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Challenges in Agricultural Trade under CUSTA

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Highlights

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Farm Foundation
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Session I - MAJOR TRADE ISSUES UNDER CUSTA

CUSTA: Good or Bad?

James Rude, University of Saskatchewan, and
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There has been a significant increase in Canada-U.S. two-way trade since the implementation of CUSTA in 1989. However, it is difficult to separate out how much of this trade is directly attributable to CUSTA. This study estimates that approximately one quarter to one third of this trade is due to other macroeconomic factors, such as income growth and the weakening Canadian dollar. This leaves a significant amount of unexplained trade that could have been the result of CUSTA. In order to examine the impacts of CUSTA, this study looked at a number of sub-sectors in terms of the degree of trade liberalization that took place and other major factors that may have affected trade. Even in cases where the impacts of CUSTA are hard to assess, the trade agreement may still be influential in that it facilitates investments and acts as an incentive to look for trade in new markets.

In order for further investments to occur, CUSTA must be viewed as an evolving mechanism that is committed to trade liberalization and capable of separating politics from trade considerations. CUSTA can be judged in terms of how effective it has been as a commitment mechanism. Or put differently, how many unfulfilled commitments have there been? On these grounds CUSTA comes up short. The commitment to develop new bilateral trade remedy rules has never been realized, and it now appears to be forgotten. Harmonization of grading standards and other technical regulations has never happened. And the elimination of border inspections of live animals has never occurred.

These unfulfilled commitments reveal as much about where we are going as about where we have been. There has been plenty of opportunity for consultation. How effective these consultations have been is not yet evident. Cooperation is needed to bring down existing barriers and to bring heavily protected sectors, such as supply management and sugar, into the fold of the agreement. Complete policy harmonization may not be necessary for integration, but some harmonization is necessary. Certain regulations need to be addressed and harmonized. Domestic support is a touchy issue. To have a truly open border, it is not possible to have very large imbalances in the levels of support provided to primary agriculture. Some of these issues will have to be solved multilaterally. However, a successful regional agreement also requires cooperation on multilateral issues. This cooperation may not be forthcoming with disparate levels of domestic support.

Many prairie grain and oilseed producers believed that CUSTA and NAFTA would bring added prosperity to the farm sector. In late 2000, prairie grain and oilseed producers find themselves in one of the lowest income positions in history, and have become pessimistic about the so-called gains to be obtained from freer trade. But one has to recognize, of course, that Canada trades with many nations, not only the United States. Even if all the agricultural trade barriers for grains and oilseeds were removed between the two countries, the gains would be small. To maximize the gains from trade liberalization, all sectors of agriculture have to move in the

direction of freer trade, not just the grains and oilseeds sectors. An additional frustration for prairie grain farmers is the relatively high level of government support afforded to American farmers. To the extent that these farm programs are not totally decoupled, Canadian farmers are competing in a world market with one hand tied behind their backs.

Major Trade Issues Under CUSTA: A Canadian Perspective

M. N. Gifford, Former Director General, International Trade Policy Directorate, Agriculture and Agri-Food Canada

Canada - United States agricultural trade more than tripled between 1989 and 1999, far surpassing growth to markets outside North America. However, the surge in bilateral trade has sometimes been marred by trade frictions which reached a peak in 1998 when certain U.S. states took unilateral measures to limit imports from Canada. The border flare-ups of the last few years indicate that the two federal governments cannot assume that once they have signed a free trade agreement their role is over. As tariffs are eliminated, differences in domestic support and marketing policies and differences in technical regulations can easily become lightning rods. Irritants can easily fester and become very politicized unless they are dealt with quickly and fairly.

Major Agricultural Trade Issues Under CUSTA, One U.S. Perspective

Cathy Jabara and John Reeder, U.S. International Trade Commission

The CUSTA model was essentially a customs union between two countries that have considerably different government programs, transportation systems, and marketing organizations. Over time, it was expected that the U.S. and Canadian programs - whether direct agricultural support, marketing programs, food, veterinary or farm chemical regulations or the other myriad government functions - would be harmonized. But in fact, this has not occurred. Non-tariff measures (NTMs), applied in a largely tariff-free environment, have formed the basis for most of the issues and disputes under the CUSTA.

The trade flow data suggest that U.S.-Canada agricultural trade has been influenced by a large number of factors that likely go far beyond the CUSTA. Factors affecting trade flows include WTO implementation, changing domestic programs, exchange rates, and a divergent regulatory environment. Given the large and growing trade between the United States and Canada, particularly in areas of processed food products, it would seem that the next important step under CUSTA is to harmonize these divergent NTMs. This will ensure that growth in trade between the two countries is due to comparative advantage, efficiency, and natural advantages, and not due to niche markets that have developed because of protection afforded to certain commodities and divergent regulations.

Session II - CUSTA'S IMPACTS ON BILATERAL AGRICULTURAL TRADE

The Impact of CUSTA on U.S. and Canadian Agricultural Trade

Thomas Vollrath, Economic Research Service, USDA

The objective of this paper is to present a broad overview of the impact of CUSTA on U.S. and Canadian agriculture by examining the established trade record from various angles. The focus is on the agricultural sector and its four subsectors: bulk commodities, processed intermediates, fresh produce & horticultural products, and high-value processed products. The empirical record shows that both countries have benefitted from trade in the post-CUSTA period, especially with respect to value-added agriculture. The United States experienced a positive shock in the first year of the agreement. Canada has continued to make in-roads capturing market share in the United States.

The Canada - U.S. Free Trade Agreement: The Case of Wheat

Vince Smith, Montana State University

This paper examines the impacts of the 1988 Canada-United States Free Trade Agreement (CUSTA) on trade between Canada and the United States in wheat. The paper begins with a brief review of CUSTA's wheat provisions and discusses their effects on trade in wheat between the two countries. The evidence shows that imports of Canadian wheat into the United States increased substantially, beginning in 1989. In particular, imports of hard spring wheat and durum wheat expanded rapidly. In contrast, almost certainly because of the operations of the Canadian Wheat Board (CWB), Canadian freight rate subsidies, and relatively inefficient components in Canada's grain handling system, imports of U.S. wheat into Canada changed very little and remained negligible.

The sharp growth in U.S. imports of Canadian durum wheat immediately led to a trade dispute over possible Canadian dumping that dragged out over the three year period, 1989 to 1992. Ironically, a binational panel eventually determined that they could find no evidence of dumping by the CWB largely because senior U.S. officials made a serious error in defining the CWB's acquisition price. A sharp rise in U.S. imports from Canada in the 1993/94 crop marketing year resulted in a trade dispute based on Section 22 of the 1933 Agricultural Adjustment Act (which has since been revoked). Under Section 22, the U.S. government could take countervailing action against imports of an agricultural commodity if those imports were adversely impacting the operation and budgetary costs of U.S. domestic farm programs. The U.S. International Trade Commission determined that Canadian wheat imports were damaging and, through bilateral negotiations, the Canadian government agreed that on a one year basis (for the 1994/95 crop year) the CWB would restrict wheat exports to the United States to no more than 1.5 million tons.

Implicitly, although the formal agreement was only for one year, the terms of the agreement were not violated until the late 1990s. In 1998, the U.S. government expressed concern about increasing levels of CWB exports to the United States and in late 1998 a memorandum of understanding between the governments of the two countries was signed and appeared to, but in

fact did not, resolve several U.S. concerns over U.S. access to the Canadian grain handling and transportation system. Subsequently, during a period of historically low world wheat prices, U.S. farmers and organizations continued to be concerned about the potential for unfair trading practices by the CWB, and in September 2000 filed a complaint with the U.S. Trade Representative's Office under Section 301 of the 1974 Trade Act.

The evidence suggests that CUSTA has been a failure with respect to North American wheat markets in that it has failed to create a free trade area in wheat or an environment in which wheat trade disputes between the United States and Canada do not occur. There is a core reason for CUSTA's failure with respect to wheat. It is simply not possible to have a free trade area for a commodity when, through an export marketing State Trade Agency, one of its participants rigorously controls and restricts major flows of the product through the country's grain handling and marketing system.

The Dynamics in the Wheat and Wheat Products Sector: United States - Canada Comparisons

Karl Rich and Ronald Babula, U.S. International Trade Commission, and Robert Romain, Laval University

The purpose of this paper is twofold. First, a vector autoregression, or VAR, model is built for each country and used to test whether the market dynamics have fundamentally changed as a result of CUSTA. Second, the VAR models for each country are used to glean the similarities and differences in the dynamics of both the wheat and wheat products markets. The model illustrates a number of observations with respect to the U.S. and Canadian wheat and wheat products market over the last 15-20 years. In the era since CUSTA's implementation, changes in U.S.-Canadian trade in wheat and wheat products, both in terms of volumes and patterns, have been significantly altered. However, statistical evidence does not support the existence of structural change. That is, there has been no change in the structure of the dynamic relationships among the variables in the wheat and wheat product market in both countries as a result of CUSTA. This result is important, as it implies the impact of the CUSTA was not so much to change the structure of the markets, but rather facilitate their movements without border impediments. The same unaltered market mechanisms in both countries seem to be handling larger volumes of wheat and wheat products in the post-CUSTA era. Further, events associated with the periods of CUSTA, NAFTA, and the temporary TRQ seemed to have little or no individual effects on the fourteen endogenous variables modeled.

The model simulations suggest that the commodity markets in both countries are quite similar, in terms of their response to shocks in prices, despite major differences in the marketing of wheat. Moreover, shocks in wheat supply appear to affect prices much less in Canada than in the United States because of the small size and export orientation of the Canadian market. Such a result has an important policy implication, in terms of understanding U.S. farmer reactions to surges in wheat imports. On the downside, both markets appear to behave differently when the prices of intermediate inputs, such as flour, are changed, suggesting that the integration of the two processed food markets has not altered many of the structural and institutional differences of these markets in either country. These institutional differences, though, may be fairly small, given the slight differences in the reactions of downstream markets, such as flour mixes and cookies and crackers, to shocks in intermediate inputs, such as flour.

Session III - CUSTA'S IMPACTS ON BILATERAL AGRICULTURAL TRADE OF LIVESTOCK

Major Issues in the U.S. Livestock Industry under CUSTA

Harlan Hughes, Professor Emeritus, North Dakota State University

A number of factors impact the North American beef industry: differences and similarities in beef production between countries; increased beef production per cow; changes in beef demand (decreasing demand for beef led to lower real prices, which led to lower quality, which, in turn, led to lower beef demand; demand, however, appears to now be increasing); exchange rates; cattle cycles; economic impacts of 1990s price depression; and trade disputes.

Canada is both a major destination for U.S. beef in the East and a major foreign supplier of beef in the West. During the last 10 years, U.S. imports of beef and veal from Canada grew from 243,564 animal equivalents in 1988 to 1.018 million animal equivalents in 1997. Canadian net imports (imports minus exports) of beef and veal have ranged from a negative 51,200 animal equivalents in 1991 to a positive 614,500 animal equivalents in 1997.

Combining live animal trade with meat trade illustrates that U.S. total imports from Canada have risen in the last decade while U.S. total beef exports to Canada rose in the early part of the decade and since then have remained rather stable. In 1997, Canada exported 1.38 million head of cattle to the United States. Including the 1.018 million animal equivalents of beef and veal, Canadian exports to the United States totaled 2.4 million animal equivalents in1997. The United States, in 1997, exported approximately 500,000 animal equivalents to Canada. This nets out to 1.9 million animal equivalents from Canada in 1997.

If Canadian imports had been eliminated, total U.S. beef supplies would have been 2.1 percent smaller in 1988 and 6.6 percent smaller in 1997. On the other hand, if U.S. imports plus exports to Canada were eliminated in 1998, total U.S. beef supplies would have been about 1.9 percent smaller. Without Canadian beef trade in either direction in 1997, U.S. beef supplies would have been 5.6 percent smaller. Using a crude 1.6 percent price flexibility, a 5.6 percent drop in U.S. beef supplies could result in a 9 percent increase in U.S. beef prices. For $60 per hundredweight slaughter cattle, 9 percent would be $5.40 per hundredweight, or $65 per 1,200 pound slaughter animal. If Canada were to sell that meat on the world market, U.S. exports to other countries would probably decrease, reducing beef prices back toward today's $60 cattle.

It is my professional judgement that banning Canadian imports would not have solved the 1990s price problem brought on by the record meat (beef, pork, and poultry) supplies. The answer to the record North American beef production, and the resulting low prices, is some form of supply reduction. I believe that the marketing system is currently signaling a reduced beef supply. Cattle feeders in both countries, however, are doing everything in their power to increase beef production through heavier carcass weights. In spite of cattle feeders, beef supply is projected to be on its way down in 2001 and beyond, and beef prices are projected to remain strong or get stronger through the year 2003.

CUSTA's Impacts on Bilateral Trade of Livestock: Pork and Poultry

Terry Crawford, Economic Research Service, USDA

CUSTA appears to have had a limited effect on the trade of pork and poultry between the United States and Canada. There were not any tariffs or quotas on the pork trade between the United States and Canada before CUSTA, which remained so after. Canada had a sanitary ban on U.S. hog imports due to the presence of pseudo-rabies in the United States. Poultry meat was free of tariffs and quotas for imports to the United States, but Canada had import quotas on poultry meat and eggs, which was increased and continued under CUSTA, allowing for modest increases in imports. While trade increased, most notably for Canadian exports of hogs to the United States, changes in trade flows appear to have been primarily determined by factors other than CUSTA.

CUSTA and U.S./Canadian Beef Trade Issues

Gary Brester, Montana State University

United States participation in trade liberalization agreements with Canada through the Canada-U.S. Free Trade Agreement (CUSTA) has generated intense debates in agricultural sectors. CUSTA mandated that live cattle and beef trade among Canada and the United States be based on competitive factors and include legal safeguards to deal with arbitrary trade restrictions. Nominal U.S. cattle prices generally increased throughout the 1970s and 1980s, but have declined steadily throughout the 1990s. Over the same period, the total U.S. beef supply increased from 25 billion pounds to 28.5 billion pounds. Imports (both beef and beef obtained from live cattle) accounted for almost 0.5 billion pounds, about 14 percent, of this increase. Canada's share of U.S. beef supplies increased by slightly over 3 percentage points during the 1990s. As a consequence, of the $8/cwt decline in slaughter price during this period, about $0.35/cwt was attributable to increased Canadian imports. The R-CALF anti-dumping challenge to U.S. imports of Canadian fed cattle lacked a logical basis and, had it been upheld, would not have had a significant positive effect on U.S. cattle prices. However, this action and future decisions regarding country-of-origin labeling and the potential restriction of USDA grade stamps to only meat produced by U.S. beef cattle will continue to generate trade tensions.

Session IV - RECENT EVOLUTION OF THE U.S. AND CANADIAN MARKETING SYSTEM

Changes in the Canadian Grain Marketing System and the Role of the Canadian Wheat Board in U.S. and Canadian Grain Trade

Ted Allen, President, United Grain Growers

There have been three important changes in the Canadian grain marketing system. First, oats was removed from the marketing jurisdiction of the Canadian Wheat Board (CWB). This change has been beneficial to Canadian farmers. Canadian oat exports to the United States has increased significantly since the early 1990s, but without the resulting friction as in the case of wheat. U.S. oat acreage has decreased over this time period, while Canadian changes in oat acreage have been small. Oats have been a textbook example of comparative advantage at work. Second, the Ontario Wheat Board allowed voluntary participation. The use of voluntary, instead of mandatory, participation has been beneficial to Ontario farmers and illustrates major differences with the CWB. Finally, there have been changes in the Canadian Wheat Board, but the changes have not been significant and have not been helpful for U.S. relations. The 1993 continental barley market was a successful experiment for Canadian farmers, but the policy was overturned. A survey showed that younger Canadian producers are less supporting of the CWB, indicating that future changes may be likely.

It is important to note that trade surpluses and deficits are not necessarily bad. It is important to look at the bigger picture. Trade liberalization may lead to surpluses or deficits in certain sectors, but if we look at the bigger picture, we are most likely better off in the end. Special interests in a democratic society, unfortunately, get special privileges, which taken separately may not seem that significant. The accumulation, however, of these special privileges weakens society economically.

Changes in Grain Marketing Industries in the United States and Canada

William Wilson, North Dakota State University

This paper describes some of the features of railroad deregulation, which provides some of the impetus for many of the changes that have occurred; a number of comparisons of the changing market structures in each country are made; implications are made for the grain handling and trading industries, and for farmers; and a number of issues are identified that are pertinent for the emerging North American grain trading industries and the pressures toward integration.

The grain trading industry has changed radically during the past two decades. Following rapid growth in world trade during the 1970s, there was a subsequent expansion in exporting capacity which generally came on steam during the 1980s. Besides this expansion in exporting capacity, the 1980s began to experience the effects of rationalization and concurrent development of excess capacity in the country grain handling industry as a result of deregulation of the railroad industry. In addition, the industry was impacted by an escalation in government intervention in grain transactions notable through the use of EEP during the 1980s. Perhaps the most important feature of the later 1990s will be implications of the increase in privatization of grain transactions.

This sector has gone through radical changes over the past two decades, and the scope of these changes has important implications for all market participants. Changes have also occurred in the structural organization of this industry in both the United States and Canada. Major changes in the United States have evolved for 20 years, commencing with deregulation of the railroad industry. That in Canada is more sporadic and generally much more regulated, and the intensity of regulations seem to be escalating. There are several major themes developed in this paper. First, U.S. farmers have benefitted immensely from the competitive environment in grain handling resulting in continuous investment in the industry, reduced costs, and adequate capacity. Second, many policy analysts seriously underestimate the intensity of competition and its positive virtues. Third, the Canadian system is hemorrhaging trying to find new rules and regulations that are generally compatible with numerous conflicting and fundamentally incompatible objectives. Finally, a number of these changes have implications for changes in the North American grain marketing system.

Changes and Issues in the Canadian Grain Transportation Industry: Impacts of Technology in Marketing

Barry Prentice, University of Manitoba

This paper examines whether continuing declines in transportation and communications costs may further decentralize the marketing of grain. The analysis begins with a survey of the factors that favor decentralization of marketing. Subsequently, the economic factors that led to the shift from sacks to bulk handling are briefly reviewed and the current system is described. The discussion continues with the impact that new innovations are having on marketing costs. The paper concludes with a short case study on the decentralization of oats marketing and Canada-U.S. trade.

Marketing channels for agricultural products become more decentralized as transportation and communication costs fall. The grain industry is an interesting mix of centralized and decentralized marketing. Grain has retained a more centralized marketing structure than other agricultural products, but over time, the processing of grains and oilseeds has become more decentralized. Transportation, handling, communications and information innovations, as well as standardization and quality control have each contributed to decentralization of the grain and oilseed industries. New oilseed crushing and milling plants are located in production areas and are largely served by semi-trailer trucks. These trucks also serve a railway-based network of country and terminal grain elevators.

The first phase of decentralization in grain handling ended by 1900. Despite a century of technological progress, the centralized system of bulk grain marketing remains largely intact. The bulk handling system has relied on economies of size to compete with the decentralizing effects of technological change. The high fixed costs of the grain industry encouraged an oligopolistic industrial structure and a re-centralization of marketing. Re-centralization of the grain industry is taking the form of consolidation and merger. This may change as technological changes favor decentralization. The increased demand for identity preserved grains, the increased supply of unitized transport, and the increased supply of information and communications are favoring decentralization of grain marketing.

Session V - MAJOR ISSUES FOR FUTURE COMMERCIAL INTEGRATION

Do We Need Further Integration of the North American Agricultural Market?

Brian Paddock, Agriculture and Agri-Food Canada

Benefits from further integration of the North American agricultural market include more efficient patterns of trade, more competitive markets, lower transaction costs, and a discipline on policy, forcing policies to be less distorted. There would also be a high degree of investment between countries. If further integration is to occur, we need to ask where we should integrate. Some areas are more difficult to integrate than others. Impediments to integration include differences of support levels, especially wheat, and differences of views on collective marketing. A more productive field for integration would be regulations, which form partial barriers to trade. There is already much integration between the United States and Canada, but areas that are not integrated occur where there are differences in policy approach. There are also a number of minor areas that could be improved.

Harmonization of Agricultural and Trade Policies

David Schweikhardt and Monika Tothova, Michigan State University

The Canada-U.S. Trade Agreement was a remarkable accomplishment that had escaped policy makers for a century. The achievements of that agreement should not be underestimated, but another stark truth should not be avoided: The policy agenda that must be addressed if further economic integration is to be achieved in North American food markets is more complex than the agenda that was accomplished in the original free trade agreement. If policy makers intend to pursue deeper economic integration of these trading partners, they will find that agricultural issues will occupy a portion of their negotiating agenda. Any movement toward increased economic integration in North American food markets must deal with at least four areas of policy: issues related to bilateral and external trade barriers; issues related to agricultural subsidies; issues related to trade remedy laws, including dumping and countervailing duty laws; and issues related to monetary integration.

Deeper economic integration could provide additional welfare gains, but this ignores the question of whether the gains realized from bilateral negotiations will be larger than the gains that might be realized by pursuing other policy issues. There is reason for suspicion that the history of U.S.-Canadian agricultural trade relations suggests that an excessive level of resources is being spent on issues that provide little net benefit to North American agriculture, while issues in which the countries might realize joint gains are ignored. The pursuit of deeper economic integration in North American food markets is only justified if it provides greater gains than other policy alternatives - such as opening other markets - that might be achieved by negotiators.

An Alternative Approach to the Resolution of Canada-U.S. Disputes Over the Canadian Wheat Board

Hartley Furtan and Murray Fulton, University of Saskatchewan

The Canadian Wheat Board (CWB) is the source of many of the agricultural disputes that have arisen between Canada and the United States over the last 10 to 15 years. Within Canada, a great deal has been written about the merits and the demerits of the CWB. There are also international concerns with the CWB. From time to time, U.S. producers and the U.S. government on their behalf, express concern over the pricing of CWB grain in both the United States and in third markets. The concern is with the single desk nature of the CWB and with the price pooling system that the CWB administers, both are believed to lead to various forms of unfair competition, such as dumping. However, these two features are key to the operation of the CWB and many observers believe without these features the CWB could not function.

This paper examines a number of issues that are associated with the CWB and are closely linked to the trade disputes. First, there is the issue as to whether or not the CWB follows the WTO rules on the operations of state trading enterprises. Second, there is an issue regarding the commercial benefits associated with grain marketing and handling and who captures these benefits. Third, there is the issue of political differences among farmers in Canada over the policy of single desk selling. Finally, there is the issue of income support levels in the two countries and the effect they have on border disputes.

These issues form the basis for a proposal that might remove or reduce Canada-U.S. border disputes. This proposal is based on the observation that the role of the CWB can be changed if there is widespread political support for its removal. For this removal to occur, other policy regimes have to be changed. First, farmers in the United States and Canada would be provided identical farm programs. Second, both governments agree to change the anti-dumping and countervail provisions currently in place, and all challenges go to a NAFTA type dispute panel. Finally, all state trading in wheat and durum would be removed. The result of these changes would be a single market with identical farm programs. As long as both governments followed the rules, grain could flow back and forth across the border as economically required. Without this broad approach to solving the problem, the industry will likely maintain the current squabbling.

Exchange Rates and Relative Pricing

MinKyoung Kim, William Nganje, and Won W. Koo
North Dakota State University

During the last decade, the U.S. dollar has appreciated against major currencies, including the Canadian dollar, Japanese yen, and Eurodollar. Specifically, the U.S. dollar has appreciated by about 33 percent in real terms compared to the Canadian dollar. Theoretically, the U.S. dollar appreciation will cause U.S. exports to decrease and imports to increase, which could lead to a considerable trade deficit with continuous dollar appreciation. The impact of the exchange rate on the U.S. trade market has long been debated.

This study examines how macroeconomic forces affect the trade balance between the United States and Canada. Variables used in this study are exchange rates, agricultural trade balance, agricultural GDP, GDP growth rates, and interest rates. More specifically, the question of exchange rate impacts on international trade between the United States and Canada is examined.

These markets are found to interact with one another. Exchange rate markets have short run dynamic relationships with agricultural trade balance, and U.S. dollar appreciation causes the U.S. agricultural trade deficit to increase. Cointegration is found among these markets for the entire time period, 1981 to 1999, and becomes stronger in the post-CUSTA era, 1990 to 1999. Meanwhile, no significant relation is found among markets before CUSTA. Beside the evidence of an equilibrium relationship among these markets in the long run, a short run relationship is found between exchange rates and agricultural trade balance. U.S. dollar appreciation causes the U.S. agricultural trade deficit to increase in the short run, and this phenomenon is significant under CUSTA based on the test of causality and impulse response. In addition, agricultural income has suffered from exchange rate shock based on the results of impulse, while no substantial impact on interest rates is found.

Trade disputes between the United States and Canada have mainly focused on institutional differences such as the Canadian Wheat Board versus free enterprise in the United States. However, the findings in this study indicate that macroeconomic factors like exchange rates may have substantial impacts on trade flows. Thus, macroeconomic factors should not be ignored when trade policies are formulated, especially when the markets are strongly integrated.

Session VI - TRADE DISPUTES AND NEGOTIATIONS

Major Issues in Trade Disputes and Future Direction

Jon Lauck, University of Minnesota Law School

It is my intention to make some comments on the current health of the international trading system, specifically where agriculture is concerned. Much of the present controversy is linked to the adoption of the Canada-U.S. Free Trade Agreement, which served as a model for the adoption of NAFTA and the Uruguay Round agreement in 1994, which created the WTO. One of the most prominent areas of trade friction in recent years has centered on the cattle industry; in particular, the sharp increase in the number of Canadian and Mexican cattle imported into the United States and the absence of a comparable increase in U.S. exports of cattle. American producers believe that the surge in imports is related to the collapse in prices and have accused the Canadians of dumping in the R-Calf case of 1998. In the end, the relevant agencies found that in fact Canada was dumping cattle in the United States, but they found that the dumping did not cause a "material injury," a seemingly implausible and contradictory finding that aggravated American cattlemen who were barely hanging on to their livelihoods. In addition to the wider debate about dumping, the imports of foreign meat have contributed to a debate about labeling. The prominence of the Canadian Wheat Board in the cattle dispute is linked to another lingering and contentious issue on the trade horizon. The United States has placed the elimination of the Canadian Wheat Board, and other such State-Trading-Enterprises, high on the agenda for the current negotiations.

There is now less unanimity when it comes to relying on agricultural exports as a safety valve for U.S. agricultural problems and a greater recognition that freer trade causes as many problems as it solves. In part, this is because exports as a remedy for farmers' problems has been oversold. The long history of the interaction between agricultural and trade policy should have been more prominent in the 1996 policy debate and the potential volatility of the export markets better understood. When constructing agricultural policy in the near future, it is critical that the prospects of agricultural export growth be assessed realistically. The dangers of basing policy on unpredictable export growth was fully realized after the collapse of the Asian market. A shift in foreign preferences is also a danger. Currently, a movement is growing in Europe to constrain the spread of American food products. There is also much concern about the ability to sell American GMO crops. In addition to growing resistance to American food exports, the prospects for greater degrees of agricultural trade liberalization, which many hoped would open previously closed markets to American products, are no longer so bright. Perhaps the greatest reason to doubt the prospects for greater trade liberalization is the Battle in Seattle and its repeat performances at the IMF and the World Economic Summit and other occasions.

My preference is for a certain kind of global capitalist development. To deny the long-term economic benefits of free trade and global economic convergence would be foolish. But to deny the criticism that globalization compounds economic inequality and gives corporations and international capital excessive control and influence would also be foolish. Political leaders would be wise to promote policies that promote decentralized economic power, such as antitrust laws and small business promotion policies, and policies that promote entrepreneurship and economic independence.

Trade Disputes: The Anti-dumping and Countervailing Duty Laws and the Role of Quantitative Economic Analysis

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The *Special Import Measures Act* (SIMA) provides the legal framework which authorizes the enforcement agencies in Canada to use trade remedial measures to protect domestic producers from injury caused by the unfair trade practices (i.e., dumping and subsidization) of foreign exporters. The WTO signatories are, however, prohibited from imposing remedial measures in the absence of the "injury determination" which is a crucial element of international trade administrative law. In North America, there are two general approaches to injury determination in investigations into complaints of dumping and subsidization. They are called the bifurcated, or two step procedure, and the unitary approach. Economists generally criticize the bifurcated approach as a way to assess the effect of dumping on the domestic industry. Economists prefer the unitary approach because of its potential to isolate the effects of dumping from all other non-dumping effects on the domestic industry. Description of two quantitative economic approaches used in the unitary approach are described and illustrated.

What Have We Learned About Trade Disputes Under NAFTA?

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This paper reports on evidence and conclusions gathered from an ongoing program which conducts workshops on trade disputes with NAFTA. The program, designed to produce and distribute economic information on policy trade relations and trade disputes, is in its seventh year of operation. There are a number of overriding conclusions which come out of the workshops: 1) a trade agreement does not assure harmony in trade relations, nor does it provide a dispute free trade environment; 2) there are more disputes to come; 3) the most effective way to resolve disputes is to avoid them; 4) despite the free trade agreement, there remains intractability in several areas of policy and trade within the NAFTA countries; 5) the role and contribution of economics to dispute resolution is limited; and 6) too few disputes are investigated and resolved within NAFTA protocols. The paper presents comments, evidence, and examples in support of these conclusions.

Session VII - PANEL DISCUSSION - BETTER TRADE RELATIONSHIPS

Charlie Mayer, Former Minister responsible to Parliament for the Canadian Wheat Board

Four areas of discussion: the high level of trade between the United States and Canada, growth in other markets, problems with Europeans, and issues for tomorrow. The open border between the United States and Canada results in increased bilateral trade volume. The high levels of trade results in trade disputes. Growth needs to be in markets outside of the United States and Canada, such as Asia and Mexico. The economies of developing countries are small but growing. These areas need to be targeted. We have larger problems with the Europeans. The Europeans spend too much on agricultural policies; Europe produces a food surplus and dumps it on the world market. There are a number of other issues and problems for the future such as environmental issues. Other issues are more important than the little skirmishes between the United States and Canada. Both countries should focus more on these issues, on growth in other markets, and on the problems with Europe. Trade should be beneficial to all.

Robert Carlson, President, North Dakota Farmers Union

One reason for the trade irritants is that farmers have not figured out how to profit from freer trade. From the perspective of a U.S. producer, complaints about freer trade include more competition, the loss of the option of using supply management programs (e.g., EEP and land set-aside programs), and a lower safety net. Harmonization should not mean the elimination of programs to meet at the lowest common denominator. A better response would be a multinational marketing agency. This would include a voluntary North Dakota pool which would cooperate with the Canadian Wheat Board. A study at North Dakota State University indicated that this would work for durum, but not for hard red spring wheat. The idea of a North Dakota pool has been favorable to North Dakota farmers. There are many hurdles, though, to overcome. There are questions regarding if it will work, and the CWB has some concerns. The pool still is an appealing idea, especially with low prices. Producers need to think in a more innovative manner.

Vincent Smith, Co-Director, Montana Trade Research Center

The price effects of the CWB are difficult to determine. Trade dispute mechanisms may be bad, but they are necessary. The North Dakota durum pool is not very viable, due to supply responses. Also, the costs associated with a marketing board are significant.

Blair Rutter, United Grain Growers

We need to build on the success of the Uruguay rounds. Three achievements from the Uruguay rounds include capping support, a dispute settlement mechanism, and tarrification of all import barriers. These achievements can be built upon by the greening of all forms of support (not being concerned with absolute values) and by respecting the choices of other countries, as long as these choices are non-distorting and do not harm the citizens of other countries.

Andrew Schmitz, University of Florida

There are a number of losers and gainers in the process. The losers in free trade need to be compensated. Supply management in Canada needs to be eliminated, and the losers in the process should be compensated. Harmonization is very difficult, Canada needs to address its problems before harmonization is possible.

Remarks
***Timothy J. Galvin, Administrator, Foreign Agricultural Service,* USDA**

Even a cursory glance at the numbers since the Free Trade Agreement took effect would lead one to conclude that our trade relationship with Canada has flourished. Two-way agricultural trade between the two countries is substantial, though Canada has faired better than the United States in this arena. A number of factors have contributed to the growth in U.S.-Canada trade, including the market-opening provisions of the Free Trade Agreement, a booming economy in the United States, and economic growth in Canada as well. But another obvious factor, especially in explaining the end of the U.S. trade surplus and the growth of Canada's surplus, is the exchange rate. It should also be noted that in Canada, 43 percent of GDP and one-third of all jobs are dependent on international trade; in the United States only 11 percent of GDP is trade-related. Another revealing indicator is Canada's dramatic increase in its reliance on a single market, the United States, as an export destination.

With agricultural exports between the two countries showing steady year-to-year gains, it is clear that our mutual interest lies in continuing to expand bilateral trade, rather than looking for ways to close borders. In that regard, we have made good progress the past couple years in strengthening our bilateral trade relationship in agriculture, and the United States and Canada have many common goals as we approach the next multilateral round of trade negotiations under the World Trade Organization (WTO). One subject that has provoked strong emotions on both sides of the border is the cost and availability of pesticides, and the apparent lack of harmonization between our two regulatory systems. Much work has been accomplished recently regarding these issues.

Despite the real progress being made in a number of areas, there remains several rather high profile issues that continue to generate some controversy, and they tend to revolve around trade in grain, livestock, and meat products. These disputes reflect some differences over the issue of domestic subsidies and the transparency of our respective export systems. U.S. support levels have been higher in the past few years, but the gap is not the wide discrepancy that some in Canada are claiming. The issue of export competition remains controversial as well, and will likely remain so as long as questions persist about the marketing practices of the Canadian Wheat Board (CWB). In my view, those questions will continue until the operations of the CWB are made more transparent.

Despite differences on some specific issues, the record of cooperation between the United States and Canada on several larger trade policy issues is a good one. We seem united on the elimination of export subsidies as a principal objective in the next round of WTO negotiations. We also agree on other major WTO objectives including improved market access in the form of further reductions in tariffs or increases in TRQs, new disciplines on domestic subsidies,

preservation of the Sanitary and Phyto-Sanitary Agreement and its requirement that SPS measures be based on sound science; and we take a similar view with regard to the adoption of biotechnology in modern agriculture. We see eye to eye on many issues and have much to gain by working together. And even though we often come to the debate with a different perspective, we should make every effort to stick to the facts, and to dispel the myths where we can.

U.S. producers have much at stake in making sure the focus is on opening markets rather than building walls. If the United States does not pursue further trade liberalization, other countries will. There is a real risk that if the United States does not engage in further trade liberalization, we will find ourselves on the outside looking in as other countries move ahead to finalize their preferential trade deals and exclude the United States. Unless we pursue the trade opportunities we have worked so hard to create, producers in other countries will reap the benefits of trade reform.

Concluding Comments

Won W. Koo, Director, Northern Plains Trade Research Center,
North Dakota State University

Papers presented in the conference focused on the issues related to agricultural trade between the United States and Canada under CUSTA. They are (1) CUSTA's impacts on bilateral agricultural trade, (2) recent evolution of the U.S. and Canadian agricultural marketing systems, (3) major issues for further commercial integration, (4) recent development in U.S. and Canadian transportation system, and (5) trade disputes and negotiations.

Although most presenters agreed that CUSTA has been good for both the United States and Canada, concerns were raised in agricultural trade. One of the concerns discussed during the conference is the substantial increase in Canadian exports of agricultural commodities relative to U.S. exports to Canada since the inception of CUSTA, which resulted in several trade disputes between the two countries, and its impacts on the Northern Plains agricultural economy. Some factors that have affected the flow of Canadian exports to the United States are differences in agricultural policies and marketing systems and appreciation of the U.S. dollar against the Canadian dollar during the last ten years. Harmonization of agricultural policies and marketing systems between the two countries may be very difficult, but it is necessary to have some harmonization to promote a "fair" trade between the two countries under the free trade agreement. In addition, the two countries should cooperate rather than continually having confrontations. One type of cooperation is Canada's voluntary export restraints of wheat exports to the United States; another is a joint effort in marketing wheat to North American and offshore markets. A North Dakota State University study found that a marketing pool for durum wheat in North Dakota is economically feasible with cooperation from the Canadian Wheat Board (CWB). Gains from the marketing pool would be significant for both durum producers in the United States and the CWB through exercising limited market power in the North American market and improving marketing efficiency.