

2022 ASSESSMENT REPORT

ECN315116 - ECONOMICS

Section A

PART I UNIT I

QUESTION 1

Cost benefit analysis is a form of project analysis which involves identifying all costs (including those difficult to measure) and all benefits of a particular project or course of action.

The costs and benefits once identified are assigned a dollar value. Strategies are used to assign a value where the cost or benefit is not naturally measurable in this way.

If the benefits exceed the costs, then the project would be regarded as being economically sound.

If there is a range of project alternatives, then the projects would be ranked in terms of net benefits.

It assists the allocation of scarce resources by identifying that usage of resources which provides the highest net benefit, and in this way maximises economic welfare.

Some students interpreted this from the perspective of opportunity cost and some credit was given to this.

QUESTION 2

Market failure is a situation where the free interplay of market forces provides a result that is unacceptable to society. Some ways in which markets may fail:

- Provision of Goods and Services (public and merit goods, demerit goods)
- Externalities
- Income Inequality
- Abuse of Market Power

Stronger responses included clear definitions and illustrated these with relevant examples.

QUESTION 3

Economic resources are the inputs used in the production and distribution of goods and services.

Often termed as the ‘factors of production’

Land	land and the resources on it or in it. Income stream is rent.
Labour	the human resources applying their labour in producing goods and services. Income stream is wages & salaries.
Capital	man-made input such as plant and machinery, buildings, computer systems. Income stream is interest.
Enterprise	human resource gathering together land, labour and capital to produce goods and services. Income stream is profit.

PART 2 UNIT 2

QUESTION 4

Consumption expenditure is expenditure by consumers on final goods and services.

Some of the many factors influencing consumption: income; propensity to consume; expectations of future; confidence; interest rates.

Investment expenditure is spending by enterprises on capital goods – those manufactured goods used for future production.

Some factors influencing – confidence; expectations of future; interest rates; expected rate of return.

Stronger responses described consumption and investment in the broader context of aggregate demand.

QUESTION 5

The government objective of full employment is reached when there is no cyclical unemployment. That is not zero unemployment, but a situation where mostly hard core and structural unemployment exists. ‘Full employment’ is a concept and the government does not have a numerical target for this.

The government objective of price stability relates to the objective of maintaining inflation within the range of 2-3%.

Some students were able to explain that both objectives are difficult to achieve simultaneously.

QUESTION 6

Governments have a role in economic management.

They have two main streams of policy available to them in order to reach their economic objectives relating to employment, price stability and growth.

Fiscal policy is exercised by governments. Simply put, deficit budgets (government expenditure greater than receipts) are expansionary and surplus budgets contractionary (government receipts greater than expenditures).

Monetary policy is exercised by the Reserve Bank of Australia by controlling interest rates (through its ability to set the cash rate). If interest rates increase then the outcome is contractionary, and if they decrease the outcome is expansionary.

In both cases the aim is to expand or contract economic activity to meet economic objectives.

PART 3 UNIT 3

QUESTION 7

Globalisation

There are a range of definitions possible – some concentrate on the international nature of relationships, others on connectedness or integration. Some are specific to Economics and others take a wider view involving general cultural characteristics. Markers accepted a range of definitions.

Generally, however, globalisation in its Economics sense is the economic interdependence of countries evidenced through international trade in goods and services, free trade agreements and liberalisation in trade in general, capital movements, movements of labour, international supply chains and outsourcing of production and business functions. Responses could also refer to the use of communications technologies and online marketing and payments systems.

Any two reasonable aspects discussed in sufficient detail were accepted.

QUESTION 8

There are three components to the current account balance:

1. The balance of trade (exports less imports).
2. Primary income balance (income earned from overseas less income paid overseas for work and financial investments).
3. Secondary income balance (unrequited transfers and some government payments).

The combined balances of these three elements provide the current account balance, which is a deficit if payments overseas exceed receipts from overseas – that is, the overall value of the three balances is negative.

Stronger responses discussed the current situation where the current account is in surplus.

QUESTION 9

A country has a comparative advantage over another country in a product if it is able to produce that product at a lower opportunity cost than that other country can achieve. The principle of comparative advantage is that each country should specialise in the area of its lowest opportunity cost. Stronger answers discussed resource allocation as part of the discussion of opportunity cost. Acceptable products that Australia has a comparative advantage in included primary products (mining, agricultural) as well as tertiary education.

Section B

PART I UNIT I

QUESTION 10

This question assessed students' underlying understanding of the circular flow of income model by tweaking the formulation of previous questions on this topic. While the vast majority of students did a reasonable job on this question, very few received full marks. 'Income' was often oversimplified to include only wages, and 'Investment' was often described as banks investing in businesses rather than businesses borrowing money to be more productive – a subtle but important distinction. 'Overseas students' should have been categorised as an export.

QUESTION 11

This question was generally well answered. Stronger responses provided both a general demand or supply factor (e.g., decrease in consumer tastes and preferences) and a specific example (e.g., concern for animal welfare). The final part of the question on the change in total revenue was successfully explained by the vast majority of students.

QUESTION 12

While this question was well answered, there were still several instances of students failing to fully annotate their graphs. Changes in the supply or demand curve as well as changes in price and quantity were aspects of student responses required for full marks. In item c), markers accepted an increase or decrease in demand if this was backed up by a reasonable explanation.

PART 2; UNIT 2

QUESTION 13

Students were mostly able to identify two characteristics likely in an economy in the expansion phase of the business cycle. Rising inflation and falling unemployment were two of the most common characteristics, and high marks were awarded to students who explained why this would happen. Monetary policy was, in some papers, confused with fiscal policy. Stronger responses discussed how changing interest rates would affect aggregate demand and therefore slow down growth in inflationary/boom phase or boost growth to reduce the severity of a downturn.

QUESTION 14

Most students correctly identified that the first part of the question would increase aggregate demand, the second would decrease it and the third would boost aggregate supply. Many students did not annotate graphs adequately with some loss of marks resulting. Many students also failed to differentiate between 'price' and 'price level' (or inflation), with the explanations resembling discussion of a market diagram rather than a macroeconomic one.

QUESTION 15

This question received relatively high marks. Stronger responses discussed the correlation and possible links between the two, with low economic growth in 2019 and early 2020 resulting in low inflation, and prices falling after the large fall in GDP in 2020. As the level of economic growth picked up inflation also started to rise. Some students also discussed that inflation could come from other sources, making the correlation a loose one rather than a firm causal relationship.

PART 3 UNIT 3

QUESTION 16

Many students avoided this question, but it was clear also that many stronger students were well-prepared and could demonstrate the methods and consequences of trade protection on a graph. The final part of the question (on the impact of a subsidy) was more likely to include errors, with stronger responses recognising that the world price would still apply unless the right shift in the supply curve was very large.

QUESTION 17

The first part of this question was well done by most students, but in the second part there were some interesting discussions that did not always address the question directly. Implications for the broader economy included the structure of the labour market, higher living standards through Australia's application of the principle of comparative advantage and the possible issues associated with loss of self-sufficiency in some critical goods. Some students

catastrophised about the likelihood of a future current account deficit, which was not evident from the data provided.

QUESTION 18

While answered well by the majority of students, some students discussed supply issues related to the Australian dollar, which did not reflect the change shown on the graph. Responses such as an increase in exports, an increase in the prices of major commodities, increased foreign investment, a rising cash rate and expectations of an appreciation by speculators were amongst the more common correct answers. Positive outcomes for the Australian economy were mostly about lower prices for consumers, but some students were also given credit for recognising that a higher value for the Australian dollar would alleviate some of the inflationary pressures evident at the time of the exam. This response was appropriate in the current context, but may not be in other economic circumstances.

Section C

PART 1 UNIT 2

QUESTION 19

- a) Students needed to convey in their answers what the term inflation was, but the important focus needed to be how each of the three factors flowed through to create either demand pull inflation or cost push inflation. Some students spent too long introducing the topic of inflation, not leaving enough time to spend on the specifics of the question.
- Students were required to explain how fiscal policy interventions (an increase in G in the Aggregate Demand formula) contributed to demand pull inflation. It is important to note that stronger answers incorporated a deeper understanding by linking the increase in Aggregate Demand to supply side constraints or firms reaching supply capacity, thus creating the environment for demand pull inflation. Some students also drew aggregate economy diagrams to reflect an increase in the general level of prices.
 - The low cost of borrowing is a monetary policy response to a slowing economy, so students were required to integrate their knowledge of monetary policy and how an expansionary/loosening stance contributes to an increase in economic activity. Specifically, students needed to explain how a reduction in the cash rate could encourage consumption and investment, thus increasing Aggregate Demand. Again, if Aggregate Demand is increasing at a faster rate than Aggregate Supply, creating shortages, then this may lead to Demand Pull Inflation.

- Students did a good job at incorporating information from the stimulus, along with their general knowledge, to give examples and explain the impacts of supply chain problems in recent years. Stronger answers discussed how shortages of inputs, or increased price for inputs, impact upon supply. Increased input costs across the economy cause a decrease in Aggregate Supply, resulting in firms increasing prices to maintain profit margins. Stronger answers named this up as creating Cost Push Inflation. Some students also drew aggregate demand and supply diagrams to depict this.
- b) Knowledge of the Reserve Bank of Australia's sustainable level of inflation was suggested as it was specifically mentioned in the question. Most students knew that the published range is 2%-3% per annum.

Many student answers focussed too heavily on cost-of-living pressures, without a lot of discussion of other economic problems. Some students also reverted to listing the problems with little background as to the nature (how/why) of the problem.

The question specifically asked for economic problems, but some students included social problems. These were given credit if there was some link back to an economic problem.

- c) This question required students to have a knowledge of what social welfare payments might entail (examples) and importantly, that those receiving social welfare payments have no bargaining power with government for increases to social welfare payments. Even if payments are indexed to inflation, the increases will be after inflation figures are announced, usually in the ensuing federal budget. Thus, a time lag is created. The impact of higher costs for those surviving on welfare payments who consume most, if not all, of their income on needs, results in this demographic group being more impacted than those with higher incomes.
- d) Students needed to integrate into their answer an understanding of a tightening/contractionary monetary policy stance. This stance needed to then be used to explain how the transmission mechanism worked to impact on the behaviour of consumers and business to reduce/influence consumption and investment, thus reducing aggregate demand, and lessening demand-pull inflationary pressures. Other transmission channels such as the impact of inflation on net exports were also included in better answers.
- e) Students needed to incorporate into their answer a knowledge of microeconomic reform in terms of what it is and its purposes and benefits to enabling efficiency improvements in the economy. This knowledge and understanding needed to be linked to addressing the effects of cost push inflation. Examples of micro economic reform, such as competition policy, privatisation, tax reform and deregulation were also discussed as a means of bringing down input costs through improvements in resource use to allow reduced cost push inflation. Other methods to boost aggregate supply such as infrastructure and education/training were mentioned by some students. Some students

used aggregate demand and supply diagrams to show the effect of microeconomic reform on prices and output, which was appropriate.

- f) Social justice is the view that everyone in a society deserves equal economic, political and social rights and opportunities. In the context of this question, it is important for students to be able to relate how a change in policy, in this case interest rates, will worsen or improve social justice outcomes for members of society. For low-income earners who spend the bulk of their income on needs, inflation will worsen the purchasing power of their income, reducing their standard of living due to not being able to satisfy as many wants as previously. If the RBA raises interest rates to address rising inflation, low-income earners are further affected as the blunt instrument of monetary policy does not discriminate between low-income earners with loans compared to high income earners with loans. The additional costs of debt servicing will mean that, for many low-income earners, debt servicing will take priority over satisfying needs, resulting in a deterioration in quality of life. However, some in Australia will benefit from rising interest rates, such as those with savings in the bank and self-funded retirees.

QUESTION 20

Question 20 was a less popular choice than Question 19.

- a) Students were required to briefly link a significant economic downturn to an expected rise in cyclical unemployment. It was important to address the question by referring to the Economic Costs of unemployment, as well as the Social Costs of unemployment. Many students were not able to distinguish the two, but were given due credit for a mixture/variety of examples. Some students provided very little detail on each problem, whereas the question asked students to describe the problems. Economic problems included lower incomes, lower consumption, increased pressure on the budget. Social problems included poverty, debt, family breakdown etc.
- b) This question required students to explain how it is difficult to control rising inflation without causing an increase in unemployment, and vice versa. For example, if the economy is experiencing Demand Pull inflation, then an appropriate policy adjustment would be a contractionary Monetary and/or Fiscal policy stance. However, this setting would cause a decrease in the rate of growth in Aggregate Demand, to better match Aggregate Supply. In doing so, this reduced rate of growth in Aggregate Demand may not be enough to sustain existing employment levels, thus reducing inflation, but with the consequence of rising unemployment. The opposite situation could have also been explained. That is, how to reduce unemployment with expansionary Fiscal and/or Monetary Policy settings without creating too much growth in Aggregate Demand that will address rising unemployment but may in turn result in Demand Pull inflation.
- c) This question was very specific and referred to the stimulus content that young Australians are overrepresented in the unemployment data. The question asked for

students to explore the reasons for this and the stimulus provided two content areas for the students to explore.

- i. Often, unskilled agricultural work that may suit the skill set of some unskilled young people is not conveniently located. Many unskilled jobs in cities where most young people live have now gone, or are few in number.
 - ii. In contrast, it is difficult for young people to gain the required skills and experience required if they have not previously worked and therefore cannot display the level of skill level required.
- d) This question was in two parts and students needed to allocate similar time and content across each part.
 - The first part was on how an expansionary Fiscal Policy stance by the Federal Government, and in particular, JobKeeper, helped address the problems of rising unemployment caused by the large fall in the rate of growth in Aggregate Demand in 2020. Students were required to explain how an increase in government expenditure assisted to maintain levels of growth in Aggregate Demand, which assisted in slowing the rate of increase in unemployment. Stronger answers explained the purpose and benefits of the JobKeeper program. Such benefits included the maintaining of income so that consumption could continue, avoiding loss of skills, the need to re-employ staff when demand recovers and assisting firms to meet wages costs. This part of the question was completed well.
 - The second part of the question required students to explain how Monetary Policy could be used to address an economic downturn and the resultant rise in unemployment. To address rising unemployment, an expansionary/loosening Monetary Policy stance is adopted by the Reserve Bank of Australia. Students needed to explain how a lowering of the cash rate would assist to stimulate Aggregate Demand to maintain existing levels of employment and grow the economy enough to create new employment opportunities for the unemployed. This theory relates to the Transmission Mechanism, although specific mention of this term was not required. Better answers discussed the impact of lower interest rates on consumption, investment, the value of the Australian Dollar and export volumes, and how these impacts would flow through the economy to increase the rate of Aggregate Demand to encourage firms to employ more resources, such as labour.
- e) This question required students to discuss both the costs and benefits for individuals, business and government of the expansionary fiscal policy measures mentioned in the stimulus. This question could be answered with a number of different focuses, as it asked for unspecified references to the stimulus. A discussion of expansionary fiscal policy, such as JobKeeper, OR increased funding for programs to support young people to become more skilled and hence, more employable, OR a combination of the above.

- The costs primarily centred around the increased level of government debt that these measures created. Stronger answers discussed:
 - The intergenerational impacts of increased debt levels.
 - The future opportunity cost, with a common statement being the need for increased future tax collections and future spending constraints that government may need to apply in order to repay debt.
 - How not all those who became unemployed were eligible for JobKeeper.
 - The benefits were well done, with students discussing the avoidance of all the economic and social problems that would have otherwise occurred with rising unemployment. For business, the maintaining of staff and productive capacity, rather than retrenching and then employing/training were discussed. The benefits of a more skilled workforce were also discussed in relation to youth employment programs. The benefits for government were the avoidance of long-term unemployment (especially Youth) that have been characteristics of previous recessions and the immediate benefit of a short-lived economic downturn.
- f) This was a relatively straightforward question, but it did require students to display their knowledge and understanding of what Microeconomic reform is. The purpose of Microeconomic reform is to increase Aggregate Supply by improving the efficiency and the productivity of producers and industries. Stronger answers linked the Youth Policy Framework to the concept of Microeconomic reform, then elaborate on the benefits to industry of a more skilled labour force.

PART 2; UNIT 3

QUESTION 21

- a) The mining boom brought a great interest in Australia by overseas companies. As Australian businesses had insufficient domestic financial resources available to develop mines, the capital flowed in from overseas to cover this 'investment gap'. And so foreign equity and foreign debt grew.

Borrowed funds incur interest charges, and equity funding is rewarded with profits remitted to overseas owners, generally in the form of dividends. The mining boom saw these payments outweigh receipts from overseas, and so the deficit in the net primary income element of the current account widened.

The other principal contributor to the current account deficit is the trade balance – the excess of exports over imports or vice versa.

The mining boom has also contributed to the trade balance element of the current account. Particularly over the past few years, as mines have moved from development

phase into production phase, mineral exports have formed an important part of Australia's balance of payments, and have provided a current account surplus by 'outweighing' the net income deficit. This has been aided by strong prices for several of Australia's mineral exports, particularly iron ore.

Students that did well used appropriate quotes from the stimulus.

- b) As explained in the stimulus, an investment gap is a situation where there are insufficient savings in the economy (domestic savings) to meet the demands for funds for investment.

In this situation, the shortfall of domestic funds is met through funds from overseas.

They may flow into the country as equity funding – both direct, where businesses operating here are actually owned by overseas entities, or portfolio where shares in businesses are owned overseas.

Alternatively, funds may be borrowed through a range of financial instruments. This will require payment of interest overseas.

Therefore, the issues arising from the investment gap is that it establishes a future stream of remittances to the overseas sector, both as reward for ownership and as costs associated with servicing debt.

- c) Possible answers (not exhaustive):

Costs

- Barrier to Australian owned businesses participation.
- Lack of commitment to Australia.
- Negative effects in Australia of business decisions taken by multi-national companies based upon their international performance (e.g., shift operations to low wage countries).

Benefits

- Introduction of advanced technologies.
- Advanced industrial methods.
- Provision of facilities for local communities .
- Availability of higher-level jobs.

- d) This leads to the school of thought that holds that foreign investment, ownership and debt is a positive contributor to the economy and our economic welfare. This point of view is that decisions made by individuals and businesses, which were economically sound

when made, will provide an outcome (a net income deficit) which is likewise economically sound.

Sometimes described as the 'consenting adults' view of the current account.

This view does not see net income deficits as an undesirable situation, rather they will be advantageous to the country by allowing more consumption and investment in productive activity than would otherwise be available.

It runs counter to the view that large deficits are necessarily bad as future cost of servicing debt and rewarding foreign owners detract from future economic welfare.

e) There were two parts to this question. Impacts could be either positive (benefits) or negative (costs).

i. Impact on business (positive).

Benefits businesses as funds are available for investment projects not otherwise available.

Foreign businesses may bring with them advanced technologies and processes not available domestically.

The connections may lead to an expanded international market for Australian businesses.

BUT (costs).

High levels of debt require stream of future repayments that may restrict future activities.

Proportion of business revenue is servicing loans or directing profits offshore and therefore not available for investment.

ii. Impacts on individuals.

Employment opportunities in businesses which may not exist without foreign funds or ownership.

BUT.

Future costs of servicing a deficit may limit returns to labour.

f) As stated in the stimulus "as a result of saving exceeding domestic investment", Australia is now a net lender to the rest of the world.

Since 2019, savings excess to Australian needs flow overseas and hence the term 'net lender'.

On the one hand this may be seen as a positive – creating such levels of savings that there is no longer a requirement to borrow overseas, hence overcoming the investment gap situation. This should also reduce the net primary income deficit over time, contributing to a long-term improvement in the current account balance.

On the other hand, it also means that there are insufficient investment opportunities being taken in Australia to ‘soak up’ available domestic savings, which are now being ‘used’ overseas. For some decades the reverse was the situation, where there were insufficient domestic funds to meet the needs of business in Australia.

QUESTION 22

a) There were two components to this question:

- i. The vast majority of responses firstly identified FTAs as ‘free trade agreements’ then discussed them as agreements between countries, including ‘bilateral multilateral or global’ agreements that reduce ‘artificial barriers’ to trade imposed by governments such as ‘tariffs quotas or subsidies’. Other inclusions, such as ‘import controls on certain products, licensing, safety considerations, biological controls may be involved’, strengthened responses.
- ii. Response strength diverged here with the strongest identifying and delineating a number of problems **addressed by FTAs** which may have included:
 - Obtain goods and services they cannot produce themselves.
 - Specialisation and comparative advantage.
 - Efficiency in resource allocation.
 - Achieve economies of scale.
 - International competitiveness.
 - Encourage innovation.
 - Reduce costs of production.
 - Increase standards of living.

Strong responses spoke to the **problems posed** by FTAs to Australian economy. Identifying **multiple problems and describing the mechanisms** that bring them about as a result of FTAs were a feature of strong responses. These included:

- Infant industries / protected industries face increased competition.
- Unemployment may rise as inefficient firms fail.

- Structural change and import competing firms/industries fail and skills and experience decline.
 - Loss of government revenue from import taxes and potential for higher transfer payments.
 - Domestic dependence on foreign industries for a range of strategic products.
 - Sovereignty implications as significant trading partners weaponise economic dependence in the political forum.
 - Cheaper imports versus increased exports can be discussed in some fashion though Australia is a net exporter and therefore this argument may not fall into the problems category.
 - Issues related to loss of culture as imports and prices lower consumption of domestic goods, services, and experiences.
 - Issues related to dumping.
- b) Students related the above points to individuals, businesses and governments and included benefits.
- c) Both positive and negative implications were used and awarded marks, with most responses considering some of the following ideas:
- Social justice (positive):
 - Increased job opportunities.
 - Social justice (negative):
 - Issues related to labour conditions for working in economies from which we now import – exploitation, wage theft, slavery, conditions, governance.
 - Issues related to structural unemployment in import competing industries and communities – loss of incomes, skills, culture. Implications for high unemployment in these communities.
 - Environment (positive):
 - Issues related to more efficient allocation of resources, fewer inputs and less waste in production.
 - Environment (negative):
 - Issues related to environmental impact of increased transportation. Increased domestic and global output leading to greater air, sea, road, rail transportation and co2 emissions.

- Issues related to environmental impact of increased output leading to increased resource use and waste – more cheaper disposable goods, landfill, plastics.
 - Issues related to greater consumption of imports from economies with fewer/weaker regulations on governance/production practices – comparative advantage achieved as a result of cost reductions in waste disposal, cheaper black and brown energy inputs. Ecosystem degradation and habitat loss etc.
- d) This impact on consumers and businesses will be varied.
- Consumers now have available to them goods which have been produced overseas. The price of these products is less due to the removal of the tariff. Also domestically produced goods must now compete with these imports and the price of the domestic goods is likely to fall. They can purchase more, or at least not spend as much on the same amount. There may also be a widening of product choice.

Students could have discussed the impacts on producers using some combination of the following:

- i. Those that compete directly with the imported product which has now fallen in price. In this circumstance they will lose revenue, and if they are already borderline then they may need to cease production. In order to survive may need to become more efficient in their production.
 - ii. Those who manufacture product for export have increased opportunities due to reduced tariffs in other countries. These producers will see sales volumes increase and revenues increase and possibly an expansion in their industry in general.
 - iii. Those who use imported product as intermediate goods, or imported bulk commodities as inputs will now buy more cheaply and hence able to maintain profit and lower price.
- e) In the short-term, exports become cheaper in overseas markets and therefore more competitive. Imports also become cheaper for Australian consumers, but this will negatively impact some Australian import competing industries.

In the long order to compete with cheaper imports businesses in those markets must become more efficient and produce more with less. Exporting industries expand and offer more employment opportunities

- f) As this question asked for the opinion of students, there was no single correct answer. Marks were allocated according to the strengths of the economic justifications used to support their view.