RECENT DEVELOPMENTS

The Changing Environment of International Commerce: The Shortage Factor

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THE CHANGING ENVIRONMENT OF INTERNATIONAL COMMERCE: THE SHORTAGE FACTOR

INTRODUCTION

Among the wonders in Mr. Ripley's catalogue of the strange occurrences of nature is a peculiar "tree" which lives even now on a windswept plateau high in the Andes. Unlike most trees, which in their growing process choke out all other sizable growth within a certain radius of their trunks, this "tree" is actually formed from the side-by-side growth of two trees: one leaf-bearing, and one fir. The result is what appears to be a single tree, but one of distinctly different character depending upon the side which is viewed. While there can be no doubt as to the separate ancestry of each, the meshed root system, the parallel trunks and the entwined branches combine to create a vital identity which is more real than apparent. It is impossible to truly know one without knowing the other.

Too often, practitioners of the law fail to appreciate the close relationship which the law shares with economic forces. This is true despite the fact that these forces operate upon the same society as does the law, and despite the fact that the nature and scope of the law are to a great extent themselves a function of these economic forces. Too often it is considered enough to ascertain what the reporter has included under the appropriate headnote in the statute book, regulation pamphlet or advance sheet. Arguably, in some areas of legal practice such an attitude is equal to the task at hand due to the pedestrian nature of the subject matter.

Such is not the case in the area which has come to be known as international commercial law. Here, the dynamics of world economics play a key role in the constant evolution and episodic revolution of the law.

It is the purpose of this comment to focus upon those factors which have had significant impact upon transnational trade within the past several months,[1] and which are likely to affect further developments in the months to come. To that end, this study[2] integrates economic[3] factors with those which, in a more orthodox sense, are purely legal.

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1. This comment focuses primarily upon the time period October 1973 through late March 1974, although it frequently touches upon previous events and contemplates future developments.

2. This comment employs a topical approach. While certain topics bearing upon or influenced by economic shortages (such as inflation) are not treated directly, they have been weighed and factored into those topics which are presented.

3. Political factors are also considered where appropriate.

I. WORLD ECONOMIC SHORTAGES

Certainly the linchpin of all developments bearing upon transnational trade during the past quarter has been economic shortage. One such shortage, that of fossil fuel, and specifically crude oil, has seemingly eclipsed the others. However, there is a broad range of commodities or "real" goods for which there is currently an international seller's market. This has resulted from the uncoordinated interaction of a number of factors, only a portion of which are political in nature. This section deals with shortages in general, and focuses upon oil. It analyzes the impact of such shortages upon various countries and types of countries, both exporting and importing, the relatively undeveloped as well as the industrialized. It highlights the resultant changes in trade relations and bargaining positions; considers the various diplomatic initiatives which have been pursued in an effort to stabilize world trade; and finally, examines the most sophisticated means yet employed in the classic and ongoing attempt to read the palm of the "invisible hand" at work in the market place. In this case the forum is the world. Each finger twitch has a potentially great significance for international commercial law.

A. *The Shortage of Oil*

1. Generally

The shortage of oil in the United States and most other Western industrialized countries[4] during the period of the Arab embargo[5] and production cutback[6] must be seen in perspective. While the move was

4. Canada occupies a unique position among western industrialized nations. While it imports oil to service its eastern provinces, it is, on balance, an oil exporting country. As with all other countries, however, the price of oil rose sharply in Canada. Thus, despite its seemingly privileged position as an exporter, its industry was still seriously affected by those higher prices.

5. The embargo extended from October 16, 1973 through March 18, 1974. On the latter date, seven of the nine Arab countries which had imposed controls upon the sale of their oil lifted that portion of those controls which forbade export to the United States. The embargo was left in effect with regard to the Netherlands. The seven nations terminating the ban on March 18 were: Saudi Arabia, Kuwait, Abu Dhabi, Qatar, Bahrain, Egypt and Algeria. The two continuing the ban were Syria and Libya. Syrian oil exports are of minimal importance. However, Libya had shipped an average of 205,000 barrels per day to the United States prior to the embargo. N.Y. Times, Mar. 19, 1974, at 20, col. 3.

6. From a global point of view the far more serious component of the Arab actions was the production cutback. In November 1973 it amounted to 25% of former output, thus taking five million barrels per day off the world market. In December, the reduction was relaxed when it was concluded that most Western European countries, the United Kingdom and Japan had sufficiently altered their foreign policy with respect to Israel. At that point, most African and Asian nations were allotted increased supplies. N.Y. Times, Mar, 19, 1974, at 20, col. 4.

unprecedented, it was not entirely unforeseeable. Well prior to the embargo, the rising demand for oil and oil derivative products, coupled with the rapid depletion in traditional sources of supply, resulted in increased price-setting leverage for all[7] oil exporters. Those of the Middle East were certainly no exception. In the two and one half years immediately preceding the embargo, the Middle-East, oil-producing countries twice succeeded in efforts to renegotiate extraction royalties.[8] Twice, they imposed what, at the time, were dramatically sharp increases.[9] Thus, the cessation of the embargo and even the restoration of production to September 1973 levels[10] only removed a certain degree[11] of intrigue from the petroleum commodity situation. The shortage is real and will continue.[12] Two questions remain: what is its impact, and secondly, what is being done about it?

7. Non-Arab exporters benefitting from the rise in price include five members of the Organization of Petroleum Exporting Countries (OPEC). They are: Iran, Venezuela, Nigeria, Indonesia and Equador. N.Y. Times, Mar. 16, 1974, at 11, col. 1.

8. The Persian Gulf states first demonstrated their collective market power at Teheran in 1971 when they forced the oil companies operating in their countries to agree to more than double the royalties they would pay during the next four years. In 1972, Saudi Arabia, Abu Dhabi and Qatar signed agreements under which the government share of ownership of the extracting firms would rise from 25% to 51% by 1982. NAT'L J. REP., 1973, at 1540.

9. Under the Teheran agreement of 1971 the producer countries' per barrel receipts had increased from $.80 which had been the prevailing rate in 1970, to $1.25 in 1971 and were scheduled to increase to $1.80 by 1985. Effective increases were still greater as a result of 1972 agreements reached in Rijadh under which the producer countries began to receive a percentage of production. NAT'L J. REP., 1973, at 1213-14.

10. By far the world's greatest exporter of crude oil, Saudi Arabia, was producing at the rate of 8.3 million barrels per day in September 1973. At the time of the lifting of the embargo against the United States in March of this year it was estimated that daily production levels stood at 7.3 million barrels per day. N.Y. Times, Mar. 19, 1974, at 1, col. 3.

11. Ultimately the intrigue remains for the embargo could be reimposed either in whole or in part. Most of the Persian Gulf states are governed by absolute rulers. While these men are highly educated and concerned with long range plans which are dependent upon oil receipts, they are sufficiently secure in their positions and desires that a reimposition must not be dismissed as an impossibility.

12. The question of how long the oil shortage will last has been widely debated and is beyond the scope of this comment. Additionally, as has been demonstrated, political factors make projections regarding oil supply problematical at best. However, it should be noted that plans do exist which, if carried out, would make Saudi Arabia the world's largest producer (surpassing the United States and the Soviet Union which currently rank first and second respectively). This would quickly end supply shortfall until alternate sources of energy such as nuclear, solar and geo-thermal were expanded to assume the bulk of the tasks now performed through the use of oil. Despite the cogent arguments for continued Arab supply controls it is perhaps significant that Saudi expansion programs continued throughout the embargo and production cutback. *See*, Farnsworth, *Oil Output and Prices*, N.Y. Times, Mar. 19, 1974, at 21, cols. 3-4.

2. IMPACT

a. Net Oil Importing Countries

The impact of the shortage upon net oil importing countries has been uniformly negative. However the degree of dislocation has varied widely, usually increasing with the extent to which a given country's economy depends upon imported oil.[13] The removal of the embargo did nothing to alter this fact.

Japan provides an example.[14] Like all industrialized countries[15] it has built and planned its economy largely upon presumptions of an abundant supply of inexpensive energy and raw materials. Primary among those assumptions was that there was, and would continue to be, abundant supplies of inexpensive petroleum. The assumption went one important step further, however; it was assumed that those supplies would not only continue to exist, but that they would continue to be made available. The distinction is as critical as it is subtle. While the oil certainly exists,[16] in general[17] its owners have simply decided to restrict its flow toward the market.[18]

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13. A recently published report indicated the following representative levels of dependency upon imported oil as a percentage of total oil demand: United Kingdom, 98%; France, 95%; United States, 16%; The Netherlands and the Federal Republic of Germany, 93%. INT'L CURRENCY REV., Jan./Feb. 1974, at 36.

In another report, using perhaps more current data, the "oil saving capacity" of several key international traders was computed. This index took into account two factors: the share of non-industrial use in total energy requirements, and the share of oil in total energy requirements. The study concluded that the countries rank as follows in order of increasing oil saving capacity: Japan, Italy, Belgium, France, United Kingdom, Germany, the Netherlands, Canada and the United States. IMF SURVEY, Jan. 7, 1974, at 5.

14. The Japanese are quite aware of their vulnerability to supply cutback. They receive between 70% and 80% of their oil from the major oil companies, none of which is Japanese. In 1972, Japan depended on imports for 83.5% of its energy and close to 100% of its oil. Approximately 81% of that oil came from the Middle East. NAT'L J. REP., 1973, at 1544.

15. This is also true of those countries whose economies are in the early stages of the industrialization process.

16. See note 12 *supra*. *See also* NAT'L J. REP., 1973, at 1546.

17. It should be kept in mind that not all oil exporting countries have engaged in production or export restrictions. See note 7 *supra*.

18. Looking at the embargo from a totally apolitical perspective, at least one point becomes clear. The uses to which oil has traditionally been put are ultimately wasteful of a precious and highly versatile commodity. As the Shah of Iran noted in an English language television broadcast early this year, there is something perverse about burning oil to run an industrialized society indefinitely. He suggested the wisdom of rapid conversion to alternate energy sources so as to divert the world's remaining oil stocks to the petrochemical industry which could then convert the crude into a variety of products for which there is a current and growing world demand. Such a sentiment, if acted upon, would have a two-edged effect upon international commerce.

Thus, a rather glaring discrepancy exists between the assumption of adequate, inexpensive and dependable oil supplies and the reality of deliberately created petroleum supply shortfall. The scramble for oil at almost any price[19] early this year illustrates the difficulty of determining what constitutes "inexpensive" at any given moment. However, two observations can be made.

The first is that a 300 to 400 percent increase[20] in the price of any basic commodity so radically alters the cost of goods produced through its use, that they must find acceptance in a totally different marketplace from the one for which the industry was designed. It would be difficult to overstate the significance of these developments for industrialized society. At *any* time such a radical disruption of a key commodity price would create a vortex capable of wrecking an entire economy.[21] However, this unique *transnational* disruption comes at a time when (a) institutions designed to coordinate, moderate, integrate and strengthen world economies are foundering in confusion and discord,[22] (b) a particularly virulent "stagflation"[23] seems certain to frustrate merely national attempts at recovery, and (c) nations, rather than growing independent of oil, will become increasingly dependent upon it.[24]

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19. Prices last November were as high as $22 per barrel. By mid-March they had settled at $8 for the same quantity of the same grade. N.Y. Times, Mar. 15, 1974, at 45, col. 8.

20. The possibility of such a wide difference in cost is merely reflective of the currently wide range of prices paid for Middle-Eastern crude oil. It should also be noted that qualitative factors still exist.

21. The most serious domestic crisis of the Kennedy administration was the threatened steel price hike and the events surrounding it. Steel, like oil, is a basic commodity. A rise in its price is reflected in ensuing months in the prices of goods manufactured through its use, a phenomenon known as the "ripple effect." Thus, from the standpoint of inflation, price increases in basic commodities are of the most virulent type.

With regard to the interaction of commodity cost escalation and world currency inflation *see generally*: Wolman, *Inflation! It's Bad but Maybe Not Cataclysmic*, N.Y. Times, Mar. 10, 1974, § 3, at 1, col. 1; Mullaney, *Inflation, The No. 1 Foe*, N.Y. Times, Feb. 24, 1974, § 3, at 14, col. 1; Malabre, *America First/U.S. Inflation Now Exceeds Increase in Many Other Lands*, Wall Street J., Mar. 13, 1974, at 1, col. 6; INT'L CURRENCY REV., Nov./Dec. 1973, at 24-33. With regard to capital spending in light of this shortage/inflation interaction, *see* Golden, *Capital-Spending Plans Gain/Energy Shortage Has Been Spur*, N.Y. Times, Mar. 1, 1974, at 35, col. 1.

22. The recent history of both the International Montary Fund and the General Agreement on Tariffs and Trade has belied the existence of a genuine determination to deal effectively with such problems as world inflation, balance of payments distortions, currency realignment and unfair trade practices. This is not an institutional shortcoming, but rather the lack of sincere input on the part of the governments constituting the bodies.

23. This is the name which has been attached to a situation which combines a generalized slowdown in economic growth with declining purchasing value of currency. *See generally* N.Y. Times, Feb. 20, 1974, at 53, col. 5.

24. Although the United States now imports only 16% of its oil from the Middle East,

The second observation flows directly from the first. A kind of domino effect is at work in the international trade arena. It is a bewildering system which has never really been charted,[25] but its basic logic can be rather easily understood. The price of a vital commodity, oil, has increased, not moderately but rapidly. Old markets traded goods made with and from[26] oil at the old, radically lower price. The old market did reasonably well. It should have, for it evolved rather slowly and adjusted more or less obediently to events. Now, that old market is being asked to trade the far more expensive goods made with and from the far more expensive oil; and to an extent which may prove surprising, it will do so. However, the real question is not whether or not the market will adapt, but rather, how it ought to adapt so as to minimize dislocations. In so phrasing the question, the issue becomes one of structures, techniques and mechanisms—the tools of the international trader and the province of the international commercial lawyer.

There is another dimension to the generalized plight of the net oil importing countries. That is the jolting trauma sustained by the economies of the world's developing nations. The majority of Latin America,[27] the newly formed Caribbean Community,[28] vast stretches of Africa[29] and the Asian subcontinent[30] have all suffered recent economic reversals. Among the chief causes has been the inability to acquire inexpensive oil. While the nature of the problem is essentially the same as for the industrialized countries (untenable price and supply assumptions), the operational effect has not been merely dislocation, but tragedy.

Lastly, two European nations, the United Kingdom[31] and Italy,[32] which had been making progress toward stronger economies have seen these trends reversed due largely to oil and oil-related matters.

b. Net Oil Exporting Countries

There were two major achievements of the net oil exporting coun-

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it may depend on those areas for as much as 40% of its oil by 1980. NAT'L J. REP., 1973, at 1540.

25. *But see* notes 76-79 *infra* and accompanying text.

26. The phrase "with and from" is used advisedly since oil is used extensively both as a constituent raw material of the petrochemical industry and as the driving force of the internal combustion engine.

27. Brazil, Argentina, Chile, Surinam, Uruguay and Paraguay must all import oil. Columbia will soon become a net oil importer. N.Y. Times, Jan. 27, 1974, § 4, at 29, col. 3.

28. *Id.*, Feb. 18, 1974, at 42, col. 1.

29. *Id.*, Mar. 17, 1974, § 1, at 20, col. 6.

30. *Id.*, Feb. 26, 1974, at 52, col. 4.

31. *Id.*, Mar. 14, 1974, at 57, col. 2.

32. *Id.*, Feb. 19, 1974, at 47, col. 6.

tries during the past quarter: they succeeded in dramatically increasing their revenues,[33] and OPEC became a household word. Both are the direct result of a consciously and tenaciously pursued policy, and while both will benefit the exporters in diverse ways, they each harbor a potential danger for these countries. While these currently appear only as scattered clouds on an otherwise glorious horizon, they may prove significant in the months to come.

Initially, the exporters are faced with the deceptively difficult problem of proper resource allocation. For some,[34] internal investment will require all or most of these funds. For these, the options are straightforward and the decision-making process should proceed along classical lines. For others[35] however, the problem is far more complex. There is no reason to believe that inflation and other shocks from the international monetary cross-current will somehow bypass these countries. Thus, "economic rent maximization"[36] becomes crucial. This task becomes all the more complex in light of the reportedly ultra-conservative investment attitude of the Arab.[37]

Secondly, the heightened notoriety of OPEC would seem to restrict the range of concerted actions which the group can seriously consider in the future. Divisions in economic goals and political allegiance divide the group,[38] and internally inconsistent trends are made all the more

33. OPEC is expected to earn $100 billion this year from exports. *Id.*, Mar. 16, 1974, at 11, col. 1.

34. Algeria, Iraq, Indonesia, Egypt and Nigeria fall into this group. *See id.*, Feb. 17, 1974 § 4, at 3, col. 8.

35. These would include Saudi Arabia, Qatar, Abu Dhabi, Bahrain, Kuwait and Libya.

36. In an attempt to make informed investment decisions, certain unspecified Arabs have reportedly solicited bids from major United States consulting concerns for a pricing study. The specific information they seek is the cost to industrialized nations of acquiring alternate energy sources. Once they are in receipt of this figure they can compute a price for oil which will in effect just undercut that switchover cost. This price would presumably guarantee a steady market for their oil and thus assure a steady, if fixed, income. With this income information, financial counselors will then be able to plot a comprehensive investment plan. *See* N.Y. Times, Mar. 15, 1974, at 45, col. 6.

37. There have been clear indications from Saudi Arabia, by far the largest potential surplus earner, that it is more interested in joint venture investments at home and elsewhere in the Middle East than in the United States. In response, several United States based companies are in various stages of planning joint ventures in Saudi Arabia. They include: Kaiser Aluminum and Chemical Corp., Marconal Corp., Bechtel Corp., Dow Chemical Co., M.W. Kellogg Co., PPG Industries Inc., Houston Natural Gas Corp., Caltex Petroleum Corp., Hercules Inc., General Motors Corp., United States Steel Corp., American Oil Co., W.R. Grace and Co., Mobil Oil Corp., Transcontinental Gas Pipeline Corp., E.I. DuPont de Nemours & Co., and Kidder, Peabody Co. Inc.

Since there are no reporting requirements for foreign investments made in the United States, it is impossible to tell with certainty how much money the producing countries are investing in this country. NAT'L J. REP., 1973, 1215.

38. Net importing countries will certainly be looking for ways in which they can

visible by the new-found notoriety.[39] In the complex chemistry that is international affairs, this could well force a substantial change in the internal dynamics and external effectiveness of the Organization.

c. *Trade Relationships*

As the sections above indicate, the oil shortage per se (as distinct from any additional shortages caused by the embargo[40]) has had a marked impact upon trade relationships. However it is useful to risk blurring the distinction between the two, and to view the embargo shortage together with the shortage per se. For while distinct, their influences upon world trade relationships interacted for a period of five months. A certain phenomenon emerged from that interaction and has become discernible. It involves oil and is apparently limited to it at this time. However it is potentially applicable (at least in theory) to several other commodities. This phenomenon has come to be known as resource diplomacy.

The underlying principle is simple and the motivation apparent. Following OPEC's example, countries producing key primary products band together, fix steep prices and keep supply at a level just below world demand. Thus, the theory goes, profits are maximized, national wealth redistributed from the relatively rich to the relatively poor and, in the process, a way is conveniently found for the primary goods producer to meet his recently increased oil bill. However, this theoretical scenario is oversimplified. Several specific conditions must be satisfied before the required united action can take place and before such action can bring about results. If such were not the case, the OPEC phenomenon would be far more familiar than it currently is. First, such cartels must take advantage of demand that is relatively insensitive to price hikes. Secondly, substitute products cannot be readily available at better prices. Thirdly, large financial reserves and relative indepen-

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subtly exploit these natural differences. Even within the strictly Arab portion of OPEC there are sharp divisions. As one observer wrote recently,

> When Israel is not at issue, Saudis are contemptuous of everyone else, Syrians are outcasts, Iraqis are at odds with all their neighbors, and, in general, there is a wide variety of different opinions on any subject. Nor is there much love lost between Arab capitals when money is at stake, and that means oil.

It must be noted that Iraq is not a member of OPEC, but the fact of a multifaceted rather than a monolithic OPEC structure becomes clear. N.Y. Times, Sept. 23, 1973, § 6 (Magazine), at 98, col. 4.

39. For example, the public disagreement displayed between Venezuelan Oil Minister, Valentin Hernandez and his Saudi counterpart, Sheikh Ahmed Zaki al-Yamani on March 16 over the question of a price reduction. *Id.*, Mar. 17, 1974, at 13, col. 1.

40. It is not at all certain what fraction of the gasoline shortage in the United States during the period of the embargo was, in fact, due to the embargo.

dence from short-run fortunes of the commodity in question are almost essential since they enable the producer to survive the foreseeable periods of limited output. Though less critical, two other factors are of considerable importance. Since such a scheme is essentially international collusion, the fewer the producers and the fewer the rivalries among them, the greater will be the chances for success. Lastly, a powerful leader can be of decisive importance.[41]

In addition to OPEC, several other commodity cartels have been formed recently. The leading non-North American copper producers have formed CIPEC.[42] While it is not at all clear which is cause and which is effect, the price of copper for nearby delivery nearly doubled during the last six months of last year.[43] In a similar move, seven nations producing a majority of the world's bauxite[44] have formed the International Association of the Producers of Bauxite.[45] Meanwhile, the coffee cartel is so well established that its members allowed the once-protective International Coffee Agreement to expire early last year.[46] Possibilities for further producer initiatives exist in tin, natural rubber, timber, tea, cocoa and pepper.[47]

The outlook for producer cartels is not, however, as bearish as it might appear to be. While commodity prices are currently at record or near record highs, the cause of this (with the exception of oil) is *not* cartel pressure. Rather it is extraordinary world-wide economic expansion. Secondly, to a certain extent these prices reflect a flight from depreciable currencies into real goods.[48] These factors do not directly bear upon the ability of producers to create effective cartels and impose sustained high prices. In and of themselves they certainly fail to make out a compelling case for a truly effective cartel. The political difficulties inherent in such an attempt, as well as the diffuse nature of most primary goods, combine to weigh the odds heavily against success. For example, after careful consideration the bauxite group decided not to impose an embargo. Their rationale was simple: it was clear that consumers would have shifted to alternate sources of supply.[49]

41. *See generally* Bergsten, *The World May Have to Live with Shortages*, N.Y. Times, Jan. 27, 1974, § 4, at 3, col. 3.

42. CIPEC stands for Conseil Intergouvernmental des Pays Exportateurs de Cuivre. Its members are: Chile, Peru, Zaire and Zambia. *Id.*

43. *Id.*

44. Bauxite is the ore from which alumina is extracted. It is alumina which is then processed into aluminum.

45. They are: Guinea, Australia, Guyana, Jamaica, Sierre Leona, Surinam and Yugoslavia. N.Y. Times, Mar. 7, 1974, at 55, col. 12.

46. *Id.*, Feb. 2, 1974, at 37, col. 1.

47. See note 41 *supra*.

48. See notes 115-17 *infra* and accompanying text.

49. See note 45 *supra*.

While the next few months may well see the formation of producers' organizations in a number of commodity areas, there will not be a proliferation of OPEC's; that is, there will be no mass movement toward true price-setting cartels. What appears far more likely are wide fluctuations in the real[50] price of primary goods as supply and demand conditions change. On balance, inflation, as well as genuine shortage and buyer confusion will combine to keep those fluctuations decidedly on the upward course they are now traveling.[51]

Thus, while resource diplomacy is currently exerting only a fraction of its potential influence upon the market, two facts must be kept in mind with regard to it. The first is that there is currently no international body effectively working to moderate the substantial dislocations in trade relationships which existing resource diplomacy has caused. The second fact to be kept in mind is that by 1985 the United States will have to import approximately one-half of all its essential raw materials.[52] That is to say that it will be absolutely dependent upon them, and in a very real sense, upon the suppliers of them.[53]

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50. A real price is one which discounts inflation absolutely and thus concentrates solely upon constant value relative to other goods.

51. Josefik, *Sudden Sell-Off/But Inflation Still a Factor,* Wall Street J., Mar. 8, 1974, at 1, col. 6 [hereinafter cited as Josefik].

52. Reston, *Two Tanks in Every Tent,* N.Y. Times, Feb. 3, 1974, at 15, col. 1.

53. One of the most noteworthy of all occurrences during the last quarter involves the suspension of all non-disbursed Export-Import Bank credits for proposed deals involving the Soviet Union, Poland, Rumania and Yugoslavia. While the technicalities of the dispute are themselves interesting, the key aspect of the suspension insofar as resource diplomacy is concerned is the subject matter of the specific deal which prompted the suspension. For over one year credits had been extended to Soviet-bloc countries under a very loose interpretation of the enabling legislation. While this was a matter of public record there had been no objections. However, when during the height of the energy frenzy credits were sought for a $49.5 million natural gas exploitation project in the Soviet Union, Senator Richard Schweiker goaded the General Accounting Office to enforce the rather explicit letter of the law. The G.A.O. ordered the suspension and an opinion from the Attorney General is currently pending. In explaining his action Senator Schweiker made reference to a potential of $6.1 billion in Export-Import Bank credits,

> I can't conceive of how any President could make the determination now that exporting $6.1 billion of American capital for energy development in the Soviet Union would be in the national interest.

The clear implication is that if the money is to be spent, it should be invested in a country where the long-range political climate offers some substantial assurance of uninterrupted supply to the United States. *Id.* Mar. 22, 1974, at 55, col. 7; *id.*, Mar. 12, 1974, at 54, col. 3.

In pertinent part the statute of the Export-Import Bank reads as follows:

> (2) The bank in the exercise of its functions shall not guarantee, insure or extend credit, or participate in any extension of credit—
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> (A) in connection with the purchase or lease of any product by a Communist country. . . , or agency or national thereof, . . .except that the prohibitions contained in this paragraph shall not apply in the case of any transaction

3. International Attempts to Deal with the Shortage of Oil

a. *Governmental*

From the foregoing sections it becomes clear that the existing structure of international trade and the organizations charged with regulating and facilitating it have failed to keep pace with the needs of the international trading community. This section focuses upon recent attempts by Western industrialized society to deal with the oil shortage and its impact upon the world economy.

Essentially two types of attempts have been made. They differ radically, both conceptually, and in operation and effect. The first, proposed and practiced by the French, is the ancient doctrine of "*sauve qui peut*" or, roughly, "every man for himself." It results in bilateralism.[54] The second, proposed by the United States, involves multilateralism[55] and interdependence. This interdependence extends not only to the economies of industrialized nations but to the broad range of international occurrences affecting them.[56]

The French position is easily understood. During the embargo many nations had engaged in what at times appeared to be a mad rush to buy oil for short and mid-range delivery, at almost any price.[57] As the mid-February, Washington energy conference was convened, such unilateral action was the rule rather than the exception. Indeed, at the conference French Foreign Minister Michel Jobert cited a published report of seven countries then attempting to conclude bilateral contracts with oil producers.[58] When he characterized the list as incomplete, no one challenged the truth of his statement.

> which the President determines would be in the national interest if he reports that determination to the Senate and the House of Representatives within thirty days after making the same.

Export-Import Bank Act of 1945 § 2(b)(3), Pub. L. No. 90-267, § 1(c), 82 Stat. 47 *as amended*, 12 U.S.C.A. § 635(b)(2), *as amended*, (Supp. 1972).

The nub of the legal controversy is whether or not the President has the statutory authority to classify trade with a designated "Communist" country as being per se in the national interest, or if he rather is required to make an individualized finding for each proposed project and present those findings to the Congress in cases where he does find trade to be in the national interest.

54. Bilateralism: so called because unilateral buyer action results in bilateral contracts.

55. Multilateralism: so called because the buyers present the sellers with a united group. The resulting contract is thus common to all the buyers, or multilateral.

56. Chief among these have been strategic considerations. Silk, *Energy Talks: Why the U.S. Position Won*, N.Y. Times, Feb. 15, 1974, at 43, col. 3 [hereinafter cited as *U.S. Position*].

57. See note 19 *supra*.

58. *U.S. Position*, *supra* note 56, at 43, col. 1.

It was not until this conference that the several aspects of the American position on multilateralism were thoroughly integrated and clearly presented to the industrialized West. At the heart of the American strategy was (and is) the proposition that in the long run the price of oil will be lower than it is now—at least in "real" terms. Secretary of State Kissinger presented a seven point proposal embodying the American multilateral position.[59] The first three points bore directly upon the realization of a lower oil price through conservation[60] and the development of alternate energy sources. The fourth point advocated a system of energy sharing[61] which, in addition to mitigating the effects of an embargo, contains the potential for helping reduce disorder in the hypersensitive international oil market.[62] The last three points were directed at institution building, with regard to both producer/consumer relations and also the vital area of oil revenue recycling.[63]

The American position was couched in the economic philosophy known as Pareto-optimality;[64] optimum economic efficiency is achieved when no one can be made better off without making someone else worse off. Secretary Kissinger suggested that the aim of all nations should be to achieve this optimality on an international scale, and that multilateralism was the proper means to that end. The American position was accepted over the vigorous objections and dissensions of the French ministers.

From a purely tactical standpoint, the United States succeeded because of two key characteristics in its approach and one very important fact of life. It established realistic goals which were widely acceptable and which genuinely served the interests of the joint community. Secondly, it subtly but decidedly linked economic and security matters.[65] Lastly, the strengthening American economic position, its sub-

59. *Id.*, at 53, col. 3.

60. Mr. Kissinger spoke in terms of a "new energy ethic". *Id.*

61. *Id.*, col. 4. There is a certain anomoly in the United States calling for a system of sharing. As of the fall of 1973 the United States government had no stockpiles of oil and no policy on stockpiles of oil. Most other major industrialized countries did. While the amount of the stockpiles varied, they averaged around the sixty day level. Traditionally, attempts at reaching sharing agreements have been thwarted by a fundamental split over whether a sharing program should apply only to imported oil or to imported oil and domestic oil both. NAT'L J. REP., 1973, at 1547.

62. Uncertainty over supply is perhaps the chief factor behind inflationary beggar-thy-neighbor runs on a commodity. To the extent that such an assured supply would limit uncertainty, it would help stabilize the market by its sheer presence.

63. The periods when the world's monetary systems have worked well were when surplus countries invested their surpluses overseas. INT'L CURRENCY REV., Jan./Feb. 1974, at 34.

64. Vilfredo Pareto (1848-1923); Italian economist. Silk, *Kissinger as Economist,* N.Y. Times, Feb. 13, 1974, at 53, col. 7.

65. *U.S. Position, supra* note 56, at 43, col. 3. The Europeans in general and the

stantial energy supplies,[66] its premiere technological capability and its unparalleled capital market,[67] all combined to form a pillar of comparative certainty toward which the other nations were attracted at a time of great confusion.[68]

The thirteen nations participating in the conference issued a joint communiqué at its conclusion.[69] In it they proposed that they monitor oil related problems through their participation in existing international organizations such as the OECD[70] and the IMF[71] when the nature of the problems were such that this method was possible. In addition, it agreed to the formation of temporary working groups on projects for which there were no other suitable bodies.[72]

Since the conclusion of the conference, the United States has continued to advocate multilateralism and the French have been actively engaged (along with an indeterminate number of other countries) in bilateral efforts to secure oil. Although neither party admits it,[73] there

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Germans in particular are very sensitive to the issue of continued United States military presence. Well aware of this, and eager to proceed on the economic front, President Nixon made a point of saying the following at a recent news conference.

> In the event that Congress gets the idea that we are going to be faced with economic confrontation and hostility from the Nine, you will find it almost impossible to get Congressional support for continued American presence at present levels on the security front.

N.Y. Times, Mar. 19, 1974, at 4, col. 4.

66. As noted above, the United States is currently the world's greatest producer of oil. See note 12 *supra*. In addition, the United States has the world's greatest coal reserve and it possesses advanced nuclear technology.

67. N.Y. Times, Feb. 18, 1974, at 39, col. 7.

68. The very *fact* of a fully synthesized and logically presented proposal was in itself a serious factor weighing in favor of its adoption.

69. Succeeding on a procedural point, France was permitted to register dissent in the document. This was acceptable to the United States since it was official policy to do everything possible not to unduly alienate the French whose co-operation is needed if the NATO and EEC documents on new structures of unity between the United States and Europe are to be completed.

70. OCED, or the Organization for Economic Cooperation and Development, is a United Nations affiliated group of 24 countries. The purpose of the group is to jointly explore matters of international economic significance. To that end it engages in research, serves as a forum for economic debate and periodically publishes studies of current international economic developments. Its members are Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States. IMF SURVEY, Jan. 7, 1974, at 1, col. 3.

71. See note 133 *infra* and accompanying text.

72. No additional information was forthcoming on what these topics might be. It is difficult to conceive of a topic over which neither the IMF nor the OECD would have subject matter jurisdiction. Thus, if these temporary working groups are convened it will most likely be for convenience purposes.

73. As for American desires for calm, see note 69 *supra*. As for the French, M. Jacques

is a very real confrontation in progress.[74] Oil is vital and that fact renders critical policies affecting the supply of oil. However, the outcome has a significance extending even beyond oil. The decision of the international community with respect to oil, and whether to act alone or in concert in attempts to secure it, will set a weighty precedent which is of the greatest importance in view of projected supply shortfalls.

b. Institutional

Governmental attempts to build an international framework for dealing with the impact of commodity shortages upon trade relationships are not completely alone. This framework, if indeed it is ever realized, will necessitate goals and institutionalized means for attaining them. The determination of precise goals will itself pose a knotty problem for an international community of such a diverse nature.[75] Assuming, however, that specific goals can be agreed upon, there remains the second hurdle of the institutionalized means for attaining them. There is nothing inherent within even the finest institution which guarantees its success. Success depends rather upon two factors: the willingness of the participants to work together to realize that success, and, equally as important, the *ability* to effectively act upon that community will.

In the realm of international trade, that ability requires a body of knowledge never before amassed: the precise mechanics of international commerce, including the impact of commodity shortage upon it. A unique international entity has been formed for the purpose of acquiring this knowledge. It is a hybrid of governmental[76] and international cooperation with what are essentially private institutions, primarily universities and institutes. Based at the Wharton School of the University of Pennsylvania, the project, known as Link, continuously coordinates economic data on the foreign trade sectors of individual countries.[77]

Kosciusko-Morizet, the Ambassador to the United States was recently quoted as saying, "I do not see this crisis. I do not see the slightest sign of hostility or confrontation." N.Y. Times, Mar. 18, 1974, at 5, col. 1.

74. On March 16, it was reported that during the preceding month American oil companies had sold, or dumped, two million tons of crude onto European markets at prices substantially below the $10.50 per barrel which the French had locked themselves into in a bilateral purchasing agreement with an Arab source. It was an obvious attempt to dissuade consumers from entering into long term arrangements with the Arabs at current price levels. *Id.*, Mar. 17, 1974, at 1, col. 8.

75. Once the decision has been made to pursue Pareto-optimality the hard question becomes the quantification of "goods." Even in good faith, countries are certain to differ sharply due to cultural predilections as well as more partisan factors.

76. The project is financed by the Social Science Research Council, the National Science Foundation and the IMF. Golden, *Linking Up the World Energy Crisis*, N.Y. Times, Jan. 27, 1974, § 3, at 1, col. 3.

77. Link utilizes what is known as econometric model building and proceeds to mar-

In contrast to the actual working of the system, which is reportedly the most sophisticated in the world, the theory behind it is clearcut. Assuming that the world economy is shaped by the interaction of a variety of factors and does not simply evolve, it is assumed that these factors must exert varying and specific impacts upon the overall system. Starting with quite simple observations, these factors are then quantified, different weights being assigned to each factor. The weights are dynamic, that is, they are subject to change in any given analysis, depending upon the other factors which the project directors[78] feel are involved in the real-world situation which the analysis is attempting to emulate. In this fashion the experience of history is brought to bear upon the convoluted calculus of contemporary trade problems.

During the past quarter, Link directors were among the first to conclude that the effect of the oil embargo would primarily be higher prices and not an economic slowdown due to inability to acquire oil. The result has been an impressive short-run record. If this reliability continues to improve,[79] it will mark a watershed not only in the development of a more orderly pattern of international commerce, but in economic history as a whole.

On a more mundane level, the system has a significance which transcends the obvious forecasting value for the international entrepreneur. Combined with the multilateral or interdependent approach to world petroleum shortage adopted in principle at the Washington energy conference, it could become a valuable tool with which to defuse future commodity crises.

B. The Shortage of Food

1. Scope

A trend has developed within the past several months which threatens to aggravate the world's perennial food shortage.[80] While it is not yet

ket projections by means of the simultaneous solution of a great number of equations. The whole complex system is held together by the simple notion that total world exports must equal total world imports. *Id.*, at 4, cols. 4-8.

78. The system is under the direction of Prof. Lawrence Klein and is supervised on a day to day basis by an economist, Keith Johnson.

79. Accuracy should continue to improve since with each computer run the system learns more about how various market factors interact. This knowledge is retained through constant updating of the master program against which all new data is evaluated.

80. There is a certain perversity in referring to a food shortage and limiting discussion to its effects upon international commerce. It is currently estimated that one and one-half billion persons are malnourished to the point of being physically underdeveloped and an additional five hundred million are believed to be starving to death. N.Y. Times, Mar. 15, 1974, at 28, col. 4.

While industrialized countries are only now beginning to feel the effects of the world clear, it may affect consumers in industrialized nations who have traditionally been insulated from such concerns.[81]

Two conceptualizations of the nature and probable impact of the trend are currently being aired. The first is typified by the official policy of the United States government. It acknowledges a "current food gap" but suggests that this could well be followed by a "food glut".[82] While sympathizing with the need for stockpiles, it concludes that the long-range situation will mirror what it sees as the experience of the last several decades—generally adequate supplies punctuated with occasional shortages.[83] The opposing view draws a sharper focus upon the current shortage, upon what it sees as a generalized private and governmental insensitivity to the problem, and upon an ominous shift in world weather patterns.[84] Its conclusion is pessimistic.

The government has relied heavily upon statistics from the Department of Agriculture which recently indicated that farmers were pressing ahead with plans for a sharp expansion in crop acreage for summer 1974 harvesting. In view of assurances of adequate fertilizer, Department economists reaffirmed their earlier predictions of record plantings in major grains.[85] However, even in view of the markedly greater acreage in use, the official projection was for "ample" food supplies,[86] not the substantial surplus which would be necessary for stockpiling.[87]

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food shortage, the economies of a large group of nations are suffering far more seriously. The agriculture of certain regions of South America, the Sahel region in Africa south of the Sahara, and the entire Asian sub-continent has been devastated by drought and drought/flood cycles. The Guyanan rice and sugar crops have been destroyed. Chad, an area which only thirty years ago exported grain, is now a virtual wasteland and the cattle of the Taureg and the Peul are dead and the people near starvation. Nigeria, Cameroun, Dahomey, Togo, Ghana and the Ivory Coast have seen their peanut, cocoa and coffee crop yields plunge drastically. In addition to this climate-caused disaster the hopes of all these countries have recently received another setback. At the very time that they required increased crop yield, the fertilizer through which such yields could possibly have been achieved became too expensive to afford. Most fertilizers used in large-scale agriculture are synthetic and petroleum based. The recent price hikes have not spared the third world.

81. One of the effects has already been felt. Food cost at the retail level is at a record high and threatens to go higher still. The other effect could be a change in the international political climate. See note 97 *infra*.

82. N.Y. Times, Feb. 8, 1974, at 39, col. 4.

83. *Id.*

84. *See generally* Alexander, *The Ominous Shift in Weather Patterns*, FORTUNE, Feb., 1974, at 90.

85. N.Y. Times, Mar. 16, 1974, at 37, col. 1.

86. *Id.*

87. The world's stockpile of food grains is extremely thin. The 178 million bushels in the United States along with several hundred million in Canada and some additional wheat in a few other industrialized countries constitute the total world supply of grain. It is probable that aggregate world holdings of grains at the end of the current crop year this summer will be equal to approximately one month's needs. *Id.*, Feb. 24, 1974, § 3, at 12, col. 8.

In rejoinder, spokesmen for those who foresee a far less secure supply situation in the months ahead take issue not with the accuracy of the government's data, but rather with its significance and interpretation. They see the corn and wheat acreage rises as largely a function of two negative factors. The first is that American cattle herds, traditionally an integral part of United States protein supply, are currently far below normal size. This has obviated the need for much of the sorghum which would normally be used as feed. A good deal of the sorghum acreage has consequently been shifted to wheat production. Thus, a substantial portion of the enlarged wheat planting is accounted for at the ultimate expense of meat protein. A second factor contributing to the projected wheat increase, it is said, is the utilization of marginal land, which cannot be seriously relied upon to produce in the amounts that government analysts predict.[88] Additionally, these critics point out that the government estimates are based upon assumptions of optimal growing conditions. This is especially true for winter wheat for which optimal conditions include the moisture it receives from melting snow-cover in the spring. Broad areas of the American wheat belt were free of snow throughout much of the 1973-74 winter,[89] due perhaps to a shift in the path of moisture-bearing winds.[90] It is not now known if the rain which was deposited during early March[91] was in sufficient amount to offset the lack of thaw moisture. It is thus impossible to determine at this time the precise scope of the projected shortage, or if there will indeed be a shortage of crisis proportion.

Regardless of which projection for the 1974 harvest proves more accurate it is undisputed that current United States grain carryover is the lowest in 27 years.[92] As a result of this, and looking to the various demands upon that supply, one trade association recently estimated that the United States would experience a grain shortfall of nearly one million bushels during the current year.[93] While this too is disputed by Agriculture Department officials,[94] it becomes clear that if the United States does have enough grain to meet all its commitments during the coming year it will be by only a slim margin. If the harvest is at all below official estimates, shortfall is virtually assured since carryover will have been taxed to its limit in meeting current demands.[96]

88. *Id.*, Mar. 15, 1974, at 43, col. 2.
89. *Id.*, Feb. 26, 1974, at 58, col. 5.
90. See note 84 *supra*.
91. Wall Street J., Mar. 12, 1974, at 32, col. 2.
92. Kneeland, *Wheat Stocks Depleted*, N.Y. Times, Feb. 26, 1974, at 20, col. 2.
93. *Id.*, at col. 3.
94. See note 85 *supra*.
95. See note 92 *supra*.
96. Demand is loosely categorized as follows: foreign sector (exports of all types),

2. SIGNIFICANCE

Insofar as international commerce is concerned, however, occurrence or non-occurrence of a food shortage in the United States during the current year is of only secondary importance to another fact. That fact is the existence of a bona fide shortfall *threat*, and the impact which that threat is exerting[97] upon the trade policies of the international community.

The question confronting the international trading community is whether the United States (or other net exporters finding themselves in a similar shortfall situation[98]) would make the political decision to interfere with the flow of grain in the international market. Certainly the power to do so exists[99] and parochial pressure to restrict exports would be enormous.[100] Further, the threat is by no means purely theoretical. There is sufficient recent precedent to make the threat of interference through export controls very real.[101]

3. RECENT DEVELOPMENTS

Currently North American agribusiness is heavily involved in selling grain to foreign markets. During the last several years these sales have become routine and foreign governments have come to rely upon a ready source of supply in either the United States or Canada.[102] Until

home market (in-country sales of all types). Not all grain retained after exports is home market, however. A large portion of each year's crop must be recommitted to the earth as seed. Additional portions are used as cattle feed.

97. The present tense is used advisedly. As is apparent from the tone of this section, the major consequences of any shortfall are prospective insofar as further price increases and consumer hardship are concerned. However, the impact of a possible shortage is currently being felt by political and trade relationships. The philosophy of Agriculture Secretary Butz is that if Americans are to trade in a free world market they must pay the going price for products, even those that are raised in great surplus at home. Undoubtedly, there are those who will disagree. *See* Kneeland, *Consumers in U.S. Face Competition For Nation's Food*, N.Y. Times, Mar. 11, 1974, at 46, col. 4.

98. Controls need not necessarily be governmental. Despite a heavy increase in Canadian wheat production last year farmers have generally refrained from delivering it to elevators for sale. *Id.*, Feb. 19, 1974, at 47, col. 7.

99. State sovereignty recognized by international law would include such action. Further, international law at least arguably recognizes a government's obligation to provide for the welfare of its citizens even to the point of abrogating trade agreements or customs. *See* RESTATEMENT (SECOND) FOREIGN RELATIONS LAW OF THE UNITED STATES § 153 (1965).

100. People the world over feel a special interest in food grown within the borders of their country. Psychologically, the line between interest and preemptive right is easily crossed.

101. On June 27, 1973 the Commerce Department imposed an embargo upon the export of cottonseed oils and soybeans. On July 5 it imposed export controls upon 41 categories of agricultural commodities. Soybeans and cottonseed oils were included among these 41, none of which could be exported from the United States without a validated license. These restrictions remained in force until September 7. NAT'L J. REP., 1973, at 1034, 1046.

102. N.Y. Times, Feb. 8, 1974, at 39, col. 4.

recently this situation was welcomed, especially by the United States.

During the late sixties and early seventies grain sales provided a substantial portion of the revenue inflow that held the United States balance of payments deficit within acceptable limits. More recently, due to the celebrated 1972 Soviet wheat deal,[103] it even made possible the first United States trade surplus in several years. However, faced with a general rise in world demand[104] and strong America-first domestic pressure,[105] the Nixon administration has made it clear that it no longer wishes to be looked to for assured supplies.[106] Simultaneously, the administration has relaxed a number of legal impediments to the importation of food[107] and quietly appropriated substantial funds for crash research and development programs so as to increase grain and protein supply.[108]

The Soviet Union, enjoying record harvests,[109] has consented to defer delivery of scheduled United States wheat shipments.[110] It has, however, deemed it prudent to commit $44 billion over five years to the agricultural development of vast tracts of currently marginal Siberian land.[111]

4. OUTLOOK

While not yet at a crisis stage, the once assured position of industrialized nations with respect to food has been seriously called into question. For the first time, it is being asked whether some entity other than the naked force of supply and demand has the responsibility for establishing a world grain stockpile,[112] and an international policy to

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103. In an interesting sidelight to the question of the shortage of food, the G.A.O. officially announced on February 12 that it could find no evidence of any wrongdoing within the Department of Agriculture with respect to the October 1972 wheat sales to the Soviet Union. *Id.*, Feb. 13, 1974, at 55, col. 2.

104. See note 81 *supra*.

105. This faction has been led in recent months by the American Baker's Association. N.Y. Times, Feb. 26, 1974, at 1, col. 6.

106. See note 82 *supra*.

107. By proclamation the President suspended limitations on the importation of wheat and milled wheat products (39 Fed. Reg. 3533 (1974)) and meat (39 Fed. Reg. 7777 (1974)). Further, he augmented the amount of cheddar cheese which could come into the country without import license by 100,000,000 pounds (39 Fed. Reg. 959 (1974)).

108. On January 29 the Department of Agriculture placed a notice in the Federal Register soliciting research proposals involving genetic work with the soybean. Funding was to be in the maximum amount of $400,000; work to be completed within five years. 39 Fed. Reg. 3700 (1974).

109. N.Y. Times, Mar. 16, 1974, at 6, col. 6.

110. *Id.*, Feb. 26, 1974, at 20, col. 6. The amount deferred was reportedly 37 million bushels.

111. N.Y. Times, Mar. 16, 1974 at 6, col. 4.

112. N.Y. Times, Feb. 24, 1974, § 3 at 12, col. 3.

regulate it. In view of the lethargy which characterizes all international initiatives, the answer to that question will evolve quite slowly. It will be influenced by factors bearing no relation to food allocation or nutritional needs, other than that both questions will exist in the international arena at the same period of time and expediency will dictate trade-offs. But an answer of sorts will evolve. Its specific nature will have a profound effect upon the manner in which international commerce in agricultural products is conducted, and consequently, upon the shape of international commercial law.

C. *Activity in Commodity Futures Markets*

1. Non-Precious Metals

Motivated by developments in the supply situations of oil, food and other real goods, investors combined to exert unprecedented pressure on world commodity markets during the last quarter. While the net result upon the current price of almost all commodities purchased for future delivery[113] was a drastic rise, analysts cautioned that sharp declines could be anticipated in at least some areas.

Led by agricultural products, commodity prices reached generally high levels in the late summer of 1973. After falling off to a slight extent by early autumn, they again excelerated, spurred largely by two factors emanating from the Middle East: the October War and the subsequent oil boycott. This trend was continued and prices were driven even higher by a truck strike in the United States early in 1974.[114]

At this juncture the market became gripped by an unprecedented psychology.[115] Rather than being used as a mechanism through which producers and manufacturers could secure future raw material supply, the market became an investment medium pitting traditional buyers against speculators. In contrast to conventional practice, many purchasers were not utilizing the market for the purpose of purchasing a specific commercial commodity. Rather, they were simply buying contracts for whatever goods had not already risen to their daily limits.[116] The result

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113. The concept of purchasing a commodity for future delivery (hence the name "future") provides certainty for industries using basic goods. It also necessitates thorough knowledge of the supply/demand situation, not merely at the present, but at the hour of delivery.

114. Josefik, *supra* note 51, at 1, col. 6.

115. While commodity markets have traditionally been considered havens for speculators against inflation, the degree to which the markets were subjected to this pressure during the last quarter was unprecedented. Rather than essentially alien forces whose impact was cushioned by the general market, these speculators seemed at times as though they had captured it.

116. Most commodity markets have placed limits upon how much value an exchange unit of any given substance may gain or lose in a single session. The rationale for this

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was a general and steep increase in prices.[117]

By the end of February, however, a variety of market factors began to exert themselves. Due to strong retail resistence to meat prices, the cost of livestock contracts began to fall. That single reversal seemed to spark a trend. Other factors combined in rapid succession to contribute to the reversal. These included: reports of an imminent cessation of the oil embargo; the decision of the Indian government to allow the sale of sterling for export; reports of renewed Peruvian anchovy fishing;[118] and information indicating that both Argentina and Australia would soon resume substantial exports of sugar and grain.[119]

However, as could be expected, this trend was itself reversed. Even as the oil embargo was in fact lifted in mid-March most futures advanced sharply on the rationale that the influx of higher-priced Arab crude would spur inflation.[120] The feeling was still apparently widespread that the holding of a contract for a real good at a fixed dollar amount was the only safe investment.

There has been sharp criticism of this investment psychology and its effects upon the commodity market. It is said that speculative investors (as distinguished from bona fide commodity traders) exert an influence upon the market which compromises the traditional function of the exchange. Currently, commodity exchanges in the United States are largely self-regulating with only limited governmental surveillance. Federal legislation which would change that situation has proceeded rapidly through the House Agriculture Committee.[121] This legislation has been expedited by the speculative pressure which the exchanges have recently experienced, and the impact which that pressure has had upon domestic and international commerce.

2. Precious Metals Generally

Nowhere was this speculative pressure upon commodities more pronounced during the last quarter than in the world's precious metals markets. Gold, silver and platinum were all bid up to record highs. Gold

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blatant interference with market factors is that, in an imperfect world, this lends a note of stability to prices which would otherwise succumb to rumor and irrational forces.

117. Soy, wheat, oats, corn, coffee, copper, cocoa and cotton were all at or near record highs. N.Y. Times, Feb. 26, 1974, at 58, col. 5.

118. *Id.*, Mar. 17, 1974, § 3, at 17, col. 1.

119. Josefik, *supra* note 51, at 1, col. 6.

120. N.Y. Times, Mar. 19, 1974, at 47, col. 5.

121. The Bill calls for a five member commission, consisting of the Secretary of Agriculture and four public representatives. They would be invested with sweeping regulatory powers. *Id.*, Feb. 28, 1974, at 54, col. 2. Elsewhere, similar sentiments were being expressed. Said one Assistant Agriculture Department Secretary in conjunction with unbridled speculation, "The days of wrist-slapping are gone." Josefik, *supra* note 51, at 16, col. 1.

more than doubled in price in the twelve-month period ending February 26 when it was traded on the London Bullion Market[122] at $184 per ounce, an increase of $60 since January 1.[123] The same day, silver enjoyed its eighteenth consecutive gaining session, fifteen of which were limit gains.[124] Because of the limitations on daily allowable price increases platinum contracts virtually ceased to be traded; there being no sellers willing to part with it.[125]

By late March the markets had experienced a "shakeout" of some of the more emotional traders and gold had settled securely[126] at the $160-$165 level, a price which was unthinkable less than one year before.[127]

3. GOLD

The behavior of the gold price reflects three factors: first, a substantial decline in supplies of new gold output and Russian sales; second, a persistently strong increase in demand for gold for uses in industry and the arts, as well as for investment, hedging and speculative purposes; and third, the growing belief that in conditions of world recession coupled with inflation and compounded by the oil shortage, the governments of key countries will be forced to employ gold for their international debt settlements at market-related prices.[128] This section addresses the first two of these factors. The third is considered in the following section.

While speculator pressure, both rational and irrational, was clearly the most remarkable factor influencing the unparalleled rise in gold prices, the *primary* cause for the rise went largely unnoticed by those not involved in the workings of the bullion market. It was, in fact, a simple case of supply outstripping demand; in effect, a gold shortage.

The free world supply of market or "private sector"[129] gold fell by as much as 140, and by no fewer than 115, tons during 1973. Most of the reduction was accounted for by a six percent South African production cutback and five and nine percent declines for Canada and the

122. London, along with Zurich, and now Winnipeg constitute the three most important bullion exchanges in the world. N.Y. Times, Feb. 26, 1974, at 49, col. 6; *id.*, Mar. 19, 1974, at 53, col. 1.

123. N.Y. Times, Feb. 27, 1974, at 1, col. 5.

124. *Id.*, at 49, col. 3.

125. *Id.*

126. It seemed secure in the sense of a stable floor, not a ceiling.

127. Unthinkable for all but Mr. James Dines who has been telling the investment world for years that the day of gold was coming. Sample declaration, "Anyone who sells gold shares is an idiot." N.Y. Times, Mar. 10, 1974, § 3, at 7, col. 1.

128. INT'L CURRENCY REV., Jan./Feb. 1974, at 39.

129. This is the gold used by artisans and industrialists and is distinct from the gold stored by governments in their central bank vaults.

United States respectively. While hard figures are impossible to secure,[130] it seems certain that the Soviet Union sold substantially fewer tons in Zurich last year than it had in 1972.[131]

At the same time demand was rising. In the United States, gold usage in industry and the arts during the last half of 1973 increased by eight percent over the same period one year earlier. Percentage increases aside, the amount used was quite high in absolute terms, approximately 240 tons. This represents an amount six times greater than the annual United States production yield. Thus, close to eighty percent of the private sector, United States demand had to be met through imports.[132]

II. WORLD MONETARY SITUATION

The two foremost developments in the world monetary forum during the last quarter have been direct effects of the commodity shortages discussed above, especially that of petroleum.

A. *Background*

In the years following World War II practically the entire non-Communist world conducted international commerce under a monetary system adopted at the Bretton Woods Conference of 1944 and rigidly presided over by the International Monetary Fund (IMF). Essentially, the system provided a means through which central banks could acquire foreign currencies required by international traders doing business in their countries. Since they and the new system would have been meaningless abstractions without it, each currency was assigned a "par" value. This gave it meaning (a) relative to the *numeraire*,[133] gold, and (b) relative to all other participating currencies.[134] Thus, through the instrumentality of the par value, international rates of exchange were set. Once set, these rates could only be changed through a formal process approved by the IMF. This system functioned relatively well for over twenty years. Success was due in large measure to the sustained purchasing power of the United States dollar, initially and traditionally the system's bulwark currency. For twenty years the dollar continued to closely approximate the purchasing power of that quantity of gold to which the system said a bearer was entitled in exchange for his dollar. However, by 1968 the dollar had suffered so badly from a series of

130. The Soviet Union does not release statistics on gold production or sales.

131. INT'L CURRENCY REV., Jan./Feb. 1974, at 39, 40.

132. *Id.*

133. The *numeraire* of a monetary system is the common unit of account in terms of which the relative value of all currencies is measured. *Annual Report of the Council of Economic Advisors*, 1974, from an excerpt reprinted in IMF SURVEY, Feb. 18, 1974, at 57.

134. This is so since each, by virtue of its par with gold, partakes of a common evaluator.

balance of payments deficits that this critical equilibrium ceased to exist. The purchasing power of the gold used to back the dollar and the whole international system had become markedly greater than the purchasing power of what the system said was an equivalent quantum of dollars.

In an attempt to put an end to speculation against the dollar and restore confidence in the established rates of exchange, a group of the West's leading trading nations agreed in March of 1968 to cease buying and selling gold on the private market. That is, they agreed to cease buying and selling gold for any amount other than the officially established price, which at that time was $35 per ounce. In so doing they created a two-tiered international gold market: gold I (official), and gold II (private). This agreement is still in force.[135] It did not, however bring about the long-range stabilization which its creators had intended. As illustrated in the sections above, the current price of private gold is approximately four times the $42.22 price of official gold.

By the early 1970's the Bretton Woods fixed-rate system had so thoroughly ceased reflecting monetary reality that a general adjustment in exchange rates was necessitated. Accordingly, in what has come to be known as the Smithsonian Agreement,[136] new par values for the dollar and other currencies were established in December, 1971. The effect was to lower the value of the dollar by 8.5 percent. However, this proved insufficient, as did the formal ten percent devaluation of February of last year. The speculative run against the dollar continued and prompted the decision by major nations to abandon the par value system and allow their currencies to find their own levels through the operation of market factors and varying degrees of central bank intervention.[137] By March 1973 this free market or float system had become the new standard. However, there was strong sentiment among many members of the IMF for the development of a somewhat firmer approach toward currency valuation. Accordingly, a special Committee on Reform of the International Monetary System, or the Committee of 20, began slow but steady progress in September 1972 toward fashioning a new structure, the nucleus of which would be a new set of exchange rates. Ideally they would be more flexible than those promulgated at Bretton Woods but less so than with the float.[138]

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135. While the agreement remains, the value of gold under the agreement has officially changed twice: once to $38 and then to $42.22.

136. So named because the conference used the buildings of the Smithsonian Institute in Washington, D.C.

137. It must be realized that all central banks do intervene in the workings of the international monetary system. They cannot help doing so as they trade for the currencies which businessmen in the home country require. The real question is to what degree do they do it and how they carry it out. See note 138 *infra*.

138. Since the spring of 1973 some countries have permitted their currencies to float

It was upon this free-floating monetary world, with gold trading limited by agreement to the official price of $42.22, and at this stage of development toward a new exchange rate structure, that the current raft of commodity shortages descended.

B. Impact

The commodity shortages have had a dual effect: they have completely postponed the structural reforms which the Committee of 20 had been studying and shifted the Committee's attention towards the formulation of interim guidelines; and, they have exerted sharp pressure upon governments to disregard their 1968 agreement to the contrary and to sell gold at private market levels, currently in excess of $160 per ounce.

1. CURRENT ACTIVITY OF THE COMMITTEE OF 20

As indicated above, in September of 1972 the Committee of 20 was charged by the IMF with exchange rate reform. The original target deadline for the presentation of a comprehensive package was the Fund's next annual meeting. But by the time this meeting was convened in September of 1973 in Nairobi, the scheme had been only partially completed. A new target date was set for the January 1974 meeting of the Committee to be held in Rome. One month after the Nairobi conference the Arab oil embargo, with its attendant production cutbacks and price increases, was imposed. By January the effects of this action had so disrupted the international monetary picture that reform in the sense of more fixed rates of currency convertibility became unrealistic. Accordingly, the finance ministers of the international trading community directed the Committee to realign its initiative. It was instructed to prepare two separate documents for presentation at its next meeting to

within a rather wide range, permitting market factors to establish the exchange rate. Central banks intervened only to maintain orderly market conditions. Some countries decided to peg their currencies to a major currency such as the dollar, allowing their rates of exchange to rise and fall as did the major currency. Seven European countries (Germany, France, Belgium, the Netherlands, Denmark, Norway and Sweden) kept their currencies relatively fixed with respect to each other while floating together with respect to other countries. But regardless of what form its floating took almost every country, to one degree or another, has intervened. It has done so by buying or selling its own or another's currency. The goal was to keep the float within bounds it thought were economically and politically acceptable. NAT'L J. REP., 1974, at 287. France removed itself from the float in late January in a move that proved to be more surprising than significant. For many years France has preached monetary self-discipline to other nations and the unannounced departure from the snake, as the joint float is known, seemed contradictory to its fixed rate philosophy. Actually, however, central bank intervention on France's part has kept the de facto devaluation of the franc to a modest 4%. *See generally* N.Y. Times, Jan. 23, 1974, at 45, cols. 6-7; *id.*, Mar. 8, 1974, at 43, col. 6.

be held in June 1974. The first was to include a collection of general principles for permanent exchange rate reform, leaving the details for a later time. Secondly, the Committee was instructed to give its top priority to those changes in international monetary rules necessary to cope with the immediate effects of the oil situation.[139]

With regard to the second of these matters, the ministers were deeply concerned lest the floating system be used by any country to gain an unfair advantage in international trade. This was, and remains, a real possibility, at least theoretically. Since the higher price of oil will cause sharply higher outflows of currency from all industrialized countries this year there will be a concomitant need to increase revenue so as to meet this expense, There are a number of means which a government could pursue in attempts to achieve this increased inflow. One of the more seductive among them involves certain central bank manipulations which bring about what has come to be known as "dirty" floating.

One certain means of increasing revenue is to increase exports and one certain means of increasing exports is to lower the price of domestically produced goods. This makes them more affordable in the eyes of foreign buyers. Sales rise and receipts follow. The valuation of the currency is the key.

Since the exchange rates, or relative values, of currencies are presently determined by market factors, and since the market can be affected by central bank operations, it is within the power of a government to raise or lower the value of its currency at any given time. By buying its currency on the open market it restricts its supply, making it harder to acquire and of greater value. Conversely, by selling its currency in great quantity, a government has the capability of driving its value down. The result is that foreign buyers will more easily acquire the amount of currency necessary to do business with exporters in the country conducting the "dirty" float. As indicated above, export revenues will rise and the country's current accounts index will come closer to balancing, despite the increased cost of imported oil.

To date there has been no indication that any country is prepared to precipitate the round of competitive devaluations which would be the inevitable consequence of a genuinely "dirty" float.[140] On the contrary, there has been evidence that countries are currently quite self-conscious about currency slides.[141] Indications are that they intend to intervene in

139. NAT'L. J. REP., 1974, at 287.

140. *See generally* N.Y. Times, Feb. 20, 1974, at 53, col. 5; IMF SURVEY, Jan. 7, 1974, at 7, col. 1.

141. Witness the French in late January intervening to maintain a relatively high value for its franc.

such a fashion as to maintain the integrity of the system, within bounds which are somewhat[142] nebulous and subject to change without notice.[143] Thus, the danger of a "dirty" float and a rush of competitive devaluations still exists and the Committee of 20 is currently at work on guidelines which will determine the outer limits of permissible central bank activity.[144]

2. THE QUESTION OF RESERVE GOLD VALUATION

The second of the two outstanding pressures which has been exerted upon the international monetary system by the effects of the oil shortage is the pressure to officially recognize the private market valuation of gold. If governments were to do so, they would automatically increase the value of their reserves by a factor of four.[145] There is a certain charm associated with this. Not only would it create vast new reserves by simple fiat, but it would also parallel the fourfold increase in the price of crude.

The United States is opposed to such action, favoring a diminished role for gold in the monetary activity of the international community.[146] Instead, the United States advocates an increased reliance upon Special Drawing Rights (SDR's), or "paper gold,"[147] to provide the increased liquidity which will be needed to finance the purchase of oil in the months to come.

The question before the international community, then, is whether the system which has been fashioned over the past thirty years will rise to the challenges occasioned by economic shortage, or if instead, it will

142. "Somewhat" is used here advisedly since past performance indicates that certain limits are significant for psychological reasons.

143. Rather than in depth consultation or even arm's length negotiation, the vogue with respect to currency moves has been a diplomatic notification to friendly governments just prior to public announcement.

144. . . . or inactivity.

145. \$42.22 x 4 = \$168.88. The current price of gold in the world's bullion markets is in the \$160 to \$165 range.

146. See note 139 *supra*. *See also* INT'L CURRENCY REV., Jan./Feb., 1974, at 43.

147. In recent months there has been considerable discussion aimed at the establishment of a new system of valuation for the SDR. The Ministers of the Committee of 20 decided at their January meeting in Rome on a solution to be applied at least for the interim period. This solution will involve setting the SDR equal in value to a "basket" of leading currencies. An SDR will have the same value, in terms of any currency, as would a basket consisting of a certain number of U.S. cents, plus a certain number of German pfennige, plus a certain number of U.K. new pence, and so on. The result will be that, as currencies float up and down against one another, the value of the SDR will remain in the center; it will appreciate in terms of weak currencies that float down, and depreciate against strong currencies that move up. By definition the SDR will remain constant in terms of the whole group of currencies composing the basket. IMF SURVEY, Feb. 4, 1974, at 40.

prove more effective to rely upon the "barbarous relic" of gold which has demonstrated undaunted tenacity as the medium of exchange *par excellence* for the past 6,000 years.

OUTLOOK

To observe that the trading world is currently experiencing a period of distinct shortage is perhaps to belabor the obvious. But to speak of "shortage" is to deal in abstraction; and as with all abstractions, shortage must be seen as a relative concept. Stripped of its emotional patina shortage really designates a condition characterized by total supply being insufficient to keep prices as low as they have traditionally been. However, the classic resolution of the problem should be the higher prices themselves. These should attract greater production initiatives, hence greater supply and ultimately lower prices. As is often said, the greatest cure for higher prices is higher prices. There is every reason to believe that this scenario will be followed in an almost instinctive reaction to the profit motive. However, this reaction is not of the knee-jerk variety. The realization of increased commodity supply requires a lead time measured not in months, but years.

Unlike a shortage in manufactured products, the shortage of primary goods is far less easily overcome. Most manufacturers have spare industrial capacity; they normally utilize less than 100 percent of their plant, and workers generally work less than full overtime. In times of increased demand this reservoir can be tapped to increase supply. However, such elasticity exists to a far lesser extent in the production process of primary goods. In the case of minerals and fossil fuels, mines and bore holes must be sunk; in the case of food, current grain supplies must be diverted from consumption to increased cattle feed and seed. This results in the greater supply of metals, petroleum, meat and grain but requires time and contributes to still higher interim prices. Lastly, since primary goods are by definition nearly impossible to dispense with, bidding for the remaining stocks will likely result in price increases far surpassing the actual shortage. In other words, a ten percent supply shortfall will likely result in a twenty-five percent price increase before a sufficient number of would-be buyers are finally shocked into withdrawing from the bidding war.

Thus, the outlook for the next several months is for continued commodity shortfall and higher prices—what has come to be known as economic dislocation. These will be reflected in the decisions of the business community, and as such, will continue to have a significant impact upon international commerce and the *raison d'etre* of international commercial law.

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