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Discussion Following the Remarks of Mr. Hufbauer and Mr. Burney

Discussion

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DISCUSSION FOLLOWING THE REMARKS OF MR. HUFBAUER AND MR. BURNEY

MR. McILROY: That brings us to our question and answer session and I see Dick Cunningham is frothing at the bit to ask the first question.

MR. CUNNINGHAM: While it is true that finding a way to resolve these disputes without litigation would probably cost me some income, I am more bedeviled like Naitches Heroes with the doctor of internal recurrence, which is certainly exemplified by softwood lumber. If things go the way they are likely to go, they would be exemplified by wheat. I have a suggestion for you to think about. There is going to be an effort by the United States to mend fences. It is now conceived as largely a U.S./Europe effort to mend fences. That effort to mend fences will not just be devoted to the geo-political issues, but will also extend to what has become quite serious set of roust between U.S. and Europe and may go more serious if we go against them with the GM Foods, which we are now threatening to do.

I would suggest, there is opportunity for Canada here because it is perfectly not only reasonable, but true, which is not always the same thing for Canada to say to the United States. It would be an appalling thing for the U.S. to do a reconciliation with Europe without including Canada in the game. To put it more on a quad basis, or something like that, so there is an effort not just to resolve things like Bisk and all of the other things that are going on between the steel and between the U.S. and Europe, but to have the same sorts of disputes looked at between the U.S. and Canada.

I think where that goes, is somewhere like what Gary is saying. I think it goes to finding some mechanism to deal with the extraordinary case between the U.S. and Canada. When you get something so political in the United States as softwood lumber or wheat or in the U.S. global standpoint as steel, they get onerous, politically driven solutions, which I call trade remedies. What you need is some sort of escape valve, some sort of mechanism whereby it would be agreed between the United States and Canada that in such a case the two governments will work together to do some sort of compromise, in advance, not after the case has become locked into the litigation process. Something where the governments have the out of saying there are prescribed paths for dealing with this. We will follow through with those paths even though what they are doing is a Dance Macabre and the paths do not really resolve the issue.

I would pose that to my Canadian friends and colleagues here as there is an opportunity, a time of opportunity here to try to get something like that and that is the sort of thing you want to be striving for.

MR. BURNEY: I guess I worry fundamentally when I hear the lawyers say this requires a political solution. After 45 million dollars worth of legal expenses, is that right? Hey, I mean that is nirvana. If you could get a political consensus between the Canadian and U.S. governments that says in the future we are going to stop these types of problems before they emerge because they would be very damaging to our mutual interest. That is nirvana. I think the officials, the lawyers would stand up and salute.

I just do not think it is a very practical possibility, especially if there is no chemistry at the top, or at the level of Ministers to get that kind of consensus. I am not saying it could not happen. I do not care how we do it, but I do not think we can start forging new avenues of cooperation unless we fix it, because it is a problem. I think it is sapping enthusiasm in some key constituencies in Canada. I think it would be extremely embarrassing for a Canadian political leader to embark on a new chapter and halfway along have the back tire of his car shot out by Mr. Wolf and his friends.

The only other comment I would like to make, is going back to Washington. The Canadian CEOs were asking just how big the hole in the fence was, because of our differences over Iraq. We got an answer, but the guy was very hesitant. He was a Brit representing Time Magazine. He said, "I have to be very careful with this answer, what I have to tell you is that with France out front, not too many have noticed where you are on this one."

I do not want to give offense to Canadians by saying that, but the reality is our different positions on Iraq has not resonated as loudly in the United States as the booing of the American National Anthem and the booing of a pee wee hockey team in Quebec City. That got more of a reaction in our Embassy in Washington according to the Embassy than our subtle differences in our position on Iraq.

So you are probably right. The administration will be inclined to mend fences in Europe. It is an ally who probably has more of a necessity in the short term. I did not get a lot of flavor of fence mending in Washington on Monday and Tuesday. I think we have to live with a state of euphoria for awhile before they recognize that.

If I could bootleg the chairman about a comment I really wanted to say in the first discussion. You heard manifestations of the Canadian obsession with multilateralism. I want to remind some of my Canadian friends that our obsession with multilateralism should never be seen as an abstract. One of the fundamental objectives of Canadian foreign policies since time memorial, is to keep the United States engaged and committed to the multilateral system. It is in that sense, extremely important for Canada to have an audience of trust and confidence in Washington, because if the Americans want to listen to anybody about the value of multilateral, it needs be the Canadians.

It is very important that we work at keeping the United States engaged in the multilateral system and not adopt the multilateral system as some sort of salvation in and of itself. Because the multilateralism system, with a reluctant or somewhat cheery United States is not very much in Canada's interest, so make the distinction between multilateralism in the abstract and multilateralism that involves and gets a major commitment from the United States.

MR. CLELAND: Mike Cleland, Canadian Gas Association. My question is directed to Gary. You talked about the focus on energy as part of this. I think that is something that is welcome in that it brings energy back into focus. The idea of a cooperative North America is also welcome.

Language has to be treated carefully in Canada. It is one of the areas that is particularly sensitive. A North American energy plan has everyone scurrying for the exits. Nonetheless, it is something you should be doing. As Stephen Flynn might have said, energy security is also an away game. Not only is about 50 percent of our oil imported from across the world, as we look forward over the next two decades, we are going to see an increasing part of our natural gas coming from other parts of the world that are not all that healthy and all that friendly. It does strike me that we do need international multilateral institutions, maybe not the I.A. The I.A. may well be obsolete. Certainly, its core mechanism for oil sharing has been obsolete for well over 20 years, but it has been stuck in institutional inertia.

Getting to my question, I am wondering if you have any reflections on where we might go with respect to international institutions on the energy side?

MR. HUFBAUER: I think unless the U.S. can forge a stronger corporation with Canada, where there is already a tremendous market, there are problems on hydroelectric where we are beginning to talk about excluding large megawatt hydropower from some definition of green energy and little things like that. Then there are some big pipeline issues.

Unless we can deal with that with Canada and begin to make some progress with Mexico, I tend to be less optimistic about broader international energy or multilateral with the other big users, namely Europe and Japan and China. There is so little commonality of interest. When you see this kind of race and so fourth with our different companies, it does sort of boggle the mind. I think maybe there is some sort of reinvention of the IEA, which might work in extreme cases maybe some building up of inventories.

I think the price the U.S. would have to pay for that is exactly what Derek said on some alternative to Kyoto or some greenhouse gas. If we cannot work it out with Canada and begin to do something in North America, I am skeptical that we can do it on a larger field.

MR. KING: I had two questions. One for Gary and one for Derek.

On this non-voting observer in the ITC, I would like to have you amplify the rule of the observer. Would s/he sit on in on the deliberations, the committee, and would they have a vote? It is an unusual setup. You might want to comment on that.

At the same time, I applaud some of the initiatives that Derek has suggested. It is all going to be a problem with the U.S. and what is in it for us. You have got a sales problem there. I wondered how you would approach that?

MR. HUFBAUER: The problem with doing anything on institutions is if you do something very big, the immediate reaction is that it is too big and we cannot take it on. If you do something rather modest, like the suggestion that I have tabled here, then the argument tends to be, "Oh, we do that anyway." That is what I heard from the bank of Canada. We do that anyway. We get all this information and so forth. It is a process we are following. There is a lot of cooperation between central banks.

It is exactly what you referenced, Henry, they do not do it anyway. They do not sit there when the ITC deliberates on these cases and decides these difficult injury determinations. They do at the Department of Commerce in terms of I think we have a lot of determinations on dumping duties and so forth, but they do not sit there in those deliberations, where, in fact it is an open issue. They read the register and can find out after the fact and probably very quickly after the fact.

I think that is where you want a sitting participant. I mean sit there and make a comment. Of course, each government is not going to send someone who is kind of noisy and loud. The person is probably going to behave like the Chinese Executive Director at the World Bank, who hardly said anything for the first several years. Developed a lot of respect for China in that decision. I think that is in practice how it would work and begin to build up this level of confidence where we hopefully could go towards some level of greater harmonization.

MR. BURNEY: I think, Henry, the sales job, as you put it, is a big challenge. It always is for Canada with the United States. What I was suggesting is that if Canada were to come up with a concrete proposal on physical security that went well beyond the smart border initiative, which with all due respect, is good housekeeping that was intended to get the border back to where it was; as opposed to charting something new. If that was accompanied by an increase in defense spending, specific funds targeted to improve our capability to protect our own shores, which is now very limited when we only have one helicopter that can fly these days. I do not underestimate the challenge, but I think the priority in Washington is going to be security. I think you have to appeal to that in order to get their attention. I think we might have a better chance of getting their attention on that

because of our European friends. The U.S. concern is about homeland security. I think we have to play our cards accordingly.

The quid pro quo has to be a range of economic issues which probably, on a plus minus adding machine, would balance out more in Canada's favor, but I would hope that the United States would see merit in some of the tidying up in terms of standards, regulations. I think the United States might see the advantage of moving towards a common external tariff, if not all the way, to a custom's union. Get it down to a manageable few so we can reduce unnecessary paperwork at the border. If we embarked on this in a twin pincher movement, I think we could get the attention of some key players. The energy point, I did not put it forth, because I see it necessarily in that order. It is a very delicate issue in Canada as the representative of the gas association mentioned. The acronym NAP is not something we want to hear in the context of North American energy.

We know this is an area of concern in the United States. We know it is a particular area of concern of the Vice President of the United States. If we were looking for a champion and we had an agenda that addressed both physical security and economic with energy as a component, it is conceivable that we could get the interest of the Vice President, if not the President, on such a package.

I remember when we were negotiating the Free Trade Agreement, one of the remarks we made to the then Secretary Baker in the Treasury Department was that here you guys are negotiating an arms control agreement with the Soviet Union, and you cannot conclude a Free Trade Agreement with your neighbor. Even then it was difficult to get attention in Washington. The thing that bedeviled the Free Trade Agreement was that it was not seen as a major initiative in the United States. It was seen as what we call scalp hunting; looking to resolve a variety of disputes with Canada.

In the end, they did see the merit. The merit of that one was more strategic in the global sense than in the bilateral sense. It is conceivable that by making strides with Canada on physical security, that could lend itself to a global objective that the United States has. As Gary properly said, our interests may not be identical. The United States may have a different agenda in terms of global security than that of Canada, but I sure hope we do not have a different agenda than security in North America.

MR. ROSEGER: Gary Rosegger from Case Western Reserve. I have a question for Dr. Hufbauer. It seems to me that with high priority given to security and for good reasons, there is, perhaps, a risk that homeland security and other securities might become another rationale for protectionist measures. Sooner or later, lobbies will catch onto security as an additional vehicle to national health and to national defense. We have worried about civil liberties. I think this is another thing we ought to worry about.

MR. HUFBAUER: Absolutely. You can undo everything that has been done in the last two trade rounds and all the preferential agreements. I think it is very easy to put the tariff equivalent. The econometrics are pretty sophisticated these days. It is easy to get the tariff equivalent of six to eight percent equivalent through security, which is mindless, not following the Stephen Flynn model, but some other level one model and undo everything.

The biggest challenge is with Canada. If we cannot achieve it with Canada, I ask how can we achieve it with China. If you want protection against Chinese textiles and apparel, if you cannot get it through rules of origin, that is a good place to start right now. You cannot get to it by sanitary measures on textiles and apparel. You cannot work the labor angle, which the protectionists are trying to do. Security would be a very good winner at the end of the day.

MR. BURNEY: Absolutely.

MR. MCILROY: It is the new MTV. We have other question.

MS. VERDUM: Emmy Verdum Department of Finance in Ottawa. My question is very similar to Henry King's question when he talked about what is in it for the U.S. I will flip it around a little bit. I would like comments from both Mr. Burney and Dr. Hufbauer on this.

One of the things that you talked about earlier was the power imbalance. You talked about common currency, but realistically, everyone knows that Canada would accept the U.S. dollar. That is really the basis of my question.

How can we get into a negotiation or discussion that is not entirely one-sided with Canada accepting U.S. trade remedies, U.S. regulations, U.S. tariffs and so on? It is both a concern of the ordinary Canadian and also is a realistic issue that we in Canada need to face going into negotiations with a more powerful country which is very strongly weighted to its current trade laws.

I would like your comments on that. You have given sort of an element of the answer in terms of talking about defense as one of the things that Canada can for its own purposes and to get U.S. support, but on the table as a positive contribution. I welcome your comments on this and how big of an issue of you see it being.

MR. BURNEY: I did say that a common currency was not in the cards, as far as I was concerned. I do not know what more I can say about it than that. I think that would be a bridge too far. I cannot really say much more about getting American attention, other than what I have said. I think they have concern about security. I think there are more things Canada can do in its own interest and bilateral interest to get the attention of the United States.

As to the perennial, as to whether a little guy can negotiate with a big guy and come out with a fair deal, I would only point you to the two existing agreements that are there. If you think that Canada was not successful in

getting mutually beneficial results out of the FTA and NAFTA, then I am not likely to be able to persuade you we can do it again.

The objective in the negotiations is not for one side to win and the other side to lose. The objective, fundamentally, is to have both sides come away with not their maximal demands, but rather with objectives being realized that serve their interest to the best extent possible. I think history of success with the two previous negotiations we had on the economic front demonstrate that both Canada and Mexico in dealing with the elephant in the middle have proven that you can negotiate successfully and get the benefits that are good for smaller countries as well as the big. Inevitably, the psychology of that kind of negotiation will be very difficult for Canadian politicians, which is why I said Canadian politicians are reluctant to take on any major initiatives with the United States. It is automatically perceived, as you had suggested, as our side being the underdog and inevitably having to accept the U.S. view of things. That is not what history would tell you, but that is certainly what five-year olds would tell you.

MR. HUFBAUER: It is a problem. Just parenthetically, I agree with what Derek has said about the common currency, about the U.S. and Canada. I do not think that is going to happen any time soon. The U.S. and Mexico are much more likely to do this because Mexico has such a history of poor currency management, which is reflected in very high risk premiums and very high interest rates for credit cards, small business, etc. So, for Mexico, the reputational advantage of linking with the dollar in a tighter way has a big pay off, but Canada does not have that very good currency reputation, so there is not anywhere near the payoff.

Enough on that. In other areas, where it tends to be more in the weeds, if I can put it that way, is where the U.S. power on the issue area has been delegated to a department or to one of these boards, one of these commissions. There is more room to make progress if there is direction from the top to make progress without running into the imbalance.

I will just take two examples. In the food safety area, this is all delegated power to the Department of Agriculture and to a lesser extent, the Food and Drug Administration. On food safety, the fact of different fido sanitary regulations on say meat or vegetables is ridiculous. If the Prime Minister and President said harmonize and here is a list of the areas you are going to come to and we are going to come to an agreed inspection and mutual recognition and so forth of the inspection process that could not happen without any blow back, at least between the U.S. and Canada. It cannot happen with Mexico. There have been too many articles about poor sanitary conditions in packaging plants that need to be quickly overcome.

Another area is the accounting rules. The U.S. is a lot less prideful of its accounting systems. When Larry Summers said, "that is one of our great national assets," a few years ago, he ended up having to correct his

statement. Yeah, we are property humble now about our accounting system. That was a good time for Canada to move in terms of Canada in doing something that makes sense for companies both in Canada and the U.S. I think you can also be extended to the markets, the regulations of financial markets, the Toronto Stock Exchange, the NASDAQ and so forth. We are in a period of kind of change of an evolution.

MR. McILROY: I, unfortunately, am going on have to bring this panel to a close. I understand I am in the delicate position between you and your lunch. I would just like to pause for a moment and thank both of these speakers for providing very provocative comments from where we go from here. Thank you very much.