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## Epilogue

# The Current State of Developments on Wheat Marketing Arrangements

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At the time of writing this in June 1984 the draft wheat marketing arrangements are nearing what is likely to be their final form.

AAC in February announced decisions in a number of areas. The decision if implemented which will produce the greatest change from the present policy was to introduce a Permit System for domestic stockfeed wheat sales between grower and end-user without requiring delivery to the AWB and without any constraints on the price negotiated between grower and buyer. Permit wheat will not be underwritten although the underwriting provisions for wheat delivered to the AWB will also put a floor in the market for this wheat. Permits should be readily available but the AWB will retain some discretionary powers to limit the issue of permits in extraordinary circumstances such as a severe drought. AAC also decided the following:

- (i) The AWB will retain full control of the export market and have its powers to trade in futures slightly extended rather than diminished. It will have its objectives, functions and powers quite explicitly stated in legislation.
- (ii) The high first advance to growers will be retained but no changes will be made to the pooling system for wheat delivered to the AWB. More information will be given to growers however about the costs of financing the first advance.
- (iii) The single remuneration agreement between the AWB and the BHA's will be replaced by separate agreements between each BHA and the AWB and will operate for the same period as the wheat marketing legislation.

While agreeing in principle to the retention of underwriting, the Tasmanian freight subsidy, and administrative determination of the human consumption price, no decisions were reached on their calculation or on the financing of the freight subsidy.

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Negotiations since February have not changed the basic structure of the proposed Permit System but have concerned the operational details. However some discussion has taken place surrounding the degree of discretionary power that the AWB should have to withhold permits. A somewhat lower level of underwriting is likely to be agreed upon and the HCP is likely to be set for three monthly periods based on a moving average of AWB forward export price quotes for ASW wheat plus a small margin, expressed in absolute dollar terms, to cover additional services provided to domestic millers compared with export customers. The position on the Tasmanian freight subsidy is unknown at this stage.

The Federal Minister for Primary Industry has also moved on the issue of AWB membership and proposed a reduction in the size of the Board from fourteen to eleven, an increase in the number of members with special qualifications but retention of a grower majority.

## A Discussion Point

In the discussion which followed the Watson and Ryan papers at the Conference, the speakers were each asked to forecast the wheat marketing system likely to be in operation in five or ten years time. Ryan and Wearing both foresaw, or at least hoped for, an efficient AWB operating in competition with private traders on the domestic and perhaps even the export market in selling Australian wheat. Watson suggested however that it seemed hard to believe that growers would allow the AWB as a statutory authority to operate completely in this way or alternatively to be sold off to world grain traders. They made no comments on the way the BHAs or railways would operate in this future marketing system.

## Some Personal Observations

Ryan rightly emphasises that the relevant issue is not what has happened in the past but what should be done in the future.<sup>1</sup> Viewed as an optimal control problem, what are the optimum time paths of the policy variables and institutions?<sup>2</sup>

There is an increasing recognition amongst economists that the old neo-classical, market failure paradigm, while providing useful insights, has not served us particularly well in making policy prescriptions. A number of bodies of theory have developed in recent years on government failure including that on regulation (e.g. Stigler 1971) and rent seeking (e.g. Tullock 1967; Krueger 1974; Buchanan *et al* 1981). Rausser (1982) reviews this literature and proposes an operational paradigm integrating the market and government failure approaches. His purpose is to allow the generation and testing of hypotheses

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<sup>1</sup> However I do not agree with Ryan's implications that *ex-post* analyses such as that made by Longworth and Knopke (1982), or Watson's conclusions based upon them, are irrelevant.

<sup>2</sup>The desirability of taking such a dynamic approach to policy prescription has been argued by Freebairn and Rausser (1974). They illustrate the use of an adoptive control model using an Australian wheat marketing policy problem as an example.

about behaviour in policy development and eventually the improvement of policy prescriptions. In my view the development of such a paradigm is vital and yet it will take many research-man-years to achieve it. In the meantime, for policy prescriptions, we can put to use the analytical framework Rausser constructs and the bodies of theory he draws upon.

Rausser's proposed framework is based upon three premises:

- (a) political and economic markets are not separable;
- (b) pure transfers (i.e. without distortionary effects on resource allocation) do not exist: and
- (c) we live in a second-best world.<sup>3</sup> (p. 823).

Once stated the truth of each of those premises may be obvious to many but none of our paradigms take them into account.

Two things would, amongst others I think, improve our ability to prescribe "near" second-best policies. Firstly, many quantitative studies are needed in the wheat industry of the costs of regulations and of rent-seeking behaviour. Secondly, more time and resources need to be expended upon isolating such second-best policies.

In regard to the first point the BAE's study which estimated a \$68 million saving from deregulation of the domestic market was a start in the right direction (BAE 1983) but much more quantitative work on potential efficiency gains is needed.<sup>4</sup> Watson's proposed study of the distribution of rents to farmers in different regions needs to be broadened, in my view, to the distribution amongst all market participants. After all, we know very little about why wheatgrowers' organizations have been prepared to accept the changes to the wheat market system that they have.<sup>5</sup> It would be foolish, I think, to believe the current moves towards deregulation are in any way an inevitable or natural process which can be sustained by qualitative rhetoric about the efficiency gains from competitive markets—no matter how desirable

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<sup>3</sup> In the specific sense of the welfare economic term as used by Lipsey and Lancaster (1956 7).

<sup>4</sup> Its impact was unfortunately (yet understandably) marred by some errors of logic and calculations. For example the \$68 m. figure is partly based upon a difference between road and rail freight rates to Sydney from grain growing regions with road cheaper. The road transport costs are based upon some single period quotations of costs when in fact road transport rates vary considerably. In N.S.W. where metropolitan mills are not obliged to take delivery by rail, any long-term differential in favour of road could be expected to have led to substitution of road for rail. This has not happened.

<sup>5</sup> Certainly we have a good idea why specific "policy disequilibrium situations" (Rausser 1982, p. 827) have arisen in wheat marketing over the last five years. The HCP formula has produced a run of prices which nobody has liked (Johnston *et al.* 1983, pp. 31-35). The grower-to-buyer arrangements have been little used, because of high BHA charges ("for wheat not received") and administratively imposed delays and costs—we think (AWB 1982). We are also getting a rapidly developing picture of why the proposed new administered HCP formula is being supported rather than a price determined by the AWB and why the Permit System is receiving such strong support. However, it would have greatly assisted the introduction of a Permit System if the concept could have been defined and its ramifications and acceptability investigated twelve months earlier. This would have avoided the current rush to develop operational and enforcement procedures with its greater danger of design errors.

and correct the deregulation and the rhetoric may be.<sup>6</sup> The adjustments to be made in the face of competition under the Permit System or fuller deregulation will produce short-run discomfort and pain which will have their inevitable political repercussions. As the bad press starts, good quantitative information will be needed to give a true picture of the market participants who are losers because of the changes, the extent of their losses, the time for which they are likely to persist plus the same information on the benefit/gainers side. Otherwise the trend to deregulation could be replaced with a trend in the opposite direction due to a mixture of fashion, short memories and ignorance of the real gains and losses.

In regard to the second point regarding investigation of second-best policies, Rausser points out that we continue to perform analyses as though a first-best world were achievable. He argues that this approach is hardly of social value. On wheat marketing and other areas the IAC has tended to make recommendations for second-best solutions which take into account various technical constraints but only a very limited set of institutional/political constraints. For example, the possibility of some State Wheat Boards being reactivated if the export monopoly of the AWB were eliminated was taken into account by the IAC. On the other hand, alternative direct sales systems on the domestic market under various degrees of AWB control were not laid out as options.<sup>7</sup> It would be desirable for the IAC to work towards this type of reporting, giving the deadweight losses and distributional effects of diverting from its preferred option. This may occur, given the Government's response to the Uhrig Report (1984).

It would also be helpful if more time were left for the development of second-best policies subsequent to presentation of the IAC's report. The greater the number of technical, institutional and political constraints considered in developing policy the more difficult it becomes to unravel the effects and

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<sup>6</sup> While economists have helped smooth, guide and perhaps accelerate the adjustment process a little, we would be deluding ourselves if we took the major credit. The policy disequilibrium created by growing illegal sales and the annoyance of large stockfeed manufacturers with this; possibilities of section 92 challenges to the AWB's powers; the concern with the limited number of grades in giving fair returns to growers; and the likelihood of a call on Federal government underwriting for the 1983-84 pool have had the greatest impact in my view.

Nevertheless it may well be, as suggested in the Introduction, that the IAC enquiry process has had a significant impact on policy development. Various hypotheses may be suggested; for example, that there is a five year lag in implementing IAC recommendations on wheat marketing (e.g., the previous IAC report on wheat marketing recommended that licensed private traders be permitted to operate on the domestic market a result not much different from the proposed Permit Scheme); that the IAC can have a significant impact provided industry participants have not been traumatized by recent exogenous shocks and losses; and that policy trends tend to be cyclical because peoples' memories are short so that the industry tends to bump from crisis to crisis going in a different direction each time.

The reason for the annoyance of large stockfeed manufacturers with illegal sales may need a little explanation. The hypothesis has been put forward that they cannot afford to be prosecuted for illegal purchase of stockfeed wheat since this could threaten continuation of necessary purchases from the AWB. Thus, excluded from the illegal market themselves, they complain about smaller firms which are able to take advantage of it.

<sup>7</sup> Watson argues (p. 113) that the IAC wheat recommendations involve a series of fall back positions and options. They are not laid out explicitly however, and nor are the opportunity costs made clear. In the absence of this, interested parties may adopt their own fall back positions in partial or complete ignorance of the IAC's reasoning, which they would not have otherwise selected.

determine what should be done. In the case of wheat policy a little over fourteen months was available to the IAC for investigations and reporting while three months was available to the SCA Working Group on Wheat Marketing Arrangements to come up with second-best policies. As it turned out a consensus was reached early in the Working Group discussion that complete deregulation of the domestic market was not an acceptable option, leaving it with the need to redo much of the IAC's work.

A further innovation which would reduce the difficulties of translating IAC recommendations into acceptable policy would be the inclusion of one of the IAC Commissioners or senior staff members in subsequent policy discussions such as the SCA Working Group deliberations. This would have considerably reduced the difficulties of and possible mistakes by the Working Group in the policy development discussed above.

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