

# CEPAL

## Review

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# CEPAL

## Review

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# International primary commodity marketing and Latin America

*Mikio Kuwayama\**

A major concern to the developing countries in the commodity area has been their insufficient participation in the marketing of export commodities and the resulting low share of the final consumer prices retained by them. In the light of the general assessment that international trade is conducted in a tightly controlled market environment, especially by transnational corporations, the paper attempts to bring to light some major features of commodity marketing, by examining the intra-firm trade in the said sector, with special reference to Latin America. The author argues that in contrast to manufactured goods exports, where intra-firm trade constitutes an important marketing mechanism, primary export commodities of importance to the region do not, in general, involve this type of marketing practices. For many commodities, the paper argues, the bulk of world trade is handled by a relatively small number of transnational, multi-product trading companies. The author subsequently gives a theoretical exposition on the modes of operations, functions and services of the transnational trading companies. Taking into consideration the peculiarities of commodity markets and the potential benefits that the organizational structure of a multi-product, multi-service trading company offers, the author asserts that this type of trading entity may be the kind of marketing organization which the countries in the region should aspire to develop for their own use. The poor performance record, examined in the paper, of international and regional entities involved in the sphere of commodity marketing and of the State trading organizations operating in the region leads the author to conclude that these entities should engage more actively in the marketing of commodities, either by taking their own initiatives or by becoming more effective co-ordinators of policies among the countries in and outside the region.

\*Staff member of the ECLAC International Trade and Development Division. This article further explores some conceptual considerations initially developed in a document of the International Trade and Development Division entitled *Comercialización y estructura de los mercados de productos básicos de América Latina y el Caribe* (LC/R.508). The author would like to thank Armando Di Filippo for his helpful comments on an earlier draft of this study.

## Introduction

The well-being of the commodity sector has been a major concern for the countries of Latin America and the Caribbean, due to its expected capability to generate export earnings on a sufficient scale, to finance development, and now especially to generate the required external financial resources. As a natural consequence of this, a substantial part of ECLAC's research efforts has been directed towards the examination of the specificities of the said sector and towards the search for solutions to the problems confronting it.

As is well known, the works of Dr. Raúl Prebisch marked a milestone in the evolution of international commodity policy. His works in the early 1950s overturned the conventional wisdom of classical economics that, as a consequence of diminishing returns on the production of commodities from a fixed stock of land, population increase and capital accumulation, the prices of such commodities would rise over the long run in relation to the prices of manufactures. Prebisch in turn made the challenging assertion that the international division of labour—the relegation of developing countries to the status of producers of primary commodities and the appointment of the industrialized countries to that of producers of manufactures—contained in itself an asymmetric division of benefits. He argued that the countries in the centre, as importers and consumers of commodities, received benefits accruing from the lower commodity prices resulting from productivity increases. Moreover, he stressed that these benefits to the centre were further increased by others accruing from the retention of productivity increases in the manufacturing sector in their own domestic markets, as improvements in labour productivity were appropriated largely by organized labour in the form of improved incomes, with little consequent downward pressure on prices. In developing countries, on the other hand, the unorganized, excess labour force reduced its negotiating capacity, allowing a major appropriation of labour productivity increases in the form of higher profits. As the rate of profits was sufficiently remunerative, the business sectors of the periphery could augment their supply even further, ceding partially the fruits of technologi-

cal progress through price reductions in world markets. These multiple benefits for the centre and impoverishing effects for the periphery, in his view, had self-perpetuating, differentiating income consequences, making the asymmetry even more severe.

In his report to UNCTAD I, Prebisch (1964) went on to identify the trend of long-term deterioration in the terms of trade of the commodity-exporting countries as the principal external constraint on their development process. He maintained that international policy should be focussed on establishing commodity agreements with the aim of reversing the long-run downward trend in the prices of the commodities exported by developing countries and on promoting national measures by developed countries to give better access to their domestic markets for commodities produced by developing countries. Prebisch recognized that, for many products, it may not be feasible to reverse long-term downward price trends of the developing countries' exports by the sole means of intergovernmental intervention in world markets in the form of commodity agreements, especially for those products facing strong competition from synthetics and substitutes. In such cases, he advocated the use of a compensatory financing mechanism to offset any deterioration in the terms of trade.

In short, instead of relying solely on the free play of market forces to stimulate development, the logic of Prebisch's argument called for positive intergovernmental actions, designed specifically to correct the worsening of the terms of trade, to improve commodity earnings prospects, and to reduce short-term fluctuations in those earnings, especially in the interests of the developing countries, on a non-reciprocal basis. This interrelationship between commodity policy and development, formulated by Prebisch, has formed the basis for all subsequent commodity negotiations and policy proposals debated in ECLAC and UNCTAD as well as in other international fora.

As the postwar history of international negotiations surrounding commodities testifies, Dr. Prebisch's arguments remain valid and their validity is further strengthened when considered in the light *first* of the very deprived state of

the commodity sector<sup>1</sup> and *second* the fact that his proposals, originally made more than 35 years ago, have continuously been put on negotiation tables (e.g., at the recent UNCTAD VII in Geneva, July 1987), though regretfully with very few concrete results.

From the outset the remedial actions initially proposed by Prebisch have faced strong opposition from the developed market economies, while the socialist countries have kept an indifferent stance on these international initiatives. The lack of progress in commodity negotiations reflects, to a large extent, the growing differences of approach between the countries of the South, which perceive the need for market intervention, and those of the North, which stress the need for solutions through the free play of market forces. The implicit assumptions made by the developed market economies on commodity markets are that they are characterized by perfect competition, with high factor mobility and the absence of market imperfections. The logic of this laissez-faire philosophy leads to the conclusion not only that any regulation of or intervention in the free play of market forces would produce a misallocation of resources, but also that the problems inherent in commodity markets are of a cyclical rather than a structural nature. Furthermore, in general, the developed countries have viewed these remedial actions purely in terms of their commercial interests, rather than as a common endeavour forming part of a broad strategy of development and international co-operation, as Prebisch had envisaged.

The perception by the South of commodity problems as "structural" has been reinforced in the post-World War II period by the transnationalization of this sector. Today, developing

<sup>1</sup>Commodity prices have shown remarkably unfavourable trends in nominal as well as in real terms: real commodity prices fell by about 30% between 1980 and 1986, and prices have now reached a level lower than in the Great Depression (1932). The resulting cumulative terms-of-trade loss in the present decade has reached US\$93 billion for the developing countries as a whole. In addition to this long-term deterioration of prices, other outstanding features of the commodity sector are: a continuing fall in the share of primary commodities in world trade; a continuing decline in the share of developing countries in world commodity export earnings in contrast with the growing role of developing countries in world commodity imports; and structural changes depressing demand and increasing supply.

countries have to contend not only with issues related to sharp fluctuations in prices and deterioration of their terms of trade, but also with unfavourable distribution of export benefits, particularly between the producers in the South and the transnational corporations (TNCs) which exercise a powerful influence in the marketing sphere of the commodity trade. The structure of the international marketing of commodities, which is the subject of the present paper, has assumed strong oligopolistic and/or oligopsonistic features, with the result that a comparatively small number of enterprises has come to handle the bulk of world trade. The limited participation of Third World producers in the final consumer prices of commodity exports has as its counterpart the highly organized trading community.

Restructuring the international commodity trading system has been one of the focal points of the North-South dialogue. The Integrated Programme for Commodities (IPC), as defined in UNCTAD Resolution 93 (IV), adopted by consensus by the international community at Nairobi in 1976, specifically calls for greater participation by Third World producers in the marketing and transport of commodities and better access of these producers to the markets of the industrialized countries. Specifically, the IPC calls, *inter alia*, for the adoption of international measures to "improve marketing, distribution and transport systems for commodity exports of developing countries, including an increase in their participation in these activities and their earnings from them".

During the course of continuing negotiations, the mandate of Nairobi was reconfirmed both in UNCTAD V at Manila in 1979 and UNCTAD VI at Belgrade in 1983, which agreed on the acceleration of the formulation of international co-operation in those specific areas.<sup>2</sup>

<sup>2</sup>In Manila, for instance, Resolution 124 (V) was adopted, without dissent, reaffirming to the international community the need to establish global co-operation, within the overall context of the IPC, in the field of the marketing and distribution of the commodity exports of developing countries. On this occasion, governments agreed to take into account, *inter alia*, the following specific aspects of the trading system from the Third World perspective: i) improvement in market transparency, including action where appropriate to improve the functioning of commodity exchanges; ii) increased technical and financial support for the development of national marketing and distribution systems of

Despite these efforts, however, there have been no concrete proposals for action, and to make it worse, the recent tendency of the industrialized countries regarding these issues is to slide back and even to question the UNCTAD mandate.<sup>3</sup>

The above dismal record of international negotiations for more than a decade and the rigid positions of the developed countries regarding these issues mean that the prospects for positive results through the instrument of North-South co-operation are indeed limited. Recent experience also supports the conclusion that seeking effective solutions to the many problems inherent in the commodity sector within a framework based exclusively on traditional commodity agreements involving both producer and consumer countries will lead to little action.<sup>4</sup> Consequently, if the developing countries seek rapid improvements in international marketing activities, these countries must look for alternative solutions. The objective of this paper is to facilitate discussions on possible solutions to achieve these goals.

Section I seeks first to identify the principal characteristics of the commodity markets by examining the U.S. intra-firm and related-party transactions. The analysis of the former is based primarily on the data contained in the recent publication, *United States Direct Investment Abroad 1982: Benchmark Survey Data*, while that of the latter is based on a non-confidential but unpublished source of information made available by the Foreign Division of the US Bureau of the Census. The latter, which gives the 1981 US related-party import trade data, is presumably the only, most up-to-date, and most comprehensive data source which allows an in-depth examination of the commodity marketing structure, and to the knowledge of the author it

developing countries; iii) examination of contracts, practices and arrangements governing the marketing of commodities; and iv) elimination of barriers to fair competition between marketing enterprises of developed and developing countries.

<sup>3</sup>The divergent views between the industrialized countries and the developing countries regarding these issues of commodity marketing and processing are documented in UNCTAD (1985 a, 1985 b).

<sup>4</sup>A summary of the events leading to this conclusion is to be found in ECLAC (1983a).

has not been analysed elsewhere.<sup>5</sup> Given the importance of the United States in global commodity trade, especially for the Latin American region,<sup>6</sup> the results derived from this data source should bring out some major characteristics of the trading systems surrounding commodities.

The results obtained suggest that though the proportion of intra-firm (or related-party) trade in total US imports is high (for example, related-party trade accounted for almost half of total U.S. merchandise imports in 1981), the share of such trade in the case of primary commodities, is, in general, relatively low. They also indicate that within commodities, the degree of "relatedness" tends to increase in proportion to the level of processing. These observations taken together seem to indicate that the participation of transnational *industrial* firms is more marked in those areas where the value-added is high. This finding is borne out by the bird's-eye look, given in Section II of the marketing structure of individual commodities which are major interest

to Latin America. In this section an attempt is also made to bring out some major factors responsible for such variability in the degree of intra-firm (or related-party) trade among different groups of products.

In contrast, as discussed in Section III, for commodities exported in a raw or semi-processed form the participation of transnational *trading* companies is high. A high level of intermediation by traders, nevertheless does not mean that the commodity markets approximate themselves to the free market operations as postulated under neoclassical theory. In this section, major characteristics and features of the commodity markets and principal agents are examined in a theoretical framework, and the conclusions drawn give little support for the wide applicability of the neoclassical theory to the behaviour of these markets.

Section IV reviews the past experience of some producers' associations and the participation of Latin American countries in them in order to draw some lessons for future actions. The performance of Latin American State Trading Organizations (STOs) is also examined. It is argued that though the consulting and co-ordinating capacities of these organizations have brought about some substantial improvements in the respective industries, the problems associated with over-production and marketing have been little touched upon by them. Examination of these cases seems to imply that only co-ordination and co-operation based on strong political will can safeguard the common interests of the respective industries, and these organizations should step forward to be directly engaged in marketing activities.

<sup>5</sup>A pioneering work analysing this census data base up to 1977 has been published by Professor G. Helleiner of the University of Toronto (Helleiner, 1981a). The analysis made in the present study deals with the 1981 trade figures. More recent figures are not available, since the U.S. Bureau of the census has decided to discontinue data collection since that date. While Helleiner's work on the U.S. related-party trade covers all product groups from all countries, this study puts emphasis on the commodity sector, with special reference to Latin America and the Caribbean. Ideally, the analysis should cover similar data for other industrialized countries, but unfortunately they are not available.

<sup>6</sup>The United States absorbs more than 30% of the Latin American and Caribbean commodity exports. Furthermore, in view of the continuing importance of commodities in U.S.-Latin American trade overall —they account for more than three-quarters of the region's exports to the United States— the results should reveal some major features of the system of trade between the two groups of countries.

## I

## The commercial environment for primary commodities: an analysis based on U.S. "intra-firm" and "related-party" transactions

### 1. U.S. intra-firm trade

International trade takes place within a very tightly controlled market environment where possibly 30-40% of global trade is on an intra-firm (broadly understood as a transaction between entities of the same concern) or related-party (between entities owning 5% or more of the total equity of the concern) basis. Another 30% is likely to constitute State trading and a further share is captive in nature as a result of sub-contracting or long-term contract agreements (UNCTAD, 1981a). Increasing rapidly in recent years are counter-trade schemes, which are estimated to account for at least 25% of world trade (Carey and McLean, 1986, p. 443). The illusionary concept of a freely competitive international market is narrowed down still further by the increasing tariff and non-tariff barriers imposed by both the developed and developing countries. Of course, some of the above are not mutually exclusive.

In view of the general acknowledgement that the developing countries' exports are pitted against a relatively small and organized group of buyers (see, for instance, UNCTC, 1983, Chapter 5), this sub-section tries to quantify and examine the degree of participation of TNCs in the marketing sphere of primary commodities. The selection of this sector reflects its vital importance for Latin American and Caribbean economies, accounting as it does for roughly 75% (excluding petroleum and its products, close to 35%) of regional merchandise exports (ECLAC, 1984 b).

A major point of interest is therefore the extent to which the transactions in commodities are intra-firm (or related-party) as against those effected at "arm's length". The term "intra-firm trade" indicates that which takes place between entities linked by direct investment,<sup>7</sup> and includes trade not only between parent firms and wholly-owned subsidiaries, and between parents

and majority-owned foreign affiliates (MOFAs), but also that between parents and minority-owned foreign affiliates. The definition of arm's length trade includes all types of sales between two or more independent entities, for either immediate or forward delivery, long-term contracts, or under preferential arrangements.

The exercise of quantifying and analysing the trading activities of TNCs is constrained by lack of data. Global intra-firm data are not available, for systematic collection of such data is presently not undertaken by governments (see note 5). The United States is the only country which collects comprehensive information in this regard and publishes it (through the Department of Commerce) in the form of benchmark surveys, the latest being *United States Direct Investment Abroad 1982* (U.S. Department of Commerce, 1985). The same organization also publishes annual surveys of the international investment position of the United States abroad and of U.S. affiliates of foreign firms operating in the U.S. The data contained in these documents, however, do not allow an examination of the marketing structure, by country and product, at a reasonably detailed level.

Nonetheless, the overall implications of the above-mentioned U.S. publications, taken together with results of other studies on other industrialized countries, are extremely important in that they show that TNCs are responsible for a large share of international trade flows. In the case of the United States, table 1 shows that in 1982 this share was approximately 40% of imports and 35% of exports by U.S. companies' affiliates abroad —being understood as entities owning 10% or more of the voting stock— or by

<sup>7</sup>Direct investment is said to exist, in the case of the United States, for example, when 10% or more of the voting securities of a foreign enterprise is owned by a U.S. person.

foreign parents with their affiliates in the United States. It has also been observed that the proportion of intra-firm exports in the total exports of the United Kingdom increased from 29% in 1976 to 31% in 1980. The 1980 survey for Japan also reveals that intra-firm trade corresponded to 26% and 25% of total national exports and imports, respectively, of that year (Japan, MITI, 1983, table 55). A sample of the world's largest industrial enterprises for 1977 showed that one-third of all parent company exports consisted of intra-firm sales, with the share varying from 45% for U.S. firms, to 30% for those based in Western Europe and 17% for Japanese firms (Dunning and Pearce, 1981).

Elaborating further exclusively on the intra-firm trade of the United States, of total U.S. imports associated with U.S. TNCs amounting to US\$120.8 billion in 1982: i) imports shipped by foreign affiliates to U.S. parents came to US\$41.6 billion (34.4%); ii) imports shipped by foreign affiliates to unaffiliated U.S. entities were US\$9.8 billion (8.1%); and iii) imports shipped by unaffiliated foreigners to U.S. parents amounted to US\$69.4 billion (57.5%). Among the three categories, only group i) falls under the definition and constitutes part of U.S.

intra-firm trade. Within this group, the U.S. 1982 benchmark survey provides data on U.S. imports shipped by MOFAs to U.S. parents at a one or two digit Standard International Trade Classification (SITC) level. United States imports shipped by MOFAs were US\$38.5 billion. In table 2, these intra-firm trade figures are contrasted with the total imports of corresponding SITC groupings in order to assess the relative importance of intra-firm trade within and across different sectors.

Looking at the data by countries of affiliates, as in the table, 32.3% of U.S. imports shipped by MOFAs were petroleum and its products, 27.4% were road motor vehicles and parts, and 22.1% were machinery. Imports of other products were relatively small. By region of MOFAs, imports from developed countries exceeded those from developing countries, overall as well as in such categories as food, petroleum and machinery.

In relation to the total U.S. import values of individual SITC groupings, imports from MOFAs to U.S. parents were most pronounced in road vehicles and parts (32.9%), machinery (20.9%), and petroleum and products (18.4%). For the developing regions as well, these three sectors were those which showed a high intra-firm trade

Table 1

## INTRA-FIRM TRADE OF THE UNITED STATES, 1982

(Billions of dollars)

Imports		Exports	
1. Imports from affiliated foreign firms	83.4	1. Exports to affiliated foreign firms	60.2
2. Imports from foreign affiliates of US parents	41.6	2. Exports to foreign affiliates of US parents	46.6
3. Total imports from affiliates (1+2)	125.9	3. Total exports to affiliates (1+2)	106.8
4. Overlap between 1 and 2	(30-35)	4. Overlap between 1 and 2	(30-35)
5. Total US merchandise imports	243.9	5. Total US merchandise exports	212.3
6. Percentage of affiliated imports (3-4)/5	37.3-39.3	6. Percentage of affiliated exports (3-4)/5	33.8-36.2

Source: Item 1: US Department of Commerce (1984, table 8). In this survey, a US affiliate is a US business enterprise in which there is foreign direct investment - that is, a single foreign person owns or controls, directly or indirectly, 10% or more of the voting securities if an incorporated business enterprise or an equivalent interest if an unincorporated business enterprise.

2: US Department of Commerce (1985 b, table 3). Affiliate is defined as "ownership directly or indirectly by one US person of 10% or more of the voting securities of an incorporated foreign business enterprise or an equivalent interest in an unincorporated foreign business enterprise".

3: Total US imports are on a Census basis and represent transaction values, f.a.s. the foreign port of exportation. Similarly, total US exports are on a Census basis and represent transaction values, f.a.s. the US port of exportation.

4: As the Department of Commerce acknowledges, exports and imports by US affiliates of foreign firms (item 1) cannot be simply added to US exports and imports associated with US parents (item 2), due to duplication in the two data sets. To the extent that US affiliates of foreign firms in turn had affiliates abroad, they would have been considered the US parents of those foreign affiliates in the 1982 annual survey. A highly preliminary match between the companies reported in both surveys indicated that the overlap for exports and imports was sizeable, roughly US\$30-35 billion each (Department of Commerce, 1985 c).



Table 2

**IMPORTANCE OF US IMPORTS SHIPPED BY MOFA's TO US PARENTS AS A PERCENTAGE  
OF OVERALL US IMPORTS, BY COUNTRY OF AFFILIATES AND BY PRODUCTS, 1982<sup>a</sup>**

*(Millions of dollars)*

Country of affiliate	Total SITC groups	Food	Beverages and tobacco	Crude materials, inedible, except fuels	Petroleum and petroleum products	Coal and coke	Chemicals	Machinery	Road vehicles and parts	Other transport equip- ment	Metal manufac- tures	Other manufac- tures	Other
	0-9	0	1	2	3	32	5	71-77	78	79	67, 68, 69	61-66, 8	4, 9
<b>Imports originating from:</b>													
<b>Developed countries<sup>b</sup></b>													
Total imports (i)	147 982	5 785	2 847	6 389	16 581	85	8 634	28 433	31 534	2 956	16 030	23 142	5 653
By MOFA's (ii)	21 813	218	210	1 017	3 494	6	1 175	3 466	10 016	245	738	1 198	30
(ii)/(i) (%)	14.7	3.8	7.4	15.9	21.1	7.1	13.6	12.2	31.7	8.3	4.6	5.2	0.5
<b>Canada</b>													
Total imports (i)	46 792	1 872	440	4 444	7 948	56	2 371	4 813	11 308	929	3 179	6 184	3 005
By MOFA's (ii)	16 551	35	51	628	<sup>d</sup>	0	<sup>d</sup>	1 645	9 855	214	245	701	<sup>d</sup>
(ii)/(i) (%)	35.4	1.9	11.6	14.1	-	-	-	34.2	87.2	23.0	7.7	11.3	-
<b>EEC (10 countries)</b>													
Total imports (i)	44 462	1 190	2 209	513	6 853	2	3 719	11 623	5 134	1 372	4 984	8 161	1 629
By MOFA's (ii)	3 266	50	132	43	383	0	546	1 172	149	30	372	372	19
(ii)/(i) (%)	7.3	4.2	6.0	8.4	5.6	-	16.7	10.1	2.9	2.2	7.5	4.6	1.2
<b>Japan</b>													
Total imports (i)	39 916	302	19	72	30	4	923	12 814	14 103	402	5 639	5 330	340
By MOFA's (ii)	762	<sup>d</sup>	0	<sup>e</sup>	0	1	17	<sup>d</sup>	2	0	<sup>d</sup>	83	0
(ii)/(i) (%)	1.9	-	-	-	-	25.0	18.4	-	-	-	-	1.6	-
<b>Total imports from all countries (i)</b>													
	254 862	15 717	3 666	9 437	67 500	91	9 885	40 794	32 074	3 236	20 414	44 219	7 923
<b>Imports by MOFA's, all countries (ii)</b>													
	38 533	921	272	1 471	12 437	6	1 331	8 511	10 549	262	1 026	1 714	34
(ii) / (i) (%)	15.1	5.9	7.4	15.6	18.4	6.6	13.5	20.9	32.9	8.1	5.0	3.9	4.3

Table 2 (concluded)

Country of affiliate	Total SITC groups	Food	Beverages and tobacco	Crude materials, inedible, except fuels	Petroleum and petroleum products	Coal and coke	Chemicals	Machinery	Road vehicles and parts	Other transport equipment	Metal manufactures	Other manufactures	Other
	0-9	0	1	2	3	32	5	71-77	78	79	67, 68, 69	61-66, 8	4, 9
<b>Imports originating from:</b>													
<b>Developing countries<sup>bc</sup></b>													
Total imports (i)	103 211	9 645	771	2 874	50 158	5	934	12 186	506	269	4 143	19 477	5 924
By MOFA's (ii)	16 720	703	62	454	8 943	0	156	5 045	3534 <sup>f</sup>	17	288	515	3
(ii)/(i) (%)	16.2	7.3	8.0	15.8	17.8	-	16.7	41.4	105.5	6.3	7.0	2.6	-
<b>Latin America</b>													
Total imports (i)	39 570	6 828	432	1 515	20 323	5	678	3 263	317	135	1 673	3 062	1 344
By MOFA's (ii)	6 251	621	39	295	3 086	0	123	1 279	534 <sup>f</sup>	<sup>d</sup>	72	189	<sup>d</sup>
(ii)/(i) (%)	15.8	9.1	9.0	19.5	15.2	-	18.9	39.2	168.5		4.3	6.2	
<b>Africa</b>													
Total imports (i)	16 399	1 088	29	383	14 265	-	9	16	-	-	478	77	117
By MOFA's (ii)	2 544	0	<sup>d</sup>	<sup>d</sup>	2 350	0	0	<sup>d</sup>	0	0	<sup>d</sup>	<sup>d</sup>	0
(ii)/(i) (%)	15.5	-			16.5		-						-
<b>Asia</b>													
Total imports (i)	47 129	1 665	309	976	15 571	-	247	8 922	189	133	1 973	16 333	578
By MOFA's (ii)	7 925	82	<sup>d</sup>	<sup>d</sup>	3 508	0	32	3 766	0	<sup>d</sup>	<sup>d</sup>	<sup>d</sup>	<sup>d</sup>
(ii)/(i) (%)	16.8	4.9			22.5		13.0	42.2					

Source: Figures for MOFA's are taken from US Department of Commerce (1985 b). Trade figures by SITC grouping are from United Nations, *Commodity Trade Statistics*.

<sup>a</sup>In this table, data for affiliates are only for non-bank affiliates of non-bank parents. MOFA's (Majority Owned Foreign Affiliates) are defined as affiliates owned more than 50% by all US parents combined.

<sup>b</sup>Excludes centrally planned economies.

<sup>c</sup>The sum of the three developing regions does not add up to the total of developing countries, due to the exclusion of Oceania.

<sup>d</sup>Suppressed to avoid disclosure of data of individual companies.

<sup>e</sup>Less than \$500 000 (+/-) or 50 employees.

<sup>f</sup>Imports shipped by MOFA's exceed the overall total, due probably to reporters' incorrect classification of transportation equipment, parts and accessories.

Table 3

**US RELATED-PARTY TRADE AS A PERCENTAGE OF TOTAL IMPORTS  
(CUSTOMS VALUES), BY US TARIFF SCHEDULE (TSUS), 1981**

TSUS schedule	Product group	Schedule number	Total imports (US\$ million) (A)	Related-party trade (US\$ million) (B)	(B)/(A) %
Schedule 1	Animal and vegetable products	100.0110-193.2560	20 261	3 440	17.0
2	Wood and paper; printed matter	200.0300-274.9040	9 647	2 405	24.9
3	Textile and textile products	300.1020-390.6000	9 780	1 377	14.1
4	Chemicals and related products	401.0200-495.2000	94 796	49 870	52.6
5	Non-metallic minerals and products thereof	511.1100-548.0500	5 874	1 099	18.7
6	Metals and metal products	601.0300-696.6000	97 127	61 413	63.2
7	Specified products; miscellaneous and non-enumerated products	700.0500-799.0000	20 179	6 727	33.3
8	Special classification provision	800.0000-870.4500	4 687	2 046	43.6
Appendix to the tariff schedules		901.0020-957.1500	363	341	93.9
<b>Total</b>			<b>259 012</b>	<b>126 788</b>	<b>49.0</b>

*Source:* Data provided by the Foreign Trade Division of the US Bureau of the Census.

ratio. Though it was not possible to make a direct comparison, due to the manner in which the SITC groupings were aggregated by the Department of Commerce, those categories usually understood to constitute primary commodities (SITC 0-4; 68) can be said to have a relatively low intra-firm ratio. Latin America does not differ significantly from other developing regions in terms of relative sectoral importance in the intra-firm import trade of the United States.

## *2. U.S. related-party trade (RPT)*

For an examination by individual country and at a much more disaggregated product level, the data employed below are those of the Foreign Trade Division of the U.S. Bureau of the Census, and show the value and volume of U.S. imports, within each individual tariff classification of the U.S. tariff schedule (TSUS) and from each country of origin, which originate from "related parties". The definition of a "related party" is a firm in which 5% or more of the voting stock is

owned by the other party with which it trades. The coverage is for both U.S. firms and for firms based outside the United States.

Examination of the 1981 figures indicates that, for that particular year, 49.0% of total U.S. merchandise imports were transacted in the form of RPT (table 3). This coincides roughly with the figures of 45.0% and 48.8% for 1975 and 1977 respectively given in the studies by Helleiner (1979; 1981), though indicating a slight increasing trend over the years. The overall figure also seems to be in conformity with the results obtained from the 1982 benchmark survey just mentioned above: a lower intra-firm import ratio of roughly 40% (table 1) could be explained by the difference in definition of the coverage of capital ownership between RPT and direct investment (10% or more of the voting securities of a foreign enterprise owned by a U.S. entity). The wide variations in RPT ratios observed among major product groups, even at the most aggregated level, are also in accordance with the results of the 1982 benchmark study. In

the case of RPT ratios, in general, high ratios were observed for manufactured goods, especially in the heavy industrial sectors, while animal and vegetable products and non-metallic minerals registered a relatively low RPT coefficient. An exception to the above was textiles and their products. Two groups (chemicals, and metals and their products) were most dominant in this respect, accounting for 74.1% of total imports and 87.8% of the RPT total.

RPT can be disaggregated further along the TSUS sub-groupings and compared with total U.S. imports, as shown in table 4. It should be noted first that within each schedule, there was a large variation from product to product, in the agricultural as well as the mineral and metal sectors. Though generalization is difficult, the RPT rose as a proportion of the total as one moved from primary products, excluding petroleum, to semi-manufactures. Within primary commodities, the degree of "related-ness" tended to increase in accordance with the level of processing/manufacturing,<sup>8</sup> an aspect to be further elaborated later on in the paper. A large number of commodities which are of major interest to the Latin American region showed an extremely low RPT ratio, as in the cases of hides and skins, sugar, beverages, cereals, spices and oilseeds.

The order of absolute RPT values at the sub-grouping level, was led by petroleum, followed by road vehicles; machinery for industrial use; electrical machinery; apparatus and appliances; iron and steel; precision apparatus; power generating machinery; general industrial machinery; office machines and automatic data processing equipment, etc. The manufacturing sectors mentioned herein were those in which high absolute import values were accompanied by high RPT ratios. As a primary commodity,

only aluminium exceeded the 1 billion dollar mark.

Lastly, on the basis of the same data it is possible to examine the degree of RPT in primary commodities with special reference to Latin America and the Caribbean, as shown in table 5.<sup>9</sup> In this exercise, the product was analysed at a 7-digit TSUS, on the assumption that further disaggregation would shed more light on the participation of TNCs in the international marketing of commodities. Furthermore, individual commodities were grouped together and compared in accordance with their degrees of processing. Products selected here were of major export interest to the region.

One of the principal findings of this exercise was that in some commodities (such as bauxite/alumina/aluminium and bananas) the RPT ratio was extremely high, while in others, it was nearly non-existent (as in sugar) or very low (in the case of cocoa beans and coffee beans). Looking at the commodity sector alone, however, it can be concluded that those items of importance to the region registered, with some exceptions, low RPT ratios. This seems to suggest that the number of commodities which display total integration from production to the last stage of external marketing is not large.

The above analysis also highlights the point that within a given commodity group (with some exceptions) a higher RPT ratio is observed for products with a higher level of processing, and thus higher value-added. Good examples of this are the product chains of: i) cocoa beans/cocoa butter/chocolate; ii) live animals/meat/meat preparations; iii) hides and skins/footwear; iv) timber/lumber/furniture; v) leaf tobacco/manufactured tobacco; and vi) some mineral ores/metals, as in the case of copper and tin. What may be inferred from this is that transnational *industrials* are involved and practice most effective market control in the downstream processing activities where the value-added is high. Those high value-added activities usually involve the use of brand names, heavy advertising and product differentiation, as

<sup>8</sup>This conclusion accords well with the findings by Helleiner on the earlier years. He indicated that this general pattern was found for the 1977 imports from both the Third World and OECD members. As he concluded, "other things being equal, one can expect increases in the role of related-party trade as industrialization proceeds in the Third World and the relative importance of their manufactured goods trade continues to rise". Mainly due to the interrelationship between RPT and manufacturing, Helleiner found that the relative importance of RPT seems to be much greater in the imports from the OECD countries than in the case of imports from the developing countries.

<sup>9</sup>Due to the very detailed nature of the information contained in the data provided by the U.S. Bureau of the Census, the figures are aggregated at the regional level. For figures at the individual tariff schedule level and by country, see ECLAC (1986 c, table 3).

Table 4

**US IMPORT STRUCTURE: RELATED-PARTY TRANSACTIONS  
BY US TARIFF SCHEDULE (TSUS), 1981**

Product sub-groupings	Product descriptions	Total imports, customs values (US\$ 000) (A)	Related-party transactions, customs values (US\$ 000) (B)	(B)/(A) (%)
101	Animals, live	359 928	45 114	12.5
102A	Bird meat	3 371	247	13.6
102B	Other meat and meat preparations	1 990 274	432 569	21.7
102	Meat and meat preparations	1 993 645	432 816	21.7
103A	Fish, fresh, chilled or frozen	1 282 896	495 229	38.6
103B	Fish, dried, salted	81 440	2 928	3.6
103C and D	Fish, prepared or preserved	230 901	40 176	17.4
103E	Crustaceans and molluscs, prepared or preserved	1 333 155	236 220	17.7
103	Fish and fish preparations	2 928 393	774 552	26.4
104A and D	Milk and cream	16 088	10 286	63.9
104B	Butter and fresh or sour cream containing over 45% butterfat	2 155	34	1.6
104C	Cheese and curd	332 062	39 202	11.8
104D	Birds' eggs and birds' egg albumen and yolks	5 541	777	14.0
104	Dairy products and eggs	335 846	50 299	14.1
105A	Hides and skins (except furskins), undressed, raw or cured	454 989	8 430	1.9
105B	Furskins	193 795	3 538	1.8
105	Hides, skins and furskins, undressed, raw or cured	648 783	11 968	1.8
106A	Plants, live	67 830	20 152	29.7
106B	Seeds of plants	57 714	6 387	11.1
106	Plants and their seeds	124 543	26 539	21.3
107	Barley, buckwheat, corn, sorghum, oats, rice, rye, wheat, starches	95 060	6 436	6.8
108	Vegetables, fresh, frozen or temporarily preserved, and dried leguminous vegetables, roots and tubers	839 061	403 165	48.0
109	Fruits and nuts, fresh or dried, prepared or preserved	1 605 124	616 484	38.4
110A	Sugar, sirups, molasses and honey	2 306 812	25 558	1.1
110B	Cocoa beans, butter, powder and chocolate	876 212	101 192	11.5
110C	Other food preparations containing cocoa or chocolate	123 759	53 484	43.4
110	Sugar, molasses, honey; cocoa and its products	3 306 783	180 234	5.5
111A	Coffee, tea, mate	3 019 422	147 390	4.9
111B	Spices	136 033	2 425	1.8
111	Coffee, tea, spices and manufactures thereof	3 155 456	149 814	4.7
112A and B	Beverages nonalcoholic	656 672	137 612	21.0
112C and D	Beverages alcoholic	2 338 086	460 091	19.7
112	Beverages	2 668 024	489 658	18.4
113	Tobacco and its manufactures	184 140	36 456	19.8
114	Oilseeds, oil nuts and oil kernels, non-specified	558 039	32 619	5.8
115	Cereal preparations and miscellaneous food preparations	1 068 893	159 967	15.0

Table 4 (continued 1)

Product sub-groupings	Product descriptions	Total imports, customs values (US\$ 000) (A)	Related-party transactions, customs values (US\$ 000) (B)	(B)/(A) (%)
Schedule 1	Animal and vegetable products	20 260 724	3 440 047	17.0
201, 202, 203	Wood, lumber, cork	3 482 229	426 074	12.2
204	Pulp and paper	5 559 341	1 824 329	32.8
205	Books, printed matter	605 633	154 453	25.5
Schedule 2	Wood and paper; printed matter	9 647 202	2 404 855	24.9
301A	Cotton fibre, waste, yarn	49 763	14 327	28.8
301B	Other textile fibres, waste, yarn, abaca, flax, hemp sisal, henequen, jute, etc.	44 402	1 740	3.9
301C	Wool and other animal hair and yarn	222 138	22 003	9.9
301D	Raw silk, yarn	12 483	2 554	20.5
301E	Manmade fibres	218 640	72 738	33.3
301F	Other yarns	1 404	564	40.2
301	Textile fibres, waste, yarn	548 829	113 927	20.8
302	Cordage, twine	103 597	12 798	12.4
303A	Cotton fabrics	590 143	37 479	6.4
303B	Fabrics, vegetable fibres	160 893	15 041	9.3
303C and D	Woven fabrics, silk, wool	205 069	13 205	6.4
303E and F	Woven fabrics, manmade fibres	553 637	180 422	32.6
303	Textile fabrics	1 509 741	258 415	17.1
304	Knitfabrics of textile fibres, narrow fabrics, lace, netting, etc., special textile fabrics and related products	310 552	124 254	40.0
305	Floor coverings, tapestries, and particles of vegetable plaiting materials	527 799	48 153	9.1
306	Wearing apparel and accessories	6 512 782	778 905	12.0
307	Bags, ornaments, ribbons, rags, wipenings	268 647	40 145	14.9
Schedule 3	Textile fibres and textile products	9 779 948	1 376 598	14.1
401	Organic chemicals and related products	2 141 409	1 133 549	52.9
402	Inorganic chemicals and related products	4 067 633	1 803 397	44.3
403	Medical and pharmaceutical products	711 178	392 081	55.1
404	Synthetic resins; and rubber and plastics materials	1 181 082	455 277	38.5
405, 406, 407	Essential oils and perfume materials, toilet, polishing and cleansing preparations	813 493	137 427	16.9
410	Crude petroleum, petroleum products	80 337 109	43 324 614	53.9
411	Fertilizers, manufactured	1 393 909	425 176	30.5
412	Explosives	20 720	4 291	20.7
413	Animal and vegetable oils and fats, processed, fatty acids, waxes of animal, vegetable or mineral origin	417 575	141 172	33.8
Schedule 4	Chemicals and related products	91 094 107	47 940 701	52.6
501	Crude materials, graphite, cement, limestone, marble, stone, mica, asbestos; natural abrasives, crude or processed, including industrial diamonds, natural or synthetic, other precious and semi-precious stones	4 153 492	624 336	15.0
502A and B	Clay and refractory construction materials	275 742	56 404	20.5

Table 4 (continued 2)

Product sub-groupings	Product descriptions	Total imports, customs values (US\$ 000) (A)	Related-party transactions, customs values (US\$ 000) (B)	(B)/(A) (%)
502C, D and E	Pottery, porcelain or china household ware, earthenware or stoneware, ceramic, and china ornamental articles	780 264	201 044	25.8
503	Glass, glassware, and articles thereof	664 104	217 332	32.7
Schedule 5	Non-metallic minerals and products thereof	5 873 604	1 099 116	18.7
601	Non-ferrous metals, ores	2 372 504	953 087	40.2
602A	Precious metals, incl. gold and silver	3 859 783	508 053	13.2
602B	Iron and steel, various types and forms	11 260 776	7 330 680	65.1
602C	Copper and copper alloys, wrought and unwrought, waste and scrap, and related products	1 151 028	213 198	18.5
602D	Aluminium and aluminium alloys, wrought and unwrought, waste and scrap, and related products	1 384 909	1 029 879	74.4
602E	Nickel and nickel alloys, wrought and unwrought, waste and scrap, and related products	895 639	563 895	63.0
602F	Tin and tin alloys, wrought and unwrought, waste and scrap and related products	645 312	182 812	28.3
602G	Lead and lead alloys, wrought and unwrought, waste and scrap, and related products	89 559	21 156	23.6
602H	Zinc and zinc alloys, wrought and unwrought, waste and scrap, and related products	562 257	104 137	18.5
602 I, J and K	Other metals and alloys, waste and scrap, and related products	616 227	36 516	5.9
602	Non-ferrous metals	20 456 490	10 072 509	49.2
603	Manufactures of metal	5 658 425	1 140 220	20.2
604A	Power generating machinery and equipment, general industrial machinery and equipment	6 342 651	2 989 773	49.1
604B	Mechanical handling equipment	1 612 466	909 889	56.4
604C	Agricultural and horticultural machinery (except tractors), food processing machinery	748 306	442 585	59.1
604D	Printing and bookbinding machinery and parts thereof	671 196	240 299	35.8
604E	Textile machinery; washing, bleaching, dying	965 313	490 416	50.8
604F	Metal working machinery, machine tools	2 268 852	1 206 397	53.2
604G	Office machines and automatic data processing equipment	3 492 998	2 565 045	73.4
604H	Shoe machinery, machinery for sorting, molding, cigarette making, audio-players, radios, etc.	1 766 375	857 068	48.5
604J	Balls, ball bearings, valves, etc.	1 554 368	779 448	50.1
604	Machinery of industrial use	19 422 528	10 480 920	54.0

Table 4 (concluded)

Product sub-groupings	Product descriptions	Total imports, customs values (US\$ 000) (A)	Related-party transactions, customs values (US\$ 000) (B)	(B)/(A) (%)
605	Electrical machinery, apparatus and appliances	11 160 255	8 048 663	72.1
606	Road vehicles, other transport equipment	31 776 287	26 574 475	83.6
Schedule 6	Metals and metal products	97 127 166	61 412 971	63.2
701A	Footwear	8 141 218	234 138	7.5
701B	Headwear of all materials	154 524	20 455	13.2
701C	Gloves of textile fibres, rubber, plastic	215 507	72 150	33.5
701D	Travel goods, handbags	290 807	51 303	17.6
701	Various wearing articles	3 802 056	378 046	9.9
702A	Contact lenses, optical lenses	779 071	293 797	37.7
702B	Medical equipment and apparatus	672 467	357 704	53.2
702C and D	Professional and scientific instruments	1 187 876	676 706	57.0
702E	Watches and clocks	1 250 716	645 961	51.6
702F	Photographic apparatus and equipment	1 463 403	1 006 109	71.7
702G	Motion-picture film, phonograph records, recorded tapes, etc.	393 874	228 781	58.1
702	Precision apparatus and equipment	5 687 406	3 209 058	56.4
703	Musical instruments, cases, parts	262 852	119 206	45.4
704A	Furniture	1 256 706	321 764	25.6
704B	Floor coverings	36 059	7 909	21.9
704	Furniture and floor coverings	1 292 765	329 673	25.5
705A	Firearms, munitions, cartridges	159 659	29 459	18.5
705B	Fishing equipment	136 999	36 809	26.9
705C	Bicycles, baby carriages	340 533	73 873	21.7
705D	Sporting equipment	1 140 403	356 968	31.3
705E	Toys	862 303	222 977	25.9
705	Sporting goods and toys	2 639 897	721 086	27.3
706, 707, 708	Other manufactured articles	1 642 567	251 002	15.3
709, and 710	Art works, antiques	725 809	35 191	4.8
712	Rubber manufactures	2 784 515	1 515 538	54.4
713 and 714	Miscellaneous	828 916	141 036	17.0
Schedule 7	Specified products; miscellaneous and non-enumerated products	20 178 878	6 726 712	33.3
801, 802, 803	US goods returned, re-imported goods	4 687 375	2 046 316	43.7
804, 805, 806	for public use and institutions	4 687 375	2 046 316	43.7
Schedule 8	Special classification provision	4 687 375	2 046 316	43.7
901, 902, 903, 904, 905	Miscellaneous	362 945	340 709	93.9
Schedule 9	Appendix to the tariff schedules	362 945	340 709	93.9
SCH 1 - 9	Total	259 011 948	126 788 024	49.0

Source: Data provided by the Foreign Trade Division of the US Bureau of the Census.



Table 5  
STRUCTURE OF US PRIMARY COMMODITY IMPORTS: RELATED-PARTY  
TRADE, BY TSUS AND BY REGION, 1981

(Thousands of dollars)

TSUS No.	Product description	Total import value (A)		Total related-party (B)		(B)/(A) %	
		Latin America	All countries	Latin America	All countries	Latin America	All countries
1061029	Beef with bone, fresh, chilled	1 380	21 523	0	42	-	0.2
1061060	Beef without bone, fresh, chilled, frozen	189 957	1 313 897	14 844	283 247	7.8	21.6
1074820	Corned beef	96 526	97 003	27 877	28 011	28.9	28.9
1074840							
1144545	Shrimps and prawns, shell-on	491 759	537 818	112 624	116 543	22.9	21.7
1201400	Cattle hides, raw or cured	136	28 716	-	1 397	-	4.9
1216138	Bovine leather, not fancy, n.s.p	18 464	29 777	-	629	-	2.1
7002960*	Footwear, leather	419 877	1 590 007	15 392	119 873	3.7	1.5
1464000	Bananas, fresh	708 956	709 496	499 621	500 048	70.5	70.5
1552045	Cane or beet sugar, syrup, molasses, n.s.p	1 483 982	2 292 585	-	17 083	-	0.7
1561000	Cocoa beans	157 131	501 346	450	16 991	0.2	3.4
1562000	Chocolate, unsweetened	78 617	89 196	8 607	10 730	10.9	12.0
1563500	Cocoa butter	125 216	228 115	13 581	29 043	10.8	12.7
1601020	Coffee, crude	1 915 862	2 769 649	46 940	113 311	2.4	4.1
1601040	Coffee, roasted or ground	32 860	40 564	1 881	4 227	5.7	10.4
1602000	Soluble or instant coffee, no additives	212 629	227 321	6 974	15 153	3.3	6.7
1653540	Orange juice, concentrated	197 581	199 108	564	565	0.3	0.3
1703210	Cigarette leaf tobacco, not stemmed	17 184	43 757	3 401	14 778	19.8	33.8
1703230							
1706020	Cigar leaf scrap tobacco	20 594	37 186	518	616	2.5	1.7
1706600	Cigars	26 271	28 045	9 979	9 981	40.0	35.6
1707000							
1708045	Tobacco, manufactured or not	75 549	146 712	9 398	26 652	12.4	18.2
2003549	Hardwood logs and timber	579	1 236	3	-	0.1	0.1
2023200							
2023420	Lumber, balsa/teak, mahogany and others	54 371	83 851	185	747	0.3	0.1
2024400							
2026600	Hardwood moldings, carvings, etc.	6 098	24 680	2 335	4 303	38.3	17.4
2070080	Articles of wood, n.s.p.	5 721	70 639	2 218	6 426	38.8	9.0
2400320	Hardwood veneers, plywood	22 758	176 739	9 078	17 396	39.9	9.8
2402360							
7272900							
7273540	Wooden chairs, furniture and parts	31 358	791 119	5 220	107 384	16.6	13.6
7275560							
3001040	Raw cotton, n.s.p.	4 573	5 246	4 026	4 026	88.0	76.7
3013000	Cotton yarn, not bleached	6 699	10 386	16	16	0.2	0.2
3044600	Sisal and henequen, waste	950	2 228	-	-	-	-
3063172	Wool finer than 58s	20 082	56 999	667	13 251	3.3	23.2
6010600	Crude bauxite	357 915	491 015	271 671	374 256	75.9	76.2
4171240	Aluminium oxide (alumina)	236 206	880 557	138 909	448 090	58.8	50.9
6180200	Aluminium, unwrought, not alloyed	901	359 001	-	309 437	-	86.2
6180650	Aluminium, unwrought, alloyed	4 428	220 244	3	27 622	0.1	12.5
6182565	Aluminium, sheets and strip	42 202	548 690	2 117	433 178	0.5	78.9
4751010	Crude petroleum, 250 deg. API or over	7 012 018	58 560 007	3 221 099	35 456 288	45.9	60.5
6012430	Iron ore	253 164	835 041	13 774	454 505	0.5	54.5
6012450							
6012760	Manganese ore	6 649	39 538	145	5 897	2.2	14.9
6015400	Tungsten ore	32 252	92 710	6 408	8 586	19.8	9.3
6021011	Lead ore, initially treated	20 309	22 272	-	-	-	-
6240350	Lead, unwrought, not alloyed	24 431	69 358	14 373	14 473	58.8	20.9
6022022	Zinc ore, initially treated	34 785	113 458	-	32 704	-	28.8
6260200	Zinc, unwrought, not alloyed	106 844	567 827	31 827	109 679	29.8	19.3
6023033	Copper ore, initially treated	17 218	55 502	97	1 843	0.1	3.3
6120640	Copper, unwrought, not alloyed	296 330	598 336	10 644	54 652	3.6	9.1
6220200	Tin, unwrought, not alloyed	130 147	645 386	13 831	182 751	10.6	28.3
6220420	Tin, unwrought, alloyed	1 152	3 688	-	1 319	-	25.8

Source: Data provided by the Foreign Trade Division of the US Bureau of the Census.

\*This group includes 7002980, 7003515, 7003530, 7004510, 7004540, 7004560.

in the case of most food and beverage markets like those of chocolate, processed tea or coffee.

The degree of RPT in Latin American commodity exports to the United States was not significantly different from that in exports from all origins. Exceptions included processed wood products, tungsten ore, lead and zinc, in which the Latin American figure was higher. In the case of petroleum, the Latin American ratio was substantially lower than the corresponding one for the world.

What can be concluded from the preceding analysis is that though intra-firm trade (or RPT) is frequently found in industries or sectors in which there is a high degree of market concentration, it is not necessarily directly correlated with it. A high concentration in production/refining/processing does not necessarily imply an accordingly high intra-firm (or RPT) ratio.

The observations made up to now raise several interesting questions, namely: i) what factors are responsible for the high RPTs in manufactures and low RPTs for primary commodities in general? and ii) what are the reasons for the varying RPT ratios among different commodities? In short, an important question is why the TNCs, trading or manufacturing alike, decide to employ intra-firm trade (or RPT) rather than arm's-length trading in some commodities and not in others.

While bearing in mind the risks involved in generalizing issues of this nature, it may be said that TNCs are more likely to seek to internalize trade operations under the form of intra-firm trading when one or more of the following factors are of importance:<sup>10</sup>

- i) When intermediate inputs are highly specific to the firm in terms of quality, specifications and technology, as in the case of many manufactured goods, or of bauxite;
- ii) When there are substantial marketing and after-sale requirements for finished product sales, as is the case in many manufactured products, but less so in primary commodities;
- iii) When there are risks of intermediate input supply disruptions;

iv) When there are problems of perishability or limited storability of the product, as exemplified by bananas, which requires very timely co-ordination between production and marketing across different national boundaries;

v) When there is a protective umbrella against rising prices which allows a rise in raw material costs to be passed on to the final product price without too much difficulty. For instance, the share of bauxite in the final price of aluminium is very low, so that a large increase in bauxite prices will not affect too much the final price of aluminium. On the other hand, as in the case of the majority of commodities, the share of raw material costs is high and this produces a higher risk, thereby inducing a higher level of intermediation (such as that offered by trading companies) in order to reduce the risks arising from sudden price changes;

vi) When there is weak tax or exchange control which increases the potential for transfer pricing.

The concept of "transaction costs" is helpful in explaining the major differences in marketing between commodities and manufactured goods. These are the costs which are incurred by the transacting parties in a market exchange in order to enforce their exclusive rights to the assets or services being traded. R.H. Coase (1937) long ago pointed out that the operation of the market is not costless, and that *internalization* of certain functions, instead of arm's-length transactions, is a rationale for creating a firm. Internalization brings about efficiency in such areas of production as transaction, contracting and enforcing contracts. The brokerage cost of finding a correct price, the cost of defining the obligations of parties in a contract, the risk of scheduling and related input costs, and costs related to foreign exchange in the case of foreign trade are not insignificant. Reduction of these costs and of the risk and uncertainty associated with them is a justification for vertical integration. By integration, the organization can occasionally use administrative fiat to set internal prices, and can control the production and marketing of intermediate products.

Business by fiat creates opportunities for price maneuverability. Predatory pricing, price discrimination and transfer pricing are often-discussed incentives for integration on the part

<sup>10</sup>Some of these points are mentioned in Helleiner (1981a, p. 54).

of the manufacturer. For the trading company also, integration in the form of a worldwide subsidiary/branch office representative network not only facilitates information flows but also increases room for such tactics.

In addition to administrative fiat, there are two other levels of transacting: the price mechanism and contracts. J.C. McManus (1972), in attempting to describe the various forms of foreign business activities by a firm, explains that "some dimensions of interdependence, those in which transacting costs are relatively low, will be constrained by the price mechanism. For others, the members of the set may choose to constrain their actions by contractual arrangements. Some combination of these two means of constraining the actions of individual producers is the alternative to the establishment of an international firm".

In conjunction with this clarification, it is important to note that among the many areas of commodity trading, intermediation is most marked in transacting materials whose quality and quantity can be relatively easily specified by a contract. Such materials include raw cotton, grains, sugar, soybeans and their products, coal, copper, tin, rubber, wool, etc. These commodities also require little or no servicing or after-care once they are handed over to the respective buyers. In contrast to other areas (e.g., importation of technology), the brokerage cost of finding a correct price and the cost of contract enforcement are relatively minor. Within the same context, W.P. Rapp (1976) argues that the general tendency in foreign trade today is for large trading companies to deal with large producers because there is a minimum desirable marketing scale for each transaction.

## II

### Market structure and price determination

As noted in the preceding section, the marketing systems for primary commodities are of great variety: some rely on arm's-length type operations, others are traded intra-firm, while others adopt a mixture of the two. The complexity of the trade structure can be confirmed by the following illustration, at the individual product level.

Most *bauxite* is traded intra-firm—some three-quarters of all bauxite mined is refined within corporate systems<sup>11</sup> or at least by related parties. The remainder is sold under long-term contracts, with only small amounts left for the spot market. Similarly, in the case of *alumina*, only some 26-30% is traded outside integrated company systems and only 5-8% is sold in the spot market (Metal Bulletin, 1986). Therefore, only a small fraction of the total volume traded is exposed to—and thus responsive to—the fluctuations of the "freeness" of the spot market.

However, within the same group, *aluminium* ingots have both a producer price and a London Metal Exchange (LME) and a New York Commodity Exchange (COMEX) price. As a matter of fact, the quotations on the exchanges have replaced the role of the producers' price, e.g., that of ALCAN, which for a long period of time was considered as the market price of aluminium.<sup>12</sup>

*Iron ore* exhibits a high concentration on both the buyer and the seller sides, as in bauxite, but prices are determined through a wide variety of mechanisms, ranging from bilateral negotiations on long-term contracts to transfer pricing.<sup>13</sup> Even short-term contracts (usually for one

<sup>11</sup>Outside the centrally planned economies, the industry continues to be dominated by the "Big Six": the Aluminum Company of America (ALCOA), Alusuisse, Pechiney-Ugine-Kuhlmann, Alcan Aluminum Ltd., Reynolds Metals, and Kaiser Aluminum and Chemical Corporation.

<sup>12</sup>One of the factors contributing greatly to the expansion of operations on the commodity exchanges in recent years, (in the cases of aluminium, nickel, copper and petroleum, for example) has been the great short-term swings in prices which made it increasingly difficult for producers to maintain long-established systems of administered prices on world markets.

<sup>13</sup>Long-term contracts are estimated to cover 70% of the international trade of iron ore. Western European long-term contracts are believed to cover about 40% of that region's iron ore import requirements, while Japan had already completed in 1976 arrangements to import all the iron ore it will need throughout the 1980's (Radetzki, 1980).

year) are often regularly renewed in such a way that relationships are built up which may extend over decades. In the case of this mineral, trading firms or trading arms of the steel companies are known to be the principal marketing agents. It is estimated that only about one-third, or even less, of world trade in this commodity is transacted in the "free" sector of the world market, i.e., without being covered by special marketing arrangements (Radetzki, 1980).

The frequency of long-term contracts for iron ore derives from the size of the investments required to mine it and the ensuing need to guarantee that the ore will be sold for a number of years, in order to ensure the company's solvency. Contracts negotiated between buyers in the Federal Republic of Germany and the Brazilian State mining company (CVRD), those between Japanese buyers and the Brazilian CVRD, and those between Japanese buyers and Australian mines normally act as "price setters" for the international market in iron ore (UNCTAD, 1984 l).

In the case of metallic *copper*, whether refined or unrefined, exports consist mainly of arm's-length transactions, and whether long- or short-term, all copper contracts are priced at some LME-related value over which a single trader rarely exercises a decisive influence. Although there is a high degree of vertical integration in the copper industry, with a few exceptions integration in copper is confined within national boundaries and the largest part of international trade takes place between independent entities. Even though LME and COMEX handle only 5-10% of the total trade in copper, their quotations act as the peg on which a much larger volume of copper contracts are based. Though the prices for sales of unrefined copper are LME-based, the determination of toll costs (deductions to cover the cost of processing) gives the buyers ample opportunities to use their negotiating power. Efforts on the part of developing country copper producers to integrate as far as the refining stage may be explained by their desire to overcome the existing imbalance in these respects. Even though there has been an increase in direct sales from countries in which national interests have assumed control over marketing,<sup>14</sup> an important part of their sales is still handled by established agents or distributors

in the major copper consuming countries (UNCTAD, 1984 h).

With regard to *tin*, since mining and smelting operations have been mostly independently owned, the marketing is generally done among independent entities. The bulk of tin concentrates traded internationally is handled either directly by the producers or indirectly through trading companies. The bulk of trade in metal has traditionally been conducted by international traders, and their role as intermediaries is more pronounced in metal than in concentrates, mainly due to the diversified use of this metal at the consumer end (UNCTAD, 1984 j). The commodity exchanges which transact metals have played an important role in the price determination of tin. However, owing to the failure of arduous negotiations to secure a breakthrough in solving the tin crisis which has existed since October 1985, LME decided to suspend transactions of this metal. Considering the large size and great influence of LME's operations before the crisis (the Kuala Lumpur Tin Market in Malaysia was believed to represent about 20% of the international tin market, while LME had an even more direct influence), it can be concluded that this product has lost an important centre for price determination.

For *lead* and *zinc*, there is a dual price structure composed of the LME price and the producers' price. With respect to zinc, the prices published in *Metal Bulletin*, based in London, and *Metal Week*, based in New York, are taken as reference prices for contracts. For this metal, producers' prices, such as the European Producer Price, have a wide application and this is especially true for concentrates. The United States Producer Price has its validity in that country's own domestic market. In comparison with lead, zinc producers have little degree of forward linkage, so that they sell their production directly to consumers: a situation which has given rise to various producers' price systems. Due to this predominance of producers' prices, the proportion of transactions actually finalized at LME for

<sup>14</sup>The Chilean Copper Corporation (CODELCO) sells its copper directly through its selling offices in London, New York, and São Paulo and a network of agents in other markets. The direct sales effort of CODELCO is reflected in the fact that only 10-20% of Chilean copper is handled by international agents.

zinc is thought to be smaller than for lead or copper.

Among agricultural products, there are a group of commodities where market conditions *seemingly* approximate to those assumed by perfect competition: there are a large number of sellers and buyers, no one of which can, to a large extent, influence the price by their own actions. This appears to hold true for commodities sold by auction (e.g., *tea* and *tobacco*), but the price formation at the auction could be substantially influenced by the actions of a limited number of large-scale buyers. In most cases, these buyers have capital links with the world-leading processing firms of the developed market economies (UNCTAD, 1978; 1984 f). Contrary to what is generally assumed, these products face a high degree of oligopoly, and the transnational processing/manufacturing firms have achieved tight control from the stage of production to retailing in the major consuming markets. A handful of large TNCs control the world market through, *inter alia*, partial or total ownership of plantations, ownership relations with brokers, concentration of buying at auctions, ownership of processing facilities, dominant shares in major consuming markets, and increased market power through product differentiation and advertising. Also included in this category of products are *bananas*, which display probably

the highest level of integration by TNCs in production and marketing activities (FAO, 1986).

For other agricultural commodities (e.g., *coffee*, *cocoa*, *sugar*, *oilseeds* and *cotton*), operations in futures markets assume particular importance. The quotations in these markets are not only heavily influenced by prevailing supply and demand situations but also by hedging and speculative activities of the marketing and producer entities involved and especially by the selling/purchasing operations of large trading companies. All these products are highly sensitive to future expectations, thus allowing traders with "inside" knowledge to reap large speculative gains. As the raw material price looms high in the price of the final consumer product in these commodities, in order to avoid disproportionate risks in holding large stocks at hand, the major processors rely heavily on traders for the acquisition of the raw materials and for their hedging at commodity exchanges. Markets for meat, sugar, and grains, which all display high participation of large trading companies in the international markets, are composed of various fragmented national markets, where preferential channels or special arrangements, tariff and non-tariff barriers or export and production subsidies are important determinants of the direction of trade.

### III

## Marketing agents and major characteristics of primary commodity markets

### 1. Principal marketing agents

The foregoing analysis seems to suggest that for many primary commodities, the bulk of world trade is handled by entities other than transnational *industrials*. Various studies on the issue of commodity trading, emphasize instead the importance of a relatively small number of multinational, multi-product trading companies which are interposed between the producers and the consumers. These companies have extensive backward and forward linkages, but their main

line of business lies in the trading phase.<sup>15</sup> According to one study (Chalmin, 1980), the bulk of the international commodity trade is in

<sup>15</sup>Though the importance of particular agents varies from product to product, it is increasingly difficult to draw a distinction on a product basis because of the very diversified activities of the trading agents. The distinction between manufacturing, mining and trading enterprises is also becoming blurred, due to their attempts to diversify into conglomerates with a wide range of interests. Manufacturing transnationals acquire or establish trading companies, trading companies expand their range of operations into manufacturing, banking, and the entire range of other services, and retailers acquire interests in manufactures.

the hands of about 50 companies, which are classified as *traders* rather than *industrials*.

The enormous size of international traders' operations and their control over the commodity sector are reflected in the fact that in 1980, of the roughly US\$980 billion global primary commodity exports, around 70 to 80% was controlled by multi-commodity traders. This figure includes US\$230 of US\$306 billion worth of crude petroleum exports under the control of the world's petroleum giants; and around US\$500 billion of US\$674 billion worth of the remainder of primary commodities, composed of agricultural, mineral and metal products and other fuels, under the control of multi-commodity traders and the trading affiliates of industrial TNCs (Clairmonte and Cavanagh, 1982).

Among international traders, the best-known are the Japanese multi-product traders, known as "sogo-shosha". This term is usually used in connection with the top nine trading firms in Japan, which controlled in 1985 more than 44% of Japanese exports and 72% of Japanese imports. Their combined total sales (domestic, exports, imports and offshore trade) accounted in the same year for 35% of the country's GNP. In 1985, the total combined sales for only the top nine companies came to US\$440 billion. Of this figure, US\$270 billion corresponded to foreign trade (imports to and exports from Japan and offshore transactions). It can be estimated, therefore, that the total foreign transactions of the nine companies — US\$135 billion one way — accounted for approximately 7% of global trade in that year (US\$1 900 billion). If the transactions by their wholly-owned subsidiaries and affiliates abroad are added to the above figures, it can be concluded that their participation in world trade rises to almost 10%. According to the *Forbes* 1985 sales ranking, excluding U.S. companies, the Mitsui Bussan Co., one of the two largest, came second only to Royal Dutch Shell. Seven of the nine sogo-shosha appear among the ten largest companies in the same ranking. Mitsui Bussan, jointly with Mitsubishi Shoji, according to a U.S. source, transacts roughly 10% of U.S. exports (U.S., Dept. of Commerce, 1985 a).

The size and complexity of commodity trading agents can also be highlighted by taking the example of Cargill, the world's largest grain

trader, a private company with registered sales exceeding US\$25 billion in 1980, which has established a network of more than 140 subsidiaries in over 30 countries (UNCTAD, 1981a). In addition to its wide commodity operations, its insurance arm offers individual and group finance, and its expertises covers bulk commodities, all facets of agriculture, marketing and speculation, handling and transportation logistics.<sup>16</sup>

## 2. Some conceptual considerations

The foregoing observations on the strong foothold maintained by transnational trading companies in the commodity sector do not necessarily lead to the conclusion that commodity markets are of a purely competitive nature. The intermediation provided by such trading companies, even though it is categorized as arm's-length, can come close to something significantly different from the purely competitive situation. The price mechanism advocated in theory under the free market system is, in many cases, not applicable to the commodity trade, where a group of oligopsonic buyers confront a large number of suppliers, as in many agricultural commodities, or similarly, where oligopsonic buyers confront a small number of oligopolistic sellers, as in some of the minerals exported by the developing countries. In these asymmetric market conditions, prices are determined not only by the prevailing market conditions, but also by the relative bargaining power of the two negotiating parties.

This type of imbalance in negotiating capacity is applicable to those cases where a powerful trading conglomerate represents a group of producing or manufacturing companies as their procurement or selling agent, either on the buying

<sup>16</sup>A small number of grain traders, including Cargill, Continental Grain, Bunge and Born, Louis Dreyfus, Barnac and Cook Industries, etc., are responsible for an extremely high percentage of world grain trade: from 1970 to 1975 the above six companies accounted for as much as 96% of world wheat exports, 95% of maize exports, 90% of oats and 80% of the sorghum exports of the United States. The same companies also accounted for roughly 80% of Argentina's wheat exports, 90% of Australia's sorghum exports, and 90% of the wheat and maize exported from the EEC. In Canada, they were responsible for the whole of the share of exports allocated to the private sector (20%), as well as for a very substantial portion of sales of the remaining 80%, which were made through the Canadian Wheat Board (UNCTAD, 1981 b).

or selling side. Large trading companies are, in general, in a position to influence market prices by the volume of their purchases, their capital strength and their sophisticated information network. What developing countries face in the commodity markets is not only the oligopsonic market structure of the developed economies but also the oligopsonically organized buying groups. The weak bargaining power of developing countries reflects the increasing market power of the multi-commodity trading agents as well as that of the giant industrialists.<sup>17</sup>

The usual presumption adopted with regard to commodity markets is that their spontaneous functioning, in perfectly competitive conditions, is basically an efficient and neutral instrument for resource allocation rather than a means of generating a particular pattern of income distribution. In reality, however, the neoclassical approach has only limited applicability to the behaviour of commodity markets, some of its major deficiencies (among others) being: i) its frequent assumption of free entry without any uncertainty as well as of the absence of any government intervention,<sup>18</sup> and its failure to deal with the externalities and market imperfection, which are an integral part of the present functioning of these markets; ii) its difficulty in explaining why markets move from one disequilibrium to another, in a continuous series of shortages and surpluses, never establishing an automatic equilibrium position; and iii) its limited capacity to produce correct and rational

market signals as regards future prices and the allocation of resources (Maizels, 1984: Helleiner, Chap. 2, 1981 b).

A serious imperfection in commodities markets is the relative scarcity of market information. In a world of perfect competition, all participants have equal and complete access to all information, and there is no uncertainty regarding future price configurations. In reality, however, the markets for information itself are highly imperfect, if they exist at all, and are characterized by bilateral monopoly or oligopoly (Helleiner, 1981 b). Uncertainty as to the future of prices, when these are as volatile as those of primary commodities, makes buying/selling, storage, shipping and financing operations much more complex and introduces a speculative element in the decision-making process. Those with the most information are placed in the best position to gain from this market imperfection.

It is generally agreed that the search for information has the characteristic that it provides increasing returns. The fixed costs of acquiring either a fixed stock or a continuing flow of information can be spread over a varying volume of transactions. Though the marginal cost of supplying information to the first user is very high, since it includes all search costs, the marginal costs of supplying subsequent users include only the cost of communication, and in most instances this is small. It is also true that since trading activities involve striking a mean between low-and high-price centres, the number of possible trades between centres will increase exponentially for every additional information/trading centre. This means that the larger the number of existing contact points, the greater will be the potential for striking business deals among them. Maintenance of these centres is extremely important, since information (especially on goods and services which are subject to continuous disturbance) is highly perishable. Thus, in order for the information to have some value to the user, he must incur costs not only for procuring the information itself, but also for maintaining and possibly up-dating and up-grading it through a trading presence in the market.

Information can always be made available to another individual without any elimination of

<sup>17</sup>Raderzki points out that price theory, whether under conditions of perfect or monopolistic competition or of oligopoly and monopoly among sellers (buyers), has little applicability to the commodity markets, as its implicit assumption in most cases is that perfect competition prevails on the other side of the market. Price theory is of little help in determining the bilateral monopoly/oligopoly price level. The theory of industrial organization also suffers from the same deficiency in that it ordinarily only studies one side of the market, implicitly assuming perfect market conditions on the other side. With regard to bargaining theory, though it provides interesting insights into behavioural patterns in two-person zero-sum games, it loses its applicability to the commodity market in general where there is mutual dependence between decision-making entities operating on each side of the market (Raderzki, 1980).

<sup>18</sup>Regarding government intervention, it is important to mention that in recent years the developed market economy countries have become much more outspoken in their opposition to international commodity agreements, on the ground that they would interfere with the free functioning of market forces. However, many commodities produced and exported by the developed countries are already subject to government intervention and controls.

the existing user's access to it. This "public property" characteristic creates the problem of the appropriability of new information for which there is no regular market.

These peculiarities taken together suggest that, as K. Arrow has pointed out, "the demand for information is difficult to discuss in the rational terms usually employed. The value of information is frequently not known in any meaningful sense to the buyer; if, indeed he knew enough to measure the value of information, he would know the information itself" (1963, p. 947). The intrinsic value of particular information depends on how the user perceives its marginal utility, and his evaluation of the information is likely to change over time as a result of market shifts. Under these circumstances, co-ordination or internalization within an administrative apparatus such as a multinational trading company, i.e., information acquisition through its domestic/foreign subsidiaries and offices, can avoid the transaction (bargaining and enforcing) costs which might have to be incurred under arm's length negotiation.<sup>19</sup>

From this standpoint, a major problem contributing to the relative weakness of trading agents of the Third World is their limited access to the information held by the private sector in the developed economies. The little information that they receive from governmental or other sources is inadequate for efficient decision-making on marketing. Unless the relative weakness of the developing countries in their information collection/screening/assessment capacity is corrected, these countries will be likely to continue supplying their products to the world market on terms and conditions laid down by the consumers, the fairness of which these countries are unable to evaluate.

Many of the world's main primary commodity exports have their prices determined on commodity exchanges.<sup>20</sup> These exchanges are often

cited as examples of markets where pure competition is found and where prices are determined by the free play of supply and demand for a given commodity. Once again, in the actual world, prices on exchanges are affected not only by the current supply and demand balance but also by expectations of supply and demand, by repercussions from the currency markets, and even by manipulation. With regard to futures, expectation as regards the basic economic factors becomes more important and the prospects for the commodity in question are weighed together with the broader economic outlook and the expectations of the currency in which the deal is denominated. Optimal pricing for each agent depends on its own expectations about future developments, its conjectures on buying and selling interests, and all the economic forces which affect future prices. Its buying/selling practices are also constrained by its financial position and utilization of its physical facilities, such as storage and shipping. In short, in a futures transaction, there is little room for the mark-up pricing common in many manufacturing activities. Prices are always in motion, and this problem is compounded by the fact that the firm is both seller and buyer simultaneously, so that its interest in one capacity might undermine that in its other capacity.

It should also be pointed out that in so far as buying/selling contracts are on a futures rather than a spot basis, there will be a greater tendency for the trading firm to have its subsidiary, affiliate or foreign office undertake the actual buying. This is because if a contract is on a spot and cash on delivery basis, the risk of possible misrepresentation of product quality can be dealt with by testing on the spot a sample of the product. Thus, when contracts are predominantly for futures, the cost of arm's-length trading tends to rise, and external transactions tend to be replaced by vertical/horizontal integration of the trading firm.

Furthermore, price determination mechanisms at commodity exchanges suffer from several serious rigidities: for some commodities there are few main producers, as in the case of tin, cocoa and coffee; for others, most of the demand comes from a few large importers, as in the case of wheat. In other cases, a few traders may loom large in the market. They are not

<sup>19</sup>The behaviour of a large trading company can be explained by its desire to protect itself from or exploit market failure. The services that a *sogo-shosha*, provides, for example, are information-intensive, and the characteristics of information, i.e., the lack of a market mechanism to determine its value and "public property" nature, create externalities.

<sup>20</sup>These products include wheat, maize, soybeans, soybean meal and oil, palm oil, coffee, cocoa, sugar, rubber, wool, cotton, orange juice, copper, tin, lead, zinc, nickel, aluminium, silver, gold and, increasingly, petroleum.



always in evidence, as they may bid in moderate quantities at any one time or through various brokers, but if they steadily pursue a specific policy they can influence the market and thereby affect its transparency. Moreover, other restrictions and distortions are created by the exchanges themselves: for example, the rules governing admission to the various classes of membership include financial requirements such as bank guarantees and paid-up capital, as well as nationality clauses.<sup>21</sup>

Imperfections in commodity markets also arise due to the large investment capital necessary to establish or expand processing capacities. The areas of processing and marketing are intricately interwoven, since often the possibilities for processing before export depend on the ability to secure, beforehand, market outlets for the processed product. Prior assurance of market possibilities is often necessary in order to raise the investment funds needed, especially for minerals and metals, where large sums are involved and the existence of long-term purchase commitments or other types of arrangements for at least a sizeable portion of the output is regarded as a partial guarantee for the potential investor. A high frequency of long-term contracts in the commodity sector, in this sense, signifies that the market is no longer competitive and free through the continuous auctioning process between buyers and sellers. The nature of the long-term contract, in turn, reflects the relative strength of both parties.

The type of price determination postulated by the neoclassical approach does not apply to the transport sector either. It is found that in the case of many commodities freight rates are as much as 20% of the CIF prices and that fluctuations and changes in freight rates have a significant impact on price, on the market demand for these products and on the net earnings of producers. However, the observed structure of freight rates, in general, does not seem to reflect the true cost of carriage, and the rates are instead determined in an arbitrary manner. The general practice in the industry is to charge "what the traffic will bear" and the most often used mea-

sure is the unit value per ton of the commodity, which has little relation to the marginal cost-based system of charges.<sup>22</sup> As a result, with high-value commodities subsidizing low-value ones, excess freight factors escalate in a similar manner to tariffs. The arbitrariness in the setting of freight rates is related, in many cases, to the different bargaining positions of the exporters and shipping companies.

In sum, contrary to the postulates of conventional theories and the solutions that they imply, commodity markets operate in far-from-equilibrium states where spontaneous self-correcting impulses fail to assert themselves.

### *3. Characteristics of transnational trading companies*

The rationale for the existence of transnational multi-product trading companies and the reason for their expansion are to be found in the very roles and functions which they play:<sup>23</sup> for example, the minimization or reduction of the risks inherent in both domestic and international trade which arise from fluctuations in commodity demand and supply as well as in exchange rates. Since it is difficult and costly to insure against these factors, the trading companies reduce risks by distributing them over many transactions. The larger the number of commodities handled, and the more diversified sales are by geographical region and types of buyers, the more widely the risks involved can be distributed. The feature of multi-commodity trading is thus explained by their desire to take advantage of the risk-reducing effect arising from scale and diversification. A wide portfolio, not restricted only to commodities but compensated by large product lines in manufactures and services and also by extensive geographical markets, reduces income fluctuations by compensating for large variations in individual product income.

The risk involved in the fluctuation of exchange rates is reduced when the net transfer of cash through clearing arrangements, as in the settlement of intra-regional or interbank accounts, is only a fraction of total transactions.

<sup>21</sup>For a summary discussion on the problems relating to the operation of commodity exchanges in the context of higher participation in them by developing countries, see UNCTAD (1983a).

<sup>22</sup>These points are raised in Yeats (1981).

<sup>23</sup>For a summary of these issues, see Yamamura (1976), Young (1978), and Roehl (1983).

It should also be borne in mind that a trading company engaged in both importing and exporting is able to buy and sell in local currencies, thereby reducing transactions across currencies to a small fraction of the total import and export business.

These companies' attribute of wide product and geographical market diversification increases the possibility of creating third-country trade or counter-trade. Unlike a single-commodity trader, the multi-commodity trading company can act, for example, as an importer of manufactured goods in exchange for exports of primary commodities or *vice versa*. When a company caters for a large clientele on both the exporting and importing sides, this can allow it to find a market for a product for which the producer has no direct marketing and distribution relationships. Similarly, in the present conditions of shortage of credit, there has been a substantial increase in the need for arrangements whereby buyers oblige sellers to provide export/markets equivalent to the hard-currency value of the goods imported.<sup>24</sup>

Another feature of transnational traders is the size of their financial operations and thereby the derived credit-worthiness, which in turn rests on their ability to reduce the risks involved in transactions and to take advantage of economies of scale in using the capital made available to them. In this manner, the trading companies can often function as providers or guarantors of credit, or can engage in trading with a variety of credit instruments rather than cash settlements. In the case of the nine largest *sogo-shosha*, credit extended by them in 1982 to their clients reached US\$58.1 billion, while they themselves received over US\$44.1 billion of loans from various banking institutions (*Sogo-shosha Nenkan*, 1984).

Another important function is their ability to reduce "transaction costs". As mentioned earlier, this term refers to the costs involved in gathering/processing/screening information about market opportunities and economic intelligence, contract negotiations and enforce-

ment, and obtaining transportation services. Regarding information, for instance, the "production" of information about market opportunities —prices and locations of sellers and buyers, their credit-worthiness, etc.— includes the costs of gathering and disseminating the information. It should be noted, however, that these costs are *fixed*, independent of the use to which the information in question is put. This points to the existence of economies of scale in information-gathering activities and also to the decline in search costs per unit of information in accordance with the expansion of the market size.

In the area of transportation, although trading companies, may not necessarily provide their own transportation, they can reduce the cost per unit of goods transported by co-ordinating shipping times and locations and cargo space. Transportation costs are also reduced through the facilities provided and arrangements made at ports of origin and destination. Such facilities and arrangements are known to have large fixed costs but only small marginal costs. After the investment in fixed costs, exporters would obtain flexibility in organizing and timing shipments, thus improving their stock-keeping and marketing operations.

Since it is known that the Japanese and the Europeans rely heavily on this type of traders and that the United States is moving gradually towards the expansion of its trading sector by adopting more dynamic and diversified trading mechanisms along these lines,<sup>25</sup> either creating similar organizations or strengthening the existing trading entities in the Latin American and the Caribbean region might be a way to prevent further intensification of the control of commodity markets by TNCs. In the context of developing economies, this type of trading organization can be an effective means of combating the inadequacies of the commodity markets, particularly in the following aspects: i) strengthening of trade leverage against TNCs; ii) strengthening of more independent commer-

<sup>24</sup>According to the National Foreign Trade Council of the United States, the number of countries requiring some form of counter-trade has increased from 28 in 1979 to 88 in 1984. The same organization reports that 8% of U.S. exports are currently subject to counter-trade -47% in the case of the aerospace industry.

<sup>25</sup>The passing of the Export Trading Company Act by the U.S. Congress on 8 October 1982 has signified a new trend towards introducing a Japanese-style trading company culture and especially towards taking advantage of the potential that the newly created companies offer for counter-trade.

cial information systems; iii) pooling of import requirements and export sales, which should strengthen the negotiating position; iv) taking advantage of economies of scale, particularly in such areas as shipping, bulk handling and stor-

age; v) co-ordination of actions aimed at overcoming restrictive and protective measures taken by the industrialized countries; and vi) amplification of compensatory trade at the regional and subregional level.

## IV

### Experiences of commodity marketing institutions in a Latin American context

#### 1. *Producers' associations*

The Third World countries' inability to control various stages of the marketing chain and their subordinate position resulting therefrom are linked with the power of the TNCs, which have firm control over finance, production, markets, transport, technology, information, etc. The development of an effective countervailing force against such a concentration of power will, to a large extent, depend on the actions which the developing countries can take at their government level. Admittedly, however, the resources required and the degree of co-ordinated action necessary to countervail these centres of economic power would be difficult to find in a small, competing, national private enterprise unit. In recognition of this fact, it has been realized that only through co-ordinated joint actions can the Third World as a whole, or the region, achieve greater participation and gradually changes, for their own benefit, in the rules governing the operations of these markets.

Realization of the above has led, in the past two decades, to the creation of numerous producers' exporters' associations, either at the regional or international level. In agricultural commodities alone, during the last two decades one can identify more than 15 producers' exporters' associations of international significance (FAO, 1984). Nevertheless, as shown below, an examination of the performance of international and regional producers' associations reveals that in general they have failed in their major undertaking, either for lack of appropriate support from the countries which created them, or because

some important producers refrained from becoming members. Furthermore divergent policies and sometimes conflicting strategies pursued by individual producing countries have had detrimental effects on the international commodity markets.

In the case of CIPEC (Consejo Intergubernamental de Países Exportadores de Cobre), collective efforts have stopped short of original expectations. The eight member countries, which together account for approximately 40% of world production, have tended to seek short-term economic benefits rather than to foster the achievement of more stable real income in longer-term perspective. In the mid-1970s, for instance, when talks on a possible copper agreement were taking place as part of the Conference on International Economic Co-operation and within the Intergovernmental Group of Experts convened by UNCTAD, the Government of Chile decided unilaterally not to adhere to a 15% production reduction previously agreed upon by the Special Conference of Ministers of CIPEC. Instead, the Chilean Government implemented a programme of production expansion (Martner, 1979, pp. 89-95). This action on the part of Chile not only reduced the price of copper internationally but also "acted as an internal brake on CIPEC activity, reducing the organization to the level of a passive spectator of events on the world markets and impeding UNCTAD talks aimed at establishing a system of price stabilization" (Martner, 1979, p. 95).

In view of its ambitious investment plans to expand production, taking advantage of its very low production costs, the Chilean strategy seems

to be to expand its capacity, in spite of the world glut. One of the main objectives of CIPEC, i.e., to promote the harmonization of decisions and policies of member countries relating to copper production and marketing, has consequently met with little success.

In the case of tin, the decision by Brazil—which has rapidly increasing production and an even higher potential for the future (in 1985 it became the second largest producer of this metal after Malaysia)—not to join the recently established Association of Tin Producing Countries (ATPC) has undermined that organization's aim to stabilize the market. Brazil, which is not a member of the International Tin Council (ITC) either, has been increasing its share of the world market at an astonishing pace, at the expense of others who have been trying to institute some orderly marketing mechanisms. Non-ATPC members increased their output when the ATPC countries reduced their tin supply to the world market from 194 000 tons in 1981 to 125 000 tons in 1983. These "cut-throat" moves not only stifle the initiatives of the members of commodity associations but also give the developed consumer countries the impression that there is no co-ordination among developing producing countries.<sup>26</sup>

Though the International Tin Council is not a producers' association, the crisis facing it implies a failure of the collective efforts to seek a reduction in production. For a long period, the Council tried to absorb the excessive world supply, especially through artificially high support prices, and the apparent supply-demand equilibrium was only achieved through the Council's constantly growing reserves. A detrimental factor leading to this result was undoubtedly the rapid increase in the production coming from some non-ITC members such as Brazil and China.

Another mineral producers' association of international character is the International Bauxite Association (IBA), which was created in 1974 and whose members are Australia, Domin-

ican Republic, Ghana, Guinea, Guyana, India, Indonesia, Jamaica, Sierra Leone, Suriname and Yugoslavia. The principal objectives of the Association are: i) to promote the orderly and rational development of the bauxite/alumina/aluminium industry in its member countries; ii) to secure for its members fair and reasonable returns from the mining, processing and marketing of bauxite and its products; and iii) to safeguard the interests of member countries in relation to the industry, which faces a high domination of TNCs.<sup>27</sup>

In spite of their potential bargaining power, the IBA's major policy instrument is the application of minimum prices for basic-grade bauxite: a system which gives the members a fair amount of latitude, with no binding commitment except that of selling their bauxite above the minimum recommended price. However, these recommended prices have not always been observed either by the TNCs or by the bauxite-producing countries. According to a specialized publication, "transnationals have regarded the IBA as a paper tiger, because of its inability to agree on fundamental issues such as pricing policy" (Latin American Commodities Report, 1982).

More exclusively at the regional level, there are several cases of producers' associations whose functioning is severely undermined by the lack of solidarity, co-ordination and political will to safeguard the long-term interests of the respective industry.

The Unión de Países Exportadores de Banano (UPEB) is a good case in point. The potential bargaining power of this group, which was created in 1974 and consists of eight members (Colombia, Costa Rica, Dominican Republic, Guatemala, Honduras, Nicaragua, Panama, and Venezuela), accounting for 17% of world production and 50% of world exports, has been stifled by Ecuador's decision, from the outset, to remain outside this regional arrangement. Ecuador is responsible for 15-20% of the world exports of this fruit.

<sup>26</sup>Recently Brazil has decided to co-operate with the ATPC and restrict tin exports to 21 000 tons from March 1987 to February 1988. This should be a crucial element in helping to achieve the ATPC's export target of no more than 105 000 tons in a bid to buoy up world prices and reduce international stocks.

<sup>27</sup>The potential importance of the IBA is reflected by the aggregated position of its 11 members in terms of total possible world bauxite reserves (72%); world bauxite and alumina production (75% and 45%, respectively); and world bauxite exports (90%).

Strictly on the issue of marketing, the Seventh Meeting of Ministers of the UPEB, held in 1976, decided to establish a commercial arm of UPEB in the form of a multinational corporation responsible for the marketing and transport of members' fruit and other related products, in order to counteract the control of TNCs in these areas.<sup>28</sup> The objective was materialized in 1977, when representatives from Colombia, Costa Rica, Honduras and Panama created the *Compañía Comercializadora Multinacional del Banano* (COMUNBANA, S.A.). This enterprise was and still is perceived as the executive instrument of UPEB marketing policies, and it is open to all members of UPEB.

It should be stressed that COMUNBANA faced an impossible task in seeking to fulfil its objectives when UPEB members refused to commit their shipments to it. At the peak of its operation, it was only able to handle one shipment of bananas a month (mainly due to shortage of fruit), whereas it was thought that buyers in the traditional import markets required weekly arrivals of bananas. From the initial 1978 contract with Yugoslavia up to the end of 1981, it marketed a quantity equivalent to 0.5% at the most of total annual world trade in bananas. The dismal performance of COMUNBANA was clearly due to the uncommitted stance of its member countries, and while it still exists on paper it has stopped its operations.

Lack of support from the countries which created a regional co-operation organization is also to be observed in the case of the *Empresa Multinacional Latinoamericana de Comercialización de Fertilizantes, S.A.* (MULTIFERT). The Panama-based company was formed in 1980 as a commercial venture, under the auspices of the Latin American Economic System (SELA), with the main objective of marketing fertilizers in order to ensure supplies of these products to and from the region and to facilitate their sale in

third markets, through the bigger bargaining power secured by the consolidation of supply and demand.

Though the performance of this organization has not been insignificant—it had total transactions of US\$129 million for the period up to February 1984—it has been far below the original expectations of the establishing nations. The transaction figures envisaged for 1980, 1982 and 1985, for instance, were US\$155 million, US\$400 million and US\$545 million respectively, which would have meant that MULTIFERT would market in those years 30%, 60% and 70% of the total purchases of the 11 members of the SELA Action Committee (ECLAC, 1984 a). The explanation for this marked difference between the forecasts and reality must be sought not only in the over-ambitious aspirations but also the lack of political commitment of the member countries which created it. Among the 11 members of the Committee, only eight subscribed to the agreement establishing MULTIFERT. Furthermore, the low import demand was related to the inconsistency of those stockholders (mainly State companies) which decided not to channel their operations through MULTIFERT. The situation became still more complex when the Government of Peru, a member country which had been the promotor of this organization, liberalized the importation of fertilizers and the *Empresa Nacional de Comercialización de Insumos* (ENCI) of that country lost its major attributes as the State monopoly. Venezuela also eliminated the State monopoly of VENFERCA. Thus, as may be seen, added to the inefficiency of MULTIFERT itself was a functional instability which worked against the sustained performance of this multinational organization.

With regard to regional co-operation in the marketing of primary commodities, the experience of the Bogotá Group (later Pancafe S.A.)<sup>29</sup> is illustrative in that it demonstrated the magnitude of the influence that can be exerted by

<sup>28</sup>The most prominent TNCs in the industry are United Brands, Castle and Cooke (a subsidiary of Standard Fruit) and Del Monte (R.J. Reynolds). These three firms control almost 100% of the banana exports from Costa Rica, Guatemala, Honduras and Panama, and a significant percentage of those of Colombia (60%) and of Ecuador (40%). On the other hand, it is estimated that 35% of the fruit produced in Central America, Colombia and Ecuador is marketed by national entities of the producer countries.

<sup>29</sup>The objective of this group, which consisted of Brazil, Colombia, Costa Rica, El Salvador, Guatemala, Honduras, Mexico and Venezuela, was to establish, manage and operate a coffee trading company, and to that end to purchase, sell, handle and market coffee.

producers in the international market place when some concerted actions are decided upon and enforced. Despite its short life, the overall high price level of coffee registered in 1978/1979 and 1979/1980 was mostly attributable to the market intervention undertaken by this group. Conservative estimates indicate that the group was able to keep the price at least 10% above the usual level during these periods. Due to the insistence of the United States and other members of the International Coffee Agreement (ICA) that this group must be liquidated as a pre-condition of their willingness to restart negotiations for a new agreement, however, the leaders of the Latin American countries decided to opt for the utilization of the economic clauses within the ICA as a price defence mechanism instead of the joint actions of the group. Nevertheless, the regional efforts made in this field generated a much better bargaining position for the producing countries in the negotiations towards the new agreement and led to a softened position by the United States, in particular, over the price ranges negotiated.

An examination of the past performance of several international and regional associations working in commodities indicates that they have stopped far short of their original aspirations. Even though they have made valuable contributions, especially in the area of information collection and dissemination, there has been little success in meeting the pressing need to control supply and co-ordinate marketing decisions. These associations have not succeeded in achieving price stabilization or some scheme of orderly marketing on the basis of reduction of supply by producers. The vested interests within the associations, the weak financial capacity of producers to collectively support the withholding of supplies, inability to withstand the effects of supply cutbacks on their national economies (e.g., on employment and foreign exchange earnings), and the fact that some countries have not joined the groups (e.g., Ecuador was not a member of UPEB) have greatly undermined the bargaining position of these organizations in international negotiation fora. Much of the blame for the unsatisfactory performance of the producers' associations is attributable to the lack of a real perception of common interests and collective trust among the producing countries.

## 2. State Trading Organizations (STOs)

Most countries engage in some form of State trading, and the Latin American countries are no exception. On a world-wide scale, estimates based on GATT documents and other sources indicate that, in the 1970s, the proportion of State trading in exports was 20-25% in New Zealand, 10-15% in Australia, 8-14% in the U.S., and 9-11% in Canada, while the proportion represented by State trading in imports was 18-20% in the U.K., 18-24% in France and 8-10% in Japan (Kostecki, 1978). With respect to Latin America, it is estimated that close to 40% of total regional imports are accounted for by government purchases, and the percentage is substantially higher in the areas of energy and foodstuffs (Ondarto and Correa, 1982; ALADI, 1985). Referring to the region again, an UNCTAD study has shown that in the 1970s, in seven (Argentina, Brazil, Jamaica, Mexico, Peru, Uruguay and Venezuela) of the eight countries surveyed, 10% or more of imports and/or exports were in the hands of State-owned producing or marketing firms (UNCTAD, 1978 b).

The general observation may be made, as confirmed in an ECLAC document (ECLAC, 1986 c), that the nature and structure of the STOs in the region is limited. Among the most important of the large-scale trading entities which are State-owned enterprises are the producers and distributors of petroleum and its products. These include Yacimientos Petrolíferos Fiscales (YPF, Argentina), Petrobras (Brazil), Petroperú (Peru), Petroven (Petróleos de Venezuela, S.A.) and ANCAP (Administración Nacional de Combustibles, Alcohol y Portland, Uruguay). The predominance of these enterprises reflects the relative importance of petroleum in the total import/export trade of the region. In non-fuel commodities, however, the STOs' inroads into world markets are not significant in terms of volume or of the variety of products handled. The participation of COBEC (Companhia Brasileira de Entrepósitos e Comercio), once often cited as one of the most influential STOs in the region, has been reduced to an almost insignificant level: in 1984, it was responsible for exports equivalent to 0.07% of the national total, whereas Interbras, a trading subsidiary of the State oil company Petrobras of Brazil (another

influential STO in the region) was responsible for roughly 3% of Brazil's total exports in the same year, not to mention its commodity exports (CACEX, Banco do Brasil, 1985).<sup>30</sup>

Some Latin American STOs are said to have achieved a high level of *direct* trade. However, it should be recognized that though a major objective is to dispense with the services of traders and brokers as intermediaries and to increase *direct* exports/imports with consumers/suppliers abroad, in many cases STOs' participation in their nation's foreign trade still involves that of other economic agents, mostly foreign. For example, in the case of imports of foodstuffs ENCI of Peru merely invites periodic offers in the forms of tenders from foreign traders, who actually carry out the import transaction. This is far from what can be called *direct* trade. Rather, the participation of the State trading entity just adds another intermediation stage.

One objective common to all STOs is the strengthening of market power, especially at the international level. Regarding exports, some of the major responsibilities assigned to STOs particularly those of the Third World, involve the purchasing and marketing of products which are major sources of foreign exchange earnings, diversification of export markets and product promotion for small- and medium-size enterprises. The disadvantages arising when several thousand producers of a given commodity compete among themselves on international markets may be reduced through some form of co-ordinated marketing or centralized production control for exports. With respect to imports, the aim is frequently to obtain more favourable prices and terms by centralizing purchases or to secure stable supplies of essential imports. These objectives relating to the external sector are correlated with domestic ones, among which the most important are promotion of domestic prices and distribution policy, integration of foreign trade into central planning,

raising government revenue, and health and strategic control considerations.

Rationales for STOs also include other arguments, such as that the government may be able to improve the country's bargaining power by utilizing its negotiating power arising from exports of other products or its capacity to import.<sup>31</sup> Also export policies effected at the government level are more likely to have a possibility of modifying the commercial policies of other governments. A State-run monopoly may be in a better position to effect deals with other STOs in bilateral/multilateral negotiations.<sup>32</sup> Furthermore, some form of government co-operation in trading is necessary in cases where private returns from entering new markets or initiating trade in new products are lower than the actual social return. If this is the case, governments may be more willing to consider the element of externality. This would apply to the case where there is a desire to break away from traditional trade links. Large orders aggregated at the national level under a State monopoly also lower the cost of procurement, transport and use of warehouse space and facilitate the systematization of import procedures.<sup>33</sup>

STOs of the developing regions can be considered an effective means of increasing intra-regional commodity trade, which at present stands at a very low level. In value terms, Latin America's intra-regional exports of commodities account for only 15% of its total commodity exports, while more than 65% goes to the developed market economies. In imports, intra-regional trade in commodities reaches only 30% (ECLAC 1986 b). In view of this imbalance, the Latin American countries have a high potential

<sup>30</sup>COBEC was established to compete with powerful trading firms involved in the marketing of soybeans, and it dealt in a number of agricultural commodities, including coffee. However, in 1981 COBEC exported only US\$32 million worth of coffee, against the national total exports of coffee of US\$1.5 billion. Interbras' impact was also negligible, accounting for only 2% of total exports of coffee beans. The figures are calculated from UNCTAD (1983 b).

<sup>31</sup>A good case can be made here by Brazil, which has become one of the world's leading counter-traders. The government-owned Interbras has been successful in offsetting at least half of its oil purchases, which account for roughly 50% of the country's import bill, by supplying food and manufactured products to oil producers on a counter-trade basis (Carey and McLean, 1986, p. 459).

<sup>32</sup>The increasing recognition of the importance of counter-trade on the part of developing country governments, for example, led ASTRO (Association of State Organizations of Developing Countries) to establish a reference service on counter-trade practices, and it plans to initiate programmes for teaching STO representatives negotiating tactics and contract practices in a counter-trade context.

<sup>33</sup>For more detailed treatment of these points, see Kostecki (1978) and Saulniers (1981).

—without adversely affecting the present level of extra-regional exports— for increasing their commodity trade among themselves. Taking into account the enormous government purchasing power—it may be repeated that close to 40% of total Latin American imports are government purchases one way or another—the expansion of intra-regional trade through exist-

ing or newly created STOs provides wide scope and opportunity for regional co-operation. Equally, the strengthening of marketing entities such as STOs could greatly increase trade flows towards other developing regions where the principal growth in world demand for many of the commodities produced in the region is foreseen.

## Conclusions

In general, the Latin American region—whether alone, or jointly with other regions of the Third World—has not been able to develop the alternative mechanisms or effectively pursue the objectives that it has been seeking in international negotiations with consumer countries. For example, the countries of the region have not been successful in implementing supply regulation schemes which could have had a significant impact on the level of prices. Similarly, as demonstrated above, the operation of a producers' association will be successful only when the appropriate institutional set-up and a real perception of common interests and collective trust among the producing countries exist and are effectively exploited. From this perspective, the countries of the region should seek to achieve maximum credibility as a negotiating entity by instituting regional co-operative actions as the starting point for developing their negotiating postures. Furthermore, if there were a real perception of common interests, there would not always be a need for supervision by the consuming countries in order to guarantee the fulfilment of export quotas or similar measures to support prices.

In view of the fact that a high proportion of world output and exports of many commodities is accounted for by Latin America, the existing regional producers' associations should engage more actively in marketing, either by taking their own initiatives in these areas or by becoming more effective co-ordinators of marketing policies among their member countries. This does not preclude the possibility of their becoming multinational trading companies.

Even though their impact on the national economy has been less than originally conceived,

considering that the relative bargaining position of the buyer vs. seller plays a critical role in price determination, State trading organizations can nevertheless be an appropriate instrument for the realization and exercise of market power, especially for the developing countries, in order to countervail the dominance of the marketing systems by developed country agents. Through this instrument, the importation of certain products can be tied, as a package, to exports of commodities, so as to secure stable and more remunerative prices for the latter. In the present economic environment in which the Latin American countries are immersed, there is a high probability that concentrated selling/purchasing at the government level will equip policy makers better to counter the increasing protectionist measures applied to them. State trading organizations are also considered an effective tool for increasing intra-regional trade in commodities and for enlarging and facilitating various counter-trade schemes with countries inside and outside the region.

There is increasing recognition on the part of Latin American governments that seeking solutions to many of the problems in the commodity sector in the exclusive framework of North-South co-operation does not lead to substantial results, and that the time has come to approach negotiations with consumer countries within a much broader framework, integrating commodities in the overall trade negotiations instead of leaving them isolated as they have been up to now. One of the pillars of this larger framework is that Latin America should integrate its regional purchasing power of goods and services into overall commodity negotiations. To exercise this power, it is imperative that the



countries in the region should establish mechanisms and instruments which link the capacity to import various products of the industrialized countries (e.g., manufactures, technology, capital goods, services, investments, etc.) to the need to

raise commodity export earnings. In this scenario, the strengthening of the existing trading entities (national or regional) and/or the creation of new ones of a more multi-product nature is seen as an urgent necessity.

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