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Across the 49th Parallel

to the Future

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Prepared by the Local Government Center at Montana State University

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to the Future

A Proceedings from a Public Forum
Considering Shared Opportunities
Under the Canadian-U.S. Free Trade Agreement

A Publication of the Local Government Center
Montana State University

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and
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Preface

This collection of papers dealing with the Canadian-U.S. Free Trade Agreement (CUSTA) originated at a conference of Albertans and Montanans convened in Great Falls, Montana, on 14-15 September 1990. The theme of the conference went well beyond a mere detailing of the provisions of the 1989 CUSTA. Implicit in the conference theme and in the title of these proceedings is the expectation of tangible and mutually beneficial CUSTA outcomes for Montana and Alberta.

While the specific pattern and symmetry in the distribution of beneficial outcomes remained less than clear to the presenters, several important considerations emerged. Foremost among these considerations is the global move toward openness and integration in international markets accompanied by the emergence of increasingly strong regional trading communities, perhaps most notably the European Community, and prospectively, a community of the Americas. The presenters' concerns also extended to an anticipated, resurgent regional bilateralism, as well as national, protective responses to mitigate adverse effects of increased regional and global competitiveness. Following in-depth elaboration of these and a number of related macro issues, the conferees turned their attention to what was intended as the core issue of the conference.

Does the CUSTA enable the development of north-south trade corridors in the Canadian-American West? More specifically, is it feasible under the CUSTA to adopt a rural development strategy for Montana and Alberta predicated upon an incipient trade corridor along Interstate Highway 15, which presently connects Edmonton-Calgary-Lethbridge across the 49th Parallel to Great Falls-Helena-Butte? To explore by analogy the feasibility of an Alberta-Montana corridor, we asked Jerry Nagel first to explain the development of the "Red River Trade Corridor Development Project," which now couples Manitoba, North Dakota, and Minnesota.

It is difficult to overstate the energizing impacts that the trade and rural development opportunities envisioned in these two papers had on the attending audience. Presented, as they were, against a global backdrop of increasing national openness, trade integration and competitiveness, Nagel and Swanson each offered a tantalizing development alternative to a region that, historically, has been dominated by global, commodity market forces beyond its control. Suffice it to say that even before the conference was adjourned, representatives from local jurisdictions on both sides of the 49th Parallel had begun planning for a follow-on implementation conference to be held in Lethbridge in the spring.

This public policy education conference was organized and sponsored by Montana State University's Local Government Center in collaboration with the Department of Agricultural Economics at the University of Minnesota, the Montana State Department of Commerce, and the Chamber of Commerce of the City of Great Falls. Enabling funding was provided by the W.K. Kellogg Foundation and the Northwest Area Foundation. Publication of these proceedings was made possible by a grant from the Canadian Embassy in Washington, D.C. and the Center for International Food and Agricultural Policy at the St. Paul campus of the University of Minnesota.

Kenneth L. Weaver
Director

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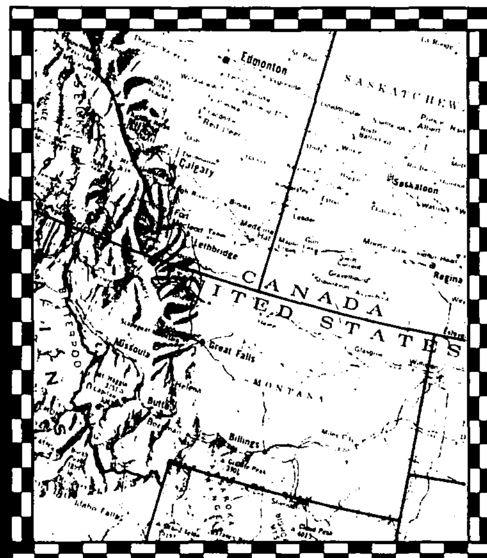

Welcome to Montana

*Governor Stan Stephens**

Back in 1948, I came to Great Falls for the first time with a Canadian hockey team. It was my first entry here because at that time my roots were in Calgary. Since then my roots have changed. I have been in this state for 40 years, and since the fall of 1988, I have served as Governor. Thus, having somewhat of an international background myself, I offer a unique perspective of the Free Trade Agreement that I hope serves my state well.

Montana is the only state that borders three Canadian provinces. We have the good fortune to butt up against British Columbia, Alberta, and a good portion of Saskatchewan. We see ourselves as having much in common with our neighbors to the north.

The Canada-U.S. Trade Agreement (CUSTA), as you know, is a young agreement that is perhaps not as well understood this side of the border as in Canada. There the Free Trade Agreement was probably the crucial issue in the 1988 Canadian election. But it never entered into the 1988 presidential election in this country to the extent that it did in Canada. So while Canadians are very conversant about the agreement, and have ready opinions, we are just beginning to understand the opportunities it affords.

Montanans have been trading with Canadians for a long time. In the early history of this state, we had steamboats coming up the Missouri River to Fort Benton that brought products not only to Montana, but many goods eventually found their way north, up "the Whoop-Up Trail" into Canada. (I suppose the Canadian Mounties at that time did not appreciate all of the products that we sent.)

Today, Montana leads the Rocky Mountain states in volume of trade going north. In 1989, over $150 million worth of goods moved from Montana to Alberta, Saskatchewan, and British Columbia. This was a $22 million increase over the numbers for 1988. Not all of the goods moved out of Montana into Canada originate in the state; many of them come from other states. Nevertheless, Montana serves as the corridor for entry into those provinces. And the door swings both ways. Our Canadian neighbors actually use it more than we do. Imports from Canada exceed the state's exports to Canada by about 6 to 1. The bulk of Canadian importation is gas and oil, much of which is value-added at Montana's benefit, because it is processed at refineries in Billings.

Since 1989, the Montana Departments of Agriculture and Commerce have been working very closely to implement the Free Trade Agreement. We have also been working with Montana business people (Jack Whittaker, Cascade County Commissioner, and others) to develop opportunities we see for Montana because of the CUSTA.

Alberta alone (take Lethbridge, Calgary, and Edmonton) provides Montana businessmen with a market of three million people. That may not sound like a lot in comparison with California or New York, but a market of three million people is significant when it is geographically closer to Montana than Portland or Denver or Minneapolis-St. Paul -- <u>and</u> it is larger. So it is a significant market.

**Governor of the State of Montana*

A Binational Welcome

Our Free Trade Education Program is showing signs of success. After holding several Free Trade Conferences across Montana, our Department of Commerce is actually receiving fewer calls today than we did a year ago. That does not tell me there is a lack of interest nor that interest is diminishing; it tells me more Montanans are beginning to understand how to pursue opportunities under the CUSTA. In short, we have helped a lot of friends with advice and direction about how to get involved in the Canadian market.

Last October I was with a delegation of Montana business firms at a trade show in Edmonton and Calgary. It was a highly successful event for Montana. I think it showed many Edmontonians and Calgarians things they had not seen before about the manufacturing and service capabilities of our state. For example, Yellowstone Furniture of Belgrade actually sold out all of their inventory at the Calgary and Edmonton shows. Their product was so successful that they came back and started an expansion of their operation at Belgrade. Montana Agates, another small firm in Glendive, Montana, received similar responses. They have contracted now with distributors in both Alberta and Saskatchewan to handle their products. Many other success stories arose from that visit -- food products, textiles, and transportation exchanges were also made.

The future for trade between our two countries and our respective provinces and states offers an opportunity to cut across the whole business profile. Small manufacturers in Montana, for example, have excellent opportunities to serve larger markets in the north. To a great degree, the economies of Alberta and Saskatchewan are comparable to that of Montana, and we are very competitive in a lot of areas. Alberta is in the petroleum business; so is Montana. Alberta and Saskatchewan are very much in the grain and cattle business. These two provinces have natural resources that are also found in Montana. We also share the business of tourism. In 1989, Montana had its best tourist year in the history of this state. This year's statistics promise to be even better. I dare say comparable figures may be reflected in the tourism numbers that are coming out of neighboring Canadian provinces. We would like to be able to take advantage of the tourist opportunities afforded Montana when people come to Banff, Jasper, and Lake Louise. By the same token, when people come to Yellowstone and Glacier Parks, this could likewise afford opportunities to our northern neighbors. There is a natural trail north and south that offers real opportunities to keep tourists in this region of North America to our mutual benefit.

In the business process we can't, of course, forget that governments are involved. The sole purpose of the CUSTA is to bring trade barriers down, over a 10-year period, and to allow freer movement of goods and services both north and south. Open communication between Montana and our Canadian provinces facilitates this process. Such was demonstrated yesterday when we had a meeting of our Montana-Alberta Boundary Advisory Committee. This group has been meeting for several years to discuss mutual problems and border crossing activities. We had a very good discussion yesterday about transportation and natural resources. I think we will see some real progress for both Canada and Montana as a result of those discussions.

At the end of October of this year, I will be going back with some of our people from state government to Calgary, Alberta. At that time we hope to announce a staff member that will represent the state of Montana in a Canadian trade and tourist office in Calgary. By the end of the year, our options will be more clearly identified as we prepare to work with our legislature. We want to have our trade representative in place in Calgary by the time the legislature convenes in January of 1991. In November we will meet in British Columbia with Premier Bill VanderZalm as part of another Montana trade show. Last fall we had a Canadian/American Friendship Day in Helena to which we invited three premiers -- Premier VanderZalm of British Columbia, Premier Getty of Alberta, and Premier Devine of Saskatchewan -- to come visit and bring delegations. The result was a very stirring program, with representatives from both sides of the border (including Al Hyland). I think we established more friendships and made some good connections that will help us build future relations.

The Free Trade Agreement is a major document that will open up great opportunities for our two countries in the 90s and beyond. One of these days we may be meeting in El Paso, Texas, to talk about the trade agreement that has opened up with Mexico. I anticipate this will come true. If we look to the European Economic Community coming together in 1992, we see an emerging market there of 315 million people. And how many people do you think live in the Pacific Rim? The world is breaking up into competitive trade zones.

There are some exciting times ahead and I look forward to being part of the discussions as far as Montana is concerned. Hopefully, we will offer things that will present not only opportunities for ourselves, but great opportunities for the neighbors we cherish north of the border.

A Provincial Welcome

*Allan W. Hyland, M.L.A.**

On behalf of the government of the Province of Alberta, I welcome you to this important conference.

Alberta takes its international relations seriously. Trade is vital to the health and vitality of our economy; exports account for some 20 percent of the province's gross domestic product. Last year, Alberta's exports of goods alone were valued at close to $13 billion. Our number one trading partner, by far, is the U.S., accounting for some $9.5 billion, or 74 percent of Alberta's total exports. Japan is a distant second, at $1.1 billion, or 8.4 percent of the total.

Alberta's experience mirrors that of Canada as a whole. The U.S. is by far Canada's largest export market, accounting for some 73 percent of total Canadian exports.

A popular misconception in the U.S. is that Japan is its largest trading partner. Such is not the case. Canada-U.S. trade is the world's largest bilateral trading relationship. In 1989, two-way trade between our countries amounted to almost 186 billion Canadian dollars. Canada is the biggest foreign customer for U.S. goods. As its largest export market, close to $90 billion worth of U.S. products were purchased there last year.

The Canada-U.S. Free Trade Agreement (CUSTA) is clearly an important document. In large part, it governs the largest two-way trading relationship in the world. It is important not only in the legal parameters it sets forth, but also in the message its spirit conveys, namely that free trade is a viable and desirable objective.

Much of the world's attention is currently being focused on the Multilateral Trade Negotiations (MTN) currently underway under the auspices of the General Agreement on Tariffs and Trade (GATT). The MTN is scheduled to wrap up, one way or the other, by the end of this year. At this point in time, the outcome appears to be hanging in the balance, as it remains unclear whether sufficient political will exists in the 97 member countries of the GATT to accept the short-term pain which may be required to achieve the long-term benefits of significant liberalization of world trade. Whatever the MTN outcome, Canada and the U.S. can take pride in the fact that the CUSTA demonstrated to the world that the forces of protectionism can be overcome and that liberalized trade can be a win-win proposition.

Alberta has been a strong supporter of the CUSTA, going back to the mid-1980s when our former Premier, Peter Lougheed, urged our federal government to enter into the negotiation of such an arrangement. The province remains a strong supporter of the agreement, despite the glitches and irritants which are inevitable in the world's largest bilateral trading relationship.

At times, undo attention is paid to disputes arising in the Canadian-American trading relationship, ignoring the fact that 99 percent of our $186 billion in annual trade is

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**Minister of the Legislature for the Constituency of Cypress-Redcliff of the Province of Alberta, Canada, since 1982. Mr. Hyland is the Chairman of the Water Resources Commission and the Agriculture & Rural Affairs Caucus Committee. He is also the Deputy Government Caucus Whip and Party Secretary.*

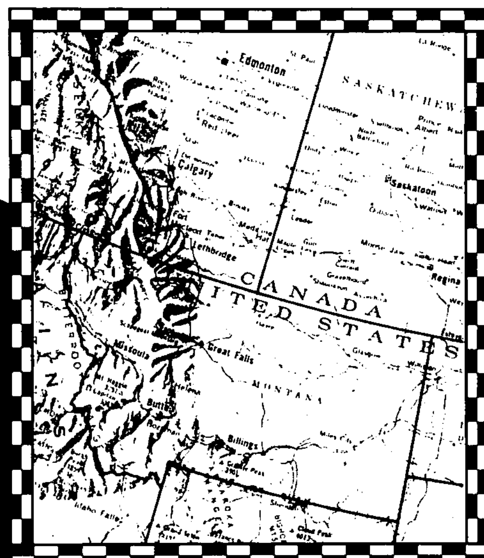
conducted in the absence of any such disputes. In reality, such disputes took place before the CUSTA came into existence. The difference now is that we have a binational system in place to resolve such disputes in an objective, fair manner. Hence, the CUSTA is a dynamic agreement, providing for further refinements in our joint quest for a liberalized and open trading relationship.

As with any good relationship, however, "give-and-take" is required. Opponents of the CUSTA in Canada still claim that our country was "taken to the cleaners" on this deal. Interestingly enough, the converse of this argument can be heard on the U.S. side of the border.

In today's increasingly competitive world, it seems clear that Canadians and Americans need to stop bickering among themselves with respect to their trading relationship. The CUSTA offers an opportunity to enhance competitiveness on both sides of the border. This can only be beneficial as we face an increasingly complex global trading environment.

Montana and Alberta share an important part of the border linking the world's largest two-way trading relationship. Surely we have an interest in doing all we can to enhance that connection.

Defining a New Relationship



An Overview

The Move Toward Increasing Openness and Integration in International Markets

*C. Ford Runge**

The Canada-U.S. Free Trade Agreement (CUSTA), initiated in the mid-1900s and concluded in 1989, should be looked at as part of a process, rather than as a solitary event. This process includes other important developments in international trade. These can be summarized as the move toward increasing openness and integration in international markets.

Agreements such as CUSTA are not really causes of this change so much as they are formal recognition by nation states that openness and integration is occurring -- and has already occurred. Hence, such agreements codify and clean up the rough edges around accomplished facts. In other words, the economies of the U.S. and Canada are already largely integrated. The agreement recognizes that fact, moves to codify it, and attempts to deal with some still disputed areas.

It does so by initiating a process which will eliminate, over 10 years, bilateral and trade restrictions according to three different time schedules. In addition, health, safety, and environmental regulations (so-called nontariff barriers) are to be identified and eliminated through a process of consultations. Sometimes overlooked, but perhaps of greatest importance, the agreement sets up a dispute resolution mechanism similar to the panels of experts used under the General Agreement on Tariffs and Trade (GATT) in Geneva, to hear specific cases under dispute. Several such panels have already been convened.

Does all of this add up to "free trade?" Probably not. Free trade is really a textbook notion used by economists in the classroom. CUSTA may come very close to free trade, but the real objective is simply to eliminate as many barriers to doing business as possible, while continuing to recognize the sovereign right of national governments and the separate and direct identities of different peoples. Throughout the full transition to this new trading regime, Americans must be sensitive to the fact that, to many Canadians, inviting integration with the U.S. economy is like inviting a bear into your canoe.

On balance, the agreement will not be all roses for everyone. But I believe it provides a very positive example to the rest of the world (especially in the context of the GATT) that the U.S. and Canada are prepared to suffer the pains of market integration in return for much larger gains. And the pains are still real. In some cases, compensation to those

**Director of the Center for International Food & Agricultural Policy and an Associate Professor in the Department of Agricultural & Applied Economics at the University of Minnesota. Dr. Runge also holds appointments in the Hubert H. Humphrey Institute of Public Affairs and the Department of Forest Resources.*

who lose may be required. By adopting a realistic approach to the gains and losses of the agreement, we will help to consolidate political support for it on both sides of the border. Integrating national economies is not free of costs, and these costs are better confronted than allowed to fester into political resentment and calls for protection.

Uhm and Koo, economists with North Dakota State University and the Canadian International Trade Tribunal in Ottawa, recently prepared some specific estimates of these gains and losses. Table 1 shows the projected impacts of the agreement over time, based on 1987 trade flow data. According to this information, Canadian imports from the U.S. will do two things: (1) displace domestic Canadian production (economists call this "trade creation"), and (2) displace imports from other countries ("trade diversion") -- the sum of which is (3) "trade expansion."

The figures are broken down here for agriculture, industry, and by country. Canadian imports from the U.S. are expected to displace $1.285 billion (Canadian) in Canadian production, while displacing $141 million in imports from other countries, leading to trade expansion of $1.426 billion, or a 3.19 percent increase. On the U.S. side, Canadian shipments are expected to displace $2.125 billion (Canadian) in U.S. activity and $211.5 million from other countries, or about $2.336 billion total. This is a 2.91 percent (nearly a 3.00 percent) expansion in trade. The overall impact on third countries is $317.8 million. Note that on a percentage basis, Canada's 3.19 percent is not as big a number as the U.S.'s 2.91 percent, because our economy is much bigger than Canada's to begin with.

The numbers suggest the following: first,

TABLE 1
Estimated Trade Expansion Effects of the FTA*
($ Canadian Million)

	Agricultural Products (b)	Industrial Commodities (c)	Total
Effects on Bilateral Trade:			
Canadian Imports from U.S.			
Trade Creation	11.4	1,273.8	1,285.2
Trade Diversion	4.3	136.7	141.0
Trade Expansion	15.7	1,410.5	1,426.0
	(0.80)	(3.30)	(3.19)
U.S. Imports from Canada			
Trade Creation	144.1	1,982.4	2,125.2
Trade Diversion	23.7	187.8	211.5
Trade Expansion	167.8	2,170.2	2,336.7
	(3.58)	(2.87)	(2.91)
Effects on ROW Trade:			
Canadian Imports from ROW	-4.3	-136.7	-106.3
U.S. Imports from ROW	-23.7	-187.8	-211.5
North American Imports from ROW	-28.0	-324.5	-317.8
	(-0.001)	(N.S.)	(N.S.)

**The estimated trade expansion effects of CUSTA are derived from the 1987 actual trade volume, agricultural products (b), and industrial commodities (c). Note that figures in parentheses are a percentage of total imports in 1987. ROW = the rest of the world; N.S. = negligibly small percentage.*

producers in the U.S. should get more benefit than producers in Canada because of Canada's relative increase in industrial imports. Consumers in Canada, however, will benefit more from free trade than consumers in the U.S., as tariff protection comes down and cheaper alternatives become available in their relatively smaller economy.

Note that exchange rates will affect all of these numbers. Finally, note that most of the impact of the agreement is between the U.S. and Canada, and not on the rest of the world.

Table 2 shows the relative levels of protection in the U.S. and Canada, giving a feel for where the "pain" might be felt most as this protection is decreased. This protection is expressed as a percentage ad valorem equivalent for both tariffs and nontariff barriers. In both the U.S. and Canada, agriculture remains quite protected, suggesting why it is fudged in the agreement and thrown back to the GATT for resolution. In contrast, gains in forestry, fishing, trapping, and mining should occur with less pain.

In manufacturing, the pain is likely to be felt most in the food and beverage industry, in textiles, knitting, clothing, and in the Canadian furniture and shipbuilding industries, at least according to these estimates.

TABLE 2
Comparison of Canadian and U.S. Trade Barriers (Bilateral Perspectives) for Selected Industries and All Industries (Aggregated)

	------ Trade Barriers* ------			
	Canada		U.S.	
Industry	Tariff	NTB	Tariff	NTB
Agriculture	3.0	8.6	2.0	10.7
Forestry	0.0	0.0	0.2	0.6
Fishing and Trapping	0.2	0.0	1.7	0.0
Mining	0.2	0.0	0.4	0.0
Manufacturing (aggregate)	5.2	1.3	3.2	1.4
Food and Beverage	5.2	6.9	3.6	8.4
Tobacco	16.5	0.0	20.7	0.0
Leather	15.7	0.0	7.5	0.0
Textiles	11.4	0.0	8.5	0.0
Knitting Mills	22.7	0.0	12.3	0.0
Clothing	19.7	0.0	10.9	0.0
Furniture and Fixtures	12.5	0.1	2.0	0.5
Shipbuilding	10.1	1.4	0.3	0.0
Goods-Production (aggregate)	4.5	1.6	2.8	1.9

**Note: Tariff estimates were derived using production data as aggregation weights. Nontariff Barriers (NTBs) are expressed as ad valorem equivalent, which includes quantitative restrictions and federal government procurement. Department of Finance, Trade Barriers Between Canada and the United States, Working Paper No. 88-3, Ottawa, 1988, p. 10 (from Uhm and Koo, 1990).*

In summary, the U.S.-Canada trade agreement is part of a process of global market integration. This process is underway in the GATT, between the U.S. and Mexico, in the Europe of 1992, between Eastern and Western Europe, and throughout Asia and the Pacific Rim. Trade agreements must go with the flow of market integration, and national economies that ignore this process do so at their own peril. However, facing the realities of integrated world markets also requires sensitivity to national objectives, traditions, and needs. The process is not all gain and no pain. It is therefore prudent to anticipate where pain will be felt, and move to accommodate it, in order to keep political momentum behind the process of trade and market integration. Doing so will be in the best interest of Montana, the West, and both the United States and Canada.

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A Global Perspective

Will the Canada-U.S. Trade Agreement (CUSTA) Enhance the Ability of the Region to Compete in the Global Economy?

*T. K. Warley**

This paper addresses the question, "Will the Canada-U.S. Free Trade Agreement (CUSTA) enhance the ability of the region to compete in the global economy?" It does this primarily by commenting on the state of the international system and the pressures on the world economy, and by placing the bilateral trade agreement in the context of the remarkable changes that are occurring in the geography of the global economy and polity. The specific question of North America's competitiveness is touched on in the final part of the paper, as is the subsidiary issue of the scope for gains through general and targeted cooperation between Canadian and United States authorities and agencies. The paper abstracts from the real and present danger of the economic dislocation that could attend a conflagration in the Middle East.

The International Economic System

As we come to the end of the longest period of sustained economic growth in the post-war era, it might be assumed that the international economic system is essentially in good shape. Such is not the case; the past boom has left a precarious foundation for future prosperity. The international system is characterized by accumulated imbalances, and the response to these by nation states is inadequate and threatens to erode the open, liberal, cooperative global economic system created over the last 40 years.

The imbalances are familiar enough: the budget, trade, and savings deficits of the U.S. and Canada and the corresponding build-up in foreign lands of dollar assets; the lack of macroeconomic policy coordination that would permit the elimination of the persistent account surpluses of Japan and West Germany and a reduction of that of the United States; interest rate-driven misalignments and volatility in exchange rates; fragility in financial markets; continuing high rates of unemployment in much of Western Europe; and the growing inequalities of income between developed and developing countries that carry a crushing and still-growing burden of debt. But perhaps the most dangerous imbalance of all is a deficiency of leadership. The new superpowers of Europe and Japan seem unwilling to play a role in managing the international economic system of trade and payments (and in maintaining collective security) that is commensurate with their stake and their ability. Meanwhile, the inability of the United States to correct its twin budget and current account deficits and reduce its indebtedness results in its having neither the means nor the authority to sustain the liberal international economic order of which it was

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**Professor of Agricultural Economics, University of Guelph*

the architect.

The actions necessary to correct these imbalances are also familiar. They begin at home with the reduction in the national budget deficit that is at the heart of an effective plan to reduce the external deficit.[1] Better coordination of macro policies of the major economies is needed. So, too, some believe, is more active management of exchange rates within target zones. The further liberalization of trade and a strengthening of the multilateral trading system is necessary to counter the tendencies toward protectionism, bilateralism, and regionalism that are undermining the GATT. A concerted approach through trade, monetary, investment, and development assistance policies is required in order to restore growth in poor and indebted developing countries. A collective effort will be required to incorporate the countries of Eastern and Central Europe and the USSR into the international systems of trade, payments, investment, and technology transfers. A concerted approach is needed to reverse the deterioration of the global environment. And finally, there needs to be a redistribution of responsibilities for attaining collective economic and security goals. These matters constituted the agenda for the recent Houston summit of the G7 countries. They are the global tasks for the years ahead.

Alas, there is little sign that nations individually and collectively are rising to the challenges. Neither the U.S. nor Canada seem to be able to muster the political will needed to reduce their domestic budget deficits (and thereby their current account deficits and external indebtedness) or to curb public and private consumption in favor of savings, investments, and exports. Neither Japan nor Europe have signalled a willingness to run the merchandise trade deficits that are required if North America is to achieve a current account surplus, and the willingness of these countries to continue to hold and acquire dollar assets is secured only by the payment of interest rates that are a threat to growth and that hold exchange rates at levels that deter investment and penalize exports.

Though it is imperative that international trade be kept open and nondiscriminatory, domestic protectionist pressures are strong, and the U.S. seems to rely increasingly on unilateral actions and bilateral negotiations (through threats to close markets, voluntary export restraints, and "process protection") in handling its trade relations. Equally, however, neither Europe nor Japan were enthusiastic about launching the Uruguay Round of GATT negotiations, their support for further liberalizing trade has been selective, and neither shows evidence of a sense of responsibility for maintaining a liberal and rule-based international trading system.

In all three regions, notions of "managed trade" have gained credence. Under this rubric, anti-dumping, countervail and safeguards measures, rules of origin, local content requirements, restrictive standards, targeted subsidies, and preferential procurement are the elements of statist "national industrial strategies" and "strategic trade policies" that together are designed to offset competitive pressures from old and new suppliers, the internationalization of markets for goods, finance and technology, the incompatibility of macro policies, and the misalignment of exchange rates. Tripolarity -- which is a de facto result of the emergence of Europe and Japan as economic superpowers and the declining ability of the United States to act as a hegemonic leader -- threatens to degenerate into rivalrous regionalism.

The New Economic Geography

Changes in political and economic geography are reinforcing the tendency for the

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[1]As a matter of identity, the trade deficit is related to the budget and savings deficits as follows: $X - M = S - I - (G-T)$. Where X is exports, M is imports, S is savings, I is investment, G is the government's expenditure, and T its revenue from taxation.

global economic order to be dominated by regional associations or blocs.

Developments in Europe promise a renaissance in "the old continent" and the emergence of "a greater Europe" of immense economic might and political influence. The completion of a genuine barrier-free market in goods, services, capital, technology, entrepreneurship, and labor by the end of 1992 will be followed by economic and monetary union and be accompanied by deepening political cooperation. A single German state will be the strongest economy in the new Europe. Beyond 1992, the European Community will forge closer links with the states of the European Free Trade Area in a larger "European Economic Space," sign association agreements with the countries of Eastern and Central Europe, and have special economic linkages to the USSR. Insofar as the creation of a larger European entity promotes accelerated economic growth, it will stimulate global trade. However, there is a fear that Europe will place its internal mission ahead of its international responsibilities, that trade preferences will divert trade, and that there will be a tendency to ameliorate the costs of adjustment to intensified internal competition by reducing competitive pressures from outside.

In Central and Eastern Europe and the USSR, we are witnessing the implosion of political structures and economic systems that were sustained only while imposed by authoritarian regimes and frozen in East-West ideological and military rivalry. To be successful in economic terms, the replacement of planning by markets must be accompanied by far-reaching changes in sectoral policies; in macro-economic policies, to cope with budget deficits, foreign debt, inflation, and overvalued exchange rates; in structural policies, to create markets for goods, services, financial assets, and labor; to establish property rights; to renovate infrastructures; and to deal with environmental externalities. Paralleling domestic transformation, these countries will have to be integrated into the international trade, monetary, and financial systems and institutions in order to give them the access to markets, public reconstruction capital, private foreign investment, technology, and management skills they need.

After decades of economic mismanagement, the entry of these countries into the international economy will likely be by measured steps. However, it is apparent that their closest associations will be with other members of "the European family," thereby reinforcing tendencies toward economic regionalism.

The Asian Pacific region is another nodal point in the world economy. Japan is the world's fourth largest economy and its people enjoy the fourth highest per capita incomes. It is a major supplier of capital and technology to the rest of the world. The area also contains "the four tigers": Taiwan, Korea, Hong Kong, and Singapore; and a third tier of populous countries with rapidly growing economies: Thailand, Malaysia, the Philippines, Indonesia, and coastal China. Together these countries constitute the world's most dynamic region. The countries of the regional economy are very diverse in terms of size, stage of development, resource endowments, technological capabilities, economic structures, ethnicity, cultures, and languages. But given the pace of development of inter-regional trade and of directed Japanese private investment and development assistance in the region, it may not be too long before regional economic (and security) institutions and a distinctive Japan-led Asian-Pacific bloc emerge. Separately, the countries of the region are already formidable competitors. Together they constitute a huge market. Acting in concert, they could exert considerable influence on the international economic system.

The increasing heterogeneity of circumstance and interest among developing countries has resulted in the disappearance of "the South" as a distinctive grouping of countries pursuing an identifiable policy agenda through stable coalitions. The problems of the developing world have slipped down the international agenda since the 1970s and are destined to slip further given the political priority and economic needs of assimilating the Eastern Bloc countries into the European and world economies. The attempt to forge a coherent approach to creating "a new international economic order" has been replaced by separate initiatives in such fields as trade policy, debt relief, resource transfers, and development cooperation. In general, the emphasis has shifted from concerted international action to national reforms.

This tour of the world's evolving economic geography finally brings us to North America. The world's first and seventh economic powers and largest bilateral trading partners are economically joined in a comprehensive trading arrangement. The prospective inclusion of Mexico would extend the preferential trading area from the Yukon to Yucatan. With regional trading arrangements arising in Central and South America, the eventual creation of a regional entity in the Americas is a possibility.

The animation for the creation of the CUSTA had both regional and global elements. For Canada, the imperative was to secure assured and improved access to the United States market so as to avoid the threat of rising U.S. protectionism (including the more vigorous resort to the "contingent protection" or "remedy" provisions of U.S. trade law) and to anticipate the possibility of regionalization of the world trade system. Additionally, learning to compete successfully in the continental market was seen by many as the key feature of the national industrial strategy required to enable Canadian firms and industries to survive in an evermore competitive global marketplace. The U.S. seems to have been led into the CUSTA by a desire to demonstrate to the rest of the world that trade could be liberalized even in difficult times and sensitive sectors, and to show that pioneering agreements could be reached in the new areas about to be addressed in the GATT such as services, investment, and intellectual property. At the same time, the formation of the North American regional trading arrangement was a strategic threat to Europe and Japan to show that bilateralism and regionalism were alternatives, should the attempt being made in the Uruguay Round to revitalize multilateralism fail.

CUSTA and the International Economic Order

This, then, is the economic landscape within which the United States and Canada must pursue their economic, political, and social objectives.

In commercial terms, it is a world of unrelenting commercial rivalry between old and new competitors. The intensity of this competition is destined to grow with the further globalization of production through the internationalization of direct foreign investment, developments in transportation, the diffusion of technology, and the rising incomes of demanding consumers.

At the same time as international exchanges are growing, however, the openness of the international economy is threatened by the weight of persistent imbalances and by erosion of that combination of ideology, interest, and influence that created the post-war institutional framework that, thus far, has permitted cooperative interdependence to flourish. In part, this is due to the diminished ability of the architect of the system, the United States, to resist the protectionist demands that are fed by its twin deficits and by its inability to project its preferences on newer superpowers. In part, too, the decline of cooperation in managing the international economic system is attributable to Europe's preoccupation with completing the Community and forging links with other European states, and to Japan's continuing adherence to mercantilist policies and a free-rider role in world affairs.

The external responses of the United States and Canada to the emergence of protectionism and "blocism" have had both negative and positive elements. Unilateralism in trade and the provision of aid to sectors threatened by international competition have been features of the trade and industrial policies of both countries. And some see the CUSTA as a further blow to nondiscrimination and multilateralism. On the positive side, both countries fought to launch the Uruguay Round, and both have sought to ensure that the GATT negotiations lead to multilaterally freer trade in goods (including the bypassed agricultural and textiles sectors), that GATT's provisions extended to trade in services, investment and intellectual property, and that strengthened rules and disciplines are fairly applied and universally observed. Both have represented the CUSTA as being not only consistent with the letter and intent of the agreement, but also as an exemplar for the international community in the ambition and comprehensiveness of its liberalization "reach" and in providing models that can be emulated at the global level.

However, the CUSTA was never intended as a vehicle for the United States and Canada to exercise a joint commercial diplomacy in the international economic institutions. Furthermore, there are important differences on specific matters in the national proposals tabled in Geneva by each country (e.g., on agricultural support and protection, subsidies-countervail, and tariff cutting). Hence, in helping reshape world trade, the two countries have followed individual (though parallel and CUSTA-consistent) paths.

What about the relationship between the CUSTA and the competitiveness of the two countries in the global economy? Since the surest route to competitiveness is to compete, at the simplest level, the dismantling of tariff and non-tariff barriers to intracontinental trade is bound to contribute to the downsizing or elimination of uncompetitive firms and industries and to survival and enlarged market shares for those firms that can profitably "design, produce and market goods and services, the price and nonprice qualities of which form a more attractive package of benefits than those of competitors."

Beyond that, the intensification of continental competitive pressures will catalyze an examination of the sources of national competitiveness and stimulate appropriate policy changes. The list of candidate topics is long. A starting point for national and sectoral competitiveness is good macro policy, including the avoidance of budget and external deficits that increase the need for capital inflows and that produce interest and exchange rates that deflate demand and disadvantage producers of traded goods and services. Other appropriate roles for government include investing in human capital and in technology development and transfer, and ensuring that domestic sector markets are characterized by an entrepreneurial culture and by competitive horizontal rivalries and collaborative vertical relationships between the producers of traded products and their providers of inputs and infrastructural services. Private industry can also expect that public policies that, unintentionally, impede competitiveness by adding costs will be changed. Examples include regulatory overload and inappropriately targeted taxation and, in the case of Canada, interprovincial trade barriers that reduce competitive pressures and impede the attainment of scale economies. Beyond that, the emerging consensual view is that national competitiveness in continental and international markets is best left to competitive forces acting on private businesses.

If the above prescription is valid, it follows that (except perhaps through the concertation of international commercial diplomacy) there are not many advantages to be gained by a cooperative U.S.-Canadian approach to the global marketplace.

The trade-liberalizing provision of the CUSTA will intensify competition in regional, national, and continental markets, and this competitive pressure is the surest source of the competitiveness needed to profitably hold and build market shares in the global economy. And, in any event, the provision of good macro, technology, education, regulation, and competition policies is a matter of national jurisdiction and responsibility, not something to be undertaken by the institutions of a trade agreement or by transborder agencies.

A National Perspective

Canada and the U.S.: Relative Competitiveness of Selected Agri-Food Industries†

*Larry Martin, C. Ford Runge, and Erna van Duren**

The announcement of the Canada-U.S. Trade Agreement (CUSTA) was immediately followed by claims in Canada's agri-food industry that it could not compete in either the processing or the producing sector. These claims were overwhelmingly based on the perception that Canada is a small country with relatively higher production costs. The argument was that minor adjustments in the U.S. would swamp Canadian industry and put much of it out of business.

In addition, many on both sides of the border held that each country's subsidies would give the other unfair advantage -- despite the fact that the Organization for Economic Cooperation and Development's (OECD's) 1987 calculations put both in the over 40 percent range of protection as measured by Producer Subsidy Equivalents (PSEs). More recent calculations by the U.S. Department of Agriculture (Roningen and Dixit, 1989) are shown later in Table 1. There is probably so much uncertainty in the calculations of PSEs that a statistician would never be able to say whether Canada's level of protection is above or below that of the U.S. (Hertel, 1990).

A third argument, heard in Canada, is that its higher short-term interest rates and correspondingly over-valued exchange rate are major impediments to the ability of the agri-food sector to compete. On the U.S. side, the argument is that Canada's 87-cent dollar, as of August 1990, would allow undercutting of U.S. prices.

Sadly, neither government did extensive analysis on the relative competitiveness of their agri-food sectors, either before or at the time of the negotiations. Canada commissioned two studies, both of which were based largely on opinions which generated a great deal of fear (de Grandpre, 1989).

The relative competitiveness of industries in the agri-food sectors of the U.S. and Canada and the adjustments that will occur because of the CUSTA remain issues of considerable interest. They are of interest because both governments are in the process of redeveloping agricultural and international trade policies. Many of the most important agricultural negotiating issues under the CUSTA were relegated to the multilateral negotiations in the Uruguay Round of the General Agreement on Tariffs and Trade (GATT). In all likelihood, the framework agreement in

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agriculture apt to emerge from the GATT in early 1991 will not provide sufficient discipline or guidance to resolve the bilateral ambiguities over agriculture under the CUSTA. Instead, recourse will be made to the dispute resolution process of both the GATT and the CUSTA itself. More important than either the GATT rules or the CUSTA provisions for the future of U.S.-Canada trade frictions will be the private business policies of those national and multinational companies involved in the agri-food industry.

Today, the paucity of information over relative competitiveness continues to exist. However, several steps are being taken in both Canada and the U.S. to lower the level of ignorance. Work in the Ministry of Agriculture's Task Force on Competitiveness in the Agri-Food Industry and projects sponsored by Industry, Science and Technology Canada and by the Industrial Restructuring Commissioner of Ontario have been initiated to address the issues. This work partially serves as background for this paper. The objectives of the paper are: (1) to put forward a framework for measuring competitiveness, (2) to discuss some general conclusions about competitiveness in the agri-food sector, and (3) to make specific comparisons for a few industries in which administered prices are used by Canada.

The Framework

Economists typically think of trade issues in terms of international trade theory. While trade theory is based on comparative advantage, many casual observers (and some who should know better) let their thinking about competitiveness slip into simplified comparisons of unit production costs. But international trade theory has value; it tells us that prices of limiting factors of production adjust to market conditions. In other words, the value of land, labor, and management are more <u>reflections</u> of competitiveness than variables that cause it. For example, we know of a tomato grower who paid $6,000 per acre for tomato land in southwestern Ontario this past year. Tomato production and processing, according to de Grandpre (1989), are parts of the agricultural industry that were supposed to disappear from Canada as a result of the CUSTA. Is the fact that tomato land in southwestern Ontario costs $6,000 per acre a factor that will contribute to its demise because it makes tomato production a high-cost industry? Or, assuming the grower is rational (which we know), is the price of $6,000 per acre an indication of how competitive southwestern Ontario <u>can be</u>? A useful hint is that two years ago into the CUSTA, Ontario's tomato processing industry contracted a record amount of tomatoes to be grown in Ontario.

Another problem is that factors like land, owners' labor, and management are so heterogeneous in their characteristics that generalizations about their prices are difficult to make, at best. All this means is that cost is not an adequate basis on which to measure competitiveness.

The problem is compounded by the fact that, when one links together the farm production and food processing components of the market, it quickly becomes obvious that we are dealing neither with homogeneous firms nor with homogeneous products and services. In both countries' agri-food sectors, we are dealing with the entire spectrum of small local companies, large domestic-based companies, and very large, internationally-based multinationals. All of them have different objectives and goals. Each attempts to be competitive through some combination of cost, differentiation, and mass, niche, or focus marketing. When one puts the reality of market differentiation and market structure together, comparisons of cost are generally quite tenuous measures of competitiveness. Consider the Honda Accord automobile. It is by no means the lowest price car in its class. However, it is very competitive.

Taking these realities into account means that a broader framework is needed. The most notable attempt to develop such a framework to date is Porter (1990), who has developed a theory of national competitiveness based on four "diamonds" (Fig. 1). In general, competitiveness is defined as the sustained ability to profitably gain and maintain market share.

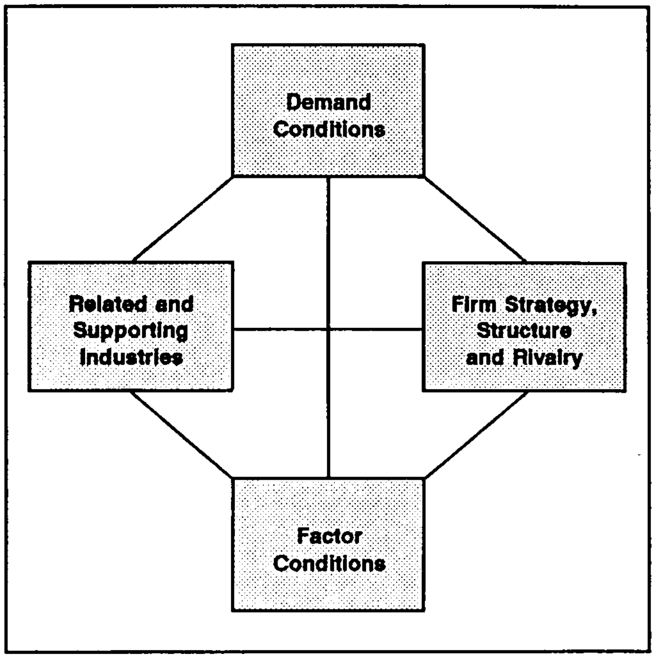

Figure 1. ***Determinants of National Competitive Advantage, Individually and Jointly.***

Porter's four diamonds are:

(1) Demand Conditions. This refers to the nature of domestic demand for the sector's product. Competitive advantage is gained when domestic demand gives firms in a sector a clear early picture of emerging demand trends and where buyers put pressure on companies to innovate faster than their foreign rivals.

(2) Factor Conditions. This refers to a country's position in factors of production such as skilled labor or infrastructure. It is the creation of factors such as skilled labor or technology that is important, not the endowment of natural factors.

(3) Related & Supporting Industries. This refers to the presence of strong suppliers of inputs into a production process. Internationally competitive home-based suppliers can create advantages in downstream industries.

(4) Firm Strategy, Structure & Rivalry. The way companies are created, organized, and managed affects competitiveness, as does the degree of domestic rivalry.

In addition to the four "diamonds" of Porter's framework for the private sector, there is also a role for government. Governments can be catalysts in assisting the sector to achieve the conditions implicit in Porter's framework. Governments can raise the aspirations of companies by providing an environment and infrastructure that encourages them to move to a higher level of competitive performance. In part, this is accomplished by the ways in which governments work in the background to improve demand and factor conditions to support supply industries and to encourage rivalry among competing firms. A fairly large leap is required to move from the basic framework developed by Porter to one that allows objective research to be done. The leap is accomplished through a classical business policy approach to analyzing competitiveness. The framework for measurement is depicted in Figure 2. The elements of the framework are described below.

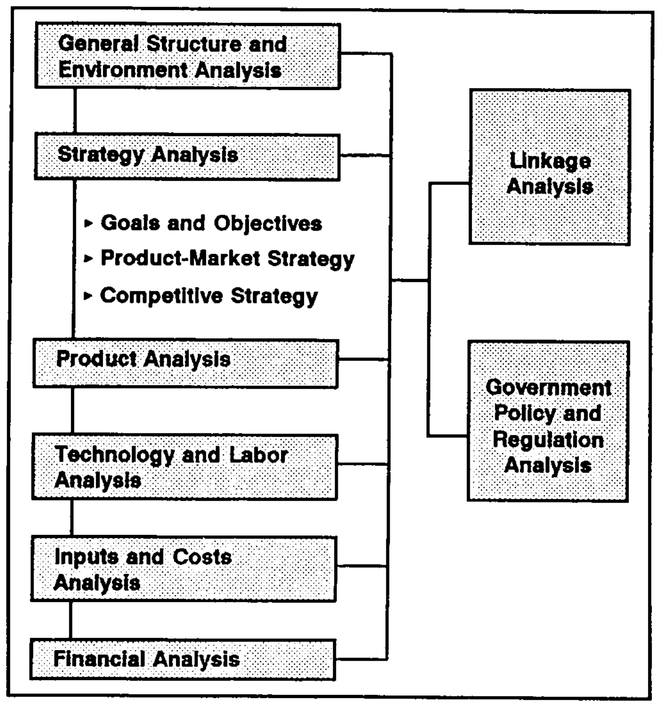

Figure 2. ***Framework for Analyzing Competitiveness Utilizing Classical Business Policy Approach.***

General Structure and Environment Assessment

The first step in developing a profile of the competitive state of an industry is to determine its general structure, how firms at various market levels relate to each other, and the economic environment in which firms in the industry operate. This step is required before the competitive strategies of the relevant groups of firms can be identified. In turn, firms' competitive strategies suggest which components of the framework for assessing competitiveness are most relevant in that industry, or industry segment.

Strategy Analysis

Firms' goals and objectives, the product-market strategies that they use to exploit the nature of demand for their products, and the supporting or competitive strategies that firms use to attempt to obtain a sustainable competitive advantage jointly determine the competitiveness of firms, and thus industries. Firms may use one or a combination of several product-market strategies including mass and niche marketing. They may also use one or a combination of competitive strategies: low delivered cost, differentiation, or a niche or focus strategy.

Product Analysis

If examination of a firm, or firms, in an industry segment which is increasing its market share indicates that many of these firms have pursued a product differentiation strategy, or a focus strategy, then the firms' products will be important in explaining competitiveness. In particular, the products marketed by these firms must be assessed relative to those of the most important competitor(s) in the domestic and/or export market. A product is defined as the set of physical, service, and perceived characteristics that a firm uses to compete within a given market. As such, the product analysis must relate to these three sets of characteristics in a manner appropriate to the level of the market. Market share analyses can be performed subsequent to the product analysis.

Technology and Labor Analysis

Whatever strategy a firm is judged to be pursuing, its technology and labor resources are likely to be important to its competitiveness. Since food production or processing technology may require either skilled or non-skilled, low-cost labor, either advanced or simple technology, the technology and labor used by various firms within the industry should be analyzed jointly.

Inputs and Costs Analysis

If initial examination of a firm or industry segment indicates that it is successful because it has pursued a mass market and low delivered cost strategy or a focus strategy, then an analysis of its inputs and costs will be relatively more important than an analysis of how its products contribute to competitiveness. Input costs can be grouped as production costs, marketing costs, and process or operations costs. Cost analysis is a tricky business because input costs reflect the prices of outputs, because business structures are seldom so similar that a variety of adjustments are not needed, and because productivity of individual inputs and the joint productivity of these inputs must be taken into account.

Financial Analysis

Since the working definition of competitiveness refers to the sustained ability to profitably gain and maintain market share, analyzing competitiveness requires examining financial performance of successful firms, an industry segment, or an industry. Constructing an appropriate indicator of profitability is a difficult task, since the best indicator of profitability varies by industry and market level, and even if the best indicator is the same across industries and market levels, acceptable levels of return vary by industry.

Government Policy and Regulation Analysis

Any of the factors discussed in the previous sections can potentially be affected by government policies and programs. The channels of potential influence are macroeconomic policy and sector-oriented programs, which affect product markets, input markets, technology, and other resources used or potentially used by firms. Each of these policy instruments interact with economic, demographic, and psychographic factors, as well as other policy instruments, to affect the competitiveness of an industry.

Using such a framework, a competitiveness assessment must begin with a general determination of whether the policy facilitates or inhibits firms at a given market level within an industry from being successful with their strategies.

Linkage Analysis

None of the components cited above can be considered in isolation, and all must be considered in an iterative fashion. For example, product-market strategies are affected by technology, which in turn affects input use and cost. The relationships among these components of the competitiveness framework, and relationships among firms and segments within an industry, are the overarching factors contributing to the competitiveness of any firm, industry segment, or industry. We call these relationships <u>linkages</u>.

Some Early Evidence About Competitiveness

As indicated earlier, two major exercises undertaken in Canada begin to measure competitiveness and to determine the necessary adjustments in a freer trading environment. The first is the work of the Task Force on Competitiveness in the Agri-Food Sector. The second is work being undertaken by Industry, Science and Technology Canada (ISTC) and Ontario's Industrial Restructuring Commission (IRC).

Task Force on Competitiveness of the Agri-Food Sector

The Task Force is one of several instituted by Agriculture Minister Mazankowski and the Provincial Ministers of Agriculture to conduct a thorough review of agricultural and food policy. This Task Force was composed of 57 members from all components of the Canadian agri-food sector. It had four months to operate. Its mandate was to identify impediments to the ability of the agri-food sector to compete and to make recommendations for change. Obviously, its organization did not allow it to apply the foregoing framework with a great deal of precision or detail. However, the Task Force organized itself into six working groups which were structured very much like the framework. They included: (1) Input Prices and Costs, (2) Technology and Human Resources, (3) Macroeconomic Policies, (4) Regulation, (5) Market Development, and (6) Collaborative Relationships (Linkages).

The conclusions of the Task Force are summarized below:

(1) Collaborative relationships between suppliers and customers are critical in achieving competitiveness. There has been too little encouragement of collaborative relationships in the past.

(2) Except for short-term interest rates and specific tax measures, Canada's macroeconomic and social policies do not impede attainment of competitiveness for this sector.

(3) There appear to be fewer differences in prices of inputs used by this sector relative to the U.S. than some people perceive. However, there are some differences that have substantial impacts on production costs for farmers and processors. Those differences should be focused on and corrected. They include oil-based energy, pesticides, and some raw products.

(4) There are difficulties in obtaining raw products by many firms in the processing industry, especially further or secondary processors. Most of these difficulties result from existing marketing structures. As a result,

there are conflicts between levels (i.e., primary and further processors) of the sector.

(5) Even if raw-product prices and input prices were equated to U.S. levels in Canada, much of the food processing industry has a high cost structure that limits the ability of many companies to be competitive. This cost structure results from diseconomies of size associated with small plants and too little adoption of advanced technology.

(6) Research and development in the food processing industry is limited and technology transfer facilities are unfocused and unspecialized. The state of technology adoption in the sector lags behind other countries and behind what is attainable.

(7) Human resources need to be upgraded in the sector at all levels, from plant worker to management.

(8) The regulatory environment in which the Canadian agri-food sector operates often hinders its development and innovation.

(9) Market development efforts by the private sector and by governments need improvement.

Competitiveness of Food Processing

Results of the work conducted for the Industrial Restructuring Commission (IRC) are interesting in that they do address costs and relative prices for several products whose prices are administered by Marketing Boards in Canada. They also illustrate numerically some of the conclusions of the Competitiveness Task Force. However, more than anything else, they indicate that there is a wide range of competitive situations that exist in the two countries.

In the remainder of this paper, we will address partial results for four commodity subsectors that were analyzed for the IRC: Chicken, Dairy, Tomatoes, and Winter Wheat.

Chicken. In the case of chicken, prices are set unilaterally by provincial Marketing Boards. There are provincial and national production quotas and import quotas on foreign products. Therefore, the market is highly protected and the Marketing Board has a large amount of power. Table 1 contains, first, the average prices in Canada and the U.S. during the pre-CUSTA period, 1985-87. They are all expressed in Canadian funds. Note that while both live and processed prices are higher in Canada, they are relatively higher for processed products. The second component of Table 1 shows the average gross margin for processed chicken per kilogram of product.

TABLE 1.
Estimated Impact of Free Trade on Margins for Primary Processed Chickens
(Canadian $/Kg.)

	Prices		Gross Margins		Net Margins
	Cdn.	U.S.	Cdn.	U.S.	Cdn.
Pre-CUSTA (1985-87)					
Raw product	109.5	93.2			
Processed product	209.8	155.1			
Pre-CUSTA (1985-87)			64.7	29.3	8.7
At landed cost w/tariff			41.4		-14.5
Without tariff			28.6		-27.4

Consistent with the observation about relative prices, Canadian processing margins are roughly double those of the U.S. The final column of Table 1 indicates the net margin after deduction of all costs. These are based on the actual operation of a major Ontario processing plant. We have no similar data for a U.S. processing plant. The last two rows of Table 1 show what the gross margin would be if (both processed and live) chickens were imported into Canada with the existing tariffs. In other words, these are the margins that would exist if Canadian processors had to sell finished product at a price equal to the U.S. price plus transportation costs and tariffs, and were able to buy live chickens under the same conditions. Another way to think about that situation is that it would reflect the estimated gross margin in Canada if the only restriction to trade was a tariff. As can be seen, this situation would give the Canadian processor a gross margin that would still be in excess of the U.S. processor. However, without adjusting for quantity, calculations of the net margin would put the Canadian processor at a distinct loss in this case.

Finally, we show the gross and net margins under the assumption that Canadian processors competed with U.S. processors under conditions with no tariff and no Marketing Board operation. In this case, the Canadian gross margin would be similar to the U.S. gross margin. However, the net margin would be nearly as large on the negative side as the gross margin is on the positive side.

These data suggest several interesting conclusions. Both the primary production and primary processing components of the chicken industry in Canada are highly protected by the pre-CUSTA situation. Second, with that protection and assuming no adjustments in the cost structure of processors, Canadian processors would be extremely noncompetitive without such protection. Of course, the foregoing conclusion was conditioned by the assumption that there would be no adjustment in cost. It does not seem logical to make that assumption, given that almost every chicken processor in Canada has complained or is complaining about an inability to get raw product. Without the protection of the Marketing Board and imports, one would expect a very different structure to emerge in the poultry processing sector.

Dairy. Table 2 presents similar data for the dairy industry. We begin Table 2 with the average raw and finished prices for fluid

TABLE 2.
Estimated Impact of Free Trade on Margins in Dairy Processing, 1985-87
($ Cdn.)

	Fluid Milk		Industrial Milk (Cheddar)		Industrial Milk (Butter)	
Pre-CUSTA Prices	**Raw ($/HL)**	**Processed ($/HL)**	**Raw ($/HL)**	**Processed ($/Kg)**	**Raw ($/HL)**	**Processed ($/Kg)**
Canadian	52.5	69.9	39.0	5.74	39.6	5.22
U.S.	38.9	50.6	35.7	3.78	35.7	4.26

	Milk			Cheddar			Butter		
	Cdn. ($/HL)		U.S.	Cdn. ($/Kg)		U.S.	Cdn. ($/Kg)		U.S.
Gross & Net Margins	**Gross**	**Net**	**Gross**	**Gross**	**Net**	**Gross**	**Gross**	**Net**	**Gross**
Pre-CUSTA	16.80	6.09	11.70	1.86	1.43	0.31	2.07	1.87	1.41
Landed U.S. Cost:									
With Tariff	11.70	1.13		0.40	-0.04		1.82	1.62	
Without Tariff	11.70	1.13		0.93	0.05		2.06	1.86	

milk, industrial milk used for cheddar cheese, and industrial milk used for butter. Our data are for Ontario in Canada and New York State in the United States. As for chicken, raw product prices are higher in Canada, but processed products are even higher in relative terms.

This seems to follow through to gross margins, which are contained in the bottom half of the table. As with chicken, we have recalculated the gross and net margins, assuming first that the protection of import quotas is relaxed to 5 percent of the previous year's production, and second, that the protection of tariffs is removed. In this case, gross margins decline rather substantially. However, they do not fall below U.S. levels. Moreover, Canadian net margins under free trade do not go negative, as they did with chicken. In fact, with respect to butter, the Canadian net margin under free trade is higher than the estimated U.S. gross margin.

These data suggest two conclusions. First, as with chicken processors, dairy processors in Canada benefit from the protection afforded under the supply and management system. However, the second conclusion is that under a free trade scenario, Canadian processors appear to be able to compete very well, at least in some product lines.

Tomatoes. Table 3 contains similar data for tomato processing. The prices in this case refer to Ontario and Michigan. They are for 1987.

Once again, it is clear that processed product prices are relatively higher than raw product prices in Canada. The analysis of gross and net margins in this commodity is interesting. In the pre-CUSTA situation, Canadian gross margins were double those of the U.S. and net margins were very healthy. When we take away the protection and go to a free trade situation, gross margins in Canada decline by about one-third, but are still higher than in the United States. However, U.S. net margins are negative.

Two interesting conclusions emerge from these data. Before CUSTA, Canadian tomato processors were able to extract greater benefits than their nominal level of protection would have suggested. There is very little protection beyond tariffs except for that potentially obtained by product regulation.

TABLE 3.
Estimated Impact of Free Trade on Margins in Tomato Processing Industry

	Prices ($/100 Kg.)	Gross Margins ($/100 Kg.)		Net Margins ($/100 Kg.)
	U.S.	Cdn.	U.S.	Cdn.
Pre-CUSTA				
Tomatoes	10.18			
Tomato paste	91.00			
Margins				
Pre-CUSTA		64.28	33.29	20.41
At landed cost w/tariff		41.79		-2.07
Without tariff		42.10		-1.76

Therefore, the difference between the actual gross margin pre-CUSTA and the gross margin of landed U.S. cost plus tariff very much represents the ability to extract economic rent. In this industry, prices are not established unilaterally by the Marketing Board. Rather, growers and processors negotiate with one another. It would seem from the one year of data contained in Table 3 that in this particular year (1987) the processors were very astute negotiators.

The second conclusion is that if processors retain their pre-CUSTA cost structure in the post-CUSTA environment, investment in tomato processing will not be particularly attractive. Many firms in the tomato processing industry have been among the loudest to complain about high raw product prices in Canada. It would appear that their complaints are well founded. Having said this, it is our distinct impression that a number of companies have made substantial strides to improve their productivity in this industry during the past two years, perhaps justifying the land prices noted earlier.

Winter Wheat. The final table (Table 4) contains prices for wheat and flour, specifically soft winter wheat. These prices are more reflective of Eastern Canada than Western Canada. Prior to the CUSTA, Canada employed a two-price system. This system generally resulted in higher domestic prices than export prices for all wheat. The higher prices in Canada were maintained by the use of import licenses that had to be obtained from the Canadian Wheat Board (CWB). In fact, the CWB never issued import licenses. Therefore, the licenses have acted as an import quota equal to zero.

TABLE 4.
Estimated Impact of Free Trade on Prices in Flour Industry

	Raw Product		Flour	
	Cdn.	U.S.	Cdn.	U.S.
Pre-CUSTA	253.70	147.20	456.80	261.53
At landed cost w/tariff	157.27		280.50	69.00
Without tariff	157.27		274.99	

With the announcement of the CUSTA, it was simultaneously announced that the two-price system for wheat would come to an end. Thus the data in Table 4 bear no reflection on what has happened since the beginning of 1989. The data do show very clearly how dramatic was the difference in relative price levels for both raw and finished product before 1989, and how much closer they will be as import licensing requirements are lifted under the CUSTA.

Conclusion

In conclusion, our initial results suggest a rather "mixed bag." Some Canadian industries will be under considerable competitive pressure if truly free trade were to occur. Others would fare well vis-a-vis their U.S. counterparts. However, it is doubtful that the GATT powers will impel such free trade, and some levels of border protection are likely to remain under the CUSTA. How, where, and how much liberalization will benefit Canada will depend on the willingness of various industries to adjust, foregoing government shelter for market expansion opportunities. Only complex and specific market-level analysis, developed under the sort of comprehensive framework discussed above, can capture the subtle and difficult issues involved in such adjustments. And even then, competitiveness is a moving and elusive analytical target.

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Regional Perspectives

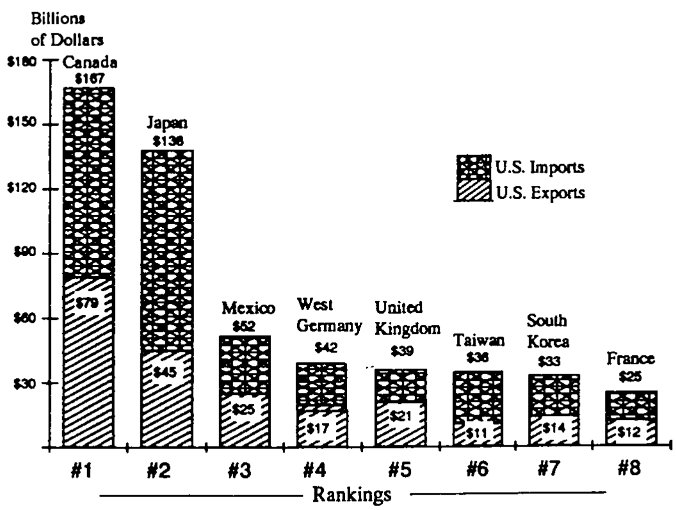
Regional Dimensions of U.S.-Canada Trade and Prospects for Trade Expansion in the "West"

*Larry D. Swanson**

While the United States' trade relationship with Japan dominates many U.S. policy discussions on international trade, U.S. trade with Canada is actually 20 percent greater than that with Japan. In terms of exports only, U.S. goods exports to Canada exceed exports to Japan by 75 percent.

The United States' trade relationship with Canada is not only large, but growing. Since 1982, two-way trade between Canada and the U.S. in both goods and services has increased by 48 percent, growing to over $205 billion in 1989 (with $167 billion of this in goods trade and the rest in services) (Fig. 1). This trade relationship is expected to expand even more under the Canada-U.S. Free Trade Agreement (CUSTA) instituted in January 1989.[1]

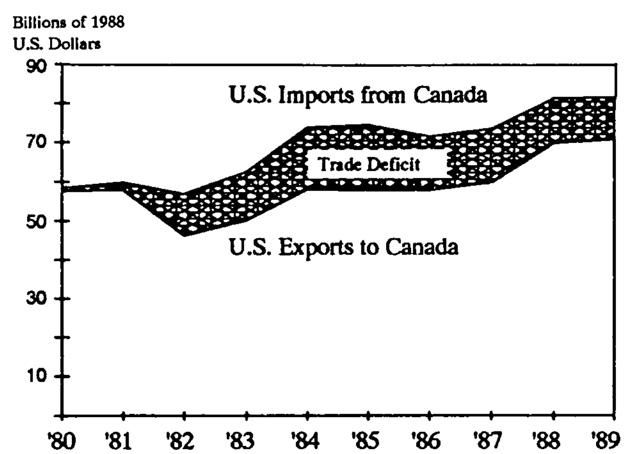
Figure 1. ***The United States' Biggest Trading Partners (Value of Goods Trade in 1989*).***



*Figures include end use trade in products and commodities only, not services trade. (Source: International Trade Administration, U.S. Dept. of Commerce.)

U.S. imports from Canada exceed its Canadian exports, but this trade deficit has been closing in recent years (Fig. 2). A strong U.S. dollar during the 1980s, making U.S. goods more expensive relative to those of other trading nations, contributed to this trade imbalance. However, the Canadian dollar has risen by more than 20 percent against

Figure 2. ***U.S. Goods Trade with Canada.***



Source: Statistics Canada

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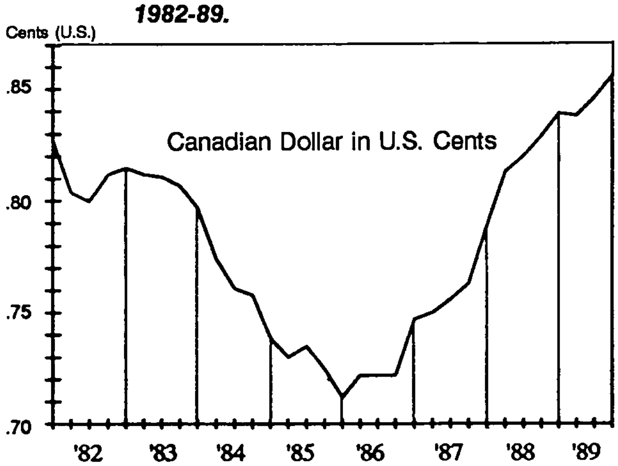
[1]An overview of the FTA is presented in a previous article by the author entitled, "The U.S.-Canada Free Trade Agreement: What It Is and Its Implications for Montana," *Montana Business Quarterly*, Bureau of Business & Economic Research, School of Business Administration, University of Montana, Missoula, Summer 1990. Portions of this discussion also are based upon this article.

the U.S. dollar since 1986, and the U.S. trade deficit has narrowed (Fig. 3).

Figure 3. ***U.S.-Canada Currency Exchange Rate, 1982-89.***



Source: International Monetary Fund, *International Financial Statistics*

Composition of U.S.-Canada Goods Trade

The single industry most involved in U.S.-Canada trade on both sides of the border is the auto industry. Trade in motor vehicles (passenger cars and trucks) and motor vehicle engines and parts is the largest export category for both the U.S. and Canada, accounting for 28 percent of U.S. goods exports to Canada and 34 percent of U.S. imports from Canada. Trade in this area has been sanctioned for years under the U.S.-Canada "Auto Pact" and an integrated, auto and auto parts manufacturing "complex" has developed on both sides of the U.S.-Canada border in the Great Lakes region.

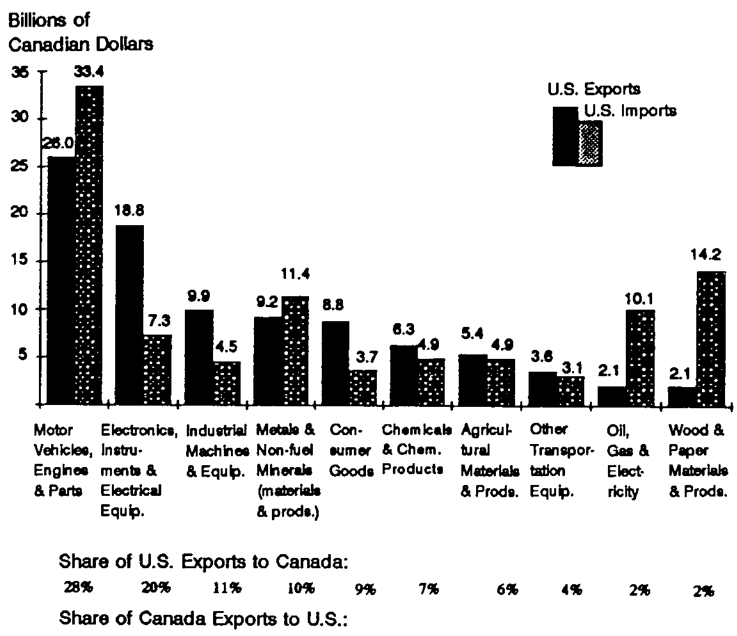
The second largest category of U.S. exports to Canada is electronics (telecommunication and computer equipment), instruments (assorted measuring and control devices and equipment), and electrical equipment in general. These products account for 20 percent of the United States' Canadian export. Other major U.S. export categories are industrial equipment (11%), metal and nonfuel mineral products (10%), and a broad array of consumer goods (9%) (Fig. 4).

Major product categories exported by Canada to the United States are wood and paper products (15%), metals and nonfuel mineral products (12%), and energy commodities including oil, natural gas, and electricity (10%). Two-way trade in agricultural commodities and products is limited, accounting for only about 6 percent of the United States' exports to Canada and 5 percent of its Canadian imports (Fig. 4).

Regional Distribution of U.S.-Canada Trade

Reflecting the large auto industry trade between the two nations as well as other industrial trade, a considerable share of U.S.-Canada goods trade is concentrated among Upper Midwest states (primarily Michigan, Ohio, and Illinois) in the United States and in Ontario, Canada's "industrial heartland," which lies directly north of these states (Fig.

Figure 4. ***Composition of U.S.-Canada Goods Trade, 1989.***



Source: Statistics Canada

5). The Upper Midwest Region accounts for 40 percent of the U.S. exports to Canada and receives 40 percent of its imports from Canada. Ontario accounts for 57 percent of Canada's exports to the U.S. and receives 70 percent of Canada's U.S. imports.

States in the Northeast Region (including New York and Pennsylvania) account for over 20 percent of U.S. exports and 28 percent of U.S. imports from Canada (Fig. 5). The Southeast Region is the third most active U.S. region in Canadian trade. Altogether, states east of the Mississippi River account for over three-fourths of U.S. export and import trade with Canada. Only a small portion of the trade, at least as it occurs in the first round of transactions between U.S. and Canadian buyers and sellers, involves western states and provinces. The Census Bureau's "Mountain Region" and the eight

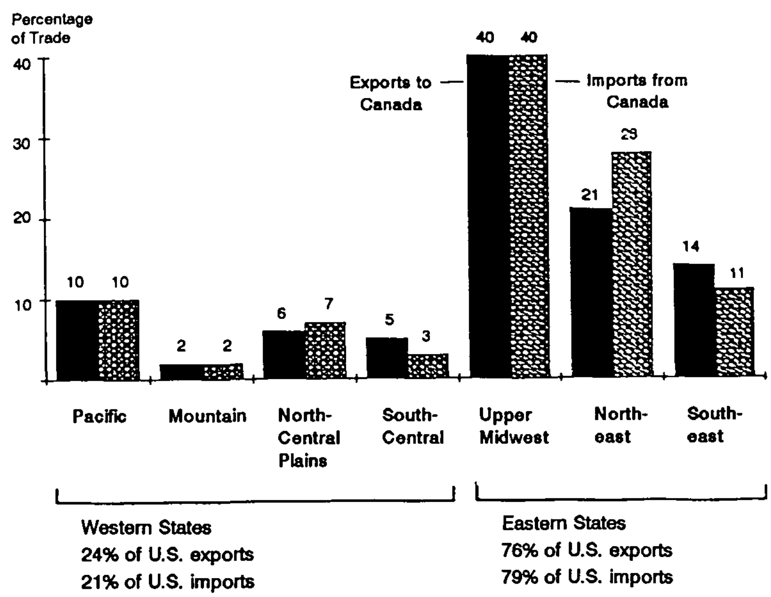
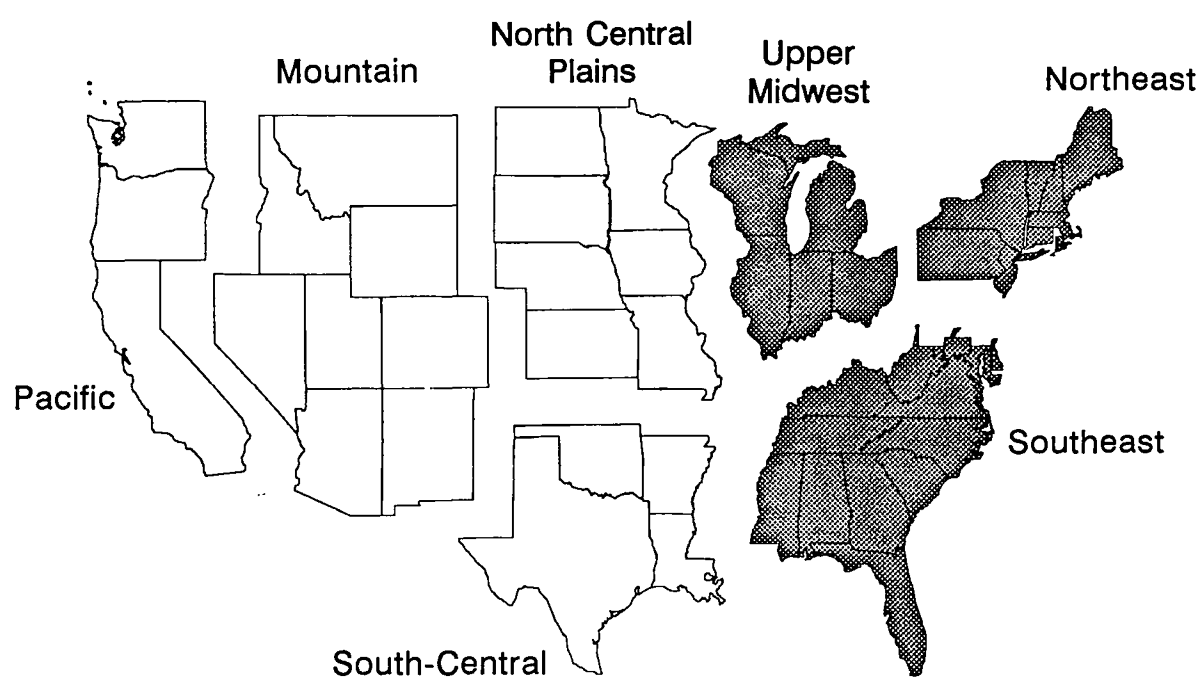


Figure 5.
U.S. Regional Distribution of U.S.-Canada Goods Trade, 1989

Source: Statistics Canada, Ottawa, and Bureau of Business & Economic Research, University of Montana (regions based upon U.S. Census Bureau regions).

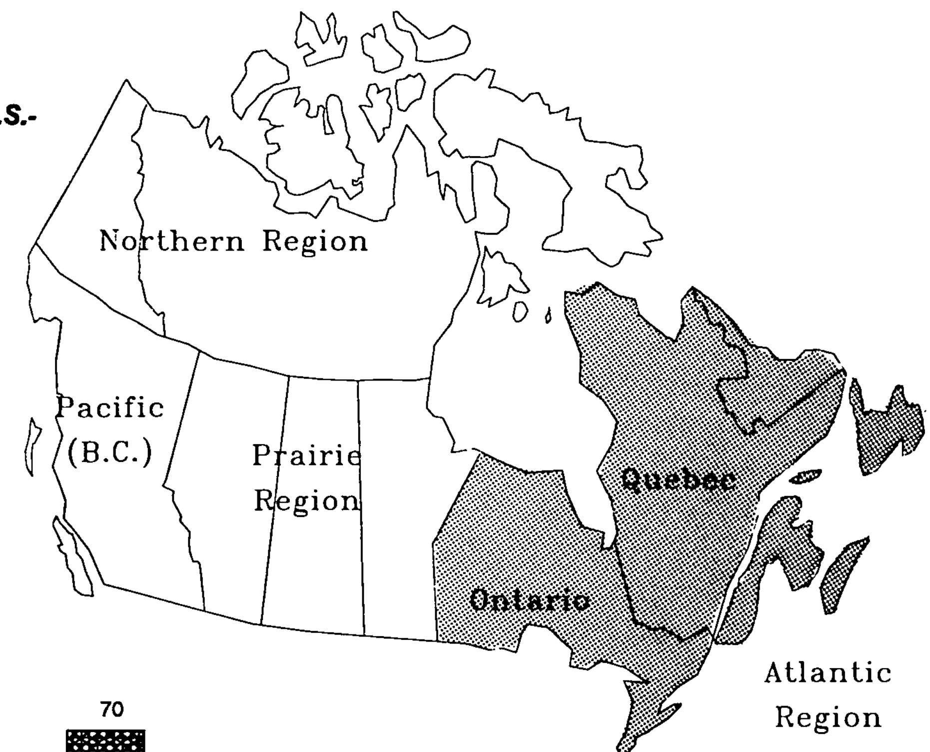


states it comprises (including Montana) is the region that has been least involved in U.S.-Canada trade, providing only 2 percent of the exports and receiving only 2 percent of the imports (Table 1, page 35).

In Canada, the regional distribution of U.S. trade is even more concentrated in the East (Fig. 6). Together, the eastern provinces of Ontario, Quebec, and the four Atlantic provinces supply nearly 80 percent of Canada's exports to the U.S. and receive 85 percent of Canada's U.S. imports (Fig. 6). The sparsely-populated northern provinces (Yukon and Northwest Territories) have very little involvement in U.S. trade. The four western provinces of British Columbia (Pacific Region) and Alberta, Saskatchewan, and Manitoba (Prairie Region) account for the balance of the trade.

Figure 6.
Canadian Regional Distribution of U.S.-Canada Goods Trade, 1989

Source: Statistics Canada, Ottawa, and Bureau of Business & Economic Research, University of Montana (regions used by Statistics Canada for trade information).



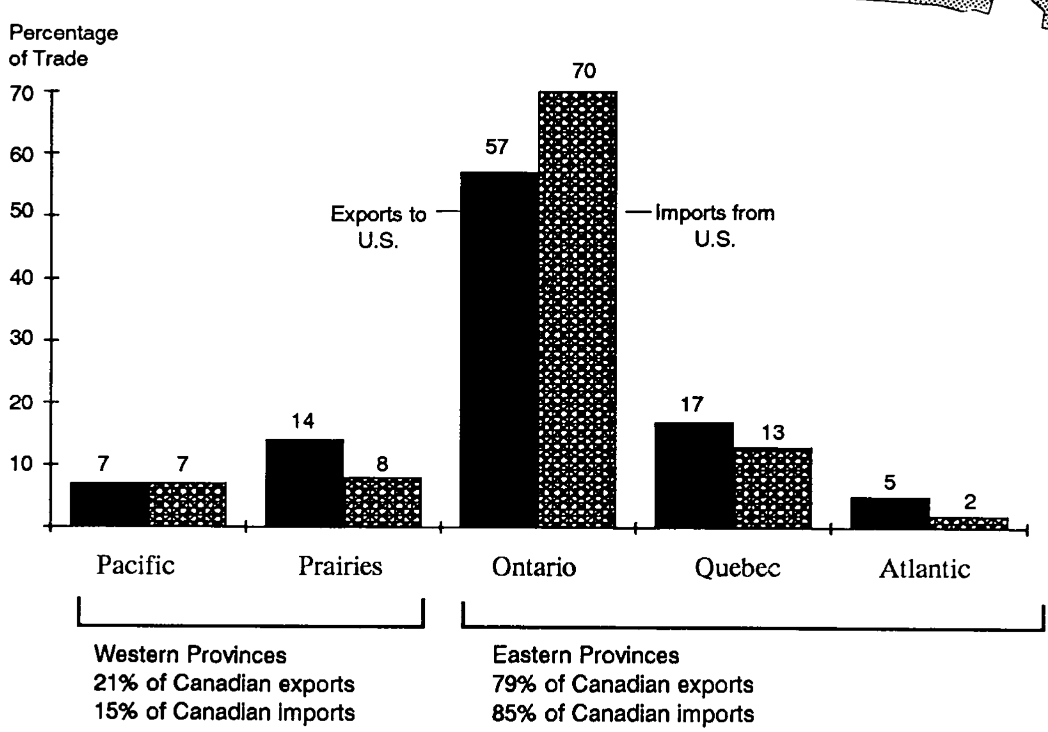


TABLE 1.
Direct Goods Trade with Canada by Rocky Mountain States*
1989
(Millions of Canadian Dollars)

States	Exports	Imports	Total Trade
Montana	$ 144.2	$ 831.4	$ 975.6
Idaho	171.3	170.8	342.1
Wyoming	57.1	40.0	97.1
Colorado	462.3	305.4	767.7
Utah	384.3	162.3	546.5
Nevada	199.9	137.6	337.5
Arizona	598.7	308.7	907.4
New Mexico	23.9	91.2	115.1
Total ($ Cdn.)	$2,041.7	$2,047.4	$4,089.0
Total ($ U.S.)	$1,724.2	$1,729.0	$3,453.2

SOURCE: Statistics Canada, Ottawa.

*States included in the U.S. Census Bureau's "Mountain Region."

Note: Totals in Canadian dollars are converted to U.S. dollars by using an average annual exchange rate in 1989 of .8445 (Source: International Monetary Fund).

Potential Expansion of North-South Trade in the West

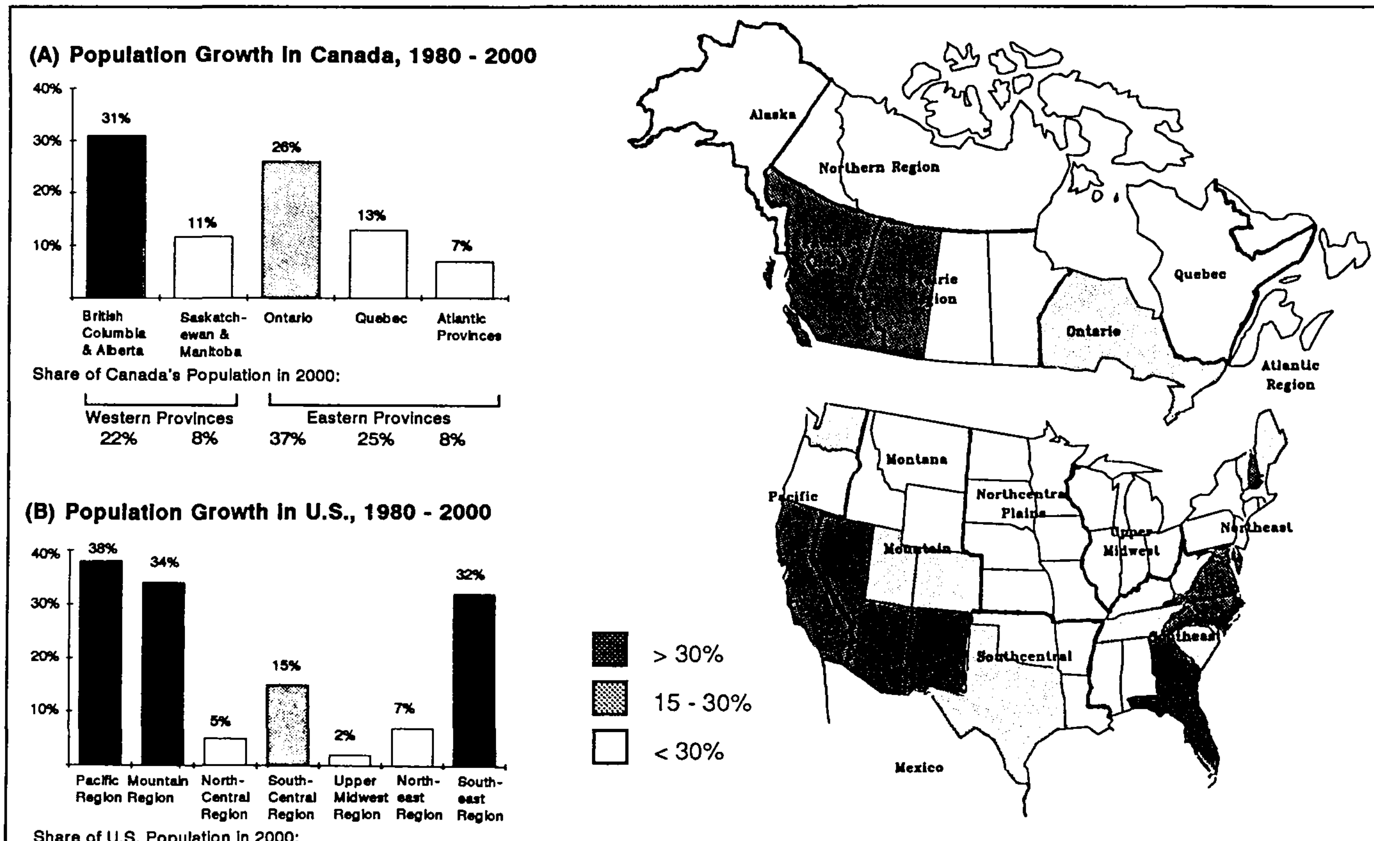
While the East is currently the focus of most U.S.-Canada trade activity, several factors point to considerable expansion in north-south trade among western states and provinces. The first is the Free Trade Agreement itself. Perhaps the most publicized elements of the agreement are its provisions for the eventual elimination of all tariffs affecting U.S.-Canada trade. However, 70 to 80 percent of the goods trade between the United States and Canada was already tariff-free prior to the CUSTA and was unaffected by this tariff-removal provision. But, for industry and product areas where tariff and other trade restrictions did exist, trade between the countries had been significantly constrained. Some of the greatest trade barriers were among products in such areas as agriculture, wood products, energy, and other natural resource-based sectors -- sectors that historically have been most protected from foreign competition by both the U.S. and Canadian governments.

In that these same industries are primarily located in the West (both in the United States and Canada), U.S.-Canada trade involving western states and provinces may have been most affected by the type of trade restrictions the CUSTA is eliminating. As trade and investment barriers are removed, regionally-defined, resource-based, industry "complexes" in agriculture, energy, wood products, mineral development, and tourism will more freely develop across the U.S.-Canada border in both directions. While some industries and firms on both sides of the border will "win" and some will "lose" as this occurs, north-south trade and commerce in the West will undoubtedly increase under this freer trade environment (and potentially increase more than what will occur in the East as a result of the Agreement).

Current and emerging population trends in both countries also may serve to increase north-south trade in the West. U.S. population growth in the last decade, and as projected for the current decade, is concentrated in three regions, two of which are in the West. By the year 2000, the population of the Pacific Region is expected to exceed its 1980 population count by 38 percent (based upon the U.S. Census Bureau's "Series A" forecast. The second fastest growing region is the Mountain Region, expected to increase in population by 34 percent during the same period. Significant population growth also is occurring in the South Central Region (primarily in Texas), which is also in the West (Fig. 7).

In Canada, two of the three fastest growing provinces are in the West as well -- British Columbia and Alberta, with expected populations in the year 2000 more than 30 percent greater than 1980 levels. The western prairie provinces of Saskatchewan and Manitoba are growing as well. Four of Canada's 10 largest cities are in these four western provinces. These include Vancouver, B.C., with a population of around 1.5 million; Edmonton, Alberta, with a population of 800,000; Calgary, Alberta, with a population of almost

Figure 7. *Current Trends in U.S. and Canada Population Growth, 1980 - 2000.*



Sources: (A) Statistics Canada, Ottawa (*Scenario III* projections). Note: The sparsely populated provinces in the "Northern Region" are excluded. (B) U.S. Census Bureau (Aug. 1989, *Series A* projections). Note: The population of Alaska is projected to increase by over 40% during this period, but this is not indicated on the map because it is so sparsely populated.

700,000; and Winnipeg, Manitoba, with a population of around 650,000.

In that trade flows toward and away from growing regions, the future regional distribution of U.S.-Canada trade among states and provinces should reflect greater activity in the West, on both sides of the border.

A third factor that could further expand north-south, transnational trade is the potential inclusion of Mexico in an even larger "tri-national trading bloc" along with the U.S. and Canada. Current U.S. trade with Mexico is exceeded only by its trade with Canada and Japan. Ways of liberalizing trade with Mexico are now being explored. If trade with Mexico by both the U.S. and Canada expands, opportunities for north-south trade and commerce across borders in the West would be further expanded as well. However, devising provisions of freer trade with Mexico will pose special problems not posed by Canada.

Development of Regional Trade Corridors

Within the transportation grid that links resources and production materials with manufacturers and processors, and manufacturers and processors with wholesalers, distributors, retailers, and customers, the movement of materials and goods involved in interregional trade tend to become channeled along particularly advantageous routes using particularly advantageous modes of transport. As trade expands and becomes routine, these routes and modes become well-defined "trade corridors." The economies of regions lying in and along these corridors are significantly affected by the continuous flow of materials, goods, and people involved in this trade.

Currently, since most U.S.-Canada trade is among eastern states and provinces, the principal north-south corridors through which most of this trade is conducted are located in the East as well. The main ones link Detroit and Toronto, Toronto and Buffalo, Montreal and New York, and New England and Quebec.

With a few exceptions (Vancouver-Seattle and Winnipeg-Minneapolis), major north-south trade corridors have yet to develop along most of the 49th parallel, which serves as the U.S.-Canada border from Minnesota in the east to the Pacific coast. However, as western states and provinces become more involved in this trade relationship, new regional patterns will emerge. As they do, north-south trade corridors in the West strategically linking growing regions in the north with growing regions in the south, will develop.

Regional Development Implications

Many regions and states in the U.S. recognize the economic development potential associated with expanding trade with Canada. Most see this potential as primarily linked to the ability of local firms to market their products in newly-emerging Canadian markets. If local or regional businesses sell more of their products in these markets, local employment and income will expand accordingly. For some regions, these types of impacts will be significant as north-south trade expands in the West.

However, expansion of U.S.-Canada trade has other regional development implications. First, with more goods and services moving across the border in both directions, increasing demands will be placed upon transportation facilities and providers. These demands will be greatest in those regions where the movement of goods and people expands the most, or along growing trade corridors. Inadequate or underdeveloped transportation facilities in these areas will require major improvements and transportation-related activity will expand, potentially having significant impacts on area income and employment.

As these regional trade corridors develop and transportation systems are improved, cities and regions along these corridors will be presented with other opportunities for regional development. Among these is the potential expansion of various types of manufacturing. This potential arises for a number of reasons.

In siting major processing and manufacturing plants, it's often desirable to locate these facilities either at or nearby the principal source or sources of supplies of key inputs used in manufacturing. Conversely, for other types of products and marketing situations, it's often desirable to locate processing facilities at or nearby the primary market or markets for the products being produced. However, these simple rules of industrial location don't always apply.

For large manufacturers servicing regionally-dispersed markets, it's sometimes difficult or uneconomical to locate production facilities at or near remote supply sources of raw materials or primary product inputs. Much of the movement of materials in commerce doesn't involve final products on their way to final markets, but rather, intermediate products or raw materials on their way to sites for further processing and manufacture before being marketed. Similarly, it's often times difficult for manufacturers to efficiently import large quantities of raw materials to processing or manufacturing sites near heavily-populated market areas.

As a result, "intermediate locations" strategically situated between transferrable input sources and dispersed final product markets often emerge as the best sites for various types of processing and manufacturing facilities. These sites tend to be found along major transportation corridors between markets and supply sources. As major new north-south trade corridors develop in the West with U.S.-Canada expansion, the local economics of cities and regions in and along these developing corridors could be significantly impacted.

Recognition of this was the impetus for the "Red River Trade Corridor Project." The project is an attempt by local officials and business persons in towns and cities from Winnipeg south into eastern North Dakota and northwestern Minnesota to find ways of furthering the Red River Basin's development as a major north-south trade corridor.

Figure 8. *Visualizing the Region.*

Implications for Montana

It's possible, if not probable, that the primary economic impact on Montana of expanding U.S.-Canada trade won't result from Montana businesses selling more of their products to Canadian customers (although this trade will undoubtedly increase in the future). Rather, the primary impacts may result from the state developing into a major corridor through which increasing trade is conducted between growing regions to the north and growing regions to the south. If this occurs, the state could then emerge as a prime intermediate location for certain manufacturing and processing of various materials and products on their way to final markets further south and further north (Fig. 8).

Examples of this are already evidenced in Montana's existing trade relationship with Canada. Trade between Montana and Canada in recent years has totalled about $700 to $800 million a year (U.S. dollars), with the value of Montana imports from Canada exceeding the state's exports to Canada by almost six times. On first blush, this trade imbalance could be construed as harmful to the state's economy. However, nearly 80 percent of Montana's Canadian imports are crude oil and other energy commodities on their way to markets in the U.S. Canadian crude oil producers supply 50 to 60 percent of the crude oil refined by Montana refineries. Montana's oil refining industry employs 700 to 800 workers with a payroll of over $40 million.

Montana's second largest Canadian import is softwood lumber, equivalent to 15 percent of Montana's own lumber production. Much of this lumber is transported from Canada by truck to reloading facilities in northwestern Montana. These facilities and the workers they employ provide Canadian lumber producers with a critical north-south rail link for servicing markets throughout the U.S.

A Canadian company is currently developing a canola oil facility in Butte that will process oil extracted from rapeseed grown in Canada and Montana into cooking oil for distribution in markets throughout the U.S. As U.S.-Canada trade expands in the West, opportunities for these types of intermediate handling, processing, and transporting of materials and products involved in this trade will undoubtedly expand in Montana.

For much of their histories, the U.S. and Canadian economies have been largely "east-west" in their orientations. Trade and interregional commerce primarily flowed east and west. However, the Free Trade Agreement and expanding U.S.-Canada trade are significantly reorienting these economies. Increasing attention is being given to "north-south" trading opportunities without the obstacles presented by national borders and accompanying trade barriers. As this occurs, "northern tier" states in the West like Montana, once somewhat geographically isolated and outside of the flow of interregional commerce, may increasingly find themselves in the crossroads of trade.

Red River Trade Corridor Development Project

*Jerry Nagel**

Introduction

There is a growing recognition among rural communities that new responses to the economic problems they face must be developed. Conferences like this that examine international economic opportunities illustrate changing strategies. Rural communities are also looking at new ways to cooperatively redefine themselves in a larger sense -- for example, how to link themselves with the rapidly changing global economy.

Cooperative economic development strategies that look beyond traditional boundaries of government and toward strategies of mutual interest are emerging throughout the globe. The Red River Trade Corridor Project, a cooperative rural development strategy, is part of this "new regionalism."

Project Background: A Timeline of Personal Experiences

The activities we pursue at work are often determined by personal experiences or interests. Such is the case with my and the Northwest Regional Development Commission's involvement with Canada.

Several years ago, a television story regarding an event in Winnipeg prompted some research on what has been done or could be done to help expand regional awareness of entertainment.

In November 1987, while visiting a friend in Winnipeg, I was introduced to several of his college-age employees who asked my thoughts on the Canada-U.S. Trade Agreement (CUSTA). Unfortunately, I had little awareness of it.

In May 1988, the Northwest Regional Development Commission organized the first meeting ever of the North Dakota, Minnesota, and Manitoba tourism departments. Ongoing discussions about tourism promotion in the Red River Basin were initiated at that time.

In June 1988, I attended a conference on CUSTA in Bemidji, Minnesota. I left with a very strong image of the president of a tool and die plant in Winnipeg looking to do business with partners in the U.S.

From a speech by Gerry Forrest of the Manitoba Ministry of Rural Development in November 1989, and later during a meeting with Michel Halbaut of Brittany, France, in the spring of 1990, I learned that rural communities in Manitoba and France shared common concerns with rural Minnesota; i.e., our young people are moving away, we have a declining tax base and declining infrastructure, and we are each concerned about our region's economic future.

History and Economic Base

These experiences led me to research why communications between areas so close together and similar in many ways were so poor. We started with a look at the historical and economic foundation of the Red River Basin. We learned that:

- The region has long been a meeting place for east and west.
- The region was settled by fur traders.
- Trade between Selkirk/Winnipeg and St. Paul once rivaled trade along the Santa Fe Trail.
- Trade was so great that after James J. Hill traveled to the region as a guest of the

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**Executive Director of the Northwest Regional Development Commission*

Canadian government in 1870, he formed a steamboat company on the Red River. Hill eventually moved into rail traffic. With financing from the Bank of Montreal, he and Norman Kittson joined forces with Donald Smith to buy the bankrupt Northern Pacific and St. Paul and Pacific Railroads to form the St. Paul, Minneapolis and Manitoba railroad. The idea was to build a northward rather than a westward link. By 1878, the railroad had built a line to the border and linked with the Canadian Pacific.

▸ With the Canadian Pacific reaching Winnipeg four years later, with the growth of the Great Northern, and with a firming of national boundaries, trade shifted to east/west markets and the economic community and importance of the Red River area as a north/south trade corridor diminished.

Hence, we learned there is a precedent for a regional economic and cultural community in the Red River Basin and, with that in mind, we began to try to better define what we were working with and towards.

In the spring of 1989, Carol Sorenson of my staff and I began to collect economic data about the region. Trying to assemble the data proved to be a bit of a challenge as each jurisdiction gathered data differently and on a different time schedule. Nevertheless, we found that:

▸ The region has 1.5 million people.

▸ The region has taxable sales of at least $17 billion, and even this is an underestimation of the economy since none of the jurisdictions tax food sales, Minnesota doesn't tax clothing sales, and hotel/motel receipts in Manitoba are not part of the data. Additionally, we are talking only taxable sales.

▸ There are 20 post-secondary institutions including: two medical schools, two law schools, three engineering schools, several technical programs, a four-year French college, and several university and private research institutes.

▸ The region has excellent transportation linkages including three east/west and one north/south national highways, several national railways, and three international airports.

In addition to the above findings, we also became aware that the recently signed Free Trade Agreement between Canada and the U.S. had created a climate of cooperation and an interest in exploring new economic opportunities between the two countries. In other words, we learned that the whole is really greater than the sum of the parts.

Conceptual Strategy

So, we knew that we were working within an economically strong regional foundation with several historical precedents; and in an environment where Minnesota, Manitoba, and North Dakota were interested in looking at new ways to work together toward mutual benefit. What we needed was a way to conceptualize the whole.

About this time, a colleague sent me a copy of the September 1988 issue of the Federal Reserve Bank of Minneapolis newsletter, Community. The newsletter contained a summary of a paper by Tom Stinson, a University of Minnesota economist. The paper suggests that rural communities need to look at new ways to cooperatively redefine, in a larger sense, their community -- to see ourselves as a community and our towns and cities as neighborhoods with distance between them.

With this idea as a conceptual foundation, we first established the Red River Trade and Development Project. The project was designed to be a rural development strategy that relied on regional, multijurisdictional cooperation that looked beyond the boundaries of government and towards our own regional self-interest.

However, we soon learned that building a project solely around the region's internal economy was only half a development strategy. As we described the project to people, we also learned about the potential for reestablishing the Red River Basin as a major north/south trade corridor.

Along the Canada-U.S. border, there are five major corridors of trade: (1) New England/Quebec, (2) Montreal/New York, (3) Toronto/Buffalo, (4) Red River Basin, and (5) Vancouver/Seattle. For energy-related activities, the eastern front of the Rocky Mountains would be a sixth corridor.

We concluded that between the eastern Rockies and the western Appalachians, the Red River Basin has a natural advantage: it is the place goods and services moving north-south through the center of North America must traverse. And as goods and services move through, there is a natural opportunity for business growth to serve the flow of commerce. Potential also exists to become an assembly point for components for goods from different parts of the continent, or to become a point of completion from which assembled goods are dispersed back out around the continent.

Further, given our central North American location, we have the potential for being the primary location for firms looking to serve their North American customers. In particular, we know that European businesses look at North America continentally versus country-by-country, and they will select North American locations for their service point. Our location has the advantage of being a good place from which to distribute.

The Northwest Regional Development Commission recognized the potential for economic diversification and growth for the area as a result of strengthened regional networks, the emerging trade opportunities with Canada, and the changing global marketplace. The Commission established the Red River Trade Marketplace and the Red River Trade Corridor Project as a strategic response to these opportunities.

So, if we have these opportunities to work together to strengthen our regional economy, how do we accomplish the tasks?

Strategy

The Red River Trade Corridor Project has two broad goals. First is to establish a long-term program of cooperation that strengthens the region's economy from within. A core element of this is the recognition of the need to orient economic directions in the region more north/south as opposed to east/west. The second goal is to establish a long-term, cooperative international marketing program that promotes the Red River Basin as the primary central North American trade corridor.

More specifically, the Red River Trade Corridor Project has four objectives:

(1) To create opportunities for businesses in Minnesota and North Dakota to develop new markets in Manitoba, and for businesses in Manitoba to develop new markets in Minnesota and North Dakota.

(2) To create opportunities for Manitoba businesses to joint venture or establish cooperative agreements with Minnesota and North Dakota firms in order to develop new U.S. markets, and for North Dakota and Minnesota firms to develop new Canadian markets through their association with Manitoba firms.

(3) To establish the Red River Basin as the primary central North American trade corridor through which goods and services moving between the two countries flow -- thus providing opportunities for new business development, for new linkages between existing businesses and firms moving goods and services through the Basin, and for expansion of businesses that serve the import/export industry.

(4) To establish the Red River Basin as the primary central North American location from which European and Pacific Rim firms can serve their North American customers -- thus providing opportunities for firms to locate new facilities in the region, for new business development to serve the needs of these firms, and for linkages to develop between existing businesses in the Basin and these new-to-the-region firms.

A key point to remember here is that a primary objective of the project is to ensure that rural communities have the opportunity to participate in the increases in cross-border and global trade. Larger communities will naturally pursue these developing opportunities because they have the resources to do so. Rural communities need access to the same opportunities.

The Program

Establishment of a long-term Red River Trade Corridor Project requires involvement from throughout the marketplace and public sectors. Direct input from these quarters into the development of the project is helping to provide a careful, accurate assessment of the region's strength, weaknesses, needs, and opportunities. It is building strong local support for the project. And it is ensuring that the long-term program design reflects the needs of the marketplace, the strengths and character of the region, and that it has identified realistic goals that will have an impact on the Basin's economy.

The Northwest Regional Development Commission, with funding from the Northwest Area Foundation, is currently developing a three-year "business plan" for a formal Red River Trade organization. This design effort is being guided by an advisory committee made up of representatives of the three jurisdictions. Committee members include business people, legislators, and economic development professionals. The formal governing board for the ongoing Red River Trade organization will be structured similarly.

In order to establish an effective program of regional and international trade, we believe the region needs to build a good trade infrastructure, much like you build any infrastructure, through sector-specific strategies that focus on the individual needs of each marketplace sector. Instead of establishing one template to lay over every sector, we are building strategies around the specific characteristics and "comfort levels" of each sector. The targeted sectors are finance, law, manufacturing, transportation, economic development, real estate, print and electronic media, and international tourism. We have also identified commercial uses of fiber-optic networks as an important program component. Leaders in each sector are involved in the design of their sector's strategy.

The Red River Trade Council will have three program components: (1) the Red River Trade and Development Network, which will primarily be our internal trade infrastructure-focused effort; (2) the Red River Trade Corridor Marketing Program, which will be our North American and global marketing effort; and (3) a "Friendly Borders" program, which is an effort to get involvement from all of the cross-border trade sectors to ensure that commerce occurs across the border as efficiently and quickly as possible.

Some of the suggested activities that would help accomplish our goals and objectives include:

- Publish a regional manufacturers' directory, or establish a computer bulletin board for manufacturer-to-manufacturer networking.
- Hold an annual trade summit with trade show, workshops, social functions, etc.
- Work with the region's media to increase awareness. Examples are a regular business column sent to all newspapers, arrangements with regional television stations to carry business news/stories, region-wide press releases on activities, etc.
- Help arrange cooperative educational programs for professional associations. Examples are workshops on international contracts, joint-venture contracts, and movement of money across the border.
- Develop marketing materials and an ongoing marketing campaign about the corridor and the region. For example, ABC tombstone business from St. Louis or Winkler just shipped 400,000 tons of widgets through the corridor. We send a card to identified businesses informing them of this activity and repeat this three to four times a year.
- Promote the region at trade shows.
- Participate in trade missions.
- Serve as location for coordinating trade follow-ups. For example, Mary Smith is in Hamburg in April where she makes a busi-

ness call. In October, John Smith will be in Hamburg on business; he will take time to stop by where Mary called, to say hello and remind the people of Mary's continued interest.

- Serve as a neutral body for cooperative discussions. For example, the project could be the neutral place to conduct discussions regarding regional ATM systems or regional bank affiliation cards.
- Identify regional weaknesses and help develop regional responses. For example, injection plastic molding or aluminum extrusion are weaknesses; the project could help develop regional responses.
- Participate in ongoing tourism efforts to increase the sense of community in the region, to help define us as neighbors, and to encourage more activity within the region.

The project is pursuing a similar targeted strategy for its international trade activities. Instead of a global shotgun approach, we have targeted specific countries or regions with which we have historical, cultural, or existing economic linkages. This targeted approach will provide more effective use of limited resources and will allow for better networking of trade efforts within the Basin.

As one example, we have targeted the 49-nation Francophone world in general, and France in particular, for activity. The Northwest Regional Development Commission, with help from the Association of the French of the North, recently hosted a tour of the Basin with representatives from Brittany, France. Of the eight sites visited, active follow-up among four parties is being pursued, including two in communities under 1,000 in population.

Global Trends

Throughout the globe, new regional economic communities are emerging and establishing links with similar regional communities. In North America, regional efforts like the one along Florida's Space Coast, or between Buffalo, New York and Toronto, Ontario, or the Pacific Northwest Economic Partnership, or the Mid-South Common Market are growing and building links. Similar efforts have also been made by northern Argentina, the high-tech city network of Europe, the Celtic region of coastal Spain, France and Ireland, and between individual provinces like Minnesota's relationship with Brittany. Additionally, new efforts along the U.S.-Mexico border are emerging, fueled by natural economic advantage and the potential for a U.S.-Mexico free trade agreement.

Some regions, like the Pacific Northwest, are moving very quickly. Legislators from five states and two provinces in the Pacific Northwest met last October and identified economic development, education, energy, and natural resource policy as areas for cooperation. These may include joint international trade development, linking research and development facilities, establishing a regional capital pool, coordinating education and training efforts, establishing regional telecommunications networks, and examining harmonization of standards and regulations to facilitate commerce. This effort is being led by the Northwest Policy Center at the University of Washington and the Pacific Northwest Economic Partnership, a program similar to the Red River Trade Corridor.

With regional efforts like these already very active, we believe it is critical that the business, economic development, academic, and research and development sectors work together to keep regions like the Red River Basin -- or, for that matter, all of Minnesota, Manitoba, and North Dakota -- globally competitive.

Where We Are Today and What We Have Learned

On February 23, 1990, we held a conference in Grand Forks, North Dakota to get input into the idea of a Red River Trade Corridor and to assess support for it. We learned that there is great interest in the idea, that we need to be focused about what we want to accomplish, that we need to build the idea from the grassroots, and that we need to continually seek input into the development and implementation of any ongoing strategies.

In the series of meetings we have had with the various market sectors, we learned that we need to be responsive to or work within each sector's "comfort range." In other words, each sector has its own pace and its own networking system that it wants to work within. Three examples illustrate:

- In May, we had a meeting of bankers in Winnipeg, hosted by the Royal Bank of Canada. We expected 10 people and had 20. The bankers are very enthused about the idea and the potential for our Red River Basin effort. However, they chose to network within an informal structure that they were comfortable with.
- The legal profession, on the other hand, has exhibited an interest in a transboundary bar association -- a fairly formal structure.
- Manufacturers want something in the middle -- not a formal structure, but regular meetings, such as an annual trade show or trade summit. They would also like a formal networking system, but they only want the system to get them together. They then want it to get out of the way.

Everyone wants the project to work within existing structures. No one wants to see new structures set up that would be above the current structures. Hence, the Red River Trade Corridor Project is seen as an effort to work within or network existing structures.

Another key point we learned is that the Manitobans, while very enthusiastic about the idea and its potential, want a strategy of "walk before you run." Anyone that tries to make things happen too quickly is slowed down. I would say that this sentiment holds true to a good degree on the U.S. side also. After all, having not talked to each other for 100 years, it's not likely we'll overcome tradition in a mere three, four, or five years.

One factor that may change the speed with which we pursue opportunities is how quickly governments move to open doors. If the region's governments want trade to happen, they can invest resources and regulatory efforts to encourage it.

We have learned that this project can neither be inclusive nor exclusive. Each community or jurisdiction needs to make up its own mind about participation and when it wants to participate.

We have learned that it is essential to include as many of the sectors as possible that are involved in cross-border commerce in order to build a border strategy. Responsibility for a good strategy does not rest solely with the customs services.

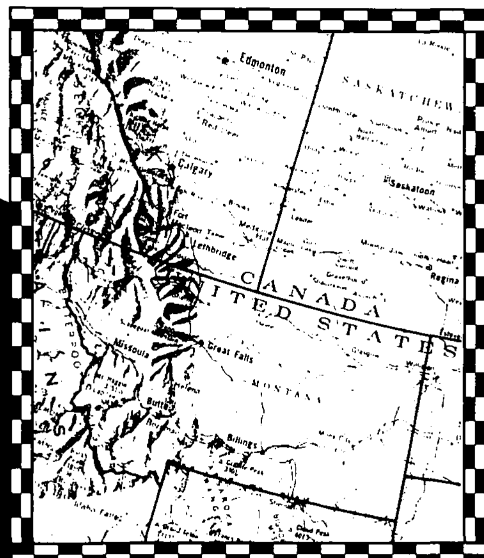
Finally, as I noted earlier, we have learned that establishing regional communities based on history, culture, and common economic goals is part of a global trend. I see this as a great opportunity to build linkages with partners throughout the globe.

Conclusion

The economic future of rural regions is tied to their ability to participate in the global economy, to provide economically and culturally rewarding opportunities for young people, and to quickly respond to new economic developments.

The Red River Trade Corridor regional cooperative economic development effort can be one part of our efforts to stimulate regional economic growth, increase global marketplace linkages, and encourage cultural sharing. The result will be the expansion of existing businesses, the development of new businesses, the location of new firms in the region, the increased export of products from the region and, ultimately, new job creation and income growth.

A Personal Reflection



Politics, Policies and Production: How to Blend Them

*R. L. M. Dawson**

It was just a short 32 years ago that I saw my first Montana sunset -- a colorful, vivid memory that will never leave me. This recollection jumps to mind whenever I visit this lovely part of North America.

In the late fall of 1958, I arrived in this beautiful country, a wide-eyed, landed immigrant full of hope and great expectations, as I joined my first job, my first company -- Cargill. Being of conservative Scottish blood, they sent me a Greyhound bus ticket from New York to Minneapolis.

In the intervening years, I have been so very fortunate. I have travelled around the world with Cargill, lived in foreign countries, and learned a lot about agriculture, about business, and about life -- only now to become so happily aware that every day there is so much more to learn.

Today I have a new and more difficult problem: I have to learn how to forget. I have to unlearn, to forget the past. The way we used to do things is changing; we even have to think differently. Learning is relatively easy; unlearning or relearning is tough. None of us likes to drop the basic props upon which we have based so much of our value system for several decades. How do you ask Lawrence Welk to come up with a completely new continental two-step rhythm so we can dance together into a brighter and better 21st century? But this rapidly shrinking global village and small continental island called North America requires us to make that shift -- to think anew.

I first met this new thinking in the world of agriculture. It's not easy to be optimistic about agriculture these days, but I do have good feelings about the future. I don't think I have seen so many real reasons to be optimistic and enthusiastic as those that are around us today. Let me tell you more about why I feel this way.

If you search through all the written words of Cargill's strategic thinking, our published mission statement, our corporate goals and philosophy, our culture, one finds one marked recurring theme. It is the belief that we should explore and develop the grand concept that through the avenue of fair trade we can enhance, to our mutual advantage, not just our own lives, but the well-being of all mankind. Is this concept all just some woolly dream, a lot of flowery words and fluffy thinking with little substance, more akin to A.A. Milne and his Winnie-the-Poo "bear of little brain?" Or is it real?

Just because we understand the importance of making a profit, that does not mean we have to worship at the altar of capitalism, making sacrifices in human misery. If our business is to take this earth's primary resources, add value to them, and then trade them, then indeed we can view these actions as an instrument of peace and prosperity.

Sometimes my friends and work colleagues will bait me when I get going on such a philosophical tack and tease me with, "Oh come on, Dick, that's stretching it a bit, isn't it?" But I don't think so. I think getting up in the morning to go to work where we try to help feed the world is a worthwhile way to spend the day. If I didn't feel that way inside, I would have to leave agriculture and do something else.

So I sometimes find myself caught up in this issue of a business philosophy of politics

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**Senior Vice President, Cargill Limited.*

and policies, of production and people, and I ask myself, "What possible contribution could this humble grain trader bring to this heady debate, usually the playground of intellectuals and academics?"

Like fools and angels, "grain merchants rush in where economists fear to tread." So come walk with me down the pathways of our imaginations and let's see where this exciting free trade initiative might lead us if we really want to follow it to its fulfillment. Let us start close to home, with this upper prairie border (we can go global later).

If there was ever a land born of those twin sisters of success -- optimism and determination -- surely these western lands are it, and that comment knows no border from Montana to the Peace River country. The livestock industry across these western borders has been close to a free trade mentality for many decades. Here the North-South move is on. Continental thinking is a fact, not a dream.

Every week, we in Winnipeg hear of new business ground being broken -- buying and selling. Our little Manitoba market is only one million people. Add 1,000 miles north-south and 1,000 miles west across the prairie provinces of Saskatchewan and Alberta, and the market population becomes 5 million. Next, add one truck-day's drive south or north, and the total market more than triples.

The whole concept has a sense of excitement and experiment about it. No wonder then that we should feel some optimism as we strive to think and act like neighbors sharing one Great Plains community, a prairie rangeland where the key role of agriculture is dominant throughout. It is the common denominator that brings us together in a mutual search for an improved world trading system in agricultural products.

Our farmers are only too aware of the mess that politicians have made of global agriculture. The farmers of the North American granary have a shared concern when they see the statistical world grain carryout at 17 percent, hovering at levels so low they have only been exceeded once in 30 years. Yet the world price of grains is still at low, uneconomic production levels -- totally distorted by the absurd global subsidy war.

No one who is connected with agriculture will look back on agriculture of the 80s with much pleasure. It has been labelled as the decade of "2-3-5" -- 2 good years, 3 fair, and 5 poor. It was characterized by some very poor decisions in politics and policies in many countries, including my own. However, if I had to identify one of the more harmful decisions that hurt us all, it would have to be the fourth day of the decade. On January 4, 1980, President Carter introduced his famous grain embargo. The world's grain industry changed that night. The signal was clear to all that food was now a political weapon and the immediate response worldwide was a resurgent drive for self-sufficiency at any price, however high the subsidy.

One could no longer trust the world's trading system for supplies, and the lesson was not lost on those whose memories of hunger were all too fresh in their minds -- both in the European Economic Community and in Japan.

So we saw the Common Market swing from a 20 million tons importer of cereals to a subsidized exporter of 20 million tons: a 40 million tons swing in a world trade of 200 million tons and a 20 percent political/policy distortion.

By 1985, the United States' percentage of world market share had dropped from around 50 percent to 30 percent. The result was the 1985 Farm Bill and the outbreak of the world's grain subsidy war. It has been going on now for five years and at a huge cost for both the combatants and for those like Canada who got caught in the crossfire. There are few real winners in such a battle, and eventually the biggest losers are the farmers as their business becomes politicized with a new kind of indecision and instability that is even less forecastable than the weather. (Have you noticed how even the weather forecasters now sound like politicians? My car radio last evening told me quite clearly that tonight's forecast of 10 percent probability of rain had a 30 percent chance of changing to 20 percent by this morning!)

It was in the middle of this political mess that the Irish Axis met in Quebec in the autumn of 1985. President Reagan and Prime Minister Mulroney launched the free trade negotiation on its bold voyage.

Shortly afterwards, in 1986, over 90 nations in Punte del Este committed the Uruguay Rounds of the GATT meetings to search for a new world trading system marked by a major reduction in government intervention. It is significant that this GATT Round is now often referred to as the "Agricultural Round" -- significant insofar as it is the first GATT Round to seriously address the issue of agricultural trade, and significant in that the Free Trade Agreement between our two countries represents a valuable precedent in agricultural negotiation.

It has not been an easy road. It has been full of jagged rocks and deep potholes, slippery puddles of yogurt, excesses of raspberries and cream, pasta indigestion from Durum wheat, squealing hogs, well-flexed subsidy muscles, and an unhappy series of customs border disputes, especially in the livestock and meat trades.

Farmers and processors on both sides of the border are now searching for clear decisions so they can go about their business of farming or secondary manufacturing without the worry of some sudden painful political act disrupting their livelihoods.

It is no secret that in the last days of Free Trade negotiations, the difficulties of the dispute mechanism almost scuttled the deal. But wiser heads prevailed and the momentum of the deal proved to be just too compelling. The negotiators had come too far to let such a splendid concept founder on the shallow sands of subsidy disputes. The very wording of the agreement relies upon the spirit of the agreement operating always within GATT principles to resolve any differences and leaves many important areas for later solution, such as definitions of subsidies and standards. One also has to remember that neither negotiator, Mr. Murphy nor Mr. Reisman, had an open authority to negotiate away their respective national laws. It will now be up to all of us to have the will to make the Free Trade deal work -- to work sensibly together to resolve differences.

No one really questions the final authority of your Congress to govern your laws nor of our House of Commons to govern ours, but it remains up to each of us to <u>remove</u> the differences so those Houses don't have to resolve our differences.

The first year of Free Trade has been a failure in this area. We desperately need to see an improvement in the effectiveness of this dispute machinery if it is going to earn the credibility needed for future years. It will be a sad day, indeed, if we are forced to exercise the clause that allows for a one-year notice to end the agreement.

We in Canada have recently embarked upon a major new direction for our national agri-food policy. The agri-food strategy is based upon four conceptual pillars: (1) a responsive market, (2) self-reliance, (3) environmental sustainability, and (4) regional support. It will eventually involve a reduction of government financial support to agriculture. We Canadians must be ready to play our part in a worldwide agreement to replace government subsidies with improved market returns. No one country can start that process alone; it has to be done multilaterally.

The good news of the day is that there are some signs that it is going to happen. We must not allow GATT to fail agriculture. The stakes in this global poker game called GATT are very high.

We are in the final weeks of the Uruguay Round talks and the posturing is nearly over. The talks are entering a most crucial stage. By mid-October, major offering positions must be on the negotiation table. It is difficult to comprehend the adverse consequences of failure: an international trading market without any discipline, a war-of-the-jungle mentality of "beggar thy neighbor," a collapse of world trade into protectionism and poverty, a rampage of debt and death throughout the Third World.

The converse is even more dynamic. A successful outcome could initiate decades of rising living standards around the world, a rational and gradual return to economic agricultural productivity by natural advantage, and those positive trends will be felt nowhere more than by the people of this region, regardless on which side of the border one lives.

Many of you will have read Mr. Gorbachev's remarkable book, Perestroika, subtitled, "A New Way of Thinking About a New World." Nothing will help us to know each other better as neighbors than an increase in trade between us. It can be one of the world's great bonding agents. Look what it has done for Europe. They are now enjoying the longest period of peace in four centuries -- burying generations of animosity in a bold move to make the next century much better than the last. They are determined to find a better way of resolving differences between nation-states, something other than jumping into uniforms and tossing bombs at each other.

Fortunately, our histories and our borders have rarely been subjected to such divisions. Nevertheless, we can learn as we admire the way the Europeans have come to honor and respect each other's differences as well as enhance their similarities -- the manner in which they are making space for each other, sensitive to their needs of individual dignity and national pride. Surely if they can surmount the obstacles and traditions that stand in their way as they form their European Union, it should be an easy step for us to think and work together continentally.

One of my 11-year-old daughter's favorite magazines is the National Geographic Magazine's children's product, World. She thinks and talks with her friends in the context of Planet Earth. As she bounces up and down to the musical tapes of "Up With People," she doesn't even have to ask, "What color is God's skin?" Because to her it doesn't matter. I must learn to march to the beat of her more beautiful drum. How about you? For example, why not come share my parks? Maybe we should issue a joint "Rocky Mountain Foothills Parks" sticker. Or what about one regional fishing stamp to put on our hunting licenses? And how about adopting the same procedure for migratory birds -- they don't care where the border is either. Does acid rain recognize borders? The clouds of Chernobyl drifted around regardless of lines on maps and national, sovereign jurisdictions.

Speaking of which, the environment and our national deficits are perhaps the two most ominous shadows overriding all other considerations for both of our nations as we share our dreams for the future. For Canadians especially, our dreadful financial deficits at both federal and provincial levels are our national disgrace and the shameful inheritance we are leaving to our children. That young daughter of mine will retire from her chosen career around the year 2050. I have a growing sense of personal shame when I think of the financial and environmental legacy of the world that I am leaving to her -- unless we move fast to correct it -- and we know what to do.

October 19th, 1987 -- a day notable as a most recent financial disaster -- was not merely an American Stock Market event. It was a global incident, within seconds. And it was a potent reminder that the nation-state as we know it is dying. Good riddance to it! A more noble conscience is rapidly emerging. Of course, national boundaries will continue. The proper exhibition of "patriotism" as we know it will now be exhibited far more in cultural pursuits and even in sports, as evidenced by the tremendous revival of national cultures throughout the smaller nations of Europe. They have not been swallowed up by their economic union -- they have prospered within it.

Of course, our national boundary will continue. The political line on the map will remain there. We will remain in our different social systems. Canada will evolve to suit its own needs as a large, extensive country. For example, we have always shared more, to try and equalize the internal regional disparities within Canada. We are a highly socialistic nation in that sense. We will go on being so, and for that we will forever probably pay larger taxes than you do in the United States. This is a reflection of the way our country is built and the way the people in it think about sharing among themselves. We are proud of our more socialistic society.

Perhaps we can also learn something from Europe. As Europeans come to honor and respect each other's national differences with sensitive civility, they are building a mutual trust that is the key to future peace. And meanwhile, the rapidly expanding trade amongst themselves is their very strength and lifeblood. The sooner we think "continentally," like that, the better for all of us in North America. This CUSTA deal is the first stepping stone in that direction. Bringing Mexico into the deal is a completely natural extension of this continental thinking.

As members of the agricultural industry, trading repercussions around the world are an important part and parcel of our daily lives. We in the grain business have contact every day with practically all of the peoples on Earth. This gives each of us a unique opportunity in our dealings with others within and beyond the boundaries of Canada to show leadership and to establish goodwill by the manner in which we conduct our trading business.

Our overseas trade and our continental trade between us as neighbors can be a positive force for good and a most worthwhile contribution to understanding and peace throughout the world at this time when all such contributions are urgently necessary. Let us each in our own way join hands together and take this opportunity to make this contribution.

My closing thought comes from that most unusual Englishman who, above all others, was capable of mobilizing the English language and sending it into battle either in the cause of war or of peace. Perhaps he got it from his American mother. Winston Churchill expressed these thoughts in his address to the Canadian people from the Chateau Laurier Hotel shortly after Christmas in 1951:

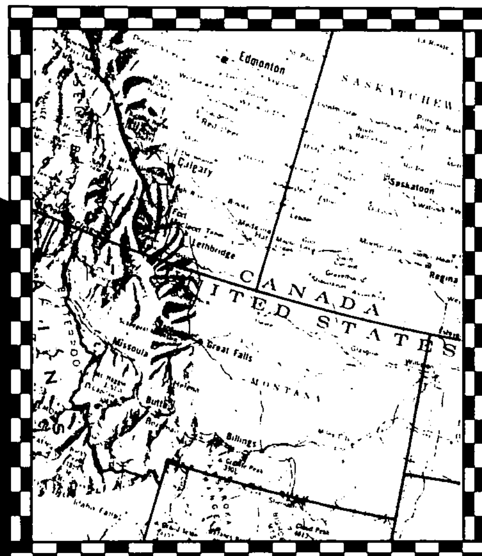
> *I believe in the unconquerable assertion of the spirit of our combined identity and survival. We have surmounted all the perils and endured all the agonies of the past. We shall provide against, and thus prevail over, the dangers and problems of the future, withhold no sacrifice, grudge no toil, seek no sordid gain, fear no foe. All will be well!*

I believe we have within us the life-strength and guiding light by which the tormented world around us may find the harbor of safety after its storm-beaten voyages.

A marvelous future awaits Canada. When I first arrived there after the Boer War, its mighty lands had but 5 million inhabitants. Now there are 14. During my grandchildren's lifetimes, there may well be 30. Upon the whole surface of the globe there is no more spacious and splendid a domain open to the activity and genius of a free people, with one hand clasped in enduring friendship with the United States, and the other spread across the ocean both to Britain and to France.

It is an honor to have been invited to share some thoughts on this concept of a Free Trade deal, but particularly to be counted as a friendly neighbor while we, each in our own way, strive to make our dreams come true for our families, our countries, this continent, and for this shrinking global village we call home.

Appendix


Edmonton
Calgary
Lethbridge
Saskatoon
Regina
CANADA
Great Falls
Missoula
MONTANA
Billings

Eximbank and FCIA Resources for Financial Export Sales

*Arthur Obester**

How can Montanans and Western Canadians use the services of the Export-Import Bank to succeed in the Global Market? Eximbank's mission as an independent federal agency is to help finance export sales of American goods and services. Exporters and bankers need Eximbank to compete in today's Global Market for a couple of reasons. Eximbank supplements commercially available financing and absorbs some of the risks the private sector will not. Eximbank also neutralizes the effect of other governments' export credit subsidies. This means exporters can compete for overseas business on the basis of price, performance, and service. By helping put together a competitive financing package, Eximbank can give an exporter the edge he needs to win a contract.

Eximbank has been in business since 1934, when Congress first chartered the bank. Since then, it has supported more than $200 billion in U.S. exports, creating and sustaining millions of American jobs.

Eximbank assistance covers about 5 percent of U.S. exports each year. But most Eximbank assistance covers exports to developing countries. With the continued reluctance of commercial banks to supply new funds to the Third World, it's a market where Eximbank's services are clearly needed.

Before considering Eximbank's programs for financing exports and how they work, a few policy points demand clarification. First, Eximbank is not an Aid Agency. It lends money to foreign buyers; it doesn't give it away. Before it will support any export credit transaction, it must have reasonable assurance it will be repaid.

Eximbank does not compete with private financial institutions. Instead, it makes it easier for them to extend credit by taking on some of the risks. It provides its own financing only when the private sector can't or won't make competitive financing available. Eximbank's mission is to support sales of U.S. goods and services. As a result, some U.S. content requirements exist for financing its exports. Legislation restricts operation in some countries; exports to others may not be supported because they're what some might refer to as "economic basket cases."

Eximbank's programs can help with both pre-export and post-export financing needs. It can help businesses get working capital for production or marketing before shipping their goods. And it can help foreign buyers get credit if they can't or won't pay cash in advance or pay by confirmed irrevocable letter of credit.

Extending credit internationally is more difficult than doing it domestically. In this country, risk is limited to the borrower's refusal or inability to pay. Overseas, the risks are different. It's harder to get good credit information. If a buyer defaults, the seller may have to sue him through an unfamiliar legal system. Political or economic conditions could keep your buyer from paying.

There's another factor. Other governments often subsidize export credits to boost their economies. That means U.S. firms must compete with foreign firms offering fixed-rate financing at below-market rates.

**Senior Marketing Officer, Export-Import Bank of the United States*

Eximbank's programs are designed to help businesses cope with these risks. Let's look at how they do it.

Eximbank offers wide access to its programs. That means any responsible party can apply to Eximbank for any program. A good place to start with many export deals is an Eximbank preliminary commitment (PC). A PC gives the terms and conditions on which Eximbank will support a proposed export transaction. It is valid for six months and can be converted into a final commitment. A PC is helpful as a negotiating tool when trying to win a contract.

Eximbank offers pre-export assistance through a Working Capital Guarantee Program, a domestic program designed to help credit-worthy exporters when they can't get working capital any other way. It works by guaranteeing lenders that if the exporter defaults, Eximbank will repay 90 percent of the loan.

The Working Capital Guarantee Program supports marketing, inventory, or production activities for potential export sales. It can be used to support production for a specific transaction or as a revolving line of credit. The loan amount can be up to 90 percent of the value of the collateral the exporter puts up. And Eximbank's collateral requirements are flexible. They include foreign receivables and goods bought with the proceeds of the loan.

Once an exporter gets to the point where he's ready to ship, we have two types of export assistance available: credit risk protection and fixed-rate financing.

Be it exporter or banker, Eximbank can protect businesses against two types of nonpayment risks. One is commercial risk, resulting from such things as economic deterioration in the borrower's market, demand fluctuations, changes in tariffs or technology, and natural disasters. The other is political risk such as war, political upheaval, or the government's failure to transfer the local currency into U.S. dollars.

Eximbank offers two credit risk protection programs: insurance, through our own agent, the Foreign Credit Insurance Association (FCIA), and guarantees.

Insurance covers mostly short-term sales. That includes such items as consumables, raw materials, commodities, spare parts, small manufactured items, and services customarily sold on terms of up to 180 days. Bulk agricultural commodities and some capital goods sold on 360-day terms are also considered short-term sales.

FCIA offers a variety of insurance policies, each designed to meet specific needs:

- *New-to-Export Policy* frees new exporters from first loss deductible risks usually found in regular insurance policies.
- *Umbrella Policy* is available to commercial lenders, state agencies, export trading companies, and similar organizations to insure their clients' export receivables.
- *Bank Letter of Credit Policy* insures banks against loss on irrevocable letters of credit issued by foreign banks for U.S. exports.
- *Financial Institution Buyer Credit Policy* insures short-term loans to foreign buyers of U.S. exports. Our Short and Medium-Term Single-Buyer policies allow exporters to cut their risks by selectively insuring foreign receivables.
- *Multi-Buyer Policy* allows more experienced exporters to expand sales by providing risk protection on sales to many different buyers.

The other way Eximbank offers exporters and lenders credit risk protection is through a guarantee program. The purpose of the program is to encourage lenders and exporters to make loans to credit-worthy foreign buyers by having Eximbank assume all of the political and most, or all, of the commercial risks of nonpayment.

Guarantees can be used to support either medium- or long-term sales. A medium-term sale usually involves terms of one to seven years and a loan value under $10 million. Most capital goods are considered medium-term sales, as are contract services and feasibility studies.

A long-term sale has a repayment term of more than seven years and/or a loan value of $10 million or more. Major products, projects, and related services are considered long-term sales.

Under Eximbank's guarantee program, the buyer must come up with a 15 percent cash payment. Eighty-five percent of the export can be financed.

Loan guarantees can be made in any readily convertible foreign currency as well as U.S. dollars. Most guarantees provide comprehensive coverage of both political and commercial risks. But "political risks only" coverage is also available.

For long-term transactions, Eximbank provides 100 percent political and commercial coverage for both exporters and lenders. For medium-term, we cover all of the political risk and 98 percent of the commercial risk. The 2 percent uncovered risk is for the account of the exporter, who has a counter-guarantee agreement with Eximbank.

Because this is credit risk protection and not Eximbank funding, lenders can charge a market interest rate. Eximbank generally doesn't guarantee all of the interest, but we'll set our guaranteed interest rate when the lender determines his.

Now let's talk about Eximbank's fixed-rate financing program. Under this program, Eximbank provides medium and long-term, fixed-rate loans directly to foreign buyers and fixed-rate funding commitments to others who make loans.

Fixed rates are set by the Organization for Economic Cooperation and Development (OECD), to which the United States belongs. Those rates vary with the per capita income of the country to which the export is going and the loan's repayment period. They are adjusted periodically.

For a poor country like India, the rate is now 9.2 percent for both medium and long-term loans. For an intermediate country like Mexico, it's 10.05 percent for medium-term and 10.55 percent for long-term.

For rich countries like Canada, the medium-term rate is what's known as a CIRR rate, which is representative of commercial lending rates in various currencies. We generally support long-term transactions for rich countries with guarantees only.

As in Eximbank's guarantee program, a 15 percent cash payment is required under the lending program. Eximbank will loan up to 85 percent of the export value of the goods. These are subsidized loans, so we must have evidence that the potential export sale has some competition from non-U.S. exporters being supported by their governments.

Since it's not easy for small businesses to find out whether they have subsidized competitors, Eximbank will waive the competition requirement if the exporter is a small business and the loan amount is $2.5 million or less.

Under another aspect of the fixed-rate financing program, lenders and exporters can borrow from Eximbank and extend competitive, fixed-rate loans. This is the intermediary loan program.

Some financial intermediaries are often reluctant to make fixed-interest rate loans because the lender's cost of funds may rise above the cost of the loan, Eximbank made it possible for banks to borrow from a rate below OECD rates. It will also lend to credit-worthy non-financial intermediaries (such as exporters) at the regular OECD interest rate. That makes it possible for exporters to fund a transaction themselves.

A couple of special programs can help businesses compete for contracts to export services:

- The Engineering Multiplier Program helps stimulate exports of U.S. design and engineering services, increasing the potential for future U.S. exports.
- Eximbank will extend loans or guarantees for up to 85 percent of the U.S. export value. Eximbank will also guarantee commercial financing for approved project-related costs in the host country of up to 15 percent of the U.S. export value.

- An Operations and Maintenance Contracts Program helps U.S. firms compete for overseas contracts to operate or maintain new or established projects.

Again, Eximbank covers up to 85 percent of the U.S. export value of the contract. The contract must provide a long-term benefit to the owner, such as training local personnel to take over operation of the project.

Having addressed the basics of Eximbank's loan and guarantee programs, let's consider the costs involved.

For FCIA insurance policies, premiums range from $.20 to $1.75 per $100, depending on the type of policy, repayment term, and other factors. For Eximbank programs, a $100 application fee is required for each transaction as well as a commitment or facility fee with final approval.

A more significant cost is the exposure fee, which covers our risk undertaking in the loan and guarantee programs. If both a loan and guarantee are supporting a transaction, the guarantee fee will be the only one charged. The exporter can increase the product cost to cover the fee and Eximbank will finance it.

Let's briefly review the basic programs Eximbank offers to support U.S. exports:

- A Domestic Working Capital Guarantee Program supports short-term loans for pre-export activities.
- Two foreign credit risk protection programs cover post-export activities. Short and medium-term FCIA insurance and medium and long-term Eximbank guarantees protect the exporter or lender from default by the foreign buyer for political or commercial reasons.
- A fixed-rate lending program covers medium and long-term sales. It's designed to make U.S. exporters competitive with exporters from other countries using fixed-rate subsidized financing.

These programs can be used individually or combined. For example, a working capital guarantee could be mixed with insurance, or a guarantee to get protection for both pre- and post-export sides of the transaction. Or the intermediary loan program could be used with a guarantee to cover different risks on the same sale.

Using Eximbank and FCIA programs can give businesses the competitive edge they need to succeed in today's global market. Eximbank is in business to help get U.S. goods and services into foreign markets. As business people explore selling in new markets, Eximbank offers valuable support.

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