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To: Members of the Executive Board

From: The Secretary

Subject: UNCTAD - Committee on Commodities - Twelfth Session

Attached for the information of Executive Directors is a report by the Fund observers on the twelfth session of the UNCTAD Committee on Commodities, held in Geneva from February 2 to 16, 1987.

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INTERNATIONAL MONETARY FUND

UNCTAD--Committee on Commodities
Twelfth Session

Report by the Fund Observers 1/

March 16, 1987

Summary

The UNCTAD Committee on Commodities held its twelfth session in Geneva during February 2-16, 1987, under the chairmanship of Mr. N. Parameswaran of Malaysia. The purpose of the session was to analyze the current situation and prospects in world commodity markets, to assess the results of the actions pursued by the international community in the commodity field, and to suggest additional remedial measures for consideration at UNCTAD VII.

The most provocative statement made at the Session was that of the representative of the UNCTAD secretariat--the Officer in Charge of the Commodities Division--who argued that the failure to implement the Integrated Programme for Commodities (IPC) embodied in Conference Resolution 93 (IV) left UNCTAD members with no other alternative than to adopt a new strategy in the commodity area. He suggested that such a strategy should include, inter alia, a substantial liberalization of tariff and non tariff barriers maintained notably by the developed countries but also by the developing countries themselves on commodity trade; the mobilization of additional financial resources for the compensation of export earnings shortfalls and for development programs and projects in the commodity sectors of the developing countries; and the establishment as appropriate of international study groups for individual commodities designed to increase market transparency. This suggestion was favorably received by Group B countries which agreed that the IPC should be deeply revised in the light of the structural changes which had affected the world economy since its adoption in 1976. But it was strongly opposed by the Group of 77 which argued that the failure to implement Conference Resolution 93 (IV) was due to a lack of political will on the part of the industrialized countries, that the Resolution was now more valid than ever in view of the depressed conditions prevailing on comodity markets, and that it should be fully reaffirmed at UNCTAD VII. Despite intensive discussions it was impossible to surmount this sharp divergence of views among two major regional groups, and the Committee limited itself to taking note of the statements made by the participants.

1/ Messrs. Carlos E. Sanson and Mr. Jack P. Barnouin.

I. Statement by the Representative of the UNCTAD Secretariat

The representative of the UNCTAD secretariat said that since 1980 the UN commodity price index had fallen at an average annual rate of nearly 5 percent, as against an increase of over 8 percent a year in the previous two decades. While the short-term fluctuations in commodity prices had continued to reflect cyclical changes in the economic activity of the industrialized countries, the downward trend in the medium run had been due to the interplay of factors of a structural nature both on the demand and supply sides. Among those factors, he mentioned, on the demand side, the growing importance of the service and high technology sectors--which use little or no raw materials--in the economic activity of the industrialized countries; the increasing substitution of traditionally used materials such as steel, copper, and aluminium by synthetic materials such as plastics, ceramic composites, and optical fibers; a continuing shift in dietary habits in developed countries away from high caloric foods; the relatively high level of interest rates in real terms which discouraged the accumulation of stocks and provided an incentive to dispose of existing stocks; and last, but not least, the agricultural support policies of major industrialized countries which had not only resulted in a severely reduced domestic demand for agricultural imports, but also had led to higher export availabilities. On the supply side, he referred to a number of other factors such as the lagged response of the supply of metals and of certain agricultural products (tea, coffee and natural rubber) to price changes and the efforts made by developing commodity exporting countries to compensate for the fall in commodity prices by an increase in the volume of their exports. Given this background he found it difficult to be optimistic about the future of commodity prices because the beneficial impact of any upsurge in the economic activity of the industrialized countries on those prices was bound to be substantially attenuated by the adverse influence of the structural factors at work.

Turning to the current status of international action on commodities, the Secretariat representative noted that over the past decade or so such action had stemmed from the IPC, which had been adopted on May 30, 1976. This Programme, he recalled, contemplated, inter alia, the establishment of a Common Fund (CF) for the financing of international commodity stocks, guaranteed national stocks, or other necessary measures within the framework of commodity arrangements; the negotiation or renegotiation of commodity agreements designed to achieve stable market conditions and/or trade promotion for 18 specified commodities; the improvement and enlargement of existing compensatory financing facilities for export earnings shortfalls; improved conditions for the processing, marketing and distribution of the above mentioned 18 commodities; and enlarged market access for the primary and processed products of developing countries. Progress on all these fronts had been extremely disappointing. The CF Agreement, although adopted ad referendum in June 1980, had not yet entered into force as the capital subscribed by the countries which had ratified it amounted to 58.51 percent of the total as against the 66.6 percent target required by the Agreement. The prolonged state of uncertainty about the implementation of the CF had tended to inhibit further international cooperative actions on commodities. It seemed therefore timely to put an end to that uncertainty by setting a deadline for the ratification of the Agreement.

As regards negotiations on individual commodities, the Secretariat representative recalled that a new international agreement with price provisions had been sucessfully concluded since the launching of the IPC (natural rubber) but two of the four agreements with similar provisions which existed at the time of the adoption of the Programme (sugar and tin) had become inoperative. Two other new agreements had been concluded (jute and jute products, and tropical timber) but those agreements included only research and development provisions. Despite intensive discussions on the eleven other commodities listed in the IPC no progress had been made towards the conclusion of agreements except, in some cases, for the formulation of certain research and development programs which could not be implemented because of a lack of finance. This clearly showed that the strategy on individual commodities needed to be reconsidered bearing in mind that not all commodities were amenable to the same remedial measures.

With respect to compensatory financing, some improvement had been introduced in the IMF CFF and in the ECC STABEX but the work in UNCTAD on the establishment of a commodity-specific complementary financing scheme had not led to any results despite eight years of intensive studies and discussions. The efforts made in UNCTAD for establishing multilateral frameworks of cooperation for the processing, marketing and distribution of commodities had also failed to yield tangible results. Finally, the problem of trade barriers affecting the export of primary and processed commodities was now more serious than ever despite the efforts made by the international community to reduce such barriers. Given the substantive difference that had emerged among and between groups of countries regarding various issues, the Secretariat was extremely doubtful "about the potential fruitfulness of continuing with the present strategy."

Turning to the future, the Secretariat representative stressed that the disappointing record of performance under the IPC did not cast doubt on the validity of the Programme's basic objective which was to eliminate the "economic imbalance between developed and developing countries." What was needed was a fundamental change in the strategy to be followed for achieving that objective. A promising approach under the new strategy was the liberalization of barriers to trade in primary and processed commodities by the industrialized countries and by the developing countries with the aim of fostering the expansion of commodity trade not only between the South and the North but also within the Third World itself. The Uruguay Round in GATT, the General System of Preferences (GSP), established under UNCTAD auspices, and the General System of Trade Preferences (GSTP) among developing countries provided a workable framework for action in this area. A second approach to be explored referred to the mobilization of additional financial resources not only for the compensatory financing of export earnings shortfalls but also for long-term development programs and projects in the commodity sectors of the developing countries. A third area for action was that of possible improvements in the domestic policies followed by the developing countries in the field of commodities including the granting of appropriate incentives to producers. A fourth option to be pursued was the conclusion of international agreements with price provisions where appropriate conditions existed for the successful implementation of such agreements, including the participation and support of the major producing and consuming countries, the setting of price targets at market-related levels, and the mobilization of adequate financial resources for buffer stock operations. Consideration also should be given in some cases to more flexible forms of cooperation between producers and consumers such as the establishment of international study groups which would undertake such activities as increased market transparency, identification of research and development projects and consideration of remedial measures for special problems.

II. General Debate

The spokesman for the Group of 77 was "surprised, deeply concerned and disappointed" that the Secretariat was abandoning commodity price stabilization as a goal to be pursued by the international community. He considered that the new strategy suggested by the Secretariat was totally inadequate because it was based exclusively "on research and development, market transparency and domestic policies." He emphasized that the approach embodied in the IPC was more valid than ever in view of the depressed conditions prevailing on world commodity markets and he called on all the countries which had not done so, particularly the major contributors, to sign and/or ratify the CF Agreement.

He also stated that efforts to improve existing International Commodity Agreements (ICAs) and to negotiate new agreements should be pursued and that in this endeavor parallel emphasis should be put on market stabilization and product development. He reiterated that his group attached particular importance to the improvement of existing facilities for the compensatory financing of export earnings shortfalls and for the establishment of a commodity-specific complementary facility. Finally, he regretted the lack of progess in the elaboration of a framework for international cooperation regarding the processing, marketing and distribution of commodities, and he suggested that further efforts should be made to identify the elements which could be included in such a framework.

The representatives of a number of developing countries (Argentina, Brazil, Ecuador, Egypt, Indonesia, Ivory Coast, Mexico, Nicaragua, Nigeria, Peru, the Philippines, Sierre Leone, Uruguay, and Venezuela) intervened in the debate to support the statement of the Group of 77.

The Spokesman for Group B said that the overall commodity price index in nominal terms after reaching a peak in 1979/80 had fallen substantially since then except for a brief rally in 1983/84. In real terms this index was now at its lowest point since the Second World War. The root causes for these low prices were complex, reflecting the interplay of macroeconomic and structural factors as well as those deriving from the characteristics of individual commodities. While any generalization was difficult it was clear that, together with recognized cyclical factors, structural factors were also at work to depress commodity markets. Among these factors, he mentioned a shift in global demand from goods to services in the industrialized countries, a less intensive use of raw materials in the manufacturing sector as a result of far-reaching technological changes, and the pursuit by certain countries of "international policies, including domestic support and exchange rate policies, which did not reflect the need to maintain the real effective competitiveness of the economies concerned." His group concluded from that assessment that the structural problems which confronted the commodity sector required structural remedies which could bear fruit only in the long run. While it was up to UNCTAD VII to define such remedial measures, a mere reaffirmation of Conference Resolution 93 (IV) would only contribute to perpetuate a situation that all UNCTAD members considered to be unsatisfactory.

The representative of the United States said that demand for most commodities continued to grow but at a slower rate than in the past. The depressing effect of that slowdown on the demand side was exacerbated by the increasing rigidity of supply in adjusting to changing market circumstances, particularly in some developing and developed countries where output was increasing despite falling prices and rising capacity. That issue as well as other outstanding issues in the commodity area needed to be further analyzed on a commodity-per-commodity and a country-per-country basis because the factors at work both on the demand and supply sides affected differently individual commodities and countries. Such further analysis should be "for analytical rather than prescriptive purposes and should fully recognize what was already being done by the international community in terms of financial resources and market access for commodities." In this context, he emphasized the important role played by the adjustment facilities provided by the IMF and World Bank.

The representative of Japan stated that the approach adopted by UNCTAD in the commodity field a decade ago needed to be thoroughly reviewed in the light of the structural changes currently affecting the world economy. He felt that the statement made by the Secretariat representative contained various constructive and useful suggestions and he agreed that a more pragmatic and flexible approach should be adopted on commodity problems, bearing in mind that not all commodities were amenable to the same type of action. Moreover, the "commodity-focused" approach traditionally followed by UNCTAD should be complemented by a "country-focused" approach which would make it possible to deal with commodity issues in the wider context of the development problems of the countries concerned.

The spokesman for the European Communities agreed that increasing emphasis should be put on economic diversification in developing commodity exporting countries and that such diversification should be based "on dynamic comparative advantage as reflected, inter alia, in unit cost of production." While the IMF, the World Bank and the regional development banks were actively supporting this process of structural adjustment, the EC had also made a conscientious effort to respond to the problems confronted by exporting countries. In this connection, he mentioned the provision of compensatory financing through STABEX to the ACP countries covered by the Lome Convention and to a substantial number of least developed countries which were not part of that convention; the operations of the SYSMIN facility which provided financial support to ACP countries, not only for revival of mining production capacity but also for diversification purposes; and the role played by the European Development Fund to finance structural adjustment programs in the same countries. Turning to the question of market access, he argued that "the EC market was one of the most open in the world both for industrial and agricultural products." His authorities, nevertheless, recognized the need to put order in the world agricultural market and they subscribed fully to the Punte del Este Declaration which expressed the willingness of the major trading countries to undertake serious negotiations in this field.

The representative of Norway said that ICAs with economic provisions constituted a valid option for stabilizing commodity prices and that further work on such agreements should be pursued on the basis of the principles adopted by consensus at the eleventh session of the Committee. However, where conditions did not exist for the successful operations of such agreements, his authorities supported the conclusion of new forms of agreements concentrating on research and development problems and/or the establishment of international study groups designed to improve market transparency. They also supported the enlargement of existing compensatory financing schemes for export earnings shortfalls and were open to the possibility of establishing a commodity-specific complementary facility.

The representative of Sweden said that given the gloomy outlook for most commodities, developing countries should intensify their efforts "to diversify away from dependence on commodity exports." The attainment of this goal required a general improvement in the world economy, further trade liberalization and a better functioning of commodity markets. The problem of compensatory financing for export earnings shortfalls should also be reconsidered in the light of the development needs of Third World countries.

The representative of Australia said that commodity exporting countries were dramatically affected by the widespread price collapse in many primary commodity markets. His authorities were strongly of the view that the most effective action the industrialized countries could take was to correct "the distortions introduced into patterns of trade and production through the market-access, income-support, and export-subsidy policies pursued by certain of them." Nowhere was the need for action greater than in the agricultural sector where the rise in subsidies should be halted and the gap between internal prices and international prices should be progressively reduced. His authorities, therefore, believe that at UNCTAD VII, governments should agree on the urgent need to improve the functioning of commodity markets through trade liberalization and a comprehensive reform of existing agricultural support policies.

The representative of Canada said that improved market access for primary and processed commodities was a sine qua non condition for achieving diversification of the production and trade structures of developing countries. The Uruguay Round offered the best means of coming to grips with the causes of that difficult and complex set of problems.

The spokesman for Group D stated that "a close link existed between the crisis in commodity markets and the economic policies of western countries including protectionism and subsidization of exports" and that "market mechanisms were unable to eliminate or even attenuate the enormous imbalance observed in commodity markets." This highlighted the need for a further strengthening of the role of UNCTAD in three basic areas: the increased participation of developing countries in the processing, marketing and distribution of their commodities, larger market access for these commodities in the industrialized countries, and the stabilization of commodity markets. As regards the latter area, the best way to achieve progress, he said, was the conclusion of ICAs of a new type such as the recent International Cocoa Agreement, which "recognized the importance of flexible mechanisms to react to changing conditions."

The representative of China referred to the downward trend followed by the prices of most commodities in recent years. Among the many factors responsible for that dismal performance, the Committee should examine those which were of a distinct policy nature. He mentioned in particular "import limitations and quotas, discriminatory treatment, import duties, internal taxes, subsidies for domestic products, especially farm products, and all other policy measures designed to limit the consumption and imports of foreign products." He called on the industrialized countries to open their markets to commodity imports with a view to strengthening the developing countries' capability for self-reliant development.

The representative of the World Bank did not expect a substantial recovery in commodity markets to occur in the near future. As for possible support action, he noted that ICAs had been the most important instrument in the effort to control supply and demand but that most of these agreements had run into serious difficulties. He believed that compensatory financing facilities had been effective in helping to overcome temporary export earnings shortfalls. With respect to structural measures, he estimated that cumulative Bank/IDA project lending for commodity production, processing and other forms of diversification had amounted so far to at least US$50 billion. Moreover, the Bank's structural adjustment lending had helped countries to enhance efficiency and modify policies for better resource use.

The representative of the IMF made a brief statement in which he analyzed some of the factors which had affected commodity markets in the 1980s.

III. Final Action

Following the general debate an effort was made in informal consultations to reach agreement on acceptable conclusions. This effort, however, was unsuccessful and at the final plenary the spokesmen for Group B and for the Group of 77 reiterated the views they had already expressed in the general debate. The Secretary-General of UNCTAD--who had been absent from Geneva at the beginning of the Session--made some brief concluding remarks. He welcomed the fact that in the lively debate which had taken place in plenary, all participants had recognized the grave consequences of the recent drop in commodity prices for the developing countries and had expressed their willingness "to explore remedial possibilities and to work towards constructive action." For his part the Secretariat, while continuing to work within the framework of Conference Resolution 93 (IV), was conscious that achievements under the IPC had fallen far short of expectations. This highlighted the need "for strengthening and adapting existing efforts and for innovations, taking account of structural factors in the commodity economy and of changes in the economic and political environment."