

Banks speculate on raw materials and food

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Banks, through their trading activities, have become the principal speculators on the Over the Counter (OTC) markets and ultimately on the futures markets for raw materials and agricultural produce, as they dispose of far greater financial means than other protagonists in the field.

A quick glance at the *Commodity business awards* [1] website reveals a list of the banks and brokers playing a major role both on the commodity markets (where raw materials are actually bought, sold and speculated upon) and on the commodity-backed derivatives market. The most frequently mentioned among these are BNP Paribas, Morgan Stanley, Crédit Suisse, Deutsche Bank and Société Générale. Some banks go even further by developing instruments that enable them to directly influence the stocks of raw materials. Such is the case for Crédit Suisse, in partnership with Glencore- Xstrata, the biggest international brokerage company dealing in raw materials [2]. Among the European banks, BNP Paribas along with Deutsche Bank is one of the most influential banks in the commodity markets, playing a key role in the raw materials derivatives sector [3]. In 2013, BNP Paribas created and marketed a new structured product containing different credits that traders can use to buy oil, minerals and agricultural produce. The issue of these securities in the form of bonds has two objectives : firstly, to remove them from the banks' books (as they are heavily weighted in terms of risk); secondly, to earn revenue on the sales of these structured products. Before launching this new product on the markets, BNP Paribas got the Fitch Agency to attribute a Triple A rating to the higher tranches of this potentially high-risk product [4]. The other big banks are keeping an eye on the outcome with a view to creating their own, should BNP Paribas succeed in winning over Pension Funds and other institutional investors to their commodity-backed securities.

Several US banks have taken their strategy for control in a share of the commodities market further; these are JP Morgan, Morgan Stanley and Goldman Sachs. For example, in the first four months of 2013, JP Morgan imported 31 million barrels of oil into the United States! The US banks own oil refineries, power stations, power grids, companies stocking metals, agricultural produce, shale gas exploitation companies, and more. How did this come about? In 2003, the Fed authorised the universal bank Citigroup to buy the trading company Phibro, on the grounds that it was normal to complement their banking activity on the commodity-backed derivatives market with storage capacity for raw materials (oil, cereals, gas, minerals, etc.). As for Morgan Stanley and Goldman Sachs, who until 2008 [5] had the status of investment bankers, after the 1999 law on banking reform that accompanied the abrogation of the Glass Steagall Act, they were able to buy up power stations, oil tankers and other infrastructures. This is how Morgan Stanley came to own barges, tankers, pipelines, and oil and gas terminals! JP Morgan, for their part, bought up the Royal Bank of Scotland's commodities division in 2010 for \$1.7 billion, enabling them to acquire 74 metal storage warehouses in the UK and the USA, while Goldman Sachs hold 112. Thus these two banks together hold more metal storage warehouses than Glencore, who have 179. Storage capacity is crucial for a company or cartel of companies (for example banks) that wants to speculate by maximum stockpiling in order to force prices up or by selling to bring them down., The aluminium market, since 2008 is a prime example. According to an investigation conducted by the New York Times, since 2010 when Goldman Sachs bought up the aluminium warehouses of Detroit, delivery time for aluminium bars

has gone from 6 weeks to 16 months. Prices have risen sharply despite the fact that the amount of aluminium stocks on the global market has increased. As a result, there have been strong reactions from companies which consume large quantities of aluminium in the manufacture of cans, such as Coca Cola and Miller, the brewers. Goldman has amassed 220 million dollars' revenue from aluminium stockpiling in Detroit alone [6].

After having made juicy profits by manipulating stock prices, the most active banks in the actual commodities market have adopted an exit strategy ; this for three main reasons. Firstly, the regulatory authorities have become aware of the manipulations practised by several banks. JP Morgan, Barclays and Deutsche Bank have been fined over several affairs including the manipulation of California's electricity market. JP Morgan have agreed to pay a fine of \$410 million in this ongoing affair [7]. The American authorities, under pressure from companies competing with banks and faced with popular disgruntlement with the banking industry in general, are seriously considering putting a curb on banks' activities on the markets of actual commodities. Secondly, The banks' profits on this market have started to decline since 2011 - 2012 and market prices are contracting. Thirdly, the hard capital (Core Tier 1) required for investments in trading companies is greater than for other types of investment (such as sovereign debt, for example). Consequently, as the banks have to increase their equity/weighted assets ratio, they reckon that they are better off unloading all or part of their investments in the actual commodities market [8]. Watch this space. Nevertheless, the banks will maintain high activity in the commodity-based derivatives market and in all areas of the financial markets relating to raw materials. The damage they can do will remain considerable unless radical measures are taken.

These banks are the prime agitators in the development of the speculative bubble which has grown out of the commodity [9] markets. When it finally bursts, the fallout will hit the banks which will mean further damage. Even more serious are the disastrous repercussions for the populations of countries in the South which export raw materials. People all over the planet stand to be affected in one way or another.

The fundamental role that speculation had on the upsurge of food and oil prices in 2007-2008

Speculation on the main US exchanges, where the world prices of commodities (Agricultural products and raw materials) are negotiated played a fundamental role in the food price increases in 2007 - 2008 [10]. This price explosion caused a dramatic 140 million increase of the number of people suffering from malnutrition in the world, bringing the total to 1 billion (1 person in seven). The principal actors in this speculation were not isolated wide boys, but institutional investors: investment banks [11], pension funds, mutual funds, insurance companies, commercial banks and the big brokerage companies such as Cargill. Hedge funds and sovereign wealth funds [12] were also involved, to a lesser degree.

Michael W. Masters, who directed a Wall Street hedge fund for 12 years, attested to the harmful effect that institutional investors have on commodity price increases, before a Congressional Committee, assembled to examine this question, in Washington on May 20, 2008 [13]. He declared: "You have to ask the question 'Are institutional investors contributing to food and energy price inflation?' And my unequivocal answer is 'YES.'" In his authoritative testimony, he explains that food and energy price inflation is not due to insufficient supply but to a sudden increase in demand from new actors in the commodities "futures" market. In the futures market, investors purchase the upcoming production: the next wheat harvest or the oil production three or six years down the line. Theoretically, the principal investors in these markets are companies wishing to guarantee their supplies of commodities essential to their operations, for example airline companies that assure their future supplies of fuel or agro-industrial firms that purchase specific cereals. Masters

demonstrates that in the US, assets allocated by institutional investors to commodity index trading on the futures market rose from \$13 billion at the end of 2003 to \$260 billion as of March 2008. The prices of the 25 basic commodities listed on these markets climbed 183% during the same period. He explains that the commodities market is a narrow market. Institutional investors such as pension funds, need only allocate 2% of their assets to overwhelm the system. In 2004 the total value of contracts on this market was about \$180 billion whereas the total value traded on shares worldwide was \$44 trillion, about 240 times more. Masters indicates that during that year, institutional investors invested \$25 billion in the futures market, accounting for 14% of that market. He shows that in the first trimester of 2008, institutional investors greatly increased their investments in this markets: \$55 billion in 52 business days. . Now there's a way to create bubbles.

The price of commodities on the futures market has immediate repercussions on the current prices of these goods. Thus, when institutional investors purchased enormous quantities of corn and wheat between 2007 and 2008, prices immediately skyrocketed.

In 2008 the Commodity Futures Trading Commission (CFTC) ruled that institutional investors could not be considered to be speculators: these investors are legitimate commercial market participants. This allows the CFTC to affirm that speculation does not influence prices on the commodity markets. Michael W. Masters severely criticises the CFTC but not so much as Michael Greenberger, lecturer in law at the University of Maryland and ex-Departmental Director at the CFTC from 1997 to 1999. Before a Senatorial Committee held on 3 June 2008 Greenberger criticised the laxity of CFTC directors, who bury their heads in the sand when faced with energy price manipulations by the institutional investors, and quoted a number of declarations they had made that are worthy of inclusion in an anthology of human hypocrisy and idiocy. According to Michael Greenberger, 80% to 90% of energy transactions on US stock markets are speculative [14]. His expertise is indisputable.

On September 22, 2008, in the throes of the United States' financial crisis, when President Bush announced a bailout plan of \$700 billion (not to mention massive liquidities that were also made available), the price of soybean jumped 61.5% because of speculation!

Jacques Berthelot, also shows the crucial role that speculation plays in the rise of agricultural prices worldwide [15]. He gives the example of the Belgian bank, KBC, which ran an advertising campaign in order to sell a new commercial product to savers called "KBC-Life MI Security Food Prices 3" that proposed to invest in six agricultural raw materials. The KBC advertising spin was: "Take advantage of the rising prices of food commodities!" The marketing diatribe presented the "shortage of water and farmland" in the form of an "opportunity" as there is now a "shortage of food products that has led to rising prices of food commodities" [16].

With regard to the American justice system, the speculators are within their rights. Paul Jorion, in an editorial published in the French newspaper *Le Monde*, calls into question the decision of a Washington tribunal which on 29 September 2012 invalidated measures taken by the CFTC "intended to fix a maximum limit to the volume of positions that one transactor can take on the commodity futures market in order to ensure that the transactor alone is not able to destabilise it" [17].

Jean Ziegler, formerly United Nations Special Rapporteur on the Right to Food, does not mince his words: "The 2007-2008 financial crisis, caused by banksterism, has had two notable consequences. Firstly, the hedge funds and major banks reoriented their activity after 2008, dropping certain segments of the financial markets and turning towards the commodity markets, particularly of agricultural produce. If we examine the three main staple crops (maize, rice and wheat), which account for 75 % of world food consumption, their prices have skyrocketed. In 18 months the price of maize has increased by 93 %, the ton of rice has risen from 105 dollars to 1010 dollars and the

price of a ton of milling wheat has doubled since September 2010 to reach 271 euros. This price explosion procures astronomical profits for the speculators but kills hundreds of thousands of women, men and children in the shanty towns. A second consequence is the rush on the part of the hedge funds and other speculators to buy arable land in the southern hemisphere. In 2011, according to the World Bank, 41 million hectares (over 101 million acres) of arable land were taken over by investment funds and multinationals in Africa alone. The result has been the expulsion of small-scale farmers.” [18]

In February 2013, in a report entitled “Réforme bancaire : ces banques françaises qui spéculent sur la faim” (Banking Reform: the French banks that speculate on famine), the NGO Oxfam France indicates that, in November 2012, the four main French banks – BNP Paribas, Société générale, Crédit agricole and Natixis (BPCE) – managed for their clients at least eighteen funds that speculate on the commodity markets. “There are two ways of speculating”, explains Clara Jamart, head of Food Security at Oxfam France, “by taking positions on markets of agricultural commodity derivatives. Or by these index funds, which monitor the prices of agricultural commodities and push them up [19]. Most of these funds were created after the start of the food crisis in 2008, with the express purpose of making profit by speculating on food and other commodities.

Similarly, in 2013 the Réseau financement alternatif (Alternative Financing Network) in Brussels denounced the involvement of six banks working in Belgium in speculating on famine in the world. Some 950 million euros belonging to clients of Belgium banks are used to speculate on food commodities [20].

Alternative proposals [21]

- To bring an end to this state of affairs, there follow 22 proposals for an alternative to the food crisis:
- ban speculation on food; it is a crime to speculate on a people’s lives, and it is for this reason that governments and international institutions must stop speculative investments on agricultural produce;
- prohibit commodity-backed derivatives;
- prohibit banks and other private financial companies from “participating” in the commodities market;
- socialise the banks, under citizens’ control, with a mission to finance projects of food sovereignty giving the priority to small-holdings, cooperatives and the public agricultural sector;
- establish or re-establish international organizations to regulate the market and the production of the main export products (coalitions of countries that produce coffee, coco bean, bananas, tea etc.) so that stable prices are assured on an international level;
- terminate Structural Adjustment Programs (SAP) that force countries to give up their food sovereignty;
- put an end to land-grabbing;
- set up global land reforms (for farmland, but also for water and seeds) to ensure that the farmers who produce food for the local population have access to resources, rather than favouring the large companies that produce for export purposes;

- create an international legal framework on food sovereignty that protects, and formally recognises every country's right to develop its own policies in order to protect its agriculture, without harming other countries (particularly in the Covenant on Economic, Social and Cultural Rights);
- terminate the thrall of exploitation caused by the mechanism of the external or internal public debt, mainly led by private banks, and put an end to the slave-like subjugation of small-holders to private lenders;
- apply a moratorium on industrial biofuels and ban genetically modified organisms;
- reform the EU's Agricultural Policy and the United State's Farm Bill, both of which have disastrous effects on the agricultural markets;
- not sign and, if need be terminate, multilateral (WTO) or bilateral (ALE et APE) free-trade agreements that conflict with food sovereignty;
- establish or re-establish agricultural import restrictions;
- restore public food reserves in every country;
- re-establish mechanisms that will guarantee stable prices for foodstuffs;
- develop production control policies in order to stabilize agricultural prices;
- control the profit margins of intermediaries.

Food security for all starts with stable food prices that cover the cost of production and ensure producers a fair income. The model of low prices, promoted by western governments to increase the mass consumption of manufactured products and services (tourism, entertainment, telecommunications, etc.), is neither socially nor environmentally sustainable. This model mainly benefits large agro-business companies and private banks, and also - by diverting the population's attention away from democratic ideas towards mass consumption - aids the political and economic elite of those countries to confiscate power.

Faced with the current food and environmental crises, radical changes must be made quickly. The proposals listed below are feasible ideas for agricultural and business policies based on food sovereignty. They would stabilize food prices at levels capable of assuring sustainable food production in the great majority of countries.

On a local level:

- support local farm production, notably by supporting farming practices and by facilitating small producers' access to credit, whether they be men or women;
- support and develop short/direct marketing channels between producers and consumers in order to ensure that prices are profitable to farmers and affordable for consumers;
- encourage the consumption of local products;
- support more autonomous forms of production that are less subject to price fluctuations than those forms of production that use chemical fertilizers (grazing on grass instead of being fed corn/soybean meal for example).

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P.S.

* <http://cadtm.org/Banks-speculate-on-raw-materials>

* Translation by Vicki Briault Manus, Adam Clark-Gimmig and Mike Krolikowski (CADTM).

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<http://cadtm.org/Banks-Fudged-health-report>

Next book due out in April 2014 (French version): Bancocratie. Published by ADEN, Brussels.

<http://www.chapitre.com/CHAPITRE/fr/BOOK/toussaint-eric/bancocratie,58547448.aspx> This will extend the series "Banks versus the People: the Underside of a Rigged Game!" published in 2012-2013 on www.cadtm.org and in another version, the series (in French only) "Et si on arrêtait de banquer ?" <http://cadtm.org/Et-si-on-arretait-de-banquer>

Footnotes

[1] <http://www.commoditybusinessawards.com/winners/winners-2013.html>

[2] Glencore-Xstrata is a trading and brokerage company for raw materials founded by the trader Marc Rich. They are based in Baar, in the canton of Zug, Switzerland, known as a tax haven favoured by high-flying tax evaders. Marc Rich, who died in 2013, was repeatedly charged with corruption and tax evasion. He received an amnesty from Bill Clinton on the last day of his presidential mandate, which caused quite a scandal. Glencore-Xstrata owns, in part or in toto, 150 mines and metallurgy sites. According to available data, before its 2013 merger with Xstrata, Glencore controlled about 60 % of global zinc stocks, 50 % of copper, 30 % of aluminium, 25 % of coal, 10 % of cereals and 3 % of oil. In 2008 this highly controversial company won the Public Eye Award for the most irresponsible multinational. Present in 50 countries, Glencore-Xstrata has 190 000 employees (see: <http://www.glencorexstrata.com/about-us/at-a-glance/> and <http://www.glencorexstrata.com/assets/Uploads/2013071-GlencoreXstrata-Factsheet.pdf>). It is headed by its main shareholder, with 16% of the shares, Ivan Galsenberg, who is said to have been paid around 60 million dollars in 2013 (see: http://lexpansion.lexpress.fr/economie/les-remunerations-des-patrons-de-glencore-xstrata-et-credit-suisse-epinglees_399326.html). Crédit Suisse and Glencore-Xstrata are close collaborators on the Chinese market. Other big companies specialised in commodities trading (other than the banks, which are very active) are Vitol (Netherlands), Cargill (United States), Trafigura (Netherlands), Noble Group (Hong-Kong/Singapore), Wilmar (Singapore), Louis Dreyfus Commodities (France), Mitsui (Japan), Mitsubishi (Japan), ADM (United States). In 2012, the combined income of Glencore and these 9 companies amounted to a colossal \$1200 billion. See Financial Times, « Tougher times for the trading titans », 15 April 2013.

[3] See the specialised site:

<http://cib.bnpparibas.com/Products-services/Managing-your-risks-and-assets/Commodity-Derivatives/page.aspx/100>

[4] Financial Times, « BNP Paribas sells commodity loans », 23 August 2013.

[5] Morgan Stanley and Goldman Sachs obtained their universal banking licence at the worst moment of the banking crisis to take full advantage of government assistance and avoid meeting the same fate as Lehman Bros.

[6] L'Echo, "Des banques américaines accusées de manipuler les matières premières (American banks accused of manipulating raw materials)", 24 July 2013,

http://www.lecho.be/actualite/entreprises_finance/Des_banques_americales_accusees_de_manipuler_les_matières_premières.9379357-3027.art (in French only).

[7] Financial Times, "JP Morgan nears commodities sale", 6 February 2014. Barclays Bank has paid a \$470 million dollar fine in this affair.

[8] JP Morgan announced in early 2014 their intention to sell off their actual commodities activities, quickly followed by Deutsche Bank. Morgan Stanley made an agreement with the Russian oil company, Rosneft, handing over part of their business.

[9] Among these market protagonists are the mining and prospecting companies, Rio Tinto, BHP, Billiton, Companhia, Vale do Rio, Doce; ExxonMobil, BP, Shell, Chevron, Total and in the foodstuffs market is, previously mentioned, Cargill, along with Nestles, Monsanto and many others including Chinese speculators.

[10] See article from 2007-2008 by same author, "Getting to the root causes of the food crisis." published 21 November 2008, <http://cadtm.org/Getting-to-the-root-causes-of-the> ; see also: Damien Millet and Eric Toussaint, "Why is there rampant famine in the 21st century and how can it be eradicated?" published 24 April 2009, <http://cadtm.org/Why-is-there-rampant-famine-in-the>

[11] Goldman Sachs, Morgan Stanley and, until their dissolution or takeover, Bear Stearns, Lehman Brothers, Merrill Lynch.

[12] Sovereign wealth funds are public institutions which, apart from a few exceptions, belong either to emerging countries like China or to oil-exporting countries. The first sovereign wealth funds were created during the second half of the 20th century by those governments that wanted to put aside a portion of their earnings from oil and manufactured products. Globally, at the beginning of 2008, institutional investors represented 70 000 USD, sovereign wealth funds \$3000 billion and hedge funds \$1000 billion.

[13] Testimony of Michael W. Masters, Managing Member/Portfolio Manager Masters Capital Management, LLC, before the Committee on Homeland Security and Governmental Affairs United States Senate http://hsgac.senate.gov/public/_files/052008Masters.pdf

[14] See testimony of Michael Greenberger, Law School Professor, University of Maryland, before the US Senate Committee regarding "Energy Market Manipulation and Federal Enforcement Regimes", 3 June 2008, p. 22.

[15] J. Berthelot, « Démêler le vrai du faux dans la flambée des prix agricoles mondiaux (Seeing through the world food price increases) », 15 July 2008, p. 51 to 56 www.cadtm.org/spip.php?article3762 (in French only).

[16] http://www.lalibre.be/index.php?view=article&art_id=419336

[17] Paul Jorion, Paul Jorion, « Le suicide de la finance (The suicide of Finance)», Le Monde, 9 October 2012 (in French only).

[18] Jean Ziegler, “Hunger is man-made and man can unmake it”, interview accorded to Eric Toussaint, published 11 February 2012 <http://cadtm.org/Hunger-is-man-made-and-man-can> Jean Ziegler is the author of Destruction massive, géopolitique de la faim, Éditions du Seuil, Paris, 2012.

[19] See (in French) Le Monde, Quatre banques françaises accusées de “spéculer sur la faim” (Four French banks accused of “speculating on famine”), 11 February 2013. http://www.lemonde.fr/economie/article/2013/02/11/quatre-banques-francaises-accusees-de-speculer-sur-la-faim_1829956_3234.html. For Oxfam’s international campaign, see The Financial Times, “Food price speculation taken off the menu”, 4 March 2013. See also the Oxfam website for “EU deal on curbing food speculation comes none too soon”, 15 January 2014, <http://www.oxfam.org/en/eu/pressroom/reactions/eu-deal-curbing-food-speculation-comes-none-to-o-soon>

[20] See (in French) <http://blogs.lecho.be/argentcontent/2013/06/des-centaines-de-millions-deuros-belges-pour-speculer-sur-la-faim.html>

[21] The section entitled “Alternative proposals” is derived from “Proposition de document de position de la Via Campesina sur les prix agricoles et la speculation (proposal of a platform by ‘La Via Campesina’ concerning agricultural prices and speculation)”, July 2008.