

## Concerning Price Comparisons

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### The US Market, Part 1

We often look to the US to see what the world would be like without the CWB single desk, for better or for worse, depending on your point of view. Many arguments have no apparent resolution.

Defenders of the CWB argue that if we lost the single desk, wheat would begin to flow in great quantities to the US and the US would slam the border shut to Canadian wheat. (Although the argument is often made about the loss of the CWB, really the issue is the single desk – the control of the CWB over the marketplace.) There is a great irony in this argument. Defenders of the CWB believe that the control of the CWB is needed to ensure a mutually agreeable wheat-trading relationship with the US – with no trade actions. Yet, every trade action by the US involving the CWB was about the CWB itself – specifically CWB control and market power – and not about wheat imports per se.

Beyond that, there's something more mundane at play here (or at least should be). Specifically, the reason wheat would want to flow south in the first place is the attraction of higher prices. Think about it. Today's street price for spring wheat in Berthold, ND is \$6.39/bu, (in Canadian dollars). At the same time the CWB's Fixed Price Contract (FPC) – which is as close as the CWB gets to a spot price – is roughly \$6.14/bu in SK and \$6.29/bu in MB.

Also, the FPC price includes an "adjustment factor" of \$2.78/t (7½ cents/bu) which adjusts the FPC price to reflect earlier sales made prior to sign up. Since this adjustment factor is positive, it means the earlier sales were made at a higher price. Disregard the adjustment factor and you get closer to what the CWB figures the spot market to be for Canadian wheat. In this case, it's \$6.06½/bu in SK – about \$0.32½/bu below the spot North Dakota price. (The difference is often much greater. If you want, I can show you the data.)

Is that enough to start trucking south? Perhaps. Perhaps not. But I'm not terribly interested in whether wheat will flow south or not in an open market. As in other open (less-regulated) markets, grain will move as little as possible in order to satisfy the demand. If it doesn't need to move south, it won't; if there is a need, it will.

I look at prices south of the border – not so much as a possible destination for wheat, but rather as a proxy for what our market values could be. Look at it this way. 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 see consistently 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.

Here's another irony. We compete with the US in many offshore markets. Sometimes they win, sometimes we win. When we win, the CWB insists it earns "premiums". And yet, the average US farmgate price is higher than ours. If you can figure out how that can happen, please let me know. We need to fix it.

## Let's Compare Premiums

Intuitively, the concept of the single desk makes sense. Farmers should benefit from collectively negotiating from a position of strength and the potential for better prices seems almost obvious. But the evidence doesn't match with the expectations. In fact, analysis of most available evidence tells a substantially different story.

The Guardians of the single desk argue that the CWB gets "premiums". 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". I'm pretty sure this means that on the whole pool, the CWB got on average \$6.65/tonne more than what the competition would have sold (premium) on the same day.

I'm not going to argue against this because I have no evidence to say it's wrong. But I have doubts because of how competitive the industry is; even the CWB says it needs to be price competitive. If buyers are paying more for Western Canadian wheat it may be for better quality, something for which the single desk cannot take credit – but that's another story.

The CWB is like a hired resource to market grain on behalf of farmers. To me, 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 it got \$10/tonne more than everyone else on the day it sold if it sold the whole crop at the bottom of the market?

It should be pretty straight forward to get average prices over the year - just sell equal amounts throughout the year. You don't even need a single desk to do that. 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.

So I compared average market prices to the CWB final pool return for a standard grade of spring wheat. As a representative of the market price, I used the CWB's own selling quotation it uses to sell wheat into the domestic milling market. These prices are meant to reflect US competitive prices so they really reflect the whole North American market. Since the pool return has some direct costs and revenues that aren't factored into the selling price at the time of the sale, I adjusted the selling quotes accordingly to make sure there was nothing that would skew the results; apples to apples.

For 08-09, the final pool return for #1CWRS 13.5 was \$311.36/tonne.

The adjusted average market price for #1 CWRS 13.5 was \$366.91/tonne.

The average CWB sales price for #1 CWRS 13.5 was \$55.55/tonne below the average market price for the crop year.

If we accept that the CWB achieved average premiums of \$6.65 over the competition on the day of the sale, then we can see that without that premium, the average CWB sales would have been \$62.20/tonne below the average market price for the year.

This analysis doesn't refute the CWB's claim of premium prices. But it's pretty tough to argue that the CWB gets any kind of premiums on sales when the pool return is so much lower than the average market price for the year.

How can that happen? There must be an explanation; and farmers deserve one.

Stay tuned.

## More Price Comparisons

My last commentary was about how the CWB's final pool return was much lower than the average "market" price for the year. It created a bit of a stir and discussion so I want to add to it.

I used the CWB's daily selling price as a reflection of the market price – it's the price they quote to domestic millers. Someone suggested that price wasn't actually the "market" price – I should use a US price, suggesting that the price I was using was just the CWB's asking price. He said that the CWB could be selling below the "asking price".

DTN collects cash prices from over 300 elevators in the Northern Plains of the USA (mostly North Dakota and Montana) each and every day, then publishes the average. Most consider this to be a very good representation of the market. Comparing the pool return to the annual average of the DTN prices and the 08-09 pool return showed the pool return was \$37.18/tonne below the average DTN price. Although this is better than the \$55.55/tonne below the average Canadian offering prices, the pool return is still substantially below average for the year.

Now, for the benefit of you doubting-Thomases, this was not a one-year event. Over the seven years ending in 08-09, the final pool return was, on average \$32.23/tonne below the DTN average. The worst performance was in 07-08 when the pool was \$63.21/tonne below the US average; the best was in 04-05 when it was \$11.36/tonne below the US average.

I asked it before. I'll ask it again: Are below average prices good enough?

Pro-CWB director's candidates explain their support of the CWB - because it's a "marketing advantage" (Stewart Wells), "the CWB has clout" (Allen Oberg), or "it provides the best opportunity for farmers to maximize their returns" (Kyle Korneychuck). How do these comments fit with these price comparisons?

I would sincerely like to see the CWB explain this. Remember, the CWB says in its Annual Report that it achieved average premiums in wheat over the competition of about \$7/tonne. How can you get premiums when the final pool returns are consistently so poor relative to the North American market? Is there something else in the pool calculation that isn't apparent?

## The US Market, Part 2

I'm being told my price comparisons (CWB pool returns to US average prices) aren't fair. Two issues were mentioned:

- "the market doesn't sell all year round. Usually, the market is lowest when the most tons have been sold."
- "...you do not have the average price that was actually received by the American farmer who sold on the open market."

The CWB uses what they call the Wheat Pool Pricing Model which establishes the pricing pace for the pool. (Page 45, 20070-08 Annual Report). If they can't sell (and price) grain to keep to the pace, they sell futures. If they're selling more than the pace allows, they buy futures. They don't say explicitly that they're shooting for the crop year average, but I doubt the approach would take them far off it.

From the September 23 commentary for the 2010-11 PRO:

At the time of this PRO, the CWB has priced approximately 24% of the expected 2010-11 crop year deliveries of wheat. A pricing level of 60% is anticipated by the end of January."

24% priced at 15% through the crop year; 60% priced 50% through the crop year. Are they skewing pricings early in the crop year? Is that what you would do this year? Just asking.

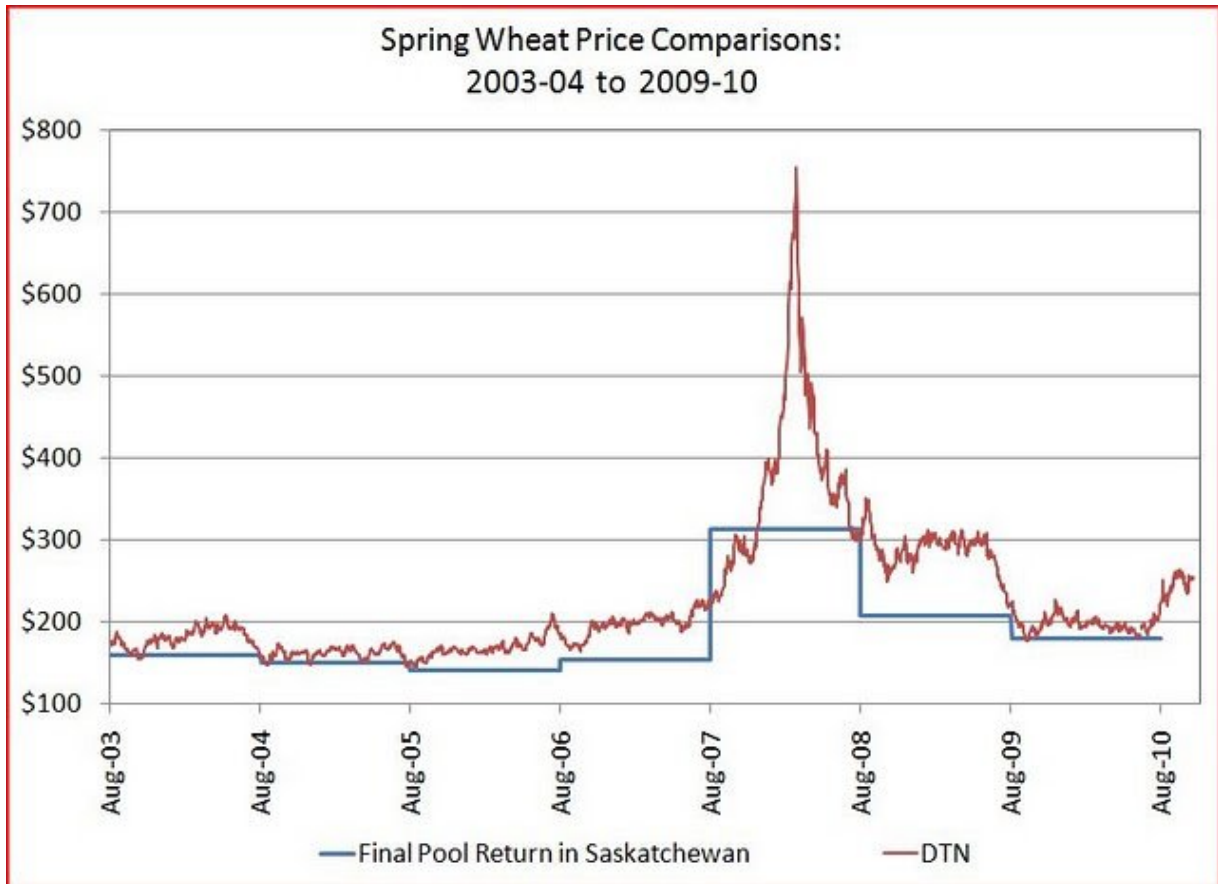
Based on the pricing model and that they say they get premiums, it would be reasonable to expect better than average pricing from the CWB.

The other comment said I hadn't considered what the US farmer had sold for. That's right; why should I care what the US farmer does when I'm not arguing to get rid of the CWB. I look at US prices to get an idea what the average market price is – not because without the CWB you could sell into the US and not because without the CWB, that's what you could expect. We compete with the US in offshore markets – why do they get more on average? I figure you deserve better than average from the CWB and it doesn't matter how you spin it, you ain't getting' it.

Forget about averages for a minute. I would like someone to explain why the pool return isn't just below average; it's often below the lowest market price (DTN) for the year. Take a look at this chart. Practically every year the Final Pool Return (the blue line) is below – or well below the lowest DTN price (the red line). Most years, the US farmer could sell it all at the lowest price of the year and he'd still be getting better prices than you.

To those who think I'm trying to dismantle the CWB – I'm not. I'm trying to help you make more money. If you can figure out how to do that with the CWB, so be it. But the way I look at it, if you

want to keep the CWB, you better start looking at it more critically, instead of just accepting it as gospel.



## Deferred Delivery Premiums

The May wheat futures contract in Minneapolis is about \$6.70/tonne higher than the December contract – the market is willing to pay that much more right now for wheat to be delivered in May instead of delivered in December.

In its Fixed Price Contracts, the CWB pays an “incremental payment” to compensate farmers for wheat delivered in later months. Farmers delivering CWB wheat on their FPC in May get \$0.60/tonne more than those delivering in December.

If the market is paying a \$6.70/tonne premium for deferred, why does the CWB only pay \$0.60/tonne?