COMMISSION OF THE EUROPEAN COMMUNITIES

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COMMISSION COMMUNICATION TO THE COUNCIL

concerning international negotiations on
a Common Fund for Commodities

UNITED NATIONS NEGOTIATING CONFERENCE ON A COMMON FUND
UNDER THE INTEGRATED PROGRAMME FOR COMMODITIES
GENEVA, 7TH NOVEMBER - 2ND DECEMBER 1977

I. THE COMMITMENT TO NEGOTIATE

1. Following the first part of the United Nations Negotiating Conference on the Common Fund (7th March - 3rd April, 1977) and the Community's decision in Rome on 25th March, 1977 that "there should be commodity price stabilisation agreements where appropriate and that there should be a Common Fund", all participants in the Conference on International Economic Co-operation (CIEC) agreed:

> "that a Common Fund should be established as a new entity to serve as a key instrument in attaining the agreed objectives of the Integrated Programme for Commodities as embodied in UNCTAD Resolution 93(IV). They also agreed that its specific purposes and objectives, as well as its other constituent elements, will continue to be negotiated in the United Nations Conference on Trade and Development (UNCTAD). /And they/ pledged themselves to secure a successful conclusion at the forthcoming resumed session of the United Nations Neogtiating Conference on a Common Fund scheduled for November 1977 at plenipotentiary level."

The Community will thus enter the second round of the negotiations, to be held in Geneva between 7th November and 2nd December, on the basis of a clear political commitment which must now be defined in a form capable of detailed presentation and defence.

2. The purpose of the present communication is to honour this political commitment by translating it into a concrete proposal for a Common Fund. Drawing on work conducted hitherto both within the Community and between the Community and its industrialised country partners, the proposal is based on the establishment of a Common Fund in the form of a pooling of the resources made available within individual buffer stock agreements, on the understanding that a sufficient number of such agreements can be induced to participate.

II. ELEMENTS FOR A COMMUNITY POSITION

Six main problem areas require attention and decision in order to determine the contents of a Community position for the reconvened Negotiating Conference, namely:

- whether or not the Common Fund's activities should be related exclusively to the financing of buffer stocks or should have a role in the financing of measures other than buffer stocks;
- whether or not special arrangements may be conceived to facilitate the participation of poorer producing developing countries in commodity agreements;
- the functioning and feasibility of a Common Fund as a pooling mechanism between buffer stock agreements;
- whether or not an element of own resources or a guarantee facility should be provided for the Common Fund and the form that this should take;
- the management and decision-making arrangements for a Common Fund;
- whether or not a provisional framework agreement might be required prior to the entry into force of sufficient buffer stock agreements and the conditions under which this would enter into operation.

These issues are outlined seriatim together with proposals in each case. It is recalled that in many detailed issues not covered here, but which may take on importance as the negotiation evolves, sufficient margin must be left to the Community's negotiators. The Commission may also wish to return in due course to the Council with appropriate supplementary proposals concerning the Community's negotiating position as and when the circumstances of the negotiation require.

III. MEASURES OTHER THAN BUFFER STOCKS

The Commission recalls that both developing and industrialised countries during the first part of the Negotiating Conference have agreed that the main function of any Common Fund should relate to the financing of buffer stocks.

The provisional position paper submitted by Group B during the March Negotiating Conference stated:

- "Whilst fully recognizing the importance of measures other than buffer stocking, the need and scope for a Common Fund in this context should be further explored having due regard to the international machinery which currently support such measures. If other measures are to be financed through a Common Fund, the account for such financing should be kept separate from that of buffer-stock financing."

It must be noted, however, that preparatory talks and negotiations so far on the 18 products covered by the UNCTAD Integrated Programme for Commodities indicate that only some of these commodities may be subject to the conclusion of commodity agreements based on buffer stocks. For certain developing commodity producing countries a role for the Common Fund in the financing of other measures than buffer stocks is of major importance and the developing countries as a group cannot envisage a successful conclusion to the Negotiating Conference without them. The Commission remains, however, of the opinion that most of the measures so far envisaged, e.g. in the Integrated Programme(1), could and should be financed by the established existing international agencies (e.g. International Bank for Reconstruction and Development (IBRD), United Nations Development Programme (UNDP), International Fund for Agricultural Development (IFAD), or regional banks). These agencies are already actively engaged in promoting commodity exports, production, and transformation in the context of overall economic development. It is hard to see what advantage to international cooperation may be obtained from the establishment of a new, inexperienced, and relatively small agency with no direct market involvement, whose decision-making procedures would scarcely be compatible with those of a development agency. A pooling mechanism operating essentially with revolving

(1) These range from promotional activities, research and development for improved product quality and use, to product processing, to diversification out of production, and to provision of infrastructure fostering trade, production or productivity.

funds for buffer stocks would not lend itself to the concessional and non-recoverable financing which "other measures" would appear essentially to involve, and any financing for other measures would require a second separate mechanism.

IV. POORER DEVELOPING PRODUCING COUNTRIES

A Common Fund based on a pooling system for buffer stock financing would help the special position of poorer producing developing countries only insofar as it achieved overall financial economies on the financing of stocks of interest to them. Discussions on certain individual commodities have shown that such countries may be disinclined to enter into stocking arrangements without an element of additional help. Such help might be provided by the International Monetary Fund's (IMF) Buffer Stocking Facility, although its interest rates are not concessional. The Commission proposes that the Community should indicate its readiness in due course to examine what elements of subsidy to IMF interest rates might be required, and whether the Common Fund may play any role in this framework.

V. THE POOLING SYSTEM

1. On the basis of Commission proposals the Council in March defined the Community's Opening Position in the Negotiating Conference in terms of a pooling system, i.e. an arrangement whereby commodity buffer stock agreements agree to deposit a proportion of their financial resources with a central pool in return for guaranteed drawing rights on that pool. This approach in turn became the core of the position put forward in the Negotiating

Conference by the Group B industrialised countries. Expert discussions before, during and since the March opening session of the Negotiating Conference have exposed a number of technical variations as to how such a pool could function without any clear choice being adopted. The purpose of this Communication is to propose formally the outline of such a pool.

2. Any form of pooling mechanism is based on a combination of agreed deposit obligations on the one hand and of maximum drawing rights on the other. The problem is to determine the optimum levels of these two elements and their relationship to each other and this from the points of view of the optimal functioning of the pool, the attainment of a maximum degree of financial "savings" to be obtained compared with the situation in which individual buffer stock agreements are financed in isolation, and the provision of sufficient attraction to induce buffer stock agreements to associate with the pool.

3. Deposit obligations. A number of ideas have been put forward:

- deposit of all financial resources made to individual agreements;
- deposit, for the first buffer stock purchases, of a given percentage of the resources made available to individual agreements;
- a system requiring individual agreements to finance a first percentage of their buffer stock purchases, with recource to the Common Fund for their later purchases in periods of greater economic difficulty.

The final scheme will very much depend on further discussions and negotiations. But on the basis of factors set out below there seems to be merit in a median course, whereby participating buffer stock agreements deposit a certain proportion only of their funds:

- Examination of the commodities that might come within a pooling system in the foreseeable future suggests that if the participating commodity agreements were to deposit around half of their funds, the Common Fund should have sufficient liquidity to meet its obligations and to achieve overall financial "savings" by means of the compensation effected.
- A requirement for individual commodity agreements to deposit more than half of their resources in the Common Fund would probably discourage them from joining in the first place. In any case the deposit obligation must be in line with the financial requirement for an average stockholding level.
- It would be easier to move towards higher deposit levels in the light of experience than to evolve in the opposite direction.

The level of overall "savings" which could be expected from the operation of a system of this kind will only become apparent in the light of experience. But on the basis of various models concerning the participation of individual commodities and the movements of markets, they may currently be assumed to be of the region of 15/20% of the total otherwise required for separate buffer stock financing.

4. Drawing rights. The maximum drawing right would be calculated as the sum of the deposit obligation plus a given percentage. This percentage would be in line with the expected proportion of "savings" to be achieved by the pool. Study hitherto suggests that this will be in the region of 15-20% and that it may provide a sufficient margin of incentive to buffer stock agreements to associate with the pool.

5. The arrangements negotiated will need to be encompassed in a set of clear rules, capable of as automatic an application as possible on a strictly non-discriminatory basis between individual commodity agreements. These will provide the terms on which bilateral agreements can be signed between these individual commodity agreements and the Common Fund. It should be a major task of the Negotiating Conference to reach agreement on these rules, having particular reference to the following points:

- Application/withdrawal: each individual commodity agreement will be free to decide whether or not to join in the Common Fund system. If they join they must accept the full obligations involved. If they decide to withdraw they should only do so after due notice. It would be desirable to establish the general rule that new commodity agreements do associate with the Common Fund and that they (a) remain within the Fund for a minimum of two years, (b) make their necessary deposit at the moment of joining and (c) agree to repay their loans in full at the moment of withdrawal, after due notice. The Common Fund should itself have the right, by duly considered majority decision, to ask for any individual commodity agreement to withdraw from the system, if it believed that its credit facilities were being abused.

- Interest rate policy: expert examination so far indicates that provision for the payment of interest on both deposits and on drawings would be more likely to guarantee the attractiveness of the pool to individual agreements and thereby its viability. Interest rates for both deposits and overdraft drawings should be closely related to going market rates. Whatever rates are applied, the rates charged on drawings should be marginally higher than those charged on deposits: the differential might be used to cover administrative costs.

VI. PROVISION OF ADDITIONAL GUARANTEE

1. The pool may, however, at times be in danger of being exhausted and for the following reasons not be able by itself to give a 100% guarantee that the credit necessary to meet all its maximum drawing right obligations would be available all the time.

- Commodity markets might move downwards at the same time and lead to such a demand for credit for financing stocking operations that the pool would become exhausted.
- Implementation of price or tonnage review clauses within commodity agreements might pose some short-term strain on the resources available.
- There may be need for ancillary resources during the initial period of stock building, particularly in connection with commodity agreements financing stocks out of levies on trade.

Some form of guarantee (or back-up) facility will, therefore, be required to enable maximum drawing rights to be guaranteed absolutely and to enable the Common Fund to act as a source of supportive loan finance in connection with initial stock building operations and/or stock building required as a result of either price or tonnage review, foreseen within commodity agreements. The Commission proposes that its maximum size might be stated as the difference (currently assumed to be 15-20%) between deposit obligations and maximum drawing rights.

2. Methods of guarantee provision. Various ways of providing such a guarantee may be envisaged, namely:

- by existing international financial institutions;
- by direct government contributions;
- by means of loans raised on the capital market with suitable collateral.

2.1 International financial institutions. Existing international organisations such as the IBRD and IMF, it has been suggested, might provide the guarantee to the Common Fund. However there are certain difficulties that would limit the Bank's efficacity:

- its terms of reference focus very much on development rather than on stabilisation of trade;
- there are several interested commodity trading countries which are not members of the Bank and it will be essential to involve them, particularly those which are prominent in commodity trade;
- complicated changes of articles might be required, with in any event decisions requiring submission to the Bank's Board.

2.2 Direct contributions. It has been suggested that participating governments should endow the Common Fund with a directly contributed element of own resources. This has met with considerable resistance from the majority of industrialised countries. An analagous suggestion that individual governments might make voluntary contributions suffer from the drawback that such an approach would not provide the certain source of supplementary financial support required.

2.3 Loan finance could be provided from the capital market. Such borrowing operations would require sufficient collateral. This collateral could be provided by:

- liens on buffer stocks;
- provision of subscribed or callable capital from participating governments.

Examination has shown that liens on buffer stocks would not on their own provide sufficient collateral for the borrowing requirements. As for capital provision by governments no case has hitherto been made indicating any advantage to be obtained from the provision of subscribed paid-up capital compared with callable capital which could provide much of if not the totality of the collateral requirements for borrowing operations.

3. The basis for financing. The Commission proposes that a combination of the above elements should be employed in order to constitute the guarantee facility. The possibility of some finance being provided by existing international financial institutions and by direct government contributions should continue to be explored. An additional borrowing requirement must, however, be expected. Collateral for part of this borrowing will be provided by liens on stocks. A residual element of collateral appears likely to be required. The Commission, therefore, proposes that all governments participating in the Fund[1], with the exception of countries with a GNP per capita below $300, should participate (on a GNP basis) in providing capital on call up to the overall maximum required, less such sums which can in time reliably be assured by international organisations, from voluntary governments contributions, or from loans raised through liens on stocks,

VII. MEMBERSHIP, MANAGEMENT, DECISION-MAKING

1. The Commission sees two major realistic choices concerning membership.
   - Membership both of commodity councils and of individual countries, with a careful balance of voting between the two;
   - reserving membership to individual countries, leaving individual commodity councils as observers, on the basis that relations between individual councils and the Fund are to be the subject of clear and automatic rules governing the Fund's operations.

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(1) Including countries which, whilst possibly not members of individual commodity agreements, are in substantial financial surplus.

The Commission proposes the second alternative. It sees the Fund as a financial mechanism and believes that the more it can operate on the basis of clear and automatic rules and limit the need for policy decisions, the better it will be. (The main policy areas where policy decisions may be required are the accession to or withdrawal from the Fund; acceptance or not of voluntary deposits; interest rate and investment policy, including the use of profits, utilisation of subscribed or callable capital; utilisation of additional voluntarily subscribed capital.)

2. Management should be placed in the hands of an Executive Manager, with a small Secretariat, who will be responsible to a Board of Management of (say) 20-25 members drawn from a Council open to all participating members as well as to observers.

3. Decision-making. Against this background steps should be taken to give those countries most involved in commodity trade or providing the major financial support for the Fund a deciding voice in policy decisions.

- One option would be for a straight voting system calling for a large majority, possible 75-80%, to approve any major policy proposal. It would have the merit of simplicity. But it might politicise decisions to the detriment of the real commercial and financial interests involved.
- An alternative to be studied would be a system of country voting within three groups, namely a consumers group, a producers group, and a finance group, with countries being able to vote in all three groups in accordance with their gross imports or exports of the commodities participating in the pool (first and second groups) and with the scale of their obligatory financial participation (third group). Major policy proposals might require a simple majority of votes, i.e. over 50% in each group in order to be adopted.

VIII. A FRAMEWORK AGREEMENT

The Community may be asked to take up a position on the early establishment of a framework agreement. This would become operational as and when enough commodity agreements were able and willing to participate. Readiness to entertain it might have the advantage of fostering acceptance by the developing countries of the pooling concept. The Commission proposes that if the advantage seems likely to be realised an indication, at a suitable moment, of agreement in principle to set up such an interim framework agreement could be useful. But it would only enter into force once sufficient buffer-stock agreements are ready to participate. To this end the Community is ready to concentrate on a limited number of commodity agreements, negotiated within a given time.

IX. COMMUNITY POLICIES INVOLVED

As was agreed by all participants at the Conference on International Economic Cooperation, the Common Fund is to serve as "a key instrument in attaining the agreed objectives of the Integrated Programme for Commodities". The establishment of the Fund thus forms a central part of the Programme and has to be considered in terms both of the purposes of the Programme as a whole and in relation to the series of commodity agreements which are to be concluded. The purposes of the Programme directly affect the operation of several Community policies. Provision will therefore need to be made at an appropriate moment for the Community as such to become a party to the arrangements establishing the Common Fund.

X. CONCLUSIONS

For the reasons set out above, and having regard to the importance of the issues and the practice followed at the Conference on International Economic Cooperation, it is proposed that the Council should decide:

- that the Community position should be along the lines set out in the present Communication, both in discussions with Group B/OECD partners and at the Negotiating Conference;

- that the Community and its Member States should participate in the Negotiating Conference as a single delegation, the spokesmen being the Présidency of the Council and the Commission, the Commission conducting negotiations for matters coming within Community competence.