

Guinea Pig
F
(A very good
E paper)

2

For Supervisor's use only

Level 2 Economics, 2009

90796 Describe economic growth and its causes and effects using economic models

Credits: Four

2.00 pm Tuesday 24 November 2009

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

Answer ALL the questions in this booklet.

If you need more space for any answer, use the page(s) provided at the back of this booklet and clearly number the question.

Check that this booklet has pages 2–8 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.

For Assessor's use only		Achievement Criteria	
Achievement		Achievement with Merit	Achievement with Excellence
Describe economic growth and its causes and effects using economic models.	<input checked="" type="checkbox"/>	Explain economic growth and its causes and effects using economic models	<input checked="" type="checkbox"/>
			Fully explain economic growth and its causes and effects using economic models. <input checked="" type="checkbox"/>
		Overall Level of Performance	<input style="width: 40px; height: 20px;" type="text" value="E"/>

4 "A" grades
6 "M" grades
2 "E" grades

You are advised to spend 40 minutes answering the questions in this booklet.

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QUESTION ONE

Economic growth can be measured by an increase in productive capacity and by an increase in real GDP.

(a) State ONE **other** measure of economic growth.

Increase in Net Social Welfare

A

(b) Explain ONE **advantage** of the measure you stated in (a).

Net social welfare is not just measured by economic factors but also non-economic factors such as improvements in healthcare, increases in the birthrate, infant mortality rate etc. These noneconomic factors can tell more than changes in the economic situation but also changes to quality of life and as a result tell us whether peoples quality of life has improved.

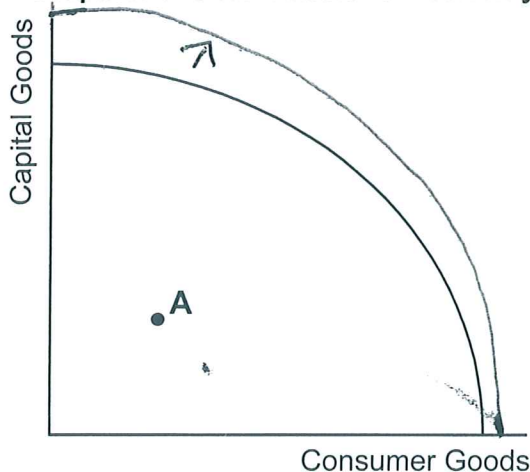
M

Explains using non-economic factors can be included to determine quality of life.

(c) (i) Show how the production possibility curve in Graph 1 should be changed to illustrate an increase in **productive capacity**.

Note: A represents the current level of output.

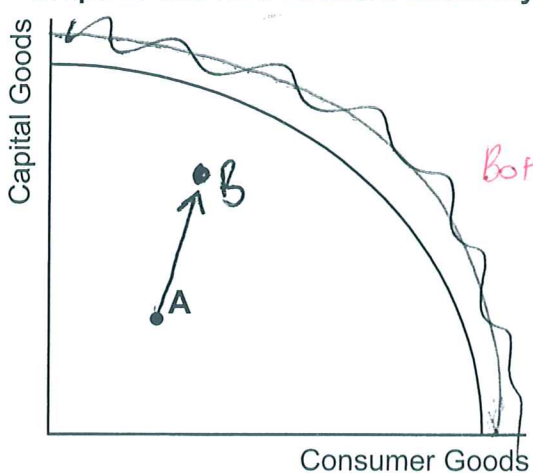
Graph 1: The New Zealand Economy



(ii) Show on Graph 2 how the current level of output should be shifted to illustrate an increase in **real GDP**.

Note: A represents the current level of output.

Graph 2: The New Zealand Economy



Both correct

A

- (d) **Fully explain** why **real GDP** is a better measure of economic growth than **nominal GDP**.
In your explanation, you should:

- define BOTH terms
- giving detailed reasons why the statement above is correct.

Nominal GDP is the value of all the goods and services produced in a country measured in the current value of the currency while Real GDP has been adjusted to take out inflation i.e. has been deflated to a base. Real GDP is a much better measure of growth because of its adjustments. This is because it ~~makes it~~ gives a true representation of whether or not the economy has grown and by how much as price rises have been factored out. As price levels are at the same level for all figures of Real GDP, ~~so they~~ can easily be compared as ~~they will it will be clear~~ when comparing countries which has the higher production, not which has the highest prices. It can also be used to compare from year to year as price levels are constant so a change figure can accurately be calculated which shows growth increases in real incomes and output or GDP rather than increases in inflation.

Has three valid points and one includes reference to real output.

E

QUESTION TWO

Assessor's
use only

Economic growth can be caused by changes in investment, technology, or resource use and by forgoing present consumption.

- (a) Describe what is meant by the term **investment**.

Investment is when firms spend income to ^{increase} ~~purchase~~ capital in order to increase productive capacity. /

A

- (b) Explain ONE possible **negative outcome** for the **environment** if **more resources** are used to achieve economic growth.

A negative outcome would be increased pollution. If more resources are used to achieve growth using the same technology or processes, the result ~~may~~ ^{will} be increases in the amount of waste produced on a straightline basis. An increased waste must be disposed of somehow and will most likely end up in landfills or ~~trashed~~ rivers which will cause pollution. /

M

Has one negative outcome and has explained how this is caused.

- (c) Explain how **improved technology** can result in economic growth.

Improved Technology can result in economic growth as it ^{can} increase efficiency and productivity with the same resources. A newer more efficient machine or other technology ^{could} ~~not~~ use the same resources as older tech, but will produce more due to the increases in productivity. As more can be produced there is an increase in productive capacity, which when shown on a Production Possibility Frontier model shows economic growth. /

M

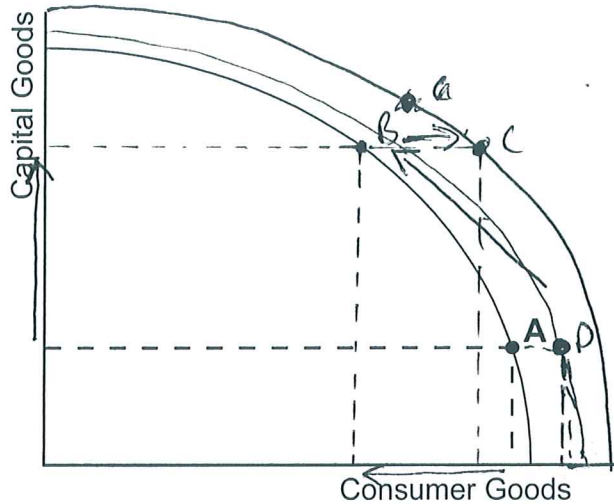
Has explained that an increase in technology will increase productivity and therefore production.

- (d) Fully explain how forgoing present consumption and increasing investment can result in future economic growth.

In your explanation, you should:

- make the appropriate changes to the production possibility curve on Graph 3 below to illustrate your answer
- give a detailed reason why future economic growth can be achieved.

Graph 3: The New Zealand Economy



Graph is correct.

(Only 1 shift of PPC is necessary)

By forgoing ~~current~~ present consumption, consumers are demanding fewer consumer goods. As a result of the ensuing oversupply, firms will receive market signals that it would be more profitable to produce capital goods. As a result firms will switch resources to producing capital goods, this will as shown on graph 3. Resources also previously allocated to the production of consumer goods can also be invested. This is when firms spend income to ~~purchase~~ ^{improve} ~~capital~~ ^{resources} either by purchasing ^{additional} new capital, training up labour or buying more land to build new factories. As more capital goods are now being produced, firms will be purchasing more capital goods which is investment. As firms will have invested in more capital goods which have been produced rather than consumer goods, their productive capacity will increase as more goods and services can be produced. This will allow B to move out to C as ~~productive~~ ^{productive} capacity has shifted outwards where as when if present consumption remained at A, future economic growth may have only moved out to D.

This answer is more detailed than required for an "E" grade at this level

Has covered all points + graph is correct.

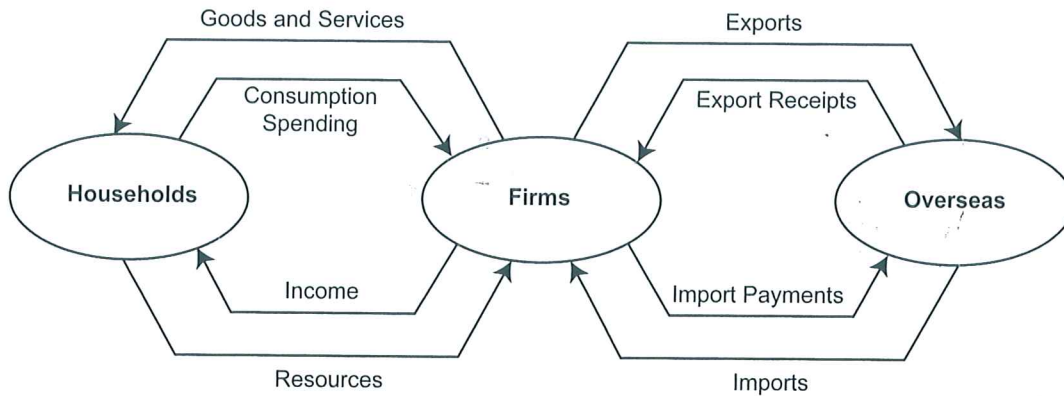
QUESTION THREE

Assessor's
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"The estimated benefit to New Zealand of a free trade agreement [with China] is a growth in exports ... of between \$225 million and \$350 million a year."

Source: <http://www.infonews.co.nz/news.cfm?l=1&t=141&id=28489>

Circular Flow Model



- (a) The circular flow model above does not include the Government Sector. Name both the **injection flow** and **withdrawal flow** associated with the Government Sector:

- (i) **injection flow** Government Spending
- (ii) **withdrawal flow** Taxation

Both correct

- (b) Explain how the withdrawal flow you stated in (a) (ii) would be affected by the **growth in exports** resulting from a free trade agreement.

As exports grow due to the FTA with China, Firms receive more income due to the more open export market there as they can sell their goods freely there without tariff or quotas making the cost of selling goods be cheaper. As firms incomes increase, the dollar amount which the government takes away in taxation also increases due to direct taxes on firms and as well as income taxes from the firms employees.

Has correctly explained how an increase in exports will increase income and income tax.

- (c) Identify and explain the **money flow**, shown in the diagram on page 6, that would be **directly** affected by the **free trade agreement** with China.

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use only

The money flow directly affected is export receipts. As Chinese importers purchase more goods from NZ exporters (Firms), they will have to pay for them. This comes in the form of export receipts which increases due to the \$225-\$300 million a year which is injected to the economy.

M
Has explained
X increases
+ linked to
exports.

*due to the cost being cheaper due to protectionism being dropped,

- (d) **Fully explain** how a free trade agreement with China could result in **economic growth** for New Zealand.

With a FTA with China, all protectionism between NZ and China is dropped. This makes the cost of trade between the nations more affordable making it more attractive. The FTA firstly causes an increase in exports. As New Zealand's market is free to access for China, Chinese consumers will demand more New Zealand goods as they will be relatively cheaper and affordable than before. As a result, NZ export receipts increase. ^{Hasn't made the link to production.} This is an injection into the circular flow and will therefore generate more real income which is economic growth. There will also be an associated increase in import payments as imports from China will be cheaper, which will mean a withdrawal from the circular flow but most likely less than the increase in export receipts as there is not much more for NZ to import from China than before. Increased export receipts boost the incomes of New Zealand producers. In turn this will lead to increased investment spending in order to increase productive capacity to supply the Chinese market. An increase in productive capacity is economic growth. This investment spending will circulate around the economy and will end up being paid out to employees as wages rise as the economy becomes richer leading to an increase in consumption spending. As explained in (b) Government spending also rises. incomes rises so the spending will ~~conversely~~ ^{conversely} rise. As consumption, investment and government spendings as well as net exports have all risen and are part of the formula for Real GDP, Real GDP rises which is economic growth.

(1 point)

M

(2nd point)