

**From Growth to Development?**  
**The Influence of Politics, Religion and Economics**  
**On Prairie Agriculture in Canada**

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## **Abstract**

The Canadian government encouraged agricultural settlement on the prairies in the late nineteenth century. A few decades later the region was the world's largest exporter of wheat. Many academics credit the 'wheat boom' with transforming Canada into a developed country and view the government's role in promoting prairie agriculture in a positive light. The emergence of a broad-based agrarian populist movement, fueled by farmers' discontent, and the collapse of the wheat boom during the Depression of the 1930s are inconsistent with this interpretation of events.

Political pressure led to regulation of grain marketing, handling and transportation, and federal government institutions played a dominant role in prairie agriculture in the immediate post-war period. The unintended consequences of these interventions contributed to a second flare-up of popular discontent and ultimately led to a sharp reduction in government involvement in the sector. The unwinding of several key initiatives in recent decades illustrates the circumstances under which longstanding policy initiatives may be reversed in order to avert a looming crisis.

The New Institutional Economics and the work of Joseph Schumpeter provide a framework for examining the reciprocal influence between institutions and economic performance. Schumpeter's insights into why institutions are modified in ways that affect the trajectory and rate of technical change are used to explain how government intervention amplified the wheat boom, exacerbated the damage done during the ensuing downturn and contributed to the declining competitiveness of prairie agriculture after World War II.

The history of prairie agriculture illustrates the origins of support for intervention, its enduring popularity, its cumulative economic costs and, ultimately, why it was unsustainable. It highlights the importance of the questions 'who benefits?', 'who pays?' and 'who decides?' when government intervention is advanced as a solution to an economic crisis.

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### Statement of Originality

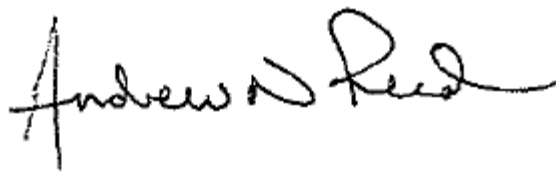
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**July 27, 2016**

It is beside the point to say that the ultimate result was not originally intended, as it would be wrong, in view of the way in which history is made by the concatenation of a series of highly improbable coincidences, to say that it was inevitable. Yet it did happen, and the reason for its happening is not too difficult to uncover. What is puzzling is the apparent lack of curiosity since then about how we got into this rut. This lack of curiosity is perhaps the strongest reason why we are still in it.

(Darling, 1980: 148)

# **Chapter 1**

## **Introduction**

This thesis examines the interaction between government policy and agriculture on the Canadian prairies over its two-hundred year history. Prairie agriculture has long been an important component of the Canadian economy and has therefore been subject to a great deal of academic scrutiny. This chapter justifies yet another study on the grounds that a) inconsistencies in the generally accepted interpretation of the historical interaction between government policy and prairie agriculture require resolution and b) that an alternate explanation consistent with the historical record sheds light on broader questions about the origin and consequences of public policy.

The introductory chapter is divided into three sections. The first outlines how crises have changed popular opinion on the optimal role of the state and poses some questions which the study sets out to answer. The second section explains why prairie agriculture constitutes a good case study for examining the origin and consequences of government intervention. The third section outlines the structure of the thesis.

### **1 Crises and Government Intervention**

The role the state should play in the economy becomes a prominent issue whenever a crisis occurs. Between the financial crisis of 2007 and the recent Eurozone crisis, the twenty-first century is off to a turbulent start. Discussions of bailouts, austerity, fiscal stimulus and the agitation of the ‘ninety-nine’ per cent who believe their living standards are threatened are frequently in the media. Initiatives that increase government involvement enjoy widespread approbation, while attempts to reduce it are condemned. Yet examples of both occur.

The current majority view seems to be that ‘markets’ are to blame, and government intervention is therefore required. Government intervention is popular because it is widely seen as a way to alleviate the negative side effects of crisis conditions arising from ‘unfettered’ markets, and to prevent similar or worse economic crises from occurring in the future.

This consensus is puzzling to those familiar with longer term trends in political economy. For centuries, the populace struggled to reduce constraints imposed on its personal freedom and ability to make economic decisions. The signing of Magna Carta 800 years ago was



celebrated last year as an important milestone in this process. Unsteady progress towards this objective is widely credited with facilitating improvements in living standards in western democracies.

The Great Depression of the 1930s appears to have been a turning point in this trend. At that time, attitudes regarding the appropriate role for government underwent a substantial shift. Many states began actively managing the economy and government intervention directed towards improving the quality of life of the populace enjoyed considerable popularity although its effectiveness was as yet unknown. The most recent financial crisis sparked renewed interest in the events that precipitated the Depression of the 1930s and governments' responses. Less attention has been paid to assessing the impact of those interventions. Recurrent crises since interventions were made in response to the Depression raise questions as to whether they were insufficient or excessive in quantity, or inappropriate in form. It is too soon to determine whether government responses to recent crises have provided a net positive benefit, but evaluating the consequences of interventions introduced in the wake of the 1930s Depression may provide some insight.

Prior to 1930, people generally favoured a smaller role for government in order to have fewer constraints on their freedom of choice. The shift in favour of more government intervention was based on the assumption that ordinary individuals would be better off as a consequence. Its continuing popularity is perplexing in light of evidence that interventions frequently generate unintended counterproductive outcomes.

Environmental protection is but one example of this contentious issue. Concern over the impact of human activity on the natural environment increases as standards of living rise. It is often assumed that private firms, when left to their own devices, will 'externalise' costs to the maximum extent possible, and that environmental damage (e.g. pollution) is inevitable unless constraints are imposed. However, the premise that market mechanisms cannot address problems such as pollution and that government intervention is therefore necessary, is challenged by a significant literature which demonstrates environmental damage is *exacerbated* by government intervention e.g. Adler (2002a, 2002b, 2004); Bliese, (1986); Desrochers (2002a, 2002b); Harvey, (1991a); Nelson (2001, 1995); Pasour (1979a, 1979b); Reed & Desrochers (2008); and the collections edited by Anderson and Yandle, 2001; Leal and Meiners (2002); Meiners and Morris (2000); Meiners and Yandle (2003); Morris (2002); and Yandle, (1999; 1999c).

The most recent example of a large scale reduction in the scope of government occurred when the Soviet Union collapsed in 1991. In this case, an economic crisis precipitated a political collapse. The low standards of living, the environmental damage and the restrictions on individual freedom inherent in the pervasive government control characteristic of Soviet socialism were only fully appreciated after the Soviet Union disappeared. Yet despite increased awareness that too much government may be undesirable, agitation for additional intervention remains pervasive.

These introductory remarks prompt four observations, each of which suggests a question:

1. Attitudes to the role government should play in the economy change: in retrospect, the Depression of the 1930s appears to have altered public opinion from believing government intervention is undesirable to the position that more government intervention is helpful. What causes dramatic changes in public opinion?
2. Crises can lead to an increase in government intervention (as was the case with Depression of the 1930s) or to less government intervention (as was the case with the collapse of the Soviet Union). What determines how governments respond to crises?
3. The political and policy-making process may lead to interventions which have negative consequences. What causes these negative outcomes?
4. Interventions which may have negative consequences often receive widespread popular support. Why does support for intervention persist after its negative consequences are revealed?

This study analyses a specific case study in order to answer these questions.

## **2 Why Prairie Agriculture makes a Good Case Study**

### **2.1 Agriculture**

Agriculture is a sector of the economy which involves the physical environment and in which government intervention is often pervasive. Historically, increases in the efficiency of agricultural production have made important contributions to economic development. Competition among commercial producers of agricultural commodities fostered experimentation with changes in the “way things are done”, a broad definition of technical change (Boulding, 1969: 126), and led to significant improvements in the productivity of land and labour in agriculture. Land use in agriculture is an aspect of technical change more readily monitored than technical change in other sectors (e.g. Boserup, 1979).

Agriculture is also a sector where the unintended consequences of prior interventions command attention. The desirability and cost-effectiveness of government intervention in agriculture has been questioned by Rausser (1992), and Pasour and Rucker (2005)<sup>1</sup> for the United States, by Knudsen (2009) for the European Union and by Luciani (2001: Chapter 3) for Canada.<sup>2</sup> Some of these negative consequences arise when policies with diametrically opposite objectives are applied in the same jurisdiction by different branches of a single bureaucracy. Pasour (1990: 240-41) summarises his analysis of the 1986 U.S. Farm Program in the following terms:

Thus while twenty-seven billion (dollars) was spent on farm programmes to increase product prices, about half as much was spent on programmes which decreased product prices. If the dollars spent on programmes were equally efficient in achieving their conflicting interests, expenditures that decrease would offset an equal amount of expenditures that increase product prices to farmers. This suggests that \$27 billion in 1986 may have been spent on activities having little (or no) impact on food costs, farm prices, or total farm income.<sup>3</sup>

Significantly, he then continues:

However this does not suggest that the programs were neutral in impact. There are important gainers and losers from farm programs, even if the expenditures are, on average, self-defeating. The identification of winners and losers is important in understanding the political support for farm programs (1990: 241).

A number of important contributions to this literature focus on the impact of technical change. Harvey (1991a) draws attention to the negative consequences which arise when agriculture in the EU is subject to the divergent objectives of national and regional agricultural policies. Initiatives to increase agricultural productivity fall under the jurisdiction of member states whereas the Common Agricultural Policy (CAP) of the European Union intervenes in product markets and disposes of surpluses. He notes that:

The consequences of technical change clearly depend on market conditions as well as on the nature of the new technology. However in agriculture these market conditions are heavily influenced by farm policy, particularly the CAP. .... The simple economic analysis presented here *strongly suggests that it is*

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<sup>1</sup> This updated a prior study of U.S. spending on agriculture (Pasour, 1990).

<sup>2</sup> An earlier work by Richard Brody MP (1983) is a succinct statement of similar issues from a British perspective.

<sup>3</sup> For the 2001 Farm Program the numbers were \$37.8 billion to increase prices and \$11.4 billion to decrease prices for a net 'waste' of nearly \$23 billion (Pasour, 1990: 308). More recently expenditure on USDA programmes have skyrocketed: in 2015, one in seven Americans benefited from the Supplemental Nutrition Assistance ('Food Stamps') Program which subsidises food purchases for low income households at a cost of \$73.9 billion USD (McMaken, 2016).

*the policies which lead to most of the problems* rather than the pace of technological change and the scientists who promote it (1991a: 194, 197; emphasis added).

Among the problems he identifies (1991a: 185) are the damage inflicted on the natural and social rural environments and the increases in ‘unsaleable surpluses’ to which interventions to promote technology change contribute. Two bureaucracies preside over the process across the EU. Taxpayers pay both to encourage technical change (through national budgets) and to dispose of the resultant surplus production (through the European Union budget).

The Green Revolution, whose goal was to dramatically improve productivity in developing countries, involved a concerted effort by international agencies to develop new “miracle seeds” and “high-yielding varieties” of wheat and rice. Griffin (1974: xi) points out that the new technology did not revolutionize production and often helped worsen the distribution of income. Even the terminology applied to this technology has changed: it is now known simply as the ‘new rice and wheat technology’ (see also Dahlberg, 1979).

Much work on agricultural policy is prompted by a crisis, or by the desire on the part of those involved to avert a looming crisis by drawing attention to disturbing trends. Hence, for example, ‘world-wide shortages of major (temperate-zone) farm commodities, particularly of cereals’ (p. xix), “the “international crisis of 1971” (p. 3) and “the dramatic rise in the price of oil at the end of 1973” (p. 5) combined to strain international economic cooperation and prompted a major British study published as *Agriculture and the State* (Davey, Josling and McFarquhar (1976). Harvey (1980: 77) warned that “continuation of the *status quo* will lead to a serious and costly constraint on western Canada’s ability to exploit its grain growing and grain exporting potential” in his evaluation of the statutory freight rate regime for grains exported from the Canadian prairies. More recently, Harvey has drawn attention to the “insanity and obscenity in the present international agricultural trading system” caused by government intervention (1991b: 312). The “insanity” is:

...developed country competitive subsidisation..... The European Community and the United States seem bent on outspending each other to retain or conquer world markets, with the result that domestic support policies become more expensive and world market prices ever more depressed.

The “obscenity” is the juxtaposition of:

...food mountains in the developed world, contrasting starkly with shortages and famines in the developing world.... Forty-five per cent of the world’s

population is dependent on agriculture and lives in the developing world, with incomes only one-fifth of the minimal prosperity levels in the lesser developed countries. Depressed world conditions and lack of access to high-income markets are critical to their survival (1991b: 312).<sup>4</sup>

Intervention to modify the market process is frequently justified for ‘social’ reasons. Proponents of intervention assume it is necessary but sometimes acknowledge the form it takes can be a problem. They argue that there must be ‘better’ ways of achieving the social and political objectives while minimising unfortunate ‘economic’ consequences such as misallocation of resources and ‘anti-social industrial’ agriculture (e.g. Harvey, 1991b: 311). However, modifying policies can be problematic. In reviewing CAP amendments, for example, Ackrill (2000: 222) concludes that “[r]eform of the CAP has been shown to be an issue of crisis management. The policy has only ever been reformed when there was an absolute need to, frequently by the smallest amount possible.”

This observation is important both in its own right, but also as a way of explaining why little attention has been devoted to how agriculture became such a problematic sector of human endeavour. Darling (1980: 148) pointed out that lack of curiosity regarding the progression of events *leading* to situations acknowledged as undesirable is one reason the situation persists (See Epigraph above, page 5). Although he was referring specifically to freight rate regulation in Canada, appreciating the origin and evolution of unintended consequences which lead to crises may help avoid ‘similar or worse’ problems in the future when addressing current policy problems.

There are several studies of agricultural policy which examine the convoluted routes which led to predicaments subsequently referred to as ‘crises’. Knudsen (2009) deals with the origins of the EU’s Common Agricultural Policy (CAP). That study emphasised that EU agricultural policy is predominantly social policy which has “to ensure a fair standard of living for the agricultural community, in particular by increasing the individual earnings of persons engaged in agriculture” as its primary objective (2009: 9). The author makes it clear that this objective did not originate with the EU, but was inherited from the founding member states. Of particular importance is the observation that “[s]ocial policy is not a technical term with an exact meaning” (2009: 11). Koning (1994) and Tracey (1982)<sup>5</sup> also examine the precursors of EU agricultural policy. Examples for U.S. agricultural policy include Gardner (2002), Luttrell (1989), Krueger (1998), and Rapp (1988). Bates’ study of

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<sup>4</sup> He concludes this paragraph, “Action which precipitates these conditions is little short of criminal.” (1991b: 312). See also Harvey (1990).

<sup>5</sup> The sub-title of the first edition of Tracy’s book was *Crisis and Adaptation Since 1880*.

agricultural policy in sub-Saharan Africa (1981) not only describes interventions which result in negative consequences in considerable detail, but also explains *why* those policies were adopted.<sup>6</sup>

## 2.2 The International Grain Market

The discussion so far suggests that the agricultural sector offers a broad spectrum of serious problems, notwithstanding a history of remedial government intervention going back to the dawn of recorded history (e.g. Tuma, 1965). The availability of grain and the price at which consumer foodstuffs derived from it are available to urban populations has long been a central issue in political economy.

Specialisation and trade underpin improvement of economic efficiency in agriculture as they do in other sectors of the economy. For a very long time wheat was the most important agricultural commodity traded internationally.<sup>7</sup> There has, however been a long-standing debate over the desirability of trade in agricultural commodities, particularly staple foodstuffs like wheat. Wheat that would be ground into flour and baked into bread was the staple foodstuff of lower and middle income urban households in Europe when industrialisation was underway, and much of it was imported despite tariff barriers.<sup>8</sup> The Corn Laws, which protected domestic wheat production in Britain, were enacted in response to a crisis in domestic agriculture after the Napoleonic Wars. The decision taken in 1846 to repeal the Corn Laws was a triumph for those lobbying for free trade (Schonhardt-Bailey, 2006; 1991; Paul, 1980). This historic step towards free trade was reversed in 1930 when Britain introduced restrictions on its domestic milling industry which discriminated against imported grain (Federico and Persson, 2007: 100-01), reintroduced tariffs on imports with the Import Duties Act and provided direct support to farmers with the Wheat Act in 1932 (Tracey, 1982: v; Mandelbaum, 1953: 13; Wilson, 1978: 242). This constitutes just one example of the general retreat from free trade in response to the widespread economic slowdown at the time.

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<sup>6</sup> Bates introduces his study by quoting Theodore Schultz: “A major source of the problem in third world agriculture is bad policy” (1981: 3).

<sup>7</sup> In terms of value, coffee is now the most important agricultural commodity traded internationally.

<sup>8</sup> It is important to recognise that ‘wheat’ is not a commodity with uniform characteristics. There are a number of types of wheat suited to different end uses. Hence durum wheat is generally used for pasta or *couscous*, hard wheats for European style breads, soft wheats for flat breads and pastries. Wheat breeding is an attempt to tailor varieties for specific end uses and growing conditions. Within each type are differences in colour and other characteristics which affect end-use performance. Grading relates a particular load or shipment to the characteristics considered ideal for that specific type of wheat.

The importance of various suppliers of wheat to the British market changed considerably after 1846. The most significant change was the availability of wheat grown on newly ploughed land in Australia, Argentina, Russia, the United States and Canada. These were the ‘developing countries’ of the era, and access to the U.K. wheat market encouraged expansion of wheat growing.

Interaction between supply and demand influenced prices paid for wheat by British buyers. However, once Britain allowed tariff free imports, wheat supply was influenced by institutional arrangements specific to each exporting country. Prices were affected not only by weather conditions and the annual decision regarding the area to be planted to wheat made by thousands of individual farmers, but also by government policies which affected production in each source nation.

When the free trade era ended, wheat prices were also affected by the policy regimes of importing nations. Recourse, to non-tariff barriers to protect wheat growers, re-imposition of tariffs and then direct subsidisation of wheat producers by Britain, the agricultural policies of the European Union and the protection afforded the farm sectors in many countries (e.g. Japan) are all examples. The differential impact of two World Wars on the availability of wheat from various sources, and the influence of those wars on European agricultural policy are also significant.

### **2.3 The Canadian Wheat Economy**

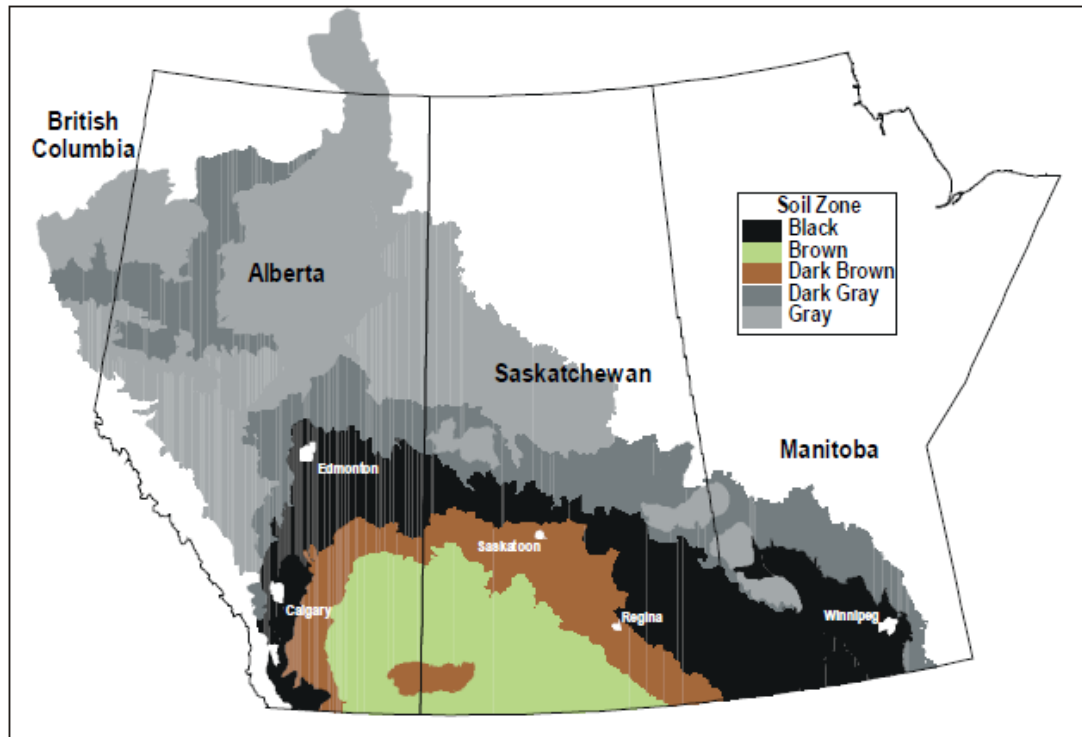
The Canadian prairies are a triangular extension of the American Great Plains north of the forty-ninth parallel of latitude. The western boundary of the region is the foothills of the Rocky Mountains. Outcroppings of pre-Cambrian rock known as the Canadian Shield form the north-eastern side of the triangle.<sup>9</sup> Although they are far from being the isotropic plain of geographic theory, the gently undulating topography and absence of trees on the southern prairies facilitated rapid expansion of wheat growing in the late nineteenth and early twentieth centuries. There are, however, distinct gradients of climate and soil which affect the suitability of the land for crop production. The main constraints on crop production are growing season moisture, which decreases as one moves west across the

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<sup>9</sup> Although the bulk of the region lies in the southern portions of Alberta (AB), Saskatchewan (SK) and Manitoba (MB) (collectively known as the Prairie Provinces), the geographical region extends into portions of the Province of British Columbia (BC). The most important of these is the Peace River District in the north east of the province. The jurisdiction of the Canadian Wheat Board (CWB) included the portions of the prairie region in BC.

southern prairies from Winnipeg, and the length of the growing season, which decreases as one proceeds north-west from Winnipeg. Both can vary a great deal from year to year.

Figure 1 Soil Zones of the Prairies



Source: Agriculture and Agri-Food Canada  
<http://www.albertasenator.ca/flashblocks/data/Soil%20at%20Risk/Prairie%20Landscapes%202000.pdf>

The majority of the wheat Britain imported from Canada after 1900 was grown in the prairie region. In 1846 this region was under the jurisdiction of the Hudson's Bay Company (HBC) which shipped furs to Europe via Hudson's Bay. At the time, what would become the agricultural portions of the Prairie Provinces of Manitoba, Saskatchewan and Alberta (AB) was the home of bison herds which provided sustenance for aboriginal tribes and those engaged in the fur trade.

Canada came into existence as a nation in 1867. Transformation of the prairie region into a source of wheat for the British market was a 'development project' implemented by the Canadian government in the late nineteenth century. Its objective was realised and the region became the largest supplier of wheat to international markets in the 1920s.

The importance of wheat exports to the Canadian economy in the first three decades of the twentieth century led to the collection of considerable data and close scrutiny by academics from a broad range of disciplines. The prairie 'wheat boom' is generally portrayed by



economic historians as a pivotal episode in Canada's economic development: a 'growth spurt' between 1896 and 1913 that lifted Canada from being one of many 'developing' nations into the elite ranks of 'developed' countries. Insofar as Canada as a whole was concerned, the prairie settlement component of the national policy was a great success: the prairies were settled, the farms established there grew a lot of wheat, the backward and forward linkages associated with the wheat 'staple'<sup>10</sup> stimulated domestic economic activity, and the export of wheat to the British market enhanced Canada's status in the British Empire.

The prairie grain economy also attracted a great deal of attention from historians, political scientists and sociologists because those producing wheat for export were frequently dissatisfied with the economic rewards they received for their efforts. They channelled their discontent into a politically potent agrarian populist movement. This movement provided the initial impetus for the sense of alienation residents of 'the West' feel towards Central Canada and to federal government policies they regarded as biased in favour of those in the more populous 'East'.<sup>11</sup> Policies promoting the exploitation of other staples added to regional discontent: coal during the settlement period, then pulp wood, non-ferrous mineral deposits and, more recently, oil reserves. It was the scale of agricultural settlement and number of individuals affected that made the dissatisfaction arising from frontier wheat particularly noteworthy. The 'dysfunctional consequences' of resource booms, particularly those that occur on the frontiers of 'developing' countries have much in common with those evident on the Canadian wheat frontier (e.g. Barham and Coombes, 1996; 1994; Barham, Bunker and O'Hearn, 1994; Corden and Neary, 1982).

Evaluating government agricultural policies is usually complicated by the fact that domestic markets are the primary destination for output. The response of urban consumers to food shortages and price increases, particularly in countries with low per capita incomes

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<sup>10</sup> The staple theory of economic growth focuses attention on variations in the impact that different exported commodities have on the domestic economy. Canadian economic history is frequently couched in terms of a succession of staples, beginning with cod (e.g. Watkins, 2003; Innis, 2003; Mackintosh, 2003).

<sup>11</sup> In the Canadian context, the "West" generally implies the Prairie Provinces and not BC. These provinces lie not only west and considerably further north than the country's most populous region lying between Windsor, Ontario and Quebec City. From the perspective of 'Westerners', the "East" is usually a disparaging allusion to financiers in Toronto and the federal government in Ottawa, in other words to Central Canada rather than the Maritime provinces. When the Chairman of the Commons Committee reviewing proposed changes to statutory freight rates charged on grain leaving the prairies (who happened to be from the Maritime province of New Brunswick) challenged the practice of western Canadians equating 'eastern' Canada with Ontario and Quebec, slighting the Maritime Provinces in the process, the Deputy Minister of Transport retorted that as an Albertan, he considered eastern Canada the entire country east of the Saskatchewan-Alberta border (Kroeger, 2009: 184).

where foodstuffs claim large shares of household income, is potentially destabilising. The Russian revolutions of the early twentieth century and the Arab Spring uprisings early in the twenty-first century are prime examples. However, export markets have accounted for the majority of prairie agricultural commodities, so the attitudes of Canadian voters and taxpayers towards policies affecting agriculture in the region have been little influenced by their role as consumers.

The Depression of the 1930s devastated the agricultural economy of the Prairie Provinces. Perversely – it will be argued -- the coincidence of the Canadian ‘wheat boom’ of the early decades of the twentieth century and the era of free trade in wheat led ‘*laissez-faire*’ to take the blame for its collapse during the Depression. At a time when government intervention in prairie agriculture was being reduced, Conway (2006: viii) wrote:

(Recent) strategies...have been largely inspired by a return to eighteenth and nineteenth century models of free trade and free markets (as) a cure for the West’s problems that had already been tried up to the Great Depression of the 1930s and found wanting.

The chapter devoted to the Depression in a history of Canada covering the period 1922 to 1939 is titled “The Crisis of Capitalism” (Thompson and Seager, 1985: Chapter 9). Conway (1979: 85) uses the same phrase.

The federal government’s response to the collapse of the prairie economy in the Great Depression had two objectives: it was an attempt to sustain the sector through circumstances considered extraordinary in terms of their severity and to prevent recurrence of depression conditions by curbing the excesses of ‘unfettered capitalism’ blamed for the downturn. Similar objectives are inherent in arguments advocating more rather than less government intervention in the face of recent crises.

The prairie region was the last of several regions drawn into the international wheat trade in the nineteenth century (Weaver, 2003: 250ff). The late entry of the prairies was not an accident. In comparison with land recently converted to cereal production elsewhere, the Canadian prairies in the late nineteenth and early twentieth century was relatively ill-suited to growing wheat and remote from ocean ports. Overall, demand for wheat was growing rapidly at the time and commercial production became viable on the prairies as production and transportation costs declined due to technical change. However, farmers were extremely vulnerable to changes in the international wheat market. This happened after World War I (WWI) when production in continental Europe rebounded and southern

hemisphere suppliers returned to the market, and during the Depression when demand for imported wheat fell by a third (de Hevesy, 1940: Appendix 9, Wilson, 1978: 241-246).

The generally accepted interpretation of the history of prairie agriculture attributes the collapse of the prairie wheat economy in the 1930s to the inherent short-comings of the '*laissez-faire*' capitalism that prevailed during the Canadian wheat boom. A series of escalating crises which punctuated the wheat boom in the decades preceding the crash of 1929 are cited as corroborating evidence. This interpretation then ascribes the gradual recovery of the wheat economy to the government intervention prompted by the depression, and uses the correlation between the recovery and government intervention to justify the conclusion that government intervention is essential to avoid the inadequacies of 'unfettered markets'. Failure to heed this lesson from the Depression risks a similar or even more severe future tragedy (e.g. Conway, 2006: 377, 382-3).

This view appears to have some validity if one looks at the situation on the Canadian prairies in the first half of the twentieth century in isolation. During the first two decades of the century the prairie farm population was vexed with the 'monopoly capitalists' who stood between them and the market for their main commodity, wheat. In addition, the regional economy depended heavily on wheat production and exports, both of which suffered devastating declines in the 1930s. It is also true that intervention to support the prairie grain economy and negotiate international agreements to stabilise the wheat market coincided with an increase in wheat prices and a reduction in the burdensome stocks of wheat carried over from one crop year to the next.<sup>12</sup> However, when attention is shifted to the entire history of prairie agriculture, significant inconsistencies emerge.

First of all, agricultural settlement on the prairies was a nineteenth century government-sponsored 'development project'. Canada spent lavishly to create the institutional infrastructure necessary to facilitate agricultural settlement on the prairies and connect the region by railways to the outside world. But the expected flood of settlers did not materialise. For four decades prior to 1900, Canada was a net exporter of people to the United States.

Second, the rapid settlement of the region that took place after 1896 and the subsequent wheat boom is generally taken as evidence that the government's prairie settlement policy

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<sup>12</sup> 'Crop years', used in the context of the prairie grain economy, run from August 1 just before the harvest of spring sown crops to July 31 of the following year.

was successful. Yet if this were true, why did so many settlers abandon their homesteads and why were so many who did persevere dissatisfied with their lot? Dales blames the high regard for Canada's policies of economic nationalism on the unwarranted influence wielded by historians. He points out that:

Economic theorists are concerned with making the best use of given resources (owned by households, firms or a nation) while historians, as a result of their interest in time and change, tend to become primarily concerned with the cause of growth of resources and to write off problems relating to the efficient use of given resources as problem in the "second order of smalls".....While the study of accretion of resources to an economy is of obvious importance, the trouble with the historian's game is that there is nothing to minimise or maximise, and therefore no basis for ending the game and declaring a winner. There is no end, short of world conquest, to the accumulation of resources within national boundaries (1966: 7-8).

The third inconsistency lies in attributing the success of prairie settlement to an enlightened government-sponsored initiative prior to 1929, but then blaming '*laissez-faire* capitalism' when everything fell apart in the Depression. Steps taken to implement the prairie settlement policy involved concerted public sector effort and considerable expenditure of public funds, the antithesis of *laissez-faire*.

Fourth, if the post-Depression era of intervention *had* remedied the difficulties it ostensibly set out to address, the story would have a happy ending and there would be no need for this re-appraisal. Yet prairie agriculture lurched through another series of escalating crises. After 1980, three key interventions that formed the basis of state control of the prairie grain economy were removed. These were long-established institutions, and hence the "effort and trauma" required to remove them was substantial (Harvey, 2008: 99; 2001: 574). This was very much the case with the steps taken to end grain freight rates fixed at nineteenth century levels by federal legislation and the state monopoly over sales of prairie wheat and barley, which were bitterly opposed by prairie farmers. Nonetheless, the regional agricultural economy adjusted to the new reality forced on it by the reversal of longstanding policies, and is now more competitive in international markets, is attracting significant investment and the sustainability of land use practices has improved.

This study of the interaction between government policy and agriculture on the prairies challenges the generally accepted interpretation that the post-Confederation policies of the Canadian government were an unqualified success, that the wheat boom was a pivotal episode in the development of the Canadian economy, and that the Depression which

devastated prairie agriculture in the 1930s was a “crisis of capitalism”. In doing so, it suggests answers to the questions raised earlier in this chapter (see above, p. 12).

This study considers the entire two hundred year history of prairie agriculture. At the outset, the region was a blank canvas without any of the institutional infrastructure the Canadian government would subsequently provide. The main advantage of such a long term perspective is that the consequences, adverse or otherwise, of particular policies may not reveal themselves in the short term. This long term perspective also reveals that the history of prairie agriculture has been a succession of crises. The *severest* crises have the potential to prompt sharp policy changes and become turning points in the region’s history. Settlement of the prairies was adopted so enthusiastically as a national priority after 1867 because it was seen as a solution to the crisis Canada West faced in the middle of the nineteenth century. The Depression crisis in the 1930s marked the onset of the period during which the state actively managed the prairie grain economy. The looming collapse of the prairie agricultural economy in the final decades of the twentieth century prompted the abandonment of several longstanding interventions.

### **3 Structure of the Study**

The next chapter (Chapter 2) outlines the theoretical framework applied in the subsequent examination of the history of prairie agriculture in Canada and the inter-country comparisons that follow the Canadian case.

The four historical chapters (3-6) address the interaction between government policy and prairie agriculture in chronological order. In each case this discussion is structured as follows:

- The crisis that led to the interventions introduced during the time period
- The ideas circulating at the time
- The interest groups which influenced policy-making, how a particular subset of current ideas was used to bolster their case, and the incentives which made specific policies attractive to influential groups
- A brief synopsis of the key interventions during the time period
- Their consequences for prairie agriculture
- Likely outcome in the absence of those interventions

The discussion in the first three sections outlines how prominent interest groups selectively used ideas in vogue at the time to bolster their arguments for government intervention in response to a crisis. The consequences of interventions generated by the political process at

a critical juncture in the history of prairie agriculture are important because they set the stage for the political response to the next crisis. The complicated and often protracted history of how specific interventions materialised out of the political process is less important. For this reason, less detail is provided.

The first historical chapter (Chapter 3) deals with the attempt to transform the prairie region into a source of wheat for international markets after Canada became a nation in 1867. This was prompted by the position in which the colonies found themselves when Britain turned away from mercantilism and the United States appeared to be interested in expanding its territory. Creating the institutional and transportation infrastructure expected to facilitate rapid settlement represented a huge financial burden for a newly constituted nation. Agricultural settlement of the prairies was considered crucial to ensuring Canada's territorial integrity. The absence of any serious challenges to Canadian sovereignty, notwithstanding the region's inability to attract settlers prior to 1896, casts doubt on this reasoning. The counterfactual suggests why a much less ambitious programme of public spending would likely have sufficed.

Chapter 4 starts in 1896, when the newly elected Liberal government faced a crisis because its predecessors' investments had failed to attract the anticipated volume of new settlers to the prairies, and ends in 1929 when wheat prices dropped abruptly. During this period the government redoubled efforts to attract immigrants to the prairies. Settlement increased dramatically and the 'wheat boom' -- which many regard as proof that efforts to settle the region 'worked' -- followed. The wheat boom is usually viewed as the 'take-off' event in Canada's economic history which propelled the nation into the ranks of the 'developed' countries. The concluding counterfactual suggests that government intervention that stimulated the expansion of prairie agriculture after 1908 counterproductive.

The Depression of the 1930s which devastated prairie agriculture is the crisis which begins Chapter 5. The policy response to the Depression and World War II led to a high degree of government involvement in the marketing and transportation of prairie grain in post-war decades. However, this heightened level of intervention did not insulate the sector from crises, and the looming collapse of the prairie grain economy emerges as the crisis addressed in Chapter 6. The counterfactual in Chapter 5 considers why a much less extensive prairie agricultural economy would have been more resilient to the Depression, and the extent to which Depression-era interventions in wheat importing and exporting countries impaired the functioning of the international wheat market.

A split which developed in prairie farmers' organisations was an important factor in the response to the looming collapse of the prairie grain sector addressed in Chapter 6. During this period prairie farm groups claiming government intervention was the problem, not the solution, challenged the mainstream view that increased government spending was the only solution to farmers' problems.

By the early 1980s, the federal Ministry of Transportation realised that its spending on prairie agriculture was unsustainable. Steps taken in the 1980s to deal with the statutory freight rates charged on agricultural commodities leaving the region by rail was the first indication of a reversal in government policy towards prairie agriculture. Despite vociferous opposition and dire predictions that a 'return to *laissez faire*' was bound to result sooner or later in a disaster equalling or exceeding that of the Depression of the 1930s, three of the most significant government interventions affecting the sector were removed. The consequences have been dramatic. The combination of poor crops and sharp increases in railway freight rates resulted in a number of years in which the net income of prairie grain farmers *in its entirety* came from government programmes. Yet the sometimes painful adjustment to the new circumstances has resulted in a much more diversified crop mix, virtual elimination of fallow from the crop rotation, an increase in the proportion of farm cash receipts generated from livestock and massive investment in the modernisation of the grain handling and transportation (GHTS). The counterfactual in Chapter 6 suggests two possible alternatives: the first considers the likely outcome if no steps had been taken to address the lack of investment in the GHTS, deregulate railway freight rates and end the Wheat Board's single desk authority to sell prairie wheat and barley; the second considers the likely outcome of a 'big bang' strategy whereby these institutional bottlenecks are dealt with in one fell swoop instead of a labourious step-wise process taking three decades.

Chapter 7 concludes the study. It points out that the model developed in Chapter 2 explains the pattern of events in each of the four time periods in the history of prairie agriculture. As Schumpeter anticipated, constraints imposed on the process of creative destruction precipitated the slide of prairie agriculture into socialism. He did not, however, foresee circumstances under which the reversal of this slide would occur. Yet this did happen in prairie agriculture, with the result that the creative/destruction process re-started and 'development' in the Schumpeterian sense finally got underway.

Although the case study demonstrates that the development of prairie agriculture was handicapped by policies whose objectives were settlement of the region and exportation of

wheat, the policy handicaps under which wheat growers in other exporting regions laboured were different and in some instances even more onerous. The institutional evolution of two of Canada's international competitors – Russia and Argentina -- is profiled in order to show how counter-productive intervention at certain junctures in their history handicapped their international competitiveness in agricultural commodity markets. The conclusion also includes a counterfactual history that spans the entire history of the region since 1896. Attention then shifts to why many of the policies adopted to 'help' the prairie grain economy seem to have failed. The final section considers some opportunities for further research.



## Chapter 2

### Theory and Methodology

The prairie settlement component of Canada's national policy was a success inasmuch as the region became a major exporter of agricultural commodities. However, this study argues that the high cost and adverse consequences of interventions implemented to expand the prairie grain economy after 1896, and to keep as much of it functioning as possible after the Depression, were ultimately counterproductive for prairie wheat growers and placed a heavy burden on taxpayers. The sharp reduction in the federal government's involvement in the sector in recent decades was a direct consequence.

The argument that many of the remedial post-1896 interventions were counter-productive hinges on divergence between the trajectory of the prairie grain economy *with* those interventions – which is available in the historical record – and a counterfactual path outlining what would likely have happened in the *absence* of those interventions. The divergence between the 'historical' and 'counterfactual' circumstances outlined in this study suggests that these interventions caused significant misallocation of human, fiscal and investment capital. Government spending on prairie agriculture was unsustainable because the mounting opportunity costs became politically untenable. Adjusting to post-intervention circumstances was painful for those directly affected. Furthermore, the undesirable consequences of intervention were unnecessary and avoidable.

This chapter outlines the theory and methodology used to make these arguments, and provides a schematic model of the evolution of prairie agricultural policy. The theory section identifies what to look for in the history, while the methodology describes how the history will be examined to confirm or deny the theory. The model suggests causal mechanisms that explain the policies adopted at four critical junctures.

The theoretical framework is based on the New Institutional Economics (NIE) and complemented by the work of Joseph Schumpeter. The New Institutional Economics provides a conceptual framework that looks at the relationships among a policy process, a market process and society at large in order to show how these relationships affect economic performance. Schumpeter is rarely mentioned in the NIE literature, but many aspects of his work involved institutional change and his understanding of the way the world works complements the institutionalist approach. Critical comments on the

relevance of the Schumpeterian explanation identify important issues the study must address and suggests the hypothesis the case study will test.

The thesis uses the analytic narrative methodology to identify patterns in historic events. An analytic narrative is a means of identifying causal relationships in the history of prairie agriculture. Those patterns may conform to expectations suggested by the hypothesis put forward. Outright rejection or modification of the theory is required if historical events are not consistent with those anticipated.

The final section lays out a model of prairie agriculture in schematic form, dividing its history into four periods. The crisis that begins each transition from one period to another is a potential turning point in terms of policy direction. Each of the four turning points in the history of prairie agriculture resulted in a different policy response: the decision to pursue a bold and novel policy, a decision to persist with that policy when it was not effective, a fundamental change in the institutional arrangements of prairie agriculture involving direct government involvement and, most recently, the reversal of those policies in order to reduce the scope of government intervention in the sector.

## **1 Theoretical Framework**

### **1.1 New Institutional Economics**

The New Institutional Economics is an umbrella term covering attempts to understand how institutions explain variations in economic performance.<sup>13</sup> Williamson (1975) coined the term to suggest improvements to the ‘Old Institutional Economics’ which recognised the importance of institutions and criticised mainstream economists for ignoring them, but was unable to offer a plausible alternative theory.

The New Institutional Economics has attempted to develop that theory by relaxing some of the unrealistic assumptions of mainstream economics (e.g. perfect knowledge), adopting an evolutionary approach (which highlights incremental change over time and space), and emphasising empirical observation over deductive reasoning. It is rooted in the work of Coase (1937), who pointed out that reducing transaction costs is the ultimate objective of private firms. The NIE recognises that institutions, broadly defined, have the same purpose. Its objectives are to understand the determinants of institutions, to explain their evolution over time, and to evaluate their impact on economic performance, efficiency, and

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<sup>13</sup> A wide range of terms are used for studies that give institutions a prominent role. “Historical institutionalist” (Pierson, 1993: 596) and “new-institutionalist” (Finbow, 1993: 672) are commonly used. New Institutional Economics is adopted as being the broadest umbrella term.

distribution. However, the involvement of a broad spectrum of disciplines in this initiative highlights inconsistencies which have yet to be resolved. Although NIE asks the interesting questions about why societies evolve in different ways, a unified theory is yet to emerge. Consequently the NIE is sometimes referred to as the institutionalist ‘approach’ which utilises theories from a broad range of disciplines and sub-disciplines.<sup>14</sup>

Asking the right questions is, however, a necessary first step. In NIE, institutions in their broadest sense “reduce uncertainty by providing a structure to everyday life” (North, 1995: 3).<sup>15</sup> They are the formal and informal rules which constrain the behaviour of political and economic actors.

To explain divergent societal trajectories it is necessary to isolate the factors which interact to generate the institutions specific to those societies.<sup>16</sup> A distinction between policy formulation which takes place in the political sphere and the consequences of policy -- determined by the way society reacts to formal rule changes -- is implicit in the NIE approach.

The distinction between the ‘market process’ and the ‘political’ or ‘policy-making process’ is also important in this case study.<sup>17</sup> The use of the term ‘market’ in this study is confined to voluntary transactions and decisions made by private parties, or ‘economic actors’.<sup>18</sup> It is nevertheless important to acknowledge that the formal landscape within which these

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<sup>14</sup> This is not a study of economic thought, so it suffices to say that some individuals associated with these sub-disciplines take issue with the approaches to which others adhere. The work of Stiglitz on information asymmetries is considered an important contribution to NIE, but his misinterpretation of the ‘Coase theorem’ leads him to quite different conclusions from others working on NIE-related themes (e.g. Pennington, 2011: 26-40; esp. 39-40). Conflicts also arise within the individual sub-disciplines. For example, Buchanan and Tullock, considered the co-founders of the Public Choice sub-discipline, have quite different views on the influence ideas exert on policy discontinuities. Compare, for example, Buchanan and Wagner (2000) and Tullock (1986).

<sup>15</sup> Loasby (2000: 305) offers an alternate: “It is by preventing the exploration of many possibilities that institutions economise each individual’s scarce resource of cognition and focus the attention of that individual on a particular range of options.”

<sup>16</sup> If the socio-economic evolution of a society as a whole is taken as the frame of reference, it becomes impossible to establish causal relationships between its components. Whether or not this is necessary is an ontological issue. Post-modernists and adherents of the Chicago School of public choice theory subscribe to the Panglossian fallacy that “whatever is has evolved, and whatever has evolved necessarily represents the most desirable or efficient state of affairs” (Pennington, 2011: 41; see also Harvey, 2001: 566). Institutions matter because individuals are not perfect. An ideal institutional environment would eliminate the adverse consequences originating in two key human shortcomings: self-interested behaviour and imperfect knowledge.

<sup>17</sup> It is particularly important given the influence of public choice theory its discussion of ‘political markets’ in which ‘policy entrepreneurs’ operate.

<sup>18</sup> The extent to which government has become involved in the economy makes it important to define the term ‘market economy’ or ‘*laissez-faire*’ economy. This study uses the classical liberal definition of a *laissez-faire* economy, namely a minimal or ‘night-watchman’ state in which government provides the rule of law which mediates disputes between private parties and enforces property rights.

decisions and transactions are made is the cumulative result of interventions generated by the political process. Some of this institutional infrastructure is beneficial because it reduces transaction costs. However, it will be argued that some of the institutional constraints imposed on prairie farmers *increased* aggregate costs and hence were counterproductive. Enduring popular support for public sector interventions which are counterproductive, at least in the medium or longer run, is one of the puzzles this study hopes to solve.

Four aspects of the NIE approach are important in the context of this dissertation.

1. The explicit distinction made between a political process which generates interventions that change the institutional environment and the consequences of those changes in the institutional environment once they take effect
2. Explicit acknowledgment that there is two-way causality between institutions and economic performance (e.g. Pierson, 1993; Hubbard, 1997: 243)
3. Recognition that changes in institutional constraints may have either adverse or beneficial impacts
4. Emphasis placed on comparative assessment of the merits of different institutional arrangements

The term *institutional environment* is used in the NIE for the formal (explicit) and informal (implicit) rules “that nurture, protect, and govern the operations of a market economy” (North, 1990: 3).<sup>19</sup> The primary focus in this study is *changes in the formal rules through public policy interventions*, and the economic and political consequences that stem from those changes. Such changes may be thought of as ‘top-down’ in the sense that they are imposed by a political or collective action process..<sup>20</sup>

Individual or collective choices are generally described as ‘rational’, but this rationality is severely constrained by two important human limitations. These are the inadequate

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<sup>19</sup> Sometimes these are referred to as the ‘hard’ institutions imposed on society by its governing structures, as opposed to ‘soft’ or informal institutions which develop spontaneously (Pennington and Barra, 2009: 14-15). The extent to which informal institutions frustrate attempts to ‘improve’ the ‘hard’ institutions is a frequent theme in ‘development studies’.

<sup>20</sup> The *institutional environment* is therefore distinct from *institutional arrangements*. The latter govern the interactions of individuals within organisations (of all types) and between organisations (Williamson, 1985, 1996). Once again, these may be formal or informal. The benefits of such formal arrangements are acknowledged when individuals and organisations voluntarily agree to be bound by them. *Institutional arrangements* are therefore the result of a *bottom-up* process.

information upon which decisions are made (the knowledge problem) and the incentives to which individuals respond (the incentive problem).<sup>21</sup>

Demsetz (1969) labelled the notion that public sector actors are necessarily and consistently benevolent and altruistic the ‘nirvana fallacy’. Disagreement over the ‘nirvana fallacy’ is one of the main impediments to reaching a consensus regarding a theory of institutional economics.<sup>22</sup> The Virginia School of public choice confirms the nirvana fallacy by applying economic insights gained from studying the allocation of resources by self-interested actors in the private sector to the behaviour of political actors. This perspective claims that self-interest in the public sector is much less likely to generate socially desirable outcomes than in the private sector due to the relative inefficiency of political markets.<sup>23</sup>

The private sector responds to changes in the formal institutional environment that result from public sector intervention. The form that response takes is heavily dependent on the informal rules in effect, and may be quite different from that anticipated by those who designed and implemented the (formal) intervention. Because that response will in turn have consequences, “new policies create new politics” through feedback.<sup>24</sup> Either ‘mass publics’ or special interests may be media for that feedback, but both the form and the consequences are different. The democratic process provides the feedback mechanism whereby the impact of changes made to the institutional environment on mass publics can influence subsequent modifications of that environment. The effectiveness of this feedback depends on a number of assumptions, namely that elected governments influence the policy agenda, that re-election prospects motivate politicians, that the dominant influence on policy formulation is the democratic process, and that the behaviour of politicians and public sector bureaucracies is conditioned by the general will.

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<sup>21</sup> For more detailed elaboration of these ideas see Pennington, 2011: 20-25.

<sup>22</sup> The other major perspectives in public choice theory are the Chicago School which concentrates “on the pure [neo-classical] economic theory of collective decision making,” and the Rochester School which applies sophisticated statistical and mathematical techniques to public choice issues. William H. Riker, a prominent figure in the ‘Rochester’ school, is credited as being the first to apply game theory in public choice contexts and for drawing attention to the importance of coalitions among interest groups (Butler, 2012: 34-36).

<sup>23</sup> “In the government sphere, as in the market, there seems to be an invisible hand, but it operates in precisely the opposite direction from Adam Smith’s: “an individual who intends only to serve the public interest by fostering government intervention is ‘led by an invisible hand to promote’ private interests ‘which was no part of his intention’” (Friedman & Friedman, 1980: 5-6; Friedman, 1986:138). Or, as Kurrild-Klitgaard (2005: 5) observes, the invisible hand of self-interest leads decision-makers “to an end that might not have been part of their intention, i.e., they are led down the road to serfdom”. See also Pennington, 2011: 24-25; Jacobs, 1994; Pasour, 1979;

<sup>24</sup> Pierson (1993: 595) credits Schattschneider (1935) as the original source of this insight and the phrase quoted.

The idea that the political process can result in changes to the institutional environment that are counterproductive is apparent whenever economic performance falters in a particular jurisdiction for an extended period of time.<sup>25</sup> This prompts the questions why institutional modifications which have counterproductive consequences receive enough support to dominate the policy agenda and why they persist for protracted periods once those consequences are widely known.

According to Nelson (2008: 7), there is a division among ‘new institutional economists’ as to whether optimal institutional arrangements can be devised by “deliberate analysis, planning and implementation.” He points out that North and Eggertsson, both prominent exponents of the institutional approach, eventually adopted the position that “institutions could not be effectively planned”. If they are correct, the potential for mistakes which lead to unfortunate consequences exists whenever formal institutions are imposed by a political process. North (1990: Part III) deals explicitly with this issue. The more recent work of Acemoglu and Robinson (2012) expands on this theme. They demonstrate the inverse relationship between general well-being and the presence of ‘extractive institutions’ imposed at the behest of special interest or elite groups in a particular society. Bates’ (1981) study of agricultural policies in post-colonial Africa explores the origin and consequences of extractive institutions in considerable detail.

Studies beyond the NIE umbrella have sought explanations for societal breakdown in terms of institutional efficiency. Tainter (1988) is perhaps the best known example. He examined a number of ancient civilisations which ultimately collapsed into oblivion. He concluded that societies become increasingly complex as they devise collective solutions to common problems. However, there comes a point when the cost of the ‘solution’ outweighs the benefits provided. The society will collapse – Tainter equates collapse with a reduction in complexity – when diminishing returns cross a threshold or tipping point beyond which recovery becomes impossible. Perhaps his most significant observation is the impact collapse has on the well-being of ordinary individuals: it *improves* appreciably once the costs of maintaining the counterproductive complexities are eliminated.

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<sup>25</sup> This is the argument implicit in Solberg (1987) and other studies which attribute the divergent performance of Canada and Australia from that of Argentina after 1920 to wise public policy in the Anglo-Saxon tradition in the former and *laissez-faire* in a society dominated by the *estanciero* class in the latter. North (1990: 101-103; 117) also discusses the differences between Spanish and English speaking societies in the Americas.

The outcomes of different institutional arrangements – both formal and informal – can only be assessed in a relative sense. This insistence on comparative institutional analysis is an aspect of NIE that distinguishes it from mainstream neoclassical analysis. According to Coase, the relevant question is whether practicable alternatives exist:

Contemplation of an optimal system may provide techniques of analysis that would otherwise have been missed, and, in certain special cases it may go far towards providing a solution. But in general its influence has been pernicious. It has directed economists' attention away from the main question, which is how alternative arrangements will actually work in practice. It has led economists to derive conclusions for economic policy from study of an abstract of a market situation. It is no accident that in the literature... we find a category 'market failure' but no category 'government failure'. Until we realize we are choosing between social arrangements which are all more or less failures, we are not likely to make much headway (1964: 195).

It is for this reason that the chronological examination of the Canadian case compares what did happen, given the sequence of government-imposed changes in the institutional environment in which prairie agriculture operated, with what might well have happened in the absence of those changes. Comparisons can also be geographical, comparing outcomes in different jurisdictions.<sup>26</sup> Therefore, after considering in some detail the evolution of the institutions which have influenced prairie agriculture, the study includes a less detailed synopsis of changes in the institutional environments of two of Canada's traditional competitors in the international wheat market. These comparisons suggest that although prairie farmers may have suffered from changes in federal government policy, intervention in other jurisdictions have been even more debilitating.

There are some specific inadequacies in the NIE approach which constrain its applicability to the Canadian case study. First, it does not explicitly examine the relationship between crises and institutional change. Second, most contributions acknowledge that ideas are important, but varying opinions exist among NIE researchers as to exactly how those ideas influence the policy-making process. Third, the frame of reference is not clearly specified when the relative merits of different institutional frameworks are discussed: what may be "better" for one group may disadvantage others. Fourth, as Nelson (2008, 1) has pointed out, "...the focus in most of these [NIE] writings has been on how prevailing institutions

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<sup>26</sup> Sheingate (2001), for example, concludes that the structure of agricultural interest groups in the United States is more fragmented than it is in France and Japan, and that the U.S. government therefore has more autonomy when it comes to agricultural policy. If so, one can merely wonder at the level public sector support for agriculture might attain were American farm organisations *less* fragmented. Tweeten (2003) however, disagrees with Sheingate's appraisal, and draws attention to the recent shift in the power base of American farm organisations -- and the parallel shift in public sector support -- from the west and mid-west to the south (2003: 167).

affect the efficiency of economic allocation and action.” However, it is technical change that is the source of improvements in productivity and hence in living standards. Nelson continues, “[t]herefore, it would seem that one can understand the role of institutions and institutional change in economic growth only if one comes to see how these variables are connected to technical change.....[and here in the NIE] there remains a significant gap between aspirations and achievements.”

Finally, interest in the way political institutions work in *practice* has made public choice theory an important component of the New Institutional Economics. However much of the research involving institutions suggests that economic and social problems can be solved by “getting the (formal) institutions right”.<sup>27</sup> Yet public choice theory is itself divided on this issue. The Virginia School points out that while getting the institutions right may be a necessary condition for improving economic outcomes, it is by no means a sufficient condition.<sup>28</sup>

The public choice example illustrates a fundamental failing of the NIE – its lack of consensus on a theoretical approach to institutional problems. NIE has attracted researchers from many disciplines, and there has been an understandable tendency to apply theoretical frameworks developed in the parent discipline. Although the NIE takes great interest in the practical implications of different political structures and the institutions they influence, the various theoretical frameworks employed within public choice make it possible to choose the theory best suited to a particular argument. This is not conducive to deriving a theory of how institutions and the economy actually co-evolve. To find a way out of this impasse, attention is turned to the work of Joseph A. Schumpeter.

## **1.2 J. A. Schumpeter**

Schumpeter was preoccupied with institutions, markets, and their interaction. Gordon (1963: 141-146) emphasises that Schumpeter out-performed many self-proclaimed institutionalists of his time, without restricting himself to their specific field of interest. Schumpeter claimed that specific institutions were required for capitalism to thrive and attempted to explain the creation and destruction of those institutions (1939: Vol. 1 p. 224). Similarly, he regarded democracy as an institutional arrangement for addressing the practical problem of political

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<sup>27</sup> This is particularly true in the field of Development Economics. Land reform in general and efforts to reform post-Soviet agriculture by formalising property rights to land in particular are good examples.

<sup>28</sup> The rival Chicago School takes the position that under a given set of circumstances, institutional arrangements and the way in which they are administered are the best that societal constraints allow at any given point in time.



organization in a complex modern society, in which rivalry to attract votes determines those allowed to exercise power (1962: Chapter XXII, esp. 269). His work on the role of technical change led him to conclude that intervention by the state might have detrimental unintended consequences and, if carried too far, could prevent capitalism from improving the living standards of the populace.

Schumpeter, like many of those working today in the field of NIE, recognised the importance of asking the relevant questions (Drucker, 1983: 1). This section summarises – in desperate brevity (one of Schumpeter’s favourite phrases) – aspects of Schumpeter’s work relevant to this study. The first part provides a synopsis of Schumpeter’s theory of economic development which occurs in the absence of government intervention (Section 1.2.1). The second part summarises his concern over what happens to an economy on which interventions are superimposed, and why such interventions become politically attractive (Section 1.2.2). Section 1.2.3 addresses criticisms of the relevance of Schumpeter’s ‘vision’ in the North American context. The final section (1.2.4) considers some relevant insights from work dealing explicitly with crises, highlights the divergence between Schumpeter’s vision and his critics, and then offers two instances where Schumpeter’s approach does seem consistent with U.S. experience.

### 1.2.1 Economic Evolution in the Absence of Government Interference

Schumpeter is best known for coining the phrase “creative destruction” to describe the process of technical change. The New Institutional Economics recognises that technical change is important, but it focuses attention primarily on the competencies and structure of specific organisations (firms or bureaucracies) and the repercussions of those structures for economic allocation. It pays less attention to the macroeconomic implications of technical change or the consequences technical change might have on the political process, both of which are important aspects of Schumpeter’s work.

Schumpeter set out to fill a gap in the economic theory of his day: a way of accounting for differences in ‘the way things were done’ over time and space and, by extension, the evolution of capitalism.<sup>29</sup> He outlined the technical change process in the book translated

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<sup>29</sup> Schumpeter’s interest in the interaction between the economy and its institutional infrastructure was inspired by Marx (Rosenberg, 2011). He used the term ‘capitalism’ to distinguish allocation determined by markets from allocation dependent on alternative institutional arrangements (i.e. feudalism and socialism: had the characteristics of Soviet socialism been more widely known during Schumpeter’s lifetime he might have realised there was no need to distinguish between the two). Widespread concern over the scale of enterprises at a time when industries were capital intensive concentrated attention on

into English with the title *The Theory of Economic Development* (TED).<sup>30</sup> This theory of development involves testing “new ways of doing things” in markets. The development process Schumpeter describes is evolutionary in the sense that entrepreneurs launch new technologies (mutations) into the market where their commercial viability is independently tested (selection). The alternative translation of *Entwicklung* – evolution – supports this interpretation.

It is important to emphasise that ‘innovation’ is a process. As Metcalfe (1998: 8) put it, “[t]echnologies do not emerge fully fledged into the world, they develop painfully in a trial and error fashion, through sequences of related innovations which are very much responses to the experience of market development.” This process defies explanation in all but its broadest sense because it is spontaneous and irrational.<sup>31</sup> Time’s ‘uni-directional arrow’ is a crucial factor. Innovations cannot be ‘un-invented,’ but both their adoption and subsequent modification to improve commercial viability occur over time and space.

Schumpeter’s interpretation of the economic process has two aspects, one static, and the other dynamic. In the static component, varying amounts of resources are transformed using a fixed array of technical processes. Any increase in resources utilized constitutes *growth*. The rate of ‘circular flow’ may be increased by adding more capacity of the known technology to satisfy an increase in demand or it may occur as consequence of ‘natural’ exogenous factors.<sup>32</sup> In this agricultural case study, both the mobilisation of previously under-utilized resources (land and labour) in a ‘routine’ production process (wheat growing) and the variability of yields (production per unit of land sown) play important roles in the growth that occurs. Yields affect the *commercial viability* of crop production at any given location.

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access to capital as the key to business success. Hence Schumpeter’s preoccupation with enterprise scale and ‘monopoly capital’. This aspect of his ‘extrapolation of observable tendencies’ proved inaccurate because motivated labour has replaced access to capital as the crucial scarce resource. However, Schumpeter was acutely aware of the difficulties inherent in predicting the future trajectory of an evolving system.

<sup>30</sup> This was Schumpeter’s PhD thesis, published in 1911. The revised and shortened second edition (1928) was translated in 1934 by British economist Redvers Opie. Andersen (2012: 631) points out that a complication arises from the fact that the German word *Entwicklung* can be translated into English either as ‘development’ or ‘evolution’. He suggests that *A Theory of Economic Evolution* would be a better title than *The Theory of Economic Development*, the title given the English version of *Theorie der wirtschaftlichen Entwicklung*. This does not, however, affect the distinction between the two modes of economic activity -- ‘growth’ and ‘development’ -- which co-exist in his model of the market process.

<sup>31</sup> It was for this reason that Rosenberg (1994; 1983) referred to technical change as a ‘black box’ process: the consequences are observable, but the process itself is obscure.

<sup>32</sup> Schumpeter’s gives putting more stage coaches together (which does not produce a train) as an example of the former, and variations in crop yields as an example of the latter.

Agricultural practices used to produce wheat also changed over time and space as the area of cultivated land expanded on the prairies. Technical change occurred as wheat growing practices which had been commercially viable elsewhere were modified to suit local conditions. Having defined growth in terms of variations in the volume of resources used by a static array of technological processes, Schumpeter turns his attention to the process whereby technology changes over time. He defined *development* as the result of a dynamic technical change process which is unaffected by 'exogenous factors'. Technical change at its most efficient is endogenous to the economic process, depending only on feedback from markets. His definition emphasises this point:

By 'development' therefore, we shall understand only such changes in economic life as are not forced upon it from the outside, but arise by its own initiative, from within (1968: 63).

In other words, 'development' is what happens when technical change occurs without interventions that impair or deflect the process of creative destruction. This dynamic component of Schumpeter's schema involves an investment boom which accompanies the diffusion of a new technology and is constrained by the real economic risks borne by adoptees. The economic downturn which inevitably follows signals that further investment in the new technology would be uneconomic. Such 'normal' recessions are essential, because it is during this phase that the old technology is rendered obsolete, firms failing to adopt the new technology are destroyed, and entrepreneurial profit dissipates to re-appear in the augmented living standards of the population at large. Therefore the 'normal' recession:

....fulfils what the boom promised. And this effect is lasting, while the phenomen[a] felt to be unpleasant are temporary. The stream of goods is enriched, production is partly reorganised, costs of production are diminished and what at first appears as entrepreneurial profit finally increases the permanent real incomes of other classes (1968: 245).

Schumpeter was aware that the economy's ability to absorb a new technology would only be revealed during the subsequent recession and hence that some over-adoption was inevitable. He referred to this as "the swarm-like effect" (1968: 255ff).<sup>33</sup> In the short term, the 'dysfunctional consequences' of technical change stem from both the elimination of

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<sup>33</sup> Schumpeter's point is that 'over-investment' or over-production is likely, but cannot be determined *a priori*. In his stylised model, the recessionary period which follows the investment boom determines which suppliers remain solvent. It is only during the subsequent downturn that the extent of unprofitable investment made during the boom is revealed. Because markets are imperfect, the unprofitability of enterprises that have recently adopted the new technology is the first sign that demand is saturated. Once recognised, further investment ceases and with it rising demand for the resources required to augment capacity. Grinder and Hegel (2005: 158) make the same point: it is during the boom phase of the cycle that the waste of social capital takes place.

non-competitive technologies and the ‘correction’ required when over-enthusiastic adoption of the new technology subsequently proves uneconomic. It is this cycle of innovative entrepreneurship, the diffusion of new technology, and the subsequent reorganisation of production that give rise to business cycles. Development is essentially a continuous process of small scale adjustments constrained by market signals.

The title of this thesis alludes to Schumpeter’s suggestion that governments play a decisive role in determining whether economic activity constitutes development or growth. The difference, according to Schumpeter, depends on whether government intervention disrupts the process of ‘creative destruction’.

### 1.2.2 Economic Evolution in the Presence of Government Intervention

It should be emphasised that Schumpeter did not object to government intervention *per se*. From the perspective of the population at large, ‘short-term dysfunctional consequences’ are inevitable because the benefits of technical change only spread throughout society when normal recessions occur. In Schumpeter’s opinion, it is the legitimate business of the state to provide a social safety net to alleviate the short-term dysfunctional consequences of those recessions. However, he also emphasises that the ability of the state to provide that safety net depends on keeping the engine driving the market process – technical change -- functioning at optimum levels (1962: 69-70).

For this reason, he examines interventions which impair the creative destruction process and speculates as to why they might be popular. This appraisal leads him to consider how the institutional framework within which capitalism operates might change over time. Schumpeter’s dynamic process of innovation and creative destruction occurs in tandem with fluctuations in growth. Having acknowledged that fluctuations in *growth* occur as a consequence of ‘natural exogenous factors’ (e.g. better or worse harvests) acting on any static array of technologies, he considers the quite different impact ‘un-natural’ exogenous factors would have on a *development* process involving technical change.

Schumpeter analysed the interaction between the political and economic spheres of society in what he considered ‘late-stage’ capitalism in *Capitalism, Socialism and Democracy* (CSD) (1962).<sup>34</sup> Schumpeter did not expect capitalism to self-destruct (Elliott, 1980: 55; McCaffrey, 2009), but he warned that interventions which impeded operation of the

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<sup>34</sup> This book, written towards the end of his life, was based on a chapter in the first edition of *Theorie der wirtschaftlichen Entwicklung* removed from the subsequent German and English editions.

capitalist process – ‘un-natural exogenous factors’ -- might precipitate the atrophy of capitalism when introduced in a climate of growing hostility to markets dominated by large-scale enterprises (1962: Chapter XIII, 143-155). These ‘un-natural’ exogenous factors are government interventions which impair the mechanism of creative destruction. Schumpeter recognised that interventions of this type would ultimately transform the ‘normal’ recessions of the development process into ‘abnormal’ recessions or ‘crises’.

The “short term dysfunctional consequences” of capitalism encourage the new middle class to seek a larger share of the benefits only capitalism can provide (Rosenberg, 1992: 192). These dysfunctional consequences are inevitably exacerbated and prolonged in crises. Crises occur when intervention amplifies the downturn in the business cycle, and a succession of crises of escalating severity introduces increasingly strident negative feedback into the political process. Schumpeter saw the political influence of the new middle class growing as it experienced a succession of crises of escalating severity. However, he blames the tendency of this group to agitate for measures likely to undermine the dynamism of capitalism on the influence wielded by a key constituency traditionally hostile to markets. Schumpeter referred to this constituency as “underemployed intellectuals and political agitators”, but it also includes journalists, lawyers, academics and bureaucrats (1962: 145-155).<sup>35</sup> Their hostility stems from the apparent inability of markets to deliver “the outcomes that the intellectuals themselves want or that they think are best. They believe that the market order needs to be steered toward perfection” (Tasic, 2010: 562). In this particular, “[t]he [sixty] years since [*CSD*] appeared have surely proved Schumpeter to be a major prophet” (Drucker 1983: 5).

Schumpeter also recognised the malleability of the collective beliefs held by the new middle class. As he put it, “...the will of the people is the product not the motive power of the political process” (1962: 263). This malleability increases as crises become more severe, and the susceptibility of the new middle class to ideologies which run counter to their own best interests rises in tandem (see also Higgs, 1987: 69-72).

Interventions that constitute “significant interference with the capitalist process” become increasingly likely in a climate of growing hostility to ‘monopoly capitalism’. Unfortunately, from Schumpeter’s perspective, these measures are supplied willingly,

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<sup>35</sup> Hayek drew attention to the more general problem of a general decline in commercial morality (1986: 147-48). The class Schumpeter describes is a segment of society well insulated from Hayek’s ‘commercial realities’.

because political incentives and the preponderance of “underemployed intellectuals” in the bureaucracy are closely aligned. As he observed, anticipating public choice economics, “...was there ever a situation that politicians did *not* consider an emergency?” (1962: 339; original emphasis).

Schumpeter was acutely aware that crises have political as well as economic consequences, although in his schema they do not have economic causes (1968: 221). When the ‘short term dysfunctional consequences’ of the development cycle are magnified by government intervention they produce crises which may be protracted in duration and severe in terms of their economic impact. It is the economic consequences of increasingly severe crises that encourage lobbying to weaken the institutional environment conducive to the dynamic vigour of capitalism. Development gives way to growth as intervention slows technical change or alters its trajectory. Intervention magnifies the growth cycle and the economic consequences of the resultant crises increase the clamour for further interventions which fuel the downward spiral. Each successive crisis is therefore a potential tipping point beyond which the dynamic component of the capitalist process -- technical change – ceases to generate the productivity changes which improve living standards across the board in the medium and longer term.

The examples of ‘extra economic’ phenomena that Schumpeter indicates will disrupt ‘development’ – war (1968: 220), the sudden abolition of a protectionist tariff (1968: 221) and “a conspicuous pulling on the reins<sup>36</sup> by the central bank” (1968: 236) – are all examples of government intervention with important consequences in this study.

Three other categories of intervention should be added to this list. The first two affect the amplitude of the business cycle. These are interventions that exaggerate the “swarm-like effect’ on the upside of the business cycle and interventions which prevent the subsequent

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<sup>36</sup> Schumpeter’s diagnosis of the slow recovery from the Depression of the 1930s written at the time is illuminating in this regard, as well as highlighting his disagreement with Keynes:

“What we face is not merely the working of capitalism, but of a capitalism which *nations are determined not to allow to function*..... For any revival which is merely due to artificial stimulus leaves part of the work of depression undone and adds, to an undigested remnant of maladjustment, new maladjustment of its own which has to be liquidated in turn, thus threatening business with another crisis ahead. Particularly, our story provides a *presumption* against remedial measures which work through money and credit. For the trouble is fundamentally *not* with money and credit, and policies of this class are particularly apt to keep up, and add to, maladjustment, and to produce additional trouble in the future.” (1934: 16, 20-21; original emphasis).

Keynes argued that economic downturns were unfortunate and unnecessary, and that it was the legitimate business of the state to use countercyclical debt-financed public spending as a temporary expedient to minimize their impact.

recession from determining the sustainable level of demand for a particular way of doing things. Artificial stimuli to encourage particular forms of economic activity fall in the former category. Interventions that prevent the *destruction* of inefficient capacity fall in the latter category.<sup>37</sup> Once again, both play a significant role in the prairie agriculture case study.

Interventions designed to stabilise the economy are, in Schumpeter's opinion, a third category of counterproductive interference with the market process.<sup>38</sup> Such interventions are more likely to be adopted if the amplitude of the business cycle has been magnified by interventions of the two preceding categories, but this is not a necessary precondition. In the quote already cited (see footnote 36, previous page) he specifically mentions "remedial measures which work through money and credit" (1934: 21). Schumpeter considered many of Roosevelt's New Deal policies prime examples of measures which prevented capitalism from functioning (1962: 64). This antipathy to stabilisation follows from Schumpeter's view that recessions are a benign and necessary part of the economic process when it operates outside the reach of government interference. Inappropriate intervention prompted by crises inevitably prolongs post-recession adjustment and/or results in mal-adjustment which lays the groundwork for the next downturn. Evolution is 'chaos with feedback', and Schumpeter recognised, perhaps instinctively, that interfering with the feedback would affect the rate or trajectory of any subsequent technical change.

When Schumpeter 'extrapolated observable tendencies' he reluctantly concluded that socialism would emerge as capitalism's 'heir-apparent'. Opinion as to whether or not his prediction has already proved correct in major western democracies is divided according to the definition of socialism employed: those who define socialism in terms of state ownership of the means of production disagree that his prognosis has been realised; those who consider less direct but otherwise effective control quasi-socialism consider his expectation already confirmed.<sup>39</sup>

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<sup>37</sup> The reluctance of governments to let the destructive phase of the development cycle operate freely leads Higgs to a pessimistic conclusion: "Laissez-faire is unrealisable, too.....In today's world, no substantial group of people is prepared to accept the personal responsibilities and to shoulder the personal risks inherent in genuine capitalism – which is, after all, as Joseph Schumpeter emphasised, a system of creative *destruction*" (2005: 297; original emphasis).

<sup>38</sup> In his review of Hayek's *The Road To Serfdom*, Schumpeter (1946: 269) wrote "[n]othing, for instance can be more striking than the parallelism between some of the policies of the Weimar Republic in the twenties and some of the policies of the United States in the thirties... Nothing, finally, could be more timely than Hayek's vigorous attack upon uncritical enthusiasms for 'stabilization'."

<sup>39</sup> See especially Hegel & Grinler (2005) and Kingston (2014). The former use the German term *Zwangswirtschaft* – literally a 'compulsion economy' -- to describe situations where interventionism has

The general observation that follows from Schumpeter's work is that both the rate and trajectory of technical change are extremely sensitive to changes in the institutional environment. The distinction between land-using and land-saving technologies used by Hayami and Ruttan (1971) illustrates how intervention might change the trajectory of technical change. If the price of land is reduced (by, for example, a homesteading scheme) or a key input is subsidised (e.g. fuel) a bias is introduced favouring land-using (or extensive) practices. In the prairie context, summerfallow – the practice of cultivating land over a growing season without planting anything -- is an example. As to the rate of technical change, a high degree of state control may remove the incentive for technical change that fear of innovation by competitors normally provides.

Changes to the institutional environment which originate in public policy are also 'lumpy': they appear suddenly, disrupting the *status quo* and require those affected to adjust the way they do things accordingly. If, as is frequently the case, those interventions persist, those adjustments become embedded in the economic relationships established in the wake of the intervention. If interventions are subsequently abandoned, as was eventually the case with several which affected prairie agriculture, another much more dramatic adjustment is required.

### *1.2.3 Critiques of Schumpeter's 'Vision'*

Two American academics, Douglass North and Robert Higgs, question the applicability of Schumpeter's vision of how politics and economic sociology interact to American history. Their objections suggest they missed the point Schumpeter was making about the origin of crises, the impact of crises on the electorate and the circumstances under which the electorate may change the prevailing ideology from one which protects the institutional infrastructure of capitalism to one which undermines that infrastructure. This discussion of their objections serves to identify the theoretical issues that lead to the hypothesis developed in the following section and tested in the historical chapters of this study.

North (1978: 967) states that, "... [t]here is simply no way to impose such a [Schumpeterian] framework on the political-economic history of the past century and a half of the United States." He offers five reasons: there were no protective strata of feudal

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gone well past the point of improving the efficiency of choice to severely curbing freedom to choose. Kingston considers intervention in major western economies in response to the financial crisis of 2008 a significant turning point because bail-outs of financial institutions were the culmination of a process which first granted bank shareholders limited liability and then created central banks as 'lenders of the last resort'. Zero interest rates are also cited as evidence that capitalism is no longer operating.



groups in the U.S.; the bourgeoisie *did* successfully run the U.S. government in the nineteenth century; anti-capitalist sentiment is not the reason federal taxes have increased; conflict among propertied groups set off the growth of government regulation; and increased regulation and government spending cannot be attributed to anti-bourgeois objectives. In North's opinion, the fundamental flaw in Schumpeter's system is his reliance on a "... Marxian two-class world in which the anti-bourgeoisie gradually gain the ascendancy over the political system" (1978: 967).

North's misinterpretation of Schumpeter derives from his emphasis on 'feudal' rather than 'protective' and on 'anti-bourgeoisie' rather than 'anti-capitalist'. For historical reasons, the United States jettisoned the 'feudal' strata early on, but North acknowledges that its non-feudal substitute was specifically designed to strengthen the state's role as protector of the institutions which facilitated operation of the creative destruction process.<sup>40</sup> This protective function remained effective for a century before it unravelled. North infers, incorrectly, that Schumpeter expected a proletarian anti-bourgeoisie class to gain control over the political process and that this did not happen in the United States. As he puts it (1978: 971):

The breakdown of the Madisonian political structure was not a consequence of the 'proletarian' losers of the nineteenth century – the indigenous Indian, the ex-slave, or the protests of the Western Federation of Miners, the Molly McGuires, [and] the IWW. It was a result of conflicting propertied groups – farmers, shippers, railroad companies, manufacturers subject to foreign competition – all attempting to protect themselves from competition.

Schumpeter's interest in Marx is widely misunderstood and often discourages closer examination of his arguments (e.g. Rosenberg, 2011).<sup>41</sup> North may well have fallen into this trap. Schumpeter explicitly included farmers in his 'new middle class' and emphasised that the *anti-capitalist* ideas originated with the 'under-employed intellectuals'. Hence he argues that the sustainability of the creative destruction process is jeopardised by capitalism's success rather than its failure. Most importantly, his 'new middle class' only agitated for measures to eliminate the 'short-term dysfunctional consequences of

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<sup>40</sup> In the Canadian case, the feudal superstructure persists, insofar as the head of government is the Queen represented federally by the Governor General and at the provincial level by a Lieutenant Governor, but the protective inclination rapidly disappeared in the twentieth century. Exclusion of property rights from the Charter of Rights and Freedoms in the Canada Constitution Act, which was personally signed by the Queen in 1982, confirmed the erosion of property rights in law.

<sup>41</sup> Higgs (1987: 244) also suggests that Schumpeter's preoccupation with a Marxian class struggle prevents him from appreciating the importance of a "separate class, neither bourgeois nor proletarian, possessing sufficient autonomy to pursue interests exclusively its own, whether material or ideological" when he is discussing the role of government authorities.

capitalism' when those consequences have been exaggerated by prior government intervention which transform normal recessions into abnormal recessions or crises. Should they be successful, Schumpeter warned, the creative destruction process could be impaired to the point it could no longer continue raising living standards.

North recognises that the Madisonian protective strata worked for a century but was eroded when relative costs of using the political process declined. It served its 'protective' function until an ideological shift occurred. North acknowledges that Schumpeter *described* the fundamental change in ideological perspective in the past century "very effectively" (1978: 974), and admits that the change "is simply not amenable to interest group analysis....". North uses the U.S. farm protest movement to make his point about the importance of ideology (1978: 973):

The private gains to farmers from following Mary Lease's directive of raising "less corn and more hell" were negligible. But they did just that because of a deep seated conviction that the system was unjust.... It may be irrational for farmers to ignore the free rider problem in organizing to transfer the gains of lower transportation costs to themselves, but they did so because of fundamental convictions about the injustice of the distribution of income.... The variety of protest and reform groups that emerged in the late nineteenth century...are simply not explicable in terms of neo-classical interest group theorizing.

North implies that pressure for government intervention arises out of the disruptive influence of what he calls 'the second economic revolution'. He attributes increased demand for the government intervention and regulation evident in the United States since 1877 to changes in enterprise organisation which involve increasingly impersonal transactions, often over considerable distances, the rise of large corporations, agglomeration and urbanisation.<sup>42</sup> North's explanation implies that the clamour for state intervention is an inevitable consequence of the evolution of capitalism, in other words it is endogenous to the economic process.<sup>43</sup> Schumpeter disagrees. He argues that crises which originate in the medium and longer term dysfunctional consequences of government intervention encourage the new middle class to lobby for interventions which undermine the creative destruction process.

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<sup>42</sup> 1877 was the date of the Munn vs Illinois legal decision which many consider the beginning of the erosion of property rights in the United States (North, 1978: 969; see also Pipes, 2000: 249).

<sup>43</sup> North starts his discussion of the implications of the organisational changes that accompanied the second industrial revolution with the statement that "[n]either economic historians nor economists have appreciated" these implications, but Schumpeter is arguably an important exception. Much of *Capitalism, Socialism and Democracy* anticipates the 'implications' North enumerates (e.g. Schumpeter, 1962: 135-142).

Robert Higgs explains the growth of U.S. government in terms of a ‘crisis hypothesis’ which involves government growth in response to a crisis and a ratchet effect which occurs because government involvement may diminish in the aftermath of a crisis but it does not return to pre-crisis levels. A succession of crises therefore explains the significant growth of government in the United States since the late nineteenth century. Despite obvious parallels, Higgs raises two main objections to Schumpeter’s vision.<sup>44</sup> First, he criticises Schumpeter for not recognising that business interests have much to gain from intervention that curbs the effectiveness of the creative/destruction mechanism and are better placed than the electorate to exploit any predisposition to toward intervention, and second that “[Schumpeter] persistently underestimated how much governmental authorities would act not as an executive committee of the bourgeoisie, or any other group, but as interested parties in their own right, especially during crises” (1987: 244). Each of these criticisms is addressed in turn.

Businesses are, of course, interested in reducing their exposure to the ‘life and death’ process of survival in an uncertain economic environment. They are susceptible to competition from new entrants, entrepreneurs with new products or more efficient ways of making similar products, foreign competition and so on. Rent-seeking was the term originally coined to describe efforts by private sector interests seeking economic benefits via the influence they can bring to bear on the process of policy formulation (Krueger, 2002, 1974; Tullock, 1993; Olson, 2000). The term ‘crony capitalism’ is now more commonly used.<sup>45</sup> Protective tariffs and subsidies to ‘preserve jobs’ are examples. Irrespective of whether the group involves business interests or some other constituency, providing benefits to one group implies costs elsewhere in society.

Schumpeter may not have anticipated the *extent* to which ‘monopoly capital’ would take advantage of the predisposition of public sector actors to impose constraints on the operation of competitive capitalism. But he was aware that the creative destruction process

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<sup>44</sup> Higgs also refers repeatedly, but without justification, to Schumpeter’s preoccupation with a Marxian class struggle. He claims that “[t]he Marxian foundations of Schumpeter’s thought served him poorly in his assessment of crises” (1987: 244). In fact, Schumpeter’s expectation that crises of increasing severity will increase the counterproductive influence of government in the economy and a crisis treadmill is entirely consistent with Higgs’s argument in *Crisis and Leviathan* (1987). Schumpeter, however, goes further than Higgs by pointing out that crises originate with government action and includes interventions which exaggerate the impact of normal recessions as well as wars.

<sup>45</sup> E.g. Krueger, 2012. Whatever the label, it is important to note that those on both the ‘right’ and ‘left’ of the political spectrum agree it is undesirable for society as a whole. Disagreement arises because those on the ‘left’ regard such behaviour as an inherent characteristic of a ‘market economy’, whereas those on the ‘right’ consider it a flaw in mixed economies.

would only function as long as the state opposed individual egoism” (Schumpeter, 1991: 110). Kingston (2014: 467) describes the implications:

The only way in which the State can fulfil this role [of opposing individual egoism] is by imposing a system of individual property rights which force ‘individual egoism’ to serve the public good in following its own interest. However, it does not take long for individuals who are being controlled in this way to grasp how much more they could gain by getting control of the law-making mechanism so as to shape property rights to suit themselves.

Feedback from established business interests seeking to modify capitalism’s institutional environment for their benefit brings concentrated pressure to bear on the policy making process.

Schumpeter was in fact *very* sceptical regarding the ability of the public sector bureaucracy to resist this pressure. He is considered one of the founding fathers of public choice theory, and was interested in the supportive role government bureaucracies might play in undermining the institutions required to sustain dynamic capitalism. The concern Schumpeter expressed regarding the ability of politicians and bureaucrats to hold the line against pressure from the ‘new middle class’ applies even more strongly to pressure brought to bear by business lobbies. He credited the Prussian civil service with thwarting the excesses of the railway age in the public interest (1939: 346), but he was critical of the tendency of its American counterpart to side with the recipients of public sector largesse, particularly railway promoters, during America’s gilded age. Schumpeter considered those administering the New Deal under Roosevelt a particularly egregious example of failure to protect the institutional environment conducive to capitalism from the assault to which it was subjected during the Depression (see discussion in Kingston, 2014: 461-63).<sup>46</sup>

Once again the key seems to be that these efforts were generally thwarted until the Progressive Era, when an ideological shift eroded the protection governmental structures had hitherto fore afforded the institutional arrangement which facilitate efficient operation of the creative/destructive process.<sup>47</sup> Like North, Higgs acknowledges the importance of an ideological shift which eroded the (Madisonian) ‘protective strata’ and predisposed public

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<sup>46</sup> Kingston 2014) and others (e.g. Allison, 2012; Friedman, 2010; 2009) draw attention to the failure of regulatory bodies in the United States and elsewhere to curb predatory innovation in the financial services sector as an explanation for the sub-prime financial debacle of 2008.

<sup>47</sup> Kolko (1965, 1963) demonstrated how business interests co-opted the Progressive Movement in the U.S. to create a political capitalism they could steer. Tullock (1986: 16-21) suggests that governments are always experimenting. ‘pushing the envelope’ or testing the limits of the electorate’s tolerance. He illustrates his argument using the example of deficit financing which followed the ideological shift which predisposed government to intervene in the economy, a predisposition which may well have been ‘discovered’ (by public sector entrepreneurs) in a similar way.

sector actors to intervention. Once again, it is the origins of the ‘ideological shift’ which are controversial. Higgs cites the inability of the state to ‘control’ the post-Civil War economic expansion, a rapid increase in under-employed intellectuals, and a touching belief that experts in government could solve social problems as factors contributing to this ideological shift.<sup>48</sup>

#### 1.2.4 Crises and Schumpeter’s Economic Sociology

Higgs’ (1987) work on the ratchet effect of crises on the size of the American government is one of a number of studies which explicitly analyse crises, and one of the few to acknowledge Schumpeter’s interest in this phenomenon.<sup>49</sup> Those relevant to the discussion of crises in the historical chapters that follow are outlined here.

Congelton (2005: 183) defines a crisis as having three characteristics: it must be unexpected, have unpleasant consequence, and require an urgent response. As he points out, this combination makes it extremely difficult to come up with effective policy. The ‘surprise’ inherent in crises magnifies the ‘knowledge problem’, and the urgency for action means that there is less opportunity to understanding the underlying problems, thereby increasing the probability that inappropriate action will be taken. The resultant policy mistakes increase the severity of subsequent crises, leading to ‘crisis cascades’ (2005: 196). This mirrors the pattern of crisis consequences Schumpeter anticipated.

However, only one crisis in the prairie agriculture case study meets this narrow definition: the Depression of the 1930s. In the other instances, the underlying problems were recognised in advance, so this study adopts a broader definition in which such ‘looming crises’ are included.

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<sup>48</sup> Higgs (1987: 113-116) concurs with Schumpeter’s position regarding the important role intellectuals play in ideological shifts. But he emphasises their influence on business interests and government bureaucrats—the groups which stood to gain from this ideological shift -- rather than on ‘the new middle class’ which had the most to lose.

<sup>49</sup> A number of studies of crises e.g. Benson (2005) and Moberg (2005) also argue that despite occasional rollbacks, government tends to expand over time in modern western democracies. However, Bologna and Martin (2013) analyse this hypothesis using data for a large number of countries and conclude that large government is not consistently the legacy of crises. O’Donnell (1978) shows how policies in Argentina have alternated between encouraging and discouraging agricultural exports. Each change in the pendulum’s direction is prompted by a crisis caused by the cumulative adverse consequences of a the policy adopted in the wake of the preceding crisis. Although the objective of policies does change dramatically, the amount of government resources devoted to those policies may not change appreciably. The well-publicised neo-liberal agendas of Reagan and Thatcher were accompanied by increases in levels of government spending expressed as a percentage of GDP (Pierson, 1994). A decline in government resources expended interfering in some sectors of the economy was more than offset by growth in other areas (e.g. defense spending by the Reagan administration).

A number of studies deal with the relationship between interest groups and crises. Some of these deal with the impact of post-collapse crises. Olson (1982) and the papers collected by Hennessy, Lutz and Scrimone (1964) show that disruption of longstanding interest group alliances in the aftermath of a war may be beneficial where the opportunity to rebuild an economy from the bottom up occurs without interference from groups which had been successful rent-seekers before and during the war.<sup>50</sup> Interest group dynamics in the post-collapse crises are relevant in the context of the discussion of the ‘big bang’ counterfactual in the final historical chapter.

Interest group dynamics in the face of a looming crisis are, however, more germane in the context of this study. In such instances defensive alliances formed with the objective of preserving the *status quo* may delay action to avert the crisis (e.g. Alesina and Drazen). The Friedmans (1984) were among the first to apply the term ‘iron triangles’ to describe alliances of disparate groups – often politicians, bureaucrats and the group targeted by an intervention – that benefit from an intervention. However, alliances among interest groups may also form to devise and advocate on behalf of solutions to the looming crisis. Lindberg’s (2007) example of agricultural policy reform in Sweden is an interesting case in point. Under such circumstances, rivalry between an alliance of groups of interests benefiting from the *status quo* and an alliance of groups attempting to change policies in effect is likely to develop. This suggests that the direction policy ultimately takes is determined by competition between coalitions of interest groups advocating different strategies, ranging from ‘stay the course’ (path dependency) to a complete reversal of policy.

Higgs and North both acknowledge that interests have long sought to manipulate the political process but that it was only relatively recently that legislators and the bureaucracy became complicit in their efforts. Both place this shift at around the time of the Progressive Era in the United States. North suggests the shift occurred as a consequence of the ‘natural evolution’ of business in the second economic revolution. Higgs emphasises popular discontent with trustified capitalism fanned by muckrakers and demagogues, a prevalent

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<sup>50</sup> Drazen & Grilli (1993) also address post-war adjustment problems and cite a number of examples where draconian measures were adopted to deal with crises. Their examples involve the out-of-control inflation caused by attempts to monetise deficits accumulated during WWI. The apparent success of these initiatives leads the authors to conclude that ‘desirable’ consequences may arise from ‘crises and emergencies.’ The key question, however seems to be desirable for whom and over what time frame. A more plausible explanation of the medium and longer term ‘success’ might be that when the adverse impacts of a severe crisis are broadly distributed, the population offers little resistance to attempts at resolution, irrespective of the form they take. Schumpeter obtained some personal experience with this aspect of crisis management when he was appointed Austrian Minister of Finance in 1919. He only lasted seven months in the job.

belief that experts in government could solve social problems, and the rapidity with which business interests took advantage of the opportunity of an increasing predisposition towards intervention on the part of government.

Higgs does acknowledge Schumpeter's insight into the role played by the growing intellectual strata in fomenting hostility to the 'trusts'. But neither he nor North enquire into whether or not prior government intervention contributed to the progressive movement's hostility towards monopoly capital. Higgs (1987) provides a very detailed examination of subsequent interventions prompted by a series of crises after the federal government was predisposed to intervene. Schumpeter's suggestion that the net effect of unintended consequences of government intervention exaggerates troughs in the business cycle is examined in this study. He claimed increasingly severe crises expand the proportion of the new middle class susceptible to anti-capitalist propaganda and lead to legislation which impedes efficient operation of the creative destruction process.

Discussion of the objections to Schumpeter's 'vision' put forward by North and Higgs suggests the origin of crises as a key question to be addressed. Both suggest the Progressive era was a significant period of 'ideological change in the United States. North considers the ideological shift endogenous, a consequence of significant changes in the structure of the economy which emerged as the second economic revolution unfolded. Higgs emphasises the benefits business interests and public sector actors were able to capture after this 'shift'.<sup>51</sup> Like Schumpeter, he acknowledges the importance of muckrakers and the growing intellectual class as an important influence on those who are susceptible to anti-capitalist propaganda; but he too leans towards an 'endogenous' explanation of how that susceptibility arises.

Schumpeter suggests an exogenous influence – government intervention -- which exaggerates the business cycle and transforms ordinary recessions into crises as the root cause of ideological change. The underlying question is therefore whether the predisposition to intervention which materialised during the Progressive era in the United States arose from 'natural' economic evolution or was 'exogenous' help required.

The prairie agriculture case study is used to test the hypothesis that the 'dysfunctional consequences' of prior government intervention (an 'exogenous' factor) play a decisive

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<sup>51</sup> Higgs (1987: 82-84, 174-194) cites the contrasting responses to drought evident in the Texas Seed Law bill vetoed by President Grover Cleveland in 1887 and the Roosevelt's Agricultural Adjustment Act in the 1930s as examples. See also Dupont (2014: esp. 571) and Haeffele-Balch and Storr (2014: esp. 590).

role in determining whether or not rivalry among interest groups for dominance of the policy agenda results in an ideological change in the attitude of the voting public to the role of government in the economy.

Two U.S. examples suggest the validity of Schumpeter's contention that agitation by mass publics for intervention which is intentionally anti-capitalist originates in abnormal recessions (or crises) that occur because prior government intervention has adversely affected the economy.

Schumpeter's work on U.S. railways is particularly relevant to this study given the major role railways and railway policies play in the history of prairie agriculture. He dealt extensively with 'railroadization' in the United States in *Business Cycles* (1939). His most important observation on the subject is perhaps that "Mid-western and Western [railway] projects could not be expected to pay for themselves in a period such as most investors care to envisage" (1939, Vol. 1: 328). *Most* U.S. railway projects were therefore realised only by means of considerable 'artificial stimuli from federal and state governments.'<sup>52</sup> The benefits obtained by railway entrepreneurs from the state were egregious examples of special interest rent-seeking which galvanised the Progressive movement.

From the perspective of railway 'entrepreneurs', artificial stimulus of railway construction is a process whereby they off-load much of the associated commercial risk. McCaffrey (2009: 15) expresses this succinctly and goes on to point out an important consequence:

Even if the state cannot literally insure against failure in the market, the net result of its interference is to finance endeavours that are viewed as riskless by those who undertake them. .... We should note briefly here that the difficulties of exposing good and bad investment under interventionism is certainly likely to generate feelings of antipathy among the members of society toward the capitalist system, especially because it might often seem as if the capitalist system is to blame for the problems that actually arise from intervention.

Eichengreen (1995) uses the behaviour of Canadian entrepreneurs in the nineteenth and early twentieth century to illustrate the consequences of government bond guarantees and public

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<sup>52</sup> An exception – the Great Northern Railway -- is important in the context of this study both because it was the closest transcontinental railway to the U.S. Canadian border and because it was built after its Canadian counterpart, the Canadian Pacific Railway (CPR).



ownership for infrastructure projects in developing countries.<sup>53</sup> He points out that the existence of guarantees creates incentives for entrepreneurs to manage the project for their personal gain. In extreme instances government intervention disconnects the entrepreneur's incentives from the survival of the enterprise, a phenomenon Akerlof and Romer (1993) observed in the context of the U.S. Savings and Loan crisis of the late 1980s. The federal and provincial government bond guarantees provided to the Canadian Northern Railway (CNoR) had the same effect (Lewis and MacKinnon, 1987).

The consequences of the public sector stimulus provided to North American railways are the subject of a recent study by White (2011). He demonstrates that crises manifest themselves in a wide range of forms when 'entrepreneurs' use public credit that shifts risk from their shoulders to others. He refers to U.S. railroad entrepreneurs as "super-heroes of bad management" (2011: 316) who "created inefficient, costly, dysfunctional corporations..... They built railways that would have been better left un-built, and flooded the market with wheat, silver, cattle and coal for which there was little or no need. They set in motion a series of catastrophes for which society paid the price" (2011: xxvi). His concluding paragraph summarises the catastrophes that might have been avoided in the United States if the counterfactual "without the extensive subsidisation of a transcontinental railroad network" had occurred.<sup>54</sup>

Both the origin and the objectives of interest groups are important in this study. The second example illustrates how victims motivated by the harm they perceive to have been inflicted by a prior intervention may agitate for redress. Pierson's discussion of feedback to the policy process from interest groups created by prior government intervention supports Schumpeter's contention without mentioning his name. Pierson points out that "policies produce politics" (1993: 597) and that "[t]he activity of interest groups often seems to follow rather than precede the adoption of public policies" (1993: 598). He cites Skocpol's (1992) study of the influence interest groups created by government policy

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<sup>53</sup> A similar study by Carlos and Lewis (1995) concentrates on one of the most egregious Canadian examples of creative financing, that of the Grand Trunk Railway which ran from Portland, Maine to Chicago via Montreal and Toronto.

<sup>54</sup> "...there might very well have been less waste, less suffering, less environmental degradation, and less catastrophic economic busts in mining, agriculture and cattle raising.... There would have been less bloodshed and slaughter [of the aboriginal population]. There would have been fewer rushes and collapses, fewer booms and busts. Much of the disastrous environmental and social history of the Great Plains might have been avoided. The issue is not whether the railways should have been built. The issue is whether they should have been built when they were built. And to that question the answer seems to be no. Quite literally, if the country had not built transcontinental railroads, it might not have needed them until much later, when it could have built them more cheaply, more efficiently and with fewer social and political costs" (White, 2011: 517)

exerted on U.S. social policy before the Depression as the classic illustration of this theme. Often such interest groups are motivated to obtain ‘extra-market’ benefits by the harm they perceive to have been inflicted by a prior policy intervention.<sup>55</sup> This is as true for special interest groups as it is for mass publics. For example, imposition of air pollution abatement requirements or employment standards becomes an argument for levelling the playing field against imports from regions lacking those restrictions.

These two examples show that resentment which breeds discontent may be directed either at the ‘trusts’ when they obtain benefits not available to others, or at the state when redress in the form of compensatory benefits is sought for damage inflicted by prior policies. This is of interest because, as will be shown in the historical case study, agrarian protest on the prairies initially targeted the national policy and subsequently shifted to the supposedly ‘laissez-faire’ capitalist system. The final U.S. example demonstrates how the distinction between private and public benefits may be distorted when broad support for is required to obtain special interest benefits.

Lobbying by mass publics and special interest groups for public sector intervention may be linked in insidious ways. Rausser (1992, 1982) drew attention to this phenomenon in the context of U.S. agricultural policies. Policies which limit the influence of the market over a sector become more palatable to legislators if they are paired with provisions which give other constituencies what they want as well. He uses the example of price supports and ‘set asides’ (1992: 137, 145-46). ‘Set-asides’ are agricultural land diverted to uses which do not add to (surplus) production. Portraying ‘set asides’ as environmentally desirable encourages those representing non-agricultural constituencies to vote for legislation which benefits agricultural producers.<sup>56</sup> Rausser points out that “[i]n a world of limited knowledge of how economic systems operate, producer-interest groups have successfully argued that ‘price stabilization’ programs are in the public interest. ... interests who share

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<sup>55</sup> Hayek made the same point. Ikeda (2005: 27) uses Hayek’s insight to explain his “self-fulfilment thesis” of intervention:

“Hayek maintains that such terms as “social injustice” have no meaning in the context of the impersonal market process because overall production and distribution therein are the unintended result of the interactions of a myriad of individuals, or groups that are small relative to the overall market order, no one of whom can be identified as responsible for any particular gain or loss. Such concepts can nevertheless serve to rally the demand to redistribute wealth. The irony is that once the redistributive intervention takes place, those who lose as a result now have a legitimate and identifiable target, i.e. the central authority and its supporters, to blame.”

<sup>56</sup> The peculiar American practice of earmarks extends the same principle more broadly across the legislative process. An ‘earmark’ provides funding for a project in the home state of the legislator whose support is needed. Funds are frequently ‘earmarked’ for bridge or road reconstruction projects, museums and science centres.

the burden of financing such programs are led to believe that such policies are ‘productive’ as opposed to ‘predatory’ transfers” (1992: footnote, p. 150).<sup>57</sup> His research shows that ‘predatory’ wolves dressed in ‘productive’ sheep’s clothing may fool the legislators but are unlikely to achieve their stated objectives.<sup>58</sup> This is a variation on the ‘Baptists and Bootleggers’ argument first proposed by Yandle (1999b; 1983): both Baptists and bootleggers sought prohibition (of alcoholic beverages), but for quite different reasons.

The prairie agriculture case study is particularly apt because the group directly affected – wheat growers – were both a special interest group seeking benefits from the political system and, for a time, a mass public with sufficient electoral clout to influence political decisions. Both attributes stemmed from the concerted effort made to promote agricultural settlement on the prairies. Farmers’ organisations first waged an ineffective campaign against government policies they perceived as being contrary to their interests. Later they were more successful when they sought to ally themselves with government in their conflict against aspects of the *laissez-faire* system they came to regard as ‘unfair’. And the reason they were perceived as unfair did not have anything to do with the institutions themselves, but with the farmers’ perspective, which was the consequence of government settlement policies.

In this study, Schumpeter’s vision of how society and its institutions function provides a remarkably accurate explanation for the history of prairie agriculture, with the exception of the final episode. During this period, deliberate steps were taken to pull back from the quasi-socialism or *Zwangswirtschaft* which prevailed in the post-World War II period. This raises questions about the sustainability of socialism that Schumpeter did not address. It also provides an opportunity to test the hypothesis that popular revolt against a prevailing ideology may result in an ideological shift *away* from government intervention as well as in favour of government intervention.

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<sup>57</sup> Rausser designates transfers considered ‘productive’ (i.e. they increase efficiency and lower transaction costs) PERTs (for ‘political-economic resource transactions’). Their objective is to correct market failures or provide public goods and they are supposedly neutral in terms of distributional effect. PESTs, (‘political-economic seeking transfers’) are explicitly intended to redistribute wealth from one social group to another and ignore the increased transaction costs and inefficiencies that result.

<sup>58</sup> Set asides are a notoriously ineffective means of reducing production because the farmers’ rational response is to ‘set aside’ the least productive land (capturing the benefit of the programme) and use more intensive production practices (e.g. more fertiliser) on the remaining productive acreage.

## **2 Methodology**

History cannot be used to predict outcomes of future policies, but failure to heed historical lessons increases the risk of doing the same thing over and over again in the hope that different results will materialise – a popular definition of insanity. History records the changing reality that individuals experience. In its most extreme form, history is purely descriptive. It suffers what Boettke (2000: 378) describes as the  $n=1$  problem: each case is unique. Conceptually, laws of nature which have universal applicability lie at the opposite extreme. The social sciences operate between these extremes and seek to identify patterns and “account for outcomes by identifying and exploring the mechanisms that generate them” (Bates, Grief, *et. al*, 1998: 11-12). Each step from descriptive history towards the ‘natural law’ end of the spectrum implies an increase in scientific content.

Any attempt to “account for outcomes” involves consideration of historic events. According to North (1977: 198):

....distinguished [economists]... from Smith and Marx to Marshall and Schumpeter ...valued economic history because it provided a dimension of time to the static world of the economist; it attempted to put together the pieces of an economic system rather than examine isolated bits of the jigsaw puzzle; it incorporated an awareness of the interdependence of economic organisation with the political and social aspects of society; it analysed the parameters that the economic theorist takes as given. In short, economic history forced on the economist a wider perspective which would not help but improve his myopic vision.

A key disagreement among those using the New Economic History is how best to integrate theory into analysis. Some advocate cliometrics, which emphasises the application of the quantitative techniques developed to support neo-classical theory to historic case studies (e.g. Hatton, O’Rourke & Taylor, 2007; North, 1997; Grief, 1997). On the positive side, such studies reaffirm the stimuli that economic conditions provide for political and institutional change emphasised by Marx and Schumpeter (Rosenberg, 1993: 11). However, this approach has been criticised because heavy reliance on quantitative techniques tends to dictate the theoretical framework. North (1997: 412) argues that the “straitjacket of neoclassical theory” limits the real world applicability of increasingly sophisticated statistical analyses.<sup>59</sup>

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<sup>59</sup> Or, as Einstein claimed, “as far as the laws of mathematics refer to reality they are not certain; and as far as they are certain they do not refer to reality.”

An alternative approach is known as the ‘analytic narrative’ technique, after a collection of papers with the same name (Bates, Grief *et al*, 1998). The analytical narrative approach creates space for quantitative analysis while “avoiding the straitjacket of neo-classical theory”. Most importantly, this approach provides a means of expanding the analytical scope beyond perfectly competitive mechanistic processes liberally hedged with *ceteris paribus* assumptions to include dynamic, evolutionary processes in which alterations to institutional rules are negotiated.

The net effect is to move historical studies away from pure narrative toward the natural law end of the scientific spectrum, while avoiding commitment to a theoretical framework considered too narrow for the task. The analytic narrative approach combines detailed exposition of factors which potentially affect ‘outcomes’ (critical junctures in the ‘narrative’) with the “logical structure of rational choice theory (as illuminated in game theory)” (Boettke, 2000: 377).

It is the *explicit* introduction of theory in order to claim the challenging middle ground between pure description and pure theory that constitutes the distinguishing feature of the analytic narrative methodology (Bates, Grief *et al.*, 1998: 12). The original collection of analytic narrative papers illustrates why the methodology is considered “a useful tool for assessing causality in situations where temporal sequencing, particular events, and path dependence must be taken into account” (Mahoney, 1999: 1165).

Just as the analytic narrative provides a means whereby what actually *did* happen may be analysed and explained, the use of counterfactuals is a technique for suggesting plausible *alternate* scenarios. The value of counterfactuals in evolutionary economics derives from recognition that multiple equilibria are possible, each involving an associated level of welfare and distribution of benefits. The actual situation is the product of history and the potential for alternative outcomes with higher welfare levels suggest “potential for regret” regarding “the road not taken” (Cowan & Foray, 1999: 3).

Fogel’s (1964) pioneering use of counterfactuals set out to answer the question of how different the economic performance of the United States might have been in the absence of railways. He attempted to reconstruct the economic process in the United States as it would have evolved without railways from the point at which they first appeared. His conclusion was essentially ‘not that much less than that which occurred with the railways that were

actually in operation'.<sup>60</sup> He does, however, note that the entire configuration of economic activity would have been significantly different.

Chambers and Gordon (1966) used the counterfactual of no Canadian wheat boom between 1901 and 1911 to highlight some weaknesses in the generally accepted 'staples' interpretation of Canadian economic history. They concluded that the contribution of the wheat boom to per capita economic growth was substantially less than usually inferred. In doing so, they implicitly question the benefit Canada obtained in return for its very considerable investment in the prairie settlement component of the national policy.

### **3 The Model**

The main purpose of the model outlined below is to answer the questions 'Who decides?' 'Who benefits?' and 'Who pays?' each time a crisis leads to changes in the institutional environment within which prairie agriculture operates. Unlike most studies of prairie agriculture, the success criterion adopted is not the contribution the sector made to the national economy, but its impact on the broader groups directly involved. The focus is primarily on prairie farmers, but also on the taxpayers who ultimately shouldered the cost of creating the prairie grain economy and the subsequent 'remedial' interventions, both of which proved counterproductive. The underlying argument is that the benefit of the wheat economy to the national economy could have been obtained at much less cost to farmers and taxpayers.

Mid-latitude agricultural case studies are well suited to game theoretic analysis because crops are raised in an annual cycle – the iterations in the 'game'. It was negative feedback from the annual efforts of increasing numbers of prairie farmers that gave impetus to the prairie populist movement of the early twentieth century.

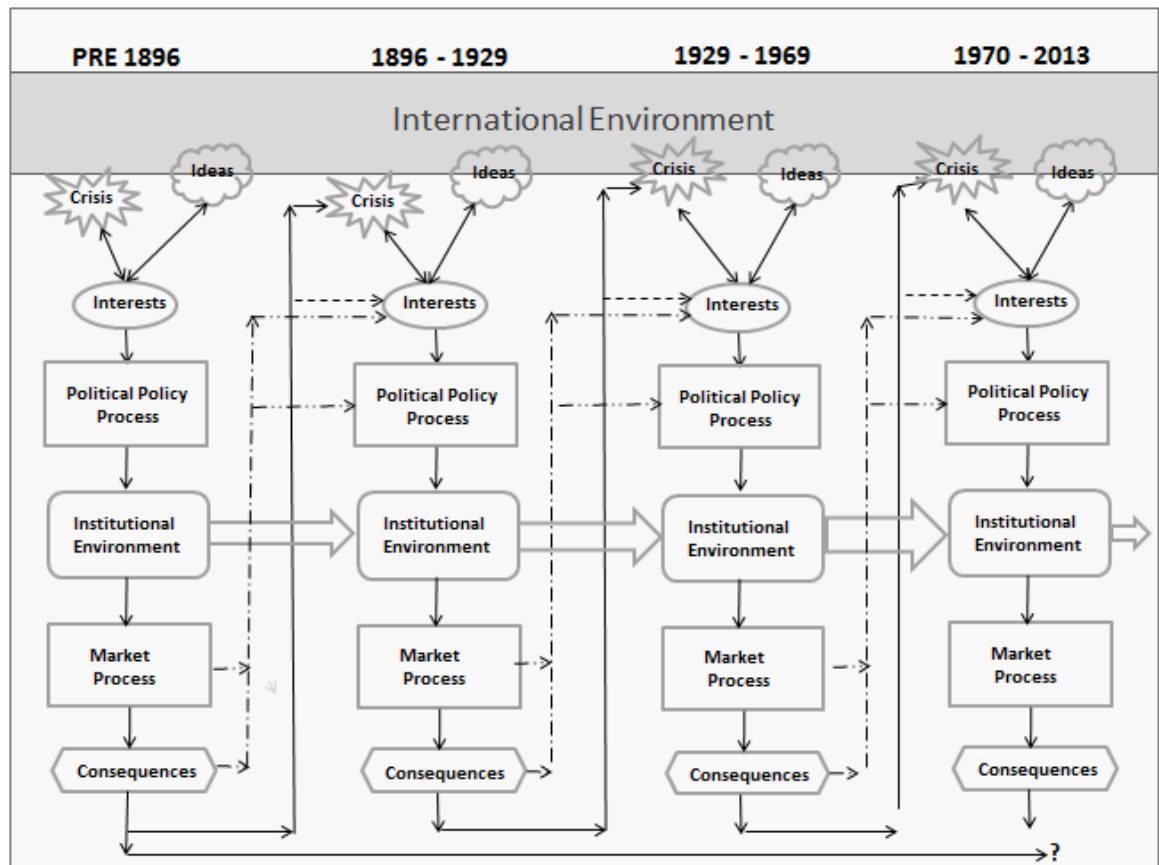
In this case study, the history of prairie agriculture is broken into four periods as shown in the schematic overleaf. Each period begins with a crisis which, in each case, is a consequence of counterproductive government action, as Schumpeter intimated. Two of the crises are domestic, whereas two, the Depression of the 1930s and the turmoil of the 1970s were international in scope.

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<sup>60</sup> Putting Fogel's conclusion alongside that of White (2011 see note 54, above, page 51) suggests that capturing the small incremental growth attributable to the railway network involved massive *and avoidable* social costs.

The central horizontal axis of the schematic represents the institutional environment. In each time period, modifications are made to the formal rules which constrain the behaviour of businesses involved in prairie agriculture. These changes to the institutional environment tend to be cumulative; hence the horizontal links between the time periods.

Figure 2 The Model Diagram



Source: Author

The changes made to the institutional environment in each time period are an outcome of the political and policy making mechanism, namely Canada's federal government. Examination of this process to identify the causal mechanisms which generate those outcomes explains the objectives pursued by the interventions introduced in each time period.

Each crisis is an opportunity to change policy. One objective is to explain why some crises lead to significant changes in policy (discontinuities or policy reform) while others do not (path dependency). Interest groups advocating a change in policy are likely to be at a disadvantage, given the propensity of beneficiaries of the *status quo* to defend existing arrangements.

The severity of the crisis, whether the crisis is of the unexpected or ‘looming’ type, and the interest group or coalition of interest groups exerting influence over the policy making process when key decisions are made are all potential factors influencing the outcome. The Depression was the only one of the four crises that could be classed as ‘unexpected’. The others are ‘looming crises’ which allow time for the marshalling of evidence and the creation of new alliances.

Ideas are depicted as being both domestic and international. Ideas in vogue at any given point of time justify an array of policies. Successful interest groups adopt ideas that enable them to enhance the popularity of the measures they advocate and increase their influence on the policy-making process.

Feedback affecting the political and policy-making process takes a number of forms. If the crisis that begins the next iteration of the process is a product of the interventions introduced in the prior period, it constitutes feedback which provides an incentive to modify the institutional environment in the next period. Feedback from the mass publics affected by those interventions would be another: this feedback is intermittently communicated directly through the democratic process of elections or mass action such as the farmer’s March on Ottawa in 1910; on a continuous basis groups representing factions of those affected (e.g. farmers’ organisations) attempted to raise the profile of regional issues on the national stage and cultivate alliances with like-minded counterparts from other regions.

Commercial entities are also interest groups that provide feedback to the policy-making process. Such entities can exert considerable influence on the policy making process because of their historical importance (for example the Canadian Pacific Railway (CPR, subsequently called CP) or the constituency they represent (the Wheat Pools). Other interest groups may not enjoy the same access to the policy process.

In the Canadian political system, Royal Commissions play an important role in the policy process. Bradford (1999: 19) refers to them as “switch point mechanisms” which “link new ideas to official policy practice.” He describes the impact of two ‘crisis’ commissions, one in the 1930s and one in the 1980s, as mechanisms whereby “framework ideas became governing paradigms through political stealth” (1999: 49).<sup>61</sup> By ‘political stealth’ he means

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<sup>61</sup> These were the Rowell-Sirois Royal Commission on Dominion Provincial Relations which was convened by the Mackenzie King government in 1937 to investigate the constitutional problems highlighted by the



policy changes which take place without being sanctioned by a federal election and with minimal public input (1999: 45). Both these turning points had important implications for the subsequent policies that affected prairie agriculture.

The other main issues to be explained involve the *reaction* of commercial firms to changes in the institutional infrastructure. It is the interaction between the market process and the institutional environment that determines what happens in the economy and whether or not the changes made to the institutional environment are beneficial for society at large. The negative consequences of any counter-productive interventions manifest themselves as crises whenever business conditions take a turn for the worse. A particularly severe crisis initiates the next iteration in the chronology.

Ultimately, changes in the rules alter the relative merits of different options available to business entities. Here the objective is to explain why some policies that emerge from the political and policy-making process have counterproductive consequences in aggregate although the decisions taken by firms in response to the policies in place are 'rational' from their point of view. Schumpeter's distinction between interventions which are counterproductive and those that are not depends on whether or not they interfere with the technical change component of his stylised economic system. Prairie agriculture offers numerous examples.

Any intervention shown to have counterproductive consequences raises two important questions: why was it adopted in the first place, and why was it allowed to persist for so long? The answer to the first question seems to lie in the relative influence of particular interest groups when public sector decisions are taken. The second question is more difficult. The private sector is sometimes regarded as abandoning promising experiments too hastily (e.g. Rosenberg, 1992). But such behaviour is conditioned by acute awareness of the sunk and opportunity costs involved. Public sector spending is not constrained in the same way. As all interventions will benefit some constituencies, they naturally defend their continuation, while the broader group carrying the costs may be unaware of their source. Prairie agriculture provides some interesting examples of counterproductive interventions which persisted for extended periods of time, and an opportunity to understand the circumstances which eventually led to their abandonment.

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Depression and the Macdonald Royal Commission on the Economic Union and the Development Prospects for Canada appointed by P.E. Trudeau in 1982. The Report of the Rowell-Sirois Commission was released in 1940 and that of the Macdonald Commission in 1984, by which time Brian Mulroney was Prime Minister.

A counterfactual which argues what might well have happened in the absence of those interventions is also provided in each of the historical chapters. The costs associated with those interventions suggest that state-sponsored initiatives to expand the prairie grain economy after 1896, and to keep as much of it functioning as possible after the Depression, involved avoidable misallocation of human, fiscal and financial capital.

The argument that some of the federal interventions affecting prairie agriculture were counterproductive stems from divergence between the trajectory of the prairie grain economy with post-1896 interventions – which is available in the historical record – and the counterfactual trajectory which shows what would probably have happened in the absence of those interventions.

The counterfactual argument is represented in the schematic by the horizontal line across the bottom of the page. This line originates in the consequences at the end of the first time period and extends to the consequences to date from the dismantling of intervention in the most recent time period. The question mark at the bottom of the final period portion of the schematic poses the question whether things today might not be so very different without all the intervening interventions.

### **Chapter 3**

## **Canada and the Prairies before the ‘Wheat Boom’: 1813 – 1895**

The Hudson’s Bay Company controlled the area which was to become the prairie region of Canada for two centuries prior to 1870. Canada took steps to acquire and settle the region as part of an effort to make a transcontinental nation out of Britain’s remaining North American possessions immediately after it became a nation in 1867.

The British colonies along the St. Lawrence River set out to transform the prairies into a source of wheat for the British market as part of the solution to the difficulties they faced in the middle of the nineteenth century. This chapter describes the origins of that crisis, how the highly improbable idea of prairie agricultural settlement developed, the steps taken to bring it about and their short term consequences. It starts by providing a summary of the early history of the prairie region to serve as background to the subsequent sections.

### **1 Historical Background to 1870**

The first links between the prairies and European markets – and the first conflict between the French and the English in the region – developed as a consequence of the fur trade in the seventeenth century. In 1670 Prince Rupert, a cousin of Charles II, helped a group of investors obtain a trade monopoly over the portion of North America which drained into Hudson’s Bay.<sup>62</sup> The boreal forests in the northern portions of what became Canada’s Prairie Provinces and north-western Ontario were the principle sources of the furs that the Hudson’s Bay Company (HBC) exported to Europe. The bison herds of the prairie grasslands to the south were the source of pemmican, the dried meat which was the staple foodstuff of those who transported furs and trade goods by canoe.

French traders based in New France encroached on Hudson’s Bay Company territory via a complicated series of portages across the watershed between the Great Lakes basin and the Hudson’s Bay drainage system west of Lake Superior. The hinterland north and west of the Great Lakes became one of several theatres in the global conflict between Britain and France. When Britain took control of New France in 1763, Scotsmen assumed control of the Montreal-based fur trading companies. A series of mergers created the North-West Company (Nor’Westers) which became a formidable rival of the HBC.

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<sup>62</sup> The region was subsequently given the name Rupert’s Land by the grateful recipients of the Charter.

Liaisons between Europeans working in the fur trade and native women gave rise to both English and French-speaking Metis, although the majority were Francophones. Many Francophone Metis participated in the bison hunt on the prairies, an endeavour that required military-style discipline. Several Anglophone Metis were educated in Canada and Britain, and some became prominent critics of the HBC.

Lord Selkirk was drawn into the rivalry between the two fur trading companies by his efforts to establish agricultural colonies in British North America to provide alternative employment for tenants evicted from Scottish estates during the highland clearances. Selkirk accumulated a controlling interest in the HBC when the British government refused him the right to establish a colony in Rupert's Land because it was under the Company's jurisdiction. The agricultural colony that he founded at the confluence of the Red and Assiniboine Rivers in 1812 straddled the Nor'Wester's main transportation routes. This led to conflict and frustrated early experiments with agriculture in the region. The long-running dispute reached a climax in 1816 in a skirmish between Metis buffalo hunters and colonists. This incident became known as the Seven Oaks Massacre.<sup>63</sup>

Administrative responsibility for the colony passed to the HBC on Selkirk's death in 1820 and the rival fur trading companies merged the following year. The efficiency of the company's operations in North America improved dramatically under the leadership of George Simpson. The new entity stopped using rivers flowing into the Great Lakes and the St. Lawrence and reverted to using Hudson's Bay as its sole *entrepot*. The economy of Montreal suffered badly when its role in the fur trade ended abruptly. Simpson reduced reliance on locally recruited labour, alienating the Metis and transforming them into willing allies of U.S. fur traders and groups lobbying against the HBC, both in Britain and its North American colonies.

In 1849 a Metis, Pierre-Guillaume Sayer, was convicted of illegally trafficking furs into the U.S., but no sentence was passed. His trial marked the end of the HBC's monopoly over the regional trade, and the first round in the struggle with the U.S. for economic and political domination of the region.

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<sup>63</sup> There were twenty-one fatalities on the colonists' side and one Metis. The two sides quickly recognized the incident as an unfortunate misunderstanding, and coexisted peacefully for the next fifty years. However the incident did give the Metis a collective confidence and self-awareness they previously lacked and is widely regarded as the birth of the Metis 'nation'.

Reliance on Hudson's Bay for access to the region was abandoned after Donald Smith became manager of HBC operations. He joined forces with an American, Norman Kittson, to dominate the river boat trade between the Red River settlement and the United States. Once U.S. railways reached the Red River, it was more economic for the HBC to phase out the Hudson's Bay route and tranship trade goods and furs via US ocean ports. James Hill then joined the consortium to gain control of a bankrupt U.S. railway line and extend it to the U.S. border with Canada.<sup>64</sup>

## **2 The Crisis**

Britain changed its trade and colonial policies dramatically in the nineteenth century. The economies of the North American colonies had been integrated into empire trade under the mercantile system and these were disrupted when Britain adopted free trade. The transition to this new environment was a protracted one. The policy adjustments made in the Canadas to take advantage of these interim steps made the colony's economy even more vulnerable when Britain adopted free trade.<sup>65</sup>

The Corn Laws restricted access of all foreign wheat to the British market. However, in 1827 legislation provided preferential tariff treatment for wheat or flour shipped to Britain from Canada. American wheat diverted down the St. Lawrence to take advantage of the tariff changes increased exports and the prospect of additional trade led to significant public expenditure on canal building by the colonies.

The U.S. Drawback Acts made it advantageous to ship products into and out of Britain's North American colonies through the United States. The repeal of the Corn Laws in Britain removed the tariff advantage Canada had enjoyed and transporting U.S. wheat through the St. Lawrence canal system. This route became a poor alternative to U.S. ports which were ice-free year round. Trade declined sharply as a result.

In spite of evidence to the contrary, the concept of spending public funds on transportation infrastructure to stimulate the economy became a popular ideology in the Province of Canada. The same strategy was adopted with even greater fervour when a slump in the

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<sup>64</sup> Both Kittson and Hill were born in Canada and emigrated, along with many of their generation, to the United States as economic refugees.

<sup>65</sup> The Canada's refers to the administrative unit formed when the colonies of Upper and Lower Canada were united in 1841. Between that date and Confederation in 1867 (when they became the Provinces of Ontario and Quebec, respectively), the two subdivisions were known as Canada West and Canada East.

colonial economy coincided with the dawn of the railway age.<sup>66</sup> Railways had a number of advantages over canals, not least of which was year round operation. To offset the high initial capital cost, the Province of Canada enacted legislation under which the colonial government guaranteed the interest on bonds issued to finance railway construction.<sup>67</sup> The results were disastrous (Norrie, Owram and Emery, 2008: 159). By 1857, meeting its bond obligations absorbed sixty per cent of the colony's revenue.

One of the reasons the Province of Canada imposed tariffs on manufactured and semi-manufactured goods in 1858 and 1859 (den Otter, 1982: 165) was to pay off debts incurred to improve transportation infrastructure. These tariffs were not well received abroad: British manufacturers protested and United States manufacturers began to lobby against the Reciprocity Agreement.

Britain had negotiated the Reciprocity Agreement which allowed free trade in 'natural' or non-manufactured products between its North American colonies and the United States as partial compensation for the colonies' loss of preferential access to the British market after 1846. In return, U.S. boats were allowed to use waters adjacent to British colonies for fishing and transportation. Trade did increase, but poor harvests in the United States, the Civil War and the exclusion of Russian wheat from the European market during the Crimean War were all important contributing factors. The American decision not to renew the Reciprocity Treaty in 1866 further depressed the economies of the British colonies.

The economy of Canada West was predominantly agrarian in the first half of the nineteenth century. Economic growth involved expanding settlement – clearing forest and establishing farmsteads – in other words bringing idle resources into economic use (Aitken, 2003: 199). The agrarian economy was never subsistence oriented, but the difficulties of overland transport severely restricted scope for trade. By about 1850, Canada West had reached the limits on agricultural expansion imposed by the rocky outcroppings of the

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<sup>66</sup> Two Canadian authors produced books with the same title, *The Philosophy of Railways*: Thomas Keefer was hired in 1849 by the directors of the Montreal and Lachine railway to write a pamphlet promoting railway construction. He proved remarkably effective. In the introduction to a collection of Keefer's work, Nelles (1972: xxxix) writes: "T.C. Keefer was not so much a prophet of progress but one of its hot gossellers." Den Otter's book (1997) argues that infection of the British colonies in eastern North America in the middle of the 19<sup>th</sup> century with a philosophy of railways became the central pillar of the technological nationalism that pervaded the national policy.

<sup>67</sup> The guarantee was extended to bonds underwritten by municipal governments. Some twelve million dollars of debt incurred by municipalities was transferred to the Province in 1859. Britain was ultimately liable for debts incurred by its colonies, so the looming bankruptcy of its colony added weight to the case against colonies being espoused at the time by the 'Little England' movement.

Canadian Shield.<sup>68</sup> This started an exodus of young people from the British colony to the U.S.

The British colonies that remained in North America after the American Revolution consisted of British Columbia on the Pacific coast, the Maritime colonies of Nova Scotia, New Brunswick, Prince Edward Island and Newfoundland on the Atlantic coast, and the United Province of Canada. Although American incursions into British colonies had been repulsed during the War of 1812, there was a lingering fear in the colonies that the United States might try to annex British possessions in North America. The fate of the western part of the continent was a particular concern. The Oregon Agreement of 1864 awarded territory south of the forty-ninth parallel of latitude that had been jointly occupied to the United States. The deciding factor in the arbitration process was the extent of U.S. settlement in the territory. Rupert's Land between the Great Lakes and the Rocky Mountains was considered vulnerable to American annexationist aspirations because where colonisation had been discouraged in order to protect the fur trade.

### **3 Ideas and Ideologies**

Canada pursued a policy of economic nationalism to address its mid-nineteenth century crisis. This policy was supported by selectively adopting some of the ideas of the day to suit domestic circumstances.

Canada was content to be part of Britain's extended domestic market to the extent that it was a source of capital for infrastructure projects and a potential purchaser of wheat. Beyond that, envy of American success led Conservative party politicians in Canada's first federal government to adopt many American policies wholesale. Canadian circumstances were, however, significantly different from those in the United States.

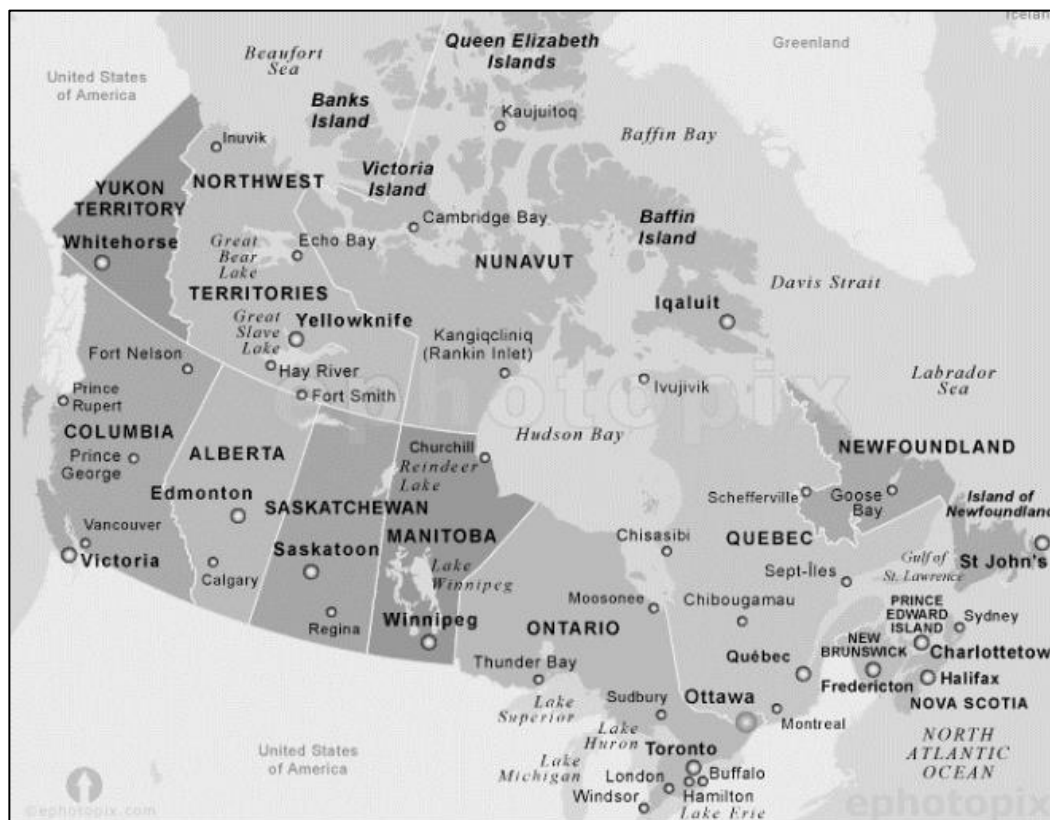
The national policy Canada pursued after 1878 rested on three main premises. The first of these was that the prairie portion of Rupert's Land had the potential to become a successful agricultural region producing wheat for export. The second was that public spending on transportation infrastructure would stimulate the economy. The third, tariff protection for manufacturing, followed U.S. precedent.

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<sup>68</sup> At this point in its history, Canada West found itself in the same position as the Thirteen (U.S.) Colonies after the Quebec Act of 1774 which denied them the opportunity to expand to the West (North, 1993: 39). Realisation that they were 'hemmed in' helped precipitate revolt by the American colonies. However beyond the Allegheny Mountains the U.S. agricultural frontier stretched west to the Rocky Mountains, whereas in British North America, the agricultural frontier was interrupted by a thousand miles of Canadian Shield north of the Great Lakes

The idea that the prairies had great agricultural potential and the ‘ideology of infrastructure’ developed out of the circumstances British colonies in North America faced in the middle of the nineteenth century. Many residents of Canada West had long suspected that the HBC deliberately hid the agricultural potential of the prairies in order to preserve its hold on the fur trade. However, most Europeans with any experience living on the prairies prior to Confederation believed they were unsuited to agriculture and that the fur trade would remain the commercial mainstay of the region (Owram, 1992: 13-14; 60-61).

Figure 3 Map of Canada



Source: <http://www.emapsworld.com/canada-political-map-black-and-white.html>

Leaders in Britain’s North American colonies did agree with one aspect of liberal economic thought: its condemnation of monopolies in general and Royal Charters in particular.<sup>69</sup> Early in the nineteenth century the HBC was criticised on humanitarian grounds because its monopoly allegedly strengthened the Company’s leverage over the native population. When railway technology became available and the prairie region became part of the

<sup>69</sup> Adam Smith wrote scathingly that “[t]o be merely useless, indeed, is perhaps the highest eulogy which can ever justly be bestowed upon a regulated company;” which enjoyed territorial monopolies granted by Royal Charters (Smith, 2000: 793). In many instances (the HBC Charter being an exception) the monopoly privileges were subsequently sanctioned by the British parliament.



potential solution to Canada West's economic problems, the HBC was seen as an obstacle to the creation of a transcontinental nation out of British North America.

The first railways across British North America were proposed as alternatives to the elusive North-West Passage. The 1849 proposals of Millington Henry Syngé and Robert Carmichael-Smyth, both British officers serving in Canada, were little more than lines drawn on a map of the continent without any knowledge of the terrain involved. The pamphleteers F. A. Wilson and A.B. Richards, who added more hyperbole to the schemes of Syngé and Carmichael-Smyth, declared that failure to construct a transcontinental railway in British North America would "brand the Government of Great Britain with the stamp of immortal imbecility" (Owram, 1992: 33)

Manufacturing was the *sine qua non* of 'development' in the nineteenth century. Canada ultimately rejected liberal ideas regarding free trade, arguing it might be suitable for countries like Britain with a well-established manufacturing base, but protection was necessary in order to achieve that status. The United States was cited as a precedent.<sup>70</sup> The German economist, Friedrich List was frequently invoked to justify protective tariffs in Canada (den Otter, 1982: 155-6; Goodwin, 1961). John A. Macdonald, the leader of the Conservative party, quoted John Rae, a local authority on the subject, who advocated intervention to promote new industries and technologies after he adopted a protectionist stance during the period he was Leader of the Opposition.<sup>71</sup>

#### **4 Interests and Incentives**

In Britain the success of the Anti-Corn Law League in bringing about the repeal of tariffs on wheat imports illustrated the indirect link between ideas and policies. Arguments favouring free trade and the minimal state were translated into policy only when the cost of defending the mercantile system abroad was under scrutiny and the political influence

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<sup>70</sup> Dales (1966: Chapter 4) argues that the correlation between a protective tariff and the impressive growth of American manufacturing in the 19<sup>th</sup> century does not demonstrate causality and that the explanation "may lie elsewhere". He makes the case that in fact it "must lie elsewhere" and that "American manufacturing provides a 'free trade' standard, or control, against which to compare Canada's manufacturing experience" (1966: 6). Both Japan after the 1867 Meiji restoration and Germany under von Bismark adopted protective tariff regimes around the time tariff policy was a subject of debate in Canada.

<sup>71</sup> Rae's 1834 book *Statement of Some New Principles on the Subject of Political Economy* was praised by John Stuart Mill but otherwise ignored outside Canada. John Stuart Mill was a guiding light of the federal Liberal party in Canada, and the Conservatives referred to his writings justifying protectionism in underdeveloped countries to embarrass their opponents (Gwyn, 2011: 279). Rae's critique of Adam Smith lays out the arguments invoked ever since to support 'patriotic industrial policy'. Goodwin (1961) and den Otter (1982) provide comprehensive reviews of the ideas favoured by the architects of the National Policy.

wielded by industrial interests was growing relative to that of landowners (e.g. Smith, 1935). The ideas that triumphed did so not because they were inherently better than the alternative but because they were championed by the interest group which emerged victorious in the struggle for votes.

The same would be true in Canada. The national policy was adopted by the Conservative party prior to the election of 1878 because it attracted a small but decisive share of the popular vote. The case for individual components of the national policy drew support from particular interest groups, and the system of political patronage in effect at the time provided those groups with significant incentives and leverage.

In Europe, social unrest and agitation against corrupt political practices were widespread in the mid-nineteenth century. In 1848 alone, major social revolutions in Europe, the publication of the Communist Manifesto and the Chartist Movement in Britain gave impetus to political reform. The United States, with its well-entrenched 'spoils system', trailed leading European countries in the campaign against public sector corruption by several decades. Britain's North American colonies lagged even further behind. Political patronage oiled the political process. Macdonald learned the patronage system in pre-Confederation politics, and he used it extremely effectively when he became Canada's first Prime Minister (Gwyn, 2011: 208-9). Respectability required employment, and politicians unapologetically passed out comfortable indoor jobs as well as contracts requiring large numbers of seasonal workers to their supporters. Contracts for infrastructure projects were prime patronage plums.

Ultimately, politicians were influenced by the popularity of the prairie settlement component of the national policy. In 1868, the MP D'Arcy McGee, stated the policy of the government succinctly when he said that "the future of the Dominion depends on our early occupation of the rich prairie land" (Owram, 1992: 76). The "important subject of western territorial expansion" was the only significant issue mentioned in the Throne Speech which opened Canada's first parliament.

Successful settlement of the prairies required a marketable product. It was the Expansionist movement which developed in Canada West that introduced the idea that wheat could replace fur as the exported staple. An extensive wheat producing region implied railway connections with ports and sources of such inputs as the farms of the day required.

Existing interest groups in the decision-making centres of the newly formed country expected to benefit.

#### **4.1 The Expansionist Movement**

Owram (1992) outlines in great detail how an Expansionist movement developed in Canada West in the middle of the nineteenth century. The original handful of Expansionists were descendants of Empire Loyalists who had received land grants from the Crown when they opted to move north after the American Revolution. Their fervent nationalism developed out of their loyalty to Britain, envy of America's economic success and fear of U.S. annexation. In a relatively short period of time they had convinced themselves, their fellow colonists, and political decision-makers that control of the North-West would enable Canadian energy and vitality to transform its vast potential into a "new Britannic Empire on these American shores" or, at least, "a jewel of the empire in the west to rival India in the east" (Owram, 1992: 57).

Unfortunately, the potential profitability of wheat farming in the North-West was largely a product of Expansionist imaginations. Natural calamities had repeatedly frustrated the Selkirk settlers' attempts to raise crops, and the colony depended heavily on raising livestock and hunting and fishing for its survival. These difficulties are significant because the rest of the prairie region turned out to be even less suited to agriculture.

Although the work of Friedrich List was used in Canada to bolster protectionist arguments, the ideas of his fellow countryman Johann Heinrich Von Thunen were ignored. In 1826 von Thunen published his treatise on the impact of transportation costs on the viability of commercial agricultural production. He developed this theory on the basis of personal experience with agricultural production on his own estate in Mecklenburg. The cost of transporting grain to market would have been recognised as an important impediment to exports from the Canadian prairies had von Thunen's insights been more widely known at the time.<sup>72</sup> As it happened, there is no evidence that any consideration whatsoever was ever given to potential constraints on the economic viability of wheat production on the prairies.

By far the most spectacular accomplishment of the Expansionist movement was its success in transforming the prairies from a frigid wilderness into the future 'granary of the empire'

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<sup>72</sup> Von Thunen's work was a critique of Ricardo's rent theory (Ohlin, 1935). It was not published in English until 1966 when a translation by Carla Wartenberg, edited by Peter Hall, appeared with the title *The Isolated State* (Hall, 1966). The more interesting question is whether the prairie settlement component of the national policy would have been less enthusiastically pursued had von Thunen and List been *equally* well known in Canada at the time.

in the minds of residents in Canada West. The Hind expedition of 1857 estimated that 40 million acres of land in the region was suitable for farming. By 1884, a publicist for the CPR had increased the estimate to 300 million acres without any further corroboration (Owram, 1992: 163).

#### **4.2 Crown Lands Department**

The Crown Lands Department was a key component of the Expansionist movement and also an important source of patronage. Although customs duties were by far the main source of government income, sales of crown lands also made a contribution. Senior positions provided privileged access to information and opened up opportunities for speculation as well as surveying and road construction contracts.

By the mid-1850s, the Crown Lands Department in Canada West was running out of land to sell. Expansion onto the prairies would give it a new lease of life. While he was head of the Department, James Cauchon warned that the dwindling availability of potential agricultural land in Canada and the relative abundance of such land in the United States would precipitate a crisis in the colony. The growing flow of Canadians to the U.S. after 1850 confirmed his assessment. He also stoked animosity towards the HBC when he published legal evidence suggesting its claim to the North West was invalid (Owram, 1992: 50-54; Meyer, 1974 Chapter III).

In 1857, the Crown Land Department, now run by Philip VonKoughnet -- another leading Expansionist -- dispatched the Hind/Dawson expedition to the HBC territory. Despite the pretence of scientific evaluation, it is likely the objective of the Hind party was to find evidence to justify the term 'fertile belt' which was already being applied to an arc of land between the Red River Settlement and Edmonton.<sup>73</sup> While the expedition was still away, the Crown Lands Department issued a map whose title, *Of the North West Part of Canada*, laid claim to the region and shamelessly depicted the entire southern prairies as "fine land" without the slightest shred of evidence. Maps based on the expedition's exploratory work published in 1860 were assiduously reproduced and became well known.

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<sup>73</sup> An expedition led by Captain John Palliser dispatched from Britain the same year concentrated on the part of the region south of the fertile belt. It returned with the assessment that the Great American Desert extended north of the 49<sup>th</sup> parallel, and this part of the region became known thereafter as 'Palliser's Triangle'.

### 4.3 Public Works

Publicly-funded projects constituted an important source of business revenue and employment in pre-confederation Canada. Railway building and the surveying which preceded it were labour intensive, and allocation of contracts for public works had long been a mechanism of political patronage. Confederation received support from segments of the population who had benefited from publicly-funded infrastructure projects in the past and anticipated more of the same in the future.

The Maritime colonies all made public funding of railways a condition for joining Confederation.<sup>74</sup> The Pacific railway was key to the Expansionist goal of a transcontinental nation, and became part of the agreement reached with British Columbia at the suggestion of Canada's negotiators. Joseph Trutch, the leading negotiator of the terms under which BC entered Confederation in 1871, was encouraged by promises of railway construction contracts and the Lieutenant-Governorship.<sup>75</sup> Construction was to begin within two years with a target completion date of 1881.<sup>76</sup>

The Pacific Scandal, which toppled Macdonald's Conservative government in 1872, exposed the extent to which railway building and politics were intertwined. The original consortium lined up to build Canada's Pacific Railway included the American railway tycoon Jay Cooke and Montreal shipping magnate Hugh Allan. Scandal ensued when it was revealed that Macdonald had accepted electioneering funds from this consortium. As den Otter (1997: 160) puts it, "opposition (to the Pacific Railway) was inspired less by patriotic concerns than by partisan considerations. Clearly, when the philosophy of railways was rendered into a multimillion dollar business proposition, it quickly degenerated into a messy political imbroglio."

### 4.4 The Manufacturing Sector

The economic and fiscal crisis that followed U.S. abrogation of the Reciprocity Agreement, and the looming need for substantial revenue for post-Confederation infrastructure projects,

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<sup>74</sup> Prince Edward Island joined Confederation in 1873. It also required a railway to join, but it made no commercial sense on a relatively small island. But the ideology of infrastructure triumphed and it was built nonetheless.

<sup>75</sup> As tariff revenue collected by the federal government was allotted to the provinces on the basis of their (non-native) population, the BC 'population' was exaggerated to induce it to join confederation.

<sup>76</sup> After various delays, the signing of the Canadian Pacific Railway contract only took place in 1881. Nonetheless a cynical sod-turning ceremony had been held in Victoria in 1872 just before the Pacific Scandal erupted merely to comply with the promise that "construction would begin within two years", a clause of the agreement which brought BC into Confederation.

combined with the political unpalatability of an across-the-board increase in tariff rates to pay for them, created an opportunity that manufacturing interests were happy to exploit.

Manufacturers were poorly organised when the first protective tariffs were introduced by the colonial administration in the late 1850s. When Macdonald became Canada's first Prime Minister, he had strong ties with manufacturing interests in Toronto and Montreal that stood to benefit from a robust protectionist policy. In the 1878 federal election, the question of tariff protection became a decisive issue. By this time the influence of manufacturers and their workforce on the political process had grown significantly. The Liberal opposition alarmed this constituency with its talk of free trade with the United States. The manufacturing lobby played an important role in keeping the Conservatives in office until 1896.

## **5 Interventions**

The interventions in the immediate post-Confederation period that would affect agriculture on the prairies had two ultimate objectives: accelerating the settlement of the region and ensuring that settlement benefited the rest of the country. These interventions fall into three broad categories: creating a conducive institutional environment, providing transportation links to connect the region to the outside world and the tariff which provided manufacturers in 'eastern' Canada with some protection from U.S. competition. The key interventions in each category are briefly outlined in turn.

### **5.1 Administrative Arrangements**

Under the British North America (BNA) Act, the federal government assumed responsibility for all issues not explicitly enumerated as provincial jurisdictions.<sup>77</sup> The latter included land, resources, education, property and civil rights, and collection of direct taxes. The provinces were also allocated responsibility for commerce, unless the commercial activities were 'for the general advantage of Canada' (BNA Act, Section 92.10). Both levels of governments shared responsibility for agriculture and immigration, although the division of responsibilities was not clearly defined.

In the short run, this was irrelevant as far as the prairies were concerned. Canada's first government led by John A. Macdonald intended to follow U.S. precedent and manage the settlement process in the Northwest Territories (NWT) as a federal initiative. The main

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<sup>77</sup> The American Constitution was specifically oriented toward limiting the power of the federal government. Hence in the American case, all powers not specified as Federal were automatically the responsibility of the individual states.

advantage was the latitude to use grants of public lands to help fund railway construction and encourage rapid settlement (Dales, 1966: 150). Creation *ab initio* of local (provincial) governments with control over land and natural resources was not entertained. Under such a scenario, they might sell land to raise revenue and thus retard settlement. Natural resources other than land were also assets whose value could be expected to increase rapidly once settlement got underway in earnest. Allocating access to mineral and timber rights was a longstanding mechanism of political patronage which the federal government wished to reserve to itself for as long as possible.<sup>78</sup>

**Table 1 Interventions in Preparation for Prairie Settlement**

<ul style="list-style-type: none"> <li>• 1867 - British North American Act (Confederation) created the Canadian nation by joining the Province of Canada with two Maritime colonies in a customs union.</li> </ul>
<ul style="list-style-type: none"> <li>• 1869 – Purchase of North West (Rupert’s Land) from Hudson’s Bay Company for 300,000 pounds sterling (GBP) and a grant of prairie land.</li> </ul>
<ul style="list-style-type: none"> <li>• 1869 – The Dominion Land Survey (DLS) begins in preparation for settlement.</li> </ul>
<ul style="list-style-type: none"> <li>• 1872-1876 - The International Boundary Commission made up of British, American and Canadian surveyors marks out the boundary between Canada and the United States along the 49<sup>th</sup> parallel of latitude.</li> </ul>
<ul style="list-style-type: none"> <li>• 1872 - Dominion Lands Act outlined the process whereby settlers could acquire ‘homestead’ land.</li> </ul>
<ul style="list-style-type: none"> <li>• 1873 - North-West Mounted Police established to enforce the rule of law.</li> </ul>

American precedents provided the basic template for prairie settlement. The American practice of surveying land into 160 acre lots and its Homestead Act were reproduced in Canada with only slight modifications.<sup>79</sup> The creation of a mounted police force to enforce the rule of law on the prairies had no American counterpart but was an important part of the effort to impose British administrative infrastructure on the region. The police force and the enlightened policy adopted towards the aboriginal population were initiatives personally

<sup>78</sup> Gustavus Meyer, an American ‘muckraker’ who made it his mission to expose crony capitalism, wrote *A History of Canadian Wealth* originally published in 1914 which dealt with Canadian examples prior to 1890 (Meyer, 1975). His research for a second volume of this study was interrupted by World War I and never completed.

<sup>79</sup> Land was surveyed in square mile ‘sections’ (640 acres) and divided into ‘quarters’ of 160 acres. The basic homestead unit was a ‘quarter section’, although subsequent modifications of the Dominion Land Act made it possible for a settler who had fulfilled the requirements necessary to obtain title to his ‘home quarter’ to purchase an adjacent quarter from the government, giving him a 320 acre farm. The additional quarter section was referred to as ‘pre-emption’

sponsored by the country's first Prime Minister, John A. MacDonald (Gwyn, 2011: Mounted police: 90-92, 118-19; 'Indian' policy - 418-21; 518-19).<sup>80</sup>

## 5.2 Transportation Infrastructure

The 'ideology of infrastructure' loomed large in post-confederation policy. The first attempt to link Winnipeg with the Great Lakes involved construction of a 'road' between the lakes and rivers that formed the route used by North-West Company fur brigades.<sup>81</sup> This project began with a survey in 1858 but construction did not begin for a decade. Prior to its completion in 1871 it was used by soldiers sent to restore order after the Metis had prevented the Lieutenant Governor dispatched from Ottawa from assuming his responsibilities. After absorbing significant public funds it was soon abandoned because travel through the United States was preferred to a tortuous but highly subsidised journey via the all Canadian route (Berton 1974: 42-3).

If nothing else, the 'Dawson Road' demonstrated the superiority of railways. Construction of the transcontinental railway was the larger of two railway projects to which the federal government committed itself in the Confederation negotiations.<sup>82</sup> At the time, American railways were already within striking distance of the 49<sup>th</sup> parallel of latitude which constituted the southern border of the prairie region.

Public investment in the CPR was a huge gamble for a country of only three and a half million people. The motive was the importance attached to rapid settlement of the prairies: should the settlement initiative fail, the railway would not have the land sales and the traffic it required to operate profitably, the country would teeter on the brink of bankruptcy and risk "falling like a ripe fruit" into the welcoming arms of the United States.

The Canadian Pacific Railway (CPR) was a public/private initiative and its construction was the largest 'mega project' of its day. The terms on which this consortium finally agreed to build and operate the Canadian Pacific Railway were widely condemned at the

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<sup>80</sup> Both initiatives were regarded as successful in the short-term, but although the treatment of the aboriginal population in Canada was extremely enlightened by American standards, it formed the basis for the multitude of unintended consequences which remain unresolved to this day.

<sup>81</sup> Tree trunks laid perpendicular to the direction of travel formed the foundation of the 'corduroy' road. It was extremely uncomfortable to use when not frozen solid and covered with snow, and this was precisely the time when the intervening lakes and rivers were navigable. It was known as the Dawson Road after the Simon J. Dawson, the Expansionist given responsibility for laying out the route by the Crown Lands Department and for supervising its construction by the federal government after Confederation.

<sup>82</sup> Section 145 of the BNA Act made provision for the construction of the five hundred mile long government-run Intercolonial Railway from the St. Lawrence to Halifax, to begin 'within six months after the union.' Sanford Fleming was appointed Chief Engineer for this project.



time as unnecessarily generous.<sup>83</sup> According to Currie (1976: 5), public funds for railway construction were “given outright in the form of cash or land, and the recipients had no further claim on the public treasury. They were expected to conduct their affairs “solely with a view to corporate profit”.

**Table 2 Interventions to Accelerate Railway Building**

<ul style="list-style-type: none"> <li>• 1871- Survey of potential routes for a transcontinental railway begins, directed by Sanford Fleming.</li> </ul>
<ul style="list-style-type: none"> <li>• Construction of railway links to the prairies frustrated by delays and corruption under both Conservative and Liberal governments prior to 1878.</li> </ul>
<ul style="list-style-type: none"> <li>• 1878 - A government contract for a railway line to connect Winnipeg to a U.S. railway at the international border is competed.</li> </ul>
<ul style="list-style-type: none"> <li>• 1881 - Contract signed between the federal government and the CPR consortium signed to construct a railway line linking pieces of line already complete or under construction from the Pacific Ocean to Montreal.</li> </ul>
<ul style="list-style-type: none"> <li>• 1885- Canadian Pacific Railway line between the Pacific Ocean and Central Canada via an all-Canadian route completed.</li> </ul>

### 5.3 Tariffs

Tariff policies adopted in post-Confederation Canada continued the protectionist policies of the Province of Canada. During the 1870s there were incessant debates over the relative merits of across the board increases and selective protection in the form of rate differentials among categories of imports. The Conservatives opted for the tariffs that provided protection for Canadian manufacturers and tariffs became a component of the national policy.

Macdonald made protection or free trade the issue in the election of 1878, recognizing the appetite of the electorate for a government that would act decisively to end the Long Depression<sup>84</sup> Cartwright, the Liberal Finance Minister, pointed out that the selective protection advocated by the Conservatives violated the principle of free trade to which Britain now adhered. He argued that “the introduction of a high protective tariff ....would tend to enrich a few, but it would diminish in the long run the wealth and comfort of the

<sup>83</sup> The Pacific Scandal delayed the signing of the contract to build the CPR until 1881. The original terms were a cash subsidy of \$25 million and 25 million acres of land – on which no taxes were to be paid until sold or 25 years had elapsed, whichever came first; the portions of the railway already constructed; public land for railway rights-of-way, stations, shops, and yards; duty free admission of imported material and equipment; and a monopoly for twenty years ‘against any line south of it unless it was a feeder line to the mainline, nor could such a line approach nearer than 15 miles of the border (MacDougall, 1968: 40-41; Friesen, 1984: 177-76). At the time \$25 million was almost twice the government’s annual revenue.

<sup>84</sup> Although the Conservatives won the election decisively, the popular vote was split and the Conservatives only obtained 52.5 per cent of the votes cast. In Manitoba, the Liberals won the popular vote (den Otter, 1997: 201-2)

many” (Morgan & Brown: 1998). This is a classic nineteenth century example of the debate over the role of the state.

Any tariff regime would provide the federal government with the means to raise revenue. The political decision to opt for tariffs that protected domestic manufacturing was interpreted after the fact as a means of providing industry in central Canada with a captive market in the West (Dales, 1966: 145-46). Adding cost to the production of wheat on the prairies by imposing a tariff on goods imported from the United States ran contrary to the objective of accelerating prairie settlement. The assumptions that wheat could be grown in the region and that settlers would rush in to do so as soon as the necessary infrastructure had been provided underlay Expansionist enthusiasm for prairie settlement. No attention was paid to whether or not wheat could in fact be produced in the region on a large scale, nor to whether any production that did occur would be profitable.

**Table 3 Interventions Affecting the Tariff Schedule**

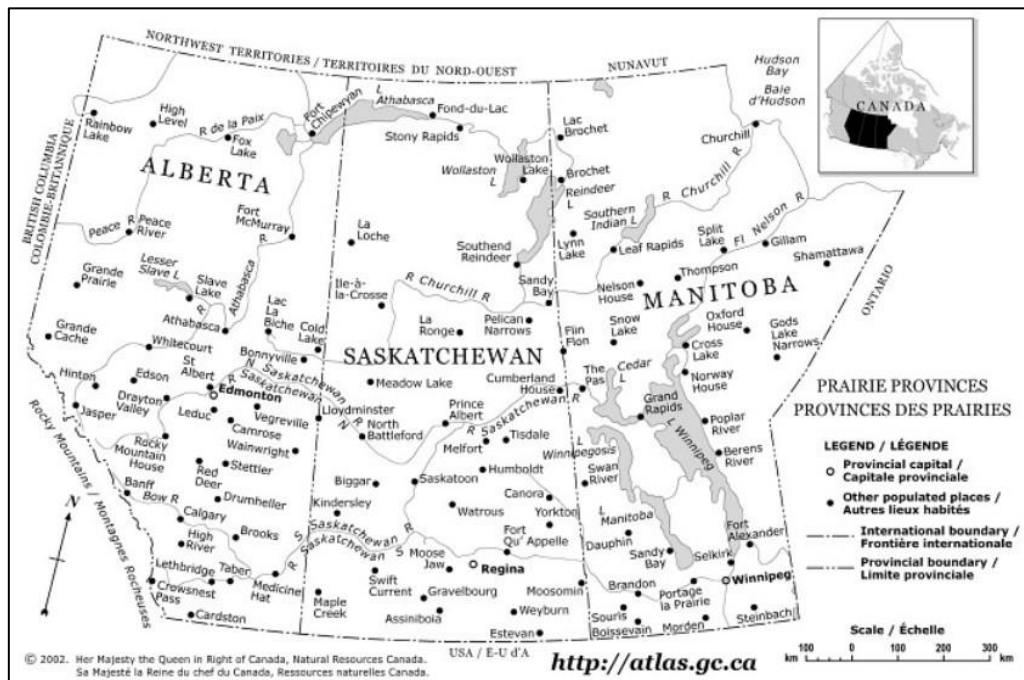
<ul style="list-style-type: none"> <li>• 1867- Tariffs on manufactured goods set at 15%. Levels set as a compromise between the low pre-Confederation rates in effect in the Maritime provinces and the higher rate applied by the Province of Canada.</li> </ul>
<ul style="list-style-type: none"> <li>• 1874 --Tariffs increased to 17.5%.</li> </ul>
<ul style="list-style-type: none"> <li>• 1879 - Tariffs increased to 30-45% on manufactured goods and to 25 per cent on farm machinery.</li> </ul>
<ul style="list-style-type: none"> <li>• 1883 - Tariffs on farm machinery rose to 35%. This increase coincided with the publication by the CPR of its freight rate schedule for western Canada.</li> </ul>

## **6 Consequences**

### **6.1 Settlement, Land Use, and Wheat Exports**

By the late 1870s, there was an arc of speculative settlement scattered through the ‘Fertile Belt’ along the Carlton Trail which ran north-west from Winnipeg. Practical experience gained from attempts to produce wheat in volume and over a wider area than that cultivated by the Red River Settlers soon indicated that the Expansionists had been overly optimistic. When the extent of the gulf between expectations and reality became apparent, it prompted widespread discontent among farmers.

Figure 4 Map of The Prairie Provinces



Source: <http://geogatis.gc.ca/api/en/nrcan-rncan/ess-sst/999362ba-2bf4-5d64-a6ca-19b88ea29d72.html>

CPR management decided to build their mainline across the southern prairies based on the then prevailing Expansionist view that the Palliser’s triangle was no less fertile than more northerly areas.<sup>85</sup> In fact, it was much less productive, but this was only realised once experiments in arable agriculture got underway. In the short run, the location of the railway dictated subsequent settlement patterns.

The anticipated tidal wave of settlers keen to take up the ‘free’ land available for homesteading did not materialise when the railway connection to the United States began operating in 1878. In its desperation to attract settlers, the federal government tried various schemes outside the homestead procedure. It modified the Dominion Lands Act in 1881 to enable colonisation companies to acquire blocks of land at two dollars an acre on attractive terms (Lalonde, 1979). There was an expectation at the time that sufficient land would be taken up under this programme in its first year of this to cover the ten million dollars *tranche* committed to the CPR. Unfortunately, the amendments to the Dominion Lands Act were made during a brief speculative boom in prairie land. The land speculation bubble

<sup>85</sup> When the railway was finally completed in 1885 it reached Burrard Inlet near the current city of Vancouver via Kicking Horse and Roger’s Passes through Selkirk Mountains. The efforts of John Macoun to dispel the ‘myth’ of Palliser’s Triangle are often implicated in the decision. However, construction of the railway across land devoid of settlement gave more flexibility regarding route and the location of future towns, and hence opportunities for the railway to profit from land sales.

broke in 1882, and interest expressed by potential colonisation companies evaporated (McCracken, 1979: 65).

The government also waived the usual requirement that each family group reside on its own quarter section of land to attract group settlements. Most of the groups who took up this option were not interested in the much anticipated economic rewards of prairie settlement. Instead they were interested in an opportunity to create an ideal society from scratch.<sup>86</sup> Only three major settlement groups persisted.<sup>87</sup> Two settlements of Mennonites were established in Manitoba in the 1870s. Mennonites had experience farming in a steppe environment and demonstrated techniques that had worked in Ukraine. In the 1880s, a group of Mormons moved to the SW corner of the region after the U.S. threatened to enforce legislation outlawing plural marriage. The Mormons had prior experience farming semi-arid land and pioneered the use of irrigation in the region.

The railway was completed in 1885 but settlers still failed to flock into the region in the substantial numbers as anticipated.<sup>88</sup> The assumption underlying the prairie settlement component of the national policy was that the region would be quickly occupied by family-owned and operated farms who had acquired land either by homesteading or by purchasing land that had been granted to the CPR. The failure of the settlement initiative prior to 1896 therefore constituted a national disaster. According to Russell's estimates (2012: 205), there were a total of only 45,000 new prairie farms established over the 20 year period from 1881 to 1900. This averages around 2,200 additional farms per year. In response, more vigorous efforts to promote immigration would be adopted.

To generate publicity material, the CPR established demonstration farms along the route of its mainline across the southern prairies. Although these farms were abandoned after a short period of time, the company continued to circulate glowing publicity material that included images of a single bumper crop in 1887. Two large scale 'bonanza farms'

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<sup>86</sup> Some of these were simply eccentric, such as Cannington Manor -- an attempt to transplant English country house living to the Canadian prairies. Some were 'utopian', including those communities which attempted to adhere to cooperative principles (e.g. the Harmony Industrial Association (Johnson, 1979)) or abstinence from alcohol (e.g. the Temperance Colonisation Society (Lalonde, 1979: 20)). Such 'utopian' attitudes would emerge later in the campaign for prohibition and the popularity of the social gospel. Although none of these survived, they are important as they reflect the 'fresh start' attitude to settlement in the region at the time.

<sup>87</sup> A third group were recruited in Iceland after a volcano erupted in 1875. They settled on the west side of Lake Manitoba, which is on the Canadian Shield rather than the prairies. The physical environment placed even more constraints on their attempts at farming than early efforts on the prairie.

<sup>88</sup> Dales (1966: 152) estimates that the population of the prairies increased by a mere 100,000 people in the decade after completion of the CPR, and the entire region with a population of only 300,000, could hardly justify the cost of building the railway.

financed by British investors also failed due to dry conditions, notwithstanding their large scale, access to capital, and reliance on the latest equipment.<sup>89</sup>

Accounts of this period in prairie history often include such statements as “after...an unusual amount of rainfall in 1885, the area reverted to its usual dry state “ (Jameson, 2011: 47 or “(in the 1880s)... a series of drought years occurred, with low yields, frosted grain and wet falls (Strange, 1954: 26). However, at the time settlers first attempted agriculture in the region, what constituted ‘normal’ weather was unknown and each season was a new experience. Frost, dry conditions, and grasshoppers<sup>90</sup> defeated many of the early attempts to raise wheat, making no distinction between the humble homesteader and the aristocratic proprietor of a bonanza farm (Clark, 1931: 42). The ubiquitous use of the term ‘drought’ itself in accounts of the struggle between settlers and the environment implies that nature should conform to human aspirations.

The first wheat exported from Manitoba was from the poor crop of 1876. It was shipped to Toronto via a circuitous route: up the Red River into the United States and thence by rail to Ontario. This purchase was made in order to obtain seed for the following years’ crop after a crop failure in Ontario. Jones (1954: 3) claims the price paid that year was probably the highest ever in real terms. The first shipment of Manitoba wheat to Britain occurred the following year, again relying on river boat transportation and U.S. railways to reach an ocean port. The first shipment of wheat to Britain by an all-Canadian route was 1,000 bushels shipped by rail to the Lakehead and hence via the Great Lakes/St. Lawrence route for transshipment into an ocean going vessel from the harvest of 1883 (Strange, 1954: 11; Wilson, 1978: 14).

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<sup>89</sup> Large scale commercial grain production was undertaken by entrepreneurs such as Major Bell and Sir John Lister-Kaye along the CPR line in the NWT as soon as it was completed (Morgan, 1979; McGowan, 1983: Chapter 5; 1975: 57-67). These two ‘bonanza farms’ at Indian Head and Balgonie, respectively, were encouraged by both the federal government and the CPR in order to showcase the agricultural potential of the region. Unfortunately, insufficient precipitation, hail and frost interfered with production of marketable grain. Both enterprises failed, notwithstanding their large scale, access to capital, reliance on the latest equipment and techniques, and their political connections. Lister-Kaye quickly turned his attention to the range cattle industry, astutely sold all his operations to British investors and made a quick fortune.

<sup>90</sup> Crops grown Manitoba in 1867, 1875 and 1876 were badly damaged by grasshoppers. In 1875 the devastation was so complete that a party was dispatched that winter to the United States to procure seed for the following spring. The seed brought back on that occasion was Red Fife, a variety originating in Canada West that subsequently became popular among growers on the U.S. plains. Among its desirable characteristics was its hardness and the shorter period required to mature. Demand for this type of wheat only materialised once the ‘Hungarian’ milling process which used steel rollers was widely adopted in the milling industry. Red Fife had been well received in the U.K. market and accounted for much of U.S. wheat exported in the 1870s.

In 1895, commercial agriculture on the prairies consisted of some disgruntled farmers producing wheat in southern Manitoba and a range cattle industry in the south-western portion of the NWT. The prairie settlement objective of the national policy was frustrated in this initial period by the tariff, which increased the cost of wheat production in the region. The decision to build the CPR over an all-Canadian route necessitated increases in the tariff rate which further discouraged would-be prairie farmers. The tariff was intended to encourage manufacturing, but an expanded market for Canadian-made goods was an additional 'benefit'.<sup>91</sup>

## **6.2 Railways**

When the CPR was finally built, the project was managed by Americans and its contract provided a tariff exemption for material and equipment imported from the U.S. This suggests the urgency attached to the settlement component of the national policy. CPR management also brought new standards of efficiency into the construction of Canadian railways, and two of their sub-contractors, David Mann and William Mackenzie would later transfer that acumen to a rival company, Canadian Northern Railway (CNoR).

The CPR's monopoly quickly emerged as one of the main frictions between the federal Conservative government and the Manitoba provincial government, under pressure from local farmers and business over freight rates (den Otter, 1982: 135). After struggling to create the CPR on the assumption that it would be self-supporting once complete, the architects of Confederation were understandably reluctant to jeopardise its survival chances.<sup>92</sup>

Macdonald persistently disallowed legislation chartering railways in Manitoba passed by the Conservative provincial government of John Norquay and when they attempted to go ahead anyway, the federal government frustrated Manitoba's efforts to raise the necessary capital and precipitated a provincial election. Both parties in the 1886 Manitoba election promised a provincial railway up the Red River Valley to link with American lines and provide competition for the CPR line. The Liberal administration of Thomas Greenway, which followed Norquay in 1888, was the short term beneficiary when the CPR agreed to relinquish the monopoly clause in exchange for a one-time federal government bond

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<sup>91</sup> Dales (1966: 145-6) argues persuasively that the logical consistency of the national policy was rationalised well after the implementation of the three components by the prominent Canadian economic historian, Harold Innis.

<sup>92</sup> Charles Tupper, now the federal Minister of Railways and Canals, stated quite bluntly at the time: "Are the interests of Manitoba and the North West to be sacrificed to the interests of Canada? I say, if it is necessary, yes" (Gwyn, 2011: 542). Such remarks did much to inflame resentment in the region.

guarantee. Greenway chose the Northern Pacific, an American company, as a joint venture partner and a Winnipeg to Emerson line and a branch line from Morris (south of Winnipeg) to Brandon (west of Winnipeg) were built in 1891. These provided a link to the United States port of Duluth on Lake Superior.

Greenway insisted that rates on the Northern Pacific and Manitoba Railway be lower than those on the CPR line on the opposite side of the Red River. The CPR responded by reducing its rates. Northern Pacific found itself saddled with a perennially unprofitable railway, under continual pressure from the Manitoba government to reduce the rates charged to ship prairie grain to the U.S. Lakehead at Duluth, and regretting the financial contributions it had presumably provided the provincial Liberal party.

Clifford Sifton, a prominent cabinet minister in the provincial administration of Thomas Greenway and an early ally of disillusioned farmers was credited with devising the ‘apparently painless’ method of financing railways’ involving government guarantees of both principal and interest on railway bonds (Hall, 2003: Dictionary of Canadian Bibliography (DCB) - Clifford Sifton).<sup>93</sup> He arranged financing on this basis for the building of the Lake Manitoba Railway.<sup>94</sup> This financial innovation was, however, nothing more than the reinvention of the pre-Confederation mechanism used to finance the ‘ideology of infrastructure’ that resulted in Canada inheriting substantial debts from its colonial predecessors.

After completing its mainline, the CPR continued constructing branch lines, mostly in Manitoba. By the end of 1896 it operated 2,176 miles of track in the western division (Ft. William to Donald, BC). Of these, 956 miles were branch lines (Eagle, 1989: 3, 105).<sup>95</sup>

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<sup>93</sup> The Sifton family was of Anglo-Irish origin and well steeped in the expansionist movement. Clifford’s father, John Sifton was a longstanding supporter of Reform Party politicians George Brown and Alexander Mackenzie. Mackenzie rewarded Sifton with contracts to build a telegraph line northwest from Winnipeg and two sections of the transcontinental railway between the Red River and Port Arthur while he was Prime Minister and Minister of Public Works. The family moved to Manitoba and John Sifton supervised this work and began farming (Hall, 2003 2003b).

Sifton was also credited with helping resolve the ‘The Manitoba Schools Question’. This was the struggle to eliminate the right to denominational schools --which the federal government had conceded to Manitoba in the immediate aftermath of the Red River Resistance. After a brief surge in settlers from Ontario and the departure of most Metis for the NWT made the province predominantly Anglophone. Sifton’s involvement in the schools issue brought him to the attention of Wilfrid Laurier, whose cabinet he joined as Minister of the Interior after the 1896 federal election.

<sup>94</sup> This line was completed between Gladstone and Dauphin Manitoba in 1896. It went bankrupt and became part of the Canadian Northern Railway.

<sup>95</sup> The only other railway company operating in the region in 1896 was the Alberta Railway and Coal Company line. The initial line ran from collieries near Lethbridge AB to the CPR mainline at Dunmore Alberta. A line to Great Falls MT. crossing the U.S. border at Coutts AB was built in 1890 to supply coal

### **6.3 The Tariff**

When the all-Canadian route became a political necessity, tariff increases were required to cover the additional cost. This meant that prairie farmers were denied the opportunity to purchase agricultural inputs at the same price as their competitors across the border in the U.S. Their options were to pay U.S. costs plus the tariff and the incremental freight rate required to bring the goods into Canada or the Canadian price which reflected the degree of tariff protection plus the more considerable freight charges required to bring the same goods from Central Canada.

Organisation of farmers in Manitoba received considerable impetus when tariffs on farm machinery were increased to 35 per cent in 1883. Vociferous protest resulted in only a token reduction (Lalonde, 1979; Solberg, 1987: 106). The farmers' movement also reacted negatively to the CPR's first freight rate schedule which was published the same year. From then on, the tariff and freight rates – whose individual impact was indistinguishable from the farmers' perspective – would be the main lightning rods of agrarian protest.

### **6.4 Political Consequences**

One of the first blunders Canada made in its haste to facilitate settlement of the prairies was to exclude those already living there from the process. In the period leading up to Canada's acquisition of Rupert's Land, the majority of the population along the Red River were Francophone Metis. The first of a trickle of protestant settlers from Canada West arrived in 1849. They naturally allied themselves with the Anglophone Metis and opposed HBC administration of Rupert's Land. Three of the early arrivals founded a newsheet, the 'Nor'Wester, which became the organ of the 'Canada Party' which sought annexation of the region by Canada.

In 1869 the arrival of a federal government survey party from Canada provoked resistance from the Francophone Metis led by Montreal-educated Louis Riel. One of the surveyors taken prisoner was subsequently tried and executed under mysterious circumstances. This incident encouraged annexationists both within the colony and across the border in Minnesota. The leaders of the 'Canada Party', John Schulz and Charles Mair, fled to Ontario and used the death of an Ontario Orangeman surveyor at the hands of Francophone Catholics to provoke anti-French sentiment in central Canada. This led to a brief surge in migration from Ontario, motivated by a desire to ensure that Anglophone Protestants

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to the Great Northern Railway and smelters at American mines (den Otter, 1982: 151). Despite a tariff imposed by the U.S., access to Canadian coal reduced the Montana price by two-thirds.



outnumbered Francophone Catholics in the Red River Settlement. The departure of many Francophone Metis for the NWT in the aftermath of the Red River Resistance helped realise this objective.

Metis resistance to the Canadian take-over was the first unintended consequence of the national policy. A number of unanticipated political problems arose: Manitoba was granted provincial status as part of the post-resistance compromise. Although it was denied the right to dispose of its public land, the federal government no longer had a completely free hand in managing the settlement process. Disputes between the two levels of government over railway charters, transfer payments and provincial boundaries followed. The struggle over provincial rights between the two levels of government compounded the alienation that originated in the economic difficulties of the farm population.

Macdonald had been warned that Metis migration to the NWT after the Riel Resistance and the failure to fulfil commitments to an already unhappy native population might lead to insurrection. The Rebellion, which broke out in 1885, was again led by Louis Riel and the Metis, but it reflected grievances keenly felt by a broad spectrum of territorial residents.

The Riel Rebellion introduced an issue, the Hudson's Bay Railway (HBR), which more than any other channelled Expansionist frustration into support for regional grievances directed at the federal government. Settler discontent was higher in the NWT than in Manitoba because it was proving more difficult to grow wheat. Administrative decisions were taken in the distant capital—Ottawa. The idea of the HBR to link wheat producers in the 'fertile belt' with foreign markets united all the dissident groups in the region. However it was of interest to the Metis and the native population only because it was *the* important issue for the settlers they sought as allies in their struggle with the federal government. For this reason it appeared in one of the petitions the insurgents dispatched to Ottawa in advance of the Riel Rebellion.<sup>96</sup>

The monopoly granted to the Canadian Pacific Railway was blamed for the high costs of agricultural inputs. When exportable surpluses of wheat were produced, the low prices farmers received for their crop were also blamed on high freight rates. The tariffs, which

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<sup>96</sup>. Although building a railway along the Carlton Trail was delayed by the CPR Syndicate's decision to build the railway across the southern prairies, a telegraph line was already in operation along the route originally proposed as far as Edmonton. Conway (2006: 41-44) suggests Macdonald intentionally ignored the three petitions in order to force a showdown which would justify extraordinary financial assistance for the railway and boost his own popularity. Irrespective of whether these allegations are true or not, the CPR did get emergency funding at a crucial time, it transported troops west to quell the Rebellion, and Macdonald died in office in 1893 (Gwyn, 2011: 447-452 & 576-577).

provided a measure of protection for manufacturers in eastern Canada and constituted the primary source of public funds at the time, also contributed to the high cost of inputs, particularly agricultural machinery. From the farmers' perspective it was difficult to disentangle the influence of the tariff and transportation on the prices they paid for the supplies they needed, so inevitably whichever grievance happened to be the subject of discussion was blamed for the combined impact.

The first farmers' movement in Manitoba, the Manitoba and North West Farmer's Union, was founded in 1883.<sup>97</sup> Its first convention resulted in a petition listing three demands addressed to the Prime Minister. The first called for an end to the routine disallowance of provincial railway charters by the federal government, the second, for removal of the tariff on farm equipment and the third, for the transfer of responsibility for Crown Lands to the Province. The convention also recommended that further settlement be discouraged until these impediments to profitable wheat production were removed.

Many of the same individuals who had been staunch proponents of Expansionism before the collapse of the brief Manitoba land boom subsequently espoused the cause of western alienation. This new 'prairie' perspective required a complete rewrite of the history of the West.<sup>98</sup>

The Nor'Westers and the Metis had become Canadian heroes because they resisted the foreign HBC and its pseudo-colony on the Red River. From this perspective, the 'real' history of the West only began in 1869 when the purchase of the region by Canada was negotiated. The *new* interpretation glorified the Red River Settlement as a pioneering agricultural experiment in the wilderness. Now it was the Nor'Westers – the first of the 'predatory eastern interests' – who were painted as the interlopers, using violence and liquor to intimidate the natives. Ultimately, even the HBC was rehabilitated as the legitimate vehicle of imperial advance into the region, recognised for its contributions to exploration, the assistance given to missionaries, and for the mutually beneficial trade it conducted with the natives. This revised interpretation of events received symbolic

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<sup>97</sup> Prairie farmers were incensed when the tariff on farm machinery was raised from 25 to 33 per cent in 1883 (Lalonde, 1979: 27). Under protest, these rates were rolled back to 20 per cent except for expensive machinery which was only reduced to 30 per cent. This rollback was interpreted as favouring 'eastern' farmers at the expense of prairie farmers. The CPR published its freight rate schedule the same year, although its mainline was still under construction.

<sup>98</sup> Owram (1992: Chapter 9) provides a detailed and compelling examination of this transformation, and the individuals and institutions involved. The Manitoba Historical and Scientific Society, founded in 1879, promoted this 'Manitoba School' of Canadian history.

confirmation in 1891 when a monument funded by a donation from the Countess of Selkirk was erected to commemorate the Seven Oaks Massacre.

Considerable effort and public funds were expended creating conditions under which Expansionist aspirations for the West might be realised. These initiatives collectively undermine the assertion that the prairie grain economy was the product of *laissez-faire* policies. On the contrary, building the transportation and institutional infrastructure was a huge public sector gamble that failed. In 1896 Canada faced precisely the same problems – massive public sector debt, net out-migration to the United States, and a stalled settlement frontier that the Province of Canada had faced in 1856, but on a much larger scale.

## **7 Counterfactual**

The main objective of this chapter has been to establish a base-line for the analysis of the impact of government policy on prairie agriculture in subsequent historical chapters. Nonetheless, this section considers what might have happened on the prairies had Canadian governments not acted as they did right after Confederation. Three questions are addressed:

- Would the western part of British North America have been annexed by the United States?
- Would the orientation of the railway network and trade have been different?
- Would the pattern of settlement have changed appreciably?

### **7.1 Would the western part of British North America have been annexed by the United States?**

Britain and its Canadian colonies clearly had an interest in maintaining control over the northern part of North America. Although the full extent of its natural resources were unknown at the time, it did constitute a territorial bridge between the Atlantic and Pacific oceans – a second-best North West Passage.<sup>99</sup> Whether British North America west of the Great Lakes would be annexed by the U.S. was ultimately a function of how much each side wanted control and how much each was prepared to pay to obtain that control.

The United States did have a propensity to expand its territory. The reaction of the Thirteen Colonies to the Quebec Act has already been mentioned. After the Revolution, Louisiana was purchased from France. Canadian Confederation was overshadowed by America's purchase of Alaska from Russia earlier the same year. In both cases, however,

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<sup>99</sup> In an 1879 speech Tupper emphasised this role of the CPR (quoted in Strange, 1954: 16).

the transaction involved a willing, increasingly desperate, and autocratic seller. Britain was none of these.

Nor can it be denied that there were U.S. interests advocating annexation from time to time. Evidence ranged from American complicity in raids on Canada by the Fenian Brotherhood to the individual efforts of Americans such as James Wickes Taylor, who made it his personal mission to extend the state of Minnesota north along the Red River into Rupert's Land.<sup>100</sup>

However, after the Oregon Agreement of 1849 the U.S. government showed little interest in Canada. Britain made the British Columbia mainland a crown colony when a series of gold rushes began in 1858. Although the vast majority of gold prospectors were Americans and negotiations were already underway with Russia for the purchase of Alaska, the U.S. made no attempts to displace Britain in the region. The American Civil War and the subsequent Reconstruction diverted attention to domestic issues after 1860. The public sector debt accumulated building canals and railways pushed Britain towards an arms-length relationship with its North American colonies. That same debt extinguished any American interest in annexation (Pennington, 2011: 730; Mather, 1881).

The relationship between the U.S. and Britain soured during the Civil War because the Confederate States built six warships in British shipyards. After the war, the U.S. claimed compensation from Britain for the damage inflicted by these vessels.<sup>101</sup> These claims were provisionally settled in 1868 but not ratified by the U.S. Senate. Early in 1871 the Alabama Claims were re-negotiated at a conference in Washington DC. The Canadian Prime Minister Macdonald participated as part of the British delegation. The right of Canada to self-determination was not in dispute after this conference.<sup>102</sup> U.S., British and Canadian surveyors made up the International Boundary Commission which started marking out the 49<sup>th</sup> parallel of latitude across the southern prairies in 1872. This demarcation line had been confirmed as the boundary in the 1818 Treaty of London (MacGregor, 1981: 24-25). British Columbia joined Confederation later the same year and the first Pacific Railway contract was signed the following year.

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<sup>100</sup> The Ramsey Resolution put before Congress but not approved in December 1867 demanded that Britain cede the HBC territory and British Columbia to the United States. Taylor was among those who instigated this resolution (den Otter, 1997: 165-66).

<sup>101</sup> The most destructive of the six vessels built in Britain was the Alabama. The U.S. claim for compensation is therefore generally referred to as the 'Alabama claim'.

<sup>102</sup> Gwyn (2011: 160-174) provides a detailed account of the Washington Conference of 1871.

## 7.2 Would the orientation of the railway network and trade have been different?

Huge importance is attached to the nation-building dimension of the CPR project in Canadian historiography. It is frequently inferred that had the CPR not been built or had it not taken its eventual all-Canadian route running north of the Great Lakes, Canada would not have become a transcontinental nation. Den Otter (1997: 159) outlines the standard interpretation of the role the CPR played in Canadian history as follows:

By dramatizing the CPR as an iron bond tying diverse colonies and territories into a mighty northern nation, the railway myth has profoundly influenced the interpretation of the first decades of the nation's history. It has created for example, two assumptions covering most accounts of the CPR's past. The first portrays the railway as primarily a patriotic adventure, an essential part of the government's national policies. The second, likewise derived from the nation-building theme, embraces the idea that the Pacific railway was always intended as an all-Canadian project financed and built entirely by Canadians through Canadian territory. By accepting these two tenets, most historians of the railway see the Pacific Scandal as a perilous moment in Canadian history, a crisis when the fledgling nation was almost lost to aggressive American manifest-destiny businessmen and politicians.

The decision that the railway would follow an 'all Canadian route' north of Lake Superior was made before the CPR contract was signed in 1881. There was an undoubted political and military value to this option: in 1885, even before the Lake Superior section was complete, the railway transported troops west to quell the Riel Rebellion.

One way of assessing the *political* value of the railway might be to consider the cash sum the federal government was prepared to invest in the project at the outset: twenty five million dollars. The accompanying land grant of 25 million acres of land "fairly fit for settlement" guaranteed a congruence of interests between the federal government's objectives and the railway over settlement: if there was no settlement, the land could not be profitably disposed of, and there would be no traffic to maintain the railway beyond its initial subsidy.

There has been on-going discussion about whether the CPR contract was excessively generous (e.g. Dales, 1966: 152; George, 1968). Notwithstanding the dearth of settlement on the prairies prior to 1900, the railway survived and showed a profit: it began paying a dividend in 1889. Transcontinental transport of high value goods from the Far East bound for Britain made a significant contribution (Pole, 1999). However such debates are beside the point: in 1879 there was only one serious contender for the project, and the Conservative government decided to proceed.

The period during which the Reciprocity Agreement between British colonies and the United States was in effect was widely perceived as benefiting the colonial economies. During the period in which the route of the railway was under discussion there remained hope that the Reciprocity Treaty might be reactivated. It is also worth pointing out that both before and since the Reciprocity Agreement, Canadian interest groups have from time to time advocated closer commercial ties with the U.S.<sup>103</sup>

Nonetheless, in the standard history much is made of the economic threat the United States posed to Canada, particularly the ability of U.S. railways to “siphon off” ‘Canadian’ commerce from the prairies in the absence of any other railway connection. This argument seems a little suspect in light of the assiduous, if ultimately ineffective, efforts of British colonies to siphon American trade down the St. Lawrence before Confederation. The entire thrust of railway building east of the Great Lakes had been to link British colonies with U.S. railways.

Jay Cooke and his Northern Pacific Railway interests are usually painted as the villains in the standard interpretation of events. Den Otter (1997: Chapter 6) demonstrates that the rampant ‘villainy’ that surfaced in the face of the prospect of a major public sector project was evenly distributed between Canadians and Americans, and between holders of public office and businessmen.

Den Otter also makes it clear that the businessmen, whether Canadian or American, were only trying to make some money on their investments. Cooke’s flirtation with the Minnesota annexationists, of which much is made by those taking a patriotic Canadian line, was merely a businessman’s reaction to an opportunity that opened up when the federal Conservatives stumbled in their efforts to bring the Red River Settlement into Confederation.

The financial difficulties Cooke faced after 1873 removed him as a potential partner when the Canadian Pacific Railway contract was finally negotiated in 1881. A ‘Canadian’ consortium led by Donald Smith, the Governor of the HBC, took over his St. Paul and Pacific Railway and completed it to the Canadian border at Pembina.

Den Otter goes on to rebut the second premise in the above quote, namely that the CPR was always intended to be a Canadian project following an all-Canadian route (1997: 158-184).

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<sup>103</sup> One of the early examples was an initiative by Montreal-based businessmen sparked by the blow dealt commerce in that city by the merger of the North-West Company and the HBC in 1821.

During the immediate post-Confederation period, it was acknowledged that branch lines from the prairies to link with U.S. railways would be the least expensive option. Indeed, until the Conservatives returned to power in 1878 this was the option pursued (den Otter, 1997: Chapter 6). The first railway built from Winnipeg under the Liberal government of Alexander Mackenzie went south to the U.S. border, and the first substantial exports of prairie wheat travelled along it to U.S. and British buyers. The high cost of the CPR was given for the unprofitability of prairie wheat production in this period: “Canadian railways are an expensive alternative to American railways rather than no railways at all” (Fowke, 1978: 69). However, there is no evidence American railways were less expensive, and the flow of early grain shipments to both Canadian and U.S. ports at the head of Lake Superior suggests there was little if any difference in rates (Norrie, 1978; MacDougall, 1966; Currie, 1940).

### **7.3 Would the pattern of settlement have changed appreciably?**

Finally, the minimal positive effect the national policy had on settlement of the prairies prior to 1896 suggests that things might not have been significantly different without these interventions. Settlers had made their way into the region despite considerable difficulties before the railway links were built, but no dramatic surge in settlement occurred once they were in place. The tariff was a disadvantage to those already trying to raise wheat in Manitoba, and ranked high on their list of grievances. The ready availability of ‘good’ land which could be farmed profitably in the United States, the destination traditionally preferred by foreign immigrants, is the consensus explanation for the lack of settlement on the Canadian prairies.

## **Chapter 4**

### **The Settlement Boom and the Wheat Economy: 1896-1929**

This chapter deals with the period in which the prairie settlement objectives of the national policy were finally realised. Investments in grain production and its associated businesses, the impressive growth in wheat exports and Canada's growing share of the international market are generally referred to as the 'wheat boom'. Use of the term 'boom' is unintentionally apt: it implies unsustainable growth. Interventions to encourage settlement and deal with the disruption of markets during World War I exaggerated the boom.

Although the profitability of farming did start to improve in the portions of the region best suited to wheat production, the large number of new arrivals prior to 1914 pushed the margin of cultivation onto land where yields were highly variable and freight charges were higher. Prairie farmers remained generally dissatisfied with the economic rewards they earned.

Effective farm organisations, farmer-owned grain handling and marketing cooperatives, and new political parties speaking for the farm population were established. Blame for the farmers' financial difficulties shifted from the federal government and the national policy to business combines: the private grain trade, institutions such as the Winnipeg Grain Exchange, and the CPR. During this period, the federal government became the farmers' ally against these new villains.

#### **1 The Crisis**

The crisis Canada faced in 1896 arose because efforts to fill the prairies with prosperous farmers in the period since Confederation had failed. Despite heavy investment to encourage agricultural settlement, creating the necessary institutional infrastructure and providing railway connections, the expected flood of settlers did not materialise. The benefits Canada anticipated from a prosperous agricultural economy on the prairies remained elusive. However, servicing the associated public sector debt weighed heavily on the government's financial resources.

When the Liberal government of Wilfrid Laurier was elected in 1896, opinion on the nature of the problem was markedly different depending on the point of view of the observer. Those outside the region who had supported the national policy because prairie wheat exports were expected to boost the national economy saw the problem as one of cost and



lack of results (e.g. Friesen, 1984: 534). For those already trying to farm in the region, the problem was low returns from wheat production.

## **2 Ideas and Ideologies**

The opinions held by prairie grain growers were heavily influenced by ideas circulating in their former homes. The initial influx of settlers to Manitoba after the Riel Resistance was predominantly from Ontario. The Mennonites who arrived in the 1870s were religious, but apolitical. Lipset (1950: 25) points out that Saskatchewan was settled by working class immigrants during a period of rising trade-unionism, a growing world socialist movement and active experimentation with cooperative organisations in Britain, Germany and Scandinavia. The influence of the British Labour Party was evident in the leadership of Saskatchewan farm organisations.<sup>104</sup> The other important influence came from the United States, where settlers on the wheat frontier also felt themselves at the mercy of the railways, the elevator companies and the grain buyers, but had no national policy to distract them from the ‘real’ culprits.

Olson (1982: 39) observed that the American wheat frontier involved a large constituency focused on common problems and, in the absence of alternatives, discussing their economic grievances became the principle leisure time activity. The same was true in Canada. Prairie winters are long, and the end of field work for the year marked the beginning of social events sponsored by farm organisations and churches at the local level.

American scholars Paul Sharp (1948) and Seymour Lipset (1950) called socio-political turmoil on the prairies between 1896 and 1929 the Agrarian Revolt and Agrarian Socialism, respectively. The social gospel gave the agrarian populist movement its moral compass.<sup>105</sup> This was a predominantly protestant religious movement which targeted social and economic injustice without delving very deeply into the origins of those ‘injustices’. On the prairies, the message preached from church pulpits reinforced the efforts of those trying to organise grassroots support for farm protest initiatives. The social gospel flourished in Canada for the same basic reasons as many other imported ideologies – it provided answers to questions that were frequently on the minds of the population. It became a vehicle for transforming those questions into social and political action.

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<sup>104</sup> While Fred Green, a former member of the British Labour Party was secretary of the Saskatchewan Grain Growers’ Association it distributed thousands of copies of the American socialist Edward Bellamy’s classics *Looking Backward* and *Equity*. For many recipients, these were their first exposure to socialist ideas.

<sup>105</sup> Allen, 1992; 1971. Its British counterpart, usually known as Christian Socialism, was predominantly an urban industrial workers’ movement.

In the period before and after the First World War (WWI), the social gospel in western Canada was a crucial ‘anti-capitalist’ influence (see especially Earl, 1992). It added a veneer of moral superiority and religious fervour to ideas of this period and played a pivotal role in turning regional discontent towards business ‘combines’ and hence away from the federal government. Many clergy were active in agrarian organisations and prominent social gospel advocates such as Rev. Salem Bland had regular columns in the Grain Growers’ Guide.<sup>106</sup>

As was the case with agrarian populism in general, the influence of the social gospel was much stronger in Canada than it was south of the border. In the United States, urban industrial workers were the mass-public most influenced by the social gospel, and its impact was evident primarily in trust-busting legislation and the union movement. In the United States, agrarian populism was a transitory phenomenon with minimum lasting repercussions (North, 1993: 40).

One reason farmer discontent was more vehement in Canada lies in differences in the two settlement processes. In the United States, large numbers of settlers were attracted to the Great Plains and minimal efforts were made to channel the flow. In Canada, the federal government actively recruited settlers and made lavish use of propaganda which wildly exaggerated the potential rewards. Disappointment was inevitable when these rewards proved difficult or impossible to realise. Under normal circumstances, a disappointed individual might decide that wheat farming had been a poor choice and try an alternative. However, the existence of large numbers in the same situation suggested the cause of collective distress lay in larger issues.<sup>107</sup> The published work of farmers of the period provides insight into the conviction that they were victims of the capitalist system (e.g. Mills, 1971; Loehr 1968; Partridge, 1925). The social gospel provided plausible explanations for their plight.

The agrarian populist movement on the prairies was reinforced by three ideologies that supported the social gospel’s notions of equity, fairness and social justice. They became deeply entrenched in the psyche of the region’s population.

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<sup>106</sup> The Grain Grower’s Guide was the newspaper published by the first cooperative wheat marketing company, the Grain Growers’ Grain Company (later United Grain Growers). The ‘Guide’ became a medium for raising awareness of the ‘bigger issues’ among its readership.

<sup>107</sup> Hayek drew attention to the fact that any intervention which disrupts economic relationships inevitably benefits some at the expense of others, thereby providing those who are disadvantaged with a legitimate grievance (e.g. Ikeda, 2005: 27). The agrarian populist movement on the Canadian prairies constitutes a large scale illustration of this phenomenon (Friesen, 1984: 193-94).

The first of these was the ‘ideology of cooperation’ which developed out of the conflict between prairie farmers and monopoly capital. It originated in the deep seated animosity prairie farmers developed towards the CPR, the private grain trade, financial institutions and the Winnipeg Grain Exchange.<sup>108</sup> Initially its focus was on alleged collusion between the CPR and the ‘line’ elevator companies. The ideology played down the profit motive in business and emphasised social responsibility.

The cooperative ideology reached its apogee in the 1920s. The collapse of wheat prices after WWI coincided with the removal of government control of grain marketing necessitated by the war. The sharp decline in prices coincided with resumption of the private grain trade and precipitated a heated debate within and among farm organisations about the best economic system for prairie farmers. Disenchantment with the *status quo* led to the exploration of a wide variety of alternative options, up to and including Soviet-style socialism

The second was the “ideology of freight rates”, a term coined by Darling (1980: 11, 67-68ff). Prairie residents convinced themselves that they bore a disproportionate burden of costs under the prevailing freight rate regime. Since freight rates influenced the price of goods brought into the region by rail as well as the price farmers received for their wheat, all prairie residents were affected and ‘freight rate discrimination’ would emerge as the dominant issue in the 1920s (Darling, 1980: 29-30, 47).

The third, the ‘ideology of equity and social justice,’ was articulated as a general principle whenever the agrarian movement sought political intervention and would eventually become the generally accepted metric of ‘good government’ in Canada.

### **3 Interests and Incentives**

#### **3.1 Farmers’ Organizations**

Prior to 1909, many farm organizations in Manitoba and adjacent areas of the United States formed and disappeared in rapid succession. Most of these groups reflected the farmers’ dissatisfaction with the financial rewards they earned. As is frequently the case, the middlemen who earned their living from handling, transporting and marketing grain were blamed. In both countries, the mainstream farm organisations were pragmatic rather than

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<sup>108</sup> The Winnipeg Grain Exchange was founded as the Winnipeg Grain and Produce Exchange, a voluntary, not-for-profit unincorporated organisation in 1887. Originally a cash market, it began trading futures contracts in 1904. It was renamed the Winnipeg Commodity Exchange in 1972 and is currently known as ICE Futures Canada.

extreme. Organisations such as the Non-Partisan League flourished briefly in North Dakota between 1915 and 1921. Detractors denigrated it for its socialist leanings and its political influence rapidly waned. On the prairies, however, farm organisations were socialist and proud of it. The ideas each wave of settlers brought into the region contributed to this attitude.

In Canada, the Territorial Grain Growers' Association (TGGA)<sup>109</sup> was formed in 1901 by farmers who believed that they had just as much right to load railcars from flat warehouses and platforms adjacent to sidings as those who had erected elevators using recently introduced bulk handling technology. They believed the CPR was not allocating railway box cars 'fairly', took legal action against the railway and won their case.<sup>110</sup> This success prompted the formation of the Manitoba Grain Growers' Association in 1905. The next target was the Winnipeg Grain Exchange where farmers believed speculators profited unfairly from their hard work. In fact, the opposite was true: the ability to hedge grain purchases reduced the risk to which traders were exposed while grain they owned was in transit.<sup>111</sup> Suspected collusion among the elevator companies and between the elevator companies and the CPR led to the creation of a farmer-owned grain marketing company, the Grain Growers' Grain Company (GGGC) in 1906.

One of the early leaders of the TGGA, Edward Partridge, was an important exception to the pragmatism practised by most farm leaders (Knuttila, 2007, 1994; 1989). Partridge was an admirer of the English socialism of John Ruskin and is frequently acknowledged as the intellectual behind agrarian discontent in western Canada.<sup>112</sup> He saw farmers as "participants in the gigantic class struggle between huge interlocking financial, industrial and commercial interests, and ... the farmers and the city workers". Partridge was very influential in shifting the blame for farmers' grievances away from the national policy to big business. He was involved in both political lobbying and cooperative initiatives. In his role as the first editor of the Grain Growers' Guide he outlined his plan for a network of state-funded grain handling facilities operating as public utility. His formal link with

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<sup>109</sup> This organization was renamed the Saskatchewan Grain Growers' Association when the NWT was divided into the provinces of Alberta and Saskatchewan in 1905.

<sup>110</sup> The CPR appealed the original decision in this case (rendered, incidentally, by Harry Partridge, the brother of the activist mentioned below) to the Supreme Court (Eagle, 1989: 82-83).

<sup>111</sup> Various Royal Commissions, including the Stamp Commission of 1930, concluded that farmers received higher prices as a consequence.

<sup>112</sup> Lipset (1950: 43), however, points out that, "...in an older, more stable society such a man would have been simply another 'crack pot' agitator. In the newly settled, loosely structured society of the West, with its numerous unresolved economic and social problems, a man of ideas could command a hearing".

GGGC, which pursued practical solutions to farmers' problems within the existing institutional framework, was short-lived.

The ideology of co-operation led farmers to organize three provincial Wheat Pools on cooperative principles when the post-World War I (WWI) price correction pushed the agrarian movement into overdrive. They combined both the marketing and handling aspects of the grain business but generally avoided open market mechanisms such as the Winnipeg Grain Exchange, the institution on which United Grain Growers (UGG) and the private grain companies relied to reduce their transaction costs.<sup>113</sup>

The three pools marketed grain through a Central Selling Agency (CSA) which established sales offices in fifteen major overseas markets. The CSA began operating on the principle that releasing grain into the market evenly throughout the crop year -- 'orderly marketing' -- would raise the annual average 'pooled price' farmers received. When this proved unsuccessful, the Pool blamed farmers who were selling their grain outside Pool channels. The proposed 'solution', making pooling compulsory at the domestic level, caused much debate. Saskatchewan became the largest wheat producing province and its entire economy was heavily dependent on this one commodity. In the late 1920s, the campaign to increase participation in voluntary pools from around 60 per cent to 100 per cent, brought together the radical and practical wings of the farmers' movement in Saskatchewan into a single organisation, the Farmers Union of Canada (Saskatchewan Section) but the Pool remained voluntary. From 1927 until the financial crash in the autumn of 1929, the more radical elements within the UFC battled the more conservative leaders of the Saskatchewan Wheat Pool (SWP) whose President, A. J. McPhail opposed the plan. Given the preoccupation of the agrarian populist movement with 'monopoly capital', it is ironic that a segment of the farm population saw a monopoly seller of Canadian wheat as the solution to their problems.

### **3.2 Politicians**

Clifford Sifton encouraged the federal Liberal party to adopt a more sympathetic position towards the grievances of prairie farmers. While a provincial politician in Manitoba, he had

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<sup>113</sup> GGGC became United Grain Growers (UGG) when it merged with the Alberta Elevator Co. in 1917. The Wheat Pools eliminated the intra-year price fluctuations that irked Pool supporters by providing a single 'pooled' price to farmers each crop year, irrespective of when grain was delivered to the local elevator. This was done by paying an initial price on delivery of grain, and a final price once the year's revenue and expenses were known. However, this required a significant on-farm storage capacity, and much of the risk was essentially transferred from 'speculators' to the farmers themselves as they lived with uncertainty regarding the value of the grain they had shipped until they received their 'final' payment.

curried favour with farmers' organisations when the Liberals occupied the Opposition benches, but had shown more sympathy to business interests once his party came to power.

Sifton appeared to be following the same path when he became Wilfred Laurier's lieutenant in the West and Minister of the Interior after the 1896 federal election. At this time, he was the only government member from the prairies who supported the national policy. The Manitoba Grain Act of 1900 obliged the railways to provide land and a siding if any ten farmers within forty miles of the shipping point wished to construct a flat warehouse. All members of parliament who represented rural ridings on the prairies, irrespective of party, voted against the Act on the grounds that the proposed legislation did not go far enough. In the federal election that same year, Sifton was one of only two Liberals elected in seven Manitoba seats.<sup>114</sup> Oliver and Douglas, Sifton's opponents on the populist fringe of the Party were elected in the NWT as well as Walter Scott, a Douglas protégé and future Premier of Saskatchewan.

In 1901, following a protest sparked by the inability of the CPR to move all the grain awaiting shipment to the Lakehead before navigation ended for the winter, Sifton recognized that the tide was against him and radically revised his stance on the grain handling and transportation issue. He switched abruptly from the side of business interests to that of the organised farmers. Hall (1985: 33-4) quotes from a letter he wrote in December of that year acknowledging that:

The class feeling among farmers is strong, and you will find I think in the course of time that even if you are successful in proving these (agitators) to be wrong, which is no doubt a comparatively easy matter, the average farmer will stick with him. A controversy with anyone of a class who inclines to stick together is very unprofitable. And in case of such [a] controversy it matters little whether you are right or wrong, the antagonism is created.

The 'agitators' in this instance were the members of Sifton's own party who routinely sided with the agrarian populist movement developing in the West. The fact that several of them were newspaper owners who adopted farmers' grievances as their editorial policy is consistent with the role Schumpeter attributed to the 'scribbling classes.'<sup>115</sup> Sifton's

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<sup>114</sup> Robert Richardson, a former dissident Liberal was elected in the Manitoba riding of Lisgar as an independent. Sifton personally paid the legal fees incurred to prosecute Richardson for election irregularities and he lost his seat in 1901 as a consequence of this case.

<sup>115</sup> Frank Oliver, the Liberal Progressive member for Alberta owned the *Edmonton Bulletin*, and Richardson owned the *Winnipeg Tribune*. To counter this dissident propaganda, Sifton purchased the *Winnipeg Free Press*.

‘conversion’ to the agrarian cause is significant insofar as it marks the start of interference with ‘unfettered’ capitalism, and the breakdown of the ‘protective strata’.

The political problem posed by such entrenched opposition was obvious: make concessions or risk losing support. Shortly after this, the Liberals conversion to the cause of agrarian populism was confirmed when they encouraged the TGGGA case against the CPR over the allocation of railway cars at Sinaluta, NWT (Hall 2011: 302-303).<sup>116</sup>

## **4 Interventions**

### **4.1 Promoting Settlement**

Sifton is generally given credit for the settlement boom which began around the turn of the century.<sup>117</sup> He was very explicit as to his objectives as Minister of the Interior: to make settlers already in the region prosperous and to increase the flow of new arrivals (Dafoe, 1931: 105). Laurier gave Sifton a free hand to stimulate settlement. His efforts were controversial insofar as he cast the net for potential settlers as far afield as central Europe, but he took decisive steps to streamline the Department of the Interior after discovering it was a bureaucracy “...in which business could not be done” (Dafoe, 1931: 133).

Sifton left the cabinet in 1905 because he disagreed with the decision to allow a separate Catholic school system in the two new provinces created that year: Saskatchewan and Alberta.<sup>118</sup> He also disagreed strongly with his successor at the Department of the Interior, Frank Oliver, over the suitability of land in the south of the region and west of the third north-south meridian (which bisects Saskatchewan) for settlement. He did not interfere with the institutional arrangement which sustained the ranching industry. He took the position that the land in that part of the prairies would be ruined for all purposes if the natural grass were ploughed up. If that were to happen, he predicted, “you will have a vast area such as Montana (the U.S. state immediately to the south) has, absolutely fit for nothing” (Dafoe, 1931: 314). He was also concerned that the CPR was taking too long to select the land to which it was entitled under its land grant, and required that they did so. After their

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<sup>116</sup> Other examples of politically motivated impositions on the private sector included pressuring the CPR to add grain transportation and handling capacity (to increase the number of wagons and locomotives, to add more terminal elevator space and to upgrade its mainline between Winnipeg and the Lakehead), that railcars be allocated on a strict first-come-first-served basis according to requests logged in the car-order book at each shipping point, and to provide land and sidings for any farmers’ group that wanted to build a loading platform or flat warehouse (Hall: 2011: 302-303). Fowke (1978: 93; 156-58) maintains concessions were only made to defuse protest and were consistent with the overriding objective of the Liberal government, namely to fill the region with settlers.

<sup>117</sup> It is frequently stated, for example, that Macdonald “built the railway” and Sifton “populated the West”.

<sup>118</sup> The Manitoba precedent was followed in these two new provinces and the federal government retained public lands to allocate in accordance with its settlement initiative.

unsuccessful experiments with Demonstration Farms in the 1880s, they chose not to select any land in the same area. This meant that when Oliver took over responsibility for the Department, all the land in the least suitable part of the region was available for homesteading and pre-emption.<sup>119</sup>

**Table 4 Interventions to Accelerate Settlement**

<ul style="list-style-type: none"> <li>• The Department of the Interior disseminated extravagant promotional propaganda touting ‘the most fertile land on earth’ which has been critiqued as a form of popular fiction (Stich, 1976; Jones, 1987).</li> </ul>
<ul style="list-style-type: none"> <li>• The Department provided financial incentives for immigration agents, steamship lines and colonization companies.</li> </ul>
<ul style="list-style-type: none"> <li>• As Minister of the Interior, Sifton streamlined the operation of the Department and widened recruiting to target farmers from eastern Europe and the United States.</li> </ul>
<ul style="list-style-type: none"> <li>• His successor, Frank Oliver, focussed heavily on attracting immigrants from the U.S. He cancelled grazing leases and made a large bloc of land in the heart of Palliser’s Triangle -- which the CPR had rejected as not being ‘fairly fit for settlement’ -- available for homesteading.</li> </ul>
<ul style="list-style-type: none"> <li>• The Dominion Experimental Farms Service (DEFS) increased the number of Experimental Stations in the region to test agricultural techniques and new varieties of wheat.</li> </ul>

Frank Oliver had been a persistent critic of national policy initiatives in general and the CPR in particular. However, once appointed Minister of the Interior he promoted prairie settlement as never before, refocusing attention on the U.S. and Britain as the likely sources of immigrants.<sup>120</sup>

The focus of the Dominion Experimental Farms Service in the early decades of settlement was directed at extending the area over which wheat could be grown. This goal was consistent with the prairie settlement objective of the national policy. Both quick-maturing wheat and encouraging the use of summerfallow served this purpose in the short run.

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<sup>119</sup> Land had been surveyed into sections a mile square divided into four ‘quarters’. When the railway selected land it was given the alternate sections to sell, leaving intervening sections available for homesteading. Where no land was allocated to the railway, each homestead quarter had an adjacent quarter that could be acquired from the government under the pre-emption option once the homestead patent was obtained. This ‘checkerboard’ settlement arrangement is described in detail by MacGregor (1981: 9-10).

<sup>120</sup> An outspoken critic of the CPR throughout his political career, he was eventually appointed to the Board of Railway Commissioners.



## 4.2 The Railways

Freight rates charged on grain were reduced under the Crow's Nest Pass Agreement of 1887 and further reduced under the Manitoba Agreement early in the twentieth century. For most of the wheat boom the farmers' grievances against the railways were the inability of railways to provide shipping capacity and branch lines fast enough to match the spread of settlement and the rapidly increasing volumes of grain to be moved. Freight rates became a contentious issue again during the post-World War I slump.

The 'Crow Rate' has been interpreted as an attempt by the CPR to increase its income in the short term by selling its land grant more quickly rather than charging higher rates on traffic generated at some future date (Wogin, 1980; Norrie, 1978). This argument assumes that grain farming was profitable, and that lower freight rates would be capitalised into the value of prairie land. The Crow Rate reduced freight rates charged for transporting grain by rail by about nineteen per cent when it was introduced.

When the Crow Rate was made into a statutory rate in 1925 it was welcomed by the farm population who regarded it as partial compensation for the tariff. The tariff increased the cost of farm inputs purchased by prairie farmers and pulled the frontier of profitable wheat growing eastwards; the Crow Rate pushed it in the opposite direction. The Crow Rate is thus an example of a change in the institutional environment justified as counteracting the impact of a prior intervention.

The Laurier government's decision to encourage transcontinental extensions of the Grand Trunk Railway and the Canadian Northern Railway was an extreme manifestation of the ideology of infrastructure. On the prairies these projects led to the duplication of railway mileage in many areas. Neither company was prepared to undertake these projects without substantial public sector guarantees. Their availability discouraged collaboration between the CPR's rivals in the region.<sup>121</sup>

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<sup>121</sup> To assist the GTR to realise its transcontinental ambitions, the Canadian government constructed a line between Winnipeg MB and Moncton, NB, a huge distance from which little or no traffic could be foreseen.

**Table 5 Interventions Affecting Railways**

<ul style="list-style-type: none"> <li>• 1897 - Crowsnest Pass Agreement –The Liberal government gave the CPR land grants and subsidies to build a railway from Alberta to Nelson, BC in exchange for CPR agreement to lower freight rates (the ‘Crow Rate’) along its existing track on eastbound grain and some westbound ‘settler effects’ in perpetuity.</li> </ul>
<ul style="list-style-type: none"> <li>• The federal government allowed the CPR to raise additional capital in exchange for an agreement that the railway would use the funds to increase grain handling capacity available during the post-harvest period. This marks the beginning of railway regulation in the West and was prompted by farmer protests against the ‘grain blockades’ of 1900 and 1901.</li> </ul>
<ul style="list-style-type: none"> <li>• 1901 - The Manitoba government provided the CNoR with bond guarantees in exchange for rate concessions. CPR rates decline in concert. (Manitoba Agreement).</li> </ul>
<ul style="list-style-type: none"> <li>• 1902- The federal Liberal government provides bond guarantees to CNoR to facilitate construction of a line north-west from Winnipeg and into Saskatchewan. Subsequent guarantees encourage CNoR to pursue plans to extend the line to Edmonton, AB and Vancouver, BC.</li> </ul>
<ul style="list-style-type: none"> <li>• 1903 –The federal government created the Board of Railway Commissioners to adjudicate railway disputes. “Railways fought the establishment of the Board because they feared it would bind them hand and foot. Before long they became its enthusiastic supporters.” (Currie, 1967: 693).</li> </ul>
<ul style="list-style-type: none"> <li>• 1903 - The federal Liberal government encouraged the Grand Trunk Railway to become a transcontinental railway and began construction of a line from Ottawa to the Lakehead on the premise that the Grand Trunk Railway would eventually lease it to link their lines in Eastern Canada with the line they were building from the Lakehead to Prince Rupert, BC via Winnipeg, Edmonton and the Yellow Head Pass.</li> </ul>
<ul style="list-style-type: none"> <li>• During the federal campaign in advance of the 1911 ‘free trade’ election, the Conservatives under Robert Borden made a commitment to western constituents to build the Hudson Bay Railway (HBR).</li> </ul>
<ul style="list-style-type: none"> <li>• An experimental shipment of wheat from Vancouver to Europe via the Panama Canal made the higher freight rates charged on westbound rail routes (the ‘Mountain Differential’) an issue for prairie farmers, and for the city of Vancouver which became actively involved in the campaign against ‘discriminatory’ freight rates (Darling, 1980: 55-82).</li> </ul>
<ul style="list-style-type: none"> <li>• 1925 – The ‘Crow’ rate, which had been temporarily suspended during WWI, became a ‘statutory’ rate for all grain transported by rail eastbound between the Rocky Mountains and Lake Superior.</li> </ul>
<ul style="list-style-type: none"> <li>• 1925 – The Board of Railway Commissioners issues Order 36769 making the Crow Rate applicable to grain moving to west coast ports through the Rocky Mountains (Currie, 1976: 100).</li> </ul>
<ul style="list-style-type: none"> <li>• 1925 - The Railway Agreement allowed the two railway companies to by-pass immigration restrictions to recruit cheap labour abroad. Despite protests, the Agreement was renewed in 1928 (Thompson and Seager, 1985: 130).</li> </ul>
<ul style="list-style-type: none"> <li>• 1929 – The federal (Liberal) government completed the extension of the CnoR line from The Pas, MB to Churchill on Hudson’s Bay.</li> </ul>

### 4.3 Grain Grading, Marketing and Handling

Legislation affecting the handling of prairie grain reflects efforts to streamline the process and reduce transaction costs. Grades were initially established on an annual basis, but the

standardized grades introduced in 1906 made it possible for buyers to assess the quality of different lots of wheat from different harvests sight unseen.

Other legislation, particularly the Manitoba Grain Act of 1900, reflected the high degree of distrust among prairie farmers towards the private grain trade, the elevator companies and the railway. Pressure was exerted by farmers' organisations on the federal government as a result of grain blockades which occurred when the CPR was unable to move the entire wheat crop to the Lakehead before the close of navigation for the winter. The resultant legislation interfered with the company's ability to manage its own affairs and absorbed resources that would otherwise have been available to address the grain transportation capacity issue. The government was motivated to quash protests by farm organisations in order to enhance the attractiveness of the region to potential settlers.

**Table 6 Interventions Affecting the Handling and Marketing of Wheat**

<ul style="list-style-type: none"> <li>• 1899 - Act to Amend the General Inspection Act made grading prairie wheat compulsory.</li> </ul>
<ul style="list-style-type: none"> <li>• Dissatisfaction with the content of the 1899 Act pertaining to provision of flat warehouse facilities at railway sidings led to the first Royal Commission on the Shipment and Transportation of Grain.</li> </ul>
<ul style="list-style-type: none"> <li>• 1900 – The Manitoba Grain Act implemented the recommendations of the Royal Commission and required the CPR to provide loading platforms where 10 or more farmers submitted a request. Flat warehouses could be constructed on railway land in exchange for a rental fee.</li> </ul>
<ul style="list-style-type: none"> <li>• 1902 – Amendment of the 1900 Act to placed greater onus on the CPR to provide flat warehouses and loading facilities, and required that railcars be allocated in the order in which requests were recorded in a 'car order book'.</li> </ul>
<ul style="list-style-type: none"> <li>• 1906 Royal Commission on the Grain Trade of Canada investigated allegations of collusion in the private grain trade, lack of adequate standards governing the operation of terminal elevators, and the practices of the Winnipeg Grain Exchange. The Commission's Report (October, 1907) recommended more oversight of terminal operations, praised the Winnipeg grain exchange and recommended against government ownership of terminal elevators</li> </ul>
<ul style="list-style-type: none"> <li>• 1908 – Both the Manitoba Grain Act and the Grain Inspection and Sale Acts were amended, implementing many of the recommendations of the 1906 Royal Commission.</li> </ul>
<ul style="list-style-type: none"> <li>• During the federal campaign in advance of the 1911 'free trade' election, the Conservatives under Robert Borden advocated government ownership of terminal elevators and made promises to western constituents to build the Hudson Bay Railway (HBR).</li> </ul>
<ul style="list-style-type: none"> <li>• Canada Grain Act of 1912 consolidated legislation affecting grain grading and handling and provided for construction of terminal elevators by the federal government. By this stage the standardized grain grades and supervision gave buyers sufficient confidence to buy prairie grain sight unseen, and enabled farmers to use warehouse receipts as collateral.</li> </ul>
<ul style="list-style-type: none"> <li>• 1909 – 1912 Manitoba experimented with a provincial (country) elevator utility. The failure of farmers to patronize government elevators discouraged Saskatchewan and Alberta from following suit.</li> </ul>
<ul style="list-style-type: none"> <li>• Government terminal elevators constructed at Port Arthur and Vancouver, and inland terminals at Moose Jaw and Saskatoon (SK), at Calgary and Edmonton (AB) and at Churchill, MB.</li> </ul>

Construction of inland and port terminal elevators by the federal government flew in the face of recommendations made by a 1906 Royal Commission. Their intermittent use and high cost confirmed the wisdom of the earlier recommendation. They did, however, serve a political purpose, capitalizing on prairie animosity to the private grain trade.

#### 4.4 World War I (WWI)

War is an extreme crisis used to justify broad-ranging interventions that supersede peacetime institutions. War is the antithesis of economics geared towards the well-being of individuals: ‘destructive destruction’ instead of ‘creative destruction’. Under wartime conditions, the state is single-mindedly focused on mobilizing resources without reference to their market value in pursuit of short-term goals. This was very much the case with the institutions imposed on the prairie grain industry during World War I. Interventions affecting prairie wheat producers during the war were coordinated with the United States.

**Table 7 Interventions Justified by World War I**

<ul style="list-style-type: none"> <li>• Winnipeg Grain Exchange was closed and the government centralized grain buying and guaranteed a price for domestic and export sales.</li> </ul>
<ul style="list-style-type: none"> <li>• Barriers to free movement of wheat across the Canada/US. Border were removed.<sup>122</sup> American wheat was shipped to Europe from Canadian ports when ships were available and Canadian wheat insufficient, and Canadian wheat destined for Britain was transformed into flour in U.S. mills to utilize available capacity (Porrirt, 1934; Wilson, 1978: 89-118).</li> </ul>
<ul style="list-style-type: none"> <li>• Purchase of grain from prairie farmers, its transportation and sale to the British wartime purchasing authority was handled by the Board of Grain Supervisors from June 1917 until July 1919.</li> </ul>
<ul style="list-style-type: none"> <li>• 1919 - A Wheat Board was organised based on an Australian precedent specifically to market the 1919 wheat crop.</li> </ul>

## 5 Consequences

### 5.1 Promoting Settlement

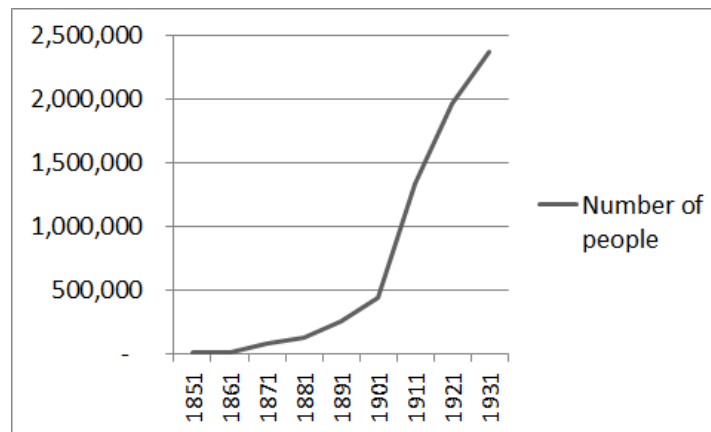
Actions taken during this period led to a surge of immigrants to the prairies. Migrants from the United States and Central and Eastern Europe joined increasing numbers arriving from Britain and northern Europe. The United States, in particular, became a major source of

<sup>122</sup>The Wilson-Underwood tariff of 1913 reduced duties on wheat entering the United States and included a provision for free entry of wheat and flour from countries prepared to reciprocate. Canada did so, and wheat prices rose sharply. The competitive position of U.S. wheat during the war was significantly enhanced by ‘tied-aid’ loans extended by the U.S. to Britain.

prairie settlers during the second phase of the Wheat Boom that took place between the short 1907-8 recession and the pre-war recession of 1913.

According to Bicha (1968), nearly 600,000 Americans crossed the border and established themselves on the prairies during this period.<sup>123</sup> The settlement of this area provided tremendous population expansion. “Within a generation after 1900 ... the population of the Prairie Provinces increased five-fold to a total of 2.4 million people. In 1900, less than one-twelfth of the Canadian population lived in the Prairie Provinces; by 1931, approximately one-quarter lived there” (Britnell and Fowke, 1949: 628).

**Figure 5 Population of the Prairie Provinces 1851 - 1931**



Source: Chart by Author, data from Statistics Canada Series A2-14.  
[http://www.statcan.gc.ca/access\\_acces/archive.action?l=eng&loc=A2\\_14-eng.csv](http://www.statcan.gc.ca/access_acces/archive.action?l=eng&loc=A2_14-eng.csv)

As more homesteaders arrived, they occupied land adjacent to the land already settled. Vigorous promotion of settlement created a demand for additional land. The settlement frontier moved rapidly west and north-west onto portions of the region less suited to wheat growing (and therefore higher production costs) and further from the only port (and therefore farm gate prices reduced by higher transportation costs). The heart of Palliser’s Triangle, which the CPR did not consider ‘fairly fit for settlement’, was rapidly occupied after it was opened for settlement in 1908. Competition among new arrivals led to queues at land offices in Palliser’s Triangle, leading Dales (1966: 150, 153) to comment:

<sup>123</sup> Given that one of the basic premises behind the prairie settlement initiative in the first place was to prevent the region from being settled by Americans, this is rather ironic. Solberg (1987: 88-89) cites estimates of the number of the number of Americans arriving in Canada as high as 785,000 over the period 1897-1912, including 133,000 in 1911-12. Studies on the importance of American settlement on the prairies after 1905 include Troper (1977; 1972) and Bicha (1968; 1965; 1964).

No one, I suggest, really believes that without the homestead policy in particular and the settlement policy in general the West would not have been settled. These policies were powerless to promote settlement before 1900; after 1900 their chief effect was to promote not settlement but rapid settlement, and there is much evidence to suggest that the rapidity of settlement did much short term and long term harm in Western Canada..... And to write as if the wisdom and power of a nation-building program that is ineffective for two or three decades is somehow ‘proved’ or demonstrated’ by a subsequent period of great prosperity is to mislead the public with a monstrous example of the *post hoc ergo propter hoc* fallacy.

The history of settlement suggests that not only did homesteading run ahead of the provision of railway connections, but also that settlement of some of the least productive land in the region was ‘over-subscribed’.

The traditional explanation for the sudden interest in the Canadian prairies after 1896 involves the lack of suitable frontier land for settlement in the United States. However it is now clear that U.S. settlement continued at a very brisk rate during the Canadian wheat boom (e.g. Norrie, 1992: 247-8; Gardner, 2002). The question therefore seems to be why so many migrants, and particularly Americans, made the Canadian prairies their destination when there was land still available in the U.S. west.

Bicha’s (1965) answer is that homesteading in Canada became the preferred option for many Americans<sup>124</sup> with limited capital. The costs of starting a farm in the U.S. rose as wheat growing became more profitable in areas that had been settled longer. Under these circumstances, tenancy became more common. For similar reasons, the sons of Manitoba farmers moved west to homestead. In choosing between the American or Canadian settlement frontiers, Americans were attracted to Canada by the shorter time required to acquire title to the homestead quarter, and by the persuasive advertising of the Canadian authorities and the agents working on a commission basis (1965: 264-266).<sup>125</sup> Higher profits from wheat farming encouraged migrants to leave the U.S., but by the time they had established themselves in Canada, a series of less propitious growing seasons reversed that trend. The big advantage American migrants had over many others who ended up on the western prairies was the relative ease with which they could return to the U.S.. Bicha

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<sup>124</sup> “Americans” in this context refers to their departure point for Canada. Many were recent immigrants to the United States, and a large proportion of those arriving in Canada from the U.S. during this period were originally from Scandinavia.

<sup>125</sup> An attempt (cited in Norrie, 1992: 253-4) by Percy and Woroby to test Bicha’s agricultural ladder hypothesis (from tenancy to ownership via homesteading in Canada) shows that the level of promotional advertising expenditures was found to be significant predictor of migration in 1909 but not in 1899. Using a different approach around the same time, Borins also found advertising by the federal government to be a strong indicator of the settlement trend (Norrie, 1992: 253). Borins’ paper was published in 1982.

estimates that as many as two thirds of the Americans who crossed the border once heading north did so a second time heading south.

Government and railway promotional materials featured pictures of expansive fields of ripe wheat but made no mention of the production or price related risks potential settlers would face. Readers were left with the impression that after a short burst of hard work, “two or three crops of wheat would put a new settler on ‘easy street’” (Imrie, 1936: 4). A government program that brought harvest labour into the region from as far away as Britain contributed to this illusion: only farmers whose crops had survived through to harvest needed labour (e.g. Cherwinski, 1985). Even winter, which is a formidable phenomenon on the prairies, was never mentioned.

Figure 6 Canadian Immigration Posters

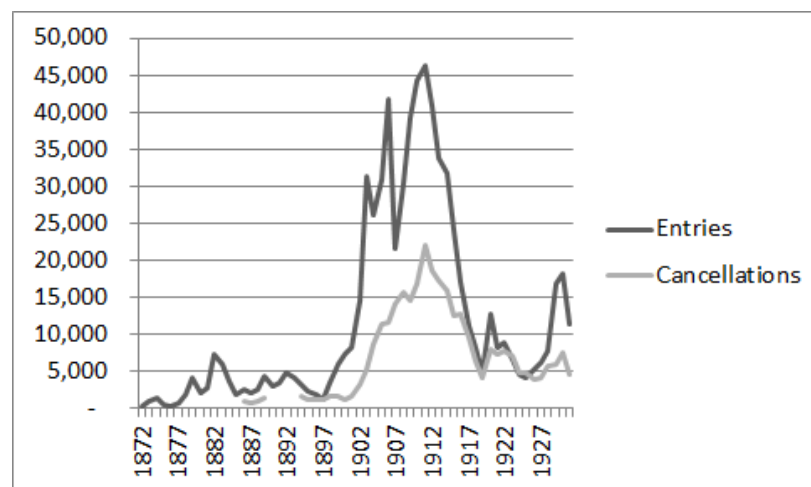




As Fowke (1978: 285) comments, the reality was quite different:

...any substantial discrepancy between homestead entries and patents issued over a period of years would indicate failure in the realisation of normal expectations. The discrepancy for the seventy years of Dominion lands administration is so pronounced as to indicate wastefulness little less than shocking. Careful estimates place the acreage entered for on a homestead basis in western Canada in the period from 1870 to 1927 at 99 million acres and the corresponding patents, to 1930, at approximately 58.2 million. These data indicate a gap of over 40 per cent between expectation and fulfilment in the first critical phase of homesteading in Canada. In terms of human beings, four out of every ten Canadian homesteaders failed to ‘prove up’, to secure title to their claim. The regional record is even worse. In Alberta, from 1905 to 1930, nearly 46 per cent of all homesteaders failed to prove up and, in Saskatchewan, in the period from 1911 to 1931, approximately 57 per cent – nearly six out of every ten – homesteaders abandoned their claims before receiving title.

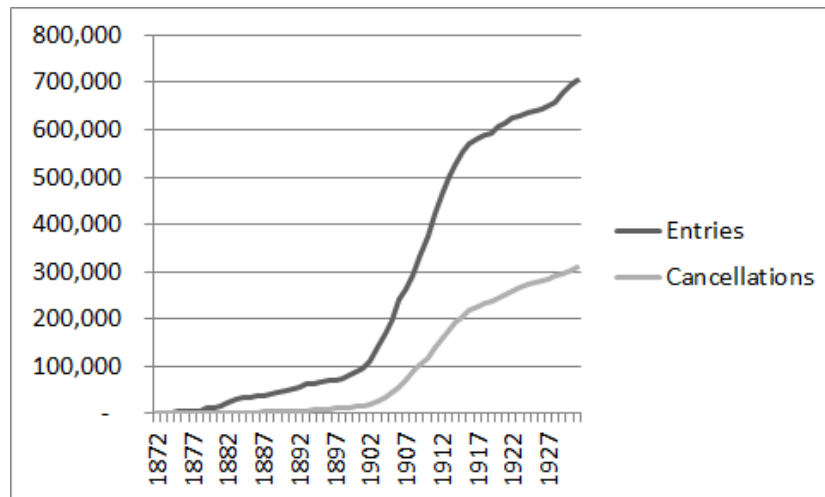
**Figure 7 Annual Homestead Entries and Cancellations, Prairie Provinces**



Source: Chart by Author, data from Statistics Canada Series L34-41  
<http://www.statcan.gc.ca/pub/11-516-x/pdf/5220014-eng.pdf>



Figure 8 Cumulative Homestead Entries and Cancellations, Prairie Provinces



Source: Chart by Author; data from Statistics Canada Series L34-41.  
<http://www.statcan.gc.ca/pub/11-516-x/pdf/5220014-eng.pdf>

The combination of improved profitability, a series of good crops and more vigorous recruiting led to even larger numbers of settlers between the settlement frontier and the profitability frontier. The federal government's enthusiastic settlement promotion after 1896 magnified 'the swarm-like effect', leaving a large numbers of farm units vulnerable to any subsequent decline in prices or 'short' or non-existent crops.

In reality, the market played a minor supporting role in the settlement initiative which was a social experiment conducted on a massive scale. It relied heavily on systematic distortion of information about the region and its prospects as a wheat growing region by the Ministry of the Interior. The CPR may be absolved from some blame because they did not have much land to sell in the driest areas. Their efforts in the south-west of the region were focused on an irrigation scheme they were in the process of developing in southern Alberta.

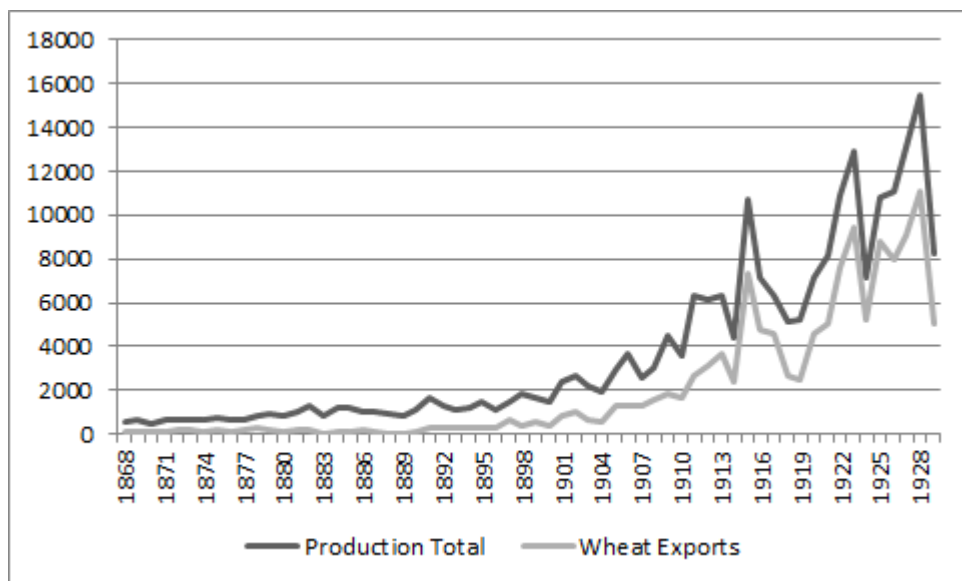
The homestead option distorted the labour market because it was relatively easy to become a proprietor. Since labour was scarce and expensive, prairie farmers sought to economise on labour as quickly as possible through mechanisation and the acquisition of additional land. However, to do so they took on debt (Adelman, 2002: 205-215; 268). Land could be, and usually was, mortgaged as soon as the homestead patent or deed was issued.

Farm creation on a huge scale and the concomitant extension of the transportation and grain handling infrastructure required to service those farms sparked an investment boom which exceed the domestic supply of capital (Offer, 1989: 157). Interest rates were at all-time lows around the turn of the century but crept upwards to attract foreign investment, first from Britain but then increasingly from the U.S.

## 5.2 Land Use

The prairies lie on the economic margin of the world wheat economy. The physical environment is a contributing factor. Wheat yields, particularly in SW Saskatchewan and SE Alberta fluctuate more than those in the wheat producing areas of Argentina or the United States (Lipset, 1950: 27). After a bumper crop throughout much of the region in 1915, dry conditions decimated crops in the centre of Palliser's Triangle. The brunt of the setback was borne by those in SE Alberta, but municipalities in Saskatchewan along the Alberta border were also affected (McManus, 2008, 2004; Jones, 1987; 1986; 1980; Fowke, 1978: 78-9).<sup>126</sup> There was an exodus of people from these recently settled areas and farm numbers plummeted. However, their departure was not acknowledged by the federal government at the time, for fear of discouraging incoming settlers. Schemes to settle World War I veterans in the prairies were indicative of the dogged pursuit of national policy objectives.<sup>127</sup>

Figure 9 Canadian Wheat Production and Exports 1869 – 1929 ('000 metric tons)



Source: Chart by Author, data from Statistics Canada Series M301-309.

[http://www.statcan.gc.ca/access/acces/archive.action?l=eng&loc=M249\\_300a-eng.csv](http://www.statcan.gc.ca/access/acces/archive.action?l=eng&loc=M249_300a-eng.csv)

Efforts by the Dominion Experimental Farms Service to make wheat growing feasible (if not profitable) over the entire region were severely tested during this period. Their blanket endorsement of summerfallow and Marquis wheat was part of a drive towards scientific

<sup>126</sup> For personal reminiscences of this period in Canadian history see especially Kroeger (2007), Eggleston (1992) and Jones (1987; 1986).

<sup>127</sup> Mercifully, relatively small numbers of WWI veterans signed up for the Soldier Settlement Scheme. Land for the scheme was found in Palliser's Triangle, carved out of Aboriginal reservations and a bloc of land vacated by Dukhobor's when a religious schism prompted a mass migration from Kamsack, SK to BC.

agriculture which, for a time, was believed to be able to surmount any natural obstacle. Summerfallow was promoted as a practice that enabled ‘good’ farmers to produce enviable crops anywhere even in very dry years. The experience in the Alberta ‘Dry Belt’ demonstrated its limitations: exposing very dry cultivated soil to the ubiquitous prairie winds led to dust storms (Russell, 2007; Jones, 1987: Chapter 8; Anderson, 1975; Palmer, 1968)

The breeding of Marquis wheat offers a good example of one of the paradoxes of technical change in agriculture: the benefits of such initiatives accrue to consumers. Production costs decline for all producers adopting the new technology, but competition among farmers drives prices down in tandem, just as Schumpeter’s model predicts. By expanding the area over which wheat could be raised without frost damage, the quantity of production rose without any benefit necessarily accruing to the producer.

These observations reinforce the importance of the commercial viability requirement for technical changes. Ability to do something differently is one thing, but if it is not commercially remunerative, there is no economic reason to adopt the new technology. Both summerfallow and Marquis wheat were adopted beyond the commercial margin of agriculture on the prairies during the prairie wheat boom, and helped amplify an expansion of wheat production not justified by commercial considerations.

### **5.3 The Railways**

Both freight rates and the tariff slowed the rate at which the profitability frontier moved west and north-west across the region. As CPR management repeatedly emphasized, the profitability of prairie farming was just as much in their company’s interest as it was in the farmer’s (e.g. Eagle, 1989: 205-208). The CPR’s interest in settling the prairies was also aligned with that of the federal government, except perhaps for the fact that the railway had included the proviso that land it selected as its grant should be ‘fairly fit for settlement’, whereas the government objective was to carpet the entire region with homesteaders.

Under the Crowsnest Pass Agreement, the CPR was committed to hold freight rates constant on lines then in existence. This removed one uncertainty homesteaders faced: the future trajectory of freight rates. Grain growers came to consider the Crow Rate partial compensation for the tariff which increased their costs. Unfortunately, the surge of settlers into Palliser’s Triangle after 1908 would soon demonstrate that many of them were trying to grow wheat beyond the profitability frontier.

In the short run the Crow's Nest Pass Agreement was eclipsed by the Manitoba Agreement, and prevailing freight rates were set below the 'Crow' level until the war. Once the Manitoba Agreement was in effect, access to railways and the level of service supplanted rates charged as grain growers' dominant grievances with the railways.

Perhaps the most significant short term impact of the Crow Rates and the subsequent Manitoba Agreement was to divert most of the prairie wheat traffic from U.S. railways and ports to Thunder Bay. Although freight rates on the prairies were a little lower than those in adjacent areas of the U.S. before 1896, the reduction of Canadian rates under the Crowsnest Pass and Manitoba Agreements widened the disparity (MacDougall, 1966; especially page 50).<sup>128</sup> Thus the alternative route through the U.S. was a less attractive outlet for Canadian grain. This concentrated the flow of grain onto a grain handling and transportation infrastructure that was not growing fast enough to keep pace when late harvests and high yields compounded the effect of a rapid increase in land area seeded to wheat.

Left to its own devices, the CPR would have concentrated its resources in high traffic areas. Then it too would have experimented with extending its network and providing appropriate service in an iterative process. The rapid spread of settlers and competition from government subsidised railways, particularly Canadian Northern, threw the process into reverse: the railways found themselves under pressure to extend their branch line networks as quickly as possible. These branch lines were inevitably poorly served with railcars and locomotives until capital became available to supply them. Hence the westward progression of 'grain blockades', the bottlenecks that occurred when farmers and grain handling companies wanted large crops moved to port between harvest and the close of navigation on the Great Lakes for the winter.

The federal government reacted to the grain blockades by regulating the operational decisions of the CPR. It obliged the railways to provide facilities for wheat growers who wanted to ship grain without relying on elevators. The year before this legislation (The Manitoba Grain Act of 1903) was passed, a similar proposal had been dismissed out of hand by both the Prime Minister and the Leader of the Opposition as 'socialistic' (Hall,

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<sup>128</sup> Canadian settlers were of course convinced that the CPR was charging exorbitant rates compared with U.S. railways. Norrie points out that the 1895 Report of the Railway Rates Commission refers to higher rates in Canada than the U.S. in its introduction, but the material in the body of the report tells the opposite story (Norrie, 1978). MacDougall (1966) provides detailed information regarding the difficulty of comparing rates in jurisdictions where the pattern of wheat production was different. U.S. rates started to decline only in 1908 (MacDougall, 1966: 50).

2011: 300, 303). Clifford Sifton was well aware that using outdated technology to load grain tied up a large number of railcars that could be more efficiently used servicing elevators (Hall, 2011: 297-298), but he was dealing with a political problem rather than a problem of logistics.

Such requirements exacerbated the CPR's already difficult task of maintaining the profitability of its prairie network. As Schumpeter has emphasised, the benefits of more productive technology are only realisable if the less productive technology is eliminated. However, the adoption of the most efficient bulk-handling technology of the day was resisted by those who stood to benefit most from its widespread use.

The Laurier government soon discovered the negative consequences of providing financial support to the two additional transcontinental railways when, facing bankruptcy, both became wards of the federal government. They were eventually amalgamated with the railways the government already owned to form Canadian National Railways (CNR subsequently called CN) which became a significant long-term drain on the nation's fiscal resources. As a government entity, CNR was particularly susceptible to political pressure to expand its branch line network on the prairies, and "hundreds of miles were added in the prairie region" at public expense in the 1920s (Fowke, 1978: 287).

#### **5.4 Grain Grading**

Regulation of grain grading provided Canada with a competitive advantage in the international wheat trade. It is one of the few examples where government intervention in the prairie grain industry provided a public good that reduced transaction costs. Once in place, prairie grain could be purchased sight unseen on the strength of a "Certificate Final" which specified its grade (Solberg, 1987: 140-41).<sup>129</sup>

It is, however, important to emphasise that grain grading was not imposed on prairie agriculture in the same manner as interventions such as the tariff, aggressive promotion of settlement and subsidized railway building. The advantages of a standardised grading system were apparent to all those involved in the handling, marketing and transportation of grain, and the CPR had a vested interest in preventing sub-standard grain entering the

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<sup>129</sup> In the United States samples of grain consignments were made available to prospective buyers and according to White (2011: 144) the small number of classifications established for Canadian grain "... enabled a buyer in Liverpool to know what he was getting when he purchased Manitoba wheat. That gave it an advantage over wheat shipped through Duluth Minnesota – the Northern Pacific's Terminus – which was very variable."

handling and storage system. Farmers also benefited, but could not be expected to give the CPR any credit for its efforts.

### **5.5 Grain Marketing and Handling**

The post-war collapse in wheat prices occurred at the same time as the end of government controlled marketing. This coincidence reinforced producer suspicions regarding the 'open' market and precipitated a spike in militancy within the grain growers' movement. Although the government had viewed the Wheat Board solely as a wartime measure, farmers called for its retention. When the government refused to remain directly involved in the marketing of wheat, three provincial wheat pools were formed as an alternative. The Pools purchased grain from farmers at an 'initial price', borrowing money from the banks to finance the payments. In return, the Pools agreed to provide wheat inventory equal to 115% of the value as collateral for the loan (Wilson, 1978: 266). If the price of wheat dropped, the value of inventory also dropped and the Pools were required to either provide additional collateral or pay down part of the loan. The Pools' aversion to the open market and the private trade led them to dispense with the routine practice of hedging grain after purchase. Any surplus in the pool accounts at the end of the marketing year was paid out as a final payment. During the 1920s these arrangements worked, but the Depression would soon reveal that they were less robust than those the private grain trade used to mitigate risk.

Short term difficulties with transportation and grain handling capacity became the basis for much of the myth that prior to the Depression the prairie grain industry was a *laissez-faire* economy. Expansionist rhetoric encouraged the view that wheat production on the prairies would be profitable. Wheat growers who found themselves *beyond* the commercial margin no longer cursed the national policy but the middle man.

### **5.6 World War I**

Until it ceased to operate during the War, the international wheat trade was an extremely sophisticated example of the market economy at work. Although prairie farmers may not have been happy with the price they received, it did reflect quite accurately the state of supply and demand at the time (Butler, 1940).

For prairie farmers the War years were a tantalising combination of high prices and poor or non-existent crops. The high cost and shortage of shipping affected imports from Argentina and shipments from Australia also suffered. Shipments from Australia were also

curtailed. Britain sought as much wheat as Canada could supply. However, Britain ended free market transactions in wheat in October 1916 and its Food Procurement Agency began purchasing wheat futures to cover its own needs and those of France and Italy as well. It quickly became apparent that the futures market would not function with only one buyer, and the Exchange was closed.

Artificially high prices during WWI extended the wheat boom by 5 years and led prairie farmers to believe that these prices represented the 'fair' value for wheat they deserved. Farmers interpreted the wartime price surge as the beginning of a new chapter in their struggle against 'monopoly capital'.

The impact of war time inflation on the structure of production was particularly hard on the agricultural sector.<sup>130</sup> Interest rates rose, but higher wheat prices and difficulties finding labour made investment in labour saving capital and land appealing. Unfortunately, those investments appeared justified only because wheat prices were distorted by war time circumstances.

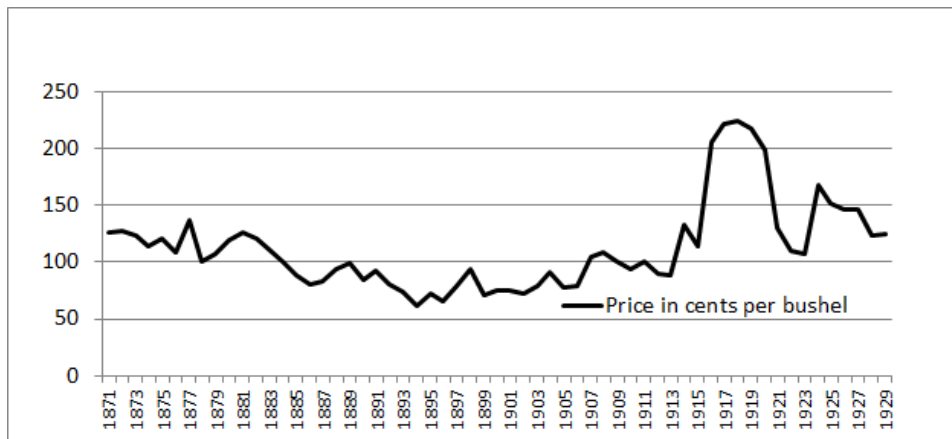
The subsequent deflation and commodity price collapse undermined the basis on which considerable investment in wheat production had been based. Financial institutions joined the railways and the private grain trade in the list of businesses that prospered on the backs of farmers, and enhanced the appeal of the social credit doctrine.<sup>131</sup> When the end of the first Canadian Wheat Board's mandate coincided with a collapse in grain prices this reinforced farmers' beliefs that the 'open market' was to blame.

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<sup>130</sup> Agriculture is at a perennial disadvantage during inflationary periods because investments with a long productive life appear much more attractive than they otherwise would. At the same time, inflated values of farm land encouraged lenders to promote borrowing (Grinder & Hagel, 2005: 149-158).

<sup>131</sup> Social Credit acknowledged the importance of profit in capitalist society in general, but objected to the heavy toll extracted from 'legitimate businesses' by financial intermediaries. This 'flaw' in the market process was discovered by an Englishman, Major Douglas. As an engineer, he believed experts should be recruited by elected governments to 'fix' this problem. Social Credit would go on to become yet another political movement in western Canada.

Figure 10 Canadian Wheat Prices 1867 - 1929



Source: Chart by Author, data from Statistics Canada Series M228-233  
[http://www.statcan.gc.ca/access\\_acces/archive.action?l=eng&loc=M228\\_238-eng.csv](http://www.statcan.gc.ca/access_acces/archive.action?l=eng&loc=M228_238-eng.csv)

Major shifts in the international wheat market after the War favoured prairie wheat growers, so their heightened discontent was misdirected. Prior to 1914, Russian and other east European countries accounted for around forty per cent of western and northern Europe’s wheat imports, with Russia providing a little more than half (Lew & McInnis, 2007: 12-13). These sources of supply dried up during the War and Russia did not re-emerge as an exporter during the 1920s. Canada replaced Russia as the largest single wheat exporter. However, the United States had increased its wartime production significantly: its share of global trade rose to 27 per cent in the first post-war half decade from 14 per cent in the comparable pre-war period. It declined over the decade as land was shifted back into other crops, but Australia and Argentina also increased their share. This meant that there was no sustained improvement in wheat prices (Olson, 1974).

Table 8 Big Four Exporters Share of World Wheat Trade (%) 5 Year Annual Averages 1909–37

	1909-10 to 1913-14	1922-23 to 1926-26	1927-28 to 1931-32	1932-33 to 1936-37
<b>United States</b>	16.0	23.2	17.7	9.0
<b>Canada</b>	13.9	36.9	34.6	37.4
<b>Argentina</b>	12.3	17.5	20.4	24.1
<b>Australia</b>	8.0	11.3	13.7	19.1
<b>Total</b>	50.3	88.9	86.4	81.5

Source: Paul de Hevesy (1940: Appendix 10 p. 99)



The disruption of agricultural production in Europe by the War also meant that it took time for domestic production in importing nations to recover to pre-war levels. As the recovery was underway, the fresh experience of the War became justification for increased protection for the agricultural sectors of several European nations (Federico & Persson, 2007: Figure 4.8, 101).

### **5.7 Political Consequences**

The federal election of 1911 was again fought on the question of freer trade with the United States. The prospect of lower tariffs and the efforts of the Liberals to cultivate the prairie farm constituency were rewarded, with Alberta and Saskatchewan both voting Liberal. However, most of the rest of the country rejected this option (although the margin of the popular vote was again very small) as they had in 1891 and the Conservatives returned to power.

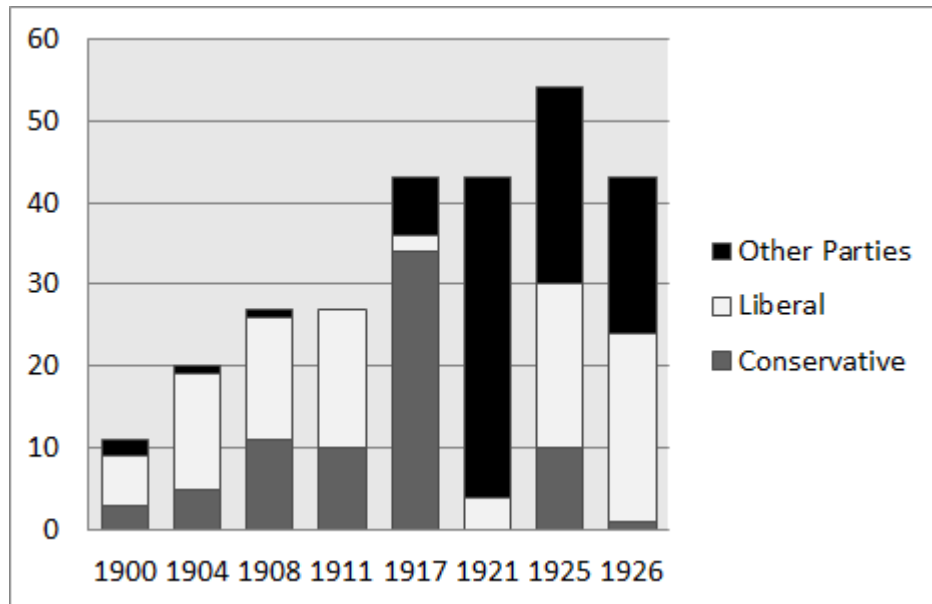
Precedents involving federal government intervention on the farmers' behalf during the period created rising expectations that government could and should intervene in the farmers' struggle against 'monopoly capital'. The net result of the national policy was to increase both the number of discontented farmers and the strength of their negative feelings. It led to the rise of divisive regional politics in Canada, with the West often voting against the majority in the rest of the country. Regional discontent led to the formation of new political parties with a socialist orientation both at the provincial and federal levels and influenced the political platform of the mainstream political parties.

At the federal level, Canada generally favoured a two party system. In contrast, the Prairies became the home of third party opposition groups who were able to use their influence during minority governments to further their regional agenda. Disappointment with the return of the grain trade to the private market combined with a simultaneous drop in wheat prices to pre-War levels were major factors contributing to the election of fifty-eight Progressive Candidates in the 1921 federal election. Members from the prairies formed the core of this bloc. The 1925 legislation which made the Crow Rate 'statutory' was introduced by a minority Liberal government in exchange for Progressive Party support for its budget from which it drew much of its support from the prairies.

At the provincial level, this period of heightened agrarian protest and disenchantment with the two mainstream political parties in provincial politics led to the election of a United

Farmers' government in Alberta in 1921 and a Progressive Party government in Manitoba in 1922.

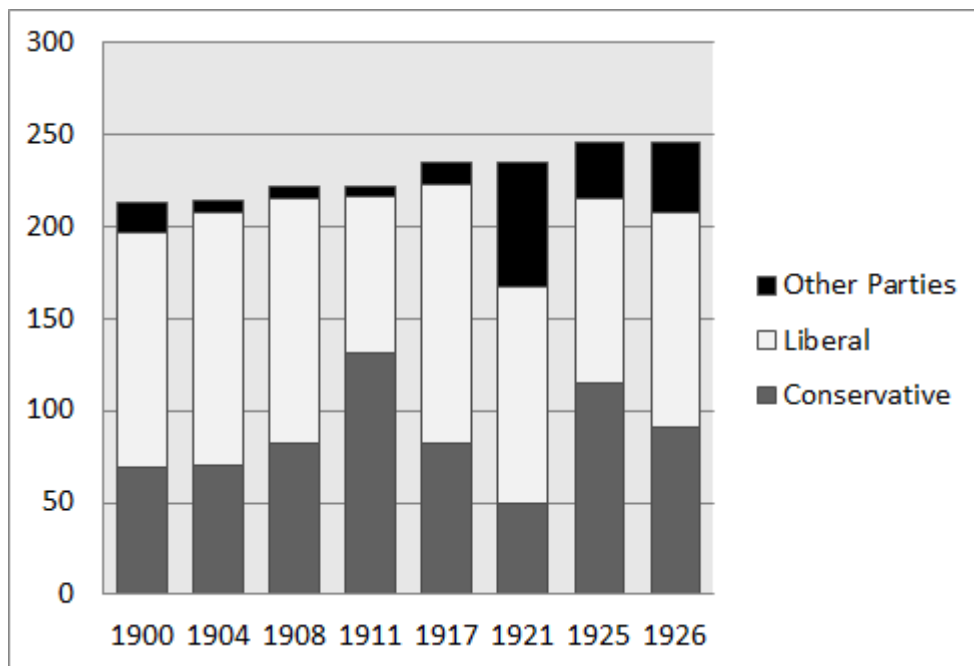
Figure 11 Federal Election Results - Prairie Provinces 1900 to 1930 (no. of seats)



Source: Chart by Author, data from Parliament of Canada

<http://www.lop.parl.gc.ca/ParlInfo/compilations/electionsandridings/ResultsParty.aspx>

Figure 12 Federal Election Results – Canada 1900 to 1930 (no of seats)



Source: Chart by Author, data from Parliament of Canada

<http://www.lop.parl.gc.ca/ParlInfo/compilations/electionsandridings/ResultsParty.aspx>

## **6 Counterfactual**

The transition between the Conservative federal governments prior to 1896 and Liberal governments from 1896 and 1911 might well have been a discontinuity in prairie agricultural policy (had the party listened to its Western constituents) but instead it exhibited path dependency: the national policy objective of rapid settlement of the prairies was pursued even more vigorously after 1896, and much more effectively. Settlers moved into the region in significant numbers and wheat exports rose dramatically. The ‘wheat boom’ was underway.

It is extremely difficult for public sector decision makers to invoke the sunk-costs argument and abandon projects upon which large sums have been spent. The counterfactual for the ‘wheat boom’ period however considers that possibility and poses the question, ‘How would the situation have been different if further federal government intervention in prairie agriculture had ceased in 1896?’

The short answer seems to be ‘the pattern of prairie settlement would have been very different’. Three interventions by the federal government accelerated settlement: the promotion initiatives of the Department of the Interior; railway policy, and the opening up of the heart of Palliser’s Triangle to homesteaders. The net effect was to exaggerate the agricultural potential of the region and induce a speculative land rush. Settlement was checked briefly by a short recession in 1907 and then again in 1914 by the pre-war economic slowdown and World War I itself.

The answer illustrates the extent to which more vigorous pursuit of federal government policies after the election of the Liberal government in 1896 amplified the ‘wheat boom’ or, to use Schumpeter’s terminology, the extent to which government-initiated modification of the prevailing institutional environment exaggerated the ‘swarm-like effect’ which occurs on the upside of a business cycle. The federal government had fallen into the trap of inhibiting development by promoting growth.

Had official efforts to promote prairie settlement ceased in 1896, the westward advance of the prairie settlement frontier would have been quickly constrained by the profitability of wheat growing. Profitability did increase in the closing years of nineteenth century, and settlers already established in Manitoba were the primary beneficiaries. Absent any additional promotion of settlement by the government, some competition for rents on the settlement frontier would be expected once profitability improved. It was the improvement

in the profitability of wheat production *combined with* successful efforts to promote settlement which exaggerated the settlement response. Efforts by the Ministry of the Interior under Sifton and Oliver were unnecessary. Evidence that these promotional efforts made a significant difference to the number of settlers arriving in the region is found in the work of Bicha (1968, 1965, 1964), Borins (1982), and Marr and Percy (1978).

Absent federal government support for construction of CNoR and Grand Trunk Pacific lines the CPR would have been able to determine the pace of settlement in Saskatchewan and Alberta. There would have been no reason to build branch lines in the dry-belt west of the 3<sup>rd</sup> meridian (which runs north south through the middle of Saskatchewan) because it had chosen to select land its land elsewhere. Without the Crow Rate Agreement and the Manitoba Agreement, freight rates would have been more onerous as settlers moved west. Most importantly, it was the federal government that provided CNoR with the bond guarantee which enabled it to extend its lines into Saskatchewan and Alberta. It is doubtful whether it would have done so in the absence of this help, so the CPR would have been able to develop lines in those provinces after it had invested in the equipment necessary to provide the service required on its Manitoba lines as grain production increased. Concentration of grain production, the provision of adequate infrastructure to handle the occasional unusually large crop in Manitoba would have created the basis for a more diversified and resilient agricultural sector in the region at much lower cost.

The other factor which supports the counterfactual is the alacrity with which the Liberal government lowered the cost of using the political system to alter the structure of business relationships during this period. The CPR had been established by the Conservative party and had a mandate to operate 'as a business' once it was complete. But the Liberals were keen to exploit animosity to the CPR within the prairie farm constituency. It had no scruples about taking the farmers' side in any and all disputes over provision of railway sidings, loading platforms and flat warehouses. In doing so, it became an ally in the farmers' struggle against monopoly capital. Ironically, without this unwelcome intrusion into its efforts to operate as a business, the CPR would have been better placed to provide Manitoba farmers with the level of service they required, instead of dissipating its capital in competitive branch line construction and obsolete grain handling technology.

The coincidence of growth in the Canadian economy between 1896 and WWI with the realisation of the longstanding prairie settlement aspirations of the Expansionist movement encouraged Canadian economic historians to credit prairie settlement as the cause of the

growth spurt. However, McInnis (2010) points out that the rate of prairie settlement accelerated most noticeably only after 1905, whereas new data on Canadian GDP shows that the growth spurt in the Canada's economic performance occurred earlier, between 1897 and 1907. He attributes the strong performance of the Canadian economy around the turn of the century to the impact of the second industrial revolution on manufacturing, the creation of a domestic steel industry, and a non-ferrous metals boom. Agriculture, as a major component of the economy at the time, also made a contribution, but the doubling of cheese exports from Ontario between 1896 and 1906 was more important than the increase in wheat exports from Manitoba.

Settlement of prairie land increasingly inappropriate for wheat production got underway in earnest after a short, sharp recession in 1907-8. Growth rates in per capita GDP from 1907 to 1913 averaged 2.27 per cent per annum whereas they had been 4.41 per cent between 1897 and 1907. Rapid westward expansion of prairie settlement was a period in which national rates of per capita GDP growth returned to their longer term trend after the 1897-1907 surge. This suggests that once what McInnis calls the real 'wheat boom' (from 1907-1913) got underway, rates of per capita increase in GDP started to wane. This is consistent with the argument of Chambers and Gordon (1966) that it was not the wheat boom that gave the Canadian economy its long anticipated growth spurt.<sup>132</sup> GDP growth during this part of the period was slowed by very rapid population growth and declining productivity in prairie agriculture as the settlement frontier moved west. As Dales pointed out, the country does not become richer in any meaningful sense if its population is getting poorer (1966:48).

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<sup>132</sup> Olson (1974: 343-47) examines the same problem from the perspective of the decline in British demand for wheat over the same period, lending credence to the Chambers and Gordon assessment.

## Chapter 5

### Collapse and Remediation: 1930 – 1969

The Great Depression of the 1930s was a global phenomenon and Canada was probably the worst hit nation. The prairies were affected both by the disruption of the international wheat market and by very poor crops. The scale and severity of suffering made it impossible for the federal government to avoid involvement. Government intervention in prairie agriculture had been relatively restrained before this period but became pervasive by the end of World War II. By that time, it included control over both rail transportation and grain marketing. Over the period 1929 to 1943 there was a major shift in two distinct but related attitudes to intervention. The first was general acceptance of the notion that intervention might be beneficial. This view arose more from the perception that the “*laissez-faire*” approach had failed (the view held by prairie grain growers) than any concrete evidence that intervention would generate superior results. The second change concerned ways in which those interventions might be financed.

The series of actions taken by the government to deal with the Depression set in motion an ‘intervention treadmill’ which further weakened the institutional framework Schumpeter considered necessary for markets to operate effectively. The Depression and World War II (WWII) had a huge influence on the institutional environment under which prairie agriculture operated. These institutional changes are outlined before attention turns to the effect these changes had on the farm population, land use, railways and grain handling. The counterfactual considers alternative policy options that might plausibly have been adopted at two distinct junctures: after the Depression began, and after World War II.

#### 1 The Crisis

A severe crisis occurred in the 1930s when there was a sharp drop in international prices for wheat and a contraction in demand. The wheat boom was over. There was also an exogenous shock in the form of a series poor harvests and dust-bowl conditions in Western North America. Through vigorous promotion, the government had encouraged a large number of settlers to homestead in areas of the prairies at or beyond the commercial margin. This made them particularly vulnerable to fluctuating conditions. A large number of farms had already been abandoned during a series of dry years that overlapped with the artificially high price of wheat during WWI. When both prices *and* production dropped for an extended period of time during the Depression, many more were left destitute and

abandoned their homesteads. The plight of prairie farmers during the Depression did not go undocumented.<sup>133</sup>

The Depression crisis of the 1930s was not a ‘normal’ recession from which capitalism would emerge reinvigorated. The federal government had actively promoted the *growth* of prairie agriculture “for the general benefit of Canada”. On the prairies this was widely interpreted as providing benefits for the manufacturing sector ‘down east’ and those involved in the grain trade. The Depression brought those who generated those benefits to their knees: thousands of farmers faced the prospect of losing their farms to foreclosure. This part of prairie history provides a compelling validation of the emphasis Schumpeter placed on short-run considerations as a factor mobilizing the democratically active majority to push for public policies that interfere with institutions essential for the smooth operation of capitalism.

Wheat sales were negatively affected by the downturn in the world economy and the policy responses of other nations. The top grade of prairie wheat sold for \$1.23 per bushel in 1925 but for only \$0.49 in 1930 and \$0.35 in 1932 (Marchildon & Anderson, 2008: 71, 77). At the beginning of this period, Canada once again found itself caught between policies of Britain and the U.S.. In 1931 Britain abandoned the gold standard but the U.S. kept it. Canada tried to steer a middle course by restricting gold outflows, but clung to the gold standard because heavy borrowings in the U.S. precluded any significant devaluation.<sup>134</sup> Canada was extremely vulnerable to any contraction of international trade. Eighty per cent of the output of Canadian farms, mines and forests was exported in 1928. Wheat exports accounted for a third of export earnings.

As Robbins pointed out, (1934: 65-66) “[w]hen a depression occurs – that is, a general contraction of trade – there is to be witnessed the odd spectacle of the nations of the world zealously endeavouring to bring about a further contraction by excluding each other’s products”. Well over a third of all Canada’s exports were destined for the United States, and exports to the U.S. were cut in half by the Smoot-Hawley Tariffs of 1930.

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<sup>133</sup> The plight of those adversely affected by economic setbacks and natural disasters in the days before social media were often ignored (Stackhouse, 2002). The scale and location of the effects of the Depression on the North American frontier is well documented. For Canadian examples see Grayson and Bliss (1971), a collection of some of the letters written (mostly by prairie farm women) to R. B. Bennett who had the great misfortune to become Prime Minister for the first time in 1930. Other examples include Bartley, 1979; Berton, 1990; Broadfoot, 1997; Broadfoot; 1988: Chapter 4, 68-94; and Douglas 1980.

<sup>134</sup> Canada did not have a Central Bank when the Depression began. It was created in 1935.

## **2 Ideas and Ideologies**

### **2.1 International**

The Depression was a time of very high unemployment in western democracies, so an alternative which offered full employment was tantalizing. Although little was known about the Soviet Union during this period, its apparent ability to provide jobs for everyone suggested that its novel institutional framework had merit. The response to the Depression in many jurisdictions can be seen as an attempt to cobble together a less drastic alternative.

Devising a system to address the ‘wheat problem’ and managing commodity trade for the benefit of all were high profile components of a broad programme to revamp and revive western economic institutions at the time. In the early decades of the last century heads of government and senior bureaucrats gathered to discuss the ‘Wheat Problem’ probably even more frequently than they gather to discuss global warming today.<sup>135</sup> Canada took a prominent role in these discussions because, as the largest single exporter of wheat at the time, it had much to gain or lose.

Wilson (1978: 346-8) claims that the Monetary and Economic Conference held in London in 1933 demonstrated a ‘break-through in economic thinking’ as the British and French delegations acknowledged the importance of raising prices for primary products, including wheat. However, use of the term ‘economic’ seems suspect as such conferences provided a forum where economic considerations were replaced by the political realities in importing countries. Importers in the early 1930s were of two minds in this regard: in Britain there was strong sentiment against taxation of food; on the continent there was support for higher prices for domestic producers provided national (and later, regional) self-sufficiency increased. Neither supported higher prices for distant exporters who had added production capacity since the repeal of the Corn Laws. These conferences are of interest chiefly because the early steps towards a pan-European organisation can be detected. As buyers in a buyer’s market, cooperation on the part of European importing nations was more effective than cooperation among exporters.

Malenbaum (1953: 17) points out the great irony of the Depression for the international grain trade: “[in]creases in bread prices were generally attributed to increased wheat prices – increases due principally to government action made necessary by over-abundance of wheat in the world.”

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<sup>135</sup> A publication of the Food Research Institute of Stanford University reviews sixteen such conferences held in 1930 and the first five months of 1931 (Taylor, 1932).



## **2.2 Influence of Agrarian Populism**

As the impact of the Depression spread, so did the ideology of prairie agrarian populism. It ultimately changed the trajectory of public policy in Canada in general and influenced the creation of social safety net programmes, such as unemployment insurance. T. C. Douglas, the leader of the Saskatchewan's first socialist government, is considered the father of the national health insurance programme.

The Depression increased interest in two of agrarian populism's more radical ideas that had been debated since the end of the First World War. The first was a broad critique of the economic system which linked prairie farmers to their markets. It blamed the farmers' lack of purchasing power on the profits drained out of the system by monopoly capital. The second was social credit. Each led to the emergence of a new political party: the Cooperative Commonwealth Federation (CCF) and Social Credit. The social gospel played an important role in the formative years of both parties.

For the majority of this period, the underlying philosophy of the farm movement was that of agricultural exceptionalism (Davis, 1935). This school of thought maintains that agriculture is inherently disadvantaged in the market process because large numbers of farmers are dealing with a small number of suppliers, service providers and buyers. This situation provides a rationale for countervailing government intervention to readjust the balance in the farmers' favour. In the immediate post-war period, agricultural exceptionalism was jointly articulated by a National Farmer's Union and the prairie 'Pools'.

## **2.3 Academic Influence**

The agrarian populist movement remained focused on the *perennial* disadvantages of farmers in a capitalist system. This common enemy led prairie agrarian parties to seek alliances with those championing the cause of urban workers, particularly those in Winnipeg. In contrast, progressive academics were preoccupied with the *periodic* failings of the existing system -- in other words with the business cycle. Ideas that emerged from the academic debate were subsequently adopted to justify continuation of Depression-era state intervention.

Keynes, already a well-known economist, published an article in the U.S. magazine *Atlantic Monthly* in 1932 dismissing the idea that markets could self-adjust quickly to new circumstances and advocating an increase in public sector 'investment' to stimulate

consumption, regardless of deficits. Otherwise, he concluded, the world would have to rely on wars to end recessions (Keynes, 1932: 521-26). Keynes' advice was particularly attractive because it suggested a novel approach to a severe crisis. It also provided a rationale for action already taken. The close links between Keynes and the British establishment and his reputation undoubtedly gave his prescription an edge over alternatives such as the Social Credit doctrine.

### **3 Interests and Incentives**

#### **3.1. Prairie Farmers**

On the prairies, the process anticipated by Schumpeter whereby capitalism would lose its vigour took place in two stages. In both phases farmers sought government intervention in marketing and transporting grain to counteract what were, from their perspective, the 'dysfunctional consequences' of markets.<sup>136</sup> In the first phase, prior to 1929, they sought government regulation of the CPR, support for construction of additional railways, and help creating cooperatives to supply the inputs farmers needed and as an alternative channel for marketing agricultural products. In the second phase, they campaigned against the open market in general, and the private grain trade in particular.

The onset of the Depression continued the radicalisation of the prairie farmers' movement that began with the debate over the '100 per cent pool'. An extremist faction, the Saskatchewan Farmers' Education League (SFEL), had expanded its influence over the Farmers Union of Canada (Saskatchewan Section; FUC (SS)) by 1929, but the organisation still shied away from direct political action (Spafford, 1968). In Saskatchewan, only two farmers' candidates were elected in the 1930 federal election. The precipitous decline in wheat prices and fears that the Pool's Central Selling Agency might collapse threw the farm movement into disarray. After the election, the more militant members of the farmer's movement formed an independent organisation, the Farmers' Unity League of Canada. This organisation sent fraternal greetings to the Congress of Soviets and established links with the Communist Party of Canada, based in Toronto.

At the 1931 convention of the FUC (SS), the executive advocated a use-lease system for Crown-owned land in Saskatchewan. This resolution was amended from the floor to apply to all farm land. Emboldened by this radical sentiment, the leadership endorsed direct political action. It joined forces with the Independent Labour Party the following year, and

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<sup>136</sup> Schumpeter included farmers in his 'new middle class' and considered agriculture no different from any other form of business.

the combined entity participated in the inaugural meeting of the CCF in Calgary in 1932 (Cleverly, 1998: 118-121; Spafford: 1968: 56).<sup>137</sup>

In the post-war period, the recovery of the international grain trade and several decades of general prosperity took the edge off prairie farmers' discontent. Wheat stocks carried over from one crop year to the next did sometimes reach alarming levels and prompted demands for assistance. Well-publicised food shortages in many parts of the world helped justify optimism that surpluses were a temporary phenomenon. Sales to the People's Republic of China (PRC) in 1961 and subsequent sales to the USSR were encouraged with credit concessions but provided welcome outlets for prairie wheat.<sup>138</sup> The majority of prairie farmers were incensed when the 1969 Report of the Federal Task Force on Agriculture suggested that the solution to farmers' problems lay in fewer farmers (Canada: Department of Agriculture: 1969).

### **3.2 The Unemployed**

Unemployment was rampant on the prairies due to the collapse of the wheat economy and the abrupt halt of railway construction. Railway labourers, many of whom had entered the country in large numbers under the Railway Agreement, formed a large contingent of the unemployed. Large numbers of single unemployed men were provided with minimal 'relief' provided they entered one of the many purpose built camps run by the military. These camps became breeding grounds for unrest and radicalism. Communist sympathisers organised protests against 'the system' in major cities, including a 'hunger march' in Edmonton in December 1932. An "On to Ottawa March" by unemployed men, which originated in British Columbia, ended violently in Regina.<sup>139</sup>

### **3.3 Political Parties**

The devastating experience of the 1930s was the catalyst for the transformation of the social, economic and political institutions of the region. Cooperatives, which had been

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<sup>137</sup> The term 'cooperative commonwealth' originated in a book by Laurence Gronlund titled *The Coöperative Commonwealth: An Exposition of Modern Socialism* (1844). It was the term applied to the socialist utopia described in Edward Bellamy's *Looking Backward*, which was one of the books serialised in the Grain Growers' Guide. Eric Fromm described *Looking Backward* in his introduction to a 1960 edition as "one of the most remarkable books ever published in America" and "one of the few books ever published that created almost immediately on its appearance a political mass movement".

<sup>138</sup> Canadian sales during the Cold War to 'Communist' countries occurred at a time when the United States did not have diplomatic relations with the PRC and less than friendly relations with the Soviet Union. At the time Canada was critical of the U.S PL480 (Food for Peace) legislation which made discounted surplus commodities a diplomatic tool (Wilson, 1990: 233-237).

<sup>139</sup> The Regina riot took place in July 1935 while the Wheat Board legislation was being debated in Parliament (Wilson, 1978: 472).

created as an alternative to monopoly capitalism, became springboards for the popularisation of a radical ideology in which social justice and equity were given precedence over economic efficiency. These attitudes were articulated through new political parties at both the provincial and national levels.<sup>140</sup> Both the mainstream parties at the federal levels responded to the new parties by selectively adopting their social safety net programmes. In the post-war period, responsibility for social programmes was passed up from local to provincial and then to the federal level due to lack of funds.

Social Credit was based on a narrow critique of capitalism insofar as it singled out the financial sector as the villain.<sup>141</sup> According to its U.K. originator, Major Douglas, farmers and small businesses were not victims of the capitalist system as a whole, but of their dependence on credit. Social Credit acknowledged the role of profit in capitalist society in general, but objected to the heavy toll extracted from ‘legitimate’ businesses by the financial sector. For Douglas, an engineer, political economy was a technical problem: when it was broken, competent experts were needed to effect repairs. Reliance on ‘experts’ had forceful appeal at a time when decisions taken by ordinary people appeared to have delivered them into dire circumstances.

The Social Credit League won eighty-five per cent of the seats in the Alberta provincial election of 1935. Adoption of Social Credit as a political cause by William “Bible Bill” Aberhart, the head of the Calgary Prophetic Bible Institute, capitalised on the evangelical Christian tradition in the province that stretched back to the arrival of the Mormons. Despite infighting and scandal, Social Credit in Alberta survived Aberhart’s death in 1943. Ernest Manning, a colleague of Aberhart’s at his Bible Institute, succeeded him as party leader and Premier. Under Manning, the ‘Socreds’ downplayed the economic and social doctrines of Social Credit and switched to emphasizing the anti-socialist stance of the movement’s founder. It remained the governing party in Alberta until 1971.

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<sup>140</sup> Social Credit dominated provincial politics in Alberta after its election sweep in 1935; the CCF became the governing party in Saskatchewan in 1944 and the Progressive Party maintained its hold on Manitoba coalition governments under the leadership of John Bracken until 1942. During the remainder of the 1940s and 1950s, the Progressives formed the core of the Liberal Party of Manitoba. The CCF (later the New Democratic Party) and Social Credit both became federal parties. The decline of the federal Social Credit party began with the election sweep of the Diefenbaker Conservatives in 1958. Thereafter the Conservatives became the dominant right-of-center party west of Ontario.

<sup>141</sup> A tendency to associate Preston Manning, the founder of the Reform Party with the Social Credit League which his father led for many years in Alberta gave rise to the perception that Social Credit was always a ‘right wing’ party. Finkel (1992) corrects this misconception. Early Alberta ‘Socreds’ such as William Irvine and Robert Gardiner were elected in federal constituencies as Labour and CCF candidates, respectively.

The other radical political organisation that emerged as a result of the Depression was the Cooperative Commonwealth Federation (CCF). It was founded in 1932 by J.S. Woodworth, a former Methodist minister. Initially it considered itself a non-political organisation with strong links to the United Farmers Parties in Alberta and Ontario and the Progressive Party of Manitoba. In 1933, the organisation launched itself as a national political party, seeking to build on the position held by the three remaining Progressives in the federal parliament, and published *The Regina Manifesto*. The *Manifesto* was ardently anti-capitalist, reflecting the urban socialism of British immigrants with experience in the Labour party and the social gospel. It called for a planned economy in which the federal government would be responsible for full employment, socialised health services available to all, insurance against crop failure, illness, accident, old age or unemployment, and nationalisation of the financial sector and natural resources. It remained the vision statement of the party until 1956 when, it was replaced by the more moderate *Winnipeg Declaration* which favoured ‘Keynesian’ macroeconomic management over socialist remedies.<sup>142</sup>

The CCF at first relied on religious support but later its base was largely secular and increasingly urban-based. It had strong ties with the Students Christian Movement of Canada (SMCC), an ecumenical social justice movement founded in 1921, which was instrumental in the transfer of social gospel principles to a new generation of Canadians with post-secondary education.<sup>143</sup> It also drew support from The League for Social Reconstruction (LSR), a radical secular movement of socialist intellectuals which originated at the University of Toronto and McGill University (Montreal) (Horn, 1980). By the beginning of the 1930s, the universities were taking on the intellectual leadership of the social action movement.

The Saskatchewan branch of the CCF also toned down its anti-capitalist rhetoric and T. C. Douglas, a Baptist minister from Weyburn, SK who had been a federal CCF member of parliament, became the provincial party leader. He won the 1944 provincial election, forming the first socialist government in North America.<sup>144</sup> The party remained in power in Saskatchewan until 1964, but in 1961 Douglas assumed the leadership of the federal party

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<sup>142</sup> In the post-Depression period, ‘Keynesian’ became an elastic term applied to many policies of which Keynes would have been unlikely to approve. Various CCF and NDP governments in Saskatchewan used provincially owned Crown Corporations to manage natural resources, including coal, uranium, oil and gas, and potash.

<sup>143</sup> J. S. Woodworth was a frequent speaker at SCMC gatherings and exerted considerable influence on many who subsequently became prominent Canadians.

<sup>144</sup> A series of Canadian Broadcasting Corporation (CBC) programmes which aired in 2004 set out to identify the greatest Canadian. T. C. Douglas emerged as the winner.

and it was simultaneously renamed the New Democratic Party.<sup>145</sup> The CCF held power again in Saskatchewan from 1971 to 1982 under the leadership of Allan Blakeney.

### 3.4 Academics and the Civil Service

Well-intentioned academics, who had been drafted into the expanding Canadian civil service to address the Depression crisis, seized on the ideas advanced by Keynes as a basis for restructuring an institutional framework which had been tested and apparently found wanting:

The new administrators did not, in the main, get their ideas from their political supervisors: they got them from the prophets of the new age, the two Englishmen, Lord Keynes and Sir William Beveridge, and the American, James Burnham, the author of *The Managerial Revolution*. Keynes had given them the concept of the regulated economy, Beveridge the vision of social security, Burnham the idea of the managerial elite – themselves of course – whose commanding position would be based, not on economic ownership or political power, but on the special knowledge and skill which were essential to government in a time of rapid, technological and social change” (Creighton, 1976: 175).

Canadian economists who moved to influential positions in the civil service included W. A. Mackintosh and W. Clifford Clark from Queen’s University. Mackintosh, who had worked a great deal on the economic history of agriculture on the prairies, was particularly important (Mackintosh, 1934). He linked the instability of demand for staples to Keynes’ aggregate demand theory, and concluded that the solution to the prairie wheat problem lay in effective measures to stabilise demand (Richards, 1985: 49). Mackintosh adopted Keynes’ prescription of government intervention to smooth out the business cycle, and applied it to the problems of the wheat market. The prominent but futile role Canada adopted advocating international wheat agreements was one of the consequences (Wilson, 1978: Part IV p. 79 ff).

When it became apparent that the Depression was deeper and longer than any previously known downturn, the Liberal government of Mackenzie King convened a Royal Commission on Dominion-Provincial Relations (the Rowell-Sirois Commission). Mackintosh played a major role in the work of the Commission, contributing an extensive analysis published as an Appendix with the title *The Economic Background of Dominion-Provincial Relations*. This should have been a post-mortem on the prairie wheat boom.

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<sup>145</sup> The NDP became the Official Opposition in the 2011 federal election, when a revamped Conservative party with strong links to Alberta won a majority government.

However, Mackintosh's application of Keynes' insight to the staple economy deflected blame from Canada's domestic policies to the instability of aggregate demand. Bradford (1999: 31, 49) points out that the 'technocratic Keynesian' solution offered by the Rowell-Sirois Commission, was the recommendation Cabinets and bureaucrats wanted to hear.

#### **4 Interventions**

The Depression forced the federal government to deal simultaneously with three related sectors of the economy that were 'too big to fail'. The first was the prairie wheat economy itself, which was the result of efforts to implement the national policy. The second was the Central Selling Agency of the Wheat Pools which found itself in serious financial difficulties when wheat prices started to fall in 1929; the third was the railway sector, which included the government-owned Canadian National.<sup>146</sup>

Canada's response to the Depression can be divided in two phases. The first period lasted until 1935 under the Conservative Prime Minister R.B. Bennett and tried to address the crisis while adhering to the principle that governments should not incur peace time deficits. The federal government's initial reaction was also limited by constitutional constraints which placed responsibility for relief and unemployment with the municipal and provincial levels of government.

The second phase began with Bennett's belated attempt to apply Roosevelt's New Deal in Canada just before the 1935 federal election (Boyko, 2010: 363-414). After the election which returned Mackenzie King and the Liberals to office, balanced budgets were no longer a priority because of precedents set in Britain and the United States. Acceptance of deficit financing led to bolder and frequently longer term changes in institutional arrangements.

#### **4.1 Support for Prairie Farmers**

The Depression of the 1930s met the criteria for a crisis laid out by Congleton (2005: 183, 188): it was an unpleasant surprise to which an urgent response was expected. Under such circumstances those responding to crises are particularly prone to "systematic mistakes". Various measures were taken to support prairie farmers during the Depression. These

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<sup>146</sup> The debts assumed by the federal government as a consequence of the guarantees it held on railway bonds was in the order of 2 billion dollars. Although it was a tremendous sum for the time, while trade was brisk in the 1920s it could be managed. The Depression turned this debt into a crushing burden. Due to the decrease in trade, the CNR also began to lose substantial amounts of money during the Depression, and had to be further bailed out by the government.

options were chosen over the other suggested alternative, evacuating the region, because they were more practical and because of the belief that the primary causes of distress were the ‘extraordinary’ conditions of the time, rather than any fundamental imbalance between the supply and demand for wheat. CPR President Beatty was quick to add his voice to those seeking assistance for the prairie wheat sector in order to salvage some of the railway’s investment in regional branch lines (Marchildon & Anderson, 2008: 84).

Large numbers of farmers did, however, leave the stricken portions of the region on their own initiative. James Gairdner, a former Saskatchewan Premier, held the post of federal Minister of Agriculture from 1935 to 1957 in the Mackenzie King and Louis St. Laurent Liberal governments. He incessantly reminded his colleagues that federal government settlement policies were responsible for the Depression devastation of agriculture in Palliser’s Triangle and, therefore, that it had an obligation to those affected.

**Table 9 Interventions to Assist Prairie Farmers**

<ul style="list-style-type: none"> <li>• 1930 - Unemployment Relief Act provided some federal money for provincial and municipal public works initiatives. Farmers able to work on municipal projects in lieu of tax payments.</li> </ul>
<ul style="list-style-type: none"> <li>• 1931 - Unemployment and Farm Relief Act made federal government responsible for half the cost of relief payments. Intended as a temporary measure.</li> </ul>
<ul style="list-style-type: none"> <li>• 1932 - Five-cent bonus per bushel of wheat shipped. Well-intentioned, but resented by the many who had no wheat to sell.</li> </ul>
<ul style="list-style-type: none"> <li>• 1934 - Farmers’ Creditors Arrangement Act (FCCA) - provided a mechanism for farmers to restructure or obtain a partial write-down of their loans through the mediation of a government appointed Board (Thompson and Seager, 1985: 257).</li> </ul>
<ul style="list-style-type: none"> <li>• 1935 - Prairie Farm Rehabilitation Act (PFRA) - created a federal agency to rehabilitate some of the land most seriously affected by dustbowl conditions.</li> </ul>
<ul style="list-style-type: none"> <li>• 1939 - Prairie Farm Assistance Act (PFAA): designed as an institution with the purpose of delivering financial support to hard pressed farmers under emergency conditions.</li> </ul>

Difficulties originating in lack of demand and low prices were made worse by years of dry summers, hail storms, and plagues of various pests which combined to cause crop failure in some portion of the prairies every year in the 1930-1939 period. Dry summers, little crop cover and the widespread practice of cultivating summerfallow caused the dust storms which led to the use of the term ‘dirty thirties’. Some of the worst affected land, now considered unsuitable for cultivation, was returned to grass for use as community pastures under the auspices of the Prairie Farm Rehabilitation Administration (PFRA), a federal



government agency. (Marchildon & Anderson, 2008; Marchildon, 2009; See also MacEwan, 1966: Chapter 31; Gray, 1967; Canada: Department of Agriculture, 1961). Fowke, (1978: 286) acknowledges that, “[t]he Administration established under the act has worked ... with tremendous energy and enthusiasm, its efforts in substantial part devoted to *correcting the mistakes of the homestead period*” (emphasis added).

## 4.2 The Railways

It was during this period that railway rate regulation in Canada fell into what Darling (1980: 148) described as the ‘rut’ of subsidisation. The large increases in general (i.e. non-grain rates) sought by the railways after WWII re-ignited the freight rate issues. The Freight Rate Reduction Act of 1959, which provided the railways with the first subsidies not specifically tied to a particular project, was the first step on this slippery slope. Subsidisation of grain-related railway infrastructure was one of the interim steps recommended by the MacPherson Commission. It argued that as parliament had made freight rates charged to transport grain ‘statutory’, parliament would also have to devise the solution.

**Table 10 Interventions Affecting Railway Operations**

<ul style="list-style-type: none"> <li>• 1932 – 1938 – Both railways subject to supervision by a federal government board for the duration of the Depression. Both suffer a sharp drop in traffic, particularly shipments of prairie grain.</li> </ul>
<ul style="list-style-type: none"> <li>• WWII – Freight rates were frozen; but railway costs rise, leading to applications for large rate increases after the War.</li> </ul>
<ul style="list-style-type: none"> <li>• 1948 - Turgeon Royal Commission prompted by the rate increases granted after the War. Report in 1951 called for an equalisation of class rates across the country and an end to sixty years of argument over ‘freight rate discrimination’. The Railway Act was amended accordingly the same year.</li> </ul>
<ul style="list-style-type: none"> <li>• 1959 - Freight Rate Reduction Act. Provided subsidies to railway companies to cover operating expenses rather than specific capital projects in the face of union demands for higher wages and the disinclination of the Diefenbaker Conservatives to sanction any further rate increases.</li> </ul>
<ul style="list-style-type: none"> <li>• 1959 - MacPherson Royal Commission. Its Report in 1961 found that the railways did lose <i>money</i> moving grain exported by rail from the prairies and that the need to cover costs placed other shippers in jeopardy. The Report made it clear that parliament had a responsibility to make good any shortfall that arose when a railway was required to move goods at legislated rates.</li> </ul>
<ul style="list-style-type: none"> <li>• 1967 - National Transportation Act implemented the recommendations of the MacPherson Commission, and the federal government began to off-set the ‘Crow Gap’ with an <i>ad hoc</i> series of government funded programmes to keep grain from the prairies moving on the railways.</li> </ul>

### **4.3 Tariffs**

Trade restrictions were adopted by importing countries in the belief they would stimulate domestic production and ease rampant unemployment. Raising tariffs, but then holding out the possibility of negotiating reductions with countries prepared to do the same, was another justification for tariff increases during the Depression. Canadian tariffs were raised in a tit-for-tat response to the Smoot-Hawley tariffs in the U.S. and in a vain effort to maintain government revenue in the face of declining imports.

Canada also sought preferential 'empire' tariffs on wheat exported to Britain. Canada's longstanding insistence on protecting its manufacturing sector with the National Policy tariffs made this an unpopular request and Britain asked for Canadian reductions in exchange. This pitted eastern 'interests' against prairie farmers once again. British rural interests did not support preferential treatment for Canadian wheat. Although the interests of urban consumers had been important to the argument against taxes on food when the Corn Laws were under attack in the nineteenth century, they seemed to carry less weight at this time of particular economic hardship. A very modest reduction in the British tariff on wheat imported from 'empire' sources was reluctantly conceded at the Ottawa Conference in 1932.

Insofar as Canada's overall trade in wheat was concerned, the 1932 tariff concessions on 'empire wheat' had little impact: because exports from Australia and Canada by this time exceeded Britain's requirements by a substantial margin, any benefit obtained in the U.K. market was lost in the much lower prices obtainable elsewhere. Argentina and Australia were among a large number of countries that devalued their currencies in response to the British devaluation in 1931. However, the importance of commercial links to the United States prevented Canada from following suit.

Sales of farm machinery almost dried up completely during the Depression. Canadian farmers purchased over 17,000 tractors in 1928; in 1932 they purchased 892 (Thompson & Seager, 1985: 196). Under such circumstances, it was improbable any changes in tariff rates would have affected prices paid by farmers.

### **4.4 Grain Marketing and Transportation**

The farmer-owned Wheat Pools found themselves in trouble in 1929 because of their aversion to hedging grain on the futures market and efforts to hold wheat back from the

physical market in an attempt to maneuver prices higher. To prevent the banks from liquidating the Pools' assets and to obtain bank guarantees for the initial payment for the small crop of 1930, the prairie provincial Premiers asked for the Bennett government's help.

The most immediate problem that the Bennett Conservatives faced when elected in 1930 was the precarious position of the Wheat Pools. The three prairie Premiers asked the federal government to guarantee an initial payment of 70 cents per bushel for the deliveries of the 1930 crop to the Pools. This was justified by, "... the fact that producers of wheat today are passing through world conditions not of their making and that they should not be singled out as the one industry that must work through these conditions unassisted by the state" (Letter quoted in Wilson, 1978: 281). Bennett's agreement, albeit for a support price of only 60 cents per bushel, set in train a series of events that changed the way prairie wheat would be marketed for nearly seventy years.

To appease the banks and obtain loans for the initial payment, John McFarland, who had been the General Manager and a partner with Bennett in the Alberta Pacific Grain Co., took charge of the Pools' Central Selling Agency. His mandate was to sell the huge grain inventory accumulated by the Pools and to 'support' prices on the futures market by periodically intervening on the government's behalf. Given the state of wheat markets at the time, these two contradictory objectives were an onerous responsibility. The Pools' carry-overs from the 1928 and 1929 crops were not liquidated until 1935.

The price support role played by McFarland provided rent-seeking opportunities in the futures market for the private grain trade. To address this problem, the Bennett government prepared legislation to create a compulsory Wheat Board with monopoly power over the sale of all major grains and flaxseed. Under such arrangements, the futures market would cease operations, as was the case in 1919. However, these powers would only become effective were the legislation enacted by proclamation. The option of invoking the legislation at some future date amounted to a threat directed at the private grain trade. MacGibbon (1952: 35) described the proposed legislation as "a long step in the direction of state socialism for a Conservative government."<sup>147</sup>

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<sup>147</sup> MacGibbon (1952: 64) summarises the decisions that led to the Compulsory Wheat Board as follows: "A combination of causes had finally driven [the Liberal administration] into this position, rather than a tardy

By the time the legislation was finally passed, it had been significantly modified in ways that would prove ironic in light of future events. First, its mandate was restricted to wheat. Second, selling to the Board was optional. Third, it was subject to an annual renewal of its mandate. The new Wheat Board operated as an alternative to the private grain trade, with the government setting the initial price at which it would accept deliveries of wheat. When this price was higher than the open market, it acted as a ‘floor’ price. When it was lower, deliveries to the Board would cease. Although both situations occurred over the next few years, when price support was needed the burden on the treasury was high. In addition to turmoil in the markets, poor harvests meant once again that farmers with wheat to sell obtained a benefit not available to those in more dire straits.

**Table 11 Key Interventions Affecting the Marketing and Transportation of Wheat**

<ul style="list-style-type: none"> <li>• 1930 - The federal government stepped in to protect the Pool’s Central Selling Agency from bankruptcy when wheat prices declined after the initial price was set. John McFarland, a former partner of the Prime Minister in a successful grain business was appointed to dispose of the wheat stocks the Pools had accumulated.</li> </ul>
<ul style="list-style-type: none"> <li>• 1933 - Canada inaugurated efforts to negotiate international price stabilization agreements without success. First International Wheat Agreement established a minimum price and export quotas, but the agreement did not last.</li> </ul>
<ul style="list-style-type: none"> <li>• 1935 – The Canadian Wheat Board Act established a voluntary marketing agency for prairie wheat. The Act enabled government to set a floor price for the small amount of wheat produced during the remainder of the Depression.</li> </ul>
<ul style="list-style-type: none"> <li>• 1941- Feed Freight Assistance Act (FFAA). Reduced the cost of transporting prairie feed grains to other provinces in an effort to boost wartime production of livestock products.</li> </ul>
<ul style="list-style-type: none"> <li>• 1942 - The CWB took control of the allocation of railway boxcars as a wartime measure.</li> </ul>
<ul style="list-style-type: none"> <li>• 1943 - Marketing prairie-grown wheat through the CWB made compulsory. Mandate renewed annually until 1965 when it was made permanent.</li> </ul>
<ul style="list-style-type: none"> <li>• 1946 - Canada negotiated a long term post-war contract with Britain for wheat (1946-50) which specified minimum prices and quantities for each of the four crop years it covered.</li> </ul>
<ul style="list-style-type: none"> <li>• 1949 – Marketing of oats and barley added to the Wheat Board’s mandate. As a consequence, these feed grains could only be moved across provincial boundaries if they were purchased from the Wheat Board.</li> </ul>
<ul style="list-style-type: none"> <li>• 1956 – Temporary Wheat Reserves Act subsidises construction of additional grain storage capacity on the prairies to deal with mounting stocks of unsold wheat.</li> </ul>

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conversion to the belief that a national wheat board was the most desirable method of marketing the Canadian crop.”

## **5 Consequences of Intervention in Response to the Depression**

The consequences of interventions introduced in this time period fall into two categories: those resulting from the immediate response to the problems of the prairie grain economy during the Depression itself, and the longer term consequences which changed the institutional environment in which prairie agriculture operated after WWII. This section deals with the former.

A number of legislative measures were taken to assist prairie farmers during the Depression. Each resulted in unanticipated consequences. The intervention that had the greatest impact on the institutional environment in the post-WWII period resulted from an attempt to bail out the three Wheat Pools in 1930. The result was the Canadian Wheat Board (CWB).

### **5.1 The ‘Five Cent Bonus’**

Under pressure, Bennett introduced legislation in 1931 to provide farmers with a five cent per bushel bonus at a time when crop prospects in much of the Prairies were already expected to be very poor. This intervention provides a good example of a policy mistake made under the duress of a full-blown crisis. Although the program cost nearly \$13 million, it was heavily criticised as ‘inequitable’ because it provided additional funds to those who had wheat to sell, with nothing going to those who were in a much more difficult situation due to hail or ‘drought’.

### **5.2 Farmers Creditors’ Arrangement Act (1934)**

The FCAA provided a mechanism to enable distressed farmers to restructure or obtain a partial write-down of their loans through mediation of a government-appointed loan board. If agreement could not be reached, the Board was empowered to provide compulsory arbitration (Thompson and Seager, 1985: 257). The preamble to the loan repeated a familiar theme: that many farmers are unable to repay their loans due to atypical circumstances and that retaining farmers on the land as ‘efficient producers’ is in the national interest (McQueen, 1935). When the Prime Minister introduced the legislation in parliament he made it clear that its objective was “to keep the farmer on the land” (Marchildon, 2009: 285).

In the short run, many thousands of farmers obtained some benefit from the FCAA process. Whether the restructuring of loans enabled them to out-last the Depression is another question. However, the banks became extremely reluctant to lend to prairie farmers as a

direct consequence of government intervention. To compensate for a perceived shortage of credit, a number of provincial and federal initiatives were introduced to make credit available. The federal Farm Credit Corporation (FCC), launched when Diefenbaker was Prime Minister, brought the state into agriculture as a lender of last resort. Its readiness to lend money was subject to political pressure, and it tended to lend more in downturns when that pressure was most severe. Once again, efforts to stabilise the situation in the Depression had unintended consequences, and among those consequences was a situation where the commercial banks had the federal government as a competitor in the agricultural credit market.

### **5.3 The Wheat Board**

In 1938, the government announced its intention to leave the marketing of wheat to the grain trade, and confine its role to providing a safety net in case of crop failure. This, however, did not happen due to the threat of war. Between 1939 and 1942 the Board was involved in restricting accumulation of carry-over stocks. In 1943 prices improved, and the Liberal government of Mackenzie King gave the Board a ‘temporary’ monopoly to sell prairie wheat, a monopoly which in fact lasted until July 31, 2012. Fowke (1978: 276) pointed out that the compulsory Board came into being again to “arrest an advance rather than a decline in the price” (the first instance having been the WWI Board), and to ensure that Canada would be able to meet its Mutual Aid commitments in post-war Europe and negotiate a four year agreement to supply Britain<sup>148</sup>

The process for marketing wheat changed dramatically between 1930 and 1943. This synopsis illustrates the ‘concatenation of coincidences’ that progressively altered the scope of government involvement between the onset of the Depression and the end of WWII. There was no radical policy change, but there were significant alterations to the institutional environment as the result of a convoluted political process. Support for the ‘100 per cent pool’ among farmers had been limited to its extreme factions in the late 1920s. The more moderate prairie farmers were too preoccupied during the 1930s to oppose the concept. Most importantly, the Wheat Board mechanism was attractive to technocrats who believed it was possible to sort out the ‘wheat problem’ sitting around a table with representatives from exporting and importing nations. Credibility in such negotiations was enhanced when

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<sup>148</sup> The post-war supply agreement with Britain caused a great deal of ill-will because, from the Canadian perspective, Britain refused to pay the higher price warranted by market conditions during the final year of the Agreement. The Canadian government eventually made a special payment of \$65 million to prairie wheat growers as compensation (Brennan, 2011; Wilson, 1978: 846-885 & 921-928; 1017-1042).

it could be demonstrated that Canada had a mechanism in place to control the flow of prairie grain onto the international market.

#### **5.4 The Prairie Farm Assistance Act (PFAA)**

The Prairie Farm Assistance Act was the first attempt to provide financial assistance to prairie farmers in case of crop failure. Benefits were capped at a maximum of 200 acres, which was extremely modest under the circumstances but limited the exposure of the federal treasury at a difficult time. The programme represented an effort to learn from the reaction to support allocated only on the basis of wheat sales.

The voluntary Wheat Board which came into existence in 1935 made the initial price set by the government the 'floor' price for the crop year. This mechanism suffered from the same defect as the 5 cent bonus: only those with wheat to sell would benefit. Once the government had elected to support prairie wheat production, a mechanism which provided an insurance safety net to farmers in case of crop failure was required. At the time it was instituted the federal government planned to return the marketing of wheat to the private and cooperative grain companies after the 'extraordinary' Depression circumstances passed.

To fund potential pay-outs, the government reduced the floor price guaranteed by the voluntary Wheat Board and instituted a one per cent levy on grain sales. The impact was to redistribute income among farmers in the region. According to Fowke's calculations:

While the programme has been in effect, Manitoba farmers have *paid* \$3.25 in levies for each dollar they have received in payments, whereas Saskatchewan farmers have received \$2.30 and Alberta farmers \$1.55 for each dollar they have paid in levies" (Fowke, 1978: 294.; original emphasis).

The PFAA established the precedent that prairie grain growers should be compensated for losses due to 'extraordinary' circumstances. The principle that prairie farmers in the better endowed portions of the region should cross-subsidise those in the parts of the region less suited to crop production was dropped, and more emphasis was placed on farm income stabilisation over several years, with the farmer, the province and the federal government contributing matching premiums ('tripartite stabilisation'). However, the cross-subsidisation principle re-emerged in the Wheat Board quota system once the Board became compulsory in 1943.

## **5.5 Rural Depopulation and Land Use**

In 1931-32 alone, over 304,000 rural residents in southern Saskatchewan, more than one third the population of the province, relied on welfare assistance (Marchildon, 2009: 281). In 1936, the new Minister of Agriculture James Gairdner toured the heart of Palliser's Triangle where there were already 14,000 abandoned farms (Marchildon, 2009: 293). By 1937, two thirds of the entire rural population of Saskatchewan were on relief. With its income sources drying up, relief costs quickly overwhelmed the provincial budget. The other western provinces were also essentially bankrupt from 1932 onwards. It is estimated that more 200,000 individuals from Saskatchewan, and more than 250,000 from all three provinces as a whole, left the prairies between 1931 and 1941.

The weather-related set-backs that the southern prairies endured during the 1930s continued the retrenchment of agricultural settlement which had begun in the south-east Alberta dry-belt during WWI and into the early 1920s. A number of farmers in the western sections of southern Alberta had experimented with ways of reducing the impact of wind erosion. Use of mouldboard ploughs on summerfallow had been abandoned in favour of duck-foot cultivators and rod-weeders. These implements cut the roots of weeds with minimal disturbance of the soil surface. Alternating strips of crop and summerfallow were also adopted in the same region to reduce soil loss from wind erosion.

By the 1930s these practices had not been widely adopted in Saskatchewan, and the dust storms of the 1930s were particularly severe as a consequence. The main barrier to acceptance of this innovation was the pride taken in 'clean' summerfallow. Cultivation methods which left 'trash' in the form of stubble and dead weeds were considered poor farming. Only after the dust bowl of the 1930s were such practices widely more widely adopted in the southern prairies.

## **5.6 Railways**

Both railways suffered a sharp drop in revenue during the 1930s and faced serious financial difficulties. Much of that loss was blamed on the decline in shipments of prairie grain. CN losses absorbed a third of the federal government's revenue during the Depression, a time when there were many other claims on the treasury. A Royal Commission convened during the Depression considered various options which included a proposal by Sir Edward Beatty that Canadian National be managed by Canadian Pacific as a means of eliminating waste and duplication of service. This was rejected by the Royal Commission, and in 1933 the



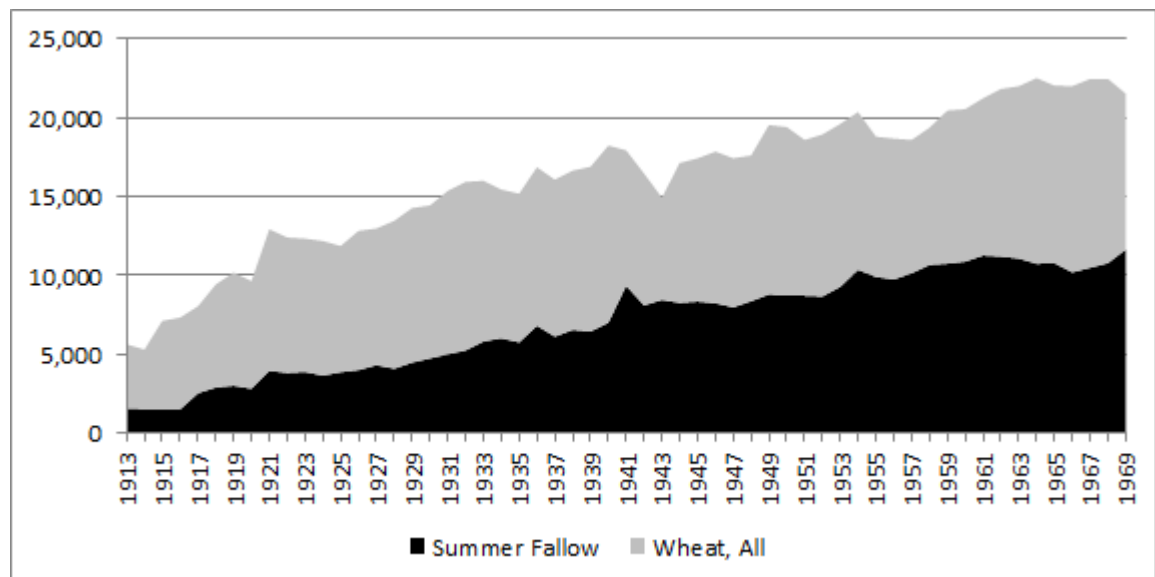
federal government placed both railways under the supervision of a joint Board for the duration of the Depression instead.

## **6 Post-War Consequences**

### **6.1 Land Use**

The Wheat Board introduced a quota system to ration market access equitably and to distribute the flow of grain evenly through the grain handling and transportation system (GHTS). Equitable access meant that wheat shipments from farms on the most productive land were restricted until those with inferior yields had delivered all their production. Since quota acres included both land seeded to wheat and summerfallow acreage, this provided an incentive to summerfallow land other than its direct economic benefits. When Wheat Board sales were small relative to the availability of grain, or the GHTS system was unable to move large quantities of wheat, country elevators would fill up and the quota system would be used to keep wheat deliveries within certain limits (Storey, 1978: 751). This aspect of the Wheat Board system became an issue when it was recognised that summerfallow contributed to land degradation by increasing soil salinity and erodibility, and accelerated the mineralisation of nutrients (Fairburn, 1984; Chapter 3; Rennie, 1979, Wilson, 1981: Chapter 4).

**Figure 13 Prairie Provinces Wheat and Summer Fallow (hectares)**

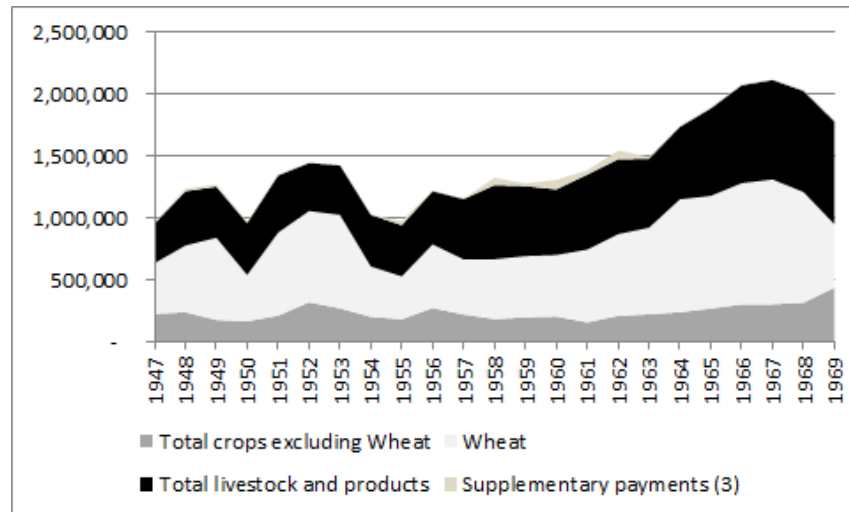


Source: Chart by Author, data from Statistics Canada Table 001-0010  
<http://www5.statcan.gc.ca/cansim/a26?lang=eng&id=10010>

Rationing access to the market via a quota system encouraged farmers on poorer land to increase their share of the market by breaking additional land. It also discouraged farmers

on the better land from maximising production. Stocks carried over from one year to the next depressed prices. The Temporary Wheat Reserve Act of 1956 subsidised the storage of wheat and growers' cash flow. On farm grain storage capacity increased significantly as stocks backed up through the GHTS from terminal elevators to country elevators, adding to the farmers' costs.

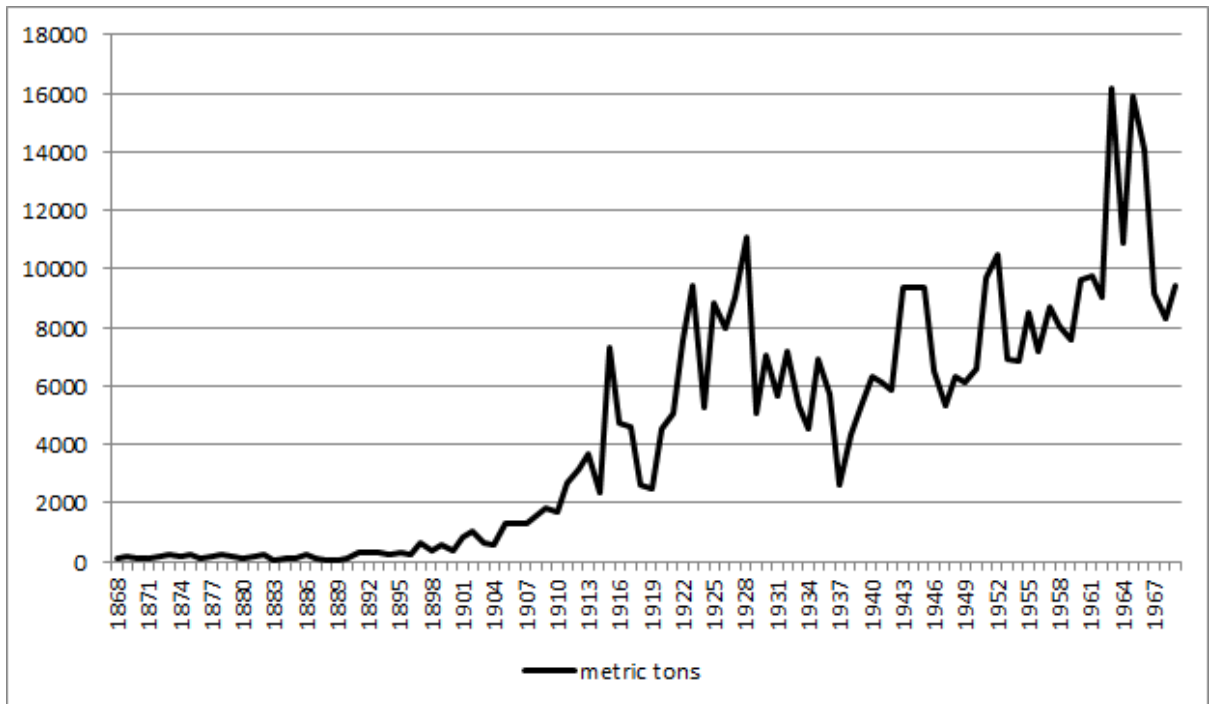
**Figure 14 Farm Cash Receipts 1947 – 1969 (000s dollars)**



Source: Chart by Author, data from Statistics Canada Table 2-0014

<http://www5.statcan.gc.ca/cansim/a26?lang=eng&retrLang=eng&id=0020014&&pattern=&stByVal=1&p1=1&p2=-1&tabMode=dataTable&csid=>

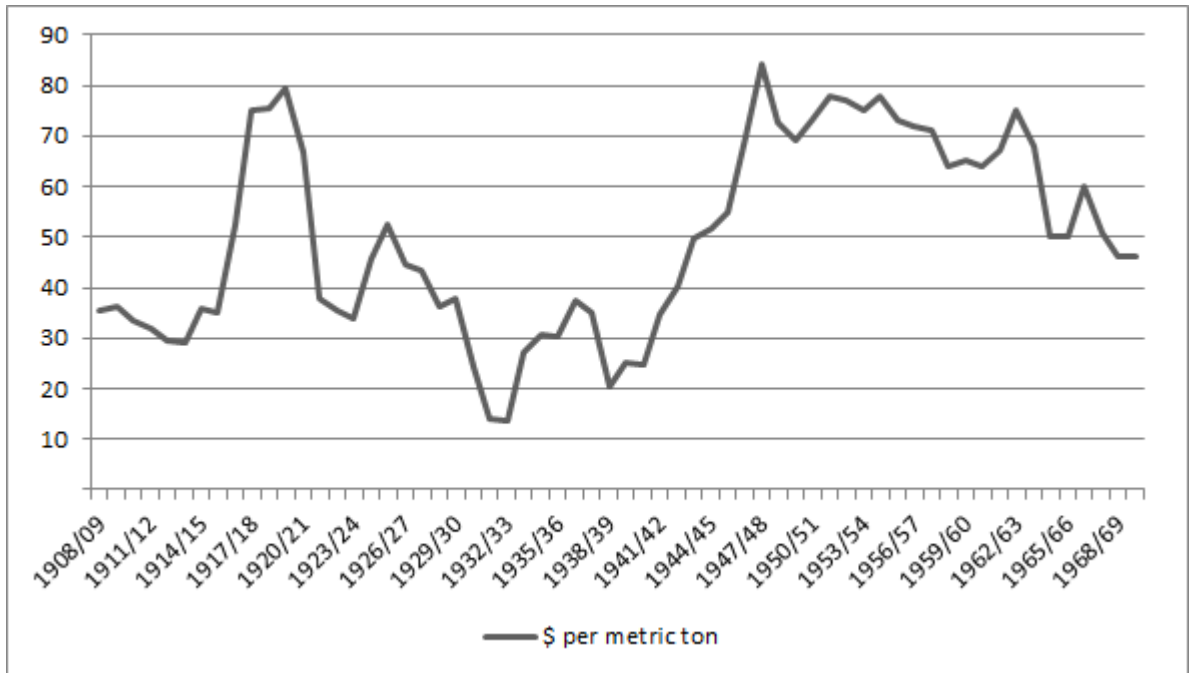
**Figure 15 Canadian Wheat Exports (metric tons) Canada**



Source: Chart by Author, data from Statistics Canada M Series 301 – 309.

[http://www.statcan.gc.ca/access\\_acces/archive.action?l=eng&loc=M249\\_300a-eng.csv](http://www.statcan.gc.ca/access_acces/archive.action?l=eng&loc=M249_300a-eng.csv)

Figure 16 World Wheat Prices (\$US per metric ton)



Source: Chart by Author, data from USDA Table 20 Wheat Prices  
<http://www.ers.usda.gov/data-products/wheat-data.aspx>

## 6.2 The Railways

The Duff Royal Commission during the Depression outlined in detail the huge financial burden the nationalised railway imposed on the government and Canadian taxpayers. The rebound of railway traffic during the war created the illusion that the situation was improving. Yet in the late 1950s the federal government began to subsidise both railways as a temporary measure until the issue which made the subsidies necessary could be addressed. In the short run, the availability of the subsidy removed any urgency to address the underlying problem. The same would be true once subsidies were provided to keep grain dependent branch lines on the prairies in operation.

The main railway issue in the post WWII period was caused by the nineteenth century Crowsnest Pass Agreement which had been extended in the 1920s by statute to cover all grain moving from the prairies by rail. This legislation did not take account of how subsequent inflation would affect the GHTS.

Requests for large rate increases to claw back ground lost while rates were frozen during the War led to two important Royal Commissions: the Turgeon Commission in 1948 and the MacPherson Commission in 1959. The 1951 Turgeon Commission Report ignored

wartime inflation, the increasing burden the CNR imposed on the public purse and the deterioration of the railway infrastructure available to move prairie grain, and focussed instead on regional pricing equity. This led to increasingly restrictive legislation to equalise general (non-grain) freight rates across Canada. Darling's (1980: 181) summary of the situation after the Turgeon Commission is relevant to the freight rate issue affecting prairie agriculture:

The Turgeon Commission's recommendations represented about the greatest length that one could go under Canadian conditions in eliminating 'freight rate discrimination' if one merely aimed to establish a practical application of a principle of equity in which the costs would be paid by the users. Beyond this point the demands for something more than equity could only be satisfied by subsidy, for the Crow's Nest Pass method of a simple statutory freezing of the rate regardless of the consequences was not likely to be repeated.

The note indicated at the end of the quote reads "And yet of course it was repeated every time a new commodity, such as rapeseed, was brought under the statutory umbrella" (1980: 250).<sup>149</sup>

Some of the requests for post-War rate increases may have been inflated by a desire to cross-subsidise grain transported at statutory rates. In 1951 the CPR advocated a doubling of the rate railways were permitted to charge for grain shipments, a suggestion that would not have dealt with the problem of future inflation.

The main impediment to any resolution of the freight rate issue as it applied to grain was the well-entrenched idea that the Crow Rate was a substantial benefit to the prairie grain grower, and that the CPR had been "given half of western Canada" in exchange for this benefit. Yet it was a benefit with a double edge: the Depression had vividly illustrated the consequences of bringing less productive portions of the region closer to the market by reducing freight rate charges. As inflation increased, it would also become a liability when the railways started to ration access when traffic moving at compensatory rates was brisk. This meant that prairie grain could not be delivered to ports to meet market commitments. Only when demand for rail capacity slackened, as it did during recessions, did the statutory rate become a benefit to prairie growers. Under such circumstances, the 'benefit' was provided at the expense of the railway's shareholders.

This freight rate issue re-emerged a decade later when the railways asked for further rate increases to cover demands for higher wages. When a railway worker's strike threatened,

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<sup>149</sup> By the time measures were taken to replace the statutory rate with a subsidy in the early 1980s there were 58 commodities eligible for the low 'Crow' freight rate.

Prime Minister Diefenbaker announced the appointment of the MacPherson Commission<sup>150</sup> to address the issue again, but simultaneously took the unprecedented step of providing subsidies to the railways to cover alleged revenue shortfalls. This was the first subsidy justified by a general revenue deficiency rather than for specified capital projects. Most importantly, this particular subsidy signalled a radical departure from the principle that railways should be “run as a business.”

It is significant that the turning point on the policy of railway subsidisation occurred when John Diefenbaker was the Conservative Prime Minister. Diefenbaker represented Saskatchewan ridings and was thoroughly steeped in the ideological rhetoric of freight rates. Darling (1980: 209) points out that his understanding of the underlying issues was seriously flawed, but that he “invariably showed a firm grasp of its political potentialities”.

The Commission’s Report was a radical departure from that of its predecessor. Three of its key recommendations were that: 1) where the railways were required to transport goods other than grain at legislated rates, they should be compensated from public funds for operating shortfalls;<sup>151</sup> 2) the country’s transportation policy should be clearly separated from its national policy; and 3) regulation should be minimized, and be consistent only with protection of the public interest. It used the existence of other modes of traffic (roads and waterways) to justify a longer term recommendation that railway rates should be determined in the marketplace. Many of the Commission’s proposals were incorporated in the National Transportation Act (NTA) of 1967.<sup>152</sup>

With respect to grain transported by rail, the MacPherson Commission concluded that the railways lost \$11 million each moving grain at statutory rates in 1958. This was the first independent attempt to quantify the “Crow Gap”, the revenue shortfall for transporting grain by rail. The Commission also pointed out that grain rates were set by statute and any changes were therefore the responsibility of parliament.

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<sup>150</sup> Diefenbaker tried to have the politically sensitive Crow Rate excluded from consideration by the Royal Commission, but failed.

<sup>151</sup> Two of the Commissioners wrote dissenting reports recommending that parliament monitor conditions in prairie agriculture with a view to raising the statutory rates to relieve taxpayers of the burden inherent in the required subsidies (Darling (1980: 224); Currie (1967)). This suggestion was acted upon in the 1990s.

<sup>152</sup> The hypersensitivity of the electorate to freight rate issues in both the West and the Maritimes and three successive elections that returned minority governments were factors delaying the implementation of the MacPherson Commission’s recommendation in the National Transportation Act of 1967. Darling (1980: 225) alleges that the recommendations were widely misunderstood which complicated the process of translating them into legislation which could be concisely explained to the electorate. More attention was paid to the Commission’s call for ‘temporary’ subsidies – which were unpopular -- than to its recommendations regarding regulatory changes that would render them unnecessary. Subsidies provided under the Freight Rate Reduction Act continued as a stop-gap measure.

The advent of lorry transport eliminated rail traffic *to* small prairie towns and most branch lines were now wholly reliant on moving grain from those ‘towns’.<sup>153</sup> The NTA made provision for the subsidisation of ‘grain dependent’ branch lines. As Earl (2011: 10) pointed out, the net effect was to remove incentives to abandon 12,000 miles of grain dependent branch lines in the short term and to push the underlying problem into the future.

Faced with increasing costs and freight rates frozen at 1899 levels, the railways altered their investment strategy. They focussed on modernizing the rolling stock used to haul non-regulated goods and commodities. Without any incentive to invest in moving grain, the railways allowed the grain transportation infrastructure to deteriorate. Grain was still transported in ageing boxcars. These boxcars had been suitable for backhauling goods to small prairie towns before lorries eliminated that traffic but were ill-suited to bulk handling of grain.

The Feed Freight Assistance Act (FFAA) of 1941 created a transportation subsidy as part of the wartime drive to increase meat production. Its objectives were to increase use of prairie-grown feed grains and to provide lower cost feed to livestock producers in other provinces. Statutory freight rates which encouraged grain exports increased the price at which feed grains were available on the domestic market. Feed Freight Assistance subsidies reduced those prices outside the prairies to offset the effect of the artificially low rates for exported grain imposed by legislation (Klein, 1994: 60). It was modified repeatedly as circumstances changed, and provides a classic illustration of an intervention prompted by the unanticipated consequences of an earlier intervention.

### **6.3 Grain Marketing**

Western Canada’s prairie grain economy was oriented primarily towards the British market in its early years. Tariff free access to the U.K. market ended with the passing of the Wheat Act of 1932. The European market for prairie wheat shrank as a consequence of a post-war drive to increase self-sufficiency, lower per capita consumption, and technical change in

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<sup>153</sup> Although population centres on the prairies are invariably referred to as towns, most of them would be considered villages or hamlets in other contexts. They were small because they were established as shipment points when grain was brought to elevators in horse drawn carts. The services these towns provided declined quickly as better roads and the internal combustion engine made travel easier. However the institutional infrastructure of the prairie grain economy (specifically the Wheat Board) ensured that grain would continue to be loaded into rail cars in each town.

baking technology which had successfully reduced the importance of ‘strong’ (and relatively expensive) wheat varieties well-suited to Canadian conditions.<sup>154</sup>

During the 1929 to 1969 time period, Canada’s share of the world market for wheat declined to an average of around 22 per cent in the 1960s and it relinquished its place as the world’s leading exporter to the U.S. after WWII. Aggressive subsidy and disposal programmes adopted by the United States and the European Union were frequently blamed for this poor performance. However, inefficiencies that resulted from the joint effects of the Wheat Board and the statutory freight rate regime for grain transportation made it increasingly difficult for the Wheat Board to meet its sales commitments.

The establishment of the Wheat Board had both domestic and international repercussions. On the prairies, the Wheat Board system became a mechanism for rationing access to markets among all prairie grain growers. The equity principle that the Board inherited from the provincial Wheat Pools required that all growers wishing to market wheat be allowed to do so. This introduced a bias in favour of extensive farming: revenue earned by the Board was distributed according to area seeded to wheat instead of to farmers able to produce most efficiently.

Without the Board, the spatial distribution of wheat production would likely have been quite different. If the market were allocated on the basis of prices, the most efficient farmers on the best quality land would have been the most successful. For a given volume of exports and hence revenue, this would have resulted in a smaller number of producers using a smaller area of land more intensively. The same revenue and a smaller number of farmers would translate into higher income for participating farmers. Put differently, under the Wheat Board system, when market conditions were not good, the pain was distributed evenly over the entire area, rather than being concentrated on marginal producers as was the case in the pre-Wheat Board era.<sup>155</sup>

On the international front, the Wheat Board was a mixed blessing. It gave the Canadian government credibility at multi-lateral consultations on the international wheat market because it was a mechanism capable of exerting control over sales volumes and, if necessary, production. The Wheat Board became a convenient instrument of national

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<sup>154</sup> This was the Chorleywood Baking Process, developed in Britain and used after 1949.

<sup>155</sup> Grain growers on the better situated land were in effect required to subsidise those on land less suited for grain production. The same redistribution effect was evident in the Prairie Farm Assistance Act (see above, p. 137).

policies. However, this was more a theoretical than practical benefit as free-riding problems consistently undermined any attempts to ‘manage’ international trade.

It was frequently claimed that marketing through a state trading agency such as the Canadian Wheat Board made it easier to obtain sales in countries which use similar institutional arrangements for their imports. During the post-war period both the USSR and China used such agencies and Canada did obtain significant supply contracts with these nations. However, they also purchased from suppliers who did not have similar arrangements when politically and economically expedient.

#### **6.4 Grain Handling**

Early experience with bulk handling of grain in western Canada illustrated the commercial benefit of both marketing and handling grain. Making the Wheat Board responsible for sales of the most important prairie grains took away a significant amount of business from the grain companies, both cooperative and private. Grain handling companies could not compete on the price they offered for Board crops as they were acting as handling agents for ‘Board’ grains. The rates grain handling companies were allowed to charge for grading, elevating and storing grain were regulated by the Canadian Grain Commission (Wilson, 1979: 22). Most importantly, farmers were required to choose a single point for all their deliveries. In the absence of any handling price differentials to encourage use of more efficient elevators, they used the closest one available.

This operating environment provided the grain handling companies with a huge incentive to capture the regulatory process and ensure that even their most inefficient elevators could operate profitably. Under such circumstances, handling charges (and costs) were higher than they would otherwise have been, and there was no incentive to invest in the latest high-throughput elevators.

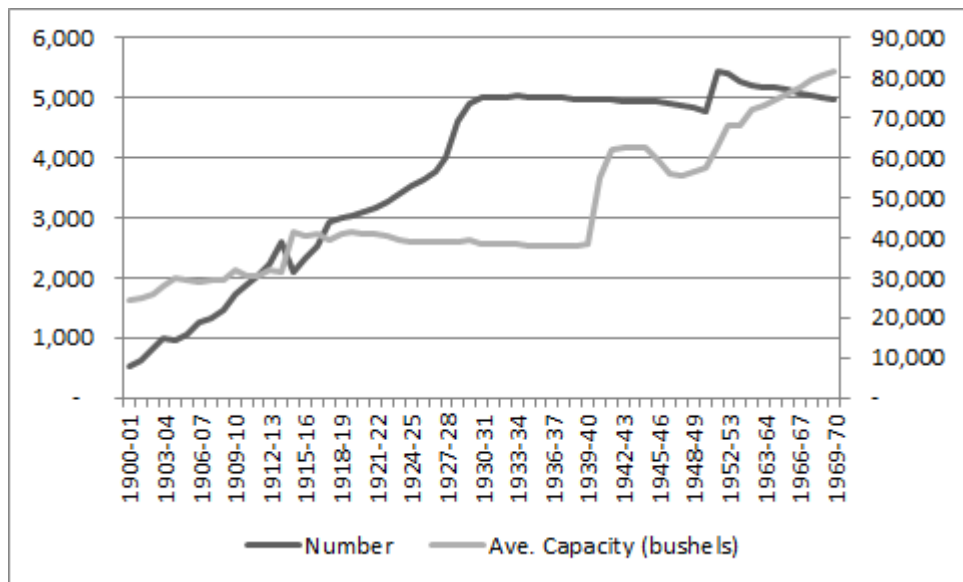
Providing producers with equal market access irrespective of location meant that the Wheat Board assumed an active role in the allocation of (increasingly scarce) railway rolling stock among prairie delivery points. Left to their own devices, the railways would have continued to control grain handling capacity and focus on where it could be used most intensively, exactly the situation that existed at the beginning of the century. Instead, by the end of WWII, the grain companies handled and the railway companies moved wheat at the behest of the Wheat Board. This arrangement eliminated serious competition among the grain companies and between the railways. Farmers delivered their grain to the nearest



elevator point, and all the elevators at the same point used the same technology and the same scale of service charges. Without competition, there was little incentive for the technical change which augments efficiency in the market process. The post-war decades were therefore a period in which the process of technical change ground to a halt in these two components of the prairie grain sector.

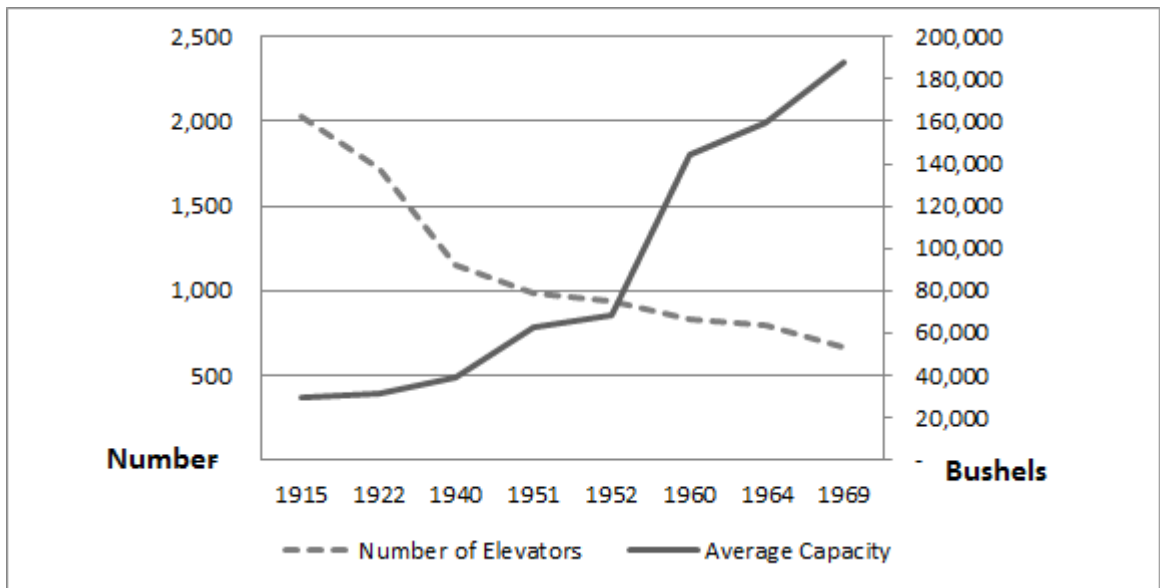
At the beginning of the twentieth century, wooden elevators were constructed at delivery points sufficiently close together along railway lines to enable horse-drawn wagons to make deliveries and return home the same day. With no incentive to change, grain handling companies did not update their elevators in the same way as their U.S. counterparts and continued using the technology of the 1920s (Earl 2000: 177; 2011: 10). By the 1970s, the capacity of combines was such that the main constraint on harvesting efficiency was the ability to haul grain away from the field fast enough, so the capacity of the lorries used increased significantly. However, such large lorries were too big to enter traditional elevators and dump grain, so two lorries were required: a large one for harvesting and a smaller one for the subsequent delivery of grain from farm storage to the local elevator.

Figure 17 Canadian Prairie Country Grain Elevators: Number & Average Capacity 1900 - 1969



Source: Chart by Author, data from Urquhart, M.C. & Buckley, K.A.H. *Historical Statistics of Canada*, Toronto: The MacMillan Company of Canada Ltd, 1965 Series L 337 -346 Grain Elevator Capacities 1911 - 1960 and Canadian Grains Commission: Grain Elevators in Canada 2013 <http://www.grainscanada.gc.ca/statistics-statistiques/geic-sgc/2013-08-01.pdf>

Figure 18 North Dakota Country Grain Elevators: Number and Average Capacity 1900 - 1969



Source: Chart by Author, data from North Dakota Grain Dealers Association cited by Ming & Wilson (1983) <http://ageconsearch.umn.edu/bitstream/23381/1/aer169.pdf>

Thus the grain handling system was locked in a regulatory stranglehold for the same reasons as the railways. Although the need for modernization was widely acknowledged, uncertainty about the future regulatory environment made it difficult to decide when and where the necessary investments should be made. The ‘country’ grain handling infrastructure on the prairies remained archaic while south of the border it evolved steadily toward an increasingly efficient system of high throughput inland terminals.

## **7 Counterfactual**

The counterfactual for this period of prairie agriculture is considered in two parts. The first deals with a possible alternative scenario from the point at which it became clear the Depression was no ‘normal’ recession. The second takes the end of WWII as the branching point.

### **7.1 An Alternate Response to the Depression**

In the case of the Depression, the element of surprise characteristic of a true crisis was very marked. The federal government faced constitutional obstacles to providing assistance to prairie residents: responsibility for relief lay with the Provinces. Provincial capacity to deal with emergency situations presupposed their control over provincial commerce and resources. The absence of capacity to cope with the demands placed on municipal and provincial governments in the Depression implied an obligation on the federal

government's part to address difficulties exacerbated by its efforts to settle the prairies. But other unintended consequences of those policies, most notably the financial obligations the federal government assumed when it set up the Canadian National Railway, limited its ability to respond without borrowing.

There were nonetheless options available to the federal government. The most significant of these involved the bail-out of the Wheat Pools at the instigation of the Provincial Premiers and the banks. Clearly Bennett found himself under a great deal of pressure on this particular issue, compounded by the empathy he felt for the part of the country in which he personally had achieved considerable success. Most importantly, this success included experience in the grain trade as a partner with Max Aitken (later Lord Beaverbrook) and John McFarland.

Failure to step in to defend the Pools would have made the banks responsible for quick sale of the grain which served as security for their loans. Prices would have been very low, but the surplus accumulated by the Pools would have disappeared and would not have depressed the market for such an extended period. It would also have kept the grain trade and the railways moving grain in reasonable quantities. Intervention by the government distorted the futures market and led inexorably to the creation of the Wheat Board.

The struggle to provide assistance to prairie farmers was channeled through such programmes as the 5 cent bonus, and the initial (floor) price in the market provided by the voluntary Wheat Board after 1935. These were costly programmes, but they were resented because they discriminated against farmers who had no crop to sell, a common occurrence in the region during the Depression years. There was therefore the option of decoupling relief payments from wheat production and providing additional funds to provincial relief initiatives. The chief advantages of this approach would have been sharing desperately needed relief payments more equitably while not distorting the admittedly unpalatable signals the market was sending at the time regarding the prospects for wheat production.

An opportunity to rationalise the Canadian railway network surfaced during the Depression, but was rejected. It was rejected at the time on the basis of the argument that a more efficient railway system would inevitably involve redundancies and 'make the Depression worse'. The outbreak of war provided another distraction. But by the time 'business as usual' resumed the warnings of the Duff Royal Commission and the willingness of CPR management to tackle the CNR problem were forgotten.

## 7.2 An Alternate Post-War Policy

After the war, quite a different set of possibilities was available. Wartime Wheat Board policies were directed more at controlling surplus production than providing wheat to the allies. A return to the private market after the war would not, therefore, have had the same impact on prices as the end of the first Wheat Board had at the end of WWI. The Liberal government planned to disband the Board in 1938, but the War made this impossible in the short term.

Support for maintaining the Board after WWII came from the Wheat Pools, which retained their aversion to the private grain trade. This influence would have been inconsequential had the federal government not come to their rescue in 1930. The Wheat Pools remained an important component of the post-War grain handling system largely because the Wheat Board adopted the Pools' philosophy of marketing and equitable treatment of farmers. Had the Wheat Board been disbanded and had the Wheat Pools survived the Depression, they would have found themselves once again in direct competition with the private grain trade. It would be presumptuous to predict how real competition for sales and the farmers' business between the two marketing approaches might have turned out in the post-war era.

Had the Wheat Board ceased to exist after WWII, as happened after WWI, a radically different scenario to the actual history becomes a possibility. Under such a scenario, the sector would have been forced to adjust rapidly to the post-war realities of the market. This would probably have implied a decline in wheat production, a reduction in arable acreage, more rapid consolidation of farms and diversification. Without the Wheat Board, the grain handling and transportation system would involve only the railways and companies handling and marketing grain. In the absence of the requirement that farmers deliver grain to a designated delivery point, grain companies would have been able to compete for grain deliveries. To do this they would have needed to invest in efficient elevator technology and provide farmers with financial incentives to transport grain longer distances by lorry. Eliminating inefficiencies would have been advantageous to all participants. As the situation unfolded, grain handling companies made money storing grain and the Wheat Board passed demurrage charges back to farmers. The grain companies would have shared a common interest in the railways providing adequate service. They might well have been at the forefront of efforts encouraging the federal government to make changes to the statutory rate before 1980, instead of fighting to preserve the *status quo*.

The statutory rate remains the most difficult element in any counterfactual argument for this time period. The CCF went into decline in the immediate post-war period and would have been unlikely to provide meaningful opposition in the federal parliament to any attempt to change the rate in the 1950-1970 period. Amending the statutory rate to put grain handled by rail on par with the recommendations made for other commodities in the MacPherson Commission Report would have avoided the protracted and as yet incomplete process of de-regulation that started in the early 1980s. This would have saved the federal government and the taxpayers a considerable amount of *ad hoc* expense in the process.

At the time of the Turgeon Commission, the price of grain was higher than it had been when the Crow Rate came into effect briefly in the 1890s and in the mid-1920s when the Crow Rate became a statutory rate. (Currie, 1967: 102). With the benefit of hindsight, the late 1950s also marked the beginning of two decades of post-war prosperity in which all regions of the country shared (Darling, 1980: 183). Had the Turgeon Commission not been distracted by the ideology of freight rates which led it to focus attention primarily on eliminating freight rate discrimination – real or imagined –the process of addressing the issues underlying the freight rate problem might have begun much earlier than was in fact the case.

Addressing the problem of the Crow Rate earlier in the region's history would have led to dramatic changes in agricultural economy of the region: a different balance between livestock and grains, no need for feed freight assistance, no discrimination between Board and non-Board grains in the allocation of railcar capacity, and the protracted phase of government subsidisation of railway grain handling capacity that occurred between the National Transportation Act of 1967 and the WGTA of 1983 avoided. Some of the unfortunate consequences of this 'subsidisation phase', such as government ownership of the majority of the grain hopper car fleet, have yet to be unravelled.

## Chapter 6

### Intervention Reversed: 1970-2013

The origins of Canadian National Railways, the Canadian Wheat Board, and the legislation of freight rates for grain were described in previous chapters. Together they constituted important components of the institutional environment in which prairie agriculture operated in the post-war period. Since 1980, this institutional environment has changed dramatically. Canadian National Railway has been privatised, the Wheat Board lost its ‘single desk’ sales mandate and was subsequently acquired by a grain trading company, and the statutory ‘Crow Rate’ disappeared. The cooperative grain companies, which perpetuated the ideological legacy of the agrarian populist movement, also disappeared. The circumstances which created the margin of opportunity to reverse some earlier interventions emerged from a growing conflict between the ideology of equity and economic reality, shifts in political and interest group dynamics and the evolution of international trade negotiations.

Reduced intervention in these three areas did not mean that Canada’s prairie farmers, politicians and bureaucrats were sudden converts to minimal state principles. Even as the ‘Crow’ rate was being dismantled in the early 1980s, the federal government increased its intervention in agriculture by creating Canagrex, a short-lived agency to promote and export commodities not covered by the Wheat Board and expanded the Farm Credit Corporation’s role (Wilson, 1990: 99-129; 96-98).<sup>156</sup>

The agrarian populist movement which became a powerful political force in the early decades of the twentieth century urged the federal government first to prevent the middlemen from exploiting their monopoly power and then to become directly involved in the handling and marketing of prairie grain. Prior to the Depression, farmers’ organisations had successfully lobbied for flat warehouses and loading platforms at railway shipping points, an end to the CPR’s monopoly, construction of the Hudson’s Bay railway, and low freight rates. When the Depression struck, the federal governments (both Conservative and Liberal) were prepared to bail-out the Wheat Pools and support wheat prices. To achieve these objectives the Bennett government installed a government appointee to take over the sales function of the Pools and prepared legislation under which a government agency

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<sup>156</sup> Canagrex was the one of the first agricultural sector victims of spending cuts made by Conservative federal government led by Brian Mulroney in the late 1980s.

would support prices and market prairie grain. The Mackenzie King government created a voluntary Wheat Board to market prairie grain when prices fell below a floor price the government set in advance. It created a separate 'support' mechanism with the intention of ending its involvement in marketing prairie grain, but WWII prevented that from happening. By the time the war ended, all remaining traces of an ideological aversion to direct state involvement in the economy had disappeared, and the Wheat Board remained in place.

In the 1970s, 1980s and 1990s a second populist movement erupted in Western Canada. Lingering resentment of the national policy and its impact on the prairies remained the foundation on which this outburst was based. The idea that the economy of the 'west' was prone to booms and busts was linked with the historical discrimination favouring manufacturers in eastern Canada. French-English antagonism also played an important role, particularly during the Liberal government of P. E. Trudeau<sup>157</sup> and the Conservative government of Brian Mulroney. But, in this instance, simmering resentment in the west was ignited not by policies affecting prairie agriculture but by the National Energy Policy (NEP) announced by the Trudeau government in 1980.

In 1971, Social Credit lost its hold on the government of Alberta to the Conservatives led by Peter Lougheed. The same year, the NDP (successor to the CCF) again formed the government in Saskatchewan under Allan Blakeney. In his memoirs, Blakeney acknowledged that attempts to shore up the prairie farm economy without the vast resources the EU and the United States were akin to those of King Canute trying to hold back the tide (2008: 5, 125).

Removal of some of the interventionist infrastructure imposed on prairie agriculture became possible because of a growing divergence of views among farm organisations regarding the value of government intervention, the resurgence of western alienation which had fiscal conservatism as one of its main tenets and recognition that the federal government could not afford an open ended financial commitment to support prairie agriculture.

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<sup>157</sup> All references to Prime Minister Trudeau refer to Pierre Elliott Trudeau, who was Prime Minister from 1968-1979 and 1980-1984. His eldest son, Justin Trudeau, became Prime Minister after leading the Liberal Party to victory in the federal election held in October 2015.

## **1 The Crisis**

Prairie agriculture was lurching towards crisis again in the 1970s. Like the Depression of the 1930s the backdrop was a series of international events which had serious repercussions on the prairies. Unlike the Depression crisis, however, it was a ‘looming’ crisis rather than a surprise. Mercifully, there was no repetition of the decade of unfavourable growing seasons which compounded the difficulties prairie farmers faced in the 1930s. Years in which crop yields were well below average did occur, most notably in 1988 and over several years early in this century.

International turmoil began with a breakdown of the institutional arrangements put in place in the immediate post-war period to facilitate trade by stabilising currency exchange rates. The anchor to the Bretton Wood system was a U.S. dollar convertible to gold at \$35 per ounce. In August 1971, the Nixon Administration ended the convertibility of the dollar at this rate, imposed wage and price controls and a tax on imports. This abrupt change in the rules encouraged the Organisation of Petroleum Exporters (OPEC) to reduce exports and precipitated a series of spikes in the price of oil and its derivatives. High rates of inflation and protracted periods of recession (‘stagflation’) followed in many ‘developed’ western economies.

The oil price shocks of the early 1970s were just one aspect of the general turmoil in international commodity markets which resulted when endogenous changes in demand and supply were affected by the breakdown in the end of the Bretton Woods accord. Wheat was among the commodities affected. Carry-over stocks of wheat grew to levels considered burdensome during the late 1960s and farm incomes on the prairies plummeted. But a few lower than normal crops in some wheat exporting countries and a large purchase of grain from the United States by the Soviet Union in 1972 made scarcity and rapidly rising prices a concern in the early-1970s.<sup>158</sup>

The structure of the international market for wheat changed dramatically in the 1970s. Developed market economies accounted for 81 per cent of wheat imports in 1971 but only 19 per cent in 1981. Developing country markets absorbed only 2 per cent of imports in 1971 and 43 per cent in 1981. Sixteen per cent of international wheat sales went to centrally planned countries in 1971 and 38 per cent in 1981 (FAO, 1971, 1981). Canada has

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<sup>158</sup> The controversial book *Limits to Growth*, which extrapolated consumption of key non-renewable natural resources and concluded that they would soon be exhausted, was published in 1972. The other major environmental issue in the mid-1970s was concern over evidence that global temperatures were declining and that a mini ice age might be imminent.



traditionally been an exporter of high protein, hard red spring wheat, and many of the new markets did not use this type of wheat.

In 1973 Britain joined the European Union (EU) on its third attempt. At the time of its accession, Britain's agricultural policies were more liberal than the highly protectionist EU and the prospect of higher food prices was advanced as an argument against joining. Canada would once again find itself caught between Britain (and the EU's Common Agricultural Policy) and the United States when the two entities became embroiled in a competitive subsidy war the late 1970s and early 1980s. This struggle placed further downward pressure on the prices of many agricultural commodities traded internationally. The Cairns Group of countries was formed to lobby for the lowering of barriers to agricultural trade with a particular emphasis on eliminating export subsidies and domestic agricultural policies that distort trade.<sup>159</sup>

Between 1986 and 1994 the Uruguay round of the multilateral trade negotiations attempted for the first time to incorporate agricultural subsidies under General Agreement on Tariffs and Trade (GATT). These negotiations created the World Trade Organisation and were successful insofar as an agreement on agriculture was signed. Whether it has helped liberalise trade in agricultural commodities remains a contentious issue. Irreconcilable differences over agricultural trade, particularly between the United States and the European Union contributed to the breakdown of the subsequent Doha round of multi-national trade negotiations in 2008.

A significant downside of reliance on a state trading agency like the Wheat Board has been its impact on Canada's relationship with other market participants, particularly the United States.<sup>160</sup> In concept, the Board was the marketing arm of a compulsory producer cooperative. However, the Board's ability to borrow at preferential rates by virtue of its status as a Crown Corporation, its use of intergovernmental credits to sell wheat, and its tendency to secrecy regarding contract terms and prices created a great deal of suspicion and led to unsuccessful challenges of the Board's role under World Trade Organisation rules.

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<sup>159</sup> Australia, one of several Commonwealth exporters of agricultural commodities which had been disadvantaged by Britain's decision to join the EU, instigated the formation of the Group in 1986. Canada became a member of the Group, but its supply management programmes for dairy and poultry products and the payment of the 'Crow Benefit' to the railways made participation awkward. In 1997 the private sector Canadian Agri-Food Trade Alliance (CAFTA), was formed to lobby for trade liberalisation.

<sup>160</sup> The lack of criticism of state trading companies which *import* agricultural commodities is perhaps indicative of the advantage importers enjoy in a 'buyer's market' for agricultural commodities.

The crux of the problem facing prairie agriculture in the 1970s was an increasingly hostile international trading environment. In the early decades of the twentieth century when free trade in wheat trade prevailed, the price available to prairie wheat producers reflected the relationship between supply and demand as interpreted by participants. After WWII an additional layer of uncertainty was superimposed on that relationship as participating nations tried to obtain extra-market benefits at the expense of other countries. With the exception of few short periods of time, importing nations held the more advantageous position.

Crop production on the prairies is extensive, involving large areas of land and relatively low yields. The oil price shocks which began in the early 1970s had an adverse effect because cultivating large tracts of land requires fuel, and fuel prices rose sharply. Production of other agricultural inputs, particularly fertilizers, are also energy intensive. Inflation added to the problem. Land prices tend to increase significantly during inflationary periods, which is good for those who are selling and bad for those buying. Lending institutions encourage borrowing when the value of the collateral is increasing. Wheat price increases in the early 1970s encouraged expansion of many farm operations, just as the high prices of World War I had done. Volatile prices for agricultural commodities and resumption of the downward trend after the price peak of the early 1970s contributed to the economic difficulties of prairie grain growers in the late 1970s and 1980s.

The final blow for many farmers in North America, were steps taken by the Reagan Administration in the United States to break out of 'stagflation' by 'wrestling inflation to the ground'.<sup>161</sup> Interest rates were allowed to rise until inflation began to decline. Higher borrowing costs made it more difficult for those who had borrowed to expand their land base to service their debt. Lenders, and 'unfettered capitalism' were blamed, as they had been after World War I, for a shift in government policy -- "a conspicuous pulling on the reins by the central bank" (Schumpeter, 1968: 236).

Grain exports recovered well after the Depression and WWII, but Canada's share of the international wheat trade slipped from around forty per cent prior to the Depression to around twenty per cent by the 1970s.<sup>162</sup> This decrease occurred despite sizeable but

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<sup>161</sup> The rate of inflation in the United States declined from 12.5 per cent to 4.4 per cent during Reagan's two term presidency.

<sup>162</sup> In the earlier period, Canada was also exporting substantial volumes of wheat flour.

irregular purchases of wheat by the U.S.S.R and the Peoples Republic of China (PRC). In the 1970s, when markets for other commodities produced in western Canada were booming, the railways had no incentive to allocate their scarce capacity through the Rocky Mountains to ‘un-remunerative’ grain traffic.

On several occasions, the demands placed on the grain handling and transportation system exceeded its ability to cope (Bennett, 2012: 7). Prairie farmers suffered when the demurrage charged by ships awaiting cargos at ports was deducted from Wheat Board revenue (Veeman & Veeman, 1984: 95). By 1977 only 32 per cent of the cost of moving grain by rail was covered by the statutory freight rate and 18 per cent by federal government branch line subsidies. The railways were forced to subsidise fifty per cent of the cost of moving grain at legislated rates or seek higher rates from other shippers in order to cross-subsidise grain-related losses. Either way, they were disinclined to make investments in grain-transportation.

Although the need for changes in the institutional environment was widely acknowledged, uncertainty over when changes might be initiated or the form they might eventually take also discouraged investment in grain handling facilities. Country elevators, which had been state-of-the art in the 1920s, remained in use with storage capacity augmented where necessary by building annexes (Earl, 2000: 177).

There was widespread appreciation that the GHTS was unfit for purpose, and that the medium and longer term prospects for the export-oriented prairie grain economy were bleak. However, views regarding the causes of those problems and the means by which they should be resolved became increasingly polarized.

## **2 Ideas**

### **2.1 International**

During this period, tension over agricultural trade at the international level affected decisions that were made regarding prairie agriculture. A subsidy war between the EU and the United States in the late 1970s and early 1980s ramped up farm programme spending in these jurisdictions and depressed prices. In June 1987, the G7 Summit meeting in Venice ended with a commitment to long term agricultural policy reform, the objective of which “... is to allow market signals to influence the orientation of agricultural production, by

way of a progressive and concerted reduction of agricultural support...”.<sup>163</sup> The following month, prior to the start of the GATT Uruguay Round, the Americans proposed the phasing out all agricultural subsidies by the year 2000 as an objective (Wilson, 1990: 243).

Rausser (1992) describes how international trade negotiations were used to exert pressure on the domestic legislative process to curb agriculture spending. The domestic consequences of trade concessions on agricultural commodities are more palatable when other sectors in the economy stand to gain from a more liberal trade environment. The United States used this strategy to create a more conducive environment for agricultural policy reform, paving the way for the Federal Agricultural Improvement and Reform (FAIR) Act of 1996.

In smaller countries, particularly those heavily dependent on trade in agricultural commodities, options were limited. Pressure to reduce costly agricultural support programmes has come from urban majorities in a number of instances, most notably in New Zealand (Scrimgeour & Pasour, 1996; Massey, 1995) and Australia (Harris and Rae, 2006). In Sweden, economists concerned about a looming crisis spearheaded a move towards less costly policies just before the country joined the EU (Lindberg, 2007; Vail, 1993; Rabinowicz, 2006). Elsewhere, agricultural intervention remained well entrenched. A recent study estimated that agricultural subsidies amount to a billion dollars a day (Petersen, 2009). Hence, the objective announced by the Reagan Administration in 1987 was not achieved and the cost of agricultural subsidies continued to climb. U.S. farm spending increased significantly after the 1996 Farm Programme ended, and wheat producers were among the chief beneficiaries.

Although high levels of government involvement in U.S. agriculture continued, a related sector of the U.S. economy underwent deregulation. The Staggers Act of 1980 deregulated U.S. railways. By the 1970s, the inflexibility of U.S. railway regulation was blamed for bringing the industry to the brink of disaster (Caves *et al*, 2010: 29). The Staggers Act was an attempt to avert that disaster, and is generally considered a success. Two aspects of the U.S. approach to deregulation are important in the context of the longstanding controversy in Canada over the rates charged for moving grain by rail. First, the U.S. legislation enjoyed a broad spectrum of political support. Second, it was a comprehensive attempt to

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<sup>163</sup> This surprisingly clear statement of purpose was qualified in the continuation of the sentence “giving consideration to social and other concerns, such as food security, environmental protection and overall employment”  
Available at: ( <http://www.g8.utoronto.ca/summit/1987venice/communique/agriculture.html> )

deregulate U.S. railways, and there have been no significant calls for re-regulation after the fact.

## 2.2 Domestic

In the mid-1980s, a weak economy, a sharp drop in business capital investment and high unemployment and interest rates revived the debate in Canada over stronger commercial ties with the United States. The Report of the Macdonald Royal Commission was one of the catalysts for this discussion.

This Royal Commission is regarded as an important turning point in Canadian economic policy. The objective of the suggested policy reorientation was to improve the economy's capacity to adapt, particularly to changes in technology and the international environment. The Report, which was widely viewed as neo-liberal in its orientation, suggested that greater reliance on market mechanisms, less government intervention, and a free-trade arrangement with the United States were the means to achieve this objective.<sup>164</sup> Similar ideas and other alternatives were circulating at the time, but it was pressure from the business elite under the auspices of the Business Council on National Issues that influenced the policy making process in this instance (Bradford, 1999: 37, 39). Bradford (1999: 39) refers to continental free trade as the 'Trojan Horse' for a more general restructuring of relations between the state and the economy. The Canada-U.S. Trade Agreement of 1989 and the North American Free Trade Agreement of 1994 put into effect recommendations made in the Commission's report. .

The Macdonald Commission's recommendations were prompted by dissatisfaction with the consequences of technocratic Keynesianism. In the policy paradigm vacuum that resulted, the Trudeau government resorted to *ad hoc* expedients. This void created opportunities for political entrepreneurs to champion novel policy options. Mandatory wage and price controls and the National Energy Policy of the early in the 1980s were examples.

*Ad hoc* expedients were very much in evidence in efforts to keep prairie grain moving to ports by rail. The MacPherson Royal Commission had recommended abandonment of the traditional regulatory framework, the setting of rates by competition, and subsidies as a

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<sup>164</sup> The Macdonald Commission also recommended welfare reform to improve efficiency of social programmes and an elected Senate to provide better regional representation in Parliament.

temporary expedient to ease the transition. The National Transportation Act of 1967 and amendments to the same act in 1987 took steps in that direction, but the grain sector was treated as a special case. The subsidies provided to keep the grain sector functioning were unpopular and controversial, and the ultimate objective of competitive rates was not taken seriously.

The precedent of subsidies provided to grain dependent branch lines became the basis for an interim solution: government funds were made available on an *ad hoc* basis to refurbish the aging fleet of wooden boxcars, purchase hopper cars and upgrade mainlines.<sup>165</sup> Political capital was generated at both ends of the process: fabrication of steel rails and railway cars provided employment to ailing Canadian industries in the Maritimes and Central Canada, and prairie farmers could be reminded that the government was spending taxpayers' money on their behalf. These stop-gap measures also helped to push any resolution of the underlying issue out into the future.

The split that had developed between farm groups demonstrated that the debate over the optimal institutional environment and hence the extent to which government should be involved was underway in prairie agriculture well before the Macdonald Commission. The attempt to create a prairie grain economy in the nineteenth century was beset by the same knowledge and incentive problems that generated unintended consequences from initiatives consistent with technological Keynesianism. In prairie agriculture, similar unintended consequences had been revealed over a much longer period of time.

By the 1970s, taxpayers were also beginning to question the federal government's financial support to prairie agriculture. The scale of agricultural operations on the prairies was part of the reason. When farming becomes big business involving costly equipment, and particularly when its output is destined primarily for the export market, it loses much of the sympathy urban residents typically feel for the sector. Such enterprises fall into quite a different category in the minds of poorly informed urbanites than the much smaller scale farms that predominate in the hinterlands of large Canadian cities.

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<sup>165</sup> The federal government purchased 14,000 hopper cars, the Alberta and Saskatchewan governments 2000 and the Wheat Board 4000.

### **3 Interests and Incentives**

#### **3.1 Prairie Farm Interest Groups**

Prairie farm groups were remarkably cohesive until the late Sixties. The National Farmers Union (NFU), which was dominated by the cooperative institutions, namely the Pools and UGG, was the national voice for prairie farmers. By the early 1980s, two farm interest groups with diametrically opposite views regarding what ailed prairie agriculture and the remedy required were already well-established – the Palliser Wheat Growers’ Association and the Canola Council. In the late 1980s, a new umbrella organisation, the Canadian Agricultural Policy Alliance (CAPA) was formed, based on the belief that “the majority of farmers would prefer to earn their income from the market place instead of the taxpayers of Canada.” (quoted in Wilson, 1990: 145).

As its name suggests, original members of the PWGA<sup>166</sup> were mostly from Palliser’s Triangle. In this part of the prairies, yields are frequently lower but the wheat produced has higher protein content, a desirable characteristic for certain end uses. The group formed as the result of objections to the Wheat Board’s practice of sharing the price premiums it obtained for high protein wheat with all producers in the ‘pool’. From their perspective, this amounted to discrimination. Criticism of other aspects of the Board’s role in marketing prairie grain followed. The PWGA also became involved in the statutory freight rate issue. Two of the founding members of the organization reportedly summarized the state of the prairie grain industry by the 1970s as:

We have a nonprofit-oriented marketing system; a loss-oriented transportation system; and a storage-oriented handling system; this combination of ingredients very successfully keeps our grain from falling into foreign hands (Carter and Loyns, 1996: 121).

The Canola Council’s predecessor, the Rapeseed Association, brought all facets of the industry together to promote the improvement of varieties, production and sales. As a result of these efforts, canola became a ‘Cinderella’ crop on the prairies, as it struggled against the institutions developed to support the production and sale of wheat. The different institutional trajectory that canola would follow was confirmed in 1973 after a plebiscite of growers rejected enlargement of the Wheat Board’s monopoly sales role to include rapeseed.

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<sup>166</sup> The Palliser Wheat Growers Association changed its name to Western Canadian Wheat Growers Association (WCWGA) in 1985.

The CAPA was a coalition of cattle producers and non-Board commodity groups such as the Canola Council. The decision by United Grain Growers, the original grain marketing cooperative on the prairies, to support the CAPA is particularly significant.<sup>167</sup> The CAPA was very focused on issues affecting prairie agriculture and became the main supporter of those who opposed the traditional ideology of the Pools. The “pro-market” side of this debate found a valuable ally in interest groups representing exporters of non-agricultural resources who also suffered from the lack of investment in railway capacity.

The divergence in the solutions proposed by farm organisations was highlighted in testimony before the Hall Royal Commission of 1977 on statutory freight rates for prairie grain. The more traditional farm groups endorsed solutions that involved more government involvement and spending. Organisations which espoused the view that government intervention created rather than solved farmers’ problems argued for the opposite course of action. These groups were outraged when the Hall Commission recommended that the ‘Crow’ rate be applied to even more products, that branch line abandonment be curbed and that the ‘government’ should subsidise the railways.

### **3.2 Political Environment**

Western alienation exerted influence on national politics in the 1920s, and the same phenomenon was repeated with the rise of another populist party with roots in Alberta. This was the Reform Party, led by Preston Manning, the son of long-time Alberta Social Credit Premier Ernest Manning. In this incarnation, the populist spark was ignited by the 1980 National Energy Program and by the preferential treatment given to Quebec, rather than the plight of prairie farmers.<sup>168</sup>

The Liberal government’s National Energy Policy imposed a federal tax on Alberta’s oil industry on the pretext of ‘protecting’ domestic consumers from ‘oil shocks’. Natural resources are a provincial responsibility, and the federal government’s effort to re-write the rules in the favour of the ‘East’ rekindled western alienation. It also underlined the

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<sup>167</sup> Before the CAPA came into existence, the national farm body which took a less radical position than the NFU was the Canadian Federation of Agriculture (CFA). However as a national organization, the CFA found itself having to bridge a fundamental divide among Canadian agricultural producers: those oriented towards the domestic market who were protected by supply management programmes (fluid milk, eggs, poultry) and those heavily reliant on foreign markets. The latter are concentrated on the prairies, the former in the more populous regions of the country.

<sup>168</sup> The benefits Conservative Prime Minister Brian Mulroney provided to Quebec were resented in the West. Notwithstanding his Irish heritage, which he parlayed into a cosy relationship with U.S. President Reagan, Mulroney was born in Quebec and is a bilingual Roman Catholic. In his pre-political career he was a lawyer and senior executive of the Iron Ore Company of Canada.



importance of property rights protection, an issue which became a major plank in the political platforms of the Reform Party and its successors.

The Reform Party won its first federal seat in a 1989 by-election, but when Canadians swept the Mulroney Conservatives out of office in 1993 the Reform party was a major beneficiary.<sup>169</sup> Like the Progressives seventy years earlier, the Reform Party faced the challenge of extending its influence beyond the West. Its fiscal conservatism and the targeting of generous budgets for welfare and multiculturalism broadened the party's appeal in rural Ontario, recreating the alliance developed in the 1920s.

The rise of the Reform Party exerted considerable influence on the Liberal governments of Jean Chretien (1993-2003) and Paul Martin (2003-2006) and on the Conservative party platform. As Reform Party MPs, Stephen Harper (subsequently Conservative Prime Minister) and Jason Kenny, (who had previously served as President of the Canadian Taxpayers Federation), were among those who kept the focus on government spending, supporting Finance Minister Paul Martin's efforts to trim the Federal deficit in the mid-1990s. Until then, efforts by the two mainstream parties to trim spending had been motivated by a desire to reallocate those savings. As a result, Canada's debt to GDP ratio continued to grow.<sup>170</sup> In the early 1990s, international ratings agencies downgraded Canadian debt securities and Canada was compared unfavourably with heavily indebted 'third world' countries.

Harper left the Reform Party in 1997 when he felt its populist leanings limited the appeal of the Party to the 'religious right'.<sup>171</sup> His assessment proved accurate as the Reform Party and its off-shoots floundered. He joined the National Citizen's Coalition (NCC) – a lobby group campaigning for lower taxes and government spending cuts – ultimately becoming its President.<sup>172</sup> While there, he took a personal interest in the Wheat Board because it stood out as an economic issue arising from inadequate protection of property rights.<sup>173</sup>

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<sup>169</sup> Mulroney's free trade deals were unpopular and he resigned amid allegations of corruption. The Conservative party contested the next election with Kim Campbell as leader. It entered the election with a majority government and 151 seats and emerged with two.

<sup>170</sup> During the Trudeau years the federal debt to GDP ratio rose from 24 to 46 per cent.

<sup>171</sup> Preston Manning referred frequently to his father's success in purging the Alberta Social Credit Party of anti-Semitism during his twenty-five years as Premier as a warning to extremists the party attracted in its early years.

<sup>172</sup> The motto of the NCC is "More Freedom through Less Government".

<sup>173</sup> The NCC had supported some of the court cases which pitted prairie farmers against the CWB because the question hinged on definition and enforcement of property rights.

The Reform Party transformed itself into the Canadian Alliance and in 2002 Stephen Harper became its leader. The following year he engineered a merger with the rump of the Progressive Conservative Party.<sup>174</sup> Harper's initial focus on economic issues appealed to the self-interest of a broad spectrum of the population. He became Prime Minister in 2006 when the Conservatives formed a minority government.

At the provincial level, yet another new party emerged during this period. The Saskatchewan Party was formed in 1997 to create a united conservative alternative to the NDP.<sup>175</sup> It drew strong support initially from rural constituencies and made sufficient inroads in urban ridings necessary to form the provincial government only in 2007. It has since used its mandate to support private sector development in the province.<sup>176</sup>

## **4 Interventions**

### **4.1 Elimination of the Statutory 'Crow Rate'**

The low freight rates prairie farmers paid to have grain moved to ports by railway were the first of the institutional arrangements tackled by the federal government. When the 'Crow Rate' was made the statutory rate covering all grain shipments from the prairies by rail in the 1920s it was regarded as a major victory by prairie farm organisations. The unintended consequences of that legislation were widely acknowledged by the 1970s, and the controversy which surrounded efforts to legislate the rate out of existence centred largely on who should pay the rates required to efficiently move grain by rail. The convoluted process which ended up with the rates required is a fascinating example of political manoeuvring inside government, among prairie farm organisations, and among grain growers and livestock producers, food processors and those shipping other commodities by rail (Kroeger, 2009).

The first step toward dismantling the Crow Rate was championed by the Minister and Deputy Minister of Transport. In 1980, the Crow Rate was the chief budget headache for

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<sup>174</sup> Harper led the reconstituted Conservative party until it was defeated in the 2015 federal election.

<sup>175</sup> From 1982 to 1991 the Conservatives under University of Saskatchewan Agricultural Economist Grant Devine were in power in Saskatchewan. The government was plagued by scandals and allegations of mismanagement and the Conservative party went dormant in the province after being thrown out of office.

<sup>176</sup> The current senior public servant in the province, the Deputy Minister to the Premier is the former Deputy Minister of Agriculture and former Executive Director of the Western Canadian Wheat Growers, Alanna Koch.

the Department of Transportation.<sup>177</sup> Transport is a top tier Ministry in Canada, with considerably more clout and a much broader constituency than Agriculture.

**Table 12 Eliminating the Statutory ‘Crow Rate’**

<ul style="list-style-type: none"> <li>• 1974-82 – American consultant Carl Snavely conducts a series of studies to determine the magnitude of the ‘Crow Gap’. He admitted he found it puzzling that in Canada a freight rate could be considered a constitutional right.</li> </ul>
<ul style="list-style-type: none"> <li>• 1977 – Hall Royal Commission recommends that no change be made to the Crow Rate but that the list of commodities covered be expanded and the federal government should subsidise the cost borne by the railways.</li> </ul>
<ul style="list-style-type: none"> <li>• 1983 - Western Grain Transportation Act (WGTA) institutionalized the payment of a ‘Crow Benefit’ to the railways allowing shipping rates to increase, but never more than 10% of the world price for grain.</li> </ul>
<ul style="list-style-type: none"> <li>• 1995 - Repeal of the WGTA and the end of Crow Benefit payments. Producers to pay full rail freight charges up to a maximum in effect until 2001.</li> </ul>
<ul style="list-style-type: none"> <li>• 1995 - Western Grain Transition Payment Program - provided \$1.6 billion payments to farmers over 3 year period to transition them away from subsidized shipping and to compensate for the expected reduction in the value of agricultural land.</li> </ul>
<ul style="list-style-type: none"> <li>• 1996 - Canadian Transportation Act (CTA) sought to provide a degree of shipper protection. Measures included a rate cap and level of service requirements.</li> </ul>
<ul style="list-style-type: none"> <li>• 2001 – Amendments to the CTA included replacement of the maximum rate scale for grain shipments with caps on the total annual revenue that each of CN and CP railway can earn from moving regulated grain and the appointment of an independent Grain Monitor to keep track of system performance.</li> </ul>

The Deputy Minister, Arthur Kroeger, had been born in rural Alberta and therefore understood the opposition any attempt to change the statutory ‘Crow Rate’ would face. The Minister, Jean-Luc Pepin was from Quebec. He had, however, been Minister of Industry Trade and Commerce and Minister Responsible for the Canadian Wheat Board simultaneously in a previous Liberal government. Kroeger subsequently wrote an illuminating book on the subject from the perspective of someone inside the ‘black box’ of policy change (2009; Stambrook, 2011).

Pepin and Kroeger personally undertook to consult with stakeholders and emphasised the importance of a “made in western Canada” solution to the Crow Rate issue (Kroeger, 2009: 109). This contrasted sharply with the 1980 National Energy Programme (NEP), which was imposed with little warning and ignited a fire-storm of protest and even the beginnings of a western separatist movement (Pratt, 1981) Ironically, it was the short-term revenue

<sup>177</sup> Its second biggest headache was VIA Rail, the Crown Corporation which obligingly relieved the two railways of operating passenger services in 1977.

windfall from the NEP which provided the funding necessary to finance the Crow Benefit payments to the railways under the Western Grain Transportation Act (WGTA) (Kroeger, 2009: 212).

#### 4.2 Interventions Related to Railway Performance

The Duff Royal Commission during the Depression of the 1930s had rejected a proposal from the head of the CPR that the two railways be jointly managed as a way of eliminating redundancies and waste. This offer was not resurrected after the Depression. Prior to the privatisation of CN in 1995, the two railways had discussed various opportunities for collaboration motivated by the acknowledged underperformance of their operations in *eastern* Canada (Bruce 1997). The privatisation of CN was also spearheaded by political entrepreneurs who went on to run the railway after it was privatized.

**Table 13 Interventions Affecting the Efficiency of Grain Movement by Rail**

<ul style="list-style-type: none"> <li>• 1970s – subsidised various railway capital cost programmes as partial compensation for mounting grain transportation losses (‘Crow Gap’). Federal and provincial governments and the Wheat Board purchase hopper cars to replace the dwindling number of wooden box cars in the railcar fleet. The federal government funds branch line rehabilitation programmes and upgrades to railway main lines (Veeman &amp; Veeman, 1984: 95-96; Earl, 2011).</li> </ul>
<ul style="list-style-type: none"> <li>• 1979 - Created the Grain Transportation Agency to manage the hopper car fleet.</li> </ul>
<ul style="list-style-type: none"> <li>• 1995 - Canadian National Railway privatised. Terminated the federal government’s liability for operational losses.</li> </ul>
<ul style="list-style-type: none"> <li>• 1995 – GTA disbanded and allocation of railcar fleet taken over by a body representing industry participants. Car-pooling ends, paving the way for rapid adoption of unit train movement for grain.</li> </ul>
<ul style="list-style-type: none"> <li>• 1996 – Canada Transportation Act allocates responsibility for setting rates charged for movement of grain to the Canadian Transportation Agency</li> </ul>
<ul style="list-style-type: none"> <li>• 1997 – Omnitrax, a U.S. based short-line railway company purchases the Hudson’s Bay Railway from CN, and the Port of Churchill from the federal government.</li> </ul>
<ul style="list-style-type: none"> <li>• 2001 – Amendments to the Canada Transportation Act largely ignore recommendations made by a 1998 Review conducted by Willard Estey for efficiency improvements in grain transportation by rail.</li> </ul>
<ul style="list-style-type: none"> <li>• 2008 - 2013 – Amendments to the Canadian Transportation Act reverse the trend towards competitive rate-making initiated by the National Transportation Act of 1967 and give grain shippers additional powers over the level of service provided by railways (Caves, 2010: 52).</li> </ul>
<ul style="list-style-type: none"> <li>• 2014 - Fair Rail for Grain Act. Regarded by some as ‘re-regulation’ of railways prompted by dissatisfaction over insufficient surge capacity to move the bumper harvest of 2013.</li> </ul>
<ul style="list-style-type: none"> <li>• 2016 – Omnitrax announces its intention to discontinue service on the Hudson’s Bay Railway and close the Port of Churchill.</li> </ul>

### 4.3 Grain Marketing

Stephen Harper was personally responsible for the decision to end the Wheat Board's 'monopoly' over the sale of prairie wheat.<sup>178</sup> He made his intentions clear when the Conservatives formed a minority government in 2006, but the necessary legislation was introduced only after the Conservatives were elected with a majority government in 2011.<sup>179</sup> Again, the contrast with the process used to start the reform of the Crow Rate is stark. The attitude of farmers' organisations to the Wheat Board at the time reflected the deep division that had developed on the prairies over the question of whether government involvement was helpful or a hindrance.

**Table 14 Interventions Affecting the Marketing of Prairie Grain**

<ul style="list-style-type: none"><li>• 1970 - LIFT (Lower Inventories for Tomorrow) programme provided incentives for farmers to grow crops other than wheat or take land out of production when carryover stocks exceeded 27 million tonnes. The result was immediate; seeded wheat acreage dropped by one-half in that year.</li></ul>
<ul style="list-style-type: none"><li>• 1971 - A two-price wheat policy, which set a floor and a ceiling price for domestic millers, was introduced.</li></ul>
<ul style="list-style-type: none"><li>• 1974 - A revised domestic feed grain policy removed responsibility for interprovincial movement of feed grain within the prairies from the Wheat Board. Farmers or the private grain trade were allowed to sell feed grains within the region. As of the 1974-75 crop year, the CWB only handled feed grains exported from the region.</li></ul>
<ul style="list-style-type: none"><li>• 1989 - Oats removed from the jurisdiction of the Canadian Wheat Board.</li></ul>
<ul style="list-style-type: none"><li>• 2011 - Marketing Freedom for Grain Farmers Act. Legislation to eliminate the Wheat Board's status as the 'single desk' seller of prairie wheat effective Aug. 1, 2012 passed by the federal Conservative government.</li></ul>

## **5 Consequences**

### **5.1 Freight Rates**

By the 1970s, rate regulation in both the United States and Canada had discouraged the railways from maintaining or upgrading their infrastructure, resulting in severe adverse consequences for those relying on their services. The U.S. chose to address the problem swiftly with the passage of the Staggers Rail Act of 1980. This Act deregulated U.S. railways, providing significant benefits for both railroads and their users. Canada, by contrast, decided to 're-regulate' rather than deregulate.

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<sup>178</sup> Some (e.g. Swanson & Venema, 2006) maintain that the term 'monopoly' is misapplied to the wheat board and 'monopsony' should be used instead. It is the only buyer of prairie wheat but one of many sellers internationally. The more common term is used here. The controversy over who 'owns' the wheat the CWB sells is the property rights issue at the core of the dispute over the Wheat Board.

<sup>179</sup> The election occurred because the Harper government lost a no-confidence motion for being in contempt of parliament, the first time this had happened in the Commonwealth. The 2011 election was also noteworthy because the NDP became the official opposition for the first time.

The two domestic arguments for tackling the politically sensitive Crow rate were (1) to address the dysfunctional consequences of a rate fixed at nineteenth century levels and (2) the need to curb *ad hoc* government spending on grain transportation. However, there was also a concern that agricultural programmes would be under scrutiny at future international trade negotiations, and Canada's position would be enhanced if steps were taken in advance to address the issue.

The main argument for dispensing with the Crow Rate was to remove distortions attributable to the artificially low rates. The prairie livestock feeding industry and processing industries were expected to benefit. The prices of feed grains and raw materials available to livestock feeding and processing industries were increased by the value of the implicit subsidy. The Quaker Oats Company's decision to build its processing plant in Peterborough, ON and not on the prairies was often cited as an example of the detrimental effect of the Crow rate on value-added processing on the prairies.

The first step towards addressing the growing cost of subsidizing the railways was the 1984 Western Grain Transportation Act (WGTA). To compensate the railways for moving grain, as recommended by the MacPherson Commission, the 'Crow Gap' became the 'Crow Benefit'. The main controversy with the initial modification was whether to pay the 'Crow Benefit' to farmers or the railways. Providing the benefit to the farmer and allowing him/her to make decisions based on real transportation prices would have been the ideal situation. However the 'pay the farmer' recommendation was vociferously opposed by the Wheat Pools, and by Quebec livestock producers who feared direct payments to farmers would result in a sharp drop in feed grain prices, making the prairie livestock industry more competitive. Because prairie feed grain prices did not fall when the decision was taken to 'pay-the-railways', each of the Prairie Provinces provided feed grain users with subsidies as compensation. All of these programmes were cancelled in the mid-1990s due to the financial burden they imposed (Kraft and Dorion, 2000). The railways did, however, proceed with investment projects which had been on hold pending resolution of the Crow Rate issue and were allowed to abandon some 'grain dependent branch lines'.

The WGTA shared the burden of subsequent inflation-related increases in the 'Crow Benefit' between the federal government and grain producers. As a result, the government's share of payments to the railways crept up over time. By 1992 it was 720 million CDN. In 1993 the government faced a deficit of 43 billion CDN and announced 25 billion CDN of expenditure reductions. The Crow Benefit paid to the railways was unilaterally cut by 15

per cent in 1993. In 1995, the WGTA was then repealed to comply with WTO requirements that agricultural programmes that supported producer prices be reduced. The government paid prairie grain growers 1.6 billion CDN to compensate them for the reduction in land values anticipated once the Crow Benefit disappeared. The Canada Transportation Act replaced the WGTA in 1996. Its main provision was a cap imposed on the rates the railways could charge for moving grain, in other words a new Crow Rate. The stated intent of the 'rate cap' was to benefit shippers.

In 1998, Transport Canada conducted a Grain Handling and Transportation Review (Estey, 1998) which recommended that the rate cap be repealed on the grounds that it prevented the railways from passing along potential efficiency savings to shippers. When the CTA was next amended in 2001 this recommendation was ignored. However, the rate cap was replaced with a revenue cap, which had the same effect but was even more complicated to calculate and enforce.<sup>180</sup>

The underlying problem hinges on the fact that the regulations consist of a mathematical formula, which is inflexible (Bennett, 2012: 17). This rigidity is complicated by performance guarantees and the legacy of the equity principle which precludes efficiency. The logistic options involved are simply too complex to be incorporated in legislation. All these problems were demonstrated during the winter of 2013-2014 when bad weather, in combination with a bumper crop of grain on the prairies, led to complaints about railway service. The federal government's response was "Fair Rail for Grain Farmers" Act which issued directives specifying the amount of grain to be moved each week (Prentice and Parsons, 2015: 13). Prentice and Parsons (2015: 13-14) conclude that:

...the efforts of politicians to respond in the best interests of farmers have created five negative outcomes. First, western Canadian farmers have lost market share, reputation and consequently reduced incomes because the GHTS is inefficient. Second, the system is plagued with chronic administrative rationing. Third, delays in investment to modernize the GHTS mean that supply chain costs remain higher longer and are passed forward to the customer, or back to the farm level. Fourth, to the degree that grain transportation does not pay its full costs, other commodity shippers must. Therefore the revenue cap is like an export tax on all other non-agricultural products. Finally, the Revenue Cap discourages any efforts to prepare for the next super surge of demand by grain shippers, while the new measures that have been implemented do little or nothing to ameliorate the surge.

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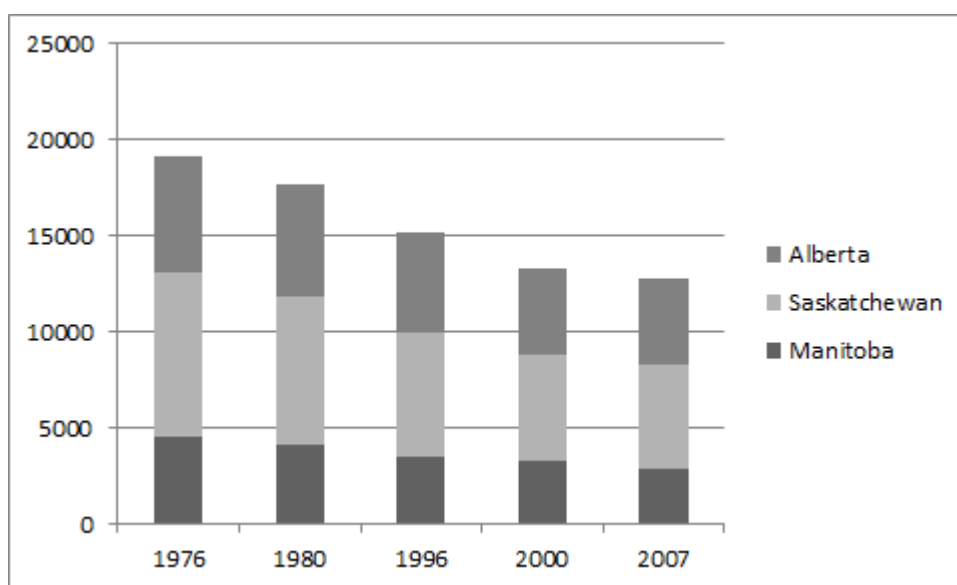
<sup>180</sup> Bennett (2012) and Prentice and Parsons (2015) enumerate the many shortcomings of the current state of grain freight regulation in western Canada in detail.

## 5.2 Railways

The privatisation of CN shook up both Canadian railways. After a long period of coexistence under the umbrella of rate regulation the two railways again embarked on a spate of cost-cutting measures. The cost base of CN was substantially reduced.

Investment in railway infrastructure increased substantially. CP had faced obstacles to raising capital while the Crow Rate was still in effect. Once the WGTA legislation was passed, it was able to raise 600 million CDN to build a second tunnel under Mount Macdonald in the Selkirk Mountains, its largest construction project since the transcontinental mainline was completed in 1885.<sup>181</sup> This tunnel removed a serious bottleneck for grain shipments destined for Asian markets. On the prairies, the two major railways were allowed to abandon a limited number of grain dependent branch lines.

Figure 19 Canadian Railway Miles Operated on the Prairies 1976 to 2007



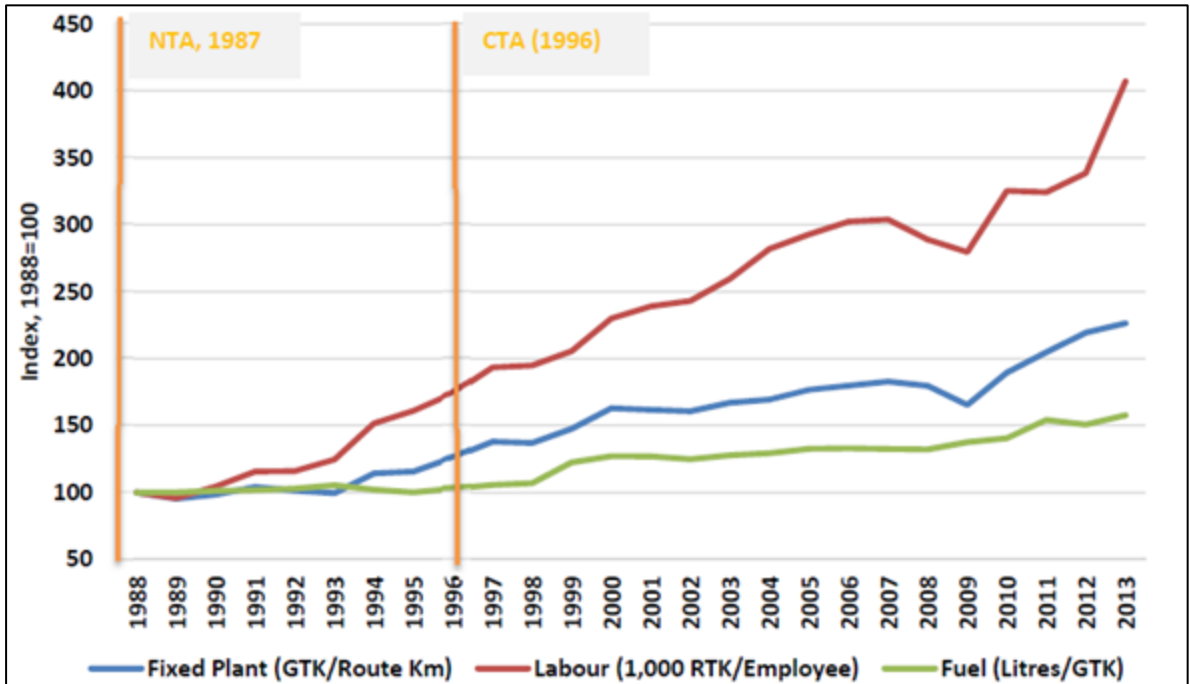
Source: Government of Canada Grain Monitoring Program

<http://www.quorumcorp.net/Downloads/SupplementalReports/TraffMktLogChanges1980-2010.pdf>

<sup>181</sup> Once again this indicates the longer term consequences of the decision to route the original transcontinental line across the southern prairies and through the Kicking Horse and Rogers passes.



Figure 20 Canadian Railway Productivity Indices Canadian Operations (1980 = 100)



Source: Railway Association of Canada, CPCS calculations

[http://www.railcan.ca/assets/images/CTA\\_Review/Submission\\_2/Appendix\\_B\\_-\\_Evolution\\_of\\_Canadian\\_Rail\\_Regulation\\_and\\_Industry\\_Performance.pdf](http://www.railcan.ca/assets/images/CTA_Review/Submission_2/Appendix_B_-_Evolution_of_Canadian_Rail_Regulation_and_Industry_Performance.pdf)

In Canada, seventy per cent of the hopper car fleet used to transport grain is still owned by government (provincial and federal), a legacy of *ad hoc* investments to keep the system going pending resolution of the Crow Rate issue. This makes maintenance and eventually the replacement of the fleet -- a cost that was estimated at 1.4 billion CDN in 1988 -- a public fiscal obligation (Parsons and Wilson, 1999: 73). This fleet is much older than those used by U.S. railways. CP Rail has identified replacing the fleet with new shorter, higher capacity hopper cars as a key opportunity for improving network capacity. However, government ownership of the cars and the negative effects of the revenue cap mean that rail car capacity remains a serious outstanding issue.

The most important consequence of the privatisation of CN was that it no longer set the efficiency standard for the Canadian rail transportation industry. For an extended period of time in the wake of privatisation, CN was able to reduce its operating costs by an average of 15 million dollars *a month* (Bruce, 1997). Efforts to improve productivity meant technical change returned to the portion of the Canadian railway sector devoted to handling grain.

The CPR had long been a participant in the U.S. market, and CN quickly followed suit. CN agreed to a merger with the U.S. railway, Burlington Northern and Santa Fe (BNSF) railway in 1999, but this was blocked by the U.S. Surface Transportation Board. CN did subsequently purchase the Illinois Central railway which extended its grain transporting network down the Mississippi Valley as far as the Gulf Coast. Reliance on east-west transportation within Canada became a thing of the past.

One of the consequences of deregulation of United States railways, the re-regulation of Canada's two railways, freer trade and the elimination of the Wheat Board's single desk selling mandate is that prairie grain shippers now have three railway options once grain is loaded on a lorry: the CNR or CPR in Canada and the BNSF which runs just south of the U.S. border.<sup>182</sup> This is ironic given that preventing U.S. railways from siphoning off 'Canadian trade' was one of the original arguments for building the CPR.

### **5.3 Grain Handling**

When attempts by the Saskatchewan Wheat Pool (SWP) to block modifications of grain freight rates failed, competition among grain handling companies became a very real possibility. Massive investment was required to bring the grain handling and transportation infrastructure up to date. Large numbers of wooden elevators needed to be replaced with a network of strategically placed inland grain terminals. This created two problems. First of all, when cooperative grain companies were formed, they depended on capital raised locally to fund elevator. Pool elevators were owned by pool 'locals' and closing them was unpopular and probably illegal. Second, it is difficult for cooperatives to obtain the large capital infusions required to upgrade facilities.

There was a rapid and complete change in the prairie landscape with the switch from wooden elevators to concrete inland terminals. The first inland terminal was built in Weyburn, SK by a consortium of farmers in the late 1970s (Driver, 2001). The Weyburn Inland Terminal (WIT) provided 'condominium' storage for individual farmers, cleaned grain to a high standard before shipment by rail and provided the ability to load unit trains. By 2005, the Saskatchewan Wheat Pool was operating forty-seven terminals with a

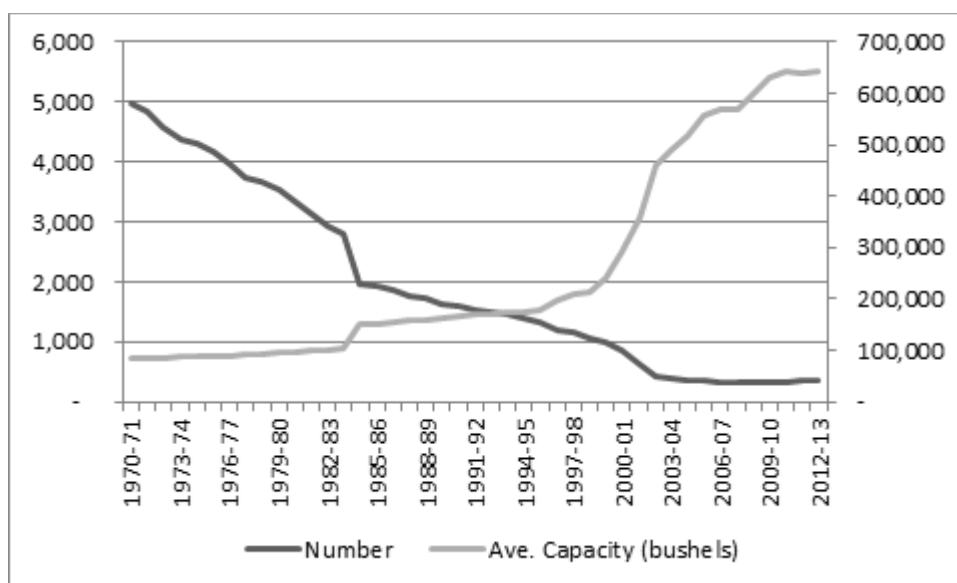
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<sup>182</sup> BNSF (Burlington Northern and Santa Fe) railway is a private company owned by Warren Buffet's Berkshire Hathaway Group. Its transcontinental line closest to the Canadian border is the original Great Northern Railway originally constructed by J.J. Hill, the Canadian-born partner of Donald Smith and Noman Kittson who was also involved in early stages of CPR construction.

combined handling capacity higher than the 500 country elevators it had in operation a decade earlier (Kroeger, 2009: 203).

Pool locals mounted a number of legal challenges to thwart the closure of locally-owned elevators as the result of head office decisions. In one case, the ultimately unsuccessful legal challenge went beyond the Supreme Court to the Governor General.<sup>183</sup> The cooperative form of organisation limits access to capital, and all the cooperative grain handling companies needed funds for the long overdue investment in modern grain handling facilities. To solve this problem the Saskatchewan Wheat Pool became a public company in the late 1990s. In 2007 it merged with Agricore United and the joint entity adopted the name Viterra. Agricore United itself was the result of a merger in 2001 between Agricore Cooperative Limited and UGG. Agricore Cooperative Limited came into being in 1998 when the Alberta Wheat Pool and Manitoba Pool Elevators merged.<sup>184</sup> In an extremely short space of time, all the cooperative grain companies disappeared and formed a single private firm. By the time steps to deal with the monopoly clause in the Wheat Board Act were announced, the Board's staunchest ally – the prairie pools – were no more.

Figure 21 Canadian Prairie Country Grain Elevators: Number & Average Capacity 1970- 2012

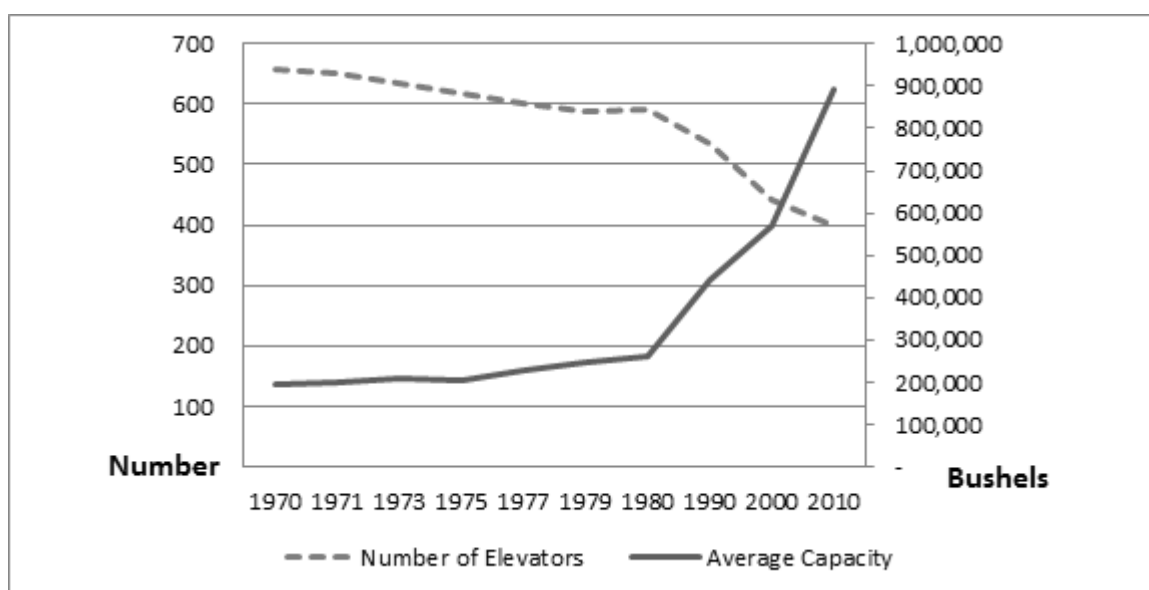


Source: Chart by Author, data from Canadian Grains Commission: Grain Elevators in Canada 2013  
<http://www.grainscanada.gc.ca/statistics-statistiques/geic-sgc/2013-08-01.pdf>

<sup>183</sup> At the time, the Governor General was Adrienne Clarkson, whose background was that of an Ontario-based author, TV personality and broadcaster.

<sup>184</sup> In 1997 these two companies made a hostile bid for UGG, prompting UGG to partner with a U.S.-based 'White Knight', Archer-Daniels-Midland Co.

Figure 22 North Dakota Country Grain Elevators: Number and Average Capacity 1970- 2012



Source: Chart by Author, data from North Dakota Grain Dealers Association cited by Ming & Wilson (1983) in *The Evolving Country Grain Marketing System in North Dakota* <http://ageconsearch.umn.edu/bitstream/23381/1/aer169.pdf> and from <http://www.ndgda.org/history.html>

## 5.4 Grain Marketing

The process of changing the Wheat Board received considerable impetus from the 1970 plebiscite on whether or not to include canola under the Board's jurisdiction. Farmers voted against the proposal. This encouraged efforts involving all participants under the umbrella of the Canola Council to expand the market and hence production which served as an example that would be repeated with other specialty crops. Canola became known as Canada's 'Cinderella crop' when these efforts met with success, and offered a route whereby farmers could 'exit' from, or at least reduce, Wheat Board influence on their business decisions.

Prior to 1974, the Wheat Board was able to buy grain in one province and sell it in another at a higher price. Prairie farmers were prevented from selling feed grains if they had transported them across provincial boundaries. Such a prohibition was widely regarded as ridiculous and difficult to enforce, but a few prairie farmers were prosecuted nonetheless. The Wheat Board also sold feed barley produced on the prairies in Ontario and Quebec under a formula designed to make it a competitive alternative to corn imported from the United States, but the private grain trade was also allowed to serve this market. As increasing amounts of feed grain were grown in central and Maritime provinces the Wheat Board lost interest in this market. Feed grains shipped east for use by eastern livestock

producers received a subsidy under the Feed Freight Assistance Program, wartime legislation to encourage livestock fattening in central Canada. This legislation was phased out beginning in 1995.

In 1989, the Conservative Minister Responsible for the Wheat Board, the Hon. Charlie Mayer removed oats from the Board's responsibility (Mayer, 2011).<sup>185</sup> Exports soared, local milling capacity was installed and oats became another attractive alternative to Board crops.

In 1993, Mayer initiated a trial during which producers were given the option of marketing their feed barley in the U.S without going through the CWB. The CWB had never sold more than 0.47 million metric tonnes (mmt) per annum of feed barley to the U.S. but in the 40 day trial period exports jumped to somewhere between 0.5 and 1.0 mmt. (Johnson & Wilson, 1994). The pilot ended when the Wheat Pools mounted a court challenge after the Conservatives lost the federal election.<sup>186</sup> To its credit, the Board did continue to sell barley into the U.S. Pacific Northwest, a market they had previously claimed did not exist (Carter & Loyns, 1999: 99).

A number of events in the 1990s increased dissatisfaction with the Wheat Board. First, the Board ran a deficit of 743 million dollars CDN for the wheat and durum pools for the 1990 crop which by law had to be paid out of public funds. Next, innovative farmers in search of ways to improve their cash flow tried to supply local processors directly but the Wheat Board insisted that processors purchase all prairie grown raw materials at the Lakehead price (i.e. the price paid after transporting it from the prairies to an export position). Third, a growing number of farmers challenged the Board's monopoly by moving lorry loads of grain into the United States. These protests caught the attention of the Canadian public, the National Citizens Coalition (NCC) and U.S. farmers and politicians.

An organisation calling itself Farmers for Justice (FFJ) organized large convoys of lorries to transport grain into the United States as acts of civil disobedience and posted signs at

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<sup>185</sup> In this chapter describing how oats ceased to be a Board grain, Mayer quotes a 'senior executive for a major Canadian food processing company as saying "Charlie, I would sooner do business with the mafia than the Canadian Wheat Board" (2011: 23).

<sup>186</sup> Mayer also tabled a proposal to change the WGTA so that the Crow Benefit would go directly to producers, but this proposal was not acted upon when the new Liberal government took office and Ralph Goodale, a Saskatchewan MP who had opposed changes to the Crow Rate as leader of the Provincial Liberal Party, was appointed federal Minister of Agriculture.

border crossings and along major highways that read: “Welcome to Canada: the Only Free Country in the World that Imprisons Farmers for Selling their own Grain.”<sup>187</sup>

The campaign against the Wheat Board focused attention on the issue of property rights. Wheat Board practices implied that farmers did not own the grain they produced, as they had no alternative but to sell it to the Board. The Wheat Board’s compulsory powers were granted under the authority of the War Measures Act in 1943. The objectives at the time were to prevent any dramatic increase in the price at which wheat was contributed to the war effort and to supply grain to help the rebuilding of Europe after the war. However, the War Measures Act was repealed in 1947, and the issue of property rights as it applied to grain grown on the prairies has been uncertain ever since.

The Wheat Board’s position was challenged as an infringement of rights protected under the Charter of Rights and Freedoms in 1996. The ‘Charter Challenge’ claimed farmers in the Wheat Board’s designated area were denied rights taken for granted by farmers elsewhere in the country. The judge in that case ruled that property and commercial rights had been intentionally excluded from ‘charter rights’ -- at the insistence of the NDP.

Scrutiny of the Board’s sales practices raised questions about its diligence in pursuing new markets. Producer efforts to identify canola markets led to concerns that Board salespeople regarded themselves more as diplomats pursuing large volume sales than grain traders. The brief experiment with a dual market for barley raised issues about whether or not the Board maximised sales revenue. Revenue is price times volume, and lack of sales volume is particularly damaging from the grain grower’s perspective because it severely limited cash flow. The evidence was inconclusive.

Changes to the Wheat Board’s mandate, announced in 2011 when the Conservative government of Stephen Harper government obtained its first majority in parliament, were extremely controversial on the Prairies. The proposed changes removed the requirement that prairie grain producers sell their wheat and barley through the Board and restored the Wheat Board to the voluntary status it operated under between 1935 and 1943. The Board briefly operated as a marketing agency, depending on the other grain companies (now also its competitors) to handle ‘Board’ grain.

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<sup>187</sup> In one high profile case, farmer Andy McMechan was held in jail for a hundred and fifty-five days. His neighbours kept his farm running in his absence.

There is no doubt that the decision to amend the Wheat Board Act was consistent with the view Harper brought with him when he returned to politics from his stint at the NCC. Opponents would no doubt consider it an ideological decision. The strategy adopted by the Harper government involved much less consultation than was the case with the Liberal government's original approach regarding the Crow Rate. This was inevitably unpopular with opponents of the change.

In July 2015, the purchase of the Canadian Wheat Board by a joint venture between Bunge North America and the Saudi Agricultural and Livestock Investment Corporation SALIC was announced.<sup>188</sup> This means that the new venture will have grain handling capacity of its own in the region.

### **5.5 Agricultural Production and Land Use**

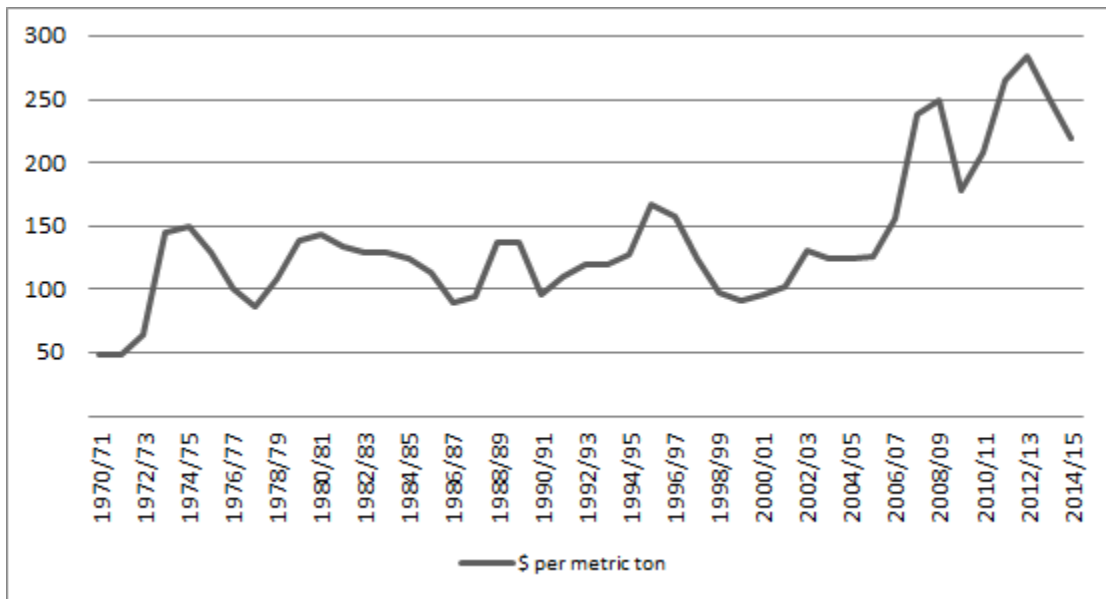
The extent to which the changes that have occurred are a direct consequence of steps taken to reduce the involvement of the federal government in prairie agriculture is difficult to assess, particularly the very recent changes in the role of the Wheat Board. The radical restructuring of prairie agriculture did not happen overnight, it was complicated, and it is not yet complete. The prairie agricultural economy went through a very difficult adjustment process after the WGTA was repealed in 1995. Elimination of the Crow Benefit coincided with relatively high commodity prices, but the first five years of the twenty-first century again brought lower commodity prices and a series of unusually dry summers. Prairie farmers generated no net income from commodity sales during those years, and what net income they did obtain came from government programmes (Furtan, 2005; Kroeger, 2009: 204-5).

Since 2006, commodity prices have increased. They were particularly high in 2008, just before the turmoil in North American financial markets began. Subsidised ethanol programmes in the U.S. which absorb a significant proportion of U. S. corn production have affected the feed grain market, but have had little impact on food grains and oilseeds. The Canadian economy as a whole, and prairie agriculture in particular, is a beneficiary of increased trade with China and other Pacific Rim countries as they develop and their populations increasingly exhibit middle class income and expenditure patterns.

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<sup>188</sup> <https://www.bungenorthamerica.com/news/65-g3-global-grain-group-completes-investment-in-cwb>

Figure 23 World Wheat Prices

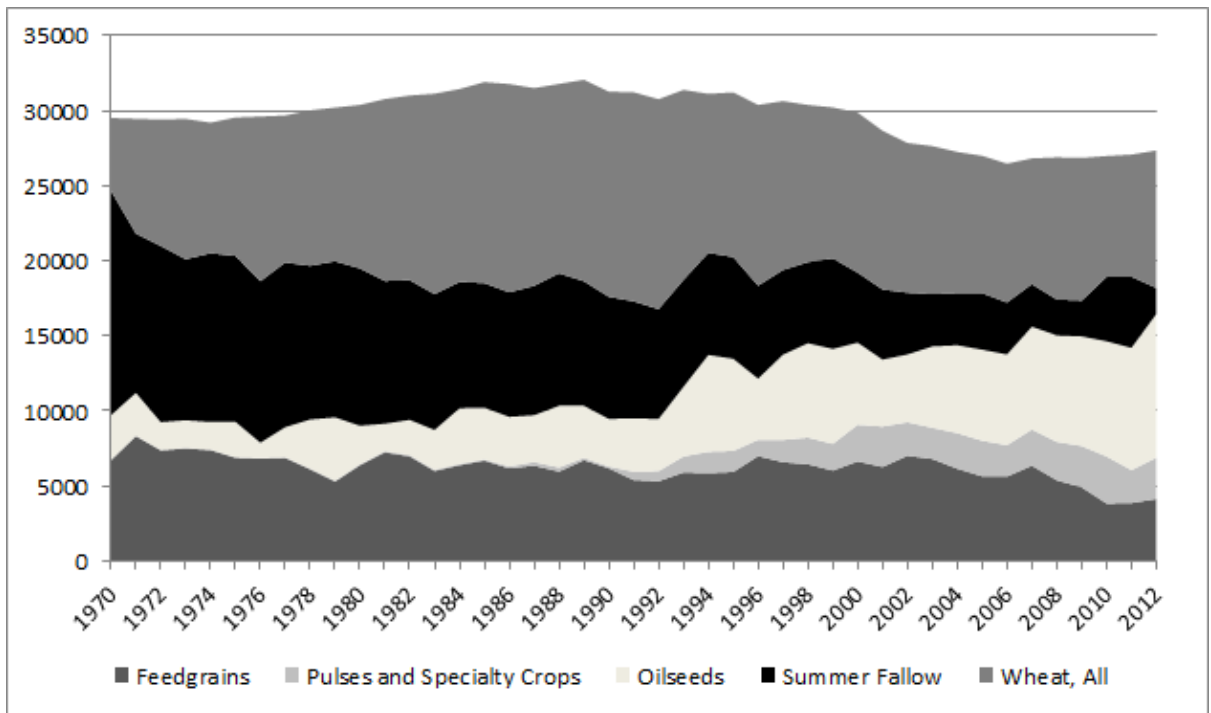


Source: Chart by Author, data from USDA Table 20 Wheat Prices  
<http://www.ers.usda.gov/data-products/wheat-data.aspx>

It was only when prairie farmers started to pay compensatory rates for grain shipped out of the region by rail in 1995 that changes in the structure of prairie agriculture began in earnest. Prior to that date the main incentive to grow non-Board commodities was to obtain cash-flow when shipment of commodities through the Board was penalised by inefficiencies in the GHTS, and to avoid the long wait for their final payment. Higher freight costs encouraged the shift to specialty crops because shipping charges were smaller relative to the value of the commodity. Prices for unprocessed grain on the prairies fell as the cost to ship it out of the region increased. Barley exports dropped sharply as more was fed to cattle on the prairies, and in several years the prairies were a feed grain deficit region. Wheat acreage fell and canola became the most important crop in terms of sales value. Most significantly, the acreage planted to crops which had not been eligible for the Crow Rate more than doubled. Crops such as canary seed, lentils, peas, mustard seed, beans and chick peas became important sources of income for prairie farmers. A large proportion of pulse production is concentrated in Saskatchewan and marketed by Alliance Grain Traders. The original business, Saskcan Pulse Trading, founded only in 2001 by Murad Al-Katib, now operates facilities in Canada, the United States, South Africa, Australia, China and Turkey. It claims to handle between 30 and 40 per cent of all internationally traded pulses crops.



Figure 24 Major Crops on the Prairies 1970 – 2012 ('000 hectares)

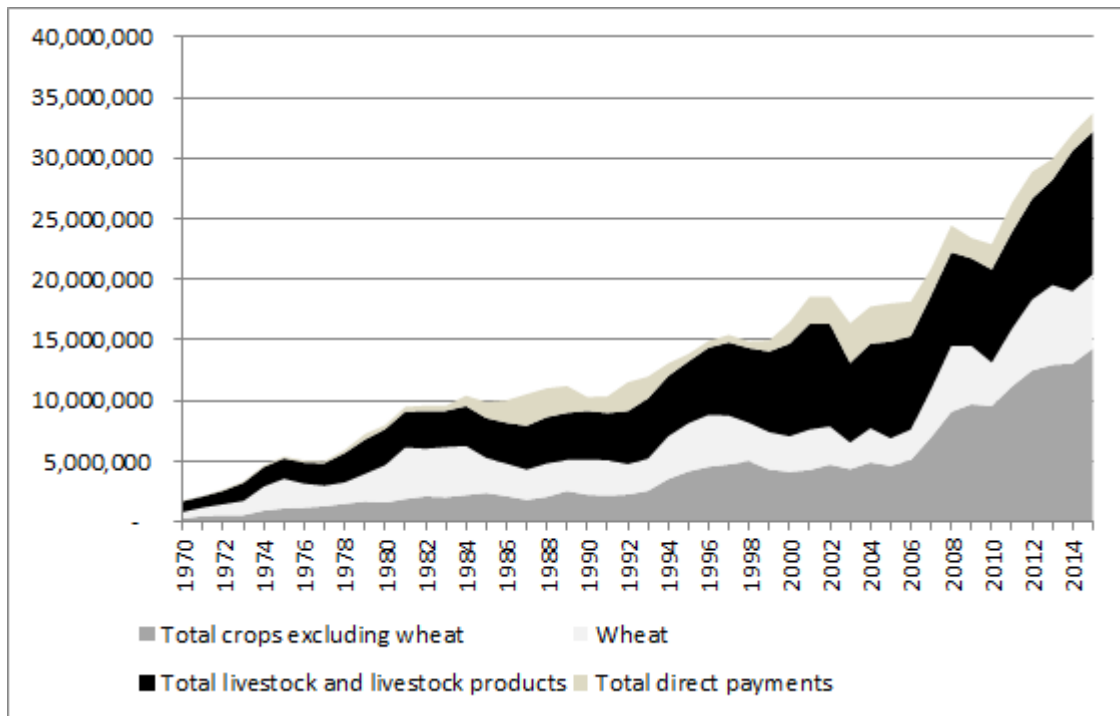


Source: Chart by Author, data from Statistics Canada Table 001-0010  
<http://www5.statcan.gc.ca/cansim/a26?lang=eng&id=10010>

The only traditional crop in which Canada continues to hold a significant share of the world market is durum, the raw material for pasta. The fears expressed by Quebec hog producers that their industry would suffer if prairie producers had access to cheaper sources of feed did not materialise. Quebec hog production has also continued to grow since the repeal of the WGTA.

Livestock production has increased significantly both in absolute terms and in terms of its importance relative to crops. After the WGTA came into effect, both Manitoba and Saskatchewan offered incentives for hog production, with predictable results. Market prices inevitably fell sharply as the additional volumes of slaughter pigs came onto the market.

Figure 25 Farm Cash Receipts 1970 – 2012 (000s dollars)



Source: Chart by Author, data from Statistics Canada Table 2-0001  
<http://www5.statcan.gc.ca/cansim/a05?lang=eng&id=0020001#customizeTab>

Expansion in the cattle industry has involved the conversion of some arable land to pasture, particularly where the topography makes the use of wide equipment impractical. A significant increase in the amount of land in crop is one of the most obvious changes in land use. Summerfallow has declined and its reduction plus the widespread adoption of minimal tillage practices has eliminated concerns over soil degradation and salinisation that became an issue in the 1970s. Studies by Lafond *et. al* (2011; 2006) suggest that the productivity of prairie soils is now generally on the increase after decades of decline.

### 5.6 Production Input Consequences

Another important aspect of farming is input supply. The most significant input for agricultural production is land. The CPR's rationale for accepting the Crow's Nest Pass Agreement was to forego some income from future freight traffic and capture it right away in higher land prices. When government provides long-term support for agriculture, as it did when low freight rates were imposed by legislation in the 1920s, land becomes a means of obtaining access to those benefits. The cost of land tends to rise to reflect the value of those benefits.

When wheat prices spiked after farmers had been encouraged by the 1970 LIFT programme to reduce production, demand (and therefore price) for land also increased. The cost of

agricultural land – as an asset with a long productive life – also tends to rise sharply during times of high inflation. As farmland is the usual collateral for longer term farm loans, an increase in its value becomes a temptation to borrow. When the ‘conspicuous pulling on the reins by the monetary authorities’ inevitably occurs, many farmers find themselves overleveraged. This happened on wide scale in North America in the early 1980s.

One consequence of the high rate of inflation in the 1970s and early 1980s was the difficulty that young farmers encountered buying land. This led CCF governments in Saskatchewan to intervene in the land market after they won the provincial election in 1971. During the 1970s they restricted sales of farm land to Saskatchewan residents expecting that this would moderate price increases. They subsequently introduced a land banking arrangement whereby farmers seeking to retire could sell their land to the provincial government and young farmers, often one of their children, could buy it back on favourable terms. Since deregulation of prairie agriculture and the election of the Saskatchewan Party in 2007 investment restrictions on ownership of agricultural land in Saskatchewan have been relaxed.

Demand for other inputs used in extensive (or land-using) grain production such as machinery, fertilizer, fuel, pesticides and herbicides, is a function of the area cultivated. Whereas grain handling and transportation firms maximise their return from handling the largest possible volume with a minimum of facilities, equipment, and route mileage, agrichemical and farm equipment suppliers benefit when the largest possible area of land is under cultivation. Such businesses would naturally be supportive of government intervention geared towards maintaining the size of the arable land base. Tax concessions on fuel for farm use are a case in point.

### **5.7 Complex System Consequences**

The piecemeal removal of three significant prairie agriculture institutions over the past thirty years has revealed the interconnected nature of the grain handling, transportation and marketing components of the system from a different perspective. These interconnections have tended to manifest themselves in ‘perverse’ outcomes as the system as a whole adjusted to the new rules after each regulatory change. Unfortunately, these adjustments have prevented prairie farmers from capturing their full share of the potential benefits of deregulation.

When deregulation of a complex system is approached in stages, the subsidiary components of the system may hinder the realization of expected benefits. Components which are ‘subsidiary’ to the three prominent prairie agriculture interventions fall into three broad categories: additional modifications of the institutional environment put in place to address unintended consequences as they arise; modifications which formally expand and acknowledge the interests of peripheral groups affected, and arrangements made independently among industry participants in order to benefit from the rules in effect at a given point in time.

This problem can be illustrated using the following three examples.

The need to allocate scarce government-owned railcars among competing users without the ability to use prices as the rationing mechanism is an obvious example in the first category. The rail car fleet was an unintended product of a statutory freight rate fixed at nineteenth century levels combined with twentieth century inflation and the Wheat Board monopoly over the sale of wheat and barley. Initially the Wheat Board allocated railcars, a responsibility it assumed under the War Measures Act in WWII. A Grain Transportation Authority (GTA), independent of the Wheat Board, was then created to take over this responsibility.<sup>189</sup>

The government announced that the GTA would end August 1, 1995, but when that date arrived plans to divest the railcar fleet had not been implemented. A committee of industry participants, the Car Allocation Policy Group (CAPG) was formed to (temporarily) fill the void. The fate of the railcar fleet was still not resolved in mid-2016. Thus, although both the ‘big issues’, the statutory freight rate and the Wheat Board, have been dealt with, the rail car problem has so far defied attempts at resolution. This underlines the fact that it is not enough to address just the obvious institutional issues: each component of the system as it has evolved under the regulatory regime needs attention.

Often subsidiary interventions expand the list of stakeholders who feel they have a vested interest in the system as a whole.<sup>190</sup> Movement of feed grains by rail was subsidised in an effort to encourage meat production in eastern Canada during WWII. Like so much wartime legislation, this intervention continued in the post-war period. Livestock

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<sup>189</sup> When the WGTA was in effect, the same institution was referred to as an ‘Agency’ rather than an ‘Authority’.

<sup>190</sup> Braybrooke and Lindblom (1970) pointed out the tendency of extraneous groups to devise ways of capitalising on a particular intervention expands the constituency of those interested, sometimes to an absurd extent: One frequent consequence of this is policy paralysis.

production did increase, but farmers in the regions affected understandably took an interest in policies that affected their source of supply.

This expansion of the reference groups involved in regulatory issues involving the prairie grain sector frustrated the ability of prairie farmers to benefit from deregulation. Quebec livestock producers played a pivotal role in ensuring that the Crow Benefit was paid to the railways instead of the farmer. Quebec farmers did not want their counterparts in the prairies to have their feed grain costs reduced, and had the political muscle (74 Liberal MPs) to make their case. They were trying to preserve a benefit that had arisen from the distortion of the inter-provincial feed grain market that resulted from artificially low rates charged to move grain out of the prairie region. It was not until the WGTA was repealed in the 1990s that producers began to deal with prices that more nearly reflected the transportation services they were using.

Cooperation among industry participants to capture some benefit from the prevailing set of rules is a third category of consequences. In the early 1980s, the two railways started to collaborate through 'car-pooling' to 'optimise' (from their perspective) the delivery of grain to terminal elevators in Vancouver and Thunder Bay. In Vancouver, CN delivered railcars to terminals on the north shore of Burrard Inlet and CP delivered railcars to terminals on the south side. Because the origin of the railcar (loaded by a grain company on behalf of the Wheat Board) was immaterial, this cooperation between the railways improved the efficiency with which available cars were used.

The incentive structure which made car-pooling attractive was the result of the way Wheat Board grain was assembled and dispatched to terminal elevators at ports. Until car-pooling was abandoned in 1995, grain companies had little incentive to upgrade their 'country' facilities. There was also no incentive to load unit trains or clean grain to export standards at inland terminals, because cars loaded by one company would be randomly switched with cars loaded by other companies on the other railway company's lines. As a result, the switch over to high throughput inland terminals was slowed. Once car-pooling ended it accelerated dramatically (Figure 21).

While the railways were 'economising' on scarce railcar capacity by pooling car deliveries, they were also using railcars inefficiently to capture the WGTA subsidy that was available for grain shipped into the United States provided it was routed through Thunder Bay (Bonsor, 1995; Carter & Loyns, 1998: 108).

The point to be emphasised is that rent-seeking opportunities exist whenever rule changes are imposed, irrespective of whether the longer term trend is towards more or less regulation at some point in the future. These instances illustrate how intermediate stages in the deregulation process were exploited to keep the benefits from reaching farmers.

The net effect is, unfortunately, that farmers feel disadvantaged by deregulation, and are quick to demand re-regulation. The Fair Rail for Grain legislation illustrates the lingering distrust of market mechanisms which leads to ideologically motivated intervention not in the farmers' interest.

## **6 Counterfactual**

The key components of the regulatory system governing prairie agriculture in the 1970s were: 1) the statutory freight rate (in effect since the 1920s), 2) the compulsory Wheat Board (which received its monopoly powers in 1943) and 3) a railway duopoly consisting of one private and one public firm. Changes made to the institutional superstructure of prairie agriculture after 1980 were traumatic for two reasons. First, prairie agriculture had adapted in response to the major interventions that had been in place for an extended period of time. Second, those interventions had unintended consequences. These consequences gave rise to a vast, interconnected network of boards, agencies and supplementary regulation put in place by the government, and a less obvious array of adaptations and 'work arounds' in the private sector to make the system function as well as possible given the imposed restraints. These factors meant that deregulation efforts were resisted by a substantial proportion of the farmers who were the intended beneficiaries of the process, and that the process of dismantling the institutional environment in place in 1980 was complicated by the subsidiary arrangement incorporated into the system to make the major interventions function..<sup>191</sup>

The counterfactual for this period considers two alternate scenarios to the historical events already outlined in this Chapter: 1) what would have happened to prairie agriculture if efforts to address the freight rate issue had been abandoned in the early 1980s? and 2) what would likely have happened if Canada had pursued a 'big bang' (or trend-breaking)

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<sup>191</sup> For example, when the federal government ended the 'Crow Benefit' subsidy and the Grain Transportation Authority effective August 1, 1995, no arrangements were in place to manage the hopper cars fleet which had been purchased to keep grain moving during the period the railways were unwilling to upgrade their grain-related infrastructure (Carter and Loynes, 1998:109).

approach to deregulation rather than a more gradual approach dragging on for three decades (from the WGTA of 1983 to the end of the Wheat Board monopoly in 2012)?

### **6.1 What would have happened to prairie agriculture if efforts to address the freight rate issue had been abandoned in the early 1980s?**

The Crow rate was the first of the major institutions tackled. The process of addressing the statutory freight rate issue was the result of a “highly improbable concatenation of coincidences”.<sup>192</sup> The reform initiative might have stalled at a number of points along the way. Stambrook (2011: 5-6) lists four major occasions when the process could easily have foundered.

Similarly, if two ambitious senior bureaucrats had not seen Canadian National Railway’s potential as a private company it might still be a crown corporation. Finally, had Prime Minister Harper not taken on ending the ‘single selling desk’ mandate of the Canadian Wheat Board as a personal mission it would likely have remained in place. Any or all of the three major initiatives which substantially changed the degree to which the federal government was directly involved in the prairie grain sector might not have happened.

Under a scenario where *none* of the three key pillars of regulation were addressed, railway infrastructure would have continued to deteriorate. The railways would have continued their efforts to obtain funding for the movement of grain from the federal government. Some money might have been forthcoming while revenue from the National Energy Programme was flowing into the Treasury. However, this was an anomalous situation which did not last. The general trend was toward larger federal government deficits, and increasing awareness of the need to bring them under control. When these deficits reached embarrassing levels in the mid-1990s, there was a concerted effort to cut government spending. Under such circumstances, the federal government would be less willing to fund stop-gap measures to keep prairie grain moving to ports.

Since the railways were unable to cover their costs shipping grain, shippers who paid compensatory rates to have their commodities moved by rail would continue to enjoy preferential access to limited railway capacity at the expense of grain traffic. The ability of the Wheat Board to have grain at the right port at the right time to meet sales commitments

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<sup>192</sup> The coincidence of a Deputy Minister (Arthur Kroeger, a bi-lingual Albertan) and a Minister (Jean-Luc Pepin from Quebec) who both understood the implications of taking on the ‘Crow’ issue but were prepared to give it priority in the face of hostility from many quarters and found themselves in the Ministry of Transport was itself ‘highly improbable’.

would deteriorate. Demurrage charges would increase and the reputation of Canada as a reliable supplier would decline. Under this scenario, the inability of the CWB to export prairie wheat on farmers' behalf would become increasingly obvious over time.

Given the financial difficulties in which the railways found themselves and uncertainty over the future of the regulatory environment affecting grain transportation, it would not be possible for the CPR to raise the capital it needed to relieve its bottleneck in the Roger's Pass. Since WWII, export markets for prairie grains and oilseeds had shifted from east to west, so this bottleneck in the Rockies was becoming an increasingly serious problem.

Canadian taxpayers would have continued to fund the operating losses of Canadian National had it remained a government-owned entity. Such losses would have exacerbated the financial difficulties the federal government faced in the mid-1990s, requiring even more severe cuts to government spending in other areas. As CN was losing money transporting grain, the government might have been keen to revisit the possibility of merging the two railways. The CPR would have been unwilling to take on additional responsibility for moving grain at a loss, so such a deal would be unlikely.

Crops not sold through the Wheat Board would become increasingly attractive options for farmers. However, since the 'Crow rate' had been extended to cover most prairie crops, shipping most non-Board commodities would have eventually been constrained by the lack of railcar capacity.

Problems shipping Board grains using traditional bulk handling methods would have encouraged the exploration of alternative shipping options. Shipping specialty crops by container would have circumvented statutory rates and the cumbersome railcar allocation process. It might well have developed more quickly, constrained only by the willingness of the railways and the grain handling companies to provide the necessary facilities on mainline sidings. This option is made particularly attractive by the backhaul potential inherent in the large number of containers which traverse the region bound for the west coast and Asia.

The only other alternative would have been to shift land into production of feed grains for consumption on the prairies. Low feed grain prices would stimulate production of beef and pork, but increased production would depend heavily on access to the U.S. market.<sup>193</sup> This

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<sup>193</sup> Trade in beef and pork between Canada and the U.S. was disrupted by an outbreak of BSE in Alberta in 2003 and further complicated in 2009 when a strain of flu affecting humans was widely referred to as



would have achieved the same objective as the subsidies provided by the provincial government when the pay-the-railways option was adopted. There would have been two main advantages: avoiding uncertainty over how long the subsidy might last, and a market induced-expansion of livestock production not complicated by the (temporary) existence of a government programme.

Since the Wheat Board would have continued to experience problems meeting its sales commitments, the returns farmers received on Board grains would plummet, increasing the differential between prices available at elevators in Canada vs. those just across the border in the U.S. Under such circumstances, the protests against the Board that occurred in the 1990s would have been more widespread and more vocal. Farmer-owned UGG did adopt a pro-reform stance and other grain cooperatives might have followed suit as the balance of opinion among their members shifted toward the deregulation alternative. The lack of government funds for stop-gap measures should have made it increasingly obvious that more government funding and the nationalisation of the CPR were not feasible options. Taxpayers and the tenor of international trade negotiations at the time were also arguments against this option.

In summary, it is highly likely that under this scenario the deterioration of the GHTS would have accelerated and the ability of the Wheat Board to retain the confidence of customers and farmers would drop. The ability of the federal government to continue its *ad hoc* support for the sector would decrease. As the grain sector moved to the brink of collapse, a broader spectrum of the affected groups would recognise that the *status quo* was unacceptable. Under such circumstances, deregulation might have been delayed but could not be postponed indefinitely.

## **6.2 What would likely have happened if Canada had pursued a ‘trend-breaking’ approach to deregulation?**

This counterfactual considers the likely outcome if a comprehensive and abrupt approach to deregulation had been followed rather than the gradual process which unfolded over more than thirty years. This option has been referred to as a ‘trend-breaking’ or ‘big bang’ approach (Button, 2010).<sup>194</sup>

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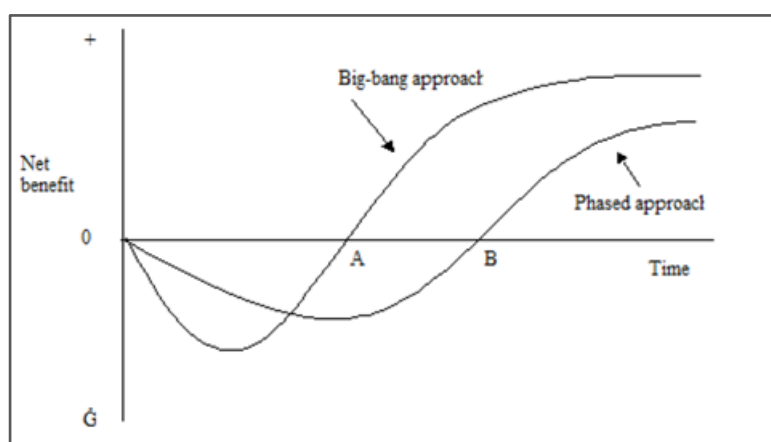
‘swine flu’. Measures in place to contain the BSE outbreak would have prevented any serious disruption of trade, but U.S. producer groups escalated the issue to reduce competition.

<sup>194</sup> The term ‘big bang’ was applied to the so-called deregulation of the financial services industry in Britain initiated by the Thatcher government in 1986. To some extent it was misnomer: it constituted re-regulation in the sense that the discipline of unlimited liability which constrained banks to limit their

According to Button & Johnson (1998; cited in Button, 2010: 12) the advantages of a ‘big bang’ approach to regulation:

[r]emoves considerable uncertainty from the market about the nature of future institutional structures and should therefore remove some of the challenges in making optimal investments. It also means that there is less opportunity for those in the industry, or for others with related interests, to manipulate the various stages of the reform process, as may be the case if the changes are phased in over a period of time. In other words, regulatory capture is less likely. Additionally, there is expectation of a significant flow of benefits, generally to users.....once the reforms have worked their way through the system.

Figure 26 The ‘Big-Bang’ Approach versus Phased Reform



Source: [http://www.pcs.usp.br/~gas/jbats/admin/arquivos/15;v6i1\\_a1.pdf](http://www.pcs.usp.br/~gas/jbats/admin/arquivos/15;v6i1_a1.pdf)

Button (2010) uses examples of deregulation in the airline industry to argue that although the initial disruption is more severe, the big bang approach provides both a larger net benefit and at an earlier date than the long, drawn out alternative.<sup>195</sup> This argument can also be applied to Canadian prairie agriculture.

Two international examples suggest that ‘big bang’ strategies for deregulation do follow this pattern. The deregulation of New Zealand’s agriculture, driven by the desire of the predominantly urban electorate to stop subsidising the sector, is often cited as a successful

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activities that had economic merit was not restored (Kingston, 2014: esp. 451). The big bang concept was further maligned when Jeffrey Sachs proposed rapid ‘deregulation’ of former Soviet Republics by imposing ‘the right institutions’ exported from the West on a system which had neither the capacity to make them work nor the experience to understand their purpose.

<sup>195</sup> These authors refer to this alternative as a ‘phased approach’ but emphasise that it is not phased in the sense that it mapped out in advance. It is an evolutionary process in the sense that options and constraints for future steps depend on the unknowable consequences of initial steps.

example (Sandrey & Vink, 2006). In this case, the rapidity with which agriculture can adjust to a complete overhaul of its institutional infrastructure was clearly demonstrated.<sup>196</sup>

Attention has been drawn to the contrast between deregulation of grain movement by rail in Canada with the impact of the Staggers Act on rail transportation in the United States. Transportation deregulation in the United States in general, and railway deregulation under the Staggers Act in particular, are also cited as examples of the ‘big bang’ approach to deregulation. Discussions of deregulation of U.S. railways in particular emphasise that the ‘crisis’ was sufficiently broadly felt that there was well-nigh unanimous recognition that dramatic changes were required, and that only comprehensive deregulation would ensure benefits would be shared between shippers and railways (Caves, *et al* 2010). The changes were made and U.S. railways and their clients benefited (MacDonald, 1989)

It must be acknowledged that railway deregulation in the United States was ostensibly much less complicated than in Canada. There was no lingering ‘ideology of freight rates’ in the U.S. case. Low freight rates on grain were not considered a ‘sacred trust’ or a ‘constitutional right’ as is sometimes claimed by Canadian opponents of change. Grain was just one of many commodities affected by an initiative which was national in scope. Although a lot more than two railways were involved, they were all private and the legislation dealt only with the relationship between the railways and shippers. Finally, there was no involvement by any agency comparable to the CWB.

Turning to the prairie case, it must be acknowledged that a ‘big bang’ approach would have entailed considerable disruption of the *status quo*. Offset against this disruption would be the following benefits:

- The benefits of moving from the grain handling infrastructure of the 1920s to the grain handling infrastructure of the late twentieth century would be achieved at the most rapid pace possible. Competition among grain companies for farmer’s grain and between the railways would lead to efficiency benefits being shared with farmers.
- All participants in the grain trade would face ‘real’ rather than ‘phoney’ prices and would make decisions accordingly. Real prices would reflect the efficiency of each

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<sup>196</sup> It is important to recognise that the New Zealand example is not a straightforward case of urban taxpayers vs recipients of agricultural ‘welfare’. First, agriculture is such an important sector of the New Zealand economy that urban employment was also affected in the short run. (One of the main medium and longer-term benefits of deregulation turned out to be more value-added processing which boosted domestic employment in downstream industries). Second, some non-rural industries lost protection from imports in tandem with the agricultural reforms, and the sense that negative consequences were broadly distributed was regarded as important for obtaining and maintaining support for the reform process.

element of the system. Farmers would have a wide range of marketing and production choices.

- A great deal of uncertainty pertaining to government policy would be removed from the system. This type of uncertainty is a major disincentive to entrepreneurial discovery at all levels in the value chain.
- From the perspective of farmers and taxpayers, one round of deregulation would involve significant savings over a repeated process, with its attendant lobbying, legal action, consultation, enquiries, appeals, research and legislation. It should be noted that these savings would not be recognised as a benefit by those who make their living from such activities.
- There would be no need to repeatedly consult with a large number of industry stakeholders when the relevant information is communicated through the price discovery process.
- There would be no opportunity for industry participants to capture the benefits of a succession of new rules without sharing them with those paying for their services. As Schumpeter indicated, the benefits of ‘doing things differently’ are only shared when there is competition.
- There would be no opportunity or incentive for backsliding. Whenever an incremental reform process is adopted, each iteration of the process is an opportunity for those who *feel* themselves disadvantaged by rule changes (i.e. they are unwilling to adapt to market realities) to counterattack. There would be no incentive to re-regulate the railway grain transportation along the lines that have been followed since 2008.
- It would avoid the inefficient process of multiple adjustments to a series of transitional rules. Such steps inevitably create rent-seeking opportunities for those at the table making the rules.
- Dispensing with the top-down rules places the onus on industry participants to develop arrangements which improve the competitiveness of the system as a whole. This is crucial when competing in international markets with suppliers operating under different institutional arrangements.

The brief review of studies which consider the impact of crises on interest group behaviour (in Chapter 2) suggests that big changes are only feasible in the face of a very serious crisis. The deregulation that occurred in prairie agriculture began with a conciliatory attempt to address the statutory freight rate issue and ended with a more autocratic decision to end the Wheat Board’s monopoly.

It seems highly unlikely that ‘big bang’ deregulation could have been implemented in the early 1980s. The combination of crisis and public will supported elimination of an open ended financial commitment to the sector by the federal government and later a roll back of spending. However, had deregulation been postponed until more recently, the crisis might have reached sufficient proportions that levels of support given the Staggers Act in the U.S. would make a similar ‘big bang’ approach feasible in prairie agriculture.

## **Chapter 7**

### **Conclusion**

This study traces the interaction between institutions and the Canadian prairie grain economy since Confederation in 1867. The history of prairie agriculture, as reinterpreted in this research, diverges significantly from the standard interpretation of the role it has played in Canada's economic history. This explanation would have us believe that the national policy was a strategy to thwart American annexationists, that wheat was the ideal staple export for the prairies and that a 'wheat boom' was a turning point in the development of the Canadian economy. This study draws attention to the inconsistencies in this standard interpretation and suggests that some of the costs incurred were excessive and unnecessary.

A framework drawn from the New Institutional Economics (NIE) and the work of Joseph Schumpeter is used to examine the reciprocal influence between institutions and economic performance. This approach considers agricultural production and marketing systems both as products of particular institutional arrangements and also as factors influencing changes in those institutions over time. In the Canadian example, the insights of Schumpeter are used to explain how farmers, railways and grain companies reacted to changes in the institutional environment.

The institutional environment affects the pace and direction of technical change and, ultimately, the efficiency of the agricultural system. Shifting interests and incentives explain the changing objectives of federal government interventions in this sector. Assessing institutional performance is difficult. However, by design, the prairie grain economy has always been oriented towards international markets. Therefore its success, or lack of it, is reflected in its success capturing international markets.

Institutions affect transaction costs, and hence the competitiveness of market participants. Over the course of history, the institutional changes affecting the Canadian prairie wheat economy have lowered and raised transaction costs, and have thus both helped and hindered its international competitiveness. Yet, some of the institutional dysfunctionality prairie wheat growers faced over the last century and a half pales in comparison with the difficulties faced by some of their counterparts.

The conclusion consists of six sections:

1. The model and prairie agriculture
2. A synopsis of the comparable institutional environments in two of Canada's international competitors, Russia and Argentina
3. A counterfactual that spans the entire history of the region
4. Reasons why some policies fail
5. Opportunities for further research
6. Concluding comment

Four questions were posed in Chapter 1:

1. What factors determine how governments respond to crises?
2. What causes dramatic changes in public opinion regarding the role of government?
3. What causes negative policy outcomes?
4. Why does popular support persist for measures after their negative consequences are known?

The first of these questions is answered in section 1, and the others are covered in section 4.

### **1 The Model and Prairie Agriculture**

The model used to examine the interaction between the economic sector and the institutional environment does explain how institutional changes affected prairie agriculture and vice versa over four historical periods. However, in the final phase, which began in the 1970s, the direction of institutional change is not consistent with Schumpeter's expectations until the very end of the period.

At the outset, the model explains how a looming crisis in British colonies in eastern North America developed, and how settlement of the prairies became such an important part of the solution Canada pursued after Confederation.

Each of the subsequent time periods also begins with a crisis. Crises, according to Schumpeter, are abnormal recessions which result when the mechanism of technical change is deflected from its natural path by alterations in the institutional environment. The crisis in 1896 resulted when government funds were spent preparing for an anticipated settlement boom and few settlers materialised. The next crisis was the Depression of the 1930s. The looming crisis in the final period of the study was the consequence of difficult conditions in international grain markets and the deterioration of the railway infrastructure needed to access those markets.

The response to each crisis reflected the influence of a dominant interest group, promoting the solution that met its own objectives. Such groups selectively appropriate ideas from those circulating at the time to support their agenda. For example, the architects of the national policy selectively adopted liberal ideas because they opened up the market for Canadian wheat, but rejected them in choosing protection for the manufacturing sector. Farmers' organisations publicised socialist ideas at a time when their constituents were trying to understand why the price they received for their wheat was so low.

As the political process involves compromise, policies may be modified as they are translated into legislation. The tortuous process whereby efforts to support wheat growers in the Depression led to a compulsory peace-time Wheat Board is a good illustration. Another is the compromise over the payment of the 'Crow Benefit' made in order to change freight rate legislation in the early 1980s.

The legislation that emerges from the political process changes the institutional infrastructure. Whether or not these modifications have the desired effect depends on how individuals and businesses respond. For example, the building of the CPR was expected to encourage settlement. However, at the time it was completed, the cost of rail service and the impact of the tariff made it difficult to produce wheat profitably. This meant that those expecting a boom in agricultural settlement once the railway was completed were disappointed. Similarly, when the Progressive bloc of MPs negotiated with the Liberals to get legislation that guaranteed low freight rates, they did not anticipate how the railways would respond in the future.

The consequences of changes in the institutional environment in one period generate feedback for future periods. That feedback may be negative or positive. If the reaction is extremely hostile, it may be expressed through the electoral process. The leaders of both of Canada's mainstream political parties were voted out of office during the Depression. Changes in market conditions also influence the motivation of various interest groups. Farmers were disappointed with the profitability of grain growing at the turn of the century and blamed the railway and the grain handling companies. For this reason, farmers' organisations pressured the Liberal party to regulate grain handling and transportation. When the Wheat Pools were on the verge of bankruptcy in 1930, they persuaded the provincial Premiers to plead their case for assistance with the Prime Minister.

The thesis argues that intervention was reasonably successful in the first period as it created an institutional environment under which orderly settlement of the prairies could take place. However, infrastructure debts accumulated prior to Confederation and the huge cost of constructing a transcontinental railway necessitated high tariffs and raised western suspicion about the motives behind the national policy. Intervention in the next two periods was, on balance, unhelpful. In the second period, redoubled efforts to promote settlement exaggerated an increase in settlement that was taking place in response to improvements in the profitability of wheat production. This was also the period in which the federal government started to regulate the grain handling and transportation system at the insistence of farmers' organisations, disrupting the process of technical change in the process. After 1929, further intervention created a rigid institutional framework for the prairie wheat economy which limited its ability to react to changes in the international market.

The standard interpretation of the history of prairie agriculture claims that the devastation of the prairie grain economy during the Depression was the result of *laissez-faire* policies. The alternative explanation offered here is that *laissez-faire* had nothing to do with the weather that decimated crops. The presence of large numbers of farmers in moisture deficient parts of the region was the result of a concerted effort on the part of the Ministry of the Interior to increase the rate of settlement which compounded the increase occurring anyway as the profitability of wheat production gradually improved. The collapse in prices was neither the result of a sudden surge in profiteering by grain exchange speculators nor a massive widening of margins in the private grain trade. The return to protectionism in Europe and the United States, the (brief) return of Russia to the international grain trade as an exporter, the growth of prairie wheat production as settlement promotion continued during the 1920s, and the un-hedged stocks accumulated by the Pools in their futile attempt to drive world prices higher, were contributing factors.

Schumpeter suggested that crises are used to justify measures which handicap the ability of businesses to react to changes occurring in markets. Technical change in its broadest sense, is the mechanism whereby the economy adjusts to changing circumstances. In the pre-Depression period, the pace of change in the businesses which linked prairie farmers to world markets was extremely rapid. However, the institutional environment discriminated against technical change in the post-WWII period. For nearly forty years, Canada's grain



handling and transportation system was highly regulated. The combination of the statutory freight rate and the Wheat Board limited the options available to farmers and the railways.

The prairie grain economy has traditionally been heavily oriented to international markets over which it exerts little influence. The deterioration of the grain handling and transportation system on which access to those markets depends was quickly recognised as looming crisis which required attention. Major changes were taking place simultaneously in the global grain market. The European Union became an exporter of wheat, reversing its earlier role. The Soviet Union and China were significant importers. The institutional environment in each exporting country influenced its competitive position. Dependence on export markets eventually prompted Canada to take steps to deal with the institutional origins of the inefficiencies that were making prairie grains uncompetitive. When changes were made to statutory railway freight rates, another period of extremely rapid technical change in the grain handling and transportation system began.

## **2 Comparative Examples of Institutional Change**

Schumpeter was concerned that a slide towards socialism was ‘almost inevitable’. His assessment might have been correct had all exporting countries been on a similar trajectory. However this was not the case. Institutional diversity explains why Schumpeter’s expectation that the highly regulated phase in prairie agriculture was unsustainable: Canada’s competitors in international markets had different institutional arrangements, some of which were conducive to maintaining or increasing their competitiveness in the international market.

The world wheat market is heavily influenced by the policies of the United States and the European Union. When Britain repealed tariffs on wheat in 1846, this signaled the beginning of a brief period of free trade in wheat.<sup>197</sup> Britain and Western Europe were the destination for most of the wheat traded internationally prior to the First World War, drawing supplies from all over the globe. There was a widespread return to highly protectionist policies in continental Europe in response to the Depression. The Second World War and the European integration project continued that trend. The Common Agricultural Policy gave rise to surplus production of wheat that was subsidised in order to ‘dispose’ of it in the international market. Since 1990, the EU has taken steps to reduce its export subsidies, but continues to spend heavily on social and regional development

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<sup>197</sup> France Germany and Italy reimposed modest tariffs in the mid-1880s but Britain, the most significant importer, maintained its free trade stance until the Depression of the 1930s

programmes. It remains a significant wheat exporter. After an attempt to cut back on farm programme spending in the 1990s, the U.S. continues to support wheat production with its government programmes.

This brief look at two competitors – Russia and Argentina -- reveals huge variability and instability of their respective institutional environments. These institutional constraints, both formal and informal, determined their relative success in the international market.

## **2.1 Russia/USSR**

Russia provides the most extreme example of how institutions can affect participation in the international wheat trade. In the late nineteenth and early twentieth centuries, Russia was the world's largest wheat exporter. After WWI, the Revolution and a civil war, the USSR remained out of the market until 1930 when it exported some 3 million metric tonnes at a time when markets were already in turmoil due to the Depression. For most of the remainder of the Soviet period, the country was a significant importer of wheat. The collapse of the Soviet system paved the way for Russia (and Ukraine) to return to the international market as exporters. Russia's share of the market has been increasing rapidly, and this trend is expected to continue.

These large swings in wheat exports are directly related to institutional changes. Russia's leaders in the nineteenth century were very conscious that the country lagged behind Western Europe and that improvements in agricultural productivity were part of the solution. Crises, in the form of military defeats, highlighted the need for change. The emancipation of the peasantry in 1862 followed Russia's defeat in the Crimea War. Under the Emancipation Act, peasant communes had to pay a redemption tax and crops like wheat, which could be sold for cash, became important. This wheat was exported, mostly through the Black Sea port of Odessa. Defeat in the Russo-Japanese war gave impetus to further efforts to improve agricultural productivity, and significant changes began with the Stolypin reforms of 1906. These changes in the institutional environment were the first attempt to encourage peasant households to separate their land holdings from the village collective. A resettlement scheme also provided subsidies and small land grants to peasant families prepared to relocate to Western Siberia along the Trans-Siberian Railway then under construction. Between 1906 and 1914 an estimated 4 million peasants moved to Siberia, and it became one of the country's grain surplus regions.

One of the first consequences of the Russian Revolution was the nationalisation of land. After a brief interlude, during which the domestic grain market continued to operate, Stalin launched a forced collectivisation drive. It was prompted by a shortfall in the grain available in major urban centres in the winter of 1928/29. Peasants who had started family farms became class enemies and the countryside was forcibly reorganised into collective farms. The Soviet period in rural areas is often referred to as “the second serfdom”.

The Soviet system in agriculture provided western analysts with numerous examples of perverse incentives. Of particular interest is the impact of the Soviet system’s aversion to innovation and technical change (Rosenberg, 1992). Agricultural production did increase significantly during the Soviet period, but involved mobilising more resources at huge cost. Under Khrushchev, a campaign to bring ‘Virgin and Idle Land’ into production in Western Siberia and Northern Kazakhstan successfully increased domestic wheat production. A similar campaign to increase corn production after Khrushchev visited a farm in the U.S. mid-west was much less successful.

Perverse incentives also affected labour productivity in agriculture. The most fascinating aspect of Soviet agriculture was the rapidity with which the rural labour force learned to play the system (Fitzpatrick, 1991). They gradually obtained all the benefits to which their urban proletarian counterparts were entitled, contributing less and less while the state invested heavily in agriculture.

Soviet agriculture depended on a wholly artificial system of pseudo-prices denominated in a non-convertible currency. When the Soviet Union collapsed, and its currency became convertible, this system no longer functioned. Agriculture had been a sector in constant crisis throughout the Soviet period. Because of this, the right to private plots was successively extended from collective farmers, to state farm employees and ultimately to the urban population in the form of ‘dacha’ allotment plots. Access to private plots and allotments helped to mitigate its impact on the population when agriculture collapsed along with the rest of the economy.

Russia’s return to the world market as an exporter is the legacy of that collapse. When the system fell apart, the main agricultural asset was an abundance of land. This land is available for rent at low rates and in large blocks.

After 1989, agricultural reform was attempted by changing the institutional framework. Privatising land was expected to give rise to a private farming movement, but this did not

happen. Distrust of others, lack of security, and an aversion to risk-taking, all legacies of serfdom and the Soviet period, discouraged entrepreneurship of this type.

However, the availability of agricultural land at a nominal cost makes corporate farming on a very large scale feasible. Modern agricultural machinery now makes it possible to capture economies of scale in agriculture. The main difficulties faced by Russian wheat exporters are the State and the embedded informal institutional environment which, according to Hedlund (2005) has changed very little since the thirteenth or fourteenth centuries. This problem is mitigated by corporate farming which is superimposed on the existing institutional environment. The Soviet period was characterized by large agricultural enterprises run by the state. There is a widespread belief (again a legacy of the Soviet period), that large, technically sophisticated agricultural operations are superior to other forms of agricultural production. Administrative red tape represents a huge barrier to small scale entrepreneurship. The scale of the large 'agro-holdings' gives them important leverage over the local authorities.

It is not possible, however, to avoid the influence of the state completely. A longstanding preoccupation with food security is also a legacy of Russia's turbulent history. Exports are periodically restricted when domestic prices spike, as they did in 2007-08 or when there are 'droughts' as in 2010.<sup>198</sup>

The other form of interference which is difficult to escape is export taxes. The decline in the world price of oil adversely affected Russia's balance of payments and has resulted in a sharp drop in the value of the rouble. The widening gap between domestic rouble prices and foreign dollar prices enables the state to capture exchange rate gains by imposing taxes on commodity exports, including wheat.

## **2.2 Argentina**

Argentina was one of the big four exporters which divided up Russia's share of the world wheat market after 1914. However, there are surprising parallels between the institutional environments in which agriculture has recently operated in both Argentina and the Soviet Union. Currently, the main difference between the two is that, despite similar institutional constraints, Russia is expanding its share of the international market for wheat while Argentina's share has dwindled to the point where it is no longer a significant wheat

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<sup>198</sup> In this instance, there was a ban on Russian grain exports in effect from August 15, 2010 until June 30, 2011.

exporter. This happened without any change in the inherent productivity of Argentina's agricultural land base. It is entirely a consequence of changes in the institutional environment. The current situation is remarkable because Argentina's production and exports of wheat exceeded those of Canada until 1910 (Solberg, 1987: 36)

The Argentine pampas is one of the most favourably endowed regions in the world in terms of agricultural potential. Land was distributed in large blocs to deserving Spaniards during the colonial period which ended in 1816. The Conquest of the Desert eliminated the native population and increased the land available for European settlement. The Argentine provinces raised public funds by selling land, again in large parcels.

These large landholdings became the basis of a grazing economy. The initial products were hides and dried meat, later wool and ultimately beef. Argentina became a British colony in all but the formal sense in the nineteenth century, relying on British capital and British markets for its products (Ferns, 1960). Unlike Canada, Argentina wholeheartedly adopted free trade as the option that best served the interests of the landed elite. "Buy from those who buy from us" became a mantra.

It was perhaps inevitable that wheat would be added to the list of Argentine exports. However, wheat production did not develop as an alternate form of land use, as in Australia. It was integrated directly into the grazing economy as a means of improving pastures: tenant farmers or sharecroppers ploughed land and raised wheat crops for a number of years, before seeding the land to more nutritious grasses and alfalfa, and then starting again with a different plot. Most of the tenant farmers were from Spain and Italy. Unlike settlers in Canada, they considered themselves temporary residents of Argentina and rarely became citizens. Solberg (1987) points out that this was an important factor in explaining the wheat growers' lack of political influence.

The pampas extends in an arc five hundred kilometers inland from Buenos Aires. Ports on the Atlantic coast or on the Parana River are much closer to grain growing regions than in Canada. Railway construction in Argentina was undertaken by British and French firms as well as the national government. The main disadvantages Argentine wheat growers had to deal with were the distance from markets in the northern hemisphere and inefficient logistics. Grain was handled in bags, and loading and unloading them into railcars or ships

was extremely labour intensive. The port of Buenos Aires was reputedly the most expensive in the world.<sup>199</sup>

The boom in Argentine wheat production ended in 1911 with an unusually poor crop. Before the sector could recover, the tightening of credit in advance of the war and depressed prices created tensions between tenant farmers and their labourers, who were demanding wage increases, and their landlords who attempted to raise rents to take advantage of strong demand for land to rent. Strikes became a common occurrence in the countryside. Argentine agriculture had a free-trade orientation, but both Britain and the United States pressured Argentina to supply cheap wheat to the allied war effort and to end shipments to Spain during WWI lest they end up in German hands (Solberg, 1987: 159-62). Finding itself in dire straits, the Argentine government imposed a tax on exports. As in the case of Canada's income tax, it was justified as a temporary 'tax on profits'. It remained in force until the Depression, when it was hidden in the machinations of the National Grain Board (JNG) which was created in 1933.

The state played a largely passive role in the wheat economy prior to the Depression. After two poor crops in a row, the squeeze on tenant farmers from high rents and the wage demands of harvest labour provoked action. A modest farmers' movement (in which the Catholic clergy played a leading role) developed in the area of northern Buenos Aires and Santa Fe where rents were particularly high. The government eventually intervened to forcibly end strikes by farm labourers which threatened to disrupt the 1919-20 harvest, one of Argentina's best ever.

During this period of more strikes and violence in the Argentine, tenant farmers embarked on a mechanisation splurge. Between 1924 and 1930, Argentina imported over 15,000 tractors and 25,000 combines free of duty, mostly from the U.S. and Canada. By 1928, there were 28,000 combines in use in Argentina. About a third came from Canada, at a time when few prairie farmers were interested in this technology (Solberg, 1997: 106-107). In Argentina, land was a variable cost, and machinery was one of the few investments tenant farmers made.

Overtly predatory policies towards agricultural exports became embedded in Argentine institutions after Peron came to power in 1943. Peronism was an *urban* populist

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<sup>199</sup> Solberg (1987:125) indicates that it was six and a half times more expensive to load a ship in Buenos Aires than in Montreal.

movement. Peron imposed protective tariffs to promote industrialisation and embarked on a nationalisation programme which included the railways. By the 1960s, Argentina had the highest average rates of protection in Latin America, and importing foreign-made farm machinery became next to impossible. The name of the Grain Board changed to the Argentine Trade Promotion Agency (IAPI) in 1950, and its control over the grains sector increased. Export taxes reached levels as high as 70 per cent of the value of the commodities exported. By the early 1970s, the agrarian situation had become so bleak that Ferns commented that “the rural economy of Argentina has tended to resemble that of the USSR in terms of stagnant productivity” (Ferns, 1973: 173).

Agricultural exports made the peculiar form of urban populism that developed in Argentina possible but, as the sector weakened under the strain, its capacity to fulfil its role declined in tandem. Conflicts between the rural export-oriented constituencies and the urban power base of populist governments increased, largely because both wheat and beef were exported and consumed by the urban population (O’Donnell, 1978). Strains on the economic system led to military take-overs and an attempt to distract attention from domestic problems with an invasion of the Malvinas, or Falkland Islands.

Chronic inflation in the late 1980s was eventually tackled with the help of a World Bank structural adjustment programme in the 1990s. The Grain Board was disbanded in 1993, and its national network of silos and ports privatised. Another objective of this programme was to finance public expenditure from land taxes instead of export taxes. Ultimately, these measures were inadequate and in 2002 the cycle started again. When the peso was de-linked from the dollar, inflation returned.

Nestor and Christina Kirchner, who were the Presidents of Argentina from 2003 to 2015 have again exploited agricultural exports to fund public spending. This strategy has been aided by the growing importance of soybeans in Argentine agriculture. Since 2002, an export tax has again been levied on agricultural products, including both wheat and soybeans. In addition, certain commodities, including wheat, have been subject to maximum export quotas. The tax was to provide revenue to the government and the quota was to keep the domestic price for wheat low for urban consumers by ensuring an adequate supply level for the domestic processing industry. Soybeans were taxed at an even higher level than wheat, as there is no domestic demand they were exempt from any export restrictions.

The plan did not achieve its objectives because producers adjusted their production decisions in response to market prices as modified by the export tax regime. From their perspective, the lack of export quotas made soybeans far more attractive than wheat despite the tax differential, and farmers started to shift production accordingly. Argentina is now the world's third largest exporter of soybeans. Area seeded to wheat dropped to its lowest level in over a hundred years in 2012/13, and its share of the world wheat market is declining. Argentina currently ranks only tenth among wheat exporters, and at the beginning of the 2015-16 crop year was unable to fulfil its sales commitments to Brazil.<sup>200</sup>

### **3 The Counterfactual Argument**

A counterfactual in an evolving system can be viewed as branches in a tree. Branching points represent decisions in the past which determine future outcomes. In each of the historical chapters, the counterfactual branch starts when a different policy decision is assumed to have been taken at the beginning of each period. In an evolutionary system, initial conditions are extremely important. This section extends the counterfactual from the beginning of the second time period through to the present day to provide a comparison with what actually happened.

In the sixty years prior to World War 1, more than forty million people left Europe for opportunities in newly settled countries. This was the largest European migration in history. Their destinations included Canada, the United States, Argentina and Australia. Given the prevailing push factors for emigration, it is highly likely that Canada would have attracted a proportion of these immigrants had economic prospects compared well with those of alternative destinations. Government intervention was an attempt to accelerate a development process which would have occurred at a much slower rate.

A slower rate of settlement would have had a number of benefits. The frontier would have moved more in concert with the technology changes that ultimately made extensive arable farming on much of the prairies commercially viable. Experimentation with wheat would have gradually determined where the commercial frontier of wheat production actually lay. Most importantly, recent immigrants would have more realistic expectations regarding the

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200 Brazil and Argentina are neighbours and both members of the Mercosur free trade area. The surge in demand for soybeans in Asia has resulted in Brazil becoming one of the world's largest wheat importers and the biggest exporter of soybeans simultaneously. Similar policies have affected beef exports. Argentine beef exports were banned in March 2006 for 180 days and when that restriction was lifted a fifteen per cent tax on was imposed on beef exports. Producers responded by reducing production and by 2012 Argentina had dropped to 11th place among exporters (behind Paraguay and Belarus).



agricultural potential of the region, and would not therefore feel victimised by government propaganda.

The Palliser's Triangle area would not have been settled so quickly, or so extensively. This would have reduced both the number of homesteading entries and the number of people who left the region due to its hostile environment. Much hardship and suffering would have been avoided. It would also have reduced the number of people already living in precarious circumstances when the Depression hit in 1929. The Wheat Boom would have been less exaggerated, and the impact of downward corrections would have been less pronounced.

In the absence of the very strong institutional bias in favour of wheat growing, the livestock industry, established prior to 1896, would have been able to expand as markets developed. There would have been no pressure to curtail the development of the cattle ranching industry or cancel its grazing leases. Leaving natural grassland for grazing would have avoided the dustbowl conditions which severely damaged large areas of land in this portion of the region during the Dirty Thirties, and during the dry-belt disaster a decade earlier.

The pace of settlement would have been heavily influenced by the willingness of railway companies to expand their networks based on commercial prospects alone. There was little use producing wheat if there was no means to get it to market. Without government support it is likely that neither of the two additional transcontinental lines would have been built before the Depression. Fewer branch lines would have been built and a lot of duplication avoided. With less pressure for extension of branch line networks, the railways would have concentrated on providing adequate rolling stock to existing lines before building new track. This would have alleviated the grain blockades which occurred periodically due to mismatch between railway capacity and the volume of crops to be shipped to the Lakehead.

Without railway problems caused by overbuilding and the additional costs associated with public/private partnership arrangements, the government would not have found itself the owner of a railway and having to spend one third of its badly needed Depression budget to cover railway costs. Canada might have avoided the rut of regulation and subsidization which led to a deteriorating grain handling and transportation infrastructure and ultimately impaired the country's ability to get prairie grain and oilseed crops to export markets.

The exaggeration of the 'swarm-like effect' was a consequence of zealous promotion of settlement by politicians and interest groups imbued with the Expansionist ideology. The

objective of the prairie settlement component of the national policy was to fill the region with settlers. This objective was pursued without regard to the situation in the region or the economics of wheat production. Although there may well have been no malign intent on the part of those who organised this experiment, it is easy to understand why prairie farmers felt victimised. Any and all interventions by the federal government prior to the Depression (with the possible exception of the Hudson's Bay Railway) were interpreted as benefiting 'the East' (e.g. Fowke, 1978; 1968: 217). National policy objectives were the root cause of western alienation.

Had the federal government had not tried to support wheat growers during the Depression with assistance tied to wheat production and had instead provided funds to the provincial governments to distribute as originally envisaged, expectations of continued government price support for wheat production might have been avoided. Without this bias, the Wheat Board may not have become 'a temporary wartime expedient' that persisted for more than 70 years.

Without the Wheat Board quota system, farmers would have likely experimented with crop diversification and relied less on summerfallow. Producers overall would have been able to produce the same volume of wheat on less land, which might have meant fewer wheat farmers but higher incomes. A less extensive land use pattern also requires a less extensive grain elevator and rail network – both would have been more efficient. In the absence of institutions such as the Canadian Wheat Board, railways and grain handling companies would have had a more straight-forward business arrangement.

The situation to which the counterfactual leads if followed through to the end of the fourth time period in the model, is remarkably similar to the situation that actually exists today. The grain trade is in private hands again. The railways are making money transporting grain. The prairie agricultural economy is much more diversified. Furthermore, Canada and the U.S. have a free trade agreement in effect, and both Canadian railways now have extensive operations in the United States. Grain moves south in significant volumes, as well as to west coast ports in Canada and Thunder Bay. It seems likely that the social and political backlash against the concerted efforts made to dramatically accelerate prairie settlement after 1896 set the agricultural economy of the region off on long and unnecessary detour. It took over a century for that detour to return to the institutional environment under which it started.

The overall conclusion reached by this study is that all the benefits of an agricultural economy on the Canadian prairies could have been realised with less cost to the taxpayer and much less suffering on the part of those who tried, often unsuccessfully, to establish viable commercial farms in the region. Several of the interventions which changed the institutional environment in which prairie agriculture evolved had unfortunate consequences. The costs of these negative consequences were borne primarily by prairie farmers and Canadian taxpayers. Those costs would have been orders of magnitude less had the interventions responsible been avoided.

When the state attempts to facilitate development it is in essence trying to make anticipated events occur sooner than they otherwise would. There was a marked difference between the technology those lured into the 'development project' tried to use (e.g. growing wheat) and the technology which was commercially viable at the time over much of the region (e.g. extensive grazing). Economic conditions do change, and entrepreneurship is all about testing opportunities to do something differently in order to determine whether it is profitable or not. Notwithstanding the very rapid pace of technical change in the grain industry at the time, the federal government forced the pace. In the process, they increased the rate of settlement but slowed the pace of technical change.

## **4 Why Policies Fail**

### **4.1 Problems of Definition**

Before addressing the question of why some policies fail, it is important to acknowledge that there is no black and white definition of what constitutes good and bad policy outcomes. First, policy objectives may not be clearly defined, which makes it difficult to determine whether or not they have achieved their goals. For example, objectives such as 'development' are vague but were used to justify many of the interventions which changed the institutional environment of the region at the end of the nineteenth century, just as they are used today to justify spending on a broad spectrum of projects

In addition, there are often problems quantifying some of the costs and benefits. These problems may be caused by the complexity of the environment, the point of view of the observer or the intangible nature of some of the costs and benefits themselves.

Interventions always lead to some winners and some losers, so what may benefit one individual or group may disadvantage another. Outcomes will therefore be judged differently by the various groups affected. As noted in the quote from Dales in Chapter 2,

economists and historians use different evaluation criteria, and historians tend to claim the national policy as a success, while economists are more skeptical. It was for this reason the success criteria adopted in this study used prairie farmers and taxpayers as the reference groups. Taxpayers have been called upon (indirectly) to support prairie agriculture in myriad ways since the onset of the Depression. The human cost of settlement failure was considerable, but it is still difficult to quantify. Assessment is exacerbated by the fact that it is the successful migrants who are disproportionately represented in the history books (e.g. Dick, 1989).

The timeframe chosen can also affect how policy outcomes are judged. In the case of many 'development projects', the evaluation is undertaken while the project is being implemented or shortly thereafter. This minimises the opportunity for negative consequences to surface. For this reason, prairie agriculture has been examined over a long time period. When viewed over an extended time frame and by looking at its impact on prairie farmers and Canadian taxpayers, institutional changes in the prairie agriculture sector between 1896 and 1980 have increased transaction costs and reduced the sector's competitiveness.

#### **4.2 What Causes Dramatic Changes in Public Opinion Regarding the Role of Government?**

This study of the interaction between government policies and economic performance over an extended period of time is unusual because there were two turning points which led to a substantial shift in attitudes toward government intervention in the economy. The work of North and Higgs discussed in Chapter 2 suggests that in the U.S., a change in attitude toward the role of government occurred in the Progressive Era, and as a consequence an increasingly interventionist response to subsequent crises encountered minimal opposition. A similar pattern is evident in Canada, apart from the fact that the ideological shift seems to have received much more of its impetus from frontier wheat production on the prairies than was the case in the United States.

Crises, the availability of new ideas, political leadership, competitive pressure or prior examples and lack of opposition have been suggested as factors that may contribute to acceptance of 'reforms' that reduce government constraints on economic behaviour. This study has considered Schumpeter's suggestion that crises stem from the unanticipated consequences of some prior government intervention, and a crisis may be the tipping point beyond which government willingness to intervene may be quite different from the *status quo ante*. The ideological shift that begins in the lead up to the next major crisis seems to

create a predisposition towards a particular course of action. It is during this gestation period that the ideological shift is nurtured by ‘underemployed intellectuals’. This explanation does seem to fit the pattern of events on the Canadian prairies leading up to the Depression.

During the first two decades of the twentieth century prairie farmers faced common problems and developed organisations which reflected that homogeneity. As has been emphasised, the grievances which gave the agrarian populist movement its cohesion were legacies of the national policy. Through religious and farm organisations they were exposed to the social gospel and socialist political theories. Grain growers’ organisations urged the federal government to act on behalf of farmers to curb what they regarded as the monopoly tendencies of the grain marketing, handling and transportation companies with whom they had dealings. Although some action was taken, and the government appeared supportive, its involvement fell well short of that expected by the more radical elements in the farm movement. When the Depression struck, the crisis created pressure for more government involvement as Schumpeter anticipated. This led to the bailout of the largest cooperative grain marketing agency, the Wheat Pool’s Central Selling Agency, and a series of subsequent interventions that ultimately led to the creation of a compulsory Wheat Board which lasted over seventy years.

There was another ideological shift in the lead up to the second-turning point, which occurred in response to the ‘looming’ crisis of the 1970s. Prairie agriculture has been the *target* of the institutional changes made since 1980, but much of the impetus for change – the ideological shift – was stronger outside the sector than it was within.

Over the last half century a number of serious undesirable consequences of government intervention that affected prairie agriculture became apparent. Opinion among prairie farmers was sharply divided over the government action required to address those problems. The impetus for the changes has come from a variety of sources: taxpayer alarm over out-of-control government spending, concern within government that the assistance prairie agriculture was receiving was an open ended financial obligation and a potential trade irritant, and concern that rail capacity issues were impairing exports from other sectors besides grain. The initial steps to address the freight rate issue were advocated by and two political entrepreneurs keen to do what was necessary and the Liberal government at the time had almost no support from the West and therefore little to lose.

This ideological shift was much weaker than that which preceded the Depression on the prairies, was more widely diffused, and the 'crisis' in which the first steps were taken to rollback government intervention was not comparable to the 1930s. The fiscal conservatism of the western protest parties in the late twentieth century was targeted more at extravagant social programmes, multiculturalism and government funding for businesses based in central Canada rather than in any wholesale adoption of liberal principles.

Steps have been taken to deal with interventions perceived to be causing major problems for the prairie grain sector, but the focus has been on the grain handling and transportation business rather than on the business of farming. Prairie farmers are understandably ambivalent about the process as it has unfolded to date, and more recently have been persuaded to agitate for re-regulation rather than more comprehensive deregulation.

#### **4.3 What causes negative policy outcomes?**

The history of western Canada's agricultural sector provides insight into why policy interventions often have unintended negative consequences when evaluated from the perspective of the taxpayer or ordinary citizen.

Policies may have value over the short term, whereas the unintended negative consequences become apparent only as circumstances change over time, as they inevitably will. Fixing freight rates in perpetuity did not anticipate subsequent inflation and serious difficulties ensued when it became pervasive.

Policymakers all suffer from the knowledge problem to varying degrees. Most of the major policy interventions outlined in this study were less successful than anticipated because those involved in the negotiation or design lacked some crucial information. Hence the decision to promote settlement on the prairies as part of the national policy was taken without asking any questions about the economic viability of wheat production in the region, nor was there any appreciation of the difficulties faced by those farming in the region.

Both political actors and other interest groups are affected by the incentive problem. Entrepreneurship, particularly in Canada West, involved extraction of benefits from the political process in exchange for political support. Eichengreen (1995) uses the example of 19<sup>th</sup> century Canadian infrastructure projects as a cautionary tale for modern 'developing' countries. He describes the perverse incentives that resulted from government bond

guarantees for canal and railway production in terms of the work of Akerlof and Romer (1993) on the U.S. savings and loan ‘crisis’ of the 1980s. In extreme cases, looting the state becomes a more attractive objective than completing the project and operating it as a going concern (see also Carlos and Lewis, 1995).

This pattern of behaviour is consistent with that outlined by Krueger (1993). The soon-to-be governors of post-Confederation Canada opted for the ‘vicious circle’ of corruption and dissipation of wealth instead of the ‘virtuous circle’ of development, despite the rhetoric of ‘nation-building’. This has been a pervasive problem in more recent post-colonial administrations.

Policies may have unintended consequence, as Wheat Board quotas did on land degradation. The political process always involves trade-offs, so the final legislation may not mirror the original aim. Policies may have been poorly crafted or not completely able to address the problems they set out to solve. The ‘five cent bonus’ scheme early in the Depression was quickly recognised as a mistake because it gave additional funds to those who were better off (if only in a relative sense) and those worst off got no help. This example also illustrates how ‘knowledge problems’ are exacerbated by crises when the pressure to act quickly is greater.

The political process involves compromise, and political strength is frequently an obstacle to policies that are intended to improve economic efficiency. Changes initially made to the statutory freight rate in the 1980s involved a pay-the-producer recommendation. This proved unacceptable to the Wheat Pools and Quebec farm sector so modifications were made which sharply reduced the benefits. The same has been true with the ending of the Crow Gap payments – where first the ‘rate cap’ and then the ‘revenue cap’ limited the benefits available to the users of rail services.

Since policies always create winners and losers, they may lead to intervention cascades whereby those adversely affected by an initial policy pressure government to redress the loss via another intervention. Prairie settlers felt victimised by the national policy, but it was not until the Depression made their situation pitiful that their appeals for redress were heeded. Prairie farm groups paved the way for the ideological predisposition toward intervention that pervaded all aspects of Canadian society in the post-war period. Unintended consequences of the major interventions in prairie agriculture after the war coupled with the predisposition towards intervention led to subsidies to offset other

subsidies: the national feed-freight assistance programme provided a freight subsidy to feed grain users outside the prairies to offset the consequences of statutory freight rates on exported grain. When the WGTA changed the rules again, the provincial governments in the prairies provided a subsidy to *their* livestock producers because the impact of the changes made on the sector were not those expected.

#### **4.4 Why does popular support persist for measures after their negative consequences are known?**

This case study demonstrates that interventions are easier to implement than dismantle, and that once in place they may persist well after their value has been dissipated. Since markets provide a mechanism whereby the economy adjusts to the new constraints inherent in each institutional change, once the process has worked through the system there is reluctance to embark on a new round of adjustments. Pressure to maintain the *status quo* may be mounted by those who believe they enjoy an advantage from the legislation and might lose that advantage under new rules. Amending a policy will cause significant short term adjustment problems with adverse economic side-effects, even though the potential general benefit is desirable.

Even though interventions may be detrimental in the medium and longer term, the benefits tend to be more obvious and immediate. Costs may be widely dispersed and less apparent, with less importance being attached to them as a consequence. Prairie farmers recognised the value of the low cost rail transportation, but did not appreciate the system-wide implications: low freight rates are no longer a benefit when there are insufficient railcars to move grain out of the region.

Individuals also interpret events or circumstances according to their own world view. They may apportion blame for their problems incorrectly as a result. During the period in which the social gospel was a dominant influence on prairie farmers it was difficult for them to see large entities such as the CPR and the private grain companies as businesses like their own and hence as potential partners. In the post-war period, prairie farmers caught up in the ideological legacy of the agrarian populist movement held views diametrically opposed to those who joined organisations such as the Palliser Wheat Growers Association.

Ideological resistance to change tends to be strong, because change involves relinquishing a previously held world view. This is one of the reasons a government intervention which disrupts the normal patterns of interaction in society seems to be necessary to change a



longstanding belief that less government is better. When the entrenched ideology supports a great deal of intervention, those who benefit are understandably inclined to generate supportive propaganda. As North and Higgs pointed out, before the Progressive Era, special interest groups were often denied the extra-market benefits they sought. Since the ideological shift, it has become easier to capture rents from steering intervention than from competition in the market place, so investments are made in keeping that ideology alive. On the deregulation side of the coin, the government also has a much larger role to play, and is reluctant to have the ideology which supports its role tarnished.

### **5 Opportunities for Further Research**

This study suggests numerous opportunities for further research. Those of particular interest include:

- 1) Technical change is the key to determining whether an economic process is generating development or growth. The diffusion of arable farming into the prairies was heavily influenced by public policy, and this study suggests that the longer term consequences of that influence were adverse. Enthusiasm to accelerate ‘development’ resulted in unsustainable growth and a prairie grain sector that would be a drain on the national economy for decades. ‘Innovation’ is a term now being used to justify sweeping government intervention. This suggests a need to better understanding of how public policy affects technical change in general.
- 2) Canada’s traditional competitors in the international grain market -- Australia, Argentina, Russia and the United States -- provide a wide array of different institutional arrangements for comparative purposes. Some preliminary discussion of Russia and Argentina was provided earlier in this Chapter. These could be expanded and similar comparisons made with the institutional environments which have affected grain production in Australia, the United States and the European Union.
- 3) Canada and the United States share many characteristics, including the close physical proximity of their respective wheat belts. However, the grain sectors in the two nations have evolved quite differently. Canada has a more centralised political system with considerable power residing in the Prime Minister’s Office and regional representation based on population. The U.S. congressional system serves as a counterweight to executive branch authority and there is strong regional representation in the legislative process. There is therefore an opportunity to explore how different legal and constitutional arrangements may have influenced the agricultural sectors in the two

countries. The trajectories of technical change in the two jurisdictions have at times diverged and at others converged. The institutional frameworks that resulted in the different institutional environments and their influence on technical change in grain production and in the GHTS should be of particular interest.

- 4) In order to ascertain the longer term consequences of institutional change on prairie agriculture this study has, of necessity, taken a high level view. Each of the potential turning points identified in this analysis provides an opportunity for more detailed investigation. Of particular interest is the process whereby the government became the 'ally' of the prairie farmer, but the regulatory regime endorsed by the ideology of the agrarian protest movement was captured by the grain handling and transportation components of the sector. Once these organisations had a 'seat at the table' they had an opportunity to influence modification of the rules. Farmers, on the other hand were allocated equitable access to the available market under the Wheat Board system, irrespective of their efficiency.
- 5) Steps were taken to deregulate prairie agriculture relatively recently, and the process is proving to be even more fascinating than the agrarian populist movement which preoccupied Canadian academics in the last century. Further monitoring is required to determine the medium-to-longer term consequences. Much more detailed work would be required to confirm trends identified in this study. Comparisons of the process in prairie agriculture with other instances of agricultural deregulation would be instructive. Recent evident of 'back-sliding' in the prairie case seems to be a consequence of the gradual approach taken and the inability of the farm population to capture the full extent of advertised benefits of deregulation. This linkage has important implications for the debate over whether 'big bang' institutional changes are feasible when only in the wake of an extremely serious crisis. This study suggests any steps toward re-regulation will lead to outcomes quite different to those anticipated at the outset, while the disadvantages absorbed by the many generating benefits for the few.
- 6) The impact of regulation on agricultural land use remains controversial, and regulation justified in the name of 'environmental protection' can have significant unintended consequences. Land use in prairie agriculture has recently changed dramatically in response to a radical change in the institutional environment. Many of those changes have been welcomed by agronomists and soil scientists, although the environmental implications were not part of the rationale for the changes made. Rapid changes in land

use on the Canadian prairies invite comparison with the situation across the border in the United States where the institutional environment has not changed substantially, but was very different to that in effect in Canada before the recent changes.

### **6 Concluding Comment**

The history of agriculture on the Canadian prairies illustrates the dangers involved when government policy is justified by ideologies in which economic considerations play no part. In Schumpeterian terms, the objective of Canada's efforts to 'develop' the prairies in the nineteenth century was growth of the national economy, not improvement of the living standards of the population. The policy of accelerating the diffusion of wheat production across the region exacerbated the impact of the Depression of the 1930s.

The earliest settlers objected to government efforts to encourage settlement in the region when wheat growing was unprofitable. An agrarian populist movement fuelled by the social gospel and a cooperative ideology took on increasingly socialist overtones. Farmers' organisations redirected distrust of the middlemen who linked the prairie grain economy with distant markets towards institutions such as the grain exchange and the railways. This significant ideological shift was reinforced by the very severe impact of the Depression on the region, as Schumpeter anticipated. The prairie grain economy was controlled by the government when it emerged from World War II.

Dissatisfaction among prairie farmers reappeared in the post-war period as the unintended consequences of the new institutional framework reduced the competitiveness of prairie grain in international markets. Prairie farm organisations became increasingly polarised over whether government involvement was the problem or the solution. The first steps were taken towards dismantling some of the high profile institutional infrastructure before a severe crisis occurred. Upgrading to competitive grain handling and transportation technology was frustrated by the piecemeal approach to deregulation. The difficulties encountered unwinding counterproductive institutions that had evolved together over an extend period of time were additional complications.

It remains to be seen whether the deregulation process will falter or continue. At the beginning of the twentieth century farmers took a strong stand against granting government favours to special interests and the consequences of government intervention were unknown. The impact of any future interventions cannot be predicted with accuracy: the

consequences of changing complex evolving systems are difficult to predict because they distort the feedback on which subsequent adjustments will be based.

The adoption of new technology will generate benefits in the form of efficiency improvements. Schumpeter argued that the benefits of technical change are evenly distributed only when competition is encouraged. For this to occur, pressure to re-regulate has to be resisted. In this context the mobilisation of prairie farmers to support the Fair Rail for Grain legislation suggests that ideology may still be ascendant over self-interest, and the re-regulation of the transportation of prairie grain by rail remains a distinct possibility. If that does turn out to be the case, the recent transition from 'growth to development' will be short-lived.

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