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# **U.S. Perspectives on the Canadian Grain Problem: A Critical Appraisal**

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## **Abstract**

The United States has imported large amounts of wheat and barley from Canada in recent years. Producers in northern-tier states and their political representatives have been strenuously objected, citing market disruption and unfair trading practices by the Canadian Wheat Board. This paper provides a summary and critique of U.S. perspectives on ‘the Canadian grain problem.’

Key Words: grain trade, wheat, barley, Canadian Wheat Board.

# U.S. Perspectives on the Canadian Grain Problem: A Critical Appraisal\*

D. Demcey Johnson\*\*

## Introduction

Grain trade presents a number of contentious issues for the United States and Canada. While both countries are traditionally net exporters, the United States has imported large amounts of Canadian wheat and barley in recent years—to the consternation of many U.S. producers. Differences in market organization between the United States and Canada, and changes in the policy environment for agricultural trade, have left plenty of room for public confusion about the causes of U.S. grain imports and whether anything can be done about it.

This paper presents a summary and critique of U.S. perspectives on the ‘Canadian grain problem.’ To be clear, it is the wheat and barley producers in northern-tier states (and their congressional representatives) who are most concerned about Canadian grain imports. While other U.S. groups have a stake in the evolution of continental grain trade—specifically, millers, maltsters, grain merchants, and their trade associations—these are overshadowed in public discourse and political influence by the concerns of grain producers. Hence, much of this critique is addressed to the perceptions (and misperceptions) of U.S. wheat and barley producers and their political advocates.

In the next section, I discuss several complaints that have surfaced in discussions about the Canadian grain problem, which can be characterized as *misguided*, *unsubstantiated*, or *irrelevant* in the current policy environment. I then turn to some meatier topics that, I suspect, will continue to dominate discussions on bilateral grain trade in years to come.

## Popular Views of the ‘Canadian Grain Problem’

Some complaints by U.S. producers are misguided. An example is the assertion that *Canadian producers reap an unfair advantage because of the exchange rate*. It is true that changing exchange rates can shift the competitive advantage between countries. However, a Montana farmer’s letter to the Joint Commission on Grains (included in Volume II of its Final Report) reveals misunderstanding on a more basic level:

A Canadian farmer told me last week that the price of a bushel of wheat in Canada and here were comparable, but if he sold it down here he could get a 35% premium because of money differences. In other words, I sell my wheat and I get \$3.50 per bushel. The Canadian dumps his load in the same pit with mine and he gets 35% more, or \$4.77 in his money.

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To the Montana farmer, it appeared that “money differences” led to a higher return for his Canadian counterpart. (Presumably, part of the problem is that Canadians stubbornly refuse to change the name of their currency. If the Canadian farmer earned 4.77 *loons* instead of *dollars*, the U.S. farmer would worry less about being cheated.)

From an economic perspective, what matters is *changes* in exchange rates and how these are passed through to costs of goods and services, rather than the *levels* of exchange rates *per se*. When the Canadian dollar loses value (depreciates), as it did during 1992-94, Canadian goods become more competitive in U.S. and offshore markets. But at the same time, the Canadian farmer’s depreciated dollar buys him less.

Although Canada’s competitive position has been enhanced by currency depreciation, this is properly viewed as a result of market forces. In an era when most governments (including Canada’s) do not directly control their exchange rates, the ‘fairness’ of currency fluctuations for U.S. producers is not really at issue.<sup>1</sup>

One of the most widely repeated, but (as yet) unsubstantiated, claims is that *Canada unfairly subsidizes its grain exports to the United States*. This is an almost reflexive allegation by some U.S. farmers and politicians. It seems to stem from the identification of the Canadian Wheat Board (CWB) as a state trading enterprise and the conviction that the CWB does not ‘play fair’ in international competition.

Farmers are also perplexed by the fact that the United States imports any wheat. After all, one half of the U.S. wheat crop is typically exported; why should a surplus producer be importing grain from Canada? Answer: It must be subsidized.

‘Subsidies’ are a slippery concept, admitting different interpretations and means of measurement.<sup>2</sup> For purposes of the Canada-United States Trade Agreement (CUSTA), trade negotiators agreed to use aggregate measures of producer subsidies (called ‘producer subsidy equivalents’ or PSEs) as a trigger for trade liberalization in the grain sector. PSEs were initially higher in the United States, which allowed Canada to delay eliminating its license requirements for wheat and barley imports. There is a residue of unhappiness among U.S. wheat and barley producers about CUSTA, which they argue was too favorable to Canada—specifically, in how subsidies were measured, and what was left out of the agreement.<sup>3</sup> However, historical measures

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<sup>1</sup>Popular concerns about exchange rates are shared by some U.S. politicians. Senator Kent Conrad of North Dakota, in explaining his opposition to *fast-track* trade legislation, complained that other countries can devalue their currencies and thereby negate the effects of lower import barriers, leaving U.S. export firms no better off than before trade liberalization (*Forum* Nov. 13, 1997). Senator Byron Dorgan of North Dakota raised other objections to fast-track; as evidence of “soft-headed” U.S. trade policies, he cited the trade agreement with Canada and the resulting “flood of unfairly subsidized Canadian grain.” (*Forum*, Sept. 28, 1997).

<sup>2</sup>See Huffbauer and Erb (pp. 9-13) for discussion.

<sup>3</sup>See North Dakota Barley Council.

show broadly similar levels of support for wheat and barley farmers in the two countries (see Ackerman, Fig. 3).

A related issue concerns the ‘dumping’ of Canadian grain on U.S. markets. Evidence of dumping would be critical to U.S. producers seeking relief from imports. As normally defined, this means selling below the cost of production (or acquisition) and transport. By that standard, CWB would clearly be dumping if it sold wheat in U.S. markets at less than the initial payment paid to producers plus cost of handling and transport. To date, there has been little evidence of dumping by Canada. (See Gray and Annand).

Claims of ‘unfair subsidies’ are less specific and therefore hard to prove or disprove. However, there is not much evidence of consistent underpricing by the Canadian Wheat Board. A 1990 ITC investigation of durum found “no consistent price difference between prices of U.S.-grown durum and imported Canadian durum” (USITC Pub. 2274, p. ix).

A 1994 ITC investigation of Canadian wheat, wheat flour, and semolina entering the U.S. market did lead to import restrictions under Section 22 of the Agricultural Adjustment Act. But Section 22 was invoked because imports caused “material interference” with USDA commodity programs, not because of Canadian subsidies. The ITC conducted price comparisons for U.S. and Canadian wheat offered to U.S. millers. They found that Canadian wheat was priced below U.S. wheat in 28 of 63 instances, with margins as large as 12.8 percent. But Canadian wheat was priced *above* U.S. wheat in 33 instances, with margins as large as 20.0 percent (USITC Pub. 2794, p. II-79).

Making direct comparisons is difficult on an ongoing basis because of the paucity of Canadian price data. There are also differences in quality, real or perceived, between ‘comparable’ U.S. and Canadian grades, and buyers may have unique contract specifications which raise or lower their costs relative to standard grades. Economists like to assume that ‘wheat is wheat’—in our jargon, a ‘homogeneous’ commodity—because that simplifies our analysis, but millers and grain traders know better.

Some claims of U.S. producers are basically correct, but practically irrelevant in the new trade policy environment. An example is the assertion that *imports of Canadian grain depress U.S. grain prices and reduce farmer income*. American farmers know this, as do their political representatives. It is an example of the ‘law of demand’ at work: as larger quantities enter the market, prices are bound to fall. Economists put numbers to this idea using a ‘demand elasticity.’ Unfortunately, different statistical models (and data sets) produce different estimates, and there is little agreement about relevant elasticities—and hence about the impact of imports on U.S. grain prices. Several studies have been published with different conclusions about these aggregate effects.<sup>4</sup>

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<sup>4</sup>Gray and Annand point to several studies, each with different estimates of the impact of wheat imports on U.S. producer income.



There are two complications to this line of analysis. First, utilization of wheat is divided into ‘food use’ and ‘feed use’ (for livestock feed). Different uses have different demand relationships. In general, imports of wheat for feed use are less likely to produce downward pressure on U.S. wheat prices. And much of the surge in U.S. imports from Canada in 1993/94 was accounted for by feed wheat.

Second, U.S. imports of Canadian grain in the last decade have been induced, in part, by a U.S. program to subsidize exports. Under the Export Enhancement Program (EEP), the U.S. government offered subsidies for exports of wheat and barley to targeted markets. Higher U.S. exports raised domestic prices, while lowering prices in Canada’s offshore markets. This created an incentive for Canada to shift exports to the U.S. market. In evaluating the impact of U.S. grain imports on prices, it is relevant to ask: Compared to what? If there had been no EEP, U.S. imports of Canadian grain would have been lower. With EEP in place, imports of Canadian grain are larger, and (estimated) price impacts are magnified.

Whatever the ‘true’ impact of grain imports on U.S. grain prices, this provides no legal basis for import restrictions. It was not always so. Section 22 was invoked to limit imports in 1995-96, but that authority lapsed with U.S. ratification of the WTO treaty. Nowadays, absent changes to existing trade agreements, grain imports from Canada are just something U.S. farmers have to live with.

### **Substantive Issues in Bilateral Grain Trade**

Having considered some of the popular (and misguided) views of U.S. producers, I now turn to some issues that seem likely to dominate discussions of Canada/U.S. grain trade in the next several years. These divide into three main areas: transportation, market access, and the role of the Canadian Wheat Board.

#### **Transportation Issues**

Several years ago, Canadian freight subsidies under the Western Grain Transportation Act (WGTA) were criticized for providing an unfair competitive advantage to Canadian grain producers. As it turned out, these U.S. criticisms were misplaced: with elimination of the WGTA subsidies in 1995, the higher cost of rail shipment to Canadian ports made southerly grain flows more attractive. Thus, eliminating subsidies induced a larger influx of Canadian grain into U.S. markets.<sup>5</sup> For U.S. producers this recalls the dictum: Be careful what you wish for, because you may get it.

While WGTA subsidies (and their removal) were the focus of much debate and analysis, other aspects of the Canadian transportation system are now coming under scrutiny—not least because of the discriminatory treatment accorded non-board and non-Canadian grains. To put this in context, it should be noted that even after subsidy elimination, Canadian rail rates (e.g.,

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<sup>5</sup>See Johnson and Wilson for an economic analysis of the effect of rail subsidies (and their removal) on continental barley flows.

from Prairie locations to ports) are substantially lower than the rates charged by U.S. carriers for similar movements. The lower Canadian rates reflect regulated rate structures. (These may change in the next several years as a result of regulatory review.) From a U.S. perspective, however, the critical point is that (comparatively) low Canadian rail rates apply legally only to grains grown in Canada.<sup>6</sup> This prevents U.S. grain shippers—especially those situated along the border—from taking advantage of low, Canadian rail rates for transshipment of U.S. grain bound for the west coast. A second, overtly discriminatory feature is the system for allocation of railcars, which gives preferential treatment to the Canadian Wheat Board. Non-board grains (including oats, canola, and any U.S. grains moving through the Canadian system) are residual claimants for railcars. This differs from the nondiscriminatory treatment given Canadian grain by U.S. rail carriers and may become a point of contention as pressures emerge for cross-border flows in both directions.

Another set of issues concerns pooling of freight costs for board grains. In Canada, all costs of marketing board grains (i.e., transportation, cleaning, and handling) are aggregated and deducted from total sale revenue. Practically, the pooling of costs is inseparable from the pooling of sale prices, yet some implications of cost pooling are worth drawing out. Although transportation differentials figure into the final prices received by producers in different locations, these bear no necessary relationship to actual shipment patterns. Unlike in the United States, where values of grain adjust instantaneously to changes in sale prices and shipping costs, in Canada the pooling mechanism masks the values (costs and prospective returns) for individual transactions. And costs of ‘inefficient’ grain movements are absorbed by all Canadian producers who sell through the Board.

This is clearly viewed as a problem in Canada—concerns about systemic inefficiencies underlie the controversy about whether the CWB should retain its single-seller status<sup>7</sup>—but why should it matter to the United States? Three reasons are suggested. First, the pooling system facilitates shipment patterns that ‘make no sense’ in terms of logistical efficiency, and would not be observed in a competitive marketing environment.<sup>8</sup> For U.S. observers, this adds to uncertainty about flows of Canadian grain and reinforces the view that the CWB is not bound by the same strictures as private grain marketing firms. Second, with losses on individual transactions obscured through cost-averaging, it is harder to gauge the ‘fairness’ of Canadian sale prices. (For that matter, it is hard for Canadian producers to know the value of their grain in terms of current sale opportunities.) Third, if marketing costs for board grains are inflated, the

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<sup>6</sup>See Wilson and Dahl for a review of constraints on Canadian market access.

<sup>7</sup>Carter and Loans conclude that higher marketing costs more than offset whatever benefits accrue to Canadian producers from the CWB’s single-seller status.

<sup>8</sup>Consider the following example recounted by a U.S. observer. The CWB had committed to sell barley to an offshore (Pacific Rim) buyer, but faced bottlenecks in the Canadian rail system. Its solution was to ship barley by truck from as far north as Edmonton, Alberta, to Great Falls, Montana, where it was placed on U.S. rail for shipment to the West Coast. In doing so, the CWB incurred trucking costs of about 25 cents/bushel. It could have saved these costs (while fulfilling its export obligation) by buying U.S. barley in Great Falls. Instead, the extra trucking costs were absorbed by Canadian producers.

effect may be to accentuate the gap between U.S. and Canadian producer prices, creating greater incentive for cross-border arbitrage.

From the U.S. perspective, the basic questions are whether trade flows are distorted by various features of the Canadian system and whether U.S. grain producers are materially affected. These have political resonance (at least in the northern plains) and may be confronted in future trade negotiations, but are analytically difficult. Many features of the Canadian system are functionally inseparable. Thus, the railcar allocation system is designed to accommodate the Wheat Board, the pooling system is a requirement of single-desk selling, and grain delivery patterns (by producers to elevators) are constrained by the pooling system.<sup>9</sup> Disentangling these features and identifying their effects on trade is not easy.

### **Unequal Market Access**

There is a common perception among U.S. producers that, despite some liberalization of trade under CUSTA, Canada has allowed limited access to its own grain markets. This is supported (at least superficially) by the fact that flows of wheat and barley have been overwhelmingly from Canada to the United States since CUSTA came into effect. The truth is a bit more complicated. Major trade barriers have been removed in Canada—specifically, import license requirements for wheat and barley, eliminated in 1995 under terms of the WTO agreement<sup>10</sup>—but other, subtler features of the Canadian system can make it impractical to import U.S. grain. Among these are requirements for end-use certificates, quality controls, and variety licensing.

When a Canadian buyer imports U.S. wheat for human consumption, the grain must be accompanied by an end-use certificate (EUC). This allows the U.S. wheat to be tracked to its final destination. En route, the U.S. wheat must also be segregated from Canadian wheat<sup>11</sup>—ostensibly to avoid compromising Canada’s system of grain quality controls. These requirements raise handling costs (since segregation of U.S. grain requires extra bin space) and reduce opportunities for re-sale by Canadian buyers. Canadian imports of U.S. feed wheat must

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<sup>9</sup>Producers throughout the Prairie Provinces have equal access to pool accounts. Thus, when the CWB announces that it is accepting delivery for a given class of grain, producers can deliver at all locations. This ensures that all producers have timely access to the initial payment. However, the simultaneous delivery of grain to multiple locations is not necessarily efficient from the standpoint of transportation and logistics.

<sup>10</sup>Canada stopped requiring import licenses for U.S. wheat in 1991. When the WTO agreement came into force, Canada converted its import license requirements into tariff-rate-quotas (TRQ). The under-access tariffs on barley were eliminated in January 1998.

<sup>11</sup>In fairness, the United States also now requires end-use certificates (EUC) for imports of Canadian wheat. There are also some U.S. restrictions on commingling of U.S. and Canadian grain—specifically, to prevent Canadian grain from being exported under U.S. subsidy programs (EEP and GSM). This policy was introduced in response to Canadian EUCs, instigated by senators unhappy about inflows of grain from Canada, and over the objections of the U.S. grain trade.

be ‘de-natured’ (by coloring some percentage of kernels) to make the grain visually distinguishable from Canadian supplies. Imports of wheat and barley for seed use are allowed only for varieties that have undergone a rigorous testing and approval process—again, to preserve the integrity of Canada’s grain quality system (USDA-FAS, p. 43).

The Joint Commission on Grains, which was convened in 1994-95 to recommend solutions to the bilateral trade dispute, noted that Canada’s system of variety controls was in conflict with the objective of achieving reciprocal market access. However, the Commission recommended that Canada take action to provide non-registered varieties (from U.S. and Canadian origins) with better access to Canada’s handling and transportation system. The Commission also recommended an end to EUC requirements in both countries (Joint Commission, Vol. 1, p. 94). To date, there has been little movement in this direction.

It may be argued that this is much ado about nothing. After all, the U.S. grain market is substantially larger than Canada’s—nine times larger in terms of total cereal grain consumption—so that even if remaining barriers to trade in Canada were removed, the overall tendency would be for grain to move from Canada to the United States. Problems of market access, from this viewpoint, are primarily important for symbolic reasons: they raise questions about the ‘fairness’ of our bilateral grain trade. This is not to deny that northbound movements could make economic sense in some instances. For example, because of growth in its livestock sector (and rise in demand for feed barley), Alberta could cease to be a barley-surplus region in the next several years. Alberta feedlots might then import barley from Montana.

Ultimately, ‘market access’ may be less significant for U.S. producers than access to Canada’s handling and transportation system, particularly in view of the favorable rates on Canadian rail shipments. It bears repeating that while U.S. rail carriers do not price their services differently for U.S. and Canadian grain, the Canadian rail carriers are not bound to provide U.S. grain with (low) regulated rates. Nor does U.S. grain have equal access (on nondiscriminatory commercial terms) to Canadian railcars or port facilities. The upshot is that U.S. grain producers cannot take advantage of the Canadian rail transportation system (i.e., for shipments to the West Coast), but must bear the high costs of shipping by U.S. rail carriers. Meanwhile, Canadian grain has unfettered access to the U.S. grain handling and transportation system—as many North Dakota and Montana producers are aware, having encountered lines of Canadian grain trucks at their local elevators.

### **Role of Canadian Wheat Board**

The Canadian Wheat Board lies at the center of U.S. complaints about our grain trade with Canada. Issues relating to state-trading enterprises (STEs)<sup>12</sup> have been elevated to the top of the USDA agenda for upcoming rounds of multilateral trade negotiations, in part because of continuing irritation over the competitive advantages enjoyed by the CWB. What are these advantages?

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<sup>12</sup>Furtan and Baylis provide background on state trading in wheat.

Unlike U.S. grain trading firms, the CWB does not compete for grain procurement. Western Canadian farmers must sell their wheat or barley to the Board unless it is for domestic feed use. This facilitates long-term marketing strategies and forward sales commitments, because the Board has a lock on grain supplies. Downside protection is provided through the Canadian Government's initial payment guarantee. This is equivalent to price insurance and represents an implicit subsidy whether or not the pool accounts wind up in deficit. U.S. trading firms, in contrast, buy price protection by hedging in futures markets. CWB borrowings are guaranteed by the government, so the Board's interest costs are low. What's more, the CWB pushes most costs of grain storage onto Canadian producers; although it enjoys certain access to supplies, the CWB takes ownership of the grain only at the time of delivery. To obtain the same position, a U.S. firm would have to buy grain (and incur storage costs) or hedge in futures markets (which also costs money).

The CWB can offer different prices to different buyers, a practice known as 'price discrimination'. Defenders of the Board hold this up as the major advantage of single-desk selling. In principle, the CWB can maximize sales revenue (net of shipping costs) by offering high prices in some markets and low prices in other markets. Whether the Board does a good job of this has been the subject of much debate in Canada.<sup>13</sup> But what does it mean for the United States?

Economic theory provides some insight. If the CWB allocates its sales optimally, theory suggests, it will sell more grain to price-responsive markets and less to price-insensitive markets. A standard for comparison is competitive market equilibrium, where selling prices (net of transport) are equalized across markets. If demand in the United States is more price-sensitive than Canada's alternative markets, then the CWB should direct more exports to the United States, that is, more than what would occur under a competitive grain marketing system. And larger U.S. import volumes must depress U.S. prices.

But U.S. utilization of wheat is comprised of both food and feed use. Suppose that Canada sends mostly food wheat to the United States. This demand is less price-sensitive than the demand for feed wheat (which depends on the price of corn and other substitutes). If, in addition, U.S. demand for food wheat is less price-sensitive than offshore demand, the preceding arguments are reversed: the CWB would direct a smaller volume of exports to the United States, compared to volumes that would occur under competitive market conditions. In that case, the net effect of the CWB's involvement is to *raise* U.S. prices, not lower them.<sup>14</sup> The point is that the ability of the CWB to practice price discrimination, *per se*, does not imply lowering of U.S. wheat prices.

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<sup>13</sup>Two studies favorable to the CWB are Kraft et al. (1996) and Schmitz et al. (1997). Carter and Loans (1996) offer a contrasting view.

<sup>14</sup>The earlier argument may still apply to trade in feed wheat. If the U.S. is a more elastic (price-sensitive) market than Canada's alternatives, CWB control should lead to higher exports to the United States. However, U.S. imports of feed wheat are somewhat episodic and do not seem to attract the same level of public concern.

The advantages associated with single-desk selling require that the CWB mask its terms of trade (prices, grain qualities, and payment terms). Pricing secrecy allows the CWB to extract large premiums in some markets, while selling at a discount elsewhere. Defenders of the Board argue that it is not fundamentally different than private U.S. grain trading firms in terms of pricing disclosure: Cargill and Continental Grain do not divulge the terms of their transactions either. However, private U.S. firms have access to extensive market information, which allows them to develop refined judgments about the prices offered by their competitors. Canada does not have comparable market information—quoted values of board grains reflect pooled returns, rather than instantaneous trading pressures—and the CWB has considerable latitude in its selling prices because it does not compete for procurement. In short, there is an asymmetry between what Canada knows about U.S. grain prices and what U.S. firms know about Canadian prices. Arguably, this asymmetry works to the advantage of the CWB in bidding competition.<sup>15</sup> The *transparency problem*, so-called, is likely to remain a point of contention between the United States and Canada. It is symptomatic of the uneasy coexistence of our two marketing systems: one dominated by a monopoly seller, the other characterized by vigorous inter-firm competition.

U.S. producer attitudes about the Wheat Board are decidedly mixed. CWB sales of wheat and barley into the United States (and some foreign markets) are viewed as pernicious. However, many U.S. producers envy the CWB's market power and marketing acumen and argue that they should have access to a similar institution—or that the Board should be opened to both U.S. and Canadian grain. Governor Ed Schafer (Republican) of North Dakota has suggested that chronic trade disputes could be resolved through “joint marketing” of U.S. and Canadian grain (*Agweek*, Nov. 17, 1997, p. 4). His argument is that joint marketing would allow the United States and Canada to exert their combined market power and extract large price premiums, particularly in a commodity like durum wheat. Senator Byron Dorgan (Democrat) of North Dakota, one of the surest critics of ‘unfair’ competition from the Canadian Wheat Board, has also voiced support for the joint marketing idea (*Forum*, Nov. 4), without proposing how this could be put into effect.<sup>16</sup> It may be argued that the U.S. Export Enhancement Program already vests something like single-desk selling powers in the U.S. Department of Agriculture, at least for subsidized export sales. How hard would it be for U.S. program administrators to consult with Winnipeg before fixing EEP bonus levels?

For various reasons, the joint marketing idea is probably a non-starter. Politically, there is little chance of any coordinated bilateral approach to state trading in grains. (The EEP program is now inactive and likely to remain so because of budgetary pressures.) The CWB is not authorized to market grains grown outside of western Canada. And while U.S. producers admire some aspects of the Canadian system, it is not clear that many would be willing to relinquish their right to make independent marketing decisions. They would like the right, but not the obligation, to sell through a pooling system. (Many Canadian producers feel the same way.)

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<sup>15</sup>The problem was more pronounced when the EEP program was active. EEP provided public disclosure of U.S. subsidy payments by importing country; from these, U.S. sale prices could be inferred with some precision.

<sup>16</sup>Actually, the idea has a long history. Schmitz et al. (1981) developed economic arguments for an international wheat export cartel.

Now consider an entirely different question: Would U.S. producers be better off if the Wheat Board were divested of its legal monopoly? The answer is not obvious. Despite U.S. complaints, it is possible that the CWB has exercised restraint in exporting to the United States—more than could be expected from a liberalized Canadian market system—either because of missed opportunities (as some Canadian critics have claimed) or because of the political sensitivity of these trade flows. The case of oats is suggestive. The Board lost its marketing authority for oats in 1989, and since that time U.S. imports of oats from Canada have steadily increased. However, this has not led to anything like the kind of public outcry that we have seen from U.S. wheat and barley producers. If the economic effects of eliminating the Wheat Board are uncertain, at least this would diffuse much of the public controversy and political posturing over U.S. grain imports.

### **Concluding Remarks**

With two radically different grain marketing systems operating side by side, there are many sources of bilateral friction in the grain sector. The role of the Wheat Board has assumed great, perhaps exaggerated importance for U.S. farmers and policymakers. However, the huge difference in market size and other transitory economic factors are surely more important for explaining flows of grain from Canada to the United States.

In several of its dimensions, the controversy over grain trade revolves around differences in regulatory regimes. These are hard to reconcile and pose questions for the United States just as they do for Canada. If Canadians enjoy relatively cheap rail transportation, that is because of Canada's regulated rate structure. The deregulation of U.S. rail rates in the 1980s, combined with the market power of U.S. rail carriers, may account for the high cost of shipping grain in northern-tier states. (Canada is in no way implicated; we did this to ourselves!) But barriers to access, on the Canadian side, elevate the importance of differences in our rail transportation systems.

Contrasts are also evident in other areas, notably grain quality and variety licensing. In the United States, producers have more latitude in terms of variety selection, and grain handlers view quality assurance (e.g., through cleaning and blending) as a commercial function, responsive to price incentives that vary across buyers through time. The Canadian system of quality assurance involves a much greater overlay of regulatory authority and restrictions (e.g., varietal controls, required segregation within the handling system, etc.). To some degree, these restrictions limit the flow of U.S. wheat and barley into Canada. But while this represents a (relatively minor) trade irritant for the United States, Canada views its grain quality system as a source of competitive advantage in international markets. Thus, Canadians argue, it is unrealistic for Canada to subordinate its quality system (and export strategy) to the goal of reduced friction over continental grain trade. U.S. observers, for their part, need convincing that any differential treatment of U.S. grain within Canada is justified.

Two final points are in order. The first is that, with or without pressure from the United States, there are impetuses for change within Canada. As part of the ongoing reform of Canadian rail transportation, there will be a review of maximum freight rates in 1999. This could lead to

complete deregulation of rail rates (which could make moot the issue of unequal access for U.S. grain) or other, more modest restructuring. The organization of the CWB is also under review. Among other things, the proposed Amendment to the Canadian Wheat Board Act would give more flexibility to the CWB in its marketing operations, risk management, and how it compensates producers<sup>17</sup>—in effect, allowing it to operate more like a commercial firm.

The second point is that pressures for integration of the U.S. and Canadian grain sectors are coming from commercial sources—in particular, from companies with substantial investments (e.g., in grain handling or processing facilities) on both sides of the border, or companies wishing to diversify their sources of supply. While interests of grain producers have dominated public discussions of trade issues, the interests of large agribusiness firms (ADM, ConAgra, AnHeuser-Busch) will militate against trade barriers in either direction.

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<sup>17</sup>The September 25, 1997, news release announcing the amendment is posted at <http://www.agr.ca/cb/news/n70925ae.html>



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