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NEW ZEALAND QUALIFICATIONS AUTHORITY
MANA TOHU MĀTAURANGA O AOTEAROA

Scholarship 2014 Economics

2.00 pm Wednesday 26 November 2014

RESOURCE BOOKLET

Refer to this booklet to answer the questions for Scholarship Economics.

Check that this booklet has pages 2–12 in the correct order and that none of these pages is blank.

YOU MAY KEEP THIS BOOKLET AT THE END OF THE EXAMINATION.

Use **Resources A to H** to answer **Question One**.

Resource A: Defining a bubble

An asset bubble is characterised by a rapid, often accelerating increase in the price of an asset, followed at some point by a precipitous decline.

...

It is also hard to distinguish a bubble from ordinary price fluctuations associated with fundamental market or economic factors.

[For copyright reasons, this resource cannot be reproduced here. See below.]

Source (extract): <https://www.vanguardinvestments.de/content/documents/Articles/Insights/market-bubbles-investor-psychology.pdf>

Resource B: New Zealand house prices

[For copyright reasons, these resources cannot be reproduced here. See below]

Current evidence of a house price bubble could include:

- panic buying by first home buyers for fear of missing out
- ...
- heavy buying from foreigners.

Source (adapted): <http://www.macrobusiness.com.au/2013/06/auckland-anatomy-of-a-housing-bubble/>

Resource C: The myth of the housing bubble

We are hearing repeated cries that the New Zealand housing market is in a bubble that's about to burst, that houses are grossly unaffordable in Auckland, that land values are escalating out of control, and that costs of construction are unbelievably high.

...

At the same time, the supply of new housing has also slowed. The current undersupply will result in further pricing pressure while we build and subdivide to bridge the supply gap.

[For copyright reasons, this resource cannot be reproduced here. See below.]

Source (adapted): Eugene Sparrow, *WEEKEND REVIEW, National Business Review*: <http://www.nbr.co.nz/article/budget-preview-myth-housing-bubble-weekend-review-wb-139409>

Resource D: Auckland housing – key facts

The table below provides a snapshot of the Auckland housing market, based on publicly available information.

| | |
|-----------|-----------------------------------------------------------------------------|
| Issue | For Auckland. |
| Ownership | Home ownership rate in Auckland has declined from 64% in 2001 to 58% today. |

[For copyright reasons, this resource cannot be reproduced here. See below.]

Source (adapted) The Ministry of Business, Innovation and Employment: <http://www.mbie.govt.nz/what-we-do/housing/housing-key-facts>

Resource E: Shortage in supply

... in a market constrained by supply, prices will rise.

- Auckland house price gains have not been driven by either speculation or surging migration but instead by the realisation that there is a supply shortage at current prices.
- ...
- Net migration inflows into NZ are now rising sharply, thanks to a great degree of a turn-around in the migration cycle with Australia.

[For copyright reasons, this resource cannot be reproduced here. See below.]

Source (adapted): Tony Alexander, *BNZ Weekly Overview*, 20 June 2013: <http://tonyalexander.co.nz/regular-publications/bnz-weekly-overview/housing-market/a-summary-of-housing/#more-1796>

Resource F: House affordability? Blame wages? Cost of home dream in Auckland – 19 incomes

Property in some of the world's biggest cities costs a lot more than in our biggest city, but Auckland wages make it much harder to get on the property ladder. It would take 19 median incomes in Auckland to buy a home for the city's median house price. In London, it takes 11 annual average incomes to reach the average house price.

...

Wages and salaries in New Zealand have fallen further behind earnings in Australia, Canada, and even the UK.

[For copyright reasons, this resource cannot be reproduced here. See below.]

Source (adapted): *New Zealand Herald*,
15 February 2013: http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=10865494;
10 December 2013: http://www.nzherald.co.nz/nz/news/article.cfm?c_id=1&objectid=11169717

Resource G: Reserve Bank exempts lending for new construction

The Government has introduced several measures in a bid to slow house-price increases, including the Reserve Bank's loan-to-value rules which restrict the total of a bank's lending to borrowers with less than a 20 per cent deposit to 10 per cent of their business.

...

By doing this, LVR restrictions should not prevent the building of new residential houses and will help to support the supply of new housing, thereby reducing some of the pressure arising from excess demand in the New Zealand housing market.

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Source (adapted): New Zealand Herald: http://www.nzherald.co.nz/nz/news/article.cfm?c_id=1&objectid=11169717;
<http://www.rbnz.govt.nz/news/2013/558565.html>

Resource H: What else might policymakers try to rein in galloping house price inflation?

Supply, supply, supply:

Measures to increase the availability of land and lower the cost of sections are key. Local and central government are working on it (Auckland Council and central government have signed a housing accord), but the supply-side response is liable to be slow.

...

Interest rates:

Mortgage rates were never going to stay at 50-year lows forever. Housing affordability is about to get a lot worse as the Reserve Bank moves to raise interest rates, though rising interest rates will also limit demand somewhat.

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Source (adapted): *New Zealand Herald* 10 December 2013 http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11169681

Use **Resources I to N** to answer **Question Two**.

Resource I: Hamilton leads the way with ‘living wage’; others may follow

Hamilton has become the first city council in New Zealand to approve paying all staff a ‘living wage’. Campaigners say the living wage, calculated at \$18.40 per hour, is the rate needed for workers to fully take part in society.

...

“It’s only fair that these people are able to enjoy a decent standard of living,” the mayor of Auckland said.

[For copyright reasons, this resource cannot be reproduced here. See below.]

Sources (adapted): http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=10885364;
http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11152641

Resource J: New Zealand living wage \$18.40 an hour

A landmark report released today identifies \$18.40 an hour as the New Zealand living wage.

...

The report defines the living wage as “the income necessary to provide not only the basic necessities, but to enable workers to participate in society”.

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Source (adapted): <http://www.scoop.co.nz/stories/PO1302/S00119/new-zealand-living-wage-1840-an-hour.htm>

Resource K: The 'living wage' and what it really means

When a "living wage" was proposed, it became clear many people did not understand what the "living wage" might mean. The proposal of \$18.40 gross per hour applied to an average family of two adults and two children, with one adult working full-time and one working half-time.

...

New Zealand's minimum wage is set at 65 per cent of the median wage and could be higher, though if it were, some, including the lesser skilled and those seeking their first job, could find it harder to get a job.

[For copyright reasons, this resource cannot be reproduced here. See below.]

By Kim Campbell, chief executive of the Employers and Manufacturers Association.

Source (adapted): *New Zealand Herald*, 8 October 2013, http://www.nzherald.co.nz/nz/news/article.cfm?c_id=1&objectid=11136325

Resource L: Workers' share of national income

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The “labour share” of national income has been falling across much of the world since the 1980s (see chart).

The OECD reckons that labour captured just 62 per cent of all income in the 2000s, down from over 66 per cent in the early 1990s.

...

Changes in employment laws have also had an effect. In the late 1970s, workers enjoyed high labour shares thanks to stiff labour-market regulation. In the early 1980s, labour- and product-market liberalisation (ie removal of regulations and reductions in union power) saw labour shares tumble.

Source (text, adapted): *The Economist*, 2 November 2013, <http://www.economist.com/news/finance-and-economics/21588900-all-around-world-labour-losing-out-capital-labour-pains>

Source (graph): OECD

Resource M: Pay rates the result of power imbalances

Over the past few decades, there has been a conscious effort to make our labour markets more flexible. This flexibility has tended to apply most effectively to those at the bottom end of the market.

...

It also assumes the task being performed by a worker can easily be performed by machine. However, employers of many minimum wage workers, such as supermarkets and rest homes, are usually not operating in perfectly competitive markets.

[For copyright reasons, this resource cannot be reproduced here. See below.]

Source (adapted): *New Zealand Herald*, 15 November 2013,
http://www.nzherald.co.nz/nz/news/article.cfm?c_id=1&objectid=11157292

Resource N: Need for a realistic target

It would be better to focus on a realistic minimum individual hourly rate than a sometimes skewed Living Wage. There has been some suggestion that the living wage concept is poorly targeted. The problem arises because two issues are merged: earning a wage that is enough to live on for the individual, and having enough money to support a family.

...

It would be better to focus on a realistic minimum individual hourly rate and ensure that Working for Families provides adequate extra income support when there are children.

[For copyright reasons, this resource cannot be reproduced here. See below.]

Source: Extracts from *New Zealand Herald*, 15 November 2013,
http://www.nzherald.co.nz/nz/news/article.cfm?c_id=1&objectid=11157291

Use **Resources O to U** to answer **Question Three**.

Resource O: New Zealand's monetary policy objective

The Reserve Bank of New Zealand Act 1989 stipulates that the Bank is to formulate and implement monetary policy directed to the economic objective of achieving and maintaining stability in the general level of prices. The Act requires that there be a Policy Targets Agreement (PTA) between the Minister of Finance and the Governor of the Reserve Bank. For the purposes of the current PTA, the policy target is to keep future CPI inflation outcomes in the range of 1 per cent to 3 per cent on average over the medium term, with a focus on keeping future average inflation near the 2 per cent target midpoint.

Source (adapted): <http://www.treasury.govt.nz/economy/overview/2012/28.htm>

Resource P: Exporters need monetary policy changes

Changes to monetary policy are needed to put an end to wealth transfers from the tradeable sector, says the New Zealand Manufacturers and Exporters Association (NZMEA): "Other countries with exchange rate stability as the central focus of monetary policy have achieved significantly higher long-run economic growth; it is time New Zealand followed their lead."

...

"Inflation inside the target band delivered at the expense of the export sector will not deliver a sustainable economy for New Zealand."

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Source (adapted): http://www.nzmea.org.nz/documents/681-exporters_need_monetary_policy.pdf
and http://www.realeconomy.co.nz/292-rbnz_policy_targets_agreement_.aspx

Resource Q: Policy not in line with competitors – economist

BERL (Business and Economic Research Ltd) chief economist Ganesh Nana says New Zealand's monetary policy is not in line with countries that New Zealand competes with.

He backs calls for a more interventionist approach to monetary policy as a way to help struggling manufacturers.

Source (adapted): <http://www.radionz.co.nz/news/political/137895/english-rejects-monetary-policy-changes-to-help-manufacturing>

Resource R: Reserve Bank needs expanded options

“The central bank should be required to consider other factors when making a call to lift interest rates – such as unemployment, economic growth, and the currency.”

Source (adapted): Colin Espiner, *Sunday Star-Times*, 16 March 2014, page A15.

Resource S: New Zealand exchange rate

[For copyright reasons, this resource cannot be reproduced here. See below]

Source: www.rmbz.govt.nz

Resource T: Monetary policy objectives in other countries

Australia

The Australian Reserve Bank Board sets interest rates so as to achieve the objectives set out in the (Australian) Reserve Bank Act 1959:

- the stability of the currency of Australia
- the maintenance of full employment in Australia
- the economic prosperity and welfare of the people of Australia.

...

Provisions reflect the broad agreement that:

- the benefits of price stability are substantial. Maintaining stable prices on a sustained basis is a crucial pre-condition for increasing economic welfare and the growth potential of an economy
- the natural role of monetary policy in the economy is to maintain price stability. Monetary policy can affect real activity only in the shorter term. But ultimately, it can only influence the price level in the economy.

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Source (adapted): <http://www.ecb.europa.eu/mopo/intro/objective/html/index.en.html>

Resource U: Macroeconomic objectives

Common macroeconomic objectives for government are:

- full employment
- economic growth
- price stability
- a balanced current account.