

# A Study of the Effects of the Canada-US Softwood Lumber Agreement

The trade of softwood lumber between the United States and Canada is one of the major forest products trade flows in the world. Since 1996, exports from the four major softwood lumber producing provinces in Canada (British Columbia, Alberta, Ontario, and Quebec) into the US have been regulated by the voluntary export restraint (VER) as defined within the “Softwood Lumber Agreement between the Government of Canada and the Government of the United States of America” (SLA). The SLA allows Canadian producers to export up to 14.7 bbf of softwood lumber without export fee and imposes high export fees on volumes exceeding the limit. The SLA is a temporary resolution of the trade dispute between the two countries that has lasted for more than fifteen years and it is set to expire on March 31<sup>st</sup>, 2001.

The objective of this study was to determine if the expected effects of the SLA on the US softwood lumber market during the period 1996-1999 have actually occurred. The study discussed four possible direct effects and five possible indirect effects that the SLA might have had on the US softwood lumber market. The study also provides a discussion of the alternative solutions that might be implemented upon the expiration of the SLA on March 31st, 2001 and a discussion of desirability/undesirability of the SLA based upon future softwood resource availability in the US.

## Direct Effects

Since the implementation of the SLA, softwood lumber exports from the four major provinces into the US have been restricted below the volume imported before the implementation of the SLA in 1995. While the two fixed bases (the “established base” without export fee, and the “lower fee base” with a \$50/mbf export fee) were mostly filled, the exported volume under the “upper fee base,” with a \$100/mbf export fee, appeared to fluctuate in response to price changes in the US. In spite of the shift of softwood lumber production from western to eastern Canada, the composition of exported volume among the four major provinces has been consistent.

An analysis of the price data shows that the SLA has increased the price of softwood lumber products in the US relative to Canada, Figure 1. A comparison of the price trends of identical softwood lumber products (i.e., eastern SPF 2x4s, KD, #1&2) in two closely located markets (i.e., Toronto and Boston) demonstrates this two-tiered price structure. The price trends show that since the implementation of the SLA, the price for softwood lumber in Boston has been nearly 15% higher than the identical product sold in Toronto. However, there was virtually no difference in the price of softwood lumber in these two markets during the period leading up to the implementation of the SLA (August 1994 – March 1996).

Despite the relative price increase in the US, softwood lumber consumption in the US has substantially increased throughout the period due to strong economic growth. Domestic softwood lumber production has also increased slightly faster than consumption during the implementation of the SLA. As a result, the market share of imported softwood lumber declined from 36.4% of total US softwood lumber consumption in 1995 to 35.2% in 1999.

## Indirect Effects

In addition to the direct effects that the SLA has had on the softwood lumber market in the US, it has also had several indirect, and unintended, effects as well. Strong demand for softwood lumber in the US, coupled with restricted exports from the four major provinces in Canada, provided other foreign suppliers with an opportunity to enter and compete in the US market, Figure 2. While softwood lumber exports from the four major provinces have been relatively stable, the SLA-exempt provinces (New Brunswick, Nova Scotia, Saskatchewan, and Manitoba) took advantage of their position to increase their softwood lumber exports into the US from 1.4 bbf during the first year of the SLA to 2.9 bbf during the fourth year. As a result, the share of the SLA-exempt provinces in total Canadian softwood lumber exports to the US jumped from 7.9% during the first year of the SLA to 15.6% during the fourth year. Similarly, exports

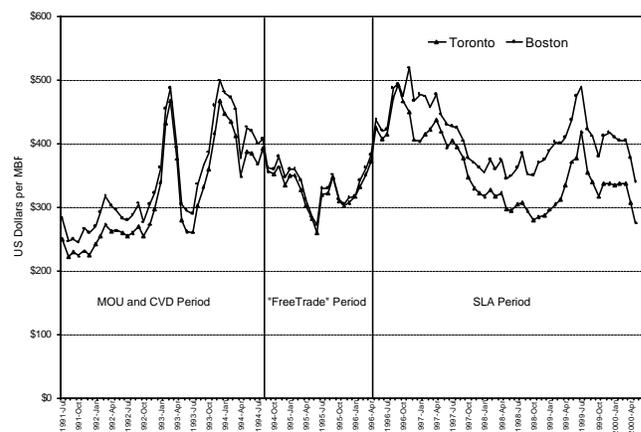
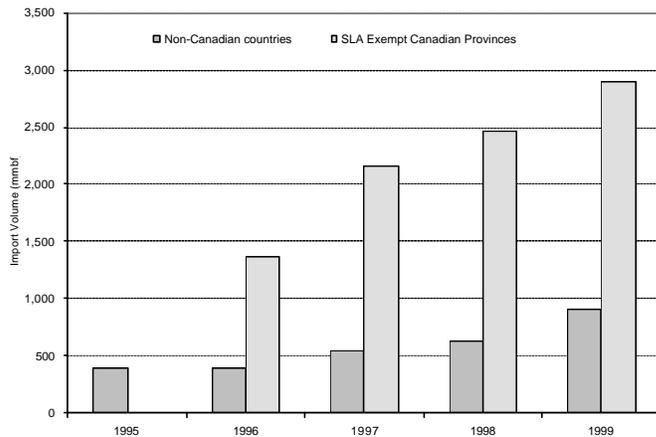


Figure 1. Trade restrictions have led to price differences for the same products in the US and Canada.



**Figure 2.** The SLA has contributed to increased lumber imports from non-Canadian countries and well as from the SLA exempt Canadian provinces.

From non-Canadian countries have jumped from 389 mmbf to 912 mmbf during the same period. As a result, the share of other countries in US softwood lumber imports has increased from 2.3% to 4.8%, Figure 2.

To avoid the voluntary export restrictions specified in the SLA, some Canadian producers seemed to have responded to the SLA by increasing their exports of softwood logs and value-added wood products to the US. US imports of softwood logs from Canada have increased substantially since the implementation of the SLA, increasing from 63 mmbf in 1995 to almost 467 mmbf in 1999. In addition, imports of value-added wood products, such as windows, doors, and roof trusses, have

also increased dramatically, although this increase can be partly attributed to the strong US housing market.

In addition, some Canadian producers have attempted to have their lumber products reclassified as remanufactured lumber products by making slight product modifications, since remanufactured lumber products are exempt from the export permit requirement under the SLA. The main product modifications have been to pre-drill, notch, or rougher-head the studs. As a result, exports of products under HS code 4418.90 (builders' joinery and carpentry of wood), which include these modified studs, increased substantially. However, these products are generally used as ordinary studs after trimming or planing the modified parts. The US Coalition for Fair Lumber Imports has appealed the classification of these products to the US Customs Office as an illegal attempt to circumvent the SLA. While the appeals by the CFLI were successful in having rougher-headed studs reclassified as softwood lumber, the other appeals are still being considered at this time.

Finally, by increasing the price and price volatility of softwood lumber in the US, the SLA may have contributed to the ongoing process of substitution of softwood lumber by wood and non-wood alternative materials. However, the extent to which the SLA has contributed to the process of material substitution is difficult to evaluate.

#### **Future Prospects for the US-Canada Softwood Lumber Trade**

There are four possible options that might be implemented at the expiration of the SLA on March 31<sup>st</sup>, 2001. These options include: 1) an extension of the current agreement, 2) the imposition of a countervailing duty by the US, 3) "fair trade" with major changes in the stumpage pricing system employed in Canada, or 4) "free trade" and the elimination of the SLA. Recent events in both Canada (with regards to the recent lowering of stumpage prices in BC) and the US (with regards to the position of the CFLI) suggest that the implementation of options 3) and 4) are unlikely. Given the current political situation in both countries, with presidential elections occurring in early November 2000 in the US and national elections occurring in late November in Canada, it is possible that the two governments might decide to extend the SLA for a short period of time. However, the CFLI insists that it will seek some type of countervailing action if Canada fails to address the stumpage price issue appropriately following the expiration of the SLA. Given the inequities that some Canadian lumber manufacturers perceive with the existing SLA, it is likely that at least some producers in Canada would prefer to see the SLA expire and be replaced with a countervailing duty, since this would impose no limit on the volume of softwood lumber that they could export to the US. Considering the restrained domestic timber supply and the uncertain future availability of Canadian softwood lumber, it is important for the US to build a cooperative relationship with Canada in order to provide secure softwood lumber supply.

*An Overview of the Effects of the Canada-US Softwood Lumber Agreement* is available from CINTRAFOR as Working Paper 80.