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PRESS RELEASE

Recent commodity price developments: causes and effects

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The commodity markets have been at the centre of attention again, since 2003 especially, due to the sharp increase in prices. Prices of oil and most metals have risen to historically high levels, and in real terms have reached their highest levels since the early eighties. The recent increase is mainly a result of the substantial expansion in demand for commodities. The latter reflects the buoyant global economic growth of the last few years and, particularly, the increasing integration of a large share of the world population into the global economy and international trade.

In part, however, the rise in oil prices was also caused by a number of developments on the supply side. Thus, the unexpectedly high demand for oil in 2004, along with a slower increase in production by non-OPEC countries, boosted the "call on OPEC" to such an extent that the unused production capacity sank to historically low levels. This made the price of oil sensitive to any change which adversely affected oil supply, such as the recurrent geopolitical tensions.

In the countries importing this commodity, any increase in the price of oil tends to generate higher inflation and lower economic growth. Unlike previous shocks, however, the global economy has resisted quite well in recent years. This was mostly due to the modified monetary policy system, the lower energy intensity of the advanced economies, the positive effects of globalisation, and the favourable cyclical conditions in which the present shock occurred.

Forecasts for commodity prices constitute an important input for planning and shaping macroeconomic policy. In the light of forward quotations, the present high oil prices are considered by market participants to be a permanent fixture. In the long term, demand for oil would - according to the latest forecast of the International Energy Agency (IEA) - increase by an average of 1.3 p.c. a year throughout the period 2005-2030. Production would rise accordingly, stepping up the "call on OPEC". With its forecast, the IEA is on the side of the optimists, since a great many analysts expect a production peak some time before 2030. Overall, the IEA as well as most other observers expect oil prices to remain high in the next few decades. A number of factors might, however, moderate future price developments. High prices could, for instance, reduce demand for oil (pursuit of greater energy efficiency, search for alternative sources of energy) and make it profitable to exploit oil fields hitherto undeveloped. The forecasts for metal prices suggest that prices will return to a more moderate level, mainly because the production capacity can be increased quite rapidly.

Because of the potentially huge economic impact of high and volatile oil prices and because of the increasing concern about the consequences of energy consumption for the environment, public authorities are bound to play a key role in the energy debate. In this respect, it is desirable for monetary policy to remain committed to the objective of medium-term price stability, even in the event of an oil shock. Apart from that, the public administration should allow the price mechanism to work freely. They should, however, envisage a number of structural measures aimed at limiting the risks associated with serious production disruptions and at ensuring a sustainable energy supply. In recent years, a number of initiatives have been taken on a European level in order to reach agreement on a common European energy and climate policy. In March of the current year, for instance, the European Council adopted an Energy Policy for Europe (EPE). The practical implementation of the latter was outlined in an energy action plan for the period 2007-2009.

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