6. In appraising the subject of possible sales to China of substantial quantities of grain, and particularly if credit is required, it should be noted:

(1) The demand situation in China affords an opportunity for Canada to develop our immediate and long-term interest in a market which may very well be a continuing buyer of wheat in volume. In this particular connection, there would be considerable advantage in consolidating our position as a supplier at this time.

(2) Volume sales to China would have a major impact on the Canadian wheat position. Given the level of wheat production experienced during the last few years, carryover stocks would be reduced to what could be considered a working inventory level. Additionally, increased marketings of grain by producers resulting from volume sales to China would substantially increase western farm income.

(3) Such credit sales may weaken Canada's bargaining position in restraining United States credit sales in other areas. There could also be interest on the part of other exporting countries and, in fact, Australia has already indicated that they are also examining further sales to China and have enquired about our intentions. The likelihood of adverse effects would depend in some degree on the extent to which our action was explained in advance to the United States and other interested countries. Insofar as this sale would remove a substantial quantity of wheat from western markets, it might in fact be welcomed and the friction among western countries over surplus wheat disposal might be lessened at least for a time.

(4) If the sale is for cash and if the agreement takes the form of a contract between the China Resources Company and the Canadian Wheat Board, it should not give rise to any special problems in our external relations. However, if credit is to be extended, both domestic and external attention, particularly in the United States, would be focused on such wider questions as our political relationship with China, including recognition. If credit were to be granted through normal export credit insurance arrangements involving an intergovernmental exchange of letters, the issue of recognition would be directly raised. It would seem desirable at next week's meeting of the Joint United States-Canadian Committee on Trade and Economic Affairs for Canadian Ministers to let their United States colleagues know, at least informally, of our interest in the China market, particularly since it is expected that there will be a full discussion of surplus disposal problems at this meeting. It can be safely assumed that the United States will already have some knowledge of the nature of the negotiations with China; moreover, there is also an obligation for all NATO countries to report any credits extended to countries in the Sino-Soviet bloc.

Conclusions

The Chinese proposal represents a potential transaction of great importance to Canada. In view of the various political and commercial implications, every effort should be made to sell for cash. However, given the potential volume of this business, limited credit not exceeding 180 days (a period not without precedent for private commercial sales) should be contemplated if this proves the only possibility, notwithstanding that uncertainty about China's foreign exchange position does not rule out the possibility of default. Given the two possible mechanisms for credit referred to in this memorandum, it would seem that fewer problems would be created by agreeing to extend the line of credit to the Wheat Board rather than amending the Export Credits Insurance Act.

It is recommended that:

(a) The Minister of Agriculture be authorized to instruct the Chief Commissioner of the Canadian Wheat Board to proceed with negotiations with representatives of the China Resources Company on the following basis: