

Box A: Developments in World Trade

After only modest growth initially following the 2001 global recession, international trade in goods and services has rebounded strongly of late, increasing by about 10 per cent in 2004, or approximately double the rate of growth in world GDP (Graph A1). In large part, this reflects the tendency for trade to fluctuate by more than output. However, it also reflects the consequences of ongoing trade liberalisation, and changing demand for final goods and factor inputs as economies develop. The recovery in world trade has been propelled mainly by China and other

east Asian economies, which are becoming increasingly engaged in international commerce (Table A1), and to a lesser extent other emerging economies. While accounting for only 5 per cent of world trade, China contributed approximately 15 per cent of the increase in trade in 2004 and became the world's third-largest merchandise exporter. In contrast, the G7 industrialised countries, despite accounting for nearly half of world trade, contributed only around a third of the increase in 2004.

The uneven contributions to growth in world trade in part reflect divergences in economic growth across regions. Hesitant demand growth in the euro area explains the modest growth

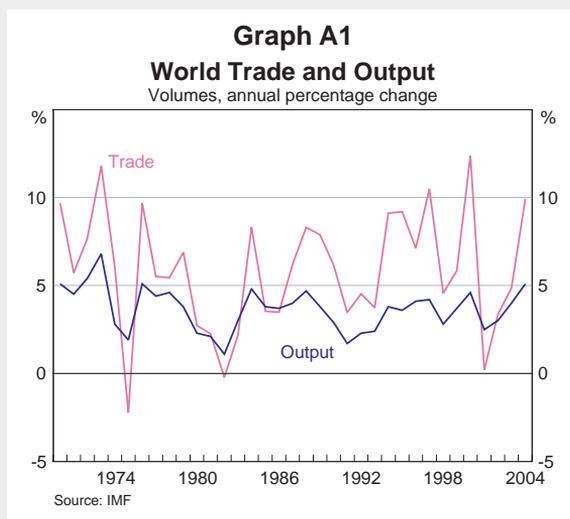


Table A1: World Trade of Goods and Services

Volumes, per cent^(a)

	World trade share	Annual export growth		Annual import growth	
		2003 ^(b)	2003	2004	2003
G7	46	1.3	7.2	3.2	7.5
United States	14	1.9	8.5	4.4	9.9
Euro area ^(c)	31	0.1	5.8	1.8	6.0
Japan	5	9.1	14.4	3.8	8.9
China	5	27.7	28.8	22.2	28.3
Other east Asia ^(d)	11	11.1	16.1	7.0	15.4

(a) Aggregates weighted by GDP at PPP exchange rates unless otherwise specified

(b) Per cent, based on US dollar values

(c) Includes intra-euro area trade

(d) Weighted using market exchange rates

Sources: CEIC; IMF; RBA; Thomson Financial; World Bank

of export and import volumes in the region, since intra-regional trade accounts for around two-thirds of the area's total trade.¹ In the United States, trade has been expanding somewhat faster, as strong domestic demand has induced ongoing growth in imports; exports have also staged a recovery, though not one that has been sufficient to arrest further widening of the trade deficit. Japan has seen yet stronger trade growth, with its trade surplus continuing to swell, underpinned by strong demand for its exports from the rest of Asia; most notably, its exports of intermediate and capital goods to China have been growing rapidly.

The east Asian region (excluding Japan) has undoubtedly recorded the most impressive trade performance. The surge in demand for ITC goods in 2003–2004 boosted the region's exports of manufactures, while the region's imports have accelerated as China increasingly calls on the rest of the world for raw materials to satisfy its ongoing process of industrialisation. There has also been a substantial change in the pattern of east Asian trade, with intra-regional trade growing in importance. In 2004, 37 per cent of east Asian merchandise exports went to economies elsewhere in the region, up from around 33 per cent five years earlier. This shift has been fuelled not only by increased final demand within the region, particularly from China, but also by a reorganisation of production processes into regional networks. Goods are increasingly being assembled in China from parts sourced elsewhere in the region, and then exported to developed countries. This largely explains why China has recorded growing trade surpluses with the US and Europe, but trade deficits with the rest of Asia.

The pattern of global trade has had major implications for the prices of traded goods and services. The emergence of China as a major producer has put downward pressure on the world price of manufactures. On the other hand, China's seemingly insatiable appetite as an importer of raw materials has contributed to the surge in world commodity prices, including oil. Consequently, commodity importers, such as east Asia, Japan and the United States, have experienced a deterioration in their terms of trade. In contrast, the rise in world commodity prices has been beneficial for commodity exporters, such as Australia and Canada, and a number of countries in Latin America and the Middle East.²

The strength of world trade and the shift in trade patterns can also be seen in global shipping freight rates, as shipping still accounts for around two-thirds of the value of all international goods transportation. In line with the pick-up in commodity demand, the Baltic Dry Index, which tracks freight prices for dry bulk goods, has soared to unprecedented levels over the past two years (Graph A2). Unsurprisingly, the pick-up in freight rates has been especially concentrated on trade routes to Asia, and the ports along these routes have become increasingly congested. Conditions are generally expected to remain tight, in part due to short-run inelasticity in the supply of ships and continued strong world activity.

As with GDP growth, world trade activity is expected to ease, but remain healthy. The IMF projects world trade to grow by 7.4 per cent in 2005. However, the recent trend of

1 Within the region, however, there have been some areas of strength. Exports have grown strongly in Germany, which has seen a more pronounced decline in its unit labour costs and faces limited competition for its exports from emerging Asian economies; in fact, Germany has also now overtaken the US to become the world's largest merchandise exporter. The euro area's import growth has been led by France and Spain, where domestic activity has been more buoyant.

2 See the article on 'Commodity prices and the terms of trade' in the RBA Bulletin, April 2005, for a more detailed discussion.

greater involvement by emerging economies in international commerce is set to continue, with China and other east Asian economies likely to account for a growing share of world trade. This can be expected to have a positive influence on the Australian economy in coming years, given Australia's proximity to the east Asian region and the strong trade links that have been cultivated with it over the past decade or so. ✎

