mo

Paper 86-41

AEWP 1986-41

NOTES FOR TALK ON A U.S.-CANADIAN BILATERAL TRADE AGREEMENT

Harold F. Breimyer
Professor and Extension
Economist Emeritus
University of Missouri-Columbia
Dept of agricultural economics

d6

Department of Agricultural Economics
University of Missouri-Columbia
Columbia, Missouri 65211

Notes for meeting with Ontario Federation of Agriculture, Toronto, November 24, 1986

Harold F. Breimyer
Professor of Agricultural Economics
and Extension Economist, Emeritus

First, three caveats or bits of candor, and one opening assessment of the current political climate.

(1) The international trade situation is so tangled and twisted that any examination, by person of high rank or low, is as reflective of the personality of the examiner as it is revealing of the empirical situation.

(2) The United States and Canada stand in a particularly ambiguous position relative to each other. We are neighbors and big trading partners. (See data in paper, "Agricultural Issues in a Comprehensive Canada-USA Trade Agreement: A Canadian Perspective," by Professors T.K. Warley of University of Guelph and R.R. Barichello of University of British Columbia.) We have similar cultural and political orientations. We hold common interests in the fabric of world agricultural trade generally. We are also competitors, particularly in the grain trade.

(3) Most commentators, and particularly economists, have trouble with the starting point for their observations. It's popular, for reasons I cannot understand, to begin with an implied assumption that domestic and international trade basically follows textbook rules of division of labor and commodity exchange, or ought to do so. The phrase that has become so common as already to be hackneyed is that we want "a level playing field." The notion is that if terms of trade were properly established, so that the playing field is level, trade will not only flourish but will redound to the benefit of all participants.

Lest I seem agnostic, I too like the idea of a level playing field. But we haven't had one, nor are we going to have one. The field has not only had a tilt. It hasn't even been flat. It has been hilly, rocky, convoluted. Moreover, it will stay more or less that way. The object most of us have in mind is to make it less so, and to avoid pressures, currently strong, to make it even worse than it is now. We can't hope for flatness or levelness. The rhetorical image hurts more than it helps.

That third caveat leads to an assessment that I have to regard as negative, even discouraging. After a half-century of observation I have arrived at a personal theory of political affairs. It's that human beings are capable of responding to the more idealized socio-political relationships only under two polar circumstances: when things are going very well, and when they are going very badly. At an intermediate stage, self-interest rivalries take over.

During prosperous times, it is not too difficult to win acceptance of liberal concessions in economic policy. No one is put at serious risk. When everyone is in desperate trouble, as was true during our depression of the 1930s, social harmony can be within reach.

The United States today is definitely in the middle ground. We Americans are neither rich nor poor, as a nation. Our economic policies are not working well but neither are they collapsing. We are bickering internally but not revolting against anything or realigning politically. Democrats and Republicans are still in close to even balance; and factions within each party are at stand-off.

Likewise, the world's agricultural trade is in serious trouble but is not yet chaotic. We can ask, is it moving to a point of such disarray that national rivalries will give way to a genuine and successful wish to design and accept workable accommodations?

My hunches are two. One, things are not yet that bad. As the saying goes, they may have to get worse before they can get better. Secondly, effective pressure to make real progress in trading relationships may come from a new, unprecedented source. It's the budgetary cost of the export subsidization being practiced, especially by the European Community and the United States.

In my country resistance is mounting to the ever rising cost of our deficiency payments to farmers, much of which constitutes subsidization of exports. In this respect our situation differs from earlier periods of imbalance. In the 1950s, for example, our protests were aimed at the cost of holding our large surplus stocks. Those stocks are huge once again, but most of the objections focus on the expensive direct Treasury payments.

As a side comment, the Reagan Administration would welcome a protest movement ideologically, but find it embarrassing politically.

Subsidization of export trade has meaning and consequences that extend far beyond the budgetary burden on the big subsidizers. In my judgment it's the most disruptive phenomenon in international agricultural trade today. It puts trading nations in competitive relationships that have little or nothing to do with their productive capacity -- their so-called international comparative advantage. Compared with the dominant role of subsidies, the many restrictive devices that countries practice so ingeniously are scarcely more than nuisances.

The European Community and the United States are of course the big players in the subsidy game. Canada is put in a difficult position. Countries such as Argentina are injured much more. It is possible that our Department of State and the Foreign Relations committees of both houses of our Congress will become so concerned for effects on international relations as to add their political pressure to urban taxpayers' objections to program costs.

The pattern of economic policies in the United States in the 1980s has been strange. A reluctance to do anything has been followed by going off wildly in a new direction. A sense of moderation has been absent. In agriculture, our PIK program of 1983 was overdone. In the 1985 farm law we did not merely edge our commodity loan rates downward, and lift compensatory direct payments a bit upward. Instead we made drastic moves -- even, I would say, rash ones.

I admit readily that our export subsidization creates problems for Canada. But I am not going into U.S.-bashing. Our internal, home-bred, critics have long complained that our price supports (commodity loans) have provided a shelter for all the world's exports. They are at least partly correct. It is also true that we have done more than most countries to restrain production and thereby shrink surpluses. The United States is on sound ground in asking Canada to do more than she has done thus far to hold down either production or the quantities made available in the grain export trade. I can readily believe that some kind of provision for dealing with oversupply should be a part of a trade agreement.

These notes on Canadian-U.S. trade relationships will not lead to many firm conclusions. The only viewpoint held dogmatically is a strong endorsement of efforts to negotiate better trade relationships. The present course in international trade leads only to what may be called, in the seldom recalled phrase from Pilgrim's Progress, a slough of despond.

Having said that, I hesitate to specify. So many issues arise. One is the choice between bilateral and multi-lateral approaches. The topic, Canadian-United States trade relations, implies bilateral negotiation. I was reared academically on the thesis that world trade should be liberalized multilaterally; that the beguilingly contradictory phrase, Most Favored Nation, ought to apply. Yet the United States and many countries have turned ever more to individual compacts.

To be sure, we can conceive of bilateral agreements that are arrived at within the context of multi-lateral agreements, and are consistent with them. Maybe a Canadian-U.S. agreement can be worked out that does not undermine any progress made in the current GATT negotiations. That would be the best of all worlds. Professor Warley, to whom I have already referred, suggests that successful bilateral agreement-making may be a precedent for progress multilaterally. I am not quite that sanguine. I fear we and most nations, finding ourselves frustrated in international tribunals, are turning to bilateral connections as a recourse, as a second-best.

I have only two further remarks. One is a candid admission that trade relations may be the clearest case where generalization is easy and specification difficult. That is to say, we can all sing paeans to the virtues of relatively free and unrestricted trade among sovereign nations. We can be equally quick to encounter trouble in achieving any liberalization that counts for much.

The moral this point leads to is that if our two countries are to arrive at better harmony, each must give up something. Professor Warley names Canada's dairy and poultry industries as blatantly over-protected. Our dairy interests also have been pretty successful politically. He takes note too of a feature of the Canadian economy from which ours is more nearly free, and that may in fact be the harshest impediment to freer (or fairer) trade. It is the much greater autonomy you accord your provinces than we do our states. With no disrespect to Canada, I have to say that one of the wisest steps taken by the drafters of our constitution was to outlaw barriers to commerce among our states.

What is to be said about what benefits might follow from an easing of trade restrictions between Canada and the United States? First of all, let me disabuse of the old but discredited thesis that open trading invariably benefits all participants and does so almost equally. That hoary notion is just not valid. Differences in bargaining relationship affect the outcome of trading.

It would be easy to suggest, in the rubric of that admission, that smaller Canada could find itself engulfed by the U.S. giant if it were to relinquish too many protective instruments. Before addressing that charge I make a distinction between commodity trade and investment. I suggest that the mutual-benefit idea applies fairly well to commodity trade. I believe it especially does so in commodity trade between the United States and Canada. The two nations are well enough balanced that they can negotiate regarding terms of commodity trade without fear that either will thereby be rendered subservient to the other.

I do not hold the same faith with regard to investment. In this respect, the United States has, in recent years, exhibited a serious degree of naivete. A decade ago it endorsed the principle of floating exchange rates for the dollar, on the disingenuous belief that the "market" (for exchange) will bring the best of all trading and investment worlds. For a time we even rejoiced in the steady rise in value of our dollar, on grounds that it showed how virile a nation we are. The strong dollar was accompanied by persistent and increasing deficits in our federal budget (a contributory cause) and a growing imbalance in our commodity trade. Also manifest was a rapid change in our international investment relationships. We incurred new debt obligations of ominous scale, and we sold assets abroad. For a long time, little alarm was sounded. Finally, about a year ago, our government came to its senses and initiated steps to bring the value of our dollar down. But it will take a long time to correct the huge payment deficit position into which we drifted. In a news story of October 27 the Wall Street Journal summed up the spot we have got ourselves into. It wrote in the trenchant terms of the "de-Americanization of the American Economy."

At the moment, the United States is not in position to invade any country with investments.

In my opinion, nations are justified in showing more protective caution in their terms of trade involving national assets than in trade in commodities and services. I am not unsympathetic with Canada's concern that the United States might almost buy it out. I am curious as to whether, in my country's divestiture of this decade, Canada, far from being dispossessed, has actually made some net gains in holdings of U.S. assets. Be that as it may, my concluding remark is that it would be mutually beneficial indeed if trade in goods and services between the United States and Canada could be liberalized to appreciable degree. I do not apply the same dictum to investment relationships. The two fields of our economic relationship should be dealt with separately.