presentation, it should be recognized that the subject is both extensive and complex, so that it represents little more than an outline of the issue; it can be elaborated upon in response to the government's priorities for bilateral trade negotiations when they are established.

PART I

Estimates of Consumer Benefits

A. Summary of Results

Studies covering the potential quantitative benefits to consumers of free trade between Canada and the United States suggest gains ranging from very small numbers up to 9% of Canadian GNP.* However, the differences in their predictions can be traced to differences in key assumptions built into the analytical models used in the studies. The key assumptions are those related to the likely effects of free trade, firstly on the pricing of Canadian produced goods and services and, secondly on the costs and productivity of Canadian producers.

On pricing, much depends on the extent to which lower import prices (after removal of tariffs) would force domestic (Canadian) producers to reduce the prices of their output. Assumptions on pricing range from one extreme to the other. Neoclassical general equilibrium models (Boadway & Treddenick) assume no direct impact of import prices on competing domestic output, of which the prices are assumed to be determined solely by domestic costs. At the other extreme is the partial equilibrium 'law-of-one-price' model, which has import and domestic prices moving exactly in step, so that cost factors have no role to play.

Harris and Cox, and Hazledine, assume 'mixed' pricing -- in their models both competing imports and domestic costs influence domestic producers' prices.

On the cost side, the results depend on whether the initial cut in prices when tariffs are eliminated forces domestic industries to improve their productivity in order to remain competitive. Neoclassical models assume essentially no productivity effect, and law-of-one-price models have only the marginal efficiency gains from cutting

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* For a listing of the authors surveyed see the reference section of the appended paper by T. Hazledine, September 1985.