DEPUTY UNITED STATES TRADE REPRESENTATIVE
EXECUTIVE OFFICE OF THE PRESIDENT
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April 29, 1986

MEMORANDUM

TO: MEMBERS OF THE TRADE POLICY REVIEW GROUP

FROM: MICHAEL B. SMITH, Chairman

SUBJECT: TPRG Meeting, May 1

I have scheduled a meeting of the TPRG for 5:00 p.m., Thursday, May 1, in Room 203 of the Winder (USTR) building. At this time, only one item is scheduled for discussion: the Section 201 case on wood cedar shakes and shingles. Attached are two papers:

1. A brief paper outlining the issue for the TPRG. In this paper we have attempted to track the format used to present the Section 201 footwear case to the EPC.

2. The much more detailed paper developed by the interagency task force on wood shakes and shingles and reviewed by the TPSC. This paper has been amended to reflect comments made at the April 23 TPSC on this subject.

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April 28, 1986

Section 201 Shakes and Shingles Case

Issue: Should the President grant import relief to the U.S. western red cedar shakes and shingles industry and, if so, what type of relief should be granted?

Background

On March 25, 1986, the U.S. International Trade Commission (ITC) advised the President that increased imports have substantially injured the U.S. western red cedar (wrc) shake and shingle industry and recommended the imposition of a 35 percent tariff for five years. The Trade Act of 1974 requires that the President decide by May 24: (1) whether to grant import relief to the industry; and (2) if relief is granted, what form and level should be required. The law requires him to determine whether relief would be in the national economic interest.

The health of the U.S. wrc shakes and shingles has generally declined in the 1978-1984 period. U.S. consumption fell from 7.5 to 5.7 million squares ("square" refers to the quantity required to cover 100 square feet of surface area). Production dropped almost steadily from 3.3 to 1.5 million squares. The number of shake and shingle establishments also fell from more than 500 to less than 300, and employment declined from 4,531 to 2,146. Capacity utilization fell from 54 percent in 1980 to only 44 percent during the first nine months of 1985. Only in the area of net income did U.S. firms show improvement, i.e., from a 5.3 percent net loss from net sales in 1981 to 3.4 percent net income in the first nine months of 1985.

Imports of shakes and shingles -- virtually all of which come from Canada -- increased in quantity terms from 3.8 million squares in 1980 to nearly 4.5 million squares in 1984. In value terms, imports during the period grew from $149.7 million to $182.6 million. On both a value and volume basis, the ratio of imports of all shakes and shingles (the majority of which are wrc) to consumption has grown from around 40 percent in 1978 to around 73 percent during the first nine months of 1985.

There are a number of difficulties this industry faces in addition to those posed by import competition. First, it is saddled with a declining resource base. Experts estimate that, at current harvesting levels, U.S. old growth red cedar will be available only until the year 2006. By contrast, Canada expects to enjoy supplies into the twenty-second century. Second, Canadian restrictions on the export of logs have exacerbated an inelastic supply situation here and increased U.S. raw materials costs relative to those in Canada. Third, substitute siding and roofing materials, e.g., asphalt, tile and fiberglas, already account for 90 percent of consumption and could take over more of the marketplace were tariffs to lead to appreciably higher

prices. Finally, as a corollary to the third point, anti-flammability treatment requirements have nearly doubled the cost of a square of wrc shakes and shingles (i.e., from $40 to $70), thereby further reducing their competitiveness.

Major Policy Objectives

The law requires the President to make his decision by considering certain statutory criteria, which are broader than those the ITC considers in determining injury. The most important economic criteria include:

1. Adjustment. Can import relief allow U.S. firms to adjust to greater international competitiveness? Would relief encourage the remaining U.S. firms -- now small, family-run operations -- to pool resources for vitally-needed research into alternative raw materials and improved anti-flammability treatments? To what extent would U.S. shake and shingle employment increase? To what extent would a price increase for wrc shakes and shingles encourage consumers to switch to alternative roofing and siding materials, thereby hastening the demise of the industry?

2. Domestic economic costs. To what extent would import relief impose costs on: (a) U.S. consumers; (b) other U.S. industries, because Canada could retaliate (despite the fact that the current zero tariff on shakes and shingles is unbound in the GATT); and (c) the U.S. economy because import restrictions will make it less efficient?

3. International economic costs. To what extent would import relief hurt Canada, whose industry is also comprised of small,labor-intensive facilities?

Notwithstanding the economic justification for granting relief, or the lack thereof, the President needs to consider certain political criteria:

1. Section 201 legislation. In light of the fact that this is the first 201 case the President has had to consider since declining import relief for nonrubber footwear, what is the risk that a rejection of protection for wrc shakes and shingles will encourage passage of pending legislation reducing presidential discretion under 201?

2. Other action involving wood products. Would granting relief complicate our efforts to find a bilateral solution to the lumber trade problem (i.e., low stumpage pricing) with Canada? Would such action improve or harm efforts to eliminate Canadian export controls on logs? Would denial of import relief encourage Congressional efforts to include natural resource pricing as a countervailable subsidy?

Policy Options

The TPSC reviewed a number of options, as required by law, and selected five for TPRG consideration. The relief options were narrowed to tariffs only with the variation being duration and extent of degressivity.

Option 1: Provide no import relief.

Advantages

- o No cost to consumers.
- o No threat of retaliation from Canada.
- o Consistent with U.S. pledge regarding standstill and rollback of protectionist measures.
- o Consistent with spirit of 201 provision, which envisions import relief as a means of promoting adjustment rather than encouraging the maintenance of noncompetitive industries.

Option 2: Adopt ITC majority recommendation of a 35 percent tariff increase for 5 years on imports of western red cedar shingles and shakes.

Advantages

- o Would serve as proof that the USG is committed to the viability of Section 201 relief as a means of affording temporary safeguard protection, particularly following the negative determination for footwear.
- o Would give us more time to assess the industry's ability to use new methods and alternative materials to achieve international competitiveness.
- o Would give the U.S. shake and shingle industry a "cushion" while the Government considers action on an important cause of the industry's competitive problem, i.e., access to unpriocessed Canadian logs.
- o Would mean less unemployment initially. Estimated that approximately 40-100 jobs would be preserved in the first tariff year. (However, employment in the industry would be below current employment levels at the end of the relief period.)
- o Domestic production may increase between 3 and 7 percent.
- o Domestic prices may increase between 4 and 9 percent, to the benefit of the industry.

- o Tariff is unbound under GATT; therefore the United State would owe no compensation to trading partners in the event of a duty increase.

Option 3: Adopt a five-year 35 percent tariff, but have the President direct the USTR to request that the ITC conduct a review of the industry's adjustment efforts after 2 years so that he can determine whether the continuation of import relief was in the national economic interest.

Advantages

- o Same as in option 2.
- o Would spur greater industry effort toward adjustment.

Option 4: Adopt a five-year degressive tariff, i.e., 35 percent in Years One and Two, 20 percent in Years Three and Four and 8 percent in Year Five.

Advantages

- o Same as in option 2 (although initial employment, production and price gains would be lost more rapidly as tariff levels declined).
- o Would be consistent with our normal practice of degressivity under Section 201.
- o Might evoke less opposition from Canada than a straight-line tariff.
- o Would create less consumer costs in Years Three through Five.

Option 5: Provide expedited trade adjustment assistance.

Advantages

- o With respect to Labor Adjustment Assistance, could assist worker adjustment by providing an opportunity to obtain alternative occupational training and by providing job search and relocation funds to certified workers.

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Section 201 Case on Wood Shakes & Shingles

ISSUE

On February 26, the U.S. International Trade Commission (USITC) voted 4-2 that wood shakes and shingles are being imported into the United States in such increased quantities as to be a substantial cause of serious injury, or threat thereof, to the domestic industry. On March 18, three Commissioners voted to recommend a 35 percent tariff, over 5 years, be placed on imports of western red cedar shakes and shingles, (Commissioners Eckes, Lodwick and Rohr), two Commissioners voted to recommend trade adjustment assistance, (Chairwoman Stern and Commissioner Brunsdale) and one Commissioner voted to recommend no relief (Commissioner Liebeler).

The USITC submitted its report to the President on March 25, 1986. Section 202(b) of the Trade Act of 1974 requires the President to "determine what methods and amount of import relief he will provide, or determine that the provision of such relief is not in the national economic interest" within 60 days after receipt of the USITC report. Thus, a decision must be taken by May 24, 1986.

OPTIONS

If the President determines that he will provide import relief, he may do so for a period not to exceed five years.[1] The relief may take the form of: (1) tariffs, (2) quotas, (3) tariff-rate quotas, (4) orderly marketing agreements, or (5) a combination of any of these actions. The President can also order expeditious consideration of adjustment assistance petitions in connection with any of these forms of relief, as well as in the case where no import relief is provided.

If the President determines that the provision of import relief is not in the national economic interest of the United States he must report to Congress the specific reasons for denying import relief. He must also advise Congress of "what other steps he is taking, beyond adjustment assistance programs, immediately available to help the industry to overcome serious injury and the workers to find productive employment."

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[1]After an initial period of five years, import relief can be extended for one three-year period if the President determines, after taking into account the advice of the USITC, that such extension is in the national interest.

The Trade Policy Staff Committee Task Force on Shakes and Shingles has developed the following basic options for review:

Option 1 -- Provide No Import Relief

Notwithstanding the extent or type of relief provided to this industry, it is unlikely that shake and shingle manufacturers will be in a better position to compete with import competition once relief is exhausted than it is now. The availability of alternative, less costly roofing and siding materials, the high cost of treating shakes and shingles to meet safety standards, and the current lack of a clearly enunciated program on the part of the industry for adjustment during the period of relief suggest that Section 201 relief would not enhance the competitiveness of this industry. However, other factors (e.g., political considerations and the possibility of improved access to raw materials through bilateral negotiations) should also be weighed in determining the appropriateness of import relief.

Advantages

- No cost to consumers.
- No threat of retaliation from Canada.
- Consistent with U.S. pledge regarding standstill and rollback of protectionist measures.
- Consistent with spirit of 201 provision, which envisions import relief as a means of promoting adjustment rather than encouraging the maintenance of noncompetitive industries.

Disadvantages

- As the first 201 case before the President since the rejection of import relief for footwear, would call into serious question the viability of Section 201 as a means of providing temporary import relief.
- Would expose the President to serious criticism from the Congress regarding his use of the 201 statute and could lead to increased calls on Capitol Hill for the elimination of presidential discretion in cases where the USITC finds injury.
- Could discourage the Northwest industry from exploring further the use of alternative raw materials and less costly methods of ensuring anti-flammability.

Option 2 -- Increase Tariffs:

Option 2(a) -- Adopt USITC Majority Recommendation of a 35 Percent Tariff Increase for 5 years on Imports of Wood Shingles and Shakes of Western Red Cedar:

We estimate that the provision of a 35 percent tariff would raise prices, increase demand for U.S.-produced wrc shakes and shingles and employment in the industry, and reduce imports from Canada for the period of relief (see Section 202(c)4). A five-year, straight line tariff is considered appropriate, since it will enable the industry to weather a downturn in demand which could accompany business cycle changes during Years 3-5 of the relief period.

Advantages

- Would serve as proof that the USG is committed to the viability of Section 201 relief as a means of affording temporary safeguard protection, particularly following the negative determination for footwear (Other 201 cases now being considered, i.e., castings, fork lift arms and apple juice, are not yet due for USITC injury determination.)

- Would give us more time to assess the industry's ability to use new methods and alternative materials to achieve international competitiveness.

- Would give the U.S. shake and shingle industry a "cushion" while the Government considers action on an important cause of the industry's competitive problem, i.e., access to unprocessed Canadian logs.

- Would mean less unemployment in the shakes and shingles industry initially. Estimated that approximately 40-100 jobs would be preserved in the first tariff year. (However, employment in the industry would be below current employment levels at the end of the relief period.)

- Domestic production may increase between 3 and 7 percent.

- Domestic prices may increase between 4 and 9 percent, to the benefit of the industry.

- Tariff is unbound under GATT; therefore the United States would owe no compensation to trading partners in the event of a duty increase.

Disadvantages

- Imposing any tariff increase could seriously jeopardize the possibility of achieving a solution with the Canadians on lumber/stumpage pricing practices.

- Possible retaliation by the Canadians even though tariff is unbound.

- Tariffs would raise questions regarding U.S. commitments to a standstill and rollback of protectionist measures.

- Provision of a five-year non-graduated tariff runs counter to our normal practice of degressivity under Section 201.

- According to analyses, tariff would be largely ineffective in promoting industry viability since domestic prices are estimated to rise by only 3 to 9 percent, and domestic output is expected to increase by at most 7 percent. In addition, the increase in employment would be small.

- Increases in shake and shingle industry employment could come at the expense of jobs in the wholesaling, distribution and importing sectors.

- Small benefits received by producers as a result of a tariff come at the expense of $14-$26 million dollars to consumers.

- Likely higher prices for consumers since it is unlikely that a tariff would be completely absorbed by Canadian shake and shingle manufacturers.

- It is highly unlikely that tariffs would promote effective adjustment over the longer term absent any change in underlying market conditions.

- Higher prices for shakes and shingles could cause consumers to switch to alternative roofing and siding materials, thereby diminishing the overall market for western red cedar shakes and shingles.

NOTE: Effect on U.S.-Canadian FTA is not clear.

Option 2(b) -- <u>Same as Option 2(a) above with the added element that the President would direct the USTR to request that the USITC conduct a review of the Industry's Adjustment Efforts after 2 years so that he can determine whether the continuation of Import Relief was in the National Economic Interest.</u>

This approach could allow the domestic industry to continue investigating whether the use of alternative species and other internal improvements will enable them during a reasonable period

of time to meet Canadian competition. As noted earlier, prospects for such adjustment do not appear bright.

The petitioners would be placed on notice that the President will determine after two years if the industry is in fact using import protection to adjust to the international competition it will face when protection is removed. He could also assess the actual effect of the tariff on the development of the market. If the industry has undertaken no effective adjustment efforts and does not appear to be able to do so, the President would be authorized to lift relief. This option could also preserve a number of shake and shingle manufacturing jobs while the President determines whether it is feasible and appropriate for him to enter into bilateral negotiations with Canada regarding log export restrictions (see supplementary option 2).

Advantages

- Same as in option 2(a).
- Would spur greater industry effort toward adjustment.

Disadvantages

- Same as in option 2(a).
- Two years might be insufficient time for industry to make a definitive judgment regarding its ability to find alternative sources of raw material supply or to develop and market other innovations (e.g., panelized products).
- Would force the President to make a difficult decision twice regarding relief for this industry.
- Removing relief after two years could place the shake and shingle industry squarely in the middle of a downturn in the highly cyclical housing market (and, hence, a downturn in demand).

Option 2(c) -- Impose a five-year degressive tariff, i.e., 35 percent in Years One and Two, 20 percent in years Three and Four and 8 percent in Year 5:

A five-year degressive tariff has been proposed as consistent with our normal practice of providing gradually scaled-back relief under Section 201.

Advantages

- Same as in Option 2(a), although domestic employment, production and price gains would be lost more rapidly as tariff levels declined.

- Would be consistent with our normal practice of degressivity under Section 201.

- Might evoke less opposition from Canada than a straight-line tariff.

- Consumer costs would be lower in Years Three through Five.

Disadvantages

- Scaling down relief during Years Three thourhg Five could exacerbate industry adjustment problems if the action coincides with a downturn in the housing market.

- Would only lead to a temporary employment increase of 26-58 in Years Three and four and 11-24 in Year Five.

- Prices to domestic producers would only rise 2-5 percent in Years Three and Four and 1-2 percent in Year Five.

Option 3 -- Impose a Quota on Imports of Western Red Cedar Shakes and Shingles: Impose a quota of 3,097 Thousand Squares (the Average Level of U.S. Imports of Western Red Cedar Shakes and Shingles over the period 1979-1983). This quota could be divided into 1,952 thousand squares for shakes and 1,145 thousand squares for shingles, representing each product's average import level over 1979-1983.

Advantages

- As in a tariff, would show that the President is willing to use Section 201; would give the industry more time to explore adjustment possibilities; and would give the U.S. Government time to decide whether to enter into supply access negotiations with Canada.

- Would enable us to strictly control imports through quantitative limits.

Disadvantages

- U.S. would be required to provide relief consistent with the provisions of GATT Article XIX, which would entail prior notice and consultation and would entitle the Canadians to compensation.

- Would conflict with the spirit of the U.S.-Canada Safeguards agreement under which both sides have committed to avoiding quota relief whenever possible.

- At best, increase in domestic shipments of shakes and shingles would be only 7 percent, and if demand is elastic, only 3 percent.

- High annual cost to consumer (between $11 and $26 million) in comparison with the total value of output and the number of jobs actually saved in the industry.

- Additional loss to the U.S. economy because foreigners are able to capture the quota rents, increased distortion of marketplace.

- Would require increased costs by the Customs Service to administer the quota.

- It is highly unlikely that quotas would promote effective adjustment over the longer term absent any change in underlying market conditions.

- Gains afforded to producers under import relief would be only a small fraction of the cost to the consumers.

- Industry does not advocate quotas.

Option 4 -- Impose a Tariff-Rate Quota on Imports of Western Red Cedar Shakes and Shingles:

Advantages

- As with a tariff, would allow imports to grow with consumption.

- Less costly to the U.S. economy if the quota levels are set at high levels, and the tariffs are set at low levels.

Disadvantages

- Same general disadvantages as those associated with both a tariff and a quota (except that the United States would not owe compensation to Canada).

Option 5 -- Negotiate an Orderly Market Agreement with Canada:

Advantages

- Similar to advantages in option 3.
- In the context of OMA negotiations, could convince the Canadians to waive their rights to compensation.
- Quantitative impact on imports is precise.

Disadvantages

- Siminar to disadvantages in option 3.
- Because the effect on prices is difficult to predict, the amount of protection provided the industry would be impossible to determine.
- Unlikely that Canada would enter into an OMA, particularly since there are no other suppliers to the U.S. market to exert influence on Canada.

Other Action:

In addition to the core options set forth above, the TPSC may wish to consider whether action should also be taken with respect to one or more of the supplementary measures listed below.

Supplementary Option 1 -- The Provision of Expedited Trade Adjustment Assistance:

In her remedy views following the USITC's investigation, Chairwoman Paula Stern argued that the industry's true objective in bringing its import relief petition to the U.S. Government was to improve the availability of raw materials to U.S. shake and shingle producers. Moreover, she said, that while a 35 percent ". . . tariff may have some price effect, domestic producers will be unable to reap the benefits of any increase in price with increased production and employment. And no matter what the price effect of a 35 percent ad valorem tariff, it will likely prove counterproductive as precious demand for domestic shingles and shakes is diverted even more quickly toward cheaper, substitute, fire-resistant products." She suggested that adjustment assistance would be an appropriate alternative to import protection. This approach normally accompanies a no relief decision and is mainly alternative to, rather than supplementary to, tariffs or quotas. Nonetheless, nothing in Section 202(3) of the Trade Act of 1974 or elsewhere precludes giving adjustment assistance in conjunction with import relief.

Under an expedited trade adjustment assistance program, petitions filed with the Department of Labor on behalf of shake and shingle workers would be processed earlier; however, the eligibility of workers to receive TAA benefits would continue to depend on the results of the case investigation. Workers would not be guaranteed eligibility for TAA benefits. Additionally, the President could direct the Secretary of Labor to utilize other available resources, including dislocated and/or disadvantaged worker programs authorized by the Job Training Partnership Act (JTPA) of 1982. In addition, the Department of Commerce Trade Adjustment Assistance Program can provide technical assistance. However, since 1979,39 firms have been certified by Commerce as eligible to apply for trade adjustment assistance; 24 received technical assistance; 19 of these 24 firms showed no improvement in their financial situation; one stabilized its financial picture; and 4 were doing signficantly better. The remaining 15 firms did not apply for assistance. None of the certified firms received any financial assistance.

Advantages

- With respect to Labor Adjustment Assistance, could assist worker adjustment by providing an opportunity to obtain alternative occupational training and by providing job search and relocation funds to certified workers.

Disadvantages

- No assurance that individual workers or firms will qualify for the either the Department of Labor or Department of Commerce programs.

- Under current legislation, workers are eligible for cash benefits only after unemployment compensation is exhausted. Only training, job search and relocation benefits could be made available earlier.

- With respect to Commerce Adjustment Assistance, historical experience for the shakes and shingles industry indictes that the program has not been effective.

- Recent legislation that has been signed into law eliminates all financial assistance. The new law does not provide direct and guaranteed loans under the Commerce Program.

- Since technical assistance is provided on a cost-share basis with the Federal Government's share not to exceed 75% under the Commerce Program, firms may not be able to afford to participate in the program.

Supplementary Option 2 -- Negotiation of Improved Access to Canadian Logs

The price differential between U.S. and Canadian red cedar logs is reported to be $60 per thousand board feet, i.e., $240 in Canada vs $300 in the United States. While some of this differential is due to natural conditions (e.g., greater accessibility of Canadian supplies), Canadian Government log export restrictions also play a role in ensuring lower prices in Canada for raw material inputs. Notwithstanding the final decision regarding import relief, unless we can negotiate improved access to Canadian logs, one of the underlying causes of U.S. industry's lack of competitiveness will remain unchanged. This supplementary option has no necessary connection to Section 201 and could be pursued whether or not statutory import relief were granted.

In the context of current discussions involving bilateral lumber trade, the United States and Canada have agreed that possible relaxation of log export restrictions would be an appropriate topic for the proposed bilateral free trade negotiations. Should we enter into consultations involving log trade, the United States may have to be prepared to offer reciprocal relaxation of its own ban on the export of stumpage from Federal lands. (While the Federal Government owns a small share of the land in the United States, most available red cedar here is located on those governmental lands.) According to the petitioner, the U S. shake and shingle industry would support a liberalization of U.S. restrictions if done on a bilateral basis. Other groups, however, would oppose such action.

RECOMMENDATION

BACKGROUND

INTRODUCTION

A. The USITC Injury Determination

On February 26, the USITC determined by a vote of 4 to 2 that wood shakes and shingles (TSUS Item 200.85) are being imported into the United States in such increased quantities as to be a substantial cause of serious injury, or threat thereof, to the domestic industry producing articles like or directly competitive with the imported articles. (Chairwoman Stern and Commissioners Eckes, Lodwick and Rohr).

Among the facts considered by the USITC in reaching this determination were:

-- U.S. consumption of wood shakes and shingles declined from 8.4 million squares in 1978 to 5.0 million squares in 1982 and then rose to 6.8 million squares in 1984.

-- Imports increased within the meaning of section 201 ("either actual or relative to domestic production"), particularly during the most recent period:

	1983	1984
Million Squares	3.8	4.5

	Jan.-Sept. 1984	Jan.-Sept. 1985
Most Recent Period	3.3	3.7

-- Domestic production declined 13 percent between 1983 and 1984, from 2.7 million squares to 2.4 million squares. This decline accelerated considerably in 1985, falling 41 percent, from 1.9 million squares to 1.4 million squares, when January-September 1985 data are compared with data for the corresponding period of 1984. It is estimated that the overall production capacity of the domestic industry fell 15 percent from 1980 to 1984. Data for the most recent period indicate that this overall decline in production capacity is continuing. It is estimated that the number of firms has declined from 445 in 1978 to 274 in 1984, or by 38 percent and for the most recent period estimates indicate a continued decline to 255 firms (ITC data).

-- Employment, like production, fell significantly in 1984 and precipitously in 1985. Annual average employment fell 11 percent between 1983 and 1984, from 2,375 to 2,146 workers. In 1985, employment fell 37 percent, from 2,146 workers in January-September 1984 to 1,572 workers in January-September 1985.

-- The domestic industry operated with significant losses from 1980 through 1982, but showed significant improvement in profitability during 1983. In 1984, the industry's financial performance weakened considerably. During January-September 1985, the industry has reported profits but they are considerably lower than those reported in 1983 or during the comparable period of 1984 (ITC data).

B. History of Trade Related Investigations

On October 7, 1982, a petition[2] was filed with the Commission and the Department of Commerce by counsel on behalf of the United States Coalition for Fair Canadian Lumber Imports, a group of 8 trade associations and more than 350 domestic producers of softwood lumber products, alleging that imports of softwood shakes and shingles from Canada were being subsidized by the Government of Canada within the meaning of section 701 of the act (19 U.S.C. 1671). Accordingly, effective October 7, 1982, the Commission instituted a preliminary countervailing duty investigation under section 703(a) of the act to determine whether there was a reasonable indication that an industry in the U.S. was materially injured, or was threatened with material injury, or the establishment of an industry in the U.S. was materially retarded, by reason of imports of such merchandise from Canada.

On the basis of the record developed in the investigation, the Commission determined on November 22, 1982, that there was a reasonable indication that an industry in the U.S. was materially injured by reason of imports from Canada of softwood shakes and shingles, provided for in item 200.85 of the Tariff Schedules of the United States, which were alleged to be subsidized by the Government of Canada.[3]

On May 31, 1983, Commerce issued its determination on softwood lumber, shakes and shingles, and fencing in one notice. The final determination was "The total estimated net subsidy for each product is de minimus, and therefore our final countervailing duty determinations are negative." Because the Commerce final determination was negative, the investigation was terminated at both Commerce and the ITC.

WOOD SHAKES AND SHINGLES INDUSTRY

Description and Uses

The products covered in USITC investigation, No. TA-201-56, are wood shakes and shingles.

These articles are thin, rectangular pieces of wood of random width

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[2]Petitions were also filed on softwood lumber and softwood fence on October 7. The cases were handled as three individual petitions by Commerce and the ITC.

[3]Commissioner Stern also determined that there was a reasonable indication of threat of serious injury by reason of the allegedly subsidized imports.

which range in length from 18-24 inches. In general, a shake has one split (rough) side and one sawn (smooth) side while a shingle is sawn on both sides. Both are used as a covering for the sides and roofs of buildings. Since shakes are somewhat thicker than shingles they are generally preferred for roofs where weathering is more intensive and thickness is an advantage. Overall, the use of shakes is predominant with shake consumption more than twice that of shingles in 1984. Over the period, 1978- 1984, apparent consumption of shakes decreased about 40 percent, while shingle consumption decreased nearly 35 percent.

About 90 percent of the shakes and shingles produced in the United States are manufactured from western red cedar with the remainder produced mainly from redwood and northern white cedar. Shakes and shingles are produced from these trees because they display desirable qualities such as: vertical grain (for ease in splitting), a low coefficient of expansion, high strength and durability, relative freedom from warping, light weight, good nailholding qualities, and resistance to rot and insect damage.

In view of the fact that the ITC has limited its recommendations to the red cedar products, and because we believe this limitation is appropriate, we have limited the industry description to red cedar products.

THE WESTERN RED CEDAR RESOURCE BASE

We have chosen to discuss the resource base first because the problems, and, indeed, the future of this industry are inexorably tied to the depletion of that base. This should be understood at the outset.

Western red cedar is found from southeastern Alaska, to northwestern California, to inland Idaho, Montana and eastern British Columbia. It survives in a variety of sites, elevations and soils.

To produce red cedar shingles or shakes which meet industry quality and size standards, manufacturers require wood which has been cut from trees of at least 25 inches in diameter (for shingles) and of at least 29 inches in diameter (for shakes). Such trees, which would be approximately 160 years old, are preferred because they have a tighter grain, a higher oil content and a smaller proportion of sapwood. In addition, it is more cost efficient to use larger diameter logs.

The U.S. Resource Base

By far the greatest concentration of western red cedar in the United States is located in western Washington, especially in three counties on Washington's Olympic Peninsula.

Current data on the supply of western red cedar on the Pacific Northwest are not available. However, certain estimates can be made on the availability of western red cedar in western Washington, and these estimates indicate a rapid depletion of this resource.

The inventory of western red cedar suitable for, but not dedicated solely to, the production of western red cedar shakes in western Washington declined 19 percent from 5.3 billion board feet in 1980 to 4.3 billion board feet in 1985. At the rate of harvest which occurred during 1980-84, the suitable domestic inventory for shakes would last until 2006. The inventory of western red cedar suitable for, but not dedicated solely to, the production of western red cedar shingles in western Washington shows about the same decline. It decreased 18 percent from 6.2 billion board feet in 1980 to 5.1 billion board feet in 1985. At the rate of harvest that occurred during 1980-84, the suitable inventory for shingles would last until 2007.

The use of the red cedar inventory is dependent upon factors other than demand for shakes and shingles. Western red cedar is seldom found in pure stands and the harvest is highly dependent on the demand and harvest of all species in a stand. Further, shakes and shingles are not the only uses for harvest. In fact, the shake and shingle industry ranks second in the consumption of the western red cedar harvest. In 1984, the Washington State harvest of western red cedar logs in excess of 100 years old, was consumed in the following proportions: lumber, 42 percent; shakes and shingles, 34 percent; exports, 30 percent; veneer and plywood, 2 percent; and posts, poles and pilings, 2 percent.

Salvage of Western Red Cedar

The petitioners have proposed several changes which they believe would encourage increased salvage of western red cedar from federal lands. The first proposal requests that "...The United States Forest Service-Special Timber Salvage Fund place increased emphasis on the expenditure of funds to prelog cedar salvage prior to final stand operations in order to increase utilization of old growth western red cedar."

According to the Forest Service, prelogging for cedar is not cost effective if there are no roads into the logging site and if the area to be logged is difficult to access. In this situation it is better to wait until the area is under contract and ready for final stand operations. At that time arrangements could be made between the cedar buyer and the regular purchaser to prelog cedar using roads and equipment which are already in place. However, in cases where the site is already accessible it may be worthwhile to use the Special Timber Salvage Fund to prelog for western red cedar since cedar logs are of relatively high value.

The Special Timber Salvage Fund currently has an annual budget of $18 million to be used nationally, $5 million of which is available to Region 6, the area with the highest concentration of western red cedar. The Salvage Fund is one of the items in the Forest Service budget which is now constrained. This means that any increase in expenditures would have to come at the expense of other operations. If it can be shown that a shift of expenditures into the Salvage Fund would result in a sufficient return on investment, the Forest Service would be amendable to such a shift.

The other recommendation put forward by the petitioners was "...that in clearcut units where 5% or more of the timber to be harvested is red cedar, that logs or chunks falling below 50 board feet be included as a portion of the per acre material and be subject to lump sum payment."

In Forest Service Region 6 there are several different methods for pricing timber. Some timber is paid for on a "per 1000 board foot net scale basis", that is, the logger pays a set price for every 1000 board feet of quality (crack free, rot free, etc.) timber. The lower quality remainder of the log is subject to a prearranged per acre, as opposed to net scale, fee. At the present time this per acre fee can only be applied to 10-30 board feet of any given log. The petitioners would like to raise this limit to 50 board feet per log. They contend that this would provide greater incentive for removing more chunks and slabs of cedar since more material would be available at this per acre "flat fee" allowing loggers access to enough wood and allowing the most efficient loggers to lower their costs by pulling out as much wood per acre as possible.

However, if the board foot limit were raised, it is likely that the Forest Service would have to raise its per acre fees since the price per acre is based on the value of the material which is to be removed. If the fee was raised it still might be possible for the most efficient logger to benefit from this change. The Forest Service is apparently willing to discuss this type of change for Region 6 if it would lend more flexibility to the system. However, they don't believe it would save money for the average purchaser since per acre fees would likely be increased.

Overall, the petitioners' two proposals would not seem to have the potential to increase significantly available supplies of western red cedar.

<u>Research on Alternative Wood Species</u>

Work has already been done by the Red Cedar Shingle & Handsplit Shake Bureau on alternative species for making shakes and shingles. It is reported that considerable research and testing was conducted on larch in the early 70's. To date, alternative

species certified by the Bureau are:

Luan mahogany
Sitka spruce
Western larch
Douglas Fir

A separate satellite Bureau has been set up to administer standards on alternative species.

For marketing purposes, producers of alternative species are listed by the Bureau in the Annual Buyers Guide but no listed producer is making shingles or shakes from these species at this time.

Over a 6-year period, extensive research and development efforts have been devoted to producing shingles from southern pine by the Texas State Forestry Research Station at Lufkin. The Red Cedar Bureau helped to fund the initial efforts of this station when it was engaged in research on cedar shingles. The station then shifted its efforts to the use of southern pine for shingles. Results of the research have been promising. Two private Texas companies are now on the verge of producing and marketing southern pine, shingles for the Texas market. As a direct result of the research two other southern state forestry agencies have started southern pine shingle market development programs.

The Red Cedar Bureau has been kept informed of the Texas Station's Research results and has helped in disseminating information on these results. Results of the research were publicized and would have been made available to the Bureau's members which make up nearly half of the list of petitioners.

The Canadian Resource Base

The western red cedar resources of Canada are concentrated in British Columbia. Western red cedar in British Columbia is located in two distinct regions--coastal and interior. More than 75 percent of the western red cedar in British Columbia is located on the coast and the vast majority of that cedar is at least 120 years old.

The approximate inventory of mature western red cedar in British Columbia was 156 billion board feet in 1984. Based on the average level of harvest of western red cedar during 1980-84, the western red cedar inventory of coastal British Columbia would last until the year 2116, and the inventory in the interior of that province would last until 2077.

In British Columbia shakes and shingles account for an even smaller amount of total harvest. It is estimated that lumber production

consumed about 70 percent of the British Columbia western red cedar harvest in 1984, shakes and shingles consumed about 25 percent, log exports about 2 percent, and plywood and siding the remaining 3 percent.

PROFILE OF THE DOMESTIC INDUSTRY

Number of Establishments

The actual number of U.S. establishments that produced wood shakes and/or shingles in 1985 is estimated to have totaled about 300, with production concentrated in the Pacific Northwest, especially in Washington. In 1985, Red Cedar Shingle and Handsplit Shake Bureau (RCSHSB), a marketing and inspection organization to which many U.S. and Canadian producers belong, reported 165 member U.S. mills accounting for about 60 percent of western red cedar shingle and shake production. Of these 165 mills, 113 were located in Washington, 32 in Oregon, 16 in Idaho, 2 in Montana, and 2 in Alaska.

The number of firms producing wood shakes and shingles (based on data for four states--Washington, Oregon, Idaho and Maine), is estimated to have declined by 38 percent between 1978 and 1984 and again by 7 percent between January and June 1984 and the corresponding period in 1985.

Work Force

The annual average number of employees in the U.S. shake and shingle industry fell from 4,531 in 1978 to 2,146 in 1984, with average employment per firm of 7.8 persons in 1984, down from 10.2 in 1978. Average annual wages in the U.S. shake and shingle industry have risen only modestly from $12,127 per employee in 1978 to $14,627 per employee in 1984. Workers are generally paid on a piecework basis.

The labor force involved in the production of wood shakes and shingles is fairly specialized. The typical worker will take about 6 months to become proficient on a shingle saw or shake resaw, at which time his/her production will be about 40 squares per 8-hour day. (A square is the quantity required to cover 100 square feet of surface area and is the usual commercial unit of measurement for shakes and shingles.)

Production

U.S. production of shakes and shingles has experienced a long downward trend. Production of all wood shakes and shingles averaged nearly 3 million squares valued at $133 million during 1978-1984. The year of greatest production was 1978 (4.7 million squares), the year of lowest production was 1982 (1.8 million squares). Production during the first 9 months of 1985 was 1.4

million squares valued at $53 million.

Wood accounts for the major cost of production, from 1980-1984 the cost of wood averaged 56 percent of net sales. (During this 1980-84 period the average price of "shake grade" red cedar logs was $350.84/1000 b.f. and the price of shingle grade red cedar logs was $279.04/1000 b.f.) After wood the second major production expense is labor which averaged 26 percent of net sales from 1980-84.

Methods of Production and Productivity

Production of shakes and shingles is aptly described as a "cottage industry," with production methods not changing significantly in recent years. In fact, the basic equipment used today is essentially the same as that used in the early 1900's. Because of the simplicity and availability of equipment, a typical shingle or shake mill can be started with a capital investment of as little as $25,000 to $30,000.

Productivity gains, which have been estimated at 6.2 percent between 1979 and 1985, are primarily due to the purchase of new sawing equipment (including automatic sawing equipment for some firms), splitters, stackers, and drying kilns. Gains in productivity may also be the result of inefficient producers leaving the marketplace. In spite of the aforementioned decline in the number of producing firms, present capacity utilization is estimated at about 50 percent. Capacity fell some 15 percent in the 1980-84, period.

CAPITAL EXPENDITURES AND FINANCIAL CONDITION

Capital expenditures for this labor intensive, troubled industry are small. Over the years 1980 to 1984, 13 reporting producers had capital expenditures of less than $1 million. This is equivalent to an annual average of less than $76,000 per reporting firm. Since these firms accounted for slightly over 13 percent of total production it is likely that this level of expenditure is probably above that of the average firm.

In the aggregate, the industry, as represented by 19 U.S. producers, experienced losses in 1980-82. Only in 1983, when prices were generally climbing and when nearly $900,000 net income was realized, did the industry perform well. During the period 1980-1984, the debt to equity ratios of the industry went from 1.11 to 2.69.

Prices

In the shingle and shake industry, product prices are affected primarily by the availability and cost of cedar logs, by the level of demand for the product from the housing market and by

prices and availability of competing materials.

Wood shakes and shingles are normally sold on an f.o.b. mill basis. Price data gathered and published in the industry publication Random Lengths Weekly Lumber Price Guide are often used as a reference point in the negotiation of transaction prices. The average composite price of shingles and shakes in 1985 was $41.01 per square.

During the period 1970-1985, the deflated index for shakes and shingles, based on the 1970 first quarter composite U.S. price for these products, shows prices at their highest level from October-December 1977 and at their lowest levels in the fourth quarter of 1970 and the second quarter of 1985. The deflated shake and shingle price index fluctuated while decreasing by 49 percent from October-December 1977 to April-June 1982, when it was 104.7. In April-June 1985, the index was 101.58. Western red cedar shake and shingle prices ended the period January-March 1970 to April-June 1985 with roughly the same price change as that of lumber and building materials in general over the same period. The shake price index was at 281 in 1984, and the index for shingles was at 336.

Marketing and Transportation

Most of the market promotion of shakes and shingles in the United States and Canada is handled by the Red Cedar and Handsplit Shake Bureau, which maintains, an inspection service that certifies the quality of each members mill's production. Since the Canadian and U.S. products are virtually identical, they are comingled by wholesalers.

Most wood shakes and shingles produced in the United States are delivered by truck, although those produced in the West destined for Eastern markets are shipped primarily by rail.

Apparent U.S. Consumption

Consumption of shakes and shingles is highly dependent upon the level of housing construction. In most years, about 75 percent of U.S. consumption of shingles and shakes is for new structures with reroofing or residing accounting for the remainder.

U.S. consumption of wood shakes and shingles declined from 8.4 million squares in 1978 to 6.8 million squares in 1984. The downward trend in U.S. consumption is due to changes in the levels of housing starts in the early eighties and to restrictive building codes.

In 1984, about 40 percent of the red cedar shakes and shingles consumed domestically were shipped to California and Texas. This is down from about 50 percent annually during 1979-81. The

decline is not due to a sudden geographic shift in markets but is largely a result of restrictive building codes, particularly those in California, which curtail or prohibit the use of these products for consumer safety reasons. California, Texas, Washington and Oregon accounted for over 60 percent of all red cedar shakes and shingles sold in the United States in 1984. The distribution pattern of western red cedar shakes differs from that of western red cedar shingles. Shakes are primarily distributed to California, whereas shingles are mostly delivered to Texas.

Competing Products

The primary competition for wood shakes and shingles is asphalt roofing shingles. These are about 30 percent less expensive than cedar products and are used extensively throughout the country. Other products that compete with wood shingles and shakes are: tile, fiberglass, metal roofing, aluminum and vinyl siding, other types of wood siding, and slate. The extent to which these products are truly interchangeable depends on the relative costs of material and installation, regional and personal preferences, and building codes. Recently wood shakes and shingles have been losing market share; this may be due to more restrictive building codes.

Imports

The United States is the leading importer of these products, which come almost entirely from Canada. Most importing of wood shakes and shingles is done by major U.S. wholesalers. The wholesaler usually mixes the imported and U.S.-produced products together for sale, since, because of product standards groups, quality differences are generally not a factor. The Seattle, Washington U.S. Customs district is the leading port of entry for imports of shakes and shingles.

U.S. imports of wood shakes and shingles rose from 3.7 million squares, valued at $162.0 million in 1978 to 4.5 million squares, valued at $182.6 million, in 1984 for an overall increase of 20 percent by quantity, and 13 percent by value, during 1978-84. Imports increased in quantity, but decreased in value, from January-September 1985. The ratio of imports to domestic production increased sharply from 79 percent in 1978 to 186 percent in 1984, and continued to increase sharply from 168 percent during January-September 1984 to 272 percent during January-September 1985.

U.S. imports of western red cedar shakes increased 49 percent in terms of quantity and 45 percent in terms of value during 1978-84. Shake imports increased in quantity but decreased in value, from January-September 1984 to January-September 1985. The ratio of imports of western red cedar shakes to domestic production

increased from 51 percent in 1978 to 162 percent in 1984 and continued to increase from January-September 1984 (151 percent) to January-September 1985 (243 percent).

The trends in imports of shingles are not nearly as volatile as those for shakes. U.S. imports of western red cedar shingles declined 28 percent in terms of quantity and 30 percent in terms of value during 1978-84. Imports rose in quantity, but declined in value from January-September 1984 to January-September 1985. Indications are that relative prices, which historically have favored the United States, have shifted over the last several years, particularly with regard to 1/2" by 24" red cedar shakes, the main import product, and now are in favor of the Canadians. This must be considered a major factor in the increasing import penetration of recent years.

Exports

U.S. exports of domestically produced wood shakes and shingles are minimal. They increased from 39,038 squares, valued at $1.3 million in 1978 to 108,502 squares, valued at $3.3 million in 1984, but fell from 97,786 squares, valued at $2.6 million, during January-Sepember 1984 to 47,031 million squares, valued at $2.2 million, during the corresponding period of 1985. Canada is by far the leading market for U.S. exports of shakes and shingles. Canada imports shakes and shingles primarily to complete large orders which can not be filled with current inventory. Most of these imports from the United States, are then exported from Canada back to the United States.

STATUTORY CRITERIA

In determining whether to grant import relief, and what method and amount, the President is required by Section 202 of the Trade Act of 1974 to take into account, in addition to other considerations he deems relevant, the following criteria:

Section 202 (c)(1): Worker Adjustment Assistance. "Information and advice from the Secretary of Labor on the extent to which workers in the industry have applied for, are receiving, or are likely to receive adjustment assistance or benefits from other manpower programs."

Since April 3, 1975, the effective date of the worker Trade Adjustment Assistance Program (TAA) under the Trade Act of 1974, the Department of Labor has certified a total of 1,075 workers in the western red cedar shake and shingle industry for benefits under the program. Benefits have been primarily in the form of cash allowances, supplementing regular state unemployment insurance payments and totaling $2,740,301 (through September 30, 1985). Eight petitions, covering 237 workers, were certified between January 1983 and March 1986; of the eligible workers eight have

received TRA payments of $7,106, and ten have received training funds of $6,245 million and two have received job search allowances of $1,580.00.

The TAA program is scheduled to expire on September 30, 1991. For FY 1986, Trade Readjustment Allowance funds are $106 million and TAA funding for training, job search, relocation and related employment services, $24.8 million.

Shake and shingle industry workers laid off might also qualify to participate in the dislocated and/or disadvantaged worker programs authorized by the Job Training Partnership Act (JTPA) of 1982. Emphasis on the JTPA Title III program is on helping dislocated workers find other employment through training, job search, relocation, and pre-layoff assistance. Unlike the TAA program, workers who apply under JTPA are not guaranteed benefits because they have been impacted by import injury. Also, JTPA Title III does not provide for income maintenance; such maintenance would be primarily through Unemployment Insurance compensation which can be collected up to a maximum of 26 weeks after layoff. Workers could, however, be targeted for the benefits under that portion of the appropriation which allows for discretionary funding by the Secretary of Labor as discussed below.

Seventy-five percent of the appropriated funds under JTPA Title III are allocated among the States and Territories, which determine, in accordance with the law and regulations, how their programs will operate, while up to 25 percent may be reserved by the Secretary of Labor (discretionary funds). The discretionary funds are made available to the Governors who apply for funds to serve individuals affected by these mass layoffs, natural disasters, Federal Government actions, or who reside in high unemployment areas or designated enterprise zones. Title III funding for the PY (Program Year) 1985 (July 1, 1985-June 30, 1986) was $222.5 million with $56 million allocated for the Secretary's fund. For PY 1986, funding declined to a level of $95.7 million with a maximum of $24 million for the Secretary's fund. Since the program has been in effect (beginning October 1, 1983) no JTPA funds have been targeted to dislocated shake and shingle workers. However, funds have been directed toward dislocated workers in the broader "wood products" industry, and may benefit some shake and shingle workers. Projects directed to wood product workers amounted to $377,446 in Idaho and $1,433,945 in Oregon during PY 1984; and $675,000 in Oregon during PY 1985.

Title II-A of the JTPA provides training and related employment and support services for the economically disadvantaged. In view of the relatively low average hourly wage rate for workers in the domestic shake and shingle industry, it is likely that some displaced workers in the industry may fall within the definition of an economically disadvantaged worker and be found eligible for

Title II-A benefits. Again, unlike TAA, workers are not guaranteed benefits because of import injury but, as indicated above, could be targeted for such benefits by the Secretary of Labor.

Potential Layoffs in the Next 12 Months

Employment is expected to decline in the next 12 months, but the rate will depend on several factors including the level of imports. It is to be expected that granting no relief to the industry will likely lead to continued increases in imports and import penetration. Changes in housing demand due to declining interest rates and the consequent, expected increase in new housing starts will affect the industry. Other considerations are the general condition of the economy, and the ability of producers to obtain logs. Projections concerning job losses if no relief is granted are discussed under section 202 (c)(9).

Prospects for Present and Potentially Separated Workers

The general outlook for most separated and potentially separated workers in the industry appears to be generally poor, according to a recent assessment by the Department of Labor. The assessment is based on a survey by the Employment and Training Administration and the Department of Labor, Employment Service vacancy data, and labor market conditions in the three major red cedar shake and shingle producing states Washington, Oregon, and Idaho.

Data provided by the U.S. Bureau of Labor Statistics indicated that in only 3 of the 19 identified western red cedar shake and shingle producing areas (i.e., counties, metropolitan statistical areas and primary metropolitan statistical areas) could labor market prospects be termed better than fair. Sixteen areas qualified as labor surplus areas--areas where unemployment has exceeded the national average by 20 percent for at least two years. The December 1985 unemployment rate nationally was 6.7; in Washington's shake and shingle producing areas, which accounts for about 80 percent of the industry employment, the average unemployment rate was 12.1 percent.

Generally, the data suggests that not granting import relief will create an even greater strain on unemployment (the average December 1985 unemployment rate for the 19 affected areas was 11.9 percent) in the industry should imports continue to increase and should there be no significant improvement in apparent domestic consumption.

Section 202(c)(2): Firm Adjustment Assistance: "Information and and advice from the Secretary of Commerce on the extent to which firms in the industry have applied for, are receiving, or are likely to receive adjustment assistance under Chapter 3 and 4."

Availability and Utilization

The Trade Act of 1974 authorized the Trade Adjustment Assistance Program, which is administered by the International Trade Administration within the Department of Commerce.

Under the Program, the Secretary of Commerce may certify a firm as eligible to apply for trade adjustment assistance if the firm meets the certification requirements. In order for a firm to be certified eligible to apply for assistance, it must show that sales or production have decreased; that it has laid off, or is about to lay off workers, or has significantly reduced their work hours; and, that increased imports of "like or directly competitive" articles have been an important reason for the declines.

Following certification, the firm may develop an approved adjustment plan and request technical and/or financial assistance to implement the plan. In the past, financial assistance has included both direct and guaranteed loans, while technical assistance includes guidance and assistance in preparing petitions and adjustments plans, as well as analysis of management, production, marketing or technical problems. This technical assistance is then followed-up with recommendations for corrective measures, feasibility studies and/or other types of consulting assistance.

Since 1979, thirty-nine wood shake and shingle firms have been certified by the Department of Commerce as eligible to apply for trade adjustment assistance. Twenty-four of the certified firms have received technical assistance at a labor-equivalent cost to the government of $77,813. None of the firms certified have received any form of direct financial assistance.

Technical assistance is provided on a cost-share basis with the Federal Government's share not to exceed 75 percent. Of the 24 firms provided with technical assistance, eight accounted for 71 percent of the Federal Government total costs. The remaining sixteen firms received, on average, less than $1500 each in government provided technical assistance. No firms have been certified since December 19, 1985, when authority for the trade adjustment assistance program expired.

The Consolidated Budget Reconciliation Act passed Congress in mid-March 1986, and was signed by the President in early April. The legislation includes the "Trade Adjustment Assistance Reform and Extenstion Act of 1986" which extends the technical assistance portion of DOC's trade adjustment program until 1991.

The legislation changes current law in a way that affects the Department of Commerce's Trade Adjustment Assistance Program in two basic areas. First, it eliminates all financial assistance; and secondly, it relaxes eligibility criteria for firm certification.

On March 31, 1986, the Department's Technical Adjustment Assistance Center in Boulder, Colorado closed. This center handled most, if not all, of the shake and shingle certifications and assistance.

A reorganization of all regional Technical Adjustment Assistance Centers is underway within the Department of Commerce at this time.

Attached in appendix A is a list of all shake and shingles firms certified since 1979, including what government expenditures, if any, were provided each firm.

Effectiveness

Trade adjustment assistance thus far provided to the domestic shake and shingle industry by the Department of Commerce seems to have had little effect in bolstering the industry. It is estimated that less than half of the firms receiving technical assistance actually implemented a program to help offset the damage incurred by Canadian imports and that 16 of those firms certified never even applied for assistance. Based upon this evidence, it appears that trade adjustment assistance in the form of technical assistance has not been effective in enhancing the industry's ability to adjust to Canadian competition or ensure its long-term survival.

The Department of Commerce statistics as of mid-1984 show that of the 39 shake and shingle firms certified, 16 never pursued assistance; 18 either went out of business or were on the brink of going out of business; one had potential for improvement; and, four were in good shape financially (see Appendix A).

Section 202 (c)(3): Ability of Domestic Industry to Adjust to Import Competition. "The probable effectiveness of import relief as a means to promote adjustment, the efforts being made or to be implemented by the industry concerned to adjust to import competition, and other considerations relative to the position of the industry in the Nation's economy."

INDUSTRY UTILIZATION OF IMPORT RELIEF

Import relief could provide some temporary assistance to the red cedar shakes and shingles industry in terms of price, output and employment. However, import relief could not by itself improve the long-term prospects of the industry unless combined with the introduction and use of a viable alternative wood product raw material. The development and marketing of such a product could indeed alter the future of the industry, but such a positive result for the red cedar shake and shingle industry now seems unlikely.

The primary result of import relief would be an increase in profits for domestic producers. The inelasticity of supply, (see section 202 (c)(4), coupled with the fact that Canadian producers will remain in the market, precludes more than a modest gain in market share for domestic producers. Further, demand for the products of this industry is likely to decline slightly in the near term.

If import relief were to go into effect, U.S. producers would be virtually certain to raise their prices to the level of the price of imports. Since the future of this industry is clearly in jeopardy because of a dwindling raw material supply and increasing competition from substitute products, producers are bound to maximize short term profits.

There is good reason for increasing concern by producers over products which substitute for the red cedar shakes and shingles. For example, a composite of asphalt and fiber glass, which may be made to look very similar to the wood product, is being aggressively marketed. This product carries a 30 year warranty and has the highest fire retardant rating. There is increasing concern over the ease with which old cedar burns. In Southern California, use of untreated red cedar shakes and shingles is not allowed. Treating with a fire retardant greatly increases cost and still does not result in a high fire retardant rating for the red cedar product. Until now, losses in markets where the untreated wood is not allowed have been pretty much offset by the opening up of new markets, but it is problematic whether this can continue. By and large, the red cedar products are luxury items used on expensive housing. Competition is therefore based on aesthetics and product characteristics more than on price.

Since increased profits would not be earmarked for any specific purpose, but would accrue to individual producers, the uses to which they would be put is conjectural. Some expanding or upgrading of plant and equipment would probably occur, and the rapidly deteriorating debt to equity condition of the industry could be somewhat improved. While upgrading of equipment and retirement of debts would certainly be positive developments, they do not by themselves provide substantial long-term improvement in the position of domestic producers. U.S. plant and equipment is already on a par with that of the Canadians, and in this inherently labor intensive industry, gains from capital improvements are comparatively limited. Financial gains could be quickly reversed with the removal of the tariff and/or with a housing recession. It is fair to say that several years of increased profitability would put producers in a better position to take advantage of any new opportunity to improve their long-term prospects, but would not provide such an opportunity.

The most serious underlying problems for this industry are the lack of raw material supply (only enough red cedar wood for 20 years or so) and the increasing competition from other products.

The best hope is for a new source of supply (alternative wood species) which can be made fire retardant at a marketable price and has the potential for market acceptance. It is unclear at this point how the research is to be done although the petitioner has requested that Federal funding be provided. It is possible, but far from certain, that the U.S. Forest Service would fund such a research project.

Section 202 (c)(4): The Effects on U.S. Consumers. "The Effect of Import Relief on Consumers (including the price and availability of the imported article and the like or directly competitive article produced in the United States) and on Competition in the Domestic Markets for Such Articles."
In accordance with the requirements of Section 201 cases, this paper examines the effects on consumers of granting relief to the shakes and shingles industry. In order to determine such effects, assumptions regading demand and supply relationships in the industry are postulated, and the resulting model is simulated in response to the imposition of different forms of import relief. The specifics of the model and the results of such simulations are described below.

The Model

In modeling the demand for Western red cedar shakes and shingles, domestic and imported goods are assumed to be close, but not perfect substitutes. Factors which may differentiate imports from domestic goods include slight differences in quality, and differences in the size of the orders that can be filled by mills in the different countries. In the model described below, an elasticity of substitution of 6 was assumed. Since empirical estimates of the market demand elasticity for shakes and shingles do not exist, knowledge of the factors influencing the demand for this product must be used to obtain a reasonable estimate. Differences in the interpretation of the relative importance of such factors, however, lead to different estimates of this elasticity. Some argue, for example, that the fact that shakes and shingles tend to be used in more expensive housing implies that demand is relatively inelastic. Others argue that the availability of close substitutes such as asphalt roofing suggests that demand should be relatively elastic. Rather than attempt to resolve these differences at this time, the model was simulated under both assumptions. The elasticity was taken to be -0.8 for the case of inelastic demand and -2.0 for the case of elastic demand. Using a framework developed by Armington (IMF Staff Papers, 1969), the total demand elasticity, the elasticity of substitution between domestic and imported goods, and the 1984 market shares, the own and cross price elasticities were computed to complete the specification of the demand side of the model.

Both domestic and import supply of shakes and shingles are assumed to be relatively inelastic and equal to 0.8 and 0.9 respectively. This assumption is reasonable because red cedar

generally is not harvested separately but instead as part of a stand of timber. Consequently, the supply of red cedar logs is not very responsive to shakes and shingles prices.

The demand and supply relations described above are assumed to conform to the constant elasticity functional forms given.

Domestic demand: $\ln D = a0 + a1 * \ln Pd + a2 * \ln Pm$
Domestic supply: $\ln D = b0 + b1 * \ln Pd$
Import demand: $\ln M = c0 + c1 * \ln Pd + c2 * \ln Pm$
Import supply: $\ln M = c0 + d1 * \ln Pm$
Where
M = quantity of imports
D = quantity of domestic shipments
Pm = price of imports
Pd = price of domestic shipments

The model was solved using 1984 as the base year and then simulated to examine the effects of imposing:

(1) The ITC recommended tariff of 35% on imported Western red cedar shakes and shingles.

(2) A quota which satisfies the industry's request for import relief and which reduces import to the average level over the representative period 1979-83.

The resulting changes in quantities and prices are used to calculate the consumer costs of the proposed import relief measures. Since the estimates themselves depend upon the elasticity assumptions of the model, interpretation of these results should focus upon the direction and relative magnitudes of the estimates rather than upon the absolute numbers. Furthermore, such estimates are based upon the assumption that the import relief will not lead other countries to impose (or refrain from removing) barriers to our exports.

The cost to consumers of saving a job in the shakes and shingles industry under import relief is also given and is calculated using a 1984 estimate of the change in industry employment required per unit of output. However, because granting import relief induces a shift of resources from one sector to another, the changes in industry employment do not indicate a net change in employment for the economy as a whole.

The results:

(1) Effects of imposing a 35% tariff:

The following table gives the percentage changes in prices and quantities and the annual consumer costs associated with imposing a 35% tariff for the cases in

which demand for shakes and shingles is either inelastic or elastic.

Table 1

	Inelastic Demand	Elastic Demand
Prices (% Change)		
Domestic	8.2	3.6
Imports	12.4	7.7
Consumption (% Change)		
Domestic	6.5	2.9
Imports	-15.2	-18.4
Employment		
Temporary Increase in Industry Jobs	97	43
Welfare		
Consumer Costs ($ million)	25.4	14.2
Per Job ($ thousands)	262	334
Producer Surplus ($ million)	6.8	2.9
Tariff Proceeds ($ million)	17.1	10.2
Deadweight Loss ($ million)	1.5	1.1
Import Penetration(%)	59	59

As shown above, the imposition of a 35% tariff is unlikely to lead to the price and output increases desired by the industry. Domestic prices are estimated to rise by only 3 to 9%, while domestic output is expected to increase by at most 7%. In addition, the inelasticity of import supply implies that the effects of the tariff on the quantity and price of imported shakes and shingles is also likely to be small. The results given above support this implication. Under either elasticity assumption, import penetration does not fall below 59%.

The small benefits received by producers as a result of a tariff come at a cost of $14-$26 million dollars to consumers. Although this cost may appear low in comparison to that experienced as a result of granting protection to other industries, these consumer costs represent between 18 and 32% of the total value of domestic skakes and shingles in 1984. In addition, the cost to consumers of preserving a single job in this industry is between $260,000 and $335,000; average annual wages per employee in 1984 were only $14,627. Hence, in comparison to the total value of the product and to the number of jobs saved in the industry, the consumer costs of granting import relief are very high.

(2) Impose a quota on imports equal to 3.097 million squares, the average level of imports over the period 1979-83.

The imposition of a quota which reduces the level of imports to 3.097 million squares will also fail to achieve the price and quantity effects desired by the petitioners. The results are given in Table 2.

Table 2

	Inelastic Demand	Elastic Demand
Prices (% Change)		
Domestic	8.4	3.0
Imports	12.7	6.3
Consumption (% Change)		
Domestic	6.7	2.4
Imports	-15.5	-15.5
Employment		
Temporary Increase in Industry Jobs	99	35
Welfare		
Consumer Costs ($ million)	25.9	11.8
(Per Job ($ thousands)	262	337
Producer Surplus ($ million)	6.9	2.4
Quota Rents ($ million)	17.4	8.6
Deadweight Loss ($ million)	1.6	0.8
Equivalent Tariff (%)	36	28
Import Penetration (%)	59	60

These results indicate that granting import relief in the form of a quota would, at best, increase domestic shipments of shakes and shingles by 7%. If demand is indeed elastic, as many believe, this increase in output is less than 3%. Once again, this small increase in domestic output is achieved at a high annual cost to consumers in comparison with the total value of output and the number jobs actually saved in the industry. The imposition of a quota also implies an additional loss to the U.S. economy because foreigners are able to capture the quota rents.

The conclusion to be drawn from the analysis of the effects of granting import relief to the shakes and shingles industry is clear. The small gains afforded to producers under import relief will be only a small fraction of the cost to consumers. These costs, reflected particularly in the high costs to consumers of saving a single industry job, call into question the efficacy of granting such import relief to this industry.

Table 1: Quota = 3.097 (Million Squares)
(Average Import Level over 1979-83)

	Inelastic Demand	Elastic Demand
Prices (% Change)		
Domestic	8.4	3.0
Imports	12.7	6.3
Consumption (% Change)		
Domestic	6.7	2.4
Imports	-15.5	-15.5
Employment		
Temporary Increase in Industry Jobs	99	35
Welfare		
Consumer Costs ($ million)	25.9	11.8
Consumer Costs per Job Saved ($ thousands)	262	337
Producer Surplus ($ million)	6.9	2.4
Quota Rents ($ million)	17.4	8.6
Deadweight Loss ($ million)	1.6	0.8
Equivalent Tariff (%)	36	28
Import Penetration (%)	59	60

Table 2: Quota on Shakes = 1.952 Million Squares
(Average Import Level Over 1979-1983)

	Inelastic Demand	Elastic Demand
Prices (% Change)		
Domestic	11.8	4.2
Imports	18.2	9.1
Consumption (% Change)		
Domestic	9.4	3.3
Imports	-21.7	-21.7
Employment		
Temporary Increase In Jobs	105	37
Welfare		
Consumer Costs ($ million)	24.5	11.2
Consumer Costs Per Job Saved ($ thousand)	233	299
Producers Surplus ($ million)	6.8	2.3
Quota Rents ($ million)	15.6	7.8
Deadweight Loss ($ million)	2.2	1.1
Equivalent Tariff (%)	55	43
Import Penetration (%)	54	55

Table 3: Quota on Shingles = 1.145 Million Squares
(Average Import Level over 1979-1983)

	Inelastic Demand	Elastic Demand
Prices (% Change)		
Domestic	1.3	0.4
Imports	1.8	0.9
Consumption (% Change)		
Domestic	1.0	0.4
Imports	-2.3	-2.3
Employment		
Temporary Increase in Industry Jobs	4	1
Welfare		
Consumer Costs ($ million)	1.3	0.6
Consumer Costs per Job Saved ($ thousand)	350	452
Producer Surplus ($ million)	0.3	0.1
Quota Rents ($ million)	0.9	0.5
Deadweight Loss ($ million)	0.1	0.01
Equivalent Tariff (%)	4.4	3.5
Import Penetration (%)	70	70

Section 202 (c)(5): "The Effect of import relief on the International Economic Interests of the United States..."

Import relief for the U.S. wood shingles and shakes industry would have a harmful effect on the international economic interests of the United States. Any unilateral action which imposes direct barriers to Canadian exports of wood shingles and shakes to the U.S. would meet with almost certain Canadian retaliation. U.S. restrictions on these imports would primarily harm a region of Canada (British Columbia) which supports closer U.S.-Canadian

economic relations and the reduction of trade barriers through bilateral trade negotiations.

Imposition of the recommended tariff on red cedar wood shingles and shakes could make resolution of the softwood lumber problem with Canada even more difficult. The Canadian Government is likely to view any trade restriction as bad faith and a harbinger of future U.S. action on the lumber issue. Canadian Embassy officials have told us that such unilateral action would be contrary to the Quebec Declaration and could undermine progress in the upcoming free trade negotiations.

In addition to the negative impact on bilateral trade relations, import restrictions would negatively affect the broader global economic interests of the United States. The imposition of a tariff would directly counter our commitment in the OECD to a standstill and rollback of protectionist measures. Other countries might feel less restrained in taking new unilateral measures. The U.S. commitment to open markets would be undermined. Imposition of import relief would subvert our efforts in various international fora to speed up tariff reductions, but would give ammunition to those opposed to a new Multilateral Trade Round, an important Administration foreign policy goal.

Section 202 (c)(6): "The impact on the United States industries and firms as a consequence of any possible modification of duties or other import restrictions which may result from international obligations with respect to compensation..."

The President and Canadian Prime Minister Mulroney agreed at the Quebec Summit "to halt protectionism in cross-border trade in goods and services" and to "reduce and eliminate existing barriers to trade." Toward this end, Canada has proposed negotiation of a comprehensive bilateral trade agreement. We expect negotiations to begin soon after the Congressional review period expires in late April.

Canadians would view any imposition of tariffs on wood shingles and shakes, imports of which come solely from Canada, as completely inconsistent with the letter and spirit of the Quebec declaration. There would be considerable political pressure on the GOC to retaliate.

The recommended remedy is on imports of wood shingles and shakes of western red cedar. Tariffs on red cedar wood shingles and shakes are not bound under the General Agreement on Tariffs and Trade (GATT). Although Canada might retaliate against U.S. products if the President imposes the recommended remedy, there is no GATT justification for such retaliation.

However, it would be difficult for the GOC to accept with equanimity imposition of tariffs on these products since, in its

split decision, half of the ITC commissioners advised against import restrictions. Indeed, a tariff could well shrink the total market share of shakes and shingles since they would be less competitive with alternative roofing materials. Adjustment assistance, as recommended by two commissioners, would seem much less objectionable to the GOC.

As noted earlier, the U.S. and Canada are currently engaged in politically and economically sensitive bilateral discussions concerning lumber trade. The outcome of these discussions will have an important impact on U.S.-Canada bilateral relations in general, and Congressional support for a free trade arrangement with Canada in particular.

We are now engaged in the process of trying to convince the GOC and Canadian public opinion that a change in Canadian timber policies is needed to counter a currently unfair advantage to Canadian lumber mills. We believe some progress can be achieved on this issue in the near future. To be successful, however, we must counter the prevailing opinion in Canada that our motives in the lumber issue are strictly protectionist by showing that changes are called for in order to establish fair trading conditions.

Given the sensitivity of the lumber issue, the imposition of import relief for red cedar shakes and shingles would probably lead the Canadian Government to retaliate with an import restriction on another U.S. product. It could also stiffen Canadian resistance in our bilateral discussions on lumber. In turn, this could erode congressional support for the comprehensive trade negotiations which offer the best prospect of major long term improvement in our bilateral trade and investment relationship.

The Canadian Government has appealed formally to the United States Government not to institute import relief in the case of wood shingles and shakes. Although the Canadians acknowledge that the U.S. wood shake and shingle industry faces severe problems, the Canadian Government believes that temporary import relief does not address the issue. Both the U.S. and Canadian industries face stiff competition from other roofing materials and granting import relief to the U.S. industry will not eliminate this competition. Moreover, they argue, imposition of a tariff will substantially increase the cost to the consumer of the product. In sum, say the Canadians, in light of limited supply and the decreasing demand for the product in the United States and the additional cost to the consumer, it can be argued that adjustment relief rather than an import tariff is the more appropriate remedy for the industry's problem.

Section 202 (c)(7): <u>Geographic Concentration of Imports.</u> "The Geographic Concentration of Imported Products Marketed in the United States."

Imports of Wood Shakes and Shingles

U.S. imports of wood shakes and shingles fell from 3.7 million squares, valued at $162.0 million, in 1978 to 3.2 million squares, valued at $109.1 million, in 1982, and then rose to 4.5 million squares, valued at $182.6 million, in 1984 and 4.9 million squares, valued at $179.4 million, in 1985. Virtually all imports of wood shakes and shingles were from Canada.

The following tabulation shows the share (in percent) of imports of shakes and shingles (by quantity) entering the leading U.S. Customs districts during 1978-85:

	1978	1979	1980	1981	1982	1983	1984	1985
Seattle, WA-----	48.2	56.1	57.8	61.3	63.8	75.7	73.1	71.0
Portland, ME----	5.3	5.5	6.0	6.3	7.1	7.3	7.5	7.7
Ogdensburg, NY--	3.1	3.5	6.5	6.3	6.5	3.0	4.0	5.9
Pembina, ND-----	17.3	10.5	11.8	8.7	6.2	3.3	2.8	4.4
St. Albans, VT--	3.5	1.9	2.5	2.8	4.1	2.6	6.6	4.3
Duluth, MN------	16.6	13.3	10.4	11.0	9.6	4.0	1.9	2.8
Detroit, MI-----	2.1	4.2	1.5	1.5	1.9	2.2	0.9	2.1
All other-------	3.9	5.0	3.5	2.1	0.8	1.9	3.2	1.8
Total-------	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Imports of Western Red Cedar Shakes and Shingles

Imports of western red cedar (wrc) shakes and shingles fell from 3.3 million squares, valued at $151.7 million, in 1978 to 2.6 million squares, valued at $99.1 million, in 1982, and then rose to 4.0 million squares, valued at $156.8 million, in 1985.

Seattle, Washington was the leading U.S. Customs district for imports of wrc shakes and shingles. The following tabulation shows the share (in percent) of imports (by quantity) entering into the Seattle, Washington, and other leading Customs districts during 1978-85.

	1978	1979	1980	1981	1982	1983	1984	1985
Seattle, WA-----	53.7	63.0	67.6	72.3	77.6	88.9	89.2	86.8
Pembina, ND-----	19.4	11.8	13.8	10.3	7.6	3.9	3.3	5.4
Duluth, MN------	18.6	15.0	12.2	13.0	11.7	4.7	2.4	3.5
Detroit, MI-----	0.9	3.7	0.9	0.6	0.4	0.4	0.3	1.3
Ogdensburg, NY--	0.2	0.1	0.0	0.1	0.3	0.1	0.8	1.0
All other-------	7.2	6.4	5.5	3.7	2.4	2.0	4.0	2.0
Total-------	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

As seen in the above tabulation, imports of wrc shakes and shingles into the Seattle, Washington Customs district increased steadily from 1978-84 before tailing off slightly in 1985. Concurrently, imports into Pembina, North Dakota, and Duluth, Minnesota, declined steadily during the period.

Although imports entered primarily into Seattle, it is known that most imports are destined for California (the primary market for shakes) and Texas (the primary market for shingles). As such, statistics on imports by Customs district are not as meaningful as data on distribution of shipments. It is believed that the distribution pattern for imports of wrc shakes and shingles does not differ significantly from the pattern for domestically produced wrc shakes and shingles.

Combined, the four States of California, Texas, Washington, and Oregon accounted for over 60 percent of all wrc shakes and shingles sold in the United States in 1984. The following tabulation shows the percentage distribution of shipments within the United States of all wrc shakes and shingles[4] by leading States during 1978-84 (in percent):

	1978	1979	1980	1981	1982	1983	1984
California------	32.8	36.8	37.7	32.2	28.6	31.6	31.6
Texas----------	15.7	13.3	13.6	15.2	11.5	11.5	10.6
Washington------	10.5	10.7	8.5	9.2	10.9	9.8	8.7
Oregon----------	6.5	7.0	7.8	6.8	6.2	8.2	9.7
All other-------	34.5	32.2	32.5	36.5	42.8	39.0	39.4
Total-------	100.0	100.0	100.0	100.0	100.0	100.0	100.0

As shown, the share of shipments to the traditional markets of California and Texas has declined in recent years, and the share going to Washington and Oregon has remained relatively stable. The share going to smaller shareholding States has increased.

Reported percentage distribution of shipments within the United States of wrc shakes and shingles by U.S. Census regions[5] indicates that no major shifts have occurred since 1978, as shown in the following tabulation (in percent):

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[4]Based on data supplied by the Red Cedar Shingle & Handsplit Shake Bureau (an association with both Canadian and U.S. members).
[5]Based on data supplied by the Red Cedar Shingle & Handsplit Shake Bureau (an association with both Canadian and U.S. members).

	1978	1979	1980	1981	1982	1983	1984
West:							
Pacific-------	50.5	55.8	54.8	49.0	46.6	50.8	51.0
Mountain------	8.0	7.9	6.4	8.0	10.3	8.6	9.8
Midwest---------	16.0	13.8	13.2	15.3	14.9	14.9	14.0
Northeast-------	3.7	3.2	4.3	4.0	5.7	5.0	4.6
South-----------	21.7	19.3	21.3	23.7	22.4	20.8	20.6
Total-------	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Imports of Northern White Cedar Shingles

Imports of northern white cedar shingles rose from 409,590 squares, valued at $10.3 million, in 1978 to 887,250 squares, valued at $22.6 million, in 1985. Such imports have historically entered, and presumably are marketed in, the northeastern U.S. Customs districts. The following tabulation shows the share (in percent) of imports (by quantity) by leading U.S. Customs district, during 1978-85:

	1978	1979	1980	1981	1982	1983	1984	1985
Portland, ME----	47.7	49.2	40.9	40.7	39.0	49.1	41.2	42.4
Ogdensbury, NY--	26.0	30.2	44.3	40.0	35.2	20.0	18.7	27.7
St. Albens, VT--	9.8	8.8	8.3	11.8	16.2	15.8	25.4	19.7
Detroit, MI-----	11.5	8.3	4.6	6.2	8.8	12.6	3.6	5.9
Buffalo, NY-----	0.4	2.2	1.1	0.6	0.3	2.1	10.0	3.9
All other-----	4.6	1.3	0.8	0.7	0.5	0.4	1.1	0.4
Total-------	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Section 202 (c)(8): The United States Market as a Focal Point for World Exports. "The Extent to which the United States is the focal point for exports of such article by reason of restraints on exports of such article to, or on imports of such article into, third country markets."

There is no indication that other countries have programs restraining trade in wood shingles and shakes. On the contrary, investigations indicate that the United States and Canada are the only countries in the world that have large commercial resources of old-growth western red cedar, from which most shakes and shingles are produced. Countries other than the United States and Canada may produce shakes and shingles for domestic consumption and exportation from other species, but the quantity of such production is believed to be insignificant. There is no significant trade between other countries in wood shingles and shakes. In 1984 and 1985, Canada exported to countries other than the United States approximately 1.5 percent in volume and 2.0 percent in value of its total exports of wood shingles and shakes. Canada supplies virtually all exports of this product to the U.S.

Section 202 (c)(9): Cost to Taxpayers, Communities and Workers. "The economic and social costs which would be incurred by taxpayers, communities, and workers, if import relief were or were not provided."

The effect of import relief not being granted to the shakes and shingles industry can be measured by its effect on taxpayers, communities, and workers.

Taxpayers - The effect of no import relief on taxpayers examines the burdens of 1) Unemployment compensation, 2) Adjustment assistance, and 3) loss of tax revenues.

(1) Unemployment Compensation

Using the latest average unemployment benefit figures,[6] it is estimated that approximately $207,000 in unemployment compensation would be paid out over a five year period. For some workers located in areas where there are few alternative employment opportunities (small towns, rural areas) the period of unemployment, hence the amount of compensation paid out, may be higher. However, available information on the location of shake and shingle mills (and the impossibility of guessing which mills would close) does not allow one to make a firm conclusion as to the ease of finding alternative employment.

(2) Adjustment Assistance

The Trade Adjustment Assistance (TAA) program will end as of September 30, 1991. In addition, the President's budget provides funds primarily for job training under the Job Training Partnership Act; shake and shingle workers could benefit from this program at least through 1986.

If import relief is not granted and domestic production of shakes and shingles continues to decline, federal, state, and local governments would lose tax revenue from manufacturers which operate at a loss or at depressed profit levels, or who cease production altogether. However, it is possible that increased profits by the most competitive domestic manufacturers (as a result of less domestic competition) might offset some or all of this decline. The largest loss of tax revenue would be attributable to the continued decline in employment in the shakes and shingles industry. The assumption that an additional 97 jobs would be lost by 1989 would mean a decline in federal and state

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[6]Using CEA's estimate of employment increase achieved with the ITC's majority recommendation of a 35 percent tariff for 5 years (based on YE January 1985 weighted average unemployment benefits) in the three major western red cedar shake and shingle producing states ($134.33 per week collected for 15.9 weeks).

personal income tax revenues. (However, please note that the State of Washington does not have a personal income tax.) Other state and local revenues such as sales taxes would also be expected to decline, due to decreased purchasing power of unemployed workers.

Communities

The financial and social costs to the communities of no import relief is dependent upon the concentration of the shake and shingles industry in each particular community. The state of Washington would appear to be hurt the most since it has over 80 percent of the jobs in the industry. In the case of the actual demise of the domestic shake and shingle industry, the disruption of the communities in the peninsular region of Washington would be great unless they are able to attract new industries. The 1985 unemployment rate of 12.1 percent does not suggest that other jobs are readily available for displaced workers.

Workers

It is difficult to assess the effect of not granting import relief. The Department of Labor estimated that employment in the industry would decline by almost 800 workers between 1984 and 1989, even if relief was granted to the industry. ITC employment data comparing the first three quarters of 1984 and 1985 shows a decline in total employment, of 574 workers while the Department of Labor estimated a decline of 208 workers for full year 1985, which suggests that the Department of Labor's calculations are conservative.

CEA calculations estimated that the ITC proposed remedy would preserve a maximum of 97 jobs in the first tariff year. All these jobs would of course not be expected to be maintained over the proposed relief period given the historical decline in employment experienced by the industry between 1978 and 1984 and given the proposed remedy. Given this scenario, employment in the industry would be below current employment levels at the end of the relief period.

The primary effect on unemployed or underemployed workers is a loss in income, though this loss is mitigated somewhat in the short run by unemployment compensation, welfare payments and adjustment assistance. In the longer run, workers may suffer a permanent drop in income levels if they find reemployment at a lower wage. In addition, workers and their families may suffer unquantifiable losses, such as the psychological stress of unemployment itself, or the stress of having to accept a less interesting new job (perhaps in a different locality). Some workers--especially older ones unwilling or unable to learn new skills--may become permanently unemployed (i.e., forced into
A rough estimate of the gross cost of unemployment to individual

shake and shingle workers who lose their jobs is almost $6,000 based on the western red cedar shake and shingle industry's average annual earnings minus maximum number of weeks a worker could receive the average State unemployment compensation and TAA payments.

Table 1.--Wood shakes and shingles: U.S. imports for consumption, by Customs district, 1978-85

Customs district	1978	1979	1980	1981	1982	1983	1984	1985
	Quantity (1,000 squares)							
Seattle, WA	1,793	2,205	2,207	2,090	2,037	2,857	3,270	3,467
Portland, ME	197	215	228	216	227	275	334	376
Ogdensburg, NY	114	136	248	214	207	114	181	287
Pembina, ND	643	411	451	297	119	126	127	215
St. Albans, VT	131	75	96	96	130	96	295	210
Duluth, MN	617	525	398	375	308	152	87	138
Detroit, MI	78	164	56	51	61	84	41	103
All other	146	203	136	73	105	67	138	86
Total	3,719	3,934	3,820	3,412	3,194	3,771	4,473	4,882
	Value (1,000 dollars)							
Seattle, WA	81,842	103,049	96,603	89,653	79,389	131,044	149,881	140,280
Portland, ME	6,673	6,812	6,773	6,912	6,937	9,073	11,886	13,057
Ogdensburg, NY	1,633	1,581	1,739	1,659	1,495	1,402	3,364	5,766
Pembina, ND	33,322	19,657	20,093	12,784	7,217	5,109	5,161	7,891
St. Albans, VT	3,536	2,347	2,790	2,281	2,510	2,582	4,337	5,215
Duluth, MN	28,571	23,413	16,249	15,851	10,627	6,200	4,279	5,408
Detroit, MI	655	834	546	542	398	455	384	357
All other	5,731	6,856	5,455	2,592	512	2,285	3,283	1,434
Total	161,963	164,549	149,702	132,274	109,085	158,150	182,575	179,408
	Unit value (per square)							
Seattle, WA	45.64	46.73	43.76	42.89	38.98	45.87	45.84	40.47
Portland, ME	33.94	31.66	29.70	32.07	30.50	32.96	35.58	34.71
Ogdensburg, NY	14.29	11.64	7.00	7.76	7.21	12.24	18.63	20.12
Pembina, ND	51.81	47.78	44.59	43.08	36.26	40.71	40.74	36.67
St. Albans, VT	26.93	31.33	29.00	23.71	19.34	26.81	14.69	24.81
Duluth, MN	46.29	44.62	40.83	42.27	34.49	40.70	49.43	39.12
Detroit, MI	8.38	5.08	9.81	10.71	6.48	5.38	9.39	3.46
All other	39.25	33.77	40.11	35.51	4.88	34.10	23.79	16.67
Average	43.55	41.83	39.19	38.77	34.16	41.94	40.81	36.75

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Table 2.--Western red cedar shakes and shingles: U.S. imports for consumption, by Customs district, 1978-85

Customs district	1978	1979	1980	1981	1982	1983	1984	1985
	Quantity (1,000 squares)							
Seattle, WA	1,777	2,202	2,206	2,088	2,036	2,856	3,266	3,465
Pembina, ND	643	411	450	297	199	126	122	214
Duluth, MN	617	525	398	375	308	152	87	138
Detroit, MI	31	128	30	18	11	14	12	51
Ogdensburg, NY	8	4	2	4	7	3	29	41
All other	234	229	178	107	63	63	147	85
Total	3,310	3,499	3,264	2,889	2,624	3,214	3,663	3,994
	Value (1,000 dollars)							
Seattle, WA	81,262	102,913	96,509	89,647	79,354	131,001	149,671	140,224
Pembina, ND	33,322	19,656	20,090	12,784	7,217	5,109	4,963	7,823
Duluth, MN	28,571	23,413	16,249	15,851	10,627	6,200	4,279	5,402
Detroit, MI	348	643	388	229	143	154	130	203
Ogdensburg, NY	64	34	26	63	80	24	806	965
All other	8,123	7,924	6,414	3,624	1,687	2,444	2,668	2,231
Total	151,690	154,583	139,676	122,198	99,108	144,932	162,517	156,848
	Unit value (per square)							
Seattle, WA	45.73	46.73	43.76	42.94	38.97	45.86	45.83	40.46
Pembina, ND	51.81	47.78	44.60	43.08	36.26	40.71	40.56	36.54
Duluth, MN	46.29	44.62	40.83	42.27	34.49	40.70	49.43	39.10
Detroit, MI	11.20	5.02	12.90	12.63	12.78	10.84	11.06	3.97
Ogdensburg, NY	8.01	8.80	15.83	15.46	11.53	8.40	28.09	23.60
All other	34.71	34.75	36.03	33.87	26.78	38.79	18.15	26.25
Average	45.83	44.20	42.80	42.30	37.77	45.10	44.37	39.27

Table 3.--Northern white cedar shingles: U.S. imports for consumption, by Customs district, 1978-85

Customs district	1978	1979	1980	1981	1982	1983	1984	1985
	Quantity (1,000 squares)							
Portland, ME	195	215	228	213	222	274	334	376
Ogdensburg, NY	106	132	247	210	200	112	152	246
St. Albans, VT	40	38	46	62	92	88	206	175
Detroit, MI	47	36	26	32	50	70	29	52
Buffalo, NY	1	10	6	3	2	12	81	34
All other	21	5	3	4	3	1	9	4
Total	410	436	556	524	569	557	811	887
	Value (1,000 dollars)							
Portland, ME	6,630	6,792	6,761	6,834	6,836	9,019	11,886	13,047
Ogdensburg, NY	1,570	1,546	1,712	1,596	1,416	1,377	2,559	4,801
St. Albans, VT	1,018	1,069	964	1,234	1,349	2,296	3,601	3,992
Detroit, MI	307	191	158	313	255	301	254	154
Buffalo, NY	62	158	226	83	51	177	1,332	348
All other	686	210	205	34	70	48	426	218
Total	10,273	9,966	10,026	10,026	9,977	13,218	20,058	22,560
	Unit value (per square)							
Portland, ME	33.96	31.66	29.69	32.10	30.74	32.96	35.58	34.71
Ogdensburg, NY	14.76	11.73	6.94	7.61	7.06	12.34	16.84	19.54
St. Albans, VT	25.27	27.81	20.81	19.92	14.64	26.12	17.46	22.78
Detroit, MI	6.51	5.31	6.19	9.64	5.08	4.28	8.71	2.95
Buffalo, NY	42.72	16.13	36.30	25.26	25.45	15.01	16.43	10.15
All other	32.67	42.00	68.33	8.50	23.33	48.00	47.33	54.50
Average	25.08	22.85	18.02	19.25	17.52	23.71	24.74	25.43

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APPENDIX A

Wood Shakes and Shingles
Certification Calendar and Technical Assistance

Name & Location of Firm	Petition Received	Determination	Technical Assistance	Code*
Big John's Shingle Mills, Inc. Caribou, Maine	8/21/79	Certified: 10/24/79	$526	-
Midway Shake Company Tillamook, Oregon	12/20/80	Certified: 2/15/80	$6,222	D
North Cross Cedar, Inc. Lyman, Washington	2/4/80	4/9/80	$1,000	A
Gold Medal Cedar Prods. Tillamook, Oregon	2/12/80	Certified: 4/24/80	$424	D
Black Mountain Cedar Products, Inc. Bonners Ferry, Idaho	2/13/80	Certified: 4/24/80	None	-
Praire Cedar Products Inc. Beaver, Washington	2/14/80	Certified: 4/30/80	$12,371	A
Oakville Shake Company Inc. Oakville, Washington	2/19/80	Certified: 4/25/80	$8,547	B
Gunter Shake, Inc. Forks, Washington	2/19/80	Certified: 2/19/80	$2,450	D
Grizzly Shake Company Inc. Forks, Washington	2/21/80	Certified: 4/28/80	None	-
C&C Cedar Products, Inc. Lebanon, Oregon	2/21/80	Certified: 4/28/80	$3,499	D
Northwest Cedar, Inc. Sedro Woolley, Washington	2/25/80	Certified: 5/2/80	None	-
Ford Cedar Products, Inc. Sultan, Washington	3/12/80 12/26/80	Certified: 2/28/80	$665	D
Powell/Adamson Enterprises, Inc. McCleary, Washington	5/20/80	Certified: 7/28/80	$368	D

*See Code Definitions on page 4.

Name & Location of Firm	Petition Received	Determination	Technical Assistance	Code*
Forest Ridge Company Copalis Crossing, Washington	6/2/80	Certified: 8/8/80	$869	D
Quinault Pacific Corp. Shelton, Washington	6/9/80	Certified 8/13/80	$4,117	D
Breaker Shake Hoquiam, Washington	6/2/80	Certified: 8/8/80	$718	D
Harbor Manufacturing, Hoquiam, Washington	6/3/80	Certified: 8/8/80	$3,022	D
Moonlight Shake Mill Pacific Beach, Wash.	6/5/80	Certified: 8/12/80	None	-
Son Cedar Products, Inc. Darrington, Washington	6/5/80	Certified: 8/11/80	$1,722	D
Shoestring Shake Co. Pe Ell, Washington	6/11/80	Certified: 8/18/80	None	-
Daniels Cedar Prods., Inc. Aberdeen, Wash.	6/13/80	Certified: 8/19/80	None	-
Pacific Logging Co. Humptulips, Wash.	6/27/80	Certified: 9/4/80	$634	D
Trinity Shake Co. Forks, Washington	7/10/80	Certified: 9/22/80	None	-
Northwest Shake Co. Hoquiam, Washington	7/14/80	Certified: 9/22/80	None	-
Taylor Cedar Products Copalis Crossing, Wash.	7/25/80	Certified: 9/30/80	$950	D
Montesano Cedar Products Montesano, Washington	9/9/80	Certified: 11/14/80	$2,758	D
Robertson Shake, Inc. Chehalis, Washington	10/14/80	Certified: 12/19/80	$1,320	A

*See Code Definitions on page 4.

Name & Location of Firm	Petition Received	Determination	Technical Assistance	Code*
D&L Shake & Ridge Company Hoquiam, Washington	10/28/80	Certified: 1/19/81	$5,302	D
D&R Cedar Products, Inc. Forks, Washington	12/22/80	Certified: 2/26/80	None	-
North Hoquiam Cedar Products, Inc. Hoquiam, Washington	7/23/80	Certified: 9/6/85	None	-
Grays Harbor Shake Hoquiam, Washington	-	Certified: 7/8/80	$7,247	D
Mt. Baker Cedar Port Angeles, WA	-	Certified: 4/3/81	$6,173	D
Newton Cedar Products Forks, WA	-	Certified: 5/22/80	$5,302	D
Suprene Cedar Concrete, WA	-	Certified: 7/30/81	$1,607	A
T&J Cedar Raymond, WA	-	Certified: 9/22/80	$8,783	E
Southeastern Cedar Kitchikan, Ak.	-	Certified: 2/12/82	None	-
B&P Shake Co. Pe Ell, WA.	-	Certified: 8/12/81	None	-
North Shore Cedar Hoquiam, WA	-	Certified: 8/12/81	None	-
Saginaw Shingle Aberdeen, Wa.	-	Certified: 8/7/81	None	-

*See Code Definitions on page 4.

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Code Definitions

*The Department of Commerce has a coding system to indentify if the Technical Adjustment Assistance Center (TAAC) did not complete a diagnostic evaluation of said firm. The coding system goes from A through E as follows:

A. Firm decided not to continue.

B. Firm decided not to cost share.

C. Management change at firm.

D. TAAC discouraged firm due to lack of viability and no prospect of developing a viable strategy.

E. Other: Sold; merged with another; liquidated.

IPRG - 5/1

Wooden Shakes & Shingles

★ EPC - Wed 5/14

2 o/cases B4 ITC:

	ITC	60 DAYS	
chilled apple juice	6/13		8/13
metal case casting	6/2		8/2
fork lift	7/17		9/17

Opts
1 - NO
2 - ITC (35%)
3 - 5 yr ITC w/ review 2 yrs
4 - 5 yr digression 35 → 8%
5 - expedited TAA

HPG. Who would complain if "yes"
potential: Canada retal? } but, not o/spoken
build assn, distrib }

- used high price homes: $200 on $150,000 house

CEA (cost/job very high)

M.S. part of prob: lack access Can logs ⇒ export restrict
Q: if Δ, how much util

P. Murphy * Can neg not maj factor – dec, either way unlikely to affect

Tom M. prob w/ ind:
Can stumpage (drive price down)
why not keep ind, no turn around, not better
\$200K/job

M.S. don't know where Packwood/Bonker et al would be

π 2½ yrs

3 ¢ 4

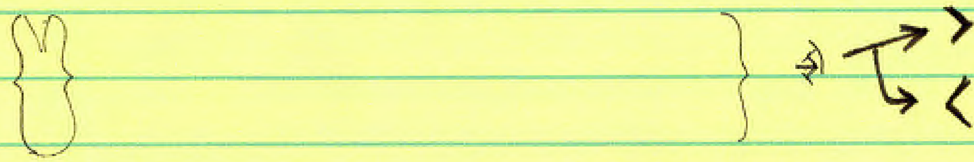
or

3 ¢ 2

3^{30} Steve Brent Sen

- Farrar's off

House hearing next mo.



DEPUTY UNITED STATES TRADE REPRESENTATIVE
EXECUTIVE OFFICE OF THE PRESIDENT
WASHINGTON, D.C. 20506
202-395-5114

UNCLASSIFIED WITH
CONFIDENTIAL ATTACHMENT

May 9, 1986

MEMORANDUM

TO: MEMBERS OF THE TRADE POLICY REVIEW GROUP

FROM: MICHAEL B. SMITH, Chairman

SUBJECT: Paper on Shakes and Shingles 201 Case

Attached for your review is a paper to be submitted for next week's EPC meeting on shakes and shingles.

Please direct your clearance and comments to Marian Barell (395-7271) by COB today.

Attachment

UNCLASSIFIED WITH
CONFIDENTIAL ATTACHMENT

May 7, 1986

Section 201 Shakes and Shingles Case

Issue: Should the President grant import relief to the U.S. western red cedar shakes and shingles industry and, if so, what type of relief should he grant?

Background

. On March 25, 1986, U.S. International Trade Commission (ITC), by 4-2 vote, advised the President that increased imports are seriously injuring U.S. wood shake and shingle industry.

. By 3-3 vote, recommended imposition of a 35 percent tariff for five years on imports of western red cedar (wrc) shakes and shingles.

. Trade Act of 1974 requires that the President decide within 60 days of receiving ITC's report, or by May 24:

(1) whether to grant import relief; and

(2) if relief is granted, what form and level are required.

. Law requires him to determine whether relief would be in national economic interest.

. Should the President choose no relief, or an approach different from that recommended by ITC, he would be required to set forth reasons for his decision and to explain steps he is taking, beyond expedited adjustment assistance, to help industry overcome serious injury. Congress may overide his decision and implement ITC decision by passing a joint resolution; the President could, however, veto this resolution.

Basic Facts

. Health of U.S. wrc shakes and shingles industry generally declined over 1978-1984 period.

(1) U.S. consumption fell from 7.5 to 5.7 million squares ("square" refers to quantity required to cover 100 square feet of surface area).

(2) Production dropped almost steadily from 4.3 to 2.1 million squares.

(3) Number of all shake and shingle establishments estimated to have fallen from 445 firms to 255 firms by June of 1985.

(4) Employment declined from 4,531 to 2,146.

(5) Capacity utilization fell from 54 percent in 1980 to 44

percent during first nine months of 1985.

(6) Only in area of net income did U.S. firms show improvement, i.e., from 5.3 percent net loss from net sales in 1982 to 3.4 percent net income in first nine months of 1985.

. Imports of wrc shakes and shingles -- virtually all of which come from Canada -- increased over period.

(1) On volume basis, imports rose from 3.3 million squares in 1980 to nearly 3.7 million squares in 1984.

(2) On value basis, imports grew from $139.7 million to $162.5 million.

(2) Ratio of imports of all shakes and shingles (majority of which are wrc) to consumption grew from 40 percent in 1978 to 73 percent during first nine months of 1985.

. Industry faces number of difficulties in addition to those posed by import competition.

(1) Saddled with declining resource base. Estimated that, at current harvesting levels, U.S. old growth red cedar will be available only until 2006. Were U.S. harvesting to rise, resource base would fall even more rapidly. By contrast, Canada expects to have supplies into twenty-second century.

(2) Canadian restrictions on log exports have exacerbated inelastic supply situation here and increased U.S. raw material costs relative to those in Canada.

(3) Substitute siding and roofing materials, e.g., asphalt, tile and fiberglas, already account for 90 percent of consumption and could take more of market were tariffs to lead to appreciably higher prices.

(4) Anti-flammability treatment requirements have nearly doubled cost of a square of wrc shakes and shingles (i.e., from $40 to $70), further reducing their competitiveness.

Major Policy Objectives

. Law requires the President to make his decision by considering certain statutory criteria, which are broader than those ITC considers in determining whether to provide import relief. Most important economic criteria include:

1. Adjustment. In this case, can import relief allow U.S. firms to adjust to greater international competitiveness? Would relief encourage remaining U.S. firms -- now small, family-run operations -- to pool resources for vitally-needed research into alternative raw materials and improved anti-flammability treatments? To what extent would U.S. shake and shingle

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employment increase? To what extent would a price increase for wrc shakes and shingles encourage consumers to switch to alternative roofing and siding materials, thereby hastening industry's demise?

2. Domestic economic costs. To what extent would import relief impose costs on: (a) U.S. consumers; (b) other U.S. industries, because Canada could retaliate (despite the fact that current zero tariff on shakes and shingles is unbound in GATT); and (c) U.S. economy because import restrictions will make it less efficient?

3. International economic costs. To what extent would import relief hurt Canada?

Agencies considered range of import relief options, including tariffs, quotas, tariff-quotas and orderly marketing agreements. The majority view was that there is little economic justification for granting relief.

However, some agencies found that relief would be warranted if, (1) industry channels increased profits generated from tariff relief (and hence higher prices) into research for alternative wood species raw materials and improved anti-flammability; (2) this research results in more competitive product with nearly limitless raw material bases; or (3) USG is able to negotiate log supply access agreement with Canada.

Finally, there was consensus that EPC might want to consider certain political criteria:

1. Risk of an alternative, less desirable, legislative solution. Given that this is first 201 case since nonrubber footwear, waht is risk that rejection of relief for wrc shakes and shingles will encourage passage of pending legislation reducing presidential discretion under 201?

2. Other action involving wood products. Would granting relief complicate efforts to find bilateral solution to lumber trade problem (i.e., low stumpage pricing) with Canada? Would such action improve or harm efforts to eliminate Canadian export controls on logs? Would denial of import relief encourage Congressional efforts to include natural resource pricing as countervailable subsidy?

Policy Options

. TPRG reviewed a number of options and selected three for EPC consideration. Relief options were narrowed to tariffs with only variations being possible duration and extent of degressivity.

Option 1: Provide no import relief.

Advantages

- o No cost to consumers.
- o No threat of retaliation from Canada.
- o Consistent with U.S. pledge regarding standstill and rollback of protectionist measures.
- o Consistent with spirit of 201, which envisions import relief as means of promoting adjustment rather than encouraging maintenance of noncompetitive industries.

Option 2: Adopt ITC majority recommendation of 35 percent tariff for five years on imports of western red cedar shingles and shakes.

Advantages

- o Would serve as proof that USG is committed to viability of Section 201 relief as means of affording temporary safeguard protection, particularly following negative determination for footwear.
- o Would give us more time to assess industry's ability to use new methods and alternative materials to achieve international competitiveness.
- o Would give U.S. shake and shingle industry "cushion" while Government considers action on important cause of industry's competitive problem, i.e., access to unprocessed Canadian logs.

  -- Industry would support immediate termination of relief were Canadian log export restrictions removed.
- o Would mean less unemployment initially. Estimated that approximately 40-100 jobs would be preserved in first tariff year. (However, employment in industry would be below current employment levels at end of relief period.)
- o Initially, domestic production may increase between 3 and 7 percent.
- o Initially, domestic prices may increase between 4 and 9 percent, to the benefit of industry.
- o Tariff is unbound under GATT; therefore United States would owe no compensation to trading partners in event of duty increase.

Option 3: Adopt five-year tariff, but have the President direct the USTR to request that ITC conduct review of industry's adjustment efforts after 30 months so that he can determine whether continuation of import relief is in national economic interest. If relief is continued,

adopt degressive tariff, i.e., to 20 percent after 30 months and 8 percent in months 54-60.

Advantages

- Same as in option 2 (although initial employment, production and price gains would be lost more rapidly as tariff levels declined).
- Would be consistent with our normal practice of degressivity under Section 201.
- Industry could support degressive tariff of this nature.
- Might evoke less opposition from Canada than straight-line tariff.
- Would create less consumer costs in months 30-60 than Option 2.
- Could spur greater industry effort toward adjustment.

  -- Industry has committed to spending $200,000 per year for each year of relief for research.

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S. Bruce Wilson OADR
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Shake / Shingle 201

PRIME MINISTER · PREMIER MINISTRE

May 23, 1986

Dear Mr. President,

I want to convey to you the profound disappointment of my government at the action you announced yesterday regarding softwood shingles and shakes. The imposition of a 35% tariff is a punitive measure against Canadian products. This unjustifiable action is all the more appalling in the context of freer trade negotiations between our two countries having been officially initiated this week.

This American initiative is pure protectionism, the precise thing you and I pledged, in Quebec and Washington, we would seek to avoid. Canada is now placed in the position of being forced to consider an appropriate response.

I deeply regret this action by the U.S. Administration.

Yours sincerely,

Brian Mulroney