ECONOMICS PRACTICE HALF YEARLY EXAMINATION

SECTION I

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

SECTION II

Question 21

(a) $\frac{125}{120} \times 100 = 104.2$

(b) The movement in the terms of trade is an improvement. An answer to this question may include any two of the following:

- An increase in demand for the economy's exports may have led overseas buyers to bid up export prices relative to imports.
- Exports, e.g. commodities, may have experience a price boom relative to import prices.
- Intense global competition for the goods this economy imports may have led to a decline in import prices relative to exports.
- Technological advances in the production of the goods this economy imports may have lowered prices relative to exports.

(c) When an economy's terms of trade improve, its export revenue is likely to be increasing relative to its import costs (if quantities remain constant). According, the balance on goods and services component of the CAD should improve, lessening the demand for foreign inflows on the capital and financial account.

(d) An answer to this question may include any two of the following:

- Australia's low level of national savings, which creates a dependence on foreign capital inflows to meet the domestic demand for funds for investment.
- Australia's persistent current account deficits, which require foreign inflows to balance the economy's external accounts.
- Australia's record as a stable, prosperous economy, which encourages foreign investment in Australia.
- Australia's high interest rate differential in comparison to key economies such as the United States, encouraging financial inflows from investors seeking to maximise returns on their investment.

Question 22

(a) An answer to this question may include any two of the following:

- An increase in global labour flows
- An increase in global investment flows
- An increase in global financial flows
- An increase in global trade flows
- The emergence of an international business cycle
- An increase in global technology flows
- The emergence of trade blocs and agreements
- The emergence of international organisations designed to oversee the stability and progress of the global economy.
- The increasing impact of transnational corporations on global trade and investment
- The increasing adoption of pro-market economic policies by countries throughout the world

(b) The World Bank assists poorer nations with economic development through providing low-cost loans and development assistance. The International Monetary Fund oversees global financial stability through assisting nations experiencing balance of payments crises.

(c) Increasing trade flows has created an international business cycle, as a downturn in one economy will spread as it demands fewer imports from other countries. The emergence of technology enables investors to react quickly to economic developments, allowing financial crises to spread rapidly. Transnational corporations seek similar policy settings wherever they operate, leading to a convergence of taxation and labour market policies. Economies will also maintain similar interest rate levels to avoid capital flight.

Question 23

(a) The exchange rate refers to the value of one country's currency in terms of another country's currency.

(b) An appreciation.

(c) An answer to this question may include any two of the following:

- The level of imports that Australians purchase influences supply of the Australian dollar, as Australians sell their Australian dollars and purchase foreign currencies to pay for exports.
- Australians seeking to invest overseas must purchase overseas currency to do so. As a result, supply of Australian dollars will increase when Australian investment overseas increases.
- Speculators' expectations influence supply of the AUD. When a depreciation is forecast, speculators will attempt to profit by selling their Australian dollars before the currency's value falls, increasing supply.

(d) An answer to this question may include any two of the following:

- An appreciation will make imports relatively cheaper for Australians, increasing the quantity of imports purchased and worsening the balance on goods and services component of the current account deficit.
- An appreciation will decrease the international competitiveness of Australia's exports, leading to a decrease in export revenue and a deterioration in the balance on goods and services component of the current account deficit.
- An appreciation will lessen the value of Australia's foreign debt, as most Australian debt is denominated in foreign currencies. This will improve the net incomes account of the current account deficit as debt servicing payments decrease.
- An appreciation will make it more expensive for foreign investors to invest in Australia, leading to a decline in investment.
- An appreciation will lessen inflationary pressures within the economy because lower-price imports will reduce imported inflation.

Question 24

(a) Australia increasingly exports to East Asian markets, such as Japan and the ASEAN nations, rather than to Europe. In addition, Australia sources an increasing proportion of its exports from China and ASEAN nations at the expense of the United States.

(b) An answer to this question may include any two of the following:

- A nation may introduce protectionist policies to shield its infant industries from competition from large foreign firms, until they grow to a point where they can benefit from economies of scale.
- A nation may introduce protectionist policies to guard against dumping, where foreign firms sell surplus goods on the domestic market at a lower price than their home market to establish market share.
- A nation may introduce protectionist policies to maintain domestic employment levels, through ensuring domestic firms' profitability by shielding them from competition.
- A nation may introduce protectionist policies to ensure that it maintains domestic production of goods and services essential to the national interest, such as food and defence equipment.

(c) Global protectionist policies distort Australia's trade flows. For instance, the European Union's subsidies to European farmers are not matched in Australia, meaning that European producers can afford to sell their products at price unprofitable for their Australian competitors. The EU's policy encouraged Australia to seek out new and profitable markets in Asia, which now account for a greater proportion of trade. Nevertheless, global protectionist policies reduce the size of Australia's export market, inhibiting the development of economies of scale.