4 The Role of State Trading in Mineral Commodity Markets

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The purpose of this paper is to examine the role played by state-trading organization (STOs) in the evolution of international minerals markets. Of particular interest are the implications regarding commodity market structure, market power and price formation. These implications are analysed here through a framework previously developed by the author.1 After a brief description of the framework, the paper addresses its application to state-trading activity in four minerals of major importance to industrialized as well as to developing economies: copper, tin, bauxite, and iron ore.

FRAMEWORK FOR ANALYSING PRICE FORMATION

As an initial step to discussing the framework, it is necessary to define state-trading organizations in a way useful for mineral-market analysis. According to Kostecki,2 state trading normally implies that imports and exports take place in terms of transactions which have been determined by governments. In some cases, the governments maintain export/import enterprises – state-trading organizations (STOs). In others, governments use central directives to determine the terms of contractual arrangements, even if the execution of those arrangements is left to private traders.

In mineral markets, state trading is practically the exclusive form of
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exchange activity in COMECON countries. State trading is also gaining prominence in developing countries, following an increase in the nationalization of mineral firms. Finally, forms of state trading have appeared in industrialized market economies, where it serves to assure control and to improve bargaining in the procurement of mineral raw materials.

The framework proposed to analyse the impact of state trading concentrates on the major factors which are thought to influence mineral price formation: market conditions, market structure and their implications. The components of that framework are further illustrated on p. 294, below. Market conditions refers to the determinants underlying mineral supply and demand flows. Supply is affected by economic, geologic, technologic and institutional determinants; other important considerations are investment and supply costs, and their respective fluctuations. Demand determinants include economic, technologic and quality or taste factors. In addition, the demand structure must be defined according to the level of demand: primary, intermediate or final demand.

Mineral market structure pertains to market organization and power, while organization refers to the configuration of the actors in the market. The latter are normally grouped according to their functions, such as sellers (producers, local processors, government and private intermediaries, and possibly multinational firms); and buyers (intermediaries, processors, and wholesale-retail distribution industries). Power refers to the quantities in which these actors appear. Among the factors on the supply side which determine these numbers are: economies of scale, absolute costs, control over technical knowledge, government policies and government control over the resource. Factors influencing numbers on the demand side would be similar.

Related to market structure are the implications which the structure has for the trading countries involved. These implications relate principally to the nature of the bargaining situation and the subsequent division of gains. A bargaining situation can be defined as the conditions which affect a mineral-producing country's effort to increase export earnings. These conditions are normally viewed in the context of the struggle between private firms or multinational mining companies (MMC) and host governments in mineral-exporting developing countries. Recently, these governments have successfully elevated their share of profits in mineral extraction, a trend which has notable implications for market control and price formation.