

**Victorian Certificate of Education
2014**

SUPERVISOR TO ATTACH PROCESSING LABEL HERE

STUDENT NUMBER Letter

ECONOMICS
Written examination

Thursday 30 October 2014

Reading time: 3.00 pm to 3.15 pm (15 minutes)

Writing time: 3.15 pm to 5.15 pm (2 hours)

QUESTION AND ANSWERBOOK

Structure of book

<i>Section</i>	<i>Number of questions</i>	<i>Number of questions to be answered</i>	<i>Number of marks</i>
A	15	15	30
B	4	4	60
			Total 90

- Students are permitted to bring into the examination room: pens, pencils, highlighters, erasers, sharpeners and rulers.
- Students are NOT permitted to bring into the examination room: blank sheets of paper and/or white out liquid/tape.
- No calculator is allowed in this examination.

Materials supplied

- Question and answer book of 27 pages.
- Answer sheet for multiple-choice questions.
- Additional space is available at the end of the book if you need extra paper to complete an answer.

Instructions

- Write your **student number** in the space provided above on this page.
- Check that your **name** and **student number** as printed on your answer sheet for multiple-choice questions are correct, **and** sign your name in the space provided to verify this.
- All written responses must be in English.

At the end of the examination

- Place the answer sheet for multiple-choice questions inside the front cover of this book.

Students are NOT permitted to bring mobile phones and/or any other unauthorised electronic devices into the examination room.

SECTION A – Multiple-choice questions**Instructions for Section A**

Answer **all** questions in **pencil** on the answer sheet provided for multiple-choice questions.

Choose the response that is **correct** or that **best answers** the question.

A correct answer scores 2, an incorrect answer scores 0.

Marks will **not** be deducted for incorrect answers.

No marks will be given if more than one answer is completed for any question.

Question 1

A major determinant of demand in one particular market could be the

- A. cost of raw materials.
- B. method of production.
- C. number of sellers in the market.
- D. disposable incomes of buyers in the market.

Question 2

Which one of the following would be recorded as a debit in Australia's balance of payments on current account?

- A. the sale of Australian wool to Italy
- B. an increase in the number of foreign tourists visiting Australia
- C. interest paid on Australian Government bonds to overseas investors
- D. a Chinese company purchasing a farming property in rural Australia

Question 3

Market power exists when

- A. the government taxes companies and individuals.
- B. consumers exercise consumer sovereignty in the market.
- C. activity in overseas economies influences Australia's exchange rate.
- D. a business is able to influence the price of a product by exercising control over demand, supply or both.

Question 4

The effect on the market for product A from a rise in the price of a complementary product B will

- A. shift the demand curve right and increase the equilibrium price.
- B. shift the demand curve left and decrease the equilibrium price.
- C. shift the supply curve left and increase the equilibrium price.
- D. shift the supply curve right and decrease the equilibrium price.

Question 5**Distribution of income by income units for selected years in Country X**
Gross income share (per cent of total income units)

	Year 1	Year 2	Year 3
Quintile			
lowest quintile	4.7	3.6	3.8
2nd quintile	9.7	9.3	9.0
3rd quintile	15.5	15.2	15.0
4th quintile	24.0	24.0	23.8
highest quintile	46.1	47.9	48.5
Gini Coefficient	0.42	0.44	0.45

Based on the table above, which one of the following statements about the distribution of income from Year 1 to Year 3 is incorrect?

- A. The distribution of income has become more uneven.
- B. The top 20 per cent of income units has been increasing its share of total gross income.
- C. The Gini Coefficients confirm that the distribution of income has become more equitable.
- D. The cumulative income share of the lowest 40 per cent of income earners has decreased.

Question 6

Which of the following events, or combination of events, may result in the Reserve Bank of Australia (RBA) adopting a more restrictive monetary policy stance?

- A. an increase in the world oil price over two consecutive months
- B. an increase in the growth of both credit and household debt to income ratio, combined with the rapid depreciation of the Australian dollar
- C. an increase in the official Australian Bureau of Statistics (ABS) unemployment rate and evidence of a higher level of labour force under-utilisation
- D. a decrease in consumer confidence and aggregate demand, accompanied by renewed concerns about declining rates of economic growth in the economies of Australia's major trading partners

Question 7**Production possibility data for a hypothetical economy – Starland**

	Combination A	Combination B	Combination C	Combination D	Combination E
Quantity of goods produced ('000)	60	35	20	8	0
Quantity of services produced ('000)	0	6	14	25	40

Based on the data in the table above for Starland, if a decision were made by the business sector to increase the quantity of goods produced from 20 000 to 35 000, the opportunity cost of attaining the increase of 15 000 goods would be

- A. 8 000 services.
- B. 15 000 goods.
- C. 20 000 services.
- D. 34 000 services.

Question 8

Which one of the following is an example of discretionary budgetary policy?

- A. a decrease in the cash interest rate target
- B. a decrease in the company tax rate from 30 per cent to 29 per cent
- C. an increase in welfare payments due to a rise in cyclical unemployment
- D. lower revenue from a minerals resource rent tax (MRRT) due to falling commodity prices

Question 9

Which one of the following is least likely to increase productivity?

- A. labour skills training
- B. innovation in work practices
- C. investment in physical capital
- D. a decline in competition in the market

Question 10

In a situation in which the inflation rate is higher than the RBA's target rate of inflation, the RBA is likely to

- A. sell government bonds in order to drive the cash interest rate up.
- B. sell government bonds in order to drive the cash interest rate down.
- C. purchase government bonds in order to drive the cash interest rate up.
- D. purchase government bonds in order to drive the cash interest rate down.

Question 11

Which one of the following is **not** an example of private investment expenditure (I) as a component of aggregate demand?

- A. A small-business owner purchases new capital equipment for a production plant.
- B. There is an increase in young married couples in Australia employing residential construction companies to build new dwellings.
- C. A small business chooses to increase production volumes while operating costs are relatively low and consciously boosts the company's stock holdings in the short term.
- D. Australian householders become cautious about future employment prospects and increase their savings in bank accounts as a means of securing their future spending capacity.

Question 12

Which one of the following government initiatives is most likely to improve non-material living standards in Australia?

- A. increased public resources directed to the provision of support services for domestic dispute resolution
- B. the introduction of industrial relations reforms that encourage businesses to negotiate directly with employees on extended working hours
- C. a high priority given to restoring the budget balance through significant cutbacks in expenditure on infrastructure development throughout Australia
- D. the successful monetary policy containment of inflation within the target zone, allowing for a slow and steady increase in real household disposable income and Real Gross Domestic Product (GDP) per capita

Question 13

Suppose Australia's interest rates are increased while the interest rates of its major trading partners remain unchanged.

Which one of the following combinations is most likely to result?

- A. the supply of Australian dollars increases and the trade-weighted index (TWI) increases
- B. the supply of Australian dollars decreases and the TWI decreases
- C. the supply of Australian dollars increases and the TWI decreases
- D. the supply of Australian dollars decreases and the TWI increases

Question 14

Assume average wages in the national economy have increased by 5 per cent per annum and average labour productivity has increased by 2 per cent per annum.

Which one of the following is the most likely outcome of these increases?

- A. an increase in real wages and a rise in the operating profits of Australian businesses
- B. an improvement in equity in income distribution as a result of the likelihood of declining unemployment
- C. an increase in inflationary pressures, reducing the price competitiveness of Australian exports and import-competing goods
- D. a significant increase in business confidence levels, resulting in much higher levels of investment by business owners in new capital resources

Question 15

Which one of the following policy changes might contribute to an improvement in equity in income distribution?

- A. raising the income tax-free threshold
- B. raising the excise tax on alcohol and tobacco
- C. lowering the highest marginal income tax rate
- D. raising the rate of the goods and services tax (GST)

SECTION B – Written responses**Instructions for Section B**

Answer **all** questions in **pen** in the spaces provided.

Question 1 (12 marks)

a. Describe what is meant by a perfectly competitive market.

2 marks

b. In a perfectly competitive market, the price mechanism might fail to allocate resources efficiently, causing market failure. Sources of market failure include:

- externalities
- asymmetric information.

Explain why externalities and asymmetric information are **each** considered to be sources of market failure. In your answer, refer to an example of a market failure related to each of these.

4 marks

Externalities _____

Asymmetric information _____

c. Outline **one** factor that influences the price elasticity of supply for a product.

2 marks

Question 2 (14 marks)

The budget position has deteriorated significantly since the 2013 Pre-Election Economic and Fiscal Outlook (PEFO). Budget deficits totalling \$123 billion are now expected across the forward estimates, with a \$47 billion deficit expected in 2013–14 ... 3.0 per cent of Gross Domestic Product (GDP). Without policy change and taking no remedial action, budget deficits would be projected in each and every year to 2023–24.

This is an unsustainable fiscal position and the Government is committed to taking the hard decisions to live within its means. The 2014–15 Budget will outline the fiscal strategy to return the budget to surplus and pay down debt.

Source: The Commonwealth of Australia, *Mid-Year Economic and Fiscal Outlook 2013–14*, Part 1: Overview, December 2013, p. 1

- a. Explain **two** economic reasons for the deterioration of the nation’s budgetary/fiscal position since 2012.

4 marks

- b. Outline **one** economic implication for the Australian economy if the projected budget deficits, as suggested by the Treasury, exist through to 2023–2024. 2 marks

- c. Explain **one** possible effect on the achievement of equity in income distribution if the government chooses to take ‘the hard decisions to live within its means’. 2 marks

Question 3 (20 marks)

a. The Australian economy experienced a rise in the rate of unemployment in 2013–2014.

- i.** Explain the difference between cyclical unemployment and structural unemployment. 2 marks

- ii.** In late 2013 and early 2014, the Australian economy experienced slower rates of economic growth.

Identify an industry sector within the Australian economy that has been affected by this slowdown. Outline **one** demand-side factor and **one** supply-side factor that may have contributed to the effect on this industry sector.

4 marks

iii. Describe **one** example of discretionary budgetary policy that could be implemented to lower the rate of structural unemployment.

2 marks

- c. Explain how **one** immigration policy and **one** microeconomic reform policy might operate to raise Australia's productive capacity and increase rates of economic growth. 6 marks

Immigration policy _____

Microeconomic reform policy _____

Question 4 (14 marks)

The inflation forecasts have been revised higher in the short term, reflecting the effect of the depreciation of the exchange rate since November [2013] and the higher-than-expected December [2013] quarter CPI outcome ... Underlying inflation is expected to be close to 3 per cent over the year to June 2014. Given the slow growth of wages and limited domestic cost pressures more generally, underlying inflation is then expected to decline to be closer to 2½ per cent. Headline inflation is expected to peak a bit higher than underlying inflation ...

Source: RBA, *Statement on Monetary Policy*, February 2014, p. 4

- a. Distinguish between headline inflation and underlying inflation.

2 marks

Selected daily exchange rates of the Australian dollar

Date	United States dollar	Trade-weighted index (TWI)
25 January 2013	1.0450	78.0
10 May 2013	1.0071	76.6
28 October 2013	0.9609	72.8
13 January 2014	0.9036	69.4
3 March 2014	0.8912	68.5

Source: RBA, Exchange Rate Data, 2014 to current

- b.** Describe **one** factor that might explain the change in the exchange rate of the Australian dollar as shown in the table above.

2 marks

c. Given the change in the exchange rate of the Australian dollar as shown in the table on page 20, describe the likely effect of this change on each of the following. 4 marks

- The goal of external stability _____

- The goal of low inflation _____

d. Explain how the operation of budgetary policy in 2014–2015 is likely to influence each of the following.

6 marks

- Aggregate demand and the effect on the achievement of the goal of low inflation

- Aggregate supply and the effect on the achievement of the goal of external stability

TURN OVER

