

5 RECOMMENDATIONS

- 5.1 We do not recommend the LME to take no action. Although the issues are complex, the combination of economic circumstances and the present loading out rate requirement is leading to a situation in which queues are longer than desirable for the LME system as a whole.
- 5.2 A universal increase in the current loading-out obligations would not be sufficient to make a fundamental difference to the length of waiting time and would impose unreasonable levels of operating costs on a very large number of warehouse/locations where excessive queues have not arisen and are unlikely to arise. This option is not recommended.
- 5.3 The queuing problem is most acute when a warehouse develops a level of stocks that, given the existing loading out rate, means that the warehouse's income reaches a level at which after all costs, capital is fully remunerated and there is still a sufficient surplus to make it possible to buy in metal at a rate equal to or in excess of the loading out rate. This in turn allows the warehouse to float its warrants on the Exchange. An increase in the loading out rate required from warehouses with very large stocks should prevent the perpetual queue from becoming entrenched and could be expected to produce a more balanced distribution of stocks, reduced premiums, reduced queues and a more rational set of prices.
- 5.4 Our prime recommendation, therefore, is that a level should be set well above the present limit in the loading-out table at which a large warehouse would be obliged substantially to increase its loading-out rate.
- 5.5 From a regulatory point of view this is a less than satisfactory conclusion. Although we believe that the present situation would be greatly improved it does not provide a guarantee that a long and persistent queue will never, in any circumstances develop. Indeed, at 300,000 tonnes there remains a theoretical maximum queue of 200 warehouse days, which would seemingly be endorsed by the LME if regulations were altered in this manner and no other changes were made. It would be irresponsible for the LME as a regulator to maintain such a policy were lengthy, persistent queues to remain.
- 5.6 Our second recommendation is therefore that loading out obligations be formally reviewed at intervals of six months, and the level at which higher loading out requirements apply lowered progressively should long and persistent queues continue to be observed.
- 5.7 The only policy option, Option 4, that would have completely eliminated long and persistent queues would have imposed prohibitive costs on warehouses and resulted in loading out requirements for some warehouses that were beyond levels that were physically possible. Such costs would be likely to affect adversely the willingness of warehouses to take in metal in times of a slack physical market, thereby introducing a distortion in the opposite direction to queues.

- 5.8 Option 5, rent rebates, could in principle address some of the issues raised by queues, though it may prove impossible to implement them across all warehouses. It is therefore recommended that rent rebates be discussed, bearing in mind that their effectiveness is contingent on their application to warehouses with long and persistent queues.
- 5.9 We suggest that the LME considers a phased approach. This would involve imposing higher loading out requirements on the warehouse/locations with the largest capacities, and, should long persistent queues continue, reducing the level of capacity to which the new loading out requirement applies.
- 5.10 A phased approach would then comprise:
- (a) Loading out requirements implemented applying higher delivery out requirements to warehouses with stocks above 300,000 tonnes.
 - (b) These requirements should be reviewed formally at intervals of six months. Should persistent and lengthy queues continue to be observed, the level of stocks at which higher loading out requirements apply should be progressively lowered.