U.N. CONFERENCE ON TRADE & DEVELOPMENT

Commodity price volatility and value addition

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‘Review and identify **policy actions** to **mitigate** the impact of highly **volatile prices and incomes** on commodity-dependent countries, and to **facilitate value addition** and greater **participation** in commodity **value chains** by commodity-producing countries
(Accra Accord, para. 93)’

Two sides to commodity dependence:

1. **Reliance on commodity *exports* for foreign exchange revenue**
2. **Reliance on commodity *imports* for food supplies**

- ✧ Both are big problems for development
- ✧ Growth of the second has doubled the commodity problem

Price volatility is a general characteristic of commodity markets

Approaches to mitigating it:

1. Work within the markets’ institutions
2. Work at the markets
3. Work around the markets
4. Replace (parts of) the markets?

1. Work within the markets’ institutions

Keep commodity markets for *commodities*

1. Regulate commodities separately from finance
2. Restrict banks to *banking* functions
3. Make the trade transparent
   - Regulator should publish transactions data
4. Restrict ‘non-commercial’ transactions
5. Stability and security
   → central clearing; position limits

Besides futures regulation?

Some other known means of dealing with commodity price volatility:

- ❑ **Agriculture policy**
  - ❖ Price supports, marketing boards, public stocks etc
- ❑ **Supply management, including international agreements**
  - ❖ Have existed e.g. for tea, wheat, tin, coffee over long periods

Agriculture policy…

"Since the accession of the UK to the European Community, and the incorporation of the UK into the Common Agricultural Policy, grain price volatility has been greatly lessened, reducing the need for a futures market."

- Michael Atkin
Agricultural Commodity Markets: A guide to futures trading (Routledge, 1989), p. 56

2. Work on the markets

Possibilities:

- Food reserves
- Minimum prices
- Restrict imports
- International guarantees of export markets
  e.g. ACP sugar and banana protocols
- Concerted supply management
  - Buffer stocks or quotas to improve the balance of supply and demand
  - Public methods can learn from the private

3. Work around the markets

There are several possibilities:

- Compensatory finance
  e.g. EU's former Stabex fund
- Place domestic or regional markets ahead of global markets
- Promote 'non-traded' crops
- Agroecology rather than agrochemicals

4. Replace the markets (or parts of them)

E.g. Replace certain stages of the value chain with alternative institutions, such as marketing boards

- This can work in developed countries. How feasible is it in present circumstances in the developing world, especially the poorest countries?

Facilitating value addition

Both middle- and low-income countries have recently experienced economic growth

- But much of it is due to high commodity prices - especially in the poorest countries
- And the general problems for poor countries in world export trade are getting deeper

Obstacles to export development

- Widening gap in resources and technology between rich and poor countries
- Relatively low prices in the long term for traditional export crops, e.g. coffee, cotton
- Problem of meeting richer countries' standards for market *entry*
- Closing of doors by developed countries
  - LDCs' market access has not been all gain. Examples:
  - Ending of preferential trade regimes for ACP countries
  - Conditions attached to EPAs

Domestic capital accumulation

This is the basis of economic development

- Achieved when a country builds its own companies and acquires technologies that are under its own control
- ➢ Essential requirement for building up exports as well as for the internal economy

Foreign trade recommendation No. 1

Continue to develop traditional commodity exports

- Improve quality
- Cooperate with neighbours
- Get whatever you can out of deals with new South-South partners

Foreign trade recommendation No. 2

Build up *regional* trade
and regional cooperation on world markets

- Trading at the same level of development
  - Reduces transport and transaction costs
  - Do R&D for what is needed on your own and neighbouring countries' markets
- This substitutes for big countries' economies of scale

Foreign trade recommendation No. 3

Concentrate on building *national* economies

- Requires emphasis on policies such as:
  - Education
  - National market integration and communications, such as roads, mobile telephony
  - Helping informal businesses to formalise and expand