**Economics Year 11 Exam Semester 2, 2019**

**Marking Guide - UNIT 2**

**Section 1 (24 marks)**

1 a

2 c

3 b

4 b

5 b

6 a

7 b

8 d

9 d

10 b

11 c

12 a

13 B

14 C

15 D

16 A

17 A

18 D

19 B

20 C

21 D

22 B

23 A

24 C

**Section 2 (36 marks)**

**Question 25 (12 marks)**

**Question 26**

1. State the headline inflation rate in March 2017
2. State the Governments inflation rate target

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|  | **Marks** |
| 1. 2.1% (accept 2.2%)
 | 1 |
| 1. 2 to 3%
 | 1 |
| **Total** | **2** |

1. Distinguish between the headline and the underlying rate of inflation. Provide **one** possible reason for their difference in March 2015. (2 marks)

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| **Description** | **Marks** |
| **Headline rate** – all prices in the CPI basket of goods**Underlying rate** – removes volatile items from the measure | 1 |
| **Reason for the difference**March 2015, underlying rate was higher than headline rate which suggests there must have been a large fall in some volatile items such as petrol or fruit and veg. | 1 |
| **Total** | **2** |

1. Describe the change in the headline inflation rate since 2017 and outline **two** main causes of this change (3 marks)

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| **Description** | **Marks** |
| **Change** Headline rate has fallen from 2.1% to 1.3% | 1 |
| **Causes**Demand Pull disinflation* Caused by low levels of demand, generally associated with a trough phase of the BC when AD is falling due to low levels of consumption and investment spending

Cost push disinflation* Occurs when falling production costs, which reflect the prices paid for productive inputs, are passed on to consumers in the form of lower prices e.g. wages falling, oil prices falling.
 | 2 |
| **Total** | **3** |

1. Explain how a period of very low inflation should affect the following sectors of Australian society. (4 marks)

* 1. Individuals on a fixed income, such as pensioners
	2. Borrowers

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| **Description** | **Marks** |
| 1. **Individuals on a fixed income, such as pensioners**
* Will be better off in times of very low inflation because the purchasing power of their fixed income will not fall by as much as in times of high inflation
* In other words, real incomes are maintained
 | 2 |
| 1. **Borrowers**
* Will tend to lose because the value of the assets they purchase will not be rising by as much as in high inflation periods
* Also, the real value of their repayments i.e. impact on their purchasing power, will not decrease over time by as much as in times of high inflation.
 | 2 |
| **Total** | **4** |

**Question 26 (12 marks)**

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| a. i. Gross domestic product (GDP) is the total market value of all final goods and services produced within an economy in a given period of time.ii. Consumption is most stable Investment is the most volatileiii. Annual: 1.8%;  Quarterly: 0.4%iv. Real GDP was **rising** (most will get this wrong!) | 1 mark1 mark1 mark1 mark1 mark1 mark |
| b. Decline in investment – low business confidenceDecline in consumption – fall in housing prices; low consumer confidenceOther factors | 1 mark1 mark |
| c. Retail sales – would be expected to fall given ‘soft’ economy & falls in household confidence Inflation – would be expected to stay low due to slowdown in economy & spare capacity in the labour marketInventory levels – would be expected to increase as spending slowsBuilding loan approvals – likely to decline due to low business & household confidence OR could argue that very low interest rates may lead to a rise in approvals | 1 mark1 mark1 mark1 mark |

**Question 27 (12 marks)**

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| a. i. Exports of goods & services – imports of goods & servicesii. $8,000 million or $8 billioniii. China | 1 mark1 mark1 mark |
| b. Increase in commodity prices (e.g. iron ore/coal) which would increase the value of Australia’s resource exportsA fall in the value of the $A would have increased the demand for Australia’s exportsOR Increased demand from China for our exports – both goods & services | 1 mark1 mark |
| c. Due to the ongoing trade (tariff) war between United states & ChinaSignificance – this will cause global growth & trade to decline which will have a negative effect on Australia’s economy causing the trade surplus, commodity prices and economic growth to all decline.  | 1 mark1-2 marks |
| d. (i) It will cause the current account deficit to decrease (the current acct = trade balance + income balance)It will cause the capital/financial account surplus to decrease (since the current & cap/financial accounts sum to zero) (ii) It will have a positive effect on the macroeconomy – an increase in net exports (ceteris paribus) will increase real GDP, national income and employment.  | 1 mark 1 mark1-2 marks |

**SECTION 3 (40 marks) – Answer TWO questions**

**Question 28** **(20 marks)**

(a) Describe three non-price factors that could increase demand and three non-price factors that could increase supply in a given market. (6 marks)

(b) Use the demand/supply model to demonstrate and explain the different equilibrium outcomes if there is an increase in both demand and supply in a market. (8 marks)

(c) Explain why price elasticity of demand is a significant concept for both business and government. (6 marks)

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| a. Any THREE non-price factors affecting demand – 1 mark eachIncome; consumer preferences; prices of related goods; expectations of consumers; population factorsAny THREE non-price factors affecting supply – 1 mark eachTechnology; costs of production; expectations of producers; number of suppliers | 1-3 marks1-3 marks |
| b. There are THREE possible outcomes:Statement saying that equilibrium qty will increase, but equil price could increase, decrease or stay the same, it depends on the relative shiftsi. If D increases more than S – equil price rises & equil qty risesii. If S increases more than D – equil price falls & equil qty risesiii. If D & S increase same amount – equil price stays constant & equil qty rises.Use of D/S models to illustrate Note: this is harder than it looks – many students will score < 4 marks | 1-2 marks1 mark1 mark1 mark1-3 marks |
| c. Significance to business – 3 marksPrice elasticity of demand determines how a change in price affects the firm’s revenue – if demand is elastic, a fall in price will increase total revenue but if demand is inelastic, a fall in price will decrease revenue.Significance to the government – 3 marksImportant for govt when placing taxes on goods such as petrol, alcohol & cigarettes – a tax will raise more revenue for the govt when D is inelastic; It also determines the effect on market efficiency – when D is inelastic a tax causes a smaller deadweight loss. | 1-3 marks1-3 marks |

**Question 29** **(20 marks)**

(a) Explain the concept of market efficiency and use a model to demonstrate why the market equilibrium is efficient. (8 marks)

(b) Identify three different types of market failure and discuss how government policy can be used to improve the market outcome. (12 marks)

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| a. Explanation of market efficiency – 4 marks Define market efficiency – maximising net benefits to society (the difference between total benefits & total costs); when total surplus (the sum of consumer & producer surplus) is maximised. Need to explain the meaning of consumer & producer surplus.Use of D/S model – 4 marksClearly show CS & PS at equilibriumNeed to explain why it is a maximum at equilibrium – demonstrate that if output is either less than or greater than equilibrium, total surplus is less i.e. there is a DWL | 1-4 marks1-4 marks |
| b. Any **Three** types – 4 marks eachExternalities (either negative or positive) – define, give an example, explain why there is market failure & how govt can correct Public goods – define, give an example, explain why there is market failure & how govt can correctCommon resource – define, give an example, explain why there is market failure & how govt can correctMarket power (monopoly) – define, give an example, explain why there is market failure & how govt can correct | 1-4 marks1-4 marks1-4 marks 1-4 marks |

**Question 30** **(20 marks)**

(a) Draw the complete (five sector) circular flow of income model. Use the model to explain the concept of equilibrium and the effect of changes in leakages and injections on the level of equilibrium. (8 marks)

(b) Distinguish between the three largest components of aggregate expenditure.  (6 marks)

(c) Discuss three determinants of economic growth. (6 marks)

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| a. Diagram showing the five different sectors, income flows & leakages & injectionsExplain the concept of equilibrium – total spending = total production. For this to occur the sum of the leakages (S + T + M) = the sum of the injections (I + G + X).Effect of changes – explain what happens to equilibrium if either leakages > injections or injections > leakages | 1-4 marks1-2 marks1-2 marks |
| b. **Consumption** – largest component (around 55% of AE); spending by households on goods 7 services; determined mainly by household income & wealth**Investment** – between 20-25% of AE; includes business spending on capital goods (machinery) plus new housing & construction; determined by business expectations, profitability & cost of finance (interest rates) **Government spending** – between 20-25% of AE; determined by govt policy as well as the business cycle; includes govt spending on g & s, govt investment on infrastructure & welfare spending | 1-2 marks1-2 marks1-2 marks |
| c. Any **THREE** determinants (3 x 2 marks)Different ways to tackle this – but key factors to discuss would be1. Growth in labour force – caused by increase in population &/or increase in participation rate; more workers (hours) increases real GDP2. Growth in Productivity – this measures increases in real GDP per worker; determined by amount of capital per worker (capital deepening) and increased efficiency of inputs (multi factor productivity). Most economists view productivity as the most important factor to increase GDP/capita over time)3. Technology – this will boost the quality of both labour & capital thereby increasing productivity4. Investment – this can be increased physical investment (capital goods, machinery, buildings, infrastructure) and increased human investment (education & training). Investment is an important factor affecting productivity | 1-2 marks1-2 marks1-2 marks1-2 marks |

**Question 31** **(20 marks)**

(a) Discuss the importance of four of the Government’s economic objectives. (12 marks)

(b) To what extent has the government achieved its economic objectives in 2019?

 Refer to current economic indicators to justify your answer. (8 marks)

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| a. Discuss Any **FOUR** economic objectives – need to define & explain importance (4 x 3 marks)1. Sustainable rate of economic growth – measured by increases in real GDP & real GDP per capita. Target is for annual growth around 3%. Increases in real GDP enable increases in income & living stds over time.2. Full employment (low unemployment) – keeping unemployment close to its ‘natural’ rate of around 4.5%. (Natural rate includes only frictional & structural unemployment). Best way to raise economic welfare is to ensure everyone has a job – increases income, builds self esteem. 3. Price stability (low inflation) – keeping the annual inflation rate to between 2-3%. High inflation distorts income distribution, decreases the value of money, increases uncertainty & has a negative effect on economic growth.4. More equitable distribution of income – equity is about fairness, attempting to increase income & benefits to the poorer/less fortunate sections of the community. This is an important role of fiscal policy through the use of tax & spending powers of the government.5. Efficient allocation of resources – ensuring that resources are allocated to their best use. This means trying to maximise total surplus across all markets. Encouraging competition in markets & resolving areas of market failure such as market power, externalities & public goods. | 1-3 marks1-3 marks1-3 marks1-3 marks1-3 marks |
| b. Students need to discuss current state of the economy with reference to key economic indicators – more likely to devote more space to the macro objectives of growth, full employment & price stability. (1-8 marks)Economic growth – the Australian economy is growing below its target rate of 3%. In 2019, the growth rate was around 1.8% (March qrt). Govt policy will be aimed at increasing GDP & employment.Unemployment – the U rate has gradually increased since the start of the year from 5% to around 5.3% in July. This is well above the target of 4.5%. The govt will try to boost spending to increase production & employment – reducing taxes & interest rates will help achieve this.Inflation – the inflation is well below the target of 2-3%. In 2019 the annual inflation rate was 1.6% (June qrt). This is indicative of a ‘soft’ economy with spare capacity in the labour market. By increasing economic activity, the govt can help to increase the inflation rate.Equity – usually measured by the Lorenz curve (Gini coefficient) but difficult to obtain current measures. With weak economic growth & rising unemployment, then it is likely that equity has decreased. | 1-3 marks1-3 marks1-3 marks1-2 marks |