Subject: Life before the Auto Pac/US-Canada Free Trade Agreement/NAFTA/CUMCA Agreement

Although the legality of President Trumps tariffs are working their way through the U.S. Supreme Court, it is likely that in someway shape or form there will be tariffs on Canadian goods including autos.

So lets take a look at what occurred before we had various free trade agreements – what did the Canadian manufacturing and tariff policy look like then?

The first large scale production of autos in Canada started in 1904 in Walkerville (now part of Windsor), Ontario and produced the Ford Model C car.[1] Although there were many attempts to build a domestic Canadian car manufacturer, Canada lacked the population, financial capacity and technological capacity to sustain a domestic industry.[2] Canadian car production mainly consisted of branch plants of American automotive companies making vehicles for the Canadian market. The cars produced in Canada were manufactured behind a tariff wall – vehicles that were produced in Canada did not pay the tariff while any vehicle imported did have the tariff.

This is very similar to what President Donald Trump is prosing for the United States – if you produce goods in America, there is not a tariff. If you import the good, the tariff applies. So what did the manufacturing landscape look like, in Canada, when we had our auto industry protected behind tariffs?

The tariffs on cars and car parts raised the domestic prices of cars to 29 to 54% higher than what the same car was sold for in the United States.[3] However, there was great increase in the investment in Canadian plants to assemble vehicles and product auto plants (the total capital invested in the Canadian automotive industry doubled in the 1920 from $40 million to $98 million in the decade).[4] So the Canadian market did have substantial production (and part of this production was exported to the United Kingdom and other Commonwealth nations), but it would be characterized as high cost and inefficient with many auto companies producing a “Canadian” version of a vehicle copied from a US design.[5]

Various federal governments tried a variety of policies to change this to 1) lower prices of car in Canada and 2) keep and increase Canadian production of vehicles. Multiple governments allowed tariff free entry of vehicles into Canada, if that vehicle manufacture used a certain percentage of Canadian produced parts in the vehicles made in Canada. Ultimately, in the 1960, a plan was developed where the percentage of Canadian made parts in each Canadian made vehicle could drop below 60% yet as long as the manufacture made enough other parts that their total Canadian value added reached 60 percent of their total output in Canada, a vehicle could be imported from the United States at a dramatically reduced tariff rate. This change led to a dramatic increase in the amount of auto parts that were manufactured in Canada and exported to the United States and lead to economies of scale.

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[1] History - CVMA
[2] Automotive Industry | The Canadian Encyclopedia
[3] https://publications.gc.ca/collections/collection_2018/mstc-cstm/NM33-1-15-eng.pdf
[4] https://publications.gc.ca/collections/collection_2018/mstc-cstm/NM33-1-15-eng.pdf
[5] https://publications.gc.ca/collections/collection_2018/mstc-cstm/NM33-1-15-eng.pdf

In time, U.S auto parts makers did not like this arrangement. Many parts suppliers demanded that this was an unfair trade practice and demanded the U.S government impose a countervailing duty on incoming Canadian parts. As a compromised (and to avoid an international incident the two federal governments put together a new set of terms for automotive trade – this agreement, formally known as the Automotive Products Trade Agreement (better known as the Auto Pact) was signed in January 1965 and led to an entirely new trading environment.

This agreement provided for completely duty-free passage of automotive vehicles and parts between Canada and the Untied States, with the largest provision from the Canadian perspective that products entering the US from Canada had to be at least 50 percent North American content. This was to prohibit other countries from exporting to the Untied States through Canada. Products entering Canada from the United States faced must more complex requirements. First, a Canadian automotive manufacture could import vehicles according to the terms of the agreement – to enjoy duty free provisions, a manufacture had to maintain its Canadian production at the level it had been the year before the agreement was signed (1964). Further, the Canadian government made separate agreements with the auto manufacturers where the Canadian subsidiaries of the US companies to carry out at least 60 percent of their future Canadian growth in Canada.

This agreement clearly favoured Canda. There could be a variety of reasons for this – possibly the US government throught they this be temporary and the agreement would be updated. Further, the US government may have wished to gain the Canadian government support for their policy on Cyprus (Greek and Turkish Cypriots clashed in Cyprus in 1964 and required the intervention of the United Nations)[6]. However, because of this agreement, the Canadian auto industry sored - everything in the Canadian industry rose in the 1960's – employment numbers, value of vehicle assembly, and value of parts manufacturers.

It should be pointed out that the Auto Pact was not free trade – it was managed trade - only if the industry did exactly what government told it to do and if the numbers and ratios all added up property, they would be allowed tariff free imports of vehicles.

During negotiations over the Canada-U.S. free trade deal in the 1980s and NAFTA in the 1990s, both sides agreed to phase out several remaining tariffs and duty remissions, especially tariffs on vehicles manufactured by automakers who weren't part of the deal. This primarily affected Asian and European producers so long as they included 50 per cent North American content, which led to the rise of their production lines here.[7]

So now back to the original question – what would the auto sector look like if we don have free trade and if tariffs are imposed by the US government? I suspect that it would look much like the late 1950's early 1960 auto sector where the Canadian government would enact substantial tariffs on any import of vehicles to protect Canadian automotive jobs. This would raise the price of Canadian vehicles for consumers and lead to greater inefficiencies in the economy.

It should also be pointed out, as I reviewed/researched this topic, that in the past, the larger relationship between countries was important. As noted above, the U.S. government may have

[6] 34. Cyprus (1960-present)
[7] How the 1965 Auto Pact kicked off Canada-U.S. free trade | TVO Today

been willing to assist the Canadian auto sector in return for the Canadian government's support for the U.S. position on Cyprus. In the past, certain countries had deeper relationships (think of the U.S. and Britian, Canada and the U.S., Norway/Sweden/Finland, etc.) which transcended individual disagreements or issues. There was a bigger picture relationship which was important. It is clear that the relationships between nations have dramatically changed.

I will leave you with a quote from U.S. President Lyndon Johnson in his official statement after finalizing Canada – United States Automotive Products Agreement in October 1965.

"Our ties with Canada are historically close, our relations cordial, our people durable friends. This agreement, originating in our common interest, arrived at for our common benefit, will make those ties even closer and more fruitful for the future."[8]

If you have any questions or concerns, please let me know.

Don

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[8] How the 1965 Auto Pact kicked off Canada-U.S. free trade | TVO Today