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UNITED NATIONS
ECONOMIC AND SOCIAL COUNCIL

Distr.: LIMITED

E/ECA/TRADE/92/19/Summary
September 1993

ENGLISH

United Nations
Economic Commission for Africa

Technical Meeting of Experts of the
Twelfth Session of the Conference
of African Ministers of Trade

Tunis, Tunisia
19-21 October, 1993

Executive Summary

Mechanisms for stabilizing the export earnings of African countries

International commodity agreements and commodity exchanges

I. INTRODUCTION

1. African economies continue to be highly dependent on foreign exchange resources earned from commodity exports. The instability of export earnings from such commodities, for some ten years now, forms the rational basis for this study which has been prepared to highlight the various measures and specific policies that can help African countries to stabilize their earnings from commodity exports.

2. The study comes in four parts. In chapter one, the problem with African commodities is briefly described. Chapter two discusses the major existing stabilization mechanisms. Chapter three reviews the African experience in the stabilization of commodity exports while chapter four makes specific policy recommendations that would improve the stabilization of African export earnings.

II. THE PROBLEM WITH AFRICAN COMMODITIES

3. There are two main dimensions to this problem: one is the preponderance of commodities in African economies and the steady decline of export earnings from such commodities.

(a) Commodities in African economies

4. African economies depend highly on export earnings from a handful of mainly agricultural commodities. According to the Fraser Report (a study covering the period 1982-1986), 66 per cent of the African countries derive more than 50 per cent of their earnings from the export of no more than two commodities. In 1987 for example, more than 82 per cent of the export earnings of African countries came from the export of commodities.

(b) Steady decline of export earnings

5. The steady decline in commodity export earnings has to do with factors relating both to supply and demand. The supply - related factors include falling prices, overproduction, price inelasticity, dollar exchange rate variations, extremely high interest rates which significantly increase storage costs and speculation.

6. With regard to demand, the factors worth mentioning include Africa's loss of certain traditional markets to competitors from Asia and Latin America, the decline in income of major consumers as a result of economic crisis, income/price elasticities combined with fairly strong demand for such products, the impact of protectionist measures taken by a number of consumer countries, the glut in the market for some of these commodities (especially tropical beverages), structural production problems such as poor productivity and the fact that African countries have ill-suited or no marketing policies for penetrating the consumer market.

III. THE MAJOR MECHANISMS FOR STABILIZING COMMODITY EXPORT REVENUE

7. The mechanisms for stabilizing export earnings from commodities can be divided into compensatory financing and price stabilization mechanisms.

(a) Compensatory financing mechanism

8. Compensatory financing mechanism address the concern for insurance *ex-post facto*. When the loss in export revenue reaches a certain threshold, these mechanisms compensate with the granting of an amount of resources determined under a set formula. The major compensatory mechanisms to which Africa has resorted are STABEX and SYSMIN within the context of various Lome Conventions adopted by the EEC and ACP countries. There has also been the compensatory financing facility of the International Monetary Fund

(b) Price stabilization mechanisms

9. Since the major limitation of compensatory financing mechanisms is that they operate *a posteriori*, they cannot prevent export revenue from declining. From this has emerged the importance of stabilization mechanisms that anticipate the major factor of instability, namely, price fluctuations. There are three such mechanisms described in this study: Commodity agreements, commodity exchanges and the facilities granted under the UNCTAD common fund for commodities.

10. The way a commodity agreement works is to stabilize prices by controlling supply. Supply may be controlled by means of a buffer stock or by production or export quotas. Commodity exchanges, on their part, can make it possible to stabilize the price of a particular commodity through what has been termed hedging. The UNCTAD common fund for commodities can help to stabilize commodity prices through the financing of vertical diversification programme in the commodity sector by way of its second window or by financing buffer stock holding operations through its first window which, unfortunately, has yet to become operational.

IV. AFRICAN EXPERIENCE IN THE STABILIZATION OF COMMODITY EXPORT EARNINGS

11. Africa has built its experience in the stabilization of commodity export earnings on the national and international fronts.

(a) National stabilization efforts: creation of marketing boards

12. National measures for export revenue stabilization have centred on the establishment of national marketing boards in most African countries. Such boards functioned relatively well until the early 1980s. When the commodity sector began to experience problems in the early 1980s, the marketing boards were no longer able to fulfil their primary role of securing remunerative prices for producers and to act as broker between producers and international buyers. Most of

these institutions have currently been reduced to skeletons of what they use to be and perform no significant economic activity. In cases, some of the countries have purely and simply dissolved them or placed them in receivership.

(b) International stabilization measures

13. African countries have also participated in most of the multilateral commodity export revenue stabilization mechanisms described in chapter three of the study. Under EEC/ACP agreements they have been partners in STABEX and SYSMIN. They have also participated in the IMF compensatory financing facility and in commodity agreements. Generally speaking, Africa has not been able to achieve stabilization by hedging and has similarly not yet been able to benefit from the UNCTAD common fund for commodities. This may be because the fund has hardly become operational.

14. It should be underscored that, generally, while these mechanisms have played a certain role in the stabilization of African commodity export revenue, they have had very limited effect and some of them, such as the commodity agreements, have had serious problems being implemented.

V. PROPOSED MEASURES FOR STABILIZING THE COMMODITY EXPORT EARNINGS OF AFRICAN COUNTRIES

15. The general policy recommendations that will specifically improve the stabilization of African commodity exports can be classified into three categories:

(a) National measures

16. Nationally, the proposed measures have to do with improving the competitiveness of African commodities by reducing their production costs and improving their quality, particularly through the adoption of more productive technologies. Macro-economic policies will have to be instituted to promote commodity production and marketing. There should be maximum vertical integration of the commodity centre. Production, distribution and marketing operations would have to be streamlined by involving the private sector more closely. Modern production, storage and marketing infrastructural facilities will have to be established or strengthened and, finally, the export earnings derive from commodities should be properly managed in their allocation to socio-economic development activities so as to raise the leading standards of the poorest and secure trickle-down effects.

(b) Subregional and regional measures

17. At the subregional and regional levels a joint programme should be initiated to promote commodity exports more specifically through the establishment of export marketing groups. Regional institutions should be set up to promote research and technology targeted at specific commodities of common interest. Financial institutions for financing external trade should be established and/or expanded. Clearing arrangements should be promoted to handle trade among countries belonging to the same subregion. A system of trade data collection and dissemination should be developed on the potential for intra-African trade and trade between Africa and the rest

of the world. Within ECA secretariat a unit should be set up specifically to deal with African commodities giving their strategic importance to the continent.

(c) International measures

18. The international measures recommended have to do with strengthening the negotiating power of African countries within multilateral trade cooperation institutions. Appropriate mechanisms should be set up to renegotiate commodity agreements or any other supply control mechanism. The Kampala meeting of August 1993 among coffee producers provides hope to coffee producers and exporters in the developing world with regard to stabilization of coffee price. A framework should be establish to enable Africa to participate in international commodity exchanges and, finally, joint ventures should be set up with the developed world to promote capital and technology transfer to the commodity sector in Africa.

VI. CONCLUSION

19. The persistent prices of African economies is the result of a host of factors with the depression in the commodity markets having led to a drastic fall in foreign exchange revenue. To overcome this crisis African countries have resorted to various stabilization mechanisms which have had little impact on stabilizing export revenue. While strongly recommending that the existing mechanisms should be revitalized, it is also of the essence to explore new avenues such as hedging on the futures markets and using the facilities provided by the UNCTAD common fund for commodities.

20. With regard to the established of regional commodity exchanges, the idea appears to be a premature response to the commodity problem as it currently exists in Africa. The low volume of intra-African trade and the barriers to such trade, excessive government control over trading activities and prices, the lack of a wide range of commodities meeting international qualities standards are all among the problems that will have to be addressed before Africa can proceed towards the establishment of regional commodity exchanges.