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Commodity dependence and diversification with some evidence on the Dominican Republic

By

José R. SÁNCHEZ-FUNG

Ambassador and Permanent Representative
of the Dominican Republic to the World Trade Organization (WTO)
and the United Nations Conference on Trade and Development (UNCTAD)

The views expressed are those of the author and do not necessarily reflect the views of UNCTAD.



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OVERVIEW

The relationship between commodities and development is a central focus of study in the theoretic and empirical academic literatures

UNCTAD has a long tradition of work in the field -currently mandated by the **Bridgetown Covenant**

This Multi-year Expert Meeting on Commodities and Development provides a valuable opportunity for thinking about recent developments in the field



In the context of this event, UNCTAD's team proposes a series of important questions, inter alia:

- Why commodities matter for development?

The path towards economic development is complicated by shocks to the prices of commodities for countries that critically depend on them



Large changes in prices can lead to

- Macroeconomic instability

via impacts on economic growth, investment, consumption, exchange rates...

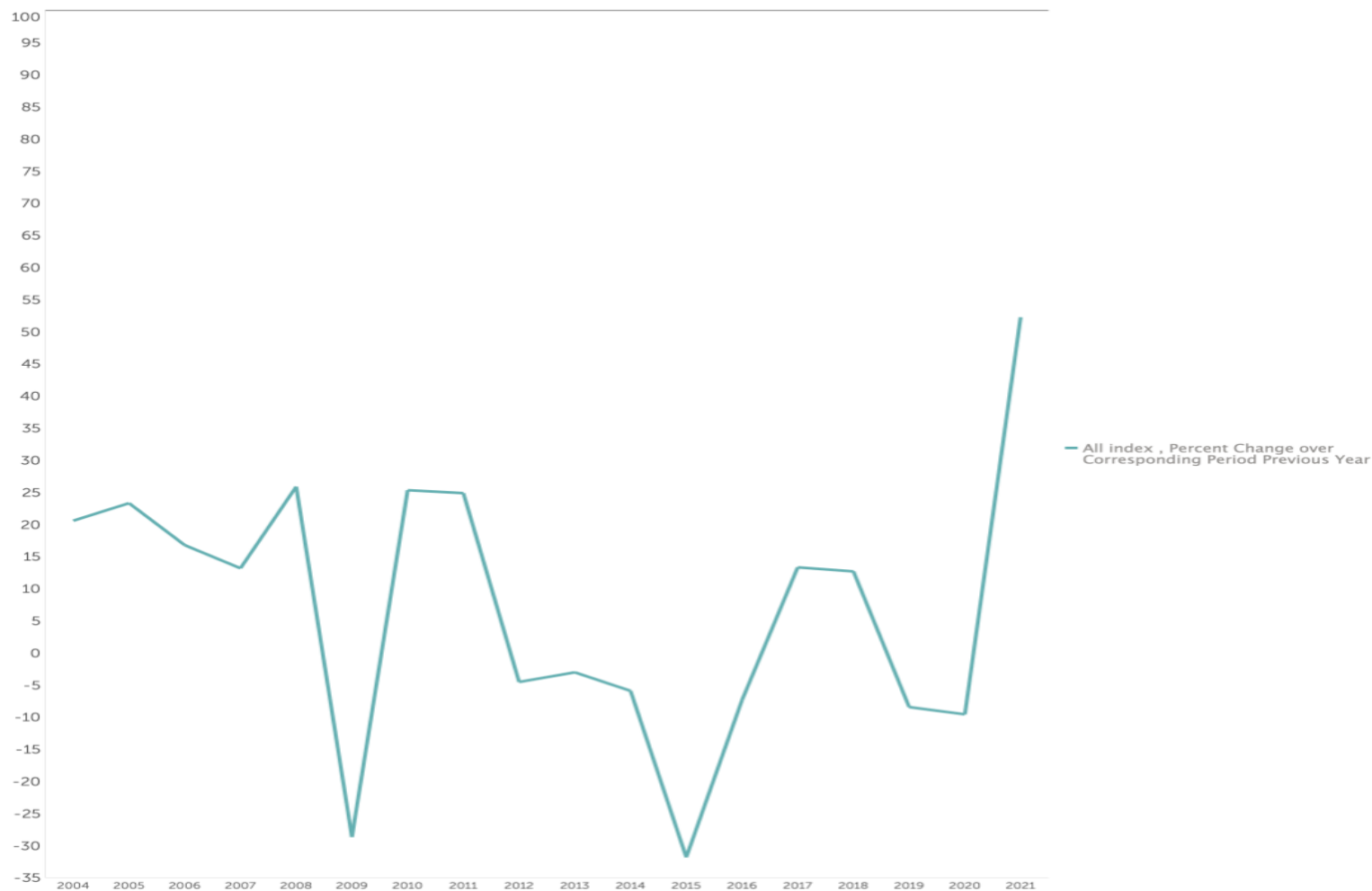
And subsequent welfare effects, including on households' consumption

The graph reveals various such aggregate shocks during the last three decades

Source: IMF's Primary Commodity Price System



Graph 1: Commodity price index (annual % change), 2004-2021



Source: Primary Commodity Price System (PCPS) (09/12/2022)
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SELECTED IDEAS FROM THE RECENT ACADEMIC LITERATURE

Developments in commodities lead to revisiting old questions in the literature

The potential effects can operate via various channels

- Macro
- Micro-sectoral

This is not the occasion to review the corresponding literature

Allow me to focus on two recent papers with ideas worth pondering relating to this meeting's theme



MACRO

Kohn et al (*American Economic Journal: Macroeconomics*, 2021)

Investigates transmission mechanism from commodities to business cycle volatility

Theoretical model including developed and developing economies

- Firms' production: commodities and manufactures
- Both face the same shocks
- Developing countries run trade surpluses in commodities and deficits in manufactures -sectoral imbalance
- But aggregate trade flows are balanced in developed economies

Analytical and empirical modelling reveal that these features lead to the amplification of shocks to commodities affecting developing economies (more volatile versus developed)

- Key driver is sectoral trade imbalance -**so argument for sectoral diversification**



CASE STUDY - Micro

Kebede (*World Bank Economic Review*, 2022)

Studies the pass through from commodity prices to domestic markets

Case study using panel data for [Ethiopia](#)

Find that reductions in coffee prices induce reductions in consumption of households dependent on that commodity

The study reveals an important effect on the welfare of children in the coffee producing sector: an increase in malnutrition



DOMINICAN REPUBLIC

The Dominican Republic using the definition in UNCTAD's report (TD/B/C.I/MEM.2/53, page 2):

An economy is defined as commodity dependent when it derives 60 per cent or more of its merchandise export revenues from primary commodities such as food, agricultural raw materials, base metals and crude oil

In 2021, minerals and agricultural exports accounted for 25% of total merchandise exports...55% excluding free trade zones

In that regard, what happened with the Dominican Republic's net (weighted) commodity terms of trade in the last 60 years?



Source: IMF's Primary Commodity Price System

Graph 2: Dominican Republic's net (weighted) commodity terms of trade, 1962-2021



Source: Commodity Terms of Trade (09/07/2022)
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The long-term development reflected in the graph is important

The Dominican Republic was ahead of this curve by diversifying its economy away from the primary sector from the 1970s towards (one of the fastest growing in Latin America since that decade)

Quoting **Pozo, Sánchez-Fung, and Santos-Paulino (2020)**:

At the beginning of the 1970s relatively few commodities accounted for a large share of total export earnings: cocoa, coffee, sugar and tobacco...these commodities amounted to over 70 per cent of total exports, but by the new millennium, primary commodities' share made up less than 5 per cent of total exports.

- ❖ Industrial (including free trade zones): Industrial exports accounted for 75% of merchandise exports in 2021
- ❖ Services (mainly tourism): **Similar in nominal terms to industrial exports in 2021**

- See **Pozo, Sánchez-Fung, and Santos-Paulino** ([Oxford University Press](#), 2013)

The paper is part of a project on development strategies at **UNU-WIDER**, Helsinki



Regardless of not being a commodity-dependent economy

The topic remains significant for understanding the impact of large swings in international commodity prices and what can be done to protect the economy from such swings

Allow me to highlight before closing my intervention

Joint report on the Dominican Republic (2020)

Production Transformation Policy Review (PTPR)

- ❖ *Development Centre* of the Organisation for Economic Co-operation and Development (OECD)
- ❖ United Nations Economic Commission for Latin America and the Caribbean (ECLAC)
- ❖ United Nations Conference on Trade and Development (UNCTAD)



The report is relevant for thinking about this meeting's broad topic

In my view, the report's key contribution is stressing the important progress made in the Dominican Republic's agro-food sector

According to the report, the Dominican Republic devotes **8.7% of its agricultural land to organic production**

That is notable and only second to Uruguay in the region

Furthermore, the Dominican Republic is the world's largest producer of organic cocoa (30% of global production) and organic bananas (55%)



Please allow me to conclude by stressing that, as Janvier noted earlier in the meeting, diversifying the economy is important and possible

- The Dominican Republic is an example showing that it can be accomplished, but is just a step in the process towards sustainable economic growth and development



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