

GENERAL AGREEMENT ON TARIFFS AND TRADE

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GROUP OF GOVERNMENTAL EXPERTS ON MEASURES AFFECTING THE WORLD MARKET FOR COPPER ORES AND CONCENTRATES

Submission by the EEC

The GATT Council, at its session of 15 July 1986, decided to create a group of governmental experts with the terms of reference:

"To examine problems falling under the competence of the General Agreement relating to current trends in world trade in copper, including the supply and demand situation for copper concentrates and refined copper, and to report to the Council".

In order to do so, the Group has at its disposal document MDF/W/10 of 2nd October 1984, entitled "Problems of trade in certain natural resource products", established by the Secretariat within the framework of the Group on natural resources.

The Group disposes also of Documents L/5286 of January 29, 1982, L/5627 of March 2, 1984, C/W/439 of May 11, 1984, L/5654 of May 14, 1984, C/M/176 of April 10, 1984, C/M/178 of June 13, 1984, C/M/179 of July 2, 1984, C/M/183 of December 10, 1984, MDF/5 of January 28, 1985 and of L/5992 of May 12, 1986, which reflect the Community's concern on the evolution of procedures under articles XXII:1 and XXII:2.

In spite of this abundance of documents, the Community deems it useful to submit to the Group's scrutiny its analysis of the evolution of the world copper economy, which is of concern to all countries taking part in the Group's work, and even to others.

In the course of the last thirty years, world copper consumption increased by over 150%. As for other metals, copper prices fluctuate considerably. At current prices, it was mainly during the period 1956-1963 that the situation proved to be the most difficult. In 1980, prices were nevertheless 125% above those of 1955, but dropped by one third in the course of the last five years.

But, in constant prices, copper's worth is hardly 40% of what it was in 1955. Although this phenomenon prevails for most commodities, the drop in real value of copper is one of the most spectacular, in spite of an almost constantly expanding market. Thus, it appears that, generally, production anticipates increases in consumption.

Furthermore, when temporary drops in consumption intervene, production tends to remain at a too high level. This can be seen in Graph 2 on Page 26 of Document MDF/W/10.

In order to understand the impact of such a situation on copper mines, it is necessary to recall what the price fixing mechanism is for copper concentrates. Traditionally, contracts are based on a formula which foresees that the price to be paid for the copper content of the concentrates when delivered is equal to the London Metal Exchange quotation on that day, minus a treatment and refining margin, expressed in U.S. cents per pound of copper, reflecting the processing costs and the profit of the smelter.

Such a formula implies that, in the contract, the refiner keeps the same margin, whatever the price for copper may be on the L.M.E. This means, on the one hand, that his profits can be decreased by increases in energy costs, labour costs or taxes. But it also means that the miners alone benefit from the increase in L.M.E. quotations or support the losses in the reverse case.

It is not easy to assess the impact exerted by such a formula on refiners and on miners due to the considerable and divergent fluctuations of the exchange rates of the U.S. dollar and of the pound sterling over recent years.

Indeed, in terms of pounds sterling, L.M.E. quotations are at present almost the same as in 1980, but the pound's value decreased considerably. In dollar terms, prices decreased by some 45% but the dollar's worth went up substantially until its recent collapse.

Under such conditions, the miners of various producing countries have been affected much more by fluctuations in exchange rates than by those of copper quotations. Normally, those which suffered most were those of the United States, but also of Canada, which entirely supported the burden of the price decrease in their own currencies. This partly explains why mine closures mainly took place in North America.

In spite of these closures and of the difficulties encountered by some countries such as Zambia, world mine production increased from 7.7 million tons in 1980 to 8.3 million tons in 1984 (in copper content).

During the same period, world output of copper metal produced from ores increased from 7.7 to 8.0 million tons. This ought to reflect a slight improvement in the raw material supply availability.

However, as far as the Community is concerned, business reality does not at all confirm what is indicated by those statistics. The experience is simply that it becomes harder and harder to secure the supplies in concentrates which it requires.

In fact, each time Community undertakings want to renew a long-term contract or even buy their raw material on the "spot market", they are confronted by a bid at a higher price made by a Japanese company.

Given the traditional price formula described above, the way to increase the purchase price offered is, for Japanese refiners, to decrease the treatment and refining margin.

This margin was, a few years ago, 23 U.S. cents per pound. Gradually, Japanese undertakings reduced their margin to 17, then 14, then 11, and sometimes buy on the spot market with a 6 to 7 U.S. cents margin, which may not cover the sole cost of the energy required for the refining, let alone labour costs, write-off charges, the heavy financial burden which confronts them and profits.

The Community has thus sought to find an explanation to this phenomenon. It discovered that the internal Japanese price was systematically above world prices, the difference varying from 6 to 14 per cent over time even 17% at present. The specific NPF duty applied to refined copper was equivalent to an ad valorem rate of 5.3% in 1981 and is of 3.7% at present (c.f. document MDF/W/10, page 70, paragraph 94).

It was obviously in the interest of Japanese copper users to import. But, for an annual consumption of the order of 1.2 - 1.3 million tons, Japan imports two to three thousand tons. Why can such a situation prevail for years if no quantitative restrictions prevail?

The Community had at the time, entered into bilateral, afterwards, multi-lateral consultations on the basis of Article XXII:1 of GATT.

The first explanation given by the Japanese authorities did not resolve the Community's perplexity but increased it even more. They supplied data on selling prices based on the analysis of the balance sheets of the refiners, which were substantially lower than the domestic producer price. They also indicated that the Japanese refiners were subject to a series of costs which do not exist in the Community. The main ones were:

- a subsidy to be paid to Japanese copper mines in order to keep them alive in spite of their poor competitiveness;
- the cost of treating water pumped from the mines which are temporarily or definitively closed;
- the financing of projects aiming at developing agriculture on the sites of the closed mines;
- the expenses to cover the debts of their mining subsidiaries.

If all these explanations were accepted, Japanese refiners should suffer considerable losses, which was certainly not the case at that time. Furthermore, they would then have had no reason to propose treatment and refining margins which represent only one half of their normal costs. So, either those extra costs are compensated by subsidies or the data on selling prices drawn from the balance sheets are incorrect.

This explains why the Japanese authorities have later abandoned the argument of additional costs which made the distortion all the more obvious.

The specialized Japanese press speaks regularly of the ceiling quotas for refined copper. When the Community raised this point, the Japanese authorities pretended that this concerned solely the quotas allocated within the framework of the General System of Preference.

But, since then, the Japanese press has become much more explicit.

In its edition of 17 March 1986, the Japan Metal Journal says:

"An import limit for the imports on the tariff basis for fiscal 1986 is fixed at 6,209 tons as against 6,028 tons for fiscal 1985. However, as the limit is only nominal, the development of the imports depends virtually on a quantity presented by MITI to wire and brass mills as a standard for voluntary restrictions. The standard quantity in fiscal 1986 is set at 40,000 tons as in fiscal 1985".

The Japanese authorities invoke the fact that Japanese copper imports are far above those 40,000 tons. This is true but in practice, the rest may only be imported by the Japanese refiners themselves to the extent that their own production does not suffice in order to cover demand. It is anyway a good deal for them since they buy at world prices and resell at a definitely higher domestic price. In fact, they gain on their imports of copper metal what they lose on their imports of concentrates.

The article of 23 December 1985 of the Japan Metal Journal indeed shows that this could not be done by the copper users. It says:

"In recent years, imports of refined copper on a tariff basis have been conducted under an administrative guidance by MITI for averting them from an excess. Under an agreement between smelters and semi-fabricators, MITI fixes the standard import quantity on the tariff basis, on a voluntarily restricted quantity, presents it to the semi-fabricators and gets them to hold down the imports within the limits of the quantity. In the case of fiscal 1985, the voluntarily restricted quantity was about 40,000 tons.

However, the endusers are out of the administrative guidance by the Ministry. Therefore, if they conduct copper imports under a tariff system on a fully-fledged scale in fiscal 1986, there is a possibility that the voluntary restriction by the semi-fabricators will become meaningless. From this possibility, general attention is being focussed on whether MITI will put the endusers under its administrative guidance in fiscal 1986 and whether the ministry can do so in reality".

The answer to this question is set out in an article of the Japan Metal Journal of 7 April 1986, which says:

"In the case of fiscal 1986, in particular, general attention was keen on the matter because endusers joined directly the imports on the tariff basis. As a result, actual imports under the tariff system were 7,000 tons more than the standard quantity fixed at 40,000 tons".

It should be noted that, furthermore, since 1st June 1986, Japanese non-ferrous metals producers benefit from a reduction in their electricity rates equivalent to 1 U.S. cent per KWH on average, which is considerable.

The Community thus considers that the elements which it brings up clearly demonstrate the mechanism set in place by the Japanese refiners in collaboration with the Japanese authorities, and how it functions.

What does it entail as consequences for the world copper economy?

First, the access to the Japanese market for third country copper producers (Chile, Korea, Peru, the Philippines, Zaire, Zambia, etc.) has a strict ceiling. The sole imports which benefit from a certain flexibility are those made by the Japanese refiners themselves when demand exceeds their production capacity.

Then, this practice makes all smelters around the world uncompetitive if they have to pay their concentrates supplies at the Japanese price.

Furthermore, this practice blocks entirely the process of North-South industrial redeployment for copper, in an artificial manner. Indeed, which developing country will build a smelter if Japan offers it contracts for its concentrates with treatment and refining margins of the order of 11 to 14 U.S. cents per pound?

The production costs of its smelters would necessarily be very much above that.

Finally, through those practices, Japanese refiners deprive their competitors from the raw materials they require. The Community considers that those are abnormal trade practices led by private industrialists with the cooperation of public authorities.

Confronted with such a threat, other countries attempt to reach a similar effect by having recourse to high duties on their imports of raw and refined copper, for example, Argentina (14%), Brazil (10 to 15%), Korea (5 to 20%), the extreme case being India (100%).

The Brazilian authorities set an internal price for periods ranging from three to six months, which is approximately twice as high as that on the London Metal Exchange. Besides, in order to get an import licence, the importer must prove that he has purchased a given tonnage of domestic copper at that fixed price. For example, in 1983, he had to buy 4 tons on the Brazilian market in order to be authorized to import 1 ton.

These practices actually boomerang against those countries which utilize them in so far as experience shows that over-protected industries are generally unable to become competitive on the export market. Besides, their copper transforming and end-using industries suffer from an obvious handicap at the level of their production costs.

In Brazil, the Government had foreseen that domestic consumption of copper would increase from 250,000 tons in 1980 to 650,000 tons in 1990. What happens is exactly the reverse, since transformers and endusers have reacted very negatively to the dramatic increase of domestic copper prices. Consequently, consumption collapsed in 1981 and consumption anticipated for 1986 is still 20% under that of 1980. Over and above, the plan to build a second smelter has been shelved.

In Korea, according to the copper producers themselves, in 1981, production costs were 51 U.S. cents per pound (refining costs 24 U.S. cents plus 27 U.S. cents for financial changes).

In the same years, they purchased concentrates with a treatment and refining margin of 17 U.S. cents per pound of copper content, i.e., one third of real costs. The second third was redeemed through the tariff protection and the last third was covered by government subsidies. This situation should not have changed very much since then.

The Community has prepared the present document in order to facilitate the analysis of the economic situation and of the role played by the various operators. Once this is done, it intends to develop its views with regard to the GATT provisions which cover the practices described above.