**Victorian Certificate of Education
2003**

ECONOMICS
Written examination

Wednesday 5 November 2003

Reading time: 3.00 pm to 3.15 pm (15 minutes)
Writing time: 3.15 pm to 5.15 pm (2 hours)

QUESTION BOOK

Structure of book

Section	Number of questions	Number of questions to be answered	Number of marks	Suggested times (minutes)
A	15	15	30	30
B	3	3	60	90
			Total 90	120

- 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 book of 7 pages.
- Answer sheet for multiple-choice questions.
- One or more script books.

Instructions
- Write your **student number** in the space provided on the front page(s) of the script book(s).
- 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 all other used script books and the answer sheet for multiple-choice questions inside the front cover of the first script book.
- You may keep this question book.

Students are NOT permitted to bring mobile phones and/or any other electronic communication 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

Which one of the following could make Australia less internationally competitive?

A. rising productivity

B. an increase in Australia's inflation rate

C. a depreciation in the value of the Australian dollar

D. a fall in the general level of Australian interest rates

Question 2

Which one of the following factors would have a different effect on the rate of economic growth from the other three factors?

A. a drought across Australia

B. a world economic recession

C. a decrease in the general level of Australian interest rates

D. a decline in business expectations about the state of the economy

Question 3

Which one of the following statements about an externality is **not** correct?

A. An externality is always negative.

B. An externality is a 'side effect' or spillover not captured by the market.

C. An externality is where private cost/benefit diverges from social cost/benefit.

D. An externality is a cost or benefit on a third party not captured by the market.

Question 4

The cash interest rate is the Reserve Bank of Australia's

A. operating target.

B. intermediate target.

C. monetary policy goal.

D. mortgage interest rate.

Question 5

Commonwealth Government Budget Data

Year	Government revenue ($bn)	Government expenses ($bn)
1	100	90
2	120	100
3	115	120

With reference to the Commonwealth Government Budget data above, which one of the following statements is true?

A. A budget surplus was recorded in all years.

B. A smaller budget surplus was recorded in year 2 when compared with year 1.

C. The budget outcome moved from surplus in year 2 to deficit in year 3.

D. In year 3 the budget outcome is likely to have a contractionary effect on economic activity.

Question 6

Which one of the following may cause the unemployment rate to rise?

A. school retention rates increase

B. Australian universities offer more places

C. an increase in the labour force participation rate

D. school leavers increase their tendency to travel overseas

Question 7

In the 1980s and early 1990s, Australia ran a guaranteed minimum price scheme for wool.

The fact that, by the early 1990s, there was a stockpile of unsold wool in Australia of almost five million bales, shows that the guaranteed minimum price

A. was above the equilibrium price of wool.

B. was below the equilibrium price for wool.

C. was equal to the equilibrium price of wool.

D. applied only to the supply side of the wool market and not the demand side of the market.

Question 8

National defence is unlikely to be supplied in a market economy since

A. defence is always a responsibility of the government.

B. it is too expensive for any private firm to supply defence.

C. a private firm would not have the power to make it compulsory for people to join the defence forces.

D. it is not possible to exclude people from enjoying the benefits of defence, even if they do not pay a price to a private supplier of defence.

Question 9

During the summer months, it is likely that in a purely competitive market the price of woollen scarves would

A. increase and the quantity of woollen scarves sold would increase.

B. decrease and the quantity of woollen scarves sold would decrease.

C. increase and the quantity of woollen scarves sold would decrease.

D. decrease and the quantity of woollen scarves sold would increase.

Question 10

A weak global economy and strong domestic spending have combined to produce the worst Australian trade deficit on record, with imports exceeding exports by almost $3 billion in December.

Australian Financial Review, 1 February 2003.

Based on the information in this quotation, we would expect that in December the Australian dollar would have

A. appreciated as a result of the strong domestic spending leading to an increase in aggregate demand.

B. depreciated since currency speculators would have bought the Australian dollar while it was relatively cheap.

C. appreciated as the Reserve Bank of Australia would have tightened monetary policy in order to reduce the size of the trade deficit.

D. depreciated since increased import spending and decreased spending on Australian exports lowered the overall demand for Australian currency.

Question 11

The operator of a tourist resort on Australia's Gold Coast was quoted as saying that 'a stronger Australian dollar will be bad for her business'.

This is most likely because a stronger dollar

A. means that Australian residents are more able to afford holidays in other countries, while residents in other countries are less likely to take their holidays in Australia.

B. leads to a higher rate of inflation in Australia and this will discourage people from taking holidays.

C. reduces the value of Australians' income and this will lower the demand for tourism.

D. causes higher interest rates in Australia and this will lead to a recession.

Question 12

A redistribution of income away from the richest ten per cent of society towards the poorest ten per cent of society will

A. increase the Gini coefficient and move the Lorenz Curve closer to the 45 degree line.

B. decrease the Gini coefficient and move the Lorenz Curve closer to the 45 degree line.

C. decrease the Gini coefficient and move the Lorenz Curve further from the 45 degree line.

D. increase the Gini coefficient and move the Lorenz Curve further from the 45 degree line.

Question 13

Which one of the following is **not** included in the calculation of Australia's Gross Domestic Product (GDP)?

A. a consumer purchasing a new television set

B. a firm purchasing a new piece of equipment

C. a transfer payment from the government to an individual

D. the amount paid by the government to build a new hospital

Question 14

In a situation in which the inflation rate is higher than the Reserve Bank's target rate of inflation, the Reserve Bank will

A.   purchase government bonds in order to drive the cash interest rate down.

B.   purchase government bonds in order to drive the cash interest rate up.

C.   sell government bonds in order to drive the cash interest rate down.

D.   sell government bonds in order to drive the cash interest rate up.

Question 15

An example of a fiscal/budgetary policy weapon which could be used to try to reduce demand inflation is

A.   an increase in interest rates.

B.   a reduction in the budget surplus.

C.   an increase in personal income tax rates.

D.   an increase in government investment expenditure (G2).

SECTION B – Written responses

Instructions for Section B
Answer **all** questions in one or more script books.

Question 1

The Commonwealth budget aggregates in the period 2000–2003 are presented in the table below.

Commonwealth Budget Aggregates

	Actual	Estimates	
	2000–01	2001–02	2002–03
Underlying cash balance ($bn)	5.6	−1.2	2.1
Fiscal balance ($bn)	5.9	−3.0	0.2

Source: Budget 2002–03 Budget Statement No. 1 Fiscal Strategy and Budget Priorities Part 1 Overview at
http://www.budget.gov.au2002-03/bp1/html/Bst1.html#P37_817

a. The Commonwealth budget outcome could change from **either** surplus to deficit **or** from deficit to surplus as a result of **either** cyclical factors (automatic stabilisers) **or** structural factors (discretionary factors).

  i. Explain the difference between cyclical and structural factors.

  ii. Give an example of each.

2 + 2 = 4 marks

b.   **i.** Will taxes levied on commodities such as alcoholic beverages and tobacco products be progressive or regressive? Explain.

  ii. Outline **two** economic reasons why governments levy taxes.

2 + 4 = 6 marks

c. Outline **two** major influences on budgetary/fiscal policy settings for 2003–04.

6 marks

d. Explain how budgetary/fiscal policy has influenced the following objectives, during the period of 2001–03. Use a different example for each objective.

  i. external stability

  ii. efficiency of resource allocation

3 + 3 = 6 marks

Total 22 marks

Question 2

In recent years, Australia has been suffering an extreme drought with rainfall in many regions being well below long-run historical average levels. In releasing a special report about the economic effects of the drought (*Australian Crop Report*, 29 October 2002), the executive director of the Australian Bureau of Agriculture and Resource Economics, Dr Brian Fisher, noted the following.

> *While grain production will be well down this season, world grain prices have increased steadily since midyear, reflecting poor harvests in North America and the expected poor harvest in Australia. These higher world grain prices are being reflected in the domestic market with adverse consequences for domestic grain-using industries.*
>
> *The drought will have a significant impact on economic growth in Australia through the direct and indirect linkages between agriculture and other industries.*
>
> *Taking into account this latest downward revision to the crop forecast, the drought is now estimated to reduce the rate of economic growth in Australia in 2002–03 by around 0.7 percentage points, or around \$5.4 billion, from what would otherwise have been achieved.*

Adapted from (http://www.abareconomics.com/pages/media/2002/29oct.htm)

a. Explain how drought reduces the rate of economic growth.

4 marks

b. Explain the likely effect of a major drought on
   i. Australia's balance of payments on current account
   ii. the value of the Australian dollar.

2 + 2 = 4 marks

c. Describe the possible effect of the drought on
   i. price stability
   ii. the distribution of income.

2 + 2 = 4 marks

d. Suggest two government policies that might alleviate the economic effects of the drought and explain how they would achieve this result.

6 marks

Total 18 marks

Question 3

a. Suppose Australia was faced with both a weakening in world economic growth and increased growth in domestic spending. Explain how this environment might influence the Reserve Bank of Australia's monetary policy settings.

6 marks

b. Explain how the implementation of an expansionary monetary policy may affect the achievement of
   i. price stability
   ii. external stability.

3 + 3 = 6 marks

c. Evaluate the extent to which microeconomic reform policy has supported monetary policy in the pursuit of domestic economic stability in Australia over the last decade.

8 marks

Total 20 marks

END OF QUESTION BOOK