

## Trade — A British Columbia Perspective

In November 1999, Ministers from the 135 member nations of the World Trade Organization will gather in Seattle to set out the trade and investment agenda for a new “Millennium Round”. The new round will be negotiated over the next three years, with areas such as public health and education, agriculture and food policy, and investment likely to be on the table. Proponents intend to build on the sweeping changes in the scope and enforcement powers of glo-

the resulting economic slowdown in BC, have highlighted very well the pitfalls of a more interconnected global economy.

BC remains surprisingly dependent on traditional resource industries in its export mix, at a time when international competition in these areas is growing. The Asian market collapse exposed the province’s reliance on resource commodities and the need to add value and diversify economically. In this context, the coming WTO

negotiations pose significant challenges to the ability of policy makers to implement alternative economic development strategies and to provide essential public services.

### Hewers of Wood

Exports account for a quarter of BC’s GDP, amounting to \$26 billion in 1998. Since 1990, BC exports have grown by 56.5%. More trade, however, does not necessarily translate into higher standards of living. A closer look at the trade statistics reveals that BC is still overly dependent on the export of low value natural resources.

To be sure, higher value added activities make up a much greater share of total exports in 1998 than 1990.

**BC Exports by Commodity, 1990-98**

Commodity	Total exports, 1990	Total exports, 1998	Growth, 1990-98	Share of total exports, 1998
	(millions of dollars)		(percent)	
Wood Products	4,728	8,602	81.9	33.0
Pulp and Paper	4,620	4,859	5.2	18.6
Agriculture	498	1,106	122.1	4.2
Fish	765	806	5.4	3.1
Minerals	1,879	1,537	(16.2)	5.9
Energy	2,080	3,267	57.1	12.5
Machinery and Equipment	922	3,164	243.2	12.1
Plastics	55	288	423.6	1.1
Apparel and Accessories	44	217	393.2	0.8
Other	1,056	2,217	109.9	8.5
<b>Total</b>	<b>16,648</b>	<b>26,062</b>	<b>56.5</b>	<b>100.0</b>

Source: BC Stats, Exports (BC Origin), 1989-98

bal trade rules negotiated during the Uruguay Round, which ended in 1994.

For Canada, the 1990s have already been a decade of broad trade and investment liberalization. The benefits of free trade, however, have fallen short of the promises made by corporate and government cheerleaders. Indeed, incomes have declined in real terms over the 1990s for the typical Canadian family, and the income gap between rich and poor has grown.

British Columbians have good reason to be of two minds about trade. Trade is a driving force of BC’s economy, deeply rooted in the history of the province. Yet, the collapse of Asian markets, and

The three fastest growing export industries are machinery and equipment, plastics and apparel. Exports of machinery and equipment — including motor vehicles and parts, and electronics and communications equipment — now constitute 12.1% of total exports, more than double the 5.5% share in 1990. Over the same time period, the total value of machinery and equipment

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exports has more than tripled to over \$3 billion per year. The plastics industry has also seen huge export growth, particularly in manufactured forms. However, these three sectors remain small in relative magnitude.

Forestry is still the biggest industry in BC trade, accounting for more than half of the value of all BC exports. The wood products sector has shown the most export growth, up 82% since 1990, while the pulp and paper sector is up a modest 5%. In terms of employment, however, the impact is considerably less: BC's 91,000 workers in forestry and wood and paper manufacturing amount to less than 5% of total employment.

The export mix from forestry is still concentrated in low value products. Softwood lumber alone accounts for almost one-quarter of total exports, with another 10.6% from pulp exports. Exports of value added products such as doors, windows, furniture, siding and prefabricated houses have grown threefold over the 1990s, but still make up only 3.5% of total exports. BC's share of Canadian exports in value added wood products has declined, as export growth has occurred at a slower pace than it has in other provinces.

BC's other traditional resource areas have diminished in importance to the export mix. Mineral exports fell by 18.2% from 1990 to 1998, while fish exports in 1998 are only slightly above 1990 levels. Energy product exports have grown, but this has been largely due to growth in natural gas and electricity sales, rather than traditional coal exports.

In lumber, pulp, newsprint, minerals and coal, BC remains a major supplier to world markets. But intensified international competition, particularly from Indonesia, Chile, New Zealand, South Africa, Russia and Eastern Europe, is eroding this traditional edge. For example, exports from Russia and Eastern Europe have cut into BC exports to European market over the 1990s.

The result of this new competition is low, and volatile, commodity prices — a signal that BC needs to move in new directions to maintain standards of living.

### When Markets Collapse

As the build-up of capacity in world markets for resources increased supply, demand for these products was deeply undercut in the aftermath of panic in financial markets that started two years ago in Thailand, and spread through Asia, Russia and into Latin America. Because BC does far more trade with Asia than the other Canadian provinces (prior to the Asian meltdown, BC produced 42% of Canada's exports to Asia), BC also felt the impact.

Exports went to the US, the highest level since the 1960s. Exports to the US are up a further 23% in the first quarter of 1999 over the same period in 1998.

Moves to the US market would have been even greater if not for the *Softwood Lumber Agreement*, which put quotas on penalty-free exports to the US, based on patterns of trade prior to the Agreement (and before the Asian crisis). This restricted the ability of coastal mills that had been relying on the Asian market to shift sales to the US market. With a recovery in wood prices, however, forestry companies are now finding the US market profitable, in spite of penalties for exceeding the quota.

After several decades of diversification into Japan and other international markets, this raises the spectre that BC may be becoming too dependent on the US market — if the US economy takes a downturn, so will BC. In 1998, four-fifths of BC exports went to just two countries: the US and Japan. A further 9.3% went to the rest of Asia, and 7.9% to Europe. Overall, export destinations, as well as the export mix, could stand to be more diversified. This would provide a stronger degree of insulation from external shocks.

### BC and the Global Economy

BC needs to accelerate the move beyond its traditional comparative advantage to create a dynamic, diversified economy — in terms of what we produce and where we export to. However, there is a danger that the very tools BC needs to address these issues will be stripped away in the rush to a global economy.

Agreements under the WTO and NAFTA increasingly tie the hands of policy makers to achieve economic and social outcomes through tools such as government procurement and industrial development strategies. These agreements are also

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**Key Destinations for BC Exports, 1998**

Destination	Total Exports (millions)	Share (%)
United States	16,405	63.0
Japan	4,532	17.4
Pacific Rim (excluding Japan)	2,421	9.3
Europe	2,068	7.9
Latin America	322	1.2
Australia	226	0.9
Other	88	0.3
<b>Total</b>	<b>26,062</b>	<b>100.0</b>

Source: BC Stats, Exports (BC Origin), 1989-98

Exports to the Pacific Rim fell by 25% from 1996 to 1998.

The resulting economic downturn (the effects of which are still lingering) hit regions dependent on forestry exports the hardest. For regions like the Cariboo, the price has been reflected in high unemployment. The more economically diversified regions, like the Lower Mainland and the Capital region, on the other hand, were much more insulated from the effects of the crisis.

BC exporters have responded to collapsed markets in Asia by turning to the US. Total exports to the US jumped by 18% from 1996 to 1998. Last year, 63% of total BC

# After MacMillan Bloedel

## How will Merger-Mania affect British Columbia?

by David Peerla

On June 21st of this year, American forest giant Weyerhaeuser and MacMillan Bloedel formally announced their merger. The merger, if approved by shareholders and government regulators, will create the world's largest softwood lumber producer, with combined sales of \$13.3 billion and 40,000 workers in the US and Canada. The deal is part of a larger cross-border consolidation trend that has seen Finnish pulp and paper producer Enso merge with the Swedish firm Stora and, most recently, a bidding war between Louisiana Pacific and Boise Cascade for Montreal-based Forex.

On the surface, the MacMillan Bloedel merger is part of a much needed good news story for the BC forest industry, along with rising corporate profits and commodity prices. But the long-term outlook should give us pause for thought.

Two particular problems beset long-term recovery in the BC forest industry. First, global over-capacity in forest products will not be corrected in the short-term. The second problem is that BC forest companies, including MacMillan Bloedel, invested significantly less than their counterparts in Eastern Canada over the last four years.

The corporate turnaround strategy developed by MacMillan Bloedel CEO Tom Stephens was to cut employment, sell off divisions, abandon research and development and make MacMillan Bloedel appear attractive, in terms of stock price, in the short-run. He obviously succeeded. But the merger will do little or nothing to change MacMillan Bloedel's lack of investment in the 90s, aging small coastal mills, old growth dependent product mix, and "volume not value" corporate strategy.

Can the merger stem the tide of international competition? In a word, no.

In 1980, the high-cost forest producers in Canada were in Eastern Canada, specifically Northern Ontario. The latest Price Waterhouse comparisons show Eastern producers with a cost advantage in pulp, newsprint and lumber. What explains this dramatic turnaround? First, a difference in product mix: Eastern companies have moved up the value chain, making more newsprint and fine papers; BC companies sell more raw pulp and lumber than their Eastern Canadian counterparts. BC pulp now finds itself as a potential loser in a global game which saw the expansion of pulp capacity, particularly in Indonesia, fueled by financial capital seeking high paybacks. BC lumber is caught in the iron triangle of increasing American competition, a stagnant Japanese market and the *Softwood Lumber Agreement*, which keeps a lid on exports and squeezes profits.

Second, and most importantly, during the last commodity cycle in pulp, paper and lumber, BC firms, including MacMillan Bloedel, apparently found it easier and more profitable to seek relief from rising nominal wood and fibre costs through price increases rather than through cost-reducing capital investments. In contrast, BC's competitors in Eastern Canada, Scandinavia and the United States increased cost-cutting investment while adding little or no

capacity, thereby increasing labour productivity growth and directly lowering the growth of unit labour costs.

### Reversal of Fortune?

The BC forest industry appears to be in a profitability upswing. One reason for this is the new ability of BC companies to increase flexibility in the mill, close mills, fire thousands, and work their remaining workers harder. The MacMillan Bloedel merger, aside from being about shareholder value, is also about discipline, as the forest companies externalize environmental costs, shut plants, and cut costs in every way imaginable. So, BC profitability is recovering as labour is in retreat and environmental regulations are rolled back.

Even if there is a sustained reversal in prices for lumber, pulp and newsprint and BC regains markets at the expense of the US and Eastern Canada, the forest companies will still face severe international competition. The basic issue facing the BC industry is to manufacture products with added value. BC policy makers need to recognize, and act upon, this fact.

### The Future

Perhaps the single most disturbing feature of the current merger debate are proposals for reforming how public lands are licensed to the forest companies (so-called tenure reform). Why has the forest industry, and in particular MacMillan Bloedel, been pushing tenure reform, and why has it gone so far beyond its traditional concern with cost adjustments? Partly because the industry had already crossed the line in dealing with the *Forest Practices Code* and stumpage rollbacks, legitimizing an expanded agenda in that context. In its next great intervention, tenure reform, the industry has in mind a much wider jurisdiction, seeking to impose tenure reforms as comprehensive as those imposed on the *Forest Practices Code* and stumpage, even though such reforms are not necessary to restart the flow of investment.

The public hearings on the MacMillan Bloedel merger should provoke a fundamental debate about the character of the BC forest policy regime. The debate should focus on questions like: Will proposals to privatize public lands (what some call market-based tenure reform) increase the democratic control of the public forests? Do our relatively small and aging mills require the development of new forms of investment strategy?

We should keep at the forefront of discussion the absence of empirical evidence that mergers, reductions in stumpage and environmental deregulation are good for investment, and the abundance of historical evidence that most mergers do not work and are quietly dismantled later. The MacMillan Bloedel merger represents merely a rearrangement of existing assets — the trading of ownership shares on the stock exchange.

*David Peerla is the CCPA's Resource Researcher, and the author of a detailed study of BC's resource industries, to be released this Fall by the CCPA-BC.*

restricting our ability to regulate for environmental and health purposes, and to protect worker rights. NAFTA may even compel BC to develop a new export industry that most citizens strongly oppose — bulk water exports to the highest international bidder.

The coming Millennium Round threatens to go even further. The US wants to put all services on the table in the upcoming round (through the General Agreement on Trade in Services, or GATS). Included on the list are health care and education, which are seen by US-based companies as highly profitable growth areas, limited only by “barriers” in Europe and Canada — that is, publicly-provided systems. Other public areas, like sewage, water supply and Crown corporations are similarly in jeopardy.

Meanwhile, investment will also be on the WTO agenda. The

European Union is seeking to explicitly reignite talks at the WTO on the widely-opposed Multilateral Agreement on Investment. Alternatively, investment provisions will be discussed implicitly within the GATS negotiations — this is because allowing market access for a service necessitates allowing the movement of capital related to providing the service.

Rather than a Millennium Round, BC and Canada should push for an international agenda that recognizes that different economic models are appropriate in different countries and circumstances. Countries and regions need the flexibility to democratically set priorities for economic development and public services in ways that improve standards of living. Ultimately, this is an alternative agenda that puts trade in the service of people, not the other way around.

## Recent Indicators

### Are Corporate Head Offices leaving for Alberta?

	Number of Head Offices in Financial Post 500		
	1988	1998	Net Increase
BC	44	57	13
Alberta	53	66	13

Source: Vancouver Sun, March 27, 1999

### Employment and Earnings

	Unemployment rate (%)			Average weekly earnings (\$)	
	June 1998	May 1999	June 1999	May 1998	May 1999
BC	9.3	8.4	8.6	617.21	625.63
Canada	8.4	8.1	7.6	604.16	607.39

Note: Seasonally adjusted.

Source: BC Stats

### Unionization and Earnings in BC

	Unionized	Non-unionized
Percentage of all employees	35%	65%
Average hourly earnings	\$20.46	\$15.46

Source: BC Stats

### Low Incomes in BC

	Percent below LICO	
	1996	1997
All BC	17.9	18.2
Males	15.7	17.2
Females	20.0	19.0
Under 18	20.2	19.6
Over 65	18.5	19.8

Note: The LICO is the “low income cut-off line,” the income level where a household will, on average, spend a disproportionate share of its income on food, clothing and shelter relative to the average family.

Source: Statistics Canada

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**Editor:** Marc Lee; **Layout:** Shannon Daub

**CCPA-BC:** 815-207 West Hastings Street, Vancouver BC, V5B 1H6  
Tel: (604) 801-5121 Fax: (604) 801-5122  
www.policyalternatives.ca / Email: ccpabc@intouch.bc.ca

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