21.

(a) Identify the percentage change in Goods Trade in January 2018. (1 mark)

Approximately 5% increase

(b) Identify the linkage between countries evident in the data. (1 mark)

Trade

(c) (i) Identify the trend in globalisation from 2018 onwards. (1 mark)

Decrease in globalisation

(ii) Describe three economic effects of the trend identified in part (i). (3 marks)

1. Decreased allocative efficiency: As specialization and subsequent trade mean that resources are allocated at max efficiency, a decrease in globalisation means less of this will happen and thus resources are not allocated as efficiently as possible.
2. Decreased economic growth: As resources aren't allocated at max efficiency total output decreases and thus economic growth decreases.
3. Unemployment de increase: As output decreases, number of jobs decrease and thus unemployment increases.
4. Fall in living standards: Lower output means lower disposable income, which translates to a lower standard of living.

21.

(a) Identify the percentage change in Goods Trade in January 2018. (1 mark)

~5%

(b) Identify the linkage between countries evident in the data. (1 mark)

Trade of goods and services

(c) (i) Identify the trend in globalisation from 2018 onwards. (1 mark)

Decrease.

cost push
↑ inflation
↓ exports
→ reduction ~ growth, AD

(ii) Describe three economic effects of the trend identified in part (i). (3 marks)

As evident in graph A, levels of new export orders and goods trade ~~is decre~~ has gradually decreased since Jan 2018. Lower levels of exports could directly reduce export revenue (a component of AE) which could reduce the levels of income and output in the economy.

Decreasing levels of ~~trade suggest that~~ industrial production growth and capital goods production (graphs B and C) perhaps indicates lower levels of employment as ~~production reduces~~ levels of production and output decrease.

Finally ~~lower~~ negative industrial production growth could also indicate lower levels of productivity, perhaps increasing cost of production, and inducing cost push inflation.

21.

(a) Identify the percentage change in Goods Trade in January 2018. (1 mark)

The change in Goods Trade was about 5.3% .

(b) Identify the linkage between countries evident in the data. (1 mark)

Trade .

(c) (i) Identify the trend in globalisation from 2018 onwards. (1 mark)

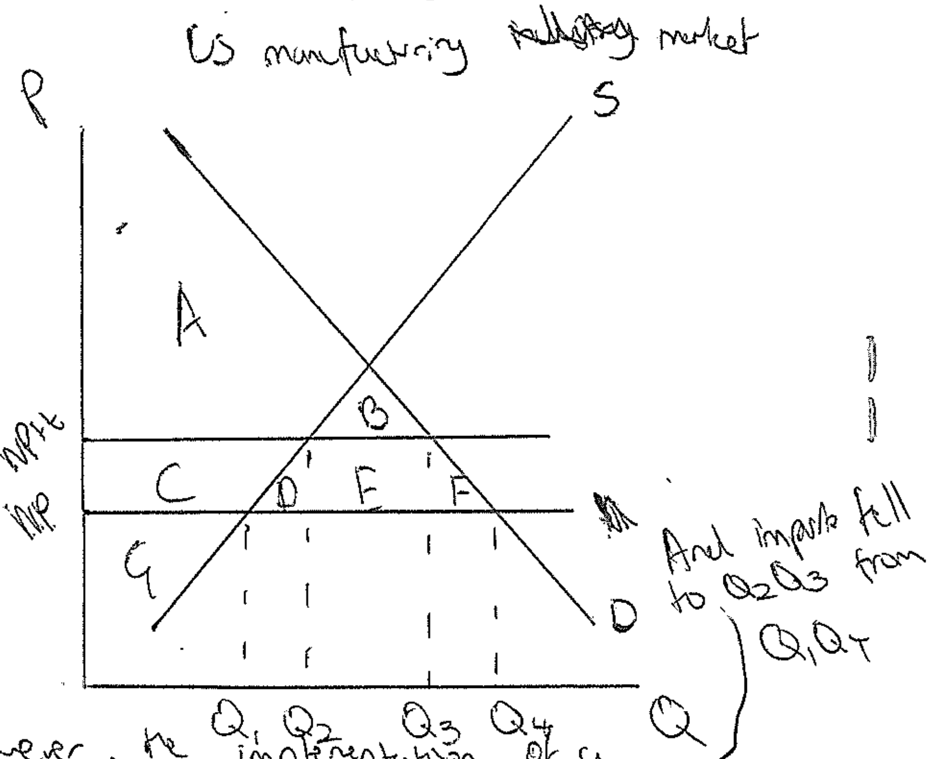
Globalisation has been on a downwards (negative) trend since 2018 .

(ii) Describe three economic effects of the trend identified in part (i). (3 marks)

One economic effect of decreased globalisation is the decline in trade resulting in reduced export and import volumes. For nations with large export sectors such as Australia this can significantly hinder economic growth. Furthermore, a fall in foreign investment as a result of reduced globalisation can limit the productive capacity of many economies restricting global economic growth figures and material living standards. Similarly, a decline in globalisation can restrict many nation's access to skilled foreign labour, limiting their productivity and promoting the wastage of scarce economic resources which is detrimental to living standards.

21

(e) During 2018, US and China have entered into a trade war which has impacted the level of world trade. Demonstrate and explain how a tariff harms the importing country and discuss the impact on the exporting country. (6 marks)



A tariff is a tax on an imported good designed to give an artificial advantage to domestic producers. Before the tariff, the US manufacturing goods market was operating at WP where there is consumer surplus at A+B+C+D+E+F ~~and consume~~ and producer surplus at G. However, the implementation of a tariff had raised ~~[illegible]~~ WP to WP+t and US consumers suffer as a result of the increase in price reducing consumption to Q3 from Q4 and reducing consumer surplus to A+B. ~~But~~ US domestic producers gain from this ~~[illegible]~~ as they are able ~~to~~ to earn more revenue and sell a greater quantity at Q2 from Q1 increasing producers surplus to G+C. The US government gain revenue at E but there is DWL at D+F as the loss in consumer welfare was greater than the gain in producer and government welfare. As a result total welfare falls in the US as a result of the tariff. Other sectors in the US also suffer from facing higher input costs decreasing their international competitiveness. For the exporting country they face lower export revenues due to a decrease in imports US importing goods, and producers suffer. Consumers will also face costs as these tariffs lead to ~~an~~ increased trade barriers and loss in foreign relationships making costs higher for consumers. Decrease in trade for the exporting country may then lead to lower economic growth, and lower levels of employment within the exporting sector as a result.

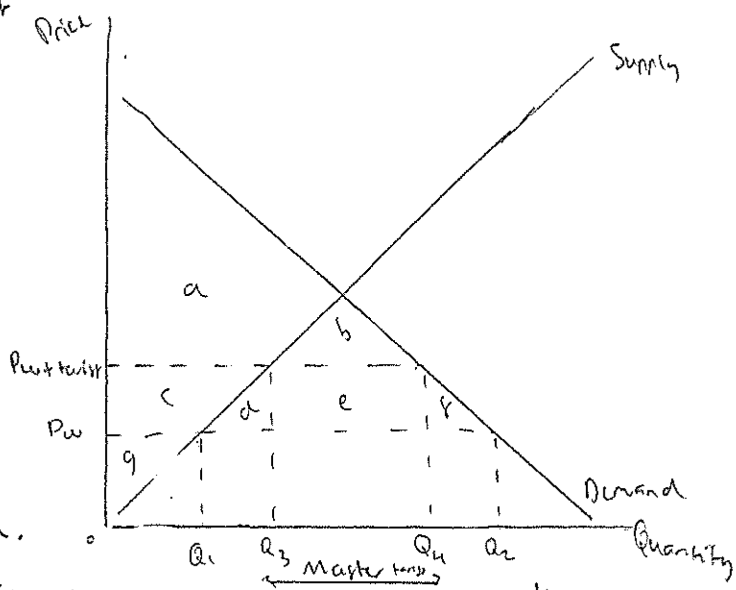
21

/ link to data. 10 An!

(e) During ~~2018~~, US and China have entered into a trade war which has impacted the level of world trade. Demonstrate and explain how a tariff harms the importing country and discuss the impact on the exporting country. (6 marks)

T ↑P ↓Q
ac.

Fig 1. Tariff on Imported Good



A tariff is an involuntary fee levied on imports by a government aiming to protect a specific domestic producer or industry. The US and China have been (in 2018) placing tariffs on each others goods, initially with Trump aiming to protect but consequently, with China retaliating with tariffs of their own. As seen in Fig 1, a tariff causes the price of the good to increase in the domestic market from Pw to Pw+tariff. This in turn, decreases the quantity demanded of the good from Q2 to Q4. Due to the increase in the goods price, imports decrease from Q1 → Q2 to Q3 → Q4 as consumers adjust their consumption, appeased by the rise in price. Therefore, the importing country's consumers lose from the tariff as the price increases and quantity consumed decreases. This is shown in Fig 1 from ~~a~~ decrease in consumer surplus from abcdef to just ab. ~~as~~ Importing country (domestic) producers in the importing competiting industries will benefit increasing their production from Q1 to Q3 and producer surplus from g to gc. However the importing countries economy as a whole will be negatively impacted as tariffs are inefficient, represented on the diagram with dead weight loss in areas d and f, illustrating loss in total welfare/surplus. Furthermore, domestic producers that are not protected by the specific tariff but may use it as an input for their production (US steel manufacturers will suffer greatly as their input costs increase over than their ~~pro~~

Continued at back

Supplementary page

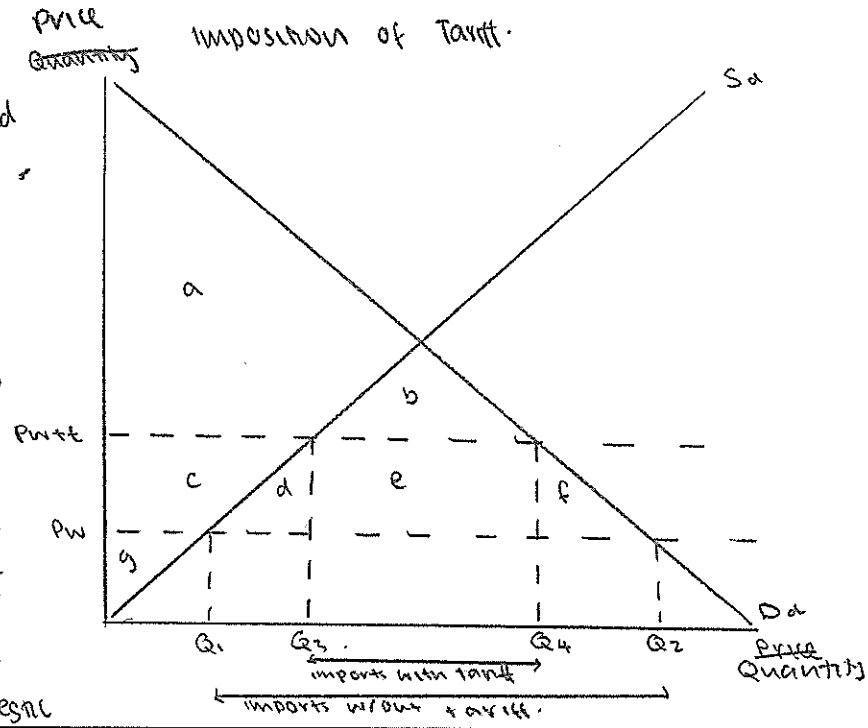
Question number: 21 e)

efficiency decrease - not - increase price of their final good so less competition. Finally, the importing country may be negatively impacted if the exporting country retaliates, as China did.

For the exporting country, the ~~dec~~ overseas (other country) demand for their goods will decrease as they cost more for overseas consumers thus depending on the price elasticity of their good, export volume will decrease. Thus it will have a negative effect on the exporting country too.

21.

(e) During 2018, US and China have entered into a trade war which has impacted the level of world trade. Demonstrate and explain how a tariff harms the importing country and discuss the impact on the exporting country. (6 marks)



A tariff is a tax imposed by the government on imported goods and services.

Without the tariff, imports quantity of the product is $Q_1 \rightarrow Q_2$, with domestic producers supplying $0 \rightarrow Q_1$. The tariff increases the price which the importing country has to pay - price rises from $P_W \rightarrow P_{W+t}$.

Due to the higher price, domestic consumption will fall, from Q_2 to Q_4. Consumers lose, with consumer surplus decreasing from area abcdef to area ab only. Domestic producers have been given an artificial advantage ~~and~~, with consumers surplus increasing from area g to area cg. ~~A~~ At P_{W+t}, domestic consumers now supply $0 \rightarrow Q_3$, and $Q_3 \rightarrow Q_4$ is imported. Area e represents the government revenue from the tariff. However area df represents the deadweight loss as a result of the implementation of the tariff. There has been a misallocation of resources, which creates inefficiencies in the importing country - the market has failed and the importing country is worse off.

The exporting country is also impacted negatively. Their exports to the ~~ex~~ importing country has decreased from Q_1Q_2 to Q_3Q_4. They face decreased export revenue : which can lower their trade balance, encourage their producers to reduce output - which can then negatively impact employment rates and incomes of those in the exporting sectors.

(c) Explain the impact of the trend described in part (b) on Australia's Trade Weighted Index. (2 marks)

The TWI is a multilateral exchange rate that measures movements of the AUD against a wide baskett of curries of Australias major trading partners. As the ToT increases there will be increased demand for the AUD. by Australian trading partners, thus the TWI will appreciate and the AUD will be worth more.

22.

(d) Explain how the current global crisis could affect Australia's terms of trade and discuss two effects of this change on the Australian economy. (6 marks)

The COVID-19 pandemic has increased global economic uncertainty, and significantly ~~b~~ decreased the economic growth of ~~at~~ all of Australias tradings partners, as their ~~ex~~ total output has decreased. This will cause a decrease in the demand for Australian exports and thus the terms of trade will decreases as XPI decreases relative to MPI. As total exports have decreased, total output in the Australian economy will decrease, and thus economic growth will decrease. As export firms such as the mining industry will contract as demand for their exports has decreased, which will cause an increase in unemployment rates in Australia as the export industry contracts. ~~It w This a~~ As demand for Australian exports has decreased, ~~there~~ demand for the AUD will also decrease. And thus there will be a depreciation in the AUD as the demand curve shifts left. This will reduce the level of consumption in the economy as imports ~~are less attractive as f~~ consumption decreases as they are now relatively more expensive. Thus, overall the COVID-19 will cause a ~~down~~ contraction in the Australian ~~eco~~ economy and decrease our terms of trade.

End of Section Two

22(d)

appreciating

(d) Explain how the current global crisis could affect Australia's terms of trade and discuss two effects of this change on the Australian economy. (6 marks)

The current global crisis is instilling a sense of both consumer and business inconfidence (is that a word? "decreasing confidence") meaning a lowered level of international trade and investment. Australia's terms of trade is heavily tied to commodity prices, which if decrease significantly as a result of the crisis* will lead to a decrease in the export price index, deteriorating the terms of trade. The import price index may also change as a result of the crisis, decreasing, but it is expected that it will not be as significant as the decrease XPI due to global supply shortages and general lack of global economic confidence. This deterioration of terms of trade has many effects on the Australian economy, primarily being the effects on Australian exports. If export prices decrease significantly, combined with the lack of demand (ie export volume), Australia's economic wellbeing suffers as less revenue is received from exports, decreasing aggregate expenditure/the trade balance and decreasing economic growth. Due to the decreased need for labour in export-orientated industries and other effects of the crisis, unemployment will increase as well. ~~Decreased demand for the AUD (from decreased to exports) will greatly/has greatly depreciated the currency~~

not a word

* due to decreased world demand

End of Section Two

(c) Explain the impact of the trend described in part (b) on Australia's Trade Weighted Index. (2 marks)

~~The TWI is a multilateral exchange rate calculated from a basket of currencies weighted according to their relative importance in Australia's trade flows. A rise in TOT would indicate export prices have risen relative to import prices. Given that our exports are predominantly inelastic, this would have led to a rise in export revenues in the short term,~~ increasing the demand for AUD and causing our TWI to increase

appreciate

22

(d) Explain how the current global crisis could affect Australia's terms of trade and discuss two effects of this change on the Australian economy. (6 marks)

The current global crisis has a significant impact on reducing aggregate demand and trade flows. This in turn, would ~~reduces~~ reduce the demand for Australia's exports as overseas economic growth is hindered, causing the XPI to decrease, presuming the TOT to decrease. In relation to Australian consumers, a ~~rise~~ fall in TOT indicates that the purchasing power of our exports fall, indicating that a reduced volume of imports ~~cannot~~ is obtained from a given quantity of exports. Given that consumers import based on comparative domestic disadvantage, this may reduce the living standards of Australian residents. ✓ Further, for Australia's inelastic resource industries, a fall in TOT will lead to a decrease in export revenue causing the resource sector to suffer. ✓ Subsequently, this is also likely to reduce the level of labour and capital resources attracted to this industry, reducing Australia's national income. ✓

End of Section Two

Question Answer: 23

a) Direction of trade: Australia's top 5 trading partners are China, Japan, United States, South Korea and Singapore. The direction of trade ~~is mainly due to the geographical~~ towards mainly East-east Asian countries is mainly due to their geographical proximity (reducing transport costs), free-trade agreements established with them (e.g. CHAFTA, KAFTA, JAEPA) as well as the relationship associated between Australia and developing countries. Developing countries or countries with an abundance of labour have a high demand for Australia's natural resources in order to feed their industries like manufacturing. On the other hand, Australia has a high reliance on these countries to provide manufactured goods as it has a comparative disadvantage in that, due to high wage costs and small amount of labour. Australia has good trade relations with the US for some of the same reasons, as well as political and historical relationships.

Pattern of trade: Australia's top 5 imports are ~~refined petroleum~~, personal travel services, refined petroleum, passenger motor vehicles, telecomm equipment and parts and crude petroleum. Our main imports thus include manufactured goods (which Australia has a comparative disadvantage in producing so it imports them), services/tourism (which has increased in importance due to the development of transport, reducing costs, and communication technologies, improving international relations) and fuels (used in Australia's ~~industries~~ capital-intensive industries that require fuel, such as mining).

Australia's top 5 exports are iron ore and concentrates, coal, natural gas, education related travel services and personal travel services. We export primarily natural resources as Australia is resource-endowed, and has a comparative advantage in producing those goods and supplying them to countries like China with a high demand for commodities. Education tourism is also a major import because of Australia's highly skilled and educated workforce and its attractive education system. Our relatively high wages are also attractive to those who may look to work in Australia after completing their studies. Tourism in general is a major export due to Australia's natural wonders which attract tourists, as well as improvements in technology which have made transport to Australia cheaper.

Question Answer: 23

Trade is quite significant to Australia and ~~makes up approximately~~
Australia has a relatively ~~high~~ low trade intensity. ~~This is primarily because~~
One reason for this is that Australian is a relatively medium-small
open economy, and is unable to achieve economies of scale like larger
economies such as the US, ~~without~~ without engagement in trade.
without trade, it also ~~to~~ will not have the same amount of competitiveness and its
associated benefits as the US would have ~~as~~ in its ~~dome~~ large
domestic economy. Australia is reliant on trade to provide it with the
goods/services that it does not have the capacity to produce, or is comparatively
disadvantaged in the production of. For example, Australia does not have the
~~an abundance~~ abundance of cheap labour that is ~~needed~~ needed for
a competitive manufacturing industry, ~~so it~~ ~~is not~~ but it is able to
supplement this by importing those goods from countries like China.
It also does not have the capacity to use all of its natural resources
, so Australia exports them, reaping the benefits of trade.

Please write out the whole word. Otherwise I'm just guessing what you are saying.

Question Answer: 23

a) Trade is the movement of goods and services across borders. Australia trades extensively with other countries, and recent globalisation has enabled Australia to grow extensively and vastly improve standards of living and economic welfare.

Australia's direction of trade is primarily directed towards other countries in the Asia-Pacific region. This can be explained by the fact that close geographic proximity results in lower transport costs, which in turn may result in higher ~~trade~~ ~~volumes of trade~~ levels of trade. Furthermore, many Asian countries like China, and India have large populations and thus require high ~~levels~~ volumes of primary commodities for infrastructure ~~energy and~~ and energy. Australia's top two way trading partners are China, Japan, US, South Korea and India. The US has a large population and and has close political ties with Australia, which may explain our economic trade with them. Australia's biggest export markets are China, Japan, and South Korea, and its biggest import markets are China, the US, and South Korea. ~~Australia~~

Australia's composition of trade reflects its comparative advantage in minerals, due to its natural resource abundance. With a ~~small~~ small and expensive labour force, Australia does not have a significant manufacturing sector, and instead tends to import final goods and services. Australia has an extensive services sector however, ~~as~~ with ~~personal~~ personal travel services and education ~~being~~ two of its biggest exports. Australia's agricultural sector is moderately significant, with exports of such goods as barley, however Australia's mineral sector is by far its biggest source of trade. ~~Also~~ This is reflected in the fact that Australia's top 5 exports are iron ore, coal, education, natural gas, and

Question Answer: 23

personal travel services, respectively. Iron ore and coal, are by far our biggest exports and are the main reason for Australia's trade balance surplus, due to large demand from such countries as China. Our service exports are also significant, due to foreign students coming to Australia to study, or foreigners coming to Australia for tourism. This is a result of Australia's ~~good reputation for education the~~ ~~too~~ good reputation of Australia's universities and its numerous tourist attractions. ✓

Australia imports goods that require labor, such as passenger motor vehicles and telecom equipment. Despite this, personal travel services are Australia's biggest import. This can be explained by the fact that Australian citizens have relatively high levels of economic welfare and standard of living and are thus able to travel overseas. Australia has a comparative ~~adv~~ disadvantage in the production of passenger motor vehicles and thus imports them heavily from countries like Japan. Australia's biggest imports are personal travel services, passenger motor vehicles, crude and refined petroleum, and telecom equipment and parts respectively. ✓

As a small, open economy, trade is extremely significant for Australia. The productivity commission has identified ~~trade as the biggy~~ increased trade over the last few decades as the single biggest ~~rega~~ reason for Australia's GDP growth, suggesting it may have expanded growth for as much as ~~8%~~ 7.5%. ✓ As a Australia has a small population, trade is significant for Australian producers in ~~allowing them to~~ giving them access to a much larger world market and allowing them to ~~expa~~ thus expand their production capacity to develop economies of scale. ~~UA~~ For example, Chinese demand for iron ore has allowed Australia's mining industry to grow significantly.

Question Answer: 23

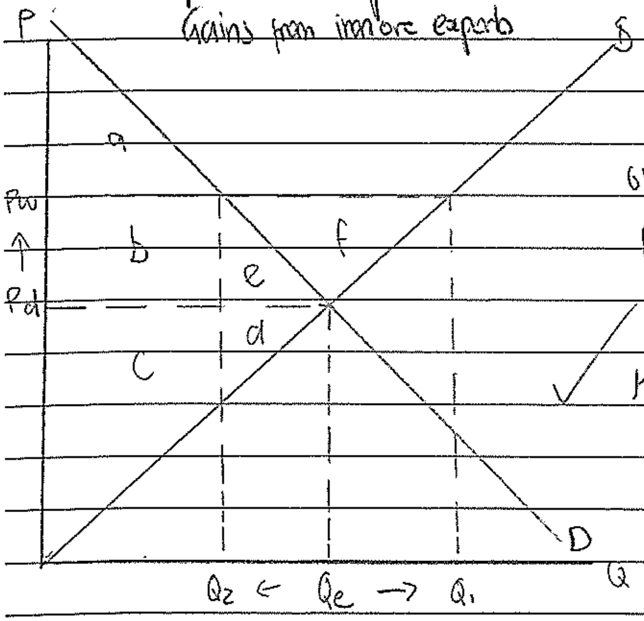
increasing domestic employment and national income, increasing GDP growth. Trade is also significant in that it ~~gives Aust~~ expands the market for domestic consumers allowing them to access a wider variety of goods and services at a lower cost. Trade has also put Australia in an advantageous ~~pos~~ political position on the world stage, due to the reliance of other countries on Australian commodities. Ultimately, trade has been very beneficial and significant for Australia, ~~giving~~, improving efficiency and allowing it to 'punch above its weight' by gaining an important international role, despite its small size

b) To explain the gains from trade, the concepts of absolute and comparative advantage must first be explained. Due to the large population of countries like China, they have an extensive labour force and a highly productive industry. Such countries may have an absolute advantage in the production of various goods and services. Absolute advantage refers to the level of output a country can produce ~~over a certai~~ of a certain good, given ~~a set~~ the same inputs. However ~~countries like~~ other countries ~~like~~ may have a comparative advantage over ~~such~~ these goods. ~~A~~ A comparative advantage refers to the ability of a country to produce a certain good/service at a lower opportunity cost than another country. ~~Although~~ Although China may have an absolute advantage over Australia in ~~in~~ iron ore for example, ~~there by~~ there would be a heavy opportunity cost for them producing iron ore, ~~would be sig~~ as they would foregoe the more effective production of another good/service. Instead, Australia has a comparative advantage in the production of iron ore due to its natural resource abundance of minerals.

The production of a par

Question Answer: 23.

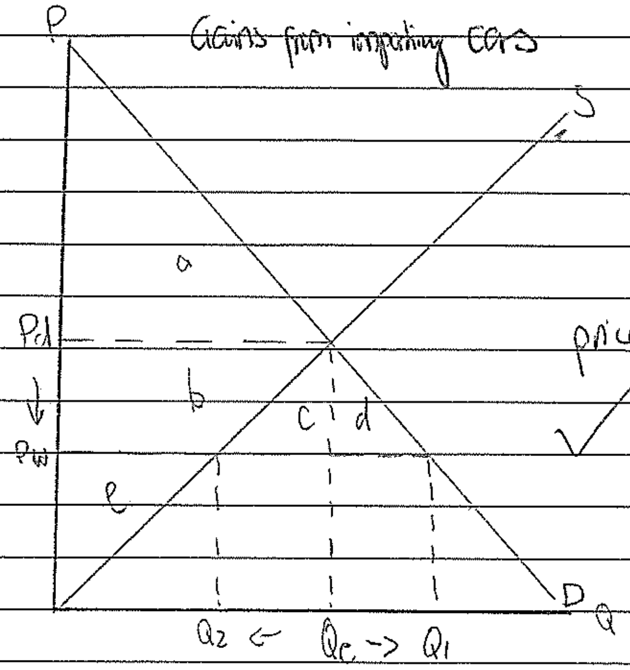
Accordingly, countries should ~~trade~~ specialise and trade to improve efficiency. Specialisation refers to the concentration of a country's productive capacity on the production of a specific variety of good or service. By specialising in the production of minerals like iron ore and coal, Australia has gained benefits from trade. Trade will ~~give~~ expand the market for domestic producers, ~~allowing~~ increasing demand and enabling them to increase their production capacity and gain higher revenues. Similarly, trade will benefit consumers by allowing them to ~~rec~~ receive ~~impo~~ ~~goo~~ imported goods and services for a cheaper price. These gains from specialisation are called static gains and can be demonstrated on an export and import diagram



As a result of Australia's comparative advantage in iron ore, it ~~is able~~ the domestic price Pd is lower than the world price Pw initially. However, by exporting this iron ore at the higher world price Pw. Accordingly, producers receive a higher price and expand their quantity produced from Qe ~~to~~ to Q2 due to the wider international market, with exports at QeQ1. Producer surplus has thus increased dramatically from a cd to cdbef, as their economic welfare increases. ~~Consumers~~ Domestic consumers will be slightly less well off, as they will have to pay a higher price Pw ~~with~~ a for a lower quantity Q2, resulting in consumer surplus decreasing minorly from abe to just a. However, the ~~benefit~~ increase in producer surplus is greater than the decrease in consumer surplus resulting in a net gain of total economic welfare at f. This is the ~~e~~ welfare gain from exports that demonstrates

Question Answer: 23

the increased efficiency of the ~~market as a~~ domestic market due to trade. ~~The~~ Imports will also benefit the domestic economy;



As a result of Australia's comparative disadvantage in the production of cars, the domestic price for cars ~~is higher than the~~ (Pd) is higher than the world price Pw, as costs of production are higher for domestic ~~cars~~ producers. By trading, and importing cars at the lower world price of Pw, consumers will benefit ~~greatly~~. ~~For cars~~ ~~The price~~ Due to imports, the price of cars has decreased for consumers from Pd to Pw, while they gain access to a wider market, increasing their quantity demanded from Qe to Q1. Thus, their consumer surplus has increased dramatically from ~~ab~~ a to abcd. Domestic producers will now have to compete with foreign producers thus reducing their market share from Qe to Q2 (as QeQ1 becomes imports). Thus producer surplus will dramatically decrease from be to e. However, ~~prod~~ the gain in domestic surplus outweighs this loss of ~~co~~ producer surplus, resulting in a net increase in total surplus at cd. Cd thus represents the efficiency and welfare gain from importing.

These static gains from trade will also lead to dynamic gains from trade. The increased competition due to the wider world market of consumers may increase efficiency, and will also lead to technological improvements ~~as~~ firms try to gain advantages over the other. This can be seen in the technological innovation caused by trade in Australia's solar energy sector, with a new \$20 billion project seeking to export solar energy.

Question Answer: 23.

to Singapore using new technologies, & beginning in 2019. Australian producers may also seek competitive advantages as a result.

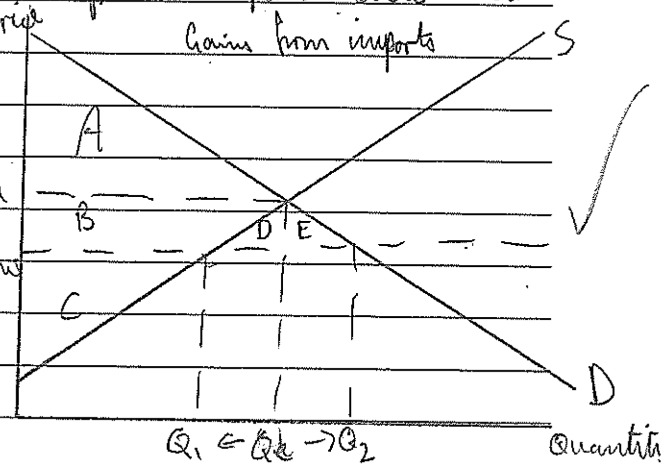
Other gains from trade include allowing ~~Aus~~ domestic producers to gain economies of scale. Increased demand from ~~for~~ ~~cheap~~ ~~ex~~ goods will allow producers to expand their production capacity which can in turn lead to rising employment and growth. This occurred in Australia's mining industry due to increased demand from China.

Finally, trade may allow countries to gain improved political relations with other countries they export to. Free trade with the US has allowed Australia to gain a strong diplomatic alliance with them. This may also have further economic benefits, with ~~Pres~~ Donald Trump excluding Australia from 2019 tariffs on steel, likely due to their strong political relationship.

Question Answer: 23 Part B

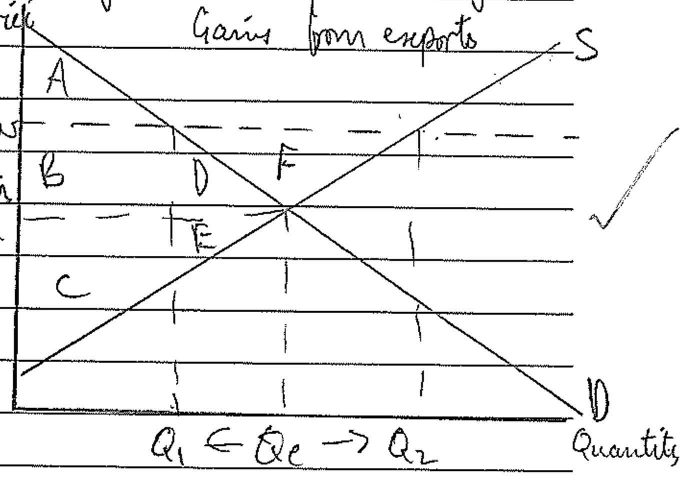
Trade is the import and export of goods and services, and gains from trade is the benefits to the economy that arise due to it engaging in trade. The gains from trade is made up of the static gains and dynamic gains. Static gains ~~are the~~ is the increase in the total welfare in the economy as a direct impact of an increase in allocative efficiency of resources. A dynamic gain is a benefit to the economy not directly due to the increase in efficiency. ✓

Static gains include the ~~benefit of~~ gains from imports and the gains from exports. When a country without comparative advantage engages in importing, it ~~com~~ operates at the lower world Price (Pw) rather than the domestic price (Pd). This causes Quantity demanded to increase from ~~Pe to P1~~ Qe to Q_2, and quantity produced falls from Qe to Q_1. Thus consumer surplus increases from A to A+B+D+E (increase by B+D+E). Producer surplus decreases from B+C to C (decrease by B). Thus as the decrease in total surplus is less than the increase, total surplus increases from A+B+C to A+B+C+D+E.



✓

When a country with comparative advantage starts to export, then it gets access to the higher Pw rather than the low Pd. Thus price rises from Pd to Pw. Due to this, quantity demanded from domestic consumers decreases from Qe to Q_1 and quantity produced increases from Qe to Q_2. Thus consumer surplus ~~increases~~ decreases from A+B+D to A (decrease by B+D). and producer surplus increases from C+E to B+D+C+E+F (increase by B+D+F). Therefore total surplus increases by F.



✓

Question Answer: ______________________

Aside from this, dynamic gains from trade include: Higher competition, Larger variety of goods for consumers, as well as ~~[illegible]~~ economies of scale.

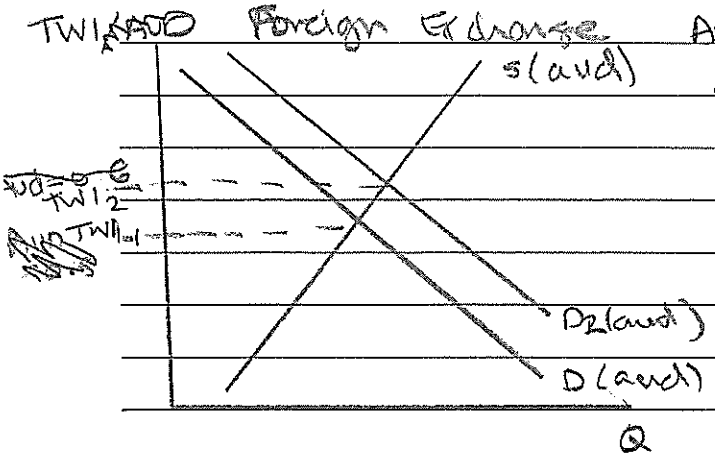
Due to the fact that domestic firms now have to compete with international firms, to survive they must innovate and make themselves more internationally competitive so that they can compete and lower their prices to match international standards ~~without~~ without going into loss. This improves our international competitiveness. E.g. Engaging in international trade has allowed us to invest into better mining equipment so that we can profit more from our ~~As we are importing foreign goods~~, commodities.

As we are importing more goods the consumers have a larger variety of goods to choose from. Means that consumers can choose to buy a product which is better suited to them and so consumers are better off. E.g. If we didn't engage in trade the only brand of car that would be available to us would be holden. Due to trade we now have access to superior brands such as Toyota.

When we specialize in an industry and then trade, it allows us to obtain economies of scale since we produce more of the same good. This is when the fixed costs of production is spread across a larger number of goods such that the price for each unit of ~~[illegible]~~ product is greatly decreased. This increases our international competitiveness.

Question Answer: 24 A

The trade weighted index is an exchange rate and a currency measure which ~~weighs~~ judges the price of the AUD in ~~relation to~~ terms of a basket of weighted currencies of its top trading partners. The partners currencies are weighted according to their significance in Australias trade. Some of the countries currencies included are the Chinese Yuan, Japanese Yen, and the US dollar. If the TWI improves, then the AUD has appreciated in relation to ~~its~~ the currencies of its major trading partners and vice versa. Four key factors affecting the movement of the TWI include; world economic growth, Australias domestic growth, the interest rate differential and movements in the terms of trade. *



An increase in world economic growth would increase the demand for Australias commodity exports as ~~industries~~ countries attempt to expand their economies. This would cause an increase in the demand for AUD, shifting it from D to D2 as they would require more AUD to purchase our exports, and hence would cause an increase in the value of the TWI from TWI1 to TWI2, causing a movement in the TWI upward.

* the TWI accounts for 90% of our top trading partners, of which 80% are from the asia pacific region.

Question Answer: 25a.

Foreign investment refers to the cross border movement of finance associated with the borrowing, lending, the purchase and sale of assets. Foreign investment transactions involve changes in the level of foreign assets and foreign liabilities. Foreign assets is Australia's investment abroad. This includes the purchase of foreign assets and lending money to overseas residents. Foreign liabilities refers to foreign investment into Australia, and can be classified as either foreign equity or foreign debt. Foreign equity is the foreign ownership of Australian assets. It increases when foreign residents purchase Australian assets such as land. Foreign debt refers to the total borrowings of Australia's public and private sectors. About 25% of Australia's foreign debt is sovereign (government) debt. Foreign debt is much more preferred by Australians as it is a much more prudent and flexible approach than selling assets. Australia has much more foreign liabilities than foreign assets, meaning that there is more foreign investment in Australia than there is foreign investment abroad.

Foreign direct investment (FDI) covers foreign financial transactions to fund new investment in Australia. It involves a foreign resident or firm purchasing or controlling share (at least 10%) of an Australian company. It is classified as foreign debt. It is undertaken with the objective to obtain a lasting interest in the company and allows the investor to exercise a significant degree of influence over the management of the company.

One of the main benefits of FDI to the Australian economy is that it helps to fund Australia's saving-investment gap. It helps to fund a higher level of investment than would otherwise be possible and hence increases the level of economic growth possible. Another benefit is that FDI and multinational corporations (MNCs) provide a channel through which knowledge and technology is transferred, thus encouraging the transfer of technology and potentially bringing managerial expertise. This can increase Australia's efficiency, making Australian industries more internationally competitive. FDI also creates new jobs, thus increasing employment and income. It increased income along with the establishment of MNCs increases taxation revenue, which the government can spend on public and merit goods, which benefit a large section of the society. FDI also allows countries to exploit comparative advantages, by increasing production capacity in those industries.

However, FDI also has many costs to the Australian economy. One cost is the loss of

Question Answer: 25a.

ownership and control, reducing economic sovereignty. Decisions affecting Australia's economy could be made overseas, and may potentially go against Australia's economic goals and policies. Another cost is that it results in an outflow of dividends and profits, which could've otherwise remained in the Australian economy. Another cost is potentially bad behaviour by MNCs. MNCs have been associated with a numbers of areas of bad practice such as tax evasion and employing foreign workers. FDI also increases the vulnerability of the Australian economy to external shock, due to the heavy reliance on foreign funds.

Question Answer: 25b.

The balance of payments is a systematic record of all the economic transactions between ~~Aus~~ the residents of Australia and the residents of the rest of the world. It is composed of the current account and the capital and financial account. An increase in foreign investment into Australia in the form of foreign liabilities is recorded as inflows (credits) in the financial account, either through the foreign direct investment or portfolio investment accounts. The financial account records money flows ~~into~~ that result from a change in ownership of Australia's foreign financial assets and liabilities. All foreign liabilities have servicing costs - foreign equity requires the payment of dividends and foreign debt requires interest payments. These servicing costs are recorded as outflows (debits) in the current account. The current account records money flows associated with the imports and exports of goods and services, income flows and non-market transfers. Specifically, they are recorded in the net primary income account of the net income account, under investment income. The net primary income account records the income earned and paid to and from overseas residents. ~~The~~ Investment income records income earned from the provision of financial capital or foreign investment. It makes up 90% of the net primary income account. Australia has a savings-investment gap due to its high level of ~~de~~ investment. Therefore, Australia relies on foreign investment to fund its investment. This means that there will always be inflows on the financial account and an outflow of the current account. ~~Thus~~ The net primary income account is always a large deficit as a result of this savings-investment gap. The balances on the current account and the capital and financial account will always balance - ~~they must~~ they sum to zero.