91403

914030

NEW ZEALAND QUALIFICATIONS AUTHORITY
MANA TOHU MĀTAURANGA O AOTEAROA

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

3

SUPERVISOR'S USE ONLY

Level 3 Economics, 2017

91403 Demonstrate understanding of macro-economic influences on the New Zealand economy

2.00 p.m. Wednesday 29 November 2017
Credits: Six

Achievement	Achievement with Merit	Achievement with Excellence
Demonstrate understanding of macro-economic influences on the New Zealand economy.	Demonstrate in-depth understanding of macro-economic influences on the New Zealand economy.	Demonstrate comprehensive understanding of macro-economic influences on the New Zealand economy.

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 2–12 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

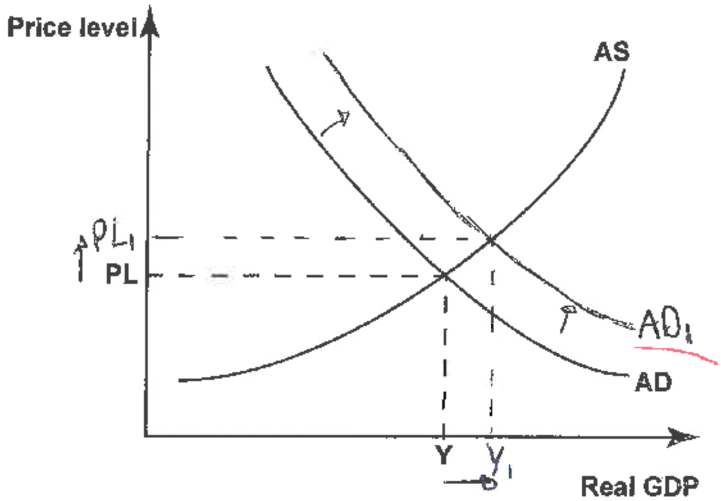
TOTAL 19

ASSESSOR'S USE ONLY

QUESTION ONE: Fiscal and supply side policies

> The 2016 Budget included spending on regional roading projects and upgrading regional tourism infrastructure, e.g. extending the New Zealand Cycle Trail.
>
> Source (adapted): http://www.treasury.govt.nz/budget/2016/at-a-glance/b16-at-a-glance.pdf
>
> The impact on long-term economic growth of this expansionary fiscal policy may be affected by the multiplier.

Graph One: The New Zealand economy



(1)

(a) (i) On Graph One above, illustrate the impact of increased spending on regional roading projects and tourism infrastructure on aggregate demand and real GDP.

(ii) Explain in detail the impact of this expansionary fiscal policy on economic growth. In your answer:

- refer to the changes made to Graph One
- explain why at least two components of aggregate demand, other than Government spending, will increase.

This initial government spending will ~~be additional~~ become income for households and firms/producers. Producers and consumers will now respend a large proportion of this income, thus increasing consumer (C) and investment (I) spending. ~~[illegible]~~ This money which is now respent on goods ~~and~~ & services and incomes/wages, is through increases in investment and consumer spending, (2) and so-on, due to the multiplier effect causing a money to flow around the circular flow until it all becomes eventually leaked out of the economy via withdrawals such as savings, taxes, import payments etc.

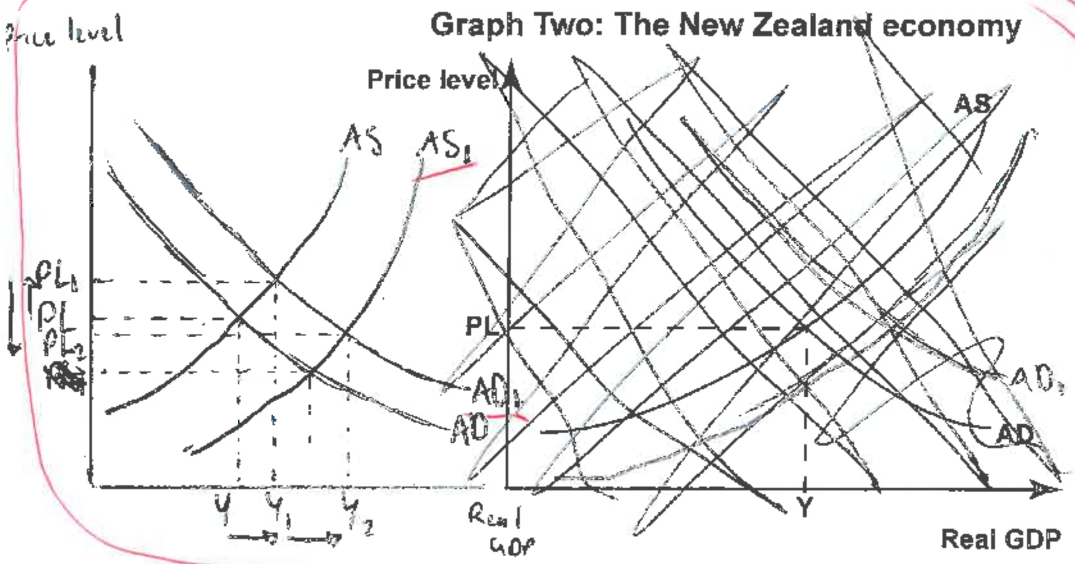
ASSESSOR'S USE ONLY

Supply side policy includes any policy that improves an economy's productive potential and its ability to produce.

Source: http://www.economicsonline.co.uk/Global_economics/Supply-side_policies.html

The 2016 Budget also included spending on tertiary education and apprenticeship programmes, to develop the skilled workforce needed for a 21st century economy.

Source (adapted): http://www.treasury.govt.nz/budget/2016/at-a-glance/b16-at-a-glance.pdf



(3)

(b) On Graph Two above, illustrate the impact of increased spending on tertiary education and apprenticeship programmes on real GDP, assuming that this expansionary fiscal policy is also an example of a supply side policy.

(c) Referring to the resource material on pages 2 and 3 and Graphs One and Two, compare and contrast the impact on long-term economic growth of these two policies. In your answer, explain in detail:

- the impact of increased spending on tertiary education and apprenticeship programmes on economic growth
- whether increased spending on regional roading projects and tourism infrastructure or increased spending on tertiary education and apprenticeship programmes would have the greater impact on long-term economic growth.

An increased spending on tertiary education and apprentice-ship programmes will cause both AD and AS to increase. AD will increase as the increase in government spending (G) will mean that more NZ goods and services, such as ~~educat~~ tertiory education, will be demanded/purchased, and as AD = C + G + I + (X − M) so an ~~increage~~ increase in G will increase AD. Hence, AD

More answer space is available on the next page.

ASSESSOR'S USE ONLY

increases to AD_1. This increase in AD causes a shortage so consumers bid up prices, causing a new equilibrium to be established with a higher Real GDP of Y_1.
This spending on tertiary education and apprenticeship programmes will also increase AS_1 in the long run. This is as ~~spendin~~ this type of spending means that there will be more skilled ~~and productive~~ workers of higher productivity in the work force in the future (after their education/apprenticeship), meaning in the future the productive capacity will increase as more goods will be able to ~~pro~~ be produced with the same amount of resources. This means that ~~AS~~ the long term AS curve will shift to the right/increase to AS_1 as the resources/workers are more productive, meaning that with the same amount of costs, more can be produced, thus increasing profitability, making producers more willing to produce so AS increases. (5)
The increase in AS causes a surplus, so producers undercut each other until equilibrium is reached, where there is an increase from Y_1 to Y_2.
Overall this policy greatly increases Real GDP in the short term and long term, meaning economic growth increases in the short and long term as Real GDP is ~~[illegible]~~ a measure of economic growth.

The fiscal policy also increases long-term economic growth due to the multiplier effect, but the supply side policy would increase long-term economic growth more, as it increases the productivity and productive capacity of the future economy ~~[illegible]~~, ~~whereas~~ so it is more sustainable, whereas the fiscal ~~policy~~ policy only increases spending in the long run via the multiplier effect and maybe ~~[illegible]~~ an increase in productive capacity (with infrastructure being spent on). (6)

E7

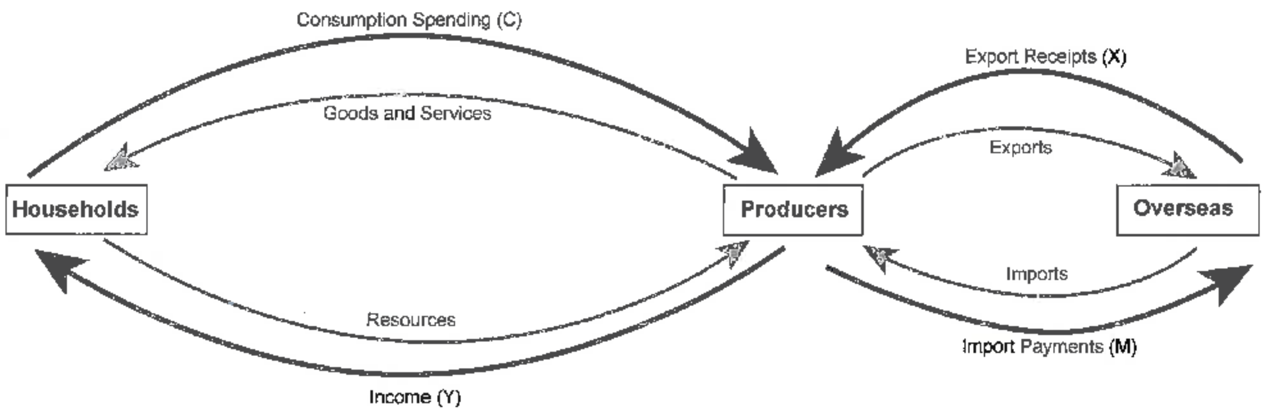
QUESTION TWO: Impact of free trade agreements on the current account and employment

ASSESSOR'S USE ONLY

As at the beginning of 2017, New Zealand has successfully concluded free trade agreements involving 16 countries that are members of the World Trade Organisation. New Zealand is negotiating to conclude another five free trade agreements involving significant economies such as India.

Source (adapted): https://www.mfat.govt.nz/en/trade/free-trade-agreements/free-trade-agreements-in-force/ and https://www.mfat.govt.nz/en/trade/free-trade-agreements/agreements-under-negotiation/.

Model One: Simple circular flow model showing New Zealand producers, households, and the overseas sector



(a) Referring to changes in the relevant real and money flows from Model One, explain in detail how New Zealand's entry into a further five free trade agreements could improve New Zealand's current account.

Free trade agreement are when their are no tariffs or trade barriers allowing for cheaper exports and imports.

The new Free Trade Aggreements (FTA'S) would mean export reciepts would rise as overseas buyers in FTA countries will have to pay relatively less due to tariff removal, meaning the demand for export increases, so ~~exports and~~ both the export and export reciept (x) flows will increase. Import payments will also rise NZ importers have to pay relatively less so demand for imports rise, thus increasing both the flows for imports and import payments (M). If both X and M increased by the same amount then there would be no effect on the current account balance. But as NZ is a small

(1)

and larger industries.

ASSESSOR'S USE ONLY

(b) Referring to changes in the relevant real and money flows from Model One, explain in detail how New Zealand's entry into a further five free trade agreements could increase employment in New Zealand.

As export reciepts has risen this means that exporters are recieving much more profit/income, and to meet increased demand for goods, they increase production. This means that these firms will ~~now~~ require/demand more resources such as labour, thus causing job opportunities and wages to increase, thus increasing employment in these firms/industries.

(2)

Firms that rely on a lot of raw imported materials, will now demand more imported raw materials and less labour, as labour seems like a relatively more expensive resource, thus decreasing employment in some of these firms.
Overall employment will increase greatly as it occurs in more industries

(c) Explain in detail whether the new free trade agreements could be more effective in helping achieve the goals of either a balanced current account or full employment for the New Zealand economy.

The new free trade agreements will be more effective in achieving the goal of full employment. This is as it is likely that the increase in export reciepts will be too large relative to the increase in import payments, therefore it will most likely cause a current account surplus. The ~~full employment caused~~ FTA will greatly increase employment ~~throughout~~, as it effects our NZ export industries and other major firms/industries, which make up a large proportion of NZ's economy, whereas employment may only slightly decrease in a few industries where imported raw materials are required, and as these industries will still need labour

(3)

ASSESSOR'S USE ONLY

to operate as increasing raw materials won't be able to be used in production without labour or capital. Therefore it is likely that the economy will move towards full employment, but although we are not in a current account deficit, it is likely that NZ's ~~was~~ current account ~~[illegible]~~ won't be balanced but will rather be in surplus. //

M5

QUESTION THREE: Impact of savings and investment on the economy

ASSESSOR'S USE ONLY

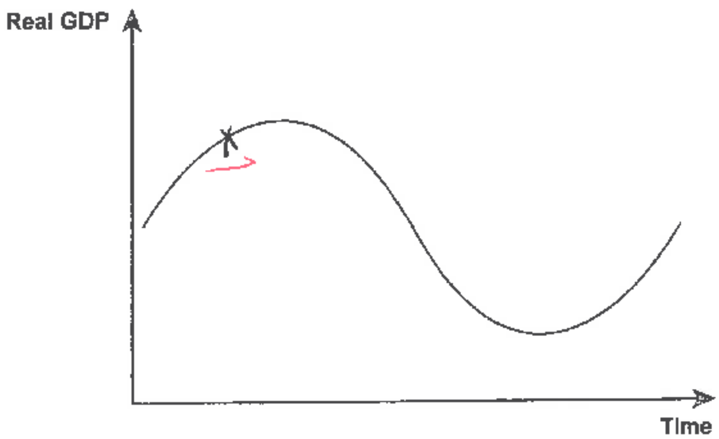
> "… saving is undeniably an important part of the economic process that gives rise to new investment and economic growth."
>
> Source (adapted): http://www.abc.net.au/money/currency/features/feat4.htm

(a) Explain in detail how increased savings may result in more investment in the economy. In your answer, define the terms "savings" and "investment".

Savings is income not spent. Therefore an increase in savings means that financial institutions will have more funds available for borrowing so they will decrease the interest rate to attract borrowing. This will cause borrowing for investment spending to increase as the cost of borrowing is less for firms now. Investment is when money is borrowed from the financial sector so that it can be spent on capital goods. ✓✓ (1)

> The magnitude of the impact of increased investment on the economy is dependent on New Zealand's position on the business cycle.

Model Two: The business cycle



(2)

(b) (i) Using Model Two, identify a possible position of the New Zealand Economy if it is close to achieving the full employment level of output.

(ii) Referring to the relevant stage of the business cycle, explain in detail why you chose the position identified in (i).

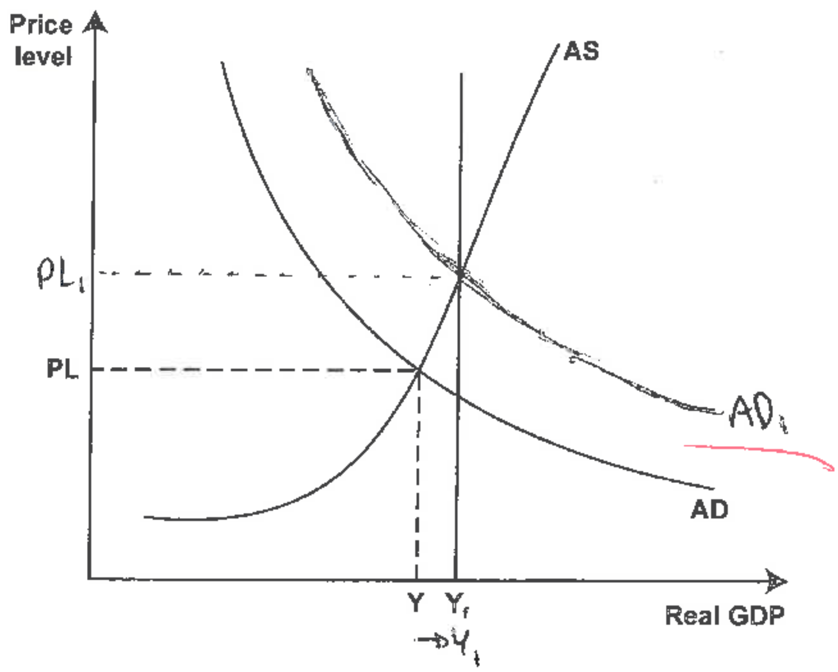
ASSESSOR'S USE ONLY

I chose point X as the point that is close to full employment as this is the point where Real GDP is nearlly at it's maximum, this means that if ~~produc~~ Real GDP is basically at it's maximum then production ~~is~~ must be high as Real GDP is ~~an~~ measure of production, High output/production means that nearlly all the resources in the economy will be required to help with this high output, thus meaning employment is nearlly ~~exactly~~ full as most resources become employed. //

(3)

(c) (i) On Graph Three below, show the impact of increased investment on the price level and real GDP, assuming that full employment is reached.

Graph Three: The New Zealand economy operating close to the full employment level of output (Y_f)



(4)

The question continues on the next page.

shown as the increase from PL to PL_1,

(ii) Referring to Graph Three and Model Two, compare and contrast the impact of increased investment on the goals of price stability and economic growth when the economy is close to full employment. In your answer, explain in detail:

- the impact of increased investment on the price level and real GDP
- the effectiveness of increased investment in achieving price stability and significant economic growth in the **short run** when the economy is operating close to the full employment level of output.

ASSESSOR'S USE ONLY

Increased investment spending means that more capital goods are demanded/purchased, therefore AD increases ~~as~~ to AD_1 as more NZ goods are demanded/purchased, and as $AD = C + G + I + (X-M)$, so any increase in I will increase AD. The increase in AD causes ~~as~~ a shortage of goods and services as Q_D is greater than Q_S, thus causing consumers to bid up prices until ~~a~~ new equilibrium is established. This increase in AD causes a very large increase in price level to PL_1, ~~and~~ due to demand-pull inflation, and a relatively small increase in Real GDP to Y_1. This is due to the position of the AD curve on the AS curve being very close to full employment, so any increase in ~~production~~ in resources required due to an increase in production, will ~~cost~~ have high costs as resources are now very scarce, thus causing a high amount of demand-pull inflation. Due to high amount of inflationary pressures, at a point where the economy is ~~in~~ a boom phase, inflation is already high so ~~the~~ added inflationary pressures is likely to cause an inflation rate above the 1-3% ~~rate~~ goal of inflation set by the government. As the economy was already in/near a boom phase before the AD shift, inflation is likely to be high due to scarce resources and economic

(5)

(6)

E7

Extra space if required.
Write the question number(s) if applicable.

QUESTION NUMBER

ASSESSOR'S USE ONLY

2a economy with already little trade barriers, imports won't increase that much but export reciepts will increase greatly, thus improving the current account balance.

3cii growth is likely to be low. Economic growth is likely to be low as production can hardly increase as not many resources are available to hire, as the economy is near full employment so resources are scarce, hence Real GDP only increases from Y to Y1. ~~Due~~ The position of the AD curve on the AS curve, ~~[illegible]~~ near full employment means resources are scarce and expensive so any increase in AD causes a very large increase in price level relative to Real GDP increases, therefore the rate of inflation is likely to increase much more than economic growth.

~~Alth~~ Although the governments goal of economic growth will be achieved, it will only be a small increase in economic growth, and the rate of inflation is likely to be above the governments target range of 1-3%. ~~This could be said due to the~~ This ~~[illegible]~~ also due to economy's position in the ~~[illegible]~~ business cycle (boom phase), and position of AD curve on AS curve relative to full employment.

(7)

Excellence exemplar 2017

Subject:	Economics	Standard:	91403	Total score:	19

Q	Grade score	Annotation
1	E7	This candidate has received E7 for this question because they: a) shifted and labelled the AD curve correctly on Graph One. (1) Explained that Consumer Spending and Investment Spending would also increase due to the multiplier effect. (2) More detailed explanations would have explained the concept of incomes being respent more fully or why the government spending would lead to more consumer and investment spending, and included references to the model to help illustrate that economic growth will increase. b) shifted and labelled the AS and AD curves correctly on Graph Two. (3) c) fully explained how the increased government spending increased AD (4), led to an increase in AS (5), and increased economic growth while including reference to Graph 2. They fully explain that the shift in AD and AS from Policy Two will have a bigger long-term impact on growth than Policy One due to the impact on productivity being more sustainable in the long term. (6) A more thorough answer could have also mentioned the possible multiplier effect of Policy Two or its reduced inflationary impact in comparison to Policy One.
2	M5	This candidate has received M5 for this question because they: a) Explained that NZ's entry into further FTA's will remove tariffs and other trade barriers and lead to increased exports and export receipts for NZ, improving NZ's Current Account. (1). A more detailed answer would have included correct reference to at least one component of the Current Account. b) Explained in detail that the increase in export receipts would lead to increased production in NZ and, due to the derived demand for labour, lead to increased employment in NZ. (2) c) Failed to provide a detailed explanation as to whether the new FTAs will be more effective in helping achieve a balanced current account or full employment for the NZ economy. (3)
3	E7	This candidate has received E7 for this question because they: a) Defined Savings and Investment. A more detailed explanation would have made the link between increasing funds saved and increasing funds available for investment more clearly. (1) b) Identified a position on the business cycle where the NZ economy would be close to achieving the full employment level of output, (2) and explained in detail why they chose this point, including that nearly all resources in the economy will be employed to achieve this level of GDP. (3) c) shifted and labelled the AD curve correctly in Graph Three so full employment is reached, (4) and fully explained how an increase in investment caused this shift. (5) Furthermore, they fully explain how the scarcity of resources when the economy is operating at full employment or the boom phase will mean that any increase in investment spending will be highly inflationary (6) and will also have little impact on economic growth. (7) A more comprehensive explanation would have specifically linked the lack of significant economic growth to the limited availability of capital resources.