

AN OVERVIEW OF THE CANADA-UNITED STATES FREE TRADE AGREEMENT

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This paper addresses Canadian/American trade relations. The two countries have completed an historic free trade agreement, or FTA as it has come to be known. To fully appreciate the importance of this agreement, it is first necessary to examine the relationship between the two countries.

Indeed, the Canada/USA relationship is unique in the world, not just because they are neighbors, but because of the intimacy and the sheer size of their association. Canada and the USA are similar in most respects. Canadians and Americans tend to regard one another not as foreigners but as kin, North American cousins if you will. Opinion surveys continue to demonstrate that Canadians and Americans like and respect one another more than they do the citizens of other countries. So much has been said and written about their 5,300-mile common border that it has come to be known as the world's longest undefended platitude!

With reference to borders and of agriculture, a border dispute supposedly occurred about ten years ago, when Jimmy Carter was President of the United States. At that time an international commission was established between the United States and Canada charged with the responsibility of ironing out a few anomalies in the border. One of those occurred in New England, where the state of Maine and the province of New Brunswick met in the middle of a potato field. Canada claimed that the farm - including farmhouse - was in Canada. The USA of course claimed that the land lay on the American side. After much surveying and high diplomacy, the commission finally agreed that the farm was indeed in the United States. This pleased the farmer immensely. As he had now become a taciturn New Englander, he wrote a letter of thanks to President Carter, expressing his particular gratitude that he would no longer have to endure another long, cold Canadian winter.

That story illustrates the closeness of the USA/Canadian relationship and, at the same time, the fact that Canadians sometimes feel a little misunderstood or taken for granted by Americans. Make no mistakes about it! Not only is the United States important to Canada, Canada is extremely important to the security and well-being of America.

MUTUAL INTERDEPENDENCE OF THE USA AND CANADA

Canada is the only country which stands between the USA and the Soviet Union over the North Pole. Through the North American air defense command and NATO they share in the defense of this continent and of Europe.

Canada is by far the biggest economic partner of the United States. The USA exports more than twice as much to Canada as to Japan, yet imported much more from Japan in 1987.

In addition to foodstuffs and raw materials, Canadians also buy vast quantities of the manufactured goods that create and maintain jobs in American factories. One-fourth of total USA exports are shipped to Canada, including one-third of its manufactured exports, accounting for more than two million American jobs.

In 1986 more than 11 million Canadians visited the United States, many of them passing through or stopping in Georgia on their way to winter vacations in Florida. That represents half of all foreign visitors to the USA - not bad for a country of 26 million.

Two-way trade between Canada and Georgia exceeded \$1.7 billion last year. Investments by Canadian companies in Georgia are worth about \$1.8 billion, according to the USA Department of Commerce, accounting for more than 22,000 Georgia jobs. The economic bonds which join the USA and Canada are important to both countries.

USA-CANADA FREE TRADE AGREEMENT

It is against that background that political leaders in the two countries began to negotiate a free trade agreement in 1986. They sought a fair and balanced agreement from which both parties would stand to gain - a win/win situation. Despite many hills and valleys, roadblocks and seemingly insurmountable obstacles, that agreement materialized, signed by President Reagan and Prime Minister Mulroney on January 2, 1988.

After the necessary legal processes in the United States Congress and Canadian Parliament were completed, the FTA was scheduled to be implemented on January 1, 1989. Congressional ratification of the FTA agreement was enacted in September, 1988.

So, what is the free trade agreement and why is it so important? In international trade law terms it is a "free trade area agreement." It is not a customs union like the European common market.

Both Canada and the USA will retain their own individual tariffs and commercial policies in dealing with outside countries. Between each other, however, all tariffs and many existing non-tariff barriers will be eliminated, on all products, industrial and agricultural.

When and if the agreement takes effect some tariffs will be eliminated immediately, others over a five-year period, and all the others by the end of ten years. Canadian tariffs are, on average, twice as high as those imposed by the USA - but they will all be gone in ten years or less!

Key parts of the agreement are rules of origin, or rules of North American content. These are designed to ensure that only products substantially of Canadian and USA origin benefit from tariff elimination. There will be no free riders in this deal.

The agreement also removes virtually all barriers to energy trade. This will provide a stable framework for investment in new energy developments that will strengthen the energy security of the two countries. And it will benefit American consumers by assuring continued access to Canadian energy supplies and a more competitive energy market. While energy supplies may be in surplus today, you only have to think back a few years to grasp the value of a North American approach to energy security.

This agreement deals in a major way with non-tariff barriers. There are new obligations on technical standards. Both countries will be committed not to use product standards as an unnecessary barrier to trade.

Similarly there are commitments not to impose quotas and other restrictions. Many existing restrictions will be phased out. Some progress was also made in further opening up of government procurement markets at the federal level.

Of perhaps even greater significance is the historic breakthrough in services trade. For the first time an international agreement will provide a code, or set of general disciplines, covering trade in a large number of service sectors. The objective is to extend the principles of national treatment, the right of commercial presence, and the right of establishment, to each other's providers of services.

The FTA will also be a trend setter in the area of investment. Canada is the largest market for USA foreign investment, totalling more than \$50 billion. Dividends on this investment contributed some \$3.5 billion to this country's current account last year.

Binding rules governing international investment relations have long been a major USA economic and foreign policy objective. At the same time, long standing Canadian restrictions in this area have been a constant, and at times serious irritant in US-Canadian bilateral relations.

Again, the deal with Canada will have an important demonstration effect for the rest of the world - as well as respond to USA concerns in Canada. What this means is that in the future, apart from certain limited exceptions which will be maintained on both sides of the border, American investors in Canada, and Canadian investors in the United States, will be treated in exactly the same way as domestic investors.

AGRICULTURE AND THE FREE TRADE AGREEMENT

Turning to agriculture, this is the first international agreement since World War II in which participants have made a substantial deal regarding the freeing of trade in agriculture, including agricultural tariffs, export subsidies, and quota restrictions. Seven rounds of multilateral negotiations failed in agriculture. This agreement is a message to the rest of the world that agriculture may be different and more difficult but good deals - substantial deals - can be made.

Why are the agricultural provisions of the FTA important to both Canada and to the United States? Agri-food in Canada is one of its largest economic sectors, contributing approximately 9% of its gross domestic product. Between regions in Canada, substantial differences exist in terms of the commodities produced, local markets and prospects, partly as a result of environment and climate. Prairie producers, who concentrate on grain and livestock production, are quite vulnerable to fluctuations in world commodity prices. In contrast, eastern agriculture, due to its larger product mix and greater emphasis on serving the domestic Canadian market, has had more stable returns. Overall, the prosperity of Canadian agriculture depends greatly on international markets, since more than one third of Canadian agricultural receipts are derived from exports.

The negotiation of the FTA has taken place at a time when there is considerable uncertainty and instability in global agricultural markets. This disarray is due to depressed international market prices caused by the agricultural policies pursued by major industrialized countries. To compound the problem, rapid improvements in technology have increased supply relative to demand, thus putting additional pressure on farm prices.

In contrast to this relatively somber global outlook, the potential for growth in agricultural trade between Canada and the USA is good. Close proximity, relatively high

economic growth rates, similar grading and distribution systems and, above all, a relatively open trade environment suggest that the Canada-USA bilateral trade should continue to grow faster than offshore markets.

Reflecting the less favorable situation in those markets, the importance of the USA market has increased significantly for Canadian farmers. In 1986, the USA was Canada's leading market for farm products, purchasing 32% of Canada's total farm exports. If grains and oilseeds are excluded, the role of the USA market becomes significantly more important. In 1986, more than 60% of Canada's non-grain and oilseed exports went to the United States.

Some key statistics reveal the importance of the USA market compared to offshore markets for some Canadian commodity producers. In 1986, the USA market took 95% of Canadian sugar exports, 89% of live cattle and swine exports, 82% of beef and pork, 77% of maple products, 70% of fruits and nuts, and 64% of the poultry and egg exports.

On the other side of the coin, the USA is Canada's main supplier of imported agri-food products, accounting for 55% of Canadian imports or approximately \$3.6 billion in 1986. Of the Southeastern states, Florida, as one might expect, is the largest supplier of Canadian requirements, to the tune of some \$326 million per year. That figure is largely orange juice concentrates and fresh fruit and vegetables. Of the seven Southeastern states, Georgia ranks second after Florida in agricultural exports to Canada. In 1987, Georgia exported more than \$39 million worth of agricultural products to Canada. Nuts, dairy, egg and honey products, meat and fresh vegetables are the most important commodities.

What this demonstrates is that the two countries enjoy a significant and growing pattern of agricultural trade which can only be mutually beneficial. From the Canadian perspective, however, this pattern has been threatened in recent years by certain USA trade actions. The United States has introduced a number of contingency protectionist actions against Canadian farm products, which has included, among others:

- a countervailing duty on live swine exports;
- an anti-dumping duty of British Columbia raspberries;
- import quotas on sugar and certain sugar-containing products;
- on-going harassment of potato shipments from our maritime provinces; and
- periodic difficulties with exports of vegetables from eastern Canada.

In addition, recent action by a number of North Central states adversely affected Canadian exports of livestock, particularly live hogs, due to alleged concerns about the use of the drug chloramphenicol by livestock breeders in Canada. Also, there have been complaints about exports to Pacific states of grain products assisted by freight subsidies. These trade irritants demonstrate the sensitive state of Canada-USA trade in farm products and the need to minimize such irritants in the future. That is what the free trade agreement, as it applies to agricultural products, is all about. It will provide an environment for the future growth of USA-Canada trade under secure and predictable access. It will allow agricultural policies of both nations and agricultural marketing systems to continue to provide a stable environment for investment and growth in both the USA and Canada. The improved economic efficiencies that will accompany the agreement will enhance the sector's competitiveness in both the North American and global context. Such aggregate macro-economic benefits should ensure that North American producers and the agri-food industry will be in a position to confront the challenges of global agri-food markets as multilateral agricultural trade reform progresses.

RESERVATIONS ON FTA

As might be expected with any agreement as comprehensive and far reaching as the FTA, not everyone is happy with all aspects. In some agricultural sectors only limited gains could be made.

Canada, for example, has traditionally taken an interventionist role in the feather industries with a system of quotas and licenses. Quotas were established for imports of USA poultry products and were then supplemented as market conditions warranted. Under the FTA, quotas remain but have been established at the average levels, including supplementary quotas, over the previous five years; a small gain.

In the USA, the sugar industry has been highly regulated while in Canada, with only 10% of our consumption produced domestically, prices reflect those of the world market. During the negotiations the USA was unwilling to give up its protectionist sugar policies and only very minor gains in market access were achieved for Canadian suppliers. The USA agreed to exempt Canada from any restrictions on imports of sugar-containing products having 10% or less sugar.

On balance, in the agricultural sector, the experts agree, the USA stands to gain somewhat more than Canada from the FTA. This is particularly true in horticultural commodities, some of which are protected in both countries through the application of seasonal tariffs. With the complete removal

of tariffs, USA produce will be able to enter Canada before our crops are ready for market, thus syphoning off the traditionally highly-priced early season sales.

So, while some individual industries on both sides of the border will no doubt require substantial adjustments, the overall effects of the FTA both as a study in macroeconomics, and from the microeconomic point of view of the consumer, will be positive. With reference to the multilateral negotiations on trade and, in particular, on agricultural trade, Canada and the USA have advanced similar positions in GATT and share many of the same goals. Both countries look forward to the elimination of all agricultural subsidies. This is particularly important to Canada which, as a major player in international agricultural (especially grain) markets, simply cannot afford to compete in subsidy wars between major economic powers such as the EEC and the USA.

Canada shares the goal of subsidy elimination, and believes that some short-term arrangements are possible to eliminate the worst of current practices. Perhaps it is not too much to hope that the Canada-USA free trade agreement will serve as an example to multilateral negotiations. When the USA and Canada, the world's two largest trading partners, with such closely linked economies, each so susceptible to the influence of the other - when nations can negotiate an agreement which is so original in its provisions, so broad in its coverage, then there is still reason to hope that we can reverse the trend of growing protectionism worldwide.

All of the benefits which we in North America stand to gain from the free trade agreement, and the example which it will set for the rest of the world, will vanish, however, if the patient should die on the operating table (or, perhaps more aptly, in the waiting room). This, unfortunately, is a real risk.

It is a paradox that one rarely hears from the supporters or beneficiaries of any trade agreement. It is a political truism that the forces of protectionism are always more focussed, always more vocal, and always better organized than interests that benefit from freer trade. So, if this important achievement is to be consummated, it is essential that consumers, the users of competitively-priced imports, and export-oriented producers of goods, services and ideas, organize to make their voices heard in support of the FTA both in Canada and in the USA.

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