NESA Student Number:……..…….

2022
Higher School Certificate
Trial Examination

Economics

General Instructions

- Reading time – 5 minutes
- Working time – 3 hours
- Write using black pen
- Calculators approved by NESA may be used
- Write your student number and/or name at the top of every page

Total marks – 100

Section I – Pages 2–12
20 marks
- Attempt Questions 1–20
- Allow about 30 minutes for this section

Section II – Pages 13–20
40 marks
- Attempt Questions 21–24
- Allow about 1 hour and 10 minutes for this section

Section III – Pages 21–22
20 marks
- Attempt either Question 25 or Question 26
- Allow about 40 minutes for this section

Section IV – Page 23
20 marks
- Attempt either Question 27 or Question 28
- Allow about 40 minutes for this section

This paper MUST NOT be removed from the examination room

Section I

20 marks
Attempt Questions 1–20
Allow about 30 minutes for this section

Instructions for answering multiple-choice questions

- Select the alternative A, B, C or D that best answers the question. Fill in the response oval completely.

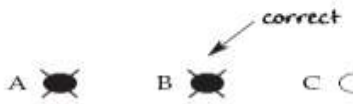
  Sample: 2 + 4 = (A) 2 (B) 6 (C) 8 (D) 9

  A ○ B ● C ○ D ○

- If you think you have made a mistake, put a cross through the incorrect answer and fill in the new answer.

  A ● B ⊗ C ○ D ○

- If you change your mind and have crossed out what you consider to be the correct answer, then indicate the correct answer by writing the word correct and drawing an arrow as follows.

Question	A	B	C	D	Question	A	B	C	D
1	○	○	○	○	11	○	○	○	○
2	○	○	○	○	12	○	○	○	○
3	○	○	○	○	13	○	○	○	○
4	○	○	○	○	14	○	○	○	○
5	○	○	○	○	15	○	○	○	○
6	○	○	○	○	16	○	○	○	○
7	○	○	○	○	17	○	○	○	○
8	○	○	○	○	18	○	○	○	○

9	○	○	○	○	19	○	○	○	○
10	○	○	○	○	20	○	○	○	○

1 Which of the following statements is most correct in relation to centralised wage determination in Australia?

A. Centralised wage determination allows State Governments to determine the national minimal wage.

B. Centralised wage determination occurs between employers and employer associations.

C. Centralised wage determination is used to maintain the national minimum wage adjusted to inflation.

D. Centralised wage determination allows for more flexibility in wage settings reflective of productivity increases.

2 Which of the following is a possible cause of demand-pull inflation?

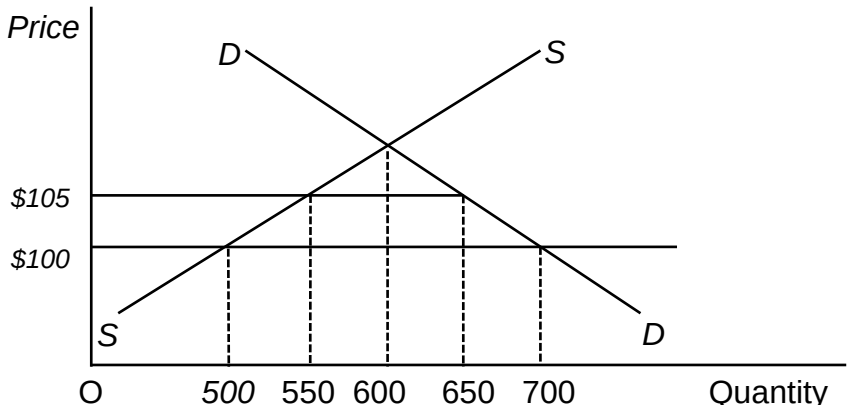
A. Labour shortages are leading to serious production constraints in the manufacturing industry.

B. A reduction in household savings has contributed to higher consumer spending.

C. Chinese COVID-19 lockdowns are causing substantial disruption to global shipping.

D. Coal plant shutdowns and coal supply issues for power generators creating gas and electricity price issues.

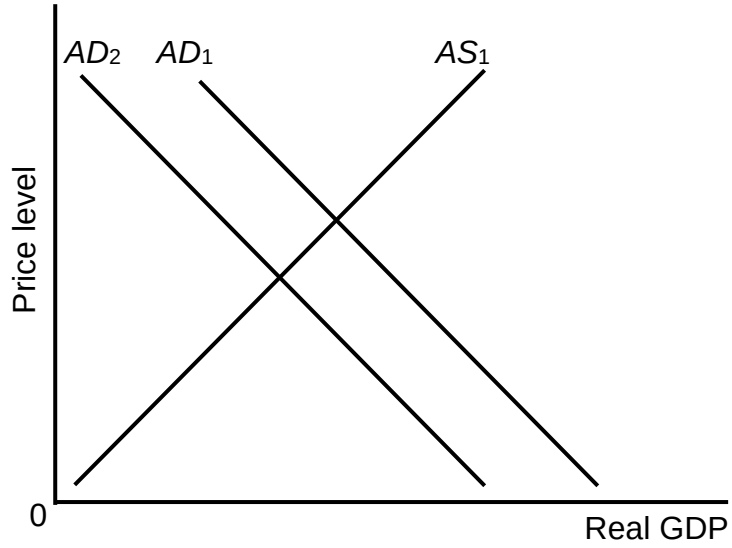
3 The following diagram shows a reduction in tariff protection reducing the price of rice cookers through the removal of a $5 tariff for each cooker sold for a hypothetical economy.



Which row of the table shows the likely effect of the change in tariff on imports and government revenue?

	Imports	*Government revenue*
A.	Increase	Increase
B.	Increase	Decrease
C.	Decrease	Decrease
D.	Decrease	Increase

4 The following diagram shows a drop in aggregate demand for a hypothetical situation for the Australian economy.



All other things being equal, the shift from AD_1 to AD_2 is most likely to have been caused by an increase in which of the following?

A. Lower levels of growth in the Chinese economy

B. Increased consumption of locally made goods and services

C. Increased government expenditure on infrastructure projects

D. Increased productivity of workers in the labour force

5 Which of the following best reflects the current composition of Australia's exports?

A. Australia's largest export category in terms of value is rural exports.

B. Australia's share of manufactured exports is greater than metals and minerals.

C. Australia's share of manufactured exports is greater than service exports.

D. Australia's share of service exports is smaller than exports of metals and minerals.

6 The following table shows data for the labour market of a hypothetical economy.

Population	*Population aged 15 years and over*	*Employed*	*Unemployed*
30 million	24 million	16 million	1 million

Which of the following statements is true for this economy?

A. The unemployment rate is 5.9 per cent and the labour force participation rate is 53 per cent.

B. The unemployment rate is 8.6 per cent and the labour force participation rate is 71 per cent.

C. The unemployment rate 5.9 per cent is and the labour force participation rate is 71 per cent.

D. The unemployment rate is 6.3 per cent and the labour force participation rate is 67 per cent.

7 The following table shows economic data for a hypothetical economy

Year	*Terms of Trade*	*Trade Weighted Index*
1	100	55
2	110	65

Which of the following best explains the change in the Terms of Trade and the Trade Weighted Index from Year 1 to Year 2?

A. The price of exported goods and services decreased compared to imported prices between Year 1 and 2
B. An increase in the production of goods and services for this hypothetical economy
C. The global demand for this economy's currency has improved from Year 1 to Year 2
D. An increase in the demand for this economy's exports of goods and services

8 A hypothetical country records an improvement in its level of economic development.

Which of the following measures would best support this statement?

A. An increase in real gross domestic product and an increase in gross domestic product per capita

B. An increase in real gross domestic product and an increase in educational attainment

C. An increase in gross domestic product per capita and an increase in the productive capacity of the economy

D. An increase in real gross domestic product per capita and an increase in life expectancy

9 The following table shows data for the Australian economy.

Australian assets owned by foreigners ($ billions)	400
Foreign assets owned by Australians ($ billions)	800
Net foreign debt ($ billions)	?
Net foreign liabilities ($ billions)	–1200

What is the value of Australia's net foreign debt?

A. - $800 billion

B. $800 billion

C. $400 billion

D. - $1600 billion

10 A hypothetical economy records a decrease in real Gross Domestic Product (real GDP) over a one-year period.

Which row of the table shows a likely global factor and a domestic factor which could have caused the change in real GDP?

	Global factor	*Domestic factor*
A.	Increase in international borrowing rates	Increase in the marginal propensity to save
B.	Decrease in war induced commodity prices	Decrease in labour supply constraints
C.	Increase in international supply chain disruptions	Increase in discretionary expenditure by the government
D.	Decrease in protectionist polices	Increase in labour productivity

11 An economy is experiencing an increase in its inflation rate yet is achieving full employment in the labour market and a positive rate of GDP growth.

What would be the appropriate stances of monetary and fiscal policies for this economy?

A. An easing of monetary policy and a tightening of fiscal policy

B. A tightening of monetary policy and an easing of fiscal policy

C. An easing of monetary policy and an easing of fiscal policy

D. A tightening of monetary policy and a tightening of fiscal policy

12 Which of the following is least likely to be an effective component of a long-term strategy to achieve net zero carbon emissions?

A. An energy policy strategy that includes measures to encourage households and corporations to change their carbon use

B. A national long-term emissions strategy to guide policy and investment decisions

C. Policies that suppress the structural adjustment required to move to a low carbon economy

D. An economy-wide carbon price to increase incentives for business investment in emissions reducing and clean energy technologies

13 In a hypothetical economy a change in the level of investment of $25 million brings about a new equilibrium level of $600 million when the multiplier is 4.

Which row of the table shows the correct value of the marginal propensity to save (MPS) and the initial equilibrium level of national income?

	Marginal propensity to save	*Initial equilibrium level of national income ($ m)*
A.	0.75	500
B.	0.25	500
C.	0.75	575
D.	0.25	575

14 What are TWO major functions of the International Monetary Fund (IMF)?

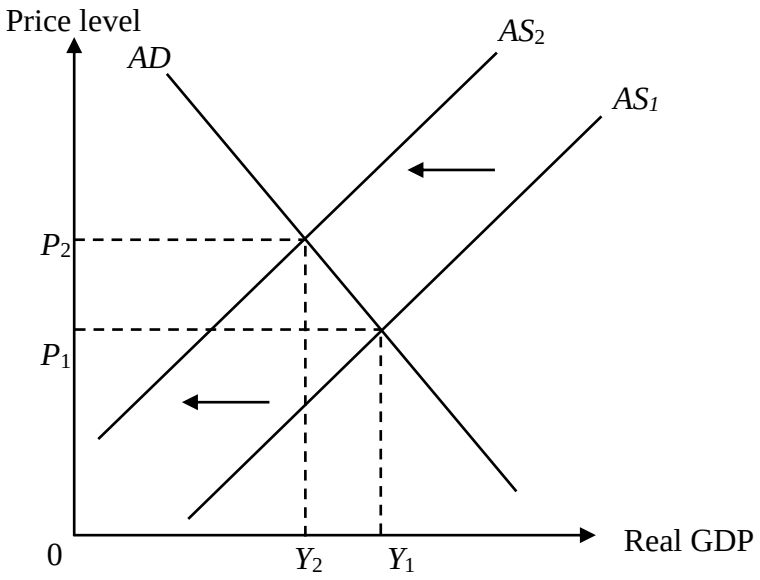
A. The provision of development aid and technical assistance to developing countries

B. The resolution of trade disputes between countries and the promotion of free trade

C. The promotion of global monetary stability and lending to crisis-affected countries

D. The promotion of Sustainable Development Goals and the reduction in global poverty

15 The following diagram shows a shift in the aggregate supply curve from AS_1 to AS_2 for an economy.



What is a possible cause and effect of the shift in the aggregate supply curve?

	Cause	Effect
A	Decrease in labour productivity	Decrease in productive capacity
B	Increase in spending	Decrease in productive capacity
C	Decrease in taxation	Increase in productive capacity
D	Increase in capital productivity	Decrease in productive capacity

16 The following table shows data for a hypothetical economy.

Year	*Nominal GDP \$ millions*	*CPI*
1	1600	100
2	1850	110

What is the real level of GDP (to the nearest whole number) in Year 2?

A. \$1600 million

B. \$1682 million

C. \$1850 million

D. \$1455 million

17 Which of the following statements is correct regarding the Long Run Phillips Curve?

A. Higher inflation can be traded off for less unemployment.

B. Lower inflation can be traded off for more unemployment.

C. There is a perfect trade-off between inflation and unemployment.

D. There is no trade-off between inflation and unemployment.

18 Which of the following would be considered the least effective microeconomic reform policy initiative?

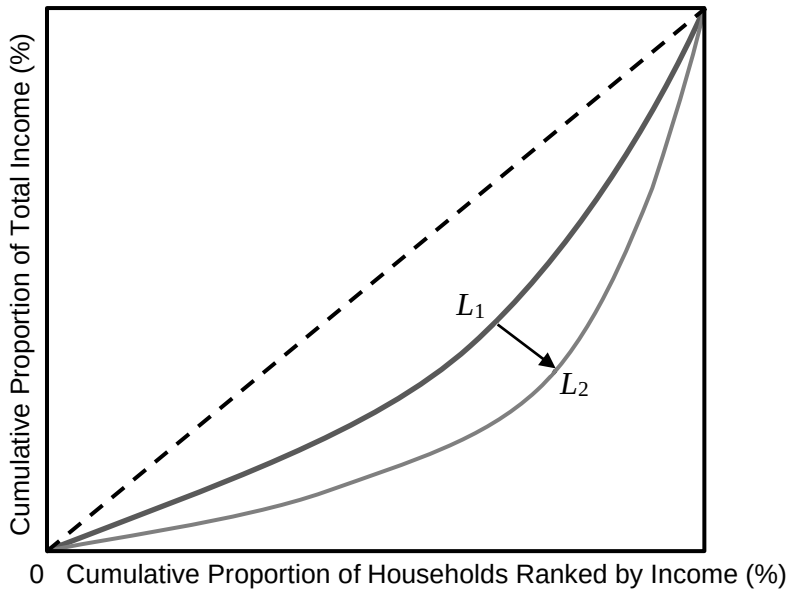
A. The government announces a funding allocation to upgrade the electricity transmission network between Australian states to improve the efficiency of the national energy market.

B. The government looks to create new competition policy legislation to improve consumer outcomes in Australian retail markets.

C. The government looks to reduce the level of JobSeeker payments to encourage the unemployed to take advantage of job opportunities.

D. The government announces a 'revenue neutral carbon tax' to help Australia reach the target of net zero emissions by 2050.

19 The following diagram shows the movement of the Lorenz Curve from L_1 to L_2.



Which of the following correctly describes the effects of the movement of the Lorenz Curve from L_1 to L_2?

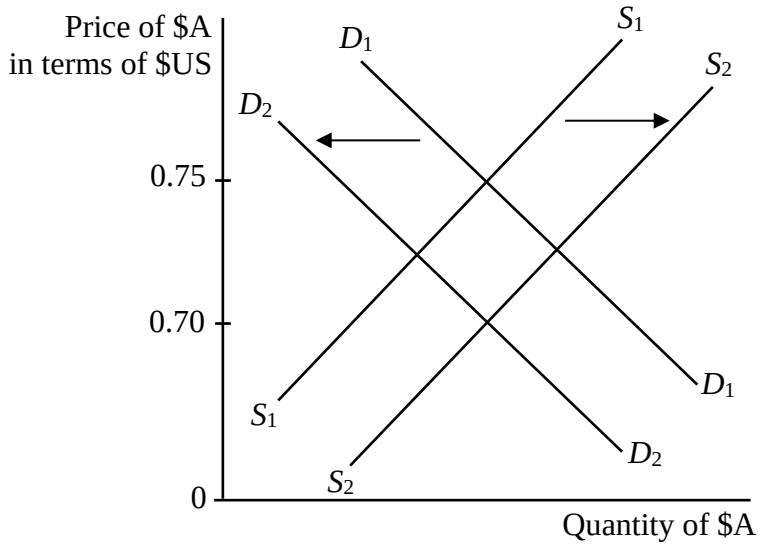
A. An increase in the Gini co-efficient and a reduction in income inequality

B. An increase in the Gini co-efficient and an increase in income inequality

C. A decrease in the Gini co-efficient and a reduction in income inequality

D. A decrease in the Gini co-efficient and an increase in income inequality

20 The following diagram represents recent movements in the demand and supply for Australian dollars in the foreign exchange market.



Assuming a floating exchange rate, which of the following actions could have caused the exchange rate to move from $US0.75 to $US0.70?

A. China imposes restrictions on the importing of Australian agricultural products and global oil prices increase.

B. Australian farmers experience increased export demand for their grain harvest while supply shortages lead to longer wait times for new imported vehicle purchases.

C. More Australians travel overseas for long awaited holidays while overseas tourist arrivals into Australia rise to levels not seen since the start of the Covid-19 pandemic.

D. The Reserve Bank of Australia raises official interest rates again and the Australian dollar falls as foreign investors respond accordingly.

Section II

40 marks
Attempt Questions 21–24
Allow about 1 hour and 10 minutes for this section

Answer the questions in the spaces provided. These spaces provide guidance for the expected length of response.

Question 21 (10 marks) **Marks**

(a) Outline ONE reason for a country entering into a bilateral trade agreement with a major trading partner. **2**

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(b) Distinguish between a bilateral trade agreement and a multilateral trade agreement. **2**

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(c) Discuss the impacts of ONE multilateral trade agreement on the Australian economy. **6**

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End of Question 21

Question 22 (10 marks)
Marks

(a) Outline what is meant by *environmental sustainability.* **1**

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(b) Explain the potential impact on the environment of continuing world economic development in both the short term and long term. **4**

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(c) Analyse the policies that the Australian government could use to reduce Australia's greenhouse gas emissions in both the short and long-term. **5**

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End of Question 22

Question 23 (10 marks) **Marks**

The following table shows balance of payments data for a hypothetical economy with a floating exchange rate.

Balance of payments components	*$ billions ($bn)*
Export goods	60
Import goods	30
Service credits	40
Service debits	100
Net primary income	–10
Net secondary income	–5

(a) What is the balance on the capital and financial account? **1**

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(b) An Australian investor purchases a 15% stake or equity in a foreign company. **4**

Explain how this transaction could impact on TWO components of Australia's balance of payments.

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Question 23 continues on the next page

Question 23 (continued) **Marks**

(c) Examine the causes of recent trends, over the last ten years, in the accounts within Australia's balance of payments. **5**

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End of Question 23

Question 24 (10 marks) **Marks**

The following table shows data for a hypothetical economy.

	Real Gross Domestic Product ($) billions	Consumer Price Index (CPI)
Year 1	10	110
Year 2	10.5	118

(a) Calculate the rate of growth in Real Gross Domestic Product (GDP) from Year 1 to Year 2. **1**

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(b) Calculate the inflation rate from Year 1 to Year 2. **1**

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(c) Explain why there may be a conflict in an attempt by a government to simultaneously achieve economic growth and price stability. **4**

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Question 24 continues on the next page

(d) Assess how a government's use of microeconomic reform policies to improve economic growth may conflict with its other objectives. **4**

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End of Question 24

Section III

20 marks
Attempt either Question 25 or Question 26
Allow about 40 minutes for this section

Answer the question on your own paper or in a writing booklet, if provided. Start the question on a new page.

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

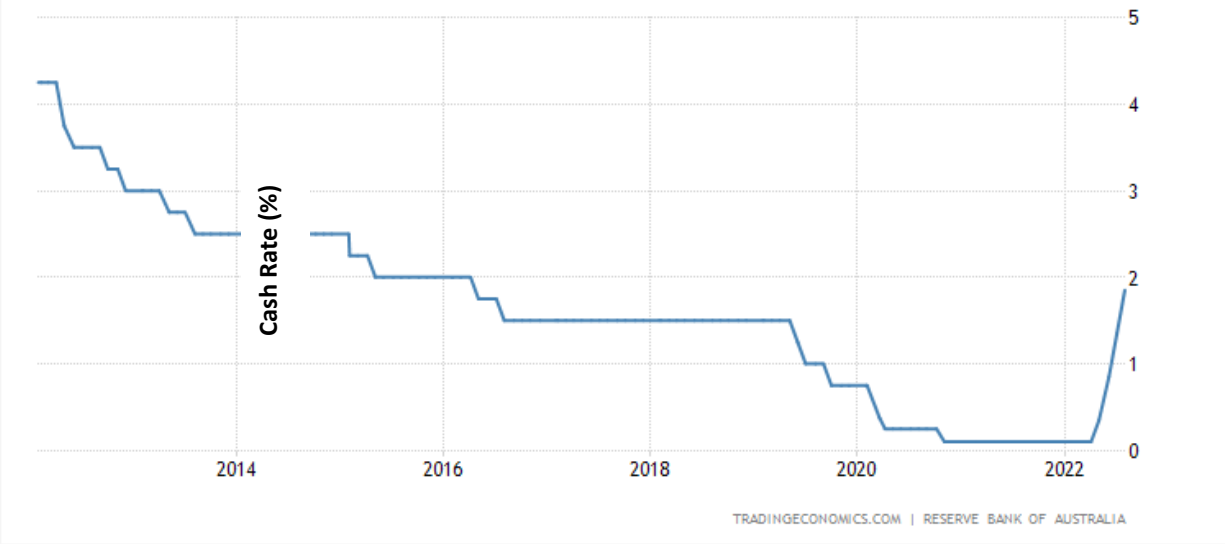
- demonstrate knowledge and understanding relevant to the question
- use the information provided
- apply relevant economic terms, concepts, relationships and theory
- present a sustained, logical and cohesive response

Question 25 (20 marks)

Explain how changes in the stance of monetary policy can impact on economic activity and the exchange rate. In your answer refer to the information provided.

> The Board judged that, given the inflation data and outlook … , it was no longer appropriate for interest rates in Australia to remain at COVID-emergency levels. The increase in the cash rate in May followed the higher-than-expected CPI outcome in the March quarter and evidence from business surveys and our own liaison that growth in labour costs had picked up and would continue to do so in the months ahead. In June, we decided to make a bigger, 50 basis points, adjustment on the basis of the additional information suggesting a further upward revision to an already high inflation forecast. The Board also gave consideration to the fact that the level of interest rates was still very low.
>
> Source: **Philip Lowe,** Governor, Reserve Bank of Australia,
> **Speech to the American Chamber of Commerce in Australia (AMCHAM)**
> Sydney – 21st June, 2022.

Australian Cash Rate Target



OR

Question 26 (20 marks)

Explain the use of fiscal policy by the Australian government to achieve the objectives of economic growth and full employment. In your answer refer to the information provided.

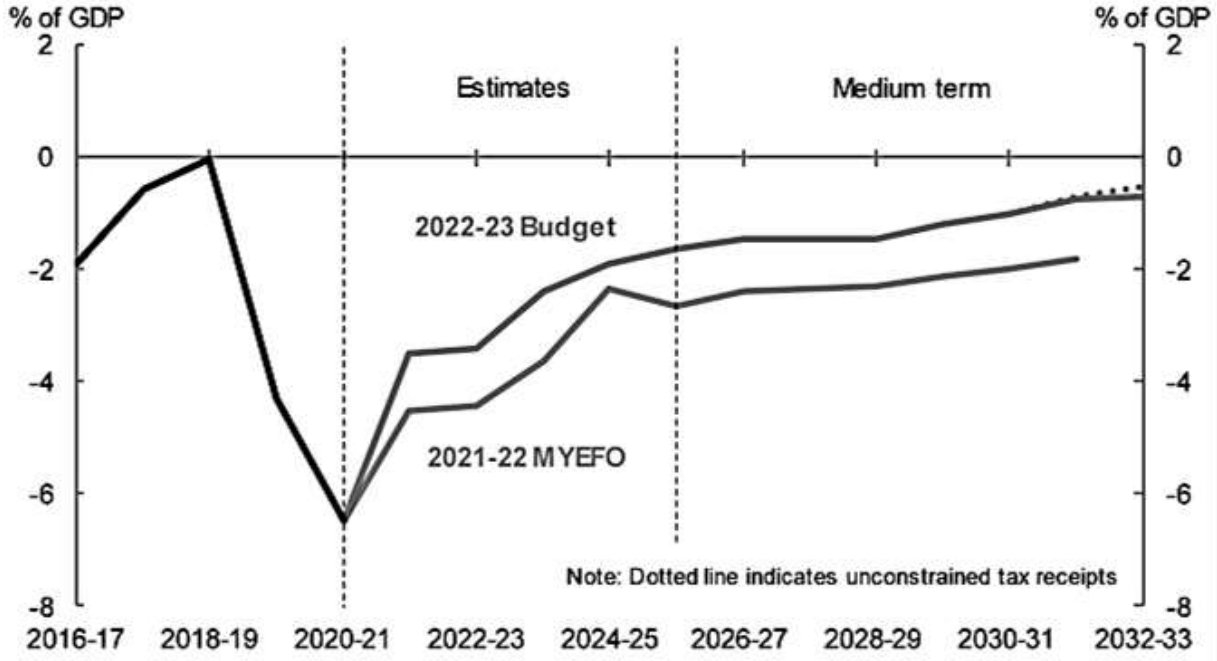
Economic and Fiscal Strategy

"The Government's economic plan, focused on job creation, is working. Amid the ongoing COVID-19 pandemic and natural disasters at home, the Australian economy has outperformed all major advanced economies, experiencing a stronger recovery in output and employment from pre-pandemic levels. The recovery is expected to continue with the unemployment rate forecast to reach 3.75% in the September quarter 2022.

Having achieved the objective of low unemployment, the Government has transitioned to the next phase of the Economic and Fiscal Strategy, which focuses on growing the economy in order to stabilise and reduce debt as a share of the economy."

Source: Commonwealth of Australia (2022), Budget Strategy and Outlook, Budget Paper No.1, 2022-23

Underlying cash balance



Source: Commonwealth of Australia (2022), *Budget Strategy and Outlook*, Budget Paper No. 1, 2022-23.

Note – MYEFO is the Mid-Year Economic and Fiscal Outlook.

Section IV

20 marks
Attempt either Question 27 or Question 28
Allow about 40 minutes for this section

Answer the question on your own paper or in a writing booklet, if provided. Start the question on a new page.

In your answer you will be assessed on how well you:
- demonstrate knowledge and understanding relevant to the question
- apply relevant economic information, terms, concepts, relationships and theory
- present a sustained, logical and cohesive response

Question 27 (20 marks)

Analyse the global and domestic causes of inflation in Australia and possible economic policy responses.

OR

Question 28 (20 marks)

Analyse recent trends in unemployment and income inequality and their impact on the Australian economy.

END OF PAPER

Answer Guide

Section 1

1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20
C	B	B	A	D	C	D	D	A	A	D	C	B	C	A	B	D	C	B	A

Section 2

Q21a (Outline)

Sketches in general terms ONE reason a country enters a bilateral FTA	**2**
Provides some general information about why a country may enter a bilateral FTA	**1**

Reasons may include:

- Achieve a reduction in protection to promote economic growth
- Increase a country's exports to improve external stability
- Reduce domestic prices- Reduce inflation
- Increase competitiveness (efficiency)

Q21b (Distinguish)

Correctly indicates the difference between a bilateral and a multi- lateral trade agreement	**2**
Provides some general information about either a bilateral or multi-lateral trade agreement	**1**

Difference is:

A bilateral FTA is between two countries and involves a reduction or removal of protection to promote trade between the two countries (Australia-USA), whereas a multilateral FTA is between 3 or more countries and its favourable over a bilateral FTA as it results in more trade between a greater number of countries (AANZFTA).

Q21c (Discuss) Identify issues and provide points for and/or against

Discuss the impacts of ONE multilateral trade agreement on the Australian economy.

Thoroughly discusses (identifies issues and provides points for and against) the impacts of one bilateral trade agreement on the Australian economy	**6**
Discusses (identifies issues and provides points for and against) the impacts of one bilateral trade agreement on the Australian economy	**5**
Demonstrates an understanding of the impacts of one bilateral trade agreement on the Australian economy	**4**

Demonstrates some understanding of the impacts of one bilateral trade agreement on the Australian economy	**3**
Provides general information of a trade agreement on the Australian economy	**2**
Provides basic information of a trade agreement on the Australian economy	**1**

Discusses the impacts (uses and example) which may be positive and/or negative and may include:
Negative impacts may include structural and regional unemployment, dumping, negative impact on infant industries
Positive impacts may include new investments leading to further economic growth and employment , transfer of technology, improved competition, lower inflation, improvement in the movement of labour. Higher levels of efficiency, improved terms of trade, higher levels of exports, improved external stability/CAD . Lack of trade may depreciate the $A and worsen out repayment issues.

22a (Outline)

Sketches in general terms what is meant by environmental sustainability	1

Outlines that individuals, firms and governments use natural resources is such a way that they are not diminished for future generations

22b (Explain)

Demonstrates a comprehensive understanding of the potential impact on the environment of continuing world economic development in both the short and long term	4
Demonstrates a sound understanding of the potential impact on the environment of continuing world economic development in both the short and long term	3
Demonstrates some understanding of the potential impact on the environment of continuing world economic development in (both or one) in the short and long term	2
Provides some general information on the impacts on the environment	1

Explains potential impacts and may include:
Higher economic growth can deteriorate the environment in the short term through pollution and depletion of natural resources such as mineral as more resources are used to increase production and satisfy consumer demand and economic growth and development

In the long term as economic growth and development occurs, incomes increase, economies are able to invest back into the environment through sustainable practises(fish farming, crop

rotation techniques) use of renewable energy etc and the environment recovers in the long term.

22c (Analyse) shows the implications"

Identify components and the relationship between them; draw out and relate implications

Analyse the policies that the Australian government could use to reduce Australia's greenhouse gas emissions in both the short and long-term **5**

Clearly identifies policies used and shows the implications of those policies in reducing Australia's gas emissions in both the short and long term	5
Identifies policies used and shows the implications of those policies in reducing Australia's gas emissions in both the short and long term	4
Identifies some aspect of a policy used and their relationship (impact) in reducing Australia's gas emissions in both or both the short and long term	3
Provide some relevant information of a policy and its impact on the environment	2
Minimal information that relates to the question	1

Analyses short term polices that can be used in the short term:
1. Renewable energy target that targets periodically an increase in the usage if renewable electricity (repeats each 12 months)
2. Emissions Reduction Target (Emissions Reduction Fund) _ formally Direct action that aimed to reduce greenhouse emissions by voluntary means

Analyses long term polices such as;
1. Signed COP26 commitment to aim for zero emissions by 2050
2. Invest $20 billion in new technologies

Other?

23(a)

Criteria	Marks
• Correctly calculates the value of the capital and financial account to be a surplus of $45 billion	**1**

Answers could include:
Balance on Current Account + Balance on Capital and Financial Account = 0 Balance on Current Account =
Balance on Goods (Exports- Imports)+ Balance on Services (Credits- Debits) + Net Primary Income + Net Secondary Income

Balance on Current Account= +30 :- 60 - 10- 5 Balance on Current Account =- $45 billion deficit

Therefore, the Balance on Capital and Financial Account must be equal to a $45 billion surplus under a floating exchange rate system.

N.B.

- **Read the question carefully - the vast majority got this wrong by writing -$45b (it is asking for KAFA, not CA).**
- **Show your working**
- **Use $ and state billions (or use $45b)**
- **Learn how to do this as it will be an easy mark in the HSC**

Question 23(b) *Outcomes assessed: H3*

Criteria	Marks
• Demonstrates a comprehensive understanding of how this transaction could impact on TWO components of Australia's balance of payments (e.g., the current account and the capital and financial account)	4
• Demonstrates a sound understanding of how this transaction could impact on TWO components of Australia's balance of payments	3
• Demonstrates some understanding of how this transaction could impact on at least ONE component of Australia's balance of payments	2
• Provides some relevant information on Australia's balance of payments	1

Answers could include:

- Debit in the financial account from the outflow of investment funds
- A future credit in the NPY account in the form of dividends and profits received
- Effects on KAFA and CA from these flows

NB

- **It was good that hardly any introductions or conclusions were used**
- **Don't leave line gaps in your responses**
- **Better responses referred to non-reversible transactions and debit and credits to give details on the transition and where it goes**
- **ST & LT was best for clarity of when the changes are recorded. There must be a simultaneous change in two areas of the BOP for any transaction (a debit and credit) but income flows on the investment would not be instantaneous**
- **To get 4 marks you needed to clearly state that the changes in the current account from NPY credits were not at the same time but future LT effects**
- **You need to show HOW the transaction impacts on the accounts e.g. what makes it a credit or debit**
- **Many stated tat the BOP is in deficit or surplus which is never correct – only the KAFA or CA can be**
- **Some incorrectly stated the foreign investment leads to interest payments (it's dividends or profits)**
- **Repayments on investments are in the financial account, not the NPY as you are reversing the original transaction and removing it from the BOP**

Sample answer

This transaction would be recorded as a debit on the financial account in Australia's balance of payments. Since the investor has purchased greater than a 10% stake in a foreign company, it would be recorded as a debit in the direct investment category of the financial account. In turn, this could lower Australia's capital and financial account surplus or increase Australia's capital and financial account deficit. Because of this transaction, the Australian investor will eventually receive income from the foreign company in the form of dividends and profits remitted from overseas. When this eventuates, this will be recorded as a credit on Australia's net primary income (NPY) in the current account. This would result in a lowering of Australia's current account deficit, or it could increase Australia's current account surplus.

Question 23(c) *Outcomes assessed: H1, H3, H4*

Criteria	Marks
• Demonstrates a comprehensive understanding of the causes of recent trends, over the last 10 years, in accounts within Australia's balance of payments (e.g., the current account and capital and financial account)	5
• Demonstrates a sound understanding of the causes of recent trends, over the last 10 years, in accounts within Australia's balance of payments	4
• Demonstrates some understanding of the causes of recent trends, over the last 10 years, in accounts within Australia's balance of payments	3
• Provides general information on the causes of trends in Australia's balance of payments	2
• Provides some relevant information about Australia's balance of payments	1

Answers could include:

- Current account deficit/surplus data
- Capital account deficit data
- Capital and financial account data – surplus and/or deficit
- Balance of goods and services data
- Net primary income data
- Cyclical causes of current account trends – exchange rate volatility, volatility in the international business cycle and domestic business cycle, speculative investment
- Structural causes of current account trends – narrow export base; lack of international competitiveness in manufacturing; long-term prices for commodities or agriculture; savings/investment gap and overseas borrowing; reliance on imports of consumer, capital and intermediate goods; capacity of mining industry and the need for foreign investment funds
- Structural causes of the capital and financial account balance – investment opportunities in Australia and abroad; savings/investment gap in Australia; low household savings ratio in Australia; Australia's growing superannuation pool and the desire of super fund managers and their clients to invest offshore to earn higher rates of return on investment funds.

N.B.

- **To get 5 marks you need to refer to Australia's recent CAS**
- **Use correct punctuation (BOGS not "bogs")**
- **Spelling of deficit was done incorrectly by a large number**

- **Many said the BOP was in deficit which is never the case (CA or KAFA will be)**
- **Better responses referred to which subaccount was affected e.g. NPY, financial etc.**
- **Depth on fewer ideas is needed to get to top marks. You have to show HOW the trends impacted the accounts**
- **Always ensure you state the direction of any flows**
- **Many said that COVID was in 2019 – 2020 it started to impact the world**
- **Interest and debt payments are different concepts so use them in the correct areas – interest (NPY) and debt (financial)**
- **Covid didn't cause the CAS as it was existing beforehand from TOT boom**
- **Again, simultaneous changes from the one transaction of debt or investment don't occur**
- **Be definitive in your response. Don't say "May have been caused", instead say something like "contributed to"**

Question 24(a) *Outcomes assessed: H11*

Criteria	Marks
• Correctly calculates the rate of growth in Real Gross Domestic Product (GDP) from Year 1 to Year 2	1

Answers could include:

Rate of growth of Real GDP = (Current GDP – Previous GDP) / Previous GDP × 100/1
= ($10.5b – $10b) / $10b × 100/1
= 5%

Therefore, the rate of growth in real GDP from Year 1 to Year 2 was 5%.

Question 24(b) *Outcomes assessed: H11*

Criteria	Marks
• Correctly calculates the inflation rate from Year 1 to Year 2	1

Answers could include:

Inflation rate = (Current CPI – Previous CPI) / Previous CPI × 100/1
= (118 – 110) /110 × 100/1
= 7.27%

Therefore, the inflation rate between Year 1 and Year 2 was 7.27%.

24 C (Explain)

Demonstrates a comprehensive understanding on why there may be a conflict in an attempt by a government to simultaneously achieve economic growth and price stability	4
Demonstrates a sound understanding on why there may be a conflict in an attempt by a government to simultaneously achieve economic growth and price stability	3
Demonstrates some understanding on why there may be a conflict in an attempt by a government to simultaneously achieve economic growth and price stability	2
Provides some general information on the possible conflict	1

Answers may include:
Economic growth is achieved through a combination of macro/micro policies. Growth normally leads to increased consumer demand. This could create demand pull inflation as the basic economic problem is unlimited wants vs limited resources. High economic growth can also create a shortage of labour who demand higher wages, (cost push inflation), therefore leading to a high cost in production which is past on to the consumers.

24 d (Assess)

Makes a comprehensive judgement (end outcome/result) on how a government may use micro reforms to improve growth but may conflict with other economic objectives	4
Demonstrates a sound judgement (end outcome/result) on how a government may use micro reforms to improve growth but may conflict with other economic objectives	3
Demonstrates basic judgement (end outcome/result) on how a government may use micro reforms to improve growth but may conflict with other economic objectives	2
Provides some general on how a government may use micro reforms to improve growth but may conflict with other economic objectives	1

Answers may include

Micro reforms aim to improve efficiency , productivity and competitiveness in the long. However, they may conflict with: (You must assess TWO)
1. structural unemployment, which in Australia is short term and the government has provided adequate support to get those who are structurally unemployed upskilled and into new jobs.
2. As micro reforms improve efficiency and productivity the more skilled workers are better able to negotiate better wages based on improved efficiency which has increased income inequality in the long term
3. As micro reforms improve an economy as it operates at full capacity labour shortages can push up wages and contributing to cost push inflation as it happed in Australi in the 2000's and again in the 2010's during the mining booms.

PLEASE NOTE: These extended response guides are lengthy and are an indicator of the various aspects of the essay that can be covered.

Question 25

	Marks
• Synthesises own knowledge and understanding with the information provided, to develop a sustained, logical and cohesive response • Integrates relevant economic terms, concepts, relationships and theory • Demonstrates a clear and comprehensive understanding of how changes in the stance of monetary policy can impact on economic activity and the exchange rate	**17-20**
• Synthesises own knowledge and understanding with the information provided, to develop a logical and cohesive response • Applies relevant economic terms, concepts, relationships and theory • Demonstrates a sound understanding of how changes in the stance of monetary policy can impact on economic activity and the exchange rate	**13-16**
• Uses own knowledge and understanding with the information provided, to develop a coherent response • Uses relevant economic terms, relationships and theory • Demonstrates some understanding of how changes in the stance of monetary can impact on economic activity AND/OR the exchange rate	**9-12**
• Presents a generalised response • Uses some economic terms • Sketches in general terms some aspects of how changes in the stance of monetary policy can impact on economic activity AND/OR the exchange rate	**5-8**

• Presents a limited response • Uses some economic terms and concepts • Lists some aspects of EITHER changes in the stance of monetary policy on economic activity OR the exchange rate	**1-4**

Essay plan: Monetary policy is the macroeconomic policy instrument that is concerned with influencing the cost and availability of money and credit in the Australian economy. Changing the stance of monetary policy through changing the cash rate impacts on the level of economic activity and the exchange rate through a process known as the monetary policy transmission mechanism. Monetary policy is one of two macroeconomic policies that can be used to address issues with aggregate demand in the economy. The other instrument is the Australian government's use of fiscal policy. The main objectives of monetary policy are the stability of the currency of Australia, the maintenance of full employment and the economic prosperity and welfare of the people of Australia

The responsibility for conducting monetary policy lies with the Reserve Bank of Australia (RBA) which is a statutory body operating independently from the Australian government. In attempting to achieve its objectives the RBA has an inflation target of between 2 per cent and 3 per cent on average over the economic cycle. The target is set in terms of the underlying inflation rate which excludes anomalies from the headline inflation rate. However, the Reserve Bank interprets and analyses a wide range of measures of consumer price inflation.

The RBA implements monetary policy by using a range of tools. The main conventional tool of monetary policy is the cash rate target and the policy interest rate corridor. The RBA also has a range of unconventional monetary policy tools that it can use such as quantitative easing and forward guidance. Changes in the stance of monetary policy occur when the Reserve Bank Board announces a change in the cash rate target. This occurs at a media release on the first Tuesday of each month of each year, except in January. There are three stances of monetary policy which the RBA can adopt:

- A contractionary stance, when the cash rate is raised to address inflationary concerns and dampen the level of economic activity by increasing the cost of borrowing

- An expansionary stance, when the cash rate is lowered to stimulate economic activity and reduce unemployment, by lowering the cost of borrowing
- A neutral stance when there is no change in the cash rate

When the RBA changes the cash rate target it is achieved through shifting the policy interest rate corridor in the cash market. The corridor provides a mechanism for implementing changes to the cash rate target. The corridor is central to how the RBA implements monetary policy, especially in relation to changing the stance of monetary policy. The change in the stance of monetary policy encourages banks to trade their Exchange Settlement balances at the cash rate target.

Following a change to the stance of monetary policy the cash market automatically trades at the new cash rate. This is achieved by the policy interest rate corridor, which resets around the new cash rate target, and banks have no incentive to trade outside of this corridor.

Since the COVID-19 recession in 2020, the RBA has also used a range of unconventional monetary policy tools. This has included forward guidance which refers to public commitments made by the RBA as to how it will conduct monetary policy in the future. As well, in 2020 the RBA introduced explicit pricing and quantity targets for the purchase of government bonds in order reduce longer-term interest rates and increase liquidity during the COVID-19 recession. Other unconventional monetary policy tools include term funding facilities, adjustments to market operations and negative interest rates.

By changing the stance of monetary policy, the RBA attempts to influence domestic interest rates and the level of economic activity through the monetary policy transmission mechanism. The transmission mechanism operates through changes in household borrowing and saving, consumer spending patterns, investment by firms, the supply of credit and asset prices. A change in the stance of monetary policy may also impact on Australia's exchange rate.

When the RBA increases the cash rate, the purpose of the contractionary stance is to curb the level of aggregate demand and reduce inflation and inflationary expectations in the economy. This was evident in mid to late 2007 and early 2008 with excessive

growth in aggregate demand causing inflation to rise to 4.5 per cent which was outside the target band of 2 per cent to 3 per cent. This was coupled with a tight labour market and high levels of capacity utilisation. By June 2008, aggregate demand had moderated due to a decrease in household spending, a reduction in the demand by households for credit and the number of businesses requiring credit for purchases and investment.

The cash rate was raised by the RBA on four occasions from 6.25 per cent in July 2007 to 7.25 per cent in March 2008. The higher interest rates helped to put upward pressure on the exchange rate. The higher returns increased the demand for Australian assets and attracted more foreign investors. During this period the Australian dollar appreciated against the US dollar from US$0.78 in 2006-07 to US$0.89 in 2007-08. Despite the rise in the Australian dollar, higher world commodity prices were supporting the level of economic activity.

Between September 2008 and April 2009, the RBA lowered the cash rate from 7 per cent to 3 per cent in response to declining global and domestic economic conditions brought about by the Global Financial Crisis (GFC). This easing in the stance of monetary policy was designed to support spending and aggregate demand in an attempt to underpin economic and employment growth to prevent rising levels of unemployment. Inflation pressures at this time had eased and inflation was within the Reserve Bank's target band of 2 per cent to 3 per cent. However, the unemployment rate had begun to rise from a low of 4.2 per cent and reached 5.8 per cent by 2009. The easing in monetary policy helped to support consumer and business confidence with higher cash flows through cuts to interest rates including mortgage rates and business borrowing rates. The global recession led to a fall in global commodity prices which led to a depreciation in the value of the Australian dollar against all currencies. The depreciation of the Australian currency was further impacted by the lower interest rate environment. The depreciation in the exchange rate helped to support the competitiveness of export and import competing industries.

A contractionary stance was adopted by the RBA from October 2009 until November 2010. Over this period of time there were seven increases in the cash rate from 3.25 per cent to 4.75 per cent. This

stance was deemed necessary by the RBA as inflation showed signs of moderate growth.

There was also growth in expenditure by the public sector, and global economic growth added to domestic demand in the Australian economy. The impact of these changes in interest rates became evident in early 2011 as household spending became more cautious and savings started to increase. As well, asset values steadied. This was apparent, for example, in a more subdued housing market. The Australian dollar continued to appreciate against the major currencies of Australia's trading partners, underpinned by the global resources boom and rising interest rates.

The contractionary stance adopted by the RBA remained in place until November 2011. At this point in time the Reserve Bank Board decided that a change in the stance of monetary policy to an expansionary stance was necessary. The cash rate was lowered from 4.75 per cent to 4.50 per cent.

From November 2011 to August 2013 the stance adopted by the RBA continued to be expansionary with the cash rate being lowered on seven occasions. The last change was in August 2013 when the cash rate was lowered to 2.5 per cent. The easing of monetary policy had supported "interest sensitive spending" for example through the housing market. This had had an effect on asset prices which increased during this time.

From November 2011 to August 2013 the stance adopted by the RBA continued to be expansionary with the cash rate being lowered on seven occasions. The last change was in August 2013 when the cash rate was lowered to 2.5 per cent. The easing of monetary policy had supported "interest sensitive spending" for example through the housing market. This had had an effect on asset prices which increased during this time.

The easing of monetary policy from late 2011 until April 2013 started to impact through a range of transmission channels during this time. The flow-on effect continued into 2014 as demand picked up in the housing market as low interest rates were accommodating and supported the borrowing of funds. As well, asset prices increased. This view was expressed by the Reserve Bank Governor at the time in the *Statement on Monetary Policy* when he stated that "dwelling prices have increased significantly over the past year".

Australian Bureau of Statistics (ABS) figures released in March 2014 also showed that lower interest rates were encouraging spending, as retail sales figures had increased by 6.2 per cent over the same period of time.

From November 2011 to August 2013 the stance of monetary policy was expansionary. The lowering of the cash rate had an impact on the exchange rate as the Australian dollar against the US dollar depreciated from US$1.03 in 2011-12 to US$0.89 in 2012-13. The easing of monetary policy along with a fall in global commodity prices and a strengthening in the US dollar assisted the re-balancing of growtl1 in the Australian economy. The exchange rate was still considered to be high by historical standards in June 2014. A lower exchange rate was considered necessary by the RBA Governor to restore competitiveness in export and import competing industries such as manufacturing, education and tourism.

The cash rate remained at 2.5 per cent from August 2013 until February 2015. Following this period, the RBA cut the cash rate seven times from February 2015 until October 2019 when the cash rate stood at 0.75 per cent. The expansionary stance of monetary policy adopted by the RBA Board during 2015 and 2016 was due to a combination of overseas and domestic factors. The predominant overseas factor was a moderation in growth of the global economy, including China's growth rate. Domestically a decline in commodity prices, a lower term of trade and a slightly sluggish labour market, were important factors when the Board considered determining the stance of monetary policy. The easing of monetary policy to support economic activity was particularly relevant in underpinning domestic demand, household credit and business investment which support economic growth.

From August 2016 until June 2019 the cash rate remained at 1.5 percent. In June, July and October 2019 the RBA reduced the cash rate in each of these months by 0.25 per cent to 0.75 per cent. The RBA's expansionary stance was deemed necessary in order to support the level of economic activity through the transmission mechanism. There continued to be uncertainty in relation to consumption, income and employment growtl1 which were not as strong as expected. As well, the demand for housing credit remained sluggish. Global trade disputes between China and the USA and Australia were also having an impact on export

industries. In their media release in October 2019 the RBA Board stated it was "prepared to ease monetary policy further if needed".

The underlying weaknesses in the Australian economy made it vulnerable to the severe economic impacts which were forecast after the confirmation of the rapid global spread of the coronavirus (COVID-19) pandemic. The Australian government took its first actions to restrict in-bound travel to Australia in early February 2020 and the World Health Organisation (WHO) declared COVID-19 a pandemic in March 2020. The coronavirus outbreak had near immediate impacts on the overseas education and travel sectors of the Australian economy.

The decision by the RBA Board in March 2020 to lower the cash rate by 25 basis points to 0.50 per cent was made in light of the global COVID-19 outbreak. This expansionary stance of monetary policy was important in supporting the Australian government's economic objectives of sustainable economic growth and full employment. Achieving these two objectives would assist in lifting inflation within the targeted range of 2 per cent to 3 per cent.

Following the RBA Board's decision in early March, the coronavirus was impacting at a rate which was extremely damaging to the global economy and the domestic economy. The Australian government introduced a large package of fiscal and financial support. The support packages were critical to the economy, businesses and individuals. The main support packages were announced from 12th March to 30th March 2020, with ongoing smaller stimulus packages continuing to be announced by the Australian, state and territory governments.

With forecasts of a looming recession for many countries, including Australia, the RBA Board held an emergency meeting on 19th March 2020. The decisions made by the Board at the meeting were to complement the fiscal response of the Australian government. The Board announced a further reduction in the cash rate to 0.25 per cent. As well, other unconventional monetary policy tools such as a large government bond purchase prograrnme were used to lift the level of economic activity. In November 2020, a further support package was announced by the Board with a reduction in the cash rate to 0.1 per cent. This expansionary stance of monetary policy remained in

place until May 2022.

The economic impact of the easing of the cash rate to a historical low level coupled with expansionary fiscal policy supported the economy through the global and domestic downturn. By May 2021 the economic recovery in Australia was stronger than expected and unemployment was declining, standing at 5.5 per cent. Inflation was still subdued and below the RBA's target

. band. Given the low borrowing rates, the housing market across Australia was very strong leading to a rise in asset prices. Over 2021, Sydney's housing market had a year-on-year growth of 33.1 per cent in house prices. In the early stages of the pandemic, the low interest rate environment and the state of the global economy impacted on the exchange rate. The Australian dollar depreciated to a low ofUS$0.55 in March 2020. Over the following 12 months despite the low cash rate the Australian dollar appreciated due to high commodity prices for Australian iron ore, coal and liquified natural gas. The terms of trade improved during this time. The Australian dollar peaked against the US dollar in February 2021 at US$0.79 cents.

The low interest rate environment adopted by the RBA Board was still the focus of monetary policy in February 2022 as the RBA Board's objectives of full employment and inflation operating within the target band remained in place. However, in March 2022 a combination of factors, including the war in the Ukraine, the spike in energy prices and global supply chain constraints were impacting on inflation. In May 2022, the RBA Board decided, "given the inflation data .and outlook" to change the stance of monetary policy from an expansionary stance to a contractionary stance by lifting the cash rate by 0.25 per cent to 0.35 per cent. The RBA Board determined, "it was no longer appropriate for interest rates in Australia to remain at the COVID-emergency levels."

The increase in the cash rate in May 2022 was followed by an increase in the cash rate by 0.50 per cent to 0.85 per cent in June 2022 and then by 0.50% to 1.35% in July 2022. The large increases in the cash rate were based on, "the additional information suggesting a further upward revision to an already high inflation forecast." These have been the largest rate rises in Australia in 22 years and the first 'back-to-back' rate rises since May 2010. Forecasts suggest that the cash rate might be around 2.5 per cent by

mid to late 2023.

Key to adopting a contractionary stance of monetary policy by the RBA Board was that inflation had increased to the highest rate in a number of years. Headline inflation was 2.1 per cent over the March quarter 2022 and 5.1 per cent over the year and underlying inflation was 3.7 per cent.

It is expected that inflation will increase further in the coming year before returning to the targeted band of 2 per cent to 3 per cent. The effects of contractionary monetary policy are likely to have wide ranging implications, however, the extent of these effects is difficult to predict at this stage. Higher interest rates will impact on mortgage repayments with Australian household debt levels being among the highest in the world. The impact on consumption at this stage is uncertain, as is the impact on investment. With many businesses still recovering from the pandemic and recording lower profits, having to deal with higher interest rates may present a challenge in containing their costs of production.

The Australian dollar in April 2022 was trading at US$0.75, but by mid-June 2022 it had depreciated to US$0.69. There are a number of factors at play in relation to the recent depreciation including rising interest rates in the United States relative to Australia's interest rates, the pandemic in China and the flow on effect to its economic growth and the demand for Australian commodities. The war in the Ukraine and the rise in commodity prices, however, is providing a buffer. The lower exchange rate will make imports more expensive which will add to inflation and possibly reduce the demand for Australian assets.

Changing the stance of monetary policy by changing the cash rate target conducted by the RBA has been a very important macroeconomic tool in its attempt to stabilise the Australian economy. Monetary policy has tended to be more effective in dampening aggregate demand during periods of high economic growth and higher inflation, than it has been in promoting aggregate demand and employment during downturns in the economy. The transmission mechanism of monetary policy through the different channels which make up the level of economic activity in Australia is very complex and the outcome of changes in the stance of monetary policy has a high degree of uncertainty.

Monetary policy and fiscal policy are the main macroeconomic management tools used by the RBA and the Australian government to achieve economic objectives and to manage the Australian economy. As price stability is one of the key economic objectives, the RBA is committed to returning the inflation rate back to the 2 per cent to 3 per cent target zone in the medium-term. The path forward to achieve this goal is uncharted and will be a major challenge for policy makers in the coming months.

Note:
Students may incorporate a relevant diagran1(s) into their responses. A relevant diagram would be one, which explains how the interest rate corridor operates in the Australian cash market.

Diagrams need to be labelled and explained correctly.

Question 26

	Marks
• Synthesises own knowledge and understanding with the information provided, to develop a logical and cohesive response • Integrates relevant economic terms, concepts, relationships and theory • Demonstrates a clear and comprehensive understanding of the use of fiscal policy by the Australian government to achieve the objectives of economic growth and full employment	**17-20**
• Synthesises own knowledge and understanding with the information. provided, to develop a logical and coherent response • Applies relevant economic terms, concepts, relationships and theory • Demonstrates a sound understanding of the use of fiscal policy by the Australian government to achieve the objectives of economic growth and full employment	**13-16**
• Uses own knowledge and understanding with the information provided, to develop a coherent response • Uses relevant economic terms, concepts, relationships and theory • Demonstrates a sound understanding of the use of fiscal policy by the Australian government OR the achievement of the objectives of economic growth and full employment	**9-12**
• Presents a generalised response • Uses some economic terms and concepts • Sketches in general terms some aspects of the use of fiscal policy by the Australian government to achieve the objectives of economic growth AND/OR full employment	**5-8**
• Presents a limited response with some relevant information • Uses some economic terms • Lists some aspects of the use of fiscal policy OR the objective of economic	**1-4**

activity OR the objective of full employment	

Essay plan: Fiscal policy refers to the use of the annual budget by the Australian government to affect the level of economic activity, resource allocation and the distribution of income. The Australian government's budget is an annual estimate of revenue and expenditure for the forthcoming financial or fiscal year (July 1st to June 30th) and is usually handed down in Parliament down by the Treasurer in May each year.

In 2022, the budget was released early on March 29th because a federal election was called on . April 10th after the budget's release, for May 21st by the former Coalition government led by former Prime Minister Scott Morrison. The budget is both an economic and a political statement and the 2022-23 budget contained many revenue and expenditure measures designed to appeal to voters and increase the Coalition's chances of winning the election and retaining government. However, this did not eventuate and the Albanese-led Labor Opposition won the election and forn1ed a new government. The new Treasurer, Jim Chalmers, on behalf of the government will release a new budget on October 29th, 2022, which will reflect the new government's budgetary priorities and an update on global and domestic economic conditions.

The main economic objectives of the Australian government are the following:

- Achieving a sustainable rate of economic growth that will result in rising income, employment growth and standards ofliving
- Price stability in terms of keeping the rate of inflation in a 2% to 3% target band, which is the operating target for the Reserve Bank of Australia's conduct of monetary policy
- Full employment in the Jabour market by creating enough jobs for people seeking work and willing and able to work
- External stability in terms of a sustainable current account balance in the balance of payments, servicing the cost of net external liabilities and maintaining the stability of the

exchange rate
- Achieving a more equitable distribution of income by targeting social welfare payments and maintaining a progressive taxation system

A significant amount of fiscal stimulus was used by the Australian government between 2020 and 2022 in response to the COVID-19 pandemic and the lockdown of the economy (including stay at home orders, widespread testing and vaccinations, social distancing and the closure of international borders) as well as helping people and communities affected by natural disasters (such as bushfires and floods) as mentioned in the stimulus material provided. The fiscal stimulus used by the Australian government included the JobKeeper payments to employers to retain staff, incentives for businesses to invest, and increases in welfare payments such as JobSeeker to maintain consumption spending. These measures were designed to support economic growth and maintain employment in the face the COVID-19 recession in 2020.

This unprecedented level of fiscal stimulus which mainly consisted of increased expenditure, coincided with a cyclical downturn in taxation revenue as consumption spending, household incomes and company profits fell. In 2020, the combination of a structural increase in expenditure with a cyclical downturn in revenue, Jed to the budget outcome moving sharply into deficit as shown in the stimulus graph provided for this question.

The underlying cash balance was-$134.2b in 2020-21 equivalent to -6.5% of GDP. This resulted from revenue of $519.9b being less than expenditure of $654.1b. Although Australia experienced a recession in 2020 with contractions in GDP in the June and September quarters, overall GDP growth was 1.5% in 2020-21. This outcome was underpinned by government or public sector spending being increased to make up for the contraction in private sector spending and to keep the economy on a path to achieving positive economic growth. The trend in the underlying cash balance can be seen in the stimulus graph provided for this question with a sharp increase in the underlying cash deficit in 2020-21, before declining in 2022 with a strong economic recovery which Jed to increased taxation revenue and lower spending on JobSeeker payments as the unemployment rate fell.

GDP growth was forecast in the 2022-23 budget at 4.25% in 2021-22, easing to 3.5% in 2022-

23. In the March quarter 2022 GDP growth was 0.8% and 3.3% through the year from the March quarter 2021 to the March quarter 2022.

Some of the main measures in the 2022-23 budget to support economic growth were $1b in tax relief to small businesses through the Technology Investment Boost program, $328m on a Modem Manufacturing Strategy, a further $2b to the National Housing and Finance Corporation to support low-cost housing and $7.1b on new regional infrastructure projects. In addition, to support consumption spending by households, the government provided a $420 payment for cost-of-living relief through the Low and Middle Income Tax Offset (LMITO) and a one off tax exempt payment of $250 to eligible welfare beneficiaries such as pensioners, veterans and concession card holders.

With the Australian economy recording positive economic growth in 2022, the Australian government's focus in the 2022-23 budget was based on an *Economic and Fiscal Strategy* to create jobs and achieve full employment in the labour market. This goal is outlined in the stimulus material for this question.

The *Economic and Fiscal Strategy* outlined in the 2022-23 budget was based on 'driving' private sector-Jed economic growth and withdrawing public sector stimulus from the economy. It was argued that this would lead to employment creation, helping to reduce the unemployment rate and at the same time reducing the size of the budget deficit and the level of public net debt. This was to be achieved by the following measures to improve the Australian government's balance sheet position:

- Stabilising and then reducing gross and net public debt over the economic cycle
- Targeting budget balance over the course of the economic cycle consistent with the debt reduction objective

The improvements in net debt and the budget balance were to be achieved by the following measures:

- Controlling the growth of government expenditure, whilst maintaining the efficiency and quality of government spending and guaranteeing the delivery of essential services such as social security, health and education
- Supporting the growth in taxation revenue through policies which drive earnings/wages growth and overall economic growth
- Maintaining a sustainable tax burden at 23.9% of GDP
- Government investment in measures to support jobs growth and private investment
- Ongoing structural reforms to boost economic growth

GDP growth was forecast in the 2022-23 budget at 3.5% in 2022-23. In the March quarter 2022 GDP growth was 0.8% and 3.3% through the year from the March quarter 2021 to the March quarter 2022. This seemed to suggest that the budget's growth forecast would be met. However, there were numerous uncertainties surrounding this growth forecast:

- Higher inflation and inflationary expectations which led to rising costs and prices in the economy including fuel, housing, food and transportation
- Higher interest rates with the Reserve Bank tightening the stance of monetary policy in May, June and July 2022 by increasing the cash rate from 0.1% to 1.35%
- Continuing global supply constraints which have pushed up the price of shipping and disrupted the distribution of goods from major manufacturing countries such as China where the government has enforced COVID-19 lockdowns in major cities such as Beijing and Shanghai
- The Russian invasion of Ukraine in early 2022 has led to rising energy prices for oil and gas and food products such as wheat

The unemployment rate peaked at 5.1% of the workforce in 2020-21, with JobKeeper payments helping to keep nearly l m workers in a job with their employer. The unemployment rate was forecast at 4.25% for 2021-22 in the 2022-23 budget but had already fallen to 3.9% in April 2022, with strong jobs growth due to an economic recovery.

The budget forecast was for the unemployment rate to fall as low as 3.5% in 2022-23. The Non-Accelerating Inflation Rate of Unemployment (NAIRU) where the unemployment rate is consistent with stable inflation was previously estimated at between 4% and 5%. Both Treasury and the Reserve Bank have revised their estimates of the NAIRU lower at between 3% and 4%. The NAIRU is taken to be the point of full employment where wage pressures should begin to increase. This has started to occur in some sectors of the economy that are highly unionised such as public sector nurses, teachers and transport workers. However, the extent to which workers can gain wage increases in the current economic environment will depend on their bargaining power, levels of productivity and employers' capacity to pay.

There were many measures in the 2022-23 budget that targeted skills training and other assistance to the unemployed, underemployed and those wishing to enter or re-enter the workforce such as young people and women:

- $2.8b over five years to upskill apprentices through a new Australian Apprenticeships Incentive System. This scheme establishes pathways to develop apprentices in priority trades.
- $52.8m to establish ReBoot and support Workforce Australia to assist the employment and training of young people. This targets an estimated 5,000 disadvantaged young people at risk of becoming long-term unemployed.
- $346.lm over five years to introduce an enhanced Paid Parental Leave Scheme for eligible working families. This is designed to help women to stay connected with the workforce and boost the female labour force participation rate.
- $228.Sm to improve the educational outcomes of school students. This includes extending National School Reform Funding by two years at a cost of $62.4m.

The Medium-Term Fiscal Strategy of the previous Coalition government outlined in the 2022-23 budget was to achieve sustainable private sector led growth to create employment and rising incomes, but at the same time to stabilise and reduce net debt as a share of GDP. With accumulated budget deficits, the net debt of the Australian Government General Government Sector was

$631.4b or 27.6% of GDP in 2021-22.

Net public debt refers to the accumulated stock of public debt used to finance successive budget deficits, especially since the Global Financial Crisis when the budget deficit increased dramatically to -$54.Sb. However, like during the GFC, the Australian government's budgetary position has deteriorated during the COVID-19 pandemic, with a large projected rise in the budget deficit and level of public debt. This is due to a deterioration in both the cyclical (non- discretionary) and structural (discretionary) components of the budget framework:

- Taxation revenue fell to $519.9b in 2020-21 as spending, incomes and profits fell during the pandemic. This meant that revenue from the PAYG tax system, the Goods and Services Tax (GST) and company tax all fell. The fall in taxation revenue is a result of the automatic stabilisers in the budgetary framework, with less tax collected as the economy entered a recession and experienced negative growth in GDP, incomes and employment. This is the cyclical component of the budget deficit. In structural terms, taxation revenue also fell because of government policies such as the instant tax write-off to support business investment and tax reductions in business activity statements.
- Government spending rose to $654.lb in 2020-21 as the structural or discretionary component of the budget was forced into deficit because of deliberate government policies to increase spending such as the $70b JobKeeper program and various measures to support household incomes such as the stimulus payments to households (e.g., one-off welfare payments and the JobSeeker payments) as well as the JobKeeper scheme designed to keep people in employment. The cyclical component of the budget deficit also rose due to the increase in the unemployment rate and the number of people applying for unemployment benefits.

Given these cyclical and structural influences on the projected budget outcome, the Australian government's budget was forecast to be an underlying cash deficit of-$78b or -3.4% of GDP in 2022-23, falling to a forecast -$56.Sb or -2.4% of GDP in 2023-24. Revenue was forecast to recover to $647.6b in 2022-23 and expenditure to fall to $625.6b. Treasury forecast the net det to grow to $714.9b or 31.1% of GDP in 2022-23 and to $772.lb or 32.6% of GDP in 2023-24. The net interest payments on the net debt were forecast at $15.lb or 0.7% of GDP in 2022-23, and $16.9b or 0.7% of GDP in 2023-24.

The challenges for the new Albanese Labor government and Treasurer Jim Chalmers are to reduce government spending and the size of the budget deficit in the short to medium-term. This can be achieved by cutting unnecessary government waste and supporting economic growth so that tax revenue begins to recover more quickly. The huge challenges are to contain rising inflation to achieve price stability and that real wage growth occurs with full employment in the labour market.

The second phase of the Australian Government's Economic and Fiscal Strategy as outlined in the stimulus material is to target budget balance (where T = G), and then stabilise and reduce net debt. This will be achieved by a recovery in tax collections, controlling expenditure growth and supporting revenue growth through policies that support rising incomes and economic growth.

The issue of Australian Government Securities (AGS) by the Australian Office of Financial Management (AOFM) is how budget deficits are funded and lead to the net debt being accumulated. The main types of AGS are Treasury Bonds, (medium to long-term), Treasury Indexed Bonds (medium to long-term) and Treasury Notes (short-term). In 2022-23, the face value of AGS on issue was projected at $977b, with higher interest rates predicted to increase net interest payments on bonds issued in the future.

The Australian government has a AAA credit rating and faces little to no difficulty in selling AGS in both domestic and overseas financial markets. However, the enormity of the bond selling program and the risk of higher interest rates adding to net interest payments will leave the government's balance sheet in a net liability position in the medium-term. Added to this is the problem of increased government spending and borrowing leading to 'crowding out' of some private sector activity as borrowing for private sector investment may become more difficult and costly, not to mention the financial burden of the net debt on future generations of taxpayers.

The Albanese government faces a very challenging set of

circumstances in managing the Australian economy in 2022-23 with high and rising inflation, higher interest rates, falling real wages, long-term pressures around productivity improvements and the large level of government debt.

Question 27

Analyse the global and domestic causes of inflation in Australia and possible economic policy responses.

	Marks
• Provides a sustained, logical and cohesive response • Integrates relevant economic terms, concepts, relationships and theory • Demonstrates a clear and comprehensive understanding of the global and domestic causes of inflation in Australia and possible economic policy responses	**17-20**
• Provides a logical and cohesive response • Applies relevant economic terms, concepts, relationships and theory • Demonstrates a sound understanding of the global and domestic causes of inflation in Australia and possible economic policy responses	**13-16**
• Develops a coherent response • Applies economic terms, concepts, relationships and theory • Demonstrates some understanding the of the global and domestic causes of inflation in Australia AND/OR possible economic policy responses	**9-12**
• Provides a generalised response • Uses some economic terms • Demonstrates some understanding of the causes of inflation in Australia AND/OR possible economic policy responses	**5-8**
• Presents a limited response • Uses some economic terms • Provides some aspects of the causes of inflation in Australia AND/OR possible economic policy responses	**1-4**

Answers could include:

- headline and underlying inflation
- trends in global and Australian inflation
- demand pull inflation, cost push inflation, imported inflation, inflationary expectations
- Global factors - supply constraints, global production costs, global inflation, external shocks such as health pandemics (COVID-19) and regional conflicts such as Russia's invasion of Ukraine
- Domestic factors - government policy, floods, consumer incomes, savings levels, costs of production including wage rises

- Government policies in response to inflation - fiscal, monetary, labour market, income distribution (transfer payments, progressive income tax, and other assistance)

General Feedback

- **Introductions were far too long! Many were over a page and repeated the points in the body**
- **Topic sentences need to show you you're answering the question and where your paragraph will be taking the reader**
- **Plan your responses to avoid lots of points crossed out (it becomes very hard to read with every third word crossed out and wastes time)**
- **Analyse means show how A causes B in detail and how B causes C in detail**
- **Don't use formulas in extended responses, explain the elements of the formula instead**
- **Ensure your tone remains formal and no political bias or judgement comes through**
- **Many were still doing tiny diagrams – spread them out and explain them in the body. They don't need a big title as you need to explain it within your point in the relevant paragraph**
- **AS and AD diagrams were overall done very poorly. These are for the whole economy, not specific industries. You must also use AS and AD (not S & D) and Price Level and real GDP (note price and quantity)**
- **Monetary Policy should always be broken down into its components**
- **Depth on fewer ideas needed and show HOW**
- **Different causes of inflation need different actions. The better responses talked about how certain policies would not be effective due to the current causes of inflation.**
- **Better responses also linked a policy to a cause which also allowed better analysis of A-->B→C**
- **Many structured around the types of inflation rather than global and domestic causes. Ensure the marker knows from the outset that you've tailored your response to the question by adding the concepts in topic sentences**
- **You are best stating the cause and then the policy as the cause comes before the effect and creates better analysis of A→B→C**
- **Not many added limitations of policies. Any question on policies should have limitations to add sophistication to your response e.g. reduced fuel excise lowers cost of living but also stimulates AD from lower taxes, negating the impact**
- **Many stated that growth leads to demand pull inflation but not if it's through supply side growth**
- **Use the correct terms e.g. Increase is different to an expansion etc**
- **cost-push and demand pull inflation relate to the whole economy, not to a specific industry**
- **house prices are not part of CPI**
- **many defined inflation as decreased value of money – it's a sustained increase in price levels over time. Some also referred to one or two prices in the economy**

causing inflation but unless it's something like oil prices (which filter through to all products) then it's not going to significantly impact on inflation)

- **many referred to supply of the AUD when they weren't talking about exchange rates. Use the correct terminology**
- **when talking about causes and policies, current context is best, even if not asking for current policies**
- **many responses tried to talk about how the change in the AUD but was only relevant if talking about the exchange rate and therefore imported inflation**
- **be careful in how you phrase things – many said the government aims to increase unemployment to address inflation. They aim to lower growth but no government ever aims to increase unemployment, it's a mere by-product in most cases**
- **as the question was on <u>responses</u> to a cause, automatic stabilisers aren't relevant as they are automatic and therefore not a response**
- **some responses focused on what naturally causes a decrease in inflation which isn't the question as it's about POLICIES to respond to inflation**

Question 28

Analyse recent trends in unemployment and income inequality and their impact on the Australian economy.

Criteria	Marks
• Provides a sustained, logical and cohesive response • Integrates relevant economic terms, concepts, relationships and theory • Demonstrates a clear and comprehensive understanding of recent trends in unemployment and income inequality and their impact on the Australian economy	**17-20**
• Provides a logical and cohesive response • Applies relevant economic terms, concepts, relationships and theory • Demonstrates a sound understanding of recent trends in unemployment and income inequality and their impact on the Australian economy	**13-16**
• Provides a coherent response • Uses relevant economic terms, concepts, relationships and theory • Demonstrates some understanding of recent trends in unemployment and income inequality AND/OR the impact of unemployment and income inequality on the Australian economy	**9-12**
• Provides a generalised response • Uses some economic terms • Demonstrates some understanding of recent trends in unemployment and income inequality AND/OR the impact of unemployment and income inequality on the Australian economy	**5-8**
• Provides a limited response • Uses some economic terms • Provides some aspects of recent trends in unemployment AND/OR income inequality in Australia	**1-4**

Answers could include:

- Trends in unemployment
- Types of unemployment
- Underemployment
- NAIRU
- Social costs
- Economic costs
- Opportunity cost
- Trends in income inequality
- Inequality for specific groups
- Gini coefficient
- MPC
- Multiplier

General Feedback

- **Introductions were far too broad! You need to show the reader what your main points will be**
- **Topic sentences need to show you you're answering the question and where your paragraph will be taking the reader**
- **Plan your responses to avoid lots of points crossed out (it becomes very hard to read with every third word crossed out and wastes time)**
- **Analyse means show how A causes B in detail and how B causes C in detail**
- **Ensure your tone remains formal and no political bias or judgement comes through**
- **Many were still doing tiny diagrams – spread them out and explain them in the body. They don't need a big title as you need to explain it within your point in the relevant paragraph**
- **AS and AD diagrams were overall done very poorly. These are for the whole economy, not specific industries. You must also use AS and AD (not S & D) and Price Level and real GDP (note price and quantity)**
- **Monetary Policy should always be broken down into its components**
- **Depth on fewer ideas needed and show HOW**
- **You need to show specific trends on the two indicators in depth. You don't need to delve into the causes of these but specifics on what has been happening is needed and be current as per the question (GFC is not recent)**
- **Many focused in depth on the causes and skipped the impacts**
- **Many skipped impacts on the economy and jumped straight to policies. To analyse you need to look at how A leads to B and then how this leads to C. The key to question was the impacts of the trends so do that in depth and you can then bring in policies if you like**
- **Wealth and income inequality are very different concepts so don't use them interchangeably**
- **Be mindful to clearly show HOW lower unemployment will lead to higher levels of growth rather than just state it as fact**
- **Various unemployment targets were listed. It is about 4.5-5% as this is the estimate of NAIRU**
- **The better responses talked about how unemployment rising in Covid ultimately led to increase in jobseeker per fortnight (doubling of payments) to counteract the fall in spending that would occur when we needed it to continue. This actually improved inequality during the lockdowns and it has worsened again since**
- **Lorenz curves were not the best to draw as they don't show much application of theory (same for PPFs)**
- **The J curve was used by numerous students but none of them correctly. J curve refers to changes in the exchange rate and how it impacts on net exports so it should only be used in an exchange rate or BOP question**
- **Many linked the two issues together throughout but the impacts of each are quite different so separating them for the most part was needed, even though some links between them could be shown**
- **Many said that unemployment caused the fall in growth but labour is a derived demand. The fall in growth caused less need for labour**