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91222



Draw a cross through the box (X) if you have NOT written in this booklet

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Mana Tohu Mātauranga o Aotearoa
New Zealand Qualifications Authority

Level 2 Economics 2024

91222 Analyse inflation using economic concepts and models

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 2–16 in the correct order and that none of these pages is blank.

Do not write in the margins (// // //). This area will be cut off when the booklet is marked.

YOU MUST HAND THIS BOOKLET TO THE SUPERVISOR AT THE END OF THE EXAMINATION.

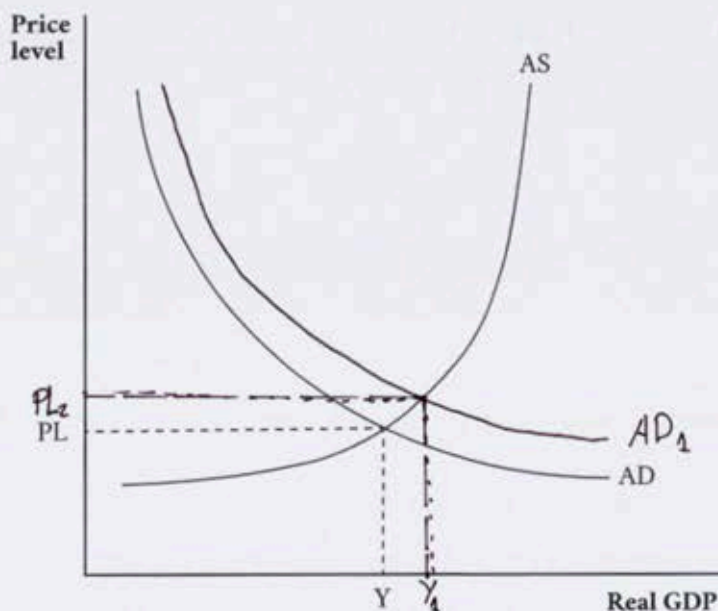
Achievement

TOTAL 10

QUESTION ONE: Causes of inflation

- (a) On Graph One below, show the impact on aggregate demand of the Fieldays event being held in the Waikato region in 2024.

Graph One: AS/AD model of the New Zealand economy



- (b) Explain the impact on inflation of the Fieldays event being held in the Waikato region in 2024. Refer to Graph One in your answer.

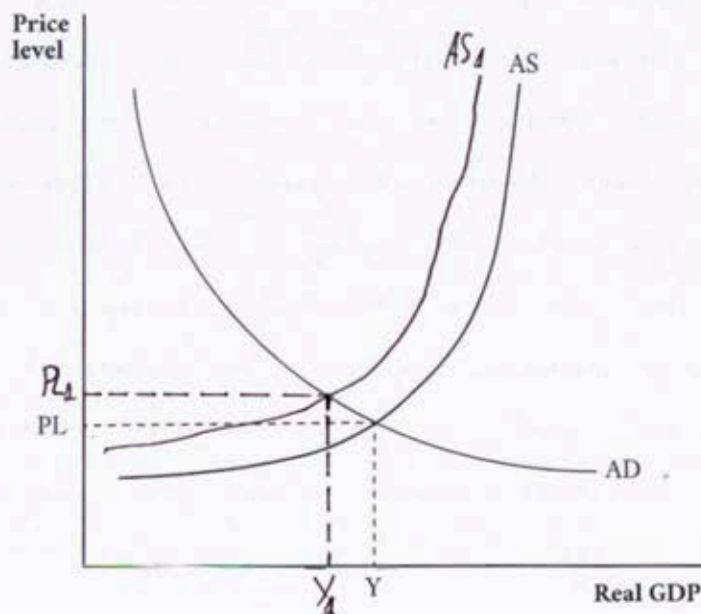
Due to the increased visitors, AD will increase to AD_2 due to a higher demand for goods and services which will result in an increase in the PL, to PL_2 which increases inflation due to the price of goods rising. This means that the general price level for all goods and services will increase, which as a result increases inflation. However the total output will increase as shown in the graph, Y to Y_2 . Inflation has increased because the price level

has increased for goods. However there is higher consumer spending as households would rather buy what they can now before it increases even further. Due to this inflation will continue to increase.



- (c) On Graph Two below, show the impact on aggregate supply of Cyclone Gabrielle and the higher production and insurance costs for New Zealand businesses.

Graph Two: AS/AD model of the New Zealand economy



- (d) Explain the impact on inflation of Cyclone Gabrielle and the higher production and insurance costs for New Zealand businesses. Refer to Graph Two in your answer.

Due to increased cost of production, there will be less total output Y, Y_1 and less supply of goods AS to AS_1 . As a result of less goods being supplied, the price level will increase PL to PL_2 . Due to insurance increasing in cost, people will spend more money to ensure that their belongings are safe and can be replaced if need be. This increases inflation as the cost of production increases, people will be laid off to try to make up from their lost profit. This increases inflation due to the rising of the general price level.

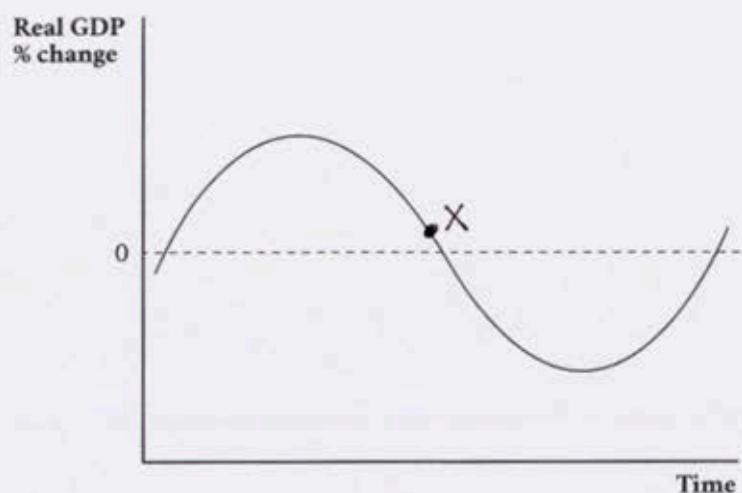
- (e) Discuss whether Fieldays or Cyclone Gabrielle is likely to have had the more significant impact on New Zealand's current inflation rate. Refer to Graphs One and Two in your answer. *

Cyclone Gabrielle is likely to have had the more significant impact on inflation. This is because, the damaged infrastructure will mean that we aren't as capable of producing the same number of goods and services making AS shift to the left (AS_1). This will increase the price level but also have fewer goods produced meaning there is a shortage of production but also an increase in the prices. This will make our exports less price competitive, and make consumer spending less confident meaning people are going to save rather than spend.

QUESTION TWO: Quantity theory of money and a recession

- (a) Identify and mark with an X the point on Model One that best represents a recession.

Model One: The business cycle



- (b) State the components of the quantity theory of money.

M: Money Supply

V: Velocity of circulation

P: Price level

Q: ~~Real~~ output

- (c) Explain why the velocity of circulation is likely to decrease during a recession.

Because there will be less money being spent by households and instead it will be saved. This is because households are less confident in spending and are unsure about the future.

- (d) Assuming all other variables remain constant, use the quantity theory of money to explain how a decrease in the velocity of circulation will impact inflation.

Assuming that all other variables are held constant, ~~if (V) were to decrease~~ if (V) were to decrease, inflation would also decrease because there is less money in circulation as it's not being spent as much and instead saved, Will decrease inflation over time as there is ^{not as much} money being spent which will cause the general price level to drop which lowers inflation.

Some experts argue that the New Zealand economy could experience a recession across the next two years, with a significant decrease in output predicted.

- (e) Use the quantity theory of money and the business cycle to explain how a recession may impact overall inflation.

In your answer, include:

- why real output may decrease during a recession
- how the change in velocity of circulation as well as real output will impact the price level in the economy.

Real output may decrease because there will be less goods produced.

The change in velocity of circulation as well as real output will impact the price level due to less money being spent and less business investments. This will lead to less consumer confidence which is a lack of spending which means firms won't make as much money.

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QUESTION THREE: Impacts of inflation

New Zealand's annual inflation rate in 2023 was 4.7 per cent. This is a decrease from the annual rate in 2022, when it was 7.2 per cent.

- (a) Define inflation.

An increase in the general price level.

- (b) Explain whether workers on the minimum wage would prefer a lower or higher inflation rate.

Workers on the minimum wage would prefer a higher inflation rate. This is because the workers wages will rise meaning they will be paid more. This therefore means that these workers can save there new increase in money or choose to spend it. So in conclusion, workers on the minimum wage would rather be ~~paid~~ in a higher inflation rate so they could be paid more.

- (c) Explain whether savers would prefer a lower or higher inflation rate.

Savers would also prefer a higher inflation rate because they would get higher interest on what they are saving. So over time this ~~sum~~ sum of money will increase greater than it would if inflation rates ~~were~~ were low. Whereas if they were saving and inflation rates were low, they would make less from what they are trying to save.

~~However~~ ~~sav~~ Savers may want to

New Zealand's annual inflation rate of 4.7 per cent in 2023 was higher than all of our major trading partners. Annual inflation was 4.0 per cent in the United Kingdom and 3.1 per cent across the European Union.

- (d) Compare and contrast the impact of New Zealand's higher inflation rate on New Zealand importers and exporters to the United Kingdom and the European Union.

NZ's exports will be less price competitive due to our exports costing more than other markets. But however, imports will become cheaper as we can now purchase more than we could before. Due to NZ's higher inflation, our exports will look less price competitive on foreign markets unlike UK's exporters which will be more price competitive as they are cheaper. However the UK ~~couldn't~~ couldn't import as much as NZ as because we have a higher inflation, we can buy more with our dollar than the UK can.

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Acknowledgements

Material from the following sources has been adapted for use in this assessment:

Question One

University of Waikato. (2019). *2019 Fieldays in New Zealand: Economic impacts for Waikato region and New Zealand*. https://www.hugheseconomics.com/_files/ugd/8f4bb1_d963cabb753b4d7c8aab6f89908b32fd.pdf

Uys, G. (2022, March 15). *Fieldays' new November date will come with big economic cost*. Stuff. <https://www.stuff.co.nz/business/farming/128046830/fieldays-new-november-date-will-come-with-big-economic-cost>

Ministry of Foreign Affairs and Trade. (2023, March). *Cyclone Gabrielle's impact on the New Zealand economy and exports - March 2023*. <https://www.mfat.govt.nz/en/trade/mfat-market-reports/cyclone-gabrielles-impact-on-the-new-zealand-economy-and-exports-march-2023>. CC-BY-4.0.

Question Three

Stats NZ. (2024, January 24). *Consumers price index: December 2023 quarter*. <https://www.stats.govt.nz/information-releases/consumers-price-index-december-2023-quarter/>. CC-BY-4.0.

Subject: Economics

Standard: 91222

Total score: 10

Q	Grade score	Marker commentary
One	A4	<p>The candidate explained that an increase in visitor numbers will increase AD and therefore the PL, and that increases in costs of production (CoP) decrease AS and therefore the PL.</p> <p>To achieve Merit, there needed to be an explanation of causes of inflation using the AD / AS model with the concept of profit margins and / or the components of AD.</p>
Two	A3	<p>The candidate identified the components of the quantity theory of money (QTOM) and described lower consumer spending as the reason for the drop in velocity of circulation.</p> <p>To achieve Merit, there needed to be a reason for the decrease in consumer spending that decreases velocity of circulation, and the candidate did not use the quantity theory of money equation to explain that a decrease in velocity of circulation would decrease inflation by a proportional amount.</p>
Three	A3	<p>The candidate defined inflation correctly and described the effect of high relative inflation in New Zealand on X and M.</p> <p>To gain Merit, there needed to be an explanation about why minimum wage earners and savers would prefer lower inflation rates with reference to purchasing power.</p>