



Signs of a commodities supercycle

What is the issue?

\n\n

\n

- Globally, the prices of commodities are rising or expected to rise.
- This is seen as a sign of a likely commodities supercycle.
- The development is to be understood in view of the relationship between commodities prices and the US dollar.

\n

\n\n

What is a supercycle?

\n\n

\n

- In economic terms, a Supercycle is the longest period or wave in the growth of a financial market.
- e.x: In 1700s, due to the Industrial Revolution in Britain, prices of coal, cotton, sugar, tea etc went up and greater quantities were produced.
- But over time, the innovation worn out, demand lowered when supply was growing, and the prices of commodities dropped, causing the end of the super-cycle.
- The last commodities super cycle was roughly from 2000 to 2014.
- This **boom in commodity prices** was largely due to the rising demand from emerging markets as well as the result of concerns over long-term supply availability.

\n

\n\n

How does US dollar influence the commodity prices?

\n\n

\n

- Historically there is an **inverse relationship** between the value of the dollar and commodity prices.

\n

- When the value of the dollar drops, other countries will have more buying power, as it takes less of their currencies to purchase a dollar.

\n

- This increased buying power naturally increases the demand and subsequently commodity prices increases and vice versa.

\n

\n\n

What happened after 2014?

\n\n

\n

- **Deviation in relationship** - The two years following the 2014 commodities supercycle witnessed a steep fall in prices.

\n

- This coincided with the slowdown in the Chinese economy and resultant poor investment in the commodities space and poor demand globally.

\n

- As a result, the association between the dollar and commodities prices reversed to a **new direct relationship**.

\n

- Despite a strengthening dollar scenario, commodity prices increased due to -

\n

\n\n

\n

1. Election of Trump as the U.S. President leading to hopes of increased public investment in infrastructure projects.

\n

2. Signs of economic recovery and stimulus investment made in Chinese infrastructure making favourable impact on commodity prices.

\n

3. Global growth was getting stronger and as a consequence there was a boom in resources.

\n

\n\n

Why is the Supercycle expected now?

\n\n

\n

- The above mentioned market euphoria around a recovery in commodities demand due to a stronger global economy has died out.

\n

- The U.S. dollar index has now dropped by almost 10% since the beginning of the year.

\n

- But there is a rise in global commodities prices, reflecting the return of inverse relationship between dollar and commodity price.

\n

\n\n

\n\n

Source: The Hindu, Business Standard

\n\n

\n

\n\n

\n\n

\n



IAS PARLIAMENT

Information is Empowering

A Shankar IAS Academy Initiative