

The long and sterile controversy over alleged Canadian subsidies fails to take into account the interests of American lumber users.

Introduction

The long-running and rancorous battle over softwood lumber stands out as the United States' largest single trade dispute with its largest trade partner. Specifically, lumber trade between Canada and the United States has been dogged for years by U.S. charges that Canadian lumber producers benefit from unfair government subsidies. To put the stakes of this dispute in some perspective, the value of U.S. softwood lumber imports from Canada nearly matches the value of U.S. carbon steel imports from the entire world.¹

Mechanisms to "resolve" the dispute have varied, but they typically have entailed the erection (or threat) of trade barriers under the U.S. countervailing duty law. Most recently, Canada and the United States signed in May 1996 the Softwood Lumber Agreement, which restricts imports of lumber from Canada by subjecting amounts in excess of agreed limits to special charges. The SLA is set to expire in April 2001, however, and both the Canadian and U.S. governments are expressing dissatisfaction with the agreement and signaling a desire for change.

Through all the iterations of this dispute, the debate has been framed in this country as a conflict between American lumber companies and Canadian lumber companies over whether a "level playing field" exists. Defining the issue in that way overlooks an important part of the equation—the other U.S. interests with a stake in this dispute. The long and sterile controversy over alleged Canadian subsidies fails to take into account the interests of American lumber users in the lumber-dealing, homebuilding, and home-furnishings industries. It also overlooks the interests of American buyers of new homes and home furnishings. Trade restrictions on Canadian lumber injure important American interests and have done so for nearly 15 years.

At the center of the controversy have been questions about the pricing of lumber on Canadian Crown lands (timberlands owned by Canada's federal and provincial governments).

From a free-market perspective, that system is clearly imperfect. But the U.S. system is not perfect either. In the end, the claim that Canadian producers enjoy an unfair advantage over their American rivals is not persuasive, and certainly is not compelling enough to justify saddling American lumber users with costs artificially inflated by trade restrictions. Accordingly, the SLA should be allowed to expire in 2001, and new trade restrictions should be avoided.

A History of Trade Restrictions

Although the dispute over Canadian lumber imports dates back many decades, it has heated up significantly since 1982. Since that time, three countervailing duty (CVD) cases have been initiated by the U.S. Department of Commerce and the International Trade Commission. Specifically, Commerce and the ITC investigated whether the Canadian federal and provincial governments were injuring U.S. softwood lumber producers by subsidizing Canadian firms. The most important alleged subsidy involved "stumpage" fees, the prices timber users pay to the government to harvest trees from Crown lands. The claim was that Canadian lumber producers benefit from below-market stumpage rates.

In the first CVD investigation (known as Lumber I) in 1983, Commerce ruled that Canada's stumpage system did not confer a subsidy to a specific industry or group of industries because it was used by a wide range of diverse businesses—including the lumber and wood products industries; the veneer, plywood, and building board industries; the pulp and paper industries; and the furniture manufacturing industries.² Commerce also concluded that the system constituted a "reasonable method for establishing stumpage prices" and thus did not provide goods at preferential rates under the standards of the U.S. law. In that regard, Commerce found that "a comparison of Canadian stumpage prices with U.S. prices would be arbitrary and capricious in view of

the wide differences between species composition; size, quality, and density of timber; terrain and accessibility of the standing timber throughout the United States and Canada.”³ Nevertheless, the review of available data showed that “Canadian prices for standing timber do not vary significantly from U.S. prices. Indeed, in some cases the Canadian price may be higher.”⁴ That decision by Commerce was upheld on appeal by the U.S. Court of International Trade.

Three years later, Commerce reversed itself in a second CVD investigation (known as Lumber II) and found that Canadian stumpage rates conferred a 15 percent subsidy. The Commerce Department’s about-face reflected, not a change in practices by the Canadian government, but a change in the way that Commerce analyzed the issue.⁵ The investigation and appeals were ultimately terminated, however, when Canada and the United States entered into a memorandum of understanding (MOU). The 1986 MOU stipulated that a 15 percent export charge would be imposed on all Canadian softwood lumber exports to the United States. Canadian provinces (notably British Columbia) subsequently implemented changes to their stumpage systems and transferred certain costs to the softwood lumber industry; the U.S. government responded by agreeing to reduced export charges.

In light of changing practices, Canada unilaterally terminated the MOU in 1991. The U.S. government responded immediately by imposing interim duties on Canadian lumber under section 301 of the Trade Act of 1974, and then initiated a new CVD investigation (Lumber III). This time, the Commerce Department found a smaller stumpage subsidy of 2.91 percent on lumber from British Columbia; in addition, though, it concluded that restrictions on exports of unprocessed logs constituted a subsidy of 3.6 percent.

Lumber III was the first of the CVD cases to occur after the signing of the U.S.-Canada Free Trade Agreement. Canada appealed both the Commerce and the ITC determinations under the binational dispute settlement procedures of the FTA. What followed was an extremely contentious process as binational panels repeatedly

overturned both the Commerce and the ITC findings while the two agencies repeatedly upheld their original determinations. Ultimately, the United States agreed to refund more than \$800 million in duties collected, and both countries agreed to enter into a “dialogue” on future lumber negotiations.

The Softwood Lumber Agreement

The victory in Lumber III took its toll on the Canadian softwood lumber industry, which paid out millions in legal fees fighting U.S. claims of subsidization. As one former Canadian trade negotiator remarked, “The prospect of fighting trade cases against the U.S. was considered too costly and fraught with risk, given the U.S. system’s arbitrary and capricious nature.”⁶ Accordingly, when threats of a new CVD case surfaced in 1995 and 1996, Canada gave in to protectionist pressures.

The compromise solution was the SLA, set to run from April 1, 1996, to March 31, 2001. Specifically, the SLA sets export quotas for companies operating in British Columbia, Alberta, Ontario, and Quebec. Those producers are permitted to ship 14.7 billion board feet of lumber a year to the United States duty-free. The next 650 million board feet are subject to a fee of \$50/thousand board feet; all greater quantities are subject to a charge of \$100/thousand board feet. Although each company’s quota is not public knowledge, the allocation of the quotas among the four provinces was based on historical shipments. Since Canadian coastal producers sent 48 percent of their wood to Japan when the SLA was signed, interior provinces hold over 75 percent of the quota because they were concentrating on U.S. markets.⁷

As part of the agreement, the United States agreed not to pursue trade remedy actions under the CVD or other trade laws. Several additional disputes, however, have arisen. U.S. customs officials reclassified three processed products (pre-drilled studs, rougher-header lumber, and notched studs) so that they fall under the scope of the SLA. Canada respond-

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ed by announcing it would appeal those reclassifications before the World Customs Organization. In the only case so far, the WCO, made up of the customs administrations of 151 member governments, ruled in favor of Canada's position that pre-drilled studs should not be covered under the SLA.⁸ WCO decisions, however, are nonbinding.

In light of those difficulties, as well as a growing awareness of the costs of protectionism on both sides of the border, both the Canadian and the U.S. governments have expressed skepticism about renewing the SLA upon its expiration.⁹ What will replace the SLA, if anything, is unclear. Protectionist interests in the United States—notably, those American lumber producers that belong to the Coalition for Fair Lumber Imports—are urging a continuation of trade restrictions. On the other side, a lobbying group of lumber-using interests called American Consumers for Affordable Homes—which has as members the National Association of Home Builders, the National Lumber and Building Material Dealers Association, and Home Depot, among others—is pushing for termination of the SLA and a return to open trade.

Bipartisan support for the free-trade solution is growing in Congress. Reps. Jim Kolbe (R-Ariz.) and Steny Hoyer (D-Md.) have introduced H. Con. Res. 252 calling for termination of the SLA; the resolution has now attracted more than 100 cosponsors. A companion resolution, Senate Con. Res. 111, has now been introduced by Sens. Don Nickles (R-Okla.), Jon Kyl (R-Ariz.), Joseph Lieberman (D-Conn.), Bob Graham (D-Fla.), Charles Grassley (R-La.), Richard Lugar (R-Ind.), and Richard Durbin (D-Ill.).

In calling for termination of the SLA, Representatives Kolbe and Hoyer have cited the need "that all consumer stakeholders be consulted in the process and that the effects of such a trade agreement on consumers in America be weighed at least equally with the effects on those companies seeking trade restraints."¹⁰ Data presented below confirm that the interests of consumers of softwood lumber have been ignored in previous rounds of the softwood lumber trade dispute.

Consumers of Softwood Lumber: The Neglected Side of the Story

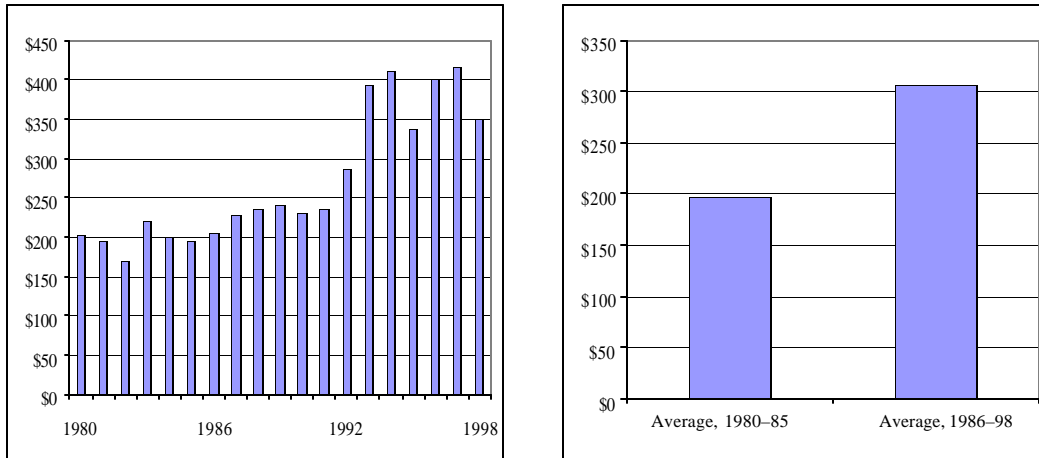
The price of lumber has risen substantially since the onset of measures to protect the U.S. softwood lumber industry (Figure 1). Between 1980 and 1985 the price of lumber averaged just under \$200 per thousand board feet, whereas between 1986 and 1998 the price averaged a little over \$300. Thus, after the imposition of trade restrictions, average lumber prices rose by about \$100 per thousand board feet. In 1999 prices rose but varied significantly from as low as \$357 per thousand board feet to as high as \$480.¹¹

Of course, not all of the \$100 per thousand board feet increase in the average price was necessarily due to the softwood lumber dispute. Other factors that shift either the demand for lumber or its supply could have played a role in driving up the price of lumber. However, our statistical analysis has found that, after controlling for those other factors, trade restrictions are responsible for raising lumber prices by between \$50 and \$80 per thousand board feet.

To isolate the effects of trade restrictions, we must first take account of other factors that affect the supply of and demand for lumber and hence influence lumber prices. The most significant factor affecting the demand for lumber is the strength of the economy. The demand for lumber is derived substantially from the demand for new or remodeled houses, which in turn depends on how well the economy is doing. The period 1980–85 was marked by two recessions, including a deep recession in 1982, while the period 1986–98 was marked by a strong expansion. As a consequence, real gross domestic product growth averaged 2 percent a year in the former period compared with 2.6 percent a year in the latter (Figure 2). The economy has performed better since 1986, likely boosting demand for and prices of lumber.

Data on housing starts are a convenient tool for measuring the likely impact of the stronger economy on lumber prices. A stronger economy boosts housing starts and thus lumber

Figure 1
Lumber Prices (per 1,000 board feet), 1980 to 1998



Source: Random Lengths, <http://www.randomlengths.com>.

prices (Figure 3). On the supply side, several factors are likely to be at work. First, one would expect the price of lumber to increase with movements in the overall producer price index, reflecting increases in the cost of inputs used in lumber production. Second, timber supplies are affected by numerous factors such as (1) changes in timber harvests from federal lands, notably in the Pacific Northwest, because of environmental concerns, and (2) changes in the volume of unprocessed timber (logs) exported from the Pacific Northwest to Japan and other Asian countries.

Statistical models establish that lumber prices do indeed depend on the factors that cause shifts in demand and supply (see Appendix). In particular, the strength of economic conditions, movements in the overall producer price index, and changes in timber supplies have an impact on the price of lumber.

After controlling for all of those other factors, though, we find that trade restrictions on Canadian imports have caused an increase in U.S. lumber prices. Our statistical work suggests that, after controlling for those factors, real (i.e., inflation-adjusted) lumber prices are higher by between \$50 and \$80 per thousand board feet as a consequence of attempts to pro-

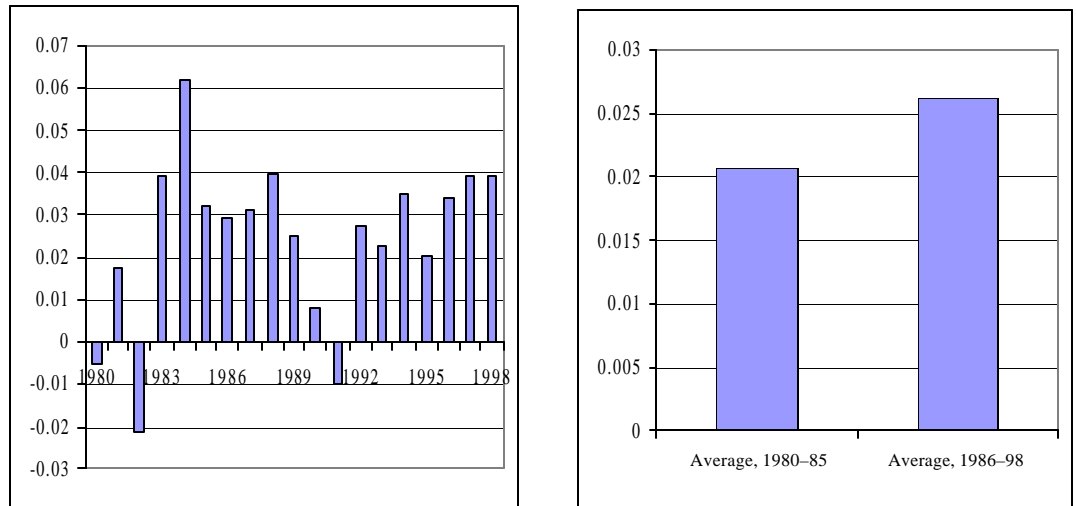
tect the U.S. softwood lumber industry. From the perspective of U.S. consumers (i.e., users) of lumber, this represents a 15 to 25 percent tax on the consumption of lumber. A more detailed description of our methodology and some representative specifications are given in the Appendix.

Interpreting the Results: Who Suffers from Softwood Lumber Protection?

At the time of the signing of the SLA, then-U.S. Trade Representative Mickey Kantor said that the trade restrictions would have “negligible, if any” impact on prices of new houses.¹² The reality is different. Construction wood is a major material used in homebuilding. Some 75 percent of softwood lumber usage in the United States is either for new home construction or repairs on existing structures.¹³ Although there is some potential for substituting other material such as steel framing, the extent to which that can be done is limited.¹⁴ Hence, increases in lumber prices are reflected, to a considerable extent, in the prices of new (or remodeled)

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Figure 2
Real GDP Growth, 1980 to 1998



Source: International Monetary Fund, *International Financial Statistics Yearbook* (Washington: IMF, 1999).

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homes. The National Association of Home Builders estimates that direct and indirect use of lumber in an average new home is about 16,000 board feet.¹⁵ The estimated increase of between \$50 and \$80 per thousand board feet in lumber prices as a result of the softwood lumber dispute therefore adds between \$800 and \$1,300 to the cost of a new home.

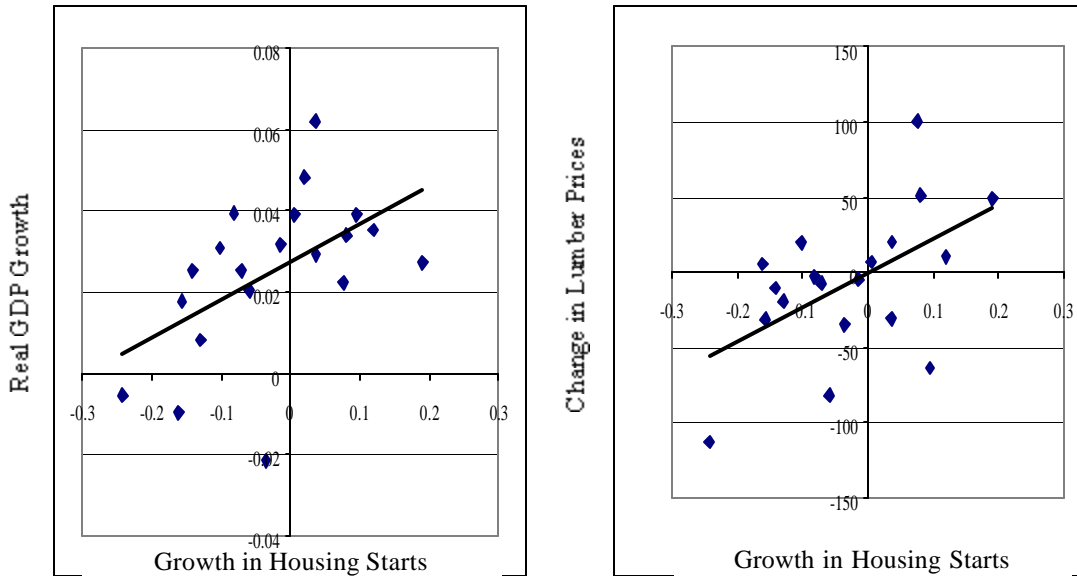
The consequence of protection in softwood lumber is that many Americans who dream of owning a home are priced out of the market. The U.S. Bureau of the Census estimates that for every \$1,000 increase in housing prices, an additional 300,000 families are unable to purchase a home.¹⁶ The bulk of those 300,000 families, of course, are lower-income families. Consumers for World Trade president Doreen L. Brown remarked, "Hurt the most are lower income Americans, first-time homebuyers and the elderly on fixed income because a higher percentage of lumber is used in lower priced housing than in more expensive homes."¹⁷ In a similar vein, the National American Indian Housing Council has stated: "Since many of our members fall into this fringe group that could be priced out of the market by inflated construction costs, the Softwood Lumber Agreement negatively impacts the work we are

trying to accomplish. . . . Affordable housing is an issue of great concern to Native Americans."¹⁸

In addition to preventing thousands of families from fulfilling their dream of owning a home, trade restrictions on softwood lumber distort and disrupt markets to the detriment of downstream industries. Home Depot, the world's largest retailer of lumber, has complained that the SLA "creates a volatility in the supplier market, to the retailer and finally to the customer."¹⁹ It was for that reason that the U.S. Forest Service actually called for an increase in Canadian imports because demand could no longer be met by domestic producers.²⁰

Smaller businesses that specialize in manufacturing products from softwood lumber also suffer. For example, some American businesses have complained that the SLA has restricted access to low-grade cedar, which otherwise would be available in abundance from Canadian suppliers. One manufacturer commented that the SLA "has caused low-grade Cedar to be in short supply and the price of Cedar to be high. . . . The U.S. simply does not have enough supply."²¹ Another remarked: "It has been difficult getting the low-grade material we need because of the quota. It creates

Figure 3
Real GDP, Housing Starts, and Lumber Prices



Source: *Random Lengths*, <http://www.randomlengths.com>; and International Monetary Fund, *International Financial Statistics Yearbook* (Washington: IMF, 1999).

artificial markets. We need a free market controlled by supply and demand.”²²

Those in favor of lumber protection, such as members of the Coalition for Fair Lumber Imports, assert that the SLA benefits workers in the logging and sawmill industries. No doubt particular companies and their workers do benefit from trade restrictions, although it is also important to point out that not all softwood lumber producers support the SLA. The CFLI, which has long presented itself as the voice of the U.S. industry, does not in fact represent the industry as a whole. Major U.S. producers, including Weyerhaeuser and Louisiana Pacific, are not members of the coalition.

Moreover, it is important to realize that the benefits of trade restrictions for some workers come at the expense of many more workers in a wide variety of industries. In 1999 there were 217,000 payroll jobs in logging and sawmills. That contrasts with some 6 million workers in lumber-using industries. Specifically, employment in downstream manufacturing industries that use softwood lumber was 510,000 in 1999, while there were 744,000 jobs in the wholesale

and retail lumber trade and more than 4.7 million in homebuilding, not counting more than a million self-employed contractors.²³ In other words, employment in lumber-using industries exceeds employment in lumber production by a ratio of better than 25 to 1. The protectionist argument in favor of the SLA is thus tantamount to saying that the commercial interests of a portion of one small industry outweigh those of many, much larger industries—not to mention the interests of millions of American homebuyers.

Our conclusion that softwood lumber trade protection harms U.S. lumber consumers confirms the findings of several previous studies. A study of the impact of the 1986 MOU on softwood lumber found that despite gains to U.S. producers of softwood lumber, there were losses to Canadian producers and U.S. consumers and efficiency costs were high.²⁴

Similarly, economists at the University of Georgia concluded that the 1987–91 lumber export tax and the import duties imposed in 1992 were prime examples of “beggar thy consumer trade policy.”²⁵ Using an estimated model of the softwood lumber market, the economists

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concluded that the 1987–91 MOU had placed the main burden on Canadian producers, with U.S. consumers bearing the second largest burden. Moreover, U.S. consumers were hurt in excess of the gains to U.S. producers. In other words, “[T]he U.S. had imposed an immiserizing trade policy on itself in order to benefit the interests of an organized lobby.”²⁶ With the switch to a CVD order in 1992, U.S. consumers again bore the second largest loss, though the loss was less than under the export tax; moreover, the U.S. government, in principle, gained enough in revenue through the import duty to compensate the consumers for their loss. But the authors argue, “If, however, a consumer suspects that taxes will not be reduced in an amount commensurate with the revenue collected from the imported lumber, then the consumer is right to feel that both trade policies gave short shrift to the U.S. consumer.”²⁷

Do Canadian Producers Have an Unfair Advantage?

Supporters of the SLA claim that trade restrictions are justified to counteract subsidies received by Canadian lumber producers. Those subsidies confer an unfair competitive advantage, the argument goes, and therefore some kind of protection is needed to create a “level playing field.” In fact, however, the evidence that the Canadian industry enjoys an unfair advantage is far from compelling.

The principal difference between the Canadian and the U.S. softwood lumber industries lies in the ownership structure of timberlands. The U.S. forest industry relies on privately owned forests for approximately 95 percent of its softwood timber supply. Indeed, much of the timber used by the U.S. lumber industry comes from lumber producers’ own holdings. Less than 5 percent comes from U.S. national forests or other public lands. The softwood timber cut on federal lands is acquired through a competitive bidding process.

In Canada, by contrast, more than 90 percent of the commercial forests that supply the softwood lumber industry are Crown lands owned by

the government—mostly provincial governments—that sets stumpage values. Lumber companies (or any other consumers of timber) are charged a stumpage fee by the provincial government to harvest the timber. Stumpage values are determined by a variety of formulas that reflect specific terms and conditions of long-term forest management agreements and timber harvesting licenses, as well as market conditions.

Differences in forest ownership aside, it should be noted that the original determination of the U.S. government in Lumber I was that the Canadian stumpage programs do not constitute subsidies. Although the Commerce Department later reversed itself in the face of severe political pressures, a binational panel ruled repeatedly that Commerce was misapplying U.S. law. The legal record, accordingly, fails to offer clear support for U.S. producers’ claims of unfair trade.

Academic studies likewise cast doubt on those claims. For example, in testimony before the binational panel in Lumber III, William Nordhaus, professor of economics at Yale University, described an “effects test” to determine the impact of stumpage prices on the U.S. market. He found that, within a given range of prices for timber, the price of lumber sold as a commodity in the United States would not be affected by changes in stumpage values.²⁸ His later work with Robert Litan of the Brookings Institution determined that Canadian stumpage values were indeed within that “normal” price range and therefore did not distort the price or quantity of logs or softwood lumber.²⁹

Furthermore, it is noteworthy that there is no evidence to suggest that Canadian timber harvesters are receiving supranormal profits from alleged subsidies. If that were the case, industry returns would be much better. Interestingly, Price Waterhouse Coopers found a forest industry average return on assets over a 10-year period of 1.0 percent in British Columbia and -0.2 percent in Eastern Canada, versus 3.1 percent in the United States.³⁰ Such returns are hardly compatible with claims that the Canadian industry benefits from a below-market cost structure.

Meanwhile, complaints that Canadian producers enjoy an “unlevel playing field” ignore the many government programs that benefit U.S. lumber producers. The United States is required to report to the World Trade Organization all government programs that constitute subsidies under WTO rules. Pursuant to that requirement, the United States has notified the WTO of a variety of special federal tax provisions that benefit the forestry industry. Those provisions include special capital gains treatment for qualifying timber sales, authorization to expense rather than capitalize timber-growing costs, a special investment tax credit and amortization schedule for reforestation expenses, and an exemption from fuel taxes for helicopters used in logging operations. The combined annual revenue loss from those provisions is \$600 million.³¹

In addition to federal subsidies, U.S. state and local subsidies to the timber industry abound. For example, North Carolina, Maine, and Wisconsin offer tax credits for new investments by timber firms, while Montana and Georgia provide direct financial assistance to the forestry industry.³²

It also bears mentioning that in Lumber III the Commerce Department found that Canadian restrictions on log exports amounted to a subsidy for Canadian lumber producers. Commerce determined: “With regard to export restraints, while they may be imposed to limit parties’ ability to export, they can also, in certain circumstances, lead those parties to provide the restrained good to domestic purchasers for less than adequate remuneration.”³³ What the Commerce Department did not mention is that the United States imposes similar bans at both the national and the state level. The Forest Resources Conservation and Short Relief Amendments Act of 1993 bans the export of logs from all federal and most state lands west of the 100th meridian. Alaska and Idaho even restrict shipments of logs to other states. Though such export restrictions are inadvisable, whether in Canada or the United States, the fact that both countries maintain them undercuts the charge that Canadian lumber producers enjoy an “unfair” advantage.

Finally, whatever the merits of the allegations that Canadian lumber is subsidized, the specific restrictions of the SLA cannot be justified as an anti-subsidy measure. The current quota and the fee structure for above-quota shipments have no basis in any calculation of the alleged level of subsidization. The provisions of the SLA were arrived at in a purely political manner; they were designed simply to reduce imports of Canadian lumber and drive up U.S. lumber prices. The SLA, consequently, has no rational relation to any plausible conception of a “level playing field.”

Addressing Environmental Concerns

Supporters of the SLA and other protectionist solutions to problems in the lumber trade also invoke concerns about the environment. Specifically, those supporters claim that Canadian subsidies encourage unsound environmental practices in Canada. The Natural Resource Defense Council, for example, alleges that subsidization “contributes to the overcutting of British Columbia’s forests.”³⁴ In response to this situation, the NRDC calls for the United States to “press for the strengthening of long-term international institutions designed to ensure the enforcement of environmental legislation.”³⁵ The SLA, apparently, is one of those institutions.

Several responses are in order. First, there are other, better ways to promote environmental goals than trade restrictions. Even if the NRDC’s claim that Canada engages in unsound environmental practices has foundation, trade restrictions are not the appropriate solution to the problem. When concerns about smokestack emissions from steel mills were prominent, the United States did not put quantitative restrictions on steel exports; such an approach would have been an absurdly roundabout and inefficient way of addressing the underlying problem. Restrictions on Canadian lumber exports would be just as ill suited to resolving any environmental problems with Canadian forestry practices.

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The SLA is the latest in a long line of trade restrictions on Canadian lumber. It should be the last.

Second, there is little reason to believe that terminating the SLA would have a significant impact on harvesting, since Canadian government officials would still determine the amount of timber that could be harvested. That amount would not necessarily change. Consequently, harvesting of timber would still occur at very close to the same rate if the SLA were terminated; ending trade restrictions would simply stop rents from being transferred to a few lumber producers in the United States at the expense of Canadian producers and U.S. consumers. Similarly, the available evidence casts doubt on whether the alleged subsidy of low stumpage rates has any significant effect on the quantity of timber harvested in Canada. Studies have shown that Canadian stumpage rates do not distort the quantity of logs harvested and that changes in stumpage rates have little impact on that quantity.³⁶ Nordhaus and Litan, for example, find that “timber production shows virtually no response to stumpage charges.”³⁷

Third, a number of private-sector initiatives are being implemented to help protect forests that some people consider endangered. Macmillan-Bloedel, now part of Weyerhaeuser, unilaterally announced that it would pursue alternatives to clear-cutting. On the user side, many companies have announced that they will not use timber that is harvested by clear-cutting; those companies include IBM, Nike, Hallmark, Bristol-Myers Squibb, 3M, and Lockheed Martin.³⁸ With regard to protecting old-growth forests, one of the top U.S. homebuilders, Kaufman and Broad, agreed to implement a wood purchasing policy that would help protect old-growth forests.³⁹ Similarly, Home Depot was the first retailer in the United States to adopt independent certification standards to guarantee that lumber does not come from endangered areas. With this in mind, Gene Ormond of Home Depot remarked: “Canada has one of the most progressive environmental standards for harvesting. It is counterproductive to limit trade with a partner that is striving to look after the environment. This would force the increased use of supply from less conscientious sources.”⁴⁰

Finally, whether or not there are legitimate environmental concerns raised by Canadian

forestry practices, the job of U.S. policymakers is to look at the effect of trade restrictions on the U.S. environment. Canada is a sovereign country and its forest policies will ultimately be decided in Ottawa and the provincial capitals. Meanwhile, trade restrictions artificially boost the cutting of U.S. forests by blocking access to foreign lumber. Those concerned about conservation of American forestry resources should recognize that ending the SLA would reduce the currently inflated demand for timber from U.S. forests.

Conclusion

The SLA is the latest in a long line of trade restrictions on Canadian lumber. It should be the last. The SLA benefits a few lumber producers here in the United States at the expense of millions of workers in lumber-using industries—not to mention millions of American homebuyers. It should not be renewed upon its expiration in April 2001.

Trade restrictions on Canadian lumber have long been justified on the ground that they ensure a “level playing field,” but the evidence that Canadian stumpage rates provide a subsidy is dubious at best. Furthermore, allegations of Canadian subsidies ignore the U.S. government programs that benefit American lumber producers.

It is clear that trade barriers do not provide a level playing field for American lumber-using industries and consumers. Workers in the major lumber-using sectors outnumber logging and sawmill workers by better than 25 to 1. Trade restrictions, by adding an estimated \$50 to \$80 per thousand board feet to the price of lumber, drive up costs and shrink profits for lumber users. And, by adding \$800 to \$1,300 to the cost of a new home, they price hundreds of thousands of people out of the housing market, denying them the dream of homeownership.

Finally, the argument that trade restrictions are needed to protect the environment is utterly specious. The connection between trade policy and harvesting practices is far too remote for trade measures to serve as sound environ-

mental policy. While Canada would be better off—economically and environmentally—with more private ownership of forests, any missteps by Canadian policymakers are no reason to deny Americans the benefits of open markets.

Appendix: Regressions

The statistical estimates given in Table A-1 are based on the estimation of a reduced-form equation for lumber prices (i.e., an equation that relates lumber prices to shifts in the demand for

lumber, the supply of lumber, and other exogenous factors). The estimation was done using annual data for the period 1977 to 1998.

Demand shifts are captured by the growth rate of housing starts. As expected, the estimated model showed a positive impact of stronger growth of housing starts on lumber prices; the impact was statistically significant. The use of real GDP growth instead of housing starts (Table A-2) gave similar qualitative results; however, the effects of real GDP growth on lumber prices were not precisely measured. The explanatory power of the equa-

Table A-1
Determinants of the Real Price of Lumber, 1977 to 1998

Explanatory Variables	(1)	(2)	(3)	(4)
Housing starts, this year's growth rate	125 (49)	130 (46)	136 (60)	157 (58)
Housing starts, previous year's growth rate	22 (47)	20 (45)	21 (48)	.
Trade conflict (0,1) dummy, 1 for years 1986 to 1995	50 (18)	.	52 (19)	.
Trade conflict (0,1) dummy, 1 for years 1996 to 1998	60 (29)	.	61 (30)	.
Trade conflict (0,1) dummy, 1 for years 1986 to 1998	.	52 (18)	.	43 (18)
Previous year's real price of lumber	0.6 (0.2)	0.6 (0.1)	0.6 (0.2)	0.8 (0.2)
Japanese real GDP, growth rate	.	.	2 (5)	6 (5)
Intercept	77 (43)	70 (37)	60 (66)	5 (57)
Adjusted R ²	0.67	0.69	0.64	0.66

Notes: Each column shows a regression of the real price of lumber on the indicated explanatory variable. Numbers in parentheses are standard errors.

tions was substantially lower than the ones reported in Table A-1; the adjusted R² was in the range 0.51 to 0.57, compared with 0.65 to

0.70 in the regressions reported in Table A-1. On the supply side, several factors were considered. The first was changes in the pro-

Table A-2
Additional Regressions: Price and Quantity of Lumber

Explanatory Variables	(1)	(2)	(3)	(4)
Housing starts, this year's growth rate	.	.	-2 (2)	-2 (2)
Housing starts, previous year's growth rate	.	.	10 (2)	10 (2)
Real GDP, this year's growth rate	675 (541)	609 (507)	.	.
Real GDP, previous year's growth rate	-597 (502)	.	.	.
Trade conflict (0,1) dummy, 1 for years 1986 to 1995	33 (23)	.	-2.0 (0.7)	.
Trade conflict (0,1) dummy, 1 for years 1996 to 1998	42 (36)	.	-1.5 (0.9)	.
Trade conflict (0,1) dummy, 1 for years 1986 to 1998	.	32 (21)	.	-2.0 (0.6)
Previous year's real price of lumber	0.7 (0.2)	0.6 (0.2)	.	.
Previous year's real consumption growth	.	.	-0.3 (0.1)	-0.3 (0.1)
Japanese real GDP, growth rate	1 (6)	-2 (5)	0.2 (0.1)	0.2 (0.1)
Intercept	62 (63)	74 (58)	1.4 (0.8)	1.4 (0.8)
Adjusted R ²	0.51	0.57	0.76	0.78

Notes: The first two columns show a regression of the real price of lumber on the indicated explanatory variables; the last two columns are regressions of the growth rate of lumber use. Numbers in parentheses are standard errors.

ducer price index (PPI) for all commodities; as the price of inputs increases, the price of lumber should increase. In the estimation, this shift was reflected by expressing the price of lumber in real terms—that is, adjusting for changes in the PPI. In addition, the estimated model included a lagged value of the real price of lumber as an explanatory variable; depending on the specification of the model, the coefficient estimate of the lag was between 0.5 and 0.8, suggesting considerable serial correlation or persistence in shocks to real lumber prices.

Other supply shifts were considered to pick up the impact of changes in timber supplies. First, some attempts were made to reflect changes in timber harvests from federal lands. As reported by the Congressional Research Service (1993), protection of the northern spotted owl has substantially reduced timber sales from federal lands since 1991.⁴¹ However, attempts to capture this effect did not yield a significant impact on the price of lumber. Second, domestic timber supplies are affected by the sale of unprocessed timber (logs) to other countries, particularly Japan. This effect was captured by using the growth rate of Japanese real GDP as an explanatory variable. As expected, real GDP growth in Japan had a positive impact on lumber prices. Put differently, the stagnation in Japanese growth in recent years is likely to have had a moderating impact on lumber prices. The estimated impact, however, was not significant.

The impact of trade restrictions on lumber prices was measured in two ways. First, a (0,1) dummy variable was used to distinguish the period of trade protection (i.e., 1986 to 1998) from the preceding period. Second, an attempt was made to distinguish the more recent period of the SLA from the earlier forms of protection. This was done through the introduction of two dummy variables: a (0,1) dummy for the period 1986 to 1995 and another (0,1) dummy for the period 1996 to 1998. The impact of the trade restrictions on real lumber prices is estimated to be in the range of \$50 to \$60 per thousand board feet.

The first two columns of Table A-2 show that replacing housing starts with real GDP gives esti-

mates that are qualitatively similar to those given in Table A-1 but less precise. On the basis of the poorer fit of these equations, the regressions with housing starts are to be preferred.

While the focus of our work has been on the impact of trade restrictions on the real price of lumber, one can also look at the estimated impacts on the quantity of lumber used. The last two columns of Table A-2 show reduced-form regressions of the real growth of lumber usage on the same set of explanatory variables used in the price regressions. As shown, housing starts boost the use of lumber, whereas trade restrictions retard it. The results for quantity, therefore, are quite consistent with the results for price in showing how a booming economy boosts both the price and the use of lumber, while trade restrictions raise the price and lower the use.

Notes

1. U.S. imports of softwood lumber from Canada under Harmonized Tariff System items 4407.10.00, 4409.10.10, 4409.10.20, and 4409.10.90—the products subject to the current U.S.-Canada Softwood Lumber Agreement—totaled \$6.94 billion in 1999. By comparison, total U.S. imports from all countries of all semifinished and finished carbon steel products—HTS sections 7207-7217—amounted to \$7.50 billion in 1999. Import statistics were obtained from <http://www.litr.com>.

2. Under the U.S. CVD law, as well as World Trade Organization rules, a government benefit is not considered a subsidy unless it is “specific” to a particular industry or group of industries. Otherwise, generally available government services like education or roads could be considered subsidies.

3. “Certain Softwood Products from Canada,” *Federal Register* 48 (May 31, 1983): 24159 (final determination).

4. *Ibid.*

5. Specifically, Commerce decided to treat forest products as a single industry and argued that the wood products industry (lumber), as well as the pulp and paper industries, are a single industry because of vertical integration. Several commentators have pointed out that there was very little evidence to support that action. Gilbert Gagne of McGill University notes that “such reasoning is very difficult to justify, as the notion of industry definition usually calls for consideration of factors relating

- to production technologies and characteristics of market demand.” Gilbert Gagne, “The Canada-US Softwood Lumber Dispute: An Assessment after 15 Years,” *Journal of World Trade* 33, no. 1 (1999): 70. Others go further, noting that “[t]he preliminary determination by the ITA in October 1986 in the Softwood Lumber dispute illustrates the extent to which legal and economic concepts have been stretched to achieve a desired political outcome.” Michael B. Percy and Christian Yoder, *The Softwood Lumber Dispute and Canada-U.S. Trade in Natural Resources* (Halifax, Institute for Research on Public Policy, 1987), pp. xxix-xxx.
6. Quoted in Gerry Shannon, “Bring Back Free Timber Trade,” *National Post*, March 10, 2000, p. C07.
 7. Justine Hunger, “First Nations Make Pitch at Softwood Discussions,” *Vancouver Sun*, December 16, 1999, p. F1.
 8. “WCO Finds in Favor of Canada in Pre-Drilled Lumber Tariff Dispute,” *Inside U.S. Trade*, May 14, 1999.
 9. See “U.S. Official Cool to Renewal of Lumber Agreement with Canada,” *Inside U.S. Trade*, October 1, 1999; and “U.S. Clarifies Position on Lumber Trade Deal with Canada,” *Inside U.S. Trade*, October 8, 1999.
 10. Jim Kolbe and Steny Hoyer, Letter to Trade Policy Staff Committee, Office of the United States Trade Representative, April 13, 2000, p. 2, available at USTR.
 11. Lew Sichelman, “Steel Starting to Make Noise in the Home Building Industry,” *Orlando Sentinel*, March 5, 2000, p. J17.
 12. Quoted in “Canada Agrees to Reduce Exports of Softwood Lumber to U.S.,” *Detroit News*, February 17, 1996, <http://detnews.com>.
 13. Free Trade Lumber Council, “The Impact of Managed Lumber Trade on US Markets,” November 1999, Appendix graph, p. 6, available from FTLC.
 14. Steel manufacturers, who have an obvious interest in making a dent in the housing construction market, envision capturing a maximum 25 percent market share from softwood lumber producers. Sichelman.
 15. National Association of Home Builders, “Submission to the Trade Policy Staff Committee Regarding Softwood Lumber Practices in Canada and Softwood Lumber Trade between the United States and Canada,” April 13, 2000, p. 2, available at USTR.
 16. This figure was calculated at the request of the National Association of Home Builders by the Bureau of the Census. The calculation was based on Census Bureau analysis described in Howard A. Savage, “Who Could Afford to Buy a House in 1995,” *Current Housing Reports*, H121/99-1, August 1999.
 17. American Consumers for Affordable Housing, “U.S. Consumer Groups Ask Trade Representative to End, And Not Extend or Renegotiate Softwood Lumber Agreement between US and Canada When It Expires in March 2001,” Press release, April 17, 2000, <http://www.acah.org>.
 18. Christopher D. Boesen, “Submission to the Trade Policy Staff Committee Regarding Softwood Lumber Practices in Canada and Softwood Lumber Trade between the United States and Canada,” April 13, 2000, p. 1, available at USTR.
 19. Gene Ormond, Home Depot’s vice president–government relations, “Submission to the Trade Policy Staff Committee Regarding Softwood Lumber Practices in Canada and Softwood Lumber Trade between the United States and Canada,” April 13, 2000, p. 1, available at USTR.
 20. “Lumber Quotas Costly on Both Sides of the Border,” *Canada NewsWire*, April 17, 2000.
 21. “Comment from the 1999 Quota Survey,” *Random Lengths*, April 16, 1999, <http://www.randomlengths.com>.
 22. *Ibid.*
 23. National Association of Home Builders, “Submission to the Trade Policy Staff Committee Regarding Softwood Lumber Practices in Canada and Softwood Lumber Trade between the United States and Canada,” April 13, 2000, p. 5, available at USTR.
 24. David N. Wear and Karen J. Lee, “U.S. Policy and Canadian Lumber: Effects of the 1986 Memorandum of Understanding,” *Forest Science* 39, no. 4 (1993): 799–815.
 25. See Giridhar Myneni, Jeffrey H. Dorfman, and Glenn C. W. Ames, “Welfare Impacts of the Canada-U.S. Softwood Lumber Trade Dispute: Beggar Thy Consumer Trade Policy,” *Canadian Journal of Agricultural Economics* 42 (1994): 261–71.
 26. *Ibid.*
 27. *Ibid.* A study for the Institute for International Economics, on the other hand, found that the consumer loss from the 1992 CVD order was greater than the gain to the U.S. treasury, and thus that compensation was not possible even in theory. Gary Clyde Hufbauer and Kimberly Ann Elliott,

Measuring the Costs of Protection in the United States (Washington: Institute for International Economics, 1994), pp. 68–69.

28. William D. Nordhaus, “The Impact of Stumpage Charges on Prices and Trade Flows in Forest Products,” February 18, 1992, in Transcript of Proceedings before U.S. Dept. of Commerce in the Matter of Softwood Lumber Products from Canada, April 29, 1992, Public Document 475, 179 In. 12 19 181 In. 1.

29. William D. Nordhaus and Robert E. Litan, “Empirical Analysis of the Effect on Stumpage on Timber Harvesting: A British Columbia Case Study,” March 5, 1992, in Canadian Complaints Joint Case Brief Concerning Alleged Stumpage Subsidies and Preferentiality, vol. III-B, attachment III-3, April 21, 1992, p. 3.

30. Price Waterhouse Coopers, “The Forest Industry in British Columbia,” 1988, p. 3.

31. United States, “New and Full Notifications Pursuant to Article XVI:1 of the GATT 1994 and Article 25 of the Subsidies and Countervailing Measures Agreement, November 19, 1998,” <http://www.wto.org>.

32. “U.S. Governments Provide Significant Subsidies to Forest Industry,” <http://www.acah.org>.

33. “Certain Softwood Products from Canada,” *Federal Register* 57 (May 28, 1992): 22570 (final

determination).

34. Natural Resource Defense Council, “Submission to the Trade Policy Staff Committee Regarding Softwood Lumber Practices in Canada and Softwood Lumber Trade between the United States and Canada,” April 13, 2000, p. 2, available at USTR.

35. *Ibid.*, pp. 10–11.

36. Price Waterhouse Coopers.

37. Nordhaus and Litan, p. 3.

38. Kim Murphy, “U.S. Activists Swing Ax at Canada’s Timber Exports,” *Los Angeles Times*, December 8, 1998.

39. Kaufman and Broad, “Top U.S. Homebuilder Announces Initiative with Environmental Group to Protect Endangered Forests,” Press release, March 2000, www.kaufmanandbroad.com.

40. Home Depot, “Submission to the Trade Policy Staff Committee Regarding Softwood Lumber Practices in Canada and Softwood Lumber Trade between the United States and Canada,” March 31, 2000, p. 2, available at USTR.

41. Congressional Research Service, “Report for Congress on Lumber Prices,” 1993, <http://www.cnie.org/nle/for-12.html>.

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