

Exchange Rates

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Definition

- An exchange rate simply refers to the value of a currency in terms of another countries currency
- The Trade Weighted Index (TWI) refers to a weighted average of a basket of currencies that is thus a more accurate determinant of exchange rate

Changes in the Exchange Rate

- The Australian Dollar is a largely free floating currency and its value is thus determined by the market forces of demand and supply on the FOREX market
- The Reserve Bank can and has stepped in to adjust the value of the Australian dollar and hence it is not a completely clean float
 - **Changes in Demand**
 - Increases in exports
 - Increased foreign investment into Australia
 - PRIDD flowing into Australia
 - **Changes in Supply**
 - Increases in imports
 - Foreign Investment out of Australia
 - PRIDD out of Australia

Determinants of the Exchange Rate

- The interest rate differential
- Global Economic Growth
- Domestic Economic Growth
- International competitiveness (Inflation)
- Commodity prices

Depreciation	Appreciation
International competitiveness rises	International competitiveness falls
Net Exports rises	Net exports fall
Aggregate Demand Increases	Aggregate demand decreases
Expansionary Effect	Contractionary effect

Trends in the AUD

- Recently hit 10 year low
- Record low interest rates have pushed Australian dollar downwards