MACROECONOMICS AT WORK EXERCISE

EXPORTS, GDP AND THE BALANCE OF TRADE

REFERENCE: C. Murphy, 'Mining boom takes heat off trade deficit', *The Australian Financial Review,* 1 September 2005, pp. 1, 4.

CHAPTERS RELEVANT TO THIS EXERCISE: 6 and 17

CONTEXT

Net exports – exports minus imports [X – M] – are one of the major elements in the determination of GDP – along with Consumption [C], Investment [I] and Government Expenditure [G] (see pp.125-9). The total value of *exports* is significant in that it is one of the major components of X – M. Exports are made up of a number of goods, (e.g. minerals), and services, (e.g. education).

The difference between X and M gives the *balance of trade* (see pp. 381-3). Where imports exceed exports, there is said to be a *trade deficit*. A trade deficit will influence a country's balance of payments with the rest of the world and also the exchange rate of its currency (see pp. 383-93).

This article is concerned, however, primarily with the composition of trade and specifically with the way in which since late 2004 there has been a marked increase in exports which, while there has been some increase in imports, it has been proportionally lower; the overall result being a reduction in the trade deficit.

QUESTIONS

1. What has been the extent of the increase in Australian exports reported in the article? What have been the major causes of this increase?

2. What effect has this had on the Australian trade and current account deficit?

3. Explain the impact that the trend in oil prices is having on the trade deficit.

4. Explain the concept of the 'terms of trade' and the effect that trends in the Australian terms of trade is having on the trade deficit.

5. What is the likely future trend in regard to both exports and imports?

6. In what sense is the improved trade situation ‘taking up the slack’ caused by reduction in other elements of aggregate demand?