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GENERAL AGREEMENT ON TARIFFS AND TRADE

Group on Cereals

STATEMENT MADE BY MR. MOORE, EXECUTIVE SECRETARY, INTERNATIONAL WHEAT COUNCIL ON 16 JULY 1965

I propose to divide my comments on point (iii)[1] into three parts. First of all I would like to make one or two general comments, secondly to deal with what I would call the basing point or in other words the terms in which a world minimum price would be expressed and the various considerations arising under that heading, and thirdly, to examine some of the criteria which would have to be used in determining the particular type of wheat used for reference purposes.

As far as my general comments are concerned, I would like to preface these by saying that I am dealing with point (iii) purely in market terms; in other words everything I say is addressed to the concept of an international price. This might conceivably be the same as the prix de référence under any "montant de soutien" arrangements, but that is not the aspect I am concerned with. I am dealing merely with some of the technical factors which have to be taken into consideration in establishing a world minimum price or a price range with a maximum and minimum.

The next two general comments I want to make will sound to you most elementary but I make no apology for putting them briefly in front of you, because I believe that they are essential to the effective working and administration of an international minimum price or price range.

The first point is that whatever formula or definition is eventually accepted must be clear and unambiguous, not merely to officials but also to traders. Governments here represented intervene in varying degrees in the trade in grains as affecting their countries, but in all countries to some extent traders also play a vital rôle. It seems to me, therefore, most essential that any international price formula should be readily intelligible to traders who do not have the same sources of reference or the historic record of the negotiations to guide them in understanding it. This is elementary, but I suggest it is a point of importance worth bearing in mind.

[1]Point (iii) of the joint studies (TN.64/Ce/W/1) relates to alternative bases for fixing an international minimum price.

Secondly, I believe it to be absolutely essential that any breach of the minimum price or any breach of the price range should be able to be determined immediately and should not require an extensive examination of many days, by an expert working party for example, before the fact is definitely established. Any remedial action, or any consequential action under whatever system this group might eventually negotiate, depends first of all on a prompt decision whether in fact a breach of the price or the price range has taken place. This is of course why, certainly in my view and I think in the view of everyone here, a clear and precise definition of differentials is vitally necessary in any improved agreement.

Coming now to the technical issues, the first question that I would like to examine is the basing point, or the terms in which the international price is to be expressed. There seem to me fundamentally to be three alternatives although within these three broad possibilities there are certain permutations and variations which perhaps we can just briefly look at.

You can base the international price in one of three places or express it in one of three different ways. First of all, you can, after selecting the reference wheat, express it by reference to some interior point in the country concerned. In other words, as under the present wheat agreement, if you have 1 or 2 Canadian Northern as the reference wheat, you can define this wheat in terms of its "in store" position at the Lake head; or if you took 2 Hard Winter ordinary you might conceivably take Kansas City as an interior point.

The second alternative would be to express the international price in f.o.b. terms and here there are various possibilities which I would like to examine more closely. At this moment, however, I simply state that the expression of the price in f.o.b. terms is a second possibility.

The third alternative would be to express the international price in c.i.f. terms. In using the word c.i.f. in this context, I am thinking not of a price which has been converted from an f.o.b. starting point to a c.i.f. basis, but rather of a decision which would fix the international marketing price in c.i.f. terms at the very beginning and not derive it at second-hand from an f.o.b. position. In other words if, for example, Hard Winters were taken as the reference wheat then a possible way of expressing the international price based on Hard Winters might, I say might, be to fix it on a c.i.f. United Kingdom or c.i.f. Rotterdam basis. I am here thinking of one single price against which various other c.i.f. positions would have to be calculated.

Now I don't think all these various alternatives are of equal merit and some of them seem to me to contain difficulties or disadvantages of a greater or lesser degree. Let us go back again, therefore, and examine some of the considerations involved in negotiating an international price for a given wheat expressed in f.o.b. terms. Here again there are one or two possibilities. You might, for example, fix the international price at say $1.50 either for a particular wheat or as a standard price applying to exporters all over the world. The latter choice would in my view be nonsense, but it is perfectly reasonable to envisage that after selecting the "reference" wheat the international price should be expressed in f.o.b. terms. At this point, however, there is one very important question which has to be answered before any further decision can be taken. The question is this: is a system envisaged whereby any two wheats of identical quality and characteristics coming from different sources, different origins, can be landed c.i.f. in any receiving country in the world at the same price? Or, alternatively, is it the intention of negotiators to allow the benefits of geographical proximity to markets to be a principle of the system? The present Wheat Agreement to a considerable extent, but not completely, works on the first principle, namely that whatever its origin any wheat of identical quality and characteristics should be capable of being landed in any receiving market in the world at approximately the same price. This levels out, as a starting point at any rate, competition between individual exporters. If on the other hand a system were to be adopted whereby, subject always to quality differentials, the price were fixed at, say, $1.50 f.o.b. Buenos Aires, St. Lawrence, Vancouver and so on, the effect would be that the relative nearness of individual exporters to the major import markets would to a considerable extent determine the pattern and the volume of their total trade in wheat. This, as I say, is not the system adopted under the Wheat Agreement.

In using an f.o.b. basis of price expression, but permitting it to work in such a way that identical wheats from different origins can be landed in any market at the same price, one is involved in a further step in the price formula, somewhat as follows. Let us suppose, for example, that we are thinking in terms of No. 2 Hard Winter ordinary and let us assume further that f.o.b. Gulf has been selected as the basing point. Again, let us assume that the minimum price has been set at $1.50, and that the market we are examining is the United Kingdom. The system would have to make it possible for Argentine wheat or for Canadian wheat, quality for quality, to be landed in the United Kingdom at the same price. The system then has to work in the following way in order to determine the appropriate f.o.b. prices in the case of Argentina and Canada and so on. The formula would take the price of $1.50 f.o.b. Gulf, add the current rate of freight to the United Kingdom, then deduct the current rate of freight from the United Kingdom either to Buenos Aires or to the St. Lawrence as the case may be and the resulting figure is the minimum f.o.b. price for Argentina or for Canada. This is largely the system used under the existing Wheat Agreement by which price equivalents, or derived prices, for various origins are worked out in this way starting from the price of the reference wheat at its basic point.

There are some variations of this method in the present Agreement in that, for example, instead of working to the country of destination and back again in each case, part of the formula makes the calculation to the United Kingdom alone. I think the rationale behind this was that at the time the United Kingdom was much the biggest commercial import market. A price worked out in this way, therefore, really set the proper international price level at the minimum of the price range. But at the 1962 negotiations the European exporters had a variation made in their formula, whereby their derived f.o.b. prices were worked not on a c. and f. United Kingdom basis but on a c. and f. country of destination basis.

I do not think it is appropriate for me at this particular point in time to press my own personal views as to which kind of system is better, but certainly I would have thought that a network of derived prices based on the principle that wheats of identical quality should be landed, whatever their origin, in any country of destination at the same price, before taking any account of quality differentials, was a fundamentally sound and equitable way of approaching the problem. I would not have thought that fixed f.o.b. prices giving the benefits of geographical proximity to markets was generally a desirable one. I would expect it seriously to distort existing patterns of trade and would confer benefits on countries near the big commercial markets, and similarly work to the disadvantage of suppliers some way away from those markets.

And now, let us have a look at the pros and cons of fixing the international price in rigid c.i.f. terms. By using the words c.i.f. terms, I mean not the process of converting an f.o.b. price by some formula or another to a c.i.f. price, but a system which ignores f.o.b. prices altogether and fixes the international price purely in c.i.f. terms, whether c.i.f. Rotterdam or c.i.f. anywhere else. This seems to me to have one great disadvantage. It means that under such a system the fluctuations in freight rates are carried by the exporter, because if you fix a firm c.i.f. price then that is the price, and if freights rise or fall it is the exporter who takes the benefit, if there is a benefit, or the disadvantages of sharp changes in freight rates. I think an extreme example will illustrate what could happen with a price determination of this kind. Let us suppose that in 1953 one had fixed an international price, if you like c.i.f. United Kingdom, in terms of sterling for the reference wheat at say £25. At that time freights United Kingdom/Australia were somewhere in the region of seventy shillings or eighty shillings a ton. For a short time three years later those rates rose to 220 shillings a ton. Similarly, St. Lawrence rates in 1953 were in the region of forty shillings and three years later they rose to 120 shillings. Under a c.i.f. basis of price fixing the increase in Australia/United Kingdom freights of 140 shillings would all have been carried by Australia; the increase in St. Lawrence rates of eighty shillings would all have been carried by Canada. This is an extreme example, but it does illustrate some of the problems of fixing prices based on a rigid c.i.f. basis. It may be said that the policing of any system of international prices would be done more quickly and effectively by operating at the c.i.f. end of the transaction. This may be so, but it does not follow that you therefore need to express the international price in rigid c.i.f. terms, because it is perfectly possible to convert at any time the f.o.b. price to a c.i.f. basis, using current freights, and then rises and falls in the freight market are not allowed to affect the net commodity return to the exporting country.

May I now go back to the third possibility, namely to fix prices in terms of some interior point, as this is done in fact at the present time under the Wheat Agreement. The reference wheat is Canadian No. 1 Northern and the base point is Fort William/Port Arthur. I think that as this has been used for many years it must be regarded as a thoroughly workable system, but there are perhaps two considerations that might be borne in mind in considering whether an interior point is a desirable way of expressing your international price. First of all, under the system of price equivalents in use in the present Wheat Agreement, Canadian internal transportation costs are an important element in the calculation. Those internal transportation costs are substantially higher during the close-of-navigation period than in the open-water season and this has the effect of making something like a 9 or 10 cents per bushel difference between a minimum price established in February and a minimum price established in April, the one being based on closed navigation costs and the other on open navigation. This, I think frankly, has certain disadvantages. The second consideration is also associated, but in a different way, with inland transportation costs. If you are going to accept a deep interior point it is absolutely essential that the normal route to the seaboard and the normal cost of moving wheat from the interior point to the seaboard should be readily calculable at any time. The existence of possible alternative routes with alternative costs would provide an unnecessary complication in my view.

I think myself, therefore, that a rigid c.i.f. basis for determining international prices is unsatisfactory. This does not mean, and I want to emphasize this again, that you cannot do your policing of any system you institute at the c.i.f. end of the transaction. I think, therefore, the choice lies between two possibilities. One possibility is to express the international price on an f.o.b. basis - not at an f.o.b. price applying uniformly to every country but on a basis which will allow equality of opportunity in every importing market. The other possibility is to express the international price at an interior point, similar to the Lake head basis under the present Agreement. I would add that I am not quite sure now whether the arguments which led people fifteen years ago to select the Lake head as the base point have quite the same force today as they did fifteen years ago. This is obviously a point for consideration by delegations.

May I now pass on to the third element of this brief review and consider just for a moment what criteria should be applied to the choice of the reference wheat. I would suggest for your consideration that the following points should be taken into account. Firstly, the reference wheat should be regularly traded on international markets, and secondly, it should be widely traded. To select a wheat which has a relatively limited performance in international trade would create considerable difficulties in the administration of the system. If for example, you wish to use the flexible f.o.b. system of expressing prices which enables all exporters to land their wheat in the country of destination on fundamentally competitive terms, this in turn means that there must be regularly and readily available current freights from the country producing the reference wheat to virtually every important market in the world, because the system cannot work unless this information is available.

In the case of Canadian wheat at the present time there are very few destinations for which either from the west coast or from the St. Lawrence there are not realistic freight rates available. This is important because the whole of this system depends on the availability of regular and not nominal rates of freight. Similarly I think that problems will undoubtedly arise if there is any degree of irregularity in the appearance of the reference wheat on world markets. I am not sure that its actual share of world trade is necessarily a criterion of the first order, but I do believe that it is essential that whatever wheat we select should be traded widely all over the world and should be traded regularly on international markets. Having said that, I think any other criteria affecting the choice of the reference wheat may bring us into point (v) and perhaps should be left for further discussion on point (v) and not at this stage. As you remember, point (v) raises the question of the inter-relationship - the link - between coarse grains and wheat. It may be that this is an argument for using a soft wheat as the reference wheat for the international price, provided always that it also satisfies the other criteria. I do not wish, however, to anticipate this aspect of the problem.

One further criterion which is absolutely essential to the selection of the reference wheat is that it should be capable of being precisely defined in terms of its grade or quality, so that the necessary quality differentials when worked out can be derived without undue difficulty from the reference wheat. In the case of Canadian hard wheat the grades are clearly defined and are regularly quoted and there is no ambiguity or uncertainty on this score. This criterion can be satisfied by other wheats as well, but it is highly important in my judgement that this degree of precision in definition should be capable of being applied to the reference wheat.