MARKER CODE		Student Personal Identification Number

South Pacific Form Seven Certificate

ECONOMICS

2018

QUESTION and ANSWER BOOKLET

Time allowed: Three hours

(An extra 10 minutes is allowed for reading this paper.)

INSTRUCTIONS

Write your **Student Personal Identification Number (SPIN)** in the space provided on the top right-hand corner of this page.

Answer **ALL QUESTIONS**. Write your answers in the spaces provided in this booklet.

If you need more space for answers, ask the Supervisor for extra paper. Write your SPIN on all extra sheets used and clearly number the questions. Attach the extra sheets at the appropriate places in this booklet.

Major Learning Outcomes (Achievement Standards)	**Skill Level & Number of Questions**				**Weight/ Time**
	Level 1 ***Uni-structural***	**Level 2** ***Multi-structural***	**Level 3** ***Relational***	***Level 4 Extended Abstract***	
Strand 1: Resource Allocation via the Market System Demonstrate understanding of the key ideas about the operation of the market system, and how decisions are made and their outcome in a modern market economy.	7	5	3	1	30% 76 min
Strand 2: Resource Allocation via the Public Sector Demonstrate understanding of resource allocation via the public sector.	4	3	2	1	20% 52 min
Strand 3: Aggregate Economic Activity and Policy Demonstrate understanding of aggregate economic activities and policies.	7	3	1	1	20% 52 min
TOTAL	**18**	**11**	**6**	**3**	**70% 180min**

Check that this booklet contains pages 2-17 in the correct order and that none of these pages are blank.

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

STRAND 1: RESOURCE ALLOCATION VIA THE MARKET SYSTEM

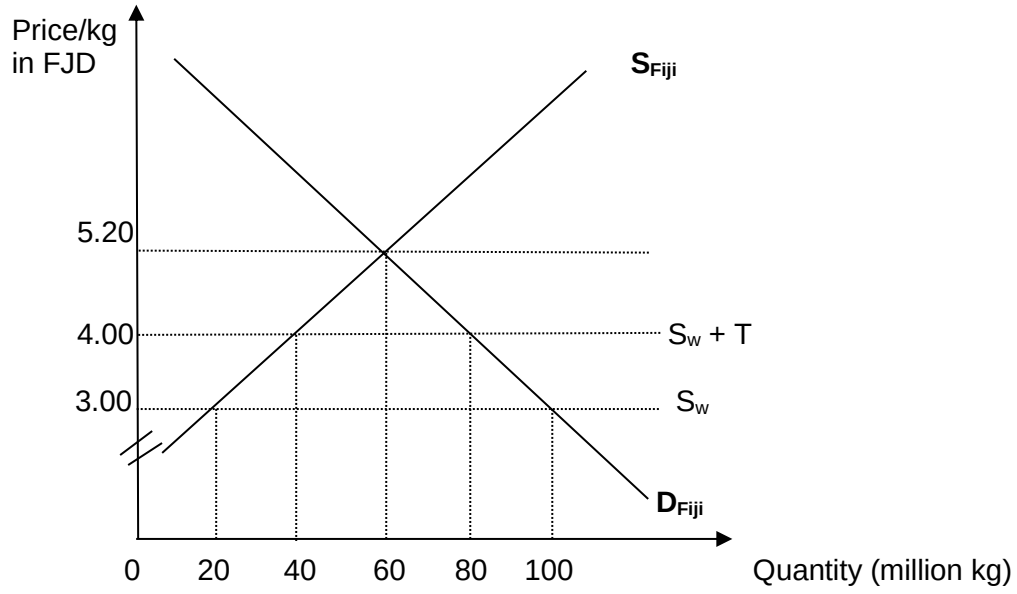
Answer **ALL** five questions in this strand.
As a guide spend no more than **76 minutes** on this strand.

1.1: Understand how the Market for an Internationally Traded Commodity Works

Trade liberalization brings real economic challenges for small Pacific Island Countries (PICs). Free trade rules (e.g. the removal of tariff) articulated under regional free trade agreements (FTAs) have created a combination of circumstances that threatened the viability of Pacific Island economies and political and social stability in the region.

Adapted from: Free Trade in the South Pacific: An Overview by Ilan Kiloe – published in *Journal of South Pacific Law (2009).*

Graph 1. The Fijian Market for Beef



Refer to **Graph 1** above to answer questions 1.1a and 1.1b.

Assessor's use only

1.1a	$S_w + T$ shows the price of beef in Fiji with a tariff imposed, and S_w is the price before the tariff. Calculate the price of beef under free trade. _____ _____ _____	**Multistructural** 2 1 0 NR

Assessor's use only

1.1b	Explain how the market for beef works with the imports when the price is $4.00 per kg.	**Relational** 3 2 1 0 NR
1.1c	Explain the effects of free trade on the domestic buyers, producers and the government.	**Relational** 3 2 1 0 NR

1.2: Explain the Concept of Marginal Utility and the Individual Demand Curve

Table 1. Below is Mary's Utility Schedule for oranges per day

Quantity Consumed	Total Utility ($)	Marginal Utility ($)
1	2	2
2	3.5	1.5
3	4	0.5
4	4.3	0.3

Assessor's use only

1.2a Use the schedule in Table 1 to construct Mary's Demand Curve for oranges per day.

Graph 2. Title: _____

Multistructural	
2	
1	
0	
NR	

1.2b Define the concept of **Marginal Utility**.

_____

_____

_____

_____

Unistructural	
1	
0	
NR	

1.2c State the Law of Demand.

_____

_____

_____

_____

Unistructural	
1	
0	
NR	

1.3: Understand Income Elasticity of Demand

The coefficient of income elasticity of demand (YED) can be used to help producers forecast demand for their products and distinguish between types of goods.

Assessor's use only

1.3a	Define **Income Elasticity of Demand (YED)**. _____ _____ _____ _____	**Unistructural** 1 0 NR
1.3bi	When Mary's income increased by 2%, her demand for Good X increased by 4%. Calculate the Income Elasticity of Demand (YED) for Good X. _____ _____ _____	**Multistructural** 2 1 0 NR
1.3bii	From your calculations in 1.3bi above, identify Good X as either luxury, normal or inferior. _____	**Unistructural** 1 0 NR

1.4: Understand the Firm's Production Costs and its Supply Curve

The table below shows the production of chairs at a furniture production firm.

Table 2. Productivity of Workers at a Furniture Production Firm.

Note: Factory workers who produce chairs are paid $10 per hour.

Total Output (number of tables)	Total hours worked	Hours required to increase output by one unit	Marginal cost of producing extra units
1	10	10	$100
2	15	5	
3	40	25	$250
4	70	30	
5	110	40	$400

Assessor's use only

1.4a Calculate the marginal cost of producing:

(i) 2 units: _____

(ii) 4 units: _____

Multistructural	
2	
1	
0	
NR	

1.4b State the Law of Diminishing Returns.

_____

_____

_____

_____

_____

Unistructural	
1	
0	
NR	

1.4c Wages of factory workers are classified as Accounting Costs.

Define **Accounting Costs**.

_____

_____

_____

_____

_____

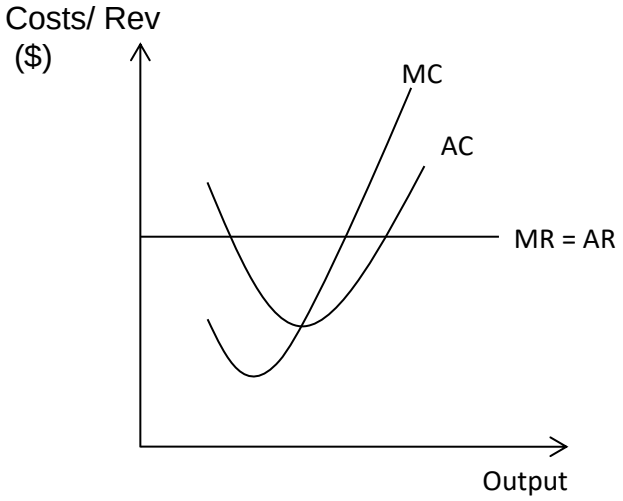
Unistructural	
1	
0	
NR	

1.5: Demonstrate an Understanding of the Role of Firms in a Market Economy

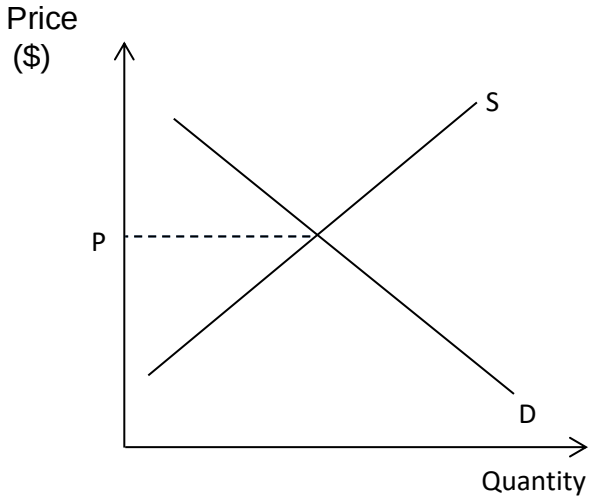
The market for milk in New Zealand is said to be a Perfectly Competitive Market.

Graph 3 shows the short run equilibrium for a milk producer while **Graph 4** shows the Market Supply and Demand curves for Milk.

Graph 3 Milk Producer



Graph 4. Market for Milk



Assessor's use only

1.5a	In the long run the firm usually earns a normal profit. Illustrate this by drawing: (i) a new AR curve on Graph 3 (**Label it AR_1**); and (ii) a new Supply curve on Graph 4 (**Label it S_1**). Explain how normal profit is achieved in the long run. _____ _____ _____ _____ _____ _____	**Relational** 3 2 1 0 NR
1.5b	Define **normal profit**. _____ _____ _____ _____	**Unistructural** 1 0 NR

Assessor's use only

1.5c	Describe **two** features of competition. (i) _____ _____ (ii) _____ _____	**Multistructural** 2 1 0 NR
1.5d	Discuss the impacts of the relationship between Average, Marginal and Total Revenue under Perfect Competition using the example of milk production above. _____ _____ _____ _____ _____ _____ _____ _____ _____ _____ _____ _____ _____ _____ _____ _____	**Extended Abstract** 4 3 2 1 0 NR

STRAND 2: RESOURCE ALLOCATION VIA THE PUBLIC SECTOR

Answer **ALL** questions in this strand.
As a guide spend no more than **52 minutes** on this strand.

2.1: Understand Market Failure as a Basis for Government Intervention

The 'free market' is not always able to achieve either allocative efficiency or equitable outcomes. These situations are defined by economists as market failure and hence provide justification for government intervention.

Assessor's use only

2.1a Define **free market**.

Unistructural	
1	
0	
NR	

2.1b List **two** factors apart from externalities, property rights and public goods that can cause market failure.

(i) _____

(ii) _____

Multistructural	
2	
1	
0	
NR	

2.1c Describe **two** features of public goods.

(i) _____

(ii) _____

Multistructural	
2	
1	
0	
NR	

2.1d Government usually intervenes in the market through the provision of public goods.

List **two** alternative methods of the collective provision of public goods.

(i) _____

(ii) _____

Multistructural	
2	
1	
0	
NR	

Assessor's use only

2.1e	Explain why public goods are not normally provided by the market.	

Relational	
3	
2	
1	
0	
NR	

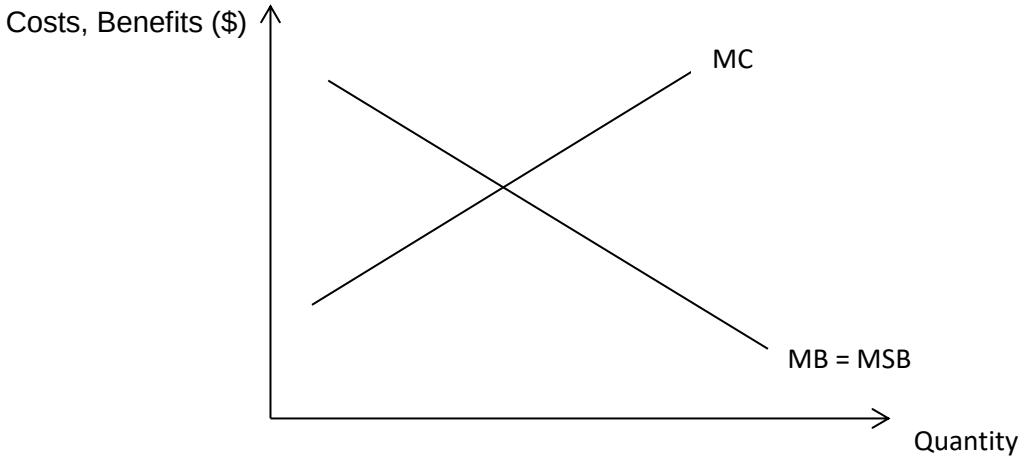
2.2: Explain Externalities and Government Intervention to Internalize Externalities

Case Study

A factory that discharges wastes into the sea wishes to expand its operations. The sea is polluted and a previously healthy fishery is badly affected. Clearly, this is a negative externality of production. This externality could be internalized without the use of government intervention if **property rights** could be established.

Source: Senior Economics, Second Edition by Geoff Evans, P.216.

Graph 5: Illustrating the Effects of the Negative Externality of Production



Assessor's use only

2.2a	Define **property rights**. _____ _____ _____ _____	**Unistructural** 1 0 NR
2.2bi	On Graph 5 above, Draw the Marginal Social Cost Curve (**Label the curve MSC**) to illustrate the negative externality of production; also identify and label the social equilibrium quantity, $\mathbf{Q_S}$.	**Relational** 3 2 1 0 NR

Assessor's use only

2.2bii	Identify the private equilibrium price (**Label it P_E**).	**Unistructural**: 1 ; 0 ; NR
2.2biii	Identify the social equilibrium price (**Label it P_S**).	**Unistructural**: 1 ; 0 ; NR
2.2c	When property rights are unclear, the government may intervene to internalize the negative externality of production. Discuss the cost implications when government uses tax to internalize the negative externality of production.	**Extended Abstract**: 4 ; 3 ; 2 ; 1 ; 0 ; NR

STRAND 3: AGGREGATE ECONOMIC ACTIVITY AND POLICY

Answer **ALL** questions in this strand.
As a guide spend no more than **52 minutes** on this strand.

3.1: Demonstrate an Understanding of National Income Accounts

Use the table below to answer questions 3.1a to 3.1c.

Table 3. National Income

National Income Components	$ million
Operating Surplus	22 000
Imports of Goods & Services	20 000
Increase in Stock	2 000
Compensation of Employees	33 000
Export of Goods & Services	19 000
Final Consumption Expenditure by Government	12 000
Final Consumption Expenditure by Private Sector	44 000
Gross Fixed Capital Formation	14 000

Assessor's use only

3.1a Use the data in Table 3 above to calculate the Gross Domestic Product using the Expenditure Approach.

Multistructural	
2	
1	
0	
NR	

3.1b Define **Real Gross Domestic Product**.

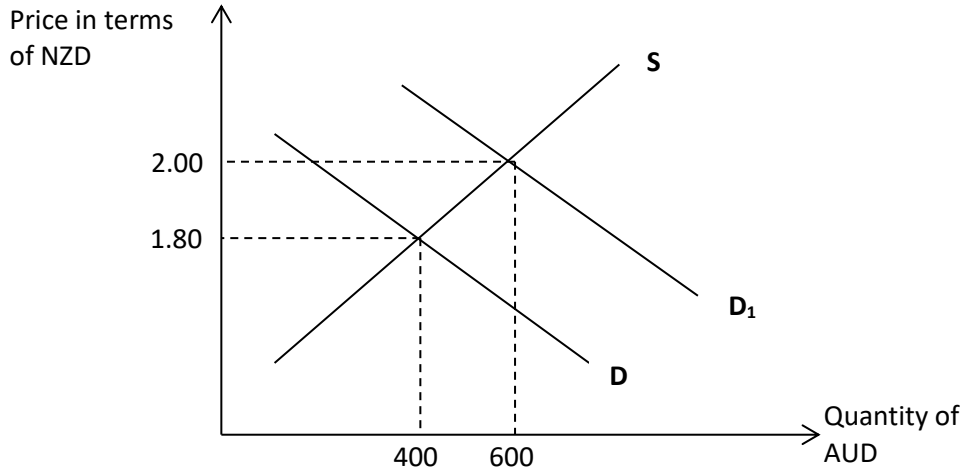
Unistructural	
1	
0	
NR	

3.1c Identify **one** component of Aggregate Demand given in the National accounts in Table 3 above.

Unistructural	
1	
0	
NR	

3.2: Understand the Operation of the Foreign Exchange Market with a Floating Exchange Rate

Graph 6 **Graph showing the Appreciation of the Australian Currency (AUD) against the New Zealand Currency (NZD)**



Assessor's use only

3.2a	Define **appreciation of the exchange rate**. _____ _____ _____ _____	**Unistructural** 1 0 NR
3.2b	Describe the supply and demand analysis in the operation of the foreign exchange market with a floating (flexible) exchange rate. _____ _____ _____ _____ _____ _____ _____	**Multistructural** 2 1 0 NR
3.2c	Describe **two** reasons for the increase in demand for the Australian currency. (i) _____ _____ (ii) _____ _____	**Multistructural** 2 1 0 NR

Assessor's use only

3.2d	Discuss the impacts of the appreciation of the exchange rate on international trade of goods and services using examples.	

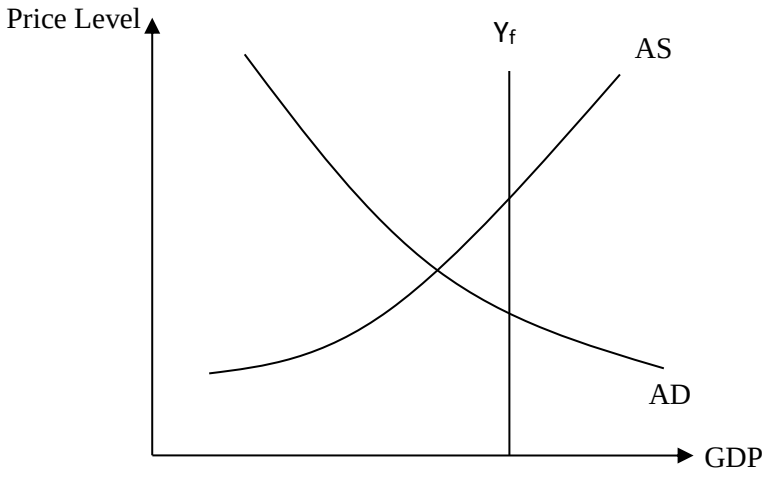
Extended Abstract	
4	
3	
2	
1	
0	
NR	

3.3: Demonstrate Understanding of the Impact of Monetary Policy

South Pacific governments are currently facing difficult macroeconomic policy choices. Inflationary pressures are present while in the last few years fiscal stimulus packages are causing concern about growing public debt levels. As a consequence, some politicians are arguing for cuts in government spending and recommended a monetary policy choice.

The Aggregate Demand/Aggregate Supply model below shows Economy Y experiencing a Recessionary Gap.

Graph 7. Aggregate Demand and Aggregate Supply Curves for Economy Y



Assessor's use only

3.3ai	On Graph 7 above, Identify the equilibrium level of prices (**Label it PL**).	**Unistructural** 1 0 NR
3.3aii	Identify the equilibrium level of production (**Label it Y_e**).	**Unistructural** 1 0 NR
3.3b	Define **monetary policy**. _____ _____ _____ _____	**Unistructural** 1 0 NR

Assessor's use only

3.3c	Name a monetary policy that can be used to eliminate the recessionary gap. _____	**Unistructural** 1 | 0 | NR |
3.3d	Explain the effect of the monetary policy mentioned in question 3.3c above on employment. _____ _____ _____ _____ _____ _____ _____ _____ _____ _____ _____ _____ _____ _____ _____	**Relational** 3 | 2 | 1 | 0 | NR |

THE END