The United States-Canadian Automotive Products Trade Agreement signed by President Johnson and Prime Minister Pearson on 16 January 1965 represents a solution to a number of serious problems which were faced by the automotive industries of the United States and Canada. These problems arose from very special characteristics, unique to the automotive industry of North America. The solution arrived at is at the same time constructive and beneficial to the partner countries, but not harmful to the trade interests of third countries.

I.

The automotive industry of the United States and Canada naturally forms, and in reality is, a single great North American industry. Virtually all of the producing firms in the one country have a corporate relationship to firms in the other country. This is true both of vehicle manufacturers and of major parts producers. The dominant financial interest in those firms is American.

The manufacturing facilities on both sides of the border produce identical items, using fully interchangeable components. The location of the industry in the two countries is, moreover, characterized by geographic proximity. The bulk of production is concentrated in Michigan, Ohio, Indiana, Western Pennsylvania, Western New York and Southern Ontario. This region forms a natural area for single industry location, enjoying a somewhat common environment in respect of raw materials, power, labour force and transportation facilities.

Consumer tastes and preferences in the two countries are virtually identical. In both countries, the consumer demands a wide variety of body styles and sizes, a wide range of accessories and frequent model changes. To meet this consumer demand, the industry in Canada produces almost the full range of the thirty separate lines of passenger cars with nearly 350 models which are produced in the United States.
The North American automotive industry is one in which costs are critically related to the volume of production. Given the frequency of model changes, the tooling and design expenses for many components must be spread over a very large number of units if the final cost is to be within tolerable limits. For many basic components, the lowest efficient production run is 100,000 units per year. In some cases, the minimum level of production is in excess of 500,000 units per year. The United States market, of course, has been large enough to take advantage of this situation and to maximize the economies of scale. This has not been true in Canada where production runs have been short and costs relatively high, even though the industry there on the whole operates in modern and otherwise efficient plants.

Out of these circumstances arose a series of disturbing problems which threatened the stability of the industry on both sides of the border. Higher cost conditions in the northern segment of the industry resulted in higher-priced products to the Canadian consumer thus limiting the size of the market.

It had for some time been apparent to officials of the United States and Canadian Governments that at the root of these problems was a basic important factor - that a single great industry was divided arbitrarily and uneconomically by tariffs and other barriers to trade. If these barriers could be removed in a way which was mutually satisfactory to the two Governments, the industry could integrate its production operations on the most efficient basis, avoiding the necessity for maintaining uneconomic duplicative facilities.

This is in short the background and economic rationale of the Agreement concluded between our two Governments.

II.

Under the Agreement of 16 January the two Governments seek the achievement at the earliest practicable date of a broader market for automotive products within which the full benefits of specialization and large-scale production can be achieved. They seek also the liberalization of automotive trade in respect of tariff barriers and other factors tending to impede it, so that the industry of both countries may participate on a fair and equitable basis in the expanding total market in North America. In pursuit of these goals, the two Governments have agreed to develop conditions in which market forces may operate effectively to attain the most economic pattern of investment, production and trade and to avoid actions which would frustrate achievement of these objectives.

The terms of the Agreement provide that Canada shall accord duty-free treatment for vehicles and for original parts imported by bona fide Canadian vehicle manufacturers. For its part, the United States Government has undertaken to seek from the Congress authority to provide duty-free importation into the United States of vehicles and original parts manufactured in Canada.
The Agreement provides for consultations at the request of either Government; and a comprehensive review will be made of progress toward the objectives of the Agreement no later than 1 January 1968.

Finally, the two parties may, by agreement, extend the access to their markets provided for under the Agreement to other countries on similar terms.

I will not attempt now to summarize the Annexes to the Agreement which have already been circulated to the contracting parties. The Annexes are technical and somewhat complex but I am prepared, as I assume is the Canadian representative, to provide any necessary clarification.

III.

In concluding the Agreement of 16 January, my Government has been mindful of the principles of the General Agreement and of the trade interests of other countries. Various alternative approaches were considered and the approach finally adopted, in the view of my Government, represents a solution that will do no harm to the trade interests of third countries.

I have already described the economic rationale of the Agreement. The Agreement is intended to facilitate the integration of the North American industry and to permit efficient production on the basis of specialization. This will result in an increased level of trade across the border. But, in our view the purposes of this Agreement are different from those historically associated with preferential arrangements. This Agreement is not intended to have nor will it have, trade diversion effects.

I would like to explain specifically why we believe the Agreement will not harm third country trade interests. In the first place, the Agreement will not affect United States imports of automotive parts from third countries. The Agreement provides duty-free treatment only for original parts. United States vehicle producers do not to any significant extent import original parts from off-shore sources. This is not surprising, since the requirements of assembly line production demand rather precise scheduling of deliveries. In 1964, the United States imported $95 million worth of automotive parts of which $44 million originated in Canada. United States imports of parts from third countries consisted primarily of replacement parts for vehicles imported from those countries. There may be some minor exceptions to this general rule, but where they exist they will be based on some special cost advantage, notwithstanding the existing 8½ per cent United States duty on automotive parts. The Agreement of January will not significantly affect whatever cost advantage may exist in these cases.

Similarly, no trade diversion should be anticipated as regards vehicles. The United States is currently the world's largest importer of vehicles. We have the lowest duties and do not maintain non-tariff barriers on vehicle imports. In 1964 we imported 534,000 motor vehicles valued at more than $575 million. In
recent years our imports of vehicles have risen as our total market has increased, but the market share in the past three years - that is, the market share of imports - has remained at about 5 per cent.

Imported vehicles have a special niche in the United States market. These vehicles attract segments of consumer demand based on size of vehicle, economy of operation, desire for special types e.g., sports cars, or on the prestige attached to owning a foreign made automobile. These factors will be unaffected by the United States/Canadian Agreement.

More important is the question of price. What may be anticipated from the Agreement is a growing exchange of vehicles between the two countries based on production of fewer models in Canada with longer production runs. The elimination of the duty on vehicles imported from Canada, however, will have no effect on the prices of any vehicles in the United States. Thus, the price relationship with vehicles imported from third countries will remain unchanged. There is, therefore, no basis for anticipating any effect on imports on vehicles from third countries.

Similar arguments can, I believe, be made for the Canadian market but this is something I would leave to the representative of Canada.

IV.

My Government recognizes that the Agreement with Canada, when implemented by United States legislation, expected to be submitted to the Congress shortly, will give rise to a technical inconsistency with Article I of the GATT. We firmly believe however that this inconsistency is more with the letter of the General Agreement than with its spirit.

We are happy that the CONTRACTING PARTIES decided to establish this Working Party in order to enable us to explain in greater detail the unique circumstances that have led my country and Canada to choose this, among alternative courses, as the best means of improving the efficiency and structure of the North American automobile industry. We shall be very much interested in the reactions of the Working Party and will give careful consideration to its views.