2002 HIGHER SCHOOL CERTIFICATE EXAMINATION

Economics

Section II (continued)

Marks

Question 24 (10 marks)

The following information refers to inflation.

> The Consumer Price Index (CPI) increased by 0.9 per cent in the December quarter, after rising by 0.3% in the September quarter, to be 3.1% higher over 2001. . . .
>
> However, the outlook for the medium term determinants of inflation has not changed substantially in the light of recent data. Wage and labour cost growth remain contained and are likely to continue to be so given the prevailing weakness in the labour market. The stability of the exchange rate over the past year, combined with downward pressure on world prices from the subdued global economy, suggests that there will be little inflationary pressure from import prices in the medium term.
>
> Adapted from Reserve Bank, *Statement on Monetary Policy*, February 2002

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(a) Define the term *inflation*. **2**

Inflation reflects the changes in the buying power of the currenly. If inflation is 10%, then ~~you~~ ~~it~~ means for the same amount of money you can buy 10% less then before the inflation.

(b) Outline TWO causes of inflation. **2**

The job wage spiral, as people start to get more higher paid ~~[illegible]~~ wage or salaries this trigers others to increase there income which causes inflation.

The RBA is the other cause of inflation it controls the inflation rate using fiscal policy.

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Marks

Question 24 (continued)

(c) Outline TWO negative effects of inflation on an economy. 2

Inflation makes things hard to value such as property also causes economic probles since the prices of foods will increase as inflation does and that can be expensive in business always having to change signs of prices.

(d) Explain TWO government economic policies that could reduce the rate of inflation in an economy. 4

Fiscal and monetary policies are used by the RBA to controll the inflation rate and keep it between 2-3%. Monetary policy is when money supply is controlled, when the cash rate is effected inflation can go up or down depending what is done. Fiscal inflation policies is when the government uses interest rate to controll inflation rates, if people are saving due to high interest rate the inflation goes down and is people are borrowing money then inflation is going up.

End of Question 24