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STATE OF THE U.S. FOREST PRODUCTS INDUSTRY

HEARING

BEFORE THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

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FIRST SESSION

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STATE OF THE U.S. FOREST PRODUCTS INDUSTRY

THURSDAY, SEPTEMBER 19, 1985

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The committee met, pursuant to notice, at 2:06 p.m., in room SD-215, Dirksen Senate Office Building, the Honorable Robert Packwood (chairman) presiding.

Present: Senators Packwood, Symms, Grassley, Baucus, and Mitchell.

[The press release announcing the hearing and the prepared statements of Senators Baucus and Mitchell follow:]

[Press Release No 85-073, Sept 11, 1985]

FINANCE COMMITTEE SETS HEARING ON THE STATE OF THE U.S. FOREST-PRODUCTS INDUSTRY

Senator Bob Packwood (R-Oregon), Chairman of the Senate Committee on Finance, announced today the scheduling of a hearing on international competitive challenges facing the U.S. forest products industry.

The hearing is scheduled to begin at 2 p.m., Thursday, September 19, 1985, in Room SD-215 of the Dirksen Senate Office Building. Senator Packwood will preside.

The hearing will address 4 principal issues:

1. Canadian softwood exports to the United States;
2. The potential Japanese market for U.S. forest product exports; and
3. Customs enforcement of U.S. laws dealing with forest product imports.
4. Other competitiveness problems facing the forest products industry.

STATEMENT BY SENATOR MAX BAUCUS
TRADE POLICY AND THE U.S. FOREST PRODUCTS INDUSTRY
SENATE FINANCE COMMITTEE
September 19, 1985

The Trade Crisis

As every member of this Committee knows, America faces a trade crisis. We're inhaling goods and currency from around the world. Last year, the trade deficit was $123 billion. During the first half of this year, it was even worse. For every $2 worth of U.S. goods going out, $3 worth of foreign goods were coming in, and the 6-month trade deficit was $70 billion.

As a result, millions of U.S. workers have lost their jobs. And U.S. industries are losing their footholds in export markets and drowning in a flood of imports here at home. These are not just declining "sunset" industries that no longer can compete. They also include some of our most efficient and competitive industries.

The Forest Products Industry

The U.S. forest products industry is a perfect example.

Our industry is the most competitive in the world. We have a huge resource base, and our mills are the most efficient anywhere. That's why the Office of Technology Assesment recently said that "The United States is well positioned to satisfy ... a major share of future world forest products requirements."

U.S. sawmill workers have made great sacrifices to maintain our competitive edge. In fact, our workers allowed their wages to be frozen during 1981 and 1982 so that their mills could survive the recession.

Nevertheless, the industry has become a victim of the international trade war. Since 1980, the industry has gone from a $400 million trade surplus to a $2 billion trade deficit. Last year, exports declined 5% and imports rose 10%.

This has had a devastating effect on the industry. Although softwood lumber consumption reached an all-time high level of 43 billion board feet in 1984, U.S. sawmills are operating at only 83% of capacity. Last year, U.S. companies reported pre-tax losses of $550 million. Since 1978, 250 sawmills have closed and 30,000 U.S. lumber industry workers have lost their jobs.

The overvalued dollar contributes significantly to the problem, by making imports cheap and exports expensive.

But unfair foreign trade practices also contribute significantly to the problem. Now, I recognize that we must be skeptical about charges of unfair foreign trade practices. Sometimes, such charges are made as a smokescreen to protect U.S. industries from competitors who are simply more efficient than they. But in the case of the U.S. forest products industry, the charge is right on target. On one hand, the U.S. industry has been shut out of the huge Japanese market by a system of high tariffs that protect inefficient Japanese mills. On the other hand, the U.S. industry has been inundated by Canadian imports that benefit from massive government subsidies.

Japan's Value-Added Strategy

In 1816, a Yankee sea captain named O'Cain tried to sell American products in Japan, but failed. "They told us," one of O'Cain's sailors wrote, "that they had plenty of everything we had to offer."

Since O'Cain's voyage, Japan has transformed itself from an isolated feudal kingdom into the free world's second-leading economic power, with a higher projected growth rate than any other industrial nation. This transformation was made possible by the open post-war trading system, which permitted Japan to import cheap raw materials and then sell its manufactured goods worldwide, especially in the United States. In fact, it's no exaggeration to say that the open trading system has benefitted Japan more than any other nation.

But some things haven't changed. Today, Japan defends its home market as stubbornly as it did in 1816. As a result, last year Japan sold us about $37 billion more worth of manufactured goods then we sold them.

The Japanese have attained this huge surplus, in part, by successfully employing a value-added strategy, by which Japan encourages imports of raw materials and discourages imports of finished products produced from those raw materials. As a result, most of the lucrative value-added processing occurs in Japan.

This value-added strategy has been especially effective regarding forest products. Japan imposes few barriers against imports of logs, but imposes many formidable barriers against imports of processed forest products. As a result, many jobs that might be in Missoula, Montana, or Bend, Oregon, are carefully protected in Sapporo or Osaka, Japan, even though U.S. workers are more than twice as productive as their Japanese counterparts.

Let me explain the problem more fully. The U.S. forest products industry is very conscious of the potential value of foreign markets, and is exporting aggressively to them. For example, U.S. exports of processed forest products increased from about 3.5 percent of total U.S. production in 1970 to more than 9 percent of total U.S. production in the early 1980's.

Many of our forest products exports are produced from softwoods like Douglas fir, ponderosa pine, lodgepole pine, and spruce, which are cut, milled, and processed throughout the Northwest. For example, western Montana is a competitive producer of softwood lumber, plywood, particleboard, and kraft-linerboard, all of which have significant existing or potential export markets.

Because it has so few harvestable forests, Japan depends heavily on forest products imports. The United States is Japan's main import supplier, and Japan is our main export customer. In 1983, we exported $1.1 billion worth of forest products to Japan; in other recent years, we have exported almost $2 billion worth.

The Japanese market is especially attractive because of Japan's active homebuilding industry. In fact, in some recent years, the number of housing starts in Japan has actually exceeded the number here. What's more, Japanese builders are beginning to use softwoods in much greater amounts than ever before, and overall Japanese construction methods are changing in ways that make the Japanese market more attractive to U.S. producers. American standards have been adopted for certain products, and the U.S. platform-frame construction method has been copied. Although this type of construction now accounts for less than 2 percent of home construction, it is expected to account for as much as 20 percent by 1990.

To capitalize on this market, American forest products companies have been working hard to sell in Japan. They've opened Tokyo offices. They've learned the language. And they've changed some of their manufacturing standards, by doing things like adding a special tint to the color of kraft linerboard (which has been done by a company in Missoula, Montana).

But, so far, Japan's high tariffs on processed forest products have prevented U.S. producers from fully participating in this substantial market. The following chart illustrates the effect Japan's tariffs have in protecting the Japanese domestic industry:

Product	Tariff	Imports as a percent of total Japanese consumption (1980)
Softwood logs	0	50
Softwood Lumber (pine & spruce/fir only) .	6-9	14
Particleboard	12	7
Plywood	15	1
Veneer	15	2
Laminated Lumber	20	*

*Less than 1 percent

Japan's high tariffs on processed forest products contrast starkly with other developed countries' tariffs. For example, America's tariffs on veneer, particleboard, and the type of plywood used in Japan range from 0 to 8 percent; the European Community's range from 0 to 10 percent. Even some less-developed Asian countries, like Taiwan, have lower tariffs on processed forest products than Japan does. In addition, Japan uses a web of non-tariff barriers, like unnecessarily complicated licensing and certification systems, to bog U.S. producers down.

Japan's protectionist value-added strategy, embodied in these high tariffs and these non-tariff barriers, is inconsistent with Japan's purported commitment to free trade. What's more, it denies the American forest products industry about $1 billion a year in potential sales. Granted, that is only a small part of our overall trade deficit. But, to the forest products industry and the workers in Montana and elsewhere who depend on it for their livelihood, it is a very significant amount.

Negotiations

For years, the U.S. Government has been urging Japan to reduce its tariffs on processed forest products, but the Japanese have refused to make significant concessions.

In January, President Reagan met with Prime Minister Nakasone, who pledged that Japan would make "further market opening efforts," especially in the key sectors of forest products, telecommunications equipment, medical equipment and pharmaceuticals, and electronics. At the time, many of us thought that this agreement was a big step forward.

We were wrong. The promised forest products concessions have not materialized. Instead, the Japanese have continued dragging their feet. At first, they refused to even consider making tariff concessions. Eventually they agreed to "positively consider" unspecified tariff reductions, but not until 1987.

This sends a negative signal at a dangerous time. A Japanese proverb says that "the sack of a man's patience is tied with a slip knot." Well, American patience is running out. Indeed, we are on the brink of a trade war. The Administration argues that we should forego retaliation against Japan, relying instead on continued negotiations to steadily open the Japanese market. But if the Japanese refuse to honor their specific January commitment to open their market to American processed forest products, we have little reason to believe that they will make the broad concessions necessary to make overall U.S.-Japanese trade truly a two-way street.

It's time to set a deadline. Unless the Japanese honor their January committment and announce a satisfactory package of forest products concessions within a reasonable period of time, we should retaliate, by restricting a like amount of Japanese imports into the U.S. I plan to offer legislation accomplishing this, either independently or as an amendment to the Finance Committee's retaliation bill, S. 1404, when it comes to the Senate floor.

I don't want to ignite a trade war with Japan. But, as Thomas Jefferson said, "Free commerce is not to be given for restrictions and vexations." We have given Japan free commerce. Japan has responded with restrictions and vexations. It's time for some reciprocity.

Canadian Subsidies

Let me turn from the Far East to the Far North, to Canada.

Canada, not Japan, is our major trading partner. Last year, our two countries traded $120 billion worth of goods, and Canada ran a $20 bilateral trade surplus with us -- which was significantly larger, on a per capita basis, than Japan's bilateral surplus.

One of Canada's major exports to the U.S. is softwood lumber. During the past decade, Canadian lumber production has almost doubled, from 11 to 21 billion board feet. U.S. imports of Canadian lumber have risen much faster than U.S. consumption: in 1975, Canadian imports comprised 19% of U.S. consumption; now, they comprise 33%. Canadian imports have penetrated all regions of the country, capturing 63% of the Northeast market, 58.5% of the Southern market, and about 40% of the Montana market.

In Canada, about 95% of the cut timber comes from government-owned land, compared to only about 28% in the U.S. When timber is harvested from private land, the price for "stumpage" (cutting rights) is, by definition, the market price. When timber is harvested on public land, the stumpage price must be set, to some extent, by the government. However, the Canadian and U.S. systems differ significantly. In both countries, the administering government agency begins by establishing an "appraisal value" for stumpage, working back from the current market price and deducting an allowance for costs and a reasonable profit. In Canada, the process ends there: the long-term lessor pays the appraised price. In the U.S., in contrast, cutting rights are then put up for competitive bid, resulting in an actual price that usually is much higher than the appraised price; given the competitive bidding process, this actual price constitutes a true market price.

The dramatic effect of these two different systems can be seen by comparing stumpage costs. U.S. market-level stumpage prices have been consistently higher than comparable Canadian prices, and now are between twice (Kootenai/Nelson) and five times (White Mountain/Quebec) as high.

The Canadians argue that that the increase in Canadian imports is caused primarily by the high value of the U.S. dollar, which rose by 21% against the Canadian dollar from 1975 to 1984. Certainly the high value of the dollar has caused part of the increase. However, it hasn't caused all of it. The Canadian's dollar argument is undercut by two facts: First, increased Canadian logging costs have more than offset the impact of the dollar; that is, Canadian logging costs have increased more than the Canadian dollar has declined; this should have been reflected in a falling Canadian market share. Second, since the beginning of this year, the value of the U.S. dollar has fallen, but Canadian imports have increased by 13%.

The Canadians also argue that Canadian cost advantages are important causes of increased Canadian imports. However, the U.S. industry probably has more cost advantages than the Canadian industry:

--The Canadian industry has higher logging costs than the U.S. industry. Rougher terrain and an unforgiving climate are two factors contributing to the difference. In addition, because Canadian forests are farther from the mills, longer roads must be constructed. Finally, the Canadians harvest more wood with a low log-to-lumber conversion rate.

--The Canadian industry does not practice as careful silvicultural practices as the American industry does. In fact, the Canadians are "strip-mining" B.C.'s forests and abandoning costly long-term reforestation efforts for short-term profits and employment.

--The U.S. industry's labor costs are lower than the Canadian industry's, $8.22 per hour for U.S. sawmill workers compared to $14.97 per hour for Canadian sawmill workers.

--Transportation costs are comparable. The Canadian industry benefits from lower freight rates, the U.S. industry from shorter distances to market.

The Legal Background

In late 1981, the Senate Finance Committee directed the International Trade Commission to conduct a study of Canadian softwood lumber imports. After an extensive investigation, the ITC reported that "major competitive conditions [between the U.S. and Canadian industries] differ primarily because of factors controlling the raw material supply" and that the Canadian raw material supply was available for between one-sixth and one-half the comparable U.S. price.

Shortly after the ITC report was released, a coalition of U.S. sawmills filed a petition alleging that "by providing stumpage for less than its market value, the Canadian government has assumed a raw material cost of producing softwood products and has provided a countervailable subsidy...."

The Commerce Department rejected the Coalition's petition. The linchpin to this decision was the legal holding that domestic subsidies were not illegal if they were "generally avialable" throughout the subsidizing country's economy and that Canadian stumpage programs were generally available because they were provided not only to the lumber industry but also to the furniture and other wood products industries.

Since that time, one court has questioned whether--as the Commerce Department assumed--there is such a "general availability" requirement implicit in our countervailing duty law. Even if there is, it seems absurd to interpret it as broadly as Commerce did, permitting availibility to a few related industries to constitute general availability. As trade law expert Gary Hufbauer says in his recent treatise on subsidies, "The general availability standard should be used sparingly to excuse only those incentives that in practice and design are used by a broad range of industries and geographic areas. Otherwise, the international community risks taking countermeasures against little subsidies while big subsidies run free."

Possible Solutions

Since the Commerce Department's decision, canadian imports have continued to rise and the U.S. industry has continued to shrivel. As a result, we're forced to witness the spectacle of an inefficient, high wage foreign competitor using bargain-basement government resources to drive American producers out of their own market. And doing so immune from our trade laws.

One way to address the problem is through negotiations. In February, the U.S. and Canadians began bilateral negotiations over forest products trade issues, including the stumpage issue. I hope the negotiations result in a satisfactory modification of Canada's pernicious subsidies.

If they don't, the axe must fall. We must revise our trade laws to outlaw practices like Canada's stumpage subsidy. Otherwise, American companies, and workers, will lose all confidence in the international trade law regime, and insist on the kind of blunt protection that could plunge the world economy into a dark downward spiral.

One reasonable solution is the "natural resource subsidies" legislation introduced by Congressman Gibbons in the House and me and Senator Long in the Senate. this legislation revises our countervailing duty law to cover certain government natural resource pricing schemes --like Canada's stumpage system and Mexico's two-tier natural gas pricing system-- that enable foreign producers to drive efficient U.S. producers right out of their own market. This legislation is completely consistent with the GATT and the Subsidies Code. And it will help restore public confidence that the open trading system still works.

Conclusion

Like most members of this Committee, I used to consider myself a free trader. I guess I still do.

But now I'm a disillusioned free trader. I'm frightened by the mounting trade deficit. And frustrated by the impotence of our trade laws.

As we search for solutions, we should avoid lurching into protectionism. That would be counterproductive, just like it was in the 1930's.

Instead, we must formulate a comprehensive trade policy that restores our fundamental competitiveness and gives efficient U.S. industries like the forest products industry a fighting chance.

I look forward to working with the other members of this Committee to accomplish this task, and help make Aamerica a powerful trading nation once again.

STATEMENT OF SENATOR GEORGE J. MITCHELL

HEARING ON STATE OF THE U.S. FOREST PRODUCTS INDUSTRY

SENATE COMMITTEE OF FINANCE

SEPTEMBER 19, 1985

For several months now, this nation has been engaged in a debate over the future course of our trade policies. Unfortunatley, that debate has not always been the most productive; the issue has tended to become polarized into the policy absolutes of protectionism on the one hand and free trade on the other.

But of course, the real world is not like that. Almost every nation in the world has adopted a range of policies to manage trade in pursuit of their own self-interest. And it must be recognized that there are reasonable policy alternatives that this nation must pursue which can neither be characterized as free trade or protectionist.

The United States will run a merchandise trade deficit of somehwere around $150 billion this year resulting in scores of plant closings and millions of displaced workers. We must adopt some sort of policy response to this trade situation without being constained by the rhetoric of free trade . Otherwise the realities of a complex international trading system where industry subsidies and unfair import restrictions are commonplace will continue to get the best of U.S. industries and their workers.

The position of the U.S. forest products industry in international trade is a good example of what is occuring in the present trading system. According to the theory of comparative advantage, the U.S. industry should be highly competitive in international commerce and run trade surpluses from year to year. The softwood lumber industry should be particularly competive against Canada. We are blessed with with ample timber supplies located near major markets. Softwood lumber industry labor rates are lower than those in Canada and productivity is higher. The appreciation of the U.S. dollar has had an affect on our lumber industry, but figures presented in testimony today will show that this dollar appreciation against the Canadian dollar since 1975 has been outweighed by a greater rate of inflation in Canada. Canadian logging and milling costs have rised faster, and productivity slower, than in the U. S. since 1975.

Yet, during this period the Canadian share of the U.S. softwood lumber market increased 65 percent. By 1984, Canadian softwood lumber imports had claimed 31 percent of the market. That market share figure continues to climb in 1985.

The U.S. paper industry also enjoys competitive advantages in international trade. It has access to abundant raw materials and a history of large capital investments to construct the most productive, state-of the-art facilities.

In spite of these comparative advantages enjoyed by the U.S. forest products industry, trade practices in other nations, including market restrictions and industry specific subsidies, have resulted in continuing forest products trade deficits. Last year, we ran a $4.6 billion trade deficit in forest products. Figures from the first quarter of 1985 indicate that deficit rising to $5.2 billion in 1985.

At todays hearing, the witnesses will document the extent of the problem both from an import and an export perspective. The evidence indicates the extent to which Canadian stumpage pricing policies subsidize softwood exports to the U.S. and cause harm to U.S. producers. Evidence will also be presented concerning the tariff and non-tariff obstacles U.S. forest products exports encounter particularly in Japan.

The harm imposed on this industry by nfair trading practices in other nations is clear. For example, in the last six years, 250 lumber mills have closed and nearly 30,000 workers have lost their jobs in lumber firms. Thousands of workers in related industries have also been affected. And this has occured even while lumber consumption in the U.S. is at record levels.

We must not permit these pracitices to continue against one of this nations most productive and naturally competitive industries. Surely some sort of reasonable trade policy response can be devised to address this situation.

I look forward to receiving the testimony today. The information we receive should help us fashion an appropriate government response to trade problems in the forest products industry.

The CHAIRMAN. The hearing will come to order, please.

This is the first time in a number of years the Finance Committee has held a hearing on the general subject of the status of timber. This hearing is not on any particular piece of legislation. It is not solely on the issue of the problem that the timber industry is facing from Canadian timber imports. It is not related to the tax bill or whether any provisions in the tax bill, such as the taxation of timber capital gains or expensing should or should not be retained. It is an overall hearing on the status of the timber industry, the problems facing the industry, and whether or not there are things that the Federal Government can and should do that would be helpful to the timber industry.

We have a great variety of witnesses, some advocating certain actions; other witnesses opposing those suggested actions. It is the first of what may be a series of hearings on this subject.

And I'm delighted to be joined today by my good friend, Senator Baucus.

Senator BAUCUS. Thank you, Mr. Chairman. Mr. Chairman, as you well know, your State of Oregon, my State of Montana, the Pacific Northwest and virtually the rest of the country generally are facing economic hard times. We are blessed in America with an enormous base of high-quality timber, the largest in the world. Our mills in the United States are the most efficient in the world. In fact, the Japanese productivity analysis will show that U.S. mills or processing plants are twice as productive as mills in Japan.

Despite that productivity, our industry is in a very difficult position. In 1980, for example, the industry had a $400 million trade surplus with foreign countries. Now 5 years later, we have a $2 billion trade deficit in forest products. Last year, our exports declined by 5 percent while our imports rose 10 percent. Two hundred and fifty American sawmills have been closed in the past few years. Thirty thousand American lumber industry workers have lost their jobs.

Part of the problem is the high value of the U.S. dollar, which makes foreign timber imports cheap; U.S. exports expensive. But there is another greater problem—unfair foreign tariffs applied by some countries, and unfair foreign subsidies practiced by others.

Our forest products are being locked out of the natural export market by unfair trade practices. And our forest products are being locked out of our own domestic market by foreign subsidies.

The Japanese, for example, love to buy our logs, but impose the world's highest tariffs on our plywood, particle board, and kraft linerboard. High tariffs preserve jobs in inefficient plants—Nagasaki, Sapporo. But those high Japanese tariffs take away jobs in the more efficient plants in Missoula, MT and elsewhere.

Meanwhile, Canada poses another kind of threat. Canada unfairly subsidies its forest products industry. Canadian stumpage subsidies allow them to undercut American producers. In 1975, 10 years ago, 19 percent of the lumber we consumed in our country came from Canada. Now it's up to 33 percent. Why the increase? Simple. American stumpage prices are set by market conditions. Canada's are subsidized by its Government.

Consequently, Canadian stumpage is half the United States price in the western part of the country, and one-fifth the New England prices. Essentially, Canadian public funds buy down the price of logs so they can sell more.

Today we are looking at ways to solve the trade problems affecting America's timber industry. One approach is to close the loopholes that allow policies like Canada's stumping subsidies, and Mexico's two-tiered natural gas pricing system. Congressman Sam Gibbons and I have introduced a bill that closes that loophole.

There are other approaches as well. As we search for solutions, we must avoid lurching into protectionism. We must formulate a comprehensive trade policy that restores our fundamental competitiveness and gives the efficient American industries, like the forest products industry, a fairer chance to compete.

Mr. Chairman, I might add, too, that Senator Nunn from Georgia has a statement he would like included in the record. He is unable to be here, but he is very interested in this issue.

The CHAIRMAN. In addition, Senator McClure cannot be here and has a statement that will be entered also.

[The prepared written statements of Senators Nunn and McClure follow:]

Statement of
SENATOR SAM NUNN
Before the
SENATE FINANCE COMMITTEE
UNITED STATES SENATE
September 19, 1985

Mr. Chairman, members of the Committee, thank you for giving me the opportunity to speak with you today concerning the flood of Canadian lumber imports entering our nation, displacing U.S. production, and eliminating U.S. jobs.

Georgia has more commercial forest acreage than any other state in the Union. About two-thirds of the entire state is classified as commercial forest land. The forest products industry is one of Georgia's largest employers. It employs more than 80,000 people and generates revenues of $8.6 billion per year. Georgia is the second largest lumber-producing state in the country, exceeded only by Oregon. Yet, in 1984, 49% of the lumber used in the state of Georgia was Canadian-produced.

Rising levels of Canadian lumber imports have had similar effects throughout the nation. Since 1975, Canada's share of the U.S. lumber market has increased from less than 19% to 33.4%. Mr. Chairman, lumber manufacturers in my state inform me that Canadian lumber is flooding our market because the price that Canadian provinces, which own more than 90% of Canada's timber, charge for timber is well below a fair market value and a small fraction of what U.S. lumber firms pay for comparable timber. My timber industry constituents feel this is simply unfair trade. I share their concerns.

In Georgia, local producers cannot compete against undervalued Canadian lumber that comes from undervalued Canadian timber, even though Canadian mills must ship a thousand miles. The Canadian industry will tell you today that it is other factors, such as the exchange rate, which have caused the flood of Canadian lumber into this country. While the strong U.S. dollar has certainly had some impact, the fact remains that Canadian provinces virtually give timber away to promote Canadian production and short-term Canadian employment.

I have cosponsored S.982 with Senator Baucus and S.1224 with Senator McClure as an indication of my concern regarding the impact of the rapid increase in Canadian imports. But I had sincerely hoped that it would be unnecessary to enact either piece of legislation. I had hoped that the Administration and the Canadian government might reach an agreement that would have curtailed Canadian lumber imports and returned them to a fair level. Such an agreement would be the best way to resolve this situation. Little progress has been made, however, in negotiations between Canada and the Administration. Therefore, it is time the Congress took action to address the import problem. While we should consider carefully the imposition of protective tariffs because of their tendency to trigger similar action by other nations, I do believe the imposition of such tariffs is justified if other avenues fail to prevent irrevocable injury to our domestic lumber industry.

In the first six months of 1985, Canadian shipments of lumber to the United States were running 15% above last year's record levels. In Georgia, the industries, communities, and families which rely upon our forest products continue to feel the adverse impact from these increases. The situation is the same throughout the U.S. lumber industry. Mr. Chairman, I commend you for holding this hearing today and I urge the Committee to take action to address the problems of rising Canadian lumber imports.

COMMENTS BY

SENATOR JAMES A. McCLURE

BEFORE THE INTERNATIONAL TRADE COMMISSION
HEARING ON CANADIAN LUMBER EXPORTS

July 23, 1985

I want to thank the Commission for the opportunity to testify here today. The issue being discussed is one that has become critical in my own state of Idaho as well as in many other states throughout the nation.

It isn't often that we in the Congress are able to take the time from our legislative responsibilities and duties to appear before hearings such as this one. But I hope our appearance at this hearing underscores the concerns we have with this issue. What is at stake on the outcome of this assembly are a lot of jobs that provide the income to feed and clothe a significant number of American families.

There are few states that do not have a forest products industry. For decades, the industry has helped provide a stable, economic base for thousands of communities and counties throughout our great nation.

The personal income from the jobs it provides is the only stable tax base that many areas have. The dollars spent within local communities generate other jobs that, in turn, make substantial contributions to state and local governments. These funds support education for our children, assistance for the elderly, and public service jobs that help to maintain our highways, domestic water and sewage treatment facilities, and local improvement projects.

When these basic jobs are lost, the question then becomes one of who will ultimately end up with the responsibility for unpaid school bond issues, and other publicly financed community improvement issues? Undoubtedly, the federal government will be called upon to "rescue" these communities as well as state and local government programs that have been dependent upon those funds for their viability.

In the current situation, it is unnecesary for us to allow the situation to go that far. Although there are many factors that contribute to the current depressed state of forest products markets, the fact is that some of them are beyond the control of the Congress; at least in the near term. On the other hand, there are some things that we can do.

I sincerely believe that the major short-term problem we face is the unbelievably high volume of softwood lumber that is being dumped on US markets by the Canadian timber industry with the obvious blessing of their government.

They now control over 32% of the US market and the latest figures indicate that the increasing trend is continuing despite denials to the contrary by the Canadians. Lumber exports to this country at the end of May, 1983 stood at 4.6 billion board feet; by the end of May in 1984 it had risen to 5.1 billion; by the end of May this year, we had already passed the 5.7 billion board foot mark!

That is an increase of almost 20% in the past two years; 11% in the past year alone! And those increases have been at the expense of jobs in the US.

Less than a decade ago, the forest products industry in Idaho provided employment for about 20,000 people. Today, that number is less than 14,000. Nationally, an estimated 22,000 jobs have disappeared during the past five years alone. The impact of such losses to states like Idaho is devastating.

In addition to the direct payroll losses incurred, there is also the loss of 25% fund money derived as a result of the harvesting of federally owned timber. These funds are used for education and road maintenance in counties with large federal land ownership patterns.

The Canadians constantly counter with claims that their own industry is in trouble and they must expand their production and markets in order to protect their industry. What my colleagues and I have a hard time understanding is why the US is constantly expected by our friends around the world to come to the rescue when they find themselves in trouble. And yet, when we have a problem of our own, there is seldom anyone willing to help. That is, unless there is something in it for them.

Our Canadian friends should remember that the health of their economy is closely tied to our own. But we do not currently have the economic strength, nor should the American people have an obligation, to support another country's economy, not even Canada's, when American jobs and perhaps the survival of a segment of our own industry is at stake.

It is the depressed market, the very heart of this issue, that precludes the harvesting of that federal timber. Because our own industry must purchase government stumpage in a competitive market while the Canadians do not, we are at a distinct market disadvantage. I'm certain that the difference in stumpage values will be discussed at length for the hearing record, so I will not address it further beyond this single aspect.

The Canadians have been quick to point to our own deficit and the strength of the US dollar as being the real culprits in the issue. However, I think that we can honestly make the assertion that their desire for obtaining as many of those strong, US dollars as possible is also a big contributor to the situation that they have chosen to ignore.

Recent Canadian government reports have been critical of the manner in which the government itself allows their forest products industry to be run. Hundreds of millions of dollars in forest funds earmarked for reforestation have been spent to fund national welfare programs and to pay off the debt on the national railroad.

Because of a system that allows a Canadian forest products company stumpage credits against funds spent for reforestation and other forest improvement work, it may be years before some of the local and provincial governments receive any money for stumpage!

On the other hand, our industry must pay for similar programs as a part of the stumpage contract award. It is due when the timber is cut and must be paid. If not, the contract may be considered to be breached and may be rescinded, leaving the company ultimately liable for damages to the government.

I could continue with numerous examples of the differences between our own system of selling and allocating government timber and that of the Canadians. To do so would probably be repetitious and redundant.

That brings us to the bottom line. Something must be done before we lose more jobs in our own country to "subsidize" those in Canada. The Canadians have been asked, friend to friend, to help us with this problem by practicing some voluntary restraint for a period of time until while we try to work out a solution. They have flatly refused, choosing instead to retain a posture bathed in professed innocence, seemingly oblivious to our plight.

Their continued refusal to come to grips with the real world in this issue leaves my colleagues and I just one other alternative: Congressional action to correct the inequities. I hope that our presence at this hearing will dramatically underline, for our Canadian counterparts, our determination to resolve this issue in one manner or another.

My colleagues and I intend to continue pressing for legislative relief unless we see substantial evidence by the Canadians that they intend to help us come up with an equitable solution. And that is clearly the preferable alternative.

I would also like some assurance from the Commission, for the record, that the current study, of which this hearing is a part, will be completed by the mid-October date now set for completion.

Thank you again for providing the opportunity and the forum in which to once again express my views on this important issue.

The CHAIRMAN. And we will start with a panel of the Honorable Don Bonker from the State of Washington; the Honorable Charles Whitley from the State of North Carolina; and the Honorable Beryl Anthony from Arkansas.

Gentlemen, welcome.

Do you know if Don is coming?

Mr. ANTHONY. Senator, I have not seen him.

The CHAIRMAN. Does he have a staffer here by any chance that knows if he is coming?

[No response.]

The CHAIRMAN. Why don't the two of you go ahead and start. If he comes, we will add him to the panel.

STATEMENT OF HON. BERYL ANTHONY, JR., REPRESENTATIVE FROM THE STATE OF ARKANSAS

Mr. ANTHONY. Senator Packwood, I'm Beryl Anthony, Jr. I represent the Fourth Congressional District in the State of Arkansas.

At one time, I served on the Agriculture Committee and I was on the Forestry Subcommittee. Since then, I have shifted over to the Ways amd Means Committee. I was on the Budget Committee in 1981 and then the latter part shifted to Ways and Means. So I have had an opportunity to see the total impact of this industry from a lot of different perspectives.

I think Senator Baucus summarized some of my feelings that the strength of the dollar, without question, is part of our overall problem. And we do have unfair trade practices inasmuch as we, China and Japan, two of our big markets for unprocessed logs, do not allow to a great extent the value-added products into their country.

But I really came today to talk more specifically about a closer problem. And that is the problem with our friendly neighbor to the North, and that is Canada. I see two things that have occurred in the last 2 years that have created tremendous problems. You will be inundated before the day is out with numbers showing how devastated this industry is.

In the past, it was principally from your State of Oregon and the northwestern parts of the United States. I can tell you now that the problem exists anywhere there is a timber base in the United States.

The dollar has created some problems. And we need the Canadian market—we will always need the Canadian market, but at the present time, their percentage of the market has increased. And I personally think it has increased as the result of an unfair subsidy.

I have studied this problem. I went to British Columbia in August with the Ways and Means Trade Subcommittee to talk directly to the governmental officials and to the industry officials. And what I found, I think, is clearly a subsidy. I happen to be a cosponsor of the piece of legislation that Senator Baucus and Sam Gibbons has introduced, the natural resources bill. I'm a strong believer in the fact that we are going to have to redefine what a subsidy is; what a grant or a bounty is. We are going to have to define the fact that when you have a residual value method of marketing your timber and you run it on a 90-day average, and you change that average every 30 days and you are willing to back down the cost of your stumpage to the fact that it will be $2 a thousand so that you can continue to undercut your competitors south of you. I can tell you that there is no way that the lumber manufacturing capacity in the United States will ever regain its past market shares under such unfair competition.

I would like to just tell you a personal story to highlight how a person became acquainted with this problem. I happen to be a fourth generation timberperson. My family has been in the timber business for many, many years. We do have two operating sawmills. So I guess to some extent I come knowing firsthand about the industry and I know the devastating impact.

We have a sawmill that is 15 miles from El Dorado, AR. Georgia Pacific has a sawmill that is just 2 miles from the city limits of El Dorado, AR. One day I left our headquarters and I was walking down the street to the corner drug store to have lunch and I noticed where this local law firm was in the process of remodeling their frontage. I was curious to see whether or not it was Georgia Pacific or International Paper, Weyerhaeuser, just exactly whose lumber it was or whether it was fir out of the Pacific Northwest.

I was startled to find out that it was Canadian lumber. Well, I went back and I asked my father, who has been in the business for over 40 years, what in the world was happening. And he said it's the worse he has ever seen, and he said the Canadians were pricing them out of the business.

And I said do you mean that they can sell lumber in El Dorado, AR cheaper than these two sawmills can, one 2 miles away and one 15 miles away. And he said that is correct. And I said why. He said because they are giving their stumpage away.

Well, with that, I took as a challenge to go study the problem. I've tried to be open-minded about it. I've met the Canadian officials anytime they wanted to meet in my office.

But, Senator Packwood, I can tell you that without some legislative relief if the Canadians fail to sit down on a bilateral basis and negotiate with our trade ambassador or with the President of the

United States directly, we will see no relief and we continue to see devastation in this industry.

And I thank you for the opportunity to be able to testify.

I would like to have my full statement accepted for the record.

The CHAIRMAN. All of the statements will be in the record in full. We have asked the witnesses to abbreviate their statements. And, Congressman, I appreciate you doing this.

[The prepared written statement of Representative Anthony follows:]

Statement of U.S. Representative Beryl Anthony, Jr.

Mr. Chairman, I am pleased to be here today and I commend you for holding today's hearing regarding the decline of the U.S. softwood lumber industry. I know how vital this industry is to the Pacific Northwest and I am sure you are aware of how important it is to the South and to my home state of Arkansas. It supplies 40,000 jobs and an annual payroll of $600 million in my home state.

It is not an overstatement to say that the timber industry in the U.S. is in deep depression even though the demand for lumber is large. Since 1979, over 250 mills in the U.S. have closed and over 30,000 jobs have been lost. There are many reasons for this crisis condition but I am here today to discuss only one -- the growing penetration of the U.S. softwood lumber market by Canada. Canada's share of the U.S. market in 1975 was 19%. It is now about 33.4% nationally and in some states it exceeds 50%. The volume of Canadian timber has risen from 5.7 billion board feet in 1975 to 14.5 billion board feet in 1985.

What concerns me most about the growing Canadian penetration of the U.S. market is that it is being accomplished by a subsidy system which appears to have the tacit support of this administration. As you know, the U.S. industry filed a countervaling duty petition against Canada in 1982 and the International Trade Commission found injury to the U.S. industry. Relief was denied by the administration due to a ruling by the International Trade Administration of the Commerce Department which ignored the injury and contended that there was no subsidy involved in Canada's lumber trade.

I have never accepted the accuracy and fairness of that ruling and neither has the U.S. industry. I went to British Columbia in August along with other members of the House Ways and Means Committee. British Columbia provides two thirds of Canada's annual production and more than half of all exports to the U.S. I met with Canadian officials and spokesmen there and again here in Washington, D.C. after my return. My objective was to study the Canadian pricing system in greater detail so I could better explain to my colleagues how the system works. My investigation clearly found a subsidy to be involved and it is an effective one.

Canada has developed a timber pricing policy which is a form of "upstream" subsidy in that the natural resource is priced arbitrarily to insure that the jobs, export sales, and economic activity associated with lumber manufacturing are maintained as much as possible regardless of the economic climate in the U.S. .Timber policy, which is largely controlled by the provinces, is a form of social policy in Canada. Rather than absorb a larger level of unemployment in their industry, Canada chooses to lower stumpage prices and expand their market share, even in the face of declining prices in the U.S.

. They are able to do this because they do not use an open bidding system such as is done in the U.S. to determine fair market prices. Rather, they compute an arbitrary price based on what is required to penetrate the U.S. market. They then allocate the components of this price backward by subtracting all costs including transportation, marketing, and an assured profit. What remains becomes the stumpage price. It theoretically could go down to zero and at that point, the Canadians would be giving the timber away to the companies who have been liscensed to cut it. They are very near that level today.

I believe this policy is unfair to U.S. companies who must compete by buying timber on the competitive market by a bidding process, whether they are buying from the U.S. Forest Service or private landowners. The Canadian pricing policy is virtually complete in its ability to adjust to a depressed market such as we have today. With each downward "rachet" of the "price", the fixed costs and profit margins of the companies doing business in Canada remain unchanged. They are not squeezed by smaller and smaller margins such as U.S. companies are presently experiencing.

A remedy must be found for this natural resource subsidy practice. It will have to be legislated because this administration seems determined to continue to aid the Canadians in hiding behind the May, 1983 decision by the International Trade Administration. The remedy we need must confront the advantage given to Canadian lumber because of the natural resource subsidy; in this case, the standing timber being virtually given away.

One approach under consideration in the House is a quota bill. This approach would limit Canadian imports to an average of their market share over the past five years. While I am a co-sponsor of this bill, I believe there are more effective means of resolving this issue which will provide the Canadians with a fair market share of our market while limiting the growth of that share.

One possible solution could be a bilateral agreement between our two countries which would limit the volume of lumber coming in. Even more preferable would be a voluntary agreement by Canada to limit their sales in order to preserve overall advantages of trade between our countries.

If none of the above solutions can be reached quickly, and the U.S. industry needs relief soon, then another approach is possible. Congress can move forward on legislation which would amend U.S. countervaling duties law to cover the kind of natural resource subsidy practices which are used by Canada and other countries to gain an unfair advantage in international trade.

The House Ways and Means Committee is presently considering a bill which Chairman Sam Gibbons and a number of other members, myself included, introduced earlier this year. Our bill would define the right to remove or extract a natural resource provided by a foreign government as a subsidy if that product is sold below fair market value and used as an input into a product exported to the U.S.. Because our present countervaling duty law is vague in this area, the remedy we have proposed would clarify this area and insure relief for U.S. producers.

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STATEMENT OF HON. CHARLES WHITLEY, REPRESENTATIVE FROM THE STATE OF NORTH CAROLINA

The CHAIRMAN. Congressman Whitley.

Mr. WHITLEY. Thank you, Mr. Chairman. I'm Congressman Charlie Whitley from North Carolina. I had the privilege of serving in the House with both of your colleagues there to your right and your left, Max Baucus and Steve Symms, with whom I served on the House Agriculture Committee.

I'm presently the chairman of the Subcommittee on Forests, Family Farms and Energy of the House Agriculture Committee. And in that capacity, I welcome the opportunity to speak to you.

I want to reiterate what my colleague said. That this is a national problem. It's not just one that's peculiar to the Pacific Northwest or to any other individual section of the country.

In my capacity as chairman of the Forests Subcommittee, I've had occasion to talk with Members from all over the country regarding this problem. And it certainly is a national one.

In my own State of North Carolina, for example, which is a heavily forested State and has some of the most productive forests in the Nation, in 1982, 32,000 North Carolinians were employed in lumber and wood products. Recent estimates indicate that over 41 percent of all the dimension lumber sold in North Carolina last year was produced in Canada, and that situation is very similar throughout the United States. Hundreds of communities dependent on the forest products industry for employment and taxes that maintain the schools and roads, have faced some bleak times despite relatively strong U.S. lumber demand.

Canada's share of the U.S. market has increased from 18.7 percent in 1975 to 33.4 in the first 6 months of 1985, and is rapidly growing.

It is a consensus, a very strong consensus, in the House—again, in all parts of the country—that while the hard dollar makes these products attractive to U.S. buyers and the quality of the Canadian softwood products is good, that the major factor is that the stumpage price, which is for all practical purposes subsidized, is the major factor that allows the Canadians to penetrate our market to this degree. And this simply, in our opinion, is not fair trade.

The problem is not new. The Canadian timber has consistently cost much less than similar U.S. timber. The U.S. industry has suffered as a result. We also think on our subcommittee that the administration already has considerable authority now to provide some relief in this area. However, it has refused and continues to refuse to act aggressively on the problem. The U.S. lumber industry is seeking to compete in a competitive market, but only on a level playing field.

If Canada remains intransigent and the administration continues to ignore the inequities and the economic disaster facing the U.S. lumber industry, then we feel that Congress must act.

The proposed legislation before both Chambers would redefine the meaning of subsidy under U.S. trade laws so that any natural resource given to a foreign manufacturer at less than the fair market value be subject to countervailing duty. That's fair. That gives our industry a chance.

I appreciate this opportunity to appear. And I will submit my full statement for the record.

The CHAIRMAN. Thank you, Congressman Whitley.

[The prepared written statement of Representative Whitley follows:]

STATEMENT OF HONORABLE CHARLES WHITLEY, CHAIRMAN
SUBCOMMITTEE ON FORESTS, FAMILY FARMS, AND ENERGY
COMMITTEE ON AGRICULTURE
SEPTEMBER 19, 1985

Mr. Chairman, members of the Committee, thank you for this opportunity to speak with you concerning the international competitive challenges facing the U.S. forest products industry.

My statement is short but it makes three points: first, Canadian softwood imports are presently seriously disturbing the market for domestically produced wood products; second, the Administration could go a long way toward resolving this problem under existing authority, but so far has not made a good faith effort to do so; and third, absent an agreement with Canada to limit these imports, Congress will be forced to take action.

North Carolina is a heavily forested State. Our forests are some of the most productive in the nation, and our forest industry is very important. In 1982, 32,000 North Carolinians were employed in lumber and wood products. However, recent estimates indicate that over 41% of the lumber sold in North Carolina was produced in Canada.

The situation is similar throughout the United States. Hundreds of communities dependent upon the forest products industry, for employment, and taxes that maintain schools and roads, are facing bleak times despite relatively strong U.S. lumber demand.

Canada's share of the U.S. market has increased from 18.7% in 1975 to 33.4% in the first six months of 1985, and it is growing rapidly. The reason that Canadian production is increasing is that the Canadian provinces offer stumpage at an extremely low price. Given this big advantage on input costs, Canadian firms can sell timber in North Carolina, a thousand miles away, at prices our local mills cannot meet. Of course, the high value of our dollar also makes these products attractive to U.S. buyers, and frankly the quality of the Canadian softwood products is good. Our homebuilders are not reluctant to use the Canadian lumber.

Because the Canadian system of selling timber is noncompetitive, Canadian provinces can offer timber to Canadian lumber firms at whatever price it takes to allow those firms to penetrate our markets. This, however, is simply not fair trade.

This problem is not new. Canadian timber has consistently cost much less than similar U.S. timber. The U.S. industry has suffered as a result. Nonetheless, the Administration and the Canadian governments have refused to act on this matter. The Canadians refuse to reorganize that a problem exists and the Administration refuses to act aggressively on the problem. The U.S. lumber industry is seeking to compete in a competitive market, but only on a level playing field. Canadian timber should be sold at fair market value, if not, they should agree to limit exports into the U.S.

If Canada remains intransigent, and the Administration continues to ignore the inequities and economic disaster facing the U.S. lumber industry, then Congress must act. Proposed legislation before both chambers would redefine the meaning of subsidy under U.S. trade laws so that any natural resource given to a foreign manufacturer at less than a fair market value would be subject to a countervailing duty. That's fair. That gives our industry a chance to compete.

Thank you for allowing me to present this testimony, Mr. Chairman, I am happy to answer any questions that you may have.

The CHAIRMAN. Let me address this to both of you, but perhaps, Congressman Anthony, to you specifically, since you are actually in the business.

Canada has been selling their timber in this fashion for the better part of a century. What has happened in the last few years to make it such a problem, since it wasn't a problem (or at least we didn't think it was) for years, and years, and years?

Mr. ANTHONY. Senator Packwood, I think the Canadians have an advantage more in a down market than they do in an up market. For instance, they have this 90-day running average. And what they do, they go back and they figure out what the end product will sell for. And then they have the residual value. And they add in what would be overhead and what would be profit. In the very last calculation that is made by the Canadian Government, that would be what would be the value of the stumpage. On an up market, they will adjust it. But interestingly enough on an up market, their contract says that they take 85 percent of the profits away from the processor. But on the down market, they will make that adjustment every 30 days.

So here, in my opinion, is where the subsidy actually does occur. As the market shrinks, as housing starts fall, as the dollar gets stronger and as the markets shrink totally, then that subsidy gives them the cut in edge to continue to penetrate our market.

I come from the South. I come from Arkansas. Two-thirds of the land is owned by nonindustrial landowners. They sell their market on an open bid. Canada does not sell theirs on an open bid. They contract with a processor on a licensing basis. They give them 15 years to cut, and it will be renewable for another 15 years if they do a good job.

In our case, we bid for the timber on the open market. Our processors are the ones that have to run the risk of the markets going up or down. If we guess wrong, we take our lumps. If we guess right, we have got to save the gravy for the lumps because we know they are going to come. It's a cyclical business, always has been.

So to me it's that adjustment right there that the Canadians are willing to make. Even if it goes down to zero, they are willing to price their stumpage at zero if they say that's what the residual value is. As a result, they will always beat us to the punch, and they will always undersell us and underprice us.

There is one extra thing that I also learned that I think is very interesting. The Canadians have just started taking advantage of this in the last 6 months, but I think it will be something that you will see increasing their ability to penetrate the markets in a broader scale. We have deregulated trucks; we have deregulated rails. The Canadians are now negotiating long-term bulk commodity contracts with both of those shippers. They will then set up inventory bases in different parts of the country. And they are in very smart business by doing this. They get a cheaper rate by getting it to a central location, and then when a supplier in Little Rock says, hey, I need some lumber, they don't have to wait a week for it to come. They will get it overnight.

So because we have deregulated our industries, we are also being punished because of that, too. Our competitors have been able to take advantage of that.

The CHAIRMAN. Congressman Whitley, do you want to comment on that?

Mr. WHITLEY. I would agree with that, Senator. All three of you being from the Pacific Northwest, you know the problems we have had there. With the sort of long-range buying policies that we've had—you bid on it now, you buy it now, you plan to cut it 1 year, 2 years, 3 years, sometime down the road, and you bid it on the basis of, one, current prices; and two, what you see as an inflationary market or rising market, and then the bottom drops out. As Mr. Anthony says, you cut at the bottom of that cycle instead of the top. And when they are free in Canada to adjust their stumpage on a very short-term basis, they are always in a position to take advantage of that rising market or the falling market. They don't take the losses in the falling market that our industry takes.

The CHAIRMAN. Senator Baucus.

Senator BAUCUS. Gentlemen, as you know, the President plans to announce a trade offensive Monday. I wonder if you could tell us what you think that trade offensive should include that might help solve this problem.

Mr. ANTHONY. I'd be happy to address it. I think the President of the United States should sit down with the Canadian Government and say, look, gentlemen, this is a problem; it's a national problem for you; it's a national problem for us; we are friendly; we want to stay friendly, and we would like to have even better free trade not only in this area, but in a lot of other areas.

I think the President needs to say that this is a growing political problem for the Canadians. And as a result, they should be willing to sit down and address this issue.

I have been led to believe that the industry in Canada is ready, that the various what we would call Governors in our States, Ministers in their States, are trying to send a message that they are ready to negotiate. If that message can get all the way back to the Canadian leaders, I think maybe we can do something.

It's basically a share of a market. That's what we have got to figure out. Is how can Canada have a proper share of this market without devastating our industry and causing us loss of jobs.

Senator BAUCUS. I hope you are right. I would say that my experience with the Canadians has been slightly different. I have met with them several times recently, as I am sure you have too—you mentioned you were with the British Columbia Premier up in British Columbia in August.

But in the meetings I have had with the British Columbia Premier and with other Canadian legislators it's clear to me that this is the one issue that really "pushes their button." There are lots of United States-Canadian issues, including some as big as acid rain. But this issue, subsidized Canadian stumpage, is the one that pushes their button more than any other. And I have found them so far to be totally resistant to any compromise. I hope that we keep explaining to them and to the world the degree to which they are unfairly subsidizing. Their position might change, but I must tell you that my experience so far as been that it is very hot.

Mr. ANTHONY. Well, specifically section 301, the President has the authority to impose tariffs.

Senator BAUCUS. That's right. I think that leads to another type leverage that we have. And I would like your reaction to it. As you well know, the Canadians want to negotiate a free trade agreement with the United States. They have access by and large to American markets now, particularly with the United States dollar as high as it is compared with the Canadian dollar. They want to maintain and continue that access to our markets. Therefore, they are trying to negotiate a free trade agreement with the United States.

My question to you, particularly since you are on the Ways and Means Committee, is: Because free trade agreements have to fast-track through your committee as well as through this committee, how much opposition there will be in your committee for a free trade agreement unless and until this Canadian stumpage problem is solved?

Mr. ANTHONY. I personally don't believe a free trade agreement could pass the Ways and Means Committee if this lumber problem is not solved.

Senator BAUCUS. Thank you.

Mr. Whitley, do you have any comments on the general approach you think the President should take when he announces the trade offensive Monday?

Mr. WHITLEY. Well, I would just hope that the President will demonstrate a personal commitment to taking some effective action in this area. A number of us met with Secretary Baldrige a couple of months ago, a bipartisan group from throughout the Nation, and stressed to him how important all this was. And when we got through, he gave us a lecture on deficit spending and the hard dollar. Well, you know, we all know about the strong dollar, but I think the President needs to demonstrate that he understands the problem. I also think if he doesn't do something about this problem, Congress will.

Senator BAUCUS. Thank you.

The CHAIRMAN. Senator Symms.

Senator SYMMS. Thank you, Mr. Chairman.

I would first like to welcome my two colleagues to this side of the Hill. I appreciate your testimony, and agree with it in general.

I would also like to say, Mr. Chairman, that my senior colleague, Senator McClure, would like to be here and testify with these two Congressmen; however, he's chairing an Appropriation Committee markup. I think you have already submitted both his statement to the ITC and his statement here to the record. But I would just like to note that.

Did I hear either one of you mention the legislation that you favored? Did you say, Beryl, if you favored any legislation?

Mr. ANTHONY. Senator Symms, I happen to be a cosponsor of the natural resource subsidy bill that Congressman Gibbons has introduced on the House side.

Senator SYMMS. How about you, Charlie?

Mr. WHITLEY. I'm not a cosponsor of that bill, Senator, but I think we ought to be pushing some legislation. It's been my experience, and I know yours, since we have been in the Congress that if we don't push legislatively, we just don't bring any effective pressure to bear.

Senator SYMMS. I agree with that conclusion. I was at one of the meetings with Senator Baucus, and when I walked out of the meeting, I said unless we are willing to move some legislation, the Premier of Canada, where he has control of the timber, isn't about to see more unemployment in British Columbia. In our case, our respective States don't have control of the timber. The Federal Government does. There are a lot of complications to cutting timber off Federal lands, as you both know, in the Pacific Northwest with all the environmental laws and other restraints and even-flow management and wilderness lockups and so forth. So we have got ourselves at a disadvantage. You know, if we go out there and open some forest and put some timber on the market, we might compete with them.

But I was told last week—and would be particularly interested, Beryl, in your comments coming from the timber industry yourself and your experience in it—I was told by an Idaho wood processor who incidentally operates one of the most modern wood processing mills in the United States, and it's all computerized and very efficient—he maintains that some of his friends that he has talked to in Canada that are competitors of his now say that they would like to reduce some of their production, but they can't do it because their competition won't reduce their production, so, in other words, they are running at even more than 100 percent; three shifts in many cases. But they can't really sit down with their own people in this country or the U.S. companies that also operate in Canada because the Americans, if they sat down and talked like they do in Canada, they would be arrested for violating antitrust laws.

But having that in mind, I don't think anything is going to happen unless the administration would take some decisive action, either with the 201 or 301 case, and apply either countervailing duty or a tariff where there is damage being done. But would you favor a tariff as opposed to a quota?

Mr. ANTHONY. A quota, obviously, is going to solve the problem the quickest. However, I think a countervailing duty tariff is the fairest way to do it. And that is the reason I have put most of my legislative efforts behind trying to redefine what a subsidy is. And then once you define what a subsidy is, then you can—if you prove that there is a subsidy, then you put the countervailing duty on it.

Senator SYMMS. Well, I have my staff preparing a bill that would have a 30-percent tariff put on dimension timber that came in from Canada. What would your interpretation of the bill you sponsor, how much would the countervailing duty be?

Mr. ANTHONY. Well, I think that would be a function of determining what the subsidy is and what percent the subsidy amounts to. And then you would offset it to say that that would create the equity between the two industries.

Senator SYMMS. Would that be 30 percent?

Mr. ANTHONY. I don't know. I'll check into——

Senator SYMMS. Fifty-sixty dollars a thousand, or would it be that high?

Mr. ANTHONY. It probably would be between 25 and 33 percent.

Senator SYMMS. Thank you very much.

Mr. Chairman, I see another one of my colleagues.

Mr. ANTHONY. Could I just make one closing comment, Senator?

The CHAIRMAN. Yes.

Mr. ANTHONY. You have asked what legislation I have supported and what I think would be the best way. My personal observation is that legislation out of the Congress is not the very best way to attack this problem. I think this is a problem that should be negotiated out between two friendly countries. We've had a long history. We want to establish even better trade. I would think without question there will be in the future some type of bilateral trade agreement sought to be resolved. Knowing that this is a tremendous problem and is going to be a sticking point, it would appear to me that the two governments should immediately sit down and try to resolve this among themselves and bring that solution to the Congress without forcing the Congress to try to act.

Mr. WHITLEY. I agree with that, Mr. Chairman. But I would again reiterate that that hasn't happened. And I think in the absence of legislative pressure, it's not very likely to happen.

Senator SYMMS. Is your bill the same as the——

Senator BAUCUS. Yes. We have the same bill.

Senator SYMMS. If I'm not a cosponsor of it, I hope you will put me on it right now.

Senator BAUCUS. You are on it right now. [Laughter.]

The CHAIRMAN. Congressman Bonker, good to have you with us. We will put your entire statement in the record. Why don't you abbreviate your written statement orally.

STATEMENT OF HON. DON BONKER, REPRESENTATIVE FROM THE STATE OF WASHINGTON

Mr. BONKER. Thank you, Mr. Chairman. I commend you and your colleagues for sponsoring this hearing. It is, indeed, a timely subject as we attempt to deal with trade problems overall, our staggering trade deficit, and also product-specific areas where we need congressional action.

I'm going to try to avoid any redundancy or rhetoric on this subject because I think you will have a good description of the basic problem from the other witnesses.

I can really sum up my statement in one theme: If the Canadians are not subsidizing their timber and wood products industry, they have nothing to fear by legislation that is before the respective committees of Congress. If the Canadians are subsidizing their industry by making available stumpage at less than market value, perhaps the time has come for the Canadians to ask themselves—as a large economically dynamic and sophisticated country—whether they ought to be subsidizing in today's economic world.

And that is a question I think many Canadians are attempting to pose to themselves. Under its current practice, Canada is risking excessive cutting, overcutting of their forest lands.

They are, in effect, subsidizing an industry that is experiencing severe difficulty, as indeed our industry is. But if we are going to play by the rules, if we are going to subscribe to trade practices and policies that are consistent with GATT and international trade law, then subsidies should not be allowed; particularly from a large and economically healthy country like Canada.

And so these are the questions that we pose as sponsors of legislation on the House side.

Second, I agree with Beryl Anthony. I do not support a legislatively mandated quota to deal with this problem. We have trade laws that are in place. We have procedures that make it possible for industries to bring their grievances before the International Trade Commission and, the International Trade Administration. We have seen this exercised once before with respect to this industry in the case that was brought claiming subsidy a few years ago. And, of course, the International Trade Administration found that the subsidy was de minimis.

I happen to believe, Mr. Chairman, that the preliminary finding of the International Trade Administration was very much in favor of our industry, but political considerations which were brought about by the intervention at very high political levels of Canadian premiers and others forced a reversal of that earlier decision.

In any case, I think it's a proper role for Congress to fill in what we see as a gap in our trade law. And that is this question of resource subsidies.

So what we are attempting to do is to put into place a definitional standard for subsidy, and leave it up to the appropriate Federal agencies when a petition is once again brought before them by our industry. Congress must provide the definitional standard of what constitutes a subsidy, and then allow our trade agencies to make a proper decision based on the full evidence at hand?

Resource subsidy legislation is in no way a protectionist bill. We are trying to avoid protectionism by dealing with unfair trade practices as they exist today. And if Canada can meet that standard, if Canada is not subsidizing their industry, they have nothing to fear from legislation that is pending before the Congress.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

[The prepared written statement of Representative Bonker follows:]

STATEMENT

by the Honorable Don Bonker
before the Senate Committee on Finance

"International Trade and the U.S. Wood Products Industry"

September 19, 1985

Mr. Chairman, I want to commend you for your leadership in convening this hearing to examine the complex and often vexing issues in the areas of international trade and our domestic wood products industry.

Given the severe problems facing our domestic industry and the tremendous pressure for action on trade legislation, this hearing is extremely timely and important.

Let me briefly summarize my comments for the benefit of the Committee:

- **First, the wood products industry has always been a strong proponent of free and open international markets. Free trade has benefitted the industry in the past and is still the best course for the long-term health of this vital sector of our economy.**
- **At the same time, Congress and the Administration can and should take firm action to eliminate unfair foreign trading practices that currently threaten the very future of our domestic wood products industry.**
- **Finally, a positive strategy of developing new markets for American wood products, coupled with the elimination of unfair foreign trade practices, is the best way to maintain and strengthen our domestic industry and avoid protectionism.**

Over the past year or so, I have been working closely with the wood products industry on a variety of efforts to enhance our international trade position. While I do not claim to have all the answers, and would welcome the input of the Committee, I would like to offer a five-point program that I believe goes a long way toward addressing the critical needs of our domestic wood products industry.

First, bring down the overvalued dollar. No matter what else the private or public sector does to help the domestic industry become more competitive in the international market, it won't be fully effective until the international currency problem is addressed. Today's distorted exchange rates hurt both ways: wood imports are cheaper, and exports are more expensive.

The conventional wisdom is that the federal budget deficit is the villain because it pushes up interest rates and invites foreign capital investment, enhancing the value of the dollar vis-a-vis other currencies.

Deficit reduction is a political and economic imperative, and Congress must continue to press for even further cuts, but I am not convinced that deficit reduction alone will solve the currency problem. In my opinion, we need more immediate and direct action along the lines of setting target zones for international exchange rates to avoid extreme fluctuations in currency values. The European Community employs such a system with noted success.

Unless the Administration recognizes the problem, there is little prospect that we can do anything about it. Recently, the Reagan Administration announced that a majority of our trading partners had agreed to a new round of GATT trade negotiations. While such talks may be helpful, I fear they are premature and ill-advised unless the currency problem is also addressed.

The Administration now has to come to Congress for the authority to negotiate a new tariff agreement. I personally believe that Congress should condition the approval of this negotiating authority upon the convening of an international monetary conference or the successful conclusion of an agreement to correct currency misalignment.

Second, the Canadian import issue must be settled. As a result of heavy governmental subsidies on stumpage, Canadian manufacturers are undercutting our long-established mills, capturing an ever-increasing share of the U.S. market.

I believe this issue boils down to one central point. If the Canadians are not subsidizing their industry, then they have nothing to fear from the legislation before Congress. If the Canadians are subsidizing, they must ask themselves why a highly developed, technologically advanced nation must resort to such dubious economic practices.

Canada's subsidies have not only distorted the U.S. market and provoked outcry from our domestic industry; these subsidies have sparked criticism from government officials, industry observers, and the general public in Canada, who are concerned that the subsidies have led to tremendous overcutting that will cripple Canada's long-term economic prospects.

Since 1975, the Canadian share of the U.S. market has grown from 18 to 31 percent. In Washington State, where we grow a few trees ourselves, Canadian lumber accounts for 33 percent of the market, dozens of sawmills have closed, and 15,000 men and women have lost their jobs in the past five years.

According to the Northwest Independent Forest Manufacturers Association, U.S. government timber sold last year for an average of roughly $90 per thousand board feet. In Canada, where the Provinces own 95 percent of all the timber, the cost was $4-7 per thousand board feet.

Perhaps the most compelling example comes from a comparison of stumpage rates in the Mount Baker-Snoqualmie National Forest in western Washington state to the Vancouver Forest Region in British Columbia. These forests are separated only by the 49th parallel and have practically identical topography, climate, accessibility, timber type, and other factors. Even after taking into account differences in road costs, annual rents, and species quality, the U.S. market price in 1984 was $95.55 per thousand board feet, while the price in Canada was only $37.31, both in U.S. dollars.

The real question is, how should Congress deal with this problem? Along with 40 of my colleagues in the House, I have introduced legislation which I believe deals with the Canadian import situation in a tough, but equitable manner.

My bill proposes a three-step process. One, we unbind the tariffs and set a one-year timeframe for the negotiations currently ongoing between our two governments. Two, if there is no agreement, a temporary ten-percent *ad valorem* duty would be imposed on Canadian wood products coming into this country. Third, if there is no agreement, my bill would redefine "subsidy" in our trade law to specifically include below-market stumpage pricing, which will enable our industry to seek proper relief under existing trade laws.

A similar resource subsidy provision has also been proposed -- on an even broader scale -- in legislation authored by Rep. Sam Gibbons of Florida, Chairman of the Ways and Means Subcommittee on Trade, and widely acknowledged as "Mr. Free Trade" in the House of Representatives.

The Gibbons bill takes a general approach to resource subsidies, while my bill is product-specific to timber. But when it comes to wood products, they have the same purpose -- to end Canadian subsidies.

Predictably, the Canadians and other groups have called these measures "protectionist," but the charge simply doesn't hold up under scrutiny. It's not protectionist to deal with unfair trade practices which distort our market. The real question posed by both the Gibbons bill and my bill is this: Are the Provinces subsidizing their industry to the extent that it gives them an unfair advantage in our domestic market? If so, the subsidy must end, or at least a countervailing duty should be imposed. If not, we have only ourselves to blame for not being competitive with our neighbors to the north.

<u>Tariffs on Certain Canadian Plywood.</u> There is another potential wood products trade problem with Canada which I believe the Committee and Congress as a whole should address.

Due to a loophole in our tariff schedules, Canada could ship large amounts of plywood to this nation at a highly preferential tariff rate. Obviously, this problem has the potential to throw many Americans out of work in the plywood sector, further exacerbating the woes of our forest products industry.

In order to correct this problem, I have introduced legislation, H.R. 2324. This bill is identical to H.R. 5182, which I introduced last session and which passed the House of Representatives as part of the Omnibus Tariff and Trade Act. Unfortunately, this provision was dropped at the 11th hour by the House-Senate conference.

Let me briefly describe the problem: currently, certain plywood sheets are being exported to the United States as "building boards" -- which face roughly a 10 percent tariff -- rather than as plywood -- which carries a 20 percent tariff. Obviously, this reduced tariff gives the Canadian plywood a competitive advantage in our market.

The tariff category called building boards was apparently intended to be a residual one for special use construction panels that did not fall into any of the plywood or wood veneer panel categories. Instead, it has become a loophole category. In the course of last year's hearings, Congress found that by simply altering the edge of a plywood sheet, foreign producers are able to get their products classified as building boards, qualifying for the dramatically lower tariff treatment. In theory, the edgework dedicates the sheet to some unspecified special construction use. In fact, these sheets are usually used just like plywood.

H.R. 2324 would revise the building board category to insure that it is used only for special use panels and not for plywood. This revision makes the U.S. tariff schedule for these products conform more closely to the international code, which contains no building board category at all. The bill should not be regarded as protectionist. Rather, it is a loophole-closer. It would restore the original intent of our Tariff Schedule, insuring equal treatment in the U.S. market between foreign and domestic producers. This legislation has the support and endorsement of the American Plywood Association, which represents both large and small U.S. plywood producers.

I am hopeful that the Committee will examine this proposal and include it in this year's omnibus tariff bill, in order to help eliminate this unnecessary loophole in our Tariff Schedule.

Third, we must increase the pressure on Japan to end its high tariffs and other barriers to U.S. finished wood products. Our wood products industry has patiently endured years and years of roadblocks and footdragging in their efforts to compete fairly in the Japanese market.

Intensive effort by both industry and by U.S. government negotiators, have resulted in very little progress. The recent "market opening" announcements by Japan have been vague and unsatisfactory. While Japan has now committed to consider opening its market to U.S. plywood and veneer, this will not occur until 1987, and no details about the scope, swiftness, or form of these market opening measures have been provided. Basically, all we have to show for our efforts is a vague promise, nothing concrete.

I strongly believe that Congress and the Administration must "up the ante," or increase the pressure on the Japanese government to take immediate and concrete steps to end these high tariffs and other barriers to American plywood, veneer, and other wood products.

One approach might be reciprocity legislation patterned after the Danforth bill on telecommunications that would unbind the tariffs on both sides and then establish a level playing field. If Japan persists with its tariffs, we would impose comparable tariffs. The President now has the authority to take these kinds of actions while remaining consistent to the GATT, but he has chosen not to exercise this authority.

Another suggestion that I have heard is for Congress to provide the States with the authority to restrict log exports from their lands. There are other potential approaches, and each obviously has its plusses and minuses, but the message to the Japanese negotiators should be clear: Congressional patience is wearing thin.

Fourth, we must work aggressively to develop a market for finished products in China. While China's heavy purchase of raw logs has been welcomed in an otherwise depressed Northwest industry, I am bothered by the long-term trends and effects of this policy.

Many of those logs come from my district, where mills are shut down and unemployment is unacceptably high. Obviously, when we harvest logs and put them in a boat, the area is denied all the economic benefits that come with processing -- jobs, capital investment, tax base, etc.

Our government should have a resource policy to insure that a fair share of these economic benefits stay at home. Until then, the alternatives are to restrict log exports (at least from public lands) or convince the Chinese to buy a mix of finished products and logs.

When I first came to Congress and faced a similar problem with Japan, I called for a log export ban. I am currently working on a different tack -- trying to increase exports of finished products to China, Japan and other Pacific Rim nations.

In July, I led a trade delegation of roughly 15 representatives of the wood products industry to China. We met with over 20 top Chinese officials in the many agencies involved in wood products trade, forestry, and housing in that nation. Our goal was to continue to urge the PRC to start buying more finished products, even as they continue to enjoy our logs.

While China's economic and employment needs are major hurdles to increased imports of finished products, our trade mission was greeted with great interest. As a follow-up to our visit, two demonstration homes will be shipped to China and constructed in the cities of Beijing and Dalian later this year. One project will be supported by U.S. government funding, the other will be wholly paid for by the U.S. wood products industry.

These demonstration units have generated a high degree of interest from both the national and local governments in China. I am very hopeful that the contacts established on the trade mission, the follow-up work centered upon the demonstation projects, and the continuing effort by industry, will result in a major new market for U.S. manufacturers.

<u>**Fifth, trade promotion is essential if we are to achieve our potential in world markets.**</u> I know American companies, individually and collectively, have made a major investment in this regard. However, more needs to be done and government has a definite role to play.

Let me cite the example of South America. The housing demands there are enormous, totaling 20 to 30 million units through the end of the century. Presently, the use of wood in home construction is almost non-existent.

Last year, Secretary of Commerce Malcolm Baldrige and I hosted a breakfast with South American Ambassadors and invited their countries to participate in a three-day wood housing seminar in Seattle. The response was overwhelming. Over 60 ministers and other officials from Latin America and the Caribbean participated. At the seminar they learned, many for the first time, about the economy, efficiency, and durability of using wood and U.S. housing technology.

Following the conference, we got the State Department to provide $350,000 to fund a number of demonstration projects in six key Latin American countries. The wood and accompanying materials have been shipped to many of these countries, and several projects have been completed. In nearly all of the nations involved, there has been enthusiastic support from the local government.

Throughout this project, we have heard that a number of problems, including a long-standing stigma against wood housing and the lack of financing, would defeat this initiative. The experience in Peru has been particularly heartening -- when the 15 demonstration projects were completed and offered for sale to the public recently, some 2400 families applied to purchase them! I will be working in the months ahead with both industry and our governmental aid agencies to develop appropriate financing opportunities.

I can see only two answers to the current furor over trade issue. Our nation can either export more or resort to protectionist measures.

This kind of bold government/private sector initiative is essential if we are to develop new markets for our nation's wood products. I learned recently of an exhibit in Peking, sponsored by the European Community, that was a big hit with the Chinese. Our government can and must do more to work with industry to see that we maintain our competitive position.

As the Chairman knows, every major newspaper in the Pacific Northwest has carried extensive articles on the state of the timber and wood products industry. It has become a sad commentary on what was once a vibrant enterprise in the region. But unlike the late 1960s, nobody is about to "turn off the light". There is considerable hope for the future; after all, we are talking about an abundant, renewable resource much in demand in today's world.

The resource has not changed, but the times and the markets have. We are now in a global community where the rules are different. That is why it is important for government, industry, and labor to put aside their adversarial impulses and begin working together to insure that this industry stays competitive.

Mr. Chairman, I want to thank you for giving me this time to testify, and I look forward to working with you on these issues of mutual concern.

The CHAIRMAN. Senator Baucus.

Senator BAUCUS. I would just like to thank each of you three. You have been working very hard on this and providing a lot of the initial work in this area, and I want to thank you for your efforts.

The CHAIRMAN. Steve.

Senator SYMMS. I echo the statement of Senator Baucus. I welcome all three of you here, and I think I have asked enough questions. So thank you very much, Don.

The CHAIRMAN. Gentlemen, thank you very much for coming over. We appreciate it.

Now if we can take a panel consisting of: Commissioner Paula Stern, the Chair of the International Trade Commission; Ambassador Michael Smith, Deputy U.S. Trade Representative; and the Honorable Daniel Amstutz, the Under Secretary for International Affairs and Commodity Programs, U.S. Department of Agriculture.

We are delighted to have you with us. We would very much appreciate it if you would follow the admirable example of the Congressmen. We will put your entire statement in the record. Please give us an abbreviated oral statement.

Ms. Stern, go right ahead.

STATEMENT OF COMMISSIONER PAULA STERN, CHAIRWOMAN, U.S. INTERNATIONAL TRADE COMMISSION, WASHINGTON, DC

Commissioner STERN. Thank you very much, Chairman Packwood. It's a pleasure to be here this afternoon, and I will try to follow that example and also give you as good a set of answers as the Congressmen seemed to have given to you this afternoon.

I thank you for the opportunity to testify. My prepared remarks, which we have submitted for the record, break down into three areas. First, the overall trade figures for the forest products industry; second, the Canadian softwood lumber import question; and then, third, the forest product exports to Japan.

For purposes of this summary, I will go directly to the Canadian imports, which seems to be one of the most contentious issues in the forest products trade area today.

The Commission is now updating our 1982 study which we made on the softwood lumber industry. That study was submitted to the Congress, specifically at the request of your committee, back in 1982. And our efforts to update should be completed by next month, and we will be delivering that study to the President's trade representative.

Recent trends in the industry show that sales of softwood lumber were responding to the increase in housing starts that we have seen over the last 2 years. Domestic production and imports have both risen. The import penetration rate has increased by 1½ percentage points in the last 3 years to just over 30 percent in 1984. And Canada supplies 99 percent of the imports into the United States.

At the center of the softwood lumber controversy with Canada seems to be the so-called stumpage issue. As you know, it was part of the Department of Commerce's countervailing duty investigation. The domestic industry argued the Canadian stumpage pricing practices were constituting a countervailable subsidy. But the Department of Commerce found ultimately that the Canadian stumpage programs were not countervailable. So that even though the International Trade Commission, an independent agency, had found on a preliminary basis that there was a reasonable indication of material injury or threat of material injury to the domestic industry, as a result of the Department of Commerce's negative decision, the case that was pending at the International Trade Commission was terminated.

Now as part of our current section 332 investigation updating that 1982 study, the Commission is again examining the facts surrounding the stumpage issue. Other factors of production we are looking at include comparing the differences in the other costs of production between the United States and Canada. A few of the most important factors are transportation costs, logging costs, wages, different tax systems, and the exchange rate differential.

I see since I have the yellow light I will not go into the details on these particular factors of competition. There are results which I think are very revealing in our 1982 study which go into differences in costs, particularly as far as transportation is concerned. And I would simply say that since 1982, the strength of the U.S. dollar vis-a-vis the Canadian dollar has amounted to 11.5 percent advantage for the Canadian producer. And that's even when relative inflation rates are taken into account. I will refer you to my table 6 of my full testimony, which demonstrates that increasing differential to the advantage of the Canadians.

I now turn from the Canadian imports to Japan and exports. Most of Japan's wood product imports are relatively raw, unprocessed goods. The import penetration rate in Japan has remained relatively low throughout the years. Several factors may account for this, including their tariffs that advance sharply by stage or processing, the technical requirements that they have, a cumbersome government standard certification system——

The CHAIRMAN. I'm going to have to ask you to conclude.

Commissioner STERN [continuing]. And cartels.

I will conclude at this point, and invite you to ask any questions which you may have on any of these conditions of competition which I mentioned as regards our domestic industry as it faces the export market and the import penetration.

The CHAIRMAN. Thank you.

[The prepared written statement of Commissioner Stern follows:]

STATEMENT OF DR PAULA STERN, CHAIRWOMAN, U.S. INTERNATIONAL TRADE COMMISSION

TRENDS IN THE INTERNATIONAL COMPETITIVENESS OF THE U.S. FOREST PRODUCTS INDUSTRY

Mr. Chairman, thank you very much for the opportunity to testify today. The Commission is well-aquainted with the plight of the forest products industry, and I hope I will be able to shed some light on recent trends in the competitiveness of that industry. Accompanying me today is David Ingersoll, the chief of our agriculture division at the Commission.

I would like to divide my remarks into three areas: first, I will present overall trade figures for the forest products industry. Second, I will focus on trends in the importation of Canadian softwood lumber. Since this is the issue with which the Commission is most familiar, most of my testimony will be devoted to exploring recent import and production trends involving softwood lumber. Third, I will offer some background information on the issue of forest product exports to Japan. While we at the Commission spend less time on export issues than on import-related concerns, I think we have some figures that will be of interest to you.

Overview of the Forest Products Sector

Table 1 provides detailed data on recent trade flows in the forest products industry. This table uses the broadest definition of the forest products industry, which includes both wood and paper products. I would like to highlight a few of these figures for you.

Forest products, like most industrial sectors, saw its trade balance erode significantly in 1984, when it registered a deficit of $4.6 billion. This represents an 80 percent deterioration from the 1983 deficit of $2.5 billion. Since exports increased only slightly in 1984, a 22 percent jump in imports accounts for the larger trade deficit.

This trend continued in the first half of 1985, when the forest products deficit reached $2.7 billion, compared with just under $2.0 billion in the first six months of 1984.

Shifting to bilateral trade figures, the major markets for U.S. exports are the European Community and Japan, each of which took 21 percent of our foreign sales, and Canada, which received 19 percent of our exports.

In contrast to this relatively even distribution of exports, imports came predominantly form Canada, which supplied 72 percent of all forest product imports in 1984.

Thus, trade with Canada swamped all other bilateral trade accounts. In 1984, we ran a $7.8 billion deficit with Canada, up from $6.6 billion in 1983 and $5.6 billion in 1982. The U.S. has consistently run surpluses in recent years with Japan and the EC.

Canadian Softwood Lumber Imports

Past Investigations

The most contentious issue involving forest products trade relates to Canadian softwood lumber imports. This issue first came to the Commission's attention in 1982, when at the request of this committee we completed a study entitled Conditions Relating to the Importation of Softwood Lumber Into the United States (No. 332-134). This study examined all relevant aspects of the competitive status of the Canadian and U.S. industries, including the importance of government policies.

On October 7, 1982, a petition was filed with the Commission and the Department of Commerce on behalf of the United States Coalition for Fair Canadian Lumber Imports, a group of eight trade associations and more than 350 domestic producers of softwood lumber products, alleging that imports of softwood lumber from Canada were being subsidized by the Government of Canada. On that date, the Commission instituted a preliminary countervailing duty investigation to determine whether there is a reasonable indication that an industry in the United States is materially injured, or threatened with material injury, or the establishment of an industry in the United States is materially retarded, by reason of imports of softwood lumber from Canada. In that preliminary countervailing duty investigation, the Commission determined in November 1982 that there was a reasonable indication that an industry in the United States is materially injured by reason of such imports.

Following the Commission's determination, the Department of Commerce conducted its preliminary and final investigations, in order to determine whether U.S. imports of softwood lumber from Canada receive benefits which constitute bounties or grants within the meaning of the countervailing duty law.

On May 24, 1983, the Department of Commerce determined that the total estimated net subsidy for softwood lumber was de minimis (in this case the level was determined to be 0.349 percent). Therefore, its final determination was negative. Our investigation was terminated, and we did not make a final injury determination.

Since the final Commerce determination in May, 1983, no petitions for countervailing duty or antidumping investigations of imports of softwood lumber have been received by the Commission. However, at the request of the U.S. Trade Representative's Office, the Commission is now updating our 1982 study of softwood lumber imports. The views of interest parties were heard at a public hearing on July 23, and we expect to deliver our final report to the USTR in early October.

Although the Commission is still working on the study, I can share with you data from official sources and public submissions to our investigation, as well as my own observations on recent trends in the industry. These figures are not necessarily those that will be contained in the final version of the Commission's study.

Recent trends

Turning to recent trends in the industry, U.S. softwood lumber consumption, according to industry sources, rose from 31.2 billion board feet in 1982 to 42.7 billion board feet in 1984. The increase in consumption was certainly fueled by a rise in the number of U.S. housing starts during the period. New home construction is a major user of softwood lumber. Therefore, the rise in U.S. housing starts from 1.1 million units in 1982 to 1.7 million units in 1983 and 1984 was an important factor in the increase in consumption of lumber.

U.S. production of softwood lumber rose during 1982-84 in response to the increased demand. According to data published by the National Forest Products Association, production rose from 23.8 billion board feet in 1982 to 31.3 billion board feet in 1984, or by almost one-third.

U.S. exports of softwood lumber showed little change during the 1982-84 period, increasing from 1.6 billion board feet to 1.8 billion board feet in 1983, before dropping to just below 1.6 billion board feet in 1984. The ratio of U.S. softwood lumber exports to U.S. production has been relatively low, averaging about 6 percent during 1982-84, but showing a downward trend. In 1984, the leading markets for such U.S. exports were Japan, receiving 34 percent in terms of quantity of U.S. exports, Canada, receiving 21 percent, and Australia, receiving 12 percent.

Also in response to the increased demand for softwood lumber, U.S. imports rose from 9.0 billion board feet, valued at $1.6 billion, in 1982 to 13.0 billion board feet, valued at just under $2.6 billion, in 1984. Imports have claimed a gradually increasing share of the U.S. market for softwood lumber. In 1984, just over 30 percent of the domestic market was supplied by imports, compared to just under 29 percent in 1982.

It should be noted that all imports of softwood lumber enter the United States duty-free. Canada historically has been the leading foreign supplier to the U.S. softwood lumber market, supplying over 99 percent, in terms of both quantity and value, of total U.S. softwood lumber imports.

<u>Stumpage</u>

At the center of the softwood lumber controversy is the charge by the U.S. industry that the Canadian forest products industry is allowed to cut timber on government-owned lands at a fraction of the timber's actual market value. This is the so-called stumpage issue. The Commission found in 1982 that the appraisal systems used for sales of timber from Government lands in the United States and Canada are similar. Both are based on a residual system in which costs of converting the standing timber to final products, plus an allowance for profit and risk, are deducted from a price determined for the final products, resulting in an appraised price for the standing timber. A major distinction between the two systems is that in the United States federally owned timber may be bid up at public auction to a level above the appraised value; however, in Canada timber is offered and usually sold at the appraised price.

As part of the Department of Commerce's countervailing duty investigation on softwood lumber in 1982, the domestic industry argued that Canadian stumpage pricing practices constituted countervailable subsidies. The industry contended that in 1980 these practices provided a subsidy equal to 65 percent of the value of U.S. imports. However, in its final determination the Department of Commerce found that the Canadian stumpage programs are not countervailable. The Department of Commerce determined that "Stumpage programs do not confer an export subsidy because they do not operate and are not intended to stimulate export rather than domestic sales and because they are not offered contingent upon export performance. The mere fact that significant quantities of products made from stumpage are exported to the United States does not mean that stumpage programs confer an export subsidy." Furthermore, Commerce determined that "stumpage programs are not provided only to a 'specific enterprise or industry, or group of enterprises or industries.' Rather, they are available within Canada on similar terms regardless of the industry or enterprise of the recipient." As part of our current section 332 investigation, the Commission is again examining the facts surrounding the stumpage issue.

Other factors of competition

The Commission not only is investigating stumpage but also is examining and comparing the other costs of production between the United States and Canada. A few of the most important factors are transportation costs, logging costs, wages, different tax systems and the exchange rate differential. For example, in the Commission's 1982 study, we found that Canadian shippers have lower costs for rail and water transport than U.S. lumber shippers to many U.S. markets. Purchasers in Richmond, Virginia can in fact buy softwood lumber form British Columbia for less than lumber from our Pacific Northwest. While part of the reason for this disadvantage to U.S. shippers--the Jones Act--continues to affect U.S. waterborne transport. In 1982 we concluded that recent changes in U.S. freight regulations might ultimately lead to more competitive U.S. rates.

Similarly, in our 1982 study we found that logging costs and wages are generally lower in Canada than in the United States. While there are clear differences in U.S. and Canadian tax systems, in 1982 we did not find them to have a significant effect on the competitive position of the two industries.

The strength of the U.S. dollar vis a vis the Canadian dollar since 1982--one fact in our ongoing study which is not confidential--has amounted to an 11.5 percent advantage for Canadian products, even when relative inflation rates are taken into account. I refer you to Table 6 of my testimony.

U.S. Exports to Japan

Japan is the single largest market in the world for forest products, importing more than $4.5 billion worth of wood and wood products in 1984 and $1.7 billion of pulp and paper. Despite Japan's significant import purchases, indications are that foreign suppliers account for less than one-fourth of Japanese consumption of wood and wood products and less than 5 percent of its market for pulp and paper products. Furthermore, most of Japan's wood product imports are of raw or relatively unprocessed goods. More than two-thirds of Japan's wood imports are logs, and about 95 percent of its imports are relatively unprocessed products such as lumber and wood chips. Nearly three-fifths of its paper and pulp imports are in the form of pulp.

The import penetration rate in Japan has remained relatively low. Several factors may account for this, including tariffs that advance sharply by stage of processing, technical requirements, a cumbersome government standards certification system, and informal cartels.

Japan is still the United States' best customer for wood products. In 1984, the United States sold Japan more than $600 million worth of logs, and about $336 million of wood pulp for papermaking. Even so, the U.S. share of the Japanese market for wood products was only about 6 percent in 1984, and U.S. suppliers accounted for less than 2 percent of the pulp and paper consumed in Japan. Though U.S. suppliers have held their own in Japan's market for raw or relatively unprocessed wood and paper, they have yet to make inroads in the market for more processed products such as plywood, particle board, panel products, and kraft linerboard.

To grasp the problem the U.S. faces with Japan, one needs to look no further than our national pastime. While the U.S. pushed for years to open up Japan's market for U.S. aluminum softball bats, a Japanese product played a role in perhaps the biggest baseball event of the year. It turns out that Pete Rose, who broke the all-time hit record just last week, uses baseball bats manufactured in Japan. Pete may not have realized just how close to the truth he might have been when he said that, for all he knew, the wood may have come from the U.S.

Recently, the United States and Japan have been conducting a series of in-depth negotiations on the forest products sector as part of the overall sector-specific talks initiated in early 1985. The main U.S. concerns are Japan's high tariffs on plywood, veneer, panel products, and kraft linerboard. Tariffs range from 3.9 percent on newsprint, to 7 percent on kraft linerboard, 15 percent on veneer, and 20 percent on plywood. Technical standards have also posed a problem for U.S. suppliers, particularly those on plywood and panel products. Japan has recently taken some steps to address U.S. concerns about particular technical standards, and announced in late July that it would make it easier for foreign suppliers to obtain certification that their products conform with these requirements.

Japan's restrictions on forest product imports have been a key bilateral issue for many years. The Japanese Government has in the past heavily protected its forest products market from foreign competition, mainly by applying high tariffs to processed products. After near-continual U.S. prodding and consistent efforts by the U.S. industry, the Japanese Government committed itself in April of this year to the gradual opening of its forest products sector. Tariffs and other restrictions are to be slowly eased starting on April 1, 1987. In the meantime, the Japanese Government is setting up a 3-year adjustment program for the industry so that it will be better able to meet the import challenge.

This concludes my presentation. again, the Commission will have much more to say on the softwood lumber question in just a few weeks when we deliver our report to the USTR. We will see that you have it as soon as possible. I would be pleased to answer any questions you may have.

Table 1.--Forest products: U.S. exports of domestic merchandise, imports for consumption, and merchandise trade balance, by leading import sources, 1980-84, January-June 1984, and January-June 1985 1/

(In thousands of dollars)

Item	1980	1981	1982	1983	1984	January-June	
						1984	1985
U.S. exports of domestic merchandise:							
Canada	1,336,847	1,583,437	1,395,589	1,558,091	1,655,283	821,921	788,495
Taiwan	100,452	101,747	105,338	157,621	199,060	104,364	97,381
United Kingdom	506,718	536,316	468,846	503,149	498,691	260,606	202,172
Japan	2,584,615	1,901,365	1,869,305	1,752,774	1,749,833	924,227	860,486
Mexico	570,620	625,648	527,138	457,239	523,452	252,729	272,368
Finland	7,229	7,784	15,704	17,115	9,516	6,359	2,727
Brazil	43,365	41,993	38,687	40,394	40,902	18,403	19,706
West Germany	577,810	527,776	470,204	503,806	450,775	246,694	199,566
Sweden	55,165	73,127	32,687	19,537	18,946	10,020	8,460
Italy	441,882	290,780	243,147	249,752	247,728	140,099	110,580
All other	3,384,085	3,527,604	3,315,434	3,098,888	3,191,302	1,590,326	1,519,937
Total	9,608,788	9,217,577	8,482,079	8,358,366	8,585,488	4,375,748	4,081,878
U.S. imports for consumption:							
Canada	7,121,189	7,378,796	6,949,123	8,162,564	9,490,139	4,650,328	4,857,762
Taiwan	291,718	320,372	282,519	389,580	461,750	208,357	206,049
United Kingdom	233,857	202,394	193,024	209,295	307,259	155,871	133,021
Japan	181,046	200,700	182,992	222,477	279,913	134,862	153,250
Mexico	161,548	190,058	204,325	239,175	271,201	141,342	129,290
Finland	106,759	86,174	74,371	149,237	260,653	141,696	165,697
Brazil	109,174	145,830	115,928	140,102	254,027	132,505	101,458
West Germany	65,270	74,462	87,694	134,969	248,548	105,067	125,775
Sweden	51,170	41,741	66,405	95,194	218,056	84,892	109,664
Italy	61,570	52,700	54,080	63,083	178,261	58,187	113,145
All other	868,556	953,975	810,151	1,002,733	1,261,352	557,476	673,137
Total	9,251,857	9,647,202	9,020,612	10,808,406	13,231,159	6,370,583	6,768,248
U.S. merchandise trade balance:							
Canada	-5,784,341	-5,795,359	-5,553,533	-6,604,472	-7,834,855	-3,828,407	-4,069,267
Taiwan	-191,265	-218,624	-177,179	-231,959	-262,690	-103,993	-108,668
United Kingdom	272,861	333,922	275,822	293,854	191,432	104,735	69,151
Japan	2,403,570	1,700,665	1,686,313	1,531,297	1,469,920	789,365	707,236
Mexico	409,072	435,590	322,812	218,064	252,251	111,387	143,078
Finland	99,530	-78,390	-58,667	-132,122	-251,137	-135,337	-162,970
Brazil	65,808	-103,836	-77,240	-99,706	-213,124	-114,102	-81,752
West Germany	512,540	453,314	382,510	368,837	202,227	141,627	73,791
Sweden	3,995	31,386	-33,718	-75,657	-199,110	-74,872	-101,204
Italy	380,312	238,080	189,067	186,669	69,467	81,912	-2,565
All other	2,515,529	2,573,629	2,505,283	2,096,155	1,929,950	1,032,850	846,800
Total	356,931	-429,624	-538,532	-2,450,039	-4,645,670	-1,994,835	-2,686,370

1/ Import values are based on Customs value; export values are based on f.a.s. value, U.S. port of export.

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Table 2.--Softwood lumber: U.S. exports of domestic merchandise, imports for consumption, and merchandise trade balance, by leading import sources, 1980-84, January-June 1984, and January-June 1985 1/

(In thousands of dollars)

Item	1980	1981	1982	1983	1984	January-June 1984	January-June 1985
U.S. exports of domestic merchandise:							
Canada	101,383	123,043	63,302	104,319	78,736	45,790	36,617
Mexico	33,546	43,841	25,097	12,943	21,746	8,920	11,765
Chile	175	202	1,016	64	54	16	19
Brazil	-	10	-	28	-	-	-
Honduras	16	18	18	1	1	1	-
Indonesia	-	7	8	-	-	-	-
Ghana	-	26	22	4	4	-	-
United Kingdom	21,533	14,661	15,576	23,378	15,850	8,310	6,582
Finland	107	71	64	70	127	66	32
New Zealand	809	678	978	706	1,237	693	379
All other	619,278	470,010	468,757	459,346	411,651	218,232	192,661
Total	776,847	652,567	574,836	600,859	592,406	281,947	248,055
U.S. imports for consumption:							
Canada	1,753,493	1,685,927	1,559,129	2,451,903	2,539,543	1,272,178	1,353,876
Mexico	801	950	559	3,056	2,731	1,491	1,027
Chile	-	10	-	312	2,042	988	2,635
Brazil	1,607	2,088	2,187	1,349	1,734	826	692
Honduras	3,674	4,055	2,628	2,575	1,444	830	745
Indonesia	-	-	-	191	845	446	5
Ghana	-	-	501	234	842	-	121
United Kingdom	549	76	12	10	651	4	127
Finland	-	-	41	-	545	-	-
New Zealand	890	781	687	445	405	188	457
All other	1,463	1,015	833	813	1,753	531	1,362
Total	1,762,477	1,694,902	1,566,577	2,460,788	2,552,526	1,277,482	1,361,047
U.S. merchandise trade balance:							
Canada	-1,652,110	-1,562,884	-1,495,827	-2,347,584	-2,460,798	-1,226,469	-1,317,259
Mexico	32,745	42,891	24,538	9,887	19,015	7,429	10,738
Chile	175	192	1,016	-248	-1,988	-972	-2,616
Brazil	-1,607	-2,078	-2,187	-1,321	-1,734	-826	-692
Honduras	-3,658	-4,073	-2,610	-2,574	-1,443	-829	-745
Indonesia	-	7	8	-191	-845	-446	-5
Ghana	-	26	-479	-230	-838	-	-121
United Kingdom	20,984	14,585	15,564	23,368	15,199	8,306	6,455
Finland	107	71	23	70	-418	66	32
New Zealand	-81	-103	291	261	832	505	-78
All other	617,815	468,995	467,924	458,533	409,898	217,701	191,299
Total	-985,630	-1,042,335	-991,739	-1,859,929	-2,023,120	-995,535	-1,112,992

1/ Import values are based on Customs value; export values are based on f.a.s. value, U.S. port of export.

Source: Compiled from official statistics of the U.S. Department of Commerce

Table 3.--Softwood lumber: U.S. exports of domestic merchandise, by principal market, 1980-84, January-June 1984, and January-June 1985

Market	1980	1981	1982	1983	1984	January-June 1984	January-June 1985
	Quantity (million board feet)						
Japan	634	506	610	594	545	268	286
Canada	364	495	254	425	331	186	145
Australia	90	123	102	141	184	103	89
Italy	186	88	83	120	89	55	43
Mexico	180	199	100	53	91	40	43
United Kingdom	53	32	36	52	33	17	15
West Germany	71	49	44	45	28	17	8
Spain	46	16	30	29	29	15	11
Trinidad and Tobago	20	24	28	26	19	10	6
China	1/	36	15	20	34	11	17
All other	323	327	313	328	203	103	92
Total	1,967	1,895	1,615	1,833	1,586	825	755
	Value (1,000 dollars)						
Japan	221,360	175,960	194,662	183,053	162,253	80,538	84,590
Canada	101,383	123,043	63,302	104,319	78,736	45,709	36,617
Australia	36,991	47,727	38,220	50,516	62,054	35,675	30,396
Italy	138,627	55,447	51,380	71,134	53,216	33,609	23,734
Mexico	33,546	43,841	25,097	12,943	21,746	8,920	11,765
United Kingdom	21,533	14,661	15,576	23,378	15,850	8,310	6,582
West Germany	42,417	27,966	24,390	22,989	14,978	9,120	4,730
Spain	30,767	8,962	17,058	15,893	14,772	7,959	6,062
Trinidad and Tobago	8,592	11,479	12,499	12,475	9,008	4,914	2,834
China	5	9,470	4,986	6,457	8,942	2,725	4,402
All other	141,626	134,011	127,668	97,702	150,851	44,468	36,343
Total	776,847	652,567	574,838	600,859	592,406	281,947	248,055
	Unit value (per thousand board feet)						
Japan	$349.22	$347.45	$318.87	$307.92	$297.85	2/ $300.51	2/ $295.77
Canada	278.88	248.35	249.62	245.70	237.99	2/ 245.75	2/ 252.53
Australia	409.16	389.34	373.18	357.38	337.32	2/ 346.36	2/ 341.53
Italy	745.11	627.67	617.71	595.04	600.16	2/ 611.07	2/ 551.95
Mexico	186.59	220.65	250.43	243.81	239.12	2/ 223.00	2/ 273.60
United Kingdom	404.37	455.63	436.45	447.70	474.60	2/ 488.82	2/ 438.80
West Germany	599.78	569.65	548.59	514.28	532.79	2/ 536.47	2/ 591.25
Spain	633.03	570.52	564.25	546.63	513.02	2/ 530.60	2/ 551.09
Trinidad and Tobago	436.79	480.61	442.37	484.97	479.13	2/ 491.40	2/ 472.33
China	283.84	260.86	323.31	328.50	261.08	2/ 247.73	2/ 258.94
All other	438.47	409.82	407.88	297.87	743.11	2/ 431.73	2/ 395.03
Total	394.97	344.34	355.84	327.81	333.76	2/ 341.75	2/ 328.55

1/ Less than 500,000 board feet.
2/ Based on rounded figures.

Source: Compiled from official statistics of the U.S. Department of Commerce.

Table 4.--Softwood lumber: U.S. imports for consumption, by principal sources, 1980-84, January-June 1984, and January-June 1985

Market	1980	1981	1982	1983	1984	January-June	
						1984	1985
	Quantity (million board feet)						
Canada	9,359	9,008	8,943	11,708	12,947	6,190	7,115
Mexico	2	1	1	12	12	7	5
Chile	0	1/	0	2	11	6	14
Brazil	2	3	3	2	3	1	3
Honduras	11	10	8	8	5	2	3
Indonesia	0	0	0	1/	1	1/	1/
Ghana	0	0	8	1	3	0	5
United Kingdom	2	1/	1/	1/	2	1/	1
Finland	0	0	1/	0	3	0	0
New Zealand	2	1	3	3	2	1	3
All Other	5	6	3	1	6	3	6
Total	9,383	9,029	8,969	11,737	12,995	6,210	7,155
	Value (1,000 dollars)						
Canada	1,753,493	1,685,927	1,559,129	2,451,903	2,539,534	1,272,178	1,353,876
Mexico	801	950	559	3,056	2,731	1,491	1,027
Chile	-	10	1	312	2,042	988	2,635
Brazil	1,607	2,088	2,187	1,349	1,734	826	692
Honduras	3,674	4,055	2,628	2,575	1,444	830	745
Indonesia	-	-	-	191	845	446	5
Ghana	-	-	501	234	842	-	121
United Kingdom	549	76	12	10	651	4	127
Finland	-	-	41	-	545	-	-
New Zealand	890	781	687	445	405	188	457
All Other	1,463	1,015	833	813	1,753	531	1,362
Total	1,762,477	1,694,902	1,566,577	2,460,788	2,552,526	1,277,482	1,361,047
	Unit value (per thousand board feet)						
Canada	$187.35	$178.17	$174.34	$209.43	$196.15	2/$205.52	$190.28
Mexico	451.74	707.26	488.12	256.44	232.72	2/ 213.00	190.05
Chile	-	377.24	-	141.94	181.61	2/ 165.00	188.90
Brazil	718.69	828.75	663.49	758.55	497.07	2/ 826.00	232.55
Honduras	346.60	406.06	314.48	331.34	315.31	2/ 415.00	293.40
Indonesia	-	-	-	608.94	610.26	2/ 223.00	196.96
Ghana	-	-	63.96	178.18	272.46	-	25.24
United Kingdom	221.73	185.22	247.82	224.07	272.23	3/	203.61
Finland	-	-	501.51	-	179.99	-	-
New Zealand	474.02	579.91	199.20	176.99	263.94	2/ 188.00	171.78
All Other	292.60	169.17	277.67	813.00	292.17	2/ 177.00	2/ 227.00
Total	187.84	187.72	174.66	209.65	196.42	2/ 205.00	190.23

1/ Less than 500,000 board feet.
2/ Based on rounded figures.
3/ Not meaningful when based on rounded figures.

Source: Compiled from official statistics of the U.S. Department of Commerce.

Table 5.--Softwood lumber: U.S. production, exports of domestic merchandise, imports for consumption, and apparent consumption, 1980-84, January-June 1984 and January-June 1985.

(Quantity in million board feet; value in millions of dollars; unit value per thousand board feet)

Year	Production 1/	Exports	Imports	Apparent consumption	Ratio (percent) of imports to apparent consumption
			Quantity		
1980	26,200	1,967	9,383	33,600	27.9
1981	24,700	1,895	9,029	31,800	28.4
1982	23,800	1,615	8,969	31,200	28.7
1983	29,800	1,833	11,737	39,700	29.6
1984	31,300	1,586	12,995	42,700	30.4
Jan.-June--					
1984	2/	825	6,210	2/	2/
1985	2/	755	7,155	2/	2/
			Value		
1980	2/	777	1,762	2/	2/
1981	2/	653	1,695	2/	2/
1982	2/	575	1,567	2/	2/
1983	2/	601	2,461	2/	2/
1984	2/	592	2,553	2/	2/
Jan.-June--					
1984	2/	282	1,277	2/	2/
1985	2/	248	1,361	2/	2/
			Unit value		
1980	-	$394.97	$187.84	-	-
1981	-	344.34	187.72	-	-
1982	-	355.84	174.66	-	-
1983	-	327.81	209.65	-	-
1984	-	333.76	196.42	-	-
Jan.-June--					
1984	-	341.75	3/ 205.71	-	-
1985	-	328.55	190.23	-	-

1/ Data published by the National Forest Products Association.
2/ Not available.
3/ Based on rounded figures.

Source: Compiled from official statistics of the U.S. Department of Commerce, except as noted.

TABLE 6.--Exchange rates, Canadian dollars per U.S. dollars, by quarters, 1977-84

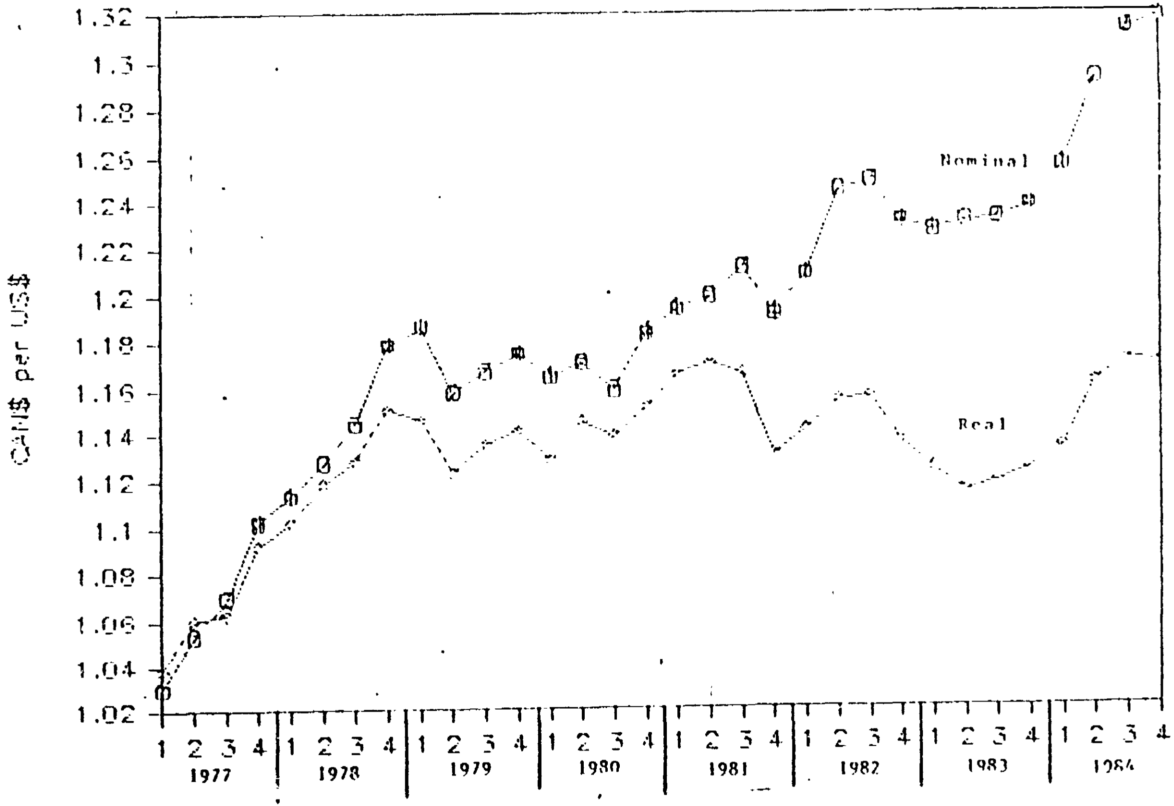


Table 7.--Japan's production, exports, imports, import penetration, and employment in the forest products sector, 1980-84.

	Value of Shipments	Total Exports	Total Imports	Apparent Consumption	Import Penetration 1/	Employ-ment
			Billion yen		Percent	Thousand
Pulp and Paper: 2/						
1980---------	6,751	250	415	6,916	6.0	279
1981---------	6,826	253	340	6,913	4.9	252
1982---------	7,774	268	386	7,892	4.9	250
1983---------	8,152	267	388	8,273	4.7	243
1984 3/------	8,562	310	422	8,674	4.8	n.a.
			Billion dollars			
1984--------	34.6	1.2	1.7	34.7		
Lumber and Wood Products: 4/						
1980---------	5,327	39	1,881	7,169	26.2	362
1981---------	4,485	37	1,182	5,630	21.0	333
1982---------	4,346	31	1,331	5,646	23.6	313
1983---------	4,186	34	1,108	5,260	21.1	301
1984 3/------	4,014	32	1,128	5,110	22.1	n.a.
			Billion dollars			
1984--------	16.1	0.1	4.5	20.4		

1/ Import penetration is the ratio of shipments to apparent consumption. Apparent consumption is here defined as shipments, minus exports, plus imports.
2/ Here defined as CCCN Nos. 47, 48, and 49.
3/ Estimated.
4/ Here defined as CCCN No. 44.

Sources: The Bank of Japan, Economic Statistics Annual, 1984 (Census of Manufactures and Indexes of Producer's Shipments by Ministry of International Trade and Industry), pp. 273-74 and 285-286; Japan Tariff Association, Japan's Exports & Imports, December issues.

Table 8.--U.S. exports of forest products to Japan, 1979 and 1982-84.

	1979		1982		1983		1984	
	Million dollars	% of Total	Million dollars	% of Total	Million dollars	% of Total	Million dollars	% of Total
Wood products:								
Softwood logs--------	1,468	75.5	829	64.9	689	63.8	631	61.8
Wood chips-----------	180	9.3	207	16.2	157	14.5	157	15.4
Softwood lumber------	254	13.1	195	15.3	183	16.9	162	15.9
Hardwood lumber------	5	- .2	11	.8	19	1.8	36	3.5
Hardwood logs--------	15	.8	8	.6	7	.6	9	.9
Softwood veneer------	-	-	2	.2	2	.2	2	.2
Softwood plywood-----	2	.1	2	.2	2	.2	2	.2
Poles, piles, posts--	2	.1	1	.2	-	.1	1	.1
Hardwood flooring----	1	-	1	.1	1	.1	2	.2
Hardwood veneer------	1	-	1	.1	1	.1	-	-
Particleboard--------	2	.1	1	.1	1	.1	1	.1
Total--------------	1,945	100.0	1,277	100.0	1,080	100.0	1,021	100.0

Source: Forest Products Division, Foreign Agricultural Service, U.S. Department of Agriculture, based on official U.S. Department of Commerce data.

Table 9.--Japanese tariffs on particular forest products.

	Japanese Final MTN Tariff Rate (1987)
Wood products:	
Unfinished pine lumber	6.0
Medium density fibreboard	6.5
Finished pine lumber	10.0
Veneer	15.0
Plywood	15.0-20.0
Particleboard	10.0-12.0
Mouldings	7.2
Builders carpentry and joinery	4.9
Paper products:	
Kraft linerboard	5.0-7.0
Solid bleached board	5.0-7.0
Other kraft paper	7.0
Other paper	6.5-7.0
Newsprint	3.9-4.1

Table 10.--Japan's imports of particular forest products, all sources, 1982-84

CCCN No.		1982 Billion yen	1982 % of Total	1983 Billion yen	1983 % of Total	1984 Billion yen	1984 % of Total
	Total, wood and articles of wood------	1,331	100.0	1,108	100.0	1,128	100.0
44.03	Wood in the rough-------	899	67.5	723	65.3	735	65.2
44.05	Wood, sawn lengthwise, but not further prepared.	178	13.4	149	13.4	139	12.3
44.09	Hoopwood; split poles, not sawn lengthwise; chipwood, drawnwood; pulpwood in chips or particles; wood shavings and sticks.	160	12.0	144	13.0	154	13.7
44.13	Wood, planed, tongued grooved, rebated, etc. but not further manufactured.	45	3.3	48	4.3	49	4.3
44.14	Wood sawn lengthwise, sliced or peeled, but not further prepared, of a thickness not exceeding 5 mm, veneer for plywood.	8	0.6	8	0.7	9	0.8
44.15	Plywood, blockboard, laminboard, battenboard, and similar laminated wood products.	3	0.2	3	0.3	7	0.6
44.23	Builders carpentry and joinery.	8	0.6	8	0.7	9	0.8
	Total, papermaking material and paper----	386	100.0	388	100.0	422	100.0
	Pulp and waste paper------	213	55.2	221	57.0	249	59.0
	Paper and paperboard------	126	32 6	124	32.0	129	30.6

Source: Japan Tariff Association, *Japan's Exports and Imports*, Commodity by Country, December issues.

STATEMENT OF AMBASSADOR MICHAEL SMITH, DEPUTY U.S. TRADE REPRESENTATIVE, WASHINGTON, DC

The CHAIRMAN. Mr. Ambassador.

Ambassador SMITH. Thank you, Mr. Chairman, for this opportunity to appear before you and your colleagues regarding the current state of the U.S. softwood lumber industry.

As Under Secretary Amstutz, as well as Chairwoman Stern, are here—and I understand Under Secretary Amstutz will be focusing largely on the current export situation and our ongoing negotiations with Japan—I will pass over that.

I think it's safe to say, sir, and no surprise to anybody that we all agree that the softwood lumber industry is facing some significant economic difficulties in the United States. And I say this even though we have seen record levels of consumption of lumber in the United States. And this is fueled by a particularly strong housing market.

But the fact is that despite the record levels of consumption, lumber prices in the United States have remained depressed, and the result has been low profits, increasing unemployment and numerous mill closings.

Now some say that this is caused by, for example, the question of overproduction of lumber in North America. Others would say that it is caused by the overvalued U.S. dollar. Some would say that it is caused by too many shipments from Canada of softwood lumber to us.

But it would seem to me that the first question, the issue of overriding concern to the U.S. softwood lumber industry, is the price of timber. And I don't think anybody would disagree that the Canadian stumpage pricing system results in prices for stumpage that are substantially below those prevailing in the United States. And as has been indicated earlier, for example, during the earlier panel, many producers here in this country believe that the existing Canadian system confers with what they term is an unfair subsidy to Canadian producers.

However, as has Chairwoman Stern has indicated, the Department of Commerce after a thorough investigation under the U.S. countervailing duty law ruled in 1983 that that stumpage system did not confer a countervailable subsidy.

I have referred briefly, sir, to the exchange rate situation, as has Chairwoman Stern. There is no question that the appreciation of the U.S. dollar has conferred a significant advantage on Canadian exports to the United States.

I have been given to understand—I don't pretend to be an expert in timber matters, but I understand that another factor is the matter of species preference. It has been argued that some lumber users prefer Canadian lumber for certain applications and are even willing to pay a premium for it.

Let me just say, sir, that this has been an issue which preoccupied Ambassador Brock before he moved to the Labor Department, and since Ambassador Yeutter has taken over, he has met on two occasions with his counterpart, Trade Minister Kellerher of Canada. I have led two negotiations or two consultations with the Canadians on this matter, and have been meeting with them regularly. And we have agreed to look at such matters in our bilateral talks, such as forest tenure and stumpage, tariff standards, log export policies, exchange rates and transportation.

The Canadians have indicated some willingness to consider mutual tariff reductions. But, thus far, in our informal talks, I would have to be frank in saying that they have not resulted in much substantive progress on the other issues.

I would like to conclude, sir, briefly by saying that we do attach a very high importance to this matter. There are no easy solutions to this particular problem. The Canadians feel just as strongly about it on the one side as we do. And we have been trying to work out with the Canadians a solution to the problem. Both Ambassador Yeutter and Minister Kellerher are committed to continue to explore all the possible ways and means to resolve this issue.

And, finally, sir, I would say that we look forward—we requested the update of the U.S. ITC study. We look forward to receiving the results of that so that we can make a better and more current assessment of the problem at hand.

Thank you.

The CHAIRMAN. Thank you, sir.

[The prepared written statement of Ambassador Smith follows:]

STATEMENT OF
AMBASSADOR MICHAEL B. SMITH
BEFORE THE
SENATE FINANCE COMMITTEE
SEPTEMBER 19, 1985

MR. CHAIRMAN:

I WANT TO THANK THE COMMITTEE FOR THE OPPORTUNITY TO APPEAR BEFORE YOU TODAY TO DISCUSS THE CURRENT STATE OF THE U.S. SOFTWOOD LUMBER INDUSTRY, INCLUDING THE IMPACT OF IMPORTS FROM CANADA. UNDERSECRETARY AMSTUTZ IS APPEARING WITH ME TODAY, AND HIS TESTIMONY WILL FOCUS ON THE CURRENT EXPORT SITUATION AND OUR ONGOING NEGOTIATIONS WITH JAPAN.

IT WILL SURPRISE NO ONE IN THIS ROOM WHEN I SAY THAT THE U.S. SOFTWOOD LUMBER INDUSTRY CURRENTLY FACES SERIOUS ECONOMIC DIFFICULTIES. I SAY THIS EVEN THOUGH WE HAVE SEEN RECORD LEVELS OF CONSUMPTION OF LUMBER IN THE UNITED STATES IN 1984 AND THUS FAR IN 1985, FUELED BY A PARTICULARLY STRONG HOUSING MARKET. IN THE PAST, HIGH LEVELS OF LUMBER CONSUMPTION RESULTED IN STRONG PRICES. TODAY, HOWEVER, DESPITE THE RECORD LEVELS OF CONSUMPTION, LUMBER PRICES HAVE REMAINED DEPRESSED. THE RESULT HAS BEEN LOW PROFITS, INCREASING UNEMPLOYMENT, AND NUMEROUS MILL CLOSINGS.

A NUMBER OF FACTORS HAVE BEEN CITED AS THE CAUSE OF THE CURRENT DEPRESSED STATE OF OUR DOMESTIC INDUSTRY. THE SITUATION IS EXTREMELY COMPLEX, AND CONVINCING ARGUMENTS HAVE BEEN MADE BY PROPONENTS ON BOTH SIDES OF THE ISSUE.

It would appear that one important factor is overproduction of lumber in North America. From 1980 to 1985, Canadian production of softwood lumber increased by 20 percent (from 18.3 to 21.9 billion board feet). During the same period, U.S. production grew by 16% (from 26.2 to 30.4 billion board feet).

Canadian shipments of softwood lumber to the United States have been increasing. In 1980, Canada shipped 9.4 billion board feet of softwood lumber to the United States, representing 51.4 percent of its total production. In the first five months of 1985, Canada shipped to the United States at an annual rate of 14.1 billion board feet, 64.4 percent of its production. Today, Canadian imports account for 30.6 percent of U.S. lumber consumption, compared to 20 percent in 1980.

The issue of overriding concern to the U.S. softwood lumber industry is the price of timber. No one will disagree that the Canadian stumpage pricing system results in prices for stumpage substantially below those prevailing in the United States. Many U.S. producers believe strongly that the existing Canadian system confers an unfair subsidy to Canadian producers. However, the U.S. Department of Commerce, after a thorough investigation under U.S. countervailing duty law, ruled in 1983 that the Canadian stumpage pricing system did not confer a countervailable subsidy.

ANOTHER SIGNIFICANT FACTOR AFFECTING THE COMPETITIVENESS OF THE U.S. INDUSTRY IS THE EXCHANGE RATE SITUATION. THE U.S. DOLLAR HAS APPRECIATED OVER 30 PERCENT SINCE 1976 WHEN THE TWO CURRENCIES TRADED AT PAR. THIS APPRECIATION HAS CONFERRED A SIGNIFICANT ADVANTAGE ON CANADIAN EXPORTS TO THE UNITED STATES. IN ADDITION, AS BOTH THE U.S. AND CANADIAN DOLLARS HAVE APPRECIATED AGAINST OTHER CURRENCIES, EXPORTS OF LUMBER FROM BOTH THE UNITED STATES AND CANADA TO OVERSEAS MARKETS HAVE DECLINED.

ANOTHER CONTRIBUTING FACTOR CITED FOR THE CURRENT PLIGHT OF THE U.S. INDUSTRY IS SPECIES PREFERENCE. IT HAS BEEN ARGUED THAT SOME LUMBER USERS PREFER CANADIAN LUMBER FOR CERTAIN APPLICATIONS, AND ARE EVEN WILLING TO PAY A PREMIUM FOR IT.

ADMINISTRATION CONCERN OVER THE STATE OF THE U.S. SOFTWOOD LUMBER INDUSTRY HAS LED TO A NUMBER OF ACTIONS. EARLIER THIS YEAR, THEN-UNITED STATES TRADE REPRESENTATIVE WILLIAM BROCK REQUESTED GOVERNMENT-TO-GOVERNMENT CONSULTATIONS WITH THE CANADIAN GOVERNMENT. OUR PURPOSE IN REQUESTING THESE CONSULTATIONS WAS TO OBTAIN A BETTER UNDERSTANDING OF THE MARKET SITUATION IN NORTH AMERICA AND THE FACTORS AFFECTING TRADE IN LUMBER AND OTHER WOOD PRODUCTS. AT TWO MEETINGS, IN FEBRUARY AND APRIL, DETAILED DISCUSSIONS COVERED A WHOLE RANGE OF FACTORS AFFECTING BILATERAL TRADE IN LUMBER AND WOOD PRODUCINGS INCLUDING: FOREST TENURE AND STUMAGE, TARIFFS, STANDARDS, LOG EXPORT POLICIES, EXCHANGE RATES, AND TRANSPORTATION.

THE CANADIANS HAVE INDICATED A WILLINGNESS TO CONSIDER MUTUAL TARIFF REDUCTIONS ON A RANGE OF WOOD PRODUCTS. THEY HAVE ALSO AGREED TO EXAMINE THE POSSIBILITY OF THE HARMONIZING OF STANDARDS WHICH AFFECT TRADE IN PLYWOOD AND OTHER WOOD PRODUCTS.

UNFORTUNATELY, THESE TALKS HAVE THUS FAR YIELDED LITTLE SUBSTANTIVE PROGRESS ON OTHER ISSUES. NEVERTHELESS, WE INTEND TO CONTINUE TO PURSUE THESE TALKS.

SINCE ASSUMING HIS POST AS UNITED STATES TRADE REPRESENTATIVE, AMBASSADOR CLAYTON YEUTTER HAS PLACED A HIGH PRIORITY ON RESOLVING THIS MAJOR IRRITANT IN OUR BILATERAL RELATIONS WITH CANADA. HE HAD DISCUSSED THE MATTER ON A NUMBER OF OCCASIONS WITH HIS COUNTERPART, CANADIAN TRADE MINISTER JAMES KELLEHER. THE CANADIANS SINCERELY BELIEVE THAT THEIR STUMPAGE PRICING SYSTEM IS NOT A SUBSIDY, PARTICULARLY IN LIGHT OF THE 1983 COMMERCE DEPARTMENT FINDING. THIS SUBJECT IS JUST AS DIFFICULT AND CONTENTIOUS FOR THEM. THERE ARE NO EASY SOLUTIONS, BUT BOTH AMBASSADOR YEUTTER AND MINISTER KELLEHER ARE COMMITTED TO CONTINUE TO EXPLORE ALL POSSIBLE WAYS AND MEANS TO RESOLVE THIS ISSUE.

IN ORDER TO OBTAIN AN UNBIASED, FACTUAL ANALYSIS OF THE LUMBER SITUATION, EARLIER THIS YEAR WE REQUESTED THAT THE U.S. INTERNATIONAL TRADE COMMISSION (USITC) UPDATE ITS 1982 FACT-FINDING REPORT ON THE COMPETITIVE FACTORS AFFECTING THE U.S. SOFTWOOD LUMBER INDUSTRY.

THE USITC UPDATE OF THE SECTION 332 STUDY IS DUE BY OCTOBER 8. AFTER WE HAVE AN OPPORTUNITY TO REVIEW THIS STUDY WITH REPRESENTATIVES OF THE DOMESTIC SOFTWOOD LUMBER INDUSTRY, WE WILL DECIDE WHERE WE GO FROM HERE.

OUR OPPOSITION TO LEGISLATIVE SOLUTIONS TO THE PROBLEMS FACING THE DOMESTIC SOFTWOOD LUMBER INDUSTRY SHOULD NOT BE MISTAKEN FOR A LACK OF CONCERN ON THE PART OF THE ADMINISTRATION FOR THE SERIOUS COMMERCIAL DIFFICULTIES CONFRONTING THIS IMPORTANT SECTOR OF OUR ECONOMY. ON THE CONTRARY, THIS ADMINISTRATION IS FIRMLY COMMITTED TO WORKING WITH THE U.S. SOFTWOOD LUMBER INDUSTRY TO FIND A SOLUTION TO THEIR PROBLEMS UNDER EXISTING LAW.

I THANK YOU FOR YOUR ATTENTION, AND I WILL BE PLEASED TO ANSWER ANY QUESTIONS THE COMMITTEE MAY HAVE.

STATEMENT OF HON. DANIEL G. AMSTUTZ, UNDER SECRETARY FOR INTERNATIONAL AFFAIRS AND COMMODITY PROGRAMS, U.S. DEPARTMENT OF AGRICULTURE, WASHINGTON, DC

The CHAIRMAN. Mr. Secretary.

Secretary AMSTUTZ. Thank you, Mr. Chairman.

While in the long term we are optimistic about the potential for U.S. wood product exports, at present our wood product sales are experiencing the same market problems as other U.S. products in export markets. U.S. solid wood exports totaled $1.3 billion during the first half of 1985, down 6 percent from the same period last year.

The reason for this decline partly relates to sluggish economies, which have reduced demand around the world; partly relates to the strength of the U.S. dollar against the currencies of other major market countries; and partly relates to trade barriers.

A bright spot in the U.S. trade situation is the continued increase in exports to the Pacific-rim countries. Trade figures show increased demand for U.S. softwood logs and veneer for plywood by Japan, Korea, Taiwan and China. U.S. exporters should anticipate further growth in sales to this region. The total ban on peninsular Malaysias and Indonesias log exports will force many countries in that region to seek alternative suppliers.

Japan is the largest export market for U.S. wood products, buying $1.02 billion worth of these products in 1984. However, Japan imports mostly raw materials and protects its own finished product manufacturers with high tariff barriers.

The U.S. forest products industry and this administration is concerned about this trade imbalance, and we have had a series of talks focused on this issue, the so-called Moss talks. Removal of Japan's restrictive import duties on wood panel products is one of our top priorities. Japan has announced the tariffs on plywood and other panel products will be reduced commencing in 1987, but we have told the government of Japan that we find this unacceptable. The Japanese announcement provides no information concerning the depth and staging of the planned cuts, and, of course, we expect the tariff reduction process should start earlier, should start no later than fiscal 1986.

In the area of wood product standards, we have made some progress, some meaningful progress. We will continue to work with Japan in this area. For example, they have agreed to consider the establishment of structural standards for panel products other than plywood.

China is an expanding and potentially huge market for U.S. solid wood products. This year, China has become our second largest export market. U.S. exports are projected to top $300 million. However, almost all our exports consist of softwood logs. And we, of course, would like to open China up to increased exports of U.S. lumber and plywood products.

Korea and Taiwan also present good and growing opportunities for U.S. exports.

The European Community is the primary overseas market for U.S. hardwood lumber, plywood, veneer and softwood plywood, the third largest market for softwood lumber and an important market for other wood products. Weak economic conditions in Europe currently and the strong U.S. dollar have softened the market for U.S. solid wood products. If these conditions improve, and we are confident they will, the European market shows promise for softwood, plywood and lumber. We have a problem with the EC quota on softwood plywood and hope that during the course of negotiations we can improve this situation.

Latin America is a promising area in the future with a chronic need for low-income, low-cost housing. And we are optimistic about opportunities in the Middle East as well.

To conclude, foreign markets do indeed offer the U.S. timber industry the opportunity to work itself out of its current oversupply problems. However, significant private sector initiatives in the area of foreign market development and government action in the area of improving market access will be needed if the industry is and realize its full export potential.

The administration is committed to achieving removal of market access barriers. And we are confident that the U.S. industry is eager to be aggressive and continually develop products for these markets.

Thank you.

[The prepared written statement of Secretary Amstutz follows:]

Statement by Daniel G. Amstutz
Under Secretary for International Affairs
and Commodity Programs
U.S. Department of Agriculture
Before the Senate Finance Committee
September 19, 1985

Mr. Chairman, members of the committee, I appreciate the opportunity to discuss with you the international competitive challenges facing the domestic timber industry.

The international arena is a source of problems as well as opportunities for the U.S. timber industry. Large imports from foreign countries, primarily Canada, have lessened the profitability of our industry to the point where mill closures are commonplace and unemployment runs high in many timber-dependent communities. At the same time, foreign markets offer the industry the opportunity to work itself out of its current oversupply problems.

I'd like to take a few minutes to outline the current export situation for the U.S. timber industry and then to discuss some of the issues and opportunities facing the industry overseas.

The U.S. Export Situation

While in the long term we are optimistic about the potential for U.S. wood product exports, at present our wood product sales are experiencing the same market problems as other U.S. agricultural products.

U.S. solid wood exports totaled $1.3 billion during the first half of 1985, down 6 percent from the same period in 1984. The reason for this decline partly relates to sluggish economies which have limited demand around the world. Also, this decrease is partly due to the strength of the U.S. dollar against the currencies of major market countries.

Softwood exports were valued at $972 million during the first half of 1985, down 2 percent from the same period in 1984. Most of the trade was in logs, lumber, and wood chips, which accounted for 59, 25 and 8 percent, respectively, of total softwood exports. Log and wood chip exports increased while sales of most other major wood commodities declined. Exports to Japan, the leading U.S. softwood market, represented about half of U.S. sales.

U.S. hardwood exports totaled $222.6 million in the first half of 1985, down 16 percent from the same period of 1984. Lumber, logs, and veneer accounted for 55, 25, and 13 percent, respectively, of the total value of hardwood export sales. Canada, West Germany and Taiwan, the top three export markets, accounted for 52 percent of total export sales.

Trade Situation With Canada

One of the most serious trade issues now facing the U.S. timber industry involves competition in the U.S. market from Canadian wood products. Since Ambassador Smith has already addressed that situation—and we are working closely with USTR on it—I will move on to discuss our export opportunities in that market.

Any real potential for U.S. exports would be in the long term and depend in large measure on the Canadian supply situation. Despite apparent reforestation problems, Canada will be a major supplier to world markets in the forseeable future.

This Administration is pursuing trade discussions with the Canadians to open the Canadian market fully to the U.S. industry. Exports to Canada have remained generally stable except for a sharp drop in softwood lumber in 1982. The major export items are softwood and hardwood lumber.

Issues and Opportunities in the Far East

A bright spot in the U.S. trade situation is the continued increase in exports to the Pacific Rim countries. Trade figures show increased demand for U.S. softwood logs and veneer for plywood by Japan, Korea, Taiwan, and China. U.S. exporters should anticipate further growth in sales to this region as the total ban on Peninsular Malaysia's and Indonesia's log exports will force many countries in that region to seek alternative suppliers.

Japan especially needs these logs for local plywood and lumber mills. In the short run, the Japanese may meet import requirements by purchasing logs from the East Malaysian states of Sabah and Sarawak, and other Southeast Asian suppliers. However, many of these suppliers are running out of exploitable forests.

Japan is the largest export market for U.S. wood products. In 1984 the United States exported $1.02 billion worth of these products to Japan, mostly raw materials such as logs ($631 million) and chips ($156 million). Softwood lumber was the only significant value-added product exported ($162 million).

This trade pattern is an example of the Japanese practice of importing raw materials duty free while protecting its own finished product manufacturers with import barriers.

Japan's tariffs on panel products (plywood, particleboard and veneer) range from 12 to 15 percent, while logs and chips enter Japan duty free. Japanese tariffs on most finished and semi-finished products are high relative to Japan's average tariff rate on nonwood commodities of less than 4 percent. As long as these barriers remain in place, market opportunities for high-value wood products will be limited.

The U.S. forest products industry is concerned about this trade imbalance—and in the past year, I have headed the U.S. delegation at a series of market access (MOSS) talks focused on Japan's forest product sector.

Our No. 1 goal in these talks is the complete phase-out of Japan's duties on plywood, veneer, particleboard, and other wood products such as lumber and molding and millwork.

Thus far, the government of Japan has committed itself in general to reducing tariffs on panel products and other wood products commencing in 1987 and to resolving various standards and other nontariff barrier issues. We will continue working diligently to bring these MOSS talks to a successful conclusion.

China is an expanding and potentially huge market for U.S. solid wood products. U.S. forest products exports to China have increased from near zero in 1979 to nearly $288 million in 1984. This year China has become our second largest export market and U.S. exports are projected to top $300 million.

Softwood logs comprise the bulk of our exports to China, accounting for 97 percent of U.S. shipments in 1983 and 94 percent in 1984. This heavily one-dimensional trade in softwood logs is a most important issue. We would like to open China to increased exports of U.S. lumber and plywood products.

The U.S. industry views China as a large undeveloped market for U.S. solid wood products. The Chinese have expressed interest in improving contacts with U.S. exporters of wood products. The National Forest Products Association (NFPA)—a trade cooperator group which USDA has been working with since 1979—sent a team of industry representatives to China during 1984 to help accomplish this goal.

Greater market opportunities also may arise from the proposed Sino-American Timber Committee, which would be organized to establish greater cooperation between the Chinese and U.S. forestry, manufacturing, and trade communities.

A team of wood products industry specialists from the Pacific Northwest also visited China this past summer. This mission was instrumental in gaining a commitment from Chinese authorities to work cooperatively to develop the wood market. The initial step in this direction will be the construction of a model wood frame house in Beijing.

Korea is another major wood importer with good potential for U.S. exporters.

The vast majority of Korea's imports are tropical hardwood logs from Southeast Asia. Korea is encountering a growing raw material supply problem generated by the log export bans instituted by traditional supplier countries such as Indonesia and Malaysia. In the long run, these restrictions may force Korea to turn increasingly to alternate suppliers, such as the United States, for softwood logs.

Increased purchases of U.S. softwood lumber could offset some Southeast Asian log imports, permitting the Korean sawmilling industry to maintain production levels by further processing this lumber to Korean specifications. Similarly, imports of U.S. softwood veneers could be used as a substitute for tropical hardwood logs, which are becoming more costly.

Taiwan is a major importer of raw tropical hardwood logs in order to supply its burgeoing wood products manufacturing industry. However, now that Indonesia and Penisular Malaysia have banned exports of hardwood logs, Taiwan is going to be looking for new suppliers. The Indonesian and Malaysian bans, along with the lowering of Taiwan's tariffs, is expected to open markets for U.S. temperate hardwood logs in the future.

Issues and Opportunities in Europe

The European Community (EC) is the primary overseas market for U.S. hardwood lumber, plywood, veneer, and softwood plywood; the third largest market for softwood lumber; and an important market for other wood products. However, weak economic conditions in Europe and a strong U.S. dollar have softened the European market for U.S. solid wood products. If these conditions improve, the European market shows promise for softwood plywood and lumber.

An essential ingredient of a market expansion program will be the liberalization of the EC quota on softwood plywood, which severely restricts the development of the European market. The EC quota stands at 600,000 cubic meters. Imports to the EC in excess of this level are dutied at 10.8 percent, with a scheduled rate reduction to 10 percent in 1987.

The EC also imposes plant health regulations which restrain trade in oak logs and lumber in order to prevent the introduction of the Oak Wilt disease into the EC. In April 1985, an EC plant health team visited the U.S. to discuss the problem. EC plant regulatory officials are planning to discuss U.S. proposed solutions to the problem in their fall meetings.

Market Opportunities in Latin America

A promising area for increasing exports of U.S. solid wood products can be Latin America. The countries comprising this region are characterized by high population growth rates and low per capita incomes. This has generated a tremendous demand for adequate low-income, low-cost housing throughout the region. The near-term housing shortfall is projected to be 4.5 million units annually; however, this shortfall could change as Latin American countries endeavor to improve their economies.

The United States is in an excellent position to capitalize on this projected demand and significantly expand exports of solid wood products. However, the Latin American opportunity is not without stiff competition from Canadian and European supplying nations. Many of these countries, particularly Canada, are also aware of the need for adequate housing in Latin America and are pursuing aggressive market development programs to secure a share of this growing market.

In many Latin American countries, market development work and credit guarantees will be successful only if high tariff barriers are reduced or eliminated. This is notable in Peru, which currently maintains a 61-percent duty (c.i.f. basis) on all imported plywood. Also, severe shortages of foreign exchange, lack of credit, low buying power and a preference for concrete homes will limit any immediate increases in U.S. lumber and plywood exports to Latin America.

The American Plywood Association, the Southern Forest Products Association, and the U.S. Government sponsored the Inter-American Housing Conference in Seattle last September. The conference demonstrated building systems and discussed financial programs that can help the region solve its housing crisis. Twenty Caribbean and Latin American countries sent representatives.

As a direct result of the Conference, Peru, Ecuador and Chile signed agreements with the American Plywood Association for low-income wood housing, and Venezuela, Jamaica, and the Dominican Republic signed with the Souther Forest Products Association.

All-wood model demonstration houses already have been constructed in Peru. The projects for Chile and Ecuador are underway. The SFPA sponsored homes are to be built in the fall. The interest the demonstration homes generated in Peru has dispelled the myth that wood housing is not accepted. Over 2,400 applications were received to purchase the 15 demonstration homes built.

Market Prospects in the Middle East

The Middle East has emerged as an important and potentially significant market for U.S. solid wood products. However, in 1984 total wood exports to this region dropped 62 percent from 1983. This decline is attributable to the poor economic conditions in the area because of a slackened demand for oil.

While the Middle Eastern market has good potential, U.S. exporters will face stiff competition from Central and Eastern European timber exporting countries which have been the region's traditional wood products suppliers. The U.S. share of this market in 1980 stood at 13.4 percent for softwood lumber and 1.4 percent for plywood.

Conclusion

I'd like summarize my remarks today by citing findings of a recent report prepared by Congress' Office of Technology Assessment. That report, entitled Wood Use: U.S. Competitiveness and Technology, concludes that the United States has the capability to become a net exporter of solid wood and paper products by the end of decade. However, the report also states that significant private sector initiatives in the area of foreign market development and government action in the area of improving market access will be needed if this promise is to become a reality.

The Administration is committed to achieving removal of market access barriers. Finally, of utmost importance, the U.S. industry will have to continually develop products suited to the market characteristics of each marketing area.

That concludes my statement, Mr. Chairman. I will be glad to respond to questions.

The CHAIRMAN. Ms. Stern, let me start with you, if I might. This hearing focuses on timber today, but I hope it is the first of a great many hearings we may have on the whole subject of protection, trade, and the issue of unfair competition. And I use that term in a different sense then it is used in connection with applications for relief under section 201 for a temporary period.

Most industries allege unfair competition. It isn't often they come in and say, "Gee, it's fair competition but we just can't stand up to it. That's kind of un-American. You don't do that.

So, I want to talk about what is unfair. Is it unfair that Canada chooses to sell its stumpage in a manner different from the way we choose to sell our stumpage?

Commissioner STERN. Senator Packwood, I'd like to answer every question that a Senator asks me, even though it may be out of my purview. In this case you have asked me a question that the Department of Commerce was responsible for answering ultimately back in 1983 when it had to look at our laws dealing with countervailing duties and interpret the laws given the facts before them.

The CHAIRMAN. That was before the 1984 act, however.

Commissioner STERN. That was before the 1984 act. And I have not put myself in a position of the Department of Commerce. I can say that when we look at the industry, we are looking at the question of whether the industry has been injured by an alleged unfair act.

The CHAIRMAN. That's a different question. You can be injured by unfair or fair competition.

Commissioner STERN. Yes. But what I'm trying to say is that I really feel you are asking me to interpret what the Department of Commerce would interpret if they got a petition.

The CHAIRMAN. Well, let me ask you—because I can shift my questions to the two gentlemen, if you want—do you want to limit your answers pretty much to injury?

Commissioner STERN. Injury and the findings that we had in our 1982 study. I can say that in our 1982 study we looked at the question of what the differential was regarding the stumpage costs. And we will be doing that again in the study that we will be delivering to the Trade Representative in a matter of several weeks.

The CHAIRMAN. Well, then, let me tell you the line of questioning I want to pursue, and I will open it up to all three of you. I will pursue the same line with the other witnesses.

Is it unfair competition that wage rates are one-tenth of ours? Is it unfair competition that countries have different and lower environmental standards than we do; therefore, less costly? Is it unfair competition that they will not reforest as we insist upon reforestation? Do other countries have to operate in exactly the same fashion and at exactly the same cost under which we operate in order for competition to be fair. Is everything else unfair, making such activities subject to tariffs, quotas or restrictions?

Commissioner STERN. Well, I can easily answer that question. I do not think it is unfair under the way we defined it in the law. And that's the reason why I pointed out these other factors of competition. And I didn't even mention the ones you did. I also mentioned the differences in logging costs, transportation costs, some of these other areas, wage differentials, some of which we do have direct control over within our own country.

The CHAIRMAN. Well, we have control over the price of timber. We could sell our timber on the same basis Canada does.

Commissioner STERN. That's true. In fact, when we had the hearing a couple of months ago, back in July, I think it was, I asked one of the members of the industry how would you like to have the Canadian system.

The CHAIRMAN. I bet they didn't like it.

Commissioner STERN. Yes, he did.

The CHAIRMAN. He did like it?

Commissioner STERN. I said given the choice between the U.S. program and the Canadian program, which would you rather have. And he made some of the people he was with uncomfortable, but he said he would like to have the Canadian one.

The CHAIRMAN. He would like to have it, if he is one of those to whom the timber is allocated. He would not like to have it if he happens to be left out. [Laughter.]

Commissioner STERN. I didn't press him.

The CHAIRMAN. Mr. Smith, limit yourself, if you will, to some of the examples of unfairness I gave. We will be faced with a whole series of bills on the floor of the Senate this year, most of which are going to allege unfair competition; most of which are going to include wage differentials. It's not going to be the argument of closed markets overseas. That's another issue and a legitimate one we ought to face.

I want to find out what is and what is not unfair competition, and to see if there is any threat not just to the lumber industry, but to industry generally. Should certain industries be protected against what is unfair, and even from certain things that are not unfair, just different.

Ambassador SMITH. Like Chairwoman Stern, I would agree that in the examples that you enunciated in your question to her that those are not unfair as is accepted thus far internationally in the General Agreement on Tariffs and Trade.

The CHAIRMAN. Is it generally accepted as fair or unfair as to the way Canadians sell stumpage?

Ambassador SMITH. I would say at the present time the international consensus is that it is not unfair. That a country, if it chooses to price its natural resources in that fashion, there is to my knowledge no international law which says that they cannot do that.

The CHAIRMAN. Senator Baucus.

Senator BAUCUS. Thank you, Mr. Chairman.

Ambassador Smith, when Dr. Yeutter was before this committee not too long ago, he was asked whether the Canadian free trade agreement would be sent up to the Congress before any resolution agreement was reached between Canada and the United States on this lumber question, his response was basically that the lumber issue be resolved first. Let me quote him directly: He said, "Well, the lumber issue will inevitably be resolved prior to the creation of a free trade zone. That is, negotiation if it is undertaken requires several years of work."

Is that still the administration's position? That this Canadian issue be resolved first, the timber issue, before the administration sends up a free trade agreement?

Ambassador SMITH. Sir, if I could come at it the other way. It's very clear that if the Canadian Government and the United States Government were to enter into negotiations on a closer trading relationship, whatever you want to call it, that would take some time. And by some time, I mean a number of years.

It is clear from both economic and political reasons that we would have to come to grips with this lumber issue if not before, certainly by the time we sent anything up. I mean that's the reality of life.

So I would say that obviously what my boss said still stands. [Laughter.]

The CHAIRMAN. That's why he's still employed. [Laughter.]

Senator BAUCUS. That's why you are where you are, as I was about to say.

I wonder if you could tell us whether the President's statement of a new trade offensive next week will address this question.

Ambassador SMITH. Sir, I have not seen the draft yet of the President's statement. I have been told, just as I was leaving the office, that it was on the way over for USTR's comments as well as for other comments. So I'm not ducking the question; I haven't seen the draft.

Senator BAUCUS. Do you think that it should be included? Should the President address the Canadian problem?

Ambassador SMITH. Well, very frankly, in my own view, I'm not sure that you should address any one particular bilateral problem over a particular bilateral problem with another country. Where do you start and where do you stop? We have lots of bilateral trade problems, as you well know, sir; certainly I know. And I'm not sure—should you single out one particular bilateral problem?

Senator BAUCUS. Let's turn to another subject, and that's the general availability test. That's something you and your agencies generally talk about. Isn't it true that other countries do not have a general availability test to the degree to which they even have countervailing duty laws? Or to ask the same question. Isn't it true that this phrase, generally available, is a phrase that somehow the Department of Commerce came up with on its own and which is not a principle that is generally practiced in international trade law?

Ambassador SMITH. Sir, would you indulge me in the liberty of asking my general counsel who is an expert in this to answer that question? He was at the Department of Commerce or came to the Department of Commerce shortly after that.

Mr. HOLMER. And I might note, Senator Baucus, shortly after the Canadian's softwood lumber decision.

The answer to your question is that it was not made up out of whole thought by the Department of Commerce. The statute refers very specifically that in order to find a domestic subsidy, you must find that the benefit is provided to a specific industry or a group of industries.

The CHAIRMAN. Say that again.

Mr. HOLMER. The statute requires that in order to find a countervailable domestic subsidy, the benefit must be provided to a specific industry or group of industries. And, therefore, in order to be able to find a subsidy, we do have to find that benefit limited to a specific industry or group. And there is not flexibility on the part of the Department to violate that statutory requirement.

Senator BAUCUS. Do other countries have the same test?

Mr. HOLMER. Well, I think it's probably safe to say that most other countries don't because most other countries don't have a countervailing duty law. The United States is really at the cutting edge, in terms of the vigorousness with which we enforce our countervailing duty and antidumping laws.

Senator BAUCUS. Is Canadian timber available to an American mill located in the United States? That is, if an American mill, sawmill, were to send its trucks up to Canada to get the Canadian logs, would that mill owner, that company, have generally available to it the lower Canadian stumpage price?

Mr. HOLMER. I'm almost certain that the situation for a U.S. company is identical to the situation for a Canadian company. That is, a Canadian company can't come down and buy U.S. Forest Service timber and take it back. Nor can a U.S. company go to Canada and take timber and bring it back.

Senator BAUCUS. Well, the reason for that is because of different stumpage prices.

The CHAIRMAN. I think he's talking about the law; not the stumpage price.

Senator BAUCUS. I know.

What about the Canadian statutes which limit U.S. investment and ownership in Canada? Are there any restrictions under Canadian laws the degree to which an American firm can invest and own a mill in Canada?

Mr. HOLMER. I don't know the answer to that question, Senator. I'm sure we would be happy to respond to you in writing.

[The information from Mr. Holmer follows:]

Hearings Before the Senate Finance Committee

September 19, 1985

1. What Canadian statutes limit U.S. investment and ownership in Canada?

a. There has been a major shift in the Government of Canada's treatment of foreign investment. On June 30, 1985, the Government repealed the "Foreign Investment Review Act" (FIRA). This 1973 act severely restricted the acquisition of Canadian businesses and the establishment of new businesses by foreign investors. FIRA subjected all acquisitions and investments by foreign investors to government review to determine whether such investments would be of "significant benefit" to Canada." Any investments deemed to be of less than "significant" benefit were denied approval. This restrictive policy had an adverse effect on U.S. investment and ownership in Canada.

The Canadian Government has replaced FIRA with the "Investment Canada Act." This Act reflects a new policy of actively encouraging investment. Accordingly, the Act repeals any form of government review of new businesses. It limits review of acquisitions of existing Canadian firms to those (1) affecting Canada's cultural heritage or national identity, (2) involving direct or indirect control by a foreign investor of a Canadian corporation with over $5 million (Canadian) in assets, or (3) involving acquisition by a foreign investor of a non-Canadian corporation which controls a Canadian firm with over $50 million in assets. While the U.S. would prefer a completely open investment policy in Canada, the new act is still a substantial improvement over FIRA.

2. Are there any restrictions under Canadian law as to the degree to which an American firm can invest and own a mill in Canada?

a. There are no restrictions on U.S. ownership of Canadian lumber mills *per se*. The acquisition of a Canadian mill would, however, be subject to review under the Investment Canada Act, assuming the acquisition falls within the criteria set out in the Act. If so, the Minister must determine that the acquisition is of "net benefit" to Canada, a less stringent standard than the "significant benefit" test of FIRA.

Mr. HOLMER. It is one of the issues that we look forward to receiving additional information from the U.S. ITC about in their section 332 study.

Senator BAUCUS. I think you will find that although Canadian firms have much more generally available opportunities to invest in U.S. mills, that it's not true that American companies have the same generally available opportunity to invest in a Canadian mill.

The CHAIRMAN. Senator Symms.

Senator SYMMS. Thank you, Mr. Chairman. And I thank all the witnesses.

Ms. Stern, I didn't read the article quite as carefully as I wish I would have now, but I did note the first couple of paragraphs that you had a statement in the paper today, I believe, saying we should have a trade strategy. Is that correct? Am I attributing that to the right person?

Commissioner STERN. Yes, sir.

Senator SYMMS. A trade strategy and a trade—well, you used the word "czar." I'm not sure that——

Commissioner STERN. No, I didn't. [Laughter.]

Senator SYMMS. Well, that's good. I didn't like that word either. [Laughter.]

But I liked the thrust of the article because I do think that we need a trade strategy. We are in a trade war right now whether—all the talk we hear about we don't want to get in a Smoot-Hawley trade war. I think most people in the Congress on both sides of the aisle generally agree with that. They don't want to get in a big protectionist war, but we are in a trade war. And it appears to me we are losing it right now.

And I just wondered do we have a strategy. I will just ask you, Ms. Stern, if you were this trade person, do you think you could solve this problem with some bilateral action that would happen much faster.

Commissioner STERN. Are we talking simply about the lumber question?

Senator SYMMS. Well, just say lumber. There are many questions.

Commissioner STERN. There are some problems. I mean I believe that over-arching all of these problems, which result in a $150 billion trade deficit after 3 years of record-breaking trade deficits and I might say record-breaking caseload at the Commission, is the dollar. I don't think that we can have so many different import-sensitive industries and failing export industries without some fundamental difficulty that we are faced with. And so I do believe that the dollar has been a comparative advantage which we have basically given to our trading partners that they are using against us.

Senator SYMMS. Well, when our original GATT agreements were set up, we did not floating exchange rates; isn't that correct?

Commissioner STERN. Yes, sir. You are absolutely correct.

Senator SYMMS. Well, Mr. Smith, do we have a strategy now?

Ambassador SMITH. Yes, sir, I think we do. I would—I don't think I would associate myself with Chairwoman Stern's remarks in that context. I think we have a strategy. I think it's a strategy that successive administrations have had since 1947. And I think it reflects a general bipartisan approach to international trade that has marked our international economic relations for 35 years. I think we do have a strategy. Certainly.

Senator SYMMS. Well, let me ask you this question just to go a little further. I have a town in the State of Idaho—but what do you tell a Congressman or a Member of Congress to tell a town where there are 4,000 people living in town and there are 800 jobs that have just recently been closed because of sawmill closures? And it's not all Canadian timber. And I think that even the company that closed said it wasn't all Canadian timber that caused the problems. It was a contributing factor. But what do you tell those people about the seeming unresponsiveness of the U.S.'s ability to countervail, for example, or our unresponsiveness to be able to react to the big dollar differential? What's the answer? What would you say if you were there speaking to them? They are out of work. They don't really want a big explanation, but they would just like to know why we don't do something.

Ambassador SMITH. I understand that, sir. I have come from a State where we saw an entire industry leave the State and move South.

I think the administration was responsive on, for example, the countervailing thing. It did act as it interpreted the law or was charged to interpret the law, as written by Congress, on the countervailing duty petition with the provisions of the law which were then in effect. We do try to work these things out under law to follow legal procedures. Some countries don't do it the way we do.

But there is not—and I don't pretend to think that there isn't—an easy answer to this. The question of unemployment or people thrown out of jobs and town and cities is a very difficult thing to respond to. But in terms of the example that you put forward, I think that we did carry out the intent of the Congress as embodied in the trade act on the countervailing duty petition.

Senator SYMMS. Well, has anything changed since 1982 when you made that? That's a follow-up question to that. When you did try to impose a countervailing duty. When our industry accused the Canadian provinces of subsidizing timber, has anything changed?

Ambassador SMITH. Well, I understand—correct me, sir—the 1984 Trade Act does include a provision on so-called upstream subsidies that some at least think could change the outcome in a new CVD case, if I understand it correctly. Stumpage could be viewed as an upstream subsidy to a single industry, loggers. And, thus, avoid the specificity issue which Al Holmer just talked about which came up in the 1983 case. And it seems to clarify that comparing prices in the country under investigation to prices outside that country is appropriate in some cases. That is what some say the 1984 Trade Act has changed.

There is, of course, no CVD case right now in front of us on the stumpage issue since the amendment of the 1984 Trade Act was passed.

Senator SYMMS. Well, how long should we expect and how long should we tell people out there that we are going to continue to see this erosion of the jobs before there is some action taken, whether it be countervailing duty or some kind of a damaging restriction or Ronald Reagan sitting down with the Prime Minister if that is what it takes to straighten out the issue?

Ambassador SMITH. Well, sir, we are—I hope that you will believe that we have been working very long and hard with the Canadians to come to grips with this problem. We have not hidden the fact to them in any way that the stumpage situation represents a real political and economic problem in this country.

I, myself, as I said, have made several trips to Canada. I met just 2 weeks ago with the Canadians on this issue. Ambassador Yeutter and before him Ambassador Brock have made it unmistakably clear that this is a problem which has to be resolved. We would prefer to resolve it within—administratively than legislatively for a variety of reasons. And we would hope that the Canadians will equally try to be forthcoming to us and help us get out of this very difficult problem.

Senator SYMMS. Well, I hear what you are saying, but I would just say I don't think we can wait. So the faster action, the better.

The CHAIRMAN. Let me ask Mr. Holmer a question. And we are delighted to have you with us, Alan, in your new capacity. Alan is one of the finest public servants I've ever known. And anybody who hires him is a genius. [Laughter]

Mr. SMITH. Thank you, sir. [Laughter.]

The CHAIRMAN. He was my administrative assistant for a number of years.

Go back to this general availability test and let me make sure I understand it. Does general availability mean that it must be generally available to the industry concerned, that is stumpage is really of use only to the timber industry and somebody in the amusement park industry probably is not interested in it. Does that satisfy the general availability test if it's available to everybody in the industry that would use it?

Mr. HOLMER. You raise one of the real cutting edge issues that was addressed by Commerce in the 1983 decision. And the language in the statutes refers—bear with me a moment—refers to domestic subsidies if provided or required by Government action to a specific industry.

What Commerce found was that the stumpage was available in Canada on similar terms regardless of the industry or enterprise of the recipient. Basically, they found that it wasn't any kind of Government action taken by Canada which limited the availability of the stumpage. Anybody in Canada who wanted to go up and bid for timber——

The CHAIRMAN. The amusement park owner could bid for the timber if the amusement park owner chose to do so. So whatever he or she does with it afterward, such as sell it to a mill, at least it is available to everyone.

Mr. HOLMER. That was the basic issue that was addressed. They found, for example, that there were a number of separate industries, that is, the lumber industries, the paper industries, the furniture manufacturing industries, which were all categorized under the both United States and Canada law as separate groups of industries, that all of those were ones that used the product. And, indeed, there wasn't any action that had been taken by the Canadian Government to limit it to any particular sector.

You asked if they have to make it generally available to everybody. That's essentially what they have done. And the fact that it is used only by a part of the Canadian business population was a factor that did not cause the Commerce Department to find that there would be a subsidy.

The CHAIRMAN. Similar situation here, then. The investment tax credit is available to everyone. The fact that businesses that lose money can't use it doesn't mean it doesn't meet the general availability test, since it is available to everyone who can make use of it.

Mr. HOLMER. Exactly. Another example, would be capital gains treatment for long-term assets, one of which happens to be the forest products industry. We would not consider that to be a countervailable domestic subsidy that could be countervailed by the Japanese we sell our finished products to Japan.

The CHAIRMAN. I have no more questions.

Senator Baucus.

Senator BAUCUS. Mr. Chairman, I think you have asked some good questions. Although Mr. Holmer is a genius, I'm not sure we have the right answers. [Laughter.]

The CHAIRMAN. I said those who hire him are geniuses. [Laughter.]

Senator BAUCUS. Right. [Laughter.]

We'll see. [Laughter.]

First of all, the statute does not use the words "generally available." That's not in the statute. So the phrase that has come up from the Department of Commerce generally through its decisions. The fact of the matter, too, in a recent case, as I am sure Mr. Holmer knows, the *Bethlehem Steel* case, the Court said that generally available—if I can find the language here: "The plain meaning of this provision"—that is, the subsidy provision, the law—"in its context does not suggest that generally available benefits are excluded from the definition of subsidy." I know other cases that have different interpretations. But there is a very recent case which very definitely stated that general availability is not the test to be used here.

Second, that makes sense to me. It seems to me that this extremely low subsidy that the Canadians practice, that is, where Canada backs down the price of its public timber in order to meet a sales price at some distant market, including as far away as Arkansas, certainly that constitutes a subsidy because it's a price much lower than the fair market value.

But, nevertheless, even if that timber is available to all timber producers, of course it's generally available to all timber producers in Canada. And it doesn't make any difference to me whether it's also "generally available" to amusement parks because the amusement park is not in the business of buying and selling timber. That's not their business.

Well, the test to me is totally irrelevant. And as we have already established, and I think you will agree, that timber in Canada is not generally available to an American timber producer. Sure, an American company in Canada can buy the timber, but an American company, say, along the Canadian border located in America, in one of the northern States in our country, cannot go buy that cheaper timber. So it's not generally available to that person.

So I must say, frankly, that this test of general availability, first, is not in the law; it is made up by the Department. And, second, doesn't make any sense. It's a test that makes some sense in some instances, but the general application of the general availability test does not make sense because it immunizes some practices that clearly are subsidies within any rational definition of the terms. The ITC in its 1982 findings found that the resources in Canada cost one-sixth, if I am correct, of what they cost in America. And then that finding was then sent over to the Department of Commerce, and the Commerce took those factual findings and for public policy reasons, found that there is not a subsidy within the term of the law because it came up with this test of general availability.

I must say that I think this whole thing is a little like "Alice in Wonderland." It does not make practical sense to me. And as I understand, too, the administration in Geneva may be attempting to reach an agreement with other countries that they, too, adopt the same test at a time when this committee and the Congress are trying to determine what is a subsidy and what isn't a subsidy.

So I must ask you, Mr. Holmer, isn't it true that there is a court decision which found that general availability is not the test? And isn't it true as a practical matter that this timber is not available by American companies in Canada? Sure, there may be a law which says the Canadian companies can't buy in America, but that's irrelevant because they don't want to buy more expensive American timber. And they are not trying to.

And so I must say that it just seems to me on the face of it that this is a subsidy. In answer to the Chairman's question, one could argue—it's a philosophical matter—whether other laws amount to unfair trade practices. One could argue philosophically whether lower wage rates amount to unfair trade practice. That's an excellent question. It really goes to the heart of the matter of what our trade laws should be all about.

It further seems to me that a subsidy is unfair. And certainly it is a subsidy when the price that the Canadians sell their timber at is calculated in a way to go beneath American producers and calculated to undersell American producers in American markets. But certainly it's much below the fair market value of what that timber would sell at for private producers in Canada or America.

The CHAIRMAN. Is it a subsidy when we give what we call subsidies to our farm sector to make them more competitive?

Senator BAUCUS. Well, we can all do the same thing, as we all do. Common markets.

The CHAIRMAN. And we may. I'm not sure which way we are going to go.

Senator BAUCUS. That's my point.

The CHAIRMAN. We may go the route of protectionism. We may lift up the borders and subsidize our exports. We won't buy any Toyotas and we won't sell any wheat and we will all live very comfortably, perhaps with higher prices, but we will all live very comfortably.

And if that's the direction we are going to go, we ought to fully understand what we are doing. But I sense we are drifting willy-nilly down a path that we don't know whence it comes out. I'm very wary of having industry after industry after industry come in and claim unfair competition. When you try to pin down what is unfair, it just turns out to be a difference in lifestyles or a difference in wage rates or a difference in environmental standards. On occasion, you get a genuine complaint about an illegal subsidy. And that we can and should stop.

We also get plenty of genuine complaints about closed markets. There is no question that they exist, and that we can prevent them, we are willing to use retaliatory power.

But that is not going to solve the fundamental question that is dividing this country. And that is: What are we going to do about overseas fair competition that is able, on occasion, to beat our industries in our markets, and from which they want protection?

Senator BAUCUS. Mr. Chairman, if I might say, I fully agree. And I think the solution really is much more presidential and congressional leadership here. It's clear that the United States does subsidize its agricultural production. It's clear the common market subsidizes. It's clear that Canada and some other countries subsidize theirs. We have this glut. The fact of the matter is to some degree if we are going to solve the agricultural——

The CHAIRMAN. Let me ask you where we would come out on this question.

Senator BAUCUS. My other point here is that the same is true with the overvalued U.S. dollar. I think most observers will say that the United States has to get its deficit down. They will say the United States should reduce its deficit—and Japan on the other side should practice a little domestic stimulus. This is a matter for the heads of states and for governments and public policymakers that come together, because the more we go down the road of specific legislation to try to address a narrow, specific problem, the deeper we are going to get ourselves into trouble.

The CHAIRMAN. I had dinner last night with Ambassador Gotlieb and I asked him when Canada was going to be presenting us with a Canadian-United States free trade agreement. And he said, well, he thought in just a couple of days at least it would be on the table and available for negotiations.

And I said I'm curious, Mr. Ambassador. Will it include open investment in both directions? Will we be able to invest freely in Canada; as Canadians may invest freely here? He said, well, there may be some things that are reserved that neither one of us would want to permit.

I understand what he is saying. But what would be the position of this country if Canada said, OK no holds barred; you want to buy our timber companies, buy them; you want to buy our publishing companies, buy them.

The tradeoff is that everything that is made in the United States can be sold in Canada without limits. Everything that's made in Canada can be sold in the United States without limits. Either of us can invest in the other country. What would be the position of the United States if our principal timber companies began investing primarily in Canada, causing mills in this country to close. The bulk of the jobs would move north. Would that be unfair competition.

Are we prepared to go down the road to that kind of a trade agreement? I don't even believe we have considered that possibility. I think if that happened, we would again be complaining about unfair competition, even though Americans would have equal access to the Canadian market and to the Canadian investments.

Senator BAUCUS. I don't think we have to worry about that because I don't think Canada is going to open up that much.

The CHAIRMAN. No, I don't think they are either.

Senator Symms.

Senator SYMMS. Thank you very much, Mr. Chairman.

And I want to come back to where I was with my questions before I ran out of time last time. I think to kind of summarize it, Ms. Stern said she didn't think we had a strategy. I said that if we have got a strategy, it looks to me like we are getting our clock cleaned. And Mr. Smith said we have got a strategy.

And if we have one, Mr. Smith, do you think it's working?

Ambassador SMITH. Do I think that the fact that we remain the world's largest exporter——

Senator SYMMS. Well, is our strategy working? I guess the question I have is the slowness of this—I've talked to a sawmill operator that I mentioned earlier. Yesterday, he tells me that not only do the Canadians get a subsidy on the stump, but now they not only have a subsidized freight system; they don't have to ship on union bottoms in their shifts. That's our problem; not theirs of course. We should take care of that law. But he said now that the Burlington Northern Railroad in one point in Washington State and one point in Montana allows the Canadians to truck timber down to a loading point and when they will contract large numbers of cars, they actually give them a preferential freight rate into Boston and other eastern markets, it's much cheaper.

How does that fit into this picture? In other words, they can get a freight rate from a U.S. rail company, if they will have enough cars, so they contract a large number of cars, and have a freight advantage over an Idaho or Montana or Washington State mill that's a smaller operator.

Ambassador SMITH. Isn't the Burlington Northern an American company and yet it is extending this to the Canadians?

Senator SYMMS. That's right.

Ambassador SMITH. I assume it's extending the same benefit to Americans.

Senator SYMMS. It is, but it isn't to the smaller American companies. If you ship 10,000 cars, you get a better freight rate than if you shift 1,000.

Ambassador SMITH. Sir, I don't know about this particular instance; it is the first I have heard of it. But you asked: Is the trade strategy working? Do you mean because we have a trade deficit on the merchandise account, that it isn't working?

Now, some people would say you have these large trade deficits; then it isn't working. Then, I would come back and say why isn't it? Why do you say that? We have created 8 million jobs. We do have a very large number of imports coming in, but our exports are still going out at the same rate or a little better than they were in 1980, not much, but a little better than they were in 1980, despite what everybody says about the high dollar.

Senator SYMMS. In other words, we are just buying more is what it amounts to?

Ambassador SMITH. No, I don't say that only, but is the trade strategy, is the principle of free trade, or a free or a fair trade working to the advantage of the United States? And let's look at it in terms of the overall terms in terms of jobs. Have we lost more jobs than we have created in the last 4 years? The answer is no. We have created more jobs than we have lost.

Senator SYMMS. OK. The chairman asked that this hearing be on timber, but let me cite a question, and maybe Ms. Stern will want to answer it and Mr. Smith, both. I have reason to believe that—and from a very competent source—that this is correct, that the Japanese who are big into the semiconductor industry tell the ITC that their costs to make a 64 KD ram is 50 cents apiece. So, they claim they are not dumping them when they come in and undercut our semiconductor producers. They tell the Internal Revenue Service that they make the 64 KD ram for $2 apiece. Now, they are either lying to one section of the U.S. Government or the other or to both. But what does it take to get a response? Is there any mechanism for the special Trade Representative—the ITC—all the parties that would be in our industry—the IRS—I have called Treasury about this and called the ITC about it and called the special Trade Representative about it and said: Can't you do something about this? Can't the two parties go together and either tax them for the profits they are making or accuse them of dumping, one or the other? But not allow this issue just to go on. In the meantime, these companies in the United States that make semiconductors are going broke. I mean, by the time our Government gets around to responding, they will all be gone, and we will be totally reliant on the Japanese for semiconductors, which I think is rather foolish. How do you answer something like that? What recommendation would you make to a U.S. Senator to correct that?

Ambassador SMITH. Sir, with regard to the semiconductor 301 case, which is now before the Office of the U.S. Trade Representative, that case is under active investigation. That use is dealing with the effects of past practices by the Japanese Government in the semiconductor field. And obviously my office has been in touch with both, if you will, the plaintiffs and the defendants on this. We have met as late as 11 last night with the Japanese on this case. We are working on that case. We accepted the case from the petitioner—from the semiconductor association—we accepted it quickly. We have begun a process. We have now had one, two, three meetings with the Japanese. This is a very complex case as, I believe, the petitioner will themselves admit. We are working with the Japanese to see if there is a resolution to this problem. But the dumping case, or the difference between what they say to the ITC and the Internal Revenue Service, I myself am not particularly aware of. I will be glad to find out and report something in writing to you when I get back to the office, but I am not quite aware of this particular element of the 64 K RAM thing. I am very aware of the 301 case which was filed and accepted by USTR in early July, and we will meet the statutory deadline by a very good measure in the resolution of that particular case.

Secretary AMSTUTZ. Senator, may I comment on the general question that you raised? Clearly, in a number of industrial areas now, we have a chronic problem of overcapacity, namely that there is not enough demand out there in the marketplace to take care of the global ability to produce. A fundamental reason for this has to relate to the fact that economies around the world are not growing as fast as all of us who are suppliers would like to see. Part and parcel of our trade strategy has been vocalized by the President frequently, at summit meetings, with the other summit countries. We are doing our best to encourage them to follow economic policies that are expansive. A net payoff from the President's belief in a free trade policy is to generate more buying power among countries who can indeed become our good customers.

Senator SYMMS. I agree with you. To get the Europeans off their socialism would help us. That would be the best thing that could happen—if they could get a free market over there and stop subsidizing and taxing everybody to death. It would help us enormously, but in the meantime, there are a lot of our natural resource producers who are really hurting.

Secretary AMSTUTZ. I understand, sir, and I understand it is awfully hard to answer that person in that town—the example you gave.

Senator SYMMS. It seems to me that we have to have a short term fix, you know, if we are in this kind of a circumstance.

Commissioner STERN. Senator Symms, if I may just respond to your question about the semiconductors because I know it is very important to you. I know Micron was the petitioner in the dumping case for which we have had a preliminary investigation and for which the Commission found affirmatively; and we will be continuing the case on to final, assuming that the Department of Commerce finds that there is an unfair trading practice going on there. I would just like you to know that the Commission felt that it was important to self-initiate a study on the semiconductor industry. However, we are required to send out our questionnaires first through the Office of Management and Budget, to obtain clearance, and we were never able to get those questionnaires cleared. They did not go out. This is the first time this has ever happened, and I think it very much is a cloud over the independence of the ability of the Commission to do studies when we see a problem looming. We did respond, as I said, to the petition of the unfair trading practice. And as far as our data that we get, we closely guard that data and we try to assure all petitioners and all parties to the Commission that we will not share confidential information with other agencies of the Government. In that way, we can get as full and as complete and as honest a record as we need in order to find independently whether there is injury to a domestic industry, feeling that there has been injury. And as I said, we are standing ready to see whether that case does return to us on a final investigation; and I would hope that, having mentioned this, that the Finance Committee would look into the ability of the Commission to operate and respond and cover section 332 investigations in light of the fact that we have been stymied in an unprecedented way.

Senator SYMMS. Thank you, Mr. Chairman. Thank you all very much.

The CHAIRMAN. Gentlemen, Ms. Stern, thank you for coming. We appreciate it very, very much.

Commissioner STERN. Thank you, sir.

The CHAIRMAN. We are going to take just about a 3 minute recess so that we can go vote. Senator Baucus should be back. We will start with the next panel of Mr. Dennison, Mr. Hagenstein, Mr. Withers, and Mr. Koelemij. And as soon as Senator Baucus comes in, he will start the panel; I will go vote and be right back.

[Whereupon, at 3:38 p.m., a brief recess was held.]

AFTER RECESS

Senator BAUCUS. Senator Packwood is on his way. In the meantime, we will reconvene the hearing and move to the second panel, the panel of Mr. Stanley Dennison, executive vice president of Georgia-Pacific; Perry Hagenstein, president of Resources Issues; Robert Withers, president of Withers Lumber Co.; and John Koelemij, president of the National Association of Home Builders. Gentlemen? Mr. Hoffman, why don't you proceed, and then we will go right down the line?

Mr. HOFFMAN. Mr. Dennison is making our statement.

Senator BAUCUS. Fine. Mr. Dennison.

STATEMENT OF STANLEY S. DENNISON, EXECUTIVE VICE PRESIDENT, BUILDING PRODUCTS, GEORGIA-PACIFIC CORP., ATLANTA, GA, AND CHAIRMAN, COALITION FOR FAIR LUMBER IMPORTS; ON BEHALF OF THE NATIONAL FOREST PRODUCTS ASSOCIATION, WASHINGTON, DC

Mr. DENNISON. Thank you, Mr. Chairman. I want to thank you for the opportunity to be here today to discuss the North American Softwood Lumber Industry. I am Stan Dennison, executive vice president for building products for Georgia Pacific Corp. I am also chairman of the U.S. Coalition for Fair Lumber Imports, which represents the landowners and manufacturers of every region of the country. With me today are Don Hoffman, manager of lumber operations for International Paper, Perry Hagenstein, president of Resources Issues, Inc., a forestry consultant. Georgia-Pacific is not only one of the largest manufacturers of American lumber, but to our knowledge we are also one of the largest importers of Canadian lumber. Last year, according to our records, Georgia-Pacific purchased about 1.5 billion feet of Canadian lumber at a cost of nearly $400 million. Georgia Pacific has remained neutral in the Canadian-U.S. lumber controversy for a long time because of our position as both a manufacturer and importer. We have always supported policies and legislation that encouraged fair—and I emphasize fair—trade. We, however, can no longer remain neutral, even though a reduction of Canadian imports could prove costly to Georgia Pacific. These imports have reached levels that are causing a liquidation of U.S. industries. Today, undervalued Canadian imports account for over one-third of all softwood lumber consumed in this country. In 1975, the Canadian lumber imports accounted for less than 19 percent of U.S. markets. In 1984, this percentage rose to almost 31 percent, and it has risen to 33.4 percent, Senator, in the first 6 months of 1985. That is overdoing the generosity of the American market in our opinion. Why are these percentages escalating? The answer is because Canadian lumber enjoys a delivered cost advantage mainly due to a very low price for timber. Canada is engaged in massive overproduction of lumber, and 68 percent of Canada's rapidly growing production is shipped to the United States. The Canadian Government set its September prices so low that Canadian lumber can be sold in the United States at whatever price they feel is needed to be competitive, regardless of how close American mills are to their own local markets. For example, stumpage prices in British Columbia interior, the largest exporting area to the United States are below the U.S. market in the south by $108.00 per thousand feet. In our country, one-third of timber production comes from Government lands, one-third from company-owned lands, and one-third from private lands, where the assessed value of timber is based on bidding at competitive auctions. The difference between competitive U.S. timber prices and noncompetitive Canadian prices are far too great and exist because of Canadian Government subsidies that U.S. producers do not enjoy from our own Government. This is disrupting markets for our nation's forest products industry and is not fair trade. In 1984, consumption in the U.S. was the highest ever, yet increases in Canadian lumber imports devastated our American industry. Does that mean I should stop, Senator?

Senator BAUCUS. Why don't you wrap up in about 2 minutes?

Mr. DENNISON. All right. Thank you. In just the last 6 years, more than 250 U.S. sawmills have closed. We estimate approximately 27,000 direct jobs have been lost because of Canadian imports. Just this year, Georgia-Pacific had to close a major efficient mill in Arkansas because we were unable to compete with Canadian lumber. It is rather staggering to close a mill in Arkansas while softwood lumber from interior British Columbia—1,000 miles away—is thriving in the same market. The U.S. softwood lumber industry is as efficient as any in the world. However, if Canadian lumber imports continue to flood into the United States, the resulting decline of the return on capital will be insufficient to justify continued reforestation on private land and investment in the U.S. softwood lumber industry. We will see even further liquidation of our American industry. We have no objection to Canadian lumber being imported into this country. It is good lumber, as our own lumber is, but the situation as it exists today is totally unfair. Free trade is fair trade, and this implies there is a balance in the quality of trade practices. U.S. lumber producers are merely seeking an opportunity to compete in a fair competitive market. We think something should be done to restore fair play for the American lumber industry. Thank you.

Senator BAUCUS. Thank you, Mr. Dennison. Mr. Hagenstein.

[The prepared statement of Stanley S. Dennison follows:]

STATEMENT OF STANLEY S. DENNISON, CHAIRMAN OF THE COALITION FOR FAIR LUMBER IMPORTS

I. THE U.S. LUMBER MARKET IS BOOMING, YET THE U.S. LUMBER INDUSTRY FACES ECONOMIC DISASTER

The U.S. softwood lumber industry is modern, efficient and, under free market conditions, highly competitive in the world market. Yet, despite a natural competitive advantage, and despite booming lumber demand, the U.S. lumber industry faces economic disaster.

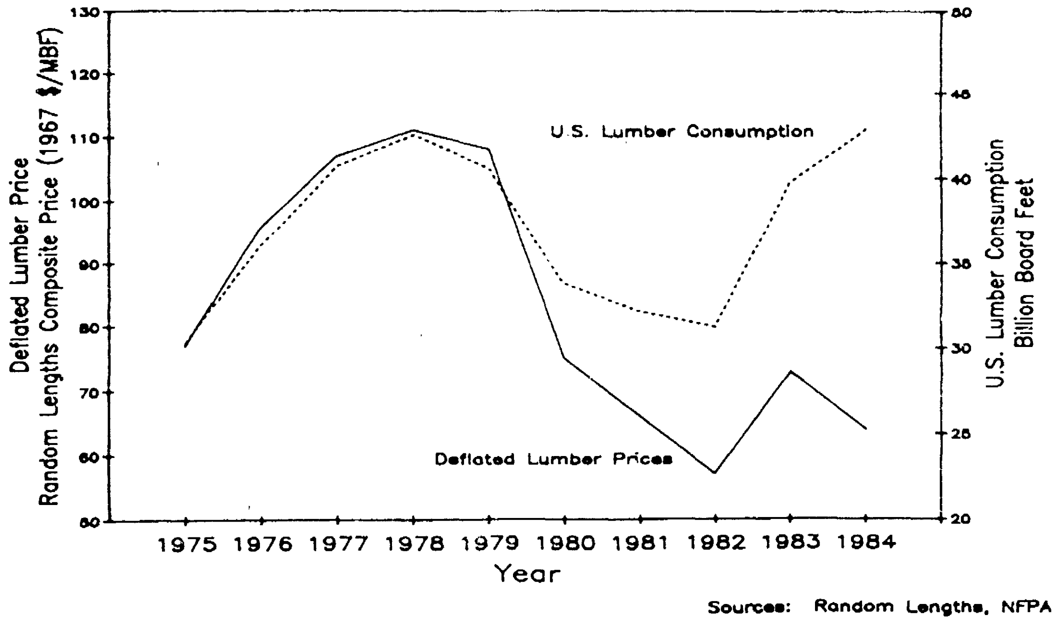
1984 was a record year for lumber consumption in the United States, approximately 43.0 billion board feet (BBF). At current rates, 1985 lumber consumption will reach a new peak of 43.5 BBF. Strong demand is fueled by a strong housing market, over 1.7 million housing starts in 1983 and in 1984. Normally, such a strong demand would result in increased lumber prices and a healthy lumber industry. The most recent recovery in the lumber market, however, has resulted in neither. See Chart 1. Prices are depressed;[1] the industry is suffering.

In the last six years, over 250 U.S. lumber mills have been forced to close. Nearly 30,000 workers employed directly by lumber firms have lost their jobs. Thousands of workers in related industries have been forced out of work. In 1984 alone, the six largest U.S. lumber producers wrote off over $550 million in softwood lumber assets, and this despite record levels of lumber consumption. . . . There is obviously something wrong in America's lumber industry.

[1] The real price that U.S. producers obtain for lumber in the Western, Inland, and Southern regions fell by 9.6%, 10.6%, and 6.5% respectively over the last six years.

U.S. SOFTWOOD LUMBER CONSUMPTION AND DEFLATED SOFTWOOD LUMBER PRICES

(Deflated Using PPI for all Commodities)



II. THE CAUSE OF THE LUMBER INDUSTRY'S PROBLEMS IS OVERPRODUCTION OF SOFTWOOD LUMBER: THE SOURCE OF THAT PROBLEM IS CANADA

Both Canadian and U.S. lumber manufacturers recognize that the source of the industry's problems is overproduction.[2] The source of that overproduction is Canada.[3]

In 1975 Canada produced 10.9 BBF of softwood lumber. At the rate of production in the first six months of 1985, Canada will produce 21.4 BBF this year, an increase of 96%. By comparison, U.S. production has only grown from 25.7 BBF to 30.6 BBF, an increase of 19%.[4] See Chart 2 and Table 1. Between fiscal years 1982 and 1983, British Columbia alone increased its timber harvest by 28%.

Not surprisingly, excess Canadian production has been shipped to the U.S. market. In 1975, only 52% of Canadian

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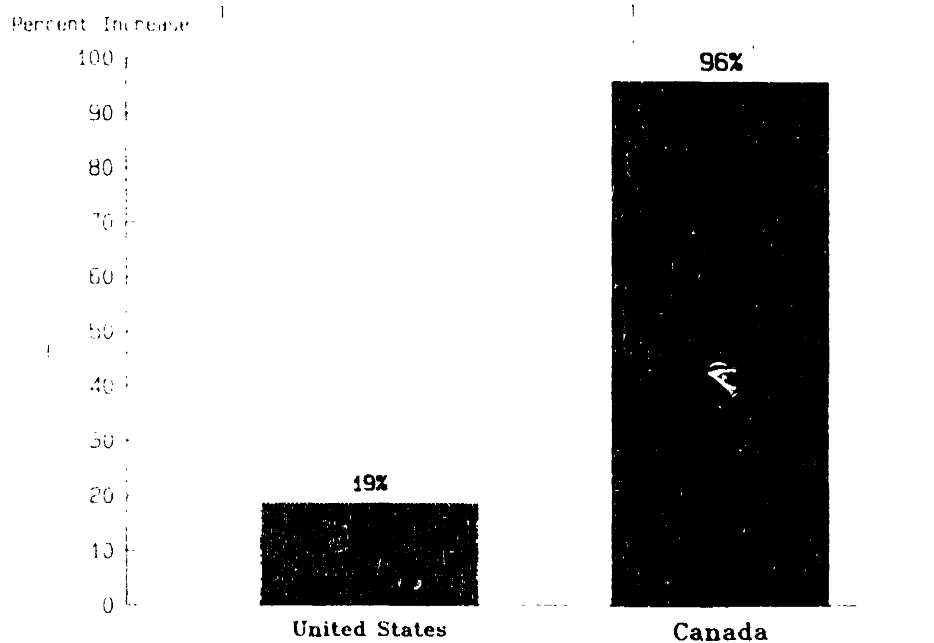
[2] See, e.g., Transcript of Testimony Before the International Trade Commission on July 23, 1985, 75 and 145-146. See Pearse, Obstacles and Opportunities for the Forest Industry, address to Interior Logging Association, 5 (Vernon, B.C., 1985). See also Business Week, 55 (May 20, 1985) (increased Canadian production fed a glutted market and some prices fell by 53% in the past five years).

[3] "J. Ronald Longstaffe, chairman of the Council of Forest Industries of B.C. . . . , says the basic reason for the fall in lumber prices is that almost all Canadian sawmills are flooding the U.S. market." Financial Post, 27 (Toronto, Oct. 8, 1983).

[4] Historically, from 1970-75, Canada's production averaged 12.6 BBF. Current production is running 70% above that historic level. By comparison, U.S. production is running only 7% above historic levels of production.

Significantly, even if Canada's share of the U.S. market was cut in half, the U.S. industry could more than meet the increased demand.

INCREASE IN SOFTWOOD LUMBER PRODUCTION BETWEEN 1975 AND 1985



Note: 1985 data projected from first six months
Source. Council of Forest Industries of BC and
the National Forest Products Association

TABLE 1

U.S. AND CANADIAN LUMBER PRODUCTION

(Billion Board Feet)

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985*
U.S.	25.7	29.7	31.7	32.1	31.4	26.2	24.7	23.8	29.8	31.3	30.6
Canada	10.9	14.9	17.2	18.4	18.6	18.3	16.6	15.9	20.3	20.6	21.4

* 1985 data estimated from production in the first six months of 1985.

Source: Council of Forest Industries of British Columbia and National Forest Products Association.

production came to the United States. In the first six months of 1985, 68% of Canada's burgeoning production is flooding into our country. See Chart 3. Canadian shipments of lumber to the United States are running 15% ahead of last year's record pace. See Chart 4. Correspondingly, Canada's share of the U.S. market has increased from 18.7% in 1975 (20.7% historically from 1970-75) to 33.4%.[5] See Chart 5 and Table 2. Clearly, the source of the overproduction of lumber in North America is Canada.

III. CANADA OVERPRODUCES BECAUSE ITS STUMPAGE PRICES ARE KEPT UNNATURALLY LOW BY PROVINCIAL GOVERNMENTS

Canada overproduces because the Canadian provinces, which own over 90% of Canada's timber, give Canadian firms stumpage, the right to cut timber, at well below fair market value. Indeed, Canadian stumpage costs a small fraction of what similar stumpage costs in the United States. Since the Canadian stumpage system is noncompetitive, and timber is virtually given away, investment in excess capacity is encouraged, and market forces do not constrain production.

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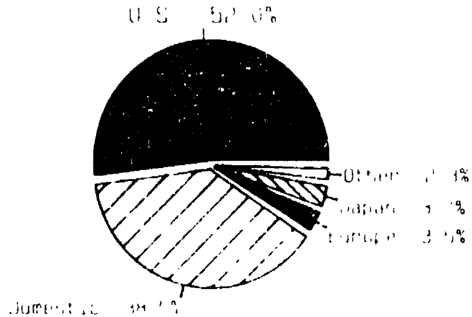
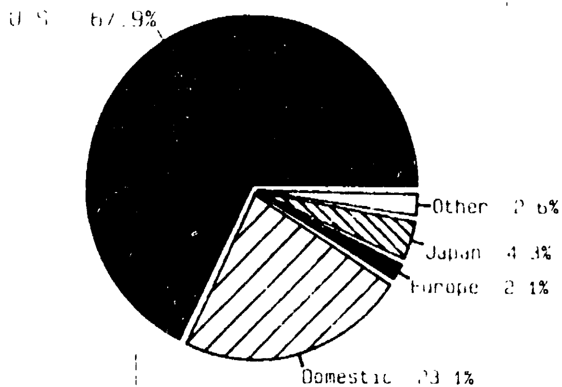
[5] All regions of the United States have been significantly affected. The Western United States share of the U.S. lumber market dropped more than 15 percentage points since 1975. In the Northeast, Canada dominates the market with 63.3%; in the Midwest, Canada controlled 51.5% of the market in 1983 (the last year for which data is available). Even in the South, with some of this country's most heavily forested states, Canada has captured 25.9% of the market.

DESTINATIONS OF CANADIAN SHIPMENTS OF SOFTWOOD LUMBER



1975
10.9 BBF



1985 (6 mos.)
21.4 BBF

CHART 3

Note Pies denote relative size of markets
Source Statistics Canada

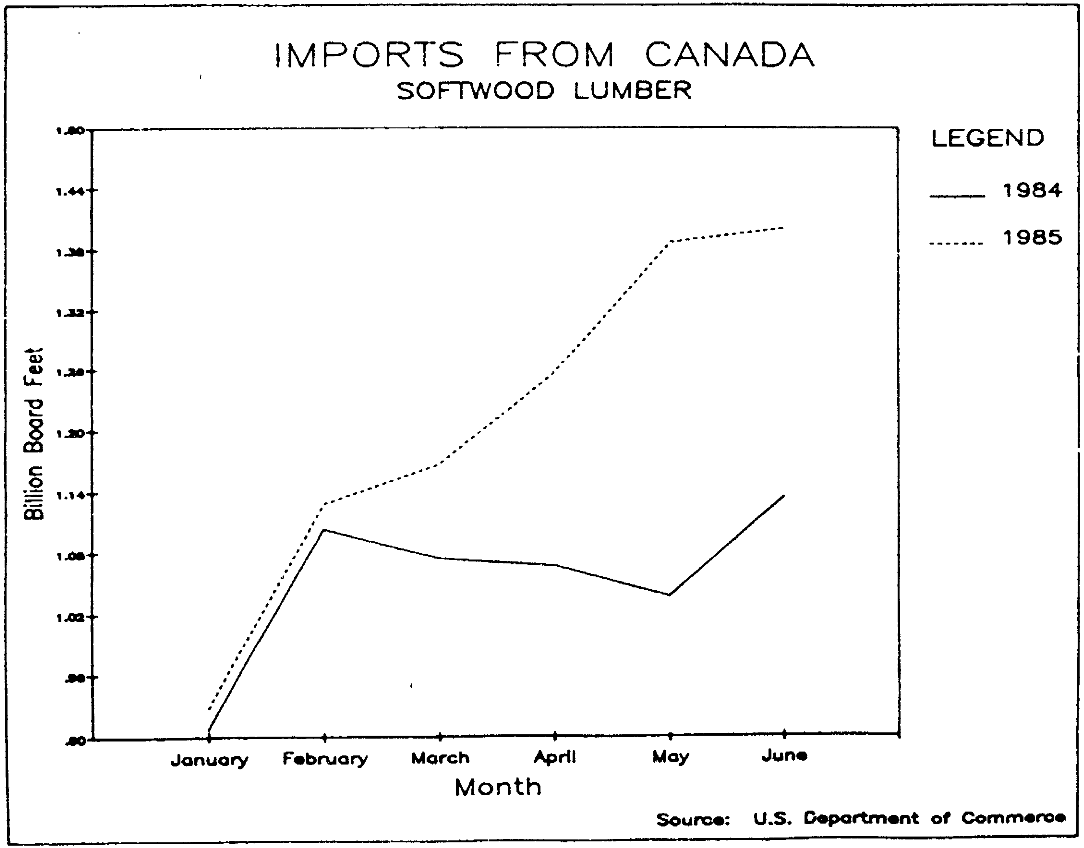
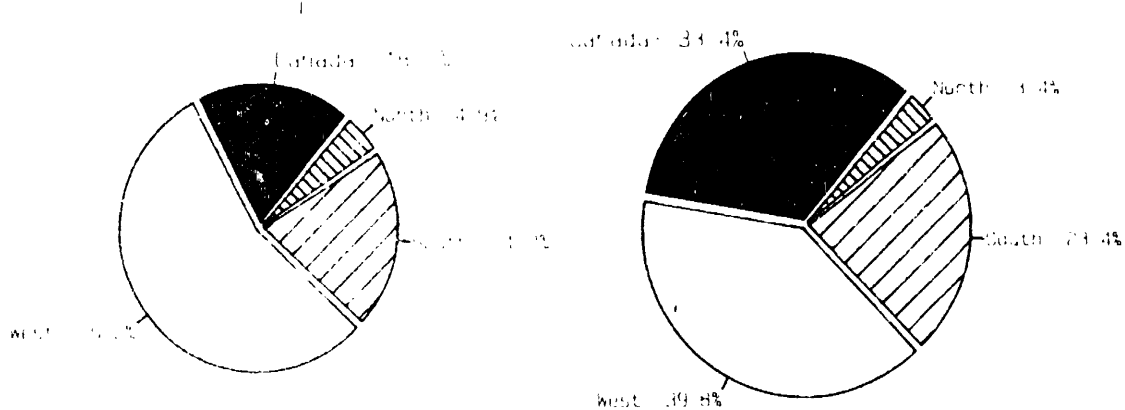

IMPORTS FROM CANADA
SOFTWOOD LUMBER
LEGEND
1984
1985
Billion Board Feet
1.50
1.44
1.38
1.32
1.26
1.20
1.14
1.08
1.02
.96
.90
January
February
March
April
May
June
Month
Source: U.S. Department of Commerce

CHART 4

REGIONAL MARKET SHARE OF U.S. LUMBER CONSUMPTION



1975

1985 (6 mos.)

Note Pies denote relative size of markets
Source: National Forest Products Association

CHART 5

TABLE 2

U.S. LUMBER DEMAND AND CANADIAN MARKET SHARE
(in billion board feet)

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985*
U.S. Demand	30.3	36.0	40.8	42.6	40.6	33.8	32.1	31.2	39.7	43.0	43.5
Canadian Imports	5.7	7.9	10.3	11.8	11.1	9.5	9.2	9.1	12.0	13.2	14.5
% Canadian	18.7	21.9	25.3	27.6	27.3	28.1	28.6	29.2	30.1	30.7	33.4

* Projected from six month data.

SOURCE: National Forest Products Association

A. Stumpage Calculations In Canada

There are essentially two methods of calculating stumpage in Canada. First, in British Columbia, which produces about 58% of the Canadian lumber shipped to the United States, stumpage prices are set using a residual value appraisal method.[6] In the rest of Canada, stumpage is set arbitrarily by provincial governmentals.[7]

The residual value appraisal method arrives at an appraised value for stumpage by determining a value for lumber, adding the value of by-products (e.g. chips) and subtracting the cost of processing the timber and a profit and risk factor. This appraisal method is used in both British Columbian and U.S. Forest Service (USFS) sales.[8] There are two major areas, however, in which USFS and B.C. sales differ.

First, British Columbia arrives at a depressed assessed value through the use of several mechanisms. Initially,

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[6] Most B.C. timber shipped to the United States comes from British Columbia's Interior Region.

[7] Approximately 10% of Canada's timber is either sold by private landowners or through the B.C. Small Business Enterprise Program. The latter program appraises timber by using the residual value method, but then auctions timber with the appraised value being a minimum bid. These competitive sales are discussed infra at "C."

[8] USFS administers sales on about 20% of the United States commercial timberlands. The rest of U.S. timber also comes from competitive markets. Sales in these markets are commonly competitive auctions and/or occur with the assistance of a professional forest consultant. Not surprisingly, prices for timber in our private markets are roughly comparable to the competitive sales on USFS land.

British Columbia _chooses_ a lumber price by "work[ing] backward from prices on the [U.S.] market," i.e. by setting lumber prices at whatever level is necessary to penetrate the U.S. market. Drushka, _Stumped_, 95 (1985). To this initial price, British Columbia adds, by regulation, $10/Bone Dry Unit (BDU) for wood chips. In fact, however, chips sell in the market for from $40-$50/BDU.

British Columbia then subtracts an exceptionally generous profit and risk factor of up to 30% (according to Canadian sources the average profit and risk actually used in 1984 was 16-17%). By comparison the maximum profit and risk in USFS sales is 18% (about 9% actually used in 1983-84). Finally, British Columbia subtracts a grossly inflated logging cost. _See_ discussion _infra_ at "D." Through these mechanisms, British Columbia arrives at a much lower assessed value than the USFS would for similar timber.

The most important difference between the British Columbian and USFS systems, however, is what they do with the assessed value. In British Columbia, lumber firms are given timber at the depressed assessed value. In the United States the assessed value becomes the minimum bid in a competitive auction that commonly results in sales prices several times the assessed value. _See_ Chart 6 and Table 3. The competitive margin in the United States indicates the effect on prices of a competitive and noncompetitive system.

Other Canadian provinces, which produce about 40% of Canada's lumber, set prices by regulation. These provinces do not even maintain the facade of capturing a fair market

COMPARISON OF ADVERTISED AND BID STUMPAGE

NATIONAL FOREST TIMBER SALES
REGION 1

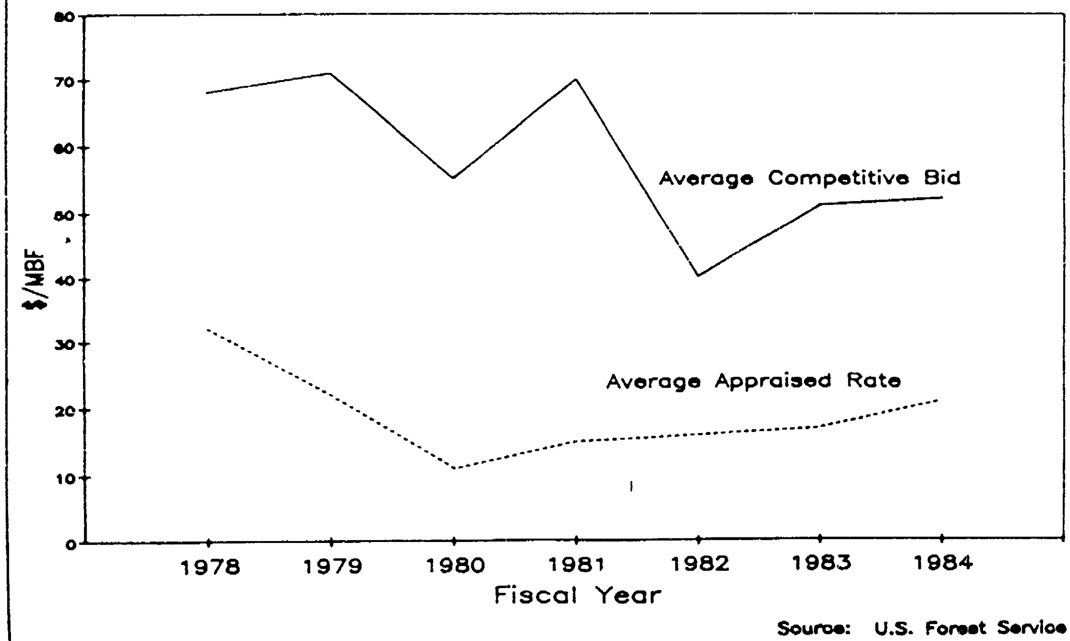

CHART 6

Table 3

RATIO OF HIGH BID FOR STUMPAGE TO U.S. FOREST SERVICE APPRAISAL PRICE 1982-84

Forest	1982 1st Half (# Sales)	1982 2nd Half (# Sales)	1983 1st Half (# Sales)	1983 2nd Half (# Sales)	1984 1st Half (# Sales)	1984 2nd Half (# Sales)
Colville						
One Bidder	1.00 (4)	1.16 (2)	1.00 (2)	1.00 (1)	1.00 (3)	1.18 (3)
Multiple Bidders	2.17 (10)	1.48 (4)	3.06 (8)	2.88 (12)	1.53 (10)	1.33 (9)
Kootenai						
One Bidder	1.00 (2)	1.00 (5)	-- (0)	1.01 (10)	1.00 (2)	1.09 (8)
Multiple Bidders	5.50 (19)	7.22 (20)	5.82 (26)	2.80 (35)	3.78 (43)	2.25 (31)
Mt. Balkler-Snoqualmie						
One Bidder	1.00 (1)	1.00 (3)	1.00 (1)	1.62 (2)	1.04 (5)	1.00 (4)
Multiple Bidders	3.18 (42)	2.56 (40)	4.78 (29)	1.46 (30)	1.35 (43)	1.18 (24)
Okanogan						
One Bidder	1.00 (3)	1.00 (3)	1.00 (1)	1.00 (1)	1.00 (1)	1.00 (3)
Multiple Bidders	9.93 (3)	1.65 (4)	3.25 (8)	2.42 (7)	4.38 (6)	3.29 (4)
Olympic (Not Including Sheltonhead)						
One Bidder	1.00 (5)	1.01 (3)	1.00 (2)	1.00 (2)	1.23 (7)	1.00 (7)
Multiple Bidders	3.57 (40)	2.38 (29)	4.52 (30)	1.86 (39)	1.50 (24)	1.37 (17)
Olympic (Sheltonhead only)						
One Bidder	1.00 (1)	1.00 (5)	1.00 (5)	1.00 (3)	-- (0)	-- (0)
Multiple Bidders	- (0)	1.19 (1)	-- (0)	-- (0)	-- (0)	-- (0)
Panhandle						
One Bidder*	1.07 (3)	1.00 (4)	1.00 (1)	1.00 (4)	1.00 (2)	1.19 (7)
Multiple Bidders	5.56 (25)	3.37 (27)	6.47 (40)	4.16 (16)	3.39 (20)	3.48 (12)

Source: U.S. Forest Service Records

* Some one bidder sales are made by sealed bid, so even in those sales, competition in the U.S. market can result in stumpage prices well in excess of the appraised value. Further, one bidder sales in 1983, for example, accounted for only about 3% of USFS volume.

value for stumpage. Commonly, a single price is used across huge tracts or an entire province even though the value of timber may differ substantially in that area. See discussion infra at "C." As is the case with British Columbia, sales in these provinces are noncompetitive.

This is the critical difference in lumber sales in the United States and in any of the Canadian provinces: U.S. sales of timber are competitive, Canadian sales are not. As a consequence, Canadian stumpage sells for far less than comparable stumpage in the United States, and Canadian stumpage sells for much less than a fair market value. It is simply unfair trade that Canadian lumber is flooding our market because of overproduction induced by provincial stumpage largesse.

B. Canadian Timber Prices Are Well Below The Cost Of Comparable U.S. Timber

The cost of Canadian stumpage is a small fraction of the cost of stumpage on what the Canadians admit are "roughly comparable" U.S. forests. See Chart 7 and Table 4. That is, from the Atlantic to the Pacific, similar trees on similar terrain immediately north of the border cost a small fraction of what timber costs south of the border. A 1980 study by David Haley, a University of B.C. forestry economist, showed that in 1978 public stumpage averaged $39.11/m^3$ in Washington and Oregon while stumpage in British Columbia was less than one-eighth of that amount. Haley, A Regional Comparison of Stumpage Values in B.C. and the U.S. Pacific Northwest, Forestry Chronicle (Oct. 1980). Even after mak-

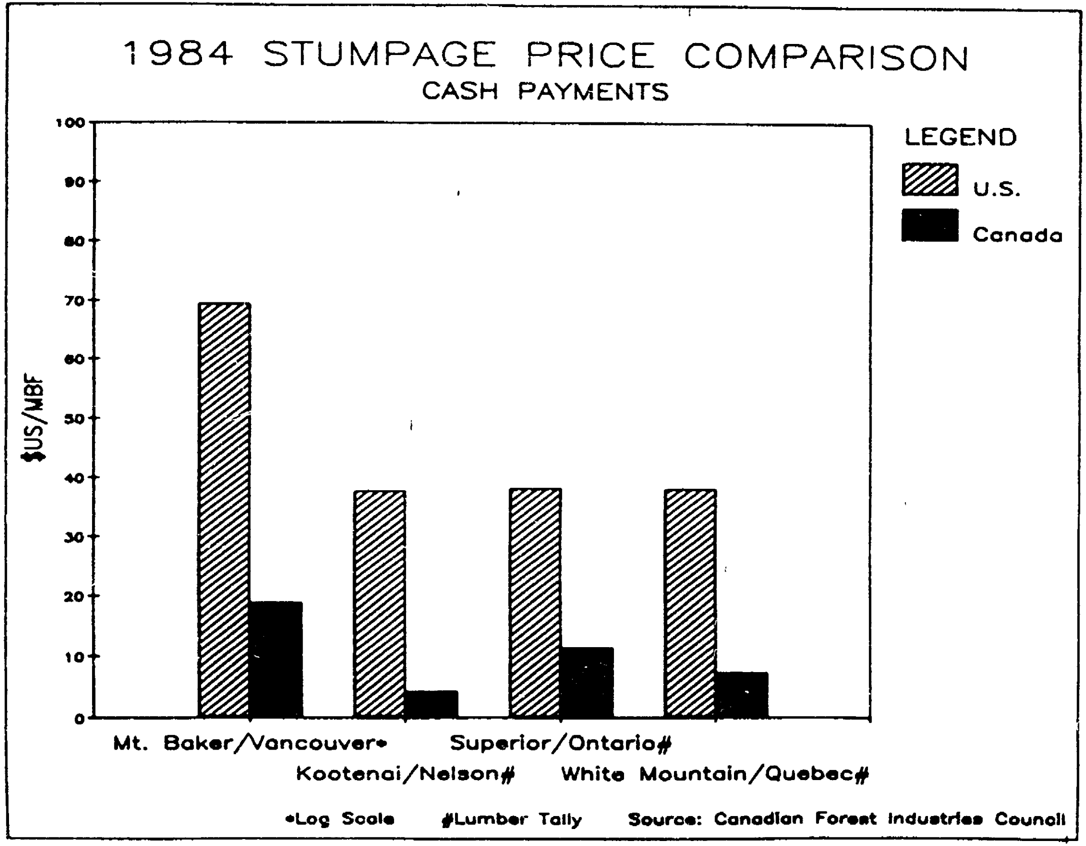
1984 STUMPAGE PRICE COMPARISON
CASH PAYMENTS
LEGEND
U.S.
Canada
$US/MBF
0
10
20
30
40
50
60
70
80
90
100
Mt. Baker/Vancouver*
Kootenai/Nelson#
Superior/Ontario#
White Mountain/Quebec#
*Log Scale
#Lumber Tally
Source: Canadian Forest Industries Council

TABLE 4

STUMPAGE PRICE COMPARISON

(Cash Payments)

Areas Compared (U.S./Canada)	Unit	1980 U.S.	1980 Canada	1982 U.S.	1982 Canada	1983 U.S.	1983 Canada	1984 U.S.	1984 Canada
Mt. Baker-Snoqualmie/ Vancouver	$US/MBF LS	88.26	61.78	50.98	15.01	63.90	16.99	69.98	19.16
Kootenai-Panhandle Nelson	$US/MBF LT	22.50	15.03	18.10	3.80	28.82	4.97	38.00	4.65
Superior/Ontario	$US/MBF LT	26.28	11.44	38.64	11.06	38.06	12.76	38.44	11.75
White Mountain/Quebec	$US/MBF LT	14.22	5.75	17.56	7.00	28.54	6.35	38.36	7.68

Source: Canadian Forest Industries Council.

ing all appropriate adjustments for terrain and quality, B.C. stumpage was a small fraction of U.S. stumpage.

Since then, Canadian stumpage prices have fallen while U.S. stumpage has increased. For example, between 1983 and 1984, as lumber consumption was increasing, stumpage prices in the Canadian Panhandle Forest actually decreased from \$4.97 to \$4.65/thousand board feet (MBF). On the comparable Kootenai Forest just south of the border, prices increased from \$28.82 to \$38.00/MBF. Clearly, Canadian prices are not controlled by market forces. No matter what adjustments or comparisons one makes, Canadian lumber firms receive massive government assistant in the form of undervalued stumpage.

C. Canadian Stumpage Prices Are Well Below A Fair Market Value

Canadian timber sold competitively, either from private land or from the B.C. Small Business Enterprise Program, garners many times the provincially set prices. Sales on private lands are "getting 10 times" the provincial price. The Citizen, Saturday Forum (Prince George, B.C., July 13, 1985) quoting MLA Bob Williams (NDP-Vancouver East). Timber sold in competitive Small Business auctions has sold for as much as 16 times the provincial prices, *id.*,[9] and such sales average three times that assessed value, three times what Canadian officials assert is a fair price for the timber.

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[9] *See also* 1 Forest Planning--Canada, No. 3, 21 (1985). "[T]imber sold through competitive bidding yields ten times more revenue than timber" sold through residual value method.

Ministry of Forests Annual Report 1983-84. Moreover, "competitive" Canadian sales still result in depressed prices for several reasons. First, there are a limited number of buyers and sellers. Second, with 90% of the country's timber supply available for virtually nothing, prices for the remaining 10% are deflated. One B.C. sawmill owner and journalist, based on the Haley study, concludes that "B.C. public coffers are being short-changed by several billion dollars a year" compared to what would be received if B.C. stumpage sold competitively. Drushka, Stumped, 109 (1985).

Similarly, Quebec and Ontario's regulated stumpage prices are clearly incapable of capturing a fair market value. Stumpage across Quebec varies by only $4.50/MBF, from $4.10 to $9.50/MBF. Yet figures from the Canadian cross-border comparison show a difference in 1984 delivered log costs to 22 different Quebec mills of from $96.01 to $214.10/MBF ($U.S.). In Ontario, all stumpage, no matter where it is located, costs $11.75/MBF ($U.S.), but delivered log costs, according to the Canadian data, varied from $95.48 to $197.93/MBF.[10] Since mills continue to operate on provincial timber in those parts of Quebec and Ontario where timber values are low and operating costs are high, it appears certain that mills in other parts of Quebec and Ontario are getting their timber from the Provinces at a bar-

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[10] Supplemental Joint Report to Canadian Forest Industries Council, Cross-Border Comparisons of Indicated Delivered Log Costs for 1983 and 1984 (April, 1985).

gain price, a price that fails to return fair market value to the Province. No doubt it is more expensive to log timber near the Hudson Bay than it is in southern Quebec and Ontario, but there is simply no justification for those mills immediately north of the St. Lawrence River to pay a small percentage of what mills immediately south of that river must pay for virtually identical stumpage. Clearly, Canadian provinces charge far less than a fair market value for timber.

D. High Canadian Logging Costs Do Not Justify Unnaturally Low Stumpage

The Canadian lumber industry argues that while their stumpage fees are a small fraction of U.S. stumpage on comparable forests, their logging costs are so high that the cost of logs, stumpage plus logging costs, delivered to a mill in Canada and the United States are roughly equal. To this end, Canadian lumber firms have produced a chart which shows comparable delivered log costs in Canada and the United States. This Canadian argument, however, is somewhat striking because it casually ignores allocative efficiencies. Assuming that the Canadian data are correct, all things else being equal, it would make more economic sense to log in the United States, where logging costs are lower. The Canadian data are, however, inaccurate. There is simply no reason why similar trees on similar terrain immediately north of the border should cost so much more to log.

Canadian logging costs are manipulated and inflated in order to depress stumpage prices. Logging costs are inflated in several ways. First, logging costs are averaged over huge tracts which do have large areas with less accessible terrain, and higher logging costs, than cross-border forests, thereby allowing the best timber to be sold under market.[11] Second, many efficient Canadian operations hesitate to provide logging data to the provinces because to do so would "raise everyone's stumpage prices," The Citizen, Saturday Forum (Prince George, B.C. July 13, 1985), and, as a B.C. mill owner states, when a producer knows that a Canadian forestry ministry is evaluating its operations, it "is naturally going to become rather lethargic." Drushka, Stumped, 102 (1985).[12] Finally, and possibly most importantly, logging costs are inflated through the use of creative resource accountants who "paint a picture of desperately high costs and desperately low profits, resulting in compassionately low stumpage rates." Using "sinking funds, deferred charges, accelerated depreciation, depletion allowances, reserves, offsets.... other figments of double-entry imagination" and the shifting of profits and expenses of foreign operations, these accountants paint logging cost pictures that "make Dali seem a dilettante." Id. at 105.

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[11] See, e.g., discussion of Quebec and Ontario mills supra at "C."

[12] Drushka reports that the "average efficient operator," upon whom British Columbia bases its logging costs in calculating residual value, is looked upon by market loggers as an "unproductive dolt." Drushka, Stumped, 104 (1985).

In fact, delivered log costs are substantially lower in Canada because of the huge stumpage advantage. Data Resources, Inc., in FORSIM Review (May, 1985), shows that delivered log costs in 1984 in the U.S. Inland region were about $152/MBF compared to $86 in the B.C. Interior. Similarly, log costs in the U.S. South are about $161/MBF while Quebec logs cost $116 ($U.S.). It is not surprising, therefore, that Canadian lumber is flooding our border.

As there is no competition for timber in Canada, to the limited extent that Canadian logging costs are higher than U.S. costs, it is often because the non-market Canadian system encourages inefficiency. Cost increases are passed through directly as lower stumpage. (Since a generous profit and risk is factored in, the system is essentially cost-plus.) The system creates to "some degree . . . a disincentive to be efficient." Id. at 105. MLA Bob Williams (NDP-Vancouver East) complains that Canada has "tended to accept the idea that supply of material to our forest industry should be a noncompetitive supply . . . . Our basic industry isn't really hustling entrepeneurs anymore." Quoted in 1 Forest Planning -- Canada, No. 3, 20 (1985). The results of this noncompetitive, cost-plus system is that inefficient Canadian firms continue to overproduce while more efficient U.S. firms are driven out of business.

IV. CANADIAN PROVINCES MAINTAIN UNNATURALLY LOW STUMPAGE TO INDUCE PRODUCTION AND PROMOTE SHORT-TERM CANADIAN EMPLOYMENT

Canadian provinces sell stumpage at abnormally low prices to promote production and the concomitant employment. One B.C. logger and journalist explains that because the Canadian timber market is noncompetitive many Canadian firms "knowingly overbuilt their capacity," knowing that "politicians afraid of mill closures and lost jobs" would ensure an adequate supply of undervalued timber. Peter Griffiths, Equity, 11 (April, 1984). The B.C. Ministry of Forests has supported such overcapacity to promote Canadian employment.

> T.M. Apsey, the Deputy Minister of Forests [B.C.], advised his entire staff that "Top Priority (his emphasis) must be given to smoothing out and speeding up requests to cut timber. . . . These are special times and require special measures." Mr. Apsey cited poor economic conditions.

Harrowsmith, 31 (Dec. 1983-Jan. 1984). Similarly, when a Canadian firm overcuts a strip of land, it "forces the government -- loathe to risk jobs, revenues, and votes -- into giving the company extra timber." Id. at 24-25.

Since Canadian provinces encourage production and the concomitant employment by giving Canadian lumber firms timber at unnaturally low prices, the price paid for timber does not even cover reforestation and administrative costs. The result in British Columbia in FY 1983-84 was that the Province had an $80.8 million forest deficit, $162.6 million the year before, and $123.7 million in FY 1981-82.

By charging less for timber than what a willing buyer would pay a willing seller, the Canadian provinces intentionally subsidize short-term employment. Correspondingly, when Canada exports lumber to the United States, it exports unemployment. It is simply unfair trade that Canadian mills continue to overproduce with virtually free government raw materials while U.S. mills are being closed down because of the flood of Canadian lumber.

V. CANADA'S BELOW MARKET STUMPAGE FEES DISCOURAGE REFORESTATION

In investigating the management of a tree farm license, the B.C. Ombudsman found that the forest was being mismanaged to promote "short term" employment.[13] While undervalued Canadian stumpage promotes short-term employment, fees are so low that they cannot even cover adequate reforestation.[14] For example, British Columbia allows lumber firms to offset against stumpage fees reasonable costs of reforestation and road building. As of February, 1985, British Columbia owed almost $40 million in credits which could not be offset because stumpage fees were so low. Five-Year Forest and Range Resource Program, 1985-1990 (1985). In

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[13] The Nishga Tribal Council and Tree Farm License No. 1, Public Report No. 4 (June, 1985). Indeed, with respect to the northern portion of that tree farm, 60% of the "logged area has not been properly reforested." Id. at 12.

[14] "In the [B.C.] Interior, the cost of basic silviculture -- never mind intensive forestry -- is about $1.25 per cubic metre. But stumpage is averaging about $1.21 per cubic metre!" Forest Planning--Canada, No. 2, 9 (1985).

effect, British Columbia is actually paying to have its trees cut down.

Les Reed, Professor of Forestry Policy Research at the University of B.C. and former Assistant Deputy Minister of the Canadian Forestry Service, states that British Columbia has been "following an implicit policy of forest liquidation for well over a decade." Vancouver Sun, A 1 (Feb. 18, 1985). A similar problem exists in other Canadian provinces. K.Y. Parker, former president of the Nova Scotia Woodlot Owners and Operators Association, warns that the land is being "raped and ravaged" because the Canadian lumber companies have been given "low leases and monopoly control of Crown land;" the provincial government has "given the land away." Halifax Chronicle Herald, 17 (April 6, 1985).[15] A royal commission on forestry in Nova Scotia

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[15] The Canadian industry claims that it practices "sustained-yield" forestry. In fact, the B.C. Ministry of Forests continues to redefine sustained-yield so as to vitiate its meaning. For example, 2 1976 Royal Commission on Forest Resources, Appendix D, defines sustained-yield as producing, "in perpetuity, crops of equal or nearly equal volumes of wood annually." Quoted in 1 Forest Planning--Canada, No. 3, 15 (1985). By comparison in Summary: Forest and Range Resource Analysis 1984, at 29, the B.C. Ministry acknowledges that its "sustained yield management must allow for a declining harvest...." According to Les Reed, the B.C. analysis concedes a downward trend in B.C. harvest of 10-20% within the so-called "sustained-yield." See Reed, The Second Option: An Alternate Forest Renewal Plan, Speaking Notes (April 26, 1985). Regardless of how Canadian bureaucrats redefine "sustained-yield," there will be a drastic reduction in Canadian lumber production in 10-20 years if current Canadian policies continue.

Similarly, while British Columbia has significantly increased seedling plantings, reforestation is still woefully inadequate. Those trees planted have a very low sur-

(Footnote continued)

expressed "extreme concern" over the condition of Canada's forests. "It found that only one in every three acres of woodland is regenerated to satisfactory species after logging; that only a small percentage of the logged area is being replanted ..." D. MacKay, Heritage Lost: The Crisis in Canada's Forests, vii (1985).

Reforestation has become so inadequate in Canada that Canadian governments must directly subsidize reforestation despite massive forest deficits. In 1985, the provincial and federal governments signed five-year agreements that will pump more than $350 million in direct government assistance into reforestation. In 1984, $17 million in Canadian federal jobs program funds were spent on silviculture. In the United States, by comparison, the forest industry pays for reforestation through stumpage fees.

The long-term effect of this mismanagement of Canadian forest resources will be a shortage in high quality timber supply and, ultimately, a substantial fall-down in Canadian production. A 1985 study by the University of British Columbia concluded that B.C.'s lumber industry is "15 years

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(Footnote 15 continued from previous page)
vival rate. See Vancouver Sun, C1 (May 7, 1985) (interview with Dirk Brinkman, president of Western Silvicultural Contractors Association). "The Canadian Forestry Service estimates that 25 to 50 percent of the area harvested annually fails to regenerate or reverts to non-commercial weeds." Association of British Columbia Foresters, Economic Development Opportunities in Forest Management (Sept., 1983). The total inventory of insufficiently restocked land in British Columbia is still about 1.8 million acres. The Province, 13 (Vancouver, B.C., May 29, 1985).

away from economic disaster unless massive investment is made in reforestation . . . ." Timber Trade Journal (July 13, 1985). Early in 1985, Bill Young, former Chief Forester of British Columbia, told a public audience that:

> The most recent in-depth analysis has projected that B.C. will have a one-third reduction in its annual rate of harvest if:
>
> -- forest management investments remain at the current level;
>
> -- utilization of the resource remains at the current level;
>
> -- the rate of alienation of forest land maintains the historic trend...[16]

However, a drop in Canadian production of one-third in 10-15 years will not help the U.S. lumber industry. At th time, there will be no economically viable U.S. lumber industry to rebound.[17] The long-term result is that American

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[16] See also Woodbridge, Reed, and Associates, Ltd., British Columbia's Forest Products Industry: Constraints to Growth, prepared for the Ministry of State for Economic and Regional Development, 27 (May, 1984). Significantly, depressed prices caused by Canadian overproduction also inhibit private U.S. reforestation.

[17] For example, the six largest U.S. producers wrote off over $550 million in softwood lumber assets in 1984 alone. By comparison, a survey of softwood lumber producers, representing 30% of U.S. softwood lumber production, shows capital expenditures by those companies dropping from $134 million in 1981 to $61 million in 1984. Economic Consulting Services, Inc., Summary of U.S. Lumber Questionnaire (May 1985). Clearly, the U.S. industry cannot simply await a fall-down in Canadian production.

consumers will be denied a stable, reasonably-priced supply of lumber.[18]

VI. THE CANADIAN LUMBER INDUSTRY HAS ATTEMPTED TO DIVERT ATTENTION FROM CANADA'S UNNATURALLY LOW STUMPAGE

The Canadian lumber industry has repeatedly attempted to divert attention from its undervalued stumpage and the resultant overproduction by claiming that other factors have led to the rapidly increasing share of the U.S. lumber market captured by Canadian firms. In fact, consideration of the other alleged causes for Canadian overproduction reveals that undervalued stumpage is the primary cause of the flood of Canadian imports.

For example, one purported cause of Canadian overproduction is an alleged species preference for Canadian Spruce-Pine-Fir (SPF) over Southern Yellow Pine. Even as-

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[18] In fact, Canadian firms have attempted to mislead consumers by arguing that legislation which would make Canadian timber subsidies subject to countervailing duties would increase short-term home building cost. In fact, a duty of 13.5% would increase the cost of an average home by less than $300, pennies per month amortized over the life of a mortgage. See Effects of Countervailing Duties on Natural Resource Input Subsidies, Congressional Budget Office (Sept., 1985). By comparison, mill closures and unemployment caused by undervalued Canadian lumber is wreaking economic havoc on many American communities. Not only are those communities losing jobs, but, particularly in the Western United States, the tax bases necessary to fund public schools and build roads are evaporating with the closing of mills. If Canada's share of the U.S. lumber market returned to its historic levels, U.S. production would increase by about 5.5 BBF. Employment in U.S. mills alone would increase by almost 17,000. Thousands of more jobs would be added in logging, transporting and related industries.

suming that such a preference exists, there is no species preference for Canadian SPF over Western U.S. SPF. Yet it is Western U.S. production that has been displaced from Eastern, Midwestern, and Southern markets by rapidly increasing Canadian production. See Chart 4. The alleged species preference simply does not explain the 79% increase in Canada's share of the U.S. lumber market.

A. Canada's Rapid Increase In Production And Market Share Is Not Explained By Simplistic References To The Exchange Rate: Dramatic Inflation In The Canadian Lumber Industry Has More Than Offset The Appreciation Of The U.S. Dollar

From 1975 to 1984, while Canada's share of the U.S. lumber market increased by about 65%, the U.S. dollar appreciated 21% relative to the Canadian dollar. One would expect that this appreciation in the value of the U.S. dollar would result in Canadian logging and milling costs decreasing by 21% relative to U.S. costs. Such a cost advantage for Canadian lumber firms might account for their increased share of the U.S. market. The Canadian cost advantage, however, would only materialize if the rates of inflation in the Canadian and U.S. lumber industries were about equal. In fact, inflation in the Canadian lumber industry has totally overwhelmed any cost advantage that Canadian lumber firms would have had from the appreciation of the dollar.

For example, from 1980 to 1984 logging costs in B.C.'s Vancouver and Nelson Forests, <u>expressed in U.S. dollars</u>, increased by 39% and 36% respectively. In the same period, logging costs on comparable U.S. forests, the Mount Baker and Kootenai, decreased by 4% and 2%.[19] Obviously, the appreciation of the U.S. dollar did not result in a logging cost advantage to Canadian lumber firms. In fact, the Canadians assert that their 1984 logging costs, denominated in current U.S. dollars, were 55% higher on the Vancouver Forest than on the comparable U.S. Mt. Baker Forest, 27% higher on the Nelson than the Kootenai, and 28% higher on the Quebec Domanial Forest than the White Mountain.[20]

U.S. sawmill productivity equals or exceeds Canadian sawmill productivity, see "C" infra, and U.S. hourly wage rates are substantially lower than Canadian rates.[21] The strong dollar has not given Canadian firms a comparative

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[19] See Supplemental Joint Report to Canadian Forest Industries Council, Cross-Border Comparisons of Indicated Delivered Log Costs for 1983 and 1984 (Joint Report) (April, 1985) and Joint Report to the Canadian Softwood Lumber Committee (Feb., 1983).

[20] Even if one compares the percentage of change in average variable ex-stumpage prices in U.S. dollars, costs in the British Columbia Interior increased more rapidly than Inland or Southern U.S. costs from 1975 to 1984 and from 1980 to 1984. From 1980-84, production costs of British Columbia Interior mills increased 9% more than costs of Southern U.S. mills. See Prehearing Brief on Behalf of the Coalition for Fair Lumber Imports Concerning Canadian Softwood Lumber Imports (Prehearing Brief), submitted to the International Trade Commission (ITC), 42 (July 16, 1985). The Canadian Forest Industries Council argues that since the U.S. dollar appreciated by 17% from 1980-84 that Canadian mills gained a production cost advantage. Post-Hearing memorandum of the Canadian Forest Industries Council (Post-Hearing Memo), submitted to the ITC, 21 (Aug. 6, 1955). The Canadian Council is simply wrong. British Columbia costs increased faster than U.S. costs after adjusting all costs to U.S. dollars, i.e., taking the appreciation of the U.S. dollar into account. See Prehearing Brief at 42.

[21] U.S. Bureau of Labor Statistics and Statistics Canada.

cost advantage in any of the major lumber production non-stumpage cost components.

With respect to stumpage, however, from 1975 to 1984 the cost of stumpage in the United States rose markedly while stumpage costs on comparable forests in Canada fell dramatically. For example, from 1975 to 1984, stumpage prices in the U.S. Inland and Southern regions increased by 57% and 98% respectively while stumpage in the B.C. Interior fell by 79%. FORSIM Review, Data Resources, Inc. (May, 1985). This stumpage advantage has resulted in the flood of Canadian lumber into the United States. The favorable exchange rate has, no doubt, helped Canadian provinces by limiting the amount of lumber assistance and the size of forest deficits which they would have had to provide and incur to maintain the phenomenal level of Canadian production, but it is not the primary cause of the rapid increase in Canadian production and market share.[22]

B. Canada's Rapid Increase In Production And Market Share Is Not Explained By Productivity Differences: U.S. Mill Workers Are At Least As Productive, And U.S. Mills At Least As Efficient, As Canadian Workers And Mills

The U.S. lumber industry is very efficient. Currently, the productivity of U.S. lumber mill employees is about 378

[22] Indeed, from February through June of 1985 (the last month for which data is available), imports of Canadian lumber escalated rapidly while the U.S. dollar fell. Clearly, simplistic references to the appreciating dollar do not explain complex market forces.

MBF/year.[23] The productivity of U.S. workers is at least comparable with that of Canadian workers. For example, even assuming that the data of the International Woodworkers of America (IWA), located in Vancouver, is correct, Canadian productivity is 388 MBF/year.[24] Significantly, while productivity in the two countries is similar, U.S. labor costs are lower. In 1984, the U.S. hourly wage rates for sawmills

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[23] Economic Consulting Services Inc., Summary of U.S. Lumber Questionnaire (May, 1985). Bureau of Labor Statistics data also show U.S. productivity above 330 MBF.

[24] Productivity and Unit Production Costs in the Softwood Lumber Industries of the United States and Canada (IWA Productivity), submitted by the IWA to the ITC, Table 9 (July, 1985).

The IWA substantially underestimates the productivity of U.S. mill employees. To arrive at U.S. productivity, the IWA subtracts hardwood mill employment from total lumber mill employment (using Standard Industrial Classification 2421) and divides U.S. production by the resulting number of employees. Id. Table 9, n.8. The IWA ignores the fact that S.I.C. 2421 includes remanufacturers of lumber, e.g., employees in mills that make moldings, trusses, and sills. This error leads the IWA to conclude that in 1984 softwood mill employment in the United States was about 137,000. Id. In fact, softwood sawmills in the U.S. employed only about 93,500(est.). Bureau of Labor Statistics and 1982 Census of Manufacturers. By grossly overestimating the number of U.S. softwood mill employees, the IWA grossly underestimates U.S. productivity.

Further, the IWA overestimates productivity of Canadian workers. For example, in the Northern Interior region of British Columbia, the IWA data show the productivity of its union workers to be more than twice the national average. IWA Productivity at Table 9A. Not only is this phenomenal level of productivity unexplained, but the IWA then uses this productivity in calculating the productivity of the entire Northern Interior region. Id. at Table 9, n.5. The effect of such guesses and estimates is significant. In this case, if the production and employment in the Northern Interior is excluded from Canadian productivity calculations, average Canadian productivity drops from 388 MBF/employee to 329 MBF/employee.

and planing mills averaged $8.22,[25] while Canadian mill labor rates averaged $12.23 ($U.S.), including wage rates of $14.97 in British Columbia.[26] Canadian firms did not gain a cost advantage through productivity or labor costs.

In fact, this data does not consider the effect of the type of lumber produced at various mills. That is, U.S. mills create proportionately more lumber which requires a great deal of milling time, e.g. clear and odd-size lumber. Canadian mills produce proportionately more dimension lumber which requires much less milling time.[27] U.S. mill employees add a higher value to the lumber that they produce. Therefore, even though gross output per employee may be comparable, this comparison of production per employee does not provide a complete picture of productivity. Considering all factors, there is no basis for asserting that Canadian productivity is higher than U.S. productivity. It is likely that the opposite is the case.

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[25] Bureau of Labor Statistics.

[26] Statistics Canada. The IWA estimates of wage rates are also grossly inaccurate. See A Comparison of Hourly Compensation in the Softwood Lumber and Wood Products Industries of North America, 1984-1985, submitted by IWA to the ITC (July, 1985).

[27] For example, in 1984 Canada produced less than 40% of total North American softwood lumber production but 50% of stud production.

C. Canada's Rapid Increase In Production And Market Share Is Not Explained By Any Advantage In Transportation Costs: Canadian And U.S. Transportation Costs Are Comparable

The Canadian Forest Industries Council has attempted to show that Canadian lumber firms have a transportation cost advantage to most U.S. markets.[28] The Canadian Council does this by selectively comparing rates to carefully chosen markets from various Canadian and U.S. production regions. In fact, if one compares transportation costs from all of the major producing regions to various markets, it becomes apparent that Canadian firms do not have a transportation cost advantage to most U.S. markets.[29] See Table 5. While some Canadian producers may be closer than Southern or Western producers to Northeastern markets, U.S. producers are closer to all other major lumber markets.

The Canadians also claim a transportation advantage in the use of water shipments because of the Jones Act. The Canadian data intended to demonstrate this advantage[30] ignore, however, the cost of collecting lumber and loading it on ship at its origin and the cost of distributing the lumber from the ship upon reaching the United States.[31] When these costs are included, shipping and rail rates become comparable. If ocean freight provided any real advantage,

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[28] Post-Hearing Memo at 24.

[29] Moreover, the B.C. government recently deregulated B.C. Railway's freight rates, and this is expected to raise rail transportation costs for B.C. firms. Vancouver Sun (Vancouver, B.C., July 20, 1985). Without the assistance of government regulation, B.C. rail costs may exceed U.S. costs rather than being comparable. Nevertheless, there is no indication that the flood of Canadian lumber into this country is abating.

[30] Post-Hearing Memo at Appendix A, Table 2-5

TABLE 5

U.S. and Canadian Shipping Costs, 1984[1/]
($/MBF, Point to Point)

Origin[2/]	Market					
	Los Angeles	Dallas	Miami	Atlanta	Chicago	Boston
South	$101	$14	$42	$26	$29	$ 53
West	30	75	88	87	76	103
B.C. Interior	47	67	86	86	67	91
Quebec	119	68	56	45	32	17

Source: International Paper Company Transportation Department, Dallas, Texas

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1/ Assumptions

- Pounds/MBF Lumber

-- Douglas Fir (West), Kiln Dried	1800 lb/MBF
-- Southern Yellow Pine (South), K.D.	2000 lb/MBF
-- Spruce/Pine/Fir (Canada), K.D.	1550 lb/MBF

- 150,000 lb/Car Rail Car

2/ Origination Points

Gurdon, Arkansas	(South)
Gardiner, Oregon	(West)
Kamloops, British Columbia	(B.C.)
Quebec City, Quebec	(Que)

shippers would utilize it heavily. In fact, only about 3% of total U.S. lumber consumption, up from 2% in 1975, came to the United States from British Columbia by ship. By comparison, Canada's share of the U.S. market increased by 15 percentage points over the same period.

Generally, a comparison of transportation costs for U.S. and Canadian lumber producers shows that Canada has not gained a significant competitive advantage from transportation. See Table 5. Rather, Canadian firms gain their advantage from government-supported stumpage rates.

VII. CRITICAL PROBLEMS IN THE U.S. LUMBER INDUSTRY WILL ONLY GET WORSE UNTIL REMEDIAL ACTION IS TAKEN AGAINST UNFAIR PROVINCIAL CANADIAN STUMPAGE PRACTICES

The U.S. lumber industry faces economic disaster because of overproduction of softwood lumber. The source of that overproduction is Canada's stumpage systems that induce production with unnaturally low stumpage fees. The result of Canada's policies has been the liquidation of the U.S. lumber industry and Canadian forests. In time, if current Canadian policies are unchecked, Canadian production will fall-off substantially, but there will be no economically viable U.S. lumber industry to rebound. Ultimately, the result of Canada's overproduction will be an unstable supply of reasonably priced lumber for American consumers.

To correct the inequities in the North American lumber market would not be an act of protectionism. Free trade must mean fair trade. The U.S. lumber industry seeks only an opportunity to compete on the merits in a competitive lumber market.

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[31] See id. at Appendix A, p. 2.

STATEMENT OF PERRY HAGENSTEIN, PRESIDENT, RESOURCES ISSUES, INC., WAYLAND, MA

Mr. HAGENSTEIN. Thank you, Mr. Chairman. My name is Perry Hagenstein. I am president of Resources Issues, Inc., Wayland, MA. I am a resource economist, doing an independent consulting business. I am testifying on behalf of the U.S. timber industry. I have a very short statement. I have submitted a longer statement for the record. The way in which timber prices are set in Canada helps to explain why the Canadian producers can price their lumber low enough to compete in U.S. markets, even as far as the South. The price of practically all timber in Canada is set and administered by the provincial governments. In the United States, it is competition among potential buyers in the open market that sets the prices for both private and public timber. This competition assures that the timber owner receives full and fair value. The lack of competition in placing timber in Canada leads to prices below full value, gives Canadian lumber producers a cost advantage in their efforts to penetrate U.S. lumber markets. The Canadian provinces also sell timber that is not economically viable if the cost of sales, administration, and reforestation following logging are considered. Each province says that its policy is to maintain harvest levels. This can only be done if cut-over lands are reforested. A comparison of cash payments to the provinces for timber with the costs of sales, administration, and reforestation shows that the payments for timber cannot cover these costs for much of the timber that is harvested. In effect, the provinces are subsidizing timber production and maintaining high harvest levels now at the expense of future harvests in Canada. The strength of the U.S. dollar has been used as an explanation for the high level of lumber imports from Canada, but a careful look at the changes in Canada's lumber share of the U.S. market and changes in the value of the U.S. dollar relative to the Canadian dollar on a year to year basis shows no consistent relationship. Furthermore, a Canadian inflation rate that is higher than the U.S. rate combined with extraordinary increases in Canadian logging and sawmilling costs during the past 10 years offset much or all of the potential advantage to the Canadian producers of a strong U.S. dollar. The failure of the Canadian provinces to charge full market value for timber and their willingness to sell timber at prices that do not cover costs and sales, administration, and reforestation are primary reasons why Canadian lumber has penetrated the U.S. markets so effectively. Thank you.

Senator BAUCUS. Thank you, Mr. Hagenstein. Mr. Koelemij.

[The prepared written statement of Mr. Hagenstein follows:]

STATEMENT BY PERRY R. HAGENSTEIN
BEFORE THE SENATE FINANCE COMMITTEE
UNITED STATES SENATE

September 19, 1985

Timber Pricing

Canadian softwood lumber competes on the basis of price with domestic softwood lumber in U. S. markets. That it is able to do so is surprising because of the inherent disadvantage of Canadian producers in being further from these markets than domestic producers. The way in which timber prices are set in the Canadian provinces helps to explain why Canadian producers can price their lumber low enough to compete in U. S. markets even in the Southern states.

The first important point to recognize is that the price of timber in Canada is not set by the market. Nearly all softwood timber in Canada is owned by the provinces. In selling timber to lumber processors, the price of practically all timber is set and administered by the provincial government.

This differs sharply from the way in which timber prices are formed in the United States. Competition among potential buyers in the open market sets prices for both public and private timber throughout the United States. This competition assures that the timber owner receives full and fair value for the timber. It is this difference in the way in which timber prices are set in the two countries that accounts for much of the ability of Canadian lumber producers to penetrate domestic softwood lumber markets.

To understand how timber prices are set, it is important, first, to recognize that the process differs among the provinces. British Columbia, which accounts for over 60 percent of the Canadian softwood lumber shipments to the U. S., appraises its timber before it is sold. The appraised price is the price at which the timber is sold. In Ontario and Quebec, which together account for about 30 percent of the Canadian lumber shipments to the U. S., timber prices are set by fiat. In Ontario, there is, in effect, a single price for the entire province and it is set legislatively. In Quebec, there is a single price for each of four zones, and the price is set administratively. Stumpage prices are not varied in these huge provinces despite what are undoubtedly large differences from place to place in the real value of the timber.

It is important to understand that timber values vary widely, whether this is recognized in the pricing scheme or not. Some timber has more value than other timber because it is less costly to log, closer to markets, or of higher quality. Failure to recognize such differences in pricing timber in Ontario and Quebec assures that most of the timber will be underpriced if any timber is sold at all.

British Columbia uses a "residual value" appraisal to set its timber prices. In this approach, estimated costs of processing are subtracted from estimated values of the products that can be produced from timber to be harvested. The residual is then divided into an allowance for profit and risk, which goes to the timber purchaser, and a payment for stumpage, which goes to the province. Each timber sale is appraised and a separate price is set.

A similar "residual value" appraisal is used when tumber is sold on national forests in the western United States. The appraisal, however, serves a much different function on the national forests than it does in Canada. The appraised value is the price for timber in Canada. For national forest timber sales in the United States, the appraised value simply sets the floor at which competitive bidding starts. Any errors in the estimates of the government appraisers are crucial in Canadian timber sales because they will be directly reflected in the price of the timber. For the U. S. national forests, it is the competitive bidding process that sets the price. Errors in the estimates used in the appraisal do not show up in the price for the timber.

The effectiveness of competitive bidding in establishing a true and fair value for timber is shown by the high proportion of national forest timber sales that sell at prices in excess of the appraised price. The following table compares the average appraised price and the average "high bid," or actual sales price, for timber on several U.S. national forests just across the border from British Columbia in some recent years.

Forest	Period 2nd half 1982	 1st half 1983	 2nd half 1983	 1st half 1984	 2nd half 1984
	....	$/1,000 board	feet	....	
Okanogan					
Appraised	$20	$27	$17	$12	$12
High bid	25	76	39	51	30
Kootenai					
Appraised	5	8	16	10	11
High bid	24	46	38	35	22
Colville					
Appraised	23	13	18	20	20
High bid	31	33	50	30	25
Panhandle					
Appraised	15	14	25	18	19
High bid	46	88	99	56	32
Mt. Baker-Snoqualmie					
Appraised	23	15	59	65	45
High bid	55	73	87	88	53
Olympic					
Appraised	19	18	40	35	25
High bid	44	77	75	52	31

It is evident from this table that the average price paid for timber from these national forests exceeds the average appraised value by 25 to 500 percent or more. This difference between appraised and bid prices is simply the result of competition for timber in a normal open market. Fair value for timber to the landowner, in this case the federal government, is obtained as a result of this competition. Without such competition, the public would not receive its proper economic return on its property.

Consultant reports prepared for the Canadian Forest Industries Council contain estimates of average selling prices for timber in British Columbia. These include the cash payments for timber, which are equal to the appraised price and an adjustment for species and quality that is intended to put these payments on the same basis as for cross-border national forests in the U.S. The estimates for the Nelson region of British Columbia should be compared with those for the Okanogan, Kootenai, Colville, and Panhandle national forests in the table above. Estimates for the Vancouver region should be compared with those for the Mt. Baker-Snoqualmie and Olympic national forests.

	1982	1983	1984
	........$/1,000 board feet........		
Nelson District			
Cash payment	$ 3.80	$4.97	$ 4.65
Adjustment	5.31	5.57	11.85
	9.11	10.54	16.50
Vancouver District			
Cash payment	15.01	16.99	19.16
Adjustment	1.24	.40	(.16)
	$16.25	$17.39	$19.00

A comparison of the cash payments (i.e., the appraised values) for timber in British Columbia with appraised prices for U. S. national forest timber in adjacent parts of the United States shows that the British Columbia appraisals assign a much lower value to timber. When adjustments are made to allow for differences in species mix and quality of the timber, the British Columbia appraisals are still much lower than those in the U.S. There are some explanations for these differences.

First, the value of products from the timber are undervalued. The "residual value" appraisals start with an estimate of the value of products that can be made from the timber. Prices of logs are used in the Vancouver District and the price of lumber, F.O.B. the sawmill, is used in the Nelson District. In making the value estimates, a price of $10 per ton of chips, which are produced from residues of making lumber, is assigned by regulation. In fact, chips bring on the order of $50 per ton on the market. Thus, the appraisal significantly undervalues the products made from the timber.

Second, costs tend to be overestimated. The appraisal process uses estimates of average costs for milling and logging operations over a wide range of situations. Under any circumstances, this would substantially overestimate costs for the better situations. But if the objective of pricing timber is to encourage harvesting the lowest valued stands, and this seems to be the case in British Columbia, high cost estimates will be used because this will lower the price of the timber. Thus, there is an inherent bias in the British Columbia appraisals toward using high cost estimates.

Taken together, the underestimates of product values and the overestimates of milling and logging costs lead to appraisals that undervalue the timber. This would be little cause for concern if prices were set by competition in the market and the appraisal simply set a starting point for competition to begin, as in sales of U.S. national forest timber. Competitive bidding for timber favors those producers with the lowest costs and assures that purchasers use the highest value of product outputs when they calculate bids.

Reforestation

Timber harvests in Canada are at levels that cannot be sustained well into the future. In an influential 1978 report, Forest Management in Canada, F.L.C. Reed and Associates Ltd. of Vancouver, British Columbia, state (page iii) that "the current state of forest management in each province . . ., at best, . . . is minimal and large areas receive little or no management because of a lack of commitment as a requirement for staying in business and a lack of funds for necessary programs." The report further notes (page 143), "none of the provinces assign adequate priorities to regeneration and timber stand improvement."

The conclusions of the F.L.C. Reed report are still valid. Much of the timber inventory used in calculating timber sale targets is not economically harvestable unless subsidized in some fashion. This has not changed since the F.L.C. Reed report was issued.

The high timber sales targets and the failure to reforest cutover lands adequately are important in two ways to the issue of Canadian lumber imports. First, it is clear that the provinces are now putting more timber on the market each year than can be supplied in another decade or so. Second, timber is being underpriced because the provinces are failing to cover the costs of reforestation, which is said by the provinces to be a fundamental objective of their forestry programs.

As long as reforestation of cutover lands is a basic policy of the landowner, in this case the provinces, reforestation costs can be considered one of the costs of timber harvesting. I have no estimates of the costs of reforestation in Canada. However, reforestation costs for U.S. national forests in the Northern Region were $18.76 per 1,000 board feet of timber harvest in 1978. In 1983 dollars, this is about $27.00 per 1,000 board feet. Similar figures for the Pacific Northwest Region and the Eastern Region ($1983) are $12.75 and $17.25. Conditions in Canada might be somewhat different, but it would be surprising if these costs for reforestation were vastly different from those in parts of Canada just across the border.

The average cash payment for timber in the Nelson District in 1983 of $4.97 per 1,000 board feet of harvested timber does not cover the reforestation costs of about $27.00 per 1,000 board feet for the Northern Region national forests. In the Vancouver District, the cash payment of $16.99 barely covers the $12.75 reforestation costs for the Pacific Northwest Region.

Even if the estimates for reforestation costs would be somewhat high for conditions in British Columbia, it is clear that fees from much of the timber that is now sold cannot cover reforestation costs. If the Province's policy of reforestation is real, these costs must be met from general funds. If this is so, timber sales are being subsidized by the Province.

Exchange Rates

It is not clear that the change in favor of the U.S. dollar in the general exchange rate between the U.S. and Canada over the past decade has caused a substantial increase in softwood lumber imports from Canada. It is obvious that the Canadian dollar has weakened during the same period that lumber imports from Canada have increased. But this does not necessarily mean that increased lumber imports were the result of the change in the exchange rate.

For one thing, the rate of inflation in Canada was substantially higher than that in the U.S. since 1975. Wholesale prices in Canada went up 102 percent from 1975 to 1984, but only 77 percent in the U.S. This offsets about one-third of the advantage that Canadian processors got during this period as a result of the change in the exchange rate. In addition, there appears to have been a substantial increase in recent years in both milling and logging costs in Canada relative to the United States.

The relationship between changes in the exchange rate and changes in lumber imports is also confusing. If increased lumber imports can be explained by the increased value of the U.S. dollar in Canada, changes in the exchange rate should be followed by more or less proportionate changes in lumber imports. In fact, in some years the value of the U.S. dollar relative to the Canadian dollar has gone up and the Canadian share of the U.S. softwood lumber market has gone down. In other years, there has been no change in the value of the U.S. dollar, but the Canadian market share has increased. Relating changes in market share in one year to changes in the value of the U.S. dollar in the previous year does not improve the relationship.

As a result of these considerations, a conclusion that the increase in Canadian lumber imports has been caused by the increased value of the U.S. dollar is not warranted.

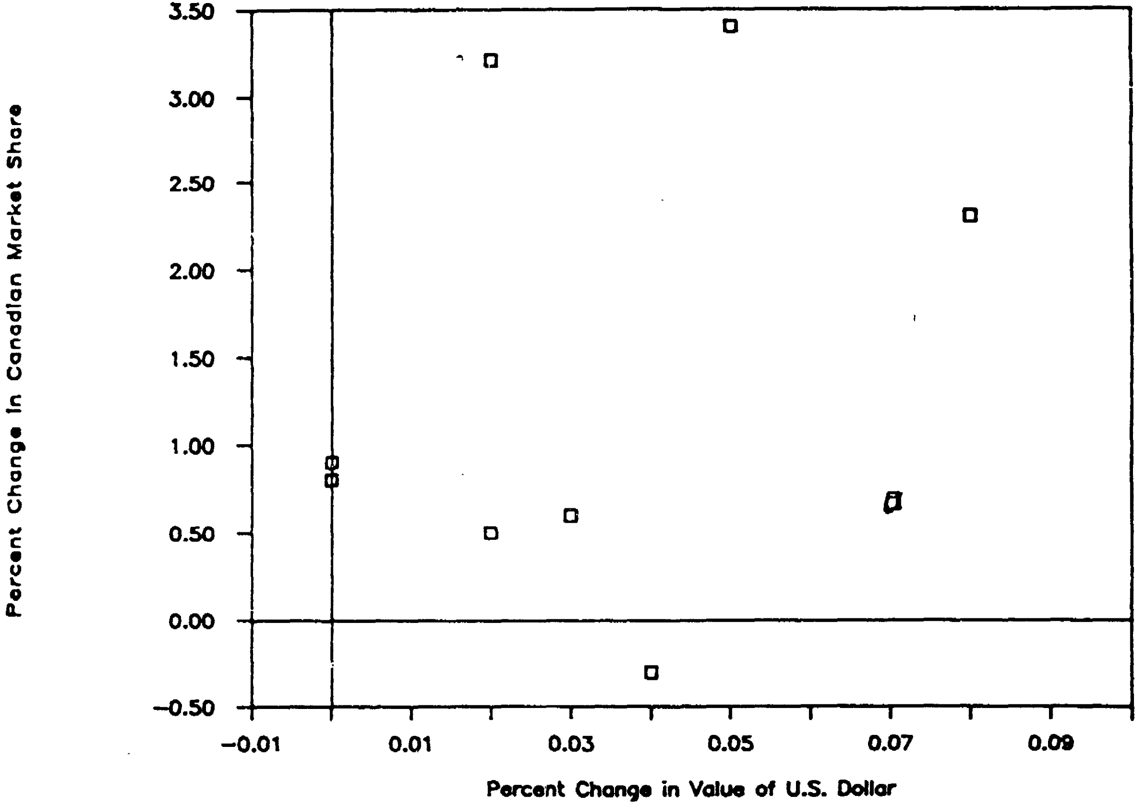
Summary

Canadian provinces sell timber at substantially less than its full and fair value. Selling timber at its low appraised value in British Columbia and at fixed administered prices in the other provinces gives Canadian lumber producers an advantage over those in the United States, who must pay full value for timber. Competitive bidding for timber in Canada would help put Canadian producers on an equal footing with U.S. producers.

Despite their stated policies, Canadian provinces are failing to reforest their cutover lands and are harvesting timber at levels that cannot long be continued. The costs of reforestation in Canada are not being covered by the selling price of timber, thereby allowing substantial amounts of otherwise uneconomic timber to be put on the market.

The large increases in imports of Canadian lumber into the U.S. over the past decade cannot be explained solely by the increased value of the U.S. dollar relative to the Canadian dollar. The effects of the increased value of the dollar have been substantially discounted by more rapid inflation and sharp increases in logging and milling costs in Canada.

MARKET SHARE VS. STRENGTH OF US DOLLAR



STATEMENT OF JOHN J. KOELEMIJ, PRESIDENT, NATIONAL ASSOCIATION OF HOME BUILDERS, WASHINGTON, DC

Mr. KOELEMIJ. Yes, sir. Mr. Chairman and members of the committee, my name is John Koelemij. I am the president of the National Association of Home Builders. I appreciate the opportunity to testify on the state of the U.S. forest products industry and ask that the written statement be made part of the record. Let me assure you that, at the beginning of my statement, I am by no means an expert on the complex issues of international trade. I am concerned about the trade deficit and the importance of retaining and increasing American jobs and not just because American workers buy the homes that we build. Our overriding concern remains the budget deficit. It is our belief that serious and sustained deficit reduction would lead to a decline in the overvalued dollar, which would strengthen our Nation's competitive position in trade, lead to lower interest rates, and create the climate for a long-term period of economic growth. But Mr. Chairman, as I said, I am not here to advise you on how to deal with the overall trade imbalance. My contribution to this debate is much narrower, but no less important to the average American consumer. In this rush to judgment on trade legislation, we are concerned that certain, perhaps unintended consequences of proposed action in this area have not been thoroughly analyzed. Simply put, we are deeply concerned that imposing a duty on Canadian softwood perhaps as high as 60 percent of the current price of Canadian lumber imports could be very damaging to the price of new homes and could compound other factors which would deprive first-time home buyers of the opportunity for home ownership. I will not go into the history of the import controversy, nor will I take your time to go over the argument of whether or not a subsidy exists. All of that appears in my written statement. I would like to mention we are satisfied that the Department of Commerce did a thorough study on the allegation of a subsidy on Canadian timber in 1982. Their findings showed that no significant subsidy existed and therefore no duty was imposed. I would like to highlight a few items from my written statement which are relevant to this topic and explain why I am here today. In 1984, the residential sector consumed 64 percent of all lumber consumed in the United States. The average annual value of residential construction from 1964 to 1984 was $67.68 billion—that is per annum. The Bureau of Labor Statistics showed single family construction worth $1 billion creates 22,000 jobs, and I might add a decrease in construction activity has an equal impact on job losses. Lumber is approximately 22 percent of the total hard construction costs. As the price of lumber increases, so does the cost of housing. For every $1,000 increase in the price of an average home, more than 300,000 families are priced out of the housing market because they will not be able to qualify. As you can see, we are talking about a significant ripple effect on the economy. We, therefore, hope that you will weigh your decision carefully when you consider duties. The events which could be set in motion as a result of the import duty could affect a large segment of the economy and deprive many first-time home buyers of the opportunity for home ownership. And I want to thank you for allowing me to testify on behalf of our home builders association, and I will be ready to answer any questions. Thank you.

The CHAIRMAN. Thank you, sir. Mr. Withers.

[The prepared written statement of Mr. Koelemij follows:]

STATEMENT OF

THE NATIONAL ASSOCIATION OF HOME BUILDERS

before the

COMMITTEE ON FINANCE

UNITED STATES SENATE

on

THE STATE OF THE U.S. FOREST PRODUCTS INDUSTRY

September 19, 1985

Mr. Chairman and Members of the Committee:

My name is John Koelemij and I am President of the National Association of Home Builders. NAHB is a trade association representing more than 133,000 members of the home building industry.

I appreciate the opportunity to testify on the state of the United States forest products industry.

Let me assure you at the beginning of my statement that I am by no means an expert on the complex issues of international trade. I am concerned about the trade deficit and the importance of retaining and increasing American jobs ... and not just because American workers buy the homes we build. But I would be less than candid if I did not emphasize to you that my overriding concern -- and that of NAHB -- remains the budget deficit and the immediate need to reduce federal spending in FY '86 and beyond. It is our belief that serious and sustained deficit reduction would lead to a decline in the overvalued dollar which would strengthen our nation's competitive position in trade, lead to lower interest rates, and create the climate for a long-term period of economic growth.

But, Mr. Chairman, as I said, I am not here to advise you on how to deal with the overall trade imbalance. My contribution to this debate is much narrower, but no less important to the average American consumer. In this "rush to judgment" on trade legislation, we are concerned that certain -- perhaps unintended -- consequences of proposed action in this area have not been thoroughly analyzed.

Simply put, we are deeply concerned that imposing a duty on Canadian softwood -- perhaps as high as 60% of the current price of Canadian lumber imports -- could be very damaging to the price of new homes and could compound other factors which would deprive first-time homebuyers of the opportunity for homeownership.

History of the Import Controversy

Mr. Chairman, the issue of alleged "subsidies" to Canadian lumber was exhaustively debated and dealt with by the Commerce Department and the International Trade Commission in 1982. At that time, some elements of the American lumber industry blamed import competition for their problems. Most lumber imports come from Canada, where lumber is produced primarily from government-owned timber.

In 1982, segments of the U.S. industry filed a countervailing duty petition seeking the imposition of duties on Canadian lumber imports to offset the alleged government subsidies to Canadian companies. Because of the importance of this issue to the homebuyer, NAHB intervened in the ITC action. U.S. Commerce Department investigators spent months analyzing the allegations of a subsidy, but ultimately concluded that no significant subsidy existed. As a result, no duties were imposed.

Current legislation introduced in both Houses of Congress containing a "removal right" provision would reverse the findings of the Commerce Department. That provision redefines "subsidy" to include the sale of a "removal right" for a natural resource such as standing timber at a price below the "fair market price". In the case of Canadian timber, fair market price is defined as the prevailing price for standing timber in the U.S. Thus, the Canadian government would be found to "subsidize" the industry if its price for standing timber were less than the price for timber in the United States. The law would then require a duty to be imposed on all Canadian lumber imports to offset this "subsidy".

While it is true that stumpage prices in Canada are often lower than stumpage prices in the United States, the existence of such price differences does not prove the existence of a subsidy. For example, a large tree on a parcel of land adjacent to a sawmill is worth considerably more than a second, identical tree on a parcel 1,000 miles from the nearest sawmill. In the case of the first tree, the mill owner must simply cut the tree and haul it next door to be manufactured into lumber. In the case of the second tree, the millowner must cut the tree, and then pay to transport it 1,000 miles before it can be utilized. The cost of transporting the log from the second tree directly reduces the value of the tree and, accordingly, leads to a perfectly justifiable difference in the price of the first tree and the price of the second tree.

Transportation costs are only one of the factors that affect the value of standing timber. Forest industry economists explain that the value of timber is nothing more than the value of the end products (lumber and wood chips), less the costs of logging the timber; transporting the logs to mill; manufacturing the end products; and transporting the end products to market. Factors which affect these costs include the species and size of the timber, the topography and climate of the area in which the timber is located, the proximity of that area to a sawmill, and the proximity of the mill to end-product markets. Thus, the value of timber includes more than the price of the standing tree. In fact, U.S. Forest Service information shows the variation in stumpage prices within the United States is just as great as the variation between the U.S. and Canada.

Current Market Conditions

Duties on lumber imports may benefit some U.S. lumber producers, but they would not address the underlying problems facing the U.S. industry. In addition, the benefit to the lumber industry in the U.S. could well be at the expense of other U.S. jobs.

One of the key factors is the exchange rate. The U.S. dollar has appreciated considerably against most foreign currencies over the past several years. This appreciation has affected the lumber industry in two ways. First, U.S. lumber exports have largely collapsed in the past few years, leaving more domestic supply to be sold for domestic consumption. Second, U.S. imports have risen as the appreciation of the dollar has given a competitive advantage to imports. This one-two punch from the exchange rate has undoubtedly contributed to current conditions in the lumber market.

Another factor that has hurt the U.S. lumber industry is transportation costs. The Jones Act prohibits the shipment of U.S. lumber to domestic ports on foreign flag vessels. Thus, U.S. lumber dealers indicate that producers in British Columbia can ship lumber to eastern markets more cheaply than producers in the Pacific Northwest can. In addition, the gradual deregulation of rail rates in both countries appears to have favored the Canadians.

A third factor that has hurt U.S. producers, especially in the Pacific Northwest, is speculative overbidding for the right to cut timber on public lands. The booming lumber market in the late 1970's led U.S. companies to overbid for timber contracts. When lumber prices did not increase in accordance with bidder's expectations, U.S. companies found themselves locked into contracts on which they could not possibly cut timber at a profit. Congress eventually provided a $1.3 billion relief package as a result of overbidding in 1982.

Impact of Possible Duties on the Housing Consumer

If legislation is passed to impose duties on Canadian timber based on the stumpage price, substantial construction cost increases can be expected to follow.

Lumber is the main building material used in home construction and housing construction currently accounts for over 60% of the softwood lumber consumed in the United States. The Census Bureau estimates that the average annual value of new residential construction from 1964 through 1984 (in constant 1977 dollars) was $67.68 billion. According to the Bureau of Labor Statistics, single-family construction worth $1 billion creates 22,000 jobs. Of those, 9,500 are in the construction and land development industries and 12,500 are in manufacturing, mining, transportation, wholesale trade, services and other industries.

Lumber is a key part of home construction. In 1984, lumber was 22% of tota ard construction costs. For the average priced house in 1984 of $79,900, that meant that lumber cost $7,910 out of total hard construction costs of $35,955. In 1984, the residential sector consumed 27.3 billion board feet, which was 64% of all softwood lumber consumed in the U.S.. Thus, the potential 60% duties on imports, and their ripple effect on other lumber prices, could increase the cost of houses by as much as several thousand dollars. NAHB estimates that for every $1,000 increase in the price of an average home, more than 300,000 families are priced out of the housing market. As you can see, an increase of even a thousand dollars could potentially knock hundreds of thousands of families out of the home owner category. We therefore, hope you will weigh your decision carefully. As home buyer demand decreases, fewer houses are built, and the industry begins laying off workers. This is a cycle with which you are all too familiar.

Finally, Mr. Chairman, I would like to address the bigger picture involving Canadian trade. The trade debate appears to focus on those countries which have imposed barriers to "free trade", but this is not the case with Canada. The United States and Canada have traditionally had a special relationship, and they are each other's best customers in international trade. The legislation now being proposed threatens that historical relationship.

In 8 of the last 10 years, the U.S. has enjoyed a trade surplus with our trading partner to the north. In 1984, the two way trade exceeded $113 billion in U.S. dollars, with Canada still the largest purchaser of U.S. exports. With the larger picture in mind, we would urge caution in considering any type of duty on Canadian softwood lumber.

In addition, 25% of the timber logged in British Columbia (Canada's biggest timber producing region) is done by U.S. companies. Thus, it seems clear that a 60% duty on Canadian timber will have an affect on the price of our domestic lumber. Currently, nearly one-third of the lumber consumed in our country is Canadian, and upward pressure on prices in one-third of the market will cause domestic prices to adjust upward as well.

In conclusion, Mr. Chairman, it is not pleasant to be here today testifying against some of our suppliers with whom we agree on most economic and housing-related issues. But I felt that we had to present our views on the possible serious consequences of impairing duties on the American homebuyer. We ask you to consider these impacts before you reach a decision to tax lumber imports. The added cost will be passed through to the end product user - the consumer. The events which could be set in motion as a result of the import duty could affect a large segment of the economy. The timber industry is important to those of us in the building industry and we would hope our domestic timber industry could be strengthened. However, we strongly question whether a hidden tax of several billion dollars on American home buyers is the best way of doing it. We, therefore, urge caution on legislative proposals to impose duties on Canadian lumber because the solution may prove more costly than problem.

Thank you for inviting me to testify. I will be happy to answer any questions you or other members of the Committee may have at this time.

STATEMENT OF ROBERT WITHERS, PRESIDENT, WITHERS LUMBER CO., INC., WOODBURN, OR, ON BEHALF OF THE NATIONAL LUMBER & BUILDING MATERIAL DEALERS ASSOCIATION, WASHINGTON, DC

Mr. WITHERS. Thank you, Mr. Packwood. I bring you greetings from Oregon.

The CHAIRMAN. It is good to have you with us.

Mr. WITHERS. And from the Economic and Political Science Departments at Polamic. My name is Bob Withers. I am president of Withers Lumber Co. of Woodburn, OR. Accompanying me today is Mr. Harry Horrocks who is the director of government affairs for the National Lumber and Building Material Dealers Association. I would like to summarize my statement and ask that the entire prepared statement, which was submitted, be made part of the record. And I would also like to introduce into the record statements submitted by six companies who are members of an ad hoc coalition consisting of 50,000 firms and representing more than 600,000 employees. The list is attached. The coalition is headed by the lumber dealers which oppose any Congressional restrictions on imported Canadian softwood lumber. Our association represents 14,000 firms spread across the United States, and we are the principal retailers of United States and Canadian softwood lumber in the country. The vast majority of our businesses are small businesses—tend to operate one yard, family-owned type, average sales of $1.6 million annually. But taken as a whole, we are a sizable industry: $31 billion in sales, employment of 260,000 workers in 25,000 locations. Withers Lumber Co. operates four retail outlets and a construction subsidiary located around Salem, OR. We have 85 full-time employees and annual sales of $10 to $12 million. Our company is 60 years old, and I have been associated with the company since 1960. Many lumber dealers across the country buy and sell a considerable percentage of Canadian lumber. Withers Lumber Co. depends almost entirely on U.S. manufactured lumber for its sales. It is interesting to note, however, that the affordability of our purchases of U.S. lumber is dependent on the price of Canadian lumber. Without this free market situation, I would be very concerned about potential U.S. lumber price increases. A great majority of our lumber is U.S. manufactured, green Douglas fir. However, we do buy a large amount in large quantities of Canadian red cedar sidings. U.S. manufactured sidings which would be comparable to the Canadian simply do not exist. The Canadian red cedar example illustrates that direct head-to-head competition for many wood species manufactured in Canada and the United States is in many cases limited. Many times it is consumer preference that dictates the type of lumber we sell. Therefore, we see no long-term advantages for anyone, including the U.S. producers, in restricting Canadian imports. The topic today is of vital interest to us because we are dependent on our customers having the ability to continue to purchase lumber at the lowest possible price, a price set by free market forces, not one artificially inflated by Government edict.

The advantage to domestic lumber producers by the imposition of tariffs or trade restrictions on Canadian lumber might seem obvious. It will allow them in the short run to increase prices, but I remind you: only at the expense of American consumers of housing. The housing industry and the American home buyer simply cannot afford at this time, when we are just emerging from one of our most difficult periods. A few things just in summary. Because of our market sensitivity to price changes, a tariff on Canadian lumber will immediately raise the price of U.S. lumber. Trade restrictions plainly and simply result in a tax to the consumer. The apparent benefit to domestic producers would at best only be temporary, but the increased prices of U.S. housing would be devastating on our building industry and our overall economy. Higher U.S. lumber prices will mean fewer people can buy lumber and fewer people can build houses. This would be especially devastating in Oregon, where according to today's Washington Post, the housing market is absolutely sick. Higher U.S. lumber prices also mean U.S. lumber producers would have to pay more for their timber since U.S. forest timber prices are based on lumber prices. Higher U.S. lumber prices will not necessarily put people back to work. The lumber manufacturing industry has changed. Given recent technological improvements, it is now able to produce a record amount of lumber with fewer workers. Higher prices——

The CHAIRMAN. I will have to ask you to conclude, Mr. Withers.

Mr. WITHERS. All right. Higher prices cannot alter this reality. Finally, high relative interest rates and the resulting inordinate strength of the U.S. dollar is the root cause of the difficulty domestic lumber mills are experiencing. Let's not treat the symptoms. Let's deal with the real problem. Thank you very much.

The CHAIRMAN. Thank you.

[The prepared written statement of Mr. Withers follows:]

NATIONAL LUMBER AND BUILDING NLBMDA MATERIAL DEALERS ASSOCIATION

STATEMENT BY

MR. ROBERT L. WITHERS
WITHERS LUMBER COMPANY, INC.
WOODBURN, OREGON

PRESENTED TO

SENATE COMMITTEE ON FINANCE

ON

STATE OF THE U.S. FOREST PRODUCTS INDUSTRY

SEPTEMBER 19, 1985

40 Ivy Street S.E. • Washington, DC 20003 • (202) 547-2230

Good afternoon. My name is Bob Withers and I am President of Withers Lumber Company, Inc. of Woodburn, Oregon. Accompanying me today is Mr. Harry Horrocks, Director of Government Affairs for the National Lumber and Building Material Dealers Association. I am very pleased to present to the Senate Committee on Finance the National Lumber and Building Material Dealers Association's views on the state of the U.S. forest products industry and, in particular, on issues relating to the importation of Canadian softwood lumber into the United States.

The National Lumber and Building Material Dealers Association is a national trade association, consisting of twenty-five federated regional and state associations of retail lumber and building material dealers. Our member dealers, totalling some 14,000 from all parts of the nation, are the principal retailers of U.S. and Canadian softwood lumber, and supply building materials to the home building, general contracting, remodeling and building maintenance industries, and to the general public. A recent survey of our membership indicates that approximately 60 percent of our retail sales are to contractors, with the remaining 40 percent of sales divided between the "do-it-yourself" public and professional remodelers.

The vast majority of our members are small businesses. They tend to operate a one yard, family-owned establishment, usually located in a small town or community. Despite our small average size --11 workers, annual sales of $1.6 million -- taken as a whole, we constitute a sizable industry, with sales of $31.43 billion, and employment of 263,369 full and part-time workers in 24,940 establishments.

Withers Lumber Company operates four retail outlets and a construction subsidiary primarily located in and around Salem, Oregon. We have 85 full-time employees and an annual sales volume of $10 - 12 million. Our company is sixty years old and I have been associated with the company since 1960.

The lumber dealer has an excellent perspective on the U.S. market and the role of Canadian lumber in that market. Lumber is our largest selling item and, as middlemen between the manufacturer and the lumber purchaser, we see on a daily basis the marketing, wood characteristic and customer preference factors that drive the lumber market.

Canadian lumber represents a sizable percentage of all lumber sold by lumber and building material dealers. In 1984, approximately 30 percent of our industry's total lumber sales volume consisted of Canadian lumber. We sell all types of Canadian wood species -- both Western and Eastern spruce-pine-fir, hem-fir, Western red cedar and Douglas fir -- though the percentage of specific wood species sales vary greatly from one region to another, and from one type of retailer to another.

Our dealers purchase Canadian lumber for a variety of reasons, including sizing, availability and specialized use. In many parts of the U.S., the major reason that retailers buy Canadian is that our customers, whether they be contractors, remodelers or do-it-yourselfers, prefer this lumber and therefore demand it. This customer demand for specific types of lumber is the most important characteristic of the retail lumber market.

This specific customer demand reflects the fact that individual sizes, grades and species of lumber behave very differently in terms of their purpose and use. The reasons for purchasing a particular item relates to the function which that item is going to serve in its final use, not to its cost, and not to whether how much of it comes from Canada or how much of it comes from the United States. For example, Canadian S-P-F is not suitable for structural or weight-bearing use, while Doug fir or American Southern yellow pine would be ideal for such purposes. In contrast, Canadian S-P-F is often preferred for framing and finishing. Lumber dealers who have in-house milling operations often depend entirely on Canadian Western S-P-F as the prime lumber ingredient in the manufacture of "pre-hung" windows, decorative doors and specialized entrance ways. Canadian Western red cedar, because of its decorative and decay-resistant characteristics, is used primarily for siding, paneling and decking. U.S.-made Southern yellow pine is a prime structural lumber used in trusses and joists and is also the principle lumber used as treating stock.

Softwood lumber from Canada possesses attributes and characteristics that make it attractive for purchase for certain specific uses. These characteristics include appearance, grade, handling advantages, supply, and most importantly, what the ultimate building purpose for which the lumber will be used.

While many lumber dealers sell a considerable percentage of Canadian lumber, Withers Lumber Company depends almost entirely on U.S. manufactured lumber for its lumber products. It is interesting to note that the affordability of our purchases of U.S. lumber is dependent on the price of Canadian lumber.

Without this free market situation, I would be very concerned about potential U.S. lumber price increases. The great majority of our lumber is U.S. manufactured green Douglas fir. However, we do buy and sell large quantities of Canadian Western red cedar siding. U.S. manufactured siding which would be comparable to Canadian cedar simply does not exist.

This Canadian Western red cedar example illustrates that direct head to head competition for many wood species manufactured in Canada and the U.S. is in many cases limited. It is consumer preference that dictates the type of lumber we sell. Therefore, we see absolutely no long term advantage -- for anyone, including U.S. producers -- in restricting Canadian imports.

In contrast, we see many major harmful effects that would result from the imposition of duties or other restrictions:

(1) Restrictions on Canadian lumber would have the immediate effect of increasing the price of <u>all</u> lumber purchased by Withers Lumber Company or by any of the approximately 24,000 lumber dealers across the United States. Certainly, Canadian lumber prices would rise, but since lumber is a commodity and subject to the supply and demand rules for all commodities, the price of U.S.-produced lumber would also rise.

Already, the prices for certain types of lumber have a history of being extremely volatile. Southern yellow pine lumber prices, for instance, have gone up and down in much like a roller coaster fashion just this past summer. During a period of 45 days this past summer the price of S-Y-P has varied by 18 percent, ranging from almost record high levels down to a much lower price. Duties or other restrictions on Canadian imports would make lumber price fluctuations even more pronounced, not only for S-Y-P, but for all wood species.

(2) Certain types of Canadian lumber could well be priced right out of the market. Some types of Canadian lumber are of vital importance to the U.S. housing market. Canadian red cedar, for example, is irreplaceable. This species and other varieties are already expensive and an artificial 30 or 40 or 50 percent price increase would have a serious impact on the cost of American housing.

(3) Restrictions on Canadian lumber and corresponding price increases in U.S. lumber would reduce demand for our principle sales product. Reduced demand would result in reduced sales and put severe strain on our dealers' operating income. Job loss and the increased possibility of lumber yards going out of business would be the natural outcome.

After an extremely difficult transition period, the majority of dealers would probably be able to cope with significant lumber price increases. However, our customers might not be so fortunate. Homebuilding is a critical part of our lumber retailing, and we are concerned with the average homebuilder's ability to absorb lumber cost increases. Most homebuilders are small companies that build 20 or fewer homes a year. Since lumber and wood products represent 20 percent of the typical contractor's costs in constructing a home, a significant price increase in lumber would severely pinch his operating costs and profits. Under this scenario, lumber and building material dealers would sell less lumber to those contractors who are building fewer homes, and loose valuable contractor customers among those who are forced out of business.

(4) Artificially high lumber prices would adversely affect the ultimate consumer of lumber -- the American home buyer. Higher priced housing would curtail the number of potential homebuyers who could afford a new home, reduce sales, and dampen one of the few booming economic sectors of our national economy. Clearly, the imposition of restrictions on Canadian lumber threaten grave economic consequences for all aspects of the housing industry and eventually for the entire nation.

We thank you for the opportunity to present our heartfelt and well-considered views.

The CHAIRMAN. I believe Senator Mitchell has a statement.

Senator MITCHELL. Mr. Chairman, thank you very much. I apologize but I had another committee that I had to attend. The issue before this committee today is a matter of grave importance to me and the State I represent. In the interest of time and so as to not delay the witnesses, I ask unanimous consent that my statement be inserted in the record at the appropriate point, and I do want to commend you for holding this hearing. I believe something must be done in this area, and I look forward to working with other members of the committee in fashioning an appropriate response to the problem.

The CHAIRMAN. Thank you.

Senator Baucus.

Senator BAUCUS. Thank you, Mr. Chairman. Gentlemen, and particularly Mr. Dennison, I would like you to comment on the degree to which the problem is related to the overvalued U.S. dollar. Could you go into a little bit more detail—both you and Mr. Hagenstein—on the degree to which the problem is not only the overvalued U.S. dollar—that certainly is part of it—but also discuss whether there are other causes?

Mr. DENNISON. I think Perry Hagenstein should comment on that.

Mr. HAGENSTEIN. Could I comment first on the impact of the exchange rate? The exchange rate undoubtedly has some influence on trade between the United States and Canada, but you really have to look at the components of the exchange rate to be sure that it is the exchange rate that is affecting things. I have looked at this to some extent and find that the inflation rates in Canada, especially in the logging and milling area for lumber processing, are much greater than they are in other segments of the sectors of the Canadian economy, as well as greater than they have been——

The CHAIRMAN. Say that again.

Mr. HAGENSTEIN. The inflation rates in logging and milling of softwood lumber in Canada have been greater over the past several years, according to Canadian figures, than has been the rate of inflation in general in the economy.

The CHAIRMAN. Generally.

Mr. HAGENSTEIN. Also, the rate of inflation in the Canadian economy has been greater than that in the United States. This offsets to a substantial extent the effects of the higher value of the U.S. dollar in recent years.

Senator BAUCUS. So, what you are saying is that Canadian costs—first of all costs associated with milling, and second, the inflation rate in Canada as a whole—are greater than in the United States?

Mr. HAGENSTEIN. Are greater than in the United States. Also, the increases in Canadian milling and logging costs have been greater than the increases in the general inflation rate in Canada. Both of these things together tend to ameliorate somewhat the effects——

Senator BAUCUS. Could you be a little more precise and say the degree to which they ameliorate the exchange rate?

Mr. HAGENSTEIN. I have no particular estimate of that.

Mr. DENNISON. I think I can give you that.

Mr. HAGENSTEIN. It is probably on the order of 50 to 60 percent, something on that order, but let Mr. Dennison answer that. That is one factor to look at. Second, I have looked at the relationship between the change in Canadian market shares of the United States lumber market and the annual change—the year-to-year changes—in the exchange rate between the United States and Canada. And I cannot see any relationship between these two measures. If you look at the general charts, the exchange rate—the value of the U.S. dollar—has been going up. The penetration of the United States market by Canadian lumber has been going up at a much greater rate, but when you look at the year-to-year changes, it looks like there is a relationship between the two. When you look at the year to year changes, it is very difficult to perceive any change whatsoever. I think on these matters of the exchange rate that it affects different countries different ways, and I take it you are looking at Japan; and you might find that the relationship between the exchange rates in Japan have followed much different patterns than they have in Canada.

Senator BAUCUS. Mr. Dennison?

Mr. DENNISON. I will give you an example on variable costs, which would include cut, haul, and manufacture in a typical lumber mill. In the U.S. south, it is $82. In B.C. interior, it averages $131. We have a $49 a thousand advantage in variable costs. And in the west, they have a little greater advantage. Just one other point. Canadians are less competitive, higher cost producers than we are; and if it weren't for their subsidized stumpage, they could not compete with us.

Senator BAUCUS. Could you also comment on the Wharton econometrics study which came out recently, saying that restrictions on Canadian lumber imports would have an adverse financial effect on the U.S. economy, particularly on the price of homes? Could either of you two respond to that?

Mr. DENNISON. I will let Perry Hagenstein take the first part, and I will take the second part.

Senator BAUCUS. All right.

Mr. HAGENSTEIN. Senator, I have looked at the Wharton study and reviewed it. It is a Wharton statement actually. Wharton did not find that there would be an increase in prices in the U.S. lumber as a result of the duty that would be placed on—an assumed duty—Canadian lumber imports. Wharton assumed that there would be an increase in prices. That is to say, the assumption by Wharton that there would be an increase in prices equal to the amount of the duty was just an assumption and nothing more. It was not a finding of the study. I find this to be a very peculiar sort of a thing for an economics study to conclude. If a duty is placed on Canadian lumber, there is going to be a decrease in imports of Canadian lumber. At the same time, there will be some increase undoubtedly on the price of lumber in the United States market in general. The extent of the increase on United States lumber prices is going to be related to the ability of the U.S. industry to respond to higher prices, given that there is about 20 percent of the capacity in the U.S. lumber industry is laid up at the present time. My guess is that they could respond very well to a modest increase in prices and hold the total increase in prices that Wharton referred to down very considerably. I think these findings that I have just mentioned—and I have also looked at the Congressional Budget Office study which came out just very recently; and the Congressional Budget Office study was very critical of the Wharton study. And I agree with the Congressional Budget Office study on this very point.

Senator BAUCUS. What was the CBO criticism?

Mr. HAGENSTEIN. The CBO criticism was exactly the same as mine, that Wharton assumed an increase in prices, rather than look at the question of how much would prices go up in the United States if a duty were placed on Canadian lumber imports.

Senator BAUCUS. Mr. Dennison?

Mr. DENNISON. The CBO study says there would be a $300 increase on the average house. That is out of an approximate average price of $75,000. Lumber is only about 3 percent of the cost of a house, so we are talking about pennies per month. But the main thing is that a short-term increase would be very limited, but the long-term damage, when we shut down American industry, and let Canadians export their unemployment to us, is so severe that in the long term they would have our market entirely. No one, I don't think, believes that they would keep their prices where they are if they get our industry shut down. They would skyrocket, and that wouldn't do anybody any good.

The CHAIRMAN. Let me ask this. Was it in your statement or Mr. Hagenstein's that said, at the rate they are going, however, with no reforestation, that in 10 to 15 years, they will have denuded their forests? That is in one of your statements, I believe.

Mr. DENNISON. I think that that is roughly true, Senator, but by the time they do that, they will have all of American industry virtually shut down.

The CHAIRMAN. Assuming that is true, and I don't know whether it is or not, but at the end of 10 or 15 years, where does the timber industry then go? There will still be a demand for wood, and there will be none left in Canada.

Mr. DENNISON. The first thing that happens is the American consumer pays a wild amount of money for his wood, and the second thing that happens is that it would take industry anywhere about 3 to 5 years to gear up to supply it from U.S. sources. And in the meantime, we would have the woods full of hardwoods—take our woods back to a climax forest. We would have lost timber because we wouldn't be able to invest in preplanning reforestation and the things that we do in intensive management, which are in general required by law, as you know.

The CHAIRMAN. Let me ask you this. As I recall, the Canadian wage rates in the mills have always—at least for the last 30 or 40 years—been comparable at to the wages in the northwest. The same union has them organized, as I recall. Is that roughly true?

Mr. DENNISON. Roughly speaking, they are higher now.

The CHAIRMAN. Higher now?

Mr. DENNISON. Higher now.

The CHAIRMAN. They certainly have always been at least comparable. This has not been a low-wage situation.

Mr. DENNISON. They are currently in general higher.

The CHAIRMAN. All right. And their mills are not any more efficient than ours?

Mr. DENNISON. Less in most cases.

The CHAIRMAN. All right.

Mr. DENNISON. Although they have doubled production in the last 10 years, Senator, to answer one of the questions you asked before.

The CHAIRMAN. That is different, though, than making their mills more efficient? You mean doubling production by doubling the number of inefficient mills?

Mr. DENNISON. Sure.

The CHAIRMAN. I am curious why, only recently, then has the stumpage issue become one of unfair competition when they have been doing it for 75 years.

Mr. DENNISON. I guess that is the point I was getting at. In the last 5 years, they have doubled their production, from about 10 billion feet to 20 billion. And that is aimed right down the throat of the American market.

Senator BAUCUS. Is the answer to the chairman's question that, even though their practice is the same, as Canada has maintained this practice for some time, that it is engaging in this practice much more aggressively on a much more widespread scale. That is, in the B.C. Province, for example, which produces about two-thirds of Canadian timber, has been to use old stumpage as part of employment since Canada has had some hard economic times, and also basically to try to penetrate not only western markets, but also in the last few years to practice much more aggressively so they can penetrate southwestern, southeastern, and in fact, all markets throughout the United States. The same practice has been there; they have just been practicing it more aggressively in approximately the last decade?

Mr. DENNISON. There are public statements to the effect that they are going to create employment by pricing their timber so that it does create employment, which means they are exporting their unemployment to us.

The CHAIRMAN. That is the key. Wages are about the same or higher. Their mills are somewhat more inefficient. It is the fact that they will not sell their timber the way we sell our timber that makes it unfair. Is that the issue?

Mr. DENNISON. That is part of it. Remember, about 95 percent of the Canadian timber is owned by the governments up there, and down here only one-third of the timber comes from Government land; and even if the Government gave us the timber, we still have to make a profit for the people who own the two-thirds of the land from which the lumber comes.

The CHAIRMAN. That is nationwide, though. That is not true in the northwest. The great bulk of our timber in the northwest is still coming off of public lands.

Mr. HAGENSTEIN. Senator, I think that the fact that the Canadians are selling timber at less than fair market value—at less than what it is worth—is evidence that they are subsidizing timber sales. And I think that is unfair.

The CHAIRMAN. Back up a minute. They are not selling it at less than it cost the Canadian Government to apparently have it, hold it, and dispose of it.

Mr. HAGENSTEIN. Yes, exactly. That is wrong. They are selling it at less than—they are selling it at prices, especially where the biggest increases have come—the biggest increases have come in interior British Columbia, in the so-called Nelson District Area, where Canadian timber is being sold at a cost—and it averages somewhere around $4 or $5 a thousand in the most recent per thousand board feet, the most recent figures that I have seen—they are selling it a cost that does not cover the sales administration cost on the order of $10 or $12 a thousand. They are selling it at a cost that also does not cover the cost of reforesting that land.

The CHAIRMAN. Should reforestation be an obligation for them? Is it an unfair practice if they will not reforest?

Mr. HAGENSTEIN. Sir, I think it is an unfair practice if it is in direct contradiction to what they say in their policy statements for the B.C. government. The B.C. government says that they have a policy of sustaining their forests and sustaining forest production over a long period of time. This is not consistent with that.

The CHAIRMAN. Now, let's back up. Whether or not they follow their own policy is not an unfair practice, whether or not it is an unfair practice in the United States. Whether they follow their policy is irrelevant. As a matter of U.S. law, should they have to reforest? Is it an unfair practice if they choose not to?

Mr. HAGENSTEIN. As a matter of U.S. law, I assume it is not an unfair practice.

The CHAIRMAN. No; I have not phrased it right. Should it be an unfair practice if they choose not to reforest and we do?

Mr. HAGENSTEIN. To the extent that it harms our industry and as it is creating an increase in imports from Canada now that cannot be sustained into the future, I guess I would conclude that that is an unfair practice; yes.

Mr. HOFFMAN. I think you don't even have to take it that far, though. I think you can look at the cost of administration in Canada, before reforestation, and they are still selling the timber below cost. So, in effect, if you were a private landowner in Canada, it would cost you more money to harvest your timber than you would get from selling it, and I think that represents a subsidy.

The CHAIRMAN. Senator Mitchell.

Senator MITCHELL. Thank you, Mr. Chairman. Mr. Dennison, in response to one of Senator Baucus' questions, you referred to the relative cost of production in the two countries, other than stumpage. And the Canadians claim that they do have higher logging costs than U.S. producers and, therefore, this justifies their lower stumpage. Do you agree with that? Could you comment on that?

Mr. DENNISON. I guess that if you look at one area, you will find they have higher costs. If they are doing high-lead logging in one area, yes, but unfortunately, Senator, they permit the averaging over a vast area of costs. Now, one mill may do it cheaper, a lot cheaper, but they take an average of the inefficient—the timber is located a long distance from it—and that is what they deduct from the selling price when they get started. And then they continue to deduct high manufacturing costs, high transportation costs; and they finally get down to a virtually zero price. One other important thing is that in this country, we have free enterprise; and two-thirds of this lumber comes off of land where somebody has got to make some money on it or it won't be reforested. It won't be harvested. It will grow up with a climax forest that goes back to the high-lead.

Senator MITCHELL. With regard to reforestation, if the Canadian policies are as suggested here—their stumpage policies leading to overproduction and inadequate reforestation—is there anybody in Canada who is disagreeing with that policy? Are there foresters, environmentalists, anybody pointing out what will occur?

Mr. HAGENSTEIN. Sure, I can comment on that. There was a very influential report, or presumably an influential report, that was written in 1978 by F. L. C. Reid and Associates. Mr. Reid is now at the University of British Columbia, but he had been the Deputy Minister of Forests—sort of the head forester—for the Federal Government in Canada over the past several years. Mr. Reid wrote in 1978 that the failure to invest in regeneration of forest lands was going to cause very serious future problems in Canada; and he has continued to say that and says that right up until today. He has made his voice known on that. The response has not been adequate.

Senator MITCHELL. Is the problem of undervalued stumpage only a British Columbia problem, or do other provinces engage in the same practice?

Mr. DENNISON. The other provinces administratively set the price at whatever price they decide it should be: $2, $6, $8, with no regard to market values because, in general, up there there is only one seller and one buyer. So, you can't have a free market that way. The Government is the seller, and there is one buyer who may be surrounded by 100,000 contiguous acres. To say that that is available to somebody else, you know, just isn't factual.

Senator MITCHELL. And are you saying, Mr. Dennison, as I take it, that the problem of undervaluing something is nationwide there? That while the price is set within each province, and it may vary among provinces, that generally, though, they all engage in very substantial undervaluation?

Mr. DENNISON. Yes, Senator.

Senator MITCHELL. For the same policy reasons that you have been discussing?

Mr. DENNISON. Yes, Senator.

Mr. HAGENSTEIN. Senator, can I elaborate on that just a little bit? In Quebec and Ontario, the Government sets by regulation a single price that covers in Ontario all of the province and in Quebec a single price in each of four very large zones. And that is equivalent to saying that timber is worth the same amount. It is like placing houses on the east coast and having Portland, ME, selling at the same fixed price as they do in Washington, DC. It just simply doesn't make good sense. Prices are set low enough that——

Senator MITCHELL. I wish I could sell my home in Portland, ME at the price I would get for it in Washington, DC. [Laughter.]

Mr. HAGENSTEIN. The prices are set low enough so that the most remote and inaccessible and worst timber can get on the market. That means that everybody else in that province that is getting timber is getting a bargain.

Senator MITCHELL. May I ask one more question, Mr. Chairman.

The CHAIRMAN. Yes.

Senator MITCHELL. Mr. Dennison and Mr. Hagenstein, what should Congress do?

Mr. DENNISON. I think we need help from the Congress, honestly, Senator. I would rather see an administrative solution, but I have been preferring seeing that for the last 10 years and I haven't seen it. And I think that Congress has to help the administration interpret the trade laws as to what is subsidy. We are not asking for protection. We are asking for fair trade, and that would be——

Senator MITCHELL. Specifically what should we do? What do you think we should do specifically?

Mr. DENNISON. Specifically what Congress should do?

Senator MITCHELL. Yes.

Mr. DENNISON. I would say that the Baucus-Gibbons-Long bill is a pretty good solution. It would at least direct an interpretation of the trade laws that would make it fair where you are involved with a natural resource. I might ask Mr. Stein to comment on that, if we have time.

Mr. STEIN. Thank you, Senator. For the record, my name is Michael Stein, and I am counsel to the Coalition for Fair Lumber Imports. And the coalition does support passage of the Baucus-Long-Gibbons bill because the problem in this area of unfair pricing of natural resources is one that is harming American industry. We believe that the interpretation given by the Commerce Department of the law—of the countervailing duty law—is really a cramped and unnecessarily rigid one. The purpose of this law is to make sure that foreign governments, when they are selling in this market, competing against American industries, don't put their thumb on the scale, that the reason for free trade and the reason why this administration is in favor of free trade is so that the doctrine of comparative advantage can work; so that those countries who can produce more efficiently, do, and can trade with countries who can produce more efficiently elsewhere. What happens, though, when a country—a government—controls an important production input and can essentially assist its domestic industry that would otherwise not be competitive to compete in our market against our more competitive industry, the lumber industry is about the best example one can think of. America has more timber closer to mills and closer to markets than Canada does. Its wage costs are lower, not higher. Its mills are more efficient. There is no basis on which Canadians can or ought to be able to sell lumber in our market for less than Americans can produce it. Nonetheless, they do because the Canadian Government is prepared essentially to give away at below market—below what they could otherwise get for their lumber, for their timber—in order to promote a sovereign policy of encouraging employment.

The CHAIRMAN. Let me ask, then, a follow-up question to that. Basically, they are giving away at an artificially low price, a natural resource? In the northwest, we by and large—we don't give away—but we sell at less than the cost of production electricity from Government dams. Is that a subsidy?

Mr. STEIN. I think it might be. The fact of the matter is that——

The CHAIRMAN. It is a natural resource that we are selling at far less than its value or cost to produce.

Mr. STEIN. It is not clear that we are selling it at less than its cost to produce, but remember, there are two tests here. One is that you export something that injures a foreign——

The CHAIRMAN. I am going to come to that second one.

Mr. STEIN. All right.

The CHAIRMAN. We have a great cluster of aluminum companies located in the northwest who depend upon that low cost power. Suppose we let the cost go up to cover the construction costs of the dams that were built 20 to 30 years ago, at artificially low interest rates. The aluminum companies are going to move elsewhere. They stay there because of the subsidized low cost of electricity. Is that an artificial subsidy in the same sense as the Canadian natural resource wood subsidy?

Mr. STEIN. The question is: What would the market pay for that electricity, and what would a willing buyer pay a willing seller for that electricity? And to the extent that it is under market, and to the extent that our exports are coming into other markets and there are no other subsidies from the other market. In other words, I believe that if, for example, Canada subsidizes its electricity substantially—for aluminum production—substantially more than we do——

The CHAIRMAN. Don't wander too for away from what I asked, please.

Mr. STEIN. Yes.

The CHAIRMAN. I will reverse the argument. We complained a couple of years ago about the artificially low price for which Mexico was selling its natural gas. We said it was below cost. They sold it to their domestic manufacturers at the same price as they sold it to their export manufacturers. We said that was an artificial subsidy. Right or wrong?

Mr. STEIN. The ammonia producers have made that claim, and we think the claim is basically correct.

The CHAIRMAN. Because they are selling a natural resource at less than cost?

Mr. STEIN. At less than—not at less than cost. Less than they could get for it in the open market, at less than a fair price.

The CHAIRMAN. All right.

Mr. STEIN. There may come times when the open market is such, for example——

The CHAIRMAN. Here is what I want to find out. The standard for fair competition for American industries in the domestic market ought to be—do all foreign markets sell their products for what the market will bear. If not, must they be charged with unfair competition.

Mr. STEIN. If they injure an American industry.

The CHAIRMAN. But that is——

Mr. STEIN. Canada ought to be able to do whatever it wants with its trees, but the question is, Should it be allowed to do with its trees, as a result of sovereign policies, sell at less than market in the United States and injure a domestic industry? We have a countervailing duty law precisely to make sure that American industries are not injured by this sort of practice.

The CHAIRMAN. But in that case, you can win a countervailing duty case and don't need any further legislation.

Mr. STEIN. If the Commerce Department had correctly interpreted the countervailing duty law in 1983, that would be true. Unfortunately for us, they interpreted the law differently, and as a result, we have to come back to the Congress and ask that the law be straightened out.

The CHAIRMAN. Senator Symms?

Senator MITCHELL. Mr. Chairman, could I just interject on that note? Coming from the only region of the country in which there is not a Federal power facility, as a result of which power rates are——

The CHAIRMAN. Are at the market rates.

Senator MITCHELL. 400 to 500 percent higher there than they are in the Western States, I understand the question that you are asking. [Laughter.]

The CHAIRMAN. We think we may have a subsidy.

Senator MITCHELL. Right. That is very valid. [Laughter.]

Senator BAUCUS. I would like to follow up on that because that is not a fair picture. Canada subsidizes its power production far more than we do. Our northwest aluminum mills could be faced with a bit of a problem because they have to pay a great deal more for it, but I think Canada is starting to subsidize Quebec at two to three mills.

The CHAIRMAN. That is where the aluminum plants could go.

Senator BAUCUS. That is correct. So, there is a subsidy that isn't fair.

Senator MITCHELL. That is why so many french-fried potato processing plants have closed down in Maine and opened up in Oregon and Washington—I mean Idaho and Washington. I just wanted to get Senator Symms back in the discussion here. [Laughter.]

The quality of the potatoes and one-fifth the rate of the electricity. [Laughter.]

Senator SYMMS. Thank you, Mr. Chairman. I want to ask a question of Stan Dennison. I have heard some people—and this may have already been asked—so, if it has been, then please mention that. I have had some people say that it was going to increase the price of newsprint if some of this protectionist legislation passed. Is there any of the legislation pending before Congress—either the Gibbons bill or the quoted bill—that would, in fact, increase the price of newsprint?

Mr. DENNISON. I don't see any reason why it should increase the price of newsprint. In general, chips for the paper industry, are a byproduct of the lumber and plywood industry. It is one of the residuals. It is also one of the residuals in the woods if you properly manage your wood. You do precommercially thin, and then you thin about 10 years later, which provides the paper industry with ample chips. There is some harvesting of timber in the United States for chips, but it is very small in relationship to the residuals that are produced. They would still be produced, and I don't see that that would increase the cost of newsprint or pulp.

Mr. HOFFMAN. Let me add a key point to that. The price of chips is a separate product, and it is traded freely in the United States and to a lesser degree in Canada. And so, if you think about it, there is a completely different set of cost structure that applies to papermill than applies to a wood products plant. They are not really affected by the stumpage price.

Senator SYMMS. Now, in 1982—and I asked this question to the Trade Ambassador—when the lumber industry accused the Canadians of subsidizing—the Canadian provinces of subsidizing—has anything changed since then?

Mr. DENNISON. The Canadians have increased their production tremendously; and as they increased it, they shot at markets that were deeper into the United States—Dallas, Atlanta, Miami, Los Angeles—and successfully did it because their cost of stumpage continued to drop.

Senator SYMMS. So, therefore, I guess you are all saying that their system of stumpage sales encourages overproduction?

Mr. DENNISON. It absolutely does. They have a policy to create employment by producing for the U.S. market regardless of how much demand there is in the U.S. market.

Senator SYMMS. Mr. Hagenstein, did you want to comment on that?

Mr. HAGENSTEIN. Yes. It does encourage overproduction by the fact that the province is absorbing some of the normal costs that should be covered by the logging costs. This means that you can log in areas that are much more remote than you would otherwise be able to log. That adds to the total amount of timber, or lumber, that is produced and adds to the overproduction. That is correct.

Senator SYMMS. We have got all kinds of overmaturity in the Pacific Northwest, if we could just get the Forest Service to give it away——

Mr. HAGENSTEIN. Give it away or pay people to take it away.

Senator SYMMS. Right.

Mr. HAGENSTEIN. We would do very well indeed, I think.

Mr. HOFFMAN. Another important point, too, on that the Canadian licensing agreement between the sawmill and the province requires that, over a 5-year period, they cut a minimum of 90 percent of the agreed-upon timber. So, over that 5-year period, if there is a period of weak market demand, they are required by law to cut all that timber and process it. If they don't, they will lose their license and go out of business. So, they have a very strong economic incentive to continue to operate, no matter what the price of lumber is.

Senator SYMMS. Thank you, Mr. Chairman. Did you all mention if you favor legislation or what you would favor? Was that question already asked?

Mr. DENNISON. Yes, the coalition favors legislation, or the bill presented as Baucus-Long-Gibbons.

Senator SYMMS. Thank you.

Senator BAUCUS. Mr. Chairman, I would just like to reestablish what the existing subsidies rules are. It it is true, isn't it, that both the United States and Canada have signed a subsidies code?

Mr. STEIN. Yes, that is true, Senator.

Senator BAUCUS. The United States has signed and Canada has signed?

Mr. STEIN. It is a signatory to the subsidies code of 19——

Senator BAUCUS. Now is it also true that the subsidies code and implementing legislation provides essentially that a subsidy amounts to a bounty or grant or some benefit bestowed by the Government directly or indirectly to a private or to a public institution which is not in accordance with commercial considerations—that is, below cost?

Mr. STEIN. The provisions of goods or services at a preferential rate is the statutory language, Senator.

Senator BAUCUS. At a preferential rate? And is it also true that Canada is providing goods and services, in this case timber, at a preferential rate?

Mr. STEIN. We believe that is true. The Commerce Department took the position—this is the nub of the issue. In 1983, the Commerce Department said that even though the rate may be well below market, below what they could get for this rate, it is not preferential because they don't prefer one sector in their economy over another sector in their economy. Since they give it away to everybody, then it is okay. And the fact is that they may be wrong on the facts here because their pulp timber is essentially provided at market, whereas their sawlogs are provided at just about the same price, which is of course well below market.

Senator BAUCUS. The point is that it costs more for the Province of British Columbia, for example, in this case to maintain timber and administer timber sales—than British Columbia is getting from the stumpage price.

Mr. STEIN. Yes. British Columbia ran an $81 million deficit on its forest products.

Mr. DENNISON. And they apparently owe $40 million to the lumber companies to reforest.

Senator BAUCUS. All right. One other quick question, Mr. Chairman. There has been some talk that the bill that has been introduced—the Baucus-Long-Gibbons bill—should be modified in some way to assure that we don't "stack the deck" against the Canadians or other countries. Could I ask you about that? Could we modify the bill in response to such criticisms?

Mr. STEIN. The bill, as presently written, would compare directly stumpage prices in the United States with stumpage prices in Canada and use as the measure of a subsidy the difference between the two prices. And the Canadians have argued that it is basically not really fair, that we should look at market conditions in Canada. We are confident that any reasoned look at what is happening in Canada will show that the sales of Canadian timber are well below market, and we would be willing to agree to an amendment of the bill that would provide the following measure of subsidy. We would say that the price of stumpage ought to be what a willing buyer would pay a willing seller in an arm's length transaction, that you should look at premarket sales in Canada and there is a B.C. program where they put timber out for bid; and the prices are generally between three and ten times what B.C. administered stumpage is. And they should look at those as well as other timber.

The CHAIRMAN. A last question of Mr. Dennison and Mr. Hagenstein. We will soon be voting on a textile bill—textile import and quota bill. The principal argument of the textile and apparel industry will be that the extraordinary wage rate differential is unfair competition. In your judgment, is that true? I mean, the differential is there; no question about that. Is that unfair competition? [Laughter.]

Mr. DENNISON. May I have counsel answer that, Senator? You know, I have a peculiar problem: 15 years in Portland and now three years in Atlanta. I would like to punt on that and give it to counsel.

Mr. STEIN. Can I answer that, Senator?

The CHAIRMAN. Yes.

Mr. STEIN. It is not necessary to define that in order to find that stumpage is unfair—Canadian stumpage is unfair—to say that any comparative advantage that another country has is unfair. Whether the low wages abroad that result in a comparative advantage for exporters of textiles should be——

The CHAIRMAN. Is it an unfair competitive advantage within the meaning of the law?

Mr. STEIN. No, Senator, it is not.

The CHAIRMAN. Thank you. I want to ask you a second question. When the representative of the apparel industry testified, I asked him this question: Can the American apparel industry compete in the American market against foreign competition based upon the present wage differential? And he said no. In that case, should we let the American apparel industry disappear?

Mr. STEIN. That is a question that I am not competent to answer, but I would say that that is a question of sovereign government policy about whether we want to keep a textile industry, not a question of whether trade is fair or unfair.

The CHAIRMAN. And if we chose to keep it, it would be because we could not compete against what you would define as fair competition?

Mr. STEIN. That is correct.

The CHAIRMAN. That is a matter of policy, and not a matter of——

Mr. STEIN. Exactly.

The CHAIRMAN. And that is exactly the way we ought to look at these issues. There may be some industries about which we will say: We are not going to let these industries disappear. We don't care if the competition is "fair." We do this in the shipbuilding industry. All military ships have to be built in this country. If we didn't build them in this country, they would all be built overseas. But we don't want our cruisers built in Tokyo, and we don't want our destroyers built in Pusan. That is not a market economy system. That is a policy decision about defense. You then begin to ask: What about timber? What about steel? What about concrete? What about textiles? What about leather? And shoes? Do we have to have those industries in this country. If you answer yes, then you reason backward and say: How do we keep them? You don't argue about fairness or unfairness. However, if you were going to follow a very strict and theoretical policy as to what is fair or unfair competition, you have to let go for those who cannot compete against fair competition. But you must understand that is what is going to happen when you do it.

Mr. STEIN. Senator, we can compete against fair competition.

The CHAIRMAN. I know it, sir. I know it, and we have proven that. I don't think there is any country in the world that can match us, even with their wage structure, because they are simply not that productive. This is even more true of Canada which is unproductive and has a high wage structure.

Mr. DENNISON. I think our big problem is, Senator, that if we let all of our industry go overseas, we lose all of our research and development along with losing the industry. And I believe we have to make something to survive in this country.

The CHAIRMAN. I agree. Thank you very much. Let's conclude with a panel of Irene Meister, John Ward, and David Luke.

Senator SYMMS. All right, Irene Meister. Dr. Meister, why don't you go right ahead. I guess we will go ahead here until we get the second bell, anyway. We won't all run off and leave you.

STATEMENT OF IRENE W. MEISTER, VICE PRESIDENT, INTERNATIONAL, AMERICAN PAPER INSTITUTE, NEW YORK, NY

Dr. MEISTER. Thank you, Mr. Chairman. I am Irene Meister, and I am vice president international, of the American Paper Institute. A description of our industry is provided in our written testimony. Many basic industries, of which paper is one, are considered sunset industries. We are different. Paper is healthy, vigorous, and under normal currency relationships, wholly cost competitive worldwide. Japan is the world's second largest producer and consumer of paper and paperboard. Their costs are considerably higher than those in the United States, especially for such products as pulp, bleachboard, and linerboard. Furthermore, some sectors of their industry are considered by their own government to be structurally unsound. The depressed industries law, which has been in effect since 1977 and is still in effect, has not cured that condition, and in an efficient capacity continues to exist. Imports, however, cannot be blamed for the depressed status of this sector. In 1984, imports of paper and paperboard from all sources around the world accounted for 3.6 percent of Japanese consumption, the smallest percentage among the industrialized countries. The share of paper products imported from the United States in 1984 is 1.9 percent of consumption. The Japanese claim that Japan's market for paper products is open. We therefore ask a simple question: Why is the share of imports so low, particularly after an aggressive effort on the part of the U.S. paper industry to increase exports to Japan? Well, Mr. Chairman, tariffs on paper products in Japan are obviously the first clear-cut barrier that affects the level of imports, not only because they increase the cost of a particular product, but also because these tariffs send a signal to the buyers that the industry remains protected. We are urging our Government to reach an agreement with Japan to equalize the tariffs on paper between the United States and Japan. We are also urging our Government to address the question of the total Japanese system which creates what we call invisible barriers. This is a very complex issue, but we have submitted our recommendations to the Government within the context of ongoing talks that the Under Secretary referred to today. We feel that our negotiators are making a major effort to solve the access problem, but there is no success as yet and we are exceedingly frustrated. We urge Congress at this time to support as strongly as possible this ongoing negoiation, while indicating to the Japanese Government that, if they fail—and indeed they are the symbol of the opening of the market for the others—that Congress then would take very strong measures. I thank you for the opportunity to be here on behalf of the institute.

Senator SYMMS. Thank you for a very concise statement. We appreciate the fact that you stayed under your time limit. Thank you. Now, we will hear from Mr. John Ward.

[The prepared written statement of Dr. Meister follows:]

TESTIMONY

OF

IRENE W. MEISTER

REPRESENTING THE

AMERICAN PAPER INSTITUTE

My name is Irene W. Meister. I am Vice President, International, of the American Paper Institute.

The American Paper Institute is a trade association representing more than 90% of the U.S. production capacity of pulp, paper and paperboard. Ours is among the ten largest U.S. manufacturing industries and, in 1984, shipments of paper and allied products accounted for nearly $96 billion. The industry operates in every state of the union and employs over 682,000 people.

Many basic industries, of which paper is one, are considered so-called "sunset" industries. By contrast, the U.S. paper industry is basically healthy because we have both accessible and adequate raw materials resources, specifically wood, waste paper and chemicals. Additionally, the industry has achieved great savings in energy, has amicable labor relations, progressive management and has continued a high level of reinvestment, even during the recent recession, which assures continuing technological progress. In 1984, the industry's exports were $4.5 billion compared to $2.5 billion a decade ago.

For several decades, the U.S. paper industry has been in the forefront of industries and agricultural enterprises that have supported the free trading system. We also believe, however, that free trade cannot be one-sided, if it is to succeed in producing similar economic benefits for the trading partners. Most major products of our industry, such as pulp, newsprint, kraft liner, recycled paperboard, bleached board, uncoated printing papers, and others, enter the United States duty free. Duties on coated paper and on writing paper are very low.

Japan is the world's second largest producer and consumer of paper and paperboard. Technologically, it is a modern industry, but its costs are considerably higher than those in the U.S., especially for certain commodity grades such as, for example, kraft linerboard, bleached board and pulp. This results from higher costs in Japan for such basic inputs as wood, energy and certain chemicals. It also appears that some sections of the Japan paper industry are structurally unsound and, for that reason, these sectors have been under the protection of the Depressed Industries Law which was first established in 1977, renewed in 1979, and again renewed in 1984. So far, however, this law has not made these sectors of the Japanese paper industry internationally competitive; considerable overcapacity, resulting in a depressed market for paperboard, continues to exist. Imports into Japan cannot be blamed for the depressed status of the Japanese paperboard industry. In 1984, imports of paper and paperboard from all sources accounted for 3.6% of Japanese consumption of these products, the smallest percentage among the industrialized countries of the world.

The share of paper products imported from the U.S. has dropped from 2.1% of Japanese consumption in 1983 to 1.9% in 1984.

The Japanese tariff on kraft linerboard is currently 8.5%. It is less than 1% in the U.S. today and will be zero in 1987. For paper and paperboard, the U.S. market is truly open, and this coupled with the high value of the dollar explains why paper imports from all sources in 1984 accounted for 13.7% of U.S. consumption. This is in spite of the fact that we have abundant wood and energy resources.

We often hear from the Japanese government and industry that Japan's market for paper products is open. We are, therefore, asking a simple question: If that is true, why is the share of imports so low, particularly after an aggressive effort on the part of the U.S. paper industry to increase exports to Japan? For example, in 1984 Japanese imports from the U.S. of kraft linerboard - which is the inner and outer linings of the corrugated box -- were down by 13% and for seven months in 1985 they were running 18% below the same period in 1984.

Tariffs on paper products in Japan are obviously the first clear cut barrier that affects the level of imports, not only because they increase the cost of a particular product, making it less competitive, especially during the period of an unfavorable yen/dollar relationship, but also -- and this is very significant

-- because these tariffs send a message to the buyer that the domestic industry remains protected. We are urging our government to reach an agreement with Japan to equalize the tariffs on paper and paperboard between the two largest producing and consuming countries, the U.S. and Japan.

The question is why some sectors of the Japanese paper industry are not responding to the normal competitive forces that would eliminate non-competitive companies, thus bringing supply/demand into a better balance while at the same time opening the market to competitive imports from the United States. The Japanese paperboard industry has now operated under the Depressed Industries Law for a long time. This was supposed to provide a means for removing inefficient overcapacity. This has not happened, and the Japanese paperboard industry continues to operate at very low operating rates. The existence of this excess inefficient capacity clearly hinders any significant expansion of our exports to Japan. Shutting off unprofitable enterprises is always painful, but this pain must be shared by both countries.

We often hear from our Japanese friends that preservation of employment, rather than profitability, is the underlying principle of Japanese industrial society. We can fully sympathize with that and, if Japan chooses to live as an isolated island economy, no one in the world would have the right to question such policies. Japan, however, is not an isolated society, and a large segment of its industrial capacity depends on exports which, in turn, have displaced employment in the United States.

Our industry is seeking an opportunity to serve the Japanese customers as a long term reliable supplier of high-quality products. The reasons why our imports are not expanding are very complex and are rooted, we believe, in various aspects of the total Japanese "system," including tariffs and invisible barriers. The high value of the dollar is also a contributing factor. Our industry unanimously supports the so-called Market Oriented Sector Selective approach, known as MOSS. The forest products industry, including paper, is among the four industries currently under intense discussions between the U.S. and Japanese Governments.

What we hope would result from these discussions is eventual equalization of tariffs and elimination of other barriers that keep import penetration for industries such as ours, at such low levels. We have provided the U.S. Government with our analysis of these barriers. So far, however, we see no results in spite of the strong efforts by our negotiators.

Our industry has reached an exceedingly high level of frustration over the lack of progress in solving the access problem. We believe that current U.S. - Japan negotiations should be given every chance and assistance in attaining a successful resolution of these difficult problems.

Congress should make it clear that it fully supports these discussions and will react strongly if they do not succeed. Increased exports of paper products to Japan will not solve the nearly $50 billion trade deficit with Japan but, together with exports from other cost competitive industries, it would go a long way in stemming the exponential growth of this deficit and in bringing the trade relationship to a more reasonable balance. This would benefit both the U.S. and Japan.

Our industry would be most pleased to keep your committee fully informed about the future developments.

STATEMENT OF JOHN WARD, VICE PRESIDENT FOR INTERNATIONAL TRADE, NATIONAL FOREST PRODUCTS ASSOCIATION, WASHINGTON, DC

Mr. WARD. Mr. Chairman, I am John Ward, vice president of international trade of the National Forest Products Association. Perhaps one of the most important, possibly the most symbolic, and probably the most difficult trade friction issue between the United States and Japan is the problem of market access for processed American wood products. The issue is important because of the huge trade involved. Japan is America's largest customer for wood products, buying over $1 billion annually. Industry estimates these exports could be increased by $500 million a year if Japan's high tariffs were eliminated. The issue is symbolic because it is a classic example of Japan restricting access for manufactured products while allowing raw materials free entry. Certain processed wood products such as veneers, softwood, plywood, particle board, laminated lumber, face tariffs as high as 20 percent. In contrast, logs have no duties. This is a major reason why Japan's imports of processed wood products account for generally less than one percent of consumption, while Japan's need for raw materials is two-thirds filled by imports. The issue is difficult because it involves a depressed industry which is powerful politically and which is backed by the protectionist Japanese Ministry of Agriculture, Forestry, and Fisheries. The United States has been pressing for tariff reduction since before the last multilateral trade negotiations. During the Multinational Trade Negotiations, the United States agreed to eliminate or drastically cut most of its wood products tariffs. In contrast, Japan's singular action of interest to the United States was to reduce its high particle duties——

Senator SYMMS. Mr. Ward, I apologize, but I have got to go over and vote because the clock is running out. So, if you will just take a brief recess, I think Senator Packwood will be back. If you will just put yourself on hold there——

Mr. WARD. I am on hold, Senator, thank you.

[Laughter.]

[Whereupon, at 4:52 p.m., a brief recess was held.]

AFTER RECESS

The CHAIRMAN. I apologize for our apparent disarray. Go right ahead. I am not even sure where you were in your testimony.

Mr. WARD. Senator, I was right in the middle.

The CHAIRMAN. Go right ahead.

Mr. WARD. All right. I had just initiated testimony by saying that we felt that the wood products tariff issue is probably the most symbolic and probably the most difficult trade issue between the United States and Japan, and certainly an important one. And then, I had gone through those points and was just saying that the U.S. industry has been pressing for tariff reduction since before the last multilateral trade negotiations. During the Multinational Trade Negotiations, the United States agreed to eliminate or drastically cut most of its wood products tariffs. In contrast, Japan's singular action of interest to the United States was to reduce its particle board duties by 3 percent, spread over a 9-year period. Well, frustrated by this inaction, in 1982 the U.S. industry made Japanese tariff reduction a primary trade policy objective. The industry launched a campaign, targetting Japanese officials to explain why the elimination of tariffs would benefit both countries. White papers in Japanese were widely distributed, and several are attached to our testimony. Many personal contacts were made, and the effort was carefully coordinated with the U.S. Government, whom I might add has been very, very helpful to us. In early 1985, stemming from an agreement between President Reagan and Prime Minister Nakasone, the MOSS talks were initiated. Unfortunately, progress on forest products has been very slow. Initial meetings were unproductive because of Japanese unwillingness to even discuss tariffs. In later working sessions, some positive steps to improve market access, as Under Secretary Amstutz mentioned, have been taken on secondary issues, such as standards. However, there has been no hint of progress on the primary issue until an announcement was made in April that wood products duties might be reduced, possibly starting in 1987, contingent upon the initiation, acceptance, and success of a rehabilitation program to be undertaken for Japan's wood products industry. On July 30, Japan clarified this vague statement to mean that tariffs on certain wood products would, in fact, be reduced, but the magnitude, phasing, and product specificity of the cuts was still left to the United States imagination. It is in this situation that the United States finds itself with Japan today. Some small progress is being made on secondary issues, but the primary problem of tariffs has not been clearly dealt with. The success of the MOSS talks hinges upon Japan specifying near-term the products involved and the depth and timing of the tariff cuts. The U.S. Government has asked Japan to eliminate all its wood tariffs immediately. The response on this important symbolic and yet difficult issue may well prove indicative of Japan's real sincerity in opening its markets, not only for wood products, but to all U.S. products and services. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, sir. Mr. Luke.

[The prepared written statement of Mr. Ward follows:]

JAPANESE MARKET POTENTIAL

FOR

U.S. FOREST PRODUCTS

A REPORT

BY

THE NATIONAL FOREST PRODUCTS ASSOCIATION

BEFORE

THE SENATE FINANCE COMMITTEE

September 19, 1985

Mr. Chairman, members of the Committee - I am John Ward, Vice President of International Trade of the National Forest Products Association. The National Forest Products Association represents over 2000 organizations and companies involved in the manufacturing and marketing of a variety of wood products throughout the United States. We greatly appreciate the opportunity to report to the Senate Finance Committee on the great market potential that exists for U.S. wood products in Japan - if only Japan's trade barriers were removed.

One of the most important, perhaps the most symbolic and probably the most difficult trade friction issue between the United States and Japan, is the problem of market access for processed American wood products, entry of which is restricted primarily by high tariffs.

The issue is important because of the huge amount of trade involved. Japan is the largest customer for U.S. wood products, buying over $1 billion in 1984. When market conditions were better in 1979, for example, U.S. exports totalled nearly $2 billion. The U.S. industry estimates that exports to Japan could be increased by as much as $500 million a year over a five-year period if these tariffs were eliminated.

The issue is symbolic because it is a classic example of Japan restricting access for manufactured products while allowing raw materials free entry. Certain processed wood products, e.g. veneer, softwood plywood, particleboard, and laminated lumber, face tariffs as high as 20 percent. In contrast, logs have no duties to surmount. This is a major reason why Japan's imports of processed wood products account for generally less than 1.0 percent of its consumption while Japan's needs for raw materials are two-thirds filled by imports. U.S. shipments, for example, are almost 80 percent raw material - specifically logs and chips. However, of the processed products protected by tariffs, we were only able to ship $10 million last year.

The issue is difficult because it involves a structurally depressed industry which is powerful politically and which is backed by the most protectionist Japanese government agency, the Ministry of Agriculture, Forestry, and Fisheries (MAFF).

The U.S. industry has been pressing for tariff reduction since before the last Multilateral Trade Negotiations (MTN) in 1979. During the MTN the United States agreed to eliminate veneer duties and cut 12 to 20 percent tariffs on plywood and 10 percent tariffs on particleboard to 8 and 4 percent respectively. In contrast, Japan's singular action on wood products of interest to the United States was to move its particleboard duties from 15 to 12 percent over a nine-year period.

Frustated by this inaction, in 1982 the U.S. industry made Japanese tariff reduction a primary trade policy objective. Supported by the U.S. government - particularly the U.S. Trade Representative, the Foreign Agricultural Service and the State Department - the industry launched an educational campaign targeting Japanese industry, ministries, Diet members and other officials to explain why the elimination of tariffs on processed wood products would benefit both countries. A series of white papers in Japanese were widely distributed (copies of two papers "Eliminating Japanese Tariffs on Processed Wood Products: Twenty Relevent Questions And Answers" and "Japanese Wood Products Tariff Elimination: Maximum Gain At Minimal Cost" are attached as Appendix A and B), many personal contacts were made, and the effort was carefully coordinated with U.S. government efforts to accomplish the same objective.

Although this tariff reduction campaign was originally initiated on a low key basis, Japanese resistance to action, particularly in the Diet and MAFF, stimulated increasing pressure by the U.S. industry and government, including many members of the U.S. Congress.

In early 1985, stemming from an agreement between President Reagan and Prime Minister Nakasone, the U.S./Japan Market Oriented Sector Specific (MOSS) talks were initiated. Forest products, which was defined to include pulp and paper as well as wood products, was designated as one of four MOSS sectors, with Under Secretary Daniel Amstutz of USDA as the principal U.S. negotiator.

The objective of these negotiations, as conceived, was to identify and remove all trade barriers. Unfortunately, progress in forest products has been slow. Initial meetings were unproductive because of Japanese unwillingness to even discuss tariffs. In later working sessions, the most recent in July with another scheduled next week in Tokyo, some positive steps to improve market access have been taken on secondary issues such as standards.

However, there was no hint of progress on the primary issue until a pronouncement was made by Japan in April that wood products duties _might_ be reduced, _possibly_ starting in 1987, _contingent_ upon the initiation, acceptance, and success of a "rehabilitation" program to be undertaken for its wood products industry. In its most recent Action Program announced July 30, Japan clarified this vague statement to mean that tariffs on certain wood products would, in fact, be reduced. But the magnitude, phasing, and product specificity of the cuts was still left to the U.S. imagination.

Mr. Chairman, it is in this stituation that the United States finds itself with Japan today on the forest products issue. Some small progress is being made on secondary issues but the primary market access problem - tariffs - has not been clearly dealt with. The success of these MOSS talks hinges upon Japan specifying, near term, the products involved and the depth and timing of the tariff cuts.

The United States government has asked Japan to eliminate all its tariffs on processed wood products immediately. U.S. negotiating teams must persist in emphasizing this request. The response on this important, symbolic and yet difficult issue may well prove indicative of Japan's real sincerity in truly opening its markets, not only to wood products, but to all U.S. products and services.

May 5, 1984

JAPANESE WOOD PRODUCTS TARIFF ELIMINATION:
MAXIMUM GAIN AT MINIMAL COST

Eliminating tariffs on processed wood products* offers an ideal opportunity for Japan to reduce trade friction with the United States.

THE ISSUE

Japan permits wood raw material free entry yet maintains high tariffs against many processed wood products. For example, wood panel products--veneer, softwood plywood, and particleboard--face duties of 12 to 15 percent.

- These rates are very high for such basic products. They are very high compared to Japan's average for all commodities. And they are very high compared to US duties of zero to 8 percent. Minimal or no reductions were made by Japan in these rates during the Tokyo Round.

- While wood raw material imports supply two thirds of Japan's consumption, panel products' share is minimal. Of $1.1 billion in US wood exports to Japan in 1983, only 0.5 percent were such products.

Therefore the US government has listed the elimination of these duties as its top priority tariff issue with Japan.

THE OPPORTUNITY FOR JAPAN

Eliminating these tariffs could provide significant pluses for Japan by:

Benefitting its Domestic Economy

- Housing could be stimulated, e.g. eliminating plywood tariffs could decrease the cost of a 2 x 4 house by 180,000 yen.
- Other products, e.g. furniture, could cost less.

Benefitting Japanese Exporting Industries

- Lessened trade friction and an improved US/Japan trade balance would result.
- Japan's exporters, threatened by growing protectionism in the United States, would have a strengthened relationship with the free trade-oriented forest industry, one of America's largest and most influential.
- The United States has offered to support tariff elimination on Japan's major plywood export to America in exchange for such action by Japan on panel products. Japan now exports 23 times more plywood to the United States as it does to Japan.

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*This paper addresses tariffs on veneer, softwood plywood, and particleboard. However the US is interested in Japan's eliminating tariffs on all processed wood products including pine lumber, wood mouldings, medium density fibreboard, and other products.

Benefitting the Japanese Wood Products Industry

- o Japan's raw material supply would be more solidly assured. Duty elimination would counter the argument of those in America who argue Japan does not want US processed wood products.
- o Wood's competitive position would be strengthened.
- o Additional US promotion could expand the total market.

POSSIBLE EFFECT ON JAPANESE PRODUCERS

Eliminating panel tariffs would, on balance, have minimal or no impact on Japanese industry.

Such action would not directly affect farmers, forest growers, or sawmillers. Its only possible impact might be on 20 particleboard and 200 plywood mills, the latter located in industrial centers and already dependent entirely upon imports. Any effect, if any, on the 50,000 employees of these mills would be minimal, slow, and orderly. To illustrate:

- o For Veneer. Japan's plywood industry would benefit from:
  - -- Lower raw material costs
  - -- Assured supply from America substituting for an expected shortfall in SE Asian raw material
  - -- Improved strength, durability, and manufacturing characteristics from US softwood
- o For Softwood Plywood. US competition for Japan's plywood industry, the world's second largest, would be gradual:
  - -- Japan's industry produces only hardwood plywood. Heavy US promotion would be essential to build user acceptance of softwood plywood.
  - -- The Japanese standard (3 x 6 ft.) would require US producers (manufacturing 4 x 8 ft.) to invest in new equipment or additional promotion.
  - -- America's development emphasis would be for structural uses of plywood, markets minimally promoted by Japanese producers to date.
- o For Particleboard. This product, dependent upon furniture markets and GNP, expanded threefold between 1970-80 and is currently renewing this growth rate. Such a growth industry needs no tariff protection.

SUMMARY

American producers, Japan's primary raw material suppliers, want equal opportunity to compete for all processed wood products. Tariff elimination on veneer, softwood plywood, and particleboard would be an important step toward accomplishing this objective. And Japan would have achieved maximum gain at minimal cost.

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ELIMINATING JAPANESE TARIFFS ON PROCESSED WOOD PRODUCTS: TWENTY RELEVANT QUESTIONS AND ANSWERS*

The U.S. government has repeatedly requested that Japan eliminate its high tariffs on processed wood products in the belief that such action would provide major benefits to both countries. Japan has to date not responded to this request.

Many questions are frequently asked regarding this issue. This paper addresses twenty of the most important.

QUESTION	ANSWER
1) How important is the U.S./Japan trade in wood products?	a) Japan is the number one wood customer of the United States and America is Japan's most important supplier. American wood exports to Japan totalled $1 billion last year and have averaged $1.5 billion annually in recent years.
2) Why does the United States want Japan to eliminate its tariffs on processed wood products?	a) The vast bulk (about 80%) of U.S. wood products to Japan are raw materials.
	b) Although lumber is significant, exports of other processed wood products are minimal. U.S. panel products exports to Japan for example, were only $6 million, less than 0.6% of the total.
	c) The United States believes high Japanese tariffs are a major reason why these processed wood exports are so small.

* Prepared by the National Forest Products Association, 1619 Massachusetts Ave., N.W., Washington, D.C. 20036 Telephone: 202-797-5820; Telex: 140950 NFPA DC

d) Reducing these barriers would place American product manufacturers in a more equitable competitive position and would result in increased trade between the two countries.

3) Would wood tariff elimination benefit Japan?

a) Yes, in many ways!
- Lower building and housing costs
- Lower costs for furniture and other products
- Lower raw material costs for plywood
- Improved raw material supply
- Improved competitive position for wood
- Increased overall demand for wood products, stimulated by an improved competitive position and more active U.S. market development efforts
- Improved U.S./Japan trade balance
- Improved U.S./Japan trade relationships
- Greater support for Japan in the United States by the U.S. forest industry.

4) On what wood products items has the United States requested tariff action?

a) The United States believes Japan should eliminate its tariffs on all wood products.

b) U.S. interest is particularly in veneer, softwood plywood, and particleboard tariffs; however, duties on pine lumber, laminated lumber, moldings and millwork, and and medium density fiberboard are also of importance.

5) Is the U.S. request for tariff elimination on wood products a new issue?	a) No. The U.S. request is an old issue. Tariff reduction on wood products was requested before and during the Tokyo Round of the Multilateral Trade Negotiations (MTN). It has been at the top of the U.S. government tariff request list for over two years.
6) Did Japan reduce its tariffs on these products during the Tokyo Round of the MTN?	a) Japan did <u>not</u> reduce its tariffs on either veneer or softwood plywood during the MTN. It did agree to reduce tariffs on particleboard from 14 to 12 percent.
7) What action did the United States take on wood tariffs during the MTN?	a) During the MTN the United States: - elimated 8 to 12 percent tariffs on veneer - reduced tariffs from 12 to 20 percent down to 8 percent for hardwood plywood,(America's largest wood import from Japan) - reduced particleboard tariffs from 12 percent down to 4 percent.
8) Has Japan responded to recent U.S. requests for tariff elimination on wood products?	a) No, Japan has initiated no new tariff reduction for wood products. Its only response has been to move up the phasing of the MTN particleboard duty reduction from 1987 to 1984.
9) How do Japan's tariffs now compare to those of other countries?	a) Japan's average tariff level for <u>all</u> products (heavily weighted to raw materials which enter duty free) is comparable to that of the U.S. and Europe.

b) However, Japan's tariffs on processed wood products are much higher than those of the United States and Europe(see table).

WOOD TARIFF RATES

	Japan	USA	European Community
		- Percent -	
Veneer	15	0	4
Plywood	15	8*	0**
Particle-board	12	4	10

* For hardwood plywood, Japan's major product.
** For 2/3 of the EC's consumption of softwood plywood; the balance must pay a 10% duty.

c) Moreover, Japan's tariffs on processed wood products are higher than those of some developing Asian countries. For example, Taiwan's rates are as follows:

WOOD TARIFF RATES
- Percent -

Veneer	2.5
Particleboard	10.0
Plywood	15.0

Although Korean rates are now higher than those of Japan, that country is considering further reductions on those products.

10) Must Japan act unilaterally on U.S. requests for wood products tariff elimination?

a) No, the United States has offered to proportionally cut its 8% tariff on "sen" plywood, the primary Japanese wood product shipped to the United States.

b) Japan exported $41 million in all plywood products to the U.S. in 1984(20 times more than the U.S. exported to Japan). About 65% of this was sen-faced plywood.

11) Are imports of processed wood products presently having a negative impact upon Japan's domestic plywood and particle-board industries?

a) No. Although total Japanese imports of these products have increased recently, they still represent only a tiny share of consumption,e.g: In 1983, veneer 1.1%; plywood 0.4%; particle-board 0.6%. Imports from the United States represent an even smaller share of Japanese consumption.

12) Have Japan's imports of processed wood products from the U.S. been increasing?

a) In the past several years Japanese imports of U.S. processed wood products have declined, been stagnant, or the amount of increase has been small.

b) Japanese imports of veneer from the U.S. grew from $693,000 in 1979 to $2.5 million in 1984, up 16% from 1983.

c) U.S. exports of softwood plywood to Japan have declined, dropping from $2.2 million in 1979 to $2 million in 1984. U.S. 1984 softwood plywood exports to Japan were up 13% from 1983.

d) U.S. exports of particleboard for Japan have also declined. In 1979 they totalled $1.8 million, and in 1980, due to a shortage in Japan, they peaked at $4.7 million. However, by 1984 U.S. exports of particleboard had dropped to $605,000. In 1984, they increased slightly by 7.6% from 1983.

e) U.S. exports of softwood lumber, some products of which face tariffs, e.g. pine and spruce/fir(6-9%) and laminated lumber(20%) have declined from $254 million to $162 million in 1984. They dropped 11.4% from 1983 level.

13) Is the Japanese housing market(the major influence on most wood products demand) presently at a very low level?

a) Japanese housing starts are projected to be up 4% in 1984 to 1.2 million units, the highest level in four years.

b) Housing starts had been nearly the same level for the prior three years - 1.10 to 1.15 million units. The highs were 1.5 to 1.6 million units occurring in 1976-9.

14) Is Japanese demand for all products in question primarily construction?

a) No. Particleboard is minimally affected by housing. Growth in this product is 70% influenced by furniture manufacturing which in turn correlates to GNP growth. Like the economy, particleboard production grew rapidly in the 1970's(it tripled), stagnated somewhat in the early 1980's and now, like GNP, is starting to grow again.

b) Even the demand for plywood is not entirely based on housing. Whereas 55% of the Japanese plywood produced goes into construction, 30% is used for furniture and 15% for packaging and other applications.

15) Is it true that Japanese action on wood tariffs would affect an an "industry" involving thousands of mills and several hundred thousand workers, particularly in small rural areas?

a) No. The priority U.S. request is for tariff elimination on veneer, softwood plywood and particleboard. These products represent a small portion of the "industry".

b) The Japanese "industry" mentioned is the <u>entire wood products industry</u> involving 250,000 workers in 20,000 mills mainly producing lumber. These mills would be virtually unaffected. Even if Japan were to reduce specialty lumber species and product duties, the effect would be minimal.

c) The panel industries (plywood, veneer, and particleboard) only involve a total of 30,000 workers in 200 plants. If the Untied States were to capture 10% of the market for panel products in 10 years, the maximum number of workers disrupted would only be 300 per year.

d) Most wood panel products plants are not in rural areas but are located near or in major population centers and ports.

16) Is the Japanese wood products industry suffering badly, with more than 1000 bankruptcies per year?

a) The Japanese wood products industry is not in as good of shape as it was in 1976-1979 when housing was more active. Neither is the U.S. industry. However, the Japanese bankruptcy failure rate, frequently quoted, exaggerates the problem. This statistic again applies to the entire wood products industry. Bankruptcies have occurred in panel products; however, they have been substantially fewer in number.

17) Is the Japanese argument reasonable that tariffs should not be reduced because their plywood industry is currently facing extreme economic difficulties(e.g. low profits, reduced production, plant closings)?

a) No. The plywood industry is cyclical and changes up and down can be expected. Japan has refused to reduce tariffs in both up and down cycles.

b) It is true that the Japanese plywood industry has current problems. According to Japanese trade journals, these economic problems have been caused by overproduction and overly high priced S.E. Asian logs(at the beginning of 1983). In fact, the industry is considering forming a depressed industry cartel, action which it has taken on occasion in the past.

c) Although fewer plywood industries are in existence today, they are larger, more efficient plants and are producing as much plywood as were 30% more mills 10 years ago.

d) Plywood production was up 8% in 1983, totalling 1.8 billion square meters, the best of the last three. Production was up 4% in the first quarter of 1984.

e) The profits of the major plywood companies in 1983 were up 43% from the prior year.

f) Veneer tariffs could be eliminated because such action would benefit the economic situation of Japan's plywood industry.(see point 19)

18) Is it true that Japan cannot eliminate tariffs on panel products because its producers are concerned about competition from Indonesia?

a) It is true that Japan is concerned about Indonesian plywood competition, the growth of which has been formidable.

b) However, veneer, softwood plywood and particleboard would only be indirectly affected and other processed products would be unaffected by such competition.

c) Moreover, Japan could eliminate tariffs on only softwood plywood, the product manufactured in North America, as opposed to hardwood plywood produced in S.E. Asia.

d) Competition from U.S. producers will come slowly because they: 1) use softwood rather than the hardwood plywood now produced and accepted in Japan(and produced in Indonesia); 2) produce 4 ft. by 8 ft. panels in contrast to the Japanese standard of 3 ft. by 6 ft.; and 3) produce generally thicker panels - more than 80 % of U.S. production is 12 millimeters and over, 75% of Japanese production is under 12 millimeters thick.

e) In other words, <u>softwood</u> plywood can be defined as a separate product from <u>hardwood</u> plywood. This difference now exists in present Japanese tariff schedules. Japan could take action on softwood plywood - without alienating its S.E. Asian neighbors - by explaining that softwood is a different product from hardwood. Furthermore, there is precedence for differential action in previous U.S./Japan trade negotiations.

19) Would eliminating tariffs on veneer hurt the Japanese plywood industry?

a) No. Eliminating tariffs on veneer, a second stage raw material, could only <u>help</u> the Japanese plywood industry. Such action would reduce costs and give producers an alternative to South Sea logs, the supply of which is being constricted by Indonesia, the Phillippines and other countries.

b) U.S. producers asked their government to eliminate tariffs on all veneer so that their costs could be reduced during the MTN Tokyo Round.

20) Would Japan's forests and forestry workers be heavily impacted by tariff reduction?

a) No. Japan's forests will be virtually unaffected.

b) Japan's plywood producers are already now 96% supplied by imported logs.

c) Japan's forests will not yield quantities of timber which are economically usable for plywood for years.

d) Industrial particleboard - the product now produced in Japan - is a low cost product which, to be competitive generally uses primarily waste material and chips. Thus, thinnings from present domestic forests are not an economic raw material alternative. Structural particleboard which uses roundwood as part of its raw material, is not now produced in Japan.

STATEMENT OF DAVID L. LUKE III, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, WESTVACO, NEW YORK, NY

Mr. LUKE. Thank you, Mr. Chairman. I am David Luke, chairman of Westvaco. I am at the hearing on behalf of the American Paper Institute. With me also is Norma Pace, senior vice president of the American Paper Institute. The trade problem is obviously and clearly creating major problems for the U.S. economy. Prior witnesses have dealt with things like subsidies and various country-specific problems. There is, however, in our view, a more pervasive problem that runs all through the trade issue, and that is the value of our currency, and that is what we would like to address your attention to today. More than 50 percent of the total trade problem is attributable to the value of the dollar. The problem looks this way, as seen through our industry. We are a strong, highly competitive industry. We are acknowledged as the low-cost producer in the world of paper products. Because of that, we are normally the supplier of choice in the paper markets of the world. With those great strengths, our exports have been growing at a very nice, steady rate, and the future looked extremely promising until we ran into the dollar. Between 1979 and 1982, the dollar moved from a condition of being undervalued to a condition of fairly normal and then a little bit above. We were able to assimilate those problems, but in 1983, the dollar began to increase in value again. In 1984, it took off at an extraordinary rate, and that destroyed our ability to compete in the world. We began to lose our customers. We began to see shrinkage in our previously strong export trends, and what was great promise and great potential was turned into a totally different situation. Our ability to control our costs has been excellent. In this country in dollars, we have controlled our costs at a lesser rate than the rate of inflation. Our problem, when we deal in the international markets though, is that we have to translate our costs and prices in dollars into the other currencies of the world. And when we do that, you take a position of strong advantage and you turn it now into a position of serious and significant disadvantage. Through no fault of our own—in fact we have invested aggressively—we have done all the things that we should do—we have gotten all the results in dollar terms that you would like—but the strengths have disappeared. Our export trends that had been growing at the rate of 15 percent per year have now turned down, and they are currently declining at the rate of about 20 percent per year; and that probably will accelerate. Imports in many sectors of our industry were minimal. They have grown from that to a reasonably significant level. In our packaging business, we deal with almost all the industries of the country, and we can see through our experience with our customers and our close relationships, the same sorts of trends occurring in many of the other major industries of the country. This is a nasty problem because currency values tend to have a delayed impact. You don't see the full magnitude of the problem for a little while. At its peak, the dollar was probably 35- or 40-percent overvalued. It has come down since then, but it has trended back up. And currently, even for a strong industry like ours, it has to come down by another 15 or 20 percent to compete. Other major trading nations of the world have learned through bitter experience that currency values have a major bearing on the economic health of such countries. We have been strong enough so that we haven't had to recognize that lesson in the United States until recently, but now we, too, are affected by the problem. We tend to believe that what has to be done is that we have to recognize that, in addition to things like inflation or employment that normally catch our attention in the economic area, currency values have now become just as important as those other things. We tend to believe that, if enough priority attention is put on the value of the dollar, there are a variety of tools, both short-term and long-term, that can be used to influence it in a constructive direction. We acknowledge that in some cases, maybe special remedies are required for particular industries. But we see no way that, on a broad-scale base, enough remedies can be applied to deal with the whole problem across the board of American industry. We think, by contrast, attention to the dollar can make a major contribution, and it is something that can be done without inviting major retaliation in other parts of the world. We would welcome your questions, and we appreciate the opportunity to appear before you.

The CHAIRMAN. Thank you.

[The prepared written statement of Mr. Luke follows:]

TESTIMONY

OF

DAVID L. LUKE, III

REPRESENTING THE

AMERICAN PAPER INSTITUTE

But in 1984, as the trade deficit soared, it became apparent that the dollar was becoming too strong and was adversely affecting U.S. manufacturing activity without economic justification. By the end of 1984, the strong dollar was contributing to shut-downs of normally competitive and efficient plants.

The paper industry is an excellent illustration of how this process works. It is a well-accepted fact that U.S. paper producers are the most cost-effective in the world.

Linerboard, the raw material used in making the paperboard shipping containers that are a major packaging medium, is an international commodity. The U.S. product generally accounts for 60% of the world's exports. In 1984, U.S. exports of linerboard fell 7.7% and so far this year they are 21% below the 1984 level. This loss is unmistakably the result of the strong dollar. While the costs of producing linerboard in the U.S. have been kept in check through heavy investments in productivity improvements, in new technology, energy efficiencies and moderating wage trends, those of its major European competitor, Sweden, have been rising.

Cost Comparisons

Recently, the American Paper Institute compared the historical costs of producing linerboard in a U.S. facility with a Swedish mill. Costs to produce linerboard in the U.S. mill advanced 29% between 1979 and 1985, while the advance in the Swedish mill amounted to 74%.

When converted into rapidly rising dollars, however, the cost disadvantage of the Swedish producers turns into an advantage: The dollar cost of Swedish output in 1985 is 10% below 1979 because of the 94% rise in the dollar compared with the kroner.

At the same time, the American cost advantage is lost in foreign markets because of the high cost of the dollar. The cost to foreign buyers increased 123% in the 1979-1985 years instead of 29% because of the high cost of dollars to foreign customers.

The direct adverse effects on exports of linerboard are compounded by significant indirect negative consequences.

1. By reducing U.S. manufacturing output, the strong dollar has weakened the domestic requirements for paperboard shipping containers and the demand for linerboard in the U.S.

2. The rising costs of U.S. linerboard for foreigners has caused them to seek substitute products and sources of supply, some of which will prove permanent.

Other products of the industry where exports have been adversely affected include folding bleached board and market pulp. Exports of bleached board, which is used in food packaging, fell 2% in 1984 and are running 20% behind 1984 reduced levels so far this year. In some markets, the decline is more than twice that.

Imports have been given a lift by the dollar. In the printing and writing grades of paper, imports now supply 10% of U.S. needs compared with 2-3% which is the historical norm.

These examples in the paper industry can be multiplied by similar experiences in many other industries. Because we are suppliers to many industries in the country, we get an early indication of changes. So far, the indications still suggest losses of markets for U.S. producers.

The current strong dollar results in worldwide business decisions that reflect currency imbalances more than considerations of cost competitiveness and efficiencies of operations. To put it another way, currency values are becoming the basis for industrial policies at a time when these values do not accurately reflect the competitive positions of industries among the various industrial countries. This has long-range implications for the health of U.S. manufacturing industries because some of these are not short-range decisions that can be easily reversed when currency values change.

Positive Effects of the Strong Dollar Have Diminished

Fluctuations in currency values within reasonable limits are not only to be expected, but can frequently bring healthy benefits to the countries involved. The important thing is that if currency fluctuations move beyond a range that is reasonably supportable by economic fundamentals, the consequences can move from beneficial to seriously negative.

During the late 1970's the trade-weighted value of the United States dollar varied between index values in the high 80s and middle and high 90s. During much of this period of time, it probably could be justifiably said that the value of the dollar was too low, but not seriously so. During 1981 and 1982, for many reasons the dollar began to gain in strength, and it moved above an index value of 100 toward a level of 120, with many beneficial impacts for the United States. The movement served as a check on inflation, and it was a measure of restored confidence in the currency of the country. It also represented a range which was reasonably supportable by economic fundamentals.

As the value of the dollar began in 1983 to move from the level of 120 to a high of 160 in February 1985, it moved out of a level which was reasonably supportable, based on fundamentals, and began to set the stage for serious negative impacts on the economy of the United States. At its high in February of this year, the dollar was probably overvalued by about 35 percent above a range which was supportable. Reducing this overvaluation toward the highs of 1982 would retain the initial beneficial impact from an increase in the value of the dollar and yet reestablish a better economic climate for the basically excessively strong dollar. It is important to note that negative impacts of changes in currency values are sometimes delayed in their appearance, but delay does not eliminate the eventual negative consequences which have recently appeared.

Immediate Action Needed

The time for action is now. We believe Congress will provide more positive and beneficial results for its constituents if it increases its attention to the all-pervasive factor in the trade deficit; namely the strong dollar. Action in this area would cure a significant part of the problem, leaving for direct government action those situations that relate to unfair trade practices, subsidies and cheating. In this way, market discipline can be preserved so that consumers get the best price and workers can retain or get jobs at decent wages.

Five Principles of Currency Reform

In considering the question of currency reform, we offer five basic principles:

1. Recognition that currency relationships can have just as important an impact on the economic health of the nation as the more familiar measures such as inflation and unemployment;

2. Recognition of the impact of both monetary and fiscal policies on currency relationships;

3. A mechanism for preventing either surges or extreme downward movements in currency values;

4. A commitment by major countries to improve the current "floating" exchange system.

5. Removals of restrictive trade barriers and other arrangements that impede trade and currency adjustments.

Proposed Action Program

We propose several actions to induce both short- and long-term solutions to the problem of severe currency misalignments.

The U.S. deficit is often cited as the major factor in the strong dollar because it is perceived as the controlling factor in the high U.S. interest rates which presumably attract foreign capital. Because these assumptions on the link between trade deficits, the dollar and government deficits are open to question and because it can appropriately be claimed that a lower government deficit will lead to a stronger dollar in the long run, we would not see budget reductions as the panacea for the dollar or the trade deficit.

Reducing the federal deficit must be a high priority for many reasons. Given the fact that strong pressures for reducing the deficit have been operating on the federal government for several years with minimal success, we recommend that while determined efforts to reduce the federal deficit continue, other solutions to the trade deficit be immediately implemented by reducing not only the dollar level but also its volatility.

Immediate Action

1. **Monetary Policies:** Until recently, many officials of the Federal Reserve have made few public comments on the strong dollar and its effects upon monetary policies and the domestic economy. It is essential that U.S. monetary authorities incorporate an assessment of the dollar value on U.S. business as well as of short-term indicators such as new orders, unemployment and inflation. Congress should insist on this.

   The concern with the dollar's value and its economic effects should be communicated regularly to the Administration and Congress, along with appropriate monetary policies to deal with the situation.

   A new set of monetary rules with new gauges of monetary policy performance is called for by the need to incorporate foreign as well as domestic pressures on U.S. economic activity. It is clear that other major industrial countries do this.

2. **Currency Reserve Fund:** Many central banks operate with appropriate reserve funds to defend currencies when needed. An effective system among the central banks of major countries should be devised for coordinated currency adjustments to moderate extreme fluctuations, up or down. Although temporary in its effect, such a fund, when used with other corrective measures can be successful and relatively inexpensive for U.S. taxpayers.

Longer-Term Solutions

3. **Foreign Economic Policies:** The policy of fostering faster growth in other countries now being pursued by the U.S. government will be helpful. It will have a better chance of succeeding when fiscal and monetary policies in the U.S. move in closer harmony.

At that stage, it will be possible to attempt to institute a more rigorous and formalized system for better coordination of economic policies among the major industrial countries. To achieve this, more positive actions in the economic summit meetings will be necessary.

These forums should also deal with the unilateral currency actions of central banks that distort world trade.

4. Currency Reform: A new monetary conference to discuss current exchange-rate relationships and mechanisms should be convened immediately.

At the very least, it would contribute to the process of understanding the varying pressures in current exchange markets and encourage the design of broad mechanisms to deal with these changing pressures in the future. The aim of these mechanisms is to provide the climate and the incentive to encourage countries to make the necessary market adjustments required to correct the currency misalignment.

The initial agenda could be provided by the Group of Ten and expanded at a later stage.

The CHAIRMAN. Mr. Luke, I am glad you brought Ms. Pace with you. She and I have shared a number of platforms at conferences around the country, and I have found her both delightful and brilliant. Is there anything we can do to bring the value of the dollar down, if we do not attack our budget deficits?

Mr. LUKE. We are both ready to respond, and I will count on Ms. Pace to supplement what I have to say. The budget deficit is important, but conventional wisdom would say that countries with large budget deficits generally have weak currency. And I think if we solve the budget deficit, probably we will see the dollar strengthen initially. There are a lot of other things that can be done as well. We know from our experience in 1984 and early 1985 that some of the things that we have done in monetary policy have definitely influenced the dollar in an upward direction. And we think that there is room in monetary policy to have an impact on the dollar.

The CHAIRMAN. Expand on that, because you are one of the few witnesses to make the point. Most witnesses say it is just the deficit. You know, if you cut the deficit in half, the value of the dollar will drop. I would love to cut the deficit in half for a whole variety of reasons, but I am not sure, just as you are not sure, that the dollar will drop.

Mr. LUKE. I think only you can tell us whether that is going to be a short-term or a long-term tool. I don't know. I won't prejudge it, but I think we have to say that the dollar might rise initially. But there are a number of other tools that can influence the value of the dollar. We have seen on a cause-and-effect basis that monetary policy can influence the value of the dollar.

The CHAIRMAN. What should we do with monetary policy to bring the value of the dollar down?

Mr. LUKE. One of the major objectives of monetary policy in recent years has been to be a watchdog over inflation, and in 1980 and 1981 it was a help before we created other tools to control inflation on a sound basis. Since that period of time, the cost of energy has dropped materially. We have improved our labor productivity as a result of capital investment. We have developed very constructive and positive relationships with our work forces that didn't exist before. We have unutilized capacity at the present time. So, I think there are a number of healthy natural restraints which would argue that inflation is likely to remain under good control. If that is the case, then I think monetary policy at this point can encompass other objectives than just making sure that there is not even the slightest possibility of a rise in inflation.

The CHAIRMAN. And by that do you mean slightly expanding the money supply. Is that one of the policies you are advocating.

Mr. LUKE. A rise in value generally occurs because there is more demand than supply.

The CHAIRMAN. Yes.

Mr. LUKE. And it would seem that there is a possibility that a slightly easier monetary policy might make a significant difference in the value of the dollar.

The CHAIRMAN. Norma.

Ms. PACE. May I supplement that?

The CHAIRMAN. Yes.

Ms. PACE. I believe that, under current practices of monetary policy, there is much too much focus on M1, and the chairman is now justifying an above-target growth in M1 by saying the disposition to use the money isn't as great as it was before. In other words, the velocity is down. What has struck me is that we have used a one-sided approach to monetary policy, and the fear that is engendered by just a little deviation of M1 from the target is just catering to a philosophy or an expectation that this is going to have a tremendous inflationary impact. So, I think we need new tools from the Federal Reserve. I think they are admitting that their existing tools aren't working properly. They have to have a nudge in order to act. They are using as a crutch the fact that the deficit is inhibiting their monetary policies. I don't think that is appropriate. I think we have to solve the Federal deficit, and I think monetary policies must recognize many things. And as Mr. Luke said, it is obvious that the demand for dollars is greater than the supply, and that is what is driving them up; and they haven't taken that into account.

The CHAIRMAN. Do you want to expand any further, Mr. Luke?

Mr. LUKE. There are other things that I think are important. Values and price psychology as well. And we have a major problem with the value of the dollar. The fact that we have the problem has not been articulated in any meaningful consistent way by our leaders in this country. Our customers in other parts of the world, in countries that are more sophisticated about currency values, were really astounded when our currency began to escalate in 1983 and then went through the roof in 1984. They knew what we were doing to ourselves, and they couldn't believe it was going to continue. That is why we kept on getting business long after the value of the dollar really had made us noncompetitive, because they thought the dollar was going to come down. Finally, it went on and on; there was no obvious response in this country; so they said, look, if nobody cares, then maybe we should act on the basis that the dollar is going to stay up there.

The CHAIRMAN. Do you think we should return to a fixed currency system?

Mr. LUKE. I don't know, and I am not an expert on that. I don't think the currencies have to be rigidly locked in, but let me give you an analogy. In the human body, our temperature can fluctuate within reasonable limits, and we are still in good health. But we all recognize that when our temperature goes outside of a reasonable range, it is time to call a doctor. I tend to believe that currency values should and probably will fluctuate, but I think we should be alert enough so that, when our currency gets outside of a reasonable range that is supported by justifiable factors, then we ought to say we have problems; and we ought to begin to look for and to use the tools that are available to us to do something about it. To the extent we don't, we are going to have a serious and continuing impact on our industry in this country. Through our customers, through our own acquaintanceships, we can see decisions being made in other parts of the world right now—products supplied from the United States are going to be sourced from another part of the world because of expectations about the dollar. We see people in other parts of the world justifying plant and equipment investments right now, based on present values of the dollar, taking markets that should logically belong to the United States, based on fundamental cost. But once those decisions are made, unfortunately, the impact is going to last for a period of time. So, we have a serious problem. The problem is not going away. It is not going to go away until we do something about it. The thing that I see that is positive on this subject is that many of the other solutions that have been offered may be practical and justifiable in an individual case. I see none of them that can be expanded across the board on a broad-scale enough basis to deal with $150 billion trade deficit. I do think that if we are willing and able to take a look at the dollar and do something, we have a tool and a mechanism there that can deal with a substantial portion of the total problem. And I think that is an approach that does not run the risk of the retaliation that is very likely if we adopt on a broad scale basis what others may call protectionist measures.

The CHAIRMAN. Dr. Meister, did you want to say something?

Dr. MEISTER. Mr. Chairman, I am speaking on Japan today.

The CHAIRMAN. I was going to come back to Japan on the next question.

Dr. MEISTER. I would like to add only one point to what Mr. Luke and Ms. Pace have said. We are competing in Europe very heavily with Sweden. And in addition to the value of the dollar, Sweden has unilaterally devalued, without any relationship to other currencies which additionally have hurt our market. Now, we hear that they are again planning additional devaluation, and certainly our Government through IMF and strengthened discipline, ought to be able in that area also to do something about it. I totally share the comments before, but this is just a small supplement.

The CHAIRMAN. Mr. Ward, you talked about the Japanese market and how protectionist it is. I have seen a fair cross section of their mills. They have a few modern mills, but by and large, most of the lumber mills I saw haven't been seen in this country for 50 years. They used to exist along the side of the road, and they were little mom-and-pop operations. Lumber, agriculture, fishing are all the backbone of the Liberal Democratic Party. Since Japan has not reapportioned its diet since 1922, it has an extraordinarily disproportionate rural influence to begin with. Then if you add a conservative party disproportionally influenced by the industries that are basically the backbone of all conservative parties every place, I don't know if we can get them to change. Clearly, those mills cannot compete against our mills. There is just no way they can compete with our mills. What do we do if they will not give in?

Mr. WARD. I think, Mr. Chairman, that are a number of things that are happening in the Congress that are in response to Japan's not giving on a number of issues. I don't know that you could isolate any single one them as it relates to the wood products issue, but the whole combination says that Japan must give and it must give in a number of areas and in areas where the United States is competitive. And our industry is one of those areas of opportunity, both the solid wood side and the paper side.

The CHAIRMAN. When I met with Ambassador Matsunaga several weeks ago, I mentioned four areas in which Japan should reduce its barriers. I said wood, beef, tobacco, and citrus. Now, that encompasses about 30 Senators, and by and large, the products don't overlap. Oregon doesn't produce any citrus, and Florida doesn't produce much wood; and neither of us produce much tobacco. You would pick up a fair aggregation of States against any anti-Japanese legislation if they would open up to just those four products. Obviously, I think they ought to open them up more. If they opened up to all imports, I don't think it would make $5 billion difference in our trade deficit, but at least psychologically, we would not be able to say, oh, well, they won't open their doors. They are going to cut off their nose to spite their face. They are going to succeed in driving this country to a protectionist trade bill that will serve neither them nor us well. And only Japan, all by itself, can do that. Other countries in aggregation might be able to do it, but Japan can succeed in doing it all by itself; and they may succeed. I don't know what to do to make them give. I am prepared to use retaliation, if necessary, to shut off some of their markets in this country—some of their very important markets. Maybe they would listen then. I think, deep down, they don't think it is going to happen. But it will happen if they don't give. And that is an entirely different issue from what we were talking about earlier about Canada and imports. This is access to markets.

Mr. WARD. It certainly is. We certainly concur with your thoughts.

Mr. LUKE. And I hope you include the paper industry in your thoughts——

[Laughter.]

The CHAIRMAN. As a matter of fact, in Oregon I include paper, particle board, or any derivative thereof that comes off the trees. [Laughter.]

Mr. LUKE. Thank you, Mr. Chairman. Sorry, but I couldn't resist.

The CHAIRMAN. You have been a most enjoyable panel. You have been very patient. Thank you for waiting all afternoon. You have been most helpful. We are recessed.

[Whereupon, at 5:15 p.m., the hearing was adjourned.]

[By direction of the chairman the following communications were made a part of the hearing record:]

CHAIRWOMAN

UNITED STATES INTERNATIONAL TRADE COMMISSION

WASHINGTON, D.C. 20436

October 11, 1985

Honorable Max Baucus
United States Senate
Washington, D.C. 20510

Dear Senator Baucus:

Thank you for writing me concerning my testimony at the Senate Finance Committee hearing on the condition of the U.S. lumber industry and recommending that certain inflation adjustments be considered during the Commission's current section 332 investigation on softwood lumber.

As you noted, table 6 of my testimony clearly indicates that, when adjusted for the relative rates of inflation in Canada and the United States, the U.S. dollar has appreciated by 8.3 percent since 1977, and by 1.2 percent since 1982.

I am very sorry for making a mistake on such an important issue. I regret any inconvenience or misunderstanding that this may have caused, and I assure you that the public version of our study will contain the correct figures. Thank you for paying such close attention to my testimony and for pointing out my error.

Regarding your second point, during the course of our investigation we converted all reported Canadian costs to U.S. dollars, on an annual basis, using the International Monetary Fund annual rate of exchange. This permitted direct comparison of costs in both countries for each year. Since such costs were available for each year under consideration, it was not necessary to adjust base costs using a general index of inflation. We will send you a copy of the Commission's report, which went to the President and the United States Trade Representative (USTR) on October 8, when it is available.

Please continue to call on us whenever we can be of assistance to you.

Sincerely,

Paula Stern
Chairwoman

STATEMENT OF T.M. (MIKE) APSEY

PRINCIPAL COORDINATOR FOR TRADE,

CANADIAN FOREST INDUSTRIES COUNCIL

The Canadian Forest Industries Council is an organization composed of the following seventeen forest products associations throughout Canada:

- Alberta Forest Products Association;
- l'Association des industries forestieres du Quebec;
- l'Association des manufacturieres de bois de sciage du Quebec;
- Canadian Lumberman's Association;
- Canadian Pulp & Paper Association;
- Canadian Wood Council;
- Cariboo Lumber Manufacturers' Association;
- Central Forest Products Association;
- Council of Forest Industries of British Columbia;
- Interior Lumber Manufacturers Association;
- Maritime Lumber Bureau;
- New Brunswick Forest Products Association;
- Northern Interior Lumber Sector (COFI);
- Nova Scotia Forest Products Association;
- Ontario Forest Industries Association;
- Ontario Lumber Manufacturers Association;
- The Western Plywood Manufacturers Association, Ltd.

These associations represent more than 2000 forest products companies from coast to coast in Canada that collectively produce $25 to $30 billion of forest products each year.

STATEMENT OF T.M. (MIKE) APSEY
PRINCIPAL COORDINATOR FOR TRADE,
CANADIAN FOREST INDUSTRIES COUNCIL
TO THE SENATE FINANCE COMMITTEE
September 19, 1985

My name is Mike Apsey. I am Principal Coordinator for Trade for the Canadian Forest Industries Council. The Council is an organization comprised of seventeen forest products associations from across Canada. These associations represent more than 2000 forest products companies which collectively produce $25 to $30 billion of forest products annually. The companies directly employ over 250,000 Canadians.

My goal is to prevent misconceptions about Canadian lumber from clouding your deliberations on conditions in the North American lumber industry.

We firmly believe that you are seeing this industry in a period of adjustment and restructuring -- and these times of flux are why some U.S. producers are pointing the finger at their Canadian counterparts. However, Canadian lumber producers are competing fairly in the U.S. market -- just as they have been for many decades.

Stumpage Prices -- A Meaningless Comparison

The most common myth currently being circulated about Canadian lumber is that stumpage -- the price paid for standing timber -- is subsidized in Canada. The first response to this charge comes from the U.S. Commerce Department itself. After an exhaustive investigation, the Commerce Department in May 1983 ruled on five independent grounds that timber pricing policies in Canada do not provide a subsidy. This was not a decision based on technicalities in the law. The Department looked at the stumpage question from every possible angle. And significantly, the U.S. producers did not appeal this decision.

Proponents of restrictions on Canadian lumber still try to breathe life into this myth by pointing out the differences between U.S. and Canadian stumpage prices. As the Department of Commerce stated in May, 1983, however:

> We believe that a comparison of Canadian stumpage prices with U.S. prices would be arbitrary and capricious in view of: (1) 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; (2) the additional payments which are required in many provinces in Canada, but not

> generally in the United States; (3) the fact that in recent years, prices in national forests in the United States have been bid anywhere between two to five years in advance of cut, without taking into account the fluctuations in demand for lumber; and (4) the fact that in recent years the U.S. Forest Service has restricted the supply of timber in certain national forests due to budgetary and environmental constraints.

As the Department noted, the value of a tree growing in a certain place depends upon a host of factors including the tree's species, quality, size, how difficult it is to log the tree, how far the tree is from mill and market, and the availability of transportation and infrastructure to bring loggers to the timber, to support cutting operations, to move the trees to the processing facilities, and then to move the product to market. According to the myth, however, none of these factors should be taken into consideration.

As a result, the price for a small tree growing near the Arctic Circle could be compared to the price for a big tree around the corner from a mill close to a major housing market, and the price difference called a subsidy. Clearly, however, the price difference is anything but a subsidy -- the tree far from the market that can only be cut down under difficult conditions is worth far less than the big tree around the corner from the mill.

The wide range of prices paid for trees harvested on the different U.S. Forest Service lands throughout the U.S. demonstrates the same point. As Appendix A shows, in 1984, the average price for timber harvested in Region 2, the Rocky Mountains, was $13.79 per thousand board feet (mbf), while in the U.S. South, Region 8, the average price was $80.89, and in the west side of Region 6, the Pacific Northwest, the average price was $100.52. These price differences do not mean that the producers in the Rocky Mountains enjoy a competitive advantage of $86.73, nor do they signify that Southern producers are subsidized by an average of about $20.00 per thousand board feet of lumber produced.

Similarly, even within any area of the U.S., stumpage prices vary widely. For example, within Region 8 (the U.S. South) alone, prices in the third quarter of 1984 for a major species, Southern pine, ranged from $6.75 to over $200. The point is, there is no reason for stumpage prices in different areas of the United States to be the same, just as there is no reason for stumpage prices in Canada to be the same as U.S. prices.

Nevertheless, those in the U.S. lumber industry pressing for restrictions on imports from Canada persist in making comparisons of stumpage prices. The misleading nature of this comparison is revealed when the costs of cutting the trees and delivering them to the sawmill are added to the stumpage prices for cross-border areas. Immediately, the illusion of lower Canadian costs evaporates.

The more complex comparison of costs to the mill gate tells a more complete story than do simple stumpage comparisons. The fact is there are major cost differences between the two countries, and these account for the differences in resource prices.

Canadian stumpage prices cannot rationally be called an unfair subsidy when they provide no cost advantage to Canadian producers compared to their U.S. counterparts. Indeed, if Canadian stumpage practices offered any major competitive advantage, one would not have expected to see U.S. companies in Canada, including several of the largest U.S. lumber producers, selling their Canadian-based operations.

U.S. Companies Cut Canadian Timber on Equal Terms with Canadians

It actually would be difficult to view Canadian stumpage practices as unfair or a problem for U.S. lumber producers under any circumstances, since U.S. lumber companies can obtain rights to cut timber in Canada on equal footing with Canadian companies. During the recent countervailing duty investigation of softwood lumber, the Commerce Department found that U.S. producers had taken considerable advantage of such rights. For example, in 1983, approximately 23% of the lumber produced in British Columbia, Canada's largest lumber producing province, was harvested by U.S. owned companies.

U.S. Agencies and Producers Acknowledge Canadian Stumpage Pricing Policies Are Fair

Finally, U.S. producers have no reasonable basis for criticizing Canada's pricing policies. The appraisal method used to price standing timber in British Columbia, the largest timber producing province in Canada, is modelled on the U.S. Forest Service system. As the August 26, 1985 Congressional Research Service Report Canadian Lumber Imports: Impacts on the U.S. Lumber Industry, pointed out, both the U.S. Forest Service and the U.S. industry maintain that the prices generated by this appraisal method represent fair market value.

Those in the U.S. advocating restrictions on Canadian lumber have pointed to the bids that can be generated above appraised values in the U.S. as the reason why the U.S. system generates fair market values. However, these bids are due to the fact that, unlike Canada, the U.S. Forest Service system values timber for sale today but allows it to be cut over two to five years in the future. In other words, the bids are due to expectations of the _future_ increase in timber values. Of course, those expectations can be wrong, as evidenced by the recent timber bailout legislation passed by the U.S. Congress.

In sum, Canadian stumpage pricing does not provide subsidies to Canadian producers and does not give Canadians any unfair advantage in U.S. markets. This myth, and the specious comparisons of U.S. and Canadian prices, should be laid to rest.

The Real Causes of U.S. Producer Dissatisfaction

The fact that there is no Canadian subsidy does not imply that there are no genuine economic issues facing the U.S. lumber industry. In fact, the entire North American lumber industry -- not only U.S. but

Canadian companies as well -- has had to deal with lower prices and higher unemployment than anticipated coming out of the latest recession. As Canadian imports have not caused the current situation, however, limiting Canadian imports is not the solution.

Exchange Rates

The value of the U.S. dollar has had a significant effect on competitive conditions, and this has heightened tensions between U.S. and Canadian producers. The U.S. dollar, once at parity with the Canadian dollar, as recently as one week ago was worth C$1.38. As a result of the high value of the U.S. dollar, Canadian lumber producers have gained some market share. Appendix B shows the remarkable correlation between the exchange rate and Canadian market share for lumber. Even proponents of legislation restricting Canadian lumber, such as Congressman Weaver, and Senators McClure, Symms, and Baucus, have acknowledged that the exchange rate is a major factor affecting current market conditions.

U.S. producers should not be permitted to lay the blame for market conditions beyond Canadian industry's control on supposedly unfair Canadian competition and thereby gain protection from fair competitors in the market place. By the same token, penalizing Canadian lumber producers is not the solution to the problem of a highly valued U.S. dollar.

To put the market share situation in historical perspective, the increase in Canadian market share is neither sudden nor dramatic. Over seven years, Canadian market share has only increased a total of 3 percentage points, from 28% in 1978 to 31% in 1984.

Production Capacity Increased During the Last Boom

The North American lumber industry is an industry without borders, and is a model of free market competition. Approximately 4,000 mills, 900 wholesale firms, 6,000 traders, 20,000 retail outlets and a large number of industrial users across the North American continent all play a role in the production, marketing and distribution of the equivalent of 3,000 to 4,000 rail carloads of lumber every day, with almost all transactions negotiated by telephone. The industry is also very cyclical -- it is one in which periods of higher returns are interspersed with periods of lower returns.

During the last boom of the late 1970's, projections of even greater demand led producers on both sides of the border to expand capacity and invest in the latest, highly efficient equipment. Just as much of that capacity began to come into operation, the recession hit. With the downturn in the lumber market, serious belt-tightening and cost-cutting measures were undertaken.

Despite the recession, these new more efficient facilities have proved capable of turning out an unprecedented amount of lumber. The growth in production in the U.S. South is particularly striking. In contrast to the Pacific Northwest, where production decreased, Southern production increased between 1978 and 1984. As a result, the South's market share increased dramatically over this period.

Because there simply is more capacity and greater efficiency in the lumber industry, there is more lumber available than previously. As a result, the latest upsurge in demand for lumber has not produced the usual sharp price increases.

Certain U.S. producers have tried to pin the blame for the U.S. unemployment on Canadian imports.

This is misleading and absolutely incorrect. Over the period 1980-84, softwood lumber production increased by 19.4 percent in the United States, while employment has been decreasing. At a time when U.S. production is, in fact, approaching record levels, it is untenable to suggest that declining employment is attributable to imports. Plainly, the decline in employment is a consequence of technological change -- the substitution of capital for labor in lumber production.

These industry conditions have been at the root of many of the U.S. producers' complaints, yet whatever problems exist are ones created by over-optimistic forecasts and normal market forces. Canadian stumpage practices certainly are not responsible, and restricting Canadian wood products from U.S. markets, a "Band-Aid" approach, as one Congressional supporter of restrictive legislation admitted, is not a valid response to the situation.

Restrictions on Canadian Wood Products Would Be Very Costly to the U.S.

The United States needs Canadian wood products. In periods of peak U.S. demand, Canadian producers have been encouraged to increase production, and even have been chastised by their U.S. customers if they did not meet customers' volume expectations. In fact, the U.S. government itself has asked for Canadian assurances that a flow of wood products from Canada would be available to meet U.S. needs.

The United States uses a full array of forest products provided by Canada. In addition to lumber, fully 57% of the newsprint used in the U.S. came from Canada in 1983, and Canada is a major supplier of pulp to U.S. customers. Many U.S. industries, including the manufactured housing industry, and industries engaged in remanufacturing rough boards into specialty products prefer Canadian products, because they offer species, size and other characteristics not available from U.S. sources. As a result, many Canadian products obtain premium prices in the U.S. All of these products would be affected, however, if legislation restricting Canadian imports were to be passed.

When these facts are taken together with the growing concerns that have developed in the United States about limits on the available supply of U.S. timber, it is difficult to see how America's construction industry, realtors, home builders and buyers, newspapers, retail lumber dealers and other users of wood products can avoid severe injury if Canadian sources of supply are curtailed. For example, U.S. producers have circulated figures indicating that duties on Canadian lumber should be in the range of 60%.[1] Duties at such levels -- or even at significantly lower levels -- could add thousands of dollars to the cost of American housing. Such cost increases would slow down housing starts, reduce employment in the construction and related trades, and force hundreds of thousands of people out of the housing market.

Moreover, import restrictions on Canadian wood products would affect one of the most important sectors of the Canadian economy, and therefore would reduce Canadians' ability to purchase U.S. goods. Canadians currently are important customers (to the tune of billions of dollars each year) for computers, citrus products, and office machinery among many other U.S. products. In fact, the U.S. and Canada are each other's largest trading partners. In 1984, two way trade exceeded $113 billion; U.S. exports to Canada exceeded U.S. exports

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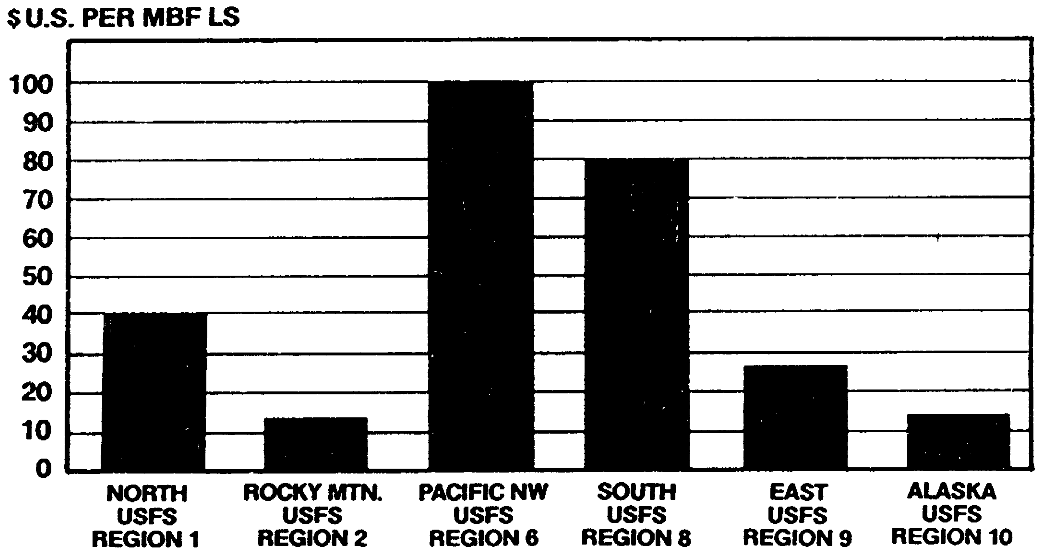
1 International Paper has published "stumpage comparisons" for 1984 involving no less than a claimed $117 difference between U.S. and Canadian stumpage prices. When this difference is compared to the average price for Canadian lumber, i.e., the ratio of the total value of Canadian lumber imports over their volume for 1984, a 60% tariff results.

to Japan and U.S. exports to the European Economic Community. Moreover, Canada represents a uniquely growing market for U.S. exports. According to the U.S. Commerce Department's most recent statistics, U.S. exports to western Europe are down 11%; to Japan, they are down 18%; to the Pacific Rim, down 11%; but to Canada, U.S. exports are up 7%.

Thus, superimposed upon all other objections to legislation against Canadian lumber is the issue of fairness to the United States' largest trading partner, not to mention fairness to the many U.S. consumers of Canadian forest products -- from home builders and home buyers to newspaper publishers and readers. It is simply not fair to "get the Canadians" by injecting into the U.S. laws artificial restrictions based on myths already so thoroughly discredited by the U.S. government.

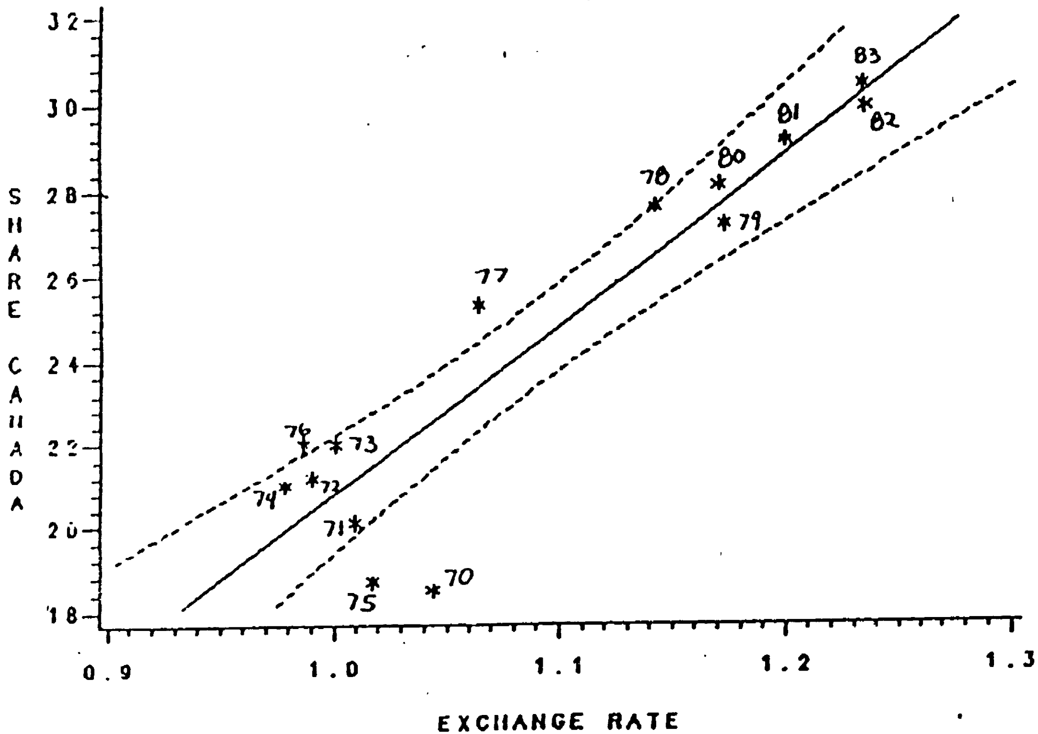
USFS STUMPAGE RATES: 1984

(Average Rates)



SOURCE: USFS

US MARKET SHARE



LINEAR REGRESSION WITH 95% CONFIDENCE LIMITS ON MEAN PREDICTED VALUES

BEFORE THE UNITED STATES SENATE
COMMITTEE ON FINANCE
THURSDAY, SEPTEMBER 19, 1985

STATEMENT OF HARRY FURMAN,
FURMAN LUMBER, INCORPORATED

I am Harry Furman, President of Furman Lumber Incorporated, the largest independent lumber wholesaler in the Eastern United States. We operate wholesale facilities in Boston, Massachusetts, New York, New York, Philadelphia, Pennsylvania, Baltimore, Maryland, Wadsworth, Ohio, Denver, Colorado, and Portland, Oregon. Our company employs a total of 175 people and in the last year sold lumber products worth over $200,000,000. These products were bought from many North American mills and were delivered to customers throughout the United States.

We have developed a very successful business. The basis of this success is our ability to procure for our customers the products they want when they want them.

The lumber industry produces a wide variety of products that serve multiple needs. Some products are better for some uses; some mills package lumber in a fashion that a particular customer wants; some mills offer better delivery and service than others. All of these factors enter into our customers' decision to purchase lumber. If a customer wants Green Douglas Fir dimension or dry S-P-F studs or perhaps Southern Yellow Pine floor joists, it is our job to make these products available. We simply can't afford to have our access to some of these products restricted.

I know that U.S. lumber industry representatives have been campaigning here for some type of restrictions on lumber imports. They claim that import restrictions would save American jobs, and protect their market share from further erosion.

What they don't mention is that lumber is a vital raw material for other industries, primarily homebuilding and non-residential construction, and that lumber sales provide jobs for tens of thousands of Americans who work for wholesale and retail lumber dealers. Higher lumber prices, and the inevitable reduction in lumber sales and consumption, would cause serious difficulties for these other industries. I firmly believe that the jobs that would be lost in construction and lumber distribution companies would far outweigh any jobs saved for U.S. lumber producing companies.

We at Furman are familiar with the difficulties experienced by U.S. lumber producers, especially in the Pacific Northwest where one of our facilities is located. But we just don't believe that the problem can be solved by penalizing Canada. Instead, we firmly believe that protectionist policies will cause far more problems than they cure.

GRAND TRUNK CORPORATION
Detroit, Michigan

SUMMARY OF POSITION
on
LEGISLATION TO RESTRICT
IMPORTS OF CANADIAN LUMBER

Statement of Grand Trunk Position

Grand Trunk Corporation and its three railroad subsidiaries strongly opposes proposed legislation in the U.S. Congress directed at lumber imports, specifically H.R. 2451 and S. 1292, which threatens to disturb the friendly trading relationship between the U.S. and Canada. U.S.-Canadian trade is the most extensive in the world, last year totalling over one-fifth of all U.S. trade, and is of vital importance to both countries. Since existing trade law is sufficient to deter unfair trade practices, enactment of this unfair legislation is unnecessary and will cause transportation companies such as Grand Trunk, consumers, home builders, manufactured housing companies and many others far more harm than the gain realized by the U.S. lumber industry.

Background

Grand Trunk Corporation (Grand Trunk), a Delaware corporation, is a wholly-owned subsidiary of the Canadian National Railroad Company, and has three operating subsidiaries, Grand Trunk Western Railroad (GTW), Duluth

Winnipeg Pacific Railway Company (DWP) and Central Vermont Railway, Inc. (CV). GTW is a Michigan and Indiana corporation, headquartered in Detroit, with 4,300 employees and over 1,300 miles of track in Ohio, Michigan, Illinois, and Indiana. DWP, a Minnesota corporation, operates from the Canadian border to the Duluth-Superior gateway and employs over 250 employees. CV, which operates from the Canadian border through Vermont, Massachusetts, New Hampshire and Connecticut, is a Vermont corporation with over 400 employees. Through these three subsidiaries, Grand Trunk carries a sizable percentage of the trade between the U.S. and Canada and contributes millions of dollars in state and local taxes, salaries and other benefits to the economy of the localities and states in which they operate. Any reduction in traffic going into or out of Canada would severely impact Grand Trunk and its employees.

History of Lumber Protectionism

In 1982, the International Trade Administration ("ITA") of the United States Department of Commerce undertook an examination of the Canadian softwood lumber industry after a petition was filed by U.S. lumber companies. The ITA found, against the allegations of the U.S. industry, that Canadian stumpage (the right granted by the government to fell standing trees on public land) was not subsidized and that the competition between the U.S. and Canada in the lumber industry was fair and open.

Despite the ITA finding, several bills have been introduced in Congress this term to impose restrictions on the import of Canadian lumber into the U.S. Most of the proposed legislation establish quotas on imported lumber. One bill, H.R. 2451, introduced by Rep. Sam Gibbons (D-Fla.) with a companion bill, S. 1292, introduced in the Senate by Sen. Max Baucus (D-Mont.), attempts to end run the ITA decision and limit softwood product imports by redefining what constitutes a "subsidy" under U.S. trade law.

The Gibbons/Baucus bill, which was specifically designed to reach Canadian lumber, requires that the cost of the "removal right" granted by a government to remove governmentally owned natural resources be compared with the cost of such right in "comparable" regions in the U.S. However, as to Canadian lumber, such comparison under the bill is unfair since it excludes factors such as tree size, location, and accessibility, which tend to make Canadian wood more costly to bring to market. Additionally, the Gibbons/Baucus bills specifically exclude services such as road building and reforestation, which are required of Canadian companies by their government, in determining cost for comparison.

Proponents of the bill claim that, if passed, the legislation could impose duties of up to 60% of the lumber's value, increasing the price accordingly. However, the 1983 ITA decision specifically found that a comparison of Canadian stumpage prices with U.S. prices would be arbitrary and capricious. A comparison of 1985 prices for delivered lumber shows that, despite the difference in stumpage costs, Canadian lumber is actually more expensive than U.S. lumber for many varities, indicating that factors other than stumpage prices must be considered when comparing U.S. and Canadian lumber prices. The object and result of the Gibbons/Baucus bill is to exclude Canadian lumber from U.S. markets by guaranteeing the addition of a substantial countervailing duty to other costs.

Effects on Grand Trunk

While it is unclear how much lumber prices would rise if Canadian imports were restricted, the effect on Grand Trunk would be severe. Grand Trunk is one of the major carriers of Canadian lumber, carrying over 65,000 carloads of Canadian lumber a year. The following chart shows the effect on Grand Trunk of reductions in cross-border traffic. Varying losses are used to illustrate the damage to Grand Trunk, since it is difficult to forecast the exact reduction in traffic volume due to the legislation. The imposition of a 60% countervailing duty on lumber would likely halt all cross-border traffic, while even a 30% duty would drastically reduce traffic. Assuming a 75%, 50% and 25% loss of lumber traffic volume, the effect on operating revenues is illustrated below:

	Revenue Loss (000) (% of Operating Revenues) 75%	50%	25%
GTW	$ 407 (*)	$ 272 (*)	$ 134 (*)
DWP	$11,474 (26%)	$7,649 (17%)	$3,827 (9%)
CV	$ 3,086 (15%)	$2,057 (10%)	$1,029 (5%)

(* Less than one percent)

As the chart indicates, Grand Trunk would suffer substantial losses. For instance, if DWP were to lose 75% of its lumber traffic, it would suffer a debilitating loss of 26% of its gross revenues. If newsprint and other wood products are included, the loss of traffic volume is even higher, with an accompanying loss of revenues. Such a drastic reduction in revenues would result in a loss of over 200 jobs at Grand Trunk, along with other likely reductions in service.

In addition to the effects on Grand Trunk and similar transportation companies, other U.S. industries would also be hard hit. The home building industry which uses the high quality Canadian lumber, some species of which are not available at all from U.S. producers due to natural tree habitat, would be forced to use more expensive U.S. lumber, raising the price of a new home by several thousand dollars and excluding thousands of families from home ownership. Residential housing starts would inevitably fall, as would the number of construction related jobs. Manufactured housing would be similarly damaged. The cost of the average new manufactured house could increase by as much as 15%, forcing many to defer purchase of a house and reducing demand, with thousands of jobs lost as a result.

Other industries which use Canadian forest products would also be impacted, such as newspapers, lumber yards and other manufacturers. In fact, the cost to the U.S. economy of lost jobs and business reductions of American companies if the Gibbons-Baucus bill or other such legislation were enacted would far outweigh any employment gains in the lumber industry.

Natural Resources Other Than Lumber

While the Gibbons/Baucus bill is directed at lumber, the bill may have other ill-considered effects because of the haste of legislative deliberations. The section on removal rights is broad enough to apply to the right to extract any natural resources which are controlled by government entities, including resources such as sulfur, potash and other minerals, and natural gas products. The effect could be to raise the price of these items through the imposition of a countervailing duty, and to thereby affect the imports of many other countries. Eighty percent of the U.S. supply of potash, a major component of fertilizer, comes from Canada and any increase in price because of the addition of a countervailing duty could further burden the already reeling U.S. farmer. These potential impacts on products from countries which use a different system of development than the U.S. ought to be investigated before being enacted into law.

Many of the products carried by the Grand Trunk railroads could be subject to countervailing duties under the removal rights section. The Gibbons/Baucus bill would add an extra duty to the cost of several natural resources imported into the U.S., thus increasing the cost of these resources to the American consumer and reducing U.S.-Canadian trade. Again assuming a 75%, 50% and 25% reduction in traffic volume of each subsidiary for the major products affected by the provision, the impact on Grand Trunk is substantial.

	Revenue Loss (000) (% of Operating Revenue)		
	75%	50%	25%
DWP			
potash	$8,509 (19%)	$5,673 (13%)	$2,836 (6%)
sulfur	$2,855 (7%)	$1,903 (4%)	$ 951 (2%)
CV			
(wood products, pulp, paper, l.p. gas)	$5,303 (25%)	$4,013 (19%)	$2,774 (13%)
GTW			
(zinc, asbestos, wood products, ore, peat, aluminum, l.p. gas)	$7,505 (2%)	$5,003 (1%)	$2,502 (*)

(* Less than one percent)

Such large reductions in revenues would lead to losses in jobs at Grand Trunk of as much as 250 employees. Other industries which use Canadian resources such as U.S. fertilizer and chemical manufacturers and metal foundries, could also be impacted.

Canadian Retaliation

Both the U.S. State Department and the Canadian Embassy have indicated that the Gibbons-Baucus bill may violate GATT (General Agreement on Tariffs and Trade), the international agreement which establishes permissible trade practices. Such legislation is likely to cause other countries to impose their own protectionist measures against the U.S., further eroding international trade.

U.S. imports of wood and paper products totalled $9.1 billion in 1984, accounting for 13.6% of all Canadian exports to the U.S. The Canadian lumber, pulp and paper products industry employs over 380,000 (3.6%) of the total Canadian labor force. It is likely that Canada would retaliate against U.S. products if the Gibbons/Baucus bill is passed.

Grand Trunk is a major carrier of U.S. manufactured goods and agricultural products into Canada. Canada accounts for 21% of all U.S. exports, importing a wide array of machinery, parts, computers, minerals, and citrus products. For instance, two-way trade between Canada and Michigan, Ohio, Illinois and Indiana amounted to over $37 billion in 1984. Any retaliation could jeopardize this vital traffic and would lead directly to lost revenues and jobs for a broad range of U.S. companies, including Grand Trunk and its subsidiaries. Indirect effects include loss of jobs in other related industries, increased costs to consumers and deterioration in U.S.-Canadian relations.

The Gibbons/Baucus bill is extremely harmful to the U.S. and to companies like Grand Trunk, both because of the immediate consequences of excluding Canadian lumber products and other natural resources from import into the U.S. and the possibility of retaliation by Canada. The bill is especially pernicious since the U.S. government has already determined that the competition between the U.S. and Canadian lumber industries was fair and that the existing remedies against the possibility of unfair trade were adequate for Canadian lumber. The interests of the U.S. and of companies such as Grand Trunk are ill-served by such legislation. We strongly urge that the Congress defeat such legislation.

BEFORE THE UNITED STATES SENATE
COMMITTEE ON FINANCE
THURSDAY, SEPTEMBER 19, 1985

STATEMENT OF PETE KETCHAM, SECRETARY-TREASURER,
HENRY H. KETCHAM LUMBER CO.

My name is Pete Ketcham, and I am Secretary-Treasurer of Henry H. Ketcham Lumber Company of Seattle, Washington. My family has long been involved in the lumber business on both sides of the border. We have lumber mills in Canada, and a wholesale lumber company in Seattle with satellite offices in Portland, Oregon, Bend, Oregon, and Parumph, Nevada. This year, we will employ 40 persons in the United States and will sell about $30 million of lumber to U.S. and Canadian customers.

Because the Committee could not let me testify today, I am submitting this statement to make known my opposition to restrictions on American access to Canadian lumber. For our company, there never has been a separate U.S. and a Canadian lumber industry -- there has only been one North American industry. We have developed our company and invested our capital on that basis. We sell lumber into Canada and we purchase lumber from Canada. These cross-border purchases occur because the products from one side are often better suited for uses on the other side than the local products. This trade makes us all better off.

In this regard, I want to emphasize that all lumber is not alike. Southern Yellow Pine is very different from Douglas Fir, which is in turn very different from Canadian Spruce-Pine-Fir. Each type of lumber is ideal for certain purposes, and inferior for others. Consequently, access to lumber produced from all species of trees, at a reasonable price, is absolutely critical to our ability to meet the needs of our customers. For that reason, restrictions on Canadian lumber are a serious threat to our business.

Moreover, restrictions on lumber imports from Canada would result in higher lumber prices for both Canadian and U.S. lumber products. The amount of the price increases would depend on the nature and severity of the import restrictions, but I firmly believe that <u>any</u> price increases would be detrimental to both U.S. lumber dealers and U.S. lumber consumers. If lumber prices rise, the demand for lumber in the United States can only fall, and lumber users will increasingly cut back their use of lumber and substitute other products. In the long run, I think this would work to the detriment of the U.S. lumber industry.

In addition, higher lumber prices will cause reduced employment in the wholesale and retail lumber industries, and reduced employment in lumber-consuming industries such as homebuilding. The prospects of substantial price increases for imported lumber reminds me somewhat of the days of oil price increases by OPEC, which may have been somewhat beneficial to U.S. oil companies, but were catastrophic for the industries that consumed oil.

For these reasons, I hope that this Committee will work vigorously to maintain free trade in North American lumber.

National Association of Home Builders
15th and M Streets, N.W., Washington, D.C. 20005
Telex 89-2600 (202) 822-0400 (800) 368-5242

John J Koelemij
1985 President

September 12, 1985

Senator Bob Packwood
Chairman
Senate Finance Committee
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman,

On behalf of the 133,000 members of the National Association of Home Builders I would like to request that a member of our Association testify before the Senate Finance Committee on September 19 concerning the State of the U.S. Forest Products Industry. We are specifically interested in addressing Canadian softwood exports to the U.S. and the impact a countervailing duty would have on the home building industry. A substantial duty on Canadian timber could increase the cost of lumber to builders by as much as 60% if the subsidy is to be determined based on the stumpage price. Any increase in the builders cost will be passed on to the home buyer.

We believe such a provision, if enacted could add substantial costs to the housing industry and increase unemployment in related sectors of the economy.

Sincerely,

John J. Koelemij

John J. Koelemij
President

JJK/das

NATIONAL LUMBER AND BUILDING NLBMDA **MATERIAL DEALERS ASSOCIATION**

September 18, 1985

Honorable Robert Packwood
Senate Finance Committee
SD-219 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Chairman Packwood:

Enclosed are the separate statements of seven companies that requested to testify at your hearing tomorrow. These companies have asked me to express their disappointment that they were not asked to appear in person, and their hope that they will be given an opportunity to do so at a future hearing before the Senate takes up any package containing legislation on the Canadian lumber issue.

I also enclose a paper that illustrates the harm that would be inflicted on U.S. industries by enactment of any of the pending proposals to restrict Canadian lumber imports. Even by extremely conservative estimates, more than 47,000 companies and 580,000 workers would be adversely affected by legislative restrictions on Canadian lumber.

Thank you for your consideration.

Sincerely,

Harry J. Horrocks II
Director, Government Affairs

Enclosures

cc: Members of the Senate
Finance Committee

40 Ivy Street S E • Washington DC 20003 • (202) 547 2230

A THREAT TO AMERICAN HOUSING, INDUSTRIES AND JOBS:

The "Removal Right" Provision of the Natural Resource Subsidy Bill

55-453 O - 86 - 9

U.S. Companies will be Harmed

*Major American industries will be hurt by the removal rights provision of the Gibbons bill (H.R. 2451). A conservative estimate is that more than 47,000 companies with 585,000 employees would be harmed. (See attachment 1.) That's why hundreds of U.S. companies and associations have spoken out in opposition to the provision, including home builders, lumber dealers, railroads, ports and manufactured housing companies. (See attachment 2.)

*Two million additional U.S. jobs depend on exports to Canada. If unfair U.S. legislation injures one of Canada's most important industries, Canada will be under tremendous pressure to respond in kind. Retaliation would deal a heavy blow to the economies of most states. To take only two examples, Florida exported $415 million of products to Canada in 1984; New Jersey exported $1.22 billion.

The Removal Right Provision is Unfair

*Canadian timber pricing is not dual pricing. U.S. companies can and do own rights to cut Canadian timber on the same terms as Canadian companies. In fact, 25% of British Columbia's lumber is produced by U.S.-owned companies.

*The Commerce Department's 1982-83 countervailing duty investigation examined the Canadian lumber issue in excruciating detail. The Department's decision that Canadian lumber products are not subsidized was not a technical decision; Commerce cited five independent reasons for its conclusion, including the fact that "Canadian prices for standing timber do not vary significantly from United States prices. Indeed, in some cases the Canadian price may be higher."

*Forestry experts agree that stumpage price comparisons, by themselves, cannot measure whether timber is fairly priced. Thus, the very basis of the removal right provision is irreparably flawed.

Attachment 1

COMPANIES AND EMPLOYEES AFFECTED
BY RESTRICTIONS ON IMPORTS OF CANADIAN LUMBER

State	# of Companies	# of Employees
Alabama	932	13,409
Alaska	107	1,376
Arizona	624	10,753
Arkansas	689	6,960
California	4,614	73,671
Colorado	994	12,673
Connecticut	605	5,831
Delaware	125	2,102
District of Columbia	65	1,245
Florida	2,546	44,497
Georgia	1,235	18,289
Hawaii	95	2,268
Idaho	313	4,663
Illinois	1,823	17,481
Indiana	1,123	14,273
Iowa	950	8,179
Kansas	734	6,863
Kentucky	764	7,206
Louisiana	940	12,958
Maine	256	2,682
Maryland	682	11,847
Massachusetts	904	9,547
Michigan	1,470	13,663
Minnesota	1,127	11,882

State	# of Companies	# of Employees
Mississippi	517	6,020
Missouri	1,214	11,560
Montana	310	2,506
Nebraska	522	5,050
Nevada	199	2,319
New Hampshire	279	2,576
New Jersey	3,066	13,653
New Mexico	355	4,462
New York	1,943	18,014
North Carolina	1,484	18,793
North Dakota	340	2,820
Ohio	1,747	19,303
Oklahoma	1,460	12,168
Oregon	999	11,731
Pennsylvania	1,907	21,963
Rhode Island	165	1,831
South Carolina	683	6,499
South Dakota	275	2,233
Tennesse	1,024	11,996
Texas	3,292	50,882
Utah	351	4,449
Vermont	164	1,557
Virginia	1,081	15,535
Washington	1,165	13,086
West Virginia	446	4,233
Wisconsin	1,099	10,065
Wyoming	183	1,555
TOTAL	49,987	591,117

Source

The preceding statewide totals represent lumber dealers, the manufactured housing industry, and home builders. The number of companies and employees are from the U.S. Department of Commerce for 1981, the most recent figures available.

This impact statement is very conservative. The following groups have been excluded: realtors, home buyers, housing contractors* non-residential building contractors, remanufacturers of all types of wood products, newspaper publishers, shippers, and stevedores.

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*/ Only "operative builders" are included in the statewide totals in this document. Operative builders are primarily engaged in constructing residential buildings as an investment rather than contracting out their services.

BEFORE THE UNITED STATES SENATE
COMMITTEE ON FINANCE
THURSDAY, SEPTEMBER 19, 1985

STATEMENT OF JOHN J. ORR,
NORTH ATLANTIC MARINE LUMBER
TERMINAL CONFERENCE

My name is John J. Orr, and I am Chairman of the North Atlantic Marine Lumber Terminal Conference. Because this issue is so important to my organization, I wish I could have testified personally. I do, however, appreciate the opportunity to submit a written statement.

Our conference represents marine lumber terminal operations at most major ports along the Northeastern seaboard, including Boston, Providence, New London, New Haven, Bridgeport, New York, New Jersey, Philadelphia, and Baltimore.

Northeastern marine lumber terminals handle hundreds of millions of board feet of Canadian lumber annually. Virtually all of this lumber comes from British Columbia, via the Panama Canal. According to our best estimates, the port revenues from shipments of Canadian lumber passing through our facilities are $15-$20 million.

A reduction in the volume of Canadian lumber imports would have a serious impact on profitability and employment at qur facilities. A reduced volume of imports would, beyond question, result in serious revenue losses at North Atlantic marine terminals and ports and would unqestionably necessitate reductions in the number of dock workers and other employees.

Furthermore, protectionist actions by the United States simply invite retaliation by our trading partners. Such retaliation would further reduce business at our port facilities. Therefore, we urge this Committee to oppose restriction on Canadian lumber.

HEARING ON: STATE OF THE U.S. FOREST PRODUCTS INDUSTRY

BEFORE THE UNITED STATES SENATE, COMMITTEE ON FINANCE

By M. J. Kuehne
Executive Vice President
Northwest Independent Forest Manufacturers

September 19, 1985
Washington, D. C.

MR. CHAIRMAN AND MEMBERS OF THE SENATE FINANCE COMMITTEE: I am M. J. Kuehne, Executive Vice President of Northwest Independent Forest Manufacturers. NIFM is an association of 55 companies which operate approximately 60 mills in Washington State . . . these companies are primarily small and medium-sized, independently-owned manufacturers of lumber, plywood, veneer and shakes & shingles.

You have called this hearing on "The State of the U.S. Forest Products Industry." I will address the state of the industry in the State of Washington, however, I believe my remarks are applicable as well to the conditions throughout the Pacific Northwest. In direct response to the question of the state of the industry; the state of the industry is "abysmal." Over the past six years, in Washington State hundreds of manufacturing facilities have closed, hundreds of others are operating at reduced levels and 17,500 direct jobs have disappeared. Employment in the industry is at the lowest level since the State began keeping employment records after WW II. Washington State employment in 1979 was 55,000 jobs in the lumber and wood products sector. In 1985 we optimistically estimate employment to be 37,500 jobs. Employment is several thousand jobs below the previous depth of the recession in 1982.

The major reason for this decline is completely beyond the control of forest products manufacturers. It is not a lack of raw materials . . . today's inventory is within 2% of the levels that existed in the late 1970's. It is not inefficient mills . . .

this state has as modern and efficient facilities as are located anywhere in the world. It is not high priced labor . . . wage rates are equal or below our major competitor in domestic and international markets, the Province of British Columbia. It is not the high interest rates . . . interest rates have declined dramatically since the late 70's. It is not for lack of demand for our products . . . in 1984 U.S. lumber and plywood consumption set an alltime record high. The major reason for the decline of the forest products industry in the State of Washington is because of trading policies of foreign countries.

British Columbia timber subsidies:

Over 90% of the timber in British Columbia is owned by the Province. The Province provides this timber to mills under a non-competitive timber allocation system. The system is designed to insure operation of mills regardless of market conditions in the world. As a result of this system, British Columbia mills have increased market share in the United States . . . and more importantly to Washington State manufacturers, right here in Washington State. British Columbia lumber has increased from approximately 23% of Washington State lumber consumption to over 33% of the lumber consumed in the state during the past six years. Canadian imports have also impacted major domestic markets outside of Washington State, the most significant being the Southwest market.

Shake and shingle manufacturing in Washington State has been even more heavily impacted. Washington is the leading state in manufacturer of wood shakes and shingles in the United States. This industry has suffered tremendous losses as British Columbia imports have increased from 37% of U.S. consumption to 77% over the past decade. The reason for the loss in market share of wood shakes and shingles is the same as with lumber, lower timber prices.

U.S. International Trade Commission in their 332 investigation published in April

1982 concluded, "It would appear from material and data collected during the course of the investigation that the primary reason for Canada's increasing market share is the loser cost of raw materials for Canadian lumber produce- " We expect that the current 332 investigation will reinforce this finding. There are at least three measures from which one might conclude that timber in British Columbia is being provided by the Province at below the fair market value to British Columbia manufacturers.

1) Comparing standing timber prices, the price of standing timber in British Columbia is from 1/5th to 1/10th the prices paid on competitively bid timber sold by the state and federal government in Washington State.

2) A comparison of the small percentage (5% to 10%) of timber that is sold by competitive auction by the Province of British Columbia. Provincial records show this timber which is competitively bid sells consistently for three times the price of allocated timber.

3) Log prices of timber delivered to the mills in coastal British Columbia is from $20 to $80 per thousand board feet cheaper for comparable species and grades than logs sold in Western Washington.

As a resolution to the contention by the government and industry of British Columbia and Canada, that their industry is not being subsidized, I have specifically requested in hearings in January of 1985 held by the U.S. International Trade Commission and by the U.S. Trade Policy Committee, that log export restrictions between the United States and Canada be bilaterally eliminated so that timber could be domestically processed in either country. The U.S. Trade Representative requested the Canadian government to consider this action but was flatly turned down. I have on several occasions asked the industry in British Columbia to support an initiative to open these raw material markets between our two countries and they have flatly stated, "No" and when questioned why stated, "No comment." Why would they so vehemently oppose free trade in raw materials between our two countries if it were not to protect the timber advantages they have with their subsidy system?

Trade with Japan:

Japanese forest products trade has been and continues to be principally log exports. Approximately 45% of all timber harvested in the State of Washington is exported as raw logs, mainly to Japan, China and Korea. Log exports today account for about 80% of solid wood exports to Japan.

U.S. manufacturers are absolutely convinced they can manufacture lumber, plywood and other solid wood products and export them to Japan at prices below those that Japan purchase from their domestic mills that are either supplied by logs from Washington State or their own forests.

As a result of pressures to limit exports of logs from the Pacific Northwest in October 1980 the Japanese industry and government announced a plan to "promote lumber imports from the United States" stating that JALC (the Japanese industry) recently reached a basic concensus to promote an increasing portion of U.S. lumber in Japanese wood product imports from the United States." The Japanese went on to promise "to take the initiative to eliminate commercial or technical ambiguities inhibiting U.S. sales." The U.S. Trade Representative at the time, Ambassador Askew, in an official announcement stated, "The U.S. objectives again pushed the initiative as a way to increase U.S. lumber imports and that improvement in the mix which currently contains a large portion of logs." He added, "the fact that the private sector in Japan which makes the key decisions in this area made this statement augurs well for the achievement of these objectives." Askew added, "The Japanese industry initiative as we understand it appears to come from the very heart of the Japanese distribution system."

The fact is the Japanese have declined to purchase increasing amounts of U.S. lumber. Japanese lumber imports from the United States were 641 million board feet in 1979, 634 million board feet in 1980 and have remained below that level ever since. In 1984, Japan imported only 545 million board feet. We estimate 1985 imports will be under 600 million board feet.

The Japanese restrict lumber imports from the U.S. by a complicated distribution system in which trading companies provide logs to Japanese mills and finance the inventory of logs, then purchase and distribute finished products.

The Japanese have restricted plywood imports from the United States for the past twenty years by first taking fifteen years to agree to standards and once now that is settled by refusing to eliminate the 20% tariff on plywood imports. Recently when pressed by Senator Evans to purchase Northwest finished wood products, the Japanese responded that to do so would hurt reforestation efforts in their own country. The response doesn't seem to make sense on the surface. However, if you realize that through the Japanese distribution system they maintain a two-tiered price system, one for lumber domestically produced and another for lumber imported. To eliminate that system and buy finished wood products competitive with that domestically manufacturered the prices for both imported logs and domestically manufactured logs would have to decline significantly. Such a decline in price would make marginally productive Japanese forest lands inoperable, making it unprofitable to reforest these marginal lands that are propped up by artificially higher domestic lumber prices.

Recommendations:

1) The most effective way to deal with the unfair Canadian lumber import situation is to pass the Gibbons-Baucus bill. This legislation will do nothing more than make it possible to redress unfair trade practices of selling a natural resource at below its fair market value. If the Canadians are not selling timber at below its fair market value they have nothing to fear from this law. If they are unfairly subsidizing timber by providing it at below its fair market value

thereby causing injury to the U.S. industry, they do indeed have much to fear. The remedy will be to impose a tariff equal to the amount of the subsidy as determined by the Department of Commerce. There is indeed nothing protectionist about the Gibbons-Baucus bill. Its passage and utilization will help to bring about free trade as it will discourage unfair trade by foreign countries.

2) There are two ways to discourage the Japanese from restricting imports of finished U.S. wood products. One would be to limit their access to logs from the Pacific Northwest, the second would be to limit Japanese access to U.S. markets for their finished goods. Legislation which rewards increased purchases of all products including logs from Japan will not encourage the purchase of finished products. The difference in price between what the Japanese pay for logs and finished lumber is very small.

As previously stated, they will pay a higher price for logs to protect their own domestic industry, thus legislation which rewards the purchase of more products in itself will not solve the problem.

The solution we recommend is to restrict the export of all timber from public lands in the Western United States to be triggered if the mix of finished wood products with raw logs does not improve to at least 50-50 by 1995.

This would have two beneficial effects. One, it would make it in Japan's interest to eliminate tariff and non-tariff barriers to finish wood products imports from the United States. Two, it would reduce the stress that high levels of log exports are having on timber supplies in Washington State.

<u>In summary</u>: The timber industry in Washington State is being significantly injured by trade practices of foreign countries which interfere with its ability to compete both in its own domestic markets and in overseas markets. There is no action industry can take to remedy this situation. It must have available laws which deal with unfair trade practices if those practices are to be eliminated and we are to achieve our goal of free trade!

BEFORE THE UNITED STATES SENATE
COMMITTEE ON FINANCE
SEPTEMBER 19, 1985

STATEMENT OF PAT POOLE, PRESIDENT
POOLE TRUCK LINES

My name is Pat Poole and I am the President of Poole Truck Lines, Inc., which is headquartered in Evergreen, Alabama. Our company has trucking terminals throughout the eastern two-thirds of the United States, including Evergreen, Birmingham, Haleyville, Mobile, and Montgomery in Alabama; Pensacola, Florida; Macon, Georgia; Moline, Illinois; Henderson, Kentucky; New Augusta and Wiggins, Mississippi; Mexico, Missouri; Spartanburg, South Carolina; Nashville, Tennessee; and Beaumont, Texas.

Our fleet has over 1,000 trucks in operation at the present time, and we employ over 1300 drivers and terminal workers. We have operating authority in all 48 states of the continental U.S., and our annual revenues exceed $70 million.

Although I would very much have preferred to testify in person before this Committee, I am appreciative of your allowing me to give you a written statement.

Our company opposes any restraints on the importation of Canadian lumber and lumber products. Each year, our revenues from shipments of Canadian lumber and lumber products to the U.S. are well over $1 million. Thus far in 1985, we have transported 356 truckloads of lumber from one Ontario company alone. Our operations in the Northeastern states depend critically on such shipments, primarily from Ontario and Quebec, to keep our trucks running.

Thus, if the United States government significantly curtails imports of lumber and lumber products, such action would have a severe, adverse impact on our firm. Clearly, our revenue loss would be substantial. In addition, we would find ourselves with a surplus of trucks and drivers, which could ultimately lead to a reduction in our fleet of trucks and in the number of drivers that we employ.

I also want to emphasize that the lumber trade in North America is a two-way street. Not only does our company transport lumber and lumber-related products from Canada to the United States, but we also transport substantial quantities of U.S.-produced lumber products to Canada. These products include oak flooring, hardwood veneers, and utility poles made of Southern pine. I am concerned that restrictions on Canadian lumber imports might lead to restrictions on U.S. exports, and thus to a further loss of business for our company.

For these reasons, I believe that restrictions on Canadian imports would be bad policy, and I urge this Committee to oppose them.

BEFORE THE UNITED STATES SENATE
COMMITTEE ON FINANCE
THURSDAY, SEPTEMBER 19, 1985

STATEMENT OF HOWARD L. ROBERTS, PRESIDENT
ROBERTS AND DYBDAHL, INC.

My name is Howard Roberts. I am President of Roberts & Dybdahl, Inc., a wholesale distributor and broker of lumber and building materials. Roberts & Dybdahl employs approximately 175 workers, operates in 13 Midwestern states, and had sales in 1984 of over $80 million. Roberts & Dybdahl also manufactures, directly or through subsidiary companies, wood trusses, farm buildings and modular homes, and operates a transportation company.

Approximately one-third of the lumber we used or sold in 1984 was of Canadian origin. The remaining two-thirds was produced in the United States.

As I am sure you can tell, any legislation affecting lumber is very important to our company, and I would have liked to have appeared before the Committee personally to present my views. Nevertheless, I am glad you will accept my written statement.

In my opinion, the problems faced by U.S. lumber producers have little or nothing to do with Candian lumber imports. Their problems are really no different than those of the Midwestern farmer, the Western rancher or the Eastern banker. We all confront the same dilemma: the state of the U.S. economy. The plight of U.S. lumber producers will improve only when Congress deals responsibly with the real source of their ills: reckless overspending by our government. Congress needs to reduce spending enough to cause interest rates to drop. When interest rates drop, the Midwestern consumer will be able to stop dreaming about his new home or new farm building and begin construction. When this construction begins, orders for lumber, both U.S. and Canadian, will flow as in past business cycles.

The problems of Roberts & Dybdahl parallel those of U.S. lumber producers. For example, in 1979 we employed over 450 people. Today we employ approximately 175.

In our opinion, restrictions on lumber imports will cause employment at our company to drop even further. Import restrictions will artificially inflate our customers' costs at the same time these customers are suffering the effects of a farm economy in a state of depression. We have a real problem that needs a real solution, not a quick-fix. As our experience with price controls demonstrates, inhibiting free market forces only leads to economic inefficiency. We do not need legislation that would help start us on a non-stop trip to international protectionism. We do not need legislation that fuels massive trade retaliation, or that interferes with free trade and artificially regulates the supply and price of lumber in the United States. What we do need is serious straightforward action by Congress to reduce spending.

BEFORE THE U.S. SENATE COMMITTEE ON FINANCE
THURSDAY, SEPTEMBER 19, 1985

STATEMENT OF STEPHEN SNAVELY, PRESIDENT,
SNAVELY FOREST PRODUCTS, INC.

My name is Steve Snavely, and I am President of Snavely Forest Products, Inc. I would have liked to have had the opportunity to testify in person before the Committee, but I appreciate your time constraints and welcome the opportunity to submit my written statement.

Our company is a major wholesaler of lumber and lumber products. We presently have lumber yards in Denver, Colorado, Dallas, Texas, Phoenix, Arizona and Pittsburgh, Pennsylvania, with additional sales offices in Medford, Oregon, and Newport Beach, California. In total, we employ in excess of 110 employees. Our sales revenue for 1985 exceeded $60 million, and I would estimate that approximately 30% of this revenue was generated by the sale of Canadian lumber products.

Our company opposes any restrictions on lumber imports. Significant restrictions on the importation of Canadian lumber would undoubtedly result in higher prices for both Canadian and U.S.-produced lumber products. In the short run, I suppose our company might benefit slightly because the value of our inventory would increase. But in the long run, we would be severely disadvantaged. Significant price increases would substantially reduce the demand for lumber and lumber products, and alternative products made of aluminum, plastics and masonry would be substituted for lumber. In addition, higher lumber prices would translate into higher prices for new homes, which would inevitably reduce the number of new homes being constructed.

As I am sure this Committee is well aware, housing is already very expensive in the United States -- a problem that is only made worse by interest rates that remain above historical norms. In my opinion, significant increases in home prices would make housing unaffordable for many Americans, further weakening the demand for our lumber.

Restrictions on Canadian imports would also make it very difficult for us to satisfy the needs of many of our customers. Typically, our customers buy Canadian lumber, especially Spruce-Pine-Fir from Western Canada, because of its highly desirable properties. The lumber is bright white, with small knots, and is easily workable. It absorbs stain well, and is available in the very long lengths that are necessary for many types of construction.

If this Canadian lumber became unavailable to us, no adequate U.S.-produced substitute would be available. The principal domestic alternative, Southern Yellow Pine and green Douglas Fir, simply would not meet the requirements of our customers, who would suffer as a consequence.

Finally, I want to point out that we do a very substantial export business to Canada, principally in hardwoods. I find it very difficult to believe that if we restrict Canadian lumber imports, our exports of lumber to Canada would not also be restricted.

Thus, our company is steadfastly opposed to restrictions on Canadian lumber imports. Such restrictions would only work to the disadvantage of lumber dealers and lumber consumers throughout the United States, and we urge this Committee to use its best efforts to maintain the free trade in lumber that now exists.

STATEMENT OF DENNIS M. CAVANAUGH

PRESIDENT AND CHIEF EXECUTIVE OFFICER

SOO LINE RAILROAD AND MILWAUKEE ROAD INC.

SUBMITTED FOR THE RECORD

SENATE FINANCE COMMITTEE

DOMESTIC TIMBER INDUSTRY HEARING

SEPTEMBER 19, 1985

Mr. Chairman and members of the committee, my name is Dennis Cavanaugh and I am President and Chief Executive Officer of the Soo Line Corporation, the holding company which owns and operates the railroads known collectively as the Soo/Milwaukee System. Thank you for the opportunity to express our concerns about proposed legislation restricting Canadian timber imports. Although I am aware that this hearing is intended to be a broad discussion of the problems facing the U.S. timber industry, I will restrict my comments to the issue of Canadian softwood imports as they directly affect the Soo/Milwaukee.

The recently combined Soo Line Railroad Company and Milwaukee Road Inc. provide rail service in the states of Minnesota, Wisconsin, North Dakota, Michigan, Illinois, Indiana, Iowa and Kansas. Connections to the Canadian Pacific Railroad are also available on the Soo/MILW system at Noyes and Portal, North Dakota and Sault Ste. Marie, Michigan. The Soo/MILW is a medium-sized, regional railroad with 8,320 employees and $732,591,000 million in annual railway operating revenues. Currently, in excess of $100 million in annual revenues or approximately 20% of our total business comes from transporting timber and wood products of Canadian origin.

Because of the importance of Canadian goods to our business, we are quite concerned about recent efforts to impose high tariffs or import quotas on Canadian wood products. Clearly, the Soo Line has a vested interest in continued timber trade with Canada. However, we do not contend that this Committee's decision should be based on our desire, or the desire of other railroads to continue hauling these products. Rather, we wish to explain that the implications of a decision to limit Canadian timber imports extend beyond the U.S. timber industry and domestic consumers of timber products.

The Soo Line is an integral part of a finely tuned market system for U.S. and Canadian wood products. For the most part, supply and demand in this market are disciplined by a myriad of purely economic factors. Customer species preference for different product uses, availability and price of the U.S. and Canadian timber supply, and transportation costs are only a few of these factors. However, when an artificial restriction (such as high duties or quotas) is imposed on a market, not only is the target market disrupted, but all of the secondary markets are also affected. We are able to give you information about the ripple effects of such a decision on the rail transportation market in the Midwest.

Anyone who has followed the recent history of Midwestern rail service knows that for many products, declining markets and pervasive truck and barge competition have severely squeezed rail profit margins. Indeed, several railroads (including the Milwaukee Road) were forced to declare bankruptcy and others were forced to abandon thousands of miles of rail lines. These changes have resulted in fewer, but healthier rail competitors and, despite the current condition of the agricultural economy, the Soo Line generally feels quite positive about the future for rail service in the Midwest.

However, a severe reduction in timber movements could not help but have an negative impact on our ability to continue some of the marginally profitable services which we provide. In addition to being a sizable percentage of our total business, the economies of long-haul movement of Canadian timber make this traffic a critical segment of our revenue base. Therefore, to the extent that Canadian timber is priced out of the U.S. market, our employees will be adversely affected and the stability of rail service to many communities in the territory we serve could be jeopardized.

The Natural Resource Subsidy Bills, S. 1292 (Baucus) and H. R. 2451 (Gibbons), are of particular concern to the Soo Line. The removal rights provisions in these bills could result in duties of up to 60% on all imported Canadian wood products and would impose a substantial hardship on all U. S. firms and consumers who buy, sell, or transport Canadian timber.

We have considered the arguments in support of and against these bills and have reached the conclusion that there is no need for legislation. You have heard or will hear all of these contentions and there is no need to repeat them here.

We only ask that in considering this legislation you recognize the far-reaching effects which it would have. The problem cannot be viewed simply as U.S. producer against Canadian producer. Many others, including consumers, manufacturers, transporters, and dealers will also be affected by your decision. Our concern is for our employees, our customers, and the communities which we serve. Passage of this legislation or any legislation reducing Canadian timber imports will adversely affect all of them.

Again, thank you for this opportunity to express our concerns. Should you wish any additional information, I will be happy to provide it.

TAXATION WITHOUT DISCRIMINATION (TWD)

SR-1, Box 23-A, New Castle, Va. 24127, 703-864-5949
Statement of Fortescue W. Hopkins, Director
Senate Committee on Finance
Hearings on Comprehensive Tax Reform

RE: Discriminatory Tax Laws

Mr. Chairman:

Today, ours is not a Government of, by and for the people. Instead, it is a Government of, by and for "ORGANIZED MINORITIES", who, with Millions of dollars in tax-free PAC contributions to or for the principal benefit of the members of the Tax Writing Committees of Congress, attempt to persuade these members to enact or to maintain discriminatory tax laws for their benefit. See Tax Notes, 8/19/85, P.922, Appendix "A", herein.

In many, if not most, instances, "Discriminatory Tax Laws" result in Congress doing "indirectly" what it would not have the power under the U.S. Constitution to do "directly". In the mean time, since the "Switch in Time to Save Nine"(1937) and having inundated themselves and all Federal Courts with extensive litigation resulting from a confused and expansive interpretation of the application of the 14th Amendment, the Justices of the Supreme Court (the "SUPREMES") are now and have been unwilling to accept their clear responsibility to curb an ever accelerating degree of discriminatory tax laws &"tax subsidies" intended to achieve non-revenue related objectives not authorized under any provision of the Constitution.

TWD hopes to have (or to be) the PAC that truly represents the "total point of view of all Americans", whether organized or not. It will, however, not contribute one thin dime to or for the benefit of any member of Congress or any candidate for national office. TWD will use its funds, primarily, for the following purposes:

1. With the help of PATRICK HENRY*, WALTER K. TULLER**(see Appendix B, herein) and the brightest independent minds available (legal or otherwise), to convince the American people that the SUPREMES have greviously erred in their failure to protect the individual citizen's Constitutional Right not to be subject to discriminatory tax laws intended to achieve non-revenue related objectives where such discrimination or objective is not authorized under any provision of the U.S. Constitution with the sincere hope that the SUPREMES (or, at least, five of them) will take cognizance of the resulting adverse public opinion to the extent that they will, then, recognize their duty and rule, accordingly.

*PATRICK HENRY'S testimony before the Virginia Constitutional Convention of 1787. See Elliotts Debates, The Michie Company, Charlottesville, Va.

**WALTER K. TULLER'S persuasive analysis of the Constitutional aspects of discriminatory taxation contained in his book, THE TAXING POWER/ STATE INCOME TAXES, Callaghan and Company(1937), the last 13 pages of which are attached hereto as Appendix B.

2. To contribute to the campaigns of state legislators who will vote for and support a call for an "OPEN CONSTITUTIONAL CONVENTION" under Article V of the U.S. Constitution to consider needed amendments to the U.S. Constitution, including:

THE TAX MAGNA CARTA

"CONGRESS SHALL MAKE NO TAX LAW THAT IS, IN THE SLIGHTEST DEGREE, DISCRIMINATORY OR INTENDED TO ACHIEVE A NON-REVENUE RELATED OBJECTIVE, WHETHER OR NOT SUCH DISCRIMINATION OR OBJECTIVE IS AUTHORIZED UNDER ANY PROVISION OF ANY CONSTITUTION."

[The foregoing proposed Amendment is considered a "base line definition". Of course, such other exceptions as may be desirable (religious, corporate-individual intergration, foreign, etc) can be added by a Constitutional Convention (or proposed as Constitutional Amendments by Congress). This way you have "Tax Reform" from the "bottom up" and not from the "top down", the only way any meaningful Tax Reform can possibly be accomplished.]

3. To defuse the political power of "ORGANIZED MINORITIES" and to make our Representative Democracy truly "Representative", State Legislators will also be asked to consider a number of needed Constitutional Amendments including one concerning PACS:

"NO CONTRIBUTION OR EXPENDITURE TO OR FOR THE BENEFIT OF THE CAMPAIGN OF ANY CANDIDATE FOR PUBLIC OFFICE WILL BE ALLOWED EXCEPT BY THE INDIVIDUAL REGISTERED VOTER OF THAT CANDIDATES DISTRICT AND, THEN, IN ONLY SUCH AMOUNTS AS PERMITTED BY THE STATE LEGISLATURE AND, FURTHER, THAT ALL SUCH AMOUNTS WHEN RECEIVED OR EXPENDED WILL BE TAXABLE AS INCOME TO THE CANDIDATE AND NO DEDUCTION OR TAX CREDIT WILL BE ALLOWED FOR THE CONTRIBUTION OR EXPENDITURE."

[If TWD attains the foregoing objective, it will truly be the "PAC TO END ALL PACS".]

CONCLUSION

PATRICK, TWD promises you that, despite the incalculable damage inflicted on America by your refusal (or inability) to accept George Washington's appointment of you as Chief Justice of the Supreme Court, your great dream of INDIVIDUAL POLITICAL RESPONSIBILITY, INDIVIDUAL ECONOMIC OPPORTUNITY, INDIVIDUAL RELIGIOUS FREEDOM AND INDIVIDUAL PERSONAL LIBERTY will not be allowed to die. TWD will re-acquaint the American people with your testimony before the Virginia Constitutional Convention of 1787, and when they test your common sense observations and predictions against current events and the events of the past two hundred years, they will believe, and you will assume your rightful place in Americas' History as our GREATEST PATRIOT. Recently, at

Williamsburg, President Reagan referred to you as the "Father of the First American Tax Revolution". It may well be that you and WALTER K. TULLER will be the Fathers of THE SECOND AMERICAN TAX REVOLUTION.

WALTER, nearly 50 years ago, you stated at the end of your classic book, THE TAXING POWER:

> "If the courts permit those in control of the legislative and executive branches of the Government to tax without due regard to constitutional limitations, particularly to impose discriminatory taxes, Constitutional Liberty is dead. Whatever forms may survive, the Government will be, in fact, Absolute. Here lies our greatest and most immediate danger. The tide today is setting toward that shore. The only hope lies in revitalizing the oath, solemnly taken by every judge of every court, to maintain and defend the Constitution of the United States." (emphasis supplied)

WALTER, in the past 50 years this "tide" of discriminatory taxation has resulted in a "tower of babel" (the Internal Revenue Code) that is about to collapse of its own weight and has become a "tidal wave" far beyond your worst expectations. TWD promises you, Walter, that it will find millions of Americans to support your cause and that this "tide" will recede, gradually, at first, and then it will go out with a roar, never to return.

Respectfully submitted,

TAXATION WITHOUT DISCRIMINATION*

by Fortescue W. Hopkins
Fortescue W. Hopkins, Director

* A Virginia non profit, non-stock corporation incorporated July 2, 1984

TAX NOTES, August 19, 1985 APPENDIX "A"

TAX REFORM HELPS MEMBERS OF TAX WRITING COMMITTEES RAKE IN THE PAC MONEY. From insurance companies wanting to preserve the tax-free appreciation of life insurance earnings, the money comes; from horse breeders who want to keep rapid depreciation of thoroughbreds, the money comes; from military contractors who want to retain favorable tax treatment of earnings from multiyear contracts, the money comes. All of it flowing to House and Senate members, and thanks to tax reform fever, a hefty chunk of the money is going to members of the tax writing committees. The politicians' hunger for money is so great, *The Wall Street Journal* reports, that it is beginning to draw groans from lobbyists, who say that they have never seen such appetites for contributions in a non-election year and that the politicians are holding too many fund-raising events too early, at too high a price.

The *Journal* writes that members of the Finance and Ways and Means Committees have nearly tripled their take from political action committees (PACs) during the first six months of 1985, to $3.6 million, compared to a similar period in the past two-year election cycle. According to the *Journal*, the tax writers, who account for about 10.5 percent of all House and Senate members, received 23.5 percent of all PAC money raised by incumbents. The leading PAC beneficiary on Capitol Hill is Finance Committee Chairman Bob Packwood, R-Ore., who raked in $691,015 from PACs from January 1 to June 30 of this year. (A spokeswoman for Packwood discounted any notions that he may be unduly influenced by the money, saying, "In Packwood's mind a PAC represents the sum total point of view of American workers.") Senate Majority Leader Robert Dole, R-Kans., and Sen. Steven Symms, R-Idaho, both Finance members were, respectively, the second and fourth highest PAC beneficiaries in the Senate. In the House, Ways and Means members Sam Gibbons, D-Fla., Henson Moore, R-La., and Pete Stark, D-Calif., were first, third and sixth, respectively.

Robert McIntyre of Citizens for Tax Justice says a "bright side" of the PAC boodle is that Congress members "might be trying to get the money now because after they do what they are going to do nobody will want to give them money anymore," but he adds that the money may lead them away from real tax reform. Others speculate that the flood of early money will give incumbents an even greater edge than in the past.

Meanwhile, Senate Finance Committee member Russell B. Long, D-La., the Committee's ranking minority member who is retiring next year, says he will be returning $360,543 in campaign contributions to individuals and PACs. *The Wall Street Journal*: Brooks Jackson, 8-9-85, p. 36. *The Washington Post*: (AP wire), 8-10-85, p. A2.

The taxing power is admittedly broad. So long as the burden is uniform, it may be that the citizen has no redress in the courts. But uniform taxation and discriminatory taxation are different things. They are different in concept and essentially different in effect. The very purpose of a discriminatory tax is to burden different citizens or different classes of citizens unequally. Its effect is or well may be to destroy one citizen and build up another. We have after all a Constitutional Government—not an Absolutism. One of the reasons why we have a Constitutional Government is because of the abuses which are possible under an Absolutism. One of the most potent of those abuses is the power to impose discriminatory taxes. Due process of law and equal protection of the laws are not idle terms. They were placed in the Constitution for a purpose. That purpose was to guarantee practical equality before the law to all citizens and to prohibit this Government from engaging in those practices common to despotic governments, among others, discriminatory taxation. Granting that the Government has some power to levy discriminatory taxes, still that power must be limited by constitutional principles else we do not have a Constitutional Government. It may be difficult to lay down any hard and fast rule as to just where those limits are.

But it is not possible that the Legislature is limited only by its own ideas of "Social Justice." This, we repeat, would mean that it is not limited at all. As nearly as the rule can be expressed in words, it is suggested that it should be substantially this: That the Legislature may discriminate in taxation in those cases, and *only* in those cases, where it might similarly discriminate by direct, substantive legislation. Where the Constitution prohibits that, it is believed it necessarily prohibits the accomplishment of the same end by the means of discriminatory taxation.

The Author makes no claim that this is the law today. There are many cases which are contrary to these views. There are also a number of cases that are entirely consistent with them. As stated at the beginning of this Chapter, it is believed fair to state that the law on this subject is far from settled. The method of treating each case by itself, with very little regard to fundamental concepts, has failed. Its result has been a multitude of inconsistent and irreconcilable decisions, frequently rendered by a bare majority of the court. It has brought the law on this subject into the utmost confusion. Yet it is a subject of the utmost importance. If wrong principles are allowed to prevail, it may result in disaster to our entire constitutional system. We have not attempted in this Chapter to try to bring order out of the chaos of decided cases. We have endeavored to analyze, as a matter of sound principle, what limitations the Constitution itself imposes and necessarily imposes upon the power of the Legislature to lay discriminatory taxes upon the citizen. We have sought to point the truth, which must be clear to any one who will consider and fairly face the facts, that the present tendency to permit to the Legislature ever-widening powers to impose discriminatory taxes on the citizen must be checked—that unless it is checked Constitutional Liberty will inevitably be destroyed.

CHAPTER XX

CAN CONSTITUTIONAL LIBERTY BE PRESERVED

The answer will probably be given by the courts. At first impression this may seem a strange statement. Upon reflection, it is believed the truth of it will be evident. The great danger of the loss of our liberties lies within, not without, this country. The danger of conquest by a foreign foe can fairly be said to be remote. The danger that some day there may be a revolution attempting to set up the dictatorship of the Proletariat is more real. But the success of such a movement seems unlikely. The danger that we, ourselves, may, more or less blindly, destroy our own liberties, is a very real danger. Two means, either of which may accomplish this end, are constantly with us. One is Bureaucracy, exercising well-nigh despotic powers incompatible with Liberty. The other is unjust and particularly discriminatory taxation under which the Legislature may exercise practically despotic powers equally incompatible with Liberty. Whether the Courts have the vision and the courage to restrain these within the limitations of the Constitution will probably determine whether Constitutional Liberty shall survive or perish.

Of what does Constitutional Liberty consist? We Americans have taken it so much for granted that we have seldom taken the time to consider what it is. In essence it consists of this: That the Constitution forbids the Government to infringe certain rights of every citizen, and provides a means whereby any attempt by the Government to infringe those rights of any citizen can be and will be nullified. Both the prohibitions upon the power of the Government and the means by which, as a practical matter, any attempted exercise of a prohibited power can be and will be nullified, are essential to Constitutional Liberty. Thus, constitutional limitations upon the power of the Government and the willingness of the Courts to strike down any attempt on the part of the Government to exercise a prohibited power, are indispensable to the preservation of Liberty. If either fails Constitutional Government and Constitutional Liberty dies. Whatever outward forms may be preserved, the Government becomes an Absolutism. There will follow the rule of the Monarch, the Dictator, or the Mob.

Except for constitutional limitations, and except there be tribunals having the power, and willing to exercise the power, to strike down unconstitutional acts by any department of the Government, the Government may do anything. Under a Government that may do anything, the citizen has no rights and no liberties. The Government may allow him some privileges. If it does, it is simply as a matter of grace. It may deprive him of them at the pleasure or caprice of those in control of the Government. A people living under the heel of such a Government is not and cannot be a free people. We repeat, Liberty exists only where each citizen has rights which the Government has no power to infringe and where, if it does attempt to infringe them, the citizen has a practicable remedy by which that attempt will be nullified and his rights protected. This is just as essential as the right itself. Of what value is a right unless it can be enforced and protected? Obviously a citizen cannot defend himself by force against the Government. Hence, if the constitutional rights and liberties of citizens are to have any validity, the courts must have the power to enforce and protect them against action by the Government itself. Otherwise whatever the Constitution may say, the fact is that the Government is absolute and there is no Liberty.

But it is not enough that the courts have the *power* to nullify the action of the Government when it violates constitutional rights. They must also be *willing* to do so. This involves two essential elements: *1st:* A state of mind wherein the preservation of the constitutional system and the liberties of the people guaranteed by the Constitution transcends any supposed expediency—whether it be called general welfare, social justice or what-you-will; *2nd:* The moral courage to uphold and preserve the liberties of the people even against themselves. Time and again the popular mind is carried away by movements which would result in breaking down constitutional limitations and in destroying the liberties of the very people who most loudly advocate the movement. It cannot too often be repeated that Liberty can exist only in a state where limitations upon the power of the Government not only exist on paper but are fearlessly enforced in fact.

In a simple civilization the task is relatively easy. In a civilization as complex as ours has become it is probably the most difficult task to which Mankind has ever set his hand. The pressure to whittle away the constitutional limitations on the power of the Government and so gradually to destroy the constitutional liberties of the citizen is unceasing and well-nigh irresistible. Only if the courts vigorously and courageously resist all encroachments by legislative or executive power—only as they fearlessly apply the principle *obsta principiis*—can the destruction of these constitutional principles be averted. (Compare ante, pages 8, 10.)

Our Government has become—and inescapably so—a Government of organized minorities. Organized minorities want something. It is for that purpose that they are organized. Usually they want something for themselves. Usually it is at the expense of the rest of the people. The rest of the people are unorganized. The country is too vast, the problems of economics, of social policy, of finance, and of all the various inter-relations of present-day life are too complex, for the general public to be organized for effective political action. Hence, they are at the mercy of the Government, which means, in fact, at the mercy of the organized minorities who can gain control of the Government. What protection have they for their rights and liberties? None, except as the courts resist and strike down every act of the legislative and executive departments which infringes upon them.

Time and again in human history great civilizations have broken down and peoples have perished. Why? Historians suggest various reasons. The Author begs leave to suggest one reason that seems common to all and that probably has its foundations in some basic principle of mass psychology. It is this: The civilization became too complex for the understanding of the average man. Hence, it fell of its own weight. A simple civilization seldom falls. The average man can understand its problems. Understanding them he can find an answer for them and can meet them. But our civilization today is the most complex that the world has ever seen. It is trite to say that the average man cannot understand it. The plain fact is that no one understands it. The complicated inter-relations of present-day life, social, economic, financial, industrial, international, are beyond the grasp of the wisest.

But there is one thing which we can all understand. That is our American constitutional system. It consists of a Government created by the Constitution—a Government whose powers are not absolute, but are limited by the Constitution—and whose citizens have rights and liberties that are above and beyond destruction or infringement by any act of the Government. This is fundamental and should be unchangeable. Citizens have certain basic rights whether the civilization is simple or complex. These rights must be preserved against any action of the Government—otherwise they are not rights.

There is a constant effort on the part of the Government, sometimes conscious, sometimes unconscious, to break down those rights. This is true no matter what the form of Government. It is just as true in our so-called popular Government, that is, our Government of and by organized minorities, as in any other form. Perhaps it is more true under our form, for the control of the Government and hence, the things which those in control want for themselves, is subject to constant change.

It is only human nature that those who have won control of the Government, usually after bitter political strife, should be intolerant of any limitations on their freedom of action. They have fought and won. They fought to accomplish some purpose. Shall a mere Constitution thwart them? If the Constitution is in the way, so much the worse for the Constitution. They immediately set themselves to find some way to circumvent it. This is natural and inevitable. Those in control of the Government solemnly resolve by legislative enactment that the measures they advocate will advance the general welfare and promote social justice. Under our system, if there is any reasonable basis for the conclusion, legislative determination of what will advance the general welfare or promote social justice is final.

Hence, if the courts accept the argument that the Government may do anything that will advance social justice, that acceptance writes the death warrant of constitutional limitations and of Liberty. If the legislative and executive departments may do anything that they believe will advance social justice, then the Constitution is no longer the supreme law of the land. The will of the group in control of the legislative and executive departments at the moment is the supreme law of the land. Both cannot be supreme. If they come in conflict, one or the other must yield. The people who created the Government have declared that the Constitution is the supreme law of the land. If it is, the action of the legislative or executive branches which conflicts with the limitations in the Constitution is void, *even though it is action which would advance social justice.* Otherwise the limitations in the Constitution upon the powers of the Government are mere idle words, without force or meaning.

Herein, the Author submits with all deference, lies the fundamental fallacy in the idea, so prevalent today, that if legislative or executive action will advance social justice, it must be sustained by the courts, even though it violates constitutional limitations or infringes upon the constitutional liberties of the citizen. The concept of the Constitution is that the supreme and transcendent consideration of general welfare and of social justice, to which all transitory ideas must yield, is the preservation of a Government of limited powers and of the constitutional rights and liberties of citizens of the United States. The rule of the Constitution, it is submitted, is this: That even though the executive and legislative branches believe that certain action is necessary to promote social justice, still that action cannot be taken unless it is action *within* the constitutional powers of the Government and unless it is action which will *not infringe* upon the constitutional liberties of the citizen. This must be so or the Government is not a Constitutional Government. A Government whose powers are limited only by its own views of social justice is not limited at all.

Many of us are prone to jump to the conclusion, without any adequate reflection, that if the *forms* of popular government are preserved, Liberty is safe. There can be no greater delusion. Forms of popular government are of little, if any, value in insuring Liberty. Indeed, popular government not restrained by constitutional limitations may be as destructive of Liberty as any other form of Despotism. Athens had an almost complete Democracy. It was so small that every citizen could know and understand its governmental problems. Yet its citizens never had Liberty. The citizen of Athens held his property and even his life at the whim and caprice of any temporary majority that might gain control of the Government. Witness Aristides, to cite but a single example. The Athenians never learned the fundamental lesson that Liberty can exist *only* where there are effective limitations upon the power of the Government and upon the power of any temporary majority of the people. Hence, magnificent as were their achievements in many other lines of thought and action, and though they had popular government in its most complete form, they never had Liberty.

The fact that mere forms of Government, even the form of popular government, is no protection to Liberty was again demonstrated in Rome. Without now going into detail, it is a fact that the *forms* of popular government were carefully observed and preserved for the better part of a century after Liberty was dead and almost forgotten.

Thus, we cannot rely upon the fact that we have elections and have other forms of popular government, as any real safeguard for the preservation of our liberties. We have one hope and only one. That is in keeping alive and in full vigor of enforcement the limitations which the Constitution imposes upon the power of the Government and all its departments. We must realize that the inevitable tendency of Government, no matter who may be in control of it, is to be intolerant of restraints upon its power and to endeavor to whittle away or evade those restraints. As above noted, two of the most potent means of accomplishing this are Bureaucracy and Taxation, particularly graduated or other discriminatory taxation. Either, if unchecked, can destroy Constitutional Liberty. Of late there has been a strong tendency to give to political officials and political bodies having no judicial responsibility, the power to determine most important questions affecting the liberty of the citizen and even to make findings of fact binding on the courts. This alone, if permitted, might well mean the end of Constitutional Liberty. It is a striking example of how little the average citizen understands the complicated forces which govern our complex civilization, that this movement has grown almost unnoticed by the public. Fortunately it seems likely that it has been or will be checked by the courts. The opinion of the court delivered by Mr. Chief Justice Hughes in St. Joseph Stockyards Co. v. U. S., 298 U. S. 38, 80 L. Ed. 1033, 56 S. Ct. 720, is, in the Author's opinion, one of the most significant and important opinions on behalf of Constitutional Liberty in this generation. It should serve to settle permanently the principal that the constitutional rights and liberties of the citizen cannot be made to depend upon findings of fact made, or other action taken by legislative, administrative, or other non-judicial bodies. It was held that when the Legislature acts within its proper sphere of legislative action, either by itself or by an agent, it may make conclusive findings, provided the requirements of due process of law are met. But it was further held that when there is presented a question whether the constitutional rights or liberties of the citizen have been infringed, the courts have the right and the duty to consider the facts independently, and determine for themselves whether such rights have been infringed. Among other things the court said (page 685):

> "The legislature cannot preclude that scrutiny or determination by any declaration or legislative finding. Legislative declaration or finding is necessarily subject to independent judicial review upon the facts and the law by courts of competent jurisdiction to the end that the *Constitution* as the supreme law of the land *may be maintained.* Nor can the legislature escape the constitutional limitation by authorizing its agent to make findings that the agent has kept within that limitation. Legislative agencies, with vary-

ing qualifications, work in a field peculiarly exposed to political demands. Some may be expert and impartial, others subservient. It is not difficult for them to observe the requirements of law in giving a hearing and receiving evidence. But to say that their findings of fact may be made conclusive where constitutional rights of liberty and property are involved, although the evidence clearly establishes that the findings are wrong and constitutional rights have been invaded, *is to place those rights at the mercy of administrative officials* and seriously to impair the security inherent in our judicial safeguards. That prospect, with our multiplication of administrative agencies, is not one to be lightly regarded. It is said that we can retain judicial authority to examine the weight of evidence when the question concerns the right of personal liberty. But if this be so, it is not because we are privileged to perform our judicial duty in that case and for reasons of convenience to disregard it in others. The principle applies when rights either of person or of property are protected by constitutional restrictions. Under our system there is no warrant for the view that the judicial power of a competent court can be circumscribed by any legislative arrangement designed to give effect to administrative action going beyond the limits of constitutional authority.''

Thus has the Supreme Court of the United States magnificently performed (even if largely unappreciated) its right and duty of preserving from one most dangerous form of attack the constitutional rights and liberties of the citizen. It is earnestly to be hoped that the courts will similarly defend those rights and liberties from the equally dangerous and destructive attacks now being made and likely to be increasingly made in the future, in the field of taxation, particularly discriminatory taxation. By this statement there is not intended the slightest suggestion of lack of courage on the part of the courts. What it is intended to suggest is how vitally important it is that the courts, as well as the public, be made to realize the fact that present tendencies and policies in the field of taxation, particularly in graduated and other discriminatory taxation, will, if permitted by the courts to be carried to their logical conclusion, inevitably destroy Constitutional Liberty—probably our entire constitutional system. If this can be made clear to the courts, one may rest confident that they will do their duty. But so complex is our economic and social system that it is often difficult to understand and appreciate the inevitable practical effects of particular taxation policies. If justification be needed for a work like the present one, it is hoped it will be found in the fact that the Author has endeavored to analyze fundamental principles and show their application to some of the practical problems of today. It is believed it is no exaggeration to state that unless the courts understand and realize the inevitable effect of present legislative tendencies in the field of taxation, and unless they fearlessly strike down taxing statutes which infringe constitutional limitations and constitutional rights, then our entire system is in grave danger of destruction.

Can our system, which consists on the one hand of constitutional limitations upon the power of the Government, and on the other of correlative rights and liberties of the citizen, long survive? We may hope but we cannot know. Already it is showing the tremendous strain and stress to which it is subjected. The old days of a simple life and a simple social, economic, and financial system are gone, probably never to return. Will a people like ours, great in number, non-homogeneous, spread over a vast territory, with diverse and frequently conflicting economic interests, long submit to those self-imposed restraints which must be preserved and maintained if our constitutional system is to survive? This is the long-range view. The short-range and more immediate question is this: Will the courts, even in the face of popular clamor, firmly resist legislative encroachments upon the limitations imposed by the Constitution upon the powers of the Government particularly when such encroachments are stealthy and are proclaimed under the guise of promoting the General Welfare and advancing Social Justice? This they must do if Constitutional Liberty is to survive. Most immediate and most pressing of all, will the courts stand firm in striking down *taxing* statutes which infringe constitutional rights? Will they do this, even in the face of the claim that the Government needs the money which such statutes will raise? This is the real crux of the question. If the courts permit those in control of the legislative and executive branches of the Government to tax without due regard to constitutional limitations, particularly to impose discriminatory taxes, Constitutional Liberty is dead. Whatever forms may survive, the Government will be, in fact, Absolute. Here lies our greatest and most immediate danger. The tide today is setting toward that shore. The only hope lies in revitalizing the oath, solemnly taken by every judge of every court, to maintain and defend the Constitution of the United States.

RESPONSE TO THE ANALYSIS OF THE I.W.A. EMPLOYMENT AND PRODUCTIVITY STUDIES BY THE U.S. COALITION FOR FAIR LUMBER IMPORTS, BEFORE THE U.S. SENATE FINANCE COMMITTEE, SEPTEMBER 19, 1985

1. Calculation of U.S. softwood sawmill productivity by the U.S. Coalition

The U.S. Coalition has stated that the average U.S. sawmill employee produced 378 board feet of lumber in 1984. That number was derived from a survey by Economic Consulting Services, Inc. in May of 1985, which apparently was conducted after they had seen a first draft of our studies. There are two serious problems with their results. First, the majority of establishments surveyed were large-and medium-sized sawmills which are affiliated with the U.S. Coalition. **Because there are in excess of 1,200 sawmills in the United States, including over 500 in the U.S. South, it literally would have been impossible in just a few weeks to expand the survey beyond the larger establishments.** It takes the U.S. Census Bureau a year to conduct a sample survey of production only for 25% of the sawmills in the United States. Because of the fragmented nature of the sawmilling industry, even that survey has encountered serious errors. So far, the corrections to the softwood lumber production numbers for the U.S. South for 1982 and 1983 amount to a whopping 6.4 billion board feet. And there is compelling evidence that there are still substantial volumes of unreported lumber production in that region. (I.W.A. productivity study, Appendix C.)

Because the U.S. Coalition survey is biased toward larger establishments, it excludes the sawmills which have the lowest lumber recovery and productivity. Small units suffer from poor economies of scale and other problems. Roughly four-fifths of all softwood sawmills in the U.S. South produce less than 25 million board feet of lumber a year, versus one-fifth in British Columbia and three-fifths in the U.S. West region.

The I.W.A. conducted a separate survey of the most efficient mills in the U.S. South and the B.C. Interior (I.W.A. productivity study, Tables 1 to 8, figures 1 and 2, and pages 1-29.) Even in those operations, however, employee output was substantially higher in the B.C. Interior. In the more efficient southern mills, average output for all employees was approximately 440,000 board feet in 1984, compared to 740,000 board feet in some B.C. Interior mills. On a per hour worked basis, the gap widens considerably because employees in the U.S. South work more hours per year than is the case in British Columbia. During 1984, hourly output in B.C. Interior mills was between 40% and 80% greater than in the U.S. Southern Pine region.

The second problem with the U.S. Coalition productivity survey is that it mixes the types of employees against which output is measured. Most companies base productivity calculations in their operating statements on production and related employees only, or at most, all employees working at the sawmill. However, the I.W.A. productivity study measures output against all employees in the sawmilling business, including head office staff, company officers, clerical employees and all others--even though they may not be physically located at the sawmill. **It should be clear that dividing lumber production by all employees gives a lower answer than if production and related employees are used as the denominator. Either series can be used consistently, but the all-employees series provides a more accurate comparison between Canada and the United States. Productivity advances in Canadian mills have caused the ratio of production employees to all employees to decline in British Columbia and Canada. That in turn has substantially increased the differential between output per production employee between the Canadian and U.S. industries. When the U.S. Coalition compares output against production employees in the United States and against all employees in Canada, it is clearly mixing apples and oranges.**

For your interest, output per employee for production employees only for 1984 is shown as Table 9B (attached). This table can be compared with Table 9 in our productivity study, which measures output against all employees. Table 9B shows that the average production employee in the B.C. Northern Interior produced 795,000 board feet per year, compared to 239,000 BF in the U.S. South. For Canada and the United States as a whole, the numbers are 468,000 and 269,000 board feet respectively. The gaps have widened from the all-employees series.

It is important to emphasize that either the all-employees or production employees series can be used. But it is highly inaccurate to mix the two series when comparing regions or countries.

The results from the I.W.A. study have been cross-checked with a number of sources, including individual mill data which we have not published. In addition, we conducted a separate survey of the U.S. South using mill capacity and employment data from the Miller Freeman, Directory of the Forest Products Industries (I.W.A. productivity study, pages 109-114). **The results from that survey confirm within a few board feet the averages calculated using U.S. government data.**

Other data confirming the I.W.A. study results are available for inspection.

In summary, the U.S. Coalition survey of U.S. sawmill productivity is in error because it omits the large number of small mills which have high chip and low lumber recovery, and consequently, low lumber productivity and high unit production costs. That error has been compounded by the comparison of output per production employee in the United States versus output per all-employee in Canada.

2. U.S. Bureau of Labor Statistics studies of productivity in the sawmilling industry

Footnote 23 of the U.S. Coalition statement reads: "Bureau of Labor Statistics data also show U.S. productivity above 330 MBF (per employee per year)." (p. 21). Frankly, the source of this quote baffles us. B.L.S. does not conduct studies which measure the absolute levels of output per employee or per hour worked. Instead, the Bureau measures trends in these series over time by deflating current dollar values of lumber shipments with price deflators from the Producer Price Index series. In order to calculate output per employee or per hour worked, B.L.S. would be faced with acquiring data similar to that shown in the I.W.A. productivity study.

To the knowledge of B.L.S. employees contacted, the agency has not done such a study. It is true that the U.S. Coalition footnote is carefully worded, ie., B.L.S. "data also show . . . ." The Coalition may somehow be convinced that some unspecified data show U.S. output at 330 thousand board feet per employee. But that is a far cry from saying that the B.L.S. itself made such a statement.

3. Alleged errors in I.W.A. productivity study

Footnote 24 includes an incredible compilation of inaccurate statements regarding the I.W.A. productivity study. The U.S. Coalition's allegations reflect a complete lack of understanding of data sources and their limitations.

(a) Employment in the U.S. softwood sawmilling industry

In the first paragraph of footnote 24, the I.W.A. is accused of substantially underestimating the productivity of U.S. sawmills by including in S.I.C. 2421 employees that are engaged in remanufacturing operations. The first problem with this statement is that it is based on an erroneous understanding of the S.I.C. codes under S.I.C. 242. There is an enormous difference between remanufacturing a piece of rough lumber into higher value lumber products such as clear grades, and further manufacturing of lumber into crafted products. The following list includes a few examples of the latter group, including those cited by the U.S. Coalition as being in S.I.C. 2421.

End product	Four-digit S.I.C. code
- shakes and shingles	2429, special product sawmills, n.e.c.
- trusses	2452, prefabricated wood buildings
- moldings, door trim, doors, door sills, baseboards, window frames and sash, almost ad infinitum	2431, millwork

- wood handles, ladders, picture frame moldings, clothesline poles, scaffolds, etc. — 2499, wood products, n.e.c.

In 1982, there were 63,000 employees in the millwork group and 56,000 employees in the 2499 miscellaneous group. None of these were included in S.I.C. 2421, sawmills and planing mills, general. It seems incredible that the U.S. Coalition has attempted to remove the employees in those other four-digit S.I.C. codes from S.I.C. 2421, when in fact they were not included in the first place.

S.I.C. 2421 itself consists of six five-digit S.I.C. groups. As the U.S. Coalition acknowledges, S.I.C. 24211, hardwood lumber employment, has already been excluded from the I.W.A. calculations. Two other groups represent some remanufacturing of lumber--but not crafted products. They are S.I.C. 24218: softwood flooring, siding, and other mill products; and S.I.C. 24219: custom sawing receipts from contract or custom sawing, kiln drying and planing of lumber or logs owned by others. According to the 1982 Census of Manufactures, at most these two S.I.C. groups employ 3,500 individuals (all employees). (That subtraction is overstated because S.I.C. 24219 includes contract sawing of logs and hardwood lumber as well.) Their removal from S.I.C. 2421 would, at most, boost average productivity in the United States to 245,000 board feet per year--well below the 388,000 board foot average in Canada, and far below the 511,000 board feet produced by the average B.C. Interior employee in 1984. Moreover, Canadian and British Columbia softwood lumber employment data have been overstated by the inclusion of shake and shingle mill employees in Canadian S.I.C. 251 (which roughly corresponds to S.I.C. 2421 in the United States.)

There is absolutely no justification for the U.S. Coalition to reduce the estimate of softwood lumber employment (S.I.C. 2421) to 93,500 from the 137,000 total stated in the I.W.A. studies. The lower estimate represents nothing more than an attempt to bend official government data to fit the results of the U.S. Coalition's May, 1985 survey. If the Coalition believes that the classification of employees by four-digit S.I.C. group is in error, then the matter should be raised

with the Bureau of Labor Statistics. B.L.S. can then send out an inspector to check on any possible problems. However, private industry data do confirm The Bureau's employment statistics for the softwood lumber industry. The problem appears to be a lack of understanding on the part of the U.S. Coalition as to which four-digit S.I.C. codes contain specific end products.

In view of those errors, the U.S. Coalition's estimate of 93,500 softwood lumber employees is clearly wrong. The I.W.A. has confirmed its results with other sources. Moreover, the International Paper Company Fact Book (The Impact of Canadian Lumber Imports to the United States: Fact Book, 1985 p. 28) estimates productivity in the United States at 250,000 board feet per employee. That number is within the ballpark of the maximum level possible if the lumber remanufacturing codes are eliminated from the S.I.C. 2421 employment totals. However, the result obtained by the U.S. Coalition in its May, 1985 survey is completely inconsistent with the average cited in the Fact Book.

(b) Impact of high value lumber production on productivity

The U.S. Coalition also complains that the I.W.A. studies understate U.S. softwood lumber productivity by neglecting the impact of sawing higher value products (p. 22). Nothing could be further from the truth. The I.W.A. productivity study dealt with this problem in some detail. (See pages 5 to 9, 78-79.) There are, however, a number of additional comments which should be made.

First, some high value production is achieved by sawing more desired species into clears and other high-grade products. For instance, 64% of U.S. Pacific Coast softwood lumber output in 1984 consisted of Douglas-fir. Consumer preference for that species in the western United States has limited Canadian penetration of that market to about one-tenth of total consumption. Since less than 9% of the British Columbia harvest last year was Douglas-fir, it is difficult for all but a few Canadian producers to compete in that market.

However, the U.S. West Coast lumber industry somewhat resembles the B.C. Coast industry. Because of the high cost of logs on the B.C. Coast, sawmills place heavy emphasis on cutting high value lumber for offshore markets and the U.S. East Coast market. In the latter region, consumers are willing to pay a higher price for green hemlock and Douglas-fir. In some B.C. Interior mills, up to one-half of total production is destined for offshore markets.

Aside from species preferences, high value lumber is also produced by remanufacturing rough lumber into high-grade products. However, in order to properly measure productivity, the number of employees involved in that process must be included in the total number of employees required to manufacture the end product. Unfortunately, the U.S. Coalition wants it both ways. In footnote 24 they erroneously subtracted cut estimated employment in crafted end products—in spite of the fact that employees in other four-digit S.I.C. groups were not included in S.I.C. 2421 in the first place. Then, after making that calculation, the Coalition insisted that calculated U.S. productivity be increased by including the additional returns brought by high-grade lumber. To do so would give their calculations the best of both worlds. But they cannot have it both ways. Either the number of employees required to produce high value lumber must be included with the additional value of the end products manufactured, or both have to be excluded from the calculations.

Our examination of softwood lumber production in the U.S. South and the B.C. Interior shows that the basic product mix is similar in both regions. Roughly 85% of total output in each region consists of dimension lumber. We conservatively estimated that between 10% and 17% may be added to the value of southern yellow pine by treating the lumber and carrying out other operations. However, that adjustment would raise productivity in the U.S. South to approximately 228,000 board feet per employee in 1984. By the same token, some B.C. Interior mills also produce clear grades and other high value products.

It is completely untrue that the I.W.A. study neglected the impact of high value lumber on productivity. A careful reading of that study shows that the subject was fully discussed. But it is important to point out that productivity is just one important factor in determining the competitiveness of lumber producing regions. For instance, consumer preference for Douglas-fir lumber in the western U.S. market, and for green hem-fir and Douglas-fir in the U.S. Atlantic states market, has enabled some B.C. Coast and U.S. West Coast sawmills to survive. However, consumers in other regions appear to be more price-conscious than lumber buyers in the Northeast and the West. And growing tendencies toward price consciousness in the Northeast has caused a steady erosion of that market by southern yellow pine and eastern Canadian lumber. Southern producers have also been able to make significant inroads into the western U.S. markets traditionally held by sawmills located in that region. That is one reason why B.C. Coast and U.S. Douglas-fir region sawmills suffered more severe employment losses than other regions between 1978 and 1984. During that time period, 29% of B.C. Coast jobs were eliminated, compared to a 20% reduction on the U.S. West Coast.

(c) Alleged I.W.A. overestimate of
<u>Canadian softwood sawmill productivity</u>

The U.S. Coalition alleges that the I.W.A. estimate of Canadian softwood sawmill productivity is too high because they have trouble believing the average calculated for the B.C. Northern Interior. Apparently, the Coalition could not understand how output per employee in the North could be "more than twice the national average."

First of all, while productivity in the Northern Interior is impressive, it is just 1.7 times the national average (665,607 versus 388,475 board feet per year). Secondly, even a superficial check of Table 9 reveals that each region and the Canadian average were calculated separately. The estimate for the B.C. North had absolutely no impact on either the average for the entire B.C. Interior or Canada. To assume otherwise, is simply wishful thinking on the part of the U.S. Coalition. Therefore, the Canadian average does not drop to 329,000 board feet per employee from 388,000 as suggested.

The U.S. Coalition then asserts that because the phenomenal level of productivity in the B.C. Northern Interior is unexplained, the "guesses and estimates" for that region are in error. We are sorry to inform the Coalition that the calculations for the Northern Interior are correct. Large-scale capital investments have been made in the northern mills over the past 10 years. They are, indeed, highly efficient. Union mills account for 80% of the total in the region. However, one of the biggest Northern Interior shippers of lumber to the U.S. market is a nonunion company. One of its plants is the second largest in the area. It pays the same rates of hourly compensation as I.W.A. operations, and has an average productivity which is very close to the level in the North.

Anyone who disbelieves the productivity numbers for the B.C. Northern Interior should view the sawmills firsthand for themselves. American visitors who have done so do not appear to argue with what they have seen.

(4) Measurement of labor costs in the United States and Canada

Certainly one of the most incredible components of both the U.S. Coalition's submissions to the U.S. International Trade Commission and to the Senate Finance Committee is its comparison of labor costs in the United States and Canada. **Those statements show a complete lack of understanding of even the most rudimentary concepts of accounting.**

(a) Total compensation per hour worked versus unit labor costs

The U.S. Coalition completely confuses the definitions of hourly labor rates and production costs per thousand board feet of lumber produced. Any accountant knows that unit labor costs, ie. per thousand board feet, determine a company's or an industry's ability to compete. They are a function of hourly labor costs and productivity. (See the I.W.A. productivity study, pages 1 to 29, Tables 1 to 6, and especially figures 1 and 2.) It is high productivity which permits B.C. Interior sawmillers to come within as little as $2 per thousand board feet of unit labor costs in the most efficient mills in the U.S. South. **B.C. producers are able to do so, in spite of the fact that total compensation costs per hour worked are almost double the levels in the most efficient sawmills in the U.S. South.**

By the same token, the most efficient sawmills in the U.S. South pay the highest hourly rates--almost $10 an hour, but have the lowest unit labor costs--$36 per thousand board feet. The average for the entire southern pine region is in excess of $60 per thousand, even though hourly compensation rates are less than half of the levels in the B.C. Interior.

Because of its lack of understanding, the U.S. Coalition seems to believe that low hourly compensation provides the U.S. South with a comparative advantage. It does not. The comparative advantage arises from the impact of productivity on unit labor and all other unit costs. (See the I.W.A. productivity study, pages 1 to 29.) In spite of a severe disadvantage in hourly labor costs, high productivity permits unit costs in the B.C. Interior mills to be very competitive with costs incurred by the southern pine industry. Stumpage has nothing to do with manufacturing in put costs per thousand board feet.

(b) Average hourly earnings versus total compensation per hour worked

One of the most ignorant comments contained in the U.S. Coalition's statement is that "the I.W.A. estimates of wage rates are also grossly inaccurate." The reason given is that stated labor rates seem to exceed numbers published by Statistics Canada. It is unfortunate that the U.S. Coalition still does not understand the difference between total compensation per hour worked and "wage rates," in spite of the fact that these concepts were thoroughly explained in our submissions to the I.T.C. "Wage rates" in government publications are in fact just the payroll earnings portion of compensation, which provide the basis for assessing individual income and other payroll taxes. They include straight-time wage rates, overtime premium, vacation pay and other wage-related benefits. Because all of this income must be reported to the appropriate taxing agencies in each country, the data is easily available for reporting to the Bureau of Labor Statistics in the United States, and to Statistics Canada. **However, as the I.W.A. submissions to the I.T.C. point out in great detail, total hourly compensation also includes employer premiums for medical care, health and welfare and private pension plans, as well as contributions for legally required benefits such as Social Security and** unemployment compensation. The costs of all of these benefits are substantial in both the United States and Canada.

Unfortunately, because of problems in collecting the costs of supplementary benefits, neither B.L.S. nor Statistics Canada publishes total compensation costs per hour worked. Their publications are restricted to payroll earnings only. Since the mix of payroll earnings and supplemental benefits is quite different in each country, it is not accurate to limit the comparison of hourly labor costs to just payroll earnings.

Finally, the I.W.A. has extensive experience in costing collective agreements, including a large number of cases under both the U.S. Pay Board Controls program of the early 1970's and the Canadian Anti-Inflation Program of the late 1970's. Moreover, the lumber industry in British Columbia also has in-depth experience, and we are usually able to agree on the numbers, even though each party does its work independently. We can prove that the hourly compensation costs cited in the I.W.A. submissions are correct. Given the coverage limitations of Statistics Canada data, it is not accurate to use their publications to challenge those calculations.

It is clear that the comments by the U.S. Coalition on the I.W.A. productivity study contain serious factual errors. Since those errors have a substantial impact on the comparison of productivity in the softwood lumber industries of the United States and Canada, it is important to correct any false impressions which have been created.

TABLE 9B

SOFTWOOD LUMBER PRODUCTION, EMPLOYMENT AND PRODUCTION PER PRODUCTION* EMPLOYEE IN THE UNITED STATES AND CANADA, BY REGION, 1984

Region	Board feet per employee
B.C. Coast	408,970
U.S. Pacific	327,566
Oregon and Washington	347,328
B.C. Interior	610,108
B.C. Northern Interior	795,201
U.S. Mountain	260,162
Idaho and Montana	301,547
U.S. West	313,766
British Columbia	532,014
U.S. South	239,143
Eastern Canada	368,785
Total United States	268,915
Total Canada	467,479

Production employees only. Excludes non-production employees included in the all-employee group in Table 9.

TABLE 12A

OUTPUT PER HOUR WORKED IN THE SOFTWOOD SAWMILL INDUSTRY FOR SELECTED REGIONS OF THE UNITED STATES AND CANADA, 1984

(Board feet per hour worked: production and related employees only)

British Columbia	316.8
B.C. Northern Interior	424.1
B.C. Interior	328.7
Oregon and Washington	189.9
Idaho and Montana	148.8
U.S. South	118.7
United States	138.7