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Trade Surplus Hits 40-Year High as Commodity Prices and Volumes Rise

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Higher commodity prices are making a significant impact on the broader Australian economy, including GDP growth and trade.

Once again Australian data illustrated the dramatic impact of higher commodity prices on the broader economy.

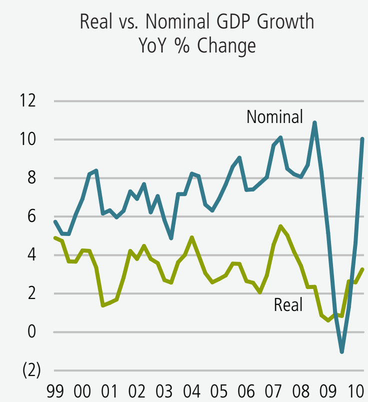
Second-quarter real GDP growth was a stronger-than-expected 1.2% quarter on quarter (non-annualized), taking year-on-year growth to 3.3%. The strength of spending was spread fairly evenly. For example:

- Household consumption spending rose 1.6%—the strongest reading since mid-2007—with the services sector again garnering an increased share of the consumer's purse. The figures, along with July's firmer-than-expected retail numbers, are consistent with our thesis that consumption growth should be solid through the second half of 2010 (see "Is the Australian Consumer Spending Slowdown an Illusion?" *Australasian Economic Update*, August 10, 2010).
- Nonresidential construction spending (+2.0%) and housing construction (+5.0%) rose in the quarter, and the pipeline remains strong for both areas—particularly for mining-related projects.
- Trade volumes were strong, with imports up 3% and exports up 5.6%. A large part of the export story reflects the mining sector, with resource export volumes up 11.6% in the quarter. The mining capital expenditure up-swing—now into its eighth year—is finally feeding through to better trade performance.

For all the focus on real GDP figures, perhaps the best illustration of the impact of higher commodity prices can be seen in nominal GDP. The rise in the terms of trade has been driving a wedge between nominal and real GDP growth for more than a decade. That wedge has had little to do with domestically driven inflation, which has averaged 2.6% a year over the last 10 years; instead, it has been an effect of export prices. The wedge was much in evidence during the quarter: while real GDP rose a modest 3.3% year on year, nominal GDP increased by a whopping 10% **(Display 1)**, helped by a 17% rise in export prices and a 6% fall in import prices over the year.

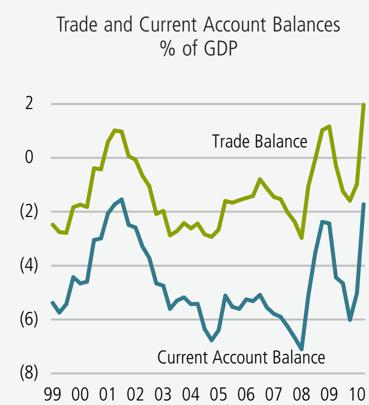
These relative price trends—in combination with increases in volumes—have caused a big turnaround in Australia's trade

Display 1
Nominal GDP Growth Back at 10%



As of August 2010
Source: Australian Bureau of Statistics

Display 2
Dramatic Trade Reversal



As of August 2010
Source: Australian Bureau of Statistics

position. The second-quarter trade surplus was 2% of GDP—the biggest since the early 1970s and a five percentage point reversal from the 3%-of-GDP deficit in early 2008. In turn, the current account deficit has contracted to just 1.7% of GDP from 7.1% at the start of 2008 **(Display 2)**. The boost in export prices effectively represents a big increase in real purchasing power for domestic residents. The Australian Bureau of Statistics tries to take this purchasing power impact into account by calculating Real Net National Disposable Income, which may be characterized as a broad measure of national well-being. It rose 5% in the quarter, or 9.5% over the past 12 months (compared with the 3.3% rise in GDP). No wonder Australians seem relaxed about the fact they still have no government—almost two weeks after a federal election! ■