

UNIT 3B ECO Sample Extended Answer Questions

1. During 2009 the RBA has been under pressure from many groups in regard to its cash rate.

(i) Explain the differing groups reasons for the RBA to increase or leave unchanged its cash rate.

(10 marks)

(ii) Explain the possible effects on Australia's balance of payments of an increase in interest rates.

(10 marks)

Description	Marks
• Define cash rate; current rate	1
• Those wanting rates left unchanged include farmers; homeowners and renters; households(want to maintain discretionary spending income); exporters/import-competing businesses(concerned of flow-on effects if AUD rises); politicians	1-6
• Those wanting increased rates include retirees; businesses owing payments o/seas(benefit from flow-on effect of AUD rise).	1-4
Total	10
• Increased foreign investment (FI) leads to increased capital inflow into the Financial Account which will lead to future increased interest payments and thus worsening net income and CAD.	1-4
• Increased FI leads to ↑AUD which is likely to lead to a worsening net goods and services and CAD. Net income likely to improve due to lower interest payments. AUD model.	1-5
• Less household spending on imports, due to increased mortgage payments.	1
• Increase in both KAS and CAD.	1
Total	10
Total	20

2. Explain and illustrate, using three recent examples, how MER can lead to the simultaneous achievement of economic growth, price stability and full employment.

(20 marks)

Description	Marks
• Define MER. Define the gov't objectives and state 'target' rates.	1-3
• AD/AS model of successful MER.	1-2
• Areas include tariffs, tax, labour, deregulation, education/training, transport, communication. Must explain in relation to achieving the gov't objective(s).	3x5=15
Total	20