



Tanna Moutono

Very well researched Tanna! You clearly have an excellent understanding of factors affecting the SA.

well done

Issue Study

AT

Subject:

Economics

Task No.

7

Final date for submission:

Monday 29th July 2013

Task:

Issue Study (approx. 1,500 words)

Choose one current Australian macroeconomic issue (E.g. the federal budget, potential interest rate increases/decreases, the currently decreasing value of the \$A). You are required to analyse and evaluate its effect on the Australian economy. In doing this, you should include the following:

- Consider a variety of perspectives on the issue
- Use correctly referenced current news articles
- Use correctly labeled diagrams to assist in showing what has happened and its effect on the economy
- Analyse and evaluate the effects of this issue on
 - Individuals
 - Business
 - Government

Be sure to include references as footnotes.

Depreciating value of the Australian dollar: effects on individuals, businesses and the government

The currently decreasing value of the Australian dollar has had a number of effects on individuals, businesses and the government within the Australian economy. The dollar has been pushed down due to a number of reasons including the economic recovery of the United States, lower interest rates, low investor sentiment, a bad outlook on Chinese manufacturing data, a fall in commodity prices, lower GDP growth figures and weak consumer sentiment figures. This has had a number of positive and negative effects on businesses, individuals and the government within the Australian economy. In a positive light, the lower Australian dollar has resulted in boosted domestic output, (as export prices are more attractive), increased profits for Australian based manufacturers as a result of the relatively high import costs, an expected increase for the tourism industry and the potential for a sooner rise to surplus (as the low dollar results in a higher budget deficit).² Negatively, the rapidly depreciating dollar has caused economic instability and as a result low confidence and a decreased standard of living. Predictions have been made that unemployment will increase and more interest rate cuts will occur, which is good for mortgage owners, but extremely negative for the economy. The Australian economy has been affected in many ways due to the rapidly depreciating value of the dollar.

The US economic recovery¹ has played a significant role in lowering the value of the Australian dollar. Positive economic data from the United States has meant that the US dollar has "rally [rallied] against all major currencies", while the Australian dollar has fallen, making the impact of the depreciated dollar even stronger when compared against the strong US dollar². The position of the US dollar is currently so favourable that the US Federal Reserve has released information that the central bank will begin to slow down its stimulus program³. The strong US dollar means that the relative value of the Australian dollar has decreased, and it is predicted that if the US stimulus measures are slowed, the Australian dollar may begin to rise slightly in value again⁴.

Lower Australian interest rates have served to lower the value of the Australian dollar. As of May 2013, the cash rate as set by the Reserve Bank of Australia was at the lowest level on record, 2.75 per cent⁵. Lower interest rates result in depreciation of the Australian dollar value because they cause overseas investors to receive lower returns on their investment in comparison with other

¹ News.com.au, 2013, *Stock markets, dollar plunge following news from US, China*, <http://www.news.com.au/business/markets/stock-markets-dollar-plunge-following-news-from-us-china/story-e6frfm30-1226667496333>, acc. 22 June 2013

² News.com.au, 2013, *\$A weakens as sellers expect rate cuts*, <http://www.news.com.au/business/breaking-news/a-weakens-as-traders-see-us-fed-pare-back/story-e6frfkur-1226666033637>, acc. 22 June 2013

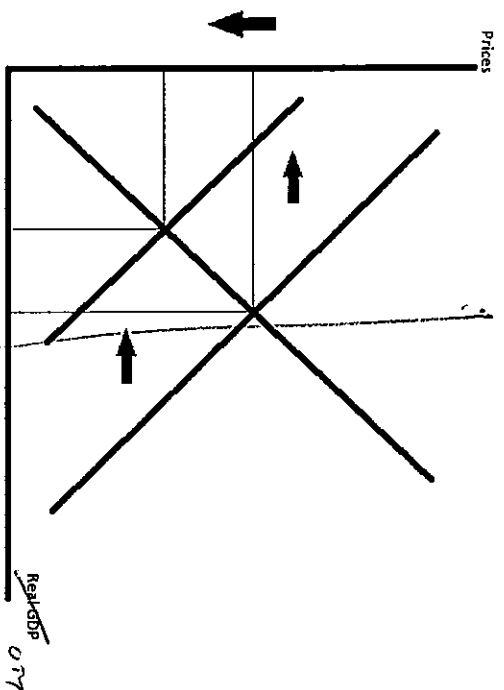
³ News.com.au, 2013, *US dollar soars on news over Fed action*, <http://www.news.com.au/business/breaking-news/us-dollar-soars-on-news-over-fed-action/story-e6frfkur-1226667269763>, acc. 22 June 2013

⁴ News.com.au, 2013, *\$A higher ahead of big central bank week*, <http://www.news.com.au/business/breaking-news/a-opens-weaker-following-falls-on-wall-st/story-e6frfkur-1226664807704>, acc. 22 June 2013

⁵ Exchange Rates, US Dollar | News.com.au, 2013, *AUD down and set to stay*, <http://www.news.com.au/business/australian-dollar/dollar-falls-to-11-month-low/story-fn6t6wad-1226644935603>, acc. 22 June 2013

companies. This decreases demand by overseas buyers for the Australian dollar. Lowered interest rates also result in lowered inflation, and hence a lowered exchange rate⁵.

Effects of lowered interest rates on overseas demand for the Australian dollar



The Australian dollar has also depreciated as a result of average domestic economic data and poorer gross domestic product growth figures than initially expected. During June, the Commonwealth Bank reported that the “Australian dollar fell following the release of gross domestic product (GDP) data” that day. The Australian Bureau of Statistics showed that GDP grew less than the expected 0.8% rate that had been predicted, growing only by 0.6% in the March quarter⁷. Meanwhile, traders are continuing to sell the Australian dollar “in the absence of any good news on the local economy”. The value of the dollar is being weakened as it is still being sold despite low demand for Australian resources⁸. The bad situation of the Australian economy at present is another factor causing the Australian dollar to depreciate.

One of the largest influences for the depreciating Australian dollar is the slower growth in China as a result of weak manufacturing data. The figures released recently have shown a bad outlook for the Chinese economy⁹, and this is affecting Australia too. Reports have shown that China’s manufacturing activity is at present the lowest it has been in nine months. This has had a heavy toll on Australia’s resource companies, which are already at present performing badly¹⁰.

⁵ Webster, N, 2007, *Economics Key Ideas SACE Stage 2 Third Edition*, Essentials Textbooks Adelaide Tuition Centre, Adelaide, Australia

⁷ Exchange Rates, US Dollar | News.com.au, 2013, *Dollar lower after GDP data*, <http://www.news.com.au/business/australian-dollar/dollar-lower-after-gdp-data/story-fn6twad-1226557467627>, acc. 22 June 2013

⁸ News.com.au, 2013, *SA weakens as seller's expect rate cuts*, <http://www.news.com.au/business/breaking-news/a-weekens-as-traders-see-us-fed-pare-back/story-e6frfkur-1226660336337>, acc. 22 June 2013

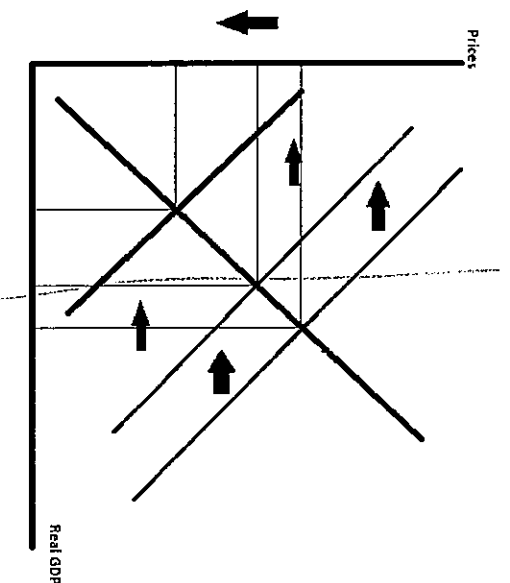
⁹ US dollar soars on news over Fed action; Exchange Rates, US Dollar | News.com.au, 2013, *AUD down and set to stay*, <http://www.news.com.au/business/australian-dollar/dollar-falls-to-11-month-low/story-fn6twad-1226644935603j>, acc. 22 June 2013

¹⁰ News.com.au, 2013, *Stock markets, dollar plunge following news from US, China*, <http://www.news.com.au/business/markets/stock-markets-dollar-plunge-following-news-from-us-china/story-e6frfm30-1226667496333>, acc. 22 June 2013

A recent fall in the prices of commodities such as iron ore has resulted in the Australian dollar remaining low and out of demand. In addition to the recent decrease in commodity prices, further falls are expected, which will only result in lowered demand¹¹.

The depreciating value of the dollar has decreased the reasons why investors would want to buy the Australian dollar, particularly causing lower investor sentiment¹². This has put further pressure on the dollar and will lead to the exchange rate falling even further. Rate cuts by the Reserve Bank of Australia have led to the lowest ever interest rates recorded in Australia. This means overseas investors are receiving less from investment in Australia than what they could receive from investment elsewhere, decreasing the amount of investment in Australia (and hence decreasing aggregate demand as investment is a component of total expenditure). The result of this is a rapid and continuous decrease in demand, which is resulting in depreciation of the dollar¹³.

Effects of continuously decreasing demand on the Australian dollar (low investment)



Weak sentiment data is yet another factor which has resulted in the lower Australian dollar. The results of the Westpac/Melbourne Institute May consumer sentiment survey showed that there was a general pessimistic attitude amongst people regarding the economy. This attitude was largely attributed to concerns over the Australian economy at present, and in particular following the release of the Federal Budget. Directly following this data release the Australian dollar dropped to 97.82 US cents¹⁴.

¹¹ The Australian, 2013, *Battered dollar expected to keep falling*,

<http://www.theaustralian.com.au/business/markets/battered-dollar-expected-to-keep-falling/story-ef6rg916-1226668461306>, acc. 24 June 2013; Exchange Rates, US Dollar | News.com.au, 2013, *AUD down and set to stay*,

<http://www.news.com.au/business/australian-dollar/dollar-falls-to-11-month-low/story-fn6t6wad-12266449356031>, acc. 22 June 2013

¹² McKenna G. and Llewellyn-Smith, D., 2013, *How low can the Aussie dollar go?*,

<http://www.theage.com.au/business/how-low-can-the-aussie-dollar-go-20130624-2os8k.html>, acc. 24 June 2013

¹³ Webster, N., 2007, *Economics Key Ideas SACE Stage 2 Third Edition*, Essentials Textbooks Adelaide Tuition Centre, Adelaide, Australia

¹⁴ Exchange Rates, US Dollar | News.com.au, 2013, *Dollar falls after weak sentiment data*,

<http://www.news.com.au/business/australian-dollar/dollar-lower-awaiting-bernanke-testimony/story-fn6t6wad-1226648048959>, acc. 22 June 2013

The depreciating Australian dollar has had many effects on the Australian government, as well as businesses and individuals within the economy as well. Some of these are positive effects.

The depreciating value of the Australian dollar has had a number of positive effects on Australian businesses. The lowered dollar has meant that export prices in Australia are more attractive for overseas buyers. This has had substantial benefits for the domestic economy and particularly business owners such as farmers and winemakers. The Australian dollar has also caused import prices to rise meaning that Australian-based manufacturers are earning even more as the relative cost makes imports less attractive. Companies that compete overseas will be selling their products at lower prices, making them more attractive and hence selling more. Companies that operate significantly overseas will also stand to gain as their repatriated profits will be increased. The tourism industry in Australia also stands to benefit from the low Australian dollar, as holidays to areas in Australia are cheaper. The tourism industry was struck heavily by the high Australian dollar, which means that the depreciation will be extremely good for that area of the economy¹⁵. Holidays in Australia will become cheaper relative to other countries, meaning that tourist-based companies and attractions will be more popular. Many Australian businesses, particularly businesses that export overseas, stand to gain from the depreciating Australian dollar¹⁶.

The depreciating Australian dollar has and will have positive effects for the Australian government. As travelling to Australia will become relatively cheaper, overseas students will be more likely to travel to Australia for education. Whilst this is a major boost to higher education institutions, it also impacts Australia positively as a whole, as more money to the institutions ensures a better educated workforce and increases the impact made by citizen contribution¹⁷. The lower Australian dollar also increases the likelihood that the Australian economy will return sooner to surplus, as the higher Australian dollar was partially responsible for the high budget deficit¹⁸, which was negatively impacting the economy as it resulted in lowered confidence figures. The Australian government has been positively impacted in some ways from the depreciating Australian dollar.

The rapidly depreciating dollar has resulted in a number of negative outcomes on individuals within the Australian economy. The speed at which the exchange rate has fluctuated has reduced consumer confidence, causing individuals to become wary in how they spend, invest and work¹⁹. In addition to this the unemployment rate has been predicted to rise from 5.5% to 5.6% over one

¹⁵ Exchange Rates, US Dollar | News.com.au, 2010, *FAQ: Winners and losers from the high Australian dollar*, <http://www.news.com.au/business/australian-dollar/faq-winners-and-losers-from-the-high-australian-dollar/story-fn6t6wad-1225939013600>, acc. 22 June 2013

¹⁶ Exchange Rates, US Dollar | News.com.au, 2010, *FAQ: Winners and losers from the high Australian dollar*, <http://www.news.com.au/business/australian-dollar/faq-winners-and-losers-from-the-high-australian-dollar/story-fn6t6wad-1225939013600>, acc. 22 June 2013; *three reasons the falling \$A is good news*

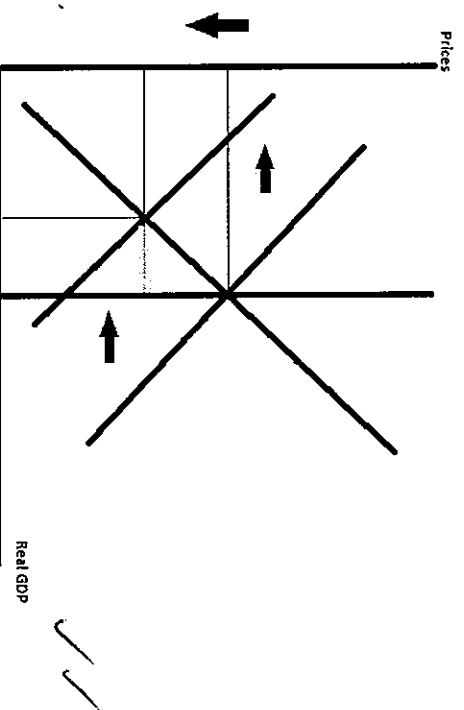
¹⁷ Exchange Rates, US Dollar | News.com.au, 2010, *FAQ: Winners and losers from the high Australian dollar*, <http://www.news.com.au/business/australian-dollar/faq-winners-and-losers-from-the-high-australian-dollar/story-fn6t6wad-1225939013600>, acc. 22 June 2013

¹⁸ Exchange Rates, US Dollar | News.com.au, 2013, *Budget fails to dent Aussie dollar*, <http://www.news.com.au/business/australian-dollar/a-opens-below-parity-on-weak-china-data/story-fn6t6wad-1226641554143>, acc. 22 June 2013; *Exchange Rates, US Dollar | News.com.au, 2013, Dollar weaker at noon after deficit*, <http://www.news.com.au/business/australian-dollar/dollar-weaker-as-wall-st-helps-greenback/story-fn6t6wad-1226642662963>, acc. 22 June 2013

¹⁹ Webster, N, 2007, *Economics Key Ideas SAGE Stage 2 Third Edition, Essentials Textbooks Adelaide* Tuition Centre, Adelaide, Australia

month, resulting in as many as 10,000 more people without jobs²⁰. Conveniences such as buying online and buying imported materials such as electronics will also decrease as the relative cost will increase. Overseas holidays will increase in price²¹. The combination of these factors and many more will result in ultimately a lower standard of living, caused by deflation.

Unemployment rate (highlighted) increases due to depreciating dollar, affecting individuals



The depreciating dollar has also had a number of effects on the Australian government. The Reserve Bank of Australia has already decreased the cash rate to the lowest level recorded in Australia ever, 2.75 per cent²². The RBA may however, be forced to create more interest rate cuts to an even lower percentage. Although the RBA is independent of the government, the lower interest rates will result in bad effects on the Australian economy in many different respects²³. The government has also been forced to delay the return of surplus until at least 2015/16, as an \$18 billion budget deficit was announced for 2013/14²⁴. This has resulted in even lower confidence in the economy.

²⁰ Exchange Rates, US Dollar | News.com.au, 2013, *Dollar recovers from big overnight fall*, <http://www.news.com.au/business/australian-dollar/dollar-recovers-from-big-overnight-fall/story-fn6t6wad-1226662217004>, acc. 22 June 2013

²¹ Exchange Rates, US Dollar | News.com.au, 2010, *FAQ: Winners and losers from the high Australian dollar*, <http://www.news.com.au/business/australian-dollar/faq-winners-and-losers-from-the-high-australian-dollar/story-fn6t6wad-1225939013600>, acc. 22 June 2013

²² Exchange Rates, US Dollar | News.com.au, 2013, *AUD down and set to stay*, <http://www.news.com.au/business/australian-dollar/dollar-falls-to-11-month-low/story-fn6t6wad-1226644935603>, acc. 22 June 2013

²³ News.com.au, 2013, *\$A weakens as sellers expect rate cuts*, <http://www.news.com.au/business/breaking-news/fa-weakens-as-traders-see-us-fed-pare-back/story-e6fftkur-1226666033637>, acc. 22 June 2013; Exchange Rates, US Dollar | News.com.au, 2013, *Dollar weakens after RBA signals rate cuts*, <http://www.news.com.au/business/australian-dollar/dollar-weakens-after-rba-signals-rate-cuts/story-fn6t6wad-1226665397205>, acc. 22 June 2013

²⁴ Exchange Rates, US Dollar | News.com.au, 2013, *Dollar weaker at noon after deficit*, <http://www.news.com.au/business/australian-dollar/dollar-weaker-as-wall-st-helps-greenback/story-fn6t6wad-1226642662963>, acc. 22 June 2013

Businesses that import from overseas have been most negatively impacted by the depreciating value of the dollar. As the dollar depreciates it becomes more expensive to buy overseas, meaning that companies using imported capital resources will have increased costs²⁵.

The rapidly depreciating value of the Australian dollar has resulted in many effects on the Australian economy. Australian businesses, individuals and the government body have faced positive and negative effects as a result of many factors affecting the exchange rate.

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²⁵ Exchange Rates, US Dollar|News.com.au, 2010, *FAQ: Winners and losers from the high Australian dollar*, <http://www.news.com.au/business/australian-dollar/faq-winners-and-losers-from-the-high-australian-dollar/story-fn6t6wad-1225939013600>, acc. 22 June 2013

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