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Rising Commodity Prices

by Hans Kolbe, Hamburg *

In the wake of faster economic growth and thus higher demand for commodities in the Western world, the upward trend of the prices for industrial raw materials continued during 1972, and indeed gathered speed, on world markets. The following contribution is an analysis of the development in the past year and attempts a preview for 1973.

On a dollar basis which means taking into account the Sterling devaluation and other changes of exchange rates, the price level of these commodities has according to the HWWA-index risen by no less than 12.4 p.c. between December 1971 and December 1972 as against 7.6 p.c. during the previous 12 months. There has rarely been as steeply a price increase since the Korean crisis. This time, extraordinary price rises were recorded particularly in the markets for agricultural commodities for industrial use like wool, hides and skins, and rubber. Up to the middle of the year there were also boom-like price gains in cotton, but the market fell back subsequently to the price level prevailing at the beginning of 1972. The upward movement of the export prices of steel, by more than 25 p.c., was also quite remarkable. Thereagainst, the price rises on the London Metal Exchange were, with the exception of lead, comparatively modest.

Turn-round of Stocks' Policy

The year 1972 began with an abrupt revival of demand, leading to substantially higher prices on nearly all commodity markets at the same time. The currency realignment of December, 1971, and the removal of the American import restrictions introduced four months previously, undoubtedly were vital stimuli. The frequently re-occurring discussions about the dollar and the acute monetary crisis in August were, during 1971, aggravating circumstances, thus creating uncertainty in the markets. Potential changes of parity relations for reasons of market technique meant an additional risk for the international commodity trade, and the dealers also saw dangers for the world's economic trend as a result of these up-

heavals. The realignment brought a decisive change of anticipations. Manufacturers and the trade began to judge the future economic development more optimistically. They felt justified in taking care of replenishing their stocks which had been reduced during 1970 and 1971.

Calming-down since Mid-1972

This phase during which the speculative expectation of higher prices had accentuated the demand for commodities additionally lasted until May 1972. It had become clear that, particularly in the cases of non-ferrous metals and rubber, the fairly sizeable carry-overs from the previous year coupled with increased production would safeguard ample supplies for quite a long time to come. Also for cotton the chances of a less tense supply situation had meanwhile improved. Thus, the fear of prices booming further became less of a driving force in these markets and manufacturers no longer saw the urgent necessity of enforcing the re-stocking process in a speculative manner.

The floating of the English pound, introduced at the end of June, once again brought monetary uncertainty into the markets. The increases of commodity prices quoted in Sterling, moreover, remained mostly below the rate of the de facto devaluation of the pound. Thus, on a dollar basis, the level of prices for industrial commodities declined between May and August 1972. The renewed revival of the demand for commodities in the autumn of last year made itself felt only rather reluctantly. Initially it extended merely to the wool markets where, it is true, prices reached a level similar to that during the Korean crisis. Substantial Japanese purchases of rubber resulted a little later in a strong recovery of prices in that market, and there was also a quick new rise of cotton prices. Buyers in the non-ferrous metal

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markets abandoned their reserved attitude only shortly before the turn of the year.

Textile Fibres Particularly Scarce

The wool markets saw a strong boom in 1972. By October prices had climbed to a level resembling that during the Korean crisis of 1951. The depression which had lasted for more than two years because of receding consumption of wool had thus taken a turn to the very opposite price development. Since the autumn of 1971 wool consumption has been growing remarkably once again. This trend, resulting from a further expansion of textile sales, is expected to be maintained also during 1973. Wool production will in the current season 1972/73 for the fourth time in succession again be smaller. Surplus stocks accumulated in producing countries in former years have meanwhile been drastically reduced so that offers will continue to be quantitatively narrow, and further rising wool prices must be expected.

On the cotton market the booming prices in the second half of 1971 continued until May 1972 and hardly slowed down at all. But later on, the chances of a less tense supply situation during the 1972/73 season led to a fairly sharp fall of prices. Precautionary purchases because of reports about adverse weather conditions in some important cotton growing areas brought cotton prices after October again to the higher level of the beginning of the year. But apparently only the production of higher qualities will be involved. In the over-all picture the chances of more comfortable cotton supplies have remained good. It is expected that consumption in 1972/73 will increase faster than during the past five years but, on the other hand, the forecast is also that, simultaneously, production will be substantially higher. But in spite of this a further rise of cotton prices in 1973 cannot be ruled out because of the recent announcement of the American Administration that in 1973/74 subsidies will be paid for a substantially smaller cotton growing area.

Overcome Slump on the Rubber Market

It seems that the slump which had lasted on the market for natural rubber for several years has been overcome. Sizeable purchases by Japanese manufacturers who feared a revaluation of the Yen have in any case since October 1972 caused a remarkable rise of the rubber price. This extraordinarily high increase of the demand will not remain a feature for long but, thereagainst, a further intensification of rubber requirements in the USA and Western Europe is expected in 1973 as a result of greater industrial activity. It is likely that the prospect of further price rises will encourage manufacturers all over the world to effect

precautionary purchases for re-stocking purposes. If rubber production is to be stepped up only insignificantly, as was the case already in 1972, the de-stocking in Malaysia would proceed rapidly (the large Malaysian rubber stockpile has continuously depressed prices). Surely, though, the competition of synthetic rubber will have a braking effect on price gains of natural rubber. Also, official American quarters could at any given time step-up the sales of natural rubber from their strategic stockpile.

On the copper markets pressure on prices lasted also during 1972. In London copper prices went up, but taking the de facto Sterling devaluation into consideration, copper has actually become cheaper for non-British users. According to statistics so far available, copper production exceeded consumption in the Western world substantially also in 1972. Producers and merchants' copper stocks, considered much too high already at the beginning of the year, have further grown since. A fundamental change of the market situation and an upward trend of copper prices cannot be reckoned with prior to a strong increase of the demand for copper coupled with a progressive economic expansion in the Western world.

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The improvement of the lead producers' market position which became noticeable already in the second half of 1971 continued during the first months of 1972. On the strength of a drastic setback of production they succeeded in substantially reducing their surplus stocks already before the end of 1971. Early in 1972 the producers in Western Europe even planned to introduce a fixed selling price and thus caused a boom on the London market for lead. But from the month of May on, buyers once again became more cautious. Lead prices, supported by producers purchases, nevertheless remained on their higher level. The expected increase of consumption will probably result in slightly higher lead prices during this year.

Weak Basic Condition of the Zinc and Tin Markets

Zinc prices have risen only slightly in 1972 although the supply has been anything but ample. It must be remembered, though, that contrary to lead the reduction of the zinc production had already brought substantially higher prices in the course of the second half of 1971. Higher zinc prices than the present ones were seen only during the Korean crisis. In 1972, production was once more increased considerably. But as producers' deliveries went up even more sharply, their stocks were further reduced. The lasting strong demand increase speaks for a further rise of zinc prices in 1973.

The reason for the rather weak basic market conditions for tin in 1972 was the fact that the increase of consumption fell considerably short of producers' expectations. Although the oversupply is not very big when relating it to total consumption, it is still large enough to strengthen the manufacturers attitude to buy more cautiously. The manager of the Buffer Pool acted with substantial purchases against foreseeably lower prices (on a dollar basis). Now, the stronger increase of tin consumption will lead to a rapid reduction of the stocks held by producers and by the Buffer Pool with the result that higher tin prices can be expected in 1973 even without additional support operations.

Rise of Commodity Prices

During 1973 a further rise of commodity prices can be expected. The re-occurring intensification of economic growth will bring in its wake an accelerated increase of commodity consumption. This, in turn, will freshly stimulate re-stocking by manufacturers.

Thereagainst the supply situation will be rather varied. It is to be expected that particularly in the cases of wool, hides and skins, and to a

somewhat lesser degree also timber, the volume of offers will again be quantitatively narrow. It is possible that on the cotton market shortages, especially for the upper grades, could soon show themselves; a general shortage might have to be reckoned with after the middle of the year if the American Government carries out the pre-announced drastic restriction of the cotton acreage. For the manufacturers of rubber and non-ferrous metals the supply situation appears very much more favourable at present because of there still being sizeable unsold stocks and production increasing strongly. In the event of a substantially quicker demand increase, furthered by a renewed change of stocks' policy and traders' speculative buying, there might well, on these markets, be a fairly speedy change of the supply and demand ratio in the producers' favour.

Under the above assumptions further price rises of nearly all industrial commodities in 1973 are to be expected. Altogether the price level on these markets can be forecasted to go up by approximately 6 p.c. between December 1972 and December 1973. On an annual average, the level of 1973 prices will be higher by about 9 p.c. than the 1972 average (in each case on dollar basis).

Greater Price Rises for Foodstuffs

There were boom-like price increases in 1972 also on the world markets for foodstuffs. The supply development simply did not keep in step with the strong demand increase. Especially sugar, cocoa, coffee, wheat and meat became dearer. Over all, the price level rose by 26.7 p.c. between December 1971 and December 1972 (dollar basis). On an annual average the price level was in 1972 — because of relatively low prices at the year's beginning — "only" 13.4 p.c. above the 1971 average.

Any forecast of the prices for foodstuffs over a calendar year is rendered difficult in view of the fact that in most cases a new crop season begins after the middle of the year. On the strength of first hints at future crop results, the price trend might already happen to be completely different to previous estimates made according to the supply/demand development as it appeared in the current season. Taking this limiting circumstance into account, further price rises can be expected throughout 1973 for wheat, cocoa, coffee, oil seeds and fodder grain. The prices of sugar and other foodstuffs are likely to fall back during 1973. Altogether, the level of prices on the markets for foodstuffs will probably rise still further during the next few months and then, until the end of the year, fall back to about what it is at present. But compared with the price level at the end of 1972, the average will in 1973 still be 13 p.c. higher than what it was in 1972.