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THE PARTIAL SUSPENSION OF GRAIN SALES TO THE USSR: AN APPRAISAL 9 MONTHS LATER

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IN THIS ISSUE

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A Chronology of Events

1 The 1979-80 crop year: sales of wheat and corn by the United States to the U.S.S.R. in the 1979-80 crop year were governed by a 5-year Grain Supply Agreement; under that agreement, the U.S.S.R. may purchase up to 8 million tons of wheat and corn in the U.S. without consultation and the U.S.S.R. is required to purchase 6 million tons. Should the U.S.S.R. wish to purchase more than 8 million tons in the U.S., an agreement must be reached between the two countries with regard to the additional purchase. Consultations between the two governments are held regularly twice a year, spring and fall. The 1979-80 crop year was the fourth year of that agreement.

2 October 3, 1979, during the regular semi-annual consultations, officials of the two governments agreed that the U.S.S.R. could purchase up to 25 million tons of corn and wheat in the fourth year of the agreement, from October 1, 1979 to October 1, 1980.

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3 December 27, 1979, Soviet troops invaded Afghanistan.

4 January 4, 1980, in response to the Soviet Union's act of aggression, President Carter announced that the U.S. would suspend all grain shipments to the U.S.S.R. in excess of the 8 million tons per year committed under the 5-year sales agreement.

5 January 4, 1980, the President also directed the Secretary of Agriculture to take the necessary actions—through commodity purchases, price support actions and grain reserve programs—to protect American farmers from any adverse effect of the sales suspension action.

6 January 6, 1980, U.S. Department of Agriculture (USDA) officials met with representatives of the grain exporting firms to discuss the impact of the sales suspensions and possible offsetting actions.

7 January 6, 1980, officials of the Commodities Futures Trading Commission (CFTC) ordered the suspension of futures trading on January 7 and 8, 1980.

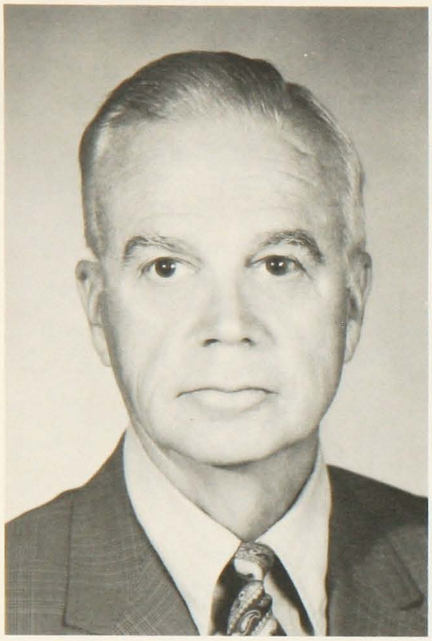
8 January 8, 1980, USDA officials announced the first of a series of actions to offset the potential decline in farm prices and incomes. This action involved changes in the farmer-owned grain reserve programs; included were: (1) wider bands between release and call prices, (2) an increase in storage payments, and (3) a 1-year interest waiver on the first 13 million tons of corn entering the reserve. Loan prices, on which release and call levels are based, were also included at that time. Other actions that followed in the winter and spring of 1980 included the announcement of an alcohol fuels program to increase the production of gasohol, the purchase of corn and wheat from farmers at country points, the increasing of target prices for corn and wheat, the opening of the grain reserve to 1979 noncompliers, and numerous other specific commodity program actions designed to protect grain growers.

9 January 12, 1980, representatives from Canada, Australia, Argentina, and the European Economic Community or Common Market (EEC) met in Washington to discuss the sales suspension by the U.S. The representatives agreed, with Argentina dissenting, to not "directly or indirectly replace" the 17 million tons blocked from shipment to the U.S.S.R. by the U.S.

10 February 1, 1980, the USDA finalized its contract assumption agreement with private grain exporters. Under the agreement the USDA would assume sales contracts made by private firms at the price which would have occurred if the Soviet sales had gone through, minus a deduction for (a) profits, (b) any premiums due to Soviet sales, and (c) a deduction for companies in a short position on January 4.

11 February 29, 1980, Agriculture Secretary Bergland announced that there would be no paid land diversion program in 1980 for crops of wheat, corn, and other feed grains.

12 May 1, 1980, Secretary Bergland affirmed that the U.S. would stand by its commitment to sell to the U.S.S.R. between 6 and 8 million tons of U.S. purchased wheat and corn during the fifth year of the agreement, October 1, 1980 to October 1, 1981.



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13 June 18, 1980, private companies were informed that informal controls over their sales of third country grain to the Soviet Union were no longer in effect.

14 July 1, 1980, Canada, Australia, and the EEC have made new grain sales for shipment to the U.S.S.R. in 1980-81, but it is anticipated by the Carter administration that these sales will not fill the void created by the decision of the U.S. to limit shipments of wheat and corn to the U.S.S.R. to 8 million metric tons in 1980-81. Argentina has not agreed to restrain sales to the Soviet Union, and has signed a 5-year agreement to supply the U.S.S.R. 4 million tons of corn and sorghum, and 500,000 tons of soybeans beginning in 1981.

Impact on the Soviet Union

It is generally agreed that the suspension of grain sales by the U.S. to the U.S.S.R. reduced grain imports into the Soviet Union from 20.6 million tons to 14.6 million tons, or by 6 million tons, between January 1, 1980 and June 30, 1980. A breakdown of the grain trade data for the Soviet Union for the various periods, with and without the sales suspension, appears in table 1.

The suspension of U.S. grain sales also forced the Soviets to purchase grain from a large number of small suppliers which resulted (1) in a serious congestion at Soviet grain receiving points, (2) in some increase in the price which the Soviets had to pay for those grain imports, and (3) in some increased transport costs to the Soviets. Thus, we conclude that the Soviets were able to obtain grain, from foreign sources, to offset about one-half of the curtailed shipments of grain from the U.S. But those offsetting supplies came at an additional cost to the Soviet Union.

As a result of these disruptions and restrictions to grain imports, livestock inventories in the socialized sector, which stood at record levels on January 1, 1980 for cattle and poultry, increased more slowly between January 1, 1980 and September 1, 1980 than for the same period in any year in the previous 5 years. Hog numbers are slightly lower on September 1, 1980 than a year earlier; the same is true for sheep and goats. The rate of growth in cattle numbers between September 1, 1979 and September 1, 1980 has been exceedingly modest. And only in poultry do numbers increase significantly between September 1, 1979 and September 1, 1980.

As a result of these inventory changes total meat production in the socialized sector of the Soviet Union actually increased from January through May 1980 over the same period in 1979. However, cumulative meat production for January through July 1980 falls 3 percent below total meat production for the same period in 1979, and declines by 4 percent for January through August in 1980 over the same period in 1979. The reasons for the sharp downturn in meat production in the summer months of 1980, it is hypothesized, are (1) animals are being fed to lighter weights as the result of a tight feed situation and (2) animals are being held back from slaughter by some farm managers in the hope of an improved feed situation—a hope that must have evaporated with the report this fall of the second poor grain crop in a row in the Soviet Union.

Milk production in the socialized sector declined steadily throughout the first half of the year, despite record low numbers as of January 1, 1980. Milk production by July 1980 was some 4 percent below that of one year earlier.

As a result of these developments, *U.S. News and World Report* observes that (worker) . . . "strikes have drawn unwelcome attention to acute shortages throughout Russia of meat and dairy products. Supplies are dwindling because of a poor harvest, a cut back on U.S. wheat exports to Russia and feed scarcities that led to premature slaughtering of cattle, poultry, and other animals this year. Further depleting stocks are food shipments to Afghanistan, Vietnam and other countries where Russia is busy establishing a presence."

The partial suspension of grain sales to the Soviet Union by the U.S. did not raise havoc in that country, but it has caused the government and the citizens of the Soviet Union more than a little inconvenience. The economic message sent the Soviet Union in the form of a partial suspension of grain sales was received and was obviously felt by the Soviets.

The Impact on the United States

The public response to the partial grain suspension to the Soviet Union was at first good among most groups and in most parts of the country. But the public mood, particularly in the Midwest, with respect to the suspension began to change in early spring. The National Governors Association in August 1980 considered, but rejected, a resolution which declared that "agricultural embargoes are ineffective, depress prices, cost the taxpayers billions of dollars and jeopardize future sales of agricultural commodities" and which specifically called for an end to the current partial suspension of grain sales to the Soviet Union. This statement has, however, become the conventional wisdom of farm leaders and the press in the Midwest. But is it a correct judgment? The effectiveness of the partial embargo in the Soviet Union has already been discussed here. Now consider the effect of the partial suspension of grain sales to the Soviet Union on domestic farm prices. Consider first the corn case.

The cash price for #2 yellow corn at Chicago stood at $2.63 per bushel on January 3, 1980. On January 9, following the announcement of the suspension and the closing of the regional grain markets to trading on January 7 and 8, the cash price of corn declined to $2.39 per bushel; and the price fell to $2.30 per bushel on January 10. Thereafter the cash price of corn at Chicago increased irregularly, but persistently, to a level of $2.68 per bushel on February 5. The cash price of corn at Chicago fluctuated between $2.60 and $2.70, or at the approximate level at which it stood on January 3, between February 5 and March 21; on that latter date the cash price of corn at Chicago fell to $2.59 per bushel. The cash price of corn at Chicago declined to $2.50 per bushel on March 27. Following March 27, the cash price of corn at Chicago rose irregularly, but persistently to $2.75 per bushel on May 8. Between May 8 and July 1, the cash price of corn at Chicago fluctuated between $2.64 per bushel and $2.81. Between July 1 and August 12, the cash price of corn at Chicago rose from $2.81 per bushel to $3.41. Between August 12 and September 17, the cash price of corn at Chicago has fluctuated around the $3.40 level, falling as low as $3.27 on August 15 and moving up as high as $3.54 on September 2.

To summarize, the cash price of corn at Chicago fell sharply for 2 days following the announcement of the partial suspension of grain sales to the Soviet Union, recovered to the presuspension level of sales in January and February, fell modestly below presuspension levels for a brief period in late March, held at or above presuspension levels in April, May, and June, and then moved up strongly in July and August. On balance the market for corn was strong during the first 9 months of 1980.

The modest weakening of the corn market in late March cannot be attributed to a decline in exports. Exports of corn in February and March were running well above exports in the same months in the previous year; and exports of corn for the first 8 months of 1980 were nearly 6 percent larger than for the same 8 months in 1979. Exports of other feed grains, close substitutes for corn, in February and March of 1980 were nearly double the level of exports in the same months of 1979, and exports of other feed grains for the first 8 months of 1980 were some 75 percent larger than in 1979. The export picture for feed grains was exceedingly strong throughout the first 8 months of 1980.

The modest weakening of the cash corn market in the latter part of March was more likely the result of the increasing expectation of a very large U.S. corn crop in 1980, and an expected buildup in feed grain stocks in 1980. The tight credit situation in farming areas in late winter and early spring could also have contributed to falling corn prices in March as farmers liquidated inventories to obtain operating capital. These developments in combination with some transportation problems operated to depress the cash corn market modestly for a brief period in late March.

What is thought, by traders and farmers, but is rarely said, is the following. If the suspended corn sales to the Soviet Union of some 12 million tons were *added* to the already strong volume of exports in the first 8 months of 1980, the price of corn would not have held steady during the first half of 1980 and increased substantially in July and August, *as it did*; the price of corn and other feed grains would have *soared* in 1980, just as they did in 1973. And this unspoken argument is to some degree correct. If the suspended sales of feed grains to the Soviet Union represent a potential net addition to exports, and that net addition had in fact been realized, the price of corn and other feed grains to farmers would have been much higher in 1980 than those prices in fact were. But the potential net addition in exports to the Soviet Union is not 12 million tons; it is only 6 million tons (table 1). The reconstructed grain trade in the first half of 1980, in which the U.S. increased its exports to new foreign buyers and new suppliers increased their exports to the Soviet Union, resulted in a net decrease in grain imports into the Soviet Union of only 6 million tons in the first 6 months of 1980.

The price story for wheat parallels that for corn, although cash wheat prices remain weaker throughout 1980 relative to the presuspension level of prices than do corn prices. The cash price of #1 hard red winter wheat at Kansas City stood at $4.40 per bushel on January 3. The cash price at Kansas City fell to $4.01 on January 10, rose to $4.49 per bushel on February 4, declined in an irregular fashion to $3.78 per bushel on April 18, fluctuated between $3.78 and $4.24 over the period April 18 and June 25, fluctuated at a slightly higher plateau between June 25 and July 31, and finally made it back to a level around $4.40 per bushel in September. In sum, cash wheat prices at Kansas City remained weak relative to the presuspension level of prices throughout most of 1980.

Why this happened is not clear. Wheat exports in the first 8 months of 1980 exceeded those of 1979 by slightly over 8 percent. And world wheat stocks were estimated to decline in 1980 from their 1979 level. Perhaps the suspension of wheat sales to the Soviet Union of some 4 million tons did have an adverse psychological impact on the U.S. wheat market. Perhaps the large U.S. wheat crop had an adverse psychological impact on the U.S. wheat market. But, although wheat prices did drag during the first half of 1980, it should be recognized that the offsetting actions taken by the federal

Table 1. Impact of suspension on Soviet grain availability (July-June marketing year basis)

Item	1978/79	1979/80 Estimates: Without suspension	1979/80 Estimates: Current	Net impact of suspension
		—Million metric tons—		
Production	237	179	179	—
USSR imports[1]				
July-Dec.	6.9	16.9	16.9	0
From U.S.	4.0	12.2	12.2	0
From others	2.9	4.7	4.7	0
Jan-June	8.7	20.6	14.6	−6
From U.S.	7.2	15.3	3.1	−12
From others	1.5	5.3	11.5	+6
Total July/June	15.6	37.5	31.0	−6
From U.S.	11.2	27.5	15.3	−12
From others	4.4	10.0	15.7	+6
Total availability	250	215	209	−6

[1]Data are based on U.S. Export Sales Reports and official statistics of foreign governments, and were provided by the USDA.

government to stabilize grain prices after the grain sales suspension were effective in preventing any major break in wheat prices. It should also be recognized that the dominant cause of the slump in grain prices in March and April was the news of favorable weather and the promise of bumper crops, and the up-turn in grain prices in July and August was the concern of traders over the news of unfavorable weather and the possible reduction in production.

The actions taken by the Carter administration to ease the burden of grain sales suspension on farmers were not without costs for the American taxpayers. The federal government has spent between $2.5 and $3.0 billion to assume the contractual obligations of exporters, to buy up grain from farmers and to encourage farmers to store more grain in the reserve. It is estimated that a half or more of those expenditures will come back to the government when crop loans are repaid and government purchased grain is sold. Thus, the costs to the taxpayer of the programs resulting from the partial suspension of grain sales should amount to $1.5 billion or less.

Finally, it should be recognized that the backing and filling of the federal bureaucracy with regard to the operation of support programs in the field created uncertainty and confusion in the minds of many grain farmers. This bureaucratic ineptness caused many farmers to become disenchanted with the support programs and to take a negative view of the entire grain suspension idea.

Striking a Balance

The operational consequences of the partial grain suspension to the Soviet Union to date can be listed under positive, neutral, and negative headings.

The positive consequences include:

1 A modest disruption of the Soviet food supply, with inconvenience and discomfort to both the government and its citizens.

2 An increase in the real cost of producing livestock products in the Soviet Union.

3 The Soviets needed to be told that the U.S. strongly disapproved of the invasion of Afghanistan, and the partial grain suspension was an effective way, short of war, to send the Soviets that message.

The neutral consequences include:

1 Offsetting actions by the federal government kept corn prices from falling below the presuspension level, except for two brief periods.

The negative consequences include:

1 Offsetting actions by the federal government failed to keep wheat prices from dragging along modestly below presuspension levels for extended periods.

2 The offsetting actions of the federal government are likely to cost U.S. taxpayers some $1.5 billion.

3 Inept formulation and administration of programs designed to protect farmers from the adverse consequences of the partial suspension of grain sales to the Soviet Union created confusion in the field and led to a negative response on the part of farmers.

These consequences can be likened to a bag of horses and bananas; they are so different in nature that they cannot be summed into a net quantitative measure of the goodness or badness of the partial grain suspension. Thus, I, as an economist, am unable to provide an evaluation, in measured units, of the desirability or lack of desirability of the partial grain suspension.

But as a policy analyst concerned with the future welfare of the U.S. I can render a judgment. In my judgment we needed to inform the Soviets of our strong disapproval of their invasion of Afghanistan. Given the many and varied circumstances of the international scene, the partial suspension of grain sales to the Soviet Union was a reasonably effective means for conveying that message to the Soviets; certainly it beat saber rattling. And the federal government was reasonably successful in protecting the most vulnerable groups in American society, namely, grain traders and grain farmers from the negative impacts of the operation. Thus, in my judgment the course of action pursued by the federal government in 1980 regarding grain sales to the Soviet Union, given the alternatives open to it, should be assigned passing, if not high, marks.

What Future Course of Action

The important question as of November 1980 is—What should be our future course of action with respect to trade with the Soviet Union? The Soviets are still in Afghanistan, seeking to conquer that country, and their efforts are being countered by stiff resistance from many Afghans. Further the Soviets experienced a very poor grain crop in 1980—the second in a row—and a continuance of the partial grain embargo, *if it could be made effective,* would really hurt the Soviets in 1981. The inconveniences of 1980 could be turned into serious disruptions in the Soviet food supply in 1981. Thus, there is an argument to be made for continuing the partial suspension of grain sales to the Soviet Union in 1981.

But to date the partial suspension of grain sales to the Soviet Union has not created serious disruptions in the Soviet food supply, and there are some good reasons why it is likely to have a lesser impact in the future than it has in the past 9 or 10 months. First, grain producing competitors of the U.S. are showing less willingness in the crop year 1980-81 to cooperate with the U.S. in limiting grain sales to the Soviet Union. Second, leakages of grain exports from the U.S. to the Soviet Union through third country "arrangements" are almost certain to increase in the future; the maintenance of an effective embargo of a ubiquitous product, such as grain, is extremely difficult. Third, if the grain sales suspension is maintained for a long period of time, or if it should become total, competing producers, including those in the Soviet Union, are likely to increase their longrun capacity to supply the grain needs of the Soviet Union.

For these reasons, and because the partial suspension of grain sales is not likely to hamper the Soviet war effort in Afghanistan to any noticeable degree, a reasonable course of action for the U.S. might well involve the initiation of talks leading to the renegotiation of the U.S.-Soviet grains agreement, which is due to expire in fall 1981. Continuing, expanding, and regularizing U.S. grain trade with the Soviet Union is important to the U.S. for at least two reasons: first, to help maintain a strong aggregate demand for U.S. grain production—a production that is efficient and far in excess of domestic requirements and second, to help support and promote a set of viable, peaceful relationships with the Soviet Union.

The Soviets should be interested in renegotiating the grains agreement because they are in need of a dependable, foreign source of supply of grain at reasonable prices. And in spite of the partial suspension of grain sales to the Soviet Union, they are well aware that the U.S. did honor all sales contracted under the previous agreement.

In short, in the uncertain world in which we live, both countries have need for a continued, dependable trade in grain—the U.S. to export, the Soviet Union to import. Thus, it would seem in the best interests of both countries to begin talks *now* leading to a new agreement that takes effect in fall 1981. And, since for diplomatic and propaganda reasons, both countries may find it difficult to come to the negotiating table, it is the position of this writer that preliminary, informal talks leading to the renegotiation of the grains agreement should begin immediately. In spite of the need on both sides, this new agreement, for reasons of national pride, could be an exceedingly difficult one to negotiate.

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