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gains enhanced access to a large, high-income market. As the example of the Auto Pact makes clear, one of the most visible benefits of freer trade is to allow industries, particularly in the manufacturing sector, to rationalize their operations and specialize in their most efficient product lines. The result is an increase in productivity, production, employment and real wages.

### **The Economic Effects of Trade Liberalization**

The potential impacts of freer trade are pervasive in a modern industrial economy. As barriers or threats of barriers to import- and export-oriented activity are reduced, the positive impacts on the economy work through several channels:

*Comparative Advantage Specialization:* Trade barriers distort production decisions. Trade liberalization, in contrast, ensures that countries specialize in producing goods in which they have a comparative advantage. They are encouraged to produce and export goods that are relatively less costly to produce domestically, and to import those that are relatively expensive to produce at home. Thus, each country acquires goods less expensively than it would otherwise. Realizing one's comparative advantage in this way makes the best use of existing resources and results in higher overall productivity and an improved standard of living.

*Lower Prices for Consumers:* Trade barriers distort prices and hence consumption decisions. Trade liberalization means lower prices for both imported goods and the domestically produced goods that compete with them. Trade liberalization also

means lower costs for imported intermediate products which in turn will lead to further reductions in consumer prices.

*Third Country Effects:* The elimination of trade barriers between Canada and the United States will ensure that goods produced in one country are cheaper in the other country's market. Canada's domestic producers will have a competitive advantage in the U.S. market compared to suppliers from other countries, and vice versa. Americans will buy more Canadian goods and Canadians will buy more American goods, helping both Canadian and U.S. industries. Our overseas trading partners will gain, however, from Canada-U.S. free trade, since the resulting higher real incomes in Canada and the United States will also lead to higher imports from these countries. Third countries will also benefit to the extent that the Agreement acts as a model for, and increases the likelihood of, multilateral trade liberalization.

*Economies of Scale:* Both foreign and domestic trade barriers impose costs. This is particularly the case for smaller economies. They prevent domestic firms from becoming large enough to capitalize on economies of scale available in markets of larger size. The removal of the trade barriers permits domestic firms to operate larger and more specialized plants, which lead to lower unit costs of production. The capacity to specialize and to exploit the economies of large-scale