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NZQA

NEW ZEALAND QUALIFICATIONS AUTHORITY
MANA TOHU MĀTAURANGA O AOTEAROA

QUALIFY FOR THE FUTURE WORLD
KIA NOHO TAKATŪ KI TŌ ĀMUA AO!

Level 2 Economics, 2015

91223 Analyse international trade using economic concepts and models

2.00 p.m. Thursday 12 November 2015
Credits: Four

Achievement	Achievement with Merit	Achievement with Excellence
Analyse international trade using economic concepts and models.	Analyse international trade in depth using economic concepts and models.	Analyse international trade comprehensively using economic concepts and models.

Check that the National Student Number (NSN) on your admission slip is the same as the number at the top of this page.

You should attempt ALL the questions in this booklet.

If you need more room for any answer, use the extra space provided at the back of this booklet.

Check that this booklet has pages 2–11 in the correct order and that none of these pages is blank.

YOU MUST HAND THIS BOOKLET TO THE SUPERVISOR AT THE END OF THE EXAMINATION.

Excellence

TOTAL 21

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QUESTION ONE: NEW ZEALAND DAIRY EXPORTS

At $15.5 billion, dairy exports make up almost a third of New Zealand's annual goods exports.

Source (adapted): http://www.rbnz.govt.nz/research_and_publications/speeches/2014/5721595.html

(a) Identify TWO of the top five New Zealand goods exports, by value, other than dairy exports.

(1) Wood products (forest products), log, timber

(2) Meat

Around 95% of New Zealand's dairy production is exported.

Source (adapted): http://www.dcanz.com/about-nz-dairy-industry/dairying-today

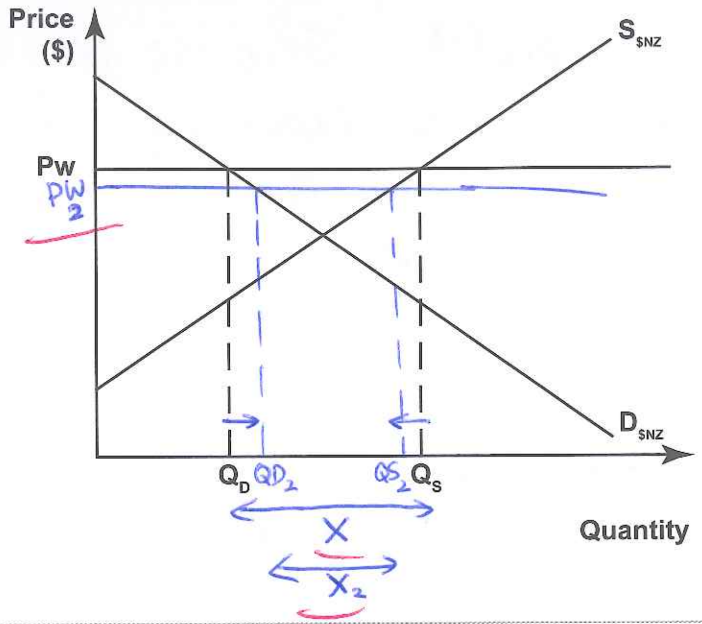
Falling oil prices, geopolitical uncertainty in Russia and Ukraine, and subdued demand from China are all contributing to weak worldwide demand for dairy products.

Source (adapted): http://www.fonterra.com/nz/en/Hub+Sites/News+and+Media/Media+Releases (10 Dec 2014)

(b) Discuss the impact that a decrease in world demand for dairy products could have on the Current Account of the New Zealand Balance of Payments, when the New Zealand market is a price taker.
In your answer:

- fully label Graph One to show the impact of a lower world demand
- explain in detail whether the dairy industry will be worse off or better off from the lower world demand
- explain in detail how the impact on the dairy industry will affect New Zealand's Current Account deficit
- refer to Graph One and the resource material above.

Graph One: Market for New Zealand dairy products



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Falling oil prices and geopolitical uncertainty in Russia & Ukraine, along with subdued demand from China means there is weak world wide demand for dairy products. Lower world demand means dairy products are not worth as much in the world market and therefore the world price decreases from Pw to Pw₂. New Zealand is a price taker, meaning we cannot influence the world price as we have ~~are~~ too small/insignificant a contribution to the world dairy market – therefore we can only accept & cannot influence the world price determined by world demand, and supply only at that price. (no higher). This means the dairy industry is worse off because of the lower world demand as it means they have to accept a lower world price. This means they earn less revenue from

There is more space for your answer to Question One on the following page.

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exports as the world price is low – this means they earn less profit. Because it is now less profitable ~~to~~ to be exporting dairy, dairy farmers cut back on production in dairy products. (it is no longer worth supplying a lot for a lower price /less export receipts which leads to less revenue & profits). This is shown as a decrease in quantity supplied of dairy products in the NZ market from QS to QS_2. ~~This~~ This reduces exports from X to X_2 so therefore the dairy industry is worse off due to less exports and for a lower price. ~~The~~ Balance on goods records the dairy product exports. Balance on goods is calculated by subtracting import payments for goods (visibles) from export receipts for goods (visibles). 95% of NZ dairy ~~export~~ production is exported however due to a decrease in world price exports decrease from X to X_2 as not only has QS decreased but NZ quantity demanded has also ~~decreased~~ increased from QD to QD_2 as NZ consumers want to buy dairy at the new lower prices. And hence less than 95% is now exported, because more is being consumed in NZ itself which adds to the decrease in exports from X to X_2. As $5.5 billion (almost a third of New Zealand's annual goods exports) is dairy exports, and these exports have now decreased, this significantly reduces the balance on goods (due to the decrease in export receipts). Balance on goods is (see back)

E7

Extra space if required.

Write the question number(s) if applicable.

QUESTION NUMBER

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1(b) is part of the Current Account (NZ's record of transactions with the rest of the world) & So a decrease in balance on goods, decreases the current account. This increases the NZ current account deficit greatly as export receipts have decreases even further due to lower dairy exports (deficit is when import payments > export ~~receiptt~~ receipts so a decrease in export receipts increases the deficit). NZ ∈ more in deficit.

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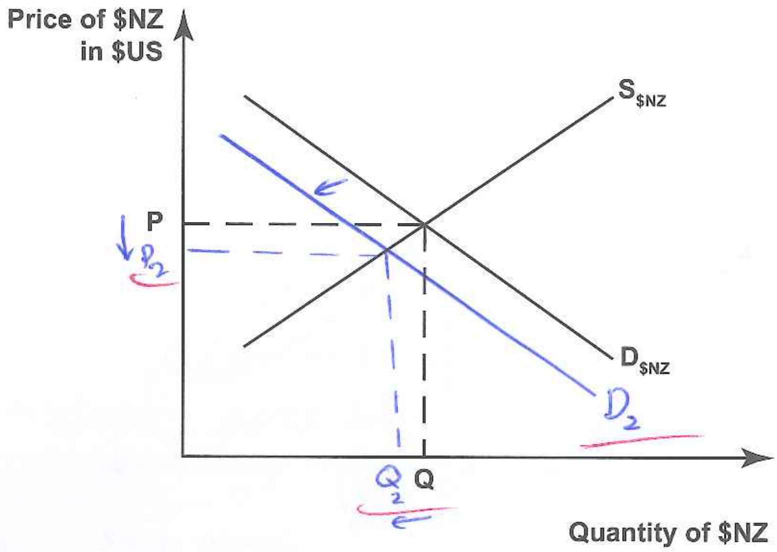
QUESTION TWO: THE EXCHANGE RATE

(a) Explain in detail the impact of decreasing demand for New Zealand dairy exports on the value of the New Zealand dollar.
In your answer:

- fully label on Graph Two the impact of decreasing demand for New Zealand dairy exports
- explain in detail the impact that you have shown on Graph Two.

Graph Two: Market for the New Zealand dollar



The decreasing demand for NZ dairy exports means less dairy exports are being exported. This means that the demand for the $NZ decreases to D2 from D. This is because dairy exporters no longer demand as much $NZ to exchange their foreign currency into. Due to lower export receipts caused by lower ~~...~~ dairy exports (caused by decreasing demand), exporters no longer have as much foreign currency revenue to exchange into $NZ so they do not demand as many $NZ. The decrease in demand means that the $NZ is not worth as much, so the $NZ depreciates from P to P2 as shown on the graph. So the decreasing demand for NZ dairy exports causes the $NZ to depreciate.

(b) Compare and contrast the impact of decreasing demand for New Zealand dairy exports with the impact of a decreasing world price of oil on the exchange rate for the New Zealand dollar. In your answer:

- fully label on Graph Three the impact of a decreasing world price of oil
- explain in detail the impact that you have shown on Graph Three
- explain in detail whether decreasing demand for New Zealand dairy exports or a decreasing world price of oil would have a greater impact on the exchange rate for the New Zealand dollar.

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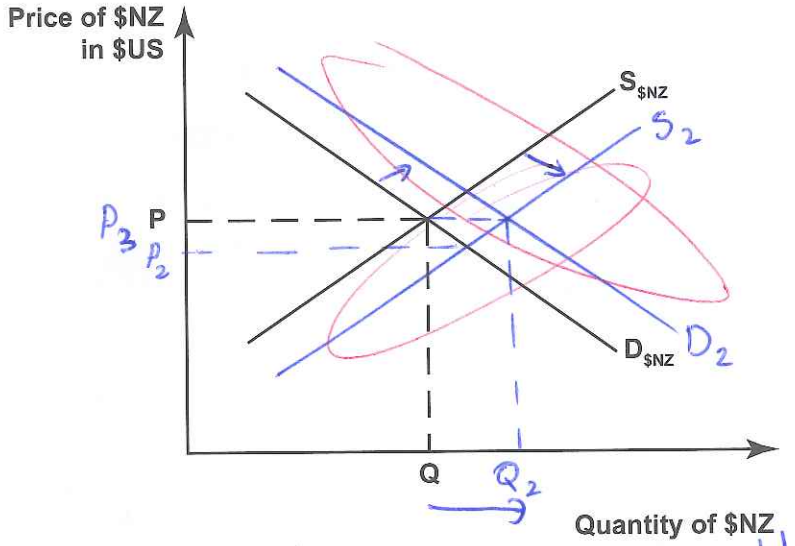
Graph Three: Market for the New Zealand dollar



The decrease in the world price of oil means that imports of oil will increase as oil is now more affordable. This increases the supply of the $NZ from S to S_2. This is because NZ importers will need more $NZ to exchange into foreign currency to buy oil imports from overseas. This increases the supply of the $NZ. However, the decrease in world price of oil affects the entire world (rather than just NZ like the decreasing demand for NZ dairy exports) – the entire world will now find it cheaper to buy oil as it now costs less. This means foreign

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markets / consumers will now ~~[illegible]~~ have more money to spend on other imports. ~~The entire world~~ Many of NZ trading partner's will be better off due to the lower prices in oil - foreign businesses will have cheaper costs of production as oil makes petrol which is used by most businesses - ~~[illegible]~~ so business transport/delivery costs decrease. This means their employees will benefit from ~~[illegible]~~ secure employment and possibly higher wages as foreign businesses now spend less on petrol. So foreign consumers are more confident possibly, in our trading partners. The depreciation of the $NZ caused by the decrease in supply from P to P_2 (more supply, less value) means NZ exports are relatively cheaper as well. These two effects of the decreasing world price of oil means that NZ can export more (not necessarily dairy) → NZ firms will also benefit from cheaper oil imports as a cost of production (petrol ~~[illegible]~~ is a resource ~~will decrease~~ has decreased) so they can produce more and hence will export more. The increase in NZ exports increases the demand for $NZ from D to D_2 as exporters demand $NZ to exchange their foreign currency export receipts into. ~~So the overall impact of th~~ An increase in demand, appreciates the $NZ value & so overall, the decreasing world price for oil would make the $NZ value stay somewhat constant at P_3. So the decreasing demand for NZ dairy exports has a greater impact as it depreciates the $NZ (graph 2) ~~[illegible]~~ where as decreasing world oil price keeps exchange rate constant.

M6

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QUESTION THREE: THE TRADE IN TOMATOES

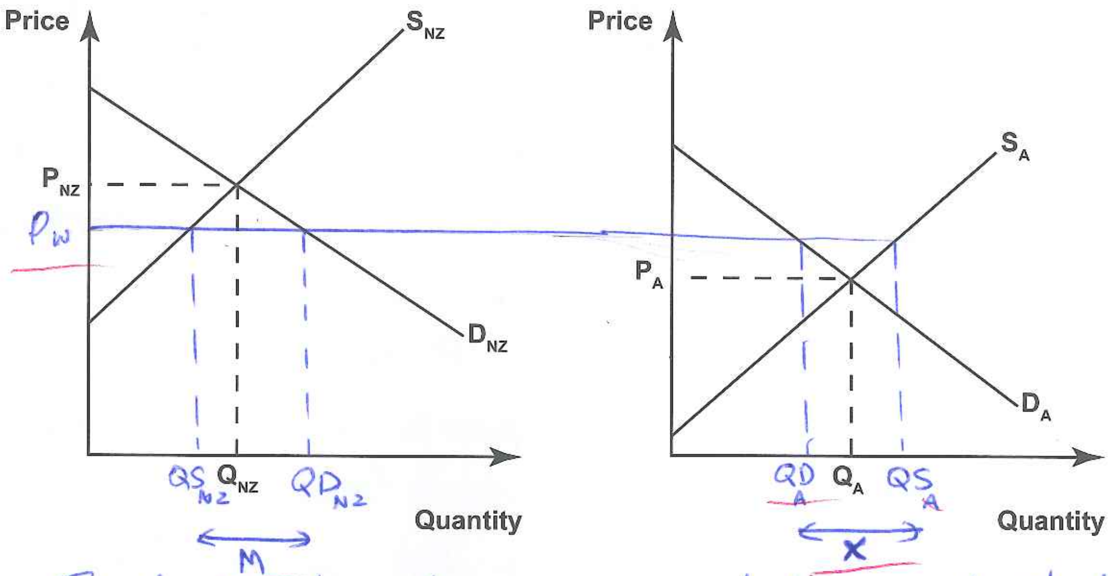
Tomatoes are a crop that can be grown in both New Zealand and Australia, and yet trade in tomatoes occurs between the two countries.

(a) Explain in detail why trade in tomatoes occurs between New Zealand and Australia. In your answer:

- fully label Graph Four to show the impact of trade on the New Zealand and Australian markets for tomatoes
- explain in detail why the trade in tomatoes occurs by referring to Graph Four.

Graph Four: Two-country model

New Zealand **Australia**



Trade in tomatoes occurs between Australia and NZ because the NZ price for tomatoes (P_{NZ}) is a lot higher than the Australian price (P_A) hence ~~NZ consumers~~ their trade results in a world price (P_w) where New Zealanders import (M) tomatoes from Australia at the lower world price. Quantity demanded in NZ (QD_{NZ}) is high due to lower world price & quantity supplied in NZ (QS_{NZ}) is low due to NZ producers not earning as much on their tomatoes at the low world price (so they cut production). This shortage where demand is greater than supply causes them to import. Australia has the opposite situation & they have greater supply QS_A (to sell at higher world price) than QD_A (less demand for tomatoes at higher price) so this surplus is exported (X) (supply greater than demand). Shortage of one cou

(b) Compare and contrast the impacts that the trade in tomatoes could have on the following groups:

- New Zealand tomato growers
- New Zealand tomato consumers
- New Zealand fruit and vegetable retailers.

In your answer:

- explain in detail how each group, listed above, will be worse off or better off as a result of trade
- refer to Graph Four.

NZ tomato growers are worse off because the world price is made lower by trade (as P_A – Australian price is much lower than P_{NZ}). This means their tomato produce gets a much lower price at P_W than it would at P_{NZ} (with no trade) so they earn less revenue & ~~trade~~ profit. This causes them to supply less as it is less profitable to sell tomatoes – quantity supplied is QS_{NZ} which is less than Q_{NZ} (how much they would have supplied without trade). Hence they are worse off with trade due to lower supply & lower prices earnt on their tomato produce. However, the lower world price means NZ tomato consumers are better off because they are buying tomatoes at the lower price of P_W than price P_{NZ} (before trade). The imports (M) allow them to demand more than the NZ supply (QD_{NZ} – quantity demanded in NZ) and have their wants satisfied at a lower price of P_W ~~&~~ with imports from Australia. (who export – X – their surplus of tomatoes). *see end

There is more space for your answer to Question Three on the following page.

ntry = surplus of the other. (to satisfy demands of NZ consumers).

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NZ fruit & vegetable retailers are worse off as they are competing with the cheaper imports from Australia at Pw. The NZ tomato growers are not supplying enough, for them to earn high revenue & profits.

* NZ consumers are also better off as tomato importing firms may hire more employees due to their success & profit from high tomato imports.

E7

Excellence exemplar for 91223 2015			Total score	21
Q	**Grade score**	**Annotation**		
1	E8	This candidate has received an E8 grade because they have: • given a detailed explanation of how the dairy industry / farmer is worse off from a lower world demand for dairy products, including the idea that they are worse off because the lower price will result in dairy farmers reducing their quantity supplied (Q_S to Q_{S1}), and when this is combined with lower prices it will result in lower income/revenue/profits from dairy production. • given a detailed explanation of how the impact on the dairy industry affects the Current Account, including the idea that the fall in export incomes/receipts will cause the Balance on Goods to decrease. The BOP Current Account includes the Balance on Goods, so therefore the Current Account will become a larger deficit amount. • integrated Graph One (*Pw falling, Q_S decreasing, X decreasing*) AND idea from resource material (*95% of dairy production exported*) into their detailed explanations.		
2	M6	This candidate has received an M6 grade because they have: • given a valid detailed explanation of the impact of decreasing demand for New Zealand dairy exports, including reference to Graph Two including the idea that lower demand for New Zealand dairy exports will result in lower prices and lower export revenue. New Zealand dairy exporters will have less foreign currency to convert into New Zealand dollars and, therefore, will demand fewer \$NZ. The demand for the \$NZ decreases, and as a result, the foreign exchange rate for the \$NZ falls. The \$NZ depreciates. • integrated Graph Two (*$D_{\$NZ}$ to D_2, P to P_2*) into their detailed explanations. Decreasing $S_{\$NZ}$ and/or $D_{\$NZ}$ in Graph Three and giving a detailed explanation on whether the decreasing demand for dairy exports or the decreasing world price of oil would have a greater impact on the exchange rate, integrating the changes shown on Graph Three, would have resulted in E8.		
3	E7	This candidate has received an E7 grade because they have: • given a detailed explanation, integrating the changes shown on Graph Four of how New Zealand tomato growers are worse off AND New Zealand tomato consumers are better off including the idea that when trade occurs the price of tomatoes falls in New Zealand from P_{NZ} to P_T. As a result of the lower price, New Zealand tomato growers lower their quantity supplied (Q_{NZ} to QS_{NZ}). The fall in price and fall in quantity supplied will result in falling income/revenue/profits for New Zealand tomato growers. They will be worse off. New Zealand tomato consumers, on the other hand, will be able to purchase tomatoes at the lower price (P_w) and, as a result, will increase their quantity demanded (Q_{NZ} to QD_{NZ}). New Zealand tomato consumers will be better off. Giving a detailed explanation of how NZ fruit and vegetable retailers would have been better off, integrating the changes shown in Graph Four would have resulted in E8.		