PRODUCER CARTELS:
THREAT OR OPPORTUNITY?

by Susan Hart

with a foreword

by Sir John Reiss, BEM

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APRIL 1975

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The study was undertaken under the supervision of Simon Webley a committee member of the Economic Research Council.

Susan Hart is a specialist in international economic relations.

FOREWORD

This study underlines the vital importance of raw materials to the maintenance and expansion of British industry and shows that a significant proportion of these natural resources come from both the developed and less developed Commonwealth countries. The new economic realities, dramatically brought to public attention through the operation of the Organisation of Petroleum Exporting Countries (OPEC), have emphasised the need for a new approach to the trading relationship between manufacturing countries like Britain and the raw material supplying countries.

The importance of the role of two Commonwealth countries, Australia and Canada, and of South Africa, which has close links with Britain, emphasises the need for us to maintain and develop our traditional links with them. They provide an important bridge between Britain and developing countries.

We cannot afford to ignore the implications for our future which this paper sets out and I hope that it will start a thorough-going reconsideration of the role Britain can play in taking a positive lead in the period of adjustment upon which the developed world is now embarking.

The research has been carried out by Susan Hart who is a specialist in international economic relations under the general supervision of Simon Webley who is a member of the Executive Committee of the Economic Research Council.

This is the first in a series of studies to be carried out under the auspices of the Overseas Trade Research Fund of the Economic Research Council in association with the Commonwealth Industries Association. The Fund was set up in June 1974 to enable research to be undertaken into various aspects of Britain's trade with the rest of the world and in particular with our Commonwealth partners.

JOHN REISS
President
Commonwealth Industries Association

April 1975

INTRODUCTION

The spectacular operation of the Organization of Petroleum Exporting Countries (OPEC) cartel[1] in quadrupling the price of oil in a twelve month period has profound implications for developing countries as well as for those already enjoying a high level of economic prosperity. The ability of OPEC to maintain a significant change in the economic relations between oil-consuming and oil-producing countries while escaping retaliation has already had a contagious effect. The idea of producer collusion has spilled over into other commodity fields.

It has also inaugurated an era of international redistribution of wealth; only the degree of transfer involved is still unclear. With this change in economic power comes a shift in effective political power as well. It is essential that the developed world (ie, OECD countries) recognize that a politico-economic transfer of both relative wealth and power is now underway and that these nations, both individually and collectively, assess the implications of this transfer.

This paper will examine three aspects of the situation:

1. The motivation for, and feasibility of, establishing producer cartels in non-petroleum mineral resources.
2. The potential effect of a trend toward producer collusion in non-petroleum mineral resources and in other raw materials might have on the UK's ability to maintain its high technology industry.
3. Some responses which the UK might make to mitigate or thwart the effects of the development of producer cartels or cartel-related activity in raw material trade.

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1 A cartel is an oligopolistic grouping of producer countries formally organized for the purpose of managing market forces affecting the supply of a product or commodity with a view to increasing the price of that product.

I PRODUCER COLLUSION

(a) Motivation

The success of OPEC cartel action has made it appear that transfer of political and economic leverage from developed to developing countries has happened overnight. In fact, the first clear manifestation of change began in the 1960s as many former colonial territories achieved independence. In the short period since then, the "Third World"[2] countries have begun to exercise effective co-operative voting power in the United Nations General Assembly. Today the political legitimacy of the UN rests, to a large extent, on the ability of that organization to carry through the wishes of the majority of its members and that majority opinion is no longer effectively expressed by the United States.

Nowhere has the inequality of economic situation between developing and developed countries and the new world aspirations of the former group been better expressed than at the Sixth Special Session of the UN General Assembly. Meeting in April-May 1974 to discuss the general subject of raw materials, the Members adopted a UN Declaration on the Establishment of a New International Economic Order. They proclaimed:

> The establishment of a new international economic order based on equity, sovereign equality, interdependence, common interest and co-operation among all States, irrespective of their economic and social systems, which shall correct inequalities and redress existing injustices, make it possible to eliminate the widening gap between the developed and the developing countries and ensure steadily accelerating economic and social development in peace and justice for present and future generations.[3]

2 "Third World" countries are developing countries, mostly non-industrial economies.

3 United Nations. General Assembly 3201 (S-VI). Sixth Special Session, 9 April-2 May 1974, "Declaration on the Establishment of a New International Economic Order."

With respect to raw materials the Members resolved "that the new international economic order should be founded on full respect for the following principles" among several:

> 4(e) Full permanent sovereignty of every State over its natural resources and all economic activities. In order to safeguard these resources, each State is entitled to exercise effective control over them and their exploitation with means suitable to its own situation, including the right to nationalization or transfer of ownership to its nationals, this right being an expression of the full permanent sovereignty of the State. No State may be subjected to economic, political, or other type of coercion to prevent the free and full exercise of this inalienable right;
>
> (j) Just and equitable relationship between the prices of raw materials, primary products, manufactured and semi-manufactured goods exported by developing countries and the prices of raw materials, primary commodities, manufactures, capital goods and equipment imported by them with the aim of bringing about sustained improvement in their unsatisfactory terms of trade and the expansion of the world economy;[4]

Exercise of producer collusion in the production and marketing of raw materials and primary products provides one means by which developing countries hope to improve their terms of trade with developed countries, who are the principal exporters of manufactured goods, and to garner the benefits of economic growth experienced by the industrialised countries.

The main consuming countries of the world account for less than 20% of world population, yet their economies produce 60% of the world's Gross National Product. One of the bases of the rapid post-war recovery and later the growth of industrial economies in Europe and Japan has been the import of raw materials at stable price levels compared

4 Ibid.

with the rising prices of manufactured goods which these economies exported.

In the context of the postwar increases in the level of prices of goods and services involved in international trade, the recent surge in commodity prices represents an attempt to "catch up" with the increases in prices of manufactured goods. In 1970 the index of average prices for all primary commodities was at approximately the same level as it was in 1950. In contrast, the unit value of exports of manufactured goods rose approximately 45% between 1950-70. Thus, from the point of primary product producers, the average terms of trade between their commodities and manufactures declined steadily over the period.

However, between 1970 and 1974 all prices showed substantial increases. The percentage change in the index of unit values of exports of manufactured goods was up 40% and the average index for all primary commodities rose by 100%. The net result was that by mid-1974 the terms of trade of commodity prices in relation to manufactured goods was approximately the same as it had been in 1950.[5] Raw material exporting countries of the Third World have, therefore, established a more equitable trade relationship between themselves and the developed countries in a very short period of time. In the context of the past 25-30 years, it is clear that many of these recent price rises are economically justifiable. It is equally clear that a continuation of a rapid rate of increase in raw material prices could actually reverse past trade relationships to the detriment of developed countries, although the world economic environment is not conducive to this happening at present.

Having seen what can be achieved for the terms of trade from co-ordinated action by OPEC countries, other commodity producing countries may be motivated to overcome many impediments to cartel-type action. Just how feasible is it?

(b) Feasibility

There are a number of factors to be considered when discussing the likelihood of effective producer cartelisation of

5 *Barclays Review.* "Commodity Prices in Perspective," May 1974.

non-fuel minerals and other raw materials and primary products. Very real limits exist for the use of both political and economic power which resource-rich countries can exercise. For instance, developing countries do not share the same political ambitions or internal stability. Economic incentive is not necessarily a sufficient motive for collective action where fundamental political differences exist. Conversely, political likemindedness cannot sustain effective action where a sufficient economic base is lacking. If developing countries are to exercise maximum sovereign control over their future development, including the distribution of their natural resources, they must capitalize on those political and economic factors they have in common.

In the economic sphere, OPEC is the foremost success in developing country producer co-operation. Although the opportunity exists for other producer groups to undertake similar action, it does not follow that every such attempt will be as effective. According to C. Fred Bergsten, Senior Fellow of the Brookings Institution, at least three basic conditions must exist for a cartel to operate successfully:[6]

- demand for the product must be relatively insensitive to price changes
- supply of the product must be relatively insensitive to price changes
- potential colluding countries must get along with each other.

Others have suggested even more specific requisites. Market concentration is important as is limited market accessibility; production costs and richness of resources should not differ radically; colluding countries must not only be compatible, but also must share similar expectations as a result of joint action. It would be advantageous if colluding countries had diversified economies which would permit them to absorb set-backs or to weather production cuts when and if necessary.[7] With so many variables to consider, it is not surprising that producer cartels have not been an economic and trade reality until recently.

6 C. Fred Bergsten, "The New Era in World Commodity Market," *Challenge* September-October 1974, pp. 34-42.

7 Zuhayr Mikadashi, "Collusion Could Work," *Foreign Policy,* No. 14 Spring 1974.

(c) Recent developments

There have been three recent changes in the international economic situation which enhance the feasibility of cartel formation: changes in demand patterns, increases in the market power of producers, and increases in producer perception of this power. There is evidence that the erosion of confidence in paper currencies led to a greater investment demand for commodities. At the same time, demand for commodities among rapidly growing industrialized economies in 1972-73 gave further incentives to increase prices. This resulted in a sellers' market for a wide range of products.

OPEC success demonstrated that under certain circumstances commodity prices could be increased geometrically without retaliation. OPEC countries have gone a step further by declaring a willingness, in some instances, to help other producers in their efforts to affect supplies and prices, as in the case of Venezuela's offer to help finance coffee stockpiling by Central American coffee producers. Even more encouraging, from the producer point of view, has been OPEC support of decisions taken in Dakar recently at a raw materials conference. The secretariat of the UNCTAD Committee on Commodities in 1974 proposed a multiple-commodity buffer stock to support prices of 18 commodities which account for 60% of world trade in non-oil raw materials. The February 1975 meeting in Dakar confirmed this objective and set up an 18-nation working group to decide the rules for operating the buffer stock. Algeria strongly supported the decisions of the Dakar conference and led OPEC countries in their view that a forthcoming energy conference between oil-producing and oil-consuming nations must be broadened to deal with the whole range of raw materials.

(d) Actual producer activity

Though there has been no producer action as yet as thorough and as effective as OPEC, there are a number of newly formed producer groups, and there have been some other signs of group activity as well as some unilateral action by key producers. This activity has taken many forms: decreed *prices, production cutbacks, selective embargoes, increased* royalty payments, negotiated prices, direct market intervention, stockpiling and export taxes.

Table I lists some of the action taken to date among primary resource producers of both non-fuel raw materials and some agricultural products. The list is divided into three categories:

- those products which are *subject* to *formal producer* group organization
- those products which are subject to informal, as yet unorganized, producer discussion, some activity, or unilateral action
- those products which some believe are potentially subject to some form of effective group management.

TABLE I

SOME FORMAL PRODUCER GROUPS

1. **Bauxite:** In March 1974 the seven leading bauxite exporters formed the International Bauxite Association (IBA). Jamaica accounts for 30% of world bauxite production and 75% of world bauxite exports. On May 15, 1974 Jamaica took unilateral tax action which forced a six-fold increase in Jamaican bauxite earnings.
2. **Copper:** The four principal producers of copper have worked together since 1967 in the Conseil Intergovernmental des Pays Exportateurs de Cuivre (CIPEC). Until 1974 CIPEC functioned primarily as an information clearing house and copper prices were left to the operation of the London metal market. Meeting in Peru in November 1974, CIPEC launched a three-point cartel programme, however:
   - (a) for the short-run to organize production and/or export cutbacks to be followed by price increases set by copper producers without negotiations with consumers
   - (b) for the long-term to establish a price system linking raw copper prices to prices of refined and processed copper and copper products, or to a general index of industrial prices

continued

(c) establishment of a buffer stockpile.
World copper prices tripled between January 1973 and May 1974, but they fell again by half as much as a result of demand slump.

3. **Tin:** The International Tin Council (ITC) is a group of producers and consumers alike. They maintain buffer stocks for the purpose of stabilizing prices. Tin producers are vulnerable to consumer stockpiling and substitution, however. Currently the tin producers seek a 42% increase in the guaranteed floor price of tin which is maintained by buffer stocks.
4. **Coffee:** The 42 producer members of the International Coffee Agreement (ICA) have seen fit to let that producer-consumer treaty expire. Through a series of interlocking marketing companies and by stockpile financing arrangements, they have control of world coffee prices. There are some indications that members of OPEC will come to the aid of coffee producers in their attempts to control future market prices and supplies. Coffee producers are agreed that a new pact like the ICA must have price guarantees with a provision for automatic and periodic readjustment.
5. **Bananas:** The Union of Banana Exporting Countries, newly formed, has levied sizable taxes on banana exports. The group accounts for less than half the world banana supply, however. Bananas present unique problems for cartelization, not the least of which is their perishability.
6. **Iron Ore:** Eleven iron ore exporting countries in mid-January accepted the text of a draft agreement for the establishment of an association of iron ore exporting countries.

INFORMAL PRODUCER ACTIVITY

7. **Phosphates:** The price of phosphates has recently tripled largely as a result of unilateral action taken by Morocco.
8. **Tea:** The four major producers of tea have sought to co-ordinate tea marketing and to establish floor prices.
9. **Sugar:** The 46 sugar producing countries engaged in negotiations with Britain and the EEC over future supplies and the price of UK sugar in 1976 thwarted efforts to reach agreement by January 31, 1975. Price and supply arrangements were finally completed after arduous debate in early February.

SOME PRODUCTS POTENTIALLY SUBJECT TO PRODUCER GROUP ACTION

10. **Manganese:** There is no satisfactory substitute for manganese, but it is difficult to maintain producer controls on the commodity since it is a co-product of iron production and reserves are geographically diverse.
11. **Tungsten:** There is a distinct possibility for collusion.
12. **Rubber:** Four countries have 50% of the world total of rubber.
13. **Timber:** The possibility of concerted action exists.

Table I illustrates the critical point that a trend toward co-operative producer action for the purpose of manipulating existing trade patterns with respect to some commodities is underway. The trend is based on sound economic advantage and on political will. It appears that the coming decade will be dominated by political and economic initiatives emanating from those countries outside the industrialized and Communist world. Economic and social development will be their ambitions and their success in these areas will augment both their domestic and their international political effectiveness.

(e) User country position

Viewed from the point of view of developed countries, producer cartels are a potential economic threat insofar as they interrupt or distort the traditional patterns of trade in raw materials and primary products which have sustained the economies of the industrialized world for the past quarter century. It would be prudent for raw material importers at least to consider policies which would seek to minimise the effects on their trade and payments balances of increased prices and/or decreased supplies of raw materials, which would result from newly initiated producer collusion.

Cartelization is not the only weapon that producer countries acting in concert could use to raise their incomes. There are other trade and financial strategies which producers might pursue to force their demands on consuming countries. For instance, some raw material exporters could restrict new or hamper present foreign direct investment in their countries or they could repudiate their debts to the developed world. At the same time they could deliberately undercut industrialized countries' export prices of some manufactured goods or they could expand their own exports further by becoming havens for industries hard-hit by the anti-pollution legislation enacted in many developed countries today.[8] Furthermore some attention must be given to the natural and legitimate demands which many producers are likely to make for more indigenous "downstream" processing of their resources. These are but a few of the potential hazards facing the UK and other developed countries.

To form successful cartels the developing countries will need outside assistance in the form of finance and, in nearly every case, the support of a mature economy. OPEC is a possible source of cash but the collaboration of mature economies presents a greater problem. Mature producer economies include the US, Canada, Australia and South Africa. The US, as a nearly self-sufficient nation, is not likely to collaborate with developing countries for the purpose of disrupting existing trade practices, practices which the US has had a crucial role in establishing. This leaves three countries—Canada, Australia and South Africa—all with strong Commonwealth or UK ties, which could be economically motivated to collude with other producer countries in order to raise some commodity prices. Their participation in producer group activity would provide a degree of market expertise which many of the developing countries sorely lack. Furthermore, if one of these three countries were to act as spokesman during negotiations between producers and consumers, the fact that they are developed countries as well would help to mitigate the feeling of confrontation which might otherwise arise.

8 For further discussion of these producer strategies and an examination of the criteria necessary for cartel formation and possible developed country responses to cartels see C. Fred Bergsten, "The Threat from the Third World," *Foreign Policy*, No. 11 Summer 1973.

Before considering their roles, the position of the UK vis a vis primary product producers must be examined.

II HOW VULNERABLE IS THE UNITED KINGDOM?

A real economic potential difficulty would exist for the UK if developing countries either withheld supplies or colluded to exact a price significantly different from the long-run marginal production and distribution cost. Clearly effective producer collusion in the production or marketing of certain materials would have a significant impact on the whole economic fabric of the country.

(a) Critical non-oil minerals

Not all minerals of which the UK imports 100% are critical. Some have easily obtainable substitutes and others are so plentiful that there is little likelihood of supply deficiencies. Eight non-fuel minerals which are of major importance to UK industry are listed in Table II and will be used to illustrate Britain's potential vulnerability to supply disruptions.

TABLE II

MINERALS UNDER CONSIDERATION[9]

Iron Ore	Copper
Manganese	Tin
Bauxite	Tungsten
Alumina	Molybdenum

Iron Ore: Iron ore is an essential material for industry in all industralized countries. In 1973 Britain imported three-quarters of its requirements. Iron ore is used in the production of transportation equipment; construction equipment; machinery; pipes, tubes, and other oil and gas equipment; home appliances; etc. Iron ore reserves are widely distributed throughout the world and the developing countries account for nearly one-third of known reserves. Major foreign sources of UK iron ore imports include: Canada, Sweden, Brazil and Mauretania. Canada, Brazil and Australia maintain the position that the Iron Ore exporters group, of which they are members, should be consultative, rather than active in price fixing schemes. There is a considerable potential for recycling steel scrap in developed countries.

Manganese: The UK imports more than 100% of its consumption of manganese ore, re-exporting a small amount. It imports nearly 40% of its consumption of ferro-manganese and all of its consumption of silico-manganese. Manganese is used in steel-making; in the production of construction materials, transportation equipment; machinery and equipment; appliances; pipes and tubing; chemicals and glass products; dry cell batteries; etc. Developing countries account for less than one-quarter of known reserves and developed countries for nearly half. Britain receives more than one-third of its manganese ore from South Africa, Brazil, the Soviet Union, Ghana, and Congo (Brazzaville). Because there is as yet no satisfactory substitute for manganese, a major element in steel-making, demand is probably relatively inelastic.

Bauxite: The UK imports all of its consumption of both uncalcined and calcined bauxite. Uncalcined bauxite is used chiefly for conversion to aluminium; calcined bauxite is used chiefly for abrasives, refractories, etc. The developing countries account for nearly 60% of known world bauxite reserves and the members of the International Bauxite Association account for three-quarters of world production. Ghana supplies neary two thirds of UK consumption of uncalcined bauxite and Guyana nearly 80% of calcined bauxite. Aluminium, the end product of much bauxite, is highly substitutable and recyclable.

Alumina: The UK imports nearly 60% of its alumina requirements. There has been a large increase in UK capacity in recent years. Alumina is used primarily in the production of primary aluminium, but also for abrasives, refractories, and other non-metallurgical uses. The UK receives more than half its alumina imports from Jamaica. Aluminium, the final product, is substitutable and recyclable.

9 This list is taken from a study by Sperry Lea for the British-North American Committee.

Copper: Nearly 100% of UK consumption of copper is imported. Copper is used predominately for conducting electricity. Other uses include: construction, ordnance (*shell cases*), chemicals, and coinage. Unrefined unwrought copper is used primarily for the production of refined unwrought copper, which in turn is used in the production of copper semimanufactures. Developing countries account for nearly half the world's known copper reserves and the copper producer group, CIPEC, accounts for half the world's copper production. Major UK sources of copper imports are Chile and Zambia. Commercially recoverable copper reserves can grow rapidly and recycled copper could provide a significant portion of needed consumption.

Tin: The UK imports 85% of its consumption of tin concentrates. Tin is used in the production of construction and transportation equipment; electrical equipment; plumbing and heating equipment; industrial machinery; pigments and compounds; dry cells, lithographic plates; etc. Developing countries possess nearly 80% of known world reserves and the four leading tin producers account for an equal portion of world production. Major UK sources of imports are: Bolivia, Australia, South Africa, and Argentina, Malaysia and Nigeria. There are substitutes for tin for most uses.

Tungsten: Tungsten concentrate imports account for all of UK tungsten consumption. The UK exports Ferro-tungsten. Tungsten is used in the production of metal working machinery; construction and mining machinery and equipment; transportation equipment; electric lamps; electrical equipment and machinery; industrial inorganic chemicals; etc. Nearly half the world's known reserves are located in developing countries. Major UK sources of tungsten imports are: Netherlands, Bolivia, Peru, China, and Thailand. There is a potential for effective collusion among these countries.

Molybdenum: Total UK consumption of molybdenum concentrates is imported. It is used in the production of transportation equipment; industrial machinery, machine tools; pipe, tubing, tubular production; chemicals, catalysts, pigments, lubricants; electrical, electronic equipment; etc.

Nearly two thirds of the world's known reserves are located in the developed countries. Major UK sources of molybdenum imports are: Canada, US, and the Netherlands.

(b) Producer group action and the UK

Of these eight minerals, bauxite, copper, tin, and iron ore are subject to producer group action. In some instances producer co-operation has already had an impact on prices. Jamaica, a key member of the International Bauxite Association, raised its tax levies on bauxite companies in 1974. Although the US is the principal recipient of Jamaican bauxite, Britain receives most of its alumina from Jamaica. The bauxite industry is highly concentrated so that price changes affecting aluminium companies have a spill-over effect. A fall in demand coupled with increased recycling and substitution can alleviate to some extent a situation caused by short bauxite supply or unacceptable price increases, but the time lag required to adjust to changing market conditions means that higher prices must be carried in the short run.

The International Tin Council is hampered in its attempts to raise tin prices substantially by the fact that there are substitutes for tin, and commercially recoverable tin reserves are likely to grow faster than tin prices. Furthermore, the UK has the option of drawing on its tin stockpile to offset possible price effects of short supplies in the short-run anyway.

Although CIPEC, the copper group, may have a long-term prospect for effective supply action, present indications are that there is a high price elasticity of demand for copper. While copper prices rose sharply in 1973, they fell sharply in late 1974 and early 1975 as world demand reflected economic recession.

In many cases, therefore, the effect of producer group action in raising raw material prices and/or reducing supplies may be of short-term benefit to producers. Conversely, the deleterious effect on UK industry may be short-lived as demand elasticity, substitution, and diversion from re-exports bring about increase in supplies.

When this modifying effect takes place, producer collusion will necessarily become more sophisticated and co-operation among producers will be directed toward longer-term gradual changes in overall supply conditions which developed country raw material importers may be unable to prevent. The result may be a system of carefully controlled supply[10] aimed at gradual real price rises. This will mean eventually that consumer import bills will rise and that these rises will be generally impervious to the traditional market constraints of falling demand.

(c) Trade balances

Although the prognosis for effective producer collusion with respect to these minerals is not certain, the UK situation is still not enviable. For instance, any significant price or supply changes have immediate impact on UK trade balance. There was an overall 32% rise in the value of UK imports of basic materials in 1973, two-thirds of which is accounted for by commodity price increases. Table III shows the increase in value of UK copper, aluminium, and iron imports in 1973 over the previous year.

TABLE III

Value of UK Imports of Copper, Iron, and Aluminium 1972-73

	£ millions cif		*% increase over*
	1972	*1973*	*year earlier*
Copper	207.1	339.6	64
Iron	108.0	152.0	41
Aluminium	96.7	113.2	17

Source: "UK Overseas Trade in 1973, *Trade and Industry*, 16 May, 1974

A significant factor to remember is that the UK imports some commodities from a small number of countries, many of which are Commonwealth, former colonial, or dependent territories. For each of the eight minerals discussed above, Table IV lists the UK imports as a percentage of consumption for the period 1968-1972 and the percentage of UK consumption which came from the Commonwealth and South Africa during the same period.

10 For an analysis of the problems of commodity price variations and a proposal for their stabilisation see L. St. Clare Grondona, "Built-In Basic-Economy Stabilizer," The Economic Research Council, 1972.

TABLE IV

UK Imports of Selected Minerals

	Total Imports as % of Consumption Average 1968-72	*% Consumption from Commonwealth and South Africa 1968-72*
Iron Ore	61.2	15.5
Manganese	107.7	47.8
Bauxite	100.0	67.7
Alumina	58.0	51.7
Copper (refined and unrefined)	66.6	42.4
Tin (concentrates and refined)	87.3	33.8
Tungsten	123.6	9.8
Molybdenum (concentrates)	104.2	54.2

Derived from UK trade statistics, based on volume. All figures are approximations and where more than 100% indicated there is a re-export trade and/or stock increases.

Table V lists principal Commonwealth or UK related countries which supply these eight minerals.

TABLE V

Principle UK-"linked" Suppliers of Selected UK Imports

Iron Ore	*Manganese*	*Bauxite*	*Copper*
Canada	Ghana	Ghana	Zambia
Australia	S. Africa	Australia	Canada
S. Africa		Guyana	
Tin	*Tungsten*	*Molybdenum*	*Alumina*
Australia	Australia	Canada	Jamaica
S. Africa	Rwanda		Canada
Malaysia	Singapore		
Canada			
Nigeria			

The threat to the UK vulnerability as illustrated by the supply position of these eight minerals is underscored by a number of other international economic and political factors. The increase in many commodity prices during 1972-74 reflected a general upsurge in world demand. Although this trend has had a detrimental effect on the UK terms of trade, the demand-supply relation of many of these products has been reversed in late 1974 due to the general decline in economic activity. Some commodity price changes, therefore, may present no long-term problem. However, the demand-supply situation for foodstuffs, fertilizer products, and petroleum is not so responsive to cyclical economic factors and a long-term shift in demand and supply of these materials is likely to have a profound effect on the UK economy.[11]

On the other hand, British membership in the Common Market has begun to make a permanent change in trade patterns and direction. By 1973 half of total UK imports came from Europe, compared with only 28% in 1957. The EEC countries alone accounted for 33% of total UK imports, nearly double their share in 1957.[12] Many traditional Commonwealth trade arrangements have been terminated or will be systematically phased out to be replaced with EEC trade arrangements.

Under the terms of British entry into the Common Market, a few materials of major importance, such as aluminium, lead, zinc, and newsprint, which were subject to zero or very low import duties, became dutiable under the EEC Common External Tariff (CET). Certain other materials which were dutiable in the UK were no longer dutiable under CET (but several of these had entered the UK duty free under the Commonwealth Preference Agreement anyway). In agriculture and food products, duty-free imports from the Commonwealth Preference Area represented a considerable portion of total UK

11 Petroleum is the possible exception. The prospect of U.K. self-sufficiency in oil resulting from successful exploitation of North Sea Oil may remove this strain on the U.K. trade balance for two decades at least.

12 U.K. Overseas trade in 1973, *Trade & Industry*, 16 May, 1974, p. 358.

imports and, in certain cases, are subject to high duty rates following entry.[13]

It should be noted that UK trade with the EEC countries was undergoing a major shift before entry was negotiated. For the period 1958-68 the portion of UK imports emanating from the EEC rose from 14% to 20% of the total, while imports from the Commonwealth declined from 35% to 24% of UK imports. UK exports to the EEC increased from 14% to 19% of total exports for the same period, while exports to Commonwealth countries declined from 38% to 23%.[14]

With respect to two senior Commonwealth countries, Australia and Canada, some trade risks were involved with entry. Although UK imports from both countries declined steadily and significantly between 1960 and 1970, hard wheat and barley were two Canadian products which were affected by the EEC Common Agricultural Policy (CAP). A point which may become more significant as the decade enters its second half is that certain of the Commonwealth countries produce a significant proportion of world production of key raw materials and primary products, including foodstuffs, a fact which is likely to be of increasing importance as world demand for these commodities continues to outpace supply. The UK in particular imports about half its total consumption of foodstuffs and, as has been shown, is particularly reliant on imports of certain raw materials.

Events surrounding recent changes in the postwar patterns of petroleum production and distribution have some disturbing effects on the UK. OPEC cartel price increases have had a forceful impact on Britain's petroleum import bill and subsequently on the UK visible trade account. Table VI shows the visible trade deficit and the oil portion of that deficit for 1973 and 1974. This shows a 14.8% increase in the visible trade deficit and a 48.2% increase in the oil-induced portion of that deficit between 1973 and the first three quarters of 1974.

13 H.M.S.O. "Britain and the European Communities: An Economic Assessment." (Cmnd. 4289, February 1970).

14 Ibid., pp. 23, 24.

TABLE VI

UK Visible Trade on Balance of Payments Basis

Seasonally adjusted values £ million

	Exports (fob)	*Imports (fob)*	*Visible balance*
1973	11,454	13,796	—2,342
1974	15,458	20,604	—5,146
1973 1st quarter	2,672	3,036	—364
2nd quarter	2,775	3,183	—407
3rd quarter	2,970	3,556	—586
4th quarter	3,038	4,022	—984
1974 1st quarter	3,448	4,741	—1,293
2nd quarter	3,877	5,200	—1,322
3rd quarter	4,140	5,295	—1,154
4th quarter	3,992	5,368	—1,376
1974 August	1,375	1,752	—377
September	1,436	1,793	—357
October	1,336	1,807	—471
November	1,295	1,854	—559
December	1,361	1,707	—346
1975 January p	1,546	1,807	—261
1974 Aug.-Oct.	4,146	5,352	—1,205
Nov.-Jan. 1975 p	4,202	5,368	—1,166
Percentage change*	+1.5	+0.5	

p Provisional estimates
* Percentage change: latest three months on previous three months.
Source: Trade and Industry, 20 February, 1975.

Specific conclusions as to the likely emergency of successful producer cartels are difficult to draw because there are so many variables to consider. Can cartels effectively control

the level of commodity supplies by restricting production and export when necessary with a view to raising commodity prices? There is the possibility that the UK over time could adapt to changing trade patterns and practices without undue long-term strains on its trade balance. Export diversion, commodity substitution, demand elasticity, and trade arrangements in GATT (General Agreement on Trade and Tariffs) may help in this respect. Nevertheless, it is possible to list a few tentative observations which require further consideration:

- UK industry is highly dependent on imports of several key mineral resources.
- The UK is also highly dependent on imports of foodstuffs and fuel-minerals and these products are generally demand inelastic.
- Many commodity imports come from developing countries which recently have begun to recognize the power they may exert over production and export of resources to developed countries. The desire of developing countries to improve their domestic and international social, economic, and political situations is born of genuine grievances and sound appraisal of economic advantage in many cases.
- Concerted producer manipulation of trade patterns and practices with respect to key mineral resources and primary products may have prompt adverse effects on the UK balance of trade and consequently on the overall current account balance in the future.
- Several of the UK sources of imports of essential commodities are Commonwealth countries or former colonial territories. This may provide an important mitigating factor with respect to future UK terms of trade, notwithstanding British entry into the EEC.

III SOME RESPONSES

The change which seems to be underway in the terms of trade between Third World producers of key minerals and other primary products, on the one hand, and resource users on the other, creates problems as well as advantages for the resource rich countries. While the revenues from the export of commodities may increase substantially, some countries' capacity to absorb these revenues is limited. For instance, many of the Arab OPEC countries face a severe short-term absorption problem and have turned to Western industrialized countries in order to "recycle" their oil revenue, estimated to be at least £95 billion in 1974. Here industrial societies have some advantage; they alone can supply capital goods, technology, and technological knowhow.

The OPEC situation provides a case in point. OPEC countries, particularly in the Middle East, faced with unprecedented capital inflows arising from increased petroleum prices have turned to Europe and North America to invest and to spend their revenues. The bulk of their surpluses has gone into capital markets—into short-term bank deposits—but there is clearly a trend toward spending money on capital goods. The Arab OPEC countries are just beginning to publish massive regional development plans which will require the import of capital goods, technological services, and ever-growing quantities of consumer goods as well. The UK, for instance, features heavily in hospital construction and management programmes in Iran. Downstream petrochemical development and production provide another opportunity for the export of Western technology. Banking and investment skills are still in short supply among OPEC countries. The region affords banking centres like London and New York with a capital market to tap, while these Western financial centres afford Middle Eastern investors an invaluable service and outlet.

Export of sophisticated goods and technical services helps industrial countries to offset the increased costs

to them of raw materials and, at the same time, generates job opportunities while providing developing countries with the tools to build internal social institutions and sound economic infrastructures which many of them lack at the present. If developing countries are to maximise growth of their GNPs in order to achieve the consequent social and political development, then assistance from developed countries is a requirement, not merely a possibility. Herein lies the politico-economic leverage which countries like the UK can exert to offset the potentially adverse effects on its trade balance of higher import costs and commodity shortages.

There are three UK-tied countries of particular interest which supply the UK with many of the eight minerals discussed in Chapter II. Two of them, Australia and Canada, are mature members of the Commonwealth, while South Africa has close links with the UK. All three are developed countries, major exporters of foodstuffs and minerals, and the UK conducts a significant proportion of its trade with them. Table VII shows the total value of imports and exports exchanged with these countries and the aggregate percentage of total UK trade these three countries accounted for in 1973.

TABLE VII

UK Trade with Australia, Canada and South Africa 1973 £ millions

1973	*Australia*	*Canada*	*S. Africa*	*Total UK*	*Aggregate % Total UK*
Exports	404,086	413,811	374,400	12,455,110	9.5
Imports	340,762	735,574	399,514	15,854,443	9.0

Derived from UK Trade Statistics, 1973

As producers of many primary products, these three countries play a particularly important role. They hold similar values, both political and economic, and as developed countries are less likely to pursue disruptive trade practices aimed toward other developed countries. They can and do act as moderating influences within producer organizations.

Early in January 1975 Australia voiced the opinion within the Iron Ore Exporters' Association that the group should remain consultative and not involve itself in price fixing. *Canada shared the same view. This attitude stands* in sharp contrast to the sort of action Jamaica, a former British territory, has taken with respect to its bauxite exports. Jamaica supplies 30% of world bauxite production and in May 1974 took unilateral tax levy action. Again, Australia, which is a member of the International Bauxite Association, has acted as a moderating influence within the group forestalling widespread action directed toward raising prices.

Of the five Commonwealth developing countries listed in Table VI Ghana, Singapore, Jamaica, and Zambia supply significant amounts of food, livestock, crude materials, nonferrous metals, and some manufactured goods to the UK. On the other hand, the UK exports to these countries a significant amount of the following: chemicals; manufactured goods; machinery and transport equipment; and miscellaneous manufactures. Using Standard International Trade Classifications (SITC), Table VIII lists the value of several categories of UK imports from and exports to these four developing Commonwealth countries in 1973. Nigeria has been included because it is a major former colonial UK trade partner and a member of OPEC.

TABLE VIII

Selected UK Exports To and Imports From Five Countries
1973 £ millions

UK Exports To & Imports From:	0 *Food live ans.*	2 *Crude matters*	3 *Min. Fuels*	4 *Animal& veg fats*	5 *Chems.*	6 *Manuf. goods*	7 *Machin. Equip.*	8 *Misc. Manuf.*	9 *Other*	TOTAL
Zambia										
Exports	1.38	.3	.09	.09	4.0	8.66	19.2	4.1	2.9	40.72
Imports	.06	.42	—	—	—	76.4	1.08	.18	.15	78.29
Ghana										
Exports	1.6	.3	.2	.07	5.3	6.6	12.4	2.8	.96	30.23
Imports	19.6	16.9	—	—	.2	10.9	.3	.56	.09	48.55
Singapore										
Exports	2.3	.3	.3	.2	11.9	17.4	53.9	8.2	2.7	97.2
Imports	5.6	24.5	1.2	11.4	.4	20.1	16.1	5.1	.6	84.4
Nigeria										
Exports	7.9	3.1	1.6	.2	27.4	35.4	77.4	17.4	1.4	171.4
Imports	32.8	18.6	118.0	18.4	.3	14.3	2.8	.17	1.2	189.57
Jamaica										
Exports	1.8	.33	—	.1	4.2	12.0	17.66	4.0	1.8	41.89
Imports	30.9	.06	—	—	11.5	.04	.16	.46	.38	43.5

Source: Overseas Trade Statistics of the United Kingdom. December 1973.

These bilateral trade patterns have grown both from historic ties and economic advantage. They provide the basis for mutually beneficial arrangements which could protect the UK against the effects of short-term disruptions of traditional trade patterns and at the same time ensure developing Commonwealth countries of the sophisticated know-how and access to capital on which many depend. While the UK will have to face certain alterations in the favourable terms of trade it has received from these countries in the past, both the UK and its developing country Commonwealth members stand to gain from such strengthened bilateral economic arrangements in the future.

Negotiations by blocs of countries with other blocs has considerable superficial appeal—indeed, one motivation for forming developing country primary product cartels is to respond to developed country trading blocs. However, the needs of bloc members tend to differ markedly and any interruption of either import or export trade can have a devastating effect on an individual economy.[15] As was shown in Chapter II, the UK is extremely vulnerable and therefore has every incentive to follow the French lead in the Middle East and to conclude certain bilateral "barter"-type deals with developing countries.

These type of arrangements must recognise a fundamental shift in traditional commercial arrangements between nation states. Whereas the Trade Treaty has heretofore generally been the limit of government-to-government commercial involvement, the "new economic order" as it has been called, will require more direct involvement in commercial affairs by governments. Early indications are that governments of developed countries (with the exception of France) are unsophisticated and often naive in this field and the same is true of many developing country governments. There may be scope for new institutions; for instance, ones covering whole industries to supplement existing corporations in dealing with the barter-type deals.

15 For a thorough examination of Economic bloc formation see Part I of "Economic Blocs and U.S. Foreign Policy," Ernest H. Preeg, National Planning Association, Washington, D.C.

In addition to building on traditional bilateral economic linkages with Commonwealth developing countries, there are other policies the UK could pursue in order to forestall or mitigate disruptive producer collusion. One is to recognize that these countries have a legitimate claim to a share of world resources and the material prosperity which in the past had benefited the few industrialized countries. In the type of world we now have following the Yom Kippur War of 1973, the UK and other developed countries will have to offer acceptable compensation for the continued use and consumption of raw materials.

There are a number of compensations the UK is in a position to offer in return for assured supplies of certain essential materials.[16] They include: active pursuit of international agreement to extend preferential tariff schemes to less developed countries; support of a link between international monetary co-operation and development finance; granting of more concessional aid and loan rescheduling; and the active inclusion of developing countries in international political and economic discussions.[17]

Policy based on these criteria pursued in international forums by the UK could lend political credence to the new economic reality and would ease the ensuing transfer of political and economic power to permit orderly adaptation rather than radical disruption of international trade. The role of developed Commonwealth countries in the world's economic and financial institutions where north meets south will be of crucial importance in ensuring a smooth transition to a more stable equilibrium.

16 For lucid examination of possible developed country responses to producer collusion see "Resources: the Choices for Importers," Philip Connelly, *International Affairs*, October 1974.

17 C. Fred Bergsten, "The Threat from the Third World," *Foreign Policy*, No. 11 Summer 1973.