

ECONOMICS UNITS 3 & 4

2021

TRIAL EXAM B

SUGGESTED SOLUTIONS/RESPONSES

Multiple-choice Answers

1	A	B	C	D
2	A	B	C	D
3	A	B	C	D
4	A	B	C	D
5	A	B	C	D
6	A	B	C	D
7	A	B	C	D
8	A	B	C	D
9	A	B	C	D
10	A	B	C	D
11	A	B	C	D
12	A	B	C	D
13	A	B	C	D
14	A	B	C	D
15	A	B	C	D

SECTION A – Multiple-choice questions

Instructions for Section A

Answer **all** questions in pencil on the answer sheet provided for multiple-choice questions. Choose the response that is correct or that best answers the question.

A correct answer scores 1; and incorrect answer scores 0.

Marks will not be deducted for incorrect answers.

No marks will be given if more than one answer is completed for any question

Question 1

Which of the following is **not** a pre-condition for a perfectly competitive market?

- A. firms are 'price takers'
- B. homogenous product is sold
- C. many sellers and many buyers
- D. product differentiation**

Economic Reasoning

Answer D is correct because in a perfectly competitive market homogenous products are sold – product differentiation occurs in monopolistic and oligopolistic markets.

Question 2

Which of the following is **not** considered to be a leakage from the circular flow model?

- A. exports**
- B. government taxation
- C. household savings
- D. imports

Economic Reasoning

Answer A is correct because Exports are an injection to the economy not a leakage.

Question 3

Which of the following is **best described** as a direct progressive tax?

- A. good and services tax
- B. PAYG income tax**
- C. company tax
- D. customs and excise duties

Economic Reasoning

Answer B is correct because PAYG tax increases as the level of income increase (progressive) and is levied directly on the income earner unlike GST that is charged on goods and services and is an indirect tax.

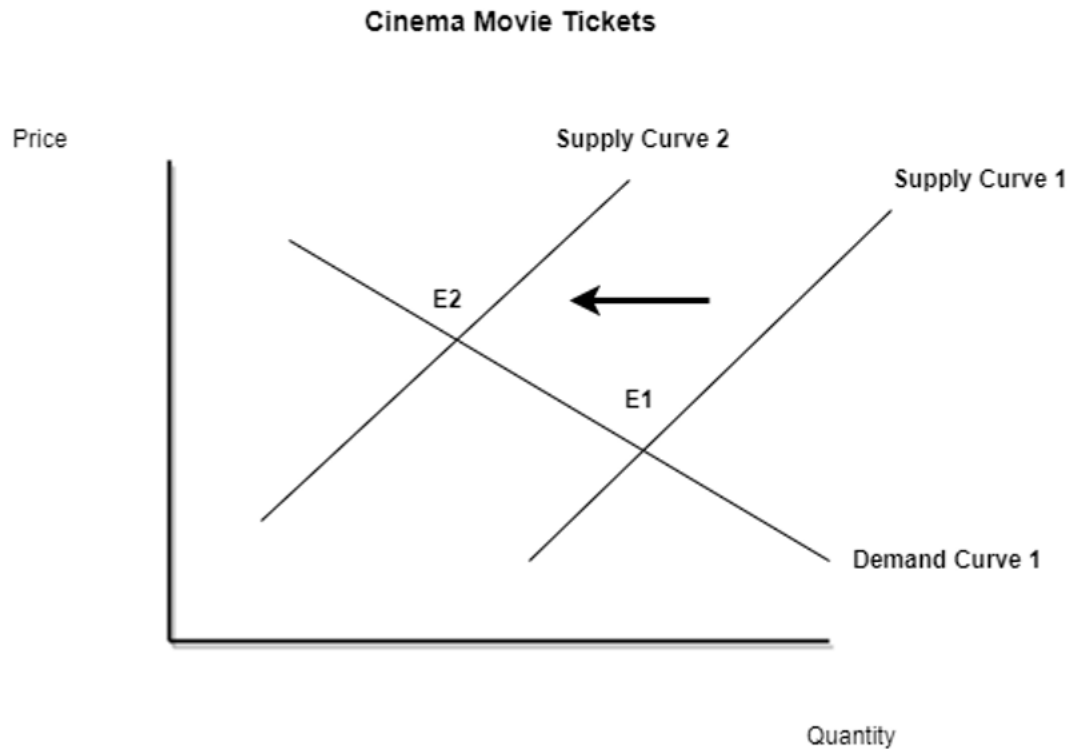


Figure 1.1 – Market for Cinema Movies

Question 4

In relation to the **Figure 1.1**, which of the following **best explains** the change in the market for cinema movie tickets?

- A. a contraction supply occurred because the costs of production decreased
- B. a decrease in demand occurred because preferences shifted to video-on-demand services such as Netflix
- C. a contraction in demand resulted from the costs of production declining
- D. a decrease in supply occurred because the costs of production increased**

Economic Reasoning

Answer D is correct because when costs of production rise it causes a disincentive for producers to produce as profit levels fall. It causes supply to decrease (shift to the left).

Question 5

Which of the following will have a positive effect on living standards in Australia?

- A. a rise in the level of COVID19 mental illness conditions
- B. a rise in the level of crime in city and suburban areas
- C. a rise in the literacy rates of newly arrived migrants to Australia**
- D. a rise in the level of serious workplace accidents

Economic Reasoning

Answer C is correct because literacy rates improving supports directly Non-material living standards advancing – quality of life is enhanced for newly arrived migrants

Question 6

The table below shows selected data for an economy

Economic Indicators	Year 1	Year 2
Productivity Growth	2%	1%
Inflation Rate	1.8%	2%

From the data in the table above it can be concluded that between Year 1 and Year 2 the economy experienced

- A. a decline in international competitiveness
- B. a decrease in the relative competitiveness of the economy in global markets
- C. a worsening of the international competitiveness within the economy
- D. all the above are correct**

Economic Reasoning

Answer D is correct. With productivity growth declining and inflation rising, Australia's international competitiveness is negatively affected

Question 7

Which of the following policy initiatives is **not** designed to affect aggregate supply and living standards?

- A. reforming welfare payments to ensure recipients are encouraged to seek employment
- B. reducing the tax burden on individuals
- C. investment in infrastructure
- D. the cash rate being decreased by the RBA**

Economic Reasoning

Answer D is correct because a decrease in the cash rate by the RBA is an AD policy – the other 3 are designed to affect AS,

Question 8

Which of the following policy initiatives **is likely** to have a different effect on aggregate demand from the other three?

- A. introduction of Job Keeper to boost household income and a cut to company tax rates
- B. withdrawal of the home stamp-duty tax for first home buyers and increase to the rate of the Newstart allowance
- C. *budgetary cutbacks on investment in National infrastructure projects***
- D. the reduction in the tax rates of the progressive income tax system of Australia

Economic Reasoning

Answer C is correct because 'cutbacks' on G2 spending slows AD. Answers A, B & D all boost the level of AD.

Question 9

Which of the following situations best explains a price elasticity of supply that is elastic?

- A. *a small percentage change in price causes a large percentage change in quantity supplied***
- B. a large percentage change in price causes a small percentage change in quantity supplied
- C. a small percentage change in price causes a large percentage change in quantity demanded
- D. a large percentage change in price causes a large percentage change in quantity demanded

Economic Reasoning

Answer A is correct because if a small change in price causes a relatively larger change in the quantity supply – high responsiveness – PES is elastic

Question 10

The table below shows selected data for an economy

Balance of payments item	\$bn
Capital and Financial Account	250
Net Services	150
Net Primary Incomes	50
Net Secondary Incomes	-100

For this economy the balance on net exports is

- A. -\$100bn and the balance on current account is -\$500bn.
- B. *-\$350bn and the balance on current account is -\$250bn.***
- C. -\$150bn and the balance on current account is \$500bn.
- D. -\$350bn and the balance on current account is \$250bn.

Economic Reasoning

Correct answer is B because the balance on the Current Account should cancel out the balance on the Capital and Financial Account - the balance on the Current Account is -



\$250bn. With the Balance on the Current Account being \$100bn before adding Net Goods, the balance on the Net Goods Account is -\$350bn

Question 11

An expansionary stance for monetary policy by the Reserve Bank of Australia (RBA) could be achieved by

- A. selling Commonwealth Government securities to decrease cash in the overnight money market
- B. buying Commonwealth Government securities to decrease cash in the overnight money market
- C. selling Commonwealth Government securities to increase cash in the overnight money market
- D. **buying Commonwealth Government securities to increase cash in the overnight money market**

Economic Reasoning

D is the correct answer. The RBA must enter the overnight money market and purchase or repurchase government securities. Increasing liquidity in the market and pressuring the cash rate downwards, supports an expansionary stance.

Question 12

Which of the following types of government expenditure is **most likely** to directly increase the household sectors disposable income?

- A. **transfer payments**
- B. current expenditure
- C. capital expenditure
- D. consumption expenditure

Economic Reasoning

The correct answer is A with transfer payments being social security payments (Newstart, Job Keeper) being directly received by economic agents in the household sector.

Question 13

In the market for second-hand motor vehicles, what effect will an increase in demand have while the level of supply remains unchanged?

- A. price will increase and quantity demanded will decrease
- B. price will decrease and quantity demanded will decrease
- C. **price will increase and quantity demanded will increase**
- D. price will decrease and quantity demanded will increase

Economic Reasoning

The correct answer is C because with the demand curve shifting right and supply staying the same the new equilibrium point will see price rises and the quantity of second-hand cars demanded increase.

Question 14

The underlying inflation rate

- A. is usually lower than the headline inflation rate when the prices of volatile goods are falling faster than other goods
- B. includes all one-off or volatile price increases in its measurement
- C. is usually higher than the headline inflation rate when the prices of volatile goods are rising faster than other goods
- D. is usually higher than the headline inflation rate when the prices of volatile goods are falling faster than other goods**

Economic Reasoning

D is the correct answer because the underlying rate of inflation removes around 20,000 items that are subject to high levels of volatility. If the volatile items are falling price faster than the core 80,000 goods of the underlying inflation rate it will cause the Underlying inflation rate to be higher than the Headline inflation rate.

Question 15

The table below shows selected Gross Domestic Product (GDP) data for a hypothetical economy

Period of time	GDP measure (\$Billions)
Year 1	80
Year 2	100
Year 3	120

Which of the following **best describes** the change/s in Gross Domestic Product (GDP) in the hypothetical economy?

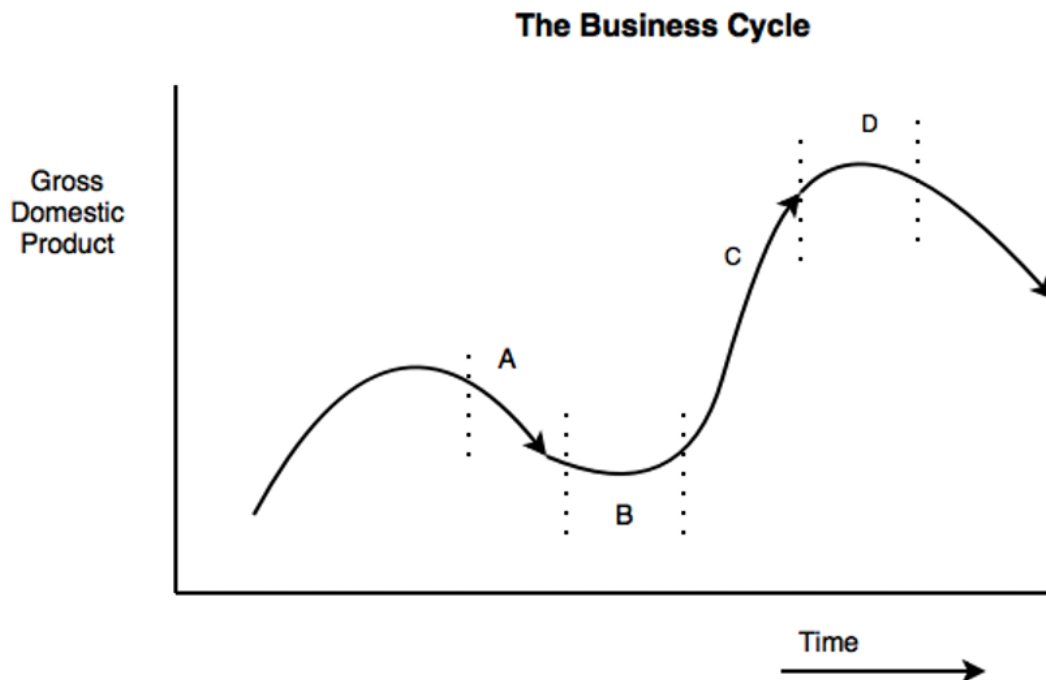
- A. The rate of change of GDP has remained unchanged through Year 1 to Year 3
- B. The rate of change of GDP has increased through Year 1 to Year 3
- C. The rate of change of GDP from Year 1 to Year 2 is smaller than the rate of change in GDP from Year 2 to Year 3
- D. The rate of change of GDP from Year 1 to Year 2 is greater than the rate of change in GDP from Year 2 to Year 3**

Economic Reasoning

D is the correct answer. From Year 1 to Year 2 it is 25% increase in GDP. From Year 2 to Year 3 it is a 20% increase in GDP. The rate of change has decreased, and the rate of change between Year 1 and Year 2 is greater than the rate of change from Year 2 to Year 3

SECTION B – Written responses

Instructions for Section B
Answer all questions in the spaces provided

Question 1 (15 marks)**Figure 1.2 – The Business Cycle**

- a. Outline the economic features of an economy that is operating at point ‘C’. (3 marks)

Suggested Solution

At point C, an economy is experiencing an expansionary phase in the business cycle. The rate of economic growth (real GDP) will be increasing and the rate of unemployment will be falling. Inflationary pressures will begin to appear, and the rate of inflation (CPI) will be rising.

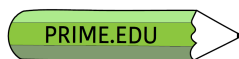
Marking Guide

1 mark for stating it is an expansionary phase.

2 marks for correctly describing the features of an economy: GDP rising, Unemployment falling and Inflation rising

Exam Tip

Past VCAA reports suggest when ‘outlining’ to be direct and brief with the response.



- b. From Figure 1.2, describe what is happening in the economy that shifts from 'A' to 'B' in the business cycle. Describe what change to one aggregate demand factor could cause this shift from 'A' to 'B'. (4 marks)

Suggested Solution

An economy that moves from section 'A' to section 'B', is moving from contractionary phase in economic activity to a trough in the business cycle (lowest point of economic activity during the business cycle). Economic growth is declining, unemployment is rising, and inflation will be at its lowest rate in the business cycle.

A decline in consumer confidence could cause the shift from 'A' to 'B'. Should the household sector become pessimistic about future levels of income, the level of household consumption spending will fall. The level of aggregate demand will slow down and there will be a decrease in the level of national spending on goods and services.

Marking Guide

2 marks for the correct description of a shift from a contraction to a trough

2 marks for the correct description of an AD factor causing the level of AD to decline

(Other possible AD factors causing a decline in AD: rise in general level of prices, rise in interest rates, fall in real disposable income, decline in business confidence, appreciation of \$AUD and decline in global economic growth)

Exam Tip

Past VCAA reports suggest when describing features of the economy key terms must be used correctly. When using key terms 'consumer confidence' incorporate the meaning of the term in the response.

- c. Describe how budgetary automatic stabilisers will operate to support an economy experiencing low levels of economic growth. (4 marks)

Suggested Solution

Automatic stabilisers are structural features of the federal budget that operate to smooth the business cycle with any deliberate changes to government spending or revenue measures. An economy with low levels of economic growth, possibly experiencing a recession will result in

the level of unemployment welfare recipients increasing. Government transfer payments providing a disposable income when otherwise no income would be received. Consumption spending on goods and services will not decline as sharply, as it would have without Newstart payments. In effect, propping up economic activity and lessening the decline in the rate of economic growth.

Marking Guide

2 marks for describing what and how automatic stabilisers operate

2 marks for explaining why a feature of automatic stabilisers will support stronger level of economic growth

Exam Tip

Past VCAA reports suggest it is appropriate to focus on just one feature of an economic concept when correctly using the concept to justify the reasoning.

Special tip – Automatic stabilisers include welfare payments and taxation receipts##

- d.** Assess how **one** budgetary initiative from the 2021-2022 budget could support the achievement of strong and sustainable economic growth. (4 marks)

Suggested Solution

The 2021-2022 budget commitment to personal income tax cuts with 10 million low to middle income earners having over \$1,000 in the next financial year. The boost to disposable incomes can support stronger rates of household consumption spending and treasury estimates predict will boost GDP by around \$4 billion in the next financial year. Moreover, contributing to a derived demand for workers increasing employment.

Stronger levels of household consumption spending will increase the level of aggregate demand and cause the rate of growth in GDP to be higher, supporting the government in their aim of achieving the fastest rate of GDP that is consistent with the goals of low inflation and full employment.

Marking Guide

1 mark for clearly stating a correct initiative from the 2021-2022 budget

2 marks for explaining why it boosts AD and stronger levels of GDP

1 mark for the link to and explanation of the goal of SSEG

Exam Tip

Examiners will know many initiatives from the 2021-2022 budget supporting growth and jobs. Use obvious ones (tax cuts/ infrastructure spending) to make the examiners life easier, if you force the examiner to research a correct obscure initiative it's annoying.

Question 2 (17 marks)

Commodity markets suffered a violent sell-off as mounting anxiety about slower global economic growth sent oil and metal prices tumbling and iron ore plunged on weaker steel demand. The Australian currency fell to a 10-month low.

Source 1: <https://www.afr.com/markets/commodities/iron-ore-enters-freefall-amid-global-commodity-sell-off>

- a. Explain why the price of Australia's number one export iron ore falling is likely to affect the Australian dollar (3 marks)

Suggested Solution

When the global prices paid for iron ore fall it has a negative effect on Australia's terms of trade and results in a depreciation of the Australian dollar. Global demand for iron ore has remained relatively stable over the past few years, but if the price paid for this commodity falls it means less foreign currency is needed to purchase the same volumes of iron ore. Demand for \$AUD in the foreign exchange market decreases and the value of \$AUD on global currency markets falls.

Marking Guide

1 mark for stating iron ore prices falling causes a depreciation of the \$AUD

2 marks for explaining why demand in FOREX declines and causes the depreciation

Exam Tip

Past VCAA reports suggest that using abbreviations such as \$AUD to stand for the Australian dollar and FOREX to stand for the foreign exchange market is accepted and will not adversely impact your score.

- b. Define international competitiveness. (2 marks)

Suggested Solution

International competitiveness refers to the ability of country to compete in global markets in producing and selling goods and services with the aim of increasing market share. In the global markets competition is based on price or non-price factors (such as service or quality).

Marking Guide

2 marks for the correct definition of international competitiveness

**Exam Tip**

Past VCAA reports suggest when providing definitions use key words. For example, with international competitiveness must include ‘**compete in global markets**’ and ‘**producing and selling goods and services**’ to get full marks.

- c. Explain the relationship between international competitiveness and dynamic efficiency. (4 marks)

Suggested Solution

International competitiveness and dynamic efficiency have a compatible or complementary relationship. Australian businesses exporting overseas and Australian businesses competing with imports can gain a competitive advantage by offering lower final prices or a better-quality product. When market conditions overseas and domestically change the speed at which Australian firms can reallocate resources to meet the changing global demands will determine whether Australia’s dynamic efficiency is high. A swift and successful reallocation that take advantage of market opportunities boosts Australia’s international competitiveness. A slow response will cost Australian businesses market share and weaken Australia’s international competitiveness.

Marking Guide

1 mark for stating the relationship is complementary

3 marks for describing why dynamic efficiency has a positive relationship with international competitiveness

Exam Tip

Past VCAA reports suggest with ‘relationship’ questions clearly decide whether it is positive/complementary relationship or whether the relationship is negative/inverse relationship.

A depreciation of the Australian dollar and increase to the official cash rate by the Reserve Bank will improve Australia’s international competitiveness.

- d. Justify using economic reasoning to what extent this statement is correct. (8 marks)

Suggested Solution

To a certain extent this statement is correct, however it’s likely that the rise in the official cash rate will negatively affect international competitiveness.

When the Australian dollar is losing value on foreign exchange markets, the depreciation of the Australian dollar has a positive effect on international competitiveness. A depreciation of the Australian dollar automatically makes Australia’s tradable exports like commodities and



agricultural produce relatively cheaper for overseas buyers. A more competitive price is available for overseas buyers like China and USA and hence Australia's international competitiveness improves.

However, when the RBA targets higher interest rates it can attract more foreign capital seeking a higher return on their investment, demand for \$AUD rises and the Australian dollar appreciates. To a certain extent this reduces Australia's international competitiveness. Foreign buyers of Australian exports will be more expensive and import competing industries will face cheaper imports, diminishing the competitiveness of Australian businesses on global markets.

Marking Guide

1 mark for addressing the extent that the statement is correct to being partially Correct

3.5 marks for the economic discussion of why a depreciation of the \$AUD improves International Competitiveness

3.5 marks for the economic discussion of why a tightening of monetary policy will cause an appreciation and diminish International Competitiveness

Exam Tip

Past VCAA reports suggest that when discussing how the \$AUD either appreciates or depreciates that the effects on demand and supply of \$AUD in the foreign exchange markets must be precisely explained

Question 3 (17 marks)

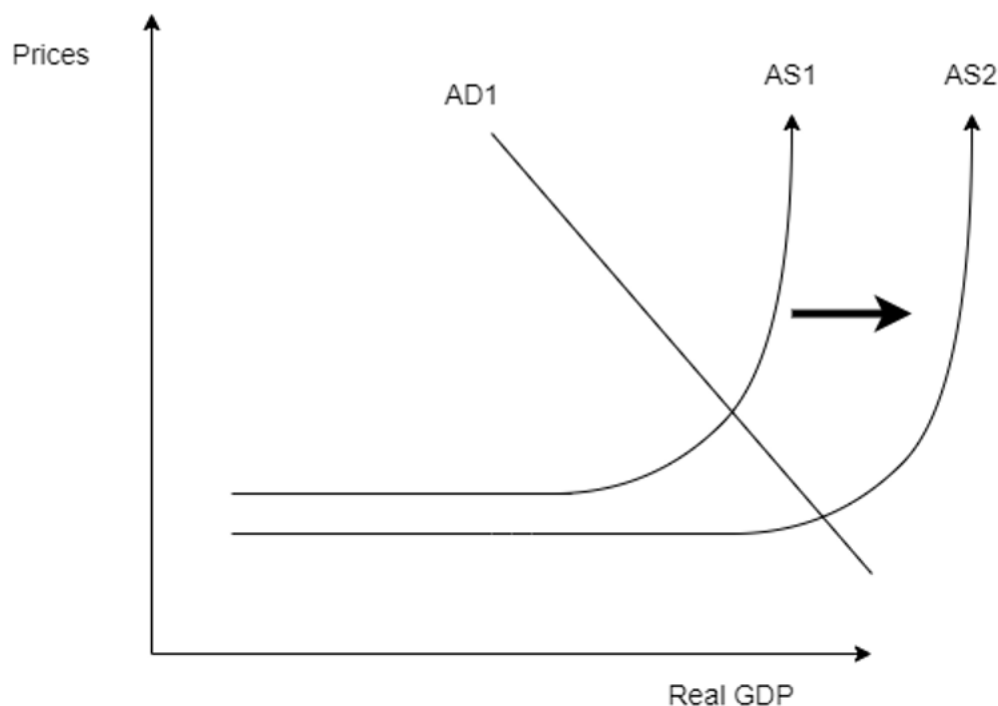


Figure 1.3 - Aggregate Demand and Aggregate Supply Graph

a. Select one of the aggregate supply factors below

- technological change
- climatic conditions

Analyse how the aggregate supply factor chosen could have caused the shift in the Figure 1.3 above. (3 marks)

Suggested Solution

With climatic conditions improving through the seasons (summer, autumn, winter and spring) of a year, the quantity of natural resources that can be utilised in production of goods and services expands and causes the aggregate supply curve to shift to the right. More favourable climatic conditions extending the ability of producers to supply a range of agricultural products resulting in the level of aggregate supply increasing from AS1 to AS2.

Marking Guide

1 mark for stating the level of aggregate supply has increased (shifted to the right)

2 marks for the analysis of why the factor caused either the willingness or ability of producers to expand

Exam Tip

Past VCAA reports suggest when explaining aggregate supply students must focus on “quantity and quality of resources” and “willingness and ability of producers to produce”.



- b. Discuss the relationship between aggregate supply and Australia's unemployment rate. (4 marks)

Suggested Solution

Aggregate supply (AS) refers to an economies ability and willingness to produce goods and services based on the quantity and quality of economic resources available. Aggregate supply usually experiences an inverse relationship with unemployment, that is as AS increases the rate of unemployment will usually decrease.

A level of AS increasing provides a stable environment for GDP to expand without unwanted inflationary pressures. Firms seeking profit will tend to employ more workers to take advantage of the opportunity to increase the profit levels of firms. Although, if AS increases while aggregate demand contracts, with the economy experiencing a deep low in economic activity, unemployment could remain unchanged or even under rare circumstances see unemployment rise while AS is increasing.

Marking Guide

1 mark for stating there is an inverse relationship between aggregate supply and unemployment

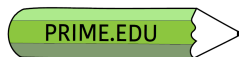
3 marks for explaining why a rise in AS contributes to a reduction in unemployment

Exam Tip

Past VCAA reports suggest that the classical theory response will always be awarded full marks if sufficiently explained. However, divergent economic thinking could also be rewarded if relevant economic theory is used to justify the response

A Treasury member said,

“...during the COVID19 pandemic the Australian governments focus has been on boosting aggregate demand...and hence in the last few years aggregate supply policies have been neglected”



- c. To what extent do you agree with the statement above. Use current knowledge and economic reasoning to justify your answer. (6 marks)

Suggested Solution

To a high extent I agree with the statement as the federal government have been forced to act quickly to stem the economic crisis caused by COVID19.

Firstly, the setting of budgetary policy is expansionary and has focus on propping up aggregate demand in the short-term. The predicted budget deficit for 2020-2021 is a \$161 billion deficit and the deficit is forecasted to fall to a deficit of \$106 billion in 2021-2022 financial year. Although, forecasts see budgetary deficits falling the current budgetary stance is highly expansionary.

In addition the short-term policy measures of Job Keeper provided employers hardest hit in 2020-2021 receiving \$1500 per fortnight to save jobs when forced to not work during lockdown. Another short-term boost to AD has been the recent one-off grants to businesses in lockdown in NSW who experience a 70% reduction in revenue. The federal government will provide up to a \$15,000 payment to help businesses cover costs while in lockdown.

However, in the 2021-2022 budget \$2.7 billion has been allocated to skills training for 170,000 apprentices and traineeships. Boosting skills of Australian workers adds to the quality and mobility of Australia's labour force and has a positive effect on aggregate supply.

In conclusion, the federal government primary focus in 2021 and over the next few years is protecting jobs and attempting to keep Australia out of a COVID19 induced recession. Hence to serve this aim AD policies have been prioritized over large-scale aggregate supply reforms.

Marking Guide

Global marking— question of sufficient detail and quality of evaluation

1-2 marks for a few points about budgetary policy

3-4 marks for addressing the stance of BP and some measures with little account of AS policies

5-6 marks for a fulsome and detailed discussion of BP measures used in the short term with some evaluation and discussion of AS policies

- d. Explain one strength and one weakness of the government using budgetary policy to influence short-term economic growth. (4 marks)

Suggested Solution

One strength of budgetary policy is its ability to target specific sectors or economic agents when influencing economic growth. For example, the one-off grants of up to \$15,000 for



businesses with nearly no revenue because of COVID19. This targeted government expenditure supports a stronger rate of GDP in the short-term.

One weakness of budgetary policy is the political constraints. It can be difficult to change tax laws and transfer payments as the bill can be blocked in lower or upper houses of parliament. Policy of merit and a strong influence on household and business spending could be blocked by a hostile senate, restricting short-term economic growth.

Marking Guide

2 marks explaining a correct strength in relation to short-term economic growth

2 marks explaining a correct weakness in relation to short-term economic growth

Exam Tip

Past VCAA reports have been critical of responses that do not explain the strengths and weaknesses of budgetary policy, monetary policy and aggregate supply policies in relation to the context or prevailing circumstances.

Question 4 (16 marks)

- a. Why is relative scarcity the reason that opportunity cost is inevitable? (4 marks)

Suggested Solution

Relative scarcity refers to the concept that an economy has a limited supply of economic resources but that within, this economy society has unlimited wants and needs that can never be fully satisfied. Consequently, decisions about what, how and how much is to be produced is decided by the market and government. In choosing to produce certain goods say, education, over a highway an opportunity costs arises. A situation where the production of educational services results in the next best alternative being forgone or given up.

Marking Guide

2 marks for an accurate description/definition of relative scarcity and opportunity cost

2 marks for explaining why relative scarcity forces opportunity cost to arise because of the necessity for decisions in production

Price Elasticity of Demand (PED) for Products

Product	Measure of PED
House	2
Milk	0.33
Netflix	4

Table 1.1 – Price Elasticity of Supply for Houses, Milk and Netflix

- b. Explain why the price elasticity of demand for Netflix is 4 and why the price elasticity of demand for Milk is 0.33. (4 marks)

Suggested Solution

Netflix with a price elasticity of demand (PED) of 4 suggest that small change in price causes a proportionally larger response in quantity demanded – 4 times in fact. A factor that gives Netflix a high PED is the market for video-on-demand has large number of substitutes such as Apple TV, Stan, Amazon Prime and Disney+.

In contrast, Milk with a PED of 0.33 has a price elasticity of demand response that is inelastic. Where a large proportional change in the price change in Milk will cause a relatively small change in the level of demand. The reason why PED for Milk is inelastic is it is considered a necessity and in addition represents a relatively small proportion of a householder's income.

Marking Guide

1 mark for stating Netflix has a PED that is elastic

1 mark for justifying this with the fact Netflix has multiple substitutes

1 mark for stating Milk has a PED that is inelastic

1 mark stating either Milk is a necessity or represents small proportion of personal income

Exam Tip

Past VCAA reports suggest its critical students demonstrate a precise knowledge of the PED being directly related to the responsiveness of the change in quantity demanded in relation to the percentage change in price.

- c. Outline two conditions of a perfectly competitive market. (2 marks)

Suggested Solution

One feature is many buyers and sellers compete within the market and act independently of each other. This way, no individual buyer or seller has enough influence or control over the market to set prices.

A second feature is the product that is sold is homogenous. Making the product sold by sellers identical and perfectly substitutable.

Marking Guide

1 mark X 2 for briefly outlining a feature of a perfectly competitive market

**Exam Tip**

Other features of perfectly competitive market:

- Price takers
- Ease of entry and exit
- Symmetry of product information exists
- Sellers aim to maximise profits and buyers aim to maximise utility

- d. Explain why government intervention in a market can (3 + 3 = 6 marks)
- i. effect the role of relative prices allocating resources
 - ii. address market failure caused by common access resources

Suggested Solution

- i. Government subsidies for producers and consumers changes the incentives for suppliers to produce a good or service. A government subsidy for consumers creates more incentive to buy the product, solar panel subsidies is a good example of a subsidy and increases demand for the number of solar panels installed across Australia. Producers will notice demand and the net profits for producers rising and are incentivized to direct more economic resources (labour and capital) into the production and installation of solar panels.
- ii. Government legislation and regulation of markets featuring a non-excludable yet rivalrous resource or good. Laws that limit or ban consumption can help support sustainability and long-term viability of these markets. Fisheries authorities that legal enforce commercial fishing quotas operate to limit the overfishing of the world's oceans. This government intervention reduces overconsumption of a common access resource and supports inter-temporal efficiency – reallocating resources to sustain economic wellbeing into the future.

Marking Guide

i. Answer

1 mark for correctly explaining one government intervention into a market. Could include subsidies, indirect taxes, government regulations and government advertising



2 marks for explaining how the intervention changes relative prices and reallocates economic resources

ii. Answer

1 mark for correctly explaining one government intervention into a market. Could include subsidies, indirect taxes, government regulations and government advertising

2 marks for explaining how the government intervention either changes the overallocation or underallocation of economic resources to improve economic wellbeing

Exam Tip

Past VCAA reports suggest relative prices changing effect the incentives associated with the allocation of economic resources and market failure involves a correction of an over or under allocation of resources through government intervention

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