**2004**
Higher School Certificate
**Trial Examination**

# Economics

**Total marks – 100**

**Section I** - Pages 2 – 8
Total marks (20)
Attempt questions 1 – 20
Allow about 35 minutes for this section

**Section II** - Pages 9 – 16
Total marks (40)
Attempt questions 21 – 24
Allow about 1 hour 15 minutes for this
section

**Section III** - Pages 17 – 18
Total marks (20)
Attempt EITHER Question 25 or 26
Allow about 35 minutes for this section

**Section IV** - Page 19
Total marks (20)
Attempt EITHER Question 27 or 28
Allow about 35 minutes for this section

**General Instructions**

- Reading time – 5 minutes

- Working time – 3 hours

- Board approved calculators may be used

- Write using black or blue pen

- Write your student number and/or name
  at the top of every page

**This paper MUST NOT be removed from the examination room**

STUDENT NUMBER/NAME: ........................

## Section I

**Total marks (20)**
**Attempt questions 1 – 20**
**Allow about 35 minutes for this section**

Select the alternative A, B, C or D that best answers the question and indicate your choice with a cross (X) in the appropriate space on the grid below.

|    | A | B | C | D |
|----|---|---|---|---|
| 1  |   |   |   |   |
| 2  |   |   |   |   |
| 3  |   |   |   |   |
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| 10 |   |   |   |   |
| 11 |   |   |   |   |
| 12 |   |   |   |   |
| 13 |   |   |   |   |
| 14 |   |   |   |   |
| 15 |   |   |   |   |
| 16 |   |   |   |   |
| 17 |   |   |   |   |
| 18 |   |   |   |   |
| 19 |   |   |   |   |
| 20 |   |   |   |   |

1. Which of the following is a likely consequence of the sale of Commonwealth Government Securities by the Reserve Bank of Australia in the money market?

   (A) A decrease in the cash rate and a contraction in economic activity.
   (B) A decrease in the cash rate and an expansion in economic activity.
   (C) An increase in the cash rate and a contraction in economic activity.
   (D) An increase in the cash rate and an expansion in economic activity.

2. What is meant by the labour force participation rate?

   (A) The percentage of the working age population who are in work.
   (B) The percentage of the population in work or looking for work.
   (C) The percentage of the population who are working.
   (D) The percentage of the working age population in work or looking for work.

3. The following table shows export/import data for a trading nation.

   | Year | Export Price Index | Import Price Index | Terms of Trade Index |
   |------|--------------------|--------------------|----------------------|
   | 2002 | 100 | 100 | 100 |
   | 2003 | 125 | 110 | |

   What is the terms of trade index for 2003?

   (A) 125
   (B) 110
   (C) 88
   (D) 114

4. Which of the following describes a role of the International Monetary Fund (IMF)?

   (A) To provide loans and foreign aid to developing countries.
   (B) To work towards the elimination of all tariff and non tariff barriers.
   (C) To provide funding for long term development projects.
   (D) To create a system of stable exchange rates.

5. The following diagram shows the market for an environmental good such as native forests.
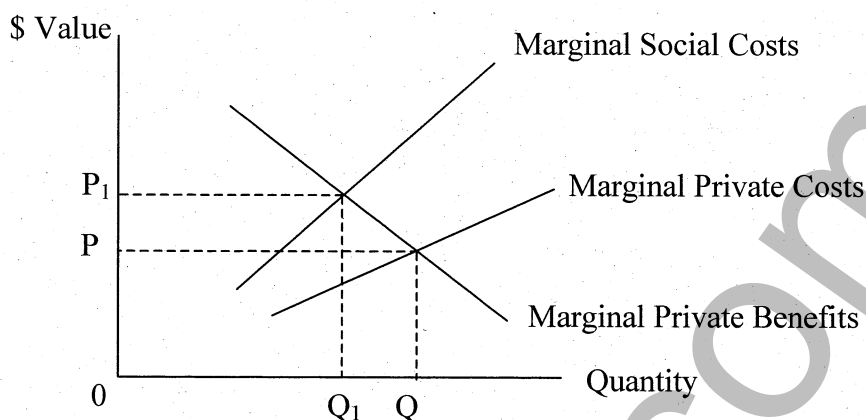


In the diagram what does the price 0P represent?

(A) The price at which the optimum production for society occurs.
(B) The price which results in significant social costs of harvesting native forests.
(C) The price at which the costs and benefits to society of harvesting native forests are equal.
(D) A price which illustrates the effect of government intervention in the market.

6. The following table shows income and consumption data for a hypothetical economy.

| Income | Consumption |
|--------|-------------|
| 0 | 60 |
| 400 | 360 |
| 800 | 660 |
| 1200 | 960 |
| 1600 | 1260 |

What is the value of the multiplier?

(A) 0.25
(B) 4.0
(C) 0.75
(D) 400

7.    What are three common features of developing countries?

(A)   Low per capita incomes, high population growth and low levels of foreign debt.
(B)   High population growth, high levels of foreign debt and high levels of capital accumulation.
(C)   Low levels of domestic savings, low levels of technology and high levels of foreign debt.
(D)   Low levels of savings, low per capita incomes and high levels of capital accumulation.

8.    The following diagram shows production possibility curves for an economy.
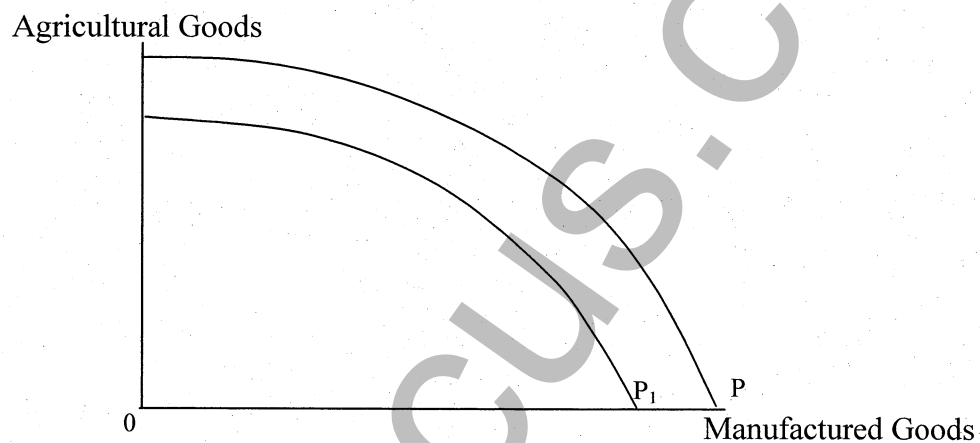


What is a possible cause of the movement of the production possibility curve from P to $P_1$?

(A)   An economic recession.
(B)   An increase in unemployment.
(C)   A technological innovation in both agriculture and manufacturing.
(D)   Economic growth.

9.    What would be two indicators of fiscal policy tightening in Australia?

(A)   Higher interest rates and reduced government spending.
(B)   Higher tax rates and reduced government spending.
(C)   Lower tax rates and increased government spending.
(D)   Lower tax rates and lower rates of interest.

10. Which of the following would most likely increase as a result of a downturn in the international business cycle?

(A) Export growth.
(B) Domestic inflation.
(C) Import prices.
(D) Domestic unemployment.

11. The following diagram shows the demand and supply of Australian dollars in the foreign exchange market.
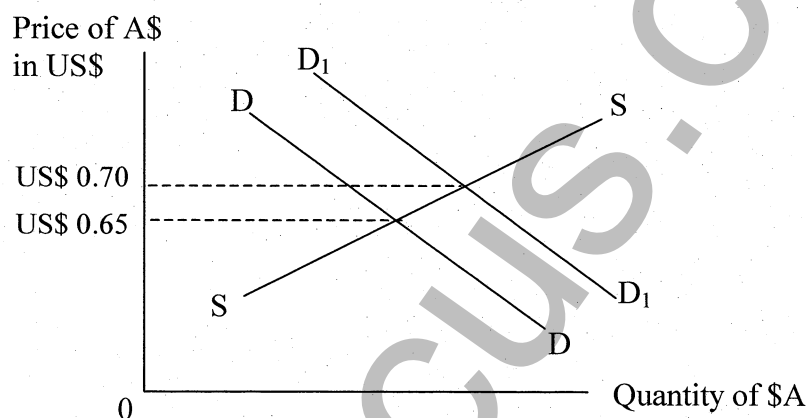


Which of the following could have caused the rise in value of the Australian dollar?

(A) An increase in Australia's economic growth.
(B) A rise in US interest rates.
(C) A rise in Australian interest rates.
(D) A rise in Australia's foreign debt.

12. What is the best indicator of the level of economic development in an economy?

(A) The economy's growth rate.
(B) The quality of life of the people within the economy.
(C) The proportion of gold in the economy's foreign exchange reserves.
(D) The proportion of GDP spent on defence items.

13. Which fiscal measure could reduce income inequalities in an economy?

(A) A decrease in the Goods and Services Tax from 10% to 5%.
(B) A decrease in the Capital Gains Tax.
(C) A decrease in the Fringe Benefits Tax.
(D) A decrease in the marginal tax rate for lower income earners.

14.    Why does the market system generally fail to produce public goods?

    (A)    Consumers in the marketplace have little demand for public goods.
    (B)    Private industry cannot restrict the benefits to only those who are willing to pay
           for public goods.
    (C)    Government business enterprises can produce public goods cheaper than private
           industry
    (D)    The existence of public goods increases the inequality of income distribution.

15.    The following table shows Consumer Price Index information for an economy.

| Year | C.P.I. |
|------|--------|
| 1    | 100    |
| 2    | 120    |
| 3    | 132    |

What is the inflation rate for Year 3?

    (A)    10%
    (B)    12%
    (C)    32%
    (D)    20%

16.    What is an acceptable economic argument for a government to impose a tariff on imports?

    (A)    To raise revenue.
    (B)    To retaliate against tariffs imposed by other countries.
    (C)    To stop imports from countries with low labour costs.
    (D)    To assist a new industry to become internationally competitive.

17.    What is a major reason for the government's use of microeconomic policies?

    (A)    To reduce inequality in the distribution of income.
    (B)    To increase aggregate demand and economic growth.
    (C)    To improve allocative efficiency and increase aggregate supply.
    (D)    To achieve price stability and full employment.

18. Why do developing countries promote policies that raise their levels of economic development?

(A) To achieve increases in population growth.
(B) To achieve higher levels of human development.
(C) To achieve greater inequality in the distribution of income.
(D) To achieve higher levels of protection from import competition.

19. Where would the payment of Qantas dividends to British Airways in the United Kingdom appear in Australia's balance of payments?

(A) A debit in the Capital and Financial Account.
(B) A debit in the Income section of the Current Account.
(C) A debit in the Goods and Services section of the Current Account.
(D) A credit in the Capital and Financial Account.

20. What combination of macroeconomic policies would the government use to reduce inflation?

(A) Lower interest rates and budget for a deficit.
(B) Raise interest rates and budget for a deficit.
(C) Lower interest rates and budget for a surplus.
(D) Raise interest rates and budget for a surplus.

## Section II

**Total marks (40)**
**Attempt questions 21 – 24**
**Allow about 1 hour 15 minutes for this part**

Answer the questions in the spaces provided

**Question 21** (10 marks)                                                                 **Marks**

The following information concerns environmental issues.

| |
|---|
| "Economists reject the environmentalists' assumption that there's an inexorable relationship between economic growth (as measured by GDP) and environmental degradation. But they do admit that our past pattern of generating GDP has produced large environmental degradation. They also admit that, if we keep going in the same direction, the degradation of the environment will reach a point where it crunches the material wellbeing that GDP measures. .......... environmental assets – such as clean air, clean water and native species – generally aren't subject to private ownership and so aren't adequately protected by market forces. So governments have to find effective ways to intervene in the market to ensure those assets are protected. In the jargon, they have to internalise the externalities." <br><br> *Source: Ross Gittins, The Sydney Morning Herald, 22 June 2002* |

(a)    Define ecologically sustainable development.                                               **1**

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(b)    Describe using an example, how environmental degradation can be viewed as a
       negative externality.                                                                          **2**

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**Question 21 continues on the next page**

Question 21 (continued)                                                                          **Marks**

(c)    Explain using an example, how government environmental policies could be used to "internalise externalities".                                                                              **3**

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(d)    Explain ONE economic benefit and ONE economic cost associated with achieving ecologically sustainable development.                                                                        **4**

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**End of Question 21**

**Question 22**  (10 marks)                                    **Marks**

The following table shows selected economic data for a country.

| Year | Employed Persons (m) | Unemployed Persons (m) | Population Aged 15+ Years (m) |
|------|----------------------|-------------------------|-------------------------------|
| 1    | 50                   | 5.5                     | 80                            |
| 2    | 55                   | 5.6                     | 82                            |
| 3    | 60                   | 5.8                     | 84                            |

(a)    Using the table state the formula for and calculate the unemployment rate in Year 2.         **2**

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(b)    Using the table state the formula for and calculate the labour force participation rate
         for Year 3.                                                                                       **2**

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(c)    Explain how structural change can lead to an increase in the level of unemployment.         **3**

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**Question 22 continues on the next page**

Question 22 (continued)                                                                    **Marks**

(d)    Explain ONE economic policy that can be used to reduce the level of unemployment.        **3**

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**End of Question 22**

**Question 23** (10 marks)                                                    **Marks**

The following information relates to a proposed free trade agreement between Australia and the United States.

> "The ultimate prize through the construction of a two way economic freeway between Australia and the US is the transformation of a 20 million market population into one of more than 300 million. Australia's perennial problem of being a relatively small economy will be resolved. The great opportunities of the future lie with the smaller and medium sized enterprises bound for the global market."
>
> *Source: The Sydney Morning Herald, 2 March 2004*

(a)    Define the term protection.                                               1

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(b)    Outline TWO methods governments can use to protect domestic industries.     2

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(c)    Explain TWO economic reasons why governments protect domestic industries.   2

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**Question 23 continues on the next page**

Question 23 (continued)                                                          **Marks**

(d)   Discuss the costs and benefits of Australia entering into a free trade agreement with
another country such as the USA.                                               **5**

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**End of Question 23**

**Question 24** (10 marks)                                                              **Marks**

The following provides information on the Australian government's use of fiscal policy.

> "The primary objective of the Government's medium-term fiscal strategy is to maintain budget balance, on average over the course of the economic cycle. This ensures that the Government is not living beyond its means. It helps deliver macroeconomic stability, encourages private investment in a lower interest rate environment, entrenches low public debt and ensures that, over time, the current account reflects private saving and investment decisions."
>
> *Source: Budget Paper No 1, Statement 1, 2004*

(a)    Define fiscal policy.                                                                          1

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(b)    Outline how automatic stabilisers play a 'countercyclical' role in the economy.        2

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(c)    Explain the role of fiscal policy in achieving macroeconomic stability for the
government.                                                                                            3

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**Question 24 continues on the next page**

Question 24 (continued)                                                                                    **Marks**

(d)    Discuss the effects of the 2004-05 fiscal policy stance on income distribution and
       economic activity.                                                                                      **4**

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**End of Question 24**

## Section III

**Total marks (20)**

**Attempt EITHER Question 25 OR Question 26**
**Allow about 35 minutes for this section**

Answer the question on a separate piece of paper.

In your answer you will be assessed on how well you:

- use your knowledge and the economic information provided
- apply economic terms, concepts, relationships and theory
- present a sustained, logical and well-structured answer to the question

**Question 25** (20 marks)

Analyse the macroeconomic policy options available to the Australian government to achieve its objectives of sustainable economic growth, full employment and price stability.

> "The outlook for the Australian economy is for continued growth, with increasing employment and low inflation. A stronger world economy in 2004-05 will support a rebalancing of growth from domestic to external sources. In year average terms, GDP growth is forecast to moderate slightly from 3.75% in 2003-04 to 3.5% in 2004-05."
>
> *Source: Budget Paper No 1, Statement 1, 2004*

**Chart 3: Underlying cash balance**
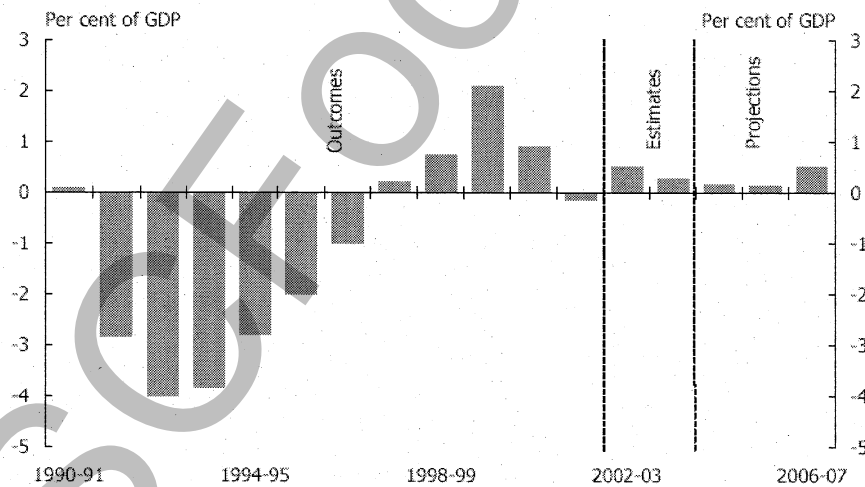


*Source: Budget Paper No1, Statement 1, 2004*

> ".... there is overwhelming evidence to suggest that countries can only have sustained expansions if they are accompanied by low inflation. It is the sustainability of the expansion which is the key to maximising economic growth and employment. Another way of expressing the aims of monetary policy based on inflation targeting is to say that its aim is to maximise the length of the economic expansion."
>
> *Source: I.J. MacFarlane, Governor of the Reserve Bank of Australia*
> *Reserve Bank Bulletin, October 2002*

**OR**

**OR**

In your answer you will be assessed on how well you:

- use your knowledge and the economic information provided
- apply economic terms, concepts, relationships and theory
- present a sustained, logical and well-structured answer to the question

**Question 26** (20 marks)

Analyse government policy options to achieve external stability in the Australian economy.

> "The terms of trade are forecast to increase strongly in 2004-05, driven by increased prices for a number of Australia's non-rural commodity exports and further declines in many import prices. This improvement in the terms of trade underpins a forecast narrowing of the current account deficit to 5 per cent of GDP in 2004-05."
>
> *Source: Budget Statement 3, 2004*

**Chart 6: Current account balance**
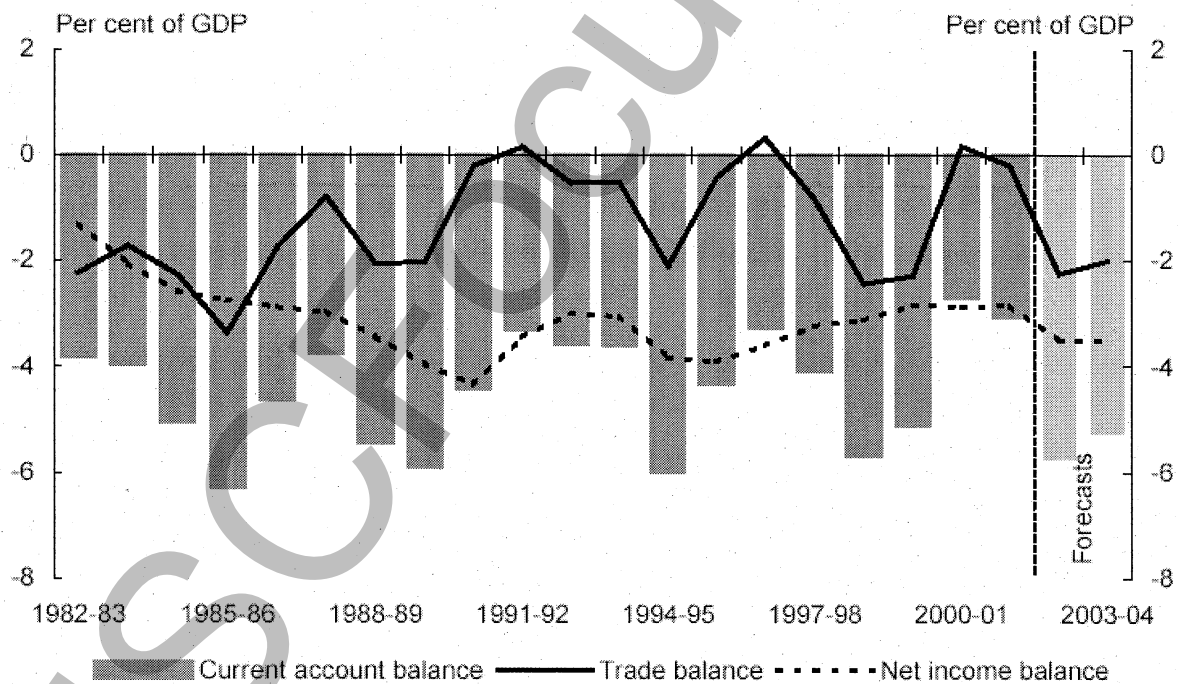


Source: ABS Cat. No. 5302.0 and 5206.0 and Treasury.

> "The widening of the current account deficit over 2002-04 reflected weak global growth and the impact of the drought on farm exports. With a pick up in world growth and sound macroeconomic and microeconomic policies, the export sector remains competitive and ready to contribute to growth in 2004-05."
>
> *Source: Budget Paper No 1, Statement 1, 2004*

## Section IV

**Total marks (20)**

**Attempt EITHER Question 27 OR Question 28**
**Allow about 35 minutes for this section**

Answer the question on a separate piece of paper.

In your answer you will be assessed on how well you:

- use economic data
- apply economic terms, concepts, relationships and theory
- present a sustained, logical and well-structured answer to the question

**Question 27**  (20 marks)

Explain how exchange rates are determined and how movements in exchange rates impact on the Australian economy.

**OR**

**Question 28**  (20 marks)

Analyse the impact of globalisation on living standards in the global economy and the economic development strategies of an economy other than Australia.

**End of paper**