US Restrictions on Canadian Lumber Exports

Economic Implications for Canada, Industries, Provinces and Communities

Summary

The 1996 Softwood Lumber Agreement between Canada and the United States expired at the end of March 2001. US lumber and timber interests have filed documents designed to restrict future Canadian exports. These actions, if successful, could impose very severe penalties on Canadian producers. The nature of penalties, time of introduction and magnitudes are now uncertain.

To trace the impacts of such actions, we have assumed that Canadian exports are reduced by $1 billion valued at 2001 prices. Three-fourths of this amount affects the economy in 2001. In 2002, the full effect of the $1 billion reduction is felt. Thereafter, restrictions are assumed to have the same proportionate effect on each year's Canadian exports as the first full year of restraint. We examine effects through 2006.

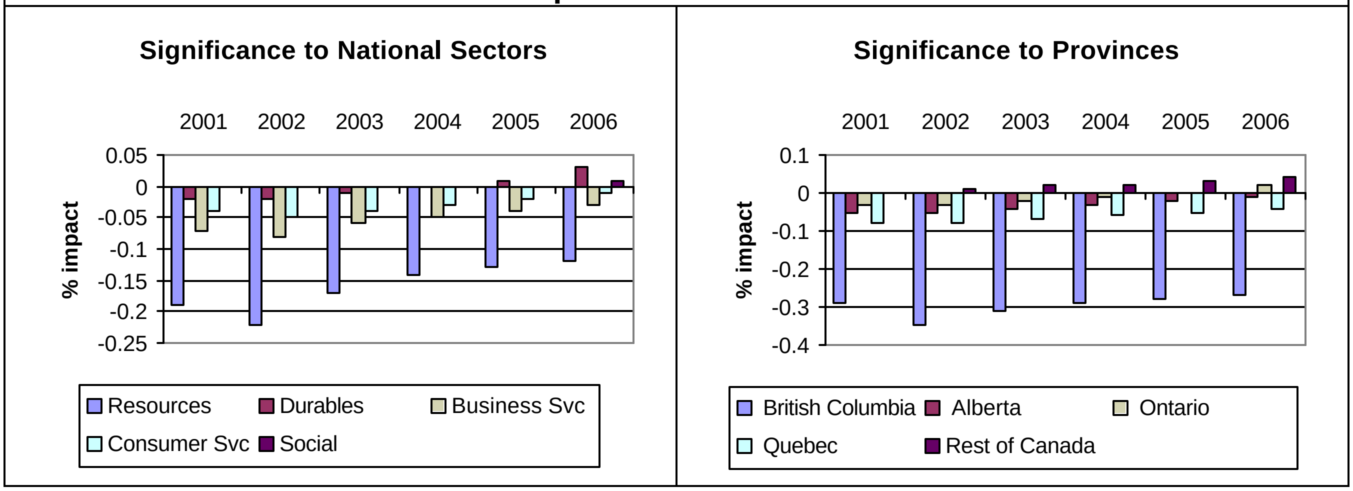
Given this scale of restraint, real production in Canadian sawmills would be reduced in 2002 by close to 5 per cent. Forestry production, which supplies the mills, is reduced by 3 per cent. We assume that only those mills in provinces (British Columbia, Alberta, Ontario and Quebec) covered by the earlier agreement are affected. There are some adjustments in productivity in the short term, but by 2003 these are largely completed. In that year job losses in the forestry and wood products industries are as follows: British Columbia (2,200), Alberta (400), Ontario (900) and Quebec (1,600).

The effects do not end there. Consumption, investment and other impacts are induced by changes to the incomes of those affected directly and indirectly. This "shock" has implications for all industries and all provinces.

The forestry and related processing industries explain most of the significant negative impact for resource industries. Consequent negative impacts on the supply of trucking and rail transport concentrate the second most significant effects among business service industries. All industries initially are reduced by adverse income effects, but with increased unemployment and reduced returns in the forestry and other industries, Canadian costs and prices are lowered. Magnitudes of this effect on inflation are small, but slowly promote some positive trade offsets. Durables manufacturing industries, faced with highly competitive markets, begin to recover and in the longer term could produce more than would occur if the initial restrictions had not been imposed. Much of this would be at the expense of US producers of the products so that this poses a small cost to

the US economy of such action. Reduced Canadian investment in equipment would also adversely affect suppliers, mainly Americans.[1]

Impacts on Real GDP



Our results suggest that overall adverse effects in British Columbia would stand out among the provinces. This follows largely from the especially high proportion of the province's output accounted for by sawmills that are dependent on softwood exports to the US. Implications for other directly affected provinces are also negative, but modest in comparison. As well, as their trade-sensitive industries begin to recover, overall provincial output moves back towards levels of activity that would occur if no export restrictions were imposed. Provinces excluded from the import restrictions are initially affected adversely through indirect and induced impacts. Longer term, lower Canadian costs of production yield positive effects for these other provinces. But both negative and positive effects are very small. Among these, we note that, while we assume no change of their sawmill exports to the US, we do assume that lower costs yield increased lumber exports to other foreign markets (partly at the expense of US exports). If these suppliers are "side swiped" or if affected mills in the four, targeted provinces compete in their provincial markets, positive effects would be mitigated or reversed. New Brunswick is the most vulnerable to "side swipe" considerations.

The proportionate effects of a $1 billion restraint range from "modest" to negligible for most industries and provinces. But impacts on many communities will be very significant. Taken to the Census Sub-Division (CSD) level, we have identified many that are at high risk. Seen against the interest of community leaders and those of provincial authorities that would have to manage dislocation, we draw several conclusions.

- Immediate concern about local impacts is focussed on rural communities where sawmills are a dominant or major source of income. Proportionately severe impacts will be in rural areas. The major urban centres will also be affected

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[1] This study does not assess effects on the US economy and implications for Canada of those. It does identify, however, several costs to the US beyond those customarily associated with higher lumber costs.

directly, however, and in all provinces, these are the most important CSD sources of lumber industry employment (and GDP). Corporate headquarters and staff are located in these centres. Indirect effects on business service industries and induced effects from lower incomes in the province will also affect urban centres.

- Canadian producer interests indicate that 300 communities are at risk. In each of the directly affected provinces we have analyzed, there are many such communities. From the perspective of provincial authorities managing dislocation, this will be a particularly difficult problem for Quebec. Managing a many-communities problem will likely be least severe in Alberta.

These results are intended to serve as a benchmark of likely effects. But real impacts will depend on the outcome of trade processes and bargaining that is only now beginning. The $1 billion impact can be scaled up (or down) to approximate the overall effect of a new regime so long as the magnitude of any change is not so large as to directly impact other trade “collaterally”. How firms, communities, and governments react may differ from the simplifying assumptions made here.

Producers and others may urge Canadian governments to react to any US restrictions. With Canadian supply displaced from the US market, there will be a temptation to go after US lumber export markets, including that of their single largest customer, Canada. If this includes restraints on US exports to Canada or subsidies to promote Canadian exports elsewhere, there are two principal arguments against this. First, Canada takes the position before US legislators that supply restraints will harm American homebuilders and consumers. Restraints on supply (action against US imports) would have the same effect on Canadian consumers. Second, the broad policy objective of Canada is to move the softwood lumber issue into a “free trade” status. Tactical targeting of American markets in Canada or elsewhere will undermine this argument.

Producers may also urge Canadian governments to take new actions to reduce costs without violating trade rules. Among these may be development of infrastructure (e.g., of transportation systems) that would contribute to reduced private costs of sales. Several considerations stand in the way of this. Other things equal, American export restraints on lumber have a negative effect on government balances. Privatization (or in the case of ports, local control) of transportation services in the last decade limits the ability of governments to intervene directly. Finally, improvement of the transportation system for purposes of reducing costs for trade in international markets will also promote more competition within Canadian markets. While consumers may cheer this initiative, officials and businesses with a provincial producer perspective may view this with misgivings.

C. Sonnen
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