London metal crisis may trigger defaults

by William Engdahl

On Oct. 24, The International Tin Council (ITC) suspended trading on the London Metal Exchange, the world's leading metals market. The emergency move was made by Pieter de Koning, Buffer Stock Manager for the London-based international tin cartel, following the sudden collapse of the price of tin from the ITC official floor price of £8,500 to £8,140 ($11,900 to $11,396). De Koning announced that he had been forced to suspend trading because he had used up all the available credit lines to support the floor price.

According to London trading sources, the immediate crisis was triggered when the lending banks demanded payment of an agreed-upon £60 million from the 22 member-nations of the ITC, to supplement the buffer stock, a price-regulating mechanism the ITC uses to control production and firm prices through accumulation of a central stockpile, called the buffer stock. Declining industrial demand in recent years, combined with increased tin production by non-ITC countries, especially Brazil and China, has created a glut in the world tin market. Despite a voluntary 30% cut, the ITC will still produce about 165,000 tons of tin in 1985. Although total demand is estimated at 184,000 tons, world stocks stand at 284,000 tons by ITC estimates.

But much more is at stake than a £60 million payment, or even the £600 million estimated loss if the ITC defaults. The ITC remains closed, although the London Metal Exchange has decided to reopen trading in tin on Nov. 18, a gamble designed to contain major financial panic. "It is an extremely serious situation," the head of one major London commodity trading house told *EIR*: "This crisis affects not just tin, but the future of London as a world financial center." One informed City of London financial source stressed that underneath the immediate crisis is a deeper potential crisis of confidence regarding all multi-national guarantees on loan obligations. In the London banking community, there is considerable apprehension that the ITC crisis could knock out vital props to the international monetary system, including loan agreements with the Inter-American Development Bank, the Asian Development Bank and perhaps even the World Bank.

The ITC crisis has jeopardized the commodity trading houses linked with international tin trading through the London Metal Exchange, as well as some of the banks heavily involved in lending on the international tin market, including Hambros Bank, ABN Bank of the Netherlands, Bank Bumiputra of Malaysia and Chase Manhattan and Shearson-Lehman of New York, which have helped finance the tin buffer stock. Until the present crisis, the buffer stock was assumed to be guaranteed by the 22 member governments of the International Tin Agreement, which established the ITC cartel in 1931.

Britain's Thatcher government has kept itself at armslength from the current situation, as it is still smarting from the 1984 collapse of the Johnson Matthey Bank, one of the five London banks which fix the daily market in gold trading. That bankruptcy has severely undermined London's traditional role as a center of international gold trading.

Because of the special regulations governing the London Metal Exchange, the failure of even one member company with so-called ring-dealing privileges, would create a "domino effect" on all the other ring-dealing members of the LME, to destroy the whole basis of the world's most important metals trading market. The LME, unlike almost every other major international market, has no central clearing system through which all deals are settled. Each deal is unprotected and depends on the other side's creditworthiness. As a result of the tin closure, all LME metals trading came to a halt, as dealers with no exposure to tin worried about trading with dealers who are.

But the crisis goes beyond London's financial institutions. The prospect of a total price collapse in tin will deal a devastating financial blow to developing countries which produce most of the world's tin. The major producers in the ITC cartel are Malaysia, Indonesia, Thailand, and Bolivia. The United States, which consumes about 30% of world tin, imports most of its tin from the Asian producers. Thus, tin is considered strategic by the U.S. government. Besides being used to coat cans for foods, tin is combined with niobium for space and nuclear superconducting alloys, and has other industrial applications such as soldering alloys, ball bearings, and chemical pesticides and fungicides.

It is estimated that tin prices will fall from the Oct. 24 suspension price of £8,140/ton to £6,000, or even as low as £4,200/ton once trading resumes. This is a devastating prospect for the economies of Malaysia, Thailand, and Bolivia, among others. To maintain the present ITC floor price of £8,140 would require massive inflows of new funds to support the buffer stock fund of the ITC at a time of general international liquidity crisis. Nobody believes such funds are forthcoming. Bolivia, which has severely repressed labor strikes called to protest the pro-IMF austerity measures of the new Paz Estenssoro government, depends on tin exports for fully one-third of its export income. Collapse of world tin prices in the coming weeks will trigger an immediate financial crisis there as well as in Thailand, where IMF austerity demands have created the most severe political crisis in Thailand's recent history.