Canada makes the investments to add value to its resources; (b) its comparative advantage is based only on raw materials. I believe Canada can and should make investments to add value in fisheries, forest products, and agriculture. It is questionable how much of Canada's comparative advantage lies in natural resources, and how much lies instead in what economists call "human capital." This includes factors such as a highly educated, skilled workforce, a dynamic inflow of talented immigrants, and an advanced service sector, particularly financial services. With specific reference to labor migration, I expect that national immigration policies will remain in force for the foreseeable future.

- (4) How can Canada be assured that U.S. state governments do not simply pick up where the federal government left off, using technical barriers or environmental regulations to protect domestic U.S. industries?

This is an important issue, which has been given new emphasis, as states such as California have become more aggressive in regulating various industries, especially agriculture. The U.S. government is being forced to play "catch-up" with various states in this area. This subject is a key one for the U.S./Canada technical committees considering harmonization of standards, since both federal and state/provincial standards are relevant.

(5) What impact will Ontario's new socialist government have on the prospects for FTA?

Bob Rae's new provincial government campaign rhetoric was confronted by the reality of the Ontario economy when he was elected. He is best thought of (like many Canadian leaders) as a capitalist with a socialist glow. I do not expect him or his government to undermine the FTA, simply because on net, Ontario has a great deal to gain. However, a deepening recession and a strong dollar are both forces which will strengthen protectionist forces, just as in the U.S.

In Quebec, parenthetically, it is reasonable to expect a continued bilingual emphasis in product labelling and marketing. This is simply part of doing business in Eastern Canada.

(6) How does the FTA relate to the negotiations with Mexico?

In the last several weeks, agreement has been reached to make Canada a full partner in the U.S./Mexico negotiations. This should help to allay Canadian concerns over these discussions and the impact of a U.S./Mexico accord on Canada. Such an accord, in my view, is likely to be less far-reaching than the FTA, and will have its greatest impacts in the petroleum sector.

(7) What effect will the Gulf War have on the FTA and international trade generally?

In a narrow sense, part of the reason Canada has come into the U.S./Mexico talks as a full partner is linked to its support for the U.S. led coalition in the Gulf. The war is also likely to help extend "fast track" negotiating authority in the Uruguay Round. More generally,

however, I fear that the war has raised resentment against Japan and Germany, who have been too slow to contribute, and will tend to reinforce the protectionist actions against them. If the war is long and costly, it will be very difficult for the American people to remain enthusiastic about their international responsibilities in both the areas of trade and security.