

## CWB Price Comparisons – What is Relevant?



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## Why Compare?

Proponents of a voluntary and competitive market often compare CWB prices – either pooled prices (either the Pool Return Outlook (PRO) or the final pool return), or PPO prices – to what they consider to be relevant prices, usually in the US. The logic is based on the premise that spring wheat, durum and malt barley from these two regions should be similar since they operate in virtually the same markets. And if they're not, this should lead to further analysis as to why.

Another approach is aimed at testing the premise that, since the CWB is a “single desk” (monopoly) seller of Western Canadian wheat and barley, and it states it gets premium prices over its competition, it should be expected to get better than average prices when compared to a neighbouring competitor. For example, for wheat in 08-09 the CWB reported a “net per-tonne price spread realized by the CWB compared to competitors’ values of \$6.65/tonne”. This in itself makes comparisons to Canada’s biggest competitor, the US, not only relevant but necessary to properly gauge the CWB’s marketing performance.

Another approach is to consider that the CWB is acting on behalf of Western Canadian farmers, and as such, it makes sense to assess its performance much like you would assess an employee hired to market grain. The true test of this arrangement is not whether it got a better price on the day it sold; rather, it should be measured on how it did compared to what prices were available over the crop year. Does it really matter if the CWB got \$10/tonne more than everyone else on the day it sold if it sold the whole crop at the bottom of the market?

But what is a good benchmark? It should be pretty straight forward to get average prices over the year just by selling equal amounts throughout the year. If you're going to pay someone to market your grain for you, you should expect greater than average returns over the crop year. If your “hired marketer” doesn't get at least average prices, you might be inclined to replace him or simply do it yourself.

## The US Market

US prices are used for comparisons, not so much as a possible destination for wheat, durum and barley but rather as a proxy for what Canadian market values could be. Both Canada and the US are large producers of wheat and typically the two largest exporters of wheat, often going head-to-head in offshore markets. When we consistently see higher prices south of the border, it's not so much a question of wanting to sell into the

US, it's more a question of being competitive with the US in offshore markets and wanting to find a way to get the same kind of farm gate returns as they do.

Practically every time and with every comparison, the US price is more attractive than the CWB pooled return or the various pricing options available to producers, such as Fixed Price, FlexPro and GrainFlo contracts, which aim to provide a “market-based” price. Also, at times, other comparisons are made: Western Canadian wheat prices are often compared to Ontario prices, and prices of Canadian grain on a landed basis in destination countries have been compared to grain from other exporting countries that compete with Canada.

The CWB refutes these arguments from various angles – arguments include comparing a pooled price to a spot price is not appropriate; pooled prices are weighted averages and the US prices used aren't – again, not an appropriate comparison; grade differences can and will skew results; the US does not export as much as Canada and therefore it is more of a domestic market than ours; and the systems are different and comparing the two leads to improper comparisons. Also, the CWB has argued that the CWB's single desk elevates prices in the US and a direct comparison should take this into consideration. For Ontario, the CWB argues the markets are completely different.

The arguments for and against the various comparisons need to be clarified; the methodology of this type of comparative analysis should not be the focus of the debate – the results should be.

## **Data Sets**

When making price comparisons, CWB prices used most often are the final pool returns or the PROs. At times, the daily prices for optional pricing programs such as FlexPro are used. When a farmgate price is needed, average deductions from the CWB's instore prices to each province are available in the PRO announcements on the CWB website.

Various price series are used to compare to CWB prices, including but not limited to:

### **Spring wheat**

- Individual daily elevator bids prices, various elevators in the Northern Plains of the US
- DTN Index daily average prices: Data Transmission Network (DTN), in association with the Minneapolis Grain Exchange collects street prices from over 300 elevators in the Northern Plains of the USA (mostly North Dakota and Montana) and aggregates them as an average, provided daily. Most consider this to be a very good representation of the market.
- Daily USDA US export prices, basis PNW ports

- USDA weighted average elevator transaction prices, covering crop year periods
- Montana Wheat and Barley Commission daily street prices for different regions in Montana
- From various sources, prices as delivered to offshore buyers from various other exporting countries (US, Australia, EU, Argentina)

### **Durum wheat**

- Individual daily elevator bids prices, various elevators in the Northern Plains of the US
- DTN Index daily average prices: Data Transmission Network (DTN), in association with the Minneapolis Grain Exchange collects street prices from over 300 elevators and aggregates them as an average, provided daily.
- USDA weighted average elevator transaction prices, covering crop year periods
- Montana Wheat and Barley Commission daily street prices for different regions in Montana
- From various sources, prices as delivered to offshore buyers from various other exporting countries (US, Mexico, EU)

### **2 Row malt barley**

- Individual daily elevator bids prices, various elevators in the Northern Plains of the US
- Contract prices from major malt companies
- Daily USDA US export prices, basis PNW ports
- USDA weighted average elevator transaction prices, covering crop year periods
- Montana Wheat and Barley Commission daily street prices for different regions in Montana
- From various sources, prices as delivered to offshore buyers from various other exporting countries (US, Australia, EU)

## **CWB Pooled Price vs US Spot Price**

From time to time, producers or analysts will compare CWB pooled prices or prices offered through optional pricing options to a US spot prices for delivery into an elevator in the Northern Plains. The CWB's response is that this is an unfair or inappropriate comparison; we tend to agree. The CWB argues correctly that the Pool Return Outlook (PRO) is a combination of sales already made and a forecast of sales that the CWB anticipates. Neither of these factors are relevant to the current "spot" market. For example, at the time of writing this, the following prices are current (CWB prices are in Canadian dollars; the US price is in US dollars – the exchange rate is near par):

	PRO <sup>1</sup>	FlexPro	US elevator <sup>2</sup>
Spring wheat	\$7.68	\$9.03	\$10.15
Durum	\$6.78	n/a	\$10.50
Malt barley	\$4.21	n/a	\$4.80
Feed barley	\$3.79	n/a	\$4.08

All CWB prices are significantly below the US prices of comparable grains. Although there are many reasons why this might be so, the fact that the CWB prices are a combination of sales made and an outlook makes them poor comparisons to spot US prices. In times of strong markets (like now), the PRO will tend to lag the spot market. Therefore, there is no sound conclusion that can be made comparing the PRO to spot prices.

The CWB also offers a pricing option called “FlexPro” which offers a daily cash price throughout the crop year. The CWB website states: “The daily price posted for the FlexPro contract is simply the current market value of wheat. The current market value of wheat is established by taking the weighted average of current prices available for shipping periods and destinations that the CWB expects to sell into for the remainder of the sales period. Because the price is an estimate of what could be sold in the future and not the current price, it too has a subjective element that can skew the price away from the relevant spot market.

## CWB Pooled Prices vs DTN Index Prices

CWB final pool returns are often compared to average US prices for the same crop year. The argument makes the assumption that comparing Canadian prices to US prices for similar grades is valid because both regions produce similar wheat, both compete in the global market, and the DTN average prices are valid representations of the US street prices. The basic premise of the comparison is that, at a minimum, the CWB should be able to exceed average prices over the year due to its alleged ability to get premium prices through the power of the single desk. And the DTN prices are a good representation of possible market-based prices.

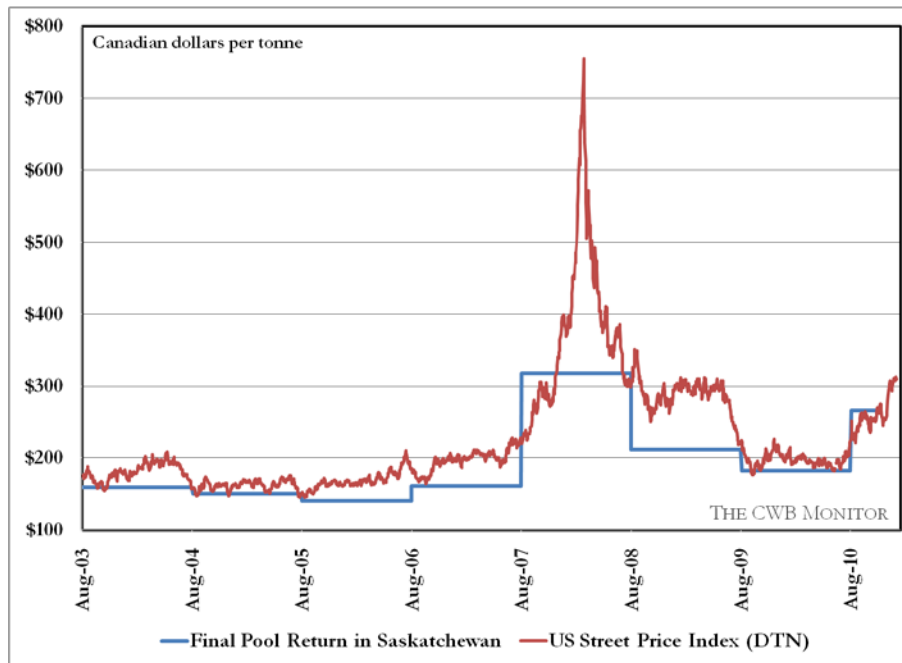
Charts 1 through 3 below depict Canada/US price comparisons over the past seven years for spring wheat, durum and malt barley respectively. The spring wheat and durum analyses compare the DTN daily average prices to the CWB average final pool returns for farmers in Saskatchewan. The 2-row malt barley analysis compares daily bids for 2-row malt barley in the Golden Triangle region of Montana to CWB final pool returns in Alberta.

<sup>1</sup> Source: CWB - the spring wheat and durum PROs are adjusted to an average SK price; the malt PRO is adjusted to an average AB price

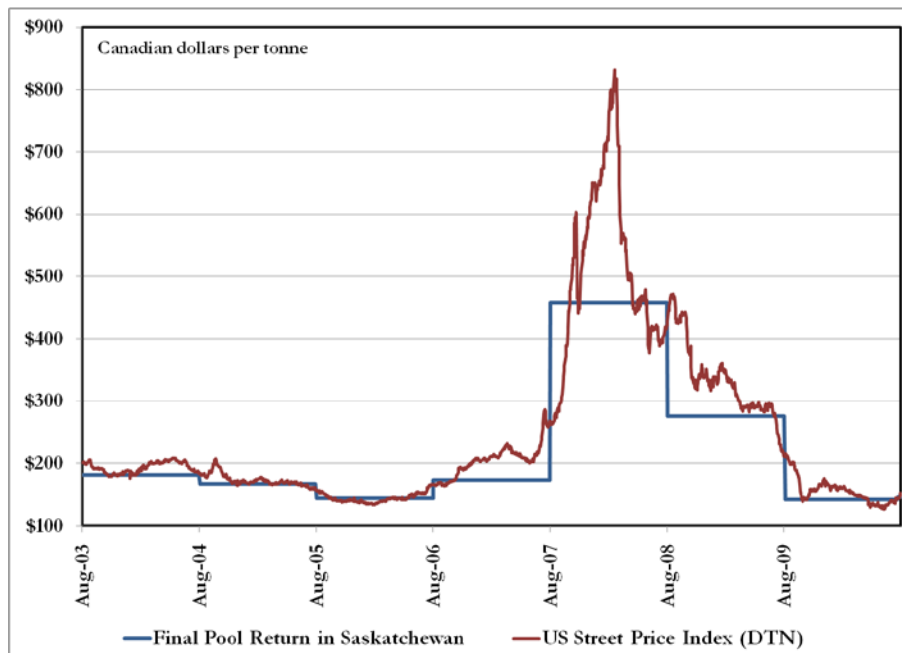
<sup>2</sup> Sources: spring wheat and durum - Berthold Elevator, Berthold, ND; malt barley – Montana Wheat and Barley Committee

These comparisons strongly suggest that the CWB pooled returns for Western Canadian farmers are not competitive with US prices; they do not even get average US prices. Many times over the last seven years the CWB final pool returns to Canadian farmers were comparable to the lowest prices in the US. On any of these crops, it could be said that the US farmer could have sold his whole crop at the lowest price seen all year and he would still get a better return than the Western Canadian farmer under the CWB system.

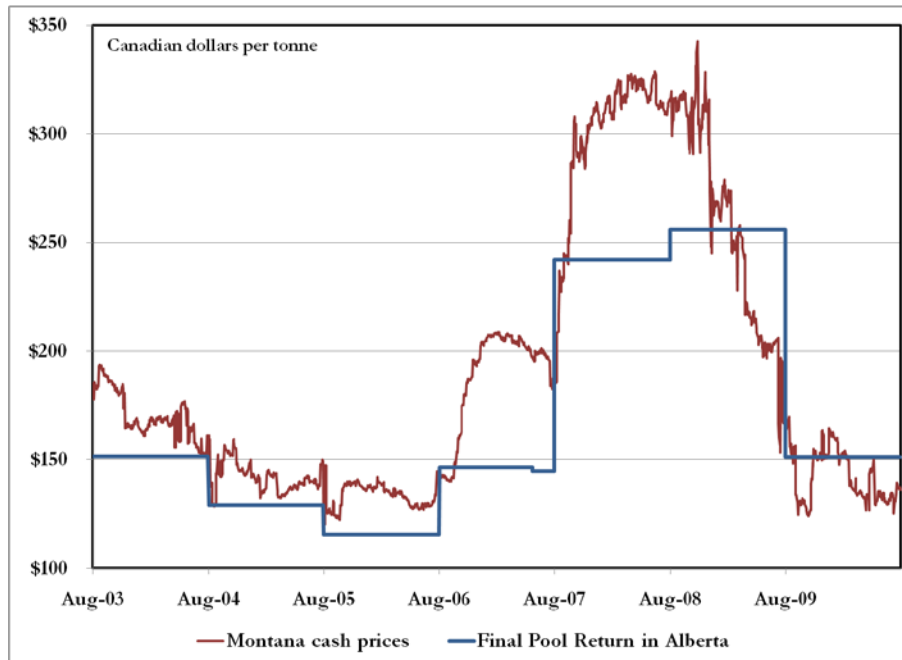
**Chart 1: Spring Wheat Price Comparisons: 03-04 to 09-10**



**Chart 2: Durum Wheat Price Comparisons: 03-04 to 09-10**



**Chart 3: 2-Row Malt Barley Comparisons: 03-04 to 09-10**



It should also be noted that with 2-row malt barley, about 80% of the crop is contracted well ahead of the crop being grown, typically at prices much higher than the prevailing cash prices. This leads to the conclusion that the average US return for 2-row malt barley is even higher in relation to the CWB's annual returns.

## The CWB's Arguments

The CWB attempts to refute price comparisons as irrelevant or misguided. It uses many arguments, some of which are addressed here.

### The US market is mostly domestic; Canada is mostly export

The CWB has often cited the relative domestic/export mix of the two countries as a factor in an effort to dismiss Canada/US comparisons on wheat. The argument is based on the premise that the US does not export as much spring wheat as Canada and therefore, the US domestic price is higher than the export market. Since the US domestic market then is divorced from export values, the CWB argues that it is inappropriate to compare Canadian pooled returns, which are heavily skewed to the lower priced export markets.

The CWB is correct in its assessment that the US exports less spring wheat than Canada. Over the last four years, exports as a proportion of production looks like this:

<b>Crop Year</b>	<b>US</b>	<b>Canadian</b>
06-07	57.6%	67.0%
07-08	66.7%	76.2%
08-09	42.9%	64.1%
09-10	33.3%	65.9%

Each year, Canada exported more spring wheat than the US. However, the US still exported from one third to two thirds of their spring wheat crop. This is substantial enough to play a significant role in price determination. Moreover, there is ample evidence in the US that the export and domestic prices arbitrage. That is to say, that the two markets compete on price and there is no evidence to suggest that the US domestic market trades at a premium to the export market.

### **The Single Desk raises US prices**

The CWB has stated a number of times that the existence and activities of the single desk supports the US market prices; this is because of orderly marketing controlling the flow of spring wheat into the US market, without which a larger flow would result, depressing US prices.

The CWB uses this to discredit any comparisons, suggesting that it is irrelevant to compare to US prices because they are “artificially” supported by the single desk; in other words, they are not representative of the market.

There is no evidence that this occurs; moreover, the CWB has never made public its economic analysis that proves this theory.

Since price comparisons are meant to address the price spread and not the absolute prices involved, and assuming the CWB also suggests that the Canadian price is equally supported by the single desk, the potential of the single desk raising the US price does nothing to dissuade the arguments away from the conclusion that the Western Canadian farmgate prices are lower than their US counterparts.

### **USDA weighted average vs CWB Pooled return (weighted average)**

The CWB has argued that the appropriate comparison would compare Canadian CWB prices to weighted average US prices, available from the USDA; according to the CWB, this would more closely approximate what the US farmer is getting for his grain. This is not necessary or sound for a couple of reasons. The Canada/US comparisons being made are not aimed at estimating what US farmers actually receive for their grain; rather, it is an exercise aimed at estimating the market values available to farmers throughout a crop year and comparing the CWB results to that market indicator.

The USDA prices that the CWB would prefer to use, include all grades of the grain in question transacted at the elevator – not just the one relevant grade. This will weigh on the US prices accordingly. Also, using this spot transaction data does not factor in sales made using deferred delivery contracts.

## **Conclusions**

The Canada/US price comparisons used over the last few years are very relevant. They clearly demonstrate that the Western Canadian farmer is uncompetitive when compared to his US counterpart. The difference in prices cannot be attributed to any single factor, although the major factors are clear – either the Canadian system has higher costs (easily tested) or the CWB is achieving lower overall prices than the market is providing.