Analyse the influence of different factors Australia's trade and financial flows

Since Australia's financial deregulation and the increase in globalisation, there has been a rise in differing factors that influence Australia's trade and financial flows. In the 1980s, under the Hawke government, the introduction of foreign policies allowed for overseas investment into Australia which meant that Australia's interest rates incentivised foreign, in addition to domestic, investments. It also allowed for the Australian economy to be influenced by the international business cycles of major trading partners such as China and the United States meaning that Australia's international competitiveness became more important and as a result, the Australian dollar was floated in 1983, which heavily influences the trade and financial flows in Australia.

The second mining boom in 2010-11 began with the increased demand for Australian commodities from China however it was mainly driven by the significant increase in foreign investment as investors seeked the economy that would give them the highest return on investment. To capitalise on the mining boom, the Reserve Bank of Australia raised the cash rate from 3% in 2009 to 4.5% in 2010-11, incentivising higher foreign investment in order to fund their capital intensive industry that was booming from the higher demand from China. As a result, the KAFA recorded an increase of $79.6 billion from the previous year, ending 2011 with a surplus of $854.7 billion. With lower global interest rates relative to Australia, domestic borrowers are more likely to take a loan from overseas as the interest paid would be relatively cheaper. However, with increased foreign investment and international borrowing, returns on investment in the form of dividends and interest had to be paid which is represented by the $5 billion worsening the NPY account. The deficit in the NPY far outweighed the surplus in the BOGS account which meant that the CAD worsened, decreasing to -3.2% of GDP in 2011 and decreased again to -4.8% in 2012. The RBA's tightening of monetary policy caused a positive interest rates differential as Australia's interest rates rose higher than those of the global economy which meant that domestic investors and savers were more likely to save their money in Australia, causing less financial outflows, increasing the KAFA surplus and similarly meant that there was less NPY credits, further worsening the NPY account and thus the CAD. Hence the level of interest rates of Australia and the global economy impacts Australia's financial flows as investors are looking for a higher return on their investments and domestic borrowers could possibly receive a loan with lower interest rates overseas.

Kommentiert [1]: This isn't the reason for raising cash rates. Monetary policy tightened in response to inflation during the Boom.

Kommentiert [2]: 'more financial inflows'

Following the second mining boom, China's economic growth began to slow leading to a significant decrease in the demand for Australian exports causing a deterioration in the terms of trade and a depreciation of the AUD. China's GDP growth fell from 7.4% to 6.9% from 2014 to 2015 causing a deterioration in the terms of trade, from 84.5 to 76 and the dollar to fall 21 US cents in the same time period. Other international business cycles such as the United States, United Kingdom and various European countries began to see contractions in their growth as political uncertainty grew from events such as the European Sovereign Debt Crisis, BREXIT and the US election. This meant that there were low levels of consumer and investor confidence as the economic outlook for Australia's major trading partners became unclear. This led to less direct investment inflows and outflows and more portfolio investments as they are more speculative in nature. This can be seen as European countries such as Belgium and the United

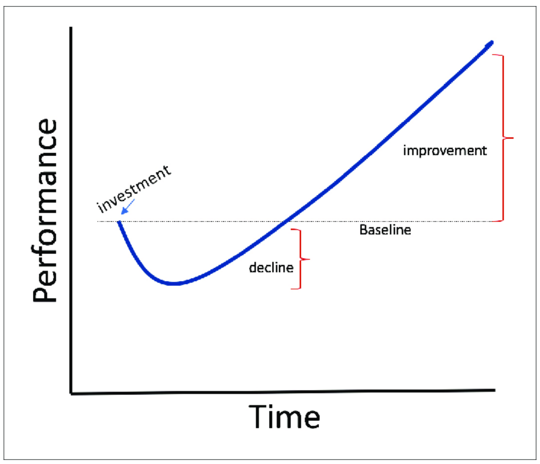
Kommentiert [3]: Perhaps combine these sentences to save words and avoid repetition

Kommentiert [4]: 'trading partners'

Kingdom who were affected by the European Sovereign Debt Crisis and the onset of Brexit had decreased their level of direct investment into Australia from 2014-2015 while unaffected countries such as Japan increased their level of direct investments. Both Belgium and the UK however had increased their level of portfolio investment into Australia, showing the speculative nature of these investments as there was economic and political uncertainty in the region.

Kommentiert [5]: Some relevant info, but needs to be linked back to trade and financial flow stats / BoP accounts

With the depreciation of the AUD in 2014-15, Australia had become increasing internationally



competitive, as dollar depreciating caused exports to become relatively cheaper to foreign consumers. This can be seen in the J-Curve Theory which states that a deprecation of the currency causes an initial deficit in the BOGS as volumes of exports and imports are kept constant so import spending increases however in the long run as volumes begin to change with respect to price, export revenue increases while there is a reduction in import spending, improving the BOGS account and possibly causing it to enter a surplus. This can be seen as in 2016-17, the demand for liquified natural gas increased significantly from China, causing the terms of trade to improve to 92.4 in 2017. As China continued to demand Australian LNG exports, the dollar appreciated from $US0.68 at the beginning of 2016 to $US0.80 by the end of 2017. This was also caused by the structural changes from the second mining boom as with the previous strong appreciation causing Dutch Disease; inefficient and uncompetitive export industries such as the Passenger Motor Vehicle manufacturing industry were phased out. As a result of these structural changes which caused a shift in the composition of Australian exports, Australia became more internationally competitive.

Kommentiert [6]: 'total import spending increases due to higher prices'

Kommentiert [7]: What did they shift towards? Evidence?

Despite the initial economic downturn caused by the COVID-19 pandemic in the beginning of 2020, Australia's recovery would cause a historic current account surplus in addition to a financial account deficit. The global economy faced recessions which prompted a recovery of government schemes such as the infrastructure packages in China. The Chinese government would initiate an economic recovery with a creation of jobs through building projects such as bridges, roads and housing however to fund these programs, the government started to demand Australian minerals. Demand had increased significantly for Australian iron ore which caused terms of trade to improve to 103.6 and the AUD to appreciate from its lowest point in March of 2020 at $US0.58 to $US0.8 in January of 2021. Coupled with lower imports due to the weak AUD at the time, BOGS stayed a surplus throughout 2020, at an average of $72.7 billion which contributed to the current account surplus of 0.2% of GDP. With the financial contagion of COVID-19 causing a decrease in global investor confidence, investments in and out of Australia decreased in value as direct investments became increasingly rare due to the uncertainty of the Australian economy. Furthermore, the Australian investments-savings gap had decreased due to the lower consumption in the economy due to worsened economic conditions meaning that individuals were saving more of their income leading to less reliance on international borrowing causing the financial account to enter a deficit. With less financial inflows, there were decreased servicing costs payments, contributing to the current account surplus. Hence, the economic conditions which impact investor and consumer confidence, in turn, influence Australia’s trade and financial flows.

Therefore, Australia’s trade and financial flows are influenced by the level of interest rates, the international business cycle, Australia’s international competitiveness and the level of investor and consumer confidence.