

2015 VCE Economics examination report

General comments

Students responded positively to the 2015 Economics examination paper. In general, students handled Section A well and there were a significant number of high-quality responses in Section B. It appeared that students managed their time appropriately in answering Section B. Most students attempted all parts of all questions. Responses were considered and addressed the question.

Many students demonstrated sophisticated knowledge of the current performance and policy settings of the Australian economy. Students who were able to correctly apply economic theory to explain current and recent changes in economic performance and policies generally earned the highest marks.

Students used a number of key economic terms and concepts well. However, students are reminded not to spend too much time defining key concepts and terms at the expense of explicitly and fully answering the specific requirements of the question.

In order to improve, students should:

- develop clearer understandings of the differences between market structures; for example, the difference between monopoly and monopolistic competition. Understanding the difference between these market structures was required to be able to answer Section B, Question 2b.
- explicitly show that they understand the meaning of the key economic goals and their relationships with aggregate demand, aggregate supply and economic policies such as the relationships being assessed in Section B, Question 1a. and 3b.
- be able to clearly distinguish the differences between aggregate demand and aggregate supply; production, productivity and productive capacity
- develop deeper knowledge of the differences between government debt and external debt
- show that they understand sources of market failure and how and why governments may intervene to address these market failures.

Specific information

Note: Student responses reproduced in this report have not been corrected for grammar, spelling or factual information.

This report provides sample answers or an indication of what answers may have included. Unless otherwise stated, these are not intended to be exemplary or complete responses.

The statistics in this report may be subject to rounding resulting in a total more or less than 100 per cent.

Section A – Multiple-choice questions

The table below indicates the percentage of students who chose each option. The correct answer is indicated by shading.

Question	% A	% B	% C	% D
1	93	2	2	3
2	2	3	10	85
3	8	82	5	5
4	12	6	31	51
5	7	69	9	14
6	2	83	12	3
7	3	3	85	9
8	52	4	40	4
9	4	7	79	10
10	24	23	4	49
11	3	4	87	6
12	5	7	82	6
13	91	3	3	3
14	9	69	14	7
15	26	3	62	9

Section B – Written responses

Question 1a.

Marks	0	1	2	3	4	Average
%	9	17	30	29	16	2.3

High-scoring responses covered the following points.

Low inflation

Low inflation is a government economic goal where the Reserve Bank of Australia (RBA) aims to maintain a sustained increase in the general level of prices to be between 2% and 3% on average over the course of the business cycle.

Aggregate demand (AD) is the total amount of spending on goods and services produced in Australia in a given period and aggregate supply (AS) is the total production of goods and services in a given period.

When AD grows faster than AS, the economy may experience shortages and capacity constraints and prices may be bid up in some markets, thus jeopardising the goal of low inflation.

If there is inadequate growth in AD and there is spare capacity in the market (AS is greater than AD), policy-makers may be concerned about excessively low inflation or deflation.

Therefore, balanced and steady growth in AD and AS means that booms and recessions are avoided and that there is stability in Australia's level of economic activity, thus creating the best conditions for achieving the goal of low inflation.

Equity in income distribution

The government's economic objective of equity in income distribution means that it is striving for a fair share of income to be distributed to all members in the economy, so that all members have access to an adequate living standard and absolute poverty is avoided.

Balanced and steady growth in AD and AS implies that there are no domestic or global macroeconomic shocks to stability in Australia's level of economic activity.

In such a climate consumer and business confidence may grow, resulting in macroeconomic expansion with consequential increases in employment opportunities, leading to steady growth in factor incomes and less reliance on welfare by Australian households. This is likely to lead to more equity in income distribution.

Some students had difficulty in addressing all the question requirements. Generally, students wrote better answers when they selected the economic goal of low inflation rather than equity in income distribution. High-scoring students were able to give accurate definitions of the goals and use this to help structure their explanations.

Question 1b.

Marks	0	1	2	Average
%	20	47	32	1.1

High-scoring responses made the following points:

- Aggregate supply (AS) represents the total volume of goods and services that suppliers are willing and able to produce.
- An increase in AS can arise from greater willingness to produce and/or the ability to produce.
- Increased AS can occur as a result of improved perceptions of profitability by the business sector. Therefore, a boost to willingness to produce may occur, which would flow through to an increase in real gross domestic product and the rate of economic growth.
- Increased AS can also arise as a result of improved quantity or quality of resources available to the business sector, with the consequent boost to productive capacity effectively shifting the national Production Possibility Frontier to the right and leading to increased real gross domestic product and the rate of economic growth.

Students were challenged by this question and did not appear to have full understanding of the relationship of how increases in aggregate supply might contribute to an increase in the rate of economic growth. Many low-scoring students assumed that aggregate supply related to production, which is incorrect, and then linked it to aggregate demand.

Question 1c.

Marks	0	1	2	3	4	Average
%	11	11	16	21	40	2.7

This question was generally well handled by students. Most students understood what is meant by a demand-side factor and had good current knowledge about demand-side factors influencing aggregate demand in Australia in 2015. The highest-scoring students were able to select a possible domestic and global demand-side factor and then detail how this factor influenced a component of aggregate demand (AD).

High-scoring students selected a range of factors including the following.

Domestic demand-side factors:

- Lower consumer confidence levels given the state of the economy and employment security issues might have reduced the willingness of households to spend, thereby reducing the consumption component of AD, thus reducing AD.
- Relatively low interest rates – interest rates were lowered in February 2015 and there has been no rise since then, creating an environment that might encourage borrowing and

spending, thus increasing consumption spending (C) and investment expenditure (I), supporting AD.

- Attempts by the Australian Government in 2014 and 2015 to display budgetary restraint, further weakening the component of government spending of AD.

Global demand-side factors:

- The sustained softening of economic growth in China, as evidenced by China's significantly lower gross domestic product and easing of interest rates in China. Consequently, there were lower levels of demand for Australia's commodity exports such as iron ore.
- The depreciation of the Australian dollar (around \$0.68 US currently) has given rise to a much healthier level of net external demand, with fewer leakages and more injections of funds arising from international trade in goods and services. This has helped to moderate the decline in AD.
- A significant deterioration in the terms of trade, largely as a result of the fall in commodity prices. The price received for exports in world markets has fallen and this means that exporters (for example, miners and farmers) receive less revenue from each unit sold. This decrease in real net disposable income (and profitability of producers) may mean that they are less inclined to invest in extra capacity. Therefore, the investment component of AD is likely to fall, resulting in slower growth in AD.

Question 1d.

Marks	0	1	2	3	4	5	6	Average
%	3	6	12	17	24	23	15	3.8

Students were required to choose two policies from the list of three provided in the question. Most students demonstrated a good understanding of the policies and were able to link them to aggregate supply reasonably well. However, students who selected environmental policy found it difficult to successfully explain the link to an increase in aggregate supply.

If students chose to respond using microeconomic reform (MER) policy, they could choose a specific MER from the list in the study design:

- trade liberalisation
- labour market reform
- deregulation of key markets
- National Competition Policy

Most students selected trade liberalisation. The following is a possible response using trade liberalisation.

The Australian Government has continued to undertake trade liberalisation over recent years, whereby barriers to trade such as tariffs (taxes on imports) and subsidies (financial support to Australian producers) are reduced and in some cases removed. This exposes Australian business to greater competition from overseas producers. This immediately imposes a discipline on them to seek the lowest-cost method of production and they are likely to seek productivity gains where they create more outputs from their labour, land and capital inputs. Inefficient industries that are unable to compete may close down and free up resources that can be utilised in industries where Australia has a comparative advantage. The resultant improvements in efficiency and productivity will likely increase the ability and willingness of businesses to supply, thus increasing aggregate supply.

The following is a possible response focused on immigration policies.

Australia continues to implement immigration policies that promote relatively high rates of immigration into Australia. For example, the Skilled Migration Program, where the government has attempted to identify areas of skill shortage in Australia and has actively permitted foreign citizens to enter Australia to fill the labour shortages in certain industries. New migrants add to the pool and skill of available labour, thus increasing the quality and quantity of labour resources. Businesses that wish to expand are more likely to find suitable labour and because there are more workers in the country, there may also be downward pressure on wages, so the costs of production may be lower. All of these factors may help to boost productivity and enhance the ability and/or willingness of firms to produce, thus increasing aggregate supply in Australia.

The following is a possible response focused on environmental policy to increase aggregate supply.

Environmental policies are measures taken by the Australian Government to progressively remove impediments to the maintenance of a clean, natural environment, locally, nationally and globally. Recent environmental policies in Australia have been focused upon taxing the largest users/consumers of carbon/fossil fuels in the belief that such consumption is contributing directly to the phenomenon of global warming and associated climate change. Other measures have also included subsidies paid to users of renewable energy sources (for example, solar panels for residences and businesses, LPG fuel systems in cars), in the hope that over time the economy may become less dependent upon environmentally damaging non-renewable sources of energy. The links to AS of such measures are complex as in the short-term it can be argued that production processes become more expensive and less profitable as the business sector attempts to adjust to the more environmentally sustainable techniques; AS may be damaged in the short-term by imposed environmental policy. Such a view was the foundation of the scrapping of the carbon tax by the current Australian Government to be replaced by the Direct Action Plan, the centrepiece of which is the creation of \$2.5 billion over four years to fund business-initiated programs that will be aimed at reducing their greenhouse gas emissions. Such initiatives have been criticised as too arbitrary/based upon voluntary action and unlikely to attract the interest of the largest corporate polluters. Proponents of climate change theory point to adverse variation in weather patterns and rising sea levels having the capacity to destroy productive capacity. So in the medium- to longer-term, it is argued that avoidance of global warming and climate change is essential to maintain a stable, natural environment for productive purposes. This creates the best conditions to enable businesses to be able and willing to produce, thus increasing aggregate supply.

Question 1e.

Marks	0	1	2	3	4	Average
%	17	12	20	29	22	2.3

This question required students to explain one feature of the relationship that existed between monetary and budgetary policy in 2015 and how this relationship may have influenced aggregate demand and living standards.

Students' ability to explain a relationship between the policies and make the link to aggregate demand was impressive, but many did not score full marks as they failed to explain how the relationship may have influenced living standards.

Students were rewarded if they made the following points:

- The Australian Government needs to implement a successful mix of budgetary policy (BP) and monetary policy (MP) in order to manage strong and sustainable growth of aggregate demand (AD) in the Australian economy.
- Without steady growth in AD, Australia could experience the symptoms of macroeconomic contraction such as increased unemployment as well as the symptoms of excessive macroeconomic expansion such as increased domestic inflation, and damage to the external trading position and environment. Steady growth in AD should lead to a steady increase in real GDP per capita – the measure of change in average material living standards.
- In 2015, Australia has experienced a historically low cash rate of interest set by the Reserve Bank of Australia (RBA), as AD was seen to be quite soft. Relatively soft AD has meant that inflation has been low (in the RBA target zone or lower) but is threatening to deliver deficient economic growth and rising unemployment. With lower interest rates in general, the aim of the easing/accommodative MP stance, through the various transmission mechanisms, has been to encourage borrowing and spending as opposed to saving, thus boosting AD, economic growth and employment, which are all seen as important in raising living standards.
- The Australian Government has been firm in its position on the need to reduce the size of the budget deficit and achieve fiscal consolidation in concern for the rapidly escalating public sector debt. This suggests that the budgetary stance in the current climate is contractionary, where options such as reducing government outlays and/or increasing taxes will see reductions in consumption, investment and government spending, thus reducing AD. This suggests a position of conflict with the MP stance. While in the short-term, such measures of fiscal consolidation can be undoing the benefits of the accommodative MP stance upon improved material living standards, the approach might be argued as essential to medium- to longer-term management of AD and living standards.
- There is a logical relationship between an accommodative MP stance and a budget deficit reduction strategy, so as to avoid the macroeconomic policy conflict of 'crowding out', whereby Australian Government demand for funds in finance markets, to fund large and increasing budget deficits, puts upward competitive pressure on domestic interest rates.

Question 2a.

Marks	0	1	2	3	4	Average
%	3	5	14	30	47	3.1

Most students responded to this question well and were able to explain the sorts of differences between a perfectly competitive market structure and an oligopolistic market structure.

The highest-scoring responses explained the following differences.

A perfectly competitive market structure is one:

- that has many buyers and sellers, all of whom possess perfect knowledge of market conditions
- where there are no barriers to enter or exit the market
- where price is the only distinguishing factor between sellers; products are homogeneous.

An oligopolistic market structure is one where:

- there are a small number of dominant suppliers controlling a high percentage of the market share
- each supplier attempts to create real or perceived product differentiation
- the power of advertising and brand loyalty can act as an entry barrier to prospective new entrants to the market.

Question 2b.

Marks	0	1	2	3	4	Average
%	6	5	11	32	46	3.1

While many students scored well in answering this question, others did not seem to understand what a monopoly was or how it operated. Many of these students seemed to confuse monopoly market structure with monopolistic competition.

A possible answer could have been:

A monopoly market structure implies that there is only one supplier of a good or service in the marketplace (that is, only one seller and there aren't any substitutes). This supplier has a high degree of market power to act in their own interest and is able to set the price and/or quantity of the product independent of market conditions. The monopolist is a price maker rather than price taker.

Depending upon the nature of the product, a monopoly situation could have disadvantageous impacts upon living standards of consumers as the market price may be higher than it would otherwise be if the single supplier had to compete with other suppliers for market share.

Paying higher prices to gain access to the product may erode a disproportionately large percentage of the household spending budget and necessitate forgoing other spending and consumption. In addition, the lack of choice for consumers may decrease their satisfaction and their non-material living standards may decline.

Question 2c.

Marks	0	1	2	3	4	Average
%	17	12	23	29	19	2.2

This question was challenging for a large number of students. While most demonstrated some understanding of a market failure and could say something about how the government might address the market failure, it was often difficult for students to make a link to how this might improve efficiency in resource allocation.

The following is an example of a possible response.

Market failure occurs when inefficiencies in resource allocation arise from the operation of relatively free market forces – that is, the free market creates outcomes that do not maximise satisfaction for all societal members with an over allocation or under allocation of resources occurring.

An example of market failure is the existence of externalities. Externalities exist where a cost (negative) is imposed on or a benefit (positive) accrues to a third party not involved in the production or consumption of a product. Negative externalities, for example, will cause an over allocation of resources to the production of the good because the producer or consumer will not take into account the external costs. For example, when cigarettes are consumed, those who smoke passively may suffer resultant illness and increased medical costs. Therefore, from society's point of view, wellbeing is not maximised and there is market failure with too many cigarettes produced and consumed. This negative externality may mean damage to the quality of life of a non-smoker if placed in a position of being subjected to passive smoking caused by a cigarette smoker in a public place (for example, a cinema). The government acknowledges that while cigarette smoking is not unlawful, smoking in a public place should be controlled, hence the government imposes strict laws banning such behaviour, with heavy fines to be applied to those who are caught breaching this law. These measures are aimed at protecting the rights of the non-smoker from their quality of life/satisfaction being harmed by the decision-making of another.

Question 2di.

Marks	0	1	2	Average
%	9	49	42	1.4

Some students struggled to explain the price change when needing to consider changes in both the demand and supply graphs. Students need to regularly practise the key skills related to constructing graphs to represent economic data, and interpret and analyse graphical data so that they have more confidence when faced with questions such as these.

The following is an example of a possible response.

The equilibrium price has fallen from \$US100 per barrel at E1 to \$US50 per barrel at E2. The price fall has been driven by an increase in supply (for example, discoveries of alternative sources of oil) and a decrease in demand for oil (perhaps due to lower rates of world economic growth). With falling demand and rising supply the \$US100 per barrel created a surplus in the market, so prices had to be reduced by suppliers to clear the market.

Question 2dii.

Marks	0	1	2	Average
%	25	52	24	1

Many students were unable to score full marks for this question. While most students seemed to understand elasticity of demand and petrol being inelastic, few then said how this might impact on household budgets.

The following is an example of a possible response.

Price elasticity of demand (PED) measures the percentage change in quantity demanded resulting from a given percentage change in price. Petrol is generally associated with a low PED because petrol is deemed by consumers and households to be a necessity with few substitutes.

Lower prices for petrol will not generally result in consumers choosing to drive their car further or more frequently (because demand is price inelastic), so the total amount spent on petrol is likely to fall. Therefore, lower prices will free up more of the weekly household budget for savings or other discretionary purchasing decisions, possibly improving the material living standards of Australian households.

Question 2diii.

Marks	0	1	2	Average
%	38	28	33	1

Some students struggled to answer this question and there was evidence of some confused thinking. For example, some students argued that the government intervenes to reduce prices because petrol is a necessity.

The highest-scoring answers argued that the government imposes an excise tax to diminish the effects of negative externalities associated with the consumption of petrol or the work of the Australian Competition and Consumer Commission (ACCC) in preventing collusion.

Question 3a.

Marks	0	1	2	Average
%	14	22	64	1.5

Most students answered this question confidently and wrote strong responses, indicating good current knowledge related to factors influencing the Reserve Bank of Australia (RBA) in their decision to lower the cash rate in February 2015. High-scoring responses impressively linked their factor to the RBA's charter goals/objectives or identified current rate versus economic goal target.

A number of factors were selected, such as the softening labour market and rising levels of unemployment, sluggish domestic economic activity, declining consumer and business confidence levels, and slower rates of economic growth.

The following is an example of a possible response.

The RBA lowered the cash rate in February 2015 to the historically low level of 2.25% after a sustained period of maintaining the cash rate at a stable but accommodative rate of 2.5%. A factor that made this possible might have been that the primary focus of the RBA in setting the monetary policy (MP) stance is the pursuit of low inflation. With inflation tracking at the lower end of the target zone of 2% to 3% over the medium-term, the RBA could afford to be more aggressive in the use of an expansionary MP stance to boost domestic demand, as the economy was experiencing an economic growth rate that was below trend and there was rising unemployment.

Question 3b.

Marks	0	1	2	3	4	Average
%	25	15	21	15	25	2

While many students showed accurate theoretical knowledge of the cash flow and exchange rate transmission channels, a number failed to link the operation of the channels to assist in the achievement of the goal of full employment.

Other students confused the cash flow channel with the cost of credit channel, and so were unable to score marks for this question.

Some students did not understand the difference between discretionary and disposable income.

In the second part of the question, some students knew that cuts in official interest rates would cause depreciation but struggled to explain how that depreciation occurred.

The following is an example of a possible response.

The cash flow transmission mechanism is activated by a change in official interest rates flowing on to interest rates for personal loans, home loans and business loans in the economy. If the cash rate is reduced, lower 'retail interest rates' will mean those consumers, households and businesses already in debt and paying variable interest rates will now find the cost of debt servicing to be less expensive, creating increased discretionary income and possibly increased spending within components of consumption spending and investment spending of aggregate demand.

The increased aggregate demand sends a signal to producers to expand output levels and as a consequence there is likely to be an increased derived demand for labour, along with other resources. This should effectively reduce the level of cyclical unemployment, with more job opportunities assisting to reduce the level and rate of unemployment overall.

The exchange rate transmission mechanism relies upon changes in domestic interest rates, relative to interest rates elsewhere in the world, impacting upon capital investment flows in and out of Australia. With declining interest rates in Australia, overseas speculative investors are less inclined to invest in interest-bearing deposits in Australia, with the net effect being an increased

supply of the \$AUD in the foreign exchange market relative to demand and a depreciation in the \$AUD. As the \$AUD depreciates, this has the capacity to increase demand for Australia's exports and import competing goods and services, as well as decreasing demand for imports by Australians. The net improvement in injections and decline in leakages of economic activity may assist to boost profitability of Australian businesses, leading to business expansion and a boost to domestic employment opportunities.

Question 3c.

Marks	0	1	2	Average
%	23	28	49	1.3

The majority of students were able to outline a possible negative impact on the economy associated with lowering the cash interest rate. The negative impacts most students selected were related to the risk that lower interest rates would lead to even more increased demand for housing, leading to even higher housing prices, and the fact that self-funded retirees rely heavily upon interest rate returns on savings for their income stream in retirement. With lower interest rates such citizens would experience a fall in income, impacting their living standards.

Question 4a.

Marks	0	1	2	Average
%	16	23	61	1.5

Given the complex nature of the current budgetary policy stance, this question was well handled by the majority of students, showing that they had a very good understanding of the current stance. The highest-scoring answers included reference to the relevant data contained in the table.

The following is an example of a possible response.

The budget deficit is expected to fall from a deficit of \$41.1 billion in 2014–15 to a deficit of \$35.1 billion in 2015–16 as measured by the underlying cash balance. It will also represent a smaller percentage of GDP – 2.6% to 2.1%. This is generally seen as a contractionary stance when comparing the 2015–16 Budget outcome with the 2014–15 Budget outcome. This is because in order to reduce the deficit the government will have to reduce government spending and/or raise taxes, which is likely to have a dampening effect on aggregate demand.

Question 4b.

Marks	0	1	2	3	4	Average
%	10	8	13	21	48	2.9

Students answered this question confidently and most students were awarded relatively high marks.

High-scoring responses made the following points:

- Budgetary outlays will tend to rise as a result of an increasing rate of unemployment. Budgetary outlays will rise through the operation of automatic stabilisers as increased unemployment levels create a larger pool of citizens who automatically qualify for social welfare payments such as the Job Search Allowance.
- Budgetary receipts will tend to decline if the rate of unemployment rises. As more citizens become unemployed, income tax collections are reduced as fewer citizens are employed. A rising rate of unemployment may also be associated with declining levels of household expenditure and consequently declining levels of indirect taxation receipts for the Australian Government from falling retail sales. Rising unemployment levels may also be associated with

a generally contracting macroeconomic climate for business, and as business profitability declines so too will the company taxation receipts of the Australian Government.

- Discretionary initiatives such as infrastructure spending, expenditure on retraining displaced workers and vocational education may need to be expanded as pressure is placed on government to respond to particularly cyclical and structural forms of unemployment. Such additional spending may be targeted at boosting AD as well as addressing the mismatch between emerging job vacancies and the skills of available workers. Other discretionary spending may also be required to address aspects of social disharmony that tend to rise in periods of increased unemployment, such as mental health issues, family disharmony and affordability of housing.

Question 4ci.

Marks	0	1	2	Average
%	28	40	32	1.1

Many students struggled with this question. A number of students did not understand how budget deficits are financed and were unable to describe the link between government budget deficits and the government/national debt. There continues to be a great deal of confusion demonstrated by students between budget deficits and current account deficits.

Students were expected to state that budget deficits by definition represent a situation where the planned budget outlays for the forthcoming 12 months exceed the planned budget receipts, necessitating additional borrowing by the Australian Government in order to be able to implement the budget plan. Any additional government borrowing must be added to the accumulated government/national (public sector) debt.

Question 4cii.

Marks	0	1	2	Average
%	13	37	50	1.4

This question was relatively well handled, even though students struggled to answer part i. correctly. Issues related to debt have been well represented in the media over the past two years, and students' had a good understanding of the current debate.

The following is an example of a possible response.

The concept of a 'legacy of debt' left to future generations implies that the fiscal excesses of the current generation will be placing an unhealthy and unfair 'burden' upon the taxpayers of the future, and more generally upon living standards to be enjoyed by citizens of the future.

Any public sector debt passed on to future generations not only has to be paid back using taxes paid by citizens in the future and/or by liquidation of community-owned assets, but also debt accumulates interest repayments, placing a further drain on the financial resources of that future generation. In simple terms, the burden of servicing and repaying an intergenerational public sector debt poses an opportunity cost consideration for that future generation – financial resources consumed in servicing and repaying such a debt will not be available for the next best alternative use (for example, infrastructure development).

Question 4d.

Marks	0	1	2	3	4	Average
%	15	12	21	30	22	2.3

Most students were able to identify a current policy and describe how the policy was likely to influence equity and make life better for some members of society.

The highest-scoring answers defined the goal of equity in the distribution of income, accurately described the policy (rather than simply and vaguely outlining the policy) and linked it to one or more aspects of equity (rather than just asserting an influence on equity such as low income earners would be better off). The sorts of policies selected included changes in the Families Package and child care arrangements, increased infrastructure spending, changes in means testing related to pensions, \$375 million in new measures to help Australia's unemployed find jobs, including measures to build employability skills, particularly for young people transitioning to work.

Most students chose a policy and described a positive likely influence. Students could also have selected a policy and described how it may worsen equity.

The following is an example of a possible response.

As part of the Families Package in the 2015–16 Budget, the government promised to create a better and fairer child care system. Part of this initiative was to modify the existing child care subsidy arrangements so that families earning less than \$65 000 would receive a subsidy of 85% of their child care fees. This provides more support to these income earners because now higher income earners will only receive a 50% subsidy (which is to be capped at \$10 000 if they earn more than \$185 000pa).

This initiative assists lower income earners in a number of ways to achieve a more dignified living standard, thus promoting improved equity. Firstly, if they are already working, their disposable income will essentially increase and the gap between higher and lower income earners will decrease, with lower income earners being able to afford to buy more goods and services. For those families where one or more members were not working the child care subsidy might encourage them to seek a job. If they find a job and are no longer reliant on welfare (such as a single-parent pension) this will also narrow the income-earning gap, thus improving equity outcomes.