MNGT6302
Economics in Management Practice

Session 2, 2015
The UNSW Business School is actively monitoring student learning and quality of the student experience in all its programs. A random selection of completed assessment tasks may be used for quality assurance, such as to determine the extent to which program learning goals are being achieved. The information is required for accreditation purposes, and only aggregated findings will be used to inform changes aimed at improving the quality of UNSW Business School programs. All material used for such processes will be treated as confidential and will not be related to course grades.
Economics in Management Practice

Course Overview

Session 2

2015

We welcome ideas to improve these course materials. Please email suggestions to coursematerials@agsm.edu.au
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# Course calendar

## Session 2, 2015

**MNGT6302 Economics in Management Practice (intensive)**  
**MBA (Executive)**

<table>
<thead>
<tr>
<th>Week no.</th>
<th>Week begins</th>
<th>Activity, dates and units</th>
<th>Assignment due (% weighting)</th>
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<tr>
<td>1</td>
<td>25-May</td>
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<td>2</td>
<td>1-Jun</td>
<td>EMP Intensive Workshop 1</td>
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<td>Saturday 13 June</td>
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<td>UNITS 1 + 2 + 3 + 4</td>
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<td>Sunday 14 June</td>
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<td>UNITS 5 + 6 + 7</td>
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<tr>
<td>3</td>
<td>8-Jun</td>
<td>Online Quiz 1 (7.5%)</td>
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<td>Opens: 10am Saturday 27 June</td>
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<td>Closes: 10pm Monday 29 June</td>
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<td>4</td>
<td>15-Jun</td>
<td>Online Quiz 2 (7.5%)</td>
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<td>Closes: 10pm Monday 13 July</td>
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<td>22-Jun</td>
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<td>(weekend between Weeks 10 &amp; 11)</td>
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<td>Saturday 1 August</td>
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<td>UNIT 8 + 9 + 10 + 11</td>
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<td>UNIT 12 + Workshop</td>
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<td>6</td>
<td>29-Jun</td>
<td>Group Assignment (40%)</td>
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<td>(end of Week 10)</td>
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<td>7</td>
<td>6-Jul</td>
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<td>11</td>
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<td>12</td>
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Course overview

When you think of what an economist does, you probably think about interest rates, unemployment, exchange rates and economic growth. These are indeed things economists are interested in. You probably don’t think though that economists can help you improve your understanding of your day-to-day business. However there are many tools that economists use that can help you improve your decision-making in business. That’s why we’ve called this course *Economics in Management Practice* – it’s all about how using an ‘economic way of thinking’ can help you:

- understand your market;
- make better decisions;
- understand the decisions that others in your market have taken;
- respond to those decisions in the best way possible;
- appraise the economy as a whole; and
- understand how factors in the macroeconomy affect consumers and firms.

Economics is a very wide discipline, so in this course we will concentrate on those aspects that most affect managers. We commence with microeconomics (including supply, demand, market structures and costs) then move into some more contemporary areas of study (including strategic interaction, principal-agent problems and outsourcing). During the last stage of the course we will turn out attention to the economy as a whole – the macroeconomy. Throughout the course we will aim to apply each economic theory that we discuss to real world business situations.

So what is the ‘economic way of thinking’ that we mentioned before? It involves a few key principles – that any decision involves trade-offs (which we refer to as opportunity costs), that individuals make decisions at the margin (they look at the increase in the benefit they receive from consuming or producing one more unit of a good or service), that freely operating markets are the best way to achieve efficient allocation of resources (getting the highest possible level of benefit out of the resources available), and that firms do not operate in isolation (so local, national and international economics can influence and affect them). Another crucial component of the ‘economic way of thinking’ is that we can understand the economic world (both micro and macro) around us more easily if we create economic models of the way that world works – models are just simplifications of the highly complex interactions that take place in real-world economies. These models allow us to study the important aspects of how decisions are made (for example: how much of which goods to consume or produce; which resources or inputs to use; or how to keep an economy on track to meet its long-term and short-term goals) without getting overburdened by too much detail. We cover a general introduction to these topics in Unit 1.
In Units 2 and 3 we apply the core elements of our ‘economic way of thinking’ to the two most fundamental components of market interaction – supply and demand. If you’ve ever heard economists talking about the increase in petrol prices over a holiday weekend, you’ve probably heard them say ‘It’s just a result of the law of supply and demand’. What they are implying is that if the demand for something increases, then in general the price of that good will rise – and since we know that the demand for petrol will rise over a holiday weekend, we should expect the price of petrol to likewise rise. Now looking at a supply, if supply of a good increases then, in general, the price of that good will fall. So if the OPEC nations decide to increase the supply of crude oil to the market, this is likely to lead to a decrease in the price of crude oil, and therefore an eventual decrease in the price of petrol at the bowser.

Since organisations exist in order to transform some type of input into an output (for example turning crude oil into petrol), Unit 4 examines how firms add value through their production process and the relationship between that process and the firm’s costs. The Unit further explores the model of a competitive market in which there are many buyers and sellers. How do firms make a profit in such a competitive market? When should they temporarily shut down and when should they permanently exit this market? What will drive new firms to enter this market? Understanding production, cost and revenue in a competitive market is an important first step in understanding the more complicated market structures that we then consider in Unit 5.

Most markets are not competitive because the firms are able to differentiate themselves from their competition in some way. Unit 5 therefore models a variety of different market structures. At one extreme is the monopoly, where there are still many buyers, but only one seller. Because this seller stands alone, it has significant market power and it is likely to make more profit than if it were operating in competition where many firms would then be supplying comparable goods or services. Unit 5 also considers another type of market structure – monopolistic competition. In this market there are many buyers and many sellers who offer similar, but not identical products. By differentiating their products, sellers can operate like monopolists in the short run to gain additional profits, but their market power is then eroded by the actions of their competitors through time.

In some markets, there is more than one firm, but fewer than many – these markets are called oligopolies. Our usual models of supply and demand won’t help us much when trying to analyse the behaviour of firms in this type of market – we therefore need to develop some other tools to help us.
In this regard, Unit 6 develops an understanding of how game theory can help us analyse markets of strategic interaction in which firms are interdependent (i.e. one firm’s profit depends on the actions of other firms in the market). For example, game theory can help us understand how other firms respond when one firm decreases the price of one of its products and what the consequences of those responses will be for each firm’s profits.

So far, we’ve only talked about things external to the firm. In Unit 7, we develop an understanding of how principal-agent problems (the subject of agency theory) affect the efficiency of outcomes in decision-making. For example, if you hide an illness from your medical insurer, you might be creating a situation of adverse selection or moral hazard, which means that the rate the insurance company charges you may not be as high as it should given your illness. We then go on to explore some of the elements and costs that managers need to consider when determining whether to keep a function inside their firm (i.e. ‘insource’ or ‘make’) or obtain it from market sources (i.e. ‘outsourcing’ or ‘buy’).

At this stage in the course we will turn our attention to the economy as a whole – the big picture! We begin in Unit 8 by explaining what some of the key issues are in the macroeconomy, using terms that you’ve probably heard every day in the news. We describe some of the key measures we use to take the temperature of the economy, such as gross domestic product (GDP) and the consumer price index (CPI). We also define the GDP price deflator, which will help us distinguish between nominal and real GDP growth – the first includes the effects of inflation, the second doesn’t. We then look at long-term goals for the macroeconomy, such as growth and productivity, as well as short-term goals, such as inflation stability and see what the links are between these long-term and short-term aspects.

In Unit 9, we examine savings, investment, the monetary system and inflation. On the first Tuesday of every month when the Reserve Bank Board meets, many mortgage holders wait with baited breath to see whether or not the cash rate will rise, and what proportion of any such rise will be on-charged to borrowers by the retail banks. But why does the Reserve Bank alter the cash rate in the first place and how does altering the cash rate affect the economy as a whole? We look at these important issues and also at how the relationship between money and interest rates can have an effect on the savings, investment, growth and inflation in our nation.

In Unit 10 we consider the international transactions of open economies. Open economies are countries, such as Australia, that interact freely with other countries around the world. An open economy needs to consider not only what occurs within its own shores but also elements such as the effects of exports, imports, capital flows and exchange rates.
In Unit 11 we develop the last of our economic models – the aggregate supply and aggregate demand model. We use this model to study short run fluctuations in the economy – what is often referred to as the Business Cycle. When considering this Business Cycle we will also need to investigate and discuss the impact of both monetary policy (enacted by the Reserve Bank) and fiscal policy (enacted by Government) on the macroeconomy.

To finish the course, Unit 12 provides an opportunity to review the material and test your knowledge as part of your preparation for the final exam. The EMP Facilitators trust that you will find the 'economic way of thinking' to be a very useful addition to your managers’ toolbox. We hope you enjoy our course.

**MBA Program Learning Goals**

The Course Learning Outcomes are what you should be able to DO by the end of this course if you participate fully in learning activities and successfully complete the assessment items.

The Learning Outcomes in this course also help you to achieve some of the overall Program Learning Goals and Outcomes for all postgraduate coursework students in the UNSW Business School. Program Learning Goals are what we want you to BE or HAVE by the time you successfully complete your degree (e.g. ‘be an effective team player’). You demonstrate this by achieving specific Program Learning Outcomes – what you are able to DO by the end of your degree (e.g. ‘participate collaboratively and responsibly in teams’).

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**MBA Program Learning Goals and Outcomes**

**Learning Goal 1: Business Management Knowledge**

Students should be able to identify and apply current knowledge of disciplinary and interdisciplinary theory and professional practice to general management and business within diverse situations

**Learning Goal 2: Critical Thinking**

Students should understand and be able to identify, research and analyse complex issues and problems in business and develop appropriate solutions

**Learning Goal 3: Communication**

Students should be able to produce written documents and oral presentations that communicate effectively complex disciplinary ideas and information for the intended audience and purpose

*continued…*
Learning Goal 4: Teamwork
Students should be able to participate collaboratively and responsibly in teams and to reflect upon their own contribution to the team and on the necessary processes and knowledge within the team to achieve specified outcomes

Learning Goal 5: Responsible Business
Students should be able to appraise ethical, environmental and sustainability considerations in decision making and in practice in business
Students should be able to consider the social and cultural implications of management practices and of business activities

Learning Goal 6: Leadership
Students should be able to reflect upon their own personal leadership style and the leadership needs of business and of teams

Learning Goal 7: International Perspective
Students should understand the needs of undertaking business within a global context
Students should be able to apply business management knowledge to business situations within global markets with due recognition for differences in cultural, legal, commercial and other issues

Learning Goal 8: Risk Management
Students should be able to demonstrate an understanding of the limits in precision and the risks associated with business models
Students should be able to appraise risk and to develop risk mitigation strategies applicable to business undertaken within uncertain and volatile environments
Course overview

Course communication

Course website

The *Economics in Management Practice* course website uses the UNSW eLearning platform called Moodle. It provides you with access to electronic resources including:
- the course notes;
- the textbook;
- additional information of interest to students, and
- the assessment details and the online quizzes.

To access the course website:

1. go to the UNSW eLearning platform and login using your zNumber as your User ID (see next section) and your zPass as your password; then
2. select the MGNT6302-Economics in Management Practice course.

zNumber and zPass

Your zNumber is your 7-digit UNSW student number with a ‘z’ in front. If your student number is 1234567 then your zNumber is z1234567.

Your zPass is the password that you use to access UNSW online services. If you are a new student then you can obtain a password by visiting the UNSW Identity Manager website: [https://idm.unsw.edu.au](https://idm.unsw.edu.au) and then selecting the ‘New User – Click HERE’ link. If you have forgotten your password then enter your zNumber and then click ‘Forgot Password?’.

Troubleshooting access to the Course Website

If you have difficulties accessing the Course Website then this may be due to either a problem at your end (with your computer, your connection, or the type of browser you are using) or a problem with the eLearning system itself. If you do experience problems accessing the website then we suggest that you try the following:

1. Check your email for any messages from the course coordinator or UNSW IT about the course website experiencing technical difficulties.
2. Determine if the problem is with your computer. Access the website from a different device at your location (such as a phone or a different computer). If the problem is with your computer, then try rebooting it. If that fails, then try clearing your browser’s cache and clear cookies (if you don’t know how to do this then type the name of your browser into a search engine with the phrase “how to clear cache and cookies”). If that fails, then try using a different internet browser.
3. If there is no problem with your computer, determine if the problem is with a firewall or your broadband connection. Try accessing the website from a device that uses a different internet connection, such as a smartphone that accesses the internet via 3G or from a home computer (if you are attempting to access the website from work).

4. If the problem is not with your connection, determine if the problem is with the web Single-Sign-On (wSSO) process that logs you onto the course website. Clear all your browser cache and cookies and try to login again.

5. If the problem appears to be with the eLearning system, try waiting one hour to see if the problem is just a short-term issue that UNSW IT are able to resolve quickly.

6. If you have done all of the above (and also waited one hour), and have not received any email notifications of a technical difficulty with the course website, then please contact IT Support at one of the contacts listed below.

Course email

The course coordinator and your facilitator may send announcements and materials to your student email address (z…….@student.unsw.edu.au). You are responsible for making sure that you have set up your student email address correctly, including the forwarding of messages to an active personal or work email address if you so require. You can do this as follows:

1. go to https://idm.unsw.edu.au
2. enter your zNumber and zPass and press ‘Login’
3. under the ‘UNSW Email’ section, add your personal or work email to the ‘Emails to this account are currently being delivered to’.

Some students prefer to set up a Gmail account at www.gmail.com to use as a repository for all of their student emails since they are free and also have generous storage limits. Emails in Gmail accounts can also be downloaded into an email client (such as Microsoft Outlook), can be viewed using a standard internet browser and can also be easily viewed on smartphones.
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IT support contact details
For support during office hours, contact the AGSM eLearning Coordinator:
Tel: +61 2 9931 9541
Email: elearning@agsm.edu.au

For after-hours support, contact the UNSW IT Service Centre:
Tel: +61 2 9385 1333
Email: itservicecentre@unsw.edu.au

Hours of operation:
Mon–Fri: 8am – 9am; 5pm – 8pm
Sat–Sun: 11am – 2pm

AGSM MBA Programs contact details

Student Experience
If you have any administrative queries, they should be addressed to:

Student Experience
AGSM MBA Programs
UNSW Business School
UNSW SYDNEY NSW 2052
Tel: +61 2 9931 9400
Fax: +61 2 9931 9205
email: studentexperience@agsm.edu.au
Learning resources

We have put together several resources to help you improve your understanding of economic concepts and gain the ‘economic way of thinking’. Your basic resource for Units 1 to 7 will be the Course Notes that have been written specifically for Economics in Management Practice at the AGSM. Your resources for Units 8 to 11 will be your textbook Principles of Macroeconomics (5th Edition) by Gans, King, Stonecash and Mankiw. Please note that any reference in these Course Notes to a textbook chapter, page and/or exercise will align with the 5th Edition of the textbook.

You will find several exercises and answers within each unit. There are also questions and problems at the end of each chapter of the text. Some of these questions have been transformed into exercises within the unit, but you may still wish to expand your understanding by attempting some of the other questions and problems in the text as well.

We have additional readings in some units that are designed to either deepen your understanding of the concepts, or show you some practical applications of the concepts. Your instructor might also provide you with readings from time-to-time from the press of the day – one of the good things about economics is that it’s in the news almost every day!

Some additional learning resources that you have to assist you in your study of Economics in Management Practice include:

- the two intensive weekend workshop sessions;
- sources of economic information in the media;
- the AGSM website and Internet references for background information; and
- your fellow class members and your personal network.

Equipment you will need

A calculator is required for this course. A standard scientific calculator available from most newsagents and bookshops should be more than adequate for the level of computations that you will encounter in this course.

It is advisable for you to have some skills in using spreadsheets such as Microsoft Excel. The course website includes some links to resources that can help improve these skills.
Algebra and Graphs

This course assumes familiarity with high-school level algebra and graphing skills. If you have rarely used algebra or graphs since high school, then you may need to review some mathematical concepts. The course website includes some links to resources that can help you improve these skills.

The main skills of algebra that you require in this course include being able to simplify equations, rearrange equations, and solve equations individually and simultaneously. The main skills of graphing that you require in this course include being able to sketch a representation of a mathematical situation, precisely graph mathematical equations, and understand/analyse points of intersection and areas on a graph.

Additional student resources and support

The University and the UNSW Business School provide a wide range of support services for students, including:

- Education Development Unit (EDU) (https://www.business.unsw.edu.au/students/resources/learning-support/consultations)
  Academic writing, study skills and maths support specifically for UNSW Business School, AGSM and MBT students. Services include workshops, online and printed resources, and individual consultations.
  EDU Office: Level 1, Quadrangle Building; Ph: +61 2 9385 5584; Email: edu@unsw.edu.au

- UNSW Learning Centre (www.lc.unsw.edu.au)
  Academic skills support services, including workshops and resources, for all UNSW students. See website for details.

- Library training and search support services
  http://info.library.unsw.edu.au

- UNSW IT Service Desk
  Technical support for problems logging in to websites, downloading documents etc. Library, Level 2; Ph: 9385 1333.
  Website www.its.unsw.edu.au/support/support_home.html

- UNSW Counselling Service (www.counselling.unsw.edu.au)
  Free, confidential service for problems of a personal or academic nature; and workshops on study issues such as ‘Coping With Stress’ and ‘Procrastination’.
  Office: Level 2, Quadrangle East Wing; Ph: +61 2 9385 5418
- **Student Equity & Disabilities Unit**  
  ([http://www.studentequity.unsw.edu.au](http://www.studentequity.unsw.edu.au)) Advice regarding equity and diversity issues, and support for students who have a disability or disadvantage that interferes with their learning.  
  Office: Ground Floor, John Goodsell Building;  
  Ph: +61 2 9385 4734

### Reading list

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<td>10</td>
<td>Chapter 14</td>
<td>Open-economy macroeconomics: Basic concepts</td>
</tr>
<tr>
<td></td>
<td>Chapter 15</td>
<td>A macroeconomic theory of the open economy</td>
</tr>
<tr>
<td>11</td>
<td>Chapter 16</td>
<td>Aggregate demand and aggregate supply</td>
</tr>
<tr>
<td></td>
<td>Chapter 17</td>
<td>The influence of monetary policy and fiscal policy on aggregate demand</td>
</tr>
<tr>
<td>12</td>
<td></td>
<td>Review</td>
</tr>
</tbody>
</table>
Assessment

Summary of requirements

In order to pass this course, you must:

- achieve an aggregate (overall) mark of at least 50%; and
- studiously undertake each piece of assessment.

Assessment 1: Online Quiz 1
Opens: 10am Saturday, 27 June 2015
Closes: 10pm Monday, 29 June 2015
Weight: 7.5%
Assesses: Units 1 to 3 inclusive
Location: Course website
Details: See below

Assessment 2: Online Quiz 2
Opens: 10am Saturday, 11 July 2015
Closes: 10pm Monday, 13 July 2015
Weight: 7.5%
Assesses: Units 4 to 6 inclusive (but may also require knowledge of earlier Units)
Location: Course website
Details: See below

Assessment 3: Group assignment
Due: 9.30am Saturday, 1 August 2015
Weight: 40%
Assesses: Units 1 to 7 inclusive
Details: See below

Assessment 4: Final exam
Date: Saturday, 22 August 2015
Weight: 45%
Assesses: Full course content
Duration: Two (2) hours
Online Quizzes 1 and 2

NOTE – all times referred to herein are AEST (Sydney).

Online Quiz 1: Assesses Units 1 to 3 inclusive.
Quiz link will open on the Course Website at 10am Saturday 27 June 2015 and will close at 10pm Monday 29 June 2015 (i.e. a 60 hour window of opportunity within which to select your preferred 3 hour period to sit the quiz).

Online Quiz 2: Assesses Units 4 to 6 inclusive (but may also require knowledge of earlier Units).
Quiz link will open on the Course Website at 10am Saturday 11 July 2015 and will close at 10pm Monday 13 July 2015 (i.e. a 60 hour window of opportunity within which to select your preferred 3 hour period to sit the quiz).

Weight: 7.5% of your overall EMP grade for each quiz (i.e. 15% in total).

Duration: Maximum of three (3) hours each quiz (see below for more details).

Format: Each quiz consists of one academic conduct declaration (not graded) and 15 randomly-selected questions (worth 1 mark each, or 0.5% of your overall EMP grade each). Questions might be in a multiple-choice format or require you to type in a numerical value after making some separate calculation(s). Each multiple choice question will have four possible solutions; and while more than one answer may be partly correct, you are required to select the single most correct answer. For questions requiring you to type in a numerical value, those numerical values will be allowed to vary from the precise answer by only a small percentage to account for rounding errors where appropriate. Negative marks will not be allocated for incorrect answers.

The objective of each online quiz is to assess whether you have achieved the learning objectives in the corresponding units and to provide you with a timely understanding of your progress in the EMP course.
You are strongly advised to attempt all Unit Exercises, Class Discussion Questions and Quick Quiz questions from each relevant Unit in your Course Notes before attempting the online quizzes. For your information the Quick Quiz questions are indicative of the type of online quiz questions that you may encounter, however they are still only a small sample set of possible questions.

You must complete each online quiz on the Course Website, moreover:

- You must complete each quiz as an individual. The quizzes are open book. When answering the questions in the quizzes you are permitted to refer to your Course Notes, lecture slides and any other official material provided by the AGSM.
- The quiz questions will range from relatively simple questions to quite challenging questions in order to assess where you sit on the full spectrum of possible understanding.
- The link to each quiz will only be available between the specified open and close dates and times as listed above. It is your responsibility to make sure that you allocate sufficient time to perform each quiz and submit your answers before the specified close date and time.
- You can commence each quiz at any time during the 60 hour window of opportunity between the open and close dates and times, however you must note that:
  - You can only access each quiz once, therefore you must commence and finish each quiz within a single continuous online session which will be limited to 3 hours duration.
  - Your 3 hour limit will commence as soon as you agree to access the quiz. The Course Website will then provide you with a visual progressive timer to indicate your time remaining.
  - Once you answer all the questions in a quiz you must submit your answers for grading. The Course Website will then automatically grade your submitted answers. If you have not submitted your answers before your 3 hour time limit expires, the Course Website will automatically grade those questions that you have attempted as at the end of your 3 hour limit.
  - If you access a quiz when less than three hours remains before the quiz close date and time, then the time available for you to complete the quiz will be shortened to only that time remaining. The visual progressive timer provided on the Course Webpage will not necessarily indicate this fact. Furthermore, if you have not submitted your answers before the quiz close date and time, the Course Website will automatically grade those questions that you have attempted as at the quiz close date and time.
During your 3 hour time limit you can return to any question and change your answer to that question if you so wish, however once you have submitted your quiz for grading it cannot be unsubmitted.

After you have submitted your quiz for grading you will be able to see your score (out of a possible 15). Then you will be able to use the “review” option to see some feedback on your attempt at the quiz.

Supplementary quizzes will not be made available to any student. If you are travelling during the time that a particular online quiz is open, then you are responsible for arranging access to the Internet so that you can complete the online quiz by the specified close date and time.

It should be noted that a list of recommended Internet browsers for use with the UNSW eLearning Website (through which the Course Website is presented) may be obtained from UNSW. Moreover the eLearning Website may be unreliable or inaccessible from some places due to firewall or other technical restrictions. UNSW also undertakes administration of the eLearning Website from time to time. If UNSW does schedule maintenance of the eLearning Website that affects the Course Website during an online quiz period for longer than 24 hours, then the Course coordinator may grant an extension to all students. The details of any such extension will be provided by email to your student email address. If the Course Website is affected for a period of less than 24 hours then it is unlikely that an extension will be granted.

Computer unavailability or difficulties will NOT be accepted as a viable excuse for non-submission or incorrect submission of any online quiz.

IMPORTANT - ACADEMIC MISCONDUCT:

You must:

- NOT collaborate in any way with anyone else in relation to any online quiz;
- NOT use any material that may have been supplied (other than officially by the AGSM) to you or to any other person in relation to a current or past online quiz;
- NOT discuss any online quiz question, answer or feedback with anyone else;
- NOT allow any other person to see or be informed of your online quiz questions, answers or feedback;
• NOT record, copy (including by taking screen shots), print or reproduce any online quiz question(s), answer(s), or feedback, in any way, shape or form; and

• NOT post or place any quiz question(s), answer(s), or feedback in any forum or any other privately or publically available location.

Violation of any of the aforementioned actions will constitute Academic Misconduct (and in some cases also a breach of copyright). This will not be tolerated and disciplinary action will be taken against you.

**Group Assignment**

**Due:** Assignments to be submitted on Moodle.

9.30am Saturday, 1 August 2015

**Weight:** 40%

**Assesses:** Units 1 to 7 inclusive

**Group Work:** Assignments should be completed in groups of between 3 and 5 students. A group may only be formed between students who have the same facilitator. You are responsible for the selection of your group members.

**Question:** The question will be posted onto the Course Website early in the session.

**Length:** 8 pages (all inclusive, except for the list of References).

**Formatting:** You should follow the standard AGSM assignment formatting requirements:

2. Select ‘Current Students’ from top menu.
3. Select ‘Academic information’ from left menu.
4. Select ‘Assessments & examinations’.
5. Navigate to ‘Document formatting requirements’.
**Group work**

We encourage group work as we believe that you will gain by discussing the topics covered in this course with a diverse group of people. Group work is also important for developing personal networks. We suggest your group contain the maximum allowable number of members.

You might like to consider the following in relation to group work:

- Your group will benefit from a high level of diversity. You are encouraged to form groups with a broad range of skills covering quantitative and Excel skills, writing and editing skills and project management and leadership skills. You should also try to form groups that cover diverse industry groups and cultural backgrounds.

- You should consider appointing a leader for the group who will adopt a ‘consultative’ style. Avoid appointing a leader who is only able to exercise an ‘autocratic’ leadership style. In the past, students have found also that groups who attempt to make every decision ‘democratically’ without a clear leader incur undue influence costs.

- Avoid splitting up individual parts of the assignment to each group member. A better approach is for each member to individually prepare a ‘rough draft’ for the assignment in a bullet-point or outline format. You can then compare the different approaches to reduce ‘Group Think’ and draw from the diversity of experience and knowledge in your group. You can then decide how best to develop the draft answers into a more comprehensive final version.

- You should consider developing a clear plan for the assignment that includes tasks, responsibilities and milestones. Aim to complete the assignment well in advance of the due date to avoid a last-minute rush. You are studying an MBA and so it is expected that you can manage your time effectively.

- If you commit to your group members to a deadline for a particular task, then it is expected that you deliver quality work on schedule. Everyone is busy with work and family commitments.

- Avoid long meetings on weekends. If you circulate drafts before meetings by email, then meetings can be used to discuss these drafts and decide on appropriate courses of action. Meetings should generally be less than one hour in duration.

- Think creatively about ways to make the group meetings enjoyable. Choice of location and some nice food can make a real difference.
Group Assignment - Assessment criteria

The Group Assignment will be graded in accordance with Standards-based guideline shown below.

<table>
<thead>
<tr>
<th>Criteria</th>
<th>'HD' &amp; 'DN' range</th>
<th>'CR' range</th>
<th>'PS' range</th>
<th>'FL' range</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Presentation &amp; Style</strong></td>
<td>Assessment is presented in exactly the stipulated format.</td>
<td>Assessment is presented with slight deviations from the stipulated format.</td>
<td>Assessment is presented with noticeable deviations from the stipulated format.</td>
<td>Assessment is presented with significant deviations from the stipulated format.</td>
</tr>
<tr>
<td>CONFORMING WITH INSTRUCTIONS [also refer to Note 1]</td>
<td>Fluent writing style that presents and analyses ideas concisely and effectively in a structured manner. Language is very clear and the meaning is easily apparent. Correct grammar, spelling and punctuation.</td>
<td>Mostly fluent writing style that presents and analyses ideas concisely and effectively but in a less structured manner. Language is clear and the meaning is generally apparent throughout. Grammar, spelling and/or punctuation have minor shortfalls.</td>
<td>Generally fluent writing style that presents and analyses ideas less concisely or less effectively and in a less structured manner. Language is sometimes unclear and the meaning is sometimes not apparent. Grammar, spelling and/or punctuation have shortfalls.</td>
<td>Writing style is not fluent or does not present or analyse ideas concisely and effectively. The text is unstructured. Language is quite unclear and the meaning is often hard to determine. Noticeable shortfalls in grammar, spelling and/or punctuation. The document lacks attention to detail.</td>
</tr>
<tr>
<td>CLARITY OF EXPRESSION (including spelling, grammar, punctuation)</td>
<td>Referring is both correct and complete.</td>
<td>Referring is generally correct and complete.</td>
<td>Referring has some shortfalls in either correctness or completeness.</td>
<td>Referring is absent or of a poor standard.</td>
</tr>
<tr>
<td>REFERENCING</td>
<td>The whole assessment presents strongly as coherent and coordinated piece of work. There is no evidence of, say, some group members doing just one part of the assignment and not assisting with any other part.</td>
<td>The assessment presents as coherent and coordinated piece of work, but with some shortfalls. For example the answers to different parts may have a different 'tone &amp; feel' indicating work splitting across the group.</td>
<td>The assessment presents as somewhat coherent and coordinated but has some noticeable lapses. For example there may be a disjointed style throughout the documents arising from students 'cutting &amp; pasting' individual pieces of work into one document.</td>
<td>The assessment presents as a non-coherent document. It appears to be an uncoordinated 'cut &amp; paste' of paragraphs written by several authors.</td>
</tr>
<tr>
<td>GROUP EFFORT</td>
<td>The assessment presents as coherent and coordinated piece of work, but with some shortfalls. For example the answers to different parts may have a different 'tone &amp; feel' indicating work splitting across the group.</td>
<td>The assessment presents as somewhat coherent and coordinated but has some noticeable lapses. For example there may be a disjointed style throughout the documents arising from students 'cutting &amp; pasting' individual pieces of work into one document.</td>
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<tr>
<td>Criteria</td>
<td>‘HD’ &amp; ‘DN’ range</td>
<td>‘CR’ range</td>
<td>‘PS’ range</td>
<td>‘FL’ range</td>
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<tr>
<td>----------</td>
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<td>------------</td>
</tr>
<tr>
<td><strong>RANGE AND UNDERSTANDING</strong></td>
<td>Comprehensive understanding of the depth, width and breadth of the topic and the theory through which to analyse it. Shows evidence of solid appropriate research. Appraises a full set of different options, has significant original content, is lateral and adopts a wide array of perspectives.</td>
<td>Sound understanding of the depth, width and breadth of the topic and the theory through which to analyse it. Shows evidence of some appropriate research. Appraises different options, has original content, is somewhat lateral and adopts a good variety of perspectives.</td>
<td>Limited understanding of the depth, width and breadth of the topic or the theory through which to analyse it. Relies on only information that is easily obtained. Appraises only a few different options and is uninspiring in regard to original content and lateral thought. Adopts a limited variety of perspectives.</td>
<td>Lacks understanding of the topic or the theory through which to analyse it. Conducts no research or uses of irrelevant information sources. Appraises only the most obvious options. Has very little lateral or original content. Adopts the most basic perspective.</td>
</tr>
<tr>
<td><strong>ECONOMIC WAY OF THINKING</strong></td>
<td>Consistently demonstrates application of critical reasoning and the ‘economic way of thinking’.</td>
<td>Demonstrates good application of critical reasoning and the ‘economic way of thinking’.</td>
<td>Demonstrates some application of critical reasoning and the ‘economic way of thinking’.</td>
<td>Does not demonstrate application of critical reasoning, nor display an ‘economic way of thinking’.</td>
</tr>
<tr>
<td><strong>APPRAISING AND ANSWERING THE QUESTION THROUGH AN ANALYTICAL APPROACH</strong></td>
<td>Displays a high level of logical analysis. Does not simply ‘describe facts’, but rather is ‘analytical’ in approach. Convinces the reader of the point at hand. Answers the question fully. Debates points very well and with confidence. Draws well supported conclusions (i.e. demonstrates reasons for final decision).</td>
<td>Displays a good level of logical analysis. Is sometimes ‘descriptive’ rather than being ‘analytical’ in approach. Answers the question well. Good debate of points is evident. Draws conclusions and provides some support to those conclusions (i.e. shows that selection of final decision follows from the analysis).</td>
<td>Displays a basic level of logical analysis. Is quite ‘descriptive’ rather than being ‘analytical’ in approach. Tells the reader a ‘story’ instead of convincing the reader with a line of argument. Answers the question simplistically. Relatively weak debate of points. Draws only obvious conclusions (i.e. presents benefits and disadvantages but does not clearly reason the final conclusion).</td>
<td>Displays illogical analysis. Presents a standard ‘book review’ and does not offer analysis. Does not answer the question. Does not debate points. Either draws unsupported conclusions (i.e. little or no explanation of how the final conclusion was reached), or draws no conclusions at all.</td>
</tr>
</tbody>
</table>

**Note 1:** Late submissions will be penalised 5% per day or part thereof. If the page limit is exceeded then the piece of work shall be assessed from the first page up to and including the page on which the page limit is reached. Pages beyond the page limit will not be read by the marker.
Assessment 3: Final Exam

Date: Saturday, 22 August 2015
Weight: 45%
Duration: 2 hours (plus 10 minutes reading time)
Assesses: Full course content

The objective of the final exam is to test the extent to which you have achieved the learning objectives of the course. For this reason the final exam will cover material from the entire course.

The final exam will consist of 2 sections:

Section A (worth 5% of your overall EMP grade) = 10 multiple-choice questions.

Section B (worth 40% of your overall EMP grade) = 4 short-answer questions with multiple parts. Some parts may be unrelated to each other. Some parts may be of a qualitative nature and others may be quantitative.

The final examination is open book. You may also bring in printed course materials and handwritten notes and unit summaries. In the exam you will additionally be allowed to use electronic devices for the purpose of referring to your digital course materials and notes only. These devices must not be connected to the internet, Wi-Fi must be disabled and tablets must be in flight mode. They must not be used to type your exam responses. However you should note that it is unlikely that you will have time to make extensive use of your course materials during the examination.

Some hints on the content of the final examination include:
• the majority of questions will focus on assessing important concepts from the relevant units rather than trivial details;
• the questions will follow an ‘audit’ style that involves testing a few concepts in depth rather than trying to assess everything covered in the course;
• the questions may combine and overlay economic concepts and seek comment on the application of those multiple concepts in a business context; and
because this is an open book exam at Masters level, do not expect any exam question to simply mimic any of the sample questions that have been provided to you throughout the course. Students should note that those questions are generally of a simpler nature than the questions that will arise in the exam – this is because the questions provided throughout the course have been designed to help you 'learn and confirm' your knowledge of individual economic concepts, while exam questions are designed to 'test' your knowledge. Exam questions may therefore combine and overlay several economic concepts and also seek comment on the application of those multiple concepts in a business context. Exam questions will be necessarily unique and challenging; so when answering them you must be ready to think on your feet.

Some hints on answering the final examination include:

- You should write your answers in a clear, logical and legible manner providing well-rounded and justifiable answers with an appropriate level of working and depth according to the marks allocated to the question. For short-answer questions, please mark the final answer clearly by underlining or highlighting it. For written questions, please note that they are marked based on the quality of the answer. Including a large quantity of largely irrelevant material in your answer may attract a penalty.
- ensure you answer the question that is actually being asked;
- ensure you answer the entire question; and
- to achieve the above, many students have benefited from reading the question carefully several times, then thinking about what the answer entails, then determining the best structure in which to present that answer, and only then have they commenced writing that answer.

Some hints for preparing for the final examination include:

- make a summary for each unit focusing on the most important concepts, diagrams and/or equations;
- work through the examples, exercises, discussion questions and quick quizzes in each unit to check and reinforce your understanding of the important concepts; and
- make sure that you can comfortably and accurately complete the sample questions provided in Unit 12 and the sample exam.
Acknowledgements

Course coordinator

Scott Muller

Scott has been associated with the AGSM since 1996. He facilitates several courses on the MBA (Executive) Program, including: Economics in Management Practice and Corporate Finance. Scott also teaches on the full-time MBA Program and in Hong Kong; most notably presenting his specialist elective course, Quantitative Business Modelling, that concentrates on the practical application of forecasting, optimisation and simulation techniques in business and finance.

Scott holds an Undergraduate Degree in Mechanical Engineering from the University of New South Wales, a Masters Degree in Science from the University of Plymouth (UK) and is a graduate of the full-time AGSM MBA Program. His PhD studies centred on the economics of large-scale commercial contracts and the associated application of game theory and auction theory.

Scott worked for several years as a mechanical engineer and senior manager in the maritime industry throughout Australia and South East Asia. He has held two diplomatic positions overseas with the Australian Government (Papua New Guinea & United Kingdom) and he has been the lead negotiator on many large commercial arrangements forged between various private and publically-listed global firms. Over the past 10 years Scott has held senior executive positions within the Banking and Finance sector and is now the Managing Director of a specialist consultancy that services a diverse range of corporations and industries across Asia.

Additional Course Writers

Robin Stonecash, Andrew Hingston
Appendix

Appendix 1  Sample Exam with suggested solutions
Appendix 1

Sample Exam with suggested solutions
This sample exam consists of two (2) Sections and is of two (2) hour duration.

**Section A**
- Consists of 10 multiple-choice questions.
- You are required to answer all questions and each question is of equal value.
- In the actual exam you will be provided with a **multiple-choice answer sheet** and you must answer all multiple-choice questions on that sheet only. For each question, circle the letter corresponding to the answer you believe is most appropriate.

**Section B**
- Consists of 4 short-answer questions, each with sub-parts that may or may not be related.
- You are required to answer all questions and each question is of equal value, however the sub-parts within a question may be of different values. The values of the sub-parts will be indicated in brackets at the end of each sub-part. The values of the sub-parts are indicative of the effort required to answer those sub-parts fully.
- In the actual exam you will be provided with four booklets and you must answer each question from Section B in a separate booklet. Moreover, you should give as full answers as possible to each question and sub-part. Ensure you clearly state and explain any assumptions on which your answers rely and show all your working for any numerical calculations (i.e. if you demonstrate you have a correct solution process to a problem, even if your final numerical result is incorrect you may receive partial marks).

**Section A - Multiple-Choice Questions**

**Question A1**
An economy is ‘efficient’ when it
a. uses its resources so as to maximise the satisfaction of wants
b. develops industries to the point of being independent of foreign suppliers
c. adopts the latest techniques in all lines of production
d. operates at a level of full employment

**Question A2**
Which of the following constitute real investment?
a. purchase of shares through the stock exchange
b. the buying of a factory completed last year
c. the building of a block of apartments
d. all of the above
Question A3
Which of the following would you regard as the best measure of change in a country’s standard of living?

a. Changes in total real income  
b. Changes in total consumers’ expenditure  
c. Changes in consumption of goods and services per head  
d. Changes in private sector expenditure per head

Question A4
A profit-maximising firm’s average total cost is minimized at 100,000 units of output. The firm has a U-shaped average cost curve. If the firm is observed to have a long-run equilibrium output of 85,000 units then it is most likely to be:

a. experiencing diseconomies of scale  
b. minimising its costs  
c. operating under monopolistic competition  
d. all of the above

Question A5
Consider this supply and demand diagram for a good in a perfectly competitive market:

A universal increase in production costs for all manufacturers of this good will cause

a. a move along the supply curve to reflect the higher cost of production  
b. a shift of the supply curve to the right to reflect the higher cost of production  
c. a percentage decrease in quantity demanded that is less than the percentage increase in equilibrium price  
d. a percentage decrease in quantity demanded that is greater than the percentage increase in equilibrium price

Question A6
Consider the following figures from an open economy’s national accounts:

<table>
<thead>
<tr>
<th></th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Exports</td>
<td>$20,000</td>
</tr>
<tr>
<td>Net Transfers</td>
<td>$6,000</td>
</tr>
<tr>
<td>Income earned from foreign-based assets</td>
<td>$1,500</td>
</tr>
<tr>
<td>Payments to foreigners owning internal assets</td>
<td>$1,000</td>
</tr>
<tr>
<td>Capital depreciation for the year</td>
<td>$2,500</td>
</tr>
</tbody>
</table>
Net Foreign Investment equals
a. $27,500
b. $26,500
c. $25,000
d. none of the above

Question A7
Consider the following data:

<table>
<thead>
<tr>
<th>Measure</th>
<th>Year X</th>
<th>Year Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>National Income</td>
<td>$80,000m</td>
<td>$120,000m</td>
</tr>
<tr>
<td>Retail Price Index</td>
<td>100</td>
<td>150</td>
</tr>
<tr>
<td>Population</td>
<td>40m</td>
<td>60m</td>
</tr>
</tbody>
</table>

In comparison to Year X, in Year Y the above country
a. enjoyed a higher standard of living
b. had a lower real national income
c. was just as well off
d. none of the above

Question A8
Consider the following two statements:

S1. Measurement of national income at constant prices indicates trends in real national income
S2. The constant price technique eliminates fluctuations in national income caused by changes in the value of money

a. S1 is correct AND S2 is correct AND S2 is a correct explanation of S1
b. S1 is correct AND S2 is correct BUT S2 is not a correct explanation of S1
c. S1 is correct AND S2 is incorrect
d. S1 is incorrect AND S2 is correct

Question A9
A poor country may find it more difficult than a rich country to achieve economic growth
a. because it has a smaller average propensity to save
b. because it has a lower capital to output ratio
c. because it has a weaker trade balance
d. because it has more idle resources

Question A10
Consider the following two statements:

S1. If purchasing-power parity holds, then the real exchange rate will equal unity
S2. Purchasing-power parity describes the force that should determine exchange rates in the long run

a. Only S1 is correct
b. Only S2 is correct
c. Both S1 and S2 are correct
d. Neither S1 nor S2 are correct
Section B - Short-Answer Questions

Sample Question B1
A competitive market is represented by the following equations (where P is the price per tonne, and Q is quantity in thousands of tonnes):

Demand: \( Q_D = 1000 - 2.5P \)
Supply: \( Q_S = 1.67P - 366.67 \)

1. If there are 20 identical firms supplying to this market, what price will prevail and what quantity will each firm produce? [4 marks]

2. Suppose an increase in fuel prices increases production costs. The supply curve shifts and the relative elasticity of supply also alters as reflected in the new supply curve, namely: \( P = 0.8Q_S + 250 \)
   Calculate the own-price elasticity of demand across the arc of the demand curve that lies between the new and old equilibrium positions. [6 marks]

Sample Question B2
1. Explain what will happen to the money supply if the public alters its habits and, instead of using credit to purchase items, it reverts to using cash [2 marks]

2. Describe four separate conditions that might occur in Australia to lead the RBA to increase the overnight cash rate. [2 marks]

3. Suppose an increase in the Australian overnight cash rate pushes the Australian interest rates above those of the US. What would happen to the value of the Australian dollar vis-à-vis the US dollar? Explain what you think will be the impact on Australian GDP? [6 marks]

Sample Question B3
1. Use the Aggregate Supply / Aggregate Demand model to explain the effects of an increase in world crude oil prices under the combined assumptions that long-run aggregate supply remains unchanged and no reaction is undertaken by Australian policy makers (i.e. neither the government nor the RBA initiate their policy instruments in response to the increase in world crude oil prices). [3 marks]

2. If a Government were to borrow more money next year than this year, explain how the elasticity of supply and also the elasticity of demand in the market for loanable funds would each govern the relative resultant interest rate movement. [4 marks]
3. On the steps of Parliament House in the country of Twolandia, the Treasurer stated:

“As you are aware, we recently returned this nation’s second consecutive budget surplus. This again shows how Mrs Whatsit and her Government have turned around the mess left by our predecessors. We are now internally discussing how best to use that surplus for the benefit of the nation. We are considering the retirement of some national debt”

In the context of dispersing a budget surplus and considering the effect on the market for loanable funds, evaluate the pros and cons of the Government’s plan to retire some national debt.

[3 marks]

Sample Question B4

In Papua New Guinea (PNG) two firms. ‘Kirupim’ and ‘Lokim’, dominate the market for outbound expatriate relocation services. After converting from Kina (the PNG currency) to dollars, the total annual revenue available in this market is estimated to be $1million. The two competitors relocate expatriate’s household effects from PNG to the expatriate’s native country at the end of the expatriate’s contracted term. They offer an end-to-end service; whereby the firm packs the household effects into crates then stores the crates in warehouses until either a berth on a ship, or space on an aeroplane becomes available. Only 20% of expatriates chose to relocate their household effects by air.

Kirupim has warehouse leasing costs that are, on average, 18% lower than Lokim. Moreover, each firm is now considering whether or not to undertake an annual advertising campaign costing $200,000. If neither firm chooses to advertise, then the current market share regime of a 50:50 split would remain, however, if one firm advertises and the other does not, then the firm advertising is expected to capture at least 80% of the market. If both firms advertise then their efforts effectively nullify each other and the market share split would stay as it is today.

1. Construct a payoff matrix for this game when the two firms make advertising decisions simultaneously. Clearly explain what ‘payoffs’ you use and why you consider them to be appropriate. What is/are the Nash Equilibrium of the simultaneous-move game? State the assumptions you have applied in your analysis and discuss the effect of relaxing those assumptions.  

5 marks

2. The Managing Director of Kirupim has suggested that Kirupim should purchase the sole Advertising firm in PNG in order to gain a competitive advantage. He has stated that this will allow Kirupim access to cheaper advertising, whilst also effectively barring Lokim from advertising. Using economics, how would you advise the Managing Director of Kirupim with respect to this course of action? Fully explain your reasoning.

5 marks

- End of Paper -
**Section A - Answers**

**Question A1** = A. By definition.

**Question A2** = C. By definition.

**Question A3** = C. By definition.

**Question A4** = C. At 85,000 units the firm would not have exhausted its economies of scale and therefore is also not minimising costs (recall that cost minimisation and profit maximisation are not the same thing). Hence it is most likely that the firm is operating under monopolistic competition.

**Question A5** = D. We first realise that the increase in production costs will shift the supply curve to the left. Moreover, observe that the old equilibrium point lies in the elastic region of the demand curve (i.e. in the top half of the demand curve), therefore elasticity is represented by a number that is more negative than -1. This means that the percentage decrease in quantity demanded must be greater than the percentage increase in price.

**Question A6** = B. In an open economy we know NFI is equal to the Current Account = \( NX + NY + NT = \$20,000 + (\$1,500 - \$1,000) + \$6,000 = \$26,500. \)

**Question A7** = D. We observe that national income (c.f. GDP) per capita did not change between Year 1 and Year 2 (because \( 80000/40 = 2000 = 120000/60 \)), but prices rose (as shown by the increase in the Retail Price Index). This suggests the country is now worse off.

**Question A8** = A. Standard theory applies.

**Question A9** = A. We know that national savings are a major source of the money demanded by firms for investment. A smaller average propensity to save therefore implies that less investment is achievable and hence it is harder for the economy to grow.

**Question A10** = C. Standard theory applies.

**Section B**

**Sample Question B1 - Answer**

1. As a learning exercise we will first go through the process of rearranging both the demand and supply equation so that each is written in terms of price instead of in terms of quantity (i.e. we want to get ‘P’ by itself on one side of the equality sign and all the other terms on the other side) [n.b. If you are good at maths then just skim over this part of the answer]

   Let’s rearrange the demand equation first:
   \[
   Q_D = 1000 - 2.5P
   \]

   There are several paths by which we could get to our desired rearranged outcome. Here we’ll just follow one such path … so let’s start by subtracting 1000 from both sides – note that we have not changed the equality by doing this because we have done the same thing to both sides!
   \[
   Q_D - 1000 = 1000 - 2.5P - 1000
   \]

   Now the ‘1000’ terms on the right-hand side (RHS) cancel out because one is negative and the other is positive (hence they sum to zero).
   \[
   Q_D - 1000 = -2.5P
   \]
We now want to get rid of the negative sign on the RHS so we multiply both sides by negative one (-1). Again we have done the same thing to both sides so the equality remains unaffected.

\[(Q_D - 1000) \times (-1) = (-2.5P) \times (-1)\]

When you multiply negative one into brackets (such as on the LHS above) you need to remember to change the sign of every term in those brackets, therefore:

\[-Q_D + 1000 = 2.5P\]

Starting an equation with a negative variable is untidy, so we simply reorder the LHS terms.

\[1000 - Q_D = 2.5P\]

Lastly, to get \(P\) on its own, we must now divide each side by 2.5. Remember that all terms on each side must be divided by 2.5 so,

\[\frac{1000}{2.5} - \frac{Q_D}{2.5} = \frac{2.5P}{2.5}\]

And since \([1000/2.5=400]\) and \([1/2.5=0.4]\) and \([2.5/2.5=1]\) this becomes:

\[400 - 0.4Q_D = P\]

Now let’s look at the supply equation:

\[Q_S = 1.67P - 366.67\]

Again we want to get \(P\) on its own on one side of the equality sign so we first add 366.67 to either side.

\[Q_S + 366.67 = 1.67P - 366.67 + 366.67\]

Now the ‘366.67’ terms on the RHS cancel out.

\[Q_S + 366.67 = 1.67P\]

Lastly we divide all the terms on each side of the equation by 1.67, so

\[\frac{Q_S}{1.67} + \frac{366.67}{1.67} = \frac{1.67P}{1.67}\]

And since \([1/1.67=0.6]\) and \([366.67/1.67=220]\) and \([1.67/1.67=1]\) this becomes:

\[0.6Q_S + 220 = P\]

Now we can consider the question at hand, but before we jump into the necessary algebra, let’s have a look at the graph below to get a visual picture of what we are actually trying to achieve:
Now we recall the two equations that we need to solve simultaneously:

Demand: \[400 - 0.4Q_D = P\]
Supply: \[0.6Q_S + 220 = P\]

And we realise that at the intersection point these must be where demand equals supply, hence:

\[400 - 0.4Q_D = 0.6Q_S + 220\]

And at the intersection point, \(Q_D\) must also be equivalent to \(Q_S\). We refer to this quantity as the “equilibrium quantity” and denote it by \(Q^*\), so we can write:

\[400 - 0.4Q^* = 0.6Q^* + 220\]

Grouping like terms (i.e. getting all the \(Q^*\) terms together on one side of the equation and getting all the numerical terms on the other side) is achieved by adding \(0.4Q^*\) to each side and also subtracting \(220\) from both sides.

\[400 - 0.4Q^* + 0.4Q^* - 220 = 0.6Q^* + 220 + 0.4Q^* - 220\]

Now by cancelling out the positive and negative like terms we can arrive at:

\[400 - 220 = 0.6Q^* + 0.4Q^*\]

We now take \(Q^*\) outside a bracket

\[400 - 220 = (0.6 + 0.4)Q^*\]

And since \([400-220=180]\) and \([0.6+0.4=1]\) we get

\[Q^* = 180 \text{ thousand tonnes}\]

(this is the “equilibrium quantity” and you can check on the diagram above to see that the intersection point is actually at \(Q = 180 \text{ thousand tonnes}\))

However we were asked to determine the output of each of 20 identical firms in this market and so each will produce \(180/20 = 90 \text{ thousand tonnes}\).

Lastly, to obtain the equilibrium price that will prevail in this market we just substitute the equilibrium quantity that we now know (i.e. calculated above at \(Q=180\)) back into either the demand or the supply equation. Let’s use the supply equation:

\[P = 0.6Q_S + 220\]
\[P^* = 0.6Q^* + 220\]
\[= (0.6 \times 180) + 220\]
\[= $328 \text{ per tonne}\]

(this is the “equilibrium price” and you can check on the diagram above to see that the intersection point is at \(P = $328 \text{ per tonnes}\))

As an aside … you could have alternatively used the demand equation to find the equilibrium price. To prove this, we do the following:

\[P = 400 - 0.4Q_D\]
\[P^* = 400 - 0.4Q^*\]
\[= 400 - (0.4 \times 180)\]
\[= $328 \text{ per tonne (which is the same answer as above)}\]

2. Again let’s have a quick look at a graph of the situation before we jump into the necessary algebra. The sketch below shows that the petrol price rise has shifted supply to the left (which aligns to the theory of a leftward supply shift due to a price rise of an input factor). We can therefore observe that the new intersection point is at a higher price but a lower quantity.
We follow the same process as in the previous question (albeit that one of our two simultaneous equations has now changed slightly).

**Demand:**  \( 400 - 0.4Q_D = P \)

**Supply:**  \( 0.8Q_S + 250 = P \)

Hence we equate:

\[
400 - 0.4Q^* = 0.8Q^* + 250
\]

\[
150 = 1.2Q^*
\]

\[
Q^* = \frac{150}{1.2} = 125 \text{ tonnes}
\]

And substituting this number into the new supply equation yields:

\[
P = 0.8Q_S + 250
\]

\[
P^* = 0.8Q^* + 250
\]

\[
= (0.8 \times 125) + 250
\]

\[
= $350 \text{ per tonne}
\]

From the answers above we can write down the values at the two ends of our arc:

<table>
<thead>
<tr>
<th>Old Equilibrium</th>
<th>New Equilibrium</th>
<th>Difference</th>
<th>Mid-Point</th>
</tr>
</thead>
<tbody>
<tr>
<td>( X_0 )</td>
<td>( X_1 )</td>
<td>((X_1 - X_0))</td>
<td>(0.5(X_1 + X_0))</td>
</tr>
<tr>
<td><strong>Price</strong></td>
<td></td>
<td><strong>$22</strong></td>
<td><strong>$339</strong></td>
</tr>
<tr>
<td><strong>Quantity</strong></td>
<td></td>
<td><strong>-55</strong></td>
<td><strong>152.5</strong></td>
</tr>
</tbody>
</table>
Sample Question B2 - Answer

1. Here the public decides to hold more currency, and it can only do so by taking reserves out of the banking system. This leaves less money for banks to lend, hence the money supply will fall.

2. You can pick any four conditions that lead to an overheating of the economy, e.g:
   - energy prices rising
   - input factor costs rising
   - wages growing faster than productivity
   - domestic debt rising too fast,
   - etc

3. You would refer to the dual-market model here. Rising interest rates brings capital inflows, hence greater demand for AUD. AUD will therefore appreciate against the USD. Higher domestic interest rate will see consumption fall, foreign investment rise (capital inflows), domestic investment fall (in the short run) and net exports fall (because appreciated AUD makes exports more expensive and imports cheaper). Overall effect on GDP is most likely to be a fall.

Sample Question B3 - Answer

1. Crude oil is a factor of production for nearly all firms (whether it be a direct factor or and indirect factor). The simplistic answer to this question is therefore that a rise in the crude oil price makes production more expensive and shifts AS left causing stagflation (increasing price levels in the economy and also lowering the quantity of output from that economy), however the questions also says that policy makers take no action therefore we need to further consider the neo-classical view that the market will self-correct. I.e. if policy makers take no action, then the lower output and associated higher unemployment from the shifting left of AS will put downward pressure on labour costs. Given time, the result is that labour costs should fall and this stimulates production again (so ASsr slowly shifts back to the right) and the economy will return to its original equilibrium position.

2. The government borrowing reduces the supply of loanable funds and shifts the supply curve left. Refer to the diagrams below to consider the effect of elasticity (in relative terms):
   - The more elastic is the supply of loanable funds, the flatter the supply curve would be, so the interest rate would rise by less.
   - The more elastic is the demand for loanable funds, the flatter the demand curve would be, so the interest rate would rise by less.
3. Reducing national debt would increase public savings and therefore increase the source of supply of loanable funds (shifts right). It would not affect the demand for loanable funds, so the overall effect is to reduce the interest rate. This stimulates private investment and economic growth.

Sample Question B4 - Answer

1. We first note that we are not provided any information about the actual cost of delivery, so we cannot truly determine profits here. For this reason we work in revenues as payoffs in the matrix. We will then be able to consider different cost structures and place any necessary caveats on our analysis. We also note that an assumption of roughly equivalent cost structures for each firm is feasible noting the business is fairly simple and it draws production factor costs from competitive markets (eg: labour, transport, storage).

Using revenues in the matrix we determine that:

- If neither firm advertises, then both receive 50% of $1mil in revenue = $500k each
- If both firms advertise, then each receives 50% of $1mil in revenue less $200k each for the advertising campaign = $500k - $200k = $300k
- If one firm advertises and the other does not, then the advertising firm receives (at least) 80% of $1mil in revenue less $200k for its advertising campaign = $800k - $200k = $600k, whilst the other firm simply receives (at most) 20% of $1mil in revenue = $200k

NOTE: Payoffs here indicate revenue, not profit

<table>
<thead>
<tr>
<th></th>
<th>Lokim</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Advertise</td>
<td>* $300k</td>
<td>$300k</td>
<td>* $600k (min)</td>
</tr>
<tr>
<td>Don’t Advertise</td>
<td>$200k (max)</td>
<td>* $600k (min)</td>
<td>$500k</td>
</tr>
</tbody>
</table>
From the above game we deduce that, when using revenues as payoffs, both firms have a dominant strategy to advertise. The Nash Equilibrium is therefore “Advertise, Advertise” generating $300k in revenue for each firm.

We need now to consider whether this game (and maybe the outcome) will differ if we relax our assumption about the similar cost structures for each firm. In this regard, we are told about warehouse leasing costs in the question, but since these are but one cost of many, we can draw no conclusion from this limited information about total costs or costs at the margin. You should recognize that a company’s decisioning in a simultaneous game is relative to itself - for example, propose Lokim were to advertise, then Kirupim is trying to simultaneously decide whether to also Advertise (revenue = $300k) or not (revenue = $200k). This decision has nothing to do with the relative costs between Lokim and Kirupim, hence cost structures will not alter the outcome of this game. You might also notice that capturing “at least 80%” of the market, giving rise to a minimum revenue stream of $600, means that irrespective of cost, this outcome must always be better than the alternative.

2. The MD’s suggestion makes little sense. Advertising is certainly not a core competency of Kirupim (whose business it is to project manage removals of household effects). Advertising is also not considered a critical input factor to Kirupim’s business (this is observed from the information that, without advertising, the removals market is today split 50/50). Kirupim does not need to have great flexibility with respect to advertising either; hence it can just buy it from the market when it needs it. There appear to be no confidential information issues either. The transaction costs of buying advertising from the market would also seem comparable (if not less than) the extra control costs that might be necessary if under an integrated model. The only advantage seen in the suggested integration is that since the advertising firm is a monopolist then Kirupim would most likely get access to cheaper advertising. But although barring Lokim from advertising may yield fiscal benefit from Kirupim in the removals market, it is counterproductive for the profitability of the advertising firm itself.