

Current Commodity Situation Critical

The current critical commodity situation and its impact on the developing countries was the subject of intense discussion at the twelfth session of UNCTAD's Committee on Commodities held in Geneva in February this year. The head of UNCTAD's Commodities Division emphasised that the short-term outlook for commodities appeared to be a continued downward pressure on prices. This trend was observed as a result of the expected continuation in the slow growth rates of developed market-economy countries. UNCTAD has estimated that the industrial growth rate of the developed countries would have to be sustained at 3 percent, at least, if most of the major commodities of export interest to developing countries are just to maintain their prices in real terms.

The longer term outlook for commodities was that unless positive adjustment measures were taken the prospects were for persistence both of excess supplies of commodities and of the declining trend in real prices. A survey of the Commodity Situation in 1986 had noted the following salient developments:

-that the commodity price index, after rising in the early 1970s, has declined since 1980 at an average annual rate of 5 percent against an increase of over 8 per cent a year for the previous two decades;

-that in the period 1981-86 commodity export earnings of developing countries declined by \$ 8 billion per year on average, despite an increase in export volumes;

-that the proportion of commodities in total world exports has fallen over the past 20 years from about 30 per cent to 17 per cent while at the same time the relative importance of developing countries in world commodity exports diminished from 34 per cent to 30 per cent and their share of world commodity imports actually rose substantially from 18 per cent to 22 per cent. Moreover, developing countries have been procuring an increasing proportion of their raw material imports from developed countries.

The discussion at the UNCTAD Committee's sessions revealed virtually

unanimous agreement both on the seriousness of the commodity situation where prices, in real terms, were at their lowest level, since the Second World War, and also on the slim prospects of substantial improvement in the near future. In addition to recognising the severity of the impact of the sharp fall in commodity prices on the economies of developing countries it was also noted that this situation had aggravated debt problems in many of these countries.

For nearly 10 years UNCTAD had attempted unsuccessfully to seek solutions to the problem of commodities through an Integrated Programme for Commodities (IPC). UNCTAD's Secretary General, K.K.S. Dadzie admitted at this session that achievements under the Programme had fallen far short of expectations. UNCTAD's Deputy Secretary General Yves Berthelot emphasised that no significant operative outcome had emerged from intergovernmental work on any of the major general cross-commodity issues comprising: the Common Fund for Commodities; processing; marketing and distributing; the liberalization of commodity trade and the compensatory financing of commodity-related shortfalls in export earnings. "The Common Fund Agreement remained "in limbo", he said.

Again, an overview in UNCTAD's Commodity Survey 1986 indicates that the world commodity economy has shown no signs of recovery. It states that stagnating demand and exces-

sive supplies of most commodities are still a feature of world commodity markets. The sharp deterioration in the terms of trade of commodity-exporting developing countries has heightened their balance-of-payments difficulties, with falling export earnings posing increased problems for debt servicing and necessitating a contraction of essential imports, which in turn adversely affects their economies, including the development of the commodity sector.

The major factors which have influenced commodity markets in recent years are cyclical factors in particular the level of economic activity in the major markets, the response of supply to demand for commodities, variations in exchange rates, especially in the currencies in which commodities are traded - and structural factors, including technological developments and protectionism, affecting the supply and demand for commodities. The analysis of these factors in the survey indicates that there is unlikely to be any marked improvement in the commodity situation in the near future.

Structural factors continue to depress demand for most commodities. The rising importance in GDP of economic activities requiring little raw material content and the declining share of food and beverages in total expenditure can be expected to continue, according to the survey. (The declining trends are illustrated in the figure).

Technological developments involving more economical use of raw material inputs, miniaturization, increased recycling and improvements in yields have exerted a strong influence on commodity markets. On the one

Changes in developing countries' exports earnings, 1980-1984
(Billions of constant United States dollars)

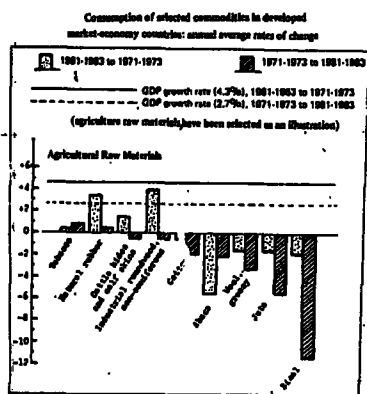
	1980 value	1981		1982			1983			1984		
		Value	Change on previous year	Value	Change on previous year		Value	Change on previous year		Value	Change on previous year	
					1980	1980		1980	1980			
Total merchandise	567.9	559.5	-8.4	500.3	-59.2	-47.6	470.8	-29.5	-37.1	504.4	+33.6	-63.5
Primary commodities including fuels	105.5	99.7	-5.8	93.6	-6.1	-11.9	97.1	+3.5	-8.4	103.6	+6.5	-1.9
Fuels	347.3	327.0	-20.3	301.2	-45.8	-46.1	236.6	-44.6	-110.7	229.8	-7.8	-118.5
Total primary	452.8	426.7	-26.1	374.8	-51.9	-78.0	333.7	-41.1	-119.1	332.4	-1.3	-120.4

Source: UNCTAD secretariat, United Nations Statistical Office data; World Bank, *Commodity, Trade and Price Trends, 1986 Edition*.

* Values in current dollars divided by the industrial market economies index of United States dollars unit values of manufactured exports (CIF) to developing countries, 1980 = 100.

hand these developments have increased supply potential but on the other hand they have reduced demand. However, a continuation of the low level of commodity prices may eventually reduce the incentive for raw material saving innovations and hence lessen their impact upon commodity markets.

An important consideration for producers of various commodities is the competition between traditional raw materials and petroleum-based synthetics of energy-intensive substitutes. The recent declines in the price of petroleum may give an edge to substitutes in competition with traditional raw materials. Hence, natural fibres and natural rubber, for which synthetic substitutes exist, as well as metals and minerals, to the extent that they can be replaced by plastics or other metals such as aluminium which is energy-intensive, are likely to face increased price competition.



Protectionism and government support policies for domestic producers have restricted imports of commodities in major industrialized countries and led to growing surpluses of many commodities on world markets and have imposed a heavy burden on taxpayers and consumers in developed countries. It seems doubtful whether a significant liberalization of trade in unprocessed and processed commodities will be forthcoming in the immediate future, even under a new round of GATT multilateral trade negotiations. Thus, the major industrialized countries' policies are likely to continue to have an adverse effect on commodity exporters. This is particularly the case in respect of cereals, cotton, meat,

rice, sugar, tobacco, vegetable oils and iron and steel, which are products of export interest to many developing countries. If the United States, EEC and other developed countries continue to escalate export subsidization in order to protect or argument trade market shares, prices of many of these commodities will decline further.

While lower prices for commodities on world markets are benefiting importers in developing countries, such benefits are likely to be only of a short-term nature since artificially low prices for imports act as a disincentive to otherwise economically viable domestic production, and in particular food production, and thus are likely to create serious structural problems for the commodity sector. Hence, developing countries have a strong interest in the improved functioning of world commodity trade.

For 1986 and 1987, most forecasts expect a slight increase in the GNP growth rates of the OECD countries, the major commodity-importing re-

gion, and a resulting positive impact on commodity demand. However, commodity prices are hardly likely to improve, since whatever pull these marginal increases in growth rates may exert on commodity prices, the large stocks and surplus production capacities now existing for many commodities will override this influence.

Changes in exchange rates are also having an impact on commodity price levels. Traditionally, when the United States dollar and sterling depreciate, commodity prices rise to a certain extent. However, the considerable recent depreciation in these currencies against other major currencies has not led to any upward movement in commodity prices.

Prices of coffee, vegetable oilseeds and oils and petroleum have recently been the subject of important changes and merit some specific comments. Climatic conditions in Brazil caused coffee prices to shoot up at the end of 1985 and their impact will likely be felt through 1987, as the re-establish-

Debt service and food and fuel imports compared to export earnings of developing countries, 1975, 1983 and 1984

	Percentage of export earnings spent on:			Combined ratio of debt service, food and fuel imports to export earnings (1+2+3)
	Debt service	Food imports	Fuel imports	
	(1)	(2)	(3)	(4)
Africa				
1975	10.8	20.7	9.5	41.0
1983	31.5	23.9	13.3	68.7
1984	30.9	23.9	11.0	65.8
Asia				
1975	5.7	11.7	10.8	28.3
1983	11.5	10.8	17.9	40.2
1984	11.3	11.2	18.4	40.9
Latin America				
1975	23.1	13.0	31.3	67.4
1983	41.0	10.9	28.2	80.1
1984	34.0	10.4	28.0	72.4
Total				
1975	10.5	13.5	15.2	39.2
1983	21.3	12.6	19.7	53.6
1984	19.6	12.7	19.8	52.1

Sources: UNCTAD, *Yearbook of International Commodity Statistics, 1985* (United Nations publication, Sales No. E.85.II.D.24); UNCTAD, *Handbook of International Trade and Development Statistics, 1985* (United Nations publication, Sales No. E.77.85.II.D.12); United Nations Statistical Office.

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ment of normal stock levels will take time. Prices of vegetable oils, on the other hand, have steadily declined and have now dipped below their 1972 levels. These low prices can be expected to continue, given protectionism and support for domestic producers in the major trading countries, technological developments, inter-vegetable-oil competition and the existence of ample supplies. While forecasts of petroleum prices had assumed a price of around \$ 15 per barrel for the near future, the downward movement in prices continues, and prices have broken the \$US 10 barrel level.

There are various reasons for being sceptical about any major improvement in commodity prices. Producers of food crops and agricultural raw materials in the developed countries continue to be isolated from the low world prices and hence there is unlikely to be any significant reduction in production. Policy changes aimed at lowering domestic prices to bring them into line with world prices have been minor. Moreover, the responses of prices of industrial raw materials to higher levels of industrial activity are likely to be weak due to the existence of over supplies on the world market, increased competition from substitutes and inter-commodity competition.

While low commodity prices, including those for petroleum, may help to keep inflation restrained in major consuming markets and may stimulate their growth, the external financial problems of commodity exporters are attaining serious proportions and are exerting increasing strain on the world financial and monetary system. The fall in commodity prices has led to gains of well over SUS 100 billion to the developed countries at the expense of the development of the third world.

It should be borne in mind that while developing countries have together earned approximately US\$ 75 billion annually from their exports of agricultural products during the past few years, the United States, EEC and Japan have spent roughly US\$ 42 billion annually on their agricultural support programmes. While such programmes have clearly exerted a downward pressure on prices for commodity exports from developing countries, and in so doing increased costs of

such programmes in many instances, lower prices for imported commodities from developing countries have facilitated a continuation of such programmes.

The overall monthly index of nominal commodity prices (denominated in United States dollars) showed some slight increase in 1983 but resumed its downward trend in 1984 and by 1985 had sunk to 1976 levels.

There has been a tendency towards over-production in most commodities, partly as a result of diversification of

commodity production in developing countries and surplus production in developed countries as a result of their policies of support to domestic producers. The state of commodity prices is a reflection of the situation.

As much as 52 per cent of developing countries' export earnings is spent in meeting the bill for debt service food and fuel imports. In this connection, it should be noted that developing countries' share in total world imports of commodities, including fuels, rose from 17 per cent in 1974 to more than 22 per cent in 1984. C.G.