

to a drop in XK. The effect of a United States tariff reduction depends on the reactions of Canadian exporters. They could leave XP fixed and reap the windfall profits or they could lower XP by the amount of the tariff and increase XK. In actuality, they are more likely to lower XP by an amount less than the tariff and take some of the gains in increased XK.

4. In the fourth case, the exports of a commodity are largely institutionally determined. Natural gas is a case in point. This does not mean that prices are not relevant. Rather, in such cases, the impact of prices and tariffs can not be realistically described by a simple linear equation. In cases such as this, judgment, based on a knowledge of the political economy surrounding the commodity, must be used when assessing the future of exports.

In the case of imports, the size of the Canadian market and the price of Canadian goods relative to that of the imported goods are relevant factors. The proxies for the size of the Canadian market depend on the good. If it is a consumer good, then Canadian personal income is generally used; however, in the case of an input to production, the real output of the using industry is applied. These equations take the form:

$$MK = f(b_1 \cdot act, b_2 \cdot MP^*(1+tr)/CP)$$

where

- MK=constant dollar imports
- act=activity variable
- MP=price of imports in Canada
- CP=price of goods produced by Canadians
- tr=Canadian tariff rate
- b₁, b₂=econometrically determined coefficients;
- b₁ is positive and b₂, negative

