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››› Commodity price decline weighs on investment

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For the commodity exporters among the developing and emerging economies, the world market price for their commodities is crucial for determining how much they can afford to import. A price drop, such as the oil price decline since mid-2014, has significantly worsened this ratio for them. But other commodities, such as mineral ores and metals, as well as agricultural resources (e.g. cotton, timber and others), have also suffered price declines in the past years. This deterioration in the terms of trade (the ratio between export and import prices) for the respective exporting countries also has potential adverse impacts on investment activity and economic growth.

Response of terms of trade depends on export concentration on natural resources

Commodity producers often focus their exports precisely on these resources, e.g. crude oil, metals or agricultural resources. Accordingly, higher commodity prices improve the terms of trade between exports and imports while lower prices do the opposite. Oil exporting countries often have a very high export concentration, so the magnitude of their terms of trade response is correspondingly strong. For countries that export agricultural commodities, on the other hand, the export share is often too low to cause a strong systematic terms of trade response to prices. The greater homogeneity of crude oil and metals and the frequent geographical concentration of deposits, in contrast to the dissimilarity of agricultural commodities, may play a role in this context.

Deteriorating terms of trade also drive prices of capital goods imports

Commodity price effects work their way into the real economy using a variety of channels, e.g. through investment. The most direct path is probably through investments in the exploration and mining of the relevant resource deposits. Lower earnings prospects as a result of lower commodity prices reduce investment incentives for the resource industries themselves but also for related sectors such as transport and logistics or construction.

At the same time, capital goods imports become more expensive when the terms of trade deteriorate. A depreciation of the exporting country's currency in the wake of falling resource prices additionally pushes up the prices of imports in local currency. For exporters, in turn, it cushions the fall in revenues.

The synchronisation between terms of trade and capital goods imports is also most pronounced for oil exporting countries, while the synchronisation of nominal capital goods imports and real investment activity is relatively high, regardless of the group of resources.

Negative cyclical influence and adverse effect on production potential

Shocks of the terms of trade weighted against the commodity exports and imports influence the potential growth of net exporting countries relatively strongly through investments and, thus, the formation of capital stock. According to IMF estimates, net exporters' potential growth could be ⅓ percentage point lower in the years 2015 to 2017 than between 2012 and 2014, with a particularly pronounced negative effect for net exporters of crude oil, natural gas and coal. ■

Figure 1: Capital goods imports and terms of trade

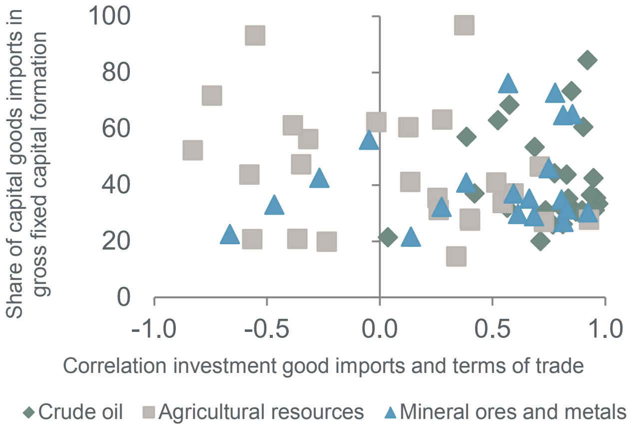
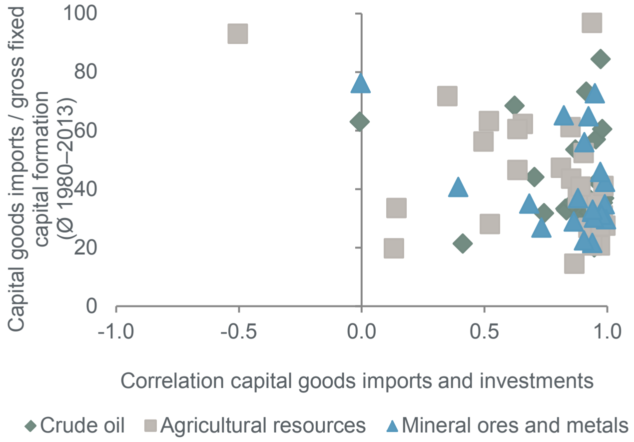


Figure 2: Capital goods imports and real gross capital formation



Note: Selection of countries according to UNCTAD depending on a) the share of resources in the country's exports and b) the share of global exports complemented by countries with a share of the respective commodities in merchandise exports of more than 30 %.

Source: UNCTAD, own calculations