

Concerning Barley

Feed Barley Exports

You've probably heard by now that the CWB is selling feed barley overseas for as much as \$1.00/bu more than what farmers are getting paid on delivery.

Holding back a portion of the sale price is the way the CWB manages risk – whether in the pool accounts, the Producer Pricing Options or through its cash trading. On the latest feed barley program, the CWB has said that farmers will get “all the margin that’s in there” after the season, as kind of a “top-up” or dividend (net of costs and after all sales returns are pooled).

Keep an eye on this one. Past experience has shown that the CWB doesn't always pay out all the margins made on these sales. Two years ago, using a similar program (Guaranteed Delivery Contracts), the CWB kept from farmers about \$1.00/bu from its feed barley trading program. About \$20 million from feed barley cash trading went straight into the Contingency Fund to cover losses from discretionary trading in wheat the year before. Last year, it kept about \$5 million from the farmers that sold malt barley through CashPlus programs.

There is a better way to do this that would provide farmers with more upfront cash and less (if any) would be diverted away from farmers and into the Contingency Fund. The CWB needs to be open to new ideas.

The Feed Barley Pool B for 2009-2010 is a bust

Every month since November 2009 the CWB issued a Pool Return Outlook (PRO) for Pool B. Starting at \$152 in November, the PRO dropped to \$150 in Feb and to \$143 in March where it stayed until July. With each PRO, the CWB commented on how the global barley prices were under pressure and not expected to move higher. The next release was the PRO final in Sept – but there was no B pool PRO reported. At that time, the CWB explained it this way: “Due to low offshore values relative to domestic feed values, there were no deliveries to the 2009-10 feed barley Pool B.”

So, even though there was no barley in the pool, each month the CWB still published its estimated return – the PRO.

How can the CWB calculate a meaningful PRO when there is no barley in the pool? Perhaps an even more important question is: Why release a meaningless PRO? Right or wrong, good or bad, it is still a market signal. In this case it's a really bad one.

I know it must be tough to feel as though you need to put out a PRO even when there is no grain in the pool, but, really!? The CWB should make it a policy that, if there is no grain in the pool,

along with each PRO, it reports there is a zero balance in the pool. That way we will all know just how meaningless the PRO really is and we can pay even less attention to it than we do now. The way it is now, the PRO – as meaningless as it is – still runs the risk of distorting domestic prices.

Or better yet, don't pool barley at all.

Does the CWB get premiums in barley?

They say they do. They have studies that say they do. The one they refer to the most was done in 2005 by Drs. Schmitz, Schmitz and Gray (I'll call them SSG).

SSG says the CWB gets more from malt barley sales than a "multiple-seller" market environment would. They say that between 1995-96 and 2003-04, the CWB earned an average "additional earning" of \$35.25/t on 6-row malt barley and \$40.29/t on 2-row malt barley. Dr. Richard Gray (the "G" in SSG) told me that the study showed that the CWB gets no premiums for feed barley. According to Dr. Gray, these additional earnings on malt barley are part of the malt premium over feed barley. SSG says that without the CWB, these "additional earnings" – the malt premium – will disappear.

SSG took a theoretical, econometric approach to this problem. I took a simpler approach. I compared the pool returns in each of the years they studied and compared them to the average domestic feed barley price in central Saskatchewan (around Saskatoon), which is about as close as you can get to the lowest priced feed barley in the country. If the CWB prices are going to shine, this is where they will shine.

The CWB's 2-row malt barley price averaged only \$7.38/t over feed and the 6-row malt barley price averaged \$6.98/t under (yes – UNDER) the lowest priced feed barley in the country.

This data shows that the CWB "malt premium" over feed is the smallest malt premium of any major barley producing region in the world.

If, as SSG says, the malt barley price would drop \$35 to \$40/t without the CWB, this means that, without the CWB, the malt barley price in western Canada would be lower than the feed barley price.

That doesn't happen anywhere else in the world; why would it happen here?

When a study using a sophisticated economical model says one thing (such as big premiums) and a simple look at real prices says another (such as no premiums) which should we believe?

We also need to ask the farmer-elected CWB directors – what are they doing to improve the malt premium over feed?

Why Barley?

In the last four years the feed barley pool has dropped from about a million tonnes to a mere 30,900 tonnes in 08-09 (both A and B pools combined). Previous years have also seen very low

tonnages in the barley pool. Although the 09-10 results have not yet been reported, the CWB has already stated that there were no deliveries in pool B.

Most of the pooled feed barley goes through an EPO and the number of producers using the EPO is reported in the Annual Report. Using the EPO participation numbers as a guide, I would say a couple of thousand producers – at best – have been delivering to the feed barley pool. More recently, it's even less; practically all the barley in the 08-09 Pool B was delivered by only 113 producers.

It's a tougher number to estimate, but I'm going to stick my neck out and guesstimate that the number of producers selling malt barley to the CWB is around 10,000 each year (works out to about 240 tonnes per producer).

The CWB says they work for 75,000 Western Canadian farmers. But when it comes to barley, I figure with less than 2,000 farmers using the feed pool and 10,000 selling malt barley, more than 87% of the producers out there are not participating in the CWB's activities in barley. (The CWB's cash trading in feed barley doesn't count; it's a drag on domestic prices, hurting all barley producers, whether they sell to the CWB or not.)

Last June, the CWB surveyed 900 Western Canadian producers. In that survey, 48% said they "prefer" "solely the CWB" to be in barley marketing. But if 87% of producers aren't even using the CWB for barley marketing, that leaves 13% that do. And we know that many producers that sell barley to the CWB would prefer not to.

It seems that instead of 48%, less than 13% of Western Canadian producers prefer the CWB in barley (demonstrated by actual deliveries).

So instead of survey results that show the CWB has 48% support in barley, I prefer to look at the estimated 13% of Western Canadian producers that market barley through the CWB as an indication of CWB support in barley. The other 87% either don't grow barley or don't find what the CWB has to offer as beneficial or attractive.

How would the CWB board of directors react to less than 13% support in barley?

How should they react?

More on Feed Barley Exports

I know I've been here before but there's just so much of this that's just not right. For instance, one thing I didn't mention before is that the way the CWB operates in the export feed barley market may actually limit how much volume it does. The CWB first tenders to grain companies for supply. Only when the barley is "in the showcase" does it sell the barley. In the time lag between originating the barley and offering it for sale, the market price can drop and that's why the CWB goes to the farmer with a discounted price.

Talk in the trade suggests the CWB may have missed sales because of this approach. By the time the tenders go out, the grain companies respond, and the CWB tries to sell, the buying interest may have been satisfied from other sources.

Let me summarize the situation (I have mentioned some of this before):

- The CWB is the only one that can sell feed barley for export.
- It may miss business because of the way it operates.
- It shows farmers only a portion of the price – as much as \$50/tonne is missing.
- It won't guarantee that farmers who sold barley will get any of the rest of the sale value. (Did you know that this is the third consecutive year that the CWB has had this kind of cash program on feed barley? And did you know that farmers never received the full sales value in the previous years?)
- The CWB buys barley through company-specific tenders with a specific sign-up window. These contracts are not well promoted or widely publicized so many farmers don't know about them or even have access to them.
- Because the export price is not transmitted to the country, domestic prices for feed barley and even feed wheat are artificially held down.

The loss to the western prairie economy is well into the hundreds of millions. Even Jim Flaherty should sit up and take notice.

I can accept losing business because you didn't have the right price, the right quality or couldn't execute in the required shipping period. That's the nature of the business. But to lose business simply because of the way you choose to operate is unacceptable, especially when you won't let anyone else try. Combine this with keeping a portion of the value from farmers and the loss in real revenue at the farm gate on all feed barley and feed wheat and this becomes downright mind boggling.

Anyone who either defends or deflects criticism of this program is blinded by ideology. Make no mistake - the single desk has cost farmers millions here and has been a drain on the western economy. I can only hope that those that defend the single desk will see this for what it is and will now engage in a more meaningful debate.

Even if you're a staunch CWB supporter, it's OK to be madder than hell about this. Now that there's a CWB directors' election going on, farmers should demand from candidates what they would do to improve this situation for farmers – all farmers.

The CWB Misses the Point on Feed Barley Debate

Late last week, the CWB commented on the feed barley debate.

(<http://www.cwb.ca/public/en/hot/record/commentary/>) Unfortunately, they still don't get it.

The CWB explained its feed barley program back in 2007-08 by saying it sold several hundred thousand tonnes purchased directly from the trade. This is quite different than buying from

farmers using Guaranteed Delivery Contracts (GDCs), as they are doing this year – but in most respects, the result is the same.

On these trades it has been estimated that the CWB made about \$50.00/tonne. To explain why it didn't distribute this excess profit to producers, the CWB said: "It would have been extremely difficult to determine which farmers contributed to those cash sales and at what prices, which is why the margins were directed to the CWB's contingency fund..."

I have to ask: Why did the CWB choose to buy from the trade and not from farmers?

First, if they bought directly from farmers using GDCs, they could have distributed the excess profits to the farmers that participated in the sales.

Second, using this program, the CWB created the same major problem in 07-08 that we're seeing right now. In both years, the CWB's actions are directly responsible for keeping the export values from having a positive impact on the domestic price of feed barley. Since The CWB made \$50/tonne in excess profits on these export sales, it's only natural that, with efficient price transparency as there would be in an open market, the domestic prices would have moved higher to compete. At 1½ tonnes/acre, that works out to \$12,000 per quarter that you could've had.

And it doesn't stop at feed barley. If you made more from selling feed barley, you'd have less cash-flow pressure to sell canola. Less selling pressure on the canola market means higher prices on canola.

A majority of The CWB board of directors feel farmers are better off with the CWB single desk. They argue that grain companies "would (naturally) buy feed barley at prices just above the domestic value, sell it at the higher international values, and retain the profit margin."

This argument is based on what would happen if you suddenly changed the rules, shut down the single desk one day and opened up the market the next. It's based on the assumption of the current dysfunctional market structure – ineffective price discovery, no appropriate hedging tools, few players and no active arbitrage between markets. The CWB fails to factor in competition and arbitrage between markets.

I argue that the market would evolve very quickly from its current makeup. We would see the rapid development of vibrant futures and options markets, active cash brokerage/trading, multiple participants (not just the big grain companies) and effective arbitrage between markets. Competition would drive handling margins lower, just as we've seen in other non-CWB commodities.

Ironically, I see the CWB playing an important role in a dual market, particularly in the early stages, in price discovery, discipline and arbitrage.

The crucial point the CWB is missing is that the rest of the barley market suffers by the way the CWB operates. And the CWB is completely myopic when it says that if there was an open market, farmers would lose.

They don't get it. Doing it the CWB way, everyone loses.