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SUPERVISOR'S USE ONLY

91222



Level 2 Economics, 2012

91222 Analyse inflation using economic concepts and models

2.00 pm Monday 12 November 2012 Credits: Four

Achievement	Achievement with Merit	Achievement with Excellence
Analyse inflation using economic concepts and models.	Analyse inflation in depth using economic concepts and models.	Analyse inflation comprehensively using economic concepts and models.

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

You should attempt ALL the questions in this booklet.

If you need more room for any answer, use the extra space provided at the back of this booklet.

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.

TOTAL

You are advised to spend one hour answering the questions in this booklet.

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QUESTION ONE: THE AGGREGATE DEMAND AND SUPPLY MODEL

Complete questions (a)–(d) to comprehensively analyse the effects of an increase in business insurance costs and beef export earnings on inflation.

(a) Define inflation.

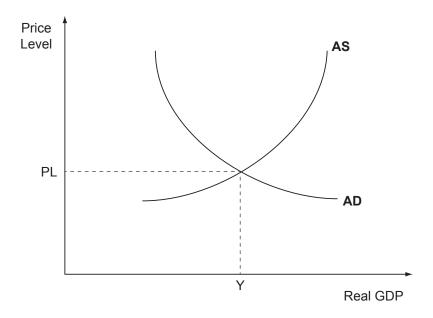
(c)

As a result of the Christchurch earthquakes thousands of New Zealand businesses are facing higher insurance costs.

Source (adapted): http://www.stuff.co.nz/the-press/business/6219582/Casino-quake-excess-jumps-to-5m

(b) On Graph One, show how an increase in insurance costs for New Zealand businesses could affect inflation. Fully label the change.

Graph One: AS/AD Model of the New Zealand Economy



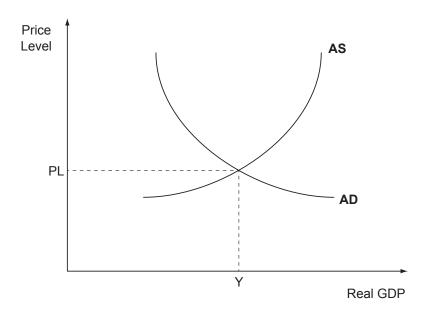
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Export beef earnings jumped 13% between 2010 and 2011.

Source (adapted): The Dominion Post, 14 January 2012

- (d) Compare and contrast the effects on inflation of an increase in insurance costs for New Zealand businesses with an increase in beef export earnings. In your answer, you should:
 - explain in detail how an increase in beef export earnings could affect inflation
 - explain in detail why an increase in insurance costs for New Zealand businesses may have a greater effect on inflation than an increase in beef export earnings
 - show changes from BOTH events on Graph Two (below)
 - refer to the changes you make on Graph Two to support your explanation.

Graph Two: AS/AD Model of the New Zealand Economy



QUESTION TWO: THE QUANTITY THEORY OF MONEY

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Complete questions (a)–(c) to comprehensively analyse the effect of changes in the money supply and consumer confidence on inflation.

(a)	Define each of the four variables used in the Quantity Theory of Money equation.						
	M:						
	V:						
	P:						
	Q:						
	M3 measure of the money supply increased by \$12 602 million between April 2011 and						
Ар	il 2012. Source (adapted): http://www.rbnz.govt.nz/statistics/monfin/c3/download.html						
(b)	Using the Quantity Theory of Money, explain in detail how an increase in the money supply could affect the price level, assuming other variables remain constant.						

The Westpac McDermott Miller consumer confidence index declined by 11 points in the December 2011 quarter.

Source (adapted): The Dominion Post, 20 December 2011

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- (c) Compare and contrast the effect on the price level of:
 - (i) an increase in the money supply while other variables remain constant
 - (ii) an increase in the money supply accompanied by a reduction in consumer confidence.

In your answer, you should:

- refer to the Quantity Theory of Money
- explain in detail how a reduction in consumer confidence will affect the velocity of circulation

explain in detail which of the two changes out of (i) and (ii) above will have a geffect on the price level.		

QUESTION THREE: EFFECTS OF INFLATION ON HOUSEHOLDS AND BUSINESSES

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Complete questions (a)–(c) to comprehensively analyse the effects of a reduction in inflation on households and businesses.

Source (adapted): The Dominion Post, 16 January 2012				
Explain in detail why cheaper prices for some food items, consumer durables, and internet access could cause disinflation but may not lead to deflation .				
Explain in detail how households AND businesses could benefit from cheaper food, consumer durables, and internet access. In your answer, you should explain how the benefit one of these two groups may have flow-on effects for the other group.				
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(i)	pare and contrast the different effects of a reduction in inflation between: a large business that employs 60 people and sells its goods mainly to overseas markets AND a small business that specialises in importing goods and selling them to the local market	
(ii)	a householder who owns a house with a fixed-interest-rate mortgage AND a householder who has a fixed income and \$60 000 savings in the bank.	

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QUESTION NUMBER	I	Extra space if required. Write the question number(s) if applicable.	
NUMBER			