

neither did the increased reliance on the U.S. as an export market increase income volatility nor would it be possible to reduce current levels of volatility through increased geographic diversification of export markets. Furthermore, they suggest that history has shown that policies designed to diversify trade simply do not work and by interfering with market system can result in lower incomes for Canadians without significantly impacting on income stability.

Kunimoto and Sawchuk examine the issue of rules of origin and the potential benefits of less restrictive rules of origin within NAFTA. They illustrate that NAFTA rules of origin are the most restrictive of any major free trade agreement and therefore there may be not insignificant gains to be had from reducing their restrictiveness. Rules of origin are necessary to the operation of any preferential trade agreement as they allow the benefits of the agreement to accrue to its members and allow signators the ability to maintain different tariffs to non-members (as opposed to a common external tariff and a defacto customs union). The cost of maintaining rules of origin can therefore be interpreted as an upper bounds to the gains from their elimination as they can not be eliminated completely. The authors place the costs of the status quo at about 1% of GDP. They also report a declining use of NAFTA which peaked in 1998, but have since fallen to 50% of Canada-US bilateral trade. This, the authors conclude, is largely as a result of the shrinking gap between MFN and NAFTA rates.

Papadaki et al examine the economic impact of two policy shocks using a CGE model. The first scenario involves the creation of a Canada-US customs union with a common external tariff for both countries set to either US MFN rates or the minimum rate of either Canada or the U.S. which the authors refer to as scenarios 1a and 1b respectively. In each of the two scenarios, the authors find a minimal impact for either country at an aggregate level. At a more detailed level, the impact for some sectors that had been protected by high tariffs is more significant, such as; the Agricultural and Forestry, Food Beverage and Tobacco, Textiles, and Clothing industries.

The second scenario explored involves the elimination of all "unobserved trade costs". The authors make no distinction between the possible sources for these costs and interpret their results as the upper bounds for the potential gains from complete Canada-US economic integration. As would be anticipated, the expected gains from this experiment are quite significant, producing a welfare improvement in the range of 6-7% of GDP as well as a substantial increase in two-way trade flows.

Papadaki et al, also provide a useful comparison of computable general equilibrium (CGE) ex ante predictions for the Canada-U.S. FTA and the NAFTA based on a variety of assumptions. Early models, based on the assumption of constant returns to scale and perfect competition, showed modest gains for Canada. Later models, however, relaxing these assumptions and expanding the models to include such things as capital mobility, showed much larger gains. Comparing these predictions to the ex post results summarized by Harris, one might conclude that the early CGE models provided the lower bound to the impacts while later models provided an upper bound. Furthermore, while all of the CGE models consistently underestimated the impacts of the two agreements on