

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

Inflation can be defined as an increase in prices due to economic factors such as ~~the~~ economic growth, the exchange rate and demand and supply.

- (b) Outline TWO causes of inflation. 2

• Wage increased cause cost-push inflation which is passed on to the consumer by producers who don't wish to lose profits.

Demand-pull inflation which is where demand outstrips the output capacity of an economy. ie 1000 000 hats are

wanted but only 500 000 can be supplied.

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Question 24 (continued)

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

Inflation increases unemployment.  
This is done or most evident as wages rise and employers cannot afford to employ so many.  
A decrease in the standard of living as things are dearer as well as decrease foreign confidence.

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

Microeconomic reform as it slows down growth and allows for a decrease in unemployment.

**End of Question 24**