Gains from Trade to Canada

The discussion thus far has addressed the broad benefits that trade brings to an economy, covering the key economic concepts, models, and theories. Clearly, many aspects of trade are intertwined. For example, liberalized trade brings about increased competition in domestic and foreign markets, increases product variety and puts downward pressure on prices. It also induces firms to specialize and produce more, but in fewer product lines, and use their particular talents, resources, and factor endowments most efficiently to their benefit. These effects, in turn, lead to supplementary benefits such as greater productivity, higher wages, and increasing prosperity. The following sections address some of these supplemental benefits of trade in the Canadian context.

Trade and specialization in Canada

Trade in international markets is driven by the search for goods and services produced elsewhere at a relatively lower price than the opportunity cost to produce them at home. In exchange for the comparatively low priced international goods, Canada supplies goods in which it specializes. The outcome is an international division of labour that produces economic welfare gains from increased specialization. Canada stands to increase growth, firms to increase output, workers to receive higher wages, and consumers to access higher quality products at reduced prices.

Canadians have the opportunity to gain from specialization in two forms: a one-time shift in resources from less to more efficient sectors or firms, and in an ongoing form as workers, firms, and the nation as a whole focus their efforts on what they do best—and become increasingly better at doing it. One-time shifts can be understood as welfare-enhancing structural changes. Here gains derive from the movement of resources from a less to a more efficient sector. However, moving forward, while a country may specialize by moving its factors of production into more efficient sectors, it is natural that, with practice, their ability to produce the goods in which they specialize would improve with time. This type of adaptation, or learning by doing, is suggestive of the second form of specialization—ongoing or dynamic specialization. Gains in this case come from increased productivity (output per hour) through a "learning by doing" process in the same sector.

While most easily understood at the industry level (for example, the auto industry), specialization can occur at finer levels as well, such as at the firm level or plant level. Nonetheless its impact can be felt throughout the economy. Research has identified the link between specialization and trade liberalization at the plant level in Canada. Baldwin et al. (2001) found a strong relation between the export intensity of plants in manufacturing industries and their specialization following a period of increased trade liberalization in the late 1980s and implementation of the CUSFTA. The average nominal tariff (customs duties paid divided by imports) decreased from 6.5 percent in 1973 (as part of the Kennedy Round) to 1.1 percent in 1996, over which time the export intensity increased, for example, from 31 percent in 1990 to 47 percent in 1997. Likewise, commodity specialization at the plant level increased sharply with the implementation of the CUSFTA. About 30 percent of Canadian manufacturing firms that operated continuously from the early