

# Economics

## Section II (continued)

Marks

### Question 24 (10 marks)

The following information refers to inflation.

The Consumer Price Index (CPI) increased by 0.9 per cent in the December quarter, after rising by 0.3% in the September quarter, to be 3.1% higher over 2001. . . .

However, the outlook for the medium term determinants of inflation has not changed substantially in the light of recent data. Wage and labour cost growth remain contained and are likely to continue to be so given the prevailing weakness in the labour market. The stability of the exchange rate over the past year, combined with downward pressure on world prices from the subdued global economy, suggests that there will be little inflationary pressure from import prices in the medium term.

Adapted from Reserve Bank, *Statement on Monetary Policy*,  
February 2002

*Material used with permission of the Reserve Bank of Australia*

- (a) Define the term *inflation*. 2

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- (b) Outline TWO causes of inflation. 2

One cause of inflation is the decrease of consumer spending or consumption.  
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Question 24 continues on page 16

Question 24 (continued)

- (c) Outline TWO negative effects of inflation on an economy. 2

One negative effect of inflation on an economy is price increases in goods and services.  
Another negative effect is that it causes investment to rise because of the price increase on goods and services this unbalances savings and consumption levels

- (d) Explain TWO government economic policies that could reduce the rate of inflation in an economy. 4

One government economic policy that could reduce the rate of inflation is increase ~~the~~ ~~monetary~~ interest rates.  
This causes people to spend or consume more, which then pushes inflation down.  
Another economic policy which could reduce the rate of inflation is

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**End of Question 24**