

AQA A-LEVEL ECONOMICS

ECONOMICS



EXAM QUESTION PACK

UNIT 2 OLD SPECIFICATION PAPERS

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General Certificate of Education
Advanced Subsidiary Examination
June 2012

Economics

ECON2

Unit 2 The National Economy

Friday 25 May 2012 9.00 am to 10.15 am

For this paper you must have:

- an objective test answer sheet
 - a black ball-point pen
 - an AQA 8-page answer book.
- You may use a calculator.

Time allowed

- 1 hour 15 minutes

Section A (ECON2/1)

- Answer **all** questions on your objective test answer sheet.
- Use a black ball-point pen. Do **not** use pencil.
- Do all rough work in this question paper, **not** on your objective test answer sheet.

Section B (ECON2/2)

- Answer **EITHER** Context 1 **OR** Context 2.
- Use black ink or black ball-point pen. Pencil should only be used for drawing.
- Write the information required on the front of your answer book. The **Examining Body** for this paper is AQA. The **Paper Reference** is ECON2/2.

Information

- The maximum mark for this paper is 75.
- There are 25 marks for **Section A**. Each question carries one mark. No deductions will be made for wrong answers.
- There are 50 marks for **Section B**. The marks for questions are shown in brackets.
- You will be marked on your ability to:
 - use good English
 - organise information clearly
 - use specialist vocabulary where appropriate.

Advice

- You are advised to spend no more than 25 minutes on **Section A** and at least 50 minutes on **Section B**.

Section A: Objective Test

Answer **all** questions in **Section A**.

Each question carries 1 mark. No deductions will be made for wrong answers.

You are advised to spend no more than 25 minutes on **Section A**.

For each question there are four alternative responses, **A**, **B**, **C** and **D**. When you have selected the response which you think is the best answer to a question, mark this response on your objective test answer sheet. If you wish to change your answer to a question, follow the instructions on your objective test answer sheet.

- 1 Which one of the following is most likely to be an example of a supply-side policy?
 - A A reduction in the rate of interest to reduce inflation
 - B An increase in government expenditure on state pensions
 - C A reduction in company taxes to encourage greater investment
 - D A rise in the exchange rate to increase exports

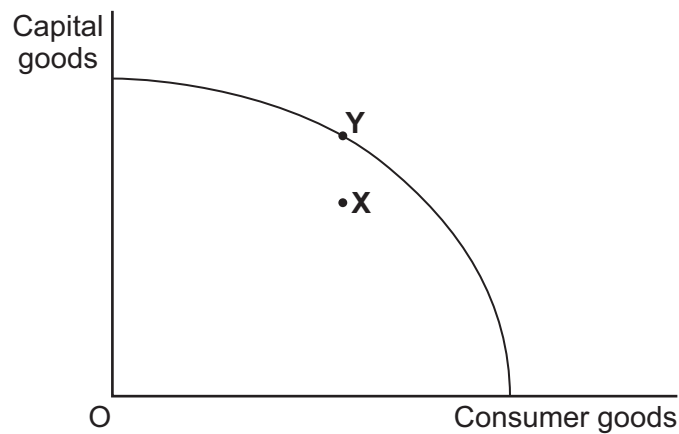
- 2 All other things being equal, which one of the following would be the most likely consequence of an appreciation in the external value of a country's currency?

An increase in

 - A the domestic price level
 - B the volume of exports
 - C employment in the domestic economy
 - D the volume of imports

- 3 Which one of the following is most likely to result in an increase in the long-run trend rate of economic growth?
 - A An increase in aggregate demand leading to inflationary pressures
 - B A sustained increase in the value of the pound on the foreign exchange market
 - C A reduction in taxes which increases risk-taking and incentives to work
 - D A sustained reduction in both inflation and labour productivity.

- 4 The diagram below shows an economy operating on its production possibility frontier at point Y.



All other things being equal, which one of the following is most likely to move the economy from point Y to point X within its production possibility frontier?

- A A decrease in inflation
 - B A decrease in investment expenditure
 - C A reduction in productive capacity
 - D A reduction in the trend rate of growth
- 5 Which one of the following best illustrates the accelerator process?
- A A change in one of the components of aggregate demand leading to a much greater increase in national income
 - B An increase in national income resulting in a proportionately larger rise in investment
 - C Government subsidies to firms for research and development helping to increase the rate of innovation
 - D An increase in government spending during a recession helping to stimulate investment

Turn over ►

- 6 The table below shows the index of Gross Domestic Product (GDP) measured at current prices and the associated price index for an economy.

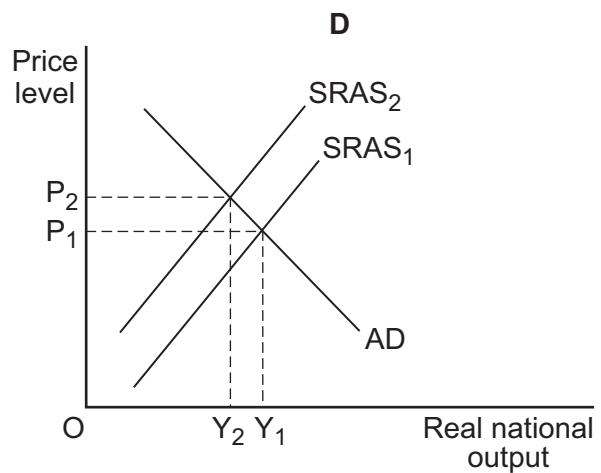
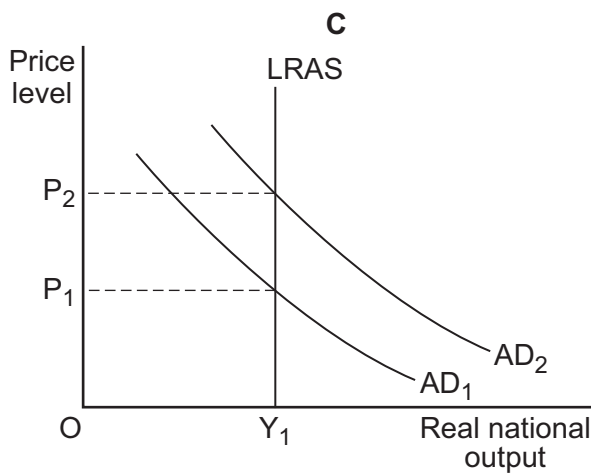
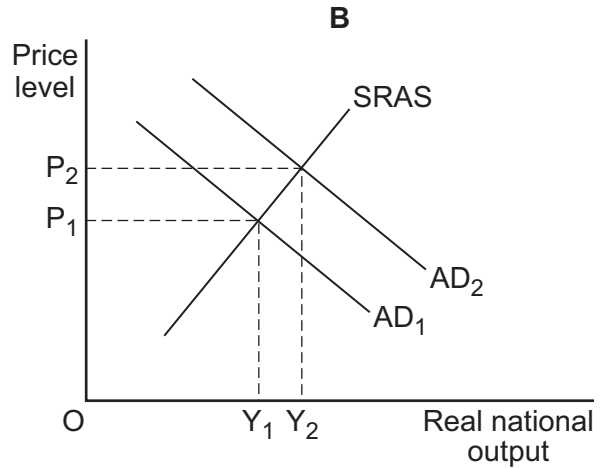
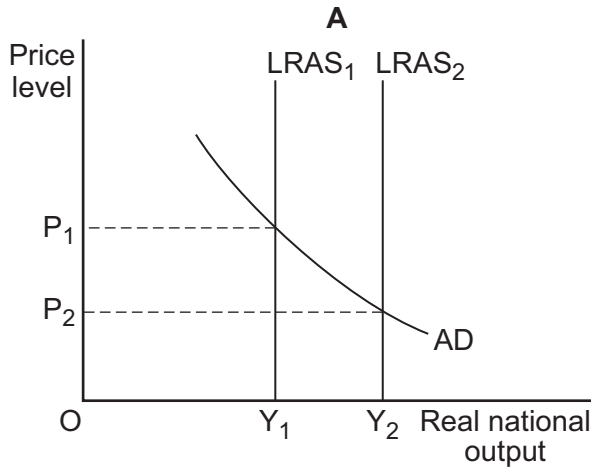
Year	Index of GDP at current prices 2005 = 100	Price index 2005 = 100
2001	80	80
2011	130	110

The table shows that between 2001 and 2011

- A real GDP rose by 50%.
 - B nominal GDP rose by 50%.
 - C real GDP rose by less than 50%.
 - D nominal GDP rose by less than 50%.
- 7 Which one of the following is most likely to result in a rightward shift of the short-run aggregate supply curve?
- A A decrease in wage rates
 - B A decrease in government spending
 - C An increase in taxation
 - D An increase in investment expenditure
- 8 A cut in income tax rates could be considered
- A both a monetary policy and a fiscal policy.
 - B both a monetary policy and a supply-side policy.
 - C both a fiscal policy and a supply-side policy.
 - D neither a monetary policy nor a fiscal policy.

- 9 The four diagrams below show aggregate demand (AD) and long-run and short-run aggregate supply (LRAS/SRAS) curves for an economy where OP_1 is the initial equilibrium price and OY_1 the initial equilibrium level of real national output.

Which diagram, **A**, **B**, **C** or **D**, shows the change resulting from an increase in innovation and productivity improvements?

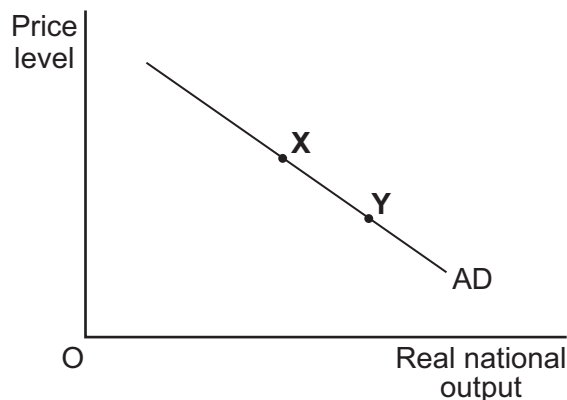


- 10 A rise in the level of domestic investment will most likely result from a rise in

- A** the current account deficit.
- B** interest rates.
- C** company profits.
- D** the exchange rate.

Turn over ►

- 11** Fiscal policy involves changes in both
- A** the budget balance and the balance of payments.
 - B** interest rates and the supply of credit.
 - C** the money supply and the exchange rate.
 - D** government spending and tax revenue.
- 12** Deflation is most likely to
- A** cause consumers to delay their purchases.
 - B** lead to a rise in interest rates.
 - C** lead to a rise in imports.
 - D** reduce the real value of any money that has been lent.
- 13** The diagram below shows an aggregate demand (AD) curve for an economy.



The movement down the aggregate demand curve from **X** to **Y** shows that

- A** as real national output rises, firms can lower their costs due to mass production.
- B** as real national output falls, the price of imported goods rises.
- C** as the price level rises, the nominal value of consumption and investment falls.
- D** as the price level falls, consumers and firms purchase more goods.

- 14** An economy is currently operating with a negative output gap. In the short run, if the rate of growth of aggregate demand is positive but less than the rate of growth of productive capacity, then the economy is most likely to experience
- A** a decrease in output.
 - B** an increase in unemployment.
 - C** a decrease in its trend rate of growth.
 - D** a decrease in exports.
- 15** The table below shows the components of the balance of payments on current account for an economy in 2011.

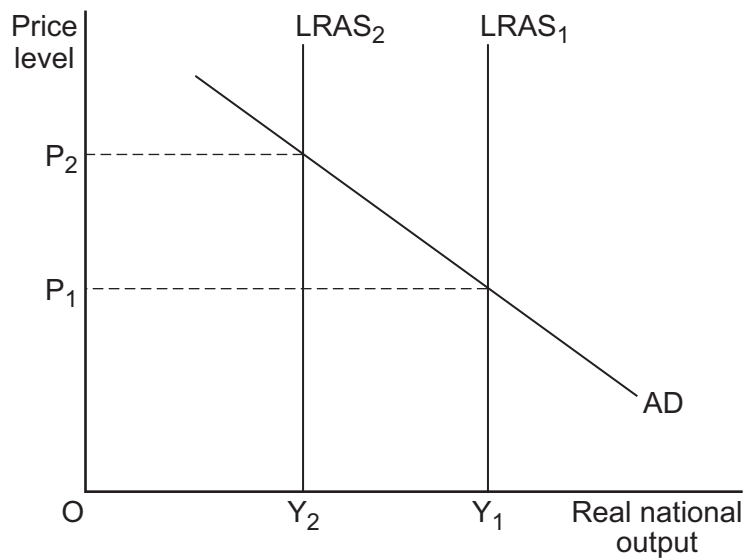
	£bn
Export of goods	500
Export of services	400
Import of goods	800
Import of services	300
Net investment income	+50
Net transfers	+100

It follows that the balance of payments on current account for 2011 is

- A** +£2150 bn
 - B** +£200 bn
 - C** –£200 bn
 - D** –£50 bn
- 16** The UK economy enters a recession but the current account deficit on the balance of payments remains high. Given these problems, which one of the following would be most likely to improve the performance of the UK economy?
- A** An increase in taxes on imported goods and a fall in the value of the pound
 - B** A fall in interest rates and a rise in the value of the pound
 - C** A fall in the money supply and an increase in taxes on imported goods
 - D** A fall in government spending and a rise in interest rates

Turn over ►

- 17 An increase in interest rates when the exchange rate is rising is most likely to lead to an increase in
- A economic growth.
 - B aggregate supply.
 - C the current account surplus.
 - D unemployment levels.
- 18 The diagram below shows the aggregate demand (AD) curve and two long-run aggregate supply (LRAS) curves for an economy.



The decline in equilibrium real national output from Y_1 to Y_2 implies that the economy

- A is operating within its production possibility frontier.
- B has a falling level of unemployment.
- C has a negative rate of economic growth.
- D is experiencing a low rate of productivity growth.

- 19** Which one of the following is an example of expansionary fiscal policy?
- A** A reduction in interest rates
 - B** An increase in the budget deficit
 - C** An increase in the money supply
 - D** An increase in tax rates
- 20** Which one of the following is most likely to lead to a fall in aggregate investment?
- A** A reduction in the level of unemployment
 - B** An increase in spare capacity in the economy
 - C** A reduction in the average level of interest rates
 - D** An increase in aggregate demand
- 21** All other things being equal, a large increase in an economy's rate of interest will cause
- A** both its aggregate demand curve and its short-run aggregate supply curve to shift to the right.
 - B** its aggregate demand curve to shift to the right and its short-run aggregate supply curve to shift to the left.
 - C** both its aggregate demand curve and its short-run aggregate supply curve to shift to the left.
 - D** its aggregate demand curve to shift to the left and its short-run aggregate supply curve to shift to the right.
- 22** Inflation in an economy is currently at 10%. Which of the following changes in monetary and fiscal policy, **A**, **B**, **C** or **D**, is most likely to reduce the rate of inflation in the economy?

	Interest rates	Government expenditure	Taxation revenue
A	Increase	Increase	Decrease
B	Decrease	Decrease	Increase
C	Increase	Decrease	Increase
D	Decrease	Increase	Increase

Turn over ►

- 23** The government introduces a policy which initially increases the budget deficit but, in the long run, increases the trend rate of economic growth.

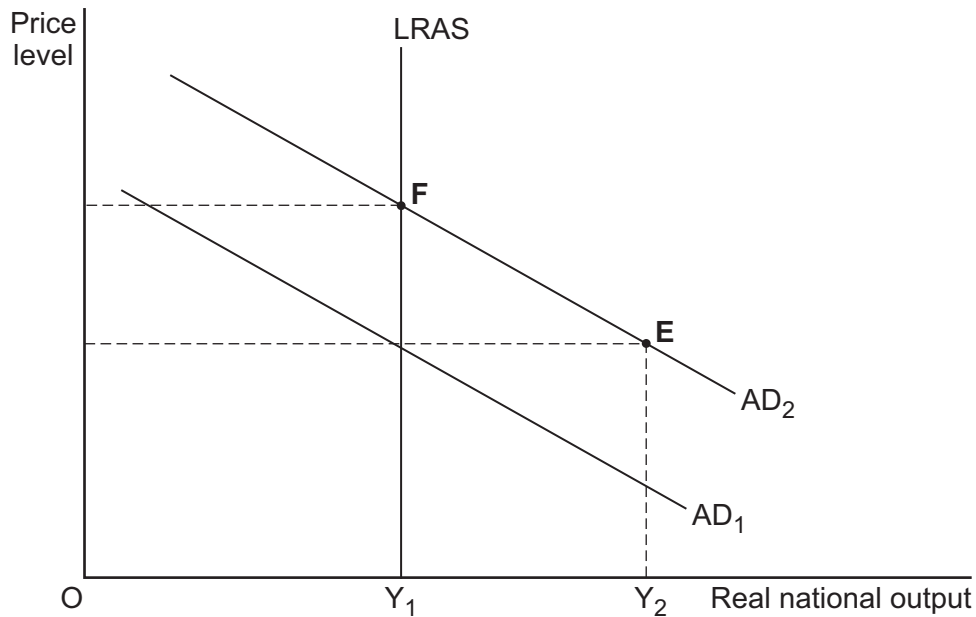
This policy is most likely to have been

- A** placing a tax on imports.
 - B** increasing subsidies for research and development.
 - C** bringing about a fall in the exchange rate.
 - D** increasing the age of retirement.
- 24** The UK steel industry pays for its imported inputs in US dollars and sells its output abroad in euros.

It follows from the above that the UK steel industry will benefit most when the pound is

- A** strong against the US dollar, weak against the euro.
- B** weak against the US dollar, weak against the euro.
- C** weak against the US dollar, strong against the euro.
- D** strong against the US dollar, strong against the euro.

- 25** The diagram below shows the aggregate demand (AD) and long-run aggregate supply (LRAS) curves for the UK economy.



The government predicts that aggregate demand will increase in the long run from AD_1 to AD_2 . All other things being equal, which one of the following policies is most likely to move the economy to a new long-run equilibrium at point **E** rather than point **F**?

- A** Pursuing an expansionary monetary policy
- B** Allowing the exchange rate to rise
- C** Increasing taxation
- D** Improving the flexibility of the labour market

**QUESTION 25 IS THE LAST
QUESTION IN SECTION A**

**On your answer sheet
ignore rows 26 to 50**

Turn over for Section B

Turn over ►

Section B: Data Response

Answer **EITHER** Context 1 **OR** Context 2.

You are advised to spend at least 50 minutes on **Section B**.

Total for this Context: 50 marks

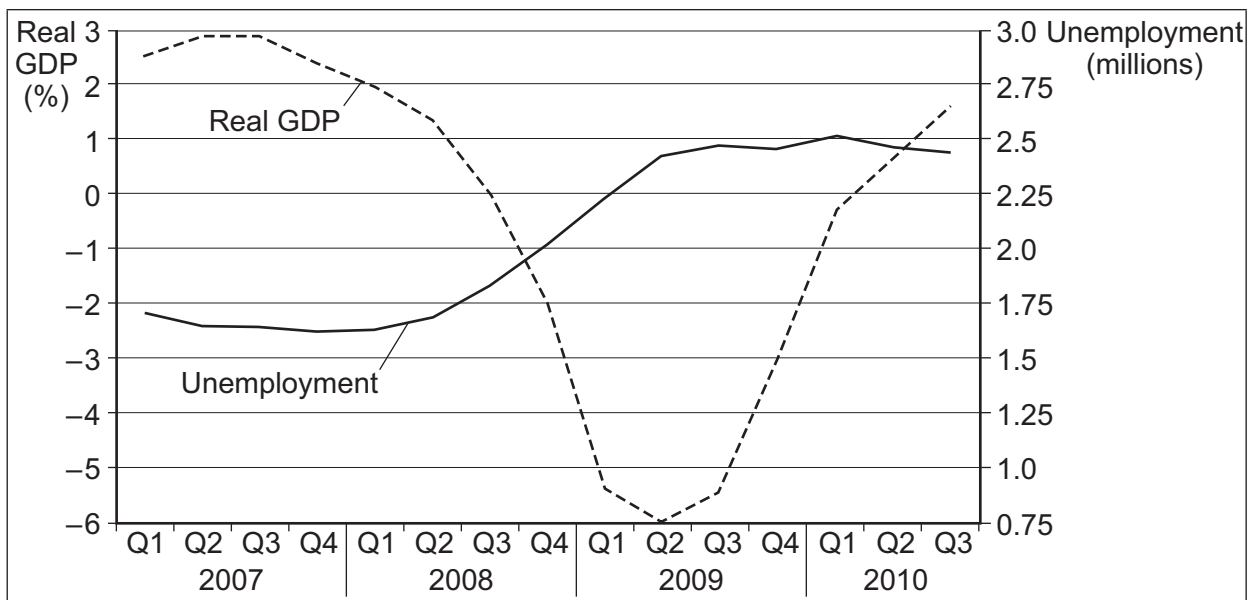
EITHER

Context 1

UNEMPLOYMENT IN THE UK

Study **Extracts A, B and C**, and then answer **all** parts of Context 1 which follow.

Extract A: UK real GDP growth (%) and unemployment (millions), 2007 to 2010, quarterly



Source: official statistics, January 2011

Extract B: Unemployment rises above 2.5 million

Figures published by the *Office for National Statistics* show that a sharp fall in employment in the public sector helped to push total unemployment above 2.5 million last month. The largest rise in unemployment was among 16 and 17 year olds, up by 19 000 to reach 206 000. The number of people employed in the public sector fell by over 33 000. However, unlike earlier in 2010 when private firms were creating jobs, employment in the private sector was unchanged. Measures designed to reduce the size of the budget deficit mean that it is inevitable that job losses in the public sector will continue during the years ahead.

The number of people who were working part-time because they could not find a full-time job increased by 46 000 to reach 1.16 million, the highest figure since comparable records began in 1992.

Source: news reports, January 2011

Extract C: 2011 will be tough for the UK economy

Economists are predicting that the first half of 2011 is going to be tough for the UK economy. The 2.5% rise in VAT and cuts in public spending will drive up unemployment. On a more positive note, the strengthening of private sector investment and the growth in exports of manufactured goods, helped by the 20% reduction in the value of the pound, should help to stimulate the economy.	1 5
Nevertheless, the overall growth in aggregate demand is likely to be less than the economy's underlying trend rate of growth and some economists have predicted that unemployment will rise to around 2.7 million. Another shock to the economy, such as a rise in interest rates triggered by high inflation, could lead to a further increase in spare capacity and even higher unemployment.	10
Since 2009, there has been some rebalancing of the UK economy away from the public sector, with 296 000 new private sector jobs more than compensating for 77 000 jobs lost in the public sector. However, it is predicted that a further 600 000 jobs will go in the public sector over the next 5 years. Regions of the UK, such as the North East, that are very dependent on the public sector, are likely to see a sharp rise in structural unemployment. Many of the jobs created by the private sector are likely to be located in the wrong places and require skills which redundant public sector staff may not be able to provide. People may be unable to move from regions of high unemployment for family reasons or because of the very high house prices in the South East, where most of the jobs are likely to appear.	15 20

Source: news reports, January 2011

- 0 1** Define the term 'structural unemployment' (**Extract C**, lines 15–16). (5 marks)
- 0 2** Using **Extract A**, identify **two** significant points of comparison between the rate of growth in real GDP and unemployment over the period shown. (8 marks)
- 0 3** **Extract C** (lines 6–8) states that 'the overall growth in aggregate demand is likely to be less than the economy's underlying trend rate of growth and some economists have predicted that unemployment will rise to around 2.7 million'.
- Explain why unemployment is likely to rise if aggregate demand grows more slowly than the underlying trend rate of growth of the economy. (12 marks)
- 0 4** **Extract B** (lines 6–8) states: 'Measures designed to reduce the size of the budget deficit mean that it is inevitable that job losses in the public sector will continue during the years ahead.'
- Using the data and your economic knowledge, discuss the view that the measures taken to reduce the size of the budget deficit will inevitably result in a rise in unemployment in the UK. (25 marks)

Turn over ►

Do **not** answer Context 2 if you have answered Context 1.

Total for this Context: 50 marks

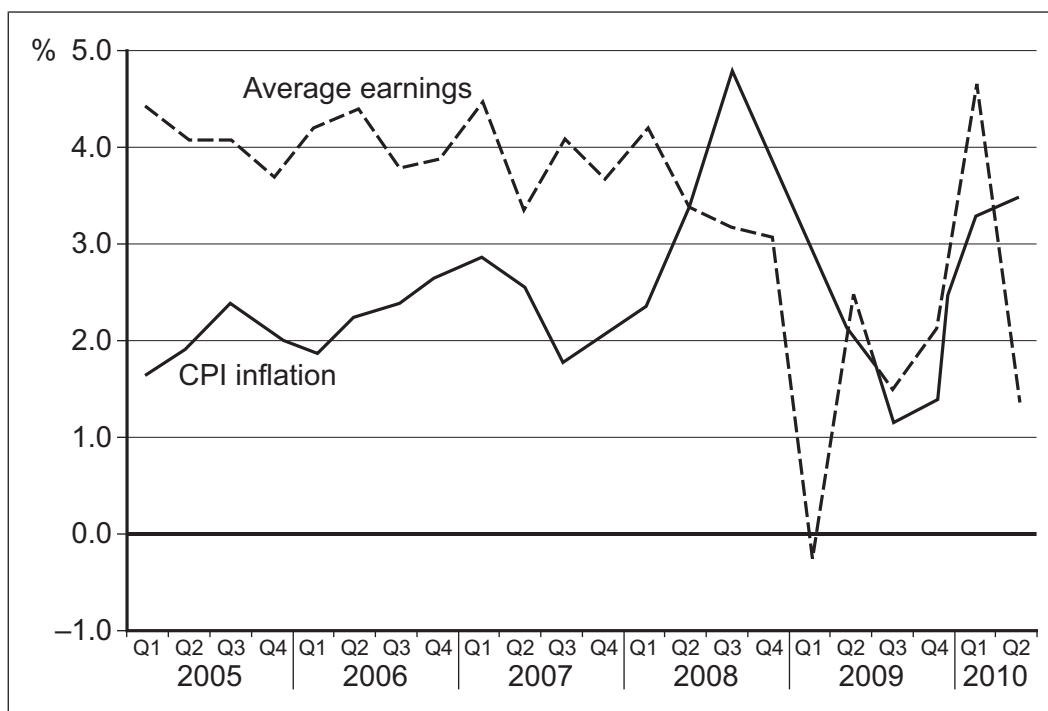
OR

Context 2

INFLATION IN THE UK

Study **Extracts D, E and F**, and then answer **all** parts of Context 2 which follow.

Extract D: CPI inflation and the rate of growth in average earnings in the UK, 2005 to 2010, quarterly



Source: official statistics, January 2011

Extract E: Inflation has been above target throughout 2010

The Bank of England's forecasts for inflation have been over-optimistic for some time now. Inflation has increased partly as a result of the fall in the value of the pound, rapidly rising commodity prices and increases in Value Added Tax (VAT). The pound has fallen by more than 20% against other currencies since the beginning of 2008, pushing up the price of imports. On top of this, the restoration of VAT to 17.5% in January 2010 increased CPI inflation by about 1%.

1

5

The further increase in VAT to 20% in January 2011 put more upward pressure on inflation. Without the effect of increases in indirect taxes, such as VAT and excise duties on petrol, inflation would have been around 1.5% over the previous 6 months. Instead, inflation has exceeded the Government's 2% target and has been over 3% for most of 2010. Inflation will continue to rise over the next few months but the Bank still believes that it will return to target in 2012.

10

Source: news reports, January 2011

Extract F: Will rising commodity prices fuel inflationary expectations?

Food prices, fuel bills, clothing and other costs are rocketing. Figures released yesterday by the United Nations (UN) <i>Food and Agriculture Organisation</i> show that global food prices rose to a record high last month. Many other raw materials and agricultural commodities are close to, or above, their previous peaks. The price of oil, although still well below the \$140 a barrel level it reached in the summer of 2008, is once more approaching \$100 a barrel. This rise in world commodity prices will ensure that inflation in the UK remains high throughout 2011. Many economists believe that this type of cost-push inflation is difficult to control through the use of interest rates.	1 5
The real danger is that inflationary expectations will increase and change people's behaviour. With rising inflation, people will be expecting higher pay. However, pay increases will be hard to obtain in the face of rising unemployment and public sector pay freezes. If wages do start to rise, firms will want to pass on the increase in costs. However, this will not be easy when household disposable income is being constrained by tax rises and benefit cuts.	10
Contractionary fiscal measures should help to reduce inflation, as might supply-side policies. However, if growth in the economy reduces the amount of spare capacity and unemployment falls, earnings may start to rise rapidly. In these circumstances, the Monetary Policy Committee of the Bank of England will raise Bank Rate to try to reduce inflation. Some think that this will be too late.	15

Source: news reports, January 2011

- 0 5** Define the term 'cost-push inflation' (**Extract F**, line 8). (5 marks)
- 0 6** Using **Extract D**, identify **two** significant points of comparison between CPI inflation and the rate of growth in average earnings over the period shown. (8 marks)
- 0 7** **Extract E** (line 2) states: 'Inflation has increased partly as a result of the fall in the value of the pound... .' Using an appropriate diagram, explain why a fall in the exchange rate is likely to increase inflation. (12 marks)
- 0 8** **Extract F** (lines 17–19) states: 'In these circumstances, the Monetary Policy Committee of the Bank of England will raise Bank Rate to try to reduce inflation.' Using the data and your economic knowledge, assess the view that the use of interest rates is the best way to control inflation in the UK. (25 marks)

END OF QUESTIONS

There are no question printed on this page



General Certificate of Education (A-level)
June 2012

Economics

ECON2

(Specification 2140)

Unit 2: The National Economy

Final

Mark Scheme

Mark schemes are prepared by the Principal Examiner and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation events which all examiners participate in and is the scheme which was used by them in this examination. The standardisation process ensures that the mark scheme covers the candidates' responses to questions and that every examiner understands and applies it in the same correct way. As preparation for standardisation each examiner analyses a number of candidates' scripts: alternative answers not already covered by the mark scheme are discussed and legislated for. If, after the standardisation process, examiners encounter unusual answers which have not been raised they are required to refer these to the Principal Examiner.

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of candidates' reactions to a particular paper. Assumptions about future mark schemes on the basis of one year's document should be avoided; whilst the guiding principles of assessment remain constant, details will change, depending on the content of a particular examination paper.

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Advanced Subsidiary Economics

June 2012

ECON2/1

Section A: Objective Test (ECON2/1)

The following list indicates the correct answers used in marking the students' responses.

KEY LIST

1.	C	9.	A	17.	D
2.	D	10.	C	18.	C
3.	C	11.	D	19.	B
4.	B	12.	A	20.	B
5.	B	13.	D	21.	C
6.	C	14.	B	22.	C
7.	A	15.	D	23.	B
8.	C	16.	A	24.	A
				25.	D

Advanced Subsidiary Economics

June 2012

ECON2/2

Mark Scheme

Section B: Data Response

General Instructions

Marks awarded to candidates should be in accordance with the following mark scheme and examiners should be prepared to use the full range of marks available. The mark scheme for most questions is flexible, permitting the candidate to score full marks in a variety of ways. Where the candidate's response to a question is such that the mark scheme permits full marks to be awarded, full marks **MUST** be given. A perfect answer is not necessarily required for full marks. But conversely, if the candidate's answer does not deserve credit, then no marks should be given.

Occasionally, a candidate may respond to a question in a reasonable way, but the answer may not have been anticipated when the mark scheme was devised. In this situation, **OR WHENEVER YOU HAVE ANY DOUBT ABOUT THE INTERPRETATION OF THE MARK SCHEME**, you must in the first instance telephone your team leader to discuss how to proceed.

Two approaches have been used in the construction of the mark scheme:

- (i) **An issue based approach.** The mark scheme for questions **01, 02, 03, 05, 06** and **07** of the data response questions adopts this approach. The mark scheme lists the marks that can be awarded for particular issues (and associated development) that the candidate might include in the answer.
- (ii) **A levels approach.** This approach is used for marking questions **04** and **08** of the data response questions. The Levels Mark Scheme on the next page identifies five levels representing differences in the quality of work. A range of marks is allocated at each level. First decide the level into which an answer falls. The level chosen should be the one which **best fits** the answer provided by the candidate. It is **not** intended that the answer should satisfy every statement in the level description. Then think in terms of awarding the mid-point mark which has been identified for that level (eg 13 marks for Level 3). Move up and down from this notional mark by considering the extent to which the answer meets the level description overall. Strength in one skill can outweigh weakness in another. When using the Levels Mark Scheme the marker **must** identify where a particular skill is being demonstrated. The **key** to be used to identify the skill is given after the levels descriptions. The question-specific mark scheme summarises the information which could be used to answer the question, but without attaching marks to particular issues.

**LEVELS OF RESPONSE MARK SCHEME
FOR USE WITH QUESTIONS 04 AND 08 ONLY**

AS LEVELS OF RESPONSE	AO1 KNOWLEDGE and UNDERSTANDING of theories, concepts and terminology	AO2 APPLICATION of theories, concepts and terminology	AO3 ANALYSIS of economic problems and issues	AO4 EVALUATION of economic arguments and evidence, making informed judgements
Level 5 22-25 marks (mid-point 24) Good analysis and good evaluation	Good throughout the answer with few errors and weaknesses	Good application to issues Good use of data to support answer	Relevant and precise with a clear and logical chain of reasoning	Good with a clear final judgement
Level 4 17-21 marks (mid-point 19) Good analysis <u>but</u> limited evaluation OR Reasonable analysis and reasonable evaluation	Good throughout the answer with few errors and weaknesses Good throughout much of the answer with few errors and weaknesses	Good application to issues Good use of data to support answer Some good application to issues. Some good use of data to support answer	Relevant and precise with a clear and logical chain of reasoning Largely relevant and well organised with reasonable logic and coherence	Limited but showing some appreciation of alternative points of view Reasonable, showing an appreciation of alternative points of view
Level 3 10-16 marks (mid-point 13) Reasonable answer, including some correct analysis but very limited evaluation	Satisfactory but some weaknesses shown	Reasonable application to issues Reasonable use of data to support answer	Reasonably clear but may not be fully developed and is perhaps confused in places with a few errors present	Superficial, perhaps with some attempt to consider both sides of the issue(s)
Level 2 4-9 marks (mid-point 7) Weak with some understanding	Limited and some errors are made	Partial application to issues with some errors Limited use of data to support answer	Partial but confused at times, lacking focus and development Limited logic and coherence	A very basic and simplistic attempt is made which is unsupported by analysis
Level 1 0-3 marks (mid-point 2) Very weak	Weak with a number of errors	Little, if any, application to issues No use of data to support answer	Poor and lacking clarity and focus	No relevant evaluation

THE KEY TO BE USED WHEN USING THE LEVELS MARK SCHEME

- D** Where a particular economic term is correctly **DEFINED** in order to help the candidate to answer the question properly.
- I** Where a relevant **ISSUE** is raised by the candidate.
- K** Where the candidate demonstrates **KNOWLEDGE** of recent developments or features of the economy which help enhance the candidate's response to the question. This should also be used where the candidate quotes relevant examples.
- Ap** Where the candidate demonstrates the ability to **APPLY** knowledge and **CRITICAL UNDERSTANDING** to problems and issues.
- An** Where the candidate demonstrates the ability to **ANALYSE** the problem using appropriate economic ideas.
- E** Where the candidate **EVALUATES** and makes judgements about the significance of various issues and arguments.

QUALITY OF WRITTEN COMMUNICATION

Quality of Written Communication (QWC) will be assessed in Questions 04 and 08 only.

Candidates will be assessed according to their ability to:

- ensure that text is legible, and that spelling, grammar and punctuation are accurate, so that meaning is clear
- select and use a form and style of writing appropriate to purpose and complex subject matter
- organise information clearly and coherently, using specialist vocabulary when appropriate.

No specific marks are awarded for QWC.

However, examiners should take into account QWC when determining the mark to be awarded for an answer. This means an answer could be taken either up (for exceptional QWC) or down (for very poor QWC) by 1 mark (and no more).

EITHER

Context 1

01 Define the term 'structural unemployment' (**Extract C**, lines 15-16). (5 marks)

For an acceptable definition such as:

- unemployment that occurs when the demand for labour is less than the supply of labour in an individual labour market
- unemployment that results from the decline in a particular industry/sector, region or occupation (at least 2 needed for full marks)
- unemployment that results from the decline in a particular industry which leaves people unemployed because they do not have the skills needed by the industries that are growing.

5 marks

Full marks should be awarded to a candidate who demonstrates a clear understanding of the term **structural unemployment** even if the definition is not exactly the same as the acceptable examples quoted above.

If the definition is inaccurate or incomplete award a maximum of 4 marks which may be broken down, for example, as follows:

Unemployment that results from the decline in a particular sector/industry of the economy.	4 marks
Unemployment that results from the decline in a particular occupation within the economy.	4 marks
Unemployment resulting from a change in the pattern of demand.	2 marks
Unemployment resulting from the immobility of labour.	2 marks
When people do not have the right skills for the jobs available	3 marks
When people are unwilling or unable to move to areas where there are jobs available	3 marks
Unemployment resulting from a change in the structure of the economy.	2 marks
For stating that structural unemployment is often classified as a form of voluntary unemployment.	1 mark
For stating that structural unemployment is long-term unemployment.	1 mark
For defining unemployment	2 marks
For one or more examples such as: • unemployment in the coal industry as a consequence of it becoming uneconomic to exploit ageing coal seams in the UK • technological unemployment • jobs on a production line being replaced by robots • unemployment due to a fall in demand for a product such as cathode ray TVs • unemployment caused by foreign competition (or changes in comparative advantage) • regional unemployment.	1 mark per example - up to a maximum of 2 marks for examples

Maximum of 4 marks if the definition is incomplete or inaccurate.

MAXIMUM FOR PART 01: 5 MARKS

02 Using **Extract A**, identify **two** significant points of comparison between the rate of growth in real GDP and unemployment over the period shown. (8 marks)

Award up to 4 marks for each point made.

Identifies a significant point of comparison. Makes accurate use of the data to support the comparison identified. Unit of measurement given accurately.	4 marks
Identifies a significant point of comparison. Makes use of the data to support the comparison identified. However, no unit of measurement is given and/or the unit of measurement is used/applied inaccurately and/or the dates aren't quoted or are inaccurate and/or only one piece of data is given when two are needed.	3 marks
Identifies a significant point of comparison. No correct use of the data to support the comparison identified.	2 marks
Identifies a significant feature of one data series but no comparison is made. Makes use of the data to support the feature identified. Unit of measurement given accurately.	1 mark

If a candidate identifies more than 2 significant points of comparison, reward the best two.

Significant points include:

- at the start of the period, unemployment was lower than at the end of the period (rose from 1.7 million to just under 2.5 million) whereas the rate of growth of real GDP was higher at the start of the period (2.5% approx.) than at the end of the period (1.7% approx)
- the lowest rate of growth in real GDP was in the 2nd quarter of 2009 (-6.0% approx.) whereas unemployment was at its lowest in the 1st quarter of 2008 (around 1.6 million) (also allow 2007 Q3 and Q4)
- the highest rates of growth of real GDP were experienced in the 2nd and 3rd quarters of 2007 (just under 3%) whereas unemployment peaked in the 1st quarter of 2010 (just over 2.5 million).
- the rate of growth of real GDP starts to fall after the 3rd quarter of 2007 and continues to fall until the 2nd quarter of 2009 (just under 3.0% to -6.0%), whereas unemployment remains fairly steady until the 2nd quarter of 2008 but then starts to rise rapidly until the 2nd quarter of 2009 (1.6 million to 2.5 million approximately) – or candidates might state that there is an inverse relationship between the rate of growth in real GDP between the 2nd quarter of 2008 and the 2nd quarter of 2009
- between the 2nd quarter of 2009 and the 3rd quarter of 2010 the rate of growth of real GDP rises (-6.0% to 1.7% approx.) but unemployment remains fairly steady (at around 2.5 million).
- in 2007, real GDP growth is relatively high (between 2% and 3%) whereas unemployment is relatively low (at around 1.6 million)
- throughout 2009, GDP growth is negative (e.g. the lowest rate of growth is -6%) whereas unemployment is high (reaching almost 2.5 million)
- the range for GDP growth is from almost 3% to -6% whereas the range for unemployment is from around 1.6 million to around 2.5 million. Allow the statement that 'GDP growth is more volatile than unemployment' as a point of comparison.

A margin of +/- 0.3% is permissible for the figures relating to real GDP growth and a margin of +/- 0.2 million is permissible for the unemployment figures.

MAXIMUM FOR PART 02: 8 MARKS

03 Extract C (lines 6 – 8) states that the ‘overall growth in aggregate demand is likely to be less than the economy’s underlying trend rate of growth and some economists have predicted that unemployment will rise to around 2.7 million’.

Explain why unemployment is likely to rise if aggregate demand grows more slowly than the underlying trend rate of growth of the economy. (12 marks)

For a candidate who provides a relevant definition, eg aggregate demand, unemployment, economic growth, trend rate of growth

**1 mark per definition
Up to a maximum of
2 marks**

Award up to 12 marks for each of the following explanations.

2 marks should be awarded for each logical link in the chain of reasoning.

If AD grows more slowly than potential output excess aggregate supply will emerge (2 marks), the economy will experience a negative output gap/spare capacity (2 marks), there will be an involuntary increase in stocks (2 marks), firms will cut back on production (2 marks) and since labour is in derived demand (2 marks) firms will reduce the number of workers employed and/or unemployment will increase (2 marks). Firms are also likely to reduce employment to cut costs and/or maintain profits (2 marks). This type of unemployment is known as demand-deficient (or cyclical) unemployment (2 marks).

Up to 12 marks

Link between rising productivity, aggregate demand and unemployment.

Up to 12 marks

Award **up to 4 additional marks** for the use of relevant diagrams, e.g. an AD/AS diagram that shows why the negative output gap increases if AD does not increase as much as AS increases (ie LRAS shifts) **OR** a diagram showing that the negative output gap increases when actual growth is less than trend growth. **OR** an equivalent production possibility diagram showing that the gap between current output and the PPC boundary has increased. To achieve all 4 marks, the size of the output gap, after the increase in AD should be larger than before the increase in AD. However, the candidate does not have to label the output gap on the diagram to achieve the full 4 marks.

**1 mark for initial
labelling of
axes and curves,
up to 3 marks for the
information shown**

**See below for
examples of how
marks should be
awarded.**

If a candidate uses a diagram to support their explanation, marks may also be awarded for the following type of a written explanation:

In the diagram, the trend growth is represented by a rightward shift in the LRAS (or PPC boundary) (2 marks). Since the increase in AD is less than the underlying trend rate of growth the amount of spare capacity in the economy (or the negative output gap) will increase (2 marks), an increase in the amount of spare capacity (negative output gap) means that unemployment has risen (2 marks).

Up to 6 marks

If an AD/AS diagram is used, the breakdown of the marks is as follows:

Axes labelled (allow on the vertical axis: Inflation or PL or £ but not Price or P; allow on the horizontal axis: Real GDP, National Output, Output or Y but not Quantity or Q). Original AD (and AS curve) labelled correctly. Dotted lines and showing the original price level and level of real GDP (PL1 Y1).	1 mark
AD shifts to the right by less than LRAS (or AS) shifts to the right	2 marks
Dotted lines and the associated labelling showing the new level of real GDP (PL2 Y2).	1 mark
Any other relevant feature of the diagram (e.g. the size(s) of the negative output gap(s)).	1 mark per feature up to a maximum of 2 marks

Examples of suitable diagrams include:

AD/AS diagram:

The diagram should show a rightward shift in both the AD and LRAS (AS) curves but the LRAS (AS) curve should shift by more than the AD curve to show that the negative output gap increases.

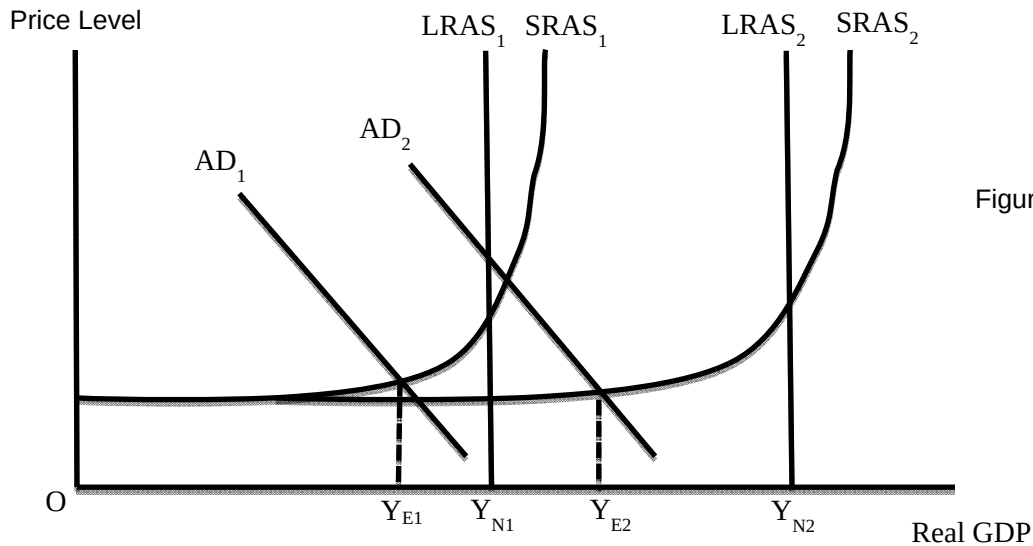


Figure 1

In Figure 1, the negative output gap increases from $(OY_{N1} - OY_{E1})$ to $(OY_{N2} - OY_{E2})$

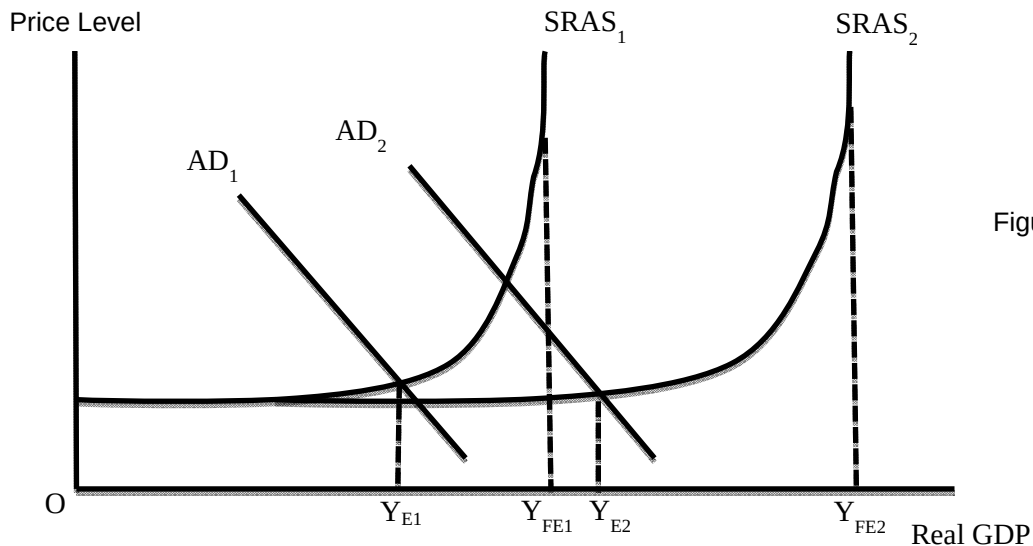
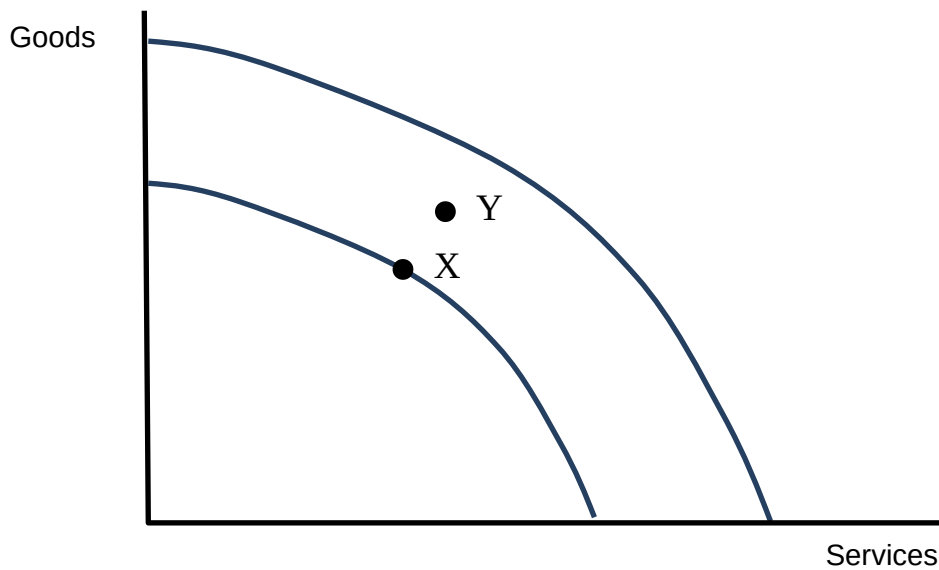


Figure 2

In Figure 2, the negative output gap increases from $(OY_{FE1} - OY_{E1})$ to $(OY_{FE2} - OY_{E2})$

If the AD/AS diagram shows a fall in AD leading to lower output and hence higher unemployment, award a maximum of 2 marks for the diagram. Similarly if the diagram just shows the effect of a rightward shift in AD, a maximum of 2 marks can be awarded.

A PPC diagram



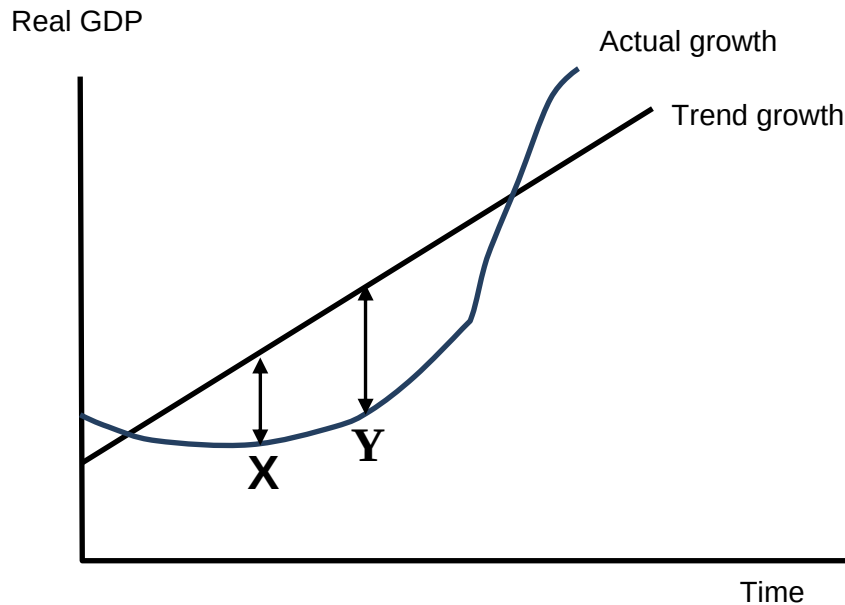
The movement from X to Y represents the actual growth of the economy resulting from the increase in AD. The rightward shift in the PPC represents the underlying trend rate of growth. The diagram shows that, since the increase in AD is less than the trend rate of growth, spare capacity (or a negative output gap) will emerge. This means that unemployment will increase.

Point X does **NOT** have to be on the PPC boundary. However, to get full marks for the diagram, the distance between X and Y should be less than the distance between the two PPCs. This means that the negative output gap will be larger at point Y than at point X.

If a PPC diagram is used, the breakdown of the marks is as follows:

Axes labelled (accept any reasonable axis labels, eg consumer goods and capital goods but NOT price level and output), the original PPC boundary and the original output of the economy.	1 mark
The new PPC shifted to the right	1 mark
The new level of output that shows an increase in the amount of spare capacity in the economy.	2 marks

A trend growth diagram that illustrates the economic cycle



The diagram shows that, over time, as the economy moves from point X to point Y, the size of the output gap increases. This happens because the growth in AD, which determines the actual rate of growth, is less than the underlying trend rate of growth. The amount of spare capacity increases and hence unemployment also increases.

To get full marks for the diagram, the vertical distance between the actual and trend growth lines must be larger at point Y than at point X.

If a trend growth diagram is used, the breakdown of the marks is as follows:

Axes labelled (accept Real GDP, GDP, Output and National Income on the vertical axis but only accept Time on the horizontal axis), the actual growth and trend growth lines (both must be labelled) and the point that the economy starts at BEFORE the 'growth in aggregate demand', eg point X in the diagram above.	1 mark
The original output gap (NB this must be a vertical line showing the vertical distance between the two curves).	1 mark
The new position for the economy that shows an increase in the amount of spare capacity in the economy.	2 marks

NB If a candidate's answer only explains why a fall in aggregate demand will cause a rise in unemployment then a **MAXIMUM OF 8 MARKS** can be awarded for 03, ie the candidate explains why unemployment will increase but doesn't focus upon "AD growing more slowly than the trend rate of growth".

MAXIMUM FOR PART 03: 12 MARKS

04 Extract B (Lines 6 – 8) states: ‘Measures designed to reduce the size of the budget deficit mean that it is inevitable that job losses in the public sector will continue during the years ahead.’

Using the data and your economic knowledge, discuss the view that the measures taken to reduce the size of the budget deficit will inevitably result in a rise in unemployment in the UK. (25 marks)

Extracts B and C provide some help to candidates and it is expected that they will make use of this material when developing their answers. It is anticipated that good answers will consider why measures to reduce the budget deficit may lead to an increase in unemployment, particularly in the short run, and why it is not necessarily inevitable that such measures will result in higher unemployment.

For this question, an answer should be limited to a maximum of 13 marks if there is no evidence of evaluation.

A maximum of **21 marks** may be awarded if there is no explicit use of the data, eg through the use of quotes or referring explicitly to the extracts.

Level 5	Good analysis <u>and</u> good evaluation	22-25 marks (mid-point 24)
Level 4	Good analysis <u>but</u> limited evaluation OR Reasonable analysis <u>and</u> reasonable evaluation	17-21 marks (mid-point 19)
Level 3	Reasonable answer, including some correct analysis but very limited evaluation	10-16 marks (mid-point 13)
Level 2	Weak with some understanding	4-9 marks (mid-point 7)
Level 1	Very weak	0-3 marks (mid-point 2)

Introduction	- Define the budget deficit. - State that reducing the deficit can be achieved by tax increases or cuts in government spending. - Some may recognise that growth in the economy will also help to reduce the deficit. - An outline of types/causes of unemployment.
Developing the response to the question: Application	- Display knowledge of the current size of the deficit and the programme for reducing the deficit. - Measures that have been adopted to reduce the deficit and how they are likely to impact on unemployment. - Use of data from Extract B to indicate that jobs have been lost in the public sector and that further job losses are likely. - Use of data from Extract C to indicate the scale of job losses in the public sector and the creation of new jobs in the private sector. - Knowledge of other developments in the UK and world economy that may have an impact on unemployment.

Developing the response to the question: Analysis	• The impact of cuts in public spending on jobs in the public sector. • The way in which cuts to public spending are likely to affect demand for private sector output and hence employment in the private sector. • The impact of tax rises on aggregate demand and hence employment. • The reduction in the deficit as a net withdrawal from the circular flow of income, reducing aggregate demand. • Possible multiplier effects of spending cuts and tax increases • Use of AD/AS diagrams. • Reasons why jobs in the private sector might increase to compensate for the loss of public sector jobs, eg low interest rates, the low exchange rate, returning confidence, renewed growth in the world economy, changes to the welfare system. • The importance of both supply-side and demand-side factors in determining what happens to unemployment.
Evaluation	• Use of the data from Extracts B and C to support arguments presented. • Use of own knowledge of recent developments in the UK economy, especially what has happened to unemployment since the start of 2011, to help support arguments presented. • Short-run versus long-run consequences of measures to reduce the size of the deficit. • The impact of the reduction in the deficit upon confidence and hence growth in the private sector. • An assessment of whether it is likely that job creation in the private sector is likely to be able to compensate for job losses in the public sector. • The problems of immobility and structural unemployment such as those referred to in Extract C. • The importance of the rate of growth of the economy as an influence on the overall level of unemployment • The impact of other policy measures on the overall level of unemployment. • The impact of developments in both the UK and world economy upon the overall level of unemployment.

*Examiners should note that credit can be given for basic evaluation if a candidate simply identifies some reasons why measures to reduce the budget deficit will increase unemployment **and** reasons why unemployment may not increase. Basic evaluation (and good analysis) would allow the answer to achieve low Level 4. Stronger evaluation is provided by candidates who are able to support their view of the impact on unemployment of measures to reduce the budget deficit by the use of evidence and/or sound economic analysis.*

**USE THE DETAILED LEVELS MARK SCHEME ON PAGES 5 & 6
WHICH OFFERS FURTHER GUIDANCE**

MAXIMUM FOR PART 04: 25 MARKS

OR

Context 2

05 Define the term 'cost-push inflation' (Extract F , line 8).	(5 marks)
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For an acceptable definition such as: - an increase in the price level (or average price of goods and services) caused by a sustained increase in firms' costs of production - where increased costs of production result in firms raising their prices leading to a rise in the price level (prices in general).	5 marks
Full marks should be awarded to a candidate who demonstrates a clear understanding of the term cost-push inflation even if the definition is not exactly the same as the acceptable examples quoted above.	

If the definition is inaccurate or incomplete award a maximum of 4 marks which may be broken down, for example, as follows:

Inflation caused by rising costs of production (ie inflation is not defined).	3 marks
For accurately defining inflation, eg the rate of increase in the price level.	2 marks
For an accurate diagram that correctly illustrates cost-push inflation.	2 marks
For stating that cost-push inflation is caused by supply-side factors/a reduction in aggregate supply	1 mark
For one or more examples of possible causes of cost-push inflation, such as: (i) Rapidly rising wages/earnings or trade union power (ii) Rising commodity/raw material/oil prices (iii) Rising import prices (iv) Increases in indirect taxes (v) Monopoly employers/profit-push inflation (vi) Fall in the exchange rate.	1 mark per example - up to a maximum of 2 marks for examples

Maximum of 4 marks if the definition is incomplete or inaccurate

MAXIMUM FOR PART 05: 5 MARKS

06 Using **Extract D**, identify **two** significant points of comparison between CPI inflation and the rate of growth in average earnings over the period shown. (8 marks)

Award up to 4 marks for each point made.

Identifies a significant point of comparison Makes accurate use of the data to support the comparison identified Unit of measurement given accurately	4 marks
Identifies a significant point of comparison Makes use of the data to support the comparison identified However, no unit of measurement is given and/or the unit of measurement is used/applied inaccurately and/or the dates aren't quoted or are inaccurate and/or only one piece of data is given when two are needed.	3 marks
Identifies a significant point of comparison No correct use of the data to support the feature identified.	2 marks
Identifies a significant feature of one data series but no comparison is made. Makes use of the data to support the feature identified Unit of measurement given accurately.	1 mark

If a candidate identifies more than 2 significant points of comparison, reward the best two.

Significant points include:

- CPI inflation was lower at the start of the period (1.7%) than at the end of the period (3.5%), whereas average earnings were growing more rapidly at the start of the period (4.4%) than at the end of the period (1.4%)
- CPI inflation peaked in the 3rd quarter of 2008 (4.8%), whereas the rate of growth of average earnings peaked in the 1st quarter of 2010 (4.7%)
- CPI inflation was lowest in the 3rd quarter of 2009 (1.2%) whereas the rate of growth of average earnings was lowest in the 1st quarter of 2009 (-0.2%)
- the rate of growth of average earnings is more volatile than CPI inflation (ranges from -0.2% to 4.7% compared to 1.2% to 4.8%)
- up until the 2nd quarter of 2008, the rate of growth of average earnings was always higher than CPI inflation (eg in the 1st quarter of 2007 the rate of growth of average earnings was 4.5% whereas CPI inflation was 2.9%)
- after the 1st quarter of 2008 (approx.), the rate of growth of average earnings and CPI inflation are far more volatile than in the earlier period **OR** after the 2nd quarter of 2008 there are times when CPI inflation is greater than the rate of growth of average earnings and vice versa. Either description must be supported by appropriate statistics
- CPI inflation is always positive whereas the growth of average earnings is negative in one quarter (eg the lowest rate of CPI inflation is 1.2% in the 3rd quarter of 2009 but in the 1st quarter of 2009 average earnings fell by 0.2%).

In this case, full marks can be awarded if the candidate states the point of comparison but only quotes the figure for the negative growth in average earnings (i.e. in the 1st quarter of 2009 the growth in average earnings was -0.2%). It must be stated that CPI inflation is always positive but it isn't necessary to quote a figure.

A margin of +/- 0.2% is permissible for either data series

MAXIMUM FOR PART 06: 8 MARKS

- 07** **Extract E** (line 2) states: 'Inflation has increased partly as a result of the fall in the value of the pound....'
- Using an appropriate diagram, explain why a fall in the exchange rate is likely to increase inflation. (12 marks)

The anticipated response for the diagram:

Figure 1

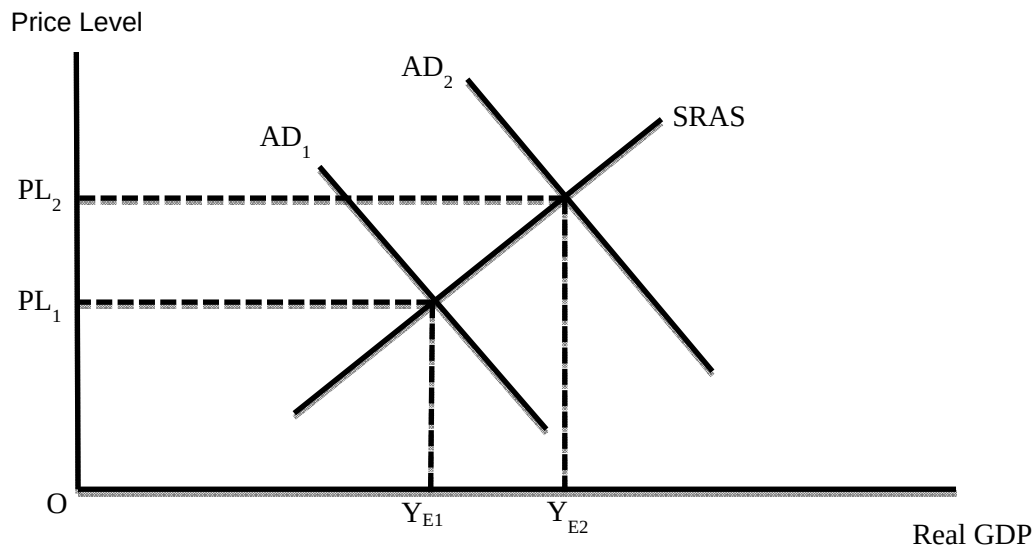
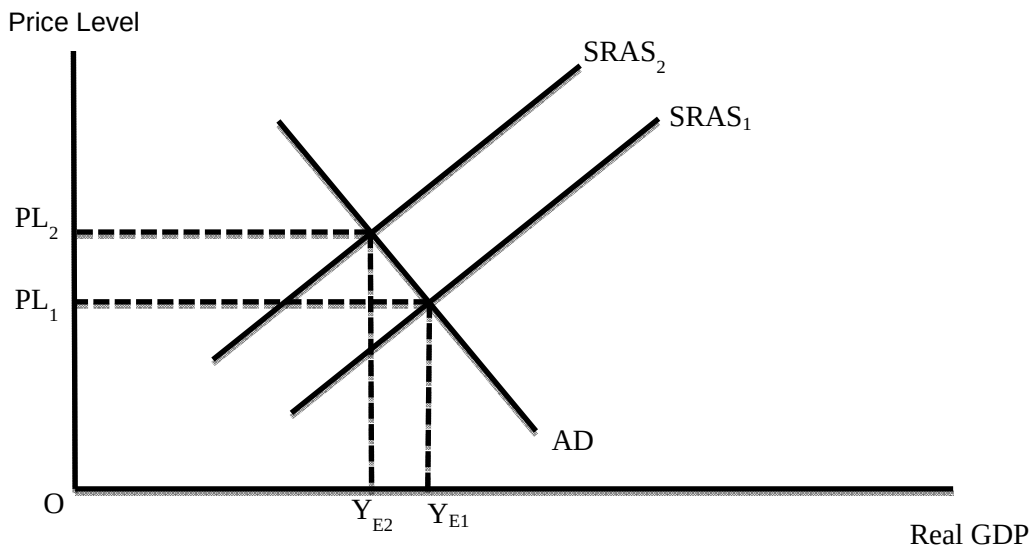


Figure 2



It is anticipated that most candidates will draw Figure 1 which shows that a fall in the exchange rate will improve the competitiveness of domestic products and hence shift AD to the right.

If a candidate draws Figure 2 showing a leftward shift in the SRAS curve, full marks can be awarded provided there is a reasonable explanation, eg the fall in the exchange rate will raise firms' costs due to a rise in the price of raw materials imported from abroad.

Full marks should also be awarded if the candidate shifts AD to the right AND shifts SRAS to the left, i.e. the rightward shift in AD showing the impact of improved competitiveness and the leftward shift in SRAS showing the impact of higher import costs.

Breakdown of the marks for the diagram:

Axes labelled (allow on the vertical axis: Inflation or PL or £ but not Price or P; allow on the horizontal axis: Real GDP, National Output, Output or Y but not Quantity or Q). Original AD (and AS curve) labelled correctly. Dotted lines and showing the original price level and level of real GDP (PL1 Y1).	1 mark
For showing a valid shift in the AD and/or AS curves	2 marks
Dotted lines and the associated labelling showing the new price level and new level of real GDP (PL2 Y2)	1 mark

Note:

- (i) To earn the first mark in the grid above, all three listed tasks must have been completed.
- (ii) Acceptable vertical axis labels are Price Level, PL or Inflation but NOT Price.
- (iii) Acceptable horizontal axis labels are Real National Output, Output, Y or Real GDP but NOT Quantity.

The anticipated written response:

For providing a relevant definition, eg, exchange rate, inflation, aggregate demand	1 mark per definition Up to a maximum of 2 marks
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Award up to 10 marks for each of the following explanations. 2 marks should be awarded for each logical link in the chain of reasoning.	
A fall in the exchange rate will reduce export prices and/or increase the price of imports (2 marks) this will increase the demand for UK products (2 marks). The rise in AD will create a buoyant environment in which firms can increase prices (2 marks) leading to demand-pull inflation (2 marks). This initial increase in prices will lead to higher wage demands (2 marks) increasing firms' costs and hence prices (2 marks).	Up to 10 marks
Links between a fall in the exchange rate, import prices, production costs and inflation.	Up to 10 marks

Up to a maximum of 10 marks for the written explanation if no diagram is attempted.

MAXIMUM FOR PART 07: 12 MARKS

08 Extract F (lines 17 – 19) states: 'In these circumstances, the Monetary Policy Committee of the Bank of England will raise Bank Rate to try to reduce inflation.'

Using the data and your economic knowledge, assess the view that the use of interest rates is the best way to control inflation in the UK. (25 marks)

Extracts D, E and F provide some help to candidates and it is expected that they will make use of this material when developing their answers. It is anticipated that good answers will consider the case for relying on the use of interest rates to control inflation and reasons why other instruments of policy may also be important if inflation is to be controlled without damaging other aspects of economic performance.

For this question, an answer should be limited to a maximum of 13 marks if there is no evidence of evaluation.

A maximum of **21 marks** may be awarded if there is no explicit use of the data, eg through the use of quotes or referring explicitly to the extracts.

Level 5	Good analysis <u>and</u> good evaluation	22-25 marks (mid-point 24)
Level 4	Good analysis <u>but</u> limited evaluation OR Reasonable analysis <u>and</u> reasonable evaluation	17-21 marks (mid-point 19)
Level 3	Reasonable answer, including some correct analysis but very limited evaluation	10-16 marks (mid-point 13)
Level 2	Weak with some understanding	4-9 marks (mid-point 7)
Level 1	Very weak	0-3 marks (mid-point 2)

Introduction	- define inflation - identify other possible policy measures, eg other elements of monetary policy, fiscal policy and supply-side policies - possible causes of inflation, eg demand-pull factors and cost-push factors.
Developing the response to the question:	- outline the role of the MPC in controlling inflation in the UK - use of Extract E to identify causes of changes in UK inflation, eg the increase in VAT - use of own knowledge to identify recent changes in the rate of inflation in the UK and the causes of such changes
Application	use of Extract F to identify other possible causes of inflation and to support the analysis of some of the causes of inflation, eg global food prices at record high.

Developing the response to the question: Analysis	• analysis of the demand-pull and cost-push inflationary processes • use of diagrams to help analyse the causes of inflation • explain how interest rates are used to influence aggregate demand • explain why controlling aggregate demand is important if inflation is to be controlled • how rising costs, eg, oil prices, wages and VAT increases, cause inflation – linked to the Extracts and earlier analysis • rising costs as part of the demand-pull inflationary process • the role of interest rates in moderating rising costs, eg wage costs • the use of fiscal policy as an instrument to help control inflation • the role of supply-side policies as a means of moderating inflationary pressures • other monetary instruments that may be used to control inflation, eg restrictions on the growth of money and credit, exchange rate policy • other policies that might be used to try to control inflation, eg, wage controls, trade union reforms.
Evaluation	• the advantages of using interest rates to control inflation, eg, excess demand is the fundamental cause of inflation, effective in reducing aggregate demand, flexibility, can be used as a signal and hence affect inflationary expectations • possible disadvantages of relying on interest rates to control inflation, eg raising interest rates may increase the measured rate of inflation, may not be effective in reducing external cost increases such as rising oil prices, possible conflicts with other policy objectives • use own knowledge and Extracts E and F to present evidence of the effectiveness of using interest rates to control inflation • the view that, in the long run, the only way to control inflation is to limit the growth of aggregate monetary demand • pros and cons of using fiscal policy to control inflation • pros and cons of using supply-side measures to control inflation • pros and cons of other measures that might be adopted to control inflation • the case for and against using a range of measures to control inflation • the UK as a very open economy in which inflation is strongly affected by events in the rest of the world • interest rates affect the exchange rate and hence can be used to influence the cost of imports • an overall assessment of whether or not the use of interest rates is the best way to control inflation in the UK.

Examiners should note that credit can be given for basic evaluation if a candidate simply identifies some of the arguments for and against relying on interest rates to control inflation. Basic evaluation (and good analysis) would allow the answer to achieve low Level 4. Stronger evaluation is provided by candidates who are able to support arguments both for and against the view that 'the use of interest rates is the best way to control inflation' by the use of evidence and/or sound economic analysis.

**USE THE DETAILED LEVELS MARK SCHEME ON PAGES 5 & 6
WHICH OFFERS FURTHER GUIDANCE**

MAXIMUM FOR PART 08: 25 MARKS



General Certificate of Education
Advanced Subsidiary Examination
January 2012

Economics

ECON2

Unit 2 The National Economy

Wednesday 18 January 2012 9.00 am to 10.15 am

For this paper you must have:

- an objective test answer sheet
 - a black ball-point pen
 - an AQA 8-page answer book.
- You may use a calculator.

Time allowed

- 1 hour 15 minutes

Section A (ECON2/1)

- Answer **all** questions on your objective test answer sheet.
- Use a black ball-point pen. Do **not** use pencil.
- Do all rough work in this question paper, **not** on your objective test answer sheet.

Section B (ECON2/2)

- Answer **EITHER** Context 1 **OR** Context 2.
- Use black ink or black ball-point pen. Pencil should only be used for drawing.
- Write the information required on the front of your answer book. The **Examining Body** for this paper is AQA. The **Paper Reference** is ECON2/2.

Information

- The maximum mark for this paper is 75.
- There are 25 marks for **Section A**. Each question carries one mark. No deductions will be made for wrong answers.
- There are 50 marks for **Section B**. The marks for questions are shown in brackets.
- You will be marked on your ability to:
 - use good English
 - organise information clearly
 - use specialist vocabulary where appropriate.

Advice

- You are advised to spend no more than 25 minutes on **Section A** and at least 50 minutes on **Section B**.

Section A: Objective Test

Answer **all** questions in **Section A**.

Each question carries 1 mark. No deductions will be made for wrong answers.

You are advised to spend no more than 25 minutes on **Section A**.

For each question there are four alternative responses, **A**, **B**, **C** and **D**. When you have selected the response which you think is the best answer to a question, mark this response on your objective test answer sheet. If you wish to change your answer to a question, follow the instructions on your objective test answer sheet.

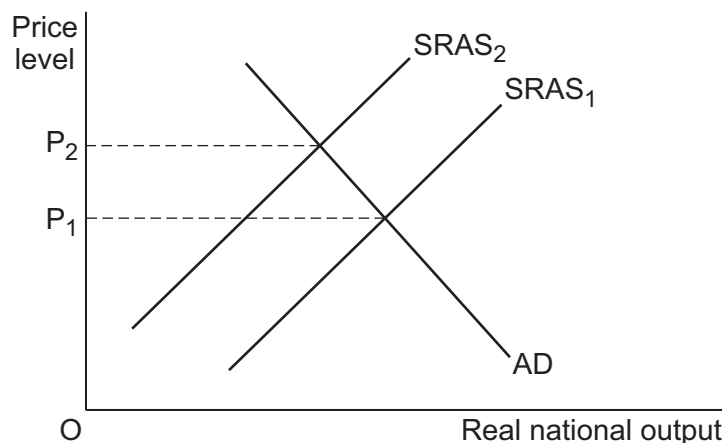
- 1 All other things being equal, lower inflation in an economy is most likely to be achieved if there is an increase in
- A productivity.
 - B exports.
 - C consumption.
 - D welfare benefits.
- 2 Structural unemployment is most likely to be caused by
- A a recession in the economy.
 - B changes in the demand for labour at different times of the year.
 - C an increase in the number of people changing jobs.
 - D the skills of the unemployed not matching those skills required for the available jobs.
- 3 The table below shows the index for nominal national income (GDP) and the price level index (CPI) for a country in 2009 and 2010.

	2009	2010
GDP	100	130
CPI	120	150

According to these figures, between 2009 and 2010 the country's real national income

- A increased.
- B decreased.
- C stayed the same.
- D changed by an amount which cannot be determined without further information.

- 4 Aggregate demand may fall as a result of a decrease in
- A savings relative to investment.
 - B the government's budget surplus.
 - C the government's budget deficit.
 - D imports.
- 5 All other things being equal, which one of the following sets of changes in an economy, **A**, **B**, **C** or **D**, would be most likely to bring about an improvement in its balance of payments deficit on current account?
- A A decrease in taxes on income, a fall in the exchange rate and a decrease in labour productivity
 - B An increase in taxes on income, a fall in the exchange rate and an increase in labour productivity
 - C An increase in government spending, a rise in the exchange rate and a decrease in labour productivity
 - D A decrease in government spending, a rise in the exchange rate and an increase in labour productivity
- 6 The diagram below represents an economy that has experienced inflation, with the price level rising from P_1 to P_2 .



The most likely cause of the inflationary pressures shown in the diagram is

- A a sustained increase in bank lending.
- B a growing budget deficit.
- C money wages increasing faster than productivity.
- D a period of time when interest rates are too low.

Turn over ►

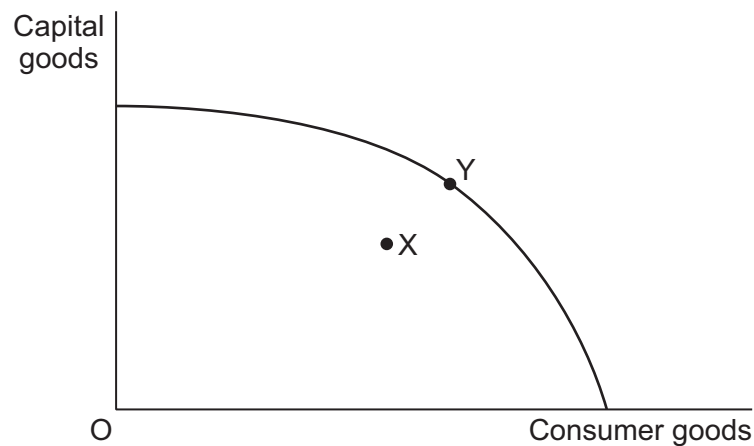
- 7 In 2010, the euro declined in value against other major currencies. All other things being equal, which one of the following combinations, **A**, **B**, **C** or **D**, indicates the most likely consequences for the economies of the eurozone?

Combination	Exports	Unemployment	Economic Growth
A	Increase	Decrease	Increase
B	Decrease	Increase	Decrease
C	Increase	Decrease	Decrease
D	Decrease	Increase	Increase

- 8 All other things being equal, more innovation in an economy is most likely to lead to

- A** a rise in the equilibrium price level.
- B** an increase in the trend rate of economic growth.
- C** a reduction in the country's international competitiveness.
- D** a fall in money spent on future research and development.

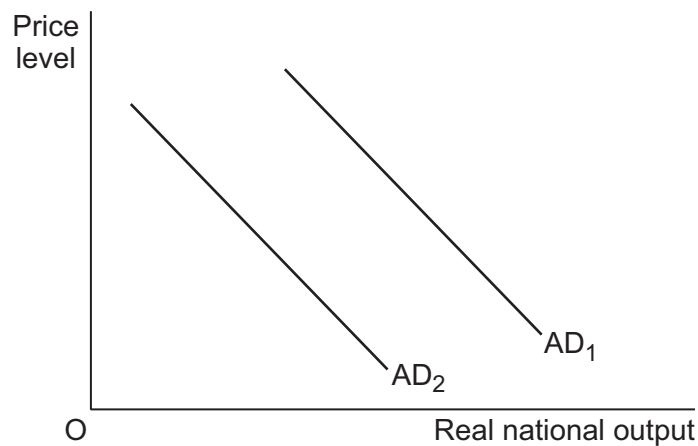
- 9 The diagram below shows an economy producing at point X within its production possibility frontier.



All other things being equal, which one of the following would be most likely to move the economy to point Y?

- A** An increase in interest rates and a reduction in exports
- B** An increase in household saving and a reduction in investment
- C** An increase in imports and a reduction in exports
- D** An increase in government spending and a reduction in the exchange rate

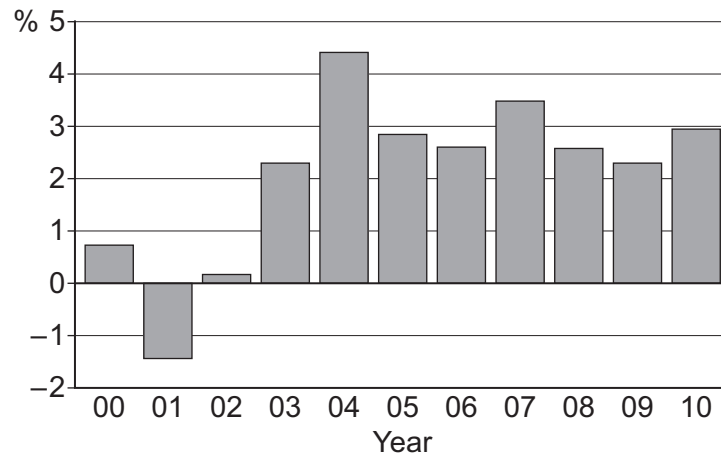
- 10 All other things being equal, which one of the following is most likely to cause the long-run aggregate supply curve to shift to the right?
- A The provision of funds by the banking system to finance investment in manufacturing
 - B An increase in consumption which causes a rise in the price level
 - C A rise in consumption which causes a fall in cyclical unemployment
 - D An increase in the provision of government unemployment-related benefits
- 11 The diagram below shows two aggregate demand (AD) curves for an economy.



The shift from AD_1 to AD_2 could be explained by an increase in

- A imports.
- B the price level.
- C costs of production.
- D investment.

- 12** The graph below shows the annual percentage change in an economy's Gross Domestic Product (GDP) between 2000 and 2010, at 2000 prices.



Assuming that inflation was constant at 2% each year, it can be concluded that

- A** real GDP decreased between 2007 and 2008.
 - B** real national output increased each year from 2002.
 - C** money GDP fell between 2000 and 2002.
 - D** real GDP was highest in 2004.
- 13** A sustained fall in the exchange rate is most likely to decrease
- A** inflation.
 - B** international competitiveness.
 - C** economic growth.
 - D** unemployment.
- 14** Which one of the following is a correct statement relating to the supply side of the economy?
- Supply-side improvements in the economy
- A** may originate in the business sector independently of government.
 - B** usually involve the use of monetary policy.
 - C** are designed to reduce the potential output of the economy.
 - D** are aimed mainly at the control of inflation.

- 15** The multiplier effect of an increase in investment in an economy is
- A** an increase in productive capacity.
 - B** a larger increase in national income than in investment.
 - C** an increase in the underlying trend rate of growth.
 - D** the movement of the economy from recession to boom.
- 16** All other things being equal, if inflation in the UK economy falls from 3% to 1%, it can be concluded that
- A** money incomes in the UK have decreased.
 - B** on average, the prices of goods and services in the UK have fallen.
 - C** UK goods have become more competitive in international markets.
 - D** the cost of living for the average person in the UK has continued to rise.
- 17** A country experiences both unemployment and persistent surpluses in the balance of payments. Which one of the following is most likely **both** to increase employment **and** to reduce a balance of payments surplus?
- A** Increasing interest rates
 - B** Increasing government expenditure
 - C** Increasing the government's budget surplus
 - D** A rise in the exchange rate
- 18** The table below shows changes in macroeconomic indicators for an economy. During a time of rising unemployment, labour productivity has increased whilst at the same time income per head has fallen.

All other things being equal, which combination, **A**, **B**, **C** or **D**, is most likely to result from these changes?

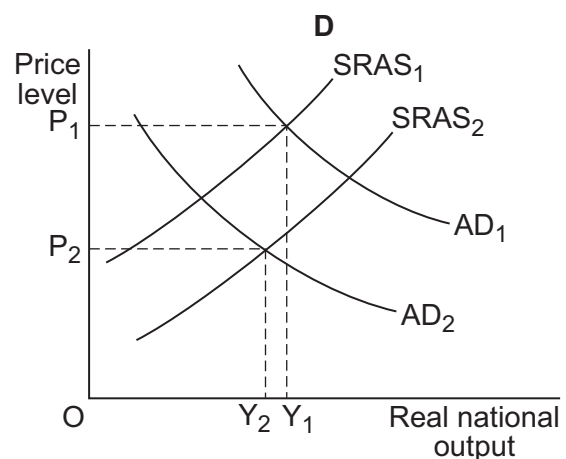
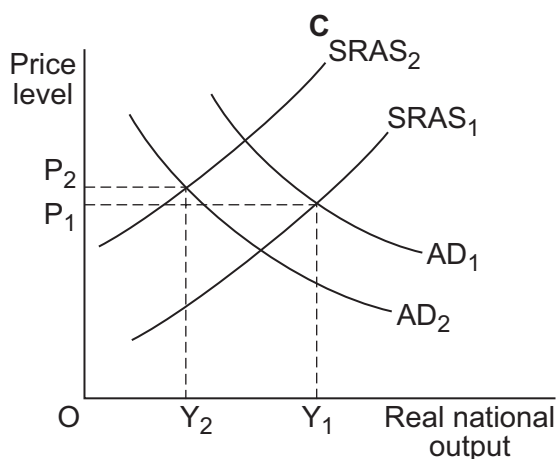
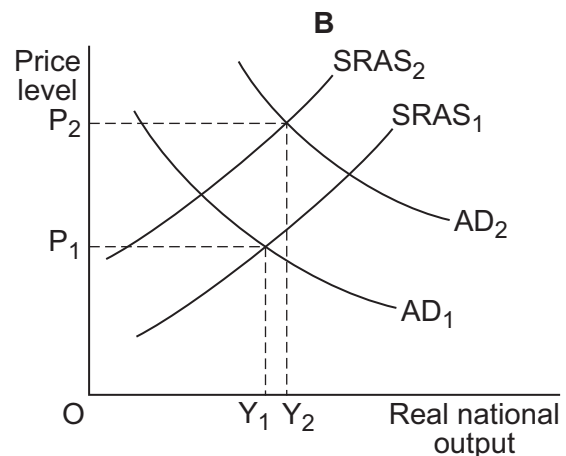
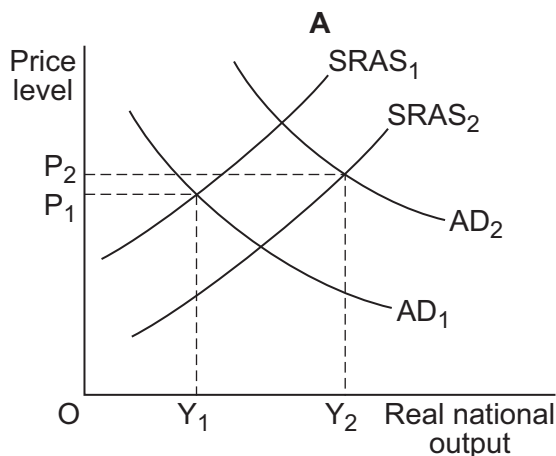
Combination	The rate of inflation	The balance of payments deficit on current account
A	Increases	Decreases
B	Decreases	Increases
C	Increases	Increases
D	Decreases	Decreases

- 19** In which one of the following situations is a government most likely to pursue an expansionary fiscal policy in order to increase aggregate demand?

When

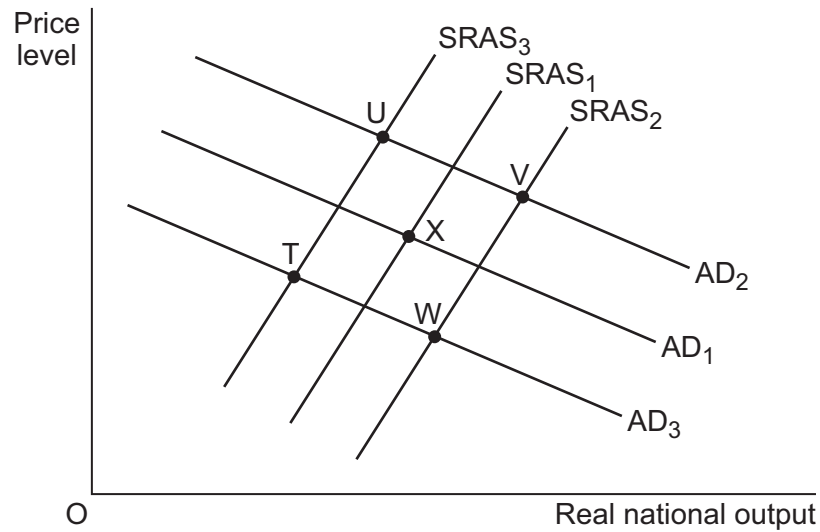
- A** there is a positive output gap
 - B** the long-run trend rate of economic growth is too low
 - C** there is a high level of structural unemployment
 - D** cyclical unemployment is increasing
- 20** The rapid expansion of large, developing economies such as China and India has led to rising world commodity prices and a larger market for the exports of countries such as the UK.

In the diagrams below, the initial equilibrium price level is P_1 and the initial equilibrium level of real national output is Y_1 . Which diagram, **A**, **B**, **C** or **D**, best illustrates the effects of such events on the UK economy?



-
- 21** Which one of the following is most likely to affect aggregate demand in the short run?
- A** An increased rate of innovation
 - B** An increase in labour productivity
 - C** An increase in government spending
 - D** An increase in the mobility of labour
- 22** In the short term, contractionary fiscal policy is most likely to cause
- A** a deterioration in the current account on the balance of payments.
 - B** a rise in unemployment.
 - C** a fall in export volumes.
 - D** an increase in the rate of inflation.
- 23** A conflict between macroeconomic policy objectives sometimes exists because
- A** demand-pull inflation requires action that increases aggregate demand.
 - B** costs can be reduced only if prices fall.
 - C** an increase in aggregate demand might reduce unemployment but result in a deterioration in the balance of payments on current account.
 - D** supply-side policies cannot be used alongside demand-management policies.
- 24** Which one of the following forms part of the institutional structure of an economy?
- A** The productivity of labour
 - B** Fiscal policy
 - C** The banking system
 - D** The underlying trend rate of growth

- 25** The diagram below shows the aggregate demand (AD) and short-run aggregate supply (SRAS) curves for an economy.



Given that X is the initial equilibrium position, what would be the new equilibrium position following an increase in the price of imported oil and a general restriction on bank lending in the economy?

- A** Point T
- B** Point U
- C** Point V
- D** Point W

**QUESTION 25 IS THE LAST
QUESTION IN SECTION A**

**On your answer sheet
ignore rows 26 to 50**

Now turn to page 12 for Section B

Turn over for Section B

Turn over ►

Section B: Data Response

Answer **EITHER** Context 1 **OR** Context 2.

You are advised to spend at least 50 minutes on **Section B**.

Total for this Context: 50 marks

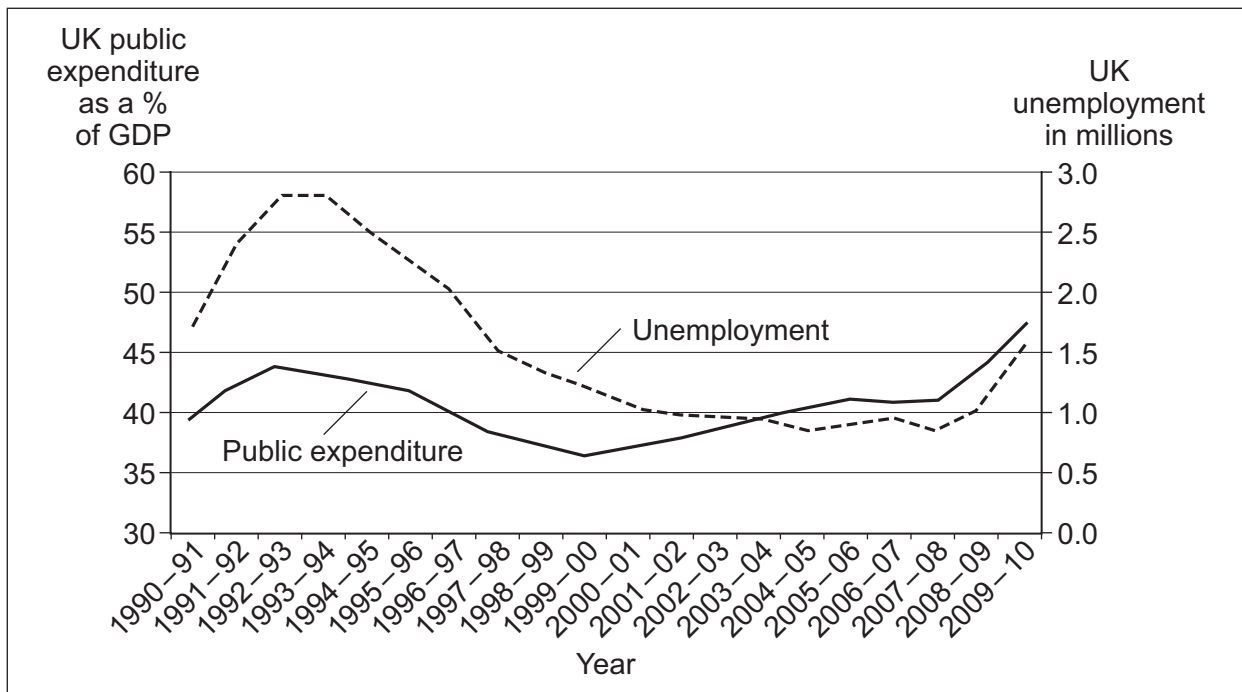
EITHER

Context 1

CUTTING PUBLIC EXPENDITURE IN THE UK

Study **Extracts A, B and C**, and then answer **all** parts of Context 1 which follow.

Extract A: UK public expenditure as a percentage of GDP and UK unemployment in millions, 1990–91 to 2009–10



Source: Office for National Statistics, October 2010

Extract B: The UK economy faces cuts in public spending

The UK economy faces a significant tightening of fiscal policy. This will be achieved primarily through reduced public sector expenditure, which includes spending on goods and services, benefit payments and wages paid to public sector employees. The measures introduced in the October 2010 Public Spending Review plan to cut government expenditure by £81 bn. This plan, laid out by the Coalition Government, implies the longest and deepest sustained period of cuts to public spending since the Second World War. It is inevitable that cuts of this size will reduce the quantity and quality of public services available.

1

5

The cuts in public expenditure are also likely to reduce aggregate demand. The disposable income of many households will fall, or grow more slowly, and some companies will face lower demand from the public sector for their goods and services. However, these effects on demand may be offset, to some extent, if the cuts in public spending improve confidence and reduce the risk of a rise in interest rates.

10

Source: news reports, October 2010

Extract C: Will cuts in public spending damage the economy?

Economists are divided over the impact that the cuts in public spending will have on the UK economy. Some argue that, while unemployment is high and people are not spending enough to provide full employment, the Government has to keep spending high to sustain the recovery and to avoid the risk of falling into another recession. Cuts in public spending will reduce company profits, lead to the cancellation of investment projects and damage the education of young people. In the long run, the quality of the labour force will deteriorate.

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However, if the Government does not reduce the size of the budget deficit, large-scale government borrowing could force up interest rates, destroying both business and consumer confidence. High interest rates are particularly damaging for the UK economy because of the high level of private sector debt. Reductions in public spending could also create opportunities for the private sector to fill the gap, encouraging more private sector investment.

10

Source: news reports, October 2010

0 1

Define the term 'disposable income' (**Extract B**, line 10).

(5 marks)

0 2

Using **Extract A**, identify **two** significant points of comparison between public expenditure as a percentage of GDP and unemployment over the period shown.

(8 marks)

0 3

Extract B (line 9) states that 'cuts in public expenditure are also likely to reduce aggregate demand'.

Explain why cuts in public expenditure are likely to reduce aggregate demand.

(12 marks)

0 4

Extract B (lines 5 – 7) states: 'This plan, laid out by the Coalition Government, implies the longest and deepest sustained period of cuts to public spending since the Second World War'.

Using the data and your economic knowledge, assess the likely impact of substantial cuts in public expenditure on the performance of the UK economy.

(25 marks)

Turn over ►

Do **not** answer Context 2 if you have answered Context 1.

Total for this Context: 50 marks

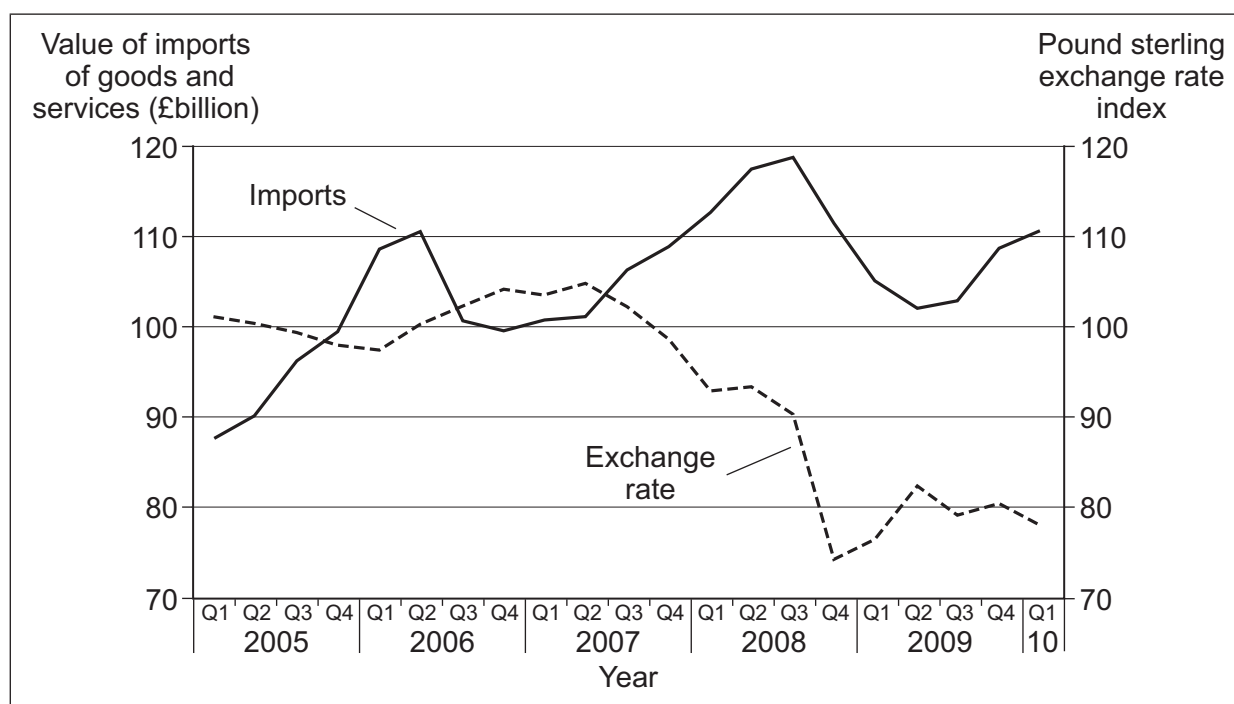
OR

Context 2

UK IMPORTS AND THE RECOVERY OF THE UK ECONOMY

Study **Extracts D, E and F**, and then answer **all** parts of Context 2 which follow.

Extract D: Total value of imports of goods and services (£billion) into the UK and the pound sterling exchange rate index, 2005 to 2010 (Q = quarter)



Source: Office for National Statistics, September 2010

Note: The pound sterling exchange rate index measures the value of the pound against a basket of other currencies.

Extract E: Spending on imports grows despite the fall in the value of the pound

The UK's balance of trade in goods and services improved at the start of the 2008–09 recession as the value of imports fell at a faster rate than exports. However, since the UK and global economies have started to recover, UK imports have grown at a faster rate than exports despite the large depreciation of the pound since the second quarter of 2007. The reduction in labour productivity during the recession also affected the competitiveness of home-produced goods.

1

5

Since the middle of 2009, imports have increased by 7%. The majority of the rise in imports since mid-2009 relates to increased imports of raw materials, semi-manufactured goods and vehicles. As the economy recovers, the manufacturing and construction sector will buy more inputs from abroad and hence some increase in imports is inevitable. However, the forthcoming rise in taxation, needed to reduce the budget deficit, should help to lessen the growth in household spending on foreign goods.

10

Source: news reports, September 2010

Extract F: Will a growing trade deficit damage the recovery from recession?

The UK's deficit on trade in goods widened to a record high in July after imports rose sharply and exports fell from the previous month. The goods deficit was £8.7 bn, the biggest deficit since figures began in 1998. However, trade in services produced a surplus of £3.8 bn. Nevertheless, the deficit on trade in goods and services widened to its highest value in almost five years. Imports increased by 3.1%, which was largely driven by an increase in imports of chemicals, pharmaceuticals, oil and semi-manufactures.	1 5
Although some of the deterioration reflects a sharp rise in imports, which is an indication of the strength of domestic demand, July's dreadful trade figures cast doubt over the ability of external trade to drive the recovery in the UK economy. With cuts in public spending and higher taxes on the horizon, the Government was hoping that the recovery would be secured by an injection of demand resulting from more exports and reduced spending on imports.	10

Source: news reports, September 2010

- 0 5** Define the term 'recovery' (**Extract F**, line 12). (5 marks)
- 0 6** Using **Extract D**, identify **two** significant points of comparison between the total value of imports of goods and services and the pound sterling exchange rate index over the period shown. (8 marks)
- 0 7** Explain how the value of imports into the UK is likely to be affected by **both** a fall in the value of the pound on the foreign exchange market **and** a reduction in UK labour productivity. (12 marks)
- 0 8** **Extract F** (lines 9 – 10) states that 'July's dreadful trade figures cast doubt over the ability of external trade to drive the recovery in the UK economy'.
- Using the data and your economic knowledge, evaluate the extent to which external trade can be relied upon to bring about a recovery in the UK economy. (25 marks)

END OF QUESTIONS

There are no questions printed on this page

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General Certificate of Education (A-level)
January 2012

Economics

ECON2

(Specification 2140)

Unit 2: The National Economy

Final

Mark Scheme

Mark schemes are prepared by the Principal Examiner and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation events which all examiners participate in and is the scheme which was used by them in this examination. The standardisation process ensures that the mark scheme covers the students' responses to questions and that every examiner understands and applies it in the same correct way. As preparation for standardisation each examiner analyses a number of students' scripts: alternative answers not already covered by the mark scheme are discussed and legislated for. If, after the standardisation process, examiners encounter unusual answers which have not been raised they are required to refer these to the Principal Examiner.

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of students' reactions to a particular paper. Assumptions about future mark schemes on the basis of one year's document should be avoided; whilst the guiding principles of assessment remain constant, details will change, depending on the content of a particular examination paper.

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Advanced Subsidiary Economics

January 2012

ECON2/1

Section A: Objective Test (ECON2/1)

The following list indicates the correct answers used in marking the students' responses.

KEY LIST

1.	A	9.	D	17.	B
2.	D	10.	A	18.	D
3.	A	11.	A	19.	D
4.	C	12.	B	20.	B
5.	B	13.	D	21.	C
6.	C	14.	A	22.	B
7.	A	15.	B	23.	C
8.	B	16.	D	24.	C
				25.	A

Advanced Subsidiary Economics

January 2012

ECON2/2

Mark Scheme

Section B: Data Response

General Instructions

Marks awarded to students should be in accordance with the following mark scheme and examiners should be prepared to use the full range of marks available. The mark scheme for most questions is flexible, permitting the student to score full marks in a variety of ways. Where the student's response to a question is such that the mark scheme permits full marks to be awarded, full marks **MUST** be given. A perfect answer is not necessarily required for full marks. But conversely, if the student's answer does not deserve credit, then no marks should be given.

Occasionally, a student may respond to a question in a reasonable way, but the answer may not have been anticipated when the mark scheme was devised. In this situation, **OR WHENEVER YOU HAVE ANY DOUBT ABOUT THE INTERPRETATION OF THE MARK SCHEME**, you must in the first instance telephone your team leader to discuss how to proceed.

Two approaches have been used in the construction of the mark scheme:

- (i) **An issue based approach.** The mark scheme for questions **01, 02, 03, 05, 06** and **07** of the data response questions adopts this approach. The mark scheme lists the marks that can be awarded for particular issues (and associated development) that the student might include in the answer.
- (ii) **A levels approach.** This approach is used for marking questions **04** and **08** of the data response questions. The Levels Mark Scheme on the next page identifies five levels representing differences in the quality of work. A range of marks is allocated at each level. First decide the level into which an answer falls. The level chosen should be the one which **best fits** the answer provided by the student. It is **not** intended that the answer should satisfy every statement in the level description. Then think in terms of awarding the mid-point mark which has been identified for that level (eg 13 marks for Level 3). Move up and down from this notional mark by considering the extent to which the answer meets the level description overall. Strength in one skill can outweigh weakness in another. When using the Levels Mark Scheme the marker **must** identify where a particular skill is being demonstrated. The **key** to be used to identify the skill is given after the levels descriptions. The question-specific mark scheme summarises the information which could be used to answer the question, but without attaching marks to particular issues.

**LEVELS OF RESPONSE MARK SCHEME
FOR USE WITH QUESTIONS 04 AND 08 ONLY**

AS LEVELS OF RESPONSE	AO1 KNOWLEDGE and UNDERSTANDING of theories, concepts and terminology	AO2 APPLICATION of theories, concepts and terminology	AO3 ANALYSIS of economic problems and issues	AO4 EVALUATION of economic arguments and evidence, making informed judgements
Level 5 22-25 marks (mid-point 24) Good analysis and good evaluation	Good throughout the answer with few errors and weaknesses	Good application to issues Good use of data to support answer	Relevant and precise with a clear and logical chain of reasoning	Good with a clear final judgement
Level 4 17-21 marks (mid-point 19) Good analysis <u>but</u> limited evaluation OR Reasonable analysis and reasonable evaluation	Good throughout the answer with few errors and weaknesses Good throughout much of the answer with few errors and weaknesses	Good application to issues Good use of data to support answer Some good application to issues. Some good use of data to support answer	Relevant and precise with a clear and logical chain of reasoning Largely relevant and well organised with reasonable logic and coherence	Limited but showing some appreciation of alternative points of view Reasonable, showing an appreciation of alternative points of view
Level 3 10-16 marks (mid-point 13) Reasonable answer, including some correct analysis but very limited evaluation	Satisfactory but some weaknesses shown	Reasonable application to issues Reasonable use of data to support answer	Reasonably clear but may not be fully developed and is perhaps confused in places with a few errors present	Superficial, perhaps with some attempt to consider both sides of the issue(s)
Level 2 4-9 marks (mid-point 7) Weak with some understanding	Limited and some errors are made	Partial application to issues with some errors Limited use of data to support answer	Partial but confused at times, lacking focus and development Limited logic and coherence	A very basic and simplistic attempt is made which is unsupported by analysis
Level 1 0-3 marks (mid-point 2) Very weak	Weak with a number of errors	Little, if any, application to issues No use of data to support answer	Poor and lacking clarity and focus	No relevant evaluation

THE KEY TO BE USED WHEN USING THE LEVELS MARK SCHEME

- D** Where a particular economic term is correctly **DEFINED** in order to help the student to answer the question properly.
- I** Where a relevant **ISSUE** is raised by the student.
- K** Where the student demonstrates **KNOWLEDGE** of recent developments or features of the economy which help enhance the student's response to the question. This should also be used where the student quotes relevant examples.
- Ap** Where the student demonstrates the ability to **APPLY** knowledge and **CRITICAL UNDERSTANDING** to problems and issues.
- An** Where the student demonstrates the ability to **ANALYSE** the problem using appropriate economic ideas.
- E** Where the student **EVALUATES** and makes judgements about the significance of various issues and arguments.

QUALITY OF WRITTEN COMMUNICATION

Quality of Written Communication (QWC) will be assessed in Questions 04 and 08 only.

Students will be assessed according to their ability to:

- ensure that text is legible, and that spelling, grammar and punctuation are accurate, so that meaning is clear
- select and use a form and style of writing appropriate to purpose and complex subject matter
- organise information clearly and coherently, using specialist vocabulary when appropriate.

No specific marks are awarded for QWC.

However, examiners should take into account QWC when determining the mark to be awarded for an answer. This means an answer could be taken either up (for exceptional QWC) or down (for very poor QWC) by 1 mark (and no more).

EITHER

Context 1

CUTTING PUBLIC EXPENDITURE IN THE UK

01	Define the term 'disposable income' (Extract B , line 10).	(5 marks)
-----------	--	-----------

For an acceptable definition such as: - gross income less income tax and national insurance contributions plus cash welfare benefits - the money that comes into a household from various sources, including welfare benefits but after taxes on income also allow - the amount of money/income that a household/individual has available to spend after tax has been deducted	5 marks
Full marks should be awarded to a candidate who demonstrates a clear understanding of the term 'disposable income' even if the definition is not exactly the same as the acceptable examples quoted above.	

If the definition is incomplete/inaccurate, marks may be broken down, for example, as follows:

Candidates who state that disposable income is the money that households have to spend after major items of expenditure, such as mortgage repayments, should be awarded a **maximum of 2 marks**. For example:

- 'the amount of money a household has to spend after bills and taxes' is worth **2 marks**
- 'the amount of money a household has to spend after paying bills' is worth **zero marks**

If the candidate states that it is the money/income that a household has available to spend (and save) then award **2 marks**.

For defining income, eg as a flow of money coming into a household	2 marks
For stating that it is income after tax	2 marks
For stating that it is after national insurance contributions have been deducted	1 mark
For stating that it includes welfare benefits	1 mark
For one or more examples of a source of income, other than welfare benefits, eg wages or dividends.	1 mark

Maximum of 4 marks if the definition is incomplete

MAXIMUM FOR PART 01: 05 MARKS

02 Using **Extract A**, identify **two** significant points of comparison between public expenditure as a percentage of GDP and unemployment over the period shown.
(8 marks)

Award up to 4 marks for each point made.

Identifies a significant point of comparison. Makes accurate use of the data to support the point of comparison. Unit of measurement given accurately (millions/% of GDP or %)	4 marks
Identifies a significant point of comparison. Makes use of the data to support the comparison identified. However, only one piece of data is given when two are needed to make a valid comparison and/or no unit of measurement is given and/or the unit of measurement is used/applied inaccurately.	3 marks
Identifies a significant point of comparison. No use of correct data to support the comparison identified.	2 marks
Identifies a significant feature of the data but no comparison is made Makes use of the data to support the feature identified Unit of measurement given accurately	1 mark

If a candidate identifies more than two significant points of comparison, reward the best two ('significant' such as highs, lows or major changes/trends over a period of time).

The significant points of comparison include:

- public expenditure as a % of GDP was lower at the start of the period (39% of GDP) than at the end of the period (approx. 47% of GDP) whereas unemployment was higher at the start of the period (1.7 million) than at the end of the period (1.6 million)
- public expenditure as a % of GDP peaked at the end of the period, i.e. in 2009-10 (approx. 47 % of GDP) whereas unemployment peaked between 1992 and 1994 at 2.8 million
- public expenditure as a % of GDP was lowest in 1999-2000 (36% of GDP) whereas unemployment was at its lowest in 2004-05 and 2007-08 at 0.8 million
- both series fluctuated over the period. Public expenditure as a % of GDP fluctuated between 36% in 1999-2000 and approx. 47% in 2009-10. Unemployment fluctuated between 2.8 million (1992-93 & 1993-94) and 0.8 million (2004-05 & 2007-08)
- between 1992-93 and 1999-2000, public expenditure fell as a % of GDP (44% to 36%) whereas unemployment started to fall in 1994-95 and did not really start to rise again until 2008-09 (2.8 million to 0.8 million)
- between 1999-2000 and 2009-2010, public expenditure rose as a % of GDP (36% to approx. 47%) whereas unemployment continued to fall slowly (or was fairly stable) after 1999-00 and didn't start to rise again until 2007-08 (between 2007-08 and 2009-10 it rose from 0.8 million to 1.6 million)
- there is some evidence of a positive/direct (but NOT proportional) relationship between unemployment and public expenditure as a % of GDP (eg between 1993/94 and 1999/00)

unemployment fell from 2.8 million to 1.2 million whilst public expenditure fell from approx. 47% of GDP to 36% of GDP)

The figures quoted above are approximations and the candidate should be allowed, without penalty, a margin of **plus or minus 1%** for the GDP figures and **plus or minus 0.1 million** for the unemployment figures.

MAXIMUM FOR PART 02: 8 MARKS

03 Extract B (line 9) states that ‘cuts in public expenditure are also likely to reduce aggregate demand’.

Explain why cuts in public expenditure are likely to reduce aggregate demand.
(12 marks)

For a candidate who provides a relevant definition, eg public expenditure, aggregate demand. Do not credit a definition of disposable income.	1 mark per definition Up to a maximum of 2 marks
For stating that public expenditure is a component of aggregate demand and hence if public expenditure falls so will aggregate demand. This statement might be linked to the AD equation. It is not sufficient to say ‘government spending falls and so aggregate demand falls’.	2 marks

Award up to 6 marks for each of the following elements of the explanation.

For stating that some public expenditure is on goods and services produced by the private sector (2 marks), for example roads, medicines and tanks (2 marks for an example), if the government spend less money on these items, firms will experience a fall in demand for their products/services (2 marks).	Up to 6 marks
For stating that cuts in welfare benefits (2 marks) will reduce disposable income (2 marks) and hence reduce consumption/aggregate demand (2 marks).	Up to 6 marks
For explaining how public sector job cuts will reduce aggregate demand.	Up to 6 marks
For explaining how the multiplier effect of a fall in public expenditure leads to further reductions in aggregate demand. To gain these marks, the explanation must follow from a valid reason why a cut in public spending will lead to an initial reduction in aggregate demand.	Up to 6 marks
For any other relevant explanation, eg public expenditure cuts reducing injections into the circular flow of income.	Up to 6 marks

If there is more than one logical chain of reasoning used by the candidate to explain why a fall in public expenditure will reduce aggregate demand, only award 2 marks for ‘and hence aggregate demand/spending/consumption will reduce/fall’ once.

Award **up to 4 additional marks** for the use of relevant diagrams. An example of an acceptable diagram is one that shows that a cut in public expenditure will shift the aggregate demand curve to the left. The diagram may or may not include an AS curve.

Do **not** give marks for the diagram if the associated written explanation invalidates the diagram.

Breakdown of the marks for the diagram:

Axes labelled (allow on the vertical axis: Inflation or PL or £ but not Price or P; allow on the horizontal axis: Real GDP, National Output, Output or Y but not Quantity or Q). Original AD (and AS curve) labelled correctly. Dotted lines and showing the original price level and level of real GDP (PL_1 Y_1).	1 mark
Leftward shift in the AD curve	2 marks
Dotted lines and the associated labelling showing the new lower level of real GDP (PL_2 Y_2) at the same given price level	1 mark

MAXIMUM FOR PART 03: 12 MARKS

04 **Extract B** (lines 5-7) states: ‘This plan, laid out by the Coalition Government, implies the longest and deepest sustained period of cuts to public spending since the Second World War’.

Using the data and your economic knowledge, assess the likely impact of substantial cuts in public expenditure on the performance of the UK economy.
(25 marks)

For this question, an answer should be limited to a maximum of 13 marks if there is no evidence of evaluation.

A maximum of **21 marks** may be awarded if there is no explicit use of the data.

Level 5	Good analysis <u>and</u> good evaluation	22-25 marks (mid-point 24)
Level 4	Good analysis <u>but</u> limited evaluation OR Reasonable analysis <u>and</u> reasonable evaluation	17-21 marks (mid-point 19)
Level 3	Reasonable answer, including some correct analysis but very limited evaluation	10-16 marks (mid-point 13)
Level 2	Weak with some understanding	4-9 marks (mid-point 7)
Level 1	Very weak	0-3 marks (mid-point 2)

Extracts A, B and C provide some help to candidates and it is expected that they will make use of this material when developing their answers. It is anticipated that good answers will consider both the short-run and long-run effects of public spending cuts for different aspects of economic performance. They are also likely to assess both the demand-side and supply-side consequences. Candidates should also be rewarded for relevant discussion of the microeconomic consequences but, on this paper, this aspect of the debate should not be the main focus of their answers.

Likely issues and areas for discussion:

Introduction	- the nature of government expenditure - explanation of economic performance and the objectives of economic policy - a brief outline of the reasons for cuts in government spending related to the size of the budget deficit.
Developing the response to the question: Application	- the current state of the UK economy and the role of aggregate demand in, for example, sustaining recovery from recession - the impact of public spending cuts on the budget balance and hence government borrowing in the UK - the impact on levels of taxation in the UK (perhaps based on the assumption that the budget deficit has to be reduced).

	- the impact on interest rates (picking up on the references in Extracts B and C) and the related consequences for UK economic performance - microeconomic implications for particular sectors of the UK economy, eg the impact on individual public services, the construction industry, the distribution of income, regional consequences - use of the data in the extracts, or own knowledge of the UK economy, to help develop any other relevant points.
Developing the response to the question: Analysis	- the effect of cuts in government spending and aggregate demand upon economic performance, eg employment, growth, inflation and the balance of payments - the multiplier effects - use of diagrams to illustrate possible demand-side consequences of public spending cuts - the likely impact of public spending cuts on the supply-side performance of an economy and the link with macroeconomic performance - use of diagrams to illustrate possible supply-side consequences of public spending cuts - the possible impact of spending cuts on consumer and business confidence and the resulting effects on private sector spending - microeconomic aspects of spending cuts - possible opportunities for growth in the private sector resulting from cuts in public spending.
Evaluation	- the extent to which, if at all, cuts in public spending are unavoidable given the size of the budget deficit - possible alternatives to cuts in public sector spending, eg increases in taxation, and their relative merits - the likelihood that the growth in private sector spending will compensate for the fall in public spending - use of evidence from the performance of the UK economy since the cuts were first implemented - discussion of the effectiveness of mechanisms through which the reduction in public sector spending might lead to a compensating increase in private spending, eg lower interest rates, lower exchange rate, less need for tax increases - discussion of extent to which the supply-side consequences are likely to be detrimental or possibly advantageous - the extent to which cuts in public spending can be achieved without harming the services provided to the general public - the distributional effects, eg are the cuts likely to fall disproportionately on the poor and/or people living in northern conurbations? - short-run versus long-run consequences - other factors that might affect the impact of cuts in public spending on economic performance, eg the growth in the world economy, the nature of the cuts, what happens to the exchange rate, the effect on industrial relations.

Examiners should note that credit can be given for basic evaluation if a candidate simply identifies some of the arguments for and against cutting public spending. Basic evaluation (and good analysis) would allow the answer to achieve low Level 4. Stronger evaluation is provided by candidates who are able to support arguments both for and against cuts in public spending by the use of evidence and/or sound economic analysis.

**USE THE DETAILED LEVELS MARK SCHEME ON PAGES 5 AND 6
FOR FURTHER CLARIFICATION**

MAXIMUM FOR PART 04: 25 MARKS

OR

Context 2

UK IMPORTS AND THE RECOVERY OF THE UK ECONOMY

05	Define the term 'recovery' (Extract F , line 12).	(5 marks)
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For an acceptable definition such as: - a phase of the economic cycle, after a recession/depression, during which real GDP starts to increase and unemployment begins to fall - it is a time when the economy begins to grow again after it has been in recession/depression/slump.	5 marks
Full marks should be awarded to a candidate who demonstrates a clear understanding of the term 'recovery' even if the definition is not exactly the same as the acceptable examples quoted above.	

If the definition is incomplete, marks may be broken down, for example, as follows:

When there is a rise in real GDP/national income/output or the economy starts to grow	2 marks
When the economy is coming out of recession	2 marks
When an economy is getting back to its trend rate of growth	2 marks
When an economy moves from a negative output gap to a positive output gap	2 marks
When unemployment is falling and/or employment is increasing.	2 marks
For an accurate and correctly labelled diagram that shows the recovery phase of the economic cycle <u>or</u> a production possibility diagram showing the economy moving from a point inside the boundary towards the boundary <u>or</u> an AD/AS diagram showing a reduction in the negative output gap	2 marks
A time when aggregate demand is rising	1 mark
For stating it is a phase of the economic cycle	1 mark

Maximum of 4 marks if the definition is incomplete

MAXIMUM FOR PART 05: 5 MARKS

- 06** Using **Extract D**, identify **two** significant points of comparison between the total value of imports of goods and services and the pound sterling exchange rate index over the period shown. **(8 marks)**

Award up to 4 marks for each point made.

Identifies a significant point of comparison. Makes accurate use of the data to support the point of comparison. Unit of measurement given accurately (£billion or £bn/index points or index).	4 marks
Identifies a significant point of comparison. Makes use of the data to support the point of comparison. However, only one piece of data is given when two are needed to make a valid comparison and/or no unit of measurement is given and/or the unit of measurement is used/applied inaccurately.	3 marks
Identifies a significant point of comparison. No use of correct data to support the comparison identified.	2 marks
Identifies a significant feature of the data but no comparison is made Makes use of the data to support the feature identified Unit of measurement given accurately	1 mark

If a candidate identifies more than two significant points of comparison, reward the best two ('significant' such as highs, lows or major changes/trends over a period of time).

The significant points of comparison include:

- the value of imports was lower at the start of the period (£88 billion) than at the start of the period (£110 billion) whereas the exchange rate index was higher at the start of the period (index of 101) than at the end of the period (index of 78)
- the value of imports peaked in 2008 Q3 (£119bn) whereas the exchange rate index peaked in 2007 Q2 (index of 105)
- the value of imports was lowest in 2005 Q1 (£88bn) whereas the exchange rate index was lowest in 2008 Q4 (index of 74)
- the value of imports and the exchange rate index both showed significant fluctuations. The value of imports fluctuated between £88bn in 2005 Q1 and £119bn in 2008 Q3 and the exchange rate index fluctuated between 74 index points in 2008 Q4 and 105 index points in 2007 Q2
- there is some evidence of an inverse relationship between the sterling exchange rate index and the value of imports, eg between 2007 Q2 and 2008 Q3, the exchange rate index fell from 105 to 80 index points whilst the value of imports rose from £101 billion to £119 billion.

The figures quoted above are approximations and the candidate should be allowed, without penalty, a margin of **plus or minus £2 billion** for the figures for value of imports and **plus or minus 2 index points** for the exchange rate index figures.

MAXIMUM FOR PART 06: 8 MARKS

07 Explain how the value of imports into the UK is likely to be affected by **both** a fall in the value of the pound on the foreign exchange market **and** a reduction in UK labour productivity. (12 marks)

For a candidate who provides a relevant definition, eg value of imports, fall in the value of the pound, labour productivity
Do **not** credit a definition of recovery.

1 marks per definition
Up to a maximum of 2 marks

For explaining how a fall in the value of the pound will affect the value of imports:

A fall in the value of the pound leads to a rise in the (sterling) price of imports into the UK (**2 marks**), imports are now less competitive (relatively dearer) than products produced in the UK (**2 marks**), as a result, the quantity of imports purchased is likely to decrease (**2 marks**), the impact on the value of imports depends on the resulting change in the quantity demanded (some might mention the price elasticity of demand) (**2 marks**).

Marks can also be awarded, **within the 8 mark constraint**, for recognising that some firms might absorb the impact of the fall in the exchange rate and leave prices unchanged.

Note: Candidates do not have to state that it is the *sterling* price of imports that rises. However, if a candidate explains why the sterling price rises then an **extra 2 marks** can be awarded but the overall constraint of 8 marks still applies.

Up to 8 marks

For explaining how a reduction in labour productivity will affect the value of imports:

A fall in labour productivity leads to a rise in firms' (unit) costs of production (**2 marks**), firms are likely to raise their prices (**2 marks**), this means imports are now more competitive in the domestic market (**2 marks**), and hence the quantity of imports purchased rises (**2 marks**), leading to a rise in the amount spent (value) on imports (**2 marks**).

Up to 8 marks

If an answer attempts to analyse the overall impact of a fall in the exchange rate combined with a fall in labour productivity on the value of imports award **2 marks**.

Award **up to 4 additional marks** for the use of relevant diagrams. An example is a diagram that shows a demand curve for imports which is used to illustrate the impact of a rise in price upon the amount spent on imports. Other acceptable diagrams include: a diagram that shows **either** a rightward shift in the AD curve as a result of a fall in the exchange rate **or** a leftward shift in the AS curve, and hence a movement along the AD curve, resulting from a fall in labour productivity.

Do **not** give marks for the diagram if the associated written explanation invalidates the diagram, eg if the explanation only relates to rising exports and this is the justification for shifting the AD curve to the right.

Breakdown of the marks for the diagram:

Axes labelled (allow on the vertical axis: Inflation or PL or £ but not Price or P; allow on the horizontal axis: Real GDP, National Output, Output or Y but not Quantity or Q). Original AD (and AS curve) labelled correctly. Dotted lines and showing the original price level and level of real GDP (PL ₁ Y ₁). NB Price and quantity is required for the labels on the axes if a micro diagram is used to show the 'demand for imports' rather than AD.	1 mark
Correct shift in the curve (or movement along the curve if a micro diagram is used to show the impact of the rise in the price of imports resulting from a fall in the exchange rate)	2 marks
New dotted lines and the associated labelling showing the new position (this will depend on the diagram drawn)	1 mark

No marks should be awarded for explanations that relate to the value of exports

A **maximum of 10 marks** can be awarded if **ONLY** the effect of a fall in the value of the pound **OR** a reduction in labour productivity is attempted.

MAXIMUM FOR PART 07: 12 MARKS

08 **Extract F** (lines 9-10) states that ‘July's dreadful trade figures cast doubt over the ability of external trade to drive the recovery in the UK economy’.

Using the data and your economic knowledge, evaluate the extent to which external trade can be relied upon to bring about a recovery in the UK economy.
(25 marks)

For this question, an answer should be limited to a maximum of 13 marks if there is no evidence of evaluation.

A maximum of **21 marks** may be awarded if there is no explicit use of the data.

Level 5	Good analysis <u>and</u> good evaluation	22-25 marks (mid-point 24)
Level 4	Good analysis <u>but</u> limited evaluation OR Reasonable analysis <u>and</u> reasonable evaluation	17-21 marks (mid-point 19)
Level 3	Reasonable answer, including some correct analysis but very limited evaluation	10-16 marks (mid-point 13)
Level 2	Weak with some understanding	4-9 marks (mid-point 7)
Level 1	Very weak	0-3 marks (mid-point 2)

Extracts D, E and F provide some help to candidates and it is anticipated that they will make use of this material when developing their answers. It is expected that the better candidates will recognise that exports represent an injection into the circular flow of income and that a rise in exports is likely to increase aggregate demand and help the economy to recover from recession. They should also appreciate that an increase in imports and a rising trade deficit represent a net withdrawal from the circular flow and may inhibit recovery. However, the better candidates are also likely to recognise that a growing trade deficit might be the consequence of the increase in prosperity and economic activity that occurs when the economy is recovering from recession and hence a growing trade deficit will not necessarily harm recovery.

Like issues and areas for discussion:

Introduction	• definitions, eg deficit on the balance of trade • the characteristics of an economy recovering from recession • a diagram to illustrate the recovery phase of the economic cycle • the role of aggregate demand in stimulating recovery.
Developing the response to the question: Application	• the consideration of recent changes in the UK external trade and the possible impact on recovery, eg the rise in the deficit as indicated in Extract F • the current state of the UK economy

	- the significance of changes in external trade given the prospects for other components of aggregate demand in the UK, eg public expenditure cuts and the effect of higher taxes - changes in the value of sterling, perhaps using the data in Extract D - use of the data in the extracts, or own knowledge of the UK economy, to help develop any other relevant points.
Developing the response to the question: Analysis	- the effect of a change in exports on aggregate demand - the effect of a change in imports on aggregate demand - why external trade can help support or hinder recovery - a trade deficit as a net withdrawal from the circular flow of income and its impact on aggregate demand - possible multiplier effects - the impact of aggregate demand upon economic activity and hence recovery from recession - the use of a suitable diagram to illustrate the above. - more fundamental causes of the growing trade deficit, eg slow growth in export markets, lack of competitiveness - reasons why, in the recovery phase, imports might increase, eg more imports of raw materials and components, more imports of consumer goods fuelled by rising incomes - the government might have to adopt policies to reduce the deficit which affect the recovery - other ways in which external trade might help to support recovery, eg increased imports of capital goods.
Evaluation	- discussion of the differing impacts that external trade can have on recovery from recession, eg depending on whether the trade balance is in deficit or surplus and whether it is growing or shrinking - the significance of a growing trade deficit (or surplus) depends on whether it is persistent or whether it is temporary - it also depends on the size of the trade deficit (or surplus) (some might discuss the size of the deficit as a percentage of GDP) - it depends on the cause of the deficit (or surplus), eg rising (or falling) imports, falling (or rising) exports, rate of growth in export markets - is the impact on aggregate demand of a growing trade deficit (or surplus) may offset by changes in other components of demand - the relevance of what happens to the sterling exchange rate - if a growing deficit is due to low productivity, a general lack of competitiveness and inadequacies on the supply-side of the economy then its impact on recovery will be serious - if the increase in the deficit is due to rising imports of capital goods and intermediate goods it may be advantageous and help to support the recovery - relevance of external trade to the UK, given the prospect of significant cuts in public expenditure.

Examiners should note that credit can be given for basic evaluation if a candidate simply identifies some of the favourable and unfavourable consequences of external trade for an economy recovering from recession. Basic evaluation and good analysis would allow the answer to achieve low Level 4. Stronger evaluation is provided by candidates who are able to use evidence and/or sound economic analysis to support their assessment of the impact of external trade on the ability of the UK economy to recover from recession. Good evaluation will also include a supported final judgement that considers the extent to which an external trade deficit is likely to affect the recovery from recession in the UK.

**USE THE DETAILED LEVELS MARK SCHEME ON PAGES 5 AND 6
FOR FURTHER CLARIFICATION**

MAXIMUM FOR PART 08: 25 MARKS



General Certificate of Education
Advanced Subsidiary Examination
January 2011

Economics

ECON2

Unit 2 The National Economy

Wednesday 19 January 2011 9.00 am to 10.15 am

For this paper you must have:

- an objective test answer sheet
 - a black ball-point pen
 - an AQA 8-page answer book.
- You may use a calculator.

Time allowed

- 1 hour 15 minutes

Instructions

- In **Section A**, answer **all** questions on your objective test answer sheet.
- In **Section B**, answer **EITHER** Question 26 **OR** Question 27 in your AQA answer book.
- For **Section A**, do all rough work in this question paper, **not** on your objective test answer sheet.

Section A (ECON2/1)

- Use a black ball-point pen. Do **not** use pencil.

Section B (ECON2/2)

- Use black ink or black ball-point pen. Pencil should only be used for drawing.
- Write the information required on the front of your answer book. The **Examining Body** for this paper is AQA. The **Paper Reference** is ECON2/2.

Information

- The maximum mark for this paper is 75.
- There are 25 marks for **Section A** and 50 marks for **Section B**.
- In **Section A**, each question carries 1 mark. No deductions will be made for wrong answers.
- In **Section B**, the marks for questions are shown in brackets.
- You will be marked on your ability to:
 - use good English
 - organise information clearly
 - use specialist vocabulary where appropriate.

Advice

- You are advised to spend no more than 25 minutes on **Section A** and at least 50 minutes on **Section B**.

Section A: Objective Test

Answer **all** questions in **Section A**.

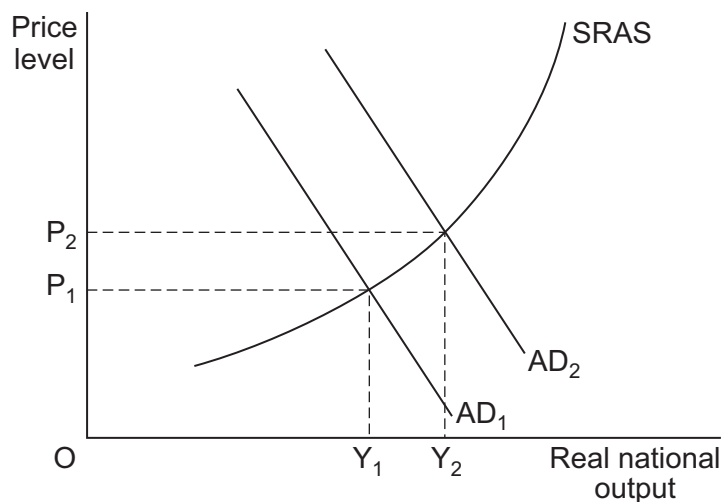
Each question carries 1 mark. No deductions will be made for wrong answers.

You are advised to spend no more than 25 minutes on **Section A**.

For each question there are four alternative responses, **A**, **B**, **C** and **D**. When you have selected the response which you think is the best answer to a question, mark this response on your objective test answer sheet. If you wish to change your answer to a question, follow the instructions on your objective test answer sheet.

- 1 Which one of the following would be an example of a loosening of fiscal policy?
 - A A fall in the money supply
 - B A rise in the rate of inflation
 - C A fall in interest rates
 - D A rise in the government budget deficit

- 2 The diagram below shows two aggregate demand (AD) curves and the short-run aggregate supply (SRAS) curve for an economy.



Which one of the following could explain the shift of the aggregate demand curve from AD_1 to AD_2 ?

An increase in

- A exports
- B savings
- C the exchange rate
- D rates of taxation

- 3 Economic growth is usually measured by the annual change in
- A the retail price index.
 - B real national income.
 - C the output of the manufacturing industry.
 - D consumer expenditure.
- 4 Which one of the following is most likely to result in a demand-side shock to the UK economy?
- A large rise in
- A world commodity prices
 - B UK wages due to a wave of strikes
 - C UK interest rates
 - D the price of imported semi-manufactured goods
- 5 The relationship between the growth of national income and the resulting increase in investment is termed the
- A accelerator.
 - B output gap.
 - C economic cycle.
 - D multiplier.
- 6 All other things being equal, which one of the following combinations, **A**, **B**, **C** or **D**, is most likely to lead to a deterioration in the UK balance of payments on current account?

	UK inflation rate	Exchange rate of the £	UK unemployment
A	Increase	Decrease	Decrease
B	Decrease	Increase	Increase
C	Increase	Increase	Decrease
D	Decrease	Decrease	Increase

- 7 The Monetary Policy Committee (MPC) of the Bank of England meets each month to decide on the rate of interest that is most likely to help it achieve the government's inflation target.

The MPC is most likely to decrease interest rates if

- A inflation is above target and the exchange rate is high and rising.
- B the rate of growth of money wages is above the rate of growth of labour productivity.
- C employment is rising.
- D there is a negative output gap.

- 8 All other things being equal, which one of the following is most likely to lead to a decrease in aggregate demand?

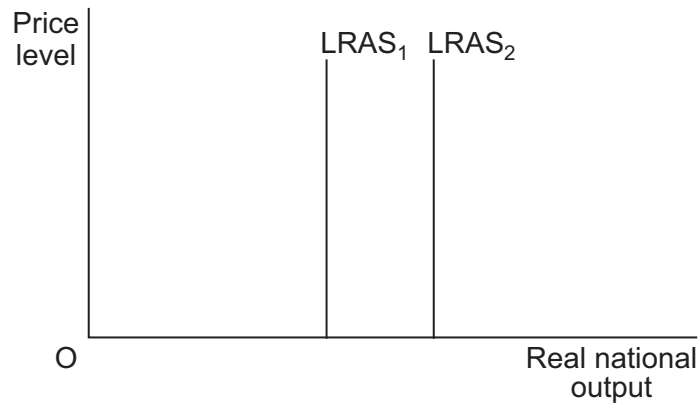
An increase in

- A imports
- B long-run aggregate supply
- C the government budget deficit
- D the surplus on the balance of payments on current account

- 9 The annual rate of inflation in the UK falls from 5 per cent to 2 per cent but the annual rate of inflation in the UK's main trading partners remains at 5 per cent. As a result, all other things being equal, it is likely that in the long term

- A UK exports will increase.
- B UK imports will increase.
- C the UK current account balance will deteriorate.
- D withdrawals from the UK circular flow of income will increase.

- 10** The diagram below illustrates an improvement in the supply-side performance of an economy.

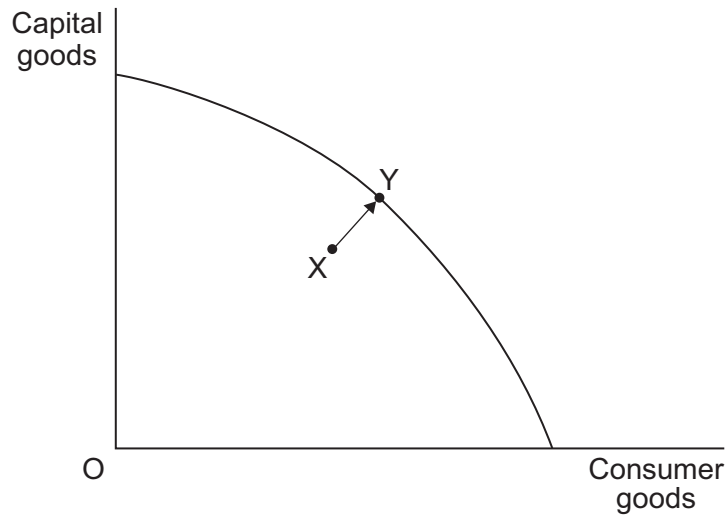


Which one of the following developments is most likely to directly cause the shift in the long-run aggregate supply curve from $LRAS_1$ to $LRAS_2$?

- A** Growth in export markets
 - B** Improvements in the banking system that increase the funds available for investment
 - C** An improvement in consumer confidence
 - D** A sustained increase in government spending on welfare benefits
- 11** Which one of the following is most likely to be an example of cyclical unemployment?
- A** Gill lost her job as a television engineer two months ago and is waiting to start a new job next month.
 - B** Brian has not worked for 15 years since losing his job as a coal miner.
 - C** Hitesh lost his job as a construction worker six months ago when a recession led to a downturn in the construction industry.
 - D** Faith works in the hotel trade as a casual chef and spends November to April out of work.

Turn over ►

- 12** The diagram below shows the production possibility frontier for an economy, where the economy is initially at point X.

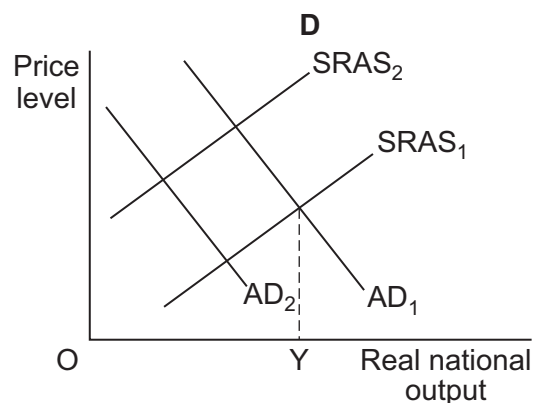
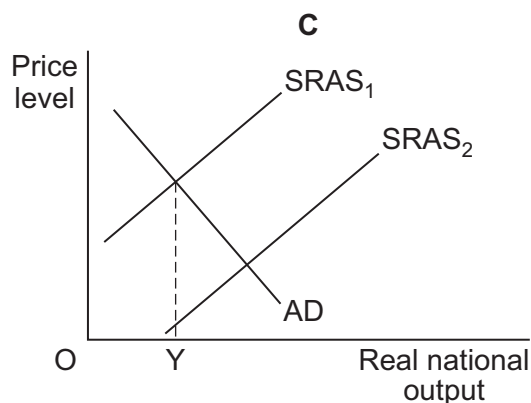
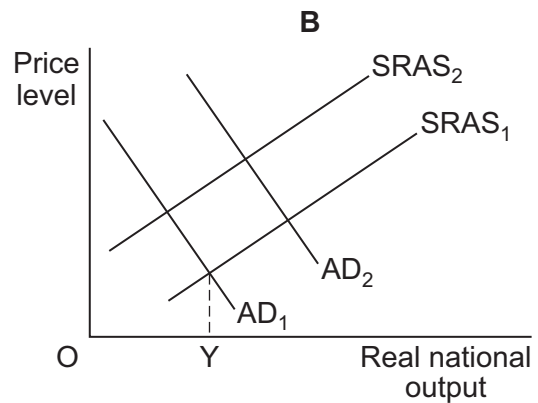
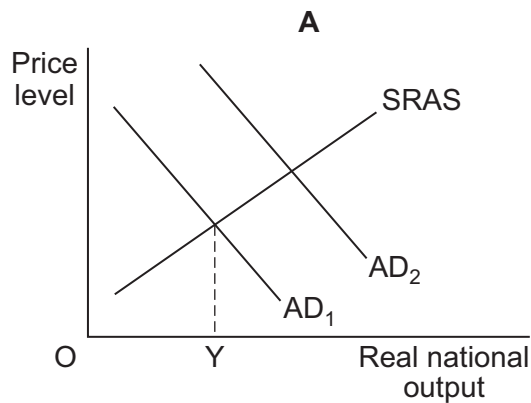


Assuming there is no change in the production possibility frontier, a movement from point X to point Y illustrates that there has been

- A** underlying economic growth.
 - B** an increase in spare capacity.
 - C** a rise in real national income.
 - D** an improvement in technology.
- 13** In October 2008, the Chancellor of the Exchequer announced plans to increase government spending on construction projects, such as schools, medical buildings, housing and leisure centres, in order to help prevent the UK economy from entering recession.
- Such a policy could best be considered an example of
- A** expansionary fiscal policy.
 - B** contractionary budgetary policy.
 - C** contractionary supply-side policy.
 - D** expansionary monetary policy.
- 14** All other things being equal, demand-pull inflation is most likely to result from an increase in
- A** the level of interest rates.
 - B** government spending.
 - C** the rate of income tax.
 - D** the cost of imported raw materials.

- 15 All other things being equal, in the long run a fall in the exchange rate is likely to
- A increase unemployment because it makes domestic products less competitive abroad.
 - B increase unemployment because it makes foreign products more competitive in the home market.
 - C reduce aggregate demand because it increases the domestic currency price of imports.
 - D increase aggregate demand because it can reduce the foreign currency price of exports.
- 16 The diagrams below show aggregate demand (AD) curves and short-run aggregate supply (SRAS) curves for an economy. The economy is initially at output OY.

Which diagram, **A**, **B**, **C** or **D**, shows the most likely impact of a rise in wage rates together with a fall in interest rates charged on consumer credit?



Turn over ►

17 All other things being equal, a large increase in interest rates in the UK is most likely to

- A decrease the size of the government budget deficit.
- B increase aggregate investment.
- C lead to an increase in bank lending.
- D decrease house prices.

18 In Country X, the underlying trend rate of growth is 2.75%. The table below shows the actual rate of growth in real national income over four successive years.

Year	Percentage growth in real national income
1	2.1 %
2	1.2 %
3	0.5 %
4	1.3 %

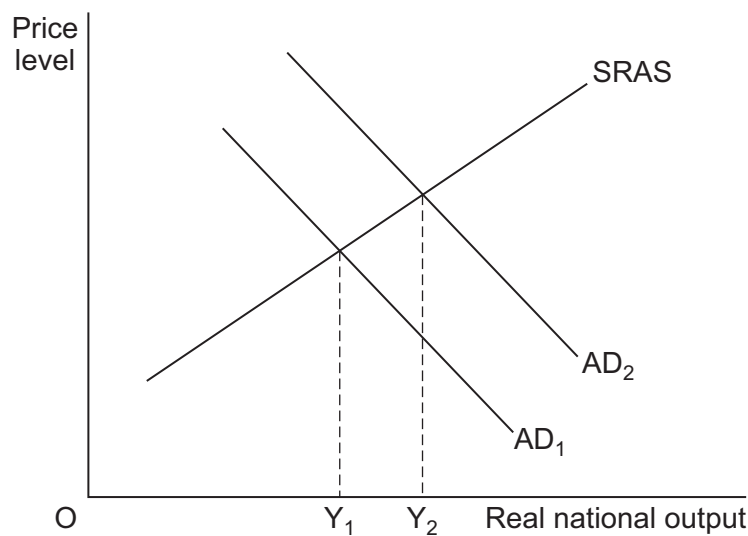
Between Year 1 and Year 4, it is most likely that

- A unemployment increased.
- B aggregate demand fell.
- C productive capacity decreased.
- D the current account on the balance of payments deteriorated.

19 A country is experiencing a balance of payments surplus but growing inflationary pressures. Which measure is most likely to reduce both a balance of payments surplus and the inflation rate?

- A A cut in interest rates
- B An appreciation of the exchange rate
- C A rise in the budget deficit
- D A decrease in government expenditure

- 20** Which one of the following is most likely to be classified as an instrument of monetary policy?
- A** Taxation
 - B** The inflation rate
 - C** The exchange rate
 - D** Government spending
- 21** The diagram below shows two aggregate demand (AD) curves and the short-run aggregate supply (SRAS) curve for an economy.

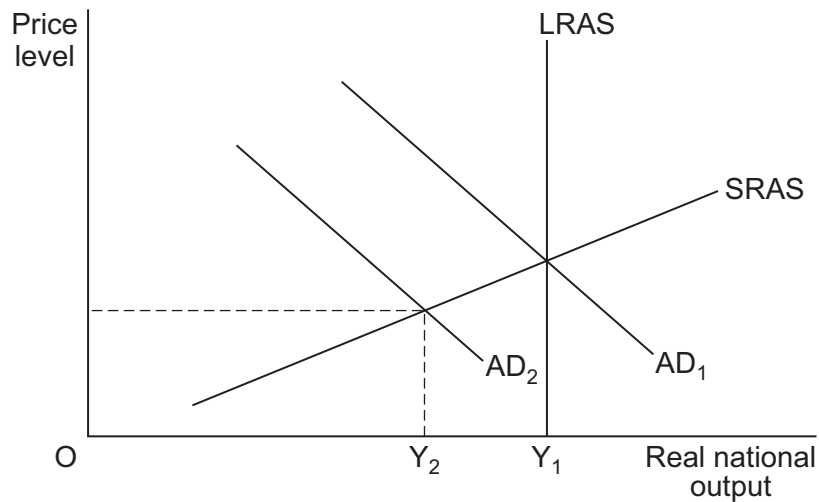


The change in real national output from Y_1 to Y_2 could be due to

- A** the introduction of new supply-side policies.
 - B** an increase in the government's budget surplus.
 - C** an expansionary monetary policy.
 - D** an increase in the current account deficit on the balance of payments.
- 22** Which one of the following is an example of fiscal policy having a direct supply-side effect?
- A** An increase in the money supply leading to greater output
 - B** A reduction in income tax boosting consumption and the supply of consumer credit from banks
 - C** A reduction in interest rates boosting investment and the productive potential of the economy
 - D** Government expenditure on retraining schemes increasing factor mobility

Turn over ►

- 23** In the diagram below, a decline in consumer confidence in an economy is represented by a leftward shift in its aggregate demand curve from AD_1 to AD_2 .



As a result of the fall in aggregate demand, output falls from Y_1 to Y_2 and unemployment rises. The type of unemployment that results from this fall in demand is best described as

- A** structural unemployment.
 - B** cyclical unemployment.
 - C** seasonal unemployment.
 - D** frictional unemployment.
- 24** Which one of the following is most likely to reduce the level of investment in a particular economy?
- A fall in
- A** the value of a country's currency on the foreign exchange market
 - B** aggregate demand in the economy
 - C** the level of unemployment
 - D** the spare capacity of the economy

- 25** Foreign companies build new factories in a country to take advantage of cheap labour and cheap land. All other things being equal, the result of this investment for that country's economy would be
- A** a movement along both its aggregate demand curve and long-run aggregate supply curve.
 - B** a movement along its aggregate demand curve and a shift in its long-run aggregate supply curve.
 - C** a shift in its aggregate demand curve and a movement along its long-run aggregate supply curve.
 - D** a shift in both its aggregate demand curve and long-run aggregate supply curve.

**QUESTION 25 IS THE LAST
QUESTION IN SECTION A**

**On your answer sheet
ignore rows 26 to 50**

Turn over for Section B

Turn over ►

Section B: Data Response

Answer **EITHER** Question 26 **OR** Question 27.
You are advised to spend at least 50 minutes on **Section B**.

EITHER

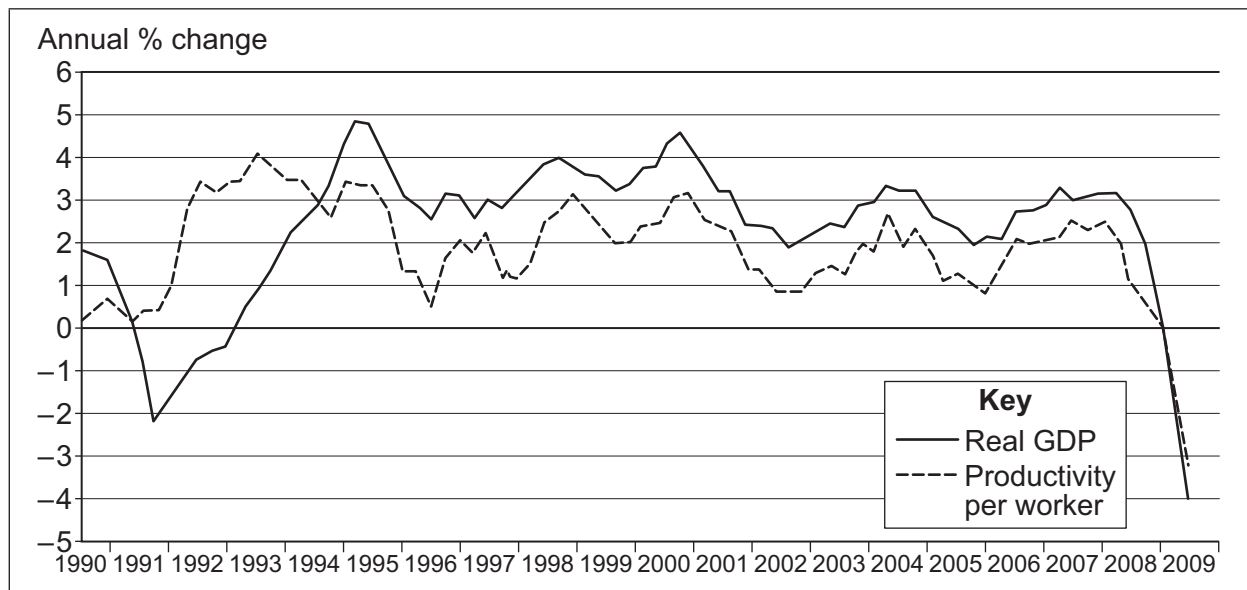
Total for this question: 50 marks

Question 26

ECONOMIC GROWTH AND RECOVERY

Study **Extracts A, B and C**, and then answer **all** parts of Question 26 which follow.

Extract A: Growth in real GDP and productivity, UK, 1990–2009



Source: adapted from *www.statistics.gov.uk*, accessed September 2009

Extract B: Achieving economic growth

With the economy in recession and unemployment rising, politicians and economists are trying to find ways of stimulating economic growth. From one year to the next, the crucial factor affecting growth is spending. If people spend more, firms will sell more and this will encourage firms to produce more. Lower bank lending, rising unemployment and a lack of confidence have contributed to lower aggregate demand and led to a negative actual rate of economic growth in the UK.	1
However, the answer to increasing the long-run trend rate of economic growth is not simply one of increasing spending. If aggregate demand persistently exceeds the capacity of the economy to produce goods and services, we will end up with high inflation and a growing balance of payments deficit. In the short run, the economy will experience a boom but this is likely to be followed by a prolonged recession.	5
If growth is to be sustained, improvements in the supply-side performance of the economy are essential. Investment and other developments that lead to higher productivity help to increase the productive capacity of the economy. In the long run, economic growth is stimulated by improvements in technology and an environment in which economic incentives provide encouragement to entrepreneurs and workers.	10
	15

Source: news reports, September 2009

Extract C: Will the recession reduce economic growth in the future?

Britain's economy shrank by a further 0.7 % in the second quarter of 2009 but it is widely expected that it should start to recover by the end of the year. The large degree of spare capacity should keep inflation low. It means that firms will find it more difficult to raise prices and may even decide to cut prices. They will also resist increases in costs. This is significant because monetary policy will need to remain loose for a long time in order to support recovery. 1 5

Nevertheless, the recession and financial crisis will probably reduce the growth of productive capacity because some firms will go out of business, the number of new firms being formed will fall and investment in physical capital will decline.

A period of recession is often accompanied by firms reducing their spending on training and cutting back on research and development. In addition, individuals who are unemployed for significant periods may view their chances of finding work as being low and therefore drop out of the labour market. This also reduces the potential output of the economy. 10

Source: news reports, September 2009

0 1 Define the term 'productive capacity' (**Extract B**, line 14). (5 marks)

0 2 Using **Extract A**, identify **two** significant points of comparison between the percentage change in real GDP and the percentage change in productivity per worker over the period shown. (8 marks)

0 3 **Extract C** (lines 2–3) suggests that the 'large degree of spare capacity should keep inflation low'.

Explain **two** reasons why the existence of spare capacity in an economy is likely to help keep inflation low. (12 marks)

0 4 **Extract B** (lines 7–8) states that 'the answer to increasing the long-run trend rate of economic growth is not simply one of increasing spending'.

Using the data and your economic knowledge, assess the importance of **both** demand-side **and** supply-side policies in helping the UK economy to achieve a prolonged period of economic growth. (25 marks)

Turn over ►

Do **not** answer Question 27 if you have answered Question 26.

OR

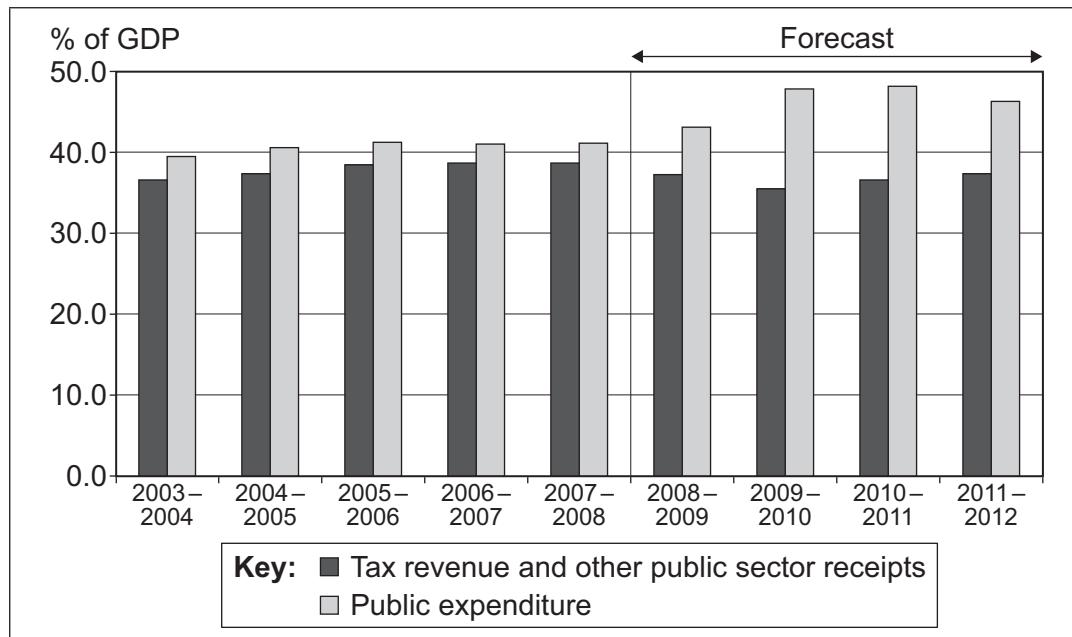
Total for this question: 50 marks

Question 27

FISCAL AND MONETARY POLICY IN THE UK

Study **Extracts D, E and F**, and then answer **all** parts of Question 27 which follow.

Extract D: Actual and forecast public sector revenue and public expenditure as a % of GDP, UK, 2003–04 to 2011–12



Source: HM Treasury, April 2009

Extract E: Fiscal policy

The overriding objective of economic policy is to maintain a stable economy. This requires low inflation, low unemployment and a steady rate of economic growth. Fiscal policy is used by governments to influence the level of aggregate demand in the economy in order to achieve their economic objectives. Fiscal measures also affect both aggregate supply and the pattern of economic activity. The tax and benefits system can influence aggregate supply by affecting incentives to work. Indirect taxes, which affect relative prices, and the way in which the government spends its money affect how the nation's scarce resources are used.	1 5
In response to the current global recession, many nations around the world have stimulated their economies by using fiscal measures and most are running a large budget deficit. The UK has been one of the major economies leading calls for fiscal action to stimulate aggregate demand. In November 2008, a number of fiscal measures were announced, including a £145 tax cut for basic-rate tax payers, a temporary 2.5% cut in VAT, £3 billion worth of investment spending brought forward from 2010 and a variety of other measures. The total cost of these measures was roughly £20 billion. The recession and expansionary fiscal policies have contributed to a significant rise in the forecast budget deficit to an estimated £175 billion (12.4 % of GDP) in 2009–10.	10 15
In a recent meeting in London, there was agreement amongst world leaders that budget deficits should not be cut back for at least a year, despite the growing concern about rising government debt. There was also agreement that expansionary policies should be withdrawn only when recovery in the world economy has been secured.	20

Source: news reports, September 2009

Extract F: Monetary policy

The Bank of England's monetary policy objective is to deliver price stability and, subject to that, to support the Government's economic objectives, including those for growth and employment. Between 1992, when inflation targeting was first introduced, and 2007, GDP growth averaged 2.8% while inflation averaged around 2.5%. This period of steady growth and low inflation was also accompanied by a reduction in the volatility of the economy.

1

5

Monetary policy is used to stimulate or slow the economy in the short run so that the economy is kept as close as possible to its long-run potential rate of growth and inflation is kept close to its target. In the long run, output and employment depend mainly on the supply side of the economy.

10

Monetary policy cannot completely eliminate cyclical fluctuations in the economy, nor will the economy be able to avoid the effects of unexpected economic shocks such as a substantial increase in oil prices.

Source: news reports, September 2009

0 5 Define the term 'budget deficit' (**Extract E**, line 11). (5 marks)

0 6 Using **Extract D**, identify **two** significant points of comparison between public sector revenue and public expenditure over the period shown. (8 marks)

0 7 **Extract E** (lines 4–5) states that fiscal measures 'affect ... the pattern of economic activity'.

Explain **two** ways in which fiscal measures can influence the pattern of economic activity. (12 marks)

0 8 **Extract E** (lines 1–2) states: 'The overriding objective of economic policy is to maintain a stable economy. This requires low inflation, low unemployment and a steady rate of economic growth.'

Using the data and your knowledge of recent economic events, assess the contribution that fiscal and monetary policies can make in maintaining a stable economy. (25 marks)

END OF QUESTIONS

There are no questions printed on this page

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**General Certificate of Education
January 2011**

Economics

ECON2

Unit 2: The National Economy

Final

Mark Scheme

Mark schemes are prepared by the Principal Examiner and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation meeting attended by all examiners and is the scheme which was used by them in this examination. The standardisation meeting ensures that the mark scheme covers the candidates' responses to questions and that every examiner understands and applies it in the same correct way. As preparation for the standardisation meeting each examiner analyses a number of candidates' scripts: alternative answers not already covered by the mark scheme are discussed at the meeting and legislated for. If, after this meeting, examiners encounter unusual answers which have not been discussed at the meeting they are required to refer these to the Principal Examiner.

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of candidates' reactions to a particular paper. Assumptions about future mark schemes on the basis of one year's document should be avoided; whilst the guiding principles of assessment remain constant, details will change, depending on the content of a particular examination paper.

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January 2011**ECON2****Advance Subsidiary Economics Unit 2****Section A: Objective Test (ECON2/1)**

The following list indicates the correct answers used in marking the candidates' responses.

KEY LIST

1.	D	9.	A	17.	D
2.	A	10.	B	18.	A
3.	B	11.	C	19.	B
4.	C	12.	C	20.	C
5.	A	13.	A	21.	C
6.	C	14.	B	22.	D
7.	D	15.	D	23.	B
8.	A	16.	B	24.	B
				25.	D

Advanced Subsidiary Economics**January 2011****ECON2/2****Mark Scheme****Section B: Data Response****General Instructions**

Marks awarded to candidates should be in accordance with the following mark scheme and examiners should be prepared to use the full range of marks available. The mark scheme for most questions is flexible, permitting the candidate to score full marks in a variety of ways. Where the candidate's response to a question is such that the mark scheme permits full marks to be awarded, full marks **MUST** be given. A perfect answer is not necessarily required for full marks. But conversely, if the candidate's answer does not deserve credit, then no marks should be given.

Occasionally, a candidate may respond to a question in a reasonable way, but the answer may not have been anticipated when the mark scheme was devised. In this situation, **OR WHENEVER YOU HAVE ANY DOUBT ABOUT THE INTERPRETATION OF THE MARK SCHEME**, you must in the first instance telephone your team leader to discuss how to proceed.

Two approaches have been used in the construction of the mark scheme:

- (i) **An issue based approach.** The mark scheme for questions **01, 02, 03, 05, 06** and **07** of the data response questions adopts this approach. The mark scheme lists the marks that can be awarded for particular issues (and associated development) that the candidate might include in the answer.
- (ii) **A levels approach.** This approach is used for marking questions **04** and **08** of the data response questions. The Levels Mark Scheme on the next page identifies five levels representing differences in the quality of work. A range of marks is allocated at each level. First decide the level into which an answer falls. The level chosen should be the one which **best fits** the answer provided by the candidate. It is **not** intended that the answer should satisfy every statement in the level description. Then think in terms of awarding the mid-point mark which has been identified for that level (eg 13 marks for Level 3). Move up and down from this notional mark by considering the extent to which the answer meets the level description overall. Strength in one skill can outweigh weakness in another. When using the Levels Mark Scheme the marker **must** identify where a particular skill is being demonstrated. The **key** to be used to identify the skill is given after the levels descriptions. The question-specific mark scheme summarises the information which could be used to answer the question, but without attaching marks to particular issues.

**LEVELS OF RESPONSE MARK SCHEME
FOR USE WITH QUESTIONS 04 AND 08 ONLY**

AS LEVELS OF RESPONSE	AO1 KNOWLEDGE and UNDERSTANDING of theories, concepts and terminology	AO2 APPLICATION of theories, concepts and terminology	AO3 ANALYSIS of economic problems and issues	AO4 EVALUATION of economic arguments and evidence, making informed judgements
Level 5 22-25 marks (mid-point 24) Good analysis and good evaluation	Good throughout the answer with few errors and weaknesses	Good application to issues Good use of data to support answer	Relevant and precise with a clear and logical chain of reasoning	Good with a clear final judgement
Level 4 17-21 marks (mid-point 19) Good analysis <u>but</u> limited evaluation OR Reasonable analysis and reasonable evaluation	Good throughout the answer with few errors and weaknesses Good throughout much of the answer with few errors and weaknesses	Good application to issues Good use of data to support answer Some good application to issues. Some good use of data to support answer	Relevant and precise with a clear and logical chain of reasoning Largely relevant and well organised with reasonable logic and coherence	Limited but showing some appreciation of alternative points of view Reasonable, showing an appreciation of alternative points of view
Level 3 10-16 marks (mid-point 13) Reasonable answer, including some correct analysis but very limited evaluation	Satisfactory but some weaknesses shown	Reasonable application to issues Reasonable use of data to support answer	Reasonably clear but may not be fully developed and is perhaps confused in places with a few errors present	Superficial, perhaps with some attempt to consider both sides of the issue(s)
Level 2 4-9 marks (mid-point 7) Weak with some understanding	Limited and some errors are made	Partial application to issues with some errors Limited use of data to support answer	Partial but confused at times, lacking focus and development Limited logic and coherence	A very basic and simplistic attempt is made which is unsupported by analysis
Level 1 0-3 marks (mid-point 2) Very weak	Weak with a number of errors	Little, if any, application to issues No use of data to support answer	Poor and lacking clarity and focus	No relevant evaluation

THE KEY TO BE USED WHEN USING THE 'LEVELS' MARKING SCHEME

- D** Where a particular economic term is correctly **DEFINED** in order to help the candidate to answer the question properly.
- I** Where a relevant **ISSUE** is raised by the candidate.
- K** Where the candidate demonstrates **KNOWLEDGE** of recent developments or features of the economy which help enhance the candidate's response to the question. This should also be used where the candidate quotes relevant examples.
- Ap** Where the candidate demonstrates the ability to **APPLY** knowledge and **CRITICAL UNDERSTANDING** to problems and issues.
- A** Where the candidate demonstrates the ability to **ANALYSE** the problem using appropriate economic ideas.
- E** Where the candidate **EVALUATES** and makes judgements about the significance of various issues and arguments.

QUALITY OF WRITTEN COMMUNICATION

Quality of Written Communication (QWC) will be assessed in Questions 04 and 08 only.

Candidates will be assessed according to their ability to:

- ensure that text is legible, and that spelling, grammar and punctuation are accurate, so that meaning is clear
- select and use a form and style of writing appropriate to purpose and complex subject matter
- organise information clearly and coherently, using specialist vocabulary when appropriate.

No specific marks are awarded for QWC.

However, examiners should take into account QWC when determining the mark to be awarded for an answer. This means an answer could be taken either up (for exceptional QWC) or down (for very poor QWC) by 1 mark (and no more).

26 ECONOMIC GROWTH AND RECOVERY**Total for this question: 50 marks****01** Define the term 'productive capacity' (**Extract B**, line 14).*(5 marks)***For an acceptable definition:**

- The amount of goods and services that the economy is capable of producing
- The amount produced when all the available factors of production are fully employed

5 marks

Full marks should be awarded to a candidate who demonstrates a clear understanding of the term **productive capacity** even if the definition is not exactly the same as the acceptable examples quoted above.

Full marks can also be awarded for an **accurately labelled** production possibility diagram, LRAS curve or trend rate of growth diagram **provided** the candidate includes a commentary, relating to the diagram, that shows that she/he understands what is meant by productive capacity of the economy.

If the definition is incomplete, marks may be broken down, for example, as follows:

The amount produced when the economy is operating on its PPB	4 marks
The amount produced when the output gap is zero	4 marks
The amount produced when the economy is operating on its LRAS curve	4 marks
When the economy is at full employment	2 marks
The maximum amount an individual firm can produce	2 marks
An accurately labelled PPB diagram or an LRAS curve or a trend rate of growth diagram	2 marks
The amount produced	1 mark
The output of the economy	1 mark
For identifying a factor that affects productive capacity	1 mark

Maximum of 4 marks if the definition is incomplete**MAXIMUM FOR PART 01: 5 MARKS**

- 0 2** Using **Extract A**, identify **two** significant points of comparison between the percentage change in real GDP and the percentage change in productivity per worker over the period shown. (8 marks)

Award up to 4 marks each for each point made:

Identifies a significant point of comparison. Makes accurate use of the data to support the point of comparison. Unit of measurement given accurately.	4 marks
Identifies a significant point of comparison. Makes use of the data to support the point of comparison. However, only one piece of data is given when two are needed to make a valid comparison and/or no unit of measurement is given and/or the unit of measurement is used/applied inaccurately.	3 marks
Identifies a significant point of comparison. No use of correct data to support the comparison identified.	2 marks
Identifies a significant feature of the data but no comparison is made Makes use of the data to support the feature identified Unit of measurement given accurately	1 mark

If a candidate identifies more than two points of comparison, reward the best two.

The valid points include:

- The growth of real GDP and productivity are both higher at the start of the period (+1.75% and +0.25% respectively) than at the end of the period (-4.0% and -3.2% respectively)
- For most of the period (1994 – 2008), the growth of real GDP is greater than growth of productivity (e.g. the difference was approximately 1% in 2002 **or** the difference averaged about 1% during this period)
- Real GDP growth was negative twice during the period (in the early 1990s (-2.1%) and at the end of the period (-4.0%)) whereas productivity growth was only negative once (towards the end of the period (-3.2%))
- The lowest rate of growth in both real GDP and in productivity was at the end of the period (2009) (-4.0% and -3.2% respectively)
- The highest rate of growth in real GDP was in 1994 (almost 5%), the highest rate of growth in productivity was towards the end of 1993 (around 4%)
- They both fluctuated during the period but the range of fluctuation was greater for real GDP growth (9%) than productivity growth (7.5%).

Candidates who confuse levels of real GDP and productivity with rates of growth of real GDP and productivity should be awarded **2 marks** providing they identify a significant point of comparison **and** make accurate use of the statistics.

The figures quoted above are approximations and the candidate should be allowed a small margin of error without penalty. However, very inaccurate statistics should not be rewarded.

MAXIMUM FOR PART 02: 8 MARKS

0 3 **Extract C** (lines 2-3) suggests that the 'large degree of spare capacity should keep inflation low'.

Explain **two** reasons why the existence of spare capacity in an economy is likely to help keep inflation low. (12 marks)

For a candidate who provides a relevant definition, eg spare capacity or inflation. **Do not credit a definition of productive capacity.**

1 mark per definition
Up to a max of 2 marks

Award up to 8 marks for each of the following reasons identified and explained. Up to 2 marks should be awarded for identifying the reason and up to a further 6 marks for explaining why it might help to keep inflation low.

Spare capacity implies that there is likely to be excess supply (or lack of demand) (**2 marks**), where there is excess supply prices are likely to fall (**2 marks**), manufacturers and retailers will be operating in a very competitive environment (**2 marks**), prices will be cut to increase sales (**2 marks**) if lots of firms are cutting prices, the rate at which the general price level is rising is likely to fall (**2 marks**)

Up to 8 marks

The existence of unemployment means that wage increases (labour costs) are less likely to increase

Up to 8 marks

Spare capacity in sectors supplying raw materials and components means that firms' material and component costs are less likely to increase

Up to 8 marks

Firms may be able to increase output without an increase in the cost per item, e.g. no need to pay overtime rates, fewer machine breakdowns

Up to 8 marks

Award **up to 4 additional marks** for the use of relevant diagrams, eg an AD/AS diagram that shows the effect on the price level when AD falls, creating spare capacity

2 marks for labelling axes/curves, 2 marks for information shown

If a candidate identifies more than two reasons, award the marks based upon the best two explanations.

A maximum of 10 marks can be awarded if the candidate only explains one reason why the existence of spare capacity is likely to keep inflation low.

MAXIMUM FOR PART 0 3: 12 MARKS

0 4 **Extract B** (lines 7-8) states that 'the answer to increasing the long-run trend rate of economic growth is not simply one of increasing spending'.

Using the data and your economic knowledge, assess the importance of **both** demand-side **and** supply-side policies in helping the UK economy to achieve a prolonged period of economic growth. (25 marks)

The best candidates, certainly those achieving Level 5, will recognise that increasing AD can lead to an increase in real GDP, hence increasing growth, up to the point where the economy reaches full capacity. They will also show that they understand that a prolonged period of economic growth can only be achieved if there are supply-side improvements that increase the full capacity level of output. These supply-side improvements might be facilitated through the use of supply-side policies and supported by measures to manage aggregate demand.

For this question, an answer should be limited to a maximum of 13 marks if there is no evidence of evaluation.

A maximum of **21 marks** may be awarded if there is no explicit use of the data, eg through the use of quotes or referring explicitly to the extracts.

Level 5	Good analysis <u>and</u> good evaluation	22-25 marks (mid-point 24)
Level 4	Good analysis <u>but</u> limited evaluation OR Reasonable analysis <u>and</u> reasonable evaluation	17-21 marks (mid-point 19)
Level 3	Reasonable answer, including some correct analysis but very limited evaluation	10-16 marks (mid-point 13)
Level 2	Weak with some understanding	4-9 marks (mid-point 7)
Level 1	Very weak	0-3 marks (mid-point 2)

Introduction	• definitions of, for example, supply-side and demand-side policies • explanation of what is meant by a 'prolonged period of economic growth', perhaps distinguishing between actual and underlying growth • a diagram to illustrate economic growth, eg AD/AS or PPC • recognition that a period of prolonged growth requires improvements in the supply-side performance of the economy
Developing the response to the question	• the main determinants of underlying (long run) growth, eg investment, technological change, growth in the labour force, education and training • ways in which supply-side policies can be used to increase the underlying rate of growth, eg by increasing the quantity of the available factors of production and their productivity

	- examples of supply-side policies and their impact on growth, eg changes in the tax-benefit system and the effect on incentives, trade union reforms and labour market flexibility, cuts in corporation tax, increased spending on education and training, subsidising spending on capital goods and R&D - the role of aggregate demand and demand-side policies in determining the actual rate of growth - the role of demand-side policies in creating a stable environment in which firms are willing to invest in capital goods, new technologies, R&D and training. - the role of monetary policy in controlling inflation might be discussed in relation to achieving a stable economic environment in which investment is likely to flourish - UK experience over the past 20 years may be used to illustrate the importance of both demand-side and supply-side policies
Evaluation	- the pros and cons of supply-side policies as a means of increasing the underlying rate of economic growth - the relative merits of free market and interventionist supply-side policies - the pros and cons of individual supply-side measures - assessing the contribution that demand-side policies can make to achieving a period of prolonged growth - recognition that demand-side policies cannot achieve a period of prolonged growth without improvements in the supply side of the economy - recognition that inappropriate demand-side policies might reduce the underlying trend rate of growth - the use of evidence from the UK economy to support arguments presented - the use of data from Extracts B & C to support their arguments

USE THE DETAILED LEVELS MARK SCHEME ON PAGES 4 AND 5 FOR FURTHER CLARIFICATION

MAXIMUM FOR PART 0 4: 25 MARKS

27 FISCAL AND MONETARY POLICY IN THE UK**Total for this question: 50 marks**

0 5	Define the term 'budget deficit' (Extract E , line 11).	(5 marks)
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For an acceptable definition: - When government is spending more than it is receiving from taxes and other charges in a financial year - When government is spending more than it is receiving from taxation	5 marks
Full marks should be awarded to a candidate who demonstrates a clear understanding of the term budget deficit even if the definition is not exactly the same as the acceptable examples quoted above.	

If the definition is incomplete, marks may be broken down, for example, as follows:

When the government needs to borrow to finance its expenditure	4 marks
The difference between government spending and taxation or defines a budget deficit as government spending less than taxation, i.e. confuses a deficit with a surplus	2 marks
The amount the government owes, ie a candidate who incorrectly defines the budget deficit as the national debt	2 marks
A policy to increase AD	1 mark
An explanation of the term 'budget'	1 mark
Government borrowing from abroad	1 mark

If a candidate states 'UK borrowing from abroad' and does not state that it is government borrowing, no marks should be awarded.

Maximum of 4 marks if the definition is incomplete or inaccurate

MAXIMUM FOR PART 0 5: 5 MARKS

0 6 Using **Extract D**, identify **two** significant points of comparison between public sector revenue and public expenditure over the period shown. (8 marks)

Award up to 4 marks each for each point made:

Identifies a significant point of comparison. Makes accurate use of the data to support the point of comparison. Unit of measurement given accurately.	4 marks
Identifies a significant point of comparison. Makes use of the data to support the point of comparison. However, only one piece of data is given when two are needed to make a valid comparison and/or no unit of measurement is given and/or the unit of measurement is used/applied inaccurately.	3 marks
Identifies a significant point of comparison. No use of correct data to support the comparison identified.	2 marks
Identifies a significant feature of the data but no comparison is made Makes use of the data to support the feature identified Unit of measurement given accurately	1 mark

If a candidate identifies more than two points of comparison, reward the best two.

The valid points include:

- Throughout the whole of the period, public expenditure as a percentage of GDP is higher than public sector revenues (eg the smallest difference is around 3% of GDP)
- The gap between the two is smaller at the start of the period (approximately 3%) than is forecast for the end of the period (approximately 9%)
- Public expenditure as a percentage of GDP is lower at the start of the period than it is forecast to be at the end of the period (approximately 39% and 46% respectively) but public sector revenues are forecast to be fairly similar (or perhaps a little higher) at the end of the period (around 37% of GDP)
- Throughout the period 2003-04 and 2007-08, the difference between the two is fairly similar (approximately 3% of GDP).

OR

- Throughout the period 2003-04 and 2007-08, both variables increase slowly (public expenditure from around 39% to 41% of GDP and public sector receipts from about 36% to 38% of GDP)
- The gap is expected to increase significantly between 2007-08 and 2010-11 (from approximately 3% of GDP to approximately 12% of GDP)
- Public expenditure as a percentage of GDP is more volatile than public sector receipts (with ranges of approximately 9% and 3% of GDP respectively)
- In the forecast period (2008-09 to 2011-12) the gap between public expenditure and taxation as a percentage of GDP is consistently higher than in the earlier period (2003-04 to 2007-08). The lowest figure in the forecast period is over 5% of GDP whereas the highest figure in the earlier period is approximately 3% of GDP.
- Public sector revenues never exceed 40% of GDP whereas, with the exception of 2003/4, public expenditure is always above 40% of GDP.

If a candidate does not make it clear, somewhere in their answer, that the figures are for spending or for taxation as a **% of GDP** then a maximum of **3 marks** can be awarded for each point of comparison.

The figures quoted above are approximations and the candidate should be allowed a small margin of error without penalty. However, very inaccurate statistics should not be rewarded.

MAXIMUM FOR PART 06: 8 MARKS

0 7 Extract E (lines 4-5) states that fiscal measures ‘affect the...pattern of economic activity’.

Explain **two** ways in which fiscal measures can influence the pattern of economic activity. (12 marks)

For a candidate who provides a relevant definition, eg fiscal measure, pattern of economic activity. **Do not credit a definition of budget deficit.**

**1 mark per definition
Up to a max of 2 marks**

Award up to 8 marks for each of the following points identified and explained. Up to 2 marks should be awarded for identifying the point and up to a further 6 marks for explaining why or how it might affect the pattern of economic activity.

An increase in a tax on a particular product, e.g. alcohol (**2 marks**), will reduce the demand for that product (**2 marks**), hence firms will produce less of the product (**2 marks**), their profits are likely to fall (**2 marks**), people will be laid-off and some firms may close (**2 marks**), consequently fewer factors of production will be used to produce the product (**2 marks**), over time, these resources are likely to be reallocated to produce other goods and services (**2 marks**).

Up to 8 marks

The impact of a rise in any other tax on the pattern of activity, eg income tax through its impact on different sectors of the community and their different spending patterns, stamp duty on the housing market

Up to 8 marks

The possible impact of higher taxes on ‘illegal activities’ resulting from taxation evasion and/or the growth in services to facilitate tax avoidance

Up to 8 marks

The impact of an increase in public expenditure on a particular area (eg health, education, defence) or project (eg building a new railway line or power station)

Up to 8 marks

An increase in government grants or subsidies, eg to finance R&D, to encourage an overseas car manufacturer to locate in the UK

Up to 8 marks

An increase in spending on welfare, ie through its impact on the pattern of spending and hence production

Up to 8 marks

Award **up to 4 marks** for the use of relevant diagrams, eg a production possibility diagram that shows, provided the economy is at full capacity, if more public sector goods are produced fewer private sector goods will be supplied.

2 marks for labelling axes/curves, 2 marks for information shown

Award up to a maximum of 8 marks in total to a candidate who explains ONLY how fiscal measures affect the LEVEL of economic activity (1 mark for identifying a point and 1 mark for each logical link in the chain of reasoning to a maximum of 8 marks. These 8 marks might also include up to 2 marks for a suitable AD/AS diagram and up to 2 marks for definitions).

If a candidate identifies more than two ways award the marks based upon the best two explanations.

A maximum of 10 marks can be awarded if the candidate only explains one way in which fiscal measures can affect the pattern of economic activity. However, a candidate who explains one way in which fiscal policy can affect the pattern of economic activity and one way in which it affects the level of economic activity can earn the full 12 marks but the part of the answer which deals with the LEVEL can only be awarded a maximum of 8 marks.

MAXIMUM FOR PART 07: 12 MARKS

0 8 **Extract E** (lines 1-2) states: 'The overriding objective of economic policy is to maintain a stable economy. This requires low inflation, low unemployment and a steady rate of economic growth'.

Using the data and your knowledge of recent economic events, assess the contribution that fiscal and monetary policies can make in maintaining a stable economy.

(25 marks)

Good answers, certainly those achieving Level 5, will address the use of both fiscal and monetary policy in achieving a stable economy and not just their use in helping an economy to recover from recession.

For this question, an answer should be limited to a maximum of 13 marks if there is no evidence of evaluation.

A maximum of **21 marks** may be awarded if there is no explicit use of the data, eg through the use of quotes or referring explicitly to the extracts.

Level 5	Good analysis <u>and</u> good evaluation	22-25 marks (mid-point 24)
Level 4	Good analysis <u>but</u> limited evaluation OR Reasonable analysis <u>and</u> reasonable evaluation	17-21 marks (mid-point 19)
Level 3	Reasonable answer, including some correct analysis but very limited evaluation	10-16 marks (mid-point 13)
Level 2	Weak with some understanding	4-9 marks (mid-point 7)
Level 1	Very weak	0-3 marks (mid-point 2)

Introduction	• definitions of, for example, fiscal policy, monetary policy, inflation, unemployment, economic growth and a stable economy • explaining that fiscal and monetary policies affect the economy by influencing aggregate demand • explaining that fiscal measures can also affect aggregate supply
Developing the response to the question	• causes of inflation • causes of unemployment • determinants of actual and underlying growth • demand-side and supply-side shocks as causes of instability • the role of monetary policy in controlling inflation in the UK • the role of monetary policy in helping to achieve low unemployment, steady growth and economic stability • the use of fiscal policy to influence aggregate demand • the role of budget deficits and surpluses • how fiscal policy might be used to influence inflation, unemployment and to help stabilise the economy • the use of fiscal policy in a severe recession • supply-side effects of fiscal policy and their role in helping to maintain a stable economy

	knowledge of recent events in the UK might be used to illustrate the above.
Evaluation	- the apparent success of UK monetary policy in controlling inflation between 1993 and 2008 - other factors that may have contributed to low inflation - the apparent success of economic policies in achieving a stable economy between 1993 and 2008 - the significance of the downturn in the UK economy that began in 2008 - the advantages of using fiscal measures in a recession - budget deficits and the growth of the national debt (although the national debt is not part of the AS specification, many candidates will be aware that a budget deficit will increase government debt and should be rewarded if they discuss this issue) - the inflexibility of fiscal policy - the benefits of using monetary policy to control inflation and stabilise the economy when the shocks to the economy are not too severe - monetary policy might prove ineffective in stimulating the economy when there is a severe recession - the flexibility of monetary policy - evidence relating to the success (or otherwise) of fiscal and monetary policies in helping the economy to recover from the recent recession - an assessment of the contribution that fiscal policy can make to achieving low inflation, low unemployment and a steady rate of economic growth through its impact on the supply-side performance of the economy - an overall assessment of the contribution that fiscal and monetary policy can make in maintaining a stable economy - the use of data from Extracts E and F to support their arguments.

USE THE DETAILED LEVELS MARK SCHEME ON PAGES 4 AND 5 FOR FURTHER CLARIFICATION

MAXIMUM FOR PART 08: 25 MARKS



General Certificate of Education
Advanced Subsidiary Examination
January 2010

Economics

ECON2

Unit 2 The National Economy

Thursday 21 January 2010 9.00 am to 10.15 am

For this paper you must have:

- an objective test answer sheet
- a black ball-point pen
- an 8-page answer book.

You may use a calculator.

Time allowed

- 1 hour 15 minutes

Instructions

- In **Section A**, answer **all** questions on your objective test answer sheet.
- In **Section B**, answer **EITHER** Question 26 **OR** Question 27 in your answer book.
- Do all rough work in this question paper, **not** on your objective test answer sheet.

Section A (ECON2/1)

- Use a black ball-point pen. Do **not** use pencil.

Section B (ECON2/2)

- Use black ink or black ball-point pen. Pencil should only be used for drawing.
- Write the information required on the front of your answer book. The **Examining Body** for this paper is AQA. The **Paper Reference** is ECON2/2.

Information

- The maximum mark for this paper is 75.
- There are 25 marks for **Section A** and 50 marks for **Section B**.
- In **Section A**, each question carries 1 mark. No deductions will be made for wrong answers.
- In **Section B**, the marks for questions are shown in brackets.
- You will be marked on your ability to:
 - use good English
 - organise information clearly
 - use specialist vocabulary where appropriate.

Advice

- You are advised to spend no more than 25 minutes on **Section A** and at least 50 minutes on **Section B**.

SECTION A: OBJECTIVE TEST

Answer **all** questions in **Section A**.

Each question carries 1 mark. No deductions will be made for wrong answers.

You are advised to spend no more than 25 minutes on **Section A**.

For each question there are four alternative responses, **A**, **B**, **C** and **D**. When you have selected the response which you think is the best answer to a question, mark this response on your objective test answer sheet. If you wish to change your answer to a question, follow the instructions on your objective test answer sheet.

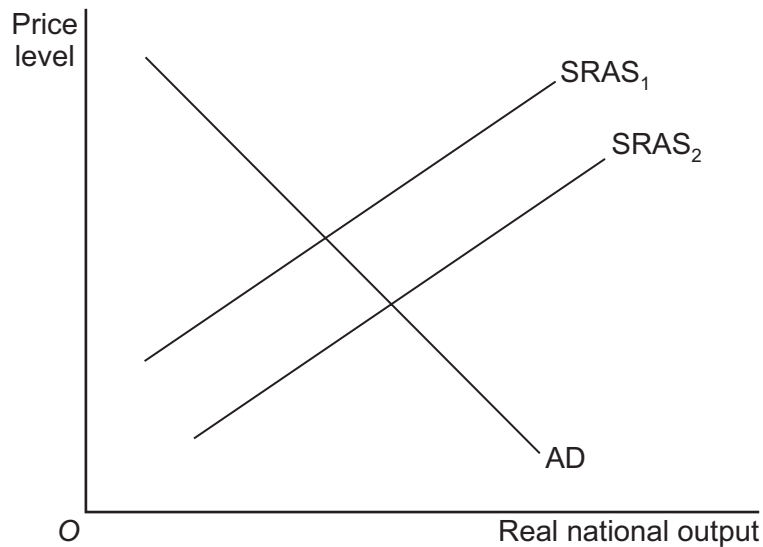
- 1** In economics, investment is best defined as

 - A** the flow of money into the stock of savings.
 - B** spending on capital goods in the economy.
 - C** the profit kept back by firms to finance future expenditure on new machinery and equipment.
 - D** the stock of economic resources such as factories and machinery.
- 2** A rise in the exchange rate together with a rise in taxes on household income is most likely to lead to a

 - A** rise in exports and a rise in business investment.
 - B** fall in imports and a rise in business investment.
 - C** fall in exports and a rise in business investment.
 - D** rise in imports and a fall in business investment.
- 3** All other things being equal, a large rise in interest rates is most likely to lead to an increase in

 - A** economic growth.
 - B** investment.
 - C** unemployment.
 - D** aggregate supply.

- 4 The diagram below shows the aggregate demand (AD) and short-run aggregate supply (SRAS) curves for an economy.



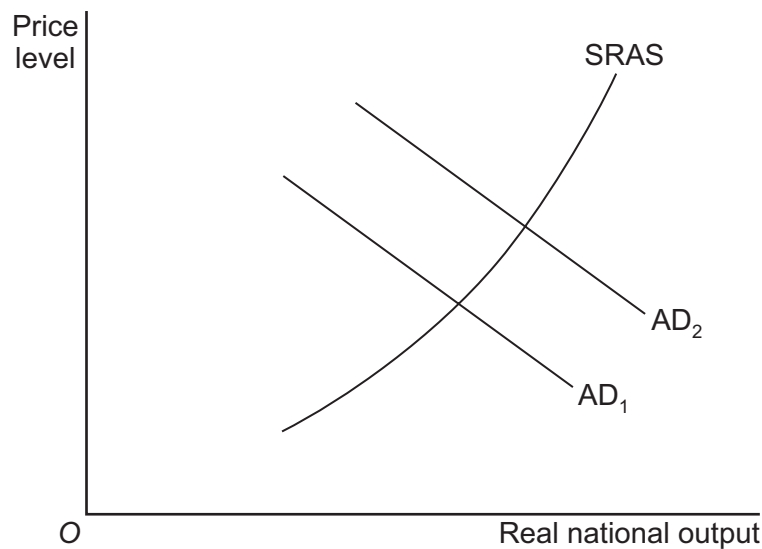
The shift of the short-run aggregate supply curve from SRAS₁ to SRAS₂ could have been caused by

- A a decrease in oil prices.
 - B an increase in employment.
 - C a decrease in the availability of credit.
 - D an increase in business costs.
- 5 All other things being equal, a government would be undertaking a contractionary fiscal policy if it reduced
- A government expenditure.
 - B interest rates.
 - C taxation.
 - D the exchange rate.
- 6 Which one of the following policies is most likely to lead to an increase in output and employment without increasing the rate of inflation?
- A Expansionary fiscal policy
 - B Expansionary monetary policy
 - C Supply-side policies
 - D Exchange rate policy

Turn over ►

-
- 7 Which one of the following is most likely to reduce inflationary pressures in the UK economy?
- A An increase in labour productivity
 - B A fall in the value of the pound
 - C The emergence of a positive output gap
 - D A reduction in the rate of interest paid on mortgages
- 8 Which one of the following is most likely to occur in the boom phase of an economic cycle?
- A Rising national income, falling unemployment and a negative output gap
 - B Rising imports, rising profits and a positive output gap
 - C Rising consumption and investment expenditure and a negative output gap
 - D Excess demand, falling employment and a positive output gap
- 9 An increase in aggregate demand is most likely to cause inflation when
- A there are substantial unemployed resources in the economy.
 - B the government is balancing its budget.
 - C the balance of payments on current account is neither in deficit nor in surplus.
 - D actual GDP is above the productive potential of the economy.

- 10** Choosing between faster economic growth and a satisfactory balance of payments best illustrates
- A** choice between different macroeconomic policy instruments.
 - B** that the short-run aggregate supply curve is vertical.
 - C** a possible conflict between competing policy objectives.
 - D** a government sacrificing future consumption in favour of current consumption.
- 11** The diagram below shows two aggregate demand (AD) curves and the short-run aggregate supply (SRAS) curve for an economy.



The shift in the aggregate demand curve from AD_1 to AD_2 could have been caused by an increase in

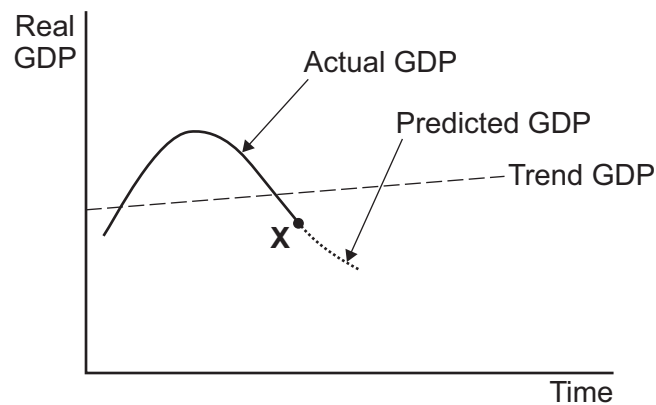
- A** imports.
 - B** labour productivity.
 - C** household savings.
 - D** the government budget deficit.
- 12** The underlying long-run trend rate of economic growth can be defined as the
- A** highest rate of economic growth achieved in the long run by an economy.
 - B** average rate of economic growth in a boom period.
 - C** rate of economic growth that can be maintained in the long run.
 - D** rate of economic growth achieved for a period of more than two quarters.

Turn over ►

13 All other things being equal, a fall in the exchange rate is likely to

- A** increase the price of exports.
- B** reduce import prices.
- C** reduce domestic demand.
- D** increase domestic employment.

14 The diagram below shows actual and trend GDP for an economy over time.



If the government is using both fiscal and monetary policies to manage the economy, what combination of policies is it most likely to implement when the economy is operating at point X?

- A** Higher taxes with lower interest rates
- B** Higher taxes with higher interest rates
- C** Lower taxes with lower interest rates
- D** Lower taxes with higher interest rates

15 The economy is experiencing a balance of payments surplus on current account and high unemployment. Which policy is most likely to reduce both the balance of payments surplus on current account and unemployment?

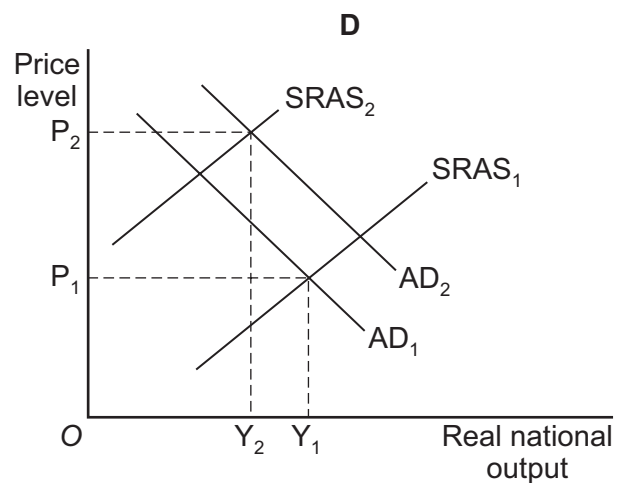
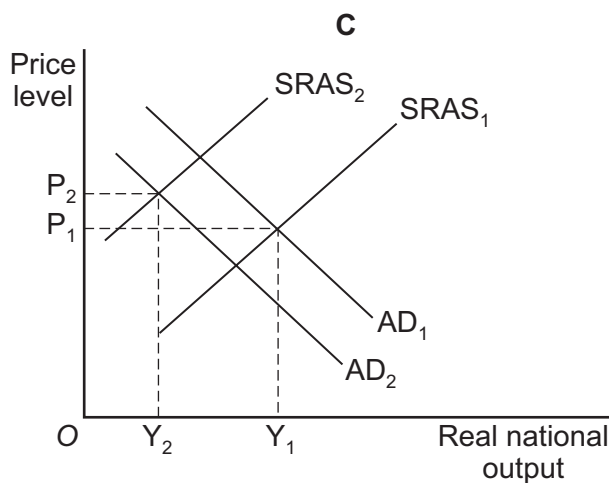
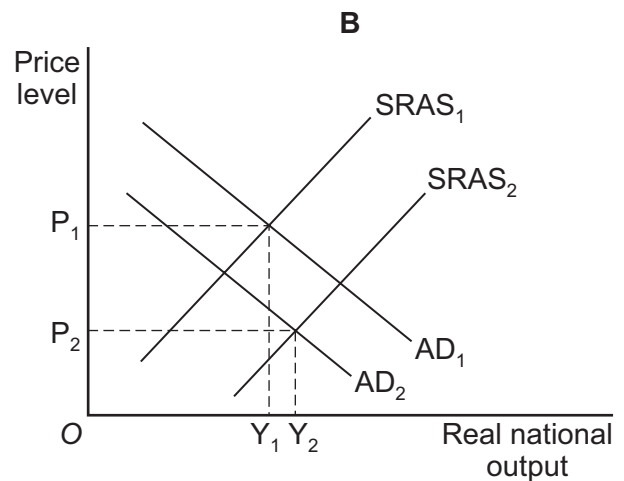
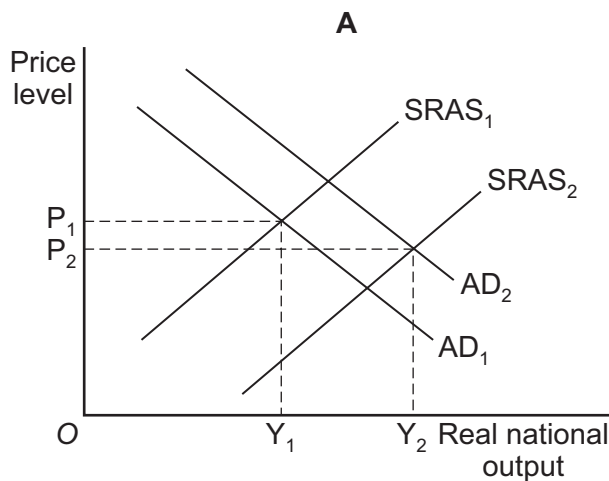
- A** A cut in income tax
- B** A rise in interest rates
- C** An increase in the exchange rate
- D** A fall in government spending

16 The short-run aggregate supply curve is drawn on the assumption that

- A investment in the economy is constant.
- B the prices of factors of production are constant.
- C the money supply is constant.
- D consumption expenditure by households is constant.

17 The diagrams below illustrate aggregate demand and aggregate supply curves for an economy. AD_1 and $SRAS_1$ represent the initial positions of the aggregate demand and short-run aggregate supply curves. AD_2 and $SRAS_2$ represent shifts in the position of the two curves.

Which one of the following diagrams indicates the effect on the economy of a general fall in wage costs and a rise in the level of exports?



Turn over ►

- 18 In the short run, an increase in a budget deficit is most likely to reduce
- A imports.
 - B unemployment.
 - C interest rates.
 - D inflation.
- 19 All other things being equal, which one of the following is most likely to reduce a balance of payments deficit on current account?
- An increase in
- A the price level
 - B consumption
 - C productivity
 - D the money supply
- 20 The table below shows index numbers for GNP per head for two countries, X and Y, in 2005 and 2009.

	GNP per head	
	2005	2009
Country X	100	120
Country Y	100	110

From the information above, it can be concluded that

- A GNP rose faster in Country X than in Country Y.
- B GNP was the same in Country X and Country Y in 2005.
- C GNP per head was, in 2009, higher in Country X than in Country Y.
- D the rate of increase of GNP per head was higher in Country X than in Country Y.

- 21 If an economy is operating on its production possibility frontier, the most likely effect of an increase in the output of capital goods is that its rate of economic growth will
- A increase now but fall in the future.
 - B remain constant now but increase in the future.
 - C remain constant now and in the future.
 - D fall now but increase in the future.
- 22 All other things being equal, a rise in the value of the pound on foreign exchange markets is most likely to increase
- A public sector borrowing in the UK.
 - B the rate of inflation in the UK.
 - C the level of interest rates in the UK.
 - D the UK's current account deficit on the balance of payments.
- 23 A supply-side policy can be used to increase
- A interest rates.
 - B government expenditure.
 - C the mobility of labour.
 - D tax rates.
- 24 Which one of the following combinations is most likely to increase aggregate demand (AD) in the UK economy?

Combination	Government spending	Taxation revenue	Exchange rate of the £
A	Falling	Rising	Rising
B	Rising	Falling	Falling
C	Rising	Rising	Falling
D	Falling	Falling	Rising

- 25** All other things being equal, which one of the following is most likely to cause a simultaneous shift to the right in both an economy's short-run and long-run aggregate supply curves?

An increase in

- A** the number of immigrants entering the country
- B** the rate of interest
- C** the rate of Value Added Tax (VAT)
- D** the minimum wage rate

**QUESTION 25 IS THE LAST
QUESTION IN SECTION A**

**On your answer sheet
ignore rows 26 to 50**

TURN TO PAGE 12 FOR SECTION B

Turn over for the next question

Turn over ►

Answer **EITHER** Question 26 **OR** Question 27.
You are advised to spend at least 50 minutes on **Section B**.

Total for this question: 50 marks

Study **Extracts A, B and C**, and then answer **all** parts of Question 26 which follows.

	2007 Quarter 4 (£bn)	2008 Quarter 1 (£bn)
Balance of trade in goods	-24.1	-22.7
Balance of trade in services	9.5	9.2
Balance of trade in goods and services	-14.6	-13.5
Income balance (including investment income)	6.9	9.0
Current transfers balance	-4.5	-3.9
Current account balance	-12.2	-8.4

Extract B: Slow growth and a falling exchange rate will affect the trade balance

The 15 economies of the eurozone (those countries that use the euro as a currency) contracted in the second quarter of 2008, experiencing growth of -0.2%. A recession in the eurozone economies will reduce UK exports and lead to lower economic activity in the UK. However, the effect of the decline in exports upon the balance of payments should be offset by a fall in foreign imports as growth in the UK slows and the sterling exchange rate falls.	1 5
The pound reached a low against the euro in April 2008 and has fallen by over 5% against the US dollar during the past month. A measure of the pound's exchange rate, the sterling exchange rate index, stood at 104.24 on the 1 January 2007 but its value closed at 91.22 on the 21 August 2008. This fall in the value of the pound will help to improve the competitiveness of UK firms and should lead to a reduction in the deficit on the balance of trade in goods and services.	 10

M/Jan10/ECON2

Extract C: The UK at a standstill in the second quarter of 2008

The longest period of sustained economic growth in Britain's history has come to an end. The latest official statistics showed zero growth for the UK economy between April and June 2008. After 63 quarters (almost 16 years) of uninterrupted economic growth, the United Kingdom economy has ground to a halt.	1
Figures show that the services sector, the backbone of the UK economy, grew by just 0.2%, while manufacturing output fell by 0.8% and household spending dropped by 0.1%. City economists said it was overseas trade which had helped to prevent the economy going into recession in the first half of 2008.	5
The recent fall in the value of the pound should help UK exporters, whose goods will be cheaper overseas, but it may also add to inflationary pressures, making it more difficult for the Bank of England to cut interest rates.	10

Source: news reports, August 2008

Question 26

- 26** (a) Define the term 'balance of trade in goods and services' (**Extract B**, line 12). (5 marks)
- (b) Using the data in **Extract A**, identify **two** components of the current account that have led to the improvement in the current account balance that occurred between the fourth quarter of 2007 and the first quarter of 2008. (8 marks)
- (c) Explain the likely effect of a recession in the eurozone upon the current account of the UK balance of payments. (12 marks)
- (d) Assess the view that a fall in the exchange rate of the pound will help to improve the performance of the UK economy. (25 marks)

Turn over ►

Do **not** answer Question 27 if you have answered Question 26.

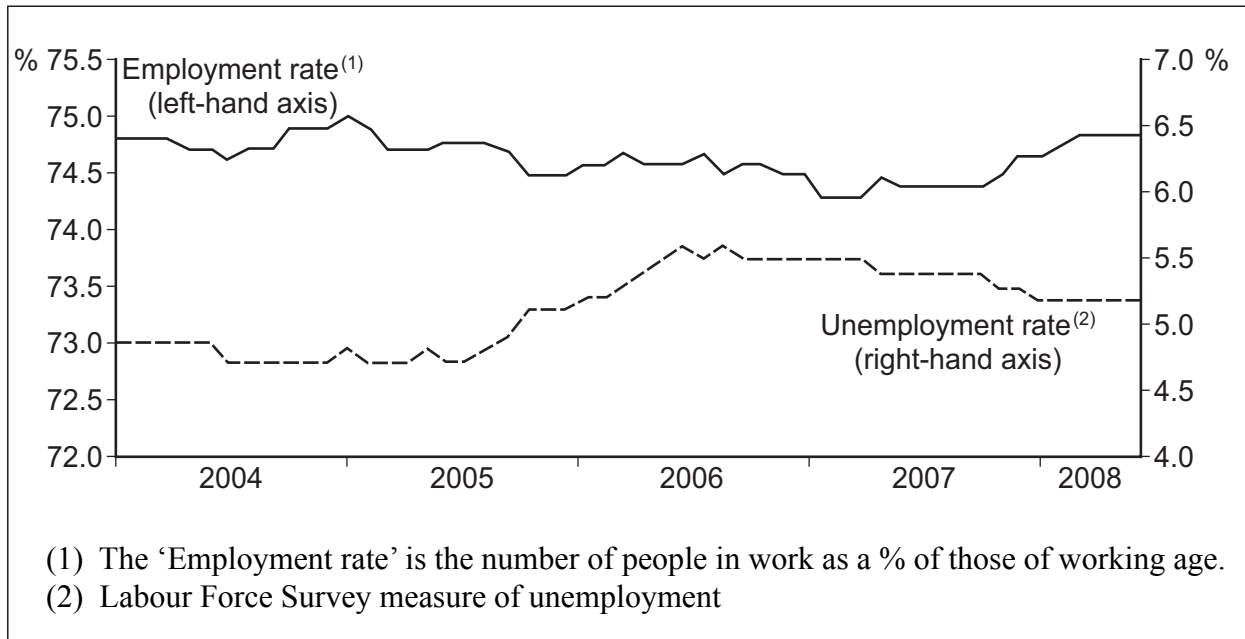
OR

Total for this question: 50 marks

27 EMPLOYMENT AND UNEMPLOYMENT

Study **Extracts D, E and F**, and then answer **all** parts of Question 27 which follows.

Extract D: Employment and unemployment rates for the UK, January 2004 to May 2008



Source: adapted from 'Economic & Labour Market Review', Vol. 2, No. 8, August 2008, www.statistics.gov.uk, accessed on 25 August 2008

Extract E: The labour market weakens

Most economists believe that a recession in the United Kingdom is inevitable.	1
The labour market is weakening, employment growth has slowed to a trickle and unemployment is rising. In June, the claimant count measure of unemployment rose by 20 100, the sixth successive monthly increase. The Labour Force Survey measure rose by 60 000 and the unemployment rate rose from 5.2% to 5.4%.	5
The number of job vacancies was also down, reflecting weaker demand conditions in the UK economy.	
The impact of the economic slowdown is becoming more widespread. Nearly every sector of the economy is affected. The credit crunch hit housebuilding and construction hard but its effects are now spreading to the rest of the economy.	10
The British Chambers of Commerce have predicted that unemployment will rise by more than 300 000 over the next two or three years, taking it close to 2 million.	

Source: news reports, July 2008

Extract F: A sustained rise in unemployment is inevitable

In recent years, the rapid increase in consumer spending provided the main contribution to the sustained growth in real GDP. However, high levels of consumer debt and falling house prices suggest that the growth in consumption in the UK is likely to fall and may even become negative.	1
Problems in the United States and the looming recession in the eurozone mean that, despite the fall in the value of the pound, United Kingdom exports are unlikely to increase sufficiently to offset the decline in domestic demand. High oil, gas and commodity prices have caused inflation to rise significantly above the 2% Consumer Prices Index (CPI) target and some economists consider it unlikely that the Bank of England will cut interest rates in the near future. A significant increase in unemployment seems inevitable and, in the short run, there is not much that a government can do about it.	5 10

Source: news reports, July 2008

Question 27

- 27 (a) Define the term 'real GDP' (**Extract F**, line 2). (5 marks)
- (b) Using **Extract D**, identify **two** significant points of comparison between changes in the employment rate and changes in the unemployment rate between January 2004 and May 2008. (8 marks)
- (c) Explain why 'weaker demand conditions in the UK economy' (**Extract E**, lines 6-7) are likely to lead to rising unemployment. (12 marks)
- (d) **Extract F** (lines 10-12) states: 'A significant increase in unemployment seems inevitable and, in the short run, there is not much that a government can do about it.'
- Evaluate alternative measures which can be used to reduce unemployment. (25 marks)

END OF QUESTIONS

There are no questions printed on this page

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General Certificate of Education

Economics

ECON2: The National Economy

Mark Scheme

2010 examination - January series

Mark schemes are prepared by the Principal Examiner and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation meeting attended by all examiners and is the scheme which was used by them in this examination. The standardisation meeting ensures that the mark scheme covers the candidates' responses to questions and that every examiner understands and applies it in the same correct way. As preparation for the standardisation meeting each examiner analyses a number of candidates' scripts: alternative answers not already covered by the mark scheme are discussed at the meeting and legislated for. If, after this meeting, examiners encounter unusual answers which have not been discussed at the meeting they are required to refer these to the Principal Examiner.

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of candidates' reactions to a particular paper. Assumptions about future mark schemes on the basis of one year's document should be avoided; whilst the guiding principles of assessment remain constant, details will change, depending on the content of a particular examination paper.

Further copies of this Mark Scheme are available to download from the AQA Website: www.aqa.org.uk

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Set and published by the Assessment and Qualifications Alliance.

January 2010**ECON2****Advance Subsidiary Economics Unit 2****Section A: Objective Test****January 2010**

The following list indicates the correct answers used in marking the candidates' responses.

1.	B	9.	D	17.	A
2.	D	10.	C	18.	B
3.	C	11.	D	19.	C
4.	A	12.	C	20.	D
5.	A	13.	D	21.	B
6.	C	14.	C	22.	D
7.	A	15.	A	23.	C
8.	B	16.	B	24.	B
				25.	A

Advanced Subsidiary Economics Unit 2

Section B: Data Response

General Instructions

Marks awarded to candidates should be in accordance with the following mark scheme and examiners should be prepared to use the full range of marks available. The mark scheme for most questions is flexible, permitting the candidate to score full marks in a variety of ways. Where the candidate's response to a question is such that the mark scheme permits full marks to be awarded, full marks **MUST** be given. A perfect answer is not necessarily required for full marks. But conversely, if the candidate's answer does not deserve credit, then no marks should be given.

Occasionally, a candidate may respond to a question in a reasonable way, but the answer may not have been anticipated when the mark scheme was devised. In this situation, **OR WHENEVER YOU HAVE ANY DOUBT ABOUT THE INTERPRETATION OF THE MARK SCHEME**, you must in the first instance telephone your team leader to discuss how to proceed.

Two approaches have been used in the construction of the mark scheme.

- (i) **An issue based approach.** The mark scheme for parts (a), (b) and (c) of the data response questions adopts this approach. The mark scheme lists the marks that can be awarded for particular issues (and associated development) that the candidate might include in the answer.
- (ii) **A levels approach.** This approach is used for marking part (d) of the data response questions. The Levels Mark Scheme on the next page identifies five levels representing differences in the quality of work. A range of marks is allocated to each level. First decide the level into which an answer falls. The level chosen should be the one which **best fits** the answer provided by the candidate. It is **not** intended that the answer should satisfy every statement in the level description. Then think in terms of awarding the mid-point mark which has been identified for that level (e.g. 14 marks for Level 3). Move up or down from this notional mark by considering the extent to which the answer meets the level description overall. Strength in one skill can outweigh weakness in another. When using the Levels Mark Scheme the marker **must** identify where a particular skill is being demonstrated. The **key** to be used to identify the skill is given after the level descriptions. The question-specific mark scheme summarises the information which could be used to answer the question, but without attaching marks to particular issues.

THE LEVELS MARK SCHEME FOR AS

Level Descriptions

In part (d) of the data response questions, approximately half the marks are available to award to candidates who demonstrate that they can evaluate economic arguments and evidence, and make informed judgements. An answer showing no evidence of evaluation, however good the analysis, should be awarded a maximum of 13 marks (in Level 3). The quality of evaluation should be the sole distinction between a Level 4 and Level 5 answer. It is not necessary for the answer to identify a wide range of issues to score the top mark. As indicated below, the **Quality of Written Communication** used should be taken into account when awarding marks.

Level 1: A very weak answer

Few, if any, relevant issues are recognised. Economic concepts and principles are not adequately understood or applied to the question. No satisfactory analysis or evaluation. There might be some evidence of organisation in the answer but generally it fails to answer the question. Descriptions and explanations lack clarity. Spelling, punctuation and grammar may be poor. There is little use of economic terminology.

0 to 6 marks

Mid-Point 4 marks

Level 2: A poor answer but some understanding is shown

One or more relevant issues are recognised. An attempt is made to use basic economic concepts to answer the question but the candidate's explanation may become confused and analysis will therefore be very limited. There may be some attempt to present alternative points of view but any attempt at evaluation is limited or superficial. There is some logic and coherence in the organisation of the answer. The candidate demonstrates some ability to spell commonly used words and to follow the standard conventions of punctuation and grammar. Some use of economic terminology is made but this is not always applied appropriately.

7 to 11 marks

Mid-Point 9 marks

Level 3: An adequate answer with some correct analysis but very limited evaluation

Two or more relevant issues are recognised. The candidate has made a reasonable attempt to apply economic concepts and ideas. A satisfactory understanding of some basic economic concepts and theories is demonstrated and there is some evidence that the candidate can analyse issues. There will be some attempt to present alternative points of view and to evaluate the issues, arguments and/or data. There is some logic and coherence in the organisation of the answer. The candidate is generally able to spell commonly used words and usually follows the standard conventions of punctuation and grammar. Some descriptions and explanations are easy to understand, but the answer may not be expressed clearly throughout. There is some evidence of the correct use of relevant economic terminology.

12 to 16 marks

Mid-Point 14 marks

Level 4: Good analysis but limited evaluation

Two or more relevant issues are identified. Good understanding of basic economic concepts and models is demonstrated. The candidate is able to apply these concepts and models to answer the question. Some appreciation of alternative points of view is shown. Satisfactory use is made of evidence and/or theoretical analysis to evaluate the issues/arguments/economic models identified and to support conclusions. Spelling is generally accurate and the standard conventions of punctuation and grammar are usually followed. The answer is well organised. Descriptions and explanations are clearly expressed. Appropriate use is made of relevant economic terminology.

17 to 21 marks

Mid-Point 19 marks

Level 5: Good analysis and evaluation

Two or more relevant issues are identified. Good understanding of basic economic concepts and models is demonstrated. The candidate is able to apply these concepts and models to answer the question. Clear understanding of alternative points of view is shown. Good use is made of evidence and/or theoretical analysis to evaluate the issues/arguments/economic models identified and to support conclusions. A clear final judgement is made. Spelling is generally accurate and the standard conventions of punctuation and grammar are usually followed. The answer is well organised. Descriptions and explanations are clearly expressed. Appropriate use is made of relevant economic terminology.

22 to 25 marks

Mid-Point 24 marks

THE KEY TO BE USED WHEN USING THE LEVELS MARK SCHEME

- D** Where a particular economic term is correctly **DEFINED** in order to help the candidate to answer the question properly.
- I** Where a relevant **ISSUE** is raised by the candidate.
- K** Where the candidate demonstrates **KNOWLEDGE** of recent developments or features of the economy which help enhance the candidate's response to the question. This should also be used where the candidate quotes relevant examples.
- Ap** Where the candidate demonstrates the ability to **APPLY** knowledge and **CRITICAL UNDERSTANDING** to problems and issues.
- A** Where the candidate demonstrates the ability to **ANALYSE** the problem using appropriate economic ideas.
- E** Where the candidate **EVALUATES** and makes judgements about the significance of various issues and arguments.

EITHER**Total for this question: 50 marks****26 TRADE, THE EXCHANGE RATE AND THE UK ECONOMY**

26 (a) Define the term 'balance of trade in goods and services' (**Extract B**, line 12).
(5 marks)

For an acceptable definition, e.g.

- (i) The total value of exports of goods and services minus the total value of goods and services that are imported
- (ii) Exports of goods and services less imports of goods and services

NB Full marks should be awarded to a candidate who demonstrates a clear understanding of the term 'balance of trade in goods and services' even if the definition isn't exactly the same as the acceptable examples quoted above. **5 marks**

If the definition is incomplete (or inaccurate) marks can be broken down, for example as follows:

The difference between exports and imports of goods and services (i.e. the candidate does not make it clear that it is calculated by subtracting imports from exports) **4 marks**

Exports minus imports (i.e. the candidate doesn't make it clear that both goods and services are included) **4 marks**

Number (or volume) of goods and services exported minus the number (or volume) of goods and services imported **4 marks**

Define the term deficit as imports greater than exports **and/or** surplus as exports greater than imports **4 marks**

Imports of goods and services minus exports of goods and services **2 marks**

Imports less exports **2 marks**

This mark scheme does not allow examiners to award 1 mark for a point. Examiners must award 0, 2 or 4 marks for each point made by the candidate.

MAXIMUM FOR PART (a): 5 MARKS

- 26 (b)** Using the data in **Extract A**, identify **two** components of the current account that have led to the improvement in the current account balance that occurred between the fourth quarter of 2007 and the first quarter of 2008. **(8 marks)**

Award up to 4 marks for each valid point made (two marks for identification and up to two marks for supporting references to the data). The valid points include:

- The fall in the deficit in the balance of trade in goods (from £24.1 billion to £22.7 billion **OR** by £1.4 billion). Alternatively, a candidate might identify the reduction in the deficit in the balance of trade in goods and services (from £14.6 billion to £13.5 billion **OR** by £1.1 billion)
- The increased surplus in the income balance (from £6.9 billion to £9.0 billion **OR** by £2.1 billion)
- The fall in the deficit in the current transfers balance (from £4.5 billion to £3.9 billion **OR** by £0.6 billion)

Give only **1 mark** for the supporting references to the data if 'billion' and/or '£' is not included.

A maximum of **4 marks** may be awarded if there is no use of correct statistics.

MAXIMUM FOR PART (b): 8 MARKS

26 (c) Explain the likely effect of a recession in the eurozone upon the current account of the UK balance of payments. **(12 marks)**

For candidates who:

define relevant terms, e.g. recession and current account of the balance of payments.

**(2 marks for each definition) - maximum of 2 marks
for definitions.**

state that the eurozone is a major market for UK exports.

2 marks

state that a recession in the eurozone is likely to lead to a deterioration in the current account balance.

2 marks

Award up to 6 marks for each effect identified and analysed

explain that a recession in the eurozone means a fall in consumer spending (and/or national income) **(2 marks)**, hence there will be a reduction in the demand for UK exports of final goods and services **(2 marks)** and the fall in UK exports increases the size of the deficit **(2 marks)**.

Up to 6 marks

2 marks should be awarded for each logical link in the chain of reasoning

explain that a recession in the eurozone means a fall in production and hence a reduction in the demand for raw materials and semi-finished goods exported from the UK. **Up to 6 marks**

explain the significance of income elasticity of demand (or the marginal propensity to import) in determining the extent of the fall in demand for UK exports (*credit to be given even though knowledge of YED and the MPM are not required for this module*). **Up to 6 marks**

explain that a recession in the eurozone may lead to lower inflation, meaning that UK exports are less competitive, reducing the demand for UK exports. **Up to 6 marks**

explain that the recession in the eurozone might lead to lower prices for European exports and that this may result in higher imports into the United Kingdom from the eurozone.

Up to 6 marks

provide a plausible explanation of the impact of a recession in the eurozone on any other component of the current account balance (e.g. a recession in the eurozone might lead to lower earnings on UK investments in Europe and hence reduce the surplus on the income balance). **Up to 6 marks per component**

Candidates who assert that a recession in the eurozone will affect the exchange rate should only be given credit for the effect on the current account of the UK balance of payments if they provide a plausible explanation of why the euro exchange rate might change.

Up to 6 marks

Any other **relevant** effect of a recession in the eurozone upon the current account of the UK balance of payments. **Up to 6 marks**

Award **up to 4 marks** for the use of relevant diagrams (**2 marks** for labelling, **2 marks** for the information shown) i.e. candidates can achieve **4 marks** for one diagram.

MAXIMUM FOR PART (c): 12 MARKS

26 (d) Assess the view that a fall in the exchange rate of the pound will help to improve the performance of the UK economy. (25 marks)

In this part of the question, candidates will need to demonstrate that they are able to evaluate issues and arguments to support a conclusion if they are to be awarded **more than 13 marks**.

Candidates who make a genuine attempt at evaluation should be well rewarded. *For this question they might identify plausible reasons why a fall in the pound might **both** improve the performance of the UK economy **and** reduce it. This might relate to the effects on a particular objective of economic policy or on the overall performance of the economy. The use of evidence to support arguments should also be rewarded as evaluation. The difference between short-run and long-run effects might also be discussed. Candidates might also discuss other factors that will affect how significant the reduction in the exchange rate is for the performance of the UK economy, e.g. inflation in the UK compared to other economies.*

Issues and areas for discussion:

Extract B and Extract C provide some help to candidates, particularly the references to the impact of a lower exchange rate upon competitiveness and the balance of trade in goods and services. It is anticipated that answers will focus on the main indicators of macroeconomic performance, i.e. inflation, growth, unemployment and the balance of payments. However, credit can also be given for discussion of other reasonable indicators of macroeconomic performance such as productivity and living standards.

- the main indicators of macroeconomic performance
- the impact of a fall in the exchange rate upon export and import prices (on competitiveness)
- the possible effects on inflation (demand-pull and cost-push)
- the possible effects on economic growth
- the possible effects on employment and unemployment
- the possible effects on the current account balance
- the effects on other indicators of economic performance such as living standards, manufacturing industry, productivity

When discussing the above, candidates can gain credit for evaluation if they recognise that the fall in the value of the pound can have both favourable and unfavourable effects on the economy, e.g. it may stimulate growth and employment but add to inflationary pressures. Further marks for evaluation might come from discussing the following:

- short-run versus long-run effects
- depends on the current state of the economy
- the significance of elasticities
- how the effects of a fall in the exchange rate might be affected by other factors, e.g. changing government policy, supply-side changes within the UK and in overseas economies

- a conclusion that attempts to bring together the arguments presented and to assess whether or not a fall in the exchange rate is likely to improve the overall performance of the UK economy

The issues identified above are intended to provide an indication of some of the areas which might be discussed. Candidates can only be expected to consider a few of these issues in the time available.

Also give credit for:

- use of diagrams, e.g. AD/AS
- use of data and reference to the UK and/or other economies
- an overview of issues raised; a final judgement that is probably contained in a concluding paragraph.

USE THE LEVELS MARK SCHEME ON PAGES 5 AND 6

MAXIMUM FOR PART (d): 25 MARKS

TOTAL FOR THIS QUESTION: 50 MARKS

OR

27 EMPLOYMENT AND UNEMPLOYMENT

Total for this question: 50 marks

27 (a) Define the term 'real GDP' (**Extract F**, line 2).

(5 marks)

For an acceptable definition, e.g.

- (i) a measure of national income with the effects of inflation removed (when inflation is taken into account is acceptable)
- (ii) the value of total expenditure with the effects of inflation removed
- (iii) national income measured at constant prices
- (iv) a measure of the total output of the economy

NB Full marks should be awarded to a candidate who demonstrates a clear understanding of the term 'real GDP' even if the definition isn't exactly the same as the acceptable examples quoted above. **5 marks**

If the definition is incomplete (or inaccurate) marks can be broken down, for example as follows:

For stating that:

'real' means that the effects of inflation have been removed (adjusted for inflation is also acceptable) **2 marks**

GDP is a measure of national income **2 marks**

GDP = output = income = expenditure **2 marks**

GDP = Gross Domestic Product **2 marks**

real is the same as measuring at constant prices (or the chained volume measure) **2 marks**

Gross is before capital consumption (depreciation) has been taken into account **2 marks**

Domestic is before net property income from abroad has been taken into account **2 marks**

$GDP = C + I + G + X - M$ **2 marks**

This mark scheme does not allow examiners to award 1 mark for a point. Examiners must award 0, 2 or 4 marks for each point made by the candidate.

MAXIMUM FOR PART (a): 5 MARKS

27 (b) Using **Extract D**, identify **two** significant points of comparison between changes in the employment rate and changes in the unemployment rate between January 2004 and May 2008. **(8 marks)**

Award up to 4 marks for each valid point made (two marks for identification and up to two marks for supporting references to the data). The valid points include:

- the rate of employment and unemployment both rose over the period as a whole (each by less than half a percent) (unemployment 4.9% to 5.2%, employment 74.8% to 74.9%. It is acceptable if employment is unchanged but they need to quote figures.)
- through most of the period a rise in employment is accompanied by a fall in unemployment (e.g. from the start of 2007 to the end of the period the employment rate rose by approximately .5% whereas the unemployment rate fell by approximately .25%)
- both the rates of employment and unemployment were fairly stable over the period (employment varied between 74.3% and 75.0% and unemployment varied between 4.7% and 5.6%)
- the largest increase in unemployment is between the middle of 2005 and the middle of 2006 and although the rate of employment fell during this period the decline was more modest (unemployment rose from around 4.7% to 5.6% whereas the employment rate fell from around 74.8% to approximately 74.5%)
- the employment rate is much greater than the unemployment rate (the employment rate is around 74% whereas the unemployment rate is around 5%)
- the unemployment rate is more volatile than the employment rate (the unemployment rate varies between 4.7% and 5.6% whereas the variation in the employment rate is between 74.2% and 75%)

Give only **1 mark** for the supporting references to the data if the % sign is not included.

A maximum of **2 marks** may be awarded if there is no comparison and a maximum of **4 marks** if there is no use of correct statistics or if a candidate confines the comparison to just one indicator.

If the candidate simply trawls through the data, award a maximum of **4 marks**.

A maximum of **6 marks** may be awarded where there is evidence of an overview being taken, even though parts of the answer give the impression of a trawl through the data.

MAXIMUM FOR PART (b): 8 MARKS

27 (c) Explain why 'weaker demand conditions in the UK economy' (**Extract E**, lines 6-7) are likely to lead to rising unemployment. **(12 marks)**

For candidates who:

define relevant terms, e.g. what is meant by 'weaker demand conditions' and/or unemployment **(2 marks for each definition) - maximum of 2 marks for definitions**

identifying one or more factors that might lead to a fall in AD **2 marks**

stating that lower demand will reduce production **(2 marks)** because a fall in aggregate demand will result in the stock of unsold goods increasing **(2 marks)** therefore firms will reduce production so that their stocks return to more normal levels **(2marks)** and they will also lower output so that it makes the new lower level of output **(2 marks)**.

2 marks should be awarded for each logical link in the chain of reasoning

explain the link between output, employment and unemployment **Up to 6 marks**

explain the significance of changes in productivity/profitability **Up to 6 marks**

explain possible multiplier effects **Up to 6 marks**

Any other convincing reasons why weaker demand conditions in the UK economy might lead to rising unemployment **Up to 6 marks**

Award **up to 4 marks** for the use of relevant diagrams (**2 marks** for labelling, **2 marks** for information shown) i.e. candidates can achieve **4 marks** for one diagram.

MAXIMUM FOR PART (c): 12 MARKS

27 (d) Extract F (lines 10-12) states: 'A significant increase in unemployment seems inevitable and, in the short run, there is not much that a government can do about it.'

Evaluate alternative measures which can be used to reduce unemployment.

(25 marks)

In this part of the question, candidates will need to demonstrate that they are able to evaluate issues and arguments to support a conclusion if they are to be awarded **more than 13 marks**.

Candidates who make a genuine attempt at evaluation should be well rewarded. *For this question candidates are likely to evaluate by discussing the advantages and disadvantages of individual policies. They should also be rewarded for comparing the relative merits of different policies. Candidates might also consider the effectiveness of the policies in dealing with different causes of unemployment and the possible conflicts with other objectives of economic policy. The difference between the long-run and short-run effects of individual policies might also be discussed. Some candidates might use their knowledge of recent developments in the United Kingdom economy and elsewhere to help them assess the pros and cons of the policies a government can use to try to reduce unemployment.*

Issues and areas for discussion:

It is anticipated that candidates will draw on some of the issues raised in the extracts such as the reference in Extract F that indicates that it is difficult for the Bank of England to cut interest rates when inflation is high. It is also possible that candidates will draw on their knowledge of the measures that have been adopted during the past decade and recent trends in the UK economy to help them to assess the alternative policies available to a government wishing to reduce unemployment.

- definition of unemployment
- types/causes of unemployment, e.g. frictional, structural and cyclical unemployment

(Although classifications of unemployment such as real wage unemployment and the natural rate of unemployment are not part of the AS specification, if candidates use these ideas in a manner which is relevant to the question they should be rewarded)

- policy measures linked to the different causes of unemployment
- increasing aggregate demand to reduce cyclical unemployment
- tax cuts as a policy to reduce unemployment
- increased government spending
- cuts in interest rates
- measures to increase the supply of money and credit
- reductions in the exchange rate
- supply-side policies to reduce unemployment
- measures to improve the geographical and occupational mobility of labour (e.g. housing market reforms and retraining)
- better job information services
- government support of particular industries
- measures to increase incentives to work, e.g. reform of the tax-benefit system

Discussion that should be rewarded as evaluation includes:

- the problems and constraints when using fiscal policy to try to reduce unemployment, e.g. large budget deficits, growing national debt, time lags
- the problems and constraints when using monetary policy to try to reduce unemployment, e.g. possible conflict with the use of interest rates to control inflation, the effect of a fall in the exchange rate on living standards, time lags
- problems and benefits of using supply-side measures to reduce unemployment, e.g. possible ineffectiveness when there is a general lack of demand, help to avoid possible conflicts with other policy objectives
- an assessment of the pros and cons of individual policy measures, e.g. measures to increase incentives to work may involve reducing the real income of those who are unemployed and may be judged to be inequitable
- constraints imposed by external events upon the effectiveness of policies to reduce unemployment, including demand-side and supply-side shocks
- possible conflicts between policy objectives as a disadvantage of some policies that are used to reduce unemployment
- short-run versus long-run effects of the different policies
- a conclusion that attempts to provide an overall assessment of the relative merits of the policies identified and discussed

The issues identified above are intended to provide an indication of some of the areas which might be discussed. Candidates can only be expected to consider a few of these issues in the time available.

Also give credit for:

- use of diagrams, e.g. AD/AS
- use of data plus reference to the UK and/or other economies
- an overview of issues raised; a final judgement that is probably contained in a concluding paragraph

USE THE LEVELS MARK SCHEME ON PAGES 5 AND 6

MAXIMUM FOR PART (d): 25 MARKS

TOTAL FOR THIS QUESTION: 50 MARKS



General Certificate of Education
Advanced Subsidiary Examination
June 2009

Economics

ECON2

Unit 2 The National Economy

Specimen paper for examinations in June 2010 onwards

This question paper uses the new numbering system and new AQA answer book

For this paper you must have:

- an objective test answer sheet
- a black ball-point pen
- an AQA 8-page answer book.

You may use a calculator.

Time allowed

- 1 hour 15 minutes

Instructions

- In **Section A**, answer **all** questions on your objective test answer sheet.
- In **Section B**, answer **EITHER** Question 26 **OR** Question 27 in your answer book.
- For **Section A**, do all rough work in your answer book, **not** on your objective test answer sheet.

Section A (ECON2/1)

- Use a black ball-point pen. Do **not** use pencil.

Section B (ECON2/2)

- Use black ink or black ball-point pen. Pencil should only be used for drawing.
- Write the information required on the front of your answer book. The **Examining Body** for this paper is AQA. The **Paper Reference** is ECON2/2.

Information

- The maximum mark for this paper is 75.
- There are 25 marks for **Section A** and 50 marks for **Section B**.
- In **Section A**, each question carries 1 mark. No deductions will be made for wrong answers.
- In **Section B**, the marks for questions are shown in brackets.
- You will be marked on your ability to:
 - use good English
 - organise information clearly
 - use specialist vocabulary where appropriate.

Advice

- You are advised to spend no more than 25 minutes on **Section A** and at least 50 minutes on **Section B**.

Section A Objective Test

Answer **all** questions in **Section A**.

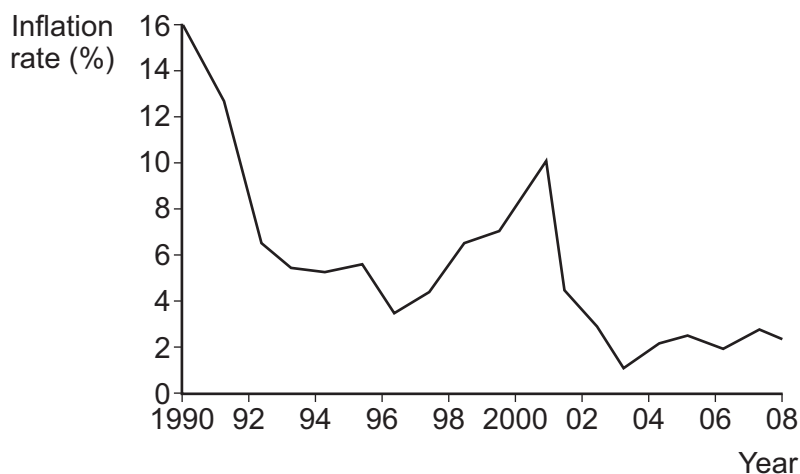
Each question carries 1 mark. No deductions will be made for wrong answers.

You are advised to spend no more than 25 minutes on **Section A**.

For each question there are four alternative responses, **A**, **B**, **C** and **D**. When you have selected the response which you think is the best answer to a question, mark this response on your objective test answer sheet. If you wish to change your answer to a question, follow the instructions on your objective test answer sheet.

- 1** An increase in imports of consumer goods is most likely to be caused by a
- A** rise in household saving.
 - B** rise in household income.
 - C** fall in the exchange rate.
 - D** fall in employment.
- 2** Real incomes rise whenever
- A** nominal incomes rise by more than the price level.
 - B** the price level rises by more than nominal incomes.
 - C** nominal incomes rise.
 - D** the rate of inflation slows down.
- 3** A current account deficit on the UK's balance of payments means that generally
- A** the total value of imports exceeds the total value of exports.
 - B** government expenditure exceeds government revenue.
 - C** the value of exports of services is less than the value of imports of services.
 - D** the volume of imports of goods and services exceeds the volume of exports of goods and services.

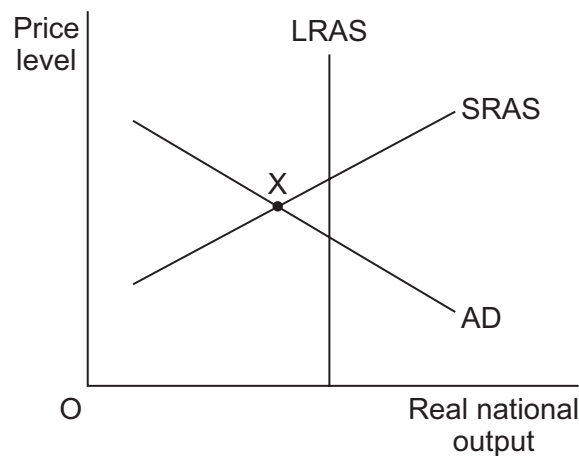
- 4 Which one of the following is an example of fiscal policy? A decision by the government to
- A decrease the exchange rate
 - B raise the minimum wage
 - C increase its budget surplus
 - D reduce the rate of interest
- 5 The economy is currently operating at its normal capacity level of output. It is estimated that the long-run trend rate of growth of the economy is around 2.5% per annum. In the coming year, it is expected that inflation will be 4% per annum and money national income will grow by 5%. Which one of the following is most likely?
- A Unemployment will fall and the economy will grow below its trend rate
 - B Employment will be stable and the economy will grow at its trend rate
 - C Employment will rise and the economy will grow above its trend rate
 - D Unemployment will increase and the growth of the economy will be below its trend rate
- 6 The graph below shows an economy's inflation rate from 1990 to 2008.



From the graph, it may be deduced that average prices

- A were lower in 2008 than in 1990.
- B fell sharply from 1990 to 1992.
- C increased each year from 1990 to 2008.
- D were lowest in 2003.

- 7 All other things being equal, when an increase in exports leads to a larger increase in national income, this illustrates
- A an improvement in the balance of payments.
 - B demand-pull inflation.
 - C an increase in long-run aggregate supply.
 - D the operation of the multiplier.
- 8 The diagram below shows the aggregate demand curve and the short-run and long-run aggregate supply curves of an economy.



The economy is currently operating at point X. At this point, the economy must be experiencing

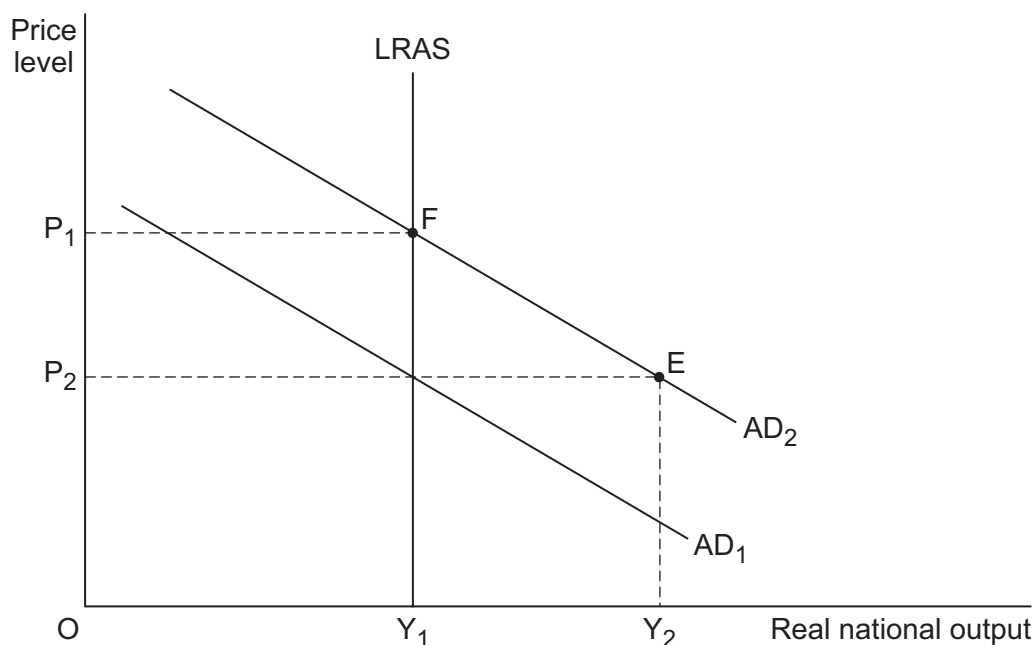
- A inflation caused by excess demand.
 - B inflation caused by increasing costs.
 - C unemployment of labour.
 - D a low rate of economic growth.
- 9 In the short run, a decrease in aggregate demand is most likely to result in a reduction in
- A government spending on welfare benefits.
 - B the unemployment rate.
 - C the budget deficit.
 - D the balance of payments deficit on the current account.

- 10 An economy is operating at full employment. Which one of the following is most likely to lead to an increase in real national output without an increase in the rate of inflation in the short term?
- A An increase in exports
 - B A reduction in interest rates
 - C An increase in manufacturing productivity
 - D An increase in government expenditure
- 11 Which one of the following is most likely to lead to a fall in aggregate investment?
- A A reduction in the level of unemployment
 - B An increase in spare capacity in the economy
 - C A reduction in the average level of interest rates
 - D An increase in aggregate demand
- 12 Inflation in an economy is currently at 10%. Which of the following changes in monetary and fiscal policy, **A**, **B**, **C** or **D**, is most likely to bring down the rate of inflation in the economy?

	Interest rates	Government expenditure	Taxation revenue
A	Increase	Increase	Decrease
B	Decrease	Decrease	Increase
C	Increase	Decrease	Increase
D	Decrease	Increase	Increase

- 13 A rise in the exchange rate of the pound sterling is likely to assist UK government policies aimed at reducing the
- A rate of inflation.
 - B level of unemployment.
 - C level of imports.
 - D balance of payments deficit.

- 14** The Consumer Prices Index (CPI) rises from 100 to 105. This shows that
- A** the inflation rate has increased by 5%.
 - B** the average price level has increased by 5%.
 - C** the price of every good has increased by 5%.
 - D** inflation in the economy is rising at a constant 5% per annum.
- 15** The diagram below shows two aggregate demand curves and the long-run aggregate supply curve for the UK economy.



The government predicts that aggregate demand will increase in the long run from AD_1 to AD_2 . Which one of the following policies is most likely to move the economy to a new long-run equilibrium at point E rather than point F ?

- A** Pursuing an expansionary monetary policy
- B** Allowing the exchange rate to rise
- C** Increasing taxation
- D** Improving the mobility of labour

- 16 Which one of the following, **A**, **B**, **C** or **D**, is most likely to be associated with an accelerator process in an economy?

	Rate of change of consumer income	Spare productive capacity in manufacturing	Supply of investment funds
A	Rising	High	Low
B	Falling	Low	High
C	Rising	Low	High
D	Falling	Low	Low

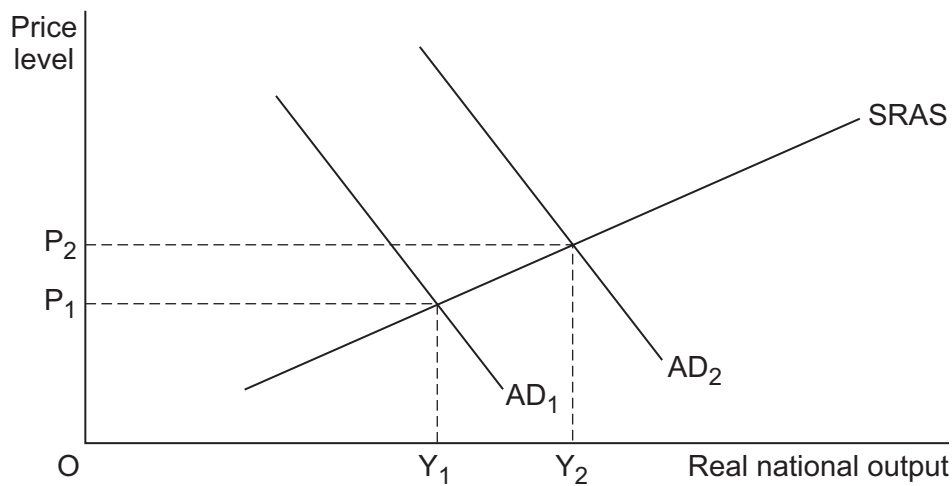
- 17 Between 2004 and 2006, an estimated 600 000 workers arrived in the UK from new members of the European Union (EU) in Eastern Europe. At the same time, inflation remained low, economic growth was strong, unemployment hardly changed and the current account position on the balance of payments deteriorated. Given this information, which one of the following is most likely to have been correct between 2004 and 2006?

- A** Inflation was low because increases in costs of imported raw materials to firms were very low.
- B** Economic growth was strong because the 600 000 workers from Eastern Europe increased the productive potential of the UK economy.
- C** Unemployment hardly changed because the arrival of 600 000 workers in the UK widened its output gap.
- D** The current account position deteriorated because inflation remained low throughout the period.

- 18 The underlying trend rate of growth in an economy is declining and the economy is also experiencing an increase in its rate of unemployment. Which one of the following is likely to be most effective in dealing with these problems?

- A** An expansionary fiscal policy and a restrictive monetary policy
- B** A restrictive monetary and fiscal policy
- C** An expansionary monetary policy and supply-side policies
- D** A restrictive fiscal policy and supply-side policies

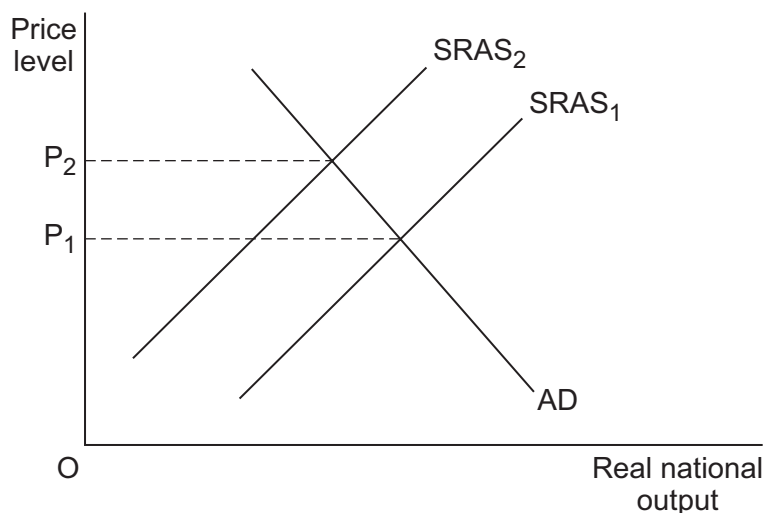
- 19** Which one of the following is most likely to be classified as a supply-side policy?
- A** An increase in subsidies on essential goods
 - B** An increase in the government budget deficit
 - C** A reduction in the exchange rate
 - D** A reduction in the tax on company profits
- 20** An economy is experiencing a balance of payments deficit and inflation. All other things being equal, which policy is most likely to reduce both the balance of payments deficit on current account and the rate of inflation?
- A** A fall in government spending
 - B** A cut in interest rates
 - C** A decrease in the rate of income tax
 - D** A reduction in the exchange rate
- 21** The diagram below shows how real national output and the price level are affected by a change in aggregate demand.



All other things being equal, the shift in the aggregate demand schedule from AD_1 to AD_2 could have been caused by an increase in

- A** the price of raw materials.
- B** the exchange rate.
- C** labour productivity.
- D** the budget deficit.

- 22** A fall in the value of the pound relative to the euro would be expected to affect the UK economy because it is likely to lead to
- A** an increase in aggregate demand.
 - B** a fall in raw material prices.
 - C** a rise in the euro price of UK exports.
 - D** a reduction in the rate of interest.
- 23** A cut in the central bank's lending rate is an example of
- A** monetary policy.
 - B** supply-side policy.
 - C** fiscal policy.
 - D** deflationary policy.
- 24** The diagram below represents an economy that has experienced inflation, with the price level rising from P_1 to P_2 .



The most likely cause of the inflationary pressures shown in the diagram is

- A** a sustained increase in the money supply.
- B** a growing budget deficit.
- C** money wages increasing faster than productivity.
- D** a period of time when interest rates are too low.

Turn over ►

- 25** Other things being equal, increased innovation in an economy is likely to lead to a
- A** fall in the equilibrium level of output.
 - B** fall in the size of the labour force.
 - C** leftward shift of the aggregate demand curve.
 - D** rightward shift of the long-run aggregate supply curve.

**Question 25 is the last
question in Section A**

**On your answer sheet
ignore rows 26 to 50**

Turn to page 12 for Section B

Turn over for the next question

Turn over ►

Section B Data Response

Answer **EITHER** Question 26 **OR** Question 27.
You are advised to spend at least 50 minutes on **Section B**.

EITHER

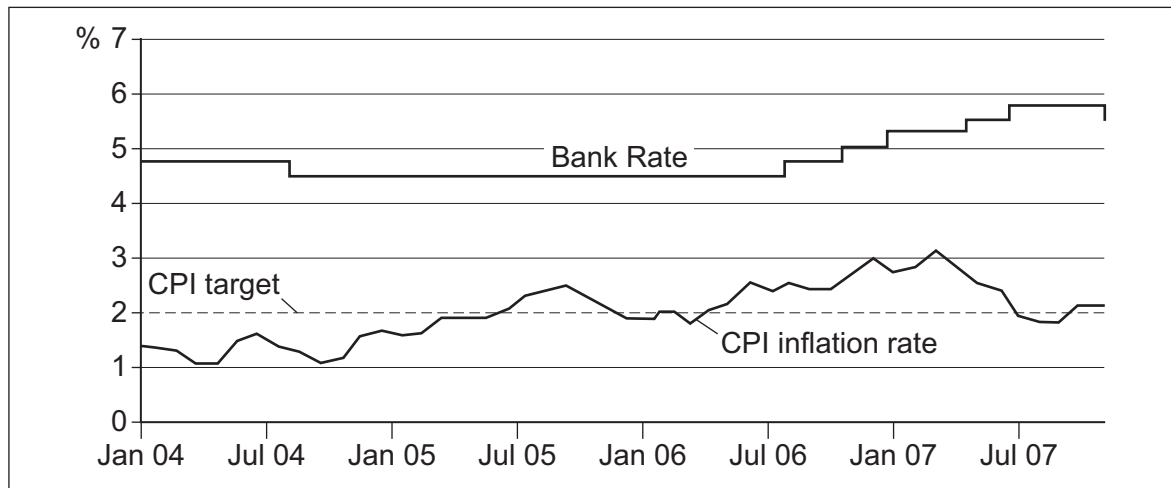
Total for this question: 50 marks

Question 26

UNITED KINGDOM INFLATION AND MONETARY POLICY

Study **Extracts A, B and C**, and then answer **all** parts of Question 26 which follows.

Extract A: UK inflation rate and Bank Rate, January 2004 to December 2007



Source: adapted from official statistics

Extract B: Monetary policy in the United Kingdom

The Bank of England's monetary policy objective is to deliver price stability and, having achieved that, to support the Government's economic objectives including those for growth and employment. Price stability is defined by the Government's inflation target of 2%. The inflation target of 2% is expressed in terms of an annual rate of inflation based on the Consumer Prices Index (CPI). If the annual rate of CPI inflation is more than 3% or less than 1%, the Governor of the Bank must write an open letter to the Chancellor explaining the reasons why inflation has increased or fallen to such an extent, and what the Bank proposes to do to ensure inflation comes back to the target.

1

5

The Bank of England uses interest rates to try to achieve the inflation target. [When the Bank changes the interest rate (currently known as the Bank Rate) it is attempting to influence the overall level of spending in the economy. When total spending grows more quickly than the volume of output produced, inflation is the result.]

10

Source: adapted from www.bankofengland.co.uk, accessed on 5 January 2008

Source: adapted from the minutes of the Monetary Policy Committee (MPC) meeting, *Bank of England*, 5 and 6 December 2007

Question 26

- Turn over for the next question**

STEMUP.CO.UK

Do **not** answer Question 27 if you have answered Question 26.

OR

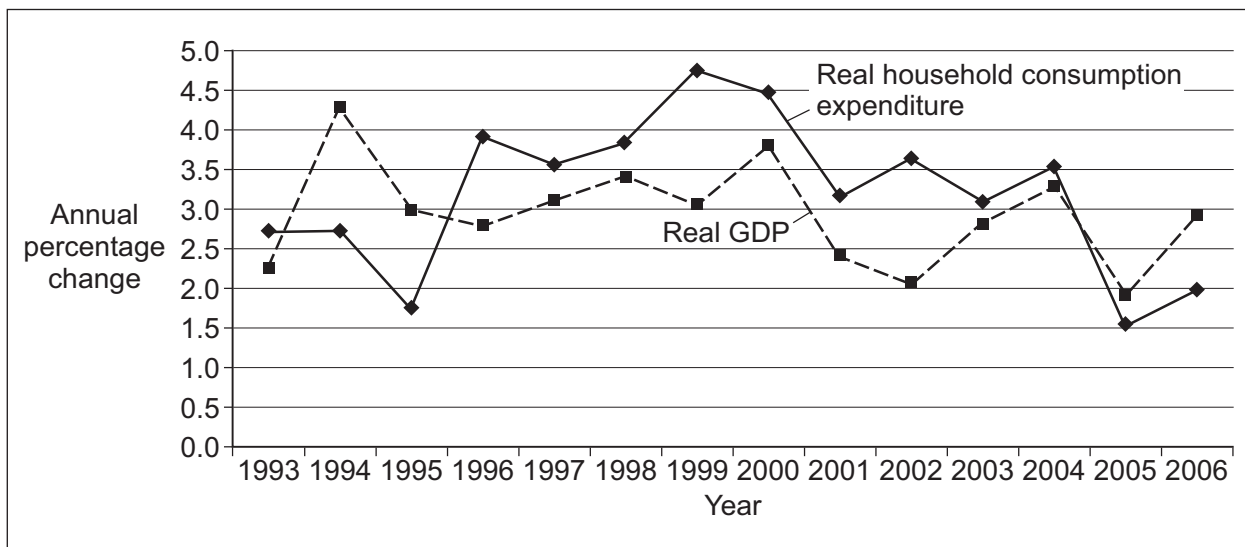
Total for this question: 50 marks

Question 27

CONSUMPTION EXPENDITURE AND THE UNITED KINGDOM ECONOMY

Study **Extracts D, E and F**, and then answer **all** parts of Question 27 which follows.

Extract D: Growth in real household consumption expenditure and real GDP, 1993 to 2006



Source: www.statistics.gov.uk

Extract E: The prospects for consumption in the United Kingdom

In 2007, the United Kingdom economy grew at a strong and steady pace. Economic activity has been supported in particular by the continued increase in consumer spending. However, future growth is likely to be affected by tighter availability of credit. If the reduction in lending also leads to a fall in house prices, this is likely to result in a further reduction in the growth of consumer expenditure.	1 5
Increased uncertainty about the future state of the economy may also lead to a rise in savings, particularly given the current high level of household debt. If real disposable income falls and job prospects deteriorate, the impact on consumption could be significant. However, the recent reduction in Bank Rate and the expectation that further cuts are on the way will help to maintain spending.	10

Source: news reports, January 2008

Extract F: Consumption and the performance of the economy

In the United Kingdom, consumption expenditure accounts for around 64% of GDP and the level of consumption is generally a good indicator of the strength of the economy. Rising consumption encourages firms to increase output and to increase employment. In the short run, rising consumption expenditure boosts economic growth but other factors, such as investment, changes in technology, productivity and the size of the working population, are likely to have a more enduring influence.	1 5
The strength of consumption relative to potential supply is also a factor in determining inflationary pressure in the economy. The balance of trade in goods and services is affected by consumer spending; United Kingdom consumers spend heavily on imports, so that when real incomes and consumption are rising, so too are imports.	10

Source: news reports, January 2008

Question 27

- 0 | 5** Define the term 'economic growth' (**Extract F**, line 5). (5 marks)
- 0 | 6** Using **Extract D**, identify **two** points of comparison between the growth in real household consumption expenditure and the growth of real GDP between 1993 and 2006. (8 marks)
- 0 | 7** **Extract E** (lines 3-4) state that 'future growth is likely to be affected by tighter availability of credit'.

Using an AD/AS diagram to help you, explain the likely effect of 'tighter availability of credit' upon output **and** employment. (12 marks)
- 0 | 8** **Extract F** (lines 2-3) state that 'the level of consumption is generally a good indicator of the strength of the economy'.

Assess the view that rising consumer expenditure is always beneficial for an economy. (25 marks)

END OF QUESTIONS

There are no questions printed on this page

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General Certificate of Education

Economics

ECON2: The National Economy

Mark Scheme

2009 examination - June series

This mark scheme uses the [new numbering system](#) which is being introduced for examinations from June 2010

Mark schemes are prepared by the Principal Examiner and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation meeting attended by all examiners and is the scheme which was used by them in this examination. The standardisation meeting ensures that the mark scheme covers the candidates' responses to questions and that every examiner understands and applies it in the same correct way. As preparation for the standardisation meeting each examiner analyses a number of candidates' scripts: alternative answers not already covered by the mark scheme are discussed at the meeting and legislated for. If, after this meeting, examiners encounter unusual answers which have not been discussed at the meeting they are required to refer these to the Principal Examiner.

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of candidates' reactions to a particular paper. Assumptions about future mark schemes on the basis of one year's document should be avoided; whilst the guiding principles of assessment remain constant, details will change, depending on the content of a particular examination paper.

Further copies of this Mark Scheme are available to download from the AQA Website: www.aqa.org.uk

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Set and published by the Assessment and Qualifications Alliance.

June 2009**ECON2****Advance Subsidiary Economics Unit 2****Section A: Objective Test****June 2009**

The following list indicates the correct answers used in marking the candidates' responses.

1.	B	10.	C	19	D
2.	A	11.	B	20	A
3.	A	12.	C	21	D
4.	C	13.	A	22	A
5.	D	14.	B	23	A
6.	C	15.	D	24	C
7.	D	16.	C	25	D
8.	C	17.	B		
9.	D	18.	C		

Advanced Subsidiary Economics**June 2009****ECON 2****Mark Scheme****Section B: Data Response****General Instructions**

Marks awarded to candidates should be in accordance with the following mark scheme and examiners should be prepared to use the full range of marks available. The mark scheme for most questions is flexible, permitting the candidate to score full marks in a variety of ways. Where the candidate's response to a question is such that the mark scheme permits full marks to be awarded, full marks **MUST** be given. A perfect answer is not necessarily required for full marks. But conversely, if the candidate's answer does not deserve credit, then no marks should be given.

Occasionally, a candidate may respond to a question in a reasonable way, but the answer may not have been anticipated when the mark scheme was devised. In this situation, **OR WHENEVER YOU HAVE ANY DOUBT ABOUT THE INTERPRETATION OF THE MARK SCHEME**, you must in the first instance telephone your team leader to discuss how to proceed.

Two approaches have been used in the construction of the mark scheme:

- (i) **An issue based approach.** The mark scheme for the first three elements of the data response questions adopts this approach. The mark scheme lists the marks that can be awarded for particular issues (and associated development) that the candidate might include in the answer.
- (ii) **A levels approach.** This approach is used for marking the final element of the data response questions. The Levels Mark Scheme on the next page identifies five levels representing differences in the quality of work. A range of marks is allocated at each level. First decide the level into which an answer falls. The level chosen should be the one which **best fits** the answer provided by the candidate. It is **not** intended that the answer should satisfy every statement in the level description. Then think in terms of awarding the mid-point mark which has been identified for that level (e.g. 14 marks for Level 3). Move up and down from this notional mark by considering the extent to which the answer meets the level description overall. Strength in one skill can outweigh weakness in another. When using the Levels Mark Scheme the marker **must** identify where a particular skill is being demonstrated. The **key** to be used to identify the skill is given after the levels descriptions. The question-specific mark scheme summarises the information which could be used to answer the question, but without attaching marks to particular issues.

THE LEVELS MARK SCHEME FOR AS

Levels Descriptions

In part (d) of the data response questions, approximately half the marks are available to award to candidates who demonstrate that they can evaluate economic arguments and evidence, and make informed judgements. An answer showing no evidence of evaluation, however good the analysis, should be awarded a maximum of 13 marks (in Level 3). The quality of the evaluation should be the sole distinction between a Level 4 and Level 5 answer. It is not necessary for the answer to identify a wide range of issues to score the top mark. As indicated below, the **Quality of Written Communication** used should be taken into account when awarding marks.

Level 1: A very weak answer

Few, if any, relevant issues are recognised. Economic concepts and principles are not adequately understood or applied to the question. No satisfactory analysis or evaluation. There might be some evidence of organisation in the answer but generally it fails to answer the question. Descriptions and explanations lack clarity. Spelling, punctuation and grammar may be poor. There is little use of economic terminology.

0 to 6 marks

Mid-Point 4 marks

Level 2: A poor answer but some understanding is shown

One or more relevant issues are recognised. An attempt is made to use basic economic concepts to answer the question but the candidate's explanation may become confused and analysis will therefore be very limited. There may be some attempt to present alternative points of view but any attempt at evaluation is limited or superficial. There is some logic and coherence in the organisation of the answer. The candidate demonstrates some ability to spell commonly used words and to follow the standard conventions of punctuation and grammar. Some use of economic terminology is made but this is not always applied appropriately.

7 to 11 marks

Mid-Point 9 marks

Level 3: An adequate answer with some correct analysis but very limited evaluation

Two or more relevant issues are recognised. The candidate has made a reasonable attempt to apply economic concepts and ideas. A satisfactory understanding of some basic economic concepts and theories is demonstrated and there is some evidence that the candidate can analyse issues. There will be some attempt to present alternative points of view and to evaluate the issues, arguments and/or data. There is some logic and coherence in the organisation of the answer. The candidate is generally able to spell commonly used words and usually follows the standard conventions of punctuation and grammar. Some descriptions and explanations are easy to understand, but the answer may not be expressed clearly throughout. There is some evidence of the correct use of relevant economic terminology.

12 to 16 marks

Mid-Point 14 marks

Level 4: Good analysis but limited evaluation

Two or more relevant issues are identified. Good understanding of some basic economic concepts and models is demonstrated. The candidate is able to apply these concepts and models to answer the question. Some appreciation of alternative points of view is shown. Satisfactory use is made of evidence and/or theoretical analysis to evaluate the issues/arguments/economic models identified and to support conclusions. Spelling is generally accurate and the standard conventions of punctuation and grammar are usually followed. The answer is well organised. Descriptions and explanations are usually clearly expressed. Appropriate use is made of relevant economic terminology.

17 to 21 marks

Mid-Point 19 marks

Level 5: Good analysis and evaluation

Two or more relevant issues are identified. Good understanding of basic economic concepts and models is demonstrated. The candidate is able to apply these concepts and models to answer the question. Clear understanding of alternative points of view is shown. Good use is made of evidence and/or theoretical analysis to evaluate the issues/arguments/economic models identified and to support conclusions. A clear final judgement is made. Spelling is generally accurate and the standard conventions of punctuation and grammar are usually followed. The answer is well organised. Descriptions and explanations are clearly expressed. Appropriate use is made of relevant economic terminology.

22 to 25 marks

Mid-Point 24 marks

THE KEY TO BE USED WHEN USING THE 'LEVELS' MARKING SCHEME

- D** Where a particular economic term is correctly **DEFINED** in order to help the candidate to answer the question properly.
- I** Where a relevant **ISSUE** is raised by the candidate.
- K** Where the candidate demonstrates **KNOWLEDGE** of recent developments or features of the economy which help enhance the candidate's response to the question. This should also be used where the candidate quotes relevant examples.
- Ap** Where the candidate demonstrates the ability to **APPLY** knowledge and **CRITICAL UNDERSTANDING** to problems and issues.
- A** Where the candidate demonstrates the ability to **ANALYSE** the problem using appropriate economic ideas.
- E** Where the candidate **EVALUATES** and makes judgements about the significance of various issues and arguments.

26 UNITED KINGDOM INFLATION AND MONETARY POLICY**Total for this question: 50 marks****01** Define the term 'negative output gap' (**Extract C**, line 11).**(5 marks)****For an acceptable definition e.g.**

- (i) When actual GDP is below the economy's productive potential
- (ii) Where the actual level of output is below the potential level of output
- (iii) Where the economy is working below full capacity
- (iv) Where the equilibrium level of output is below the full employment level of output

5 marks

NB Full marks should be awarded to a candidate who demonstrates a clear understanding of the term 'negative output gap' even if the definition isn't exactly the same as the four acceptable examples quoted above. Equally if this is shown accurately in a diagram, full marks should be awarded.

If the definition is incomplete (or inaccurate), marks can be broken down, for example as follows:

the actual level of output minus the potential level of output (i.e. the candidate defines the term output gap but doesn't attempt to explain '*negative*') **4 marks**

the term output gap is defined correctly BUT confuses a negative output gap with a positive output gap **4 marks**

the *growth* of actual output is less than the *growth* of potential output **4 marks**

a recession (or a recessionary gap) **2 marks**

there is unemployment in the economy **2 marks**

**This mark scheme does not allow examiners to award 1 mark for a point.
Examiners must award 0, 2 or 4 marks for each point made by the candidate**

MAXIMUM FOR 01 = 5 MARKS

02	Using Extract A , identify two points of comparison between the changes in Bank Rate and the changes in the CPI inflation rate between 2004 and 2007. <i>(8 marks)</i>
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Award up to 4 marks for each valid point made (two marks for identification and up to two marks for supporting references to the data). The valid points include:

- CPI inflation fluctuates by more than Bank Rate (e.g. Bank Rate from 4.5% to 5.75% whereas CPI inflation fluctuates from 1.1% to 3.1%)
- Up to July 06, there was little change in Bank Rate (either 4.5% or 4.75%) but CPI inflation fluctuated (e.g. ups and downs between 1.1% to 2.5%) whereas after July 06 both changed more frequently (e.g. Bank Rate rose in irregular steps from 4.5% to 5.75% and was then cut to 5.5% in December 07, CPI inflation fluctuated in the range 1.8% to 3.1%)
- Throughout the whole period the CPI rate of inflation was below Bank Rate although the difference between them varied (e.g. from 2% to 4%)
- Bank Rate tends to be cut when CPI inflation is below target and increased after inflation rises above the target (e.g. Bank Rate was cut in August 04 when CPI inflation was below target. It was increased in August 06, and subsequently, in a period when CPI inflation was above target and rising)
- In the period when Bank Rate is low (Jan 04 to July 06) the trend in CPI inflation is upwards (e.g. 1.1% to 3.1% in March 07) whereas when interest rates rise (Jan 06 to July 07), after a time lag, CPI inflation falls (e.g. from a peak of 3.1% in March 07 to 2.1% in November 07.)
- Between January 2004 and December 2007, both interest rates and CPI inflation rose. (Interest rates rose from 4.75% to 5.5% and inflation rose from 1.4% to 2.1%)
- The highest Bank Rate was in 2007 (5.57%) and the highest CPI inflation rate was also in 2007 (3.1%)
- The lowest Bank Rate was between 2004 and 2006 (4.5%) whereas the lowest CPI inflation rate was in 2004 (1.1%)

Award only **1 mark** for each supporting reference to the data if the % sign is missing.

Up to 4 marks may be awarded if there is no use of statistics to support the points made or if a candidate simply trawls through the data without attempting a comparison.

Up to 6 marks may be awarded where there is evidence of an overview being taken, even though parts of the answer give the impression of a trawl through the data.

Where a candidate has included more than two points, award marks to the best two points.

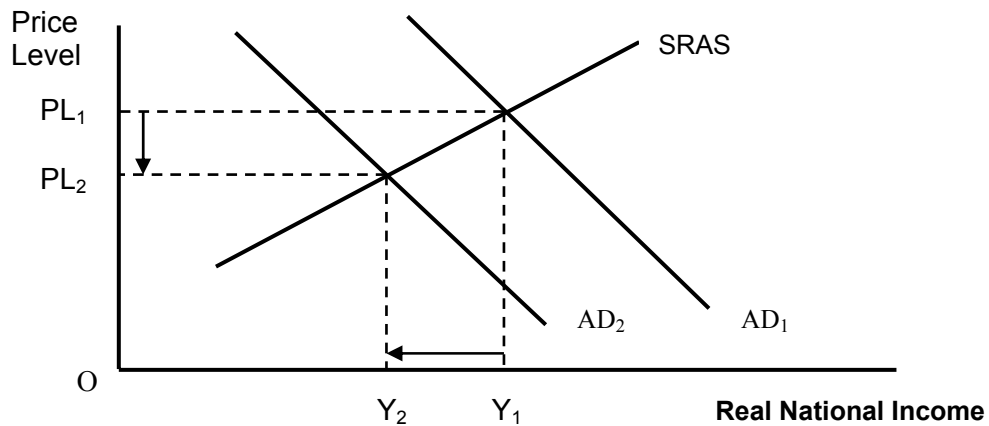
MAXIMUM FOR 02 = 8 MARKS

- 03** Using an AD/AS diagram to help you, explain the likely effect of an increase in interest rates upon inflation. *(12 marks)*

When awarding marks for the diagram, it is important to reward candidates who produce a valid response even if it is not the one which is shown below.

The anticipated response for the diagram:

An increase in interest will reduce aggregate demand and hence the diagram should show a leftward shift in the AD curve leading to a fall in the equilibrium output and price level. Most candidates are likely to draw an upward sloping SRAS curve but others might, for example, show the LRAS curve.



Breakdown of the marks for the diagram:

Axes labelled (allow Inflation, PL and Real GDP or National Output or output or Y but do NOT allow Price and Quantity) **1 mark**

Original AD and AS curves correctly labelled **1 mark**

Leftward shift in the AD curve **2 marks**

Dotted lines and associated labelling showing the original equilibrium point (Y_1 PL_1) **1 mark**

Dotted lines and associated labelling showing the new equilibrium point (Y_2 PL_2) **1 mark**

Any other relevant feature of the diagram (e.g. the amount of excess supply at the original equilibrium) **1 mark per feature up to a maximum of 2 marks**

Up to 6 marks for the diagram

The anticipated written response:

For candidates who:

define interest rates, inflation or other relevant concept

Up to 2 marks per definition
Maximum of 2 marks for definitions

explain why an increase in interest rates is likely to reduce AD (e.g. via the impact on the incentive to save, borrowing costs, mortgage repayments, the exchange rate, expectations, asset prices and wealth).

1 mark for identifying the effect and **1 mark** for explaining why it has this effect e.g. higher interest rates increase savings (**1 mark**) because savers receive a higher return on their savings (**1 mark**)
2 marks per explanation, up to 8 marks

use the diagram to explain the impact of the fall in AD on the price level and hence inflation (some may sensibly state that the most likely effect is a fall in inflation rather than a fall in the price level and they should be rewarded for doing so)
2 marks

explain why a reduction in AD is likely to reduce inflation (e.g. they might discuss the effects in the goods market, factor markets and hence wages and other factor prices)
Up to 4 marks

state or explain that a rise in interest rates will tend to increase the exchange rate and explain why a rise in the exchange rate is likely to reduce inflationary pressures (e.g. via its impact on AD and on the price of imports)
Up to 4 marks

Up to a MAXIMUM of 8 marks for the written explanation

MAXIMUM FOR 03 = 12 MARKS

04 **Extract B** (lines 11-12) states: 'When total spending grows more quickly than the volume of output produced, inflation is the result.'

Assess the view that inflation is always caused by an increase in aggregate demand.
(25 marks)

In this part of the question, candidates will need to demonstrate that they are able to evaluate issues and arguments to support a conclusion if they are to be awarded **more than 13 marks**.

Candidates who make a genuine attempt at evaluation should be well rewarded. *For this question they are likely to discuss possible causes of inflation, distinguishing between demand-pull and cost-push inflation, recognising that many economists believe that inflation can have different causes. Candidates may also discuss circumstances in which an increase in aggregate demand may or may not cause inflation, perhaps using an AD/AS diagram to support their discussion. They are likely to conclude that inflation can be caused by rising costs as well as an increase in aggregate demand and may refer to the data (especially **Extract C**) to support their conclusions.*

*Some of the best candidates may argue that rising costs result from an increase in aggregate demand and hence conclude that inflation **is** always caused by an increase in aggregate demand. Others might argue that although a short-term increase in the price level might result from an increase in costs, this cannot be sustained unless demand also increases.*

Issues and areas for discussion:

It is anticipated that candidates will draw on ideas given in **Extract C**, which outlines some of the factors that the Monetary Policy Committee consider might affect inflation. There are references to cost pressures as well as demand side influences on inflation.

- definition of inflation and aggregate demand
- explanation of the demand-pull inflationary process
- causes of an increase in aggregate demand
- give credit for the monetarist view of inflation (not expected as it is an A2 topic)
- explanation of the cost-push inflationary process
- rising wages and possibly strong trade unions as a source of cost-push inflation
- rising commodity prices as a source of cost-push inflation
- a falling exchange rate and/or an increase in the price of imports as a source of cost-push inflation
- the use of diagrams to illustrate demand-pull and cost-push inflation
- expectations and inflation
- the significance of the size of the output gap
- why inflation is likely to increase if aggregate demand grows more quickly than the volume of output produced

- circumstances when an increase in aggregate demand is not likely to cause inflation, e.g. when there is a significant negative output (or recessionary) gap or when productive capacity is increasing more rapidly than aggregate demand
- use of diagrams to illustrate the circumstances when an increase in aggregate demand may or may not lead to inflation
- increases in aggregate demand as the reason for persistently rising costs
- whether or not rising costs can cause inflation in the absence of an increase in aggregate demand
- use of the data, particularly in **Extract C**, to support arguments presented
- discussion of the Bank of England's view of the cause of inflation, perhaps making reference to **Extract B**
- a conclusion that attempts to bring together the arguments presented and to assess whether or not inflation is always caused by an increase in aggregate demand

The issues identified above are intended to provide an indication of some of the areas which might be discussed. Candidates can only be expected to consider a few of these issues in the time available.

Also give credit for:

- use of diagrams, e.g. AD/AS
- use of data plus reference to the UK and/or other economies
- an overview of issues raised; a final judgement that is probably contained in a concluding paragraph

USE THE LEVELS MARK SCHEME ON PAGES 5 AND 6

MAXIMUM FOR 04 = 25 MARKS

TOTAL FOR THIS QUESTION: 50 MARKS

27 CONSUMPTION EXPENDITURE AND UNITED KINGDOM ECONOMY**Total for this question: 50 marks**

05 Define the term 'economic growth' (**Extract F**, line 4) *(5 marks)*

For an acceptable definition e.g.

- (i) The annual percentage change/increase in the productive capacity of the economy
- (ii) The annual percentage change/increase in the output of the economy
- (iii) The annual percentage change/increase in real GDP/GNP/national income
- (iv) The change/increase in output/real GDP/productive capacity of an economy

5 marks

NB Full marks should be awarded to a candidate who demonstrates a clear understanding of the term 'economic growth' even if the definition isn't exactly the same as the acceptable examples quoted above.

If the definition is incomplete, marks may be broken down, for example as follows:

the change/increase in GDP (real is not mentioned) **4 marks**

rightward shift in the LRAS curve or rightward shift in the PPC **2 marks**

shows the output/income/productive capacity of the economy (doesn't mention change or increase) **2 marks**

an increase in aggregate demand/spending **2 marks**

This mark scheme does not allow examiners to award 1 mark for a point. Examiners must award 0, 2 or 4 marks for each point made by the candidate.

MAXIMUM FOR 05 = 5 MARKS

- 06** Using **Extract D**, identify **two** points of comparison between the growth in real household consumption expenditure and the growth of real GDP between 1993 and 2006. (8 marks)

Award up to 4 marks for each valid point made (two marks for identification and up to two marks for supporting references to the data). The valid points include:

- The change in real household consumption expenditure fluctuates by more than changes in real GDP (e.g. consumption expenditure from just under 1.5% to around 4.7% whereas real GDP fluctuates from 1.8% to 4.3%)
- For most of the period the % change in real household consumption expenditure was above the % change in real GDP (e.g. a difference of 1.7% occurred in 1999)
- There were four years when the growth in real GDP was greater than % change in real household consumption expenditure (i.e. 1994-95 and 2005-06, the difference was greatest at around 1.5% in 1994)
- The two series are *generally* positively correlated, i.e. when the % change in real household consumption expenditure is increasing the growth in real GDP also increases and vice versa (e.g. as real GDP growth rises from 2.95% in 1995 to 3.8% in 2000 real consumption expenditure grows from 1.7% to 4.5%, **OR** as the growth in real GDP slows from 3.8% in 2000 to 1.8% in 2005 real consumption expenditure growth slows from 4.5% in 2000 to around 1.5% in 2005)
- The growth in both series was positive throughout the 14-year period (e.g. the lowest rate of increase in real GDP was +1.5% and lowest rate of increase in real household consumption expenditure was +1.9%)
- In 1993 (at the start of the period), the increase in real GDP was approximately 0.5% **below** the increase in real household consumption expenditure whereas in 2006 (at the end of the period) the increase in real GDP was approximately 0.9% **above** the increase in real household consumption expenditure. **OR** The growth in real GDP was lower in 1993 than in 2006 (2.2% compared to 2.8%) whereas the growth in real household consumption expenditure was higher in 1993 than 2006 (2.7% compared to 1.9%)
- The highest rate of growth of real household consumption expenditure was in 1999 (4.7%) whereas the highest rate of growth in real GDP was in 1994 (4.3%)
- The lowest rate of growth of both series was in 2005 (1.9% for real GDP and 1.6% for real household consumption expenditure)

A maximum of **2 marks** may be awarded for each point of comparison if the candidate confuses the levels of GDP and consumption with rates of growth of GDP and consumption.

Award only **1 mark** for each supporting reference to the data if the % sign is missing.

Up to 4 marks may be awarded if there is no use of statistics to support the points made or if a candidate simply trawls through the data without attempting a comparison.

Up to 6 marks may be awarded where there is evidence of an overview being taken, even though parts of the answer give the impression of a trawl through the data.

Where a candidate has included more than two points, award marks to the best two points.

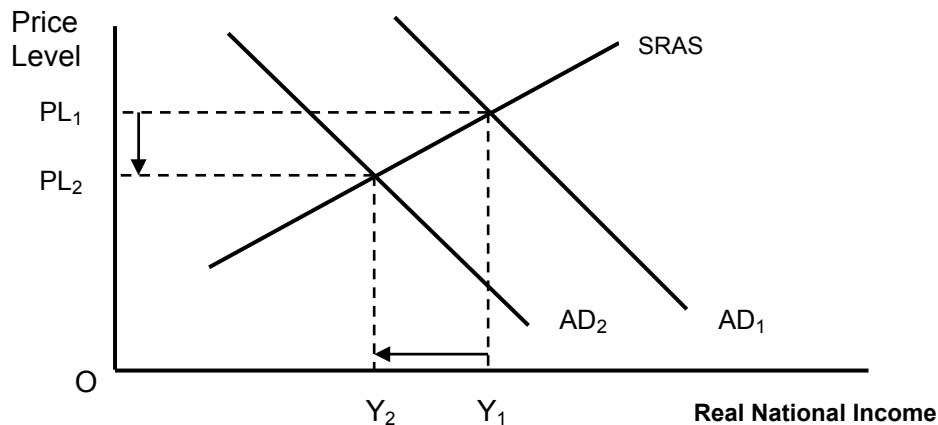
MAXIMUM FOR 06 = 8 MARKS

07 Extract E (line 3) states that 'future growth is likely to be affected by tighter availability of credit'.

Using an AD/AS diagram to help you, explain the likely effect of 'tighter availability of credit' upon output **and** employment. (12 marks)

When awarding marks for the diagram, it is important to reward candidates who produce a valid response even if it is not the one which is shown below.

The anticipated response for the diagram:



Break-down of the marks for the diagram:

Axes labelled (allow Inflation, PL and Real GDP or National Output or output or Y but do NOT allow Price and Quantity) **1 mark**

Original AD and AS curves correctly labelled **1 mark**

Leftward shift in the AD curve **2 marks**

Dotted lines and associated labelling showing the original equilibrium point (Y_1 PL_1) **1 mark**

Dotted lines and associated labelling showing the new equilibrium point (Y_2 PL_2) **1 mark**

Any other relevant feature of the diagram (e.g. the amount of excess supply at the original equilibrium) **1 mark per feature up to a maximum of 2 marks**

Reward leftward shift in AS only if there is a valid explanation for this in the written response

Up to 6 marks for the diagram

The anticipated written response:

For candidates who:

define output, employment, tighter availability of credit or any other relevant concept

Up to 2 marks per definition

Up to 2 marks for definitions

explain that if credit is tight it is likely to lead to a reduction in aggregate demand. The effect on the consumption of durable items and investment expenditure may be considered. Some candidates might also discuss the impact on the housing market, wealth and hence aggregate demand. **Up to 4 marks**

explain why 'tight credit' might lead to higher interest rates and go on to explain how higher interest rates might affect aggregate demand **Up to 4 marks**
Maximum of 4 marks for the effect on aggregate demand

explain the possible multiplier effects of a reduction in aggregate demand **Up to 4 marks**

explain why a fall in aggregate demand is likely to reduce output **Up to 4 marks**

explain the link between a fall in output and employment **Up to 4 marks**

explain how the relationship between output and employment is affected by rising productivity and/or other possible other influences, e.g. expectations about future levels of spending **Up to 4 marks**

use the diagram to explain the impact of the fall in AD on real national income/output, i.e. a simple statement such as 'In the diagram it can be seen that as aggregate demand falls from AD_1 to AD_2 , real national income, and hence output, decreases from Y_1 to Y_2 is enough for both marks. **2 marks**

Up to a MAXIMUM of 8 marks for the written explanation

Candidates who only explain the impact on output OR employment should be restricted to a maximum of 10 marks.

MAXIMUM FOR 07 = 12 MARKS

08 Extract F (line 2) states that the 'level of consumption is generally a good indicator of the strength of the economy'

Assess the view that rising consumer expenditure is always beneficial for an economy.
(25 marks)

It is anticipated that candidates will draw on ideas given in **Extracts E and F**, which identify some of the ways in which consumer expenditure may affect the performance of an economy.

Evaluation

Candidates will need to demonstrate that they are able to evaluate issues and arguments if they are to be awarded **more than 13 marks**.

Candidates who make a genuine attempt at evaluation should be well rewarded. *For this question, it is expected that candidates will discuss the impact of an increase in consumer expenditure on various aspects of economic performance. They are likely to conclude that some of these effects are favourable and others unfavourable. They might also conclude that the consequences of an increase in consumer spending depend on: the rate of increase in consumption, what is happening to the other components of aggregate demand, the current state of the economy (e.g. the output gap) and the supply-side performance of the economy. Candidates may also use the data provided and/or their knowledge of developments in the UK or other economies to support their conclusions.*

*Overall, they are likely to conclude that rising consumer spending is not always good for an economy and, although this is worth credit, they will need to support this conclusion by sound analysis and/or the use of evidence if they are to achieve **Level 4 or Level 5**.*

Issues and areas for discussion:

- an explanation of what is meant by consumer expenditure
- the impact of consumer expenditure on aggregate demand
- other components of aggregate demand
- indicators of macroeconomic performance, e.g. unemployment, inflation, growth and the balance of payments
- an analysis of the impact of rising consumer expenditure on employment and unemployment (they might refer back to part (c))
- an analysis of the impact of rising consumer expenditure on economic growth
- an analysis of the impact of rising consumer expenditure on inflation
- an analysis of the impact of rising consumer expenditure on the balance of payments
- the use of diagrams to support the above
- discussion of why the effects of a rise in consumer expenditure depend on what is happening to the other components of aggregate demand
- discussion of why the effects of a rise in consumer expenditure depend on the current state of the economy
- discussion of why the effects of a rise in consumer expenditure depend on the rate at which consumption is growing (particularly in relation to capacity)

- the significance of the supply-side performance of the economy, e.g. the flexibility of product and labour markets, productivity growth, factor mobility
- use of the data provided
- use of their own knowledge of developments in the UK and other economies
- an overall conclusion that attempts to assess whether or not rising consumer expenditure is always beneficial for an economy

The issues identified are intended to provide an indication of some of the points that might be discussed and candidates can only be expected to consider a few of these, or others of their choosing, in the time available.

Also give credit for:

- use of diagrams, e.g. AD/AS
- use of data plus reference to the UK and/or other economies
- an overview of issues raised; a final judgement that is probably contained in a concluding paragraph

USE THE LEVELS MARK SCHEME ON PAGES 4 AND 5

MAXIMUM FOR 08 = 25 MARKS

TOTAL FOR THIS QUESTION: 50 MARKS



General Certificate of Education
Advanced Subsidiary Examination
January 2009

Economics

ECON2

Unit 2 The National Economy

Friday 16 January 2009 9.00 am to 10.15 am

For this paper you must have:

- an objective test answer sheet
- a black ball-point pen
- an 8-page answer book.

You may use a calculator.

Time allowed

- 1 hour 15 minutes

Instructions

- In **Section A**, answer **all** questions on your objective test answer sheet.
- In **Section B**, answer **EITHER** Question 26 **OR** Question 27 in your answer book.
- Do all rough work in your answer book, **not** on your objective test answer sheet.

Section A

- Use a black ball-point pen. Do **not** use pencil.

Section B

- Use black ink or black ball-point pen. Pencil should only be used for drawing.
- Write the information required on the front of your answer book. The **Examining Body** for this paper is AQA. The **Paper Reference** is ECON2.

Information

- The maximum mark for this paper is 75.
- There are 25 marks for **Section A** and 50 marks for **Section B**.
- In **Section A**, each question carries 1 mark. No deductions will be made for wrong answers.
- In **Section B**, the marks for questions are shown in brackets.
- You will be marked on your ability to:
 - use good English
 - organise information clearly
 - use specialist vocabulary where appropriate.

Advice

- You are advised to spend no more than 25 minutes on **Section A** and at least 50 minutes on **Section B**.

SECTION A: OBJECTIVE TEST

Answer **all** questions in **Section A**.

Each question carries 1 mark. No deductions will be made for wrong answers.

You are advised to spend no more than 25 minutes on **Section A**.

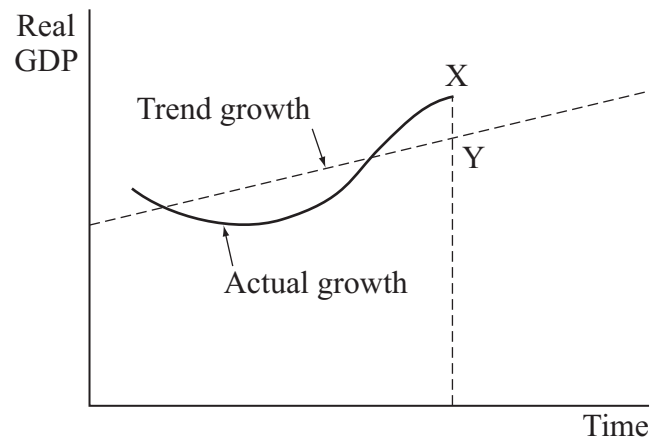
For each question there are four alternative responses, **A**, **B**, **C** and **D**. When you have selected the response which you think is the best answer to a question, mark this response on your objective test answer sheet. If you wish to change your answer to a question, follow the instructions on your objective test answer sheet.

- 1 Which one of the following statements about saving is correct?
 - A Saving is a component of aggregate demand.
 - B Saving can finance investment expenditure.
 - C In the short run, less household saving means less consumption.
 - D Increased saving increases demand-pull inflationary pressure.

- 2 An economy is currently operating inside its production possibility frontier. In the short run, if the rate of growth of aggregate demand is less than the rate of growth of productive capacity, then the economy is most likely to experience
 - A an increase in unemployment.
 - B a decrease in output.
 - C a decrease in its trend rate of growth.
 - D a decrease in imports.

- 3 As a component of aggregate demand, consumption is best defined as total expenditure in the economy
 - A on all goods and services including imports.
 - B on all goods and services minus expenditure on exports.
 - C by households on all goods and services.
 - D by households, government and firms plus expenditure on exports less expenditure on imports.

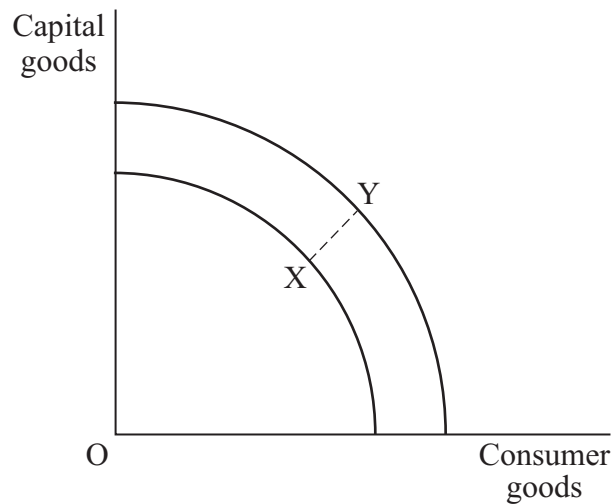
- 4 The diagram below shows the relationship between trend growth and actual growth for an economy.



The policy most appropriate to close the output gap XY by influencing aggregate demand would be

- A an increase in the rate of interest.
 - B a fall in the exchange rate of the currency.
 - C a cut in income tax rates.
 - D an increase in government spending.
- 5 Which one of the following is most likely to shift the short run aggregate supply curve to the right?
- A A fall in money wages
 - B A reduction in government spending
 - C A fall in the exchange rate
 - D A decrease in the productivity of labour
- 6 'The multiplier' usually refers to the effect of a change in the level of
- A aggregate demand upon imports.
 - B national income upon aggregate demand.
 - C saving upon investment.
 - D investment upon national income.

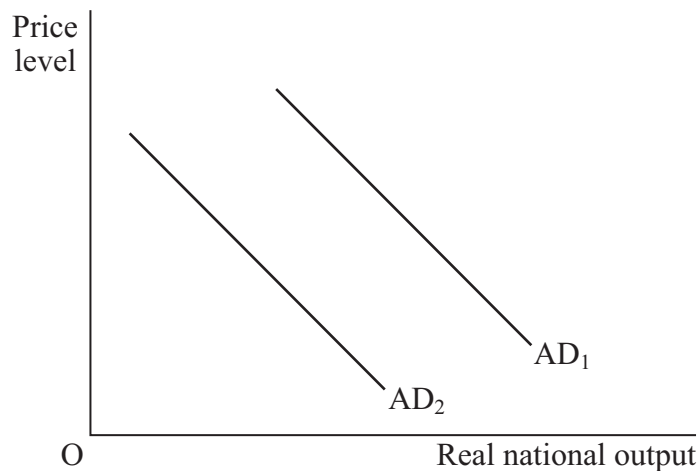
- 7 The diagram below shows two production possibility frontiers for an economy.



The movement of the economy from position X to position Y must indicate that there has been

- A a reduction in the level of unemployment.
 - B an increase in the economy's output gap.
 - C a rightward shift in the economy's long run aggregate supply curve.
 - D an increase in income per head.
- 8 Expansionary monetary policy is most likely to
- A shift the long run aggregate supply curve to the left.
 - B result from a reduction in taxation.
 - C cause a surplus on the current account of the balance of payments.
 - D shift the aggregate demand curve to the right.

- 9 The diagram below shows two aggregate demand curves for an economy.



The shift from AD_1 to AD_2 could be explained by an increase in

- A imports.
 - B the price level.
 - C costs of production.
 - D investment.
- 10 All other things being equal, an economy is most likely to experience inflation if
- A aggregate supply increases at a faster rate than aggregate demand.
 - B the country runs a balance of trade deficit at full employment.
 - C aggregate demand is increased when the economy is on its production possibility frontier.
 - D the government runs a budget deficit when long run aggregate supply increases.
- 11 A rise in the level of domestic investment will most likely result from a rise in
- A the current account deficit.
 - B interest rates.
 - C company profits.
 - D the exchange rate.

12 A sustained rise in the exchange rate is most likely to increase

- A** inflation.
- B** unemployment.
- C** economic growth.
- D** international competitiveness.

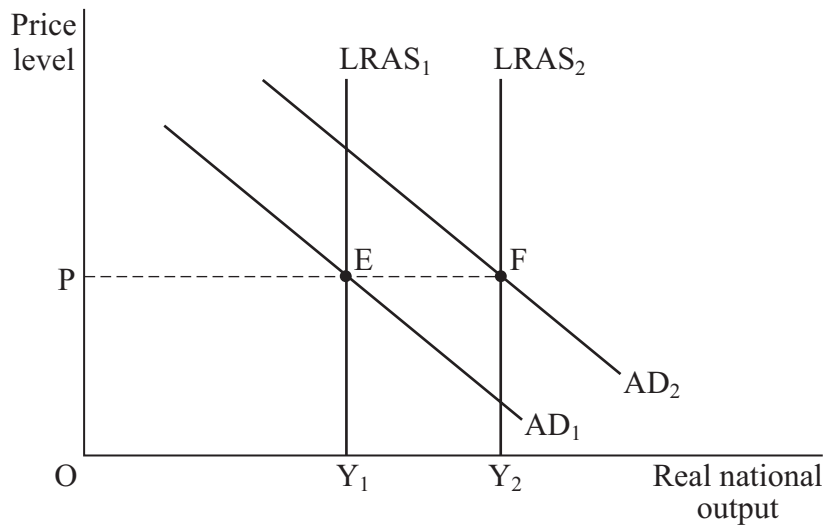
13 The table below shows the change in the Consumer Prices Index for a country between 2007 and 2008.

Year	Consumer Prices Index
2007	200
2008	210

The figures indicate that, approximately, between 2007 and 2008

- A** the purchasing power of money fell by 5%.
 - B** the rate of inflation was 10%.
 - C** the price of consumer goods increased by 10%.
 - D** the standard of living increased by 5%.
- 14** Which one of the following is most likely to be an example of a contractionary fiscal policy designed to reduce inflationary pressures?
- A** A reduction in the exchange rate
 - B** A reduction in the supply of money available to banks for lending purposes
 - C** Higher interest rates
 - D** An increase in the government budget surplus

- 15** The diagram below shows an aggregate demand/aggregate supply diagram for an economy. The economy is initially in equilibrium at E.



Which one of the following combinations of government policy is most likely to have brought about the change in equilibrium from E to F?

An increase in

- A** interest rates and unemployment benefits
 - B** government spending on transport infrastructure and vocational retraining programmes
 - C** the exchange rate and the money supply
 - D** measures to encourage emigration and greater saving
- 16** ‘The UK steel industry pays for its imported inputs in US dollars and sells its output abroad in euros.’

It follows from the above that the UK steel industry will benefit most when the pound is

- A** strong against the US dollar, weak against the euro.
- B** weak against the US dollar, weak against the euro.
- C** weak against the US dollar, strong against the euro.
- D** strong against the US dollar, strong against the euro.

Turn over ►

- 17** 'Economists predict that the negative output gap in the United Kingdom is likely to grow over the next couple of years.'

In the short run, which one of the following policies is most likely to help to prevent this negative output gap increasing?

- A** The Monetary Policy Committee (MPC) raising interest rates
- B** The government taking action to increase the exchange rate of the pound
- C** An increase in government expenditure accompanied by a growing budget deficit
- D** The implementation of supply-side policies that are designed to raise labour productivity

- 18** Which one of the following, **A**, **B**, **C** or **D**, represents the most likely outcome of cuts in interest rates for an economy, all other things being equal?

	Household saving	Household borrowing	The exchange rate of a currency
A	Fall	Fall	Fall
B	Rise	Rise	Rise
C	Rise	Fall	Rise
D	Fall	Rise	Fall

- 19** Structural unemployment is most likely to be caused by

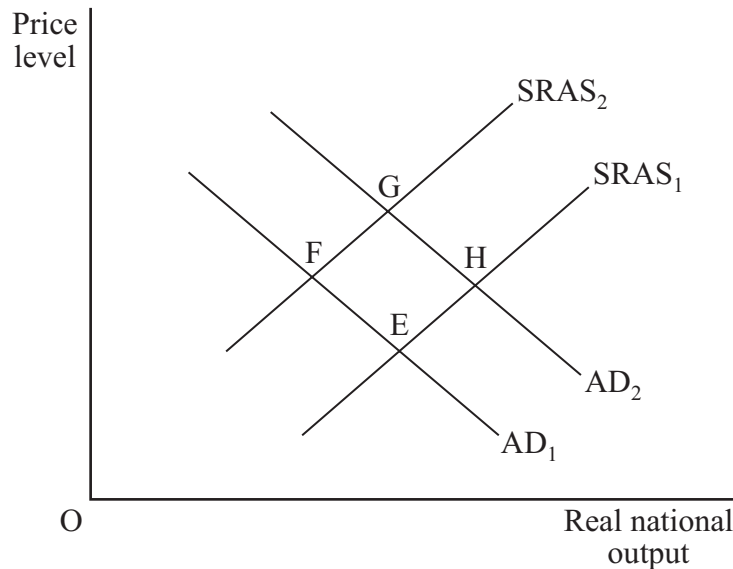
- A** a recession in the economy.
- B** changes in the demand for labour at different times of the year.
- C** an increase in the number of people changing jobs.
- D** the skills of the unemployed not matching those required for the available jobs.

- 20** All other things being equal, which one of the following is most likely to increase an economy's underlying trend rate of growth?

A rise in the rate of growth of

- A** inflation
- B** household income
- C** imports of consumer goods
- D** labour productivity

- 21 The diagram below shows the aggregate demand (AD) and short run aggregate supply (SRAS) curves for the UK economy, with the initial equilibrium at the intersection of AD_1 and $SRAS_1$ at point E.



The country experiences a 10% increase in oil prices and at the same time exports increase by 10%. As a result of these two events, equilibrium will

- A remain at point E.
 - B move to point F.
 - C move to point G.
 - D move to point H.
- 22 In recent years, the UK has experienced large deficits on the balance of payments on current account. Which one of the following would be **least** likely to reduce such deficits?
- A A rise in aggregate supply
 - B A rise in the exchange rate
 - C A rise in income tax rates
 - D A rise in productivity
- 23 Which one of the following statements relating to monetary policy is correct?
- A A cut in interest rates always increases inflation.
 - B While reducing excess demand, an interest rate rise may increase cost-push inflation.
 - C Interest rate changes have no effect on aggregate supply.
 - D An increase in interest rates will raise the level of investment.

- 24** The table below shows the value of a country's currency against other currencies, in index number form.

Year	Exchange rate index, 2006 = 100
2005	97
2006	100
2007	104
2008	107

All other things being equal, the most likely consequence of the changes in the exchange rate index shown in the table is that

- A** inflationary pressures eased.
 - B** the price of imports increased.
 - C** the balance of payments on current account improved.
 - D** there was a growth in employment in the manufacturing industry.
- 25** When there is full employment, an advantage of supply-side policies is that they
- A** immediately benefit the poor.
 - B** achieve control over the money supply.
 - C** increase the budget deficit.
 - D** can bring about an increase in output without adding to inflation.

**QUESTION 25 IS THE LAST
QUESTION IN SECTION A**

**On your answer sheet
ignore rows 26 to 50**

TURN TO PAGE 12 FOR SECTION B

There are no questions printed on this page

Turn over for the next question

Turn over ►

SECTION B: DATA RESPONSE

Answer **EITHER** Question 26 **OR** Question 27.
You are advised to spend at least 50 minutes on **Section B**.

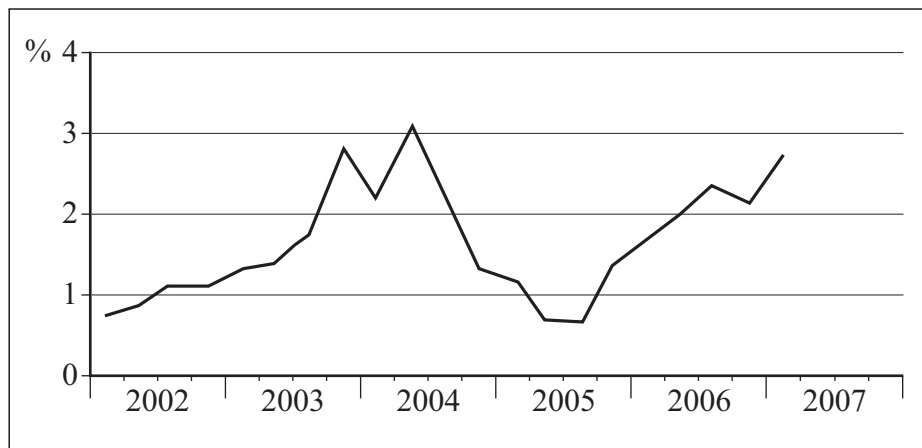
EITHER

Total for this question: 50 marks

26 PRODUCTIVITY

Study **Extracts A, B and C**, and then answer **all** parts of Question 26 which follows.

Extract A: The rate of growth of UK labour productivity, annual % change, 2002–2007



Source: adapted from www.statistics.gov.uk, accessed on 29 August 2007

Extract B: Productivity and the performance of the UK economy

Economists, when using the term ‘productivity’, are usually referring to labour productivity. For the UK, the so-called productivity gap continues to cause concern. This is the difference between UK productivity and that of similar economies. In the recent past, UK productivity has been disappointing when compared to some of our major trading partners such as France, Germany and the US.

1

5

International studies provide explanations for differences in labour productivity. Skills and investment levels are regarded as of vital importance. The UK may need higher-quality labour to be applied to more efficient machinery to bring improvements in productivity performance. In the US, it is felt that less job security than in the UK might be a factor. Labour may work harder to impress employers, and so avoid redundancy. The application of new technology is also important.

10

The UK Government views productivity growth as a key policy objective and points to competition, enterprise and innovation as important causes of improved productivity.

Source: news reports, 2008

Extract C: We must have higher productivity in the UK economy

Labour productivity is an important issue when considering UK macroeconomic performance. There is a greater likelihood that any rise in aggregate demand (AD) will be non-inflationary when improvements in productivity are able to generate greater output. This means that economic growth can be sustained over the long term, as can job creation. It must also be borne in mind that the improved competitiveness which higher productivity may bring will, in turn, help to bring the necessary improvements to the balance of payments on current account.	1 5
 Of course, benefits are likely to be even greater if higher productivity is accompanied by other supply-side developments such as increased investment, research and development (R&D), and ‘welfare-to-work’ and tax reforms to encourage the unemployed back into work.	10

Source: news reports, 2008

Question 26

- 26** (a) Define the term ‘labour productivity’ (**Extract B**, lines 1-2). *(5 marks)*
- (b) Using **Extract A**, identify **two** main features of the annual rate of growth of UK labour productivity for the period 2002 to 2007. *(8 marks)*
- (c) **Extract B** (line 6) suggests that international studies ‘provide explanations for differences in labour productivity’.
- Explain **two** determinants of labour productivity. *(12 marks)*
- (d) Using the data and your economic knowledge, assess the importance of higher labour productivity in bringing about improvements to UK macroeconomic performance. *(25 marks)*

Turn over for the next question

Do **not** answer Question 27 if you have answered Question 26.

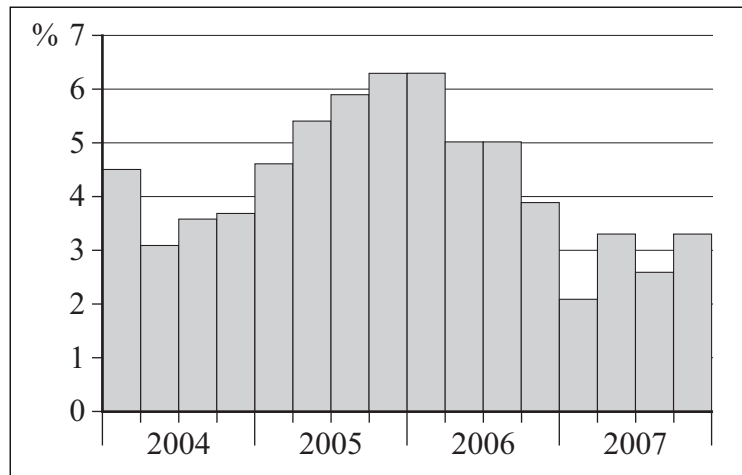
OR

Total for this question: 50 marks

27 HOUSEHOLD SAVINGS

Study **Extracts D, E and F**, and then answer **all** parts of Question 27 which follows.

Extract D: UK household savings ratio* (%), 2004–2007



* The household savings ratio is household savings expressed as a % of total disposable income (gross income less taxes but including welfare benefits).

Extract E: UK savings ratio tumbles to lowest level for 50 years

The data for 2007 have shown that the rate at which households are saving has plunged to the lowest level in almost half a century. 1

The fall indicates that, as a greater proportion of incomes is accounted for by taxation, higher mortgage payments and credit charges, some households are increasingly having to dig deeper into their savings to maintain a given life-style. However, there will also be those households which may be encouraged to save more as interest rates rise and which have the ability to do so. Providing for old age may be another reason for households to save. 5

Economists warn that consumers are beginning to struggle as the tax burden rises at the fastest rate in nine years and disposable income grows at the slowest rate in a quarter of a century. Households are increasing their borrowing to finance the desired level of current consumption. It may be, however, that borrowing cannot be maintained as interest rates rise further to deal with a worsening inflation problem. 10

Source: adapted from the *Daily Telegraph*, 30 June 2007

Extract F: Does the savings ratio matter to the UK economy?

The issue of household savings has perhaps not always been given the importance it deserves when discussing influences on an economy's macroeconomic performance. First and foremost, it is more likely that economists will discuss factors such as the role of government in inducing growth through, for example, promotion of enterprise and innovation, or the rate of growth of aggregate demand (AD), or the rate of growth of labour productivity.	1
However, the potential significance of household savings for UK macroeconomic performance needs to be recognised. Saving by households does, to some extent, provide the funds which financial institutions, such as banks, lend to businesses to finance investment, a prime mover in economic growth. Decisions to save from a given income will also help determine household consumption, a major component of AD. In turn, changes in household consumption may have consequences for the rate of inflation, jobs and the balance of payments on current account.	10

Source: news reports, 2008

Question 27

- 27 (a) Define the term ‘savings’ (**Extract E**, line 5). (5 marks)
- (b) Using **Extract D**, identify **two** main features of the UK household savings ratio for the period 2004 to 2007. (8 marks)
- (c) **Extract E** (lines 1-2) states that ‘the rate at which households are saving has plunged to the lowest level in almost half a century’.
- Explain **two** determinants of saving by households. (12 marks)
- (d) **Extract F** (lines 7-8) argues that ‘the potential significance of household savings for UK macroeconomic performance needs to be recognised’.
- Using the data and your economic knowledge, evaluate the significance of household savings for UK macroeconomic performance. (25 marks)

END OF QUESTIONS

There are no questions printed on this page

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General Certificate of Education

Economics 1141

ECON2: The National Economy

Mark Scheme

2009 examination - January series

Mark schemes are prepared by the Principal Examiner and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation meeting attended by all examiners and is the scheme which was used by them in this examination. The standardisation meeting ensures that the mark scheme covers the candidates' responses to questions and that every examiner understands and applies it in the same correct way. As preparation for the standardisation meeting each examiner analyses a number of candidates' scripts: alternative answers not already covered by the mark scheme are discussed at the meeting and legislated for. If, after this meeting, examiners encounter unusual answers which have not been discussed at the meeting they are required to refer these to the Principal Examiner.

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of candidates' reactions to a particular paper. Assumptions about future mark schemes on the basis of one year's document should be avoided; whilst the guiding principles of assessment remain constant, details will change, depending on the content of a particular examination paper.

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Advance Subsidiary Economics Unit 2**Section A: Objective Test****January 2009**

The following list indicates the correct answers used in marking the candidates' responses.

KEY LIST

1. B	9. A	17. C	25. D
2. A	10. C	18. D	
3. C	11. C	19. D	
4. A	12. B	20. D	
5. A	13. A	21. C	
6. D	14. D	22. B	
7. C	15. B	23. B	
8. D	16. A	24. A	

Advanced Subsidiary Economics Unit 2

Section B: Data Response

January 2009

General Instructions

Marks awarded to candidates should be in accordance with the following mark scheme and examiners should be prepared to use the full range of marks available. The mark scheme for most questions is flexible, permitting the candidate to score full marks in a variety of ways. Where the candidate's response to a question is such that the mark scheme permits full marks to be awarded, full marks **MUST** be given. A perfect answer is not necessarily required for full marks. But conversely, if the candidate's answer does not deserve credit, then no marks should be given.

Occasionally, a candidate may respond to a question in a reasonable way, but the answer may not have been anticipated when the mark scheme was devised. In this situation, **OR WHENEVER YOU HAVE ANY DOUBT ABOUT THE INTERPRETATION OF THE MARK SCHEME**, you must in the first instance telephone your team leader to discuss how to proceed.

Two approaches have been used in the construction of the mark scheme.

- (i) **An issue based approach.** The mark scheme for parts (a), (b) and (c) of the data response questions adopts this approach. The mark scheme lists the marks that can be awarded for particular issues (and associated development) that the candidate might include in the answer.
- (ii) **A levels approach.** This approach is used for marking part (d) of the data response questions. The Levels Mark Scheme on the next page identifies five levels representing differences in the quality of work. A range of marks is allocated to each level. First decide the level into which an answer falls. The level chosen should be the one which **best fits** the answer provided by the candidate. It is **not** intended that the answer should satisfy every statement in the level description. Then think in terms of awarding the mid-point mark which has been identified for that level (e.g. 14 marks for Level 3). Move up or down from this notional mark by considering the extent to which the answer meets the level description overall. Strength in one skill can outweigh weakness in another. When using the Levels Mark Scheme the marker **must** identify where a particular skill is being demonstrated. The **key** to be used to identify the skill is given after the level descriptions. The question-specific mark scheme summarises the information which could be used to answer the question, but without attaching marks to particular issues.

THE LEVELS MARK SCHEME FOR AS

Level Descriptions

In part (d) of the data response questions, approximately half the marks are available to award to candidates who demonstrate that they can evaluate economic arguments and evidence, and make informed judgements. An answer showing no evidence of evaluation, however good the analysis, should be awarded a maximum of 13 marks (in Level 3). The quality of evaluation should be the sole distinction between a Level 4 and Level 5 answer. It is not necessary for the answer to identify a wide range of issues to score the top mark. As indicated below, the **Quality of Written Communication** used should be taken into account when awarding marks.

Level 1: A very weak answer

Few, if any, relevant issues are recognised. Economic concepts and principles are not adequately understood or applied to the question. No satisfactory analysis or evaluation. There might be some evidence of organisation in the answer but generally it fails to answer the question. Descriptions and explanations lack clarity. Spelling, punctuation and grammar may be poor. There is little use of economic terminology.

0 to 6 marks

Mid-Point 4 marks

Level 2: A poor answer but some understanding is shown

One or more relevant issues are recognised. An attempt is made to use basic economic concepts to answer the question but the candidate's explanation may become confused and analysis will therefore be very limited. There may be some attempt to present alternative points of view but any attempt at evaluation is limited or superficial. There is some logic and coherence in the organisation of the answer. The candidate demonstrates some ability to spell commonly used words and to follow the standard conventions of punctuation and grammar. Some use of economic terminology is made but this is not always applied appropriately.

7 to 11 marks

Mid-Point 9 marks

Level 3: An adequate answer with some correct analysis but very limited evaluation

Two or more relevant issues are recognised. The candidate has made a reasonable attempt to apply economic concepts and ideas. A satisfactory understanding of some basic economic concepts and theories is demonstrated and there is some evidence that the candidate can analyse issues. There will be some attempt to present alternative points of view and to evaluate the issues, arguments and/or data. There is some logic and coherence in the organisation of the answer. The candidate is generally able to spell commonly used words and usually follows the standard conventions of punctuation and grammar. Some descriptions and explanations are easy to understand, but the answer may not be expressed clearly throughout. There is some evidence of the correct use of relevant economic terminology.

12 to 16 marks

Mid-Point 14 marks

Level 4: Good analysis but limited evaluation

Two or more relevant issues are identified. Good understanding of basic economic concepts and models is demonstrated. The candidate is able to apply these concepts and models to answer the question. Some appreciation of alternative points of view is shown. Satisfactory use is made of evidence and/or theoretical analysis to evaluate the issues/arguments/economic models identified and to support conclusions. Spelling is generally accurate and the standard conventions of punctuation and grammar are usually followed. The answer is well organised. Descriptions and explanations are clearly expressed. Appropriate use is made of relevant economic terminology.

17 to 21 marks

Mid-Point 19 marks

Level 5: Good analysis and evaluation

Two or more relevant issues are identified. Good understanding of basic economic concepts and models is demonstrated. The candidate is able to apply these concepts and models to answer the question. Clear understanding of alternative points of view is shown. Good use is made of evidence and/or theoretical analysis to evaluate the issues/arguments/economic models identified and to support conclusions. A clear final judgement is made. Spelling is generally accurate and the standard conventions of punctuation and grammar are usually followed. The answer is well organised. Descriptions and explanations are clearly expressed. Appropriate use is made of relevant economic terminology.

22 to 25 marks

Mid-Point 24 marks

THE KEY TO BE USED WHEN USING THE LEVELS MARK SCHEME

- D** Where a particular economic term is correctly **DEFINED** in order to help the candidate to answer the question properly.
- I** Where a relevant **ISSUE** is raised by the candidate.
- K** Where the candidate demonstrates **KNOWLEDGE** of recent developments or features of the economy which help enhance the candidate's response to the question. This should also be used where the candidate quotes relevant examples.
- Ap** Where the candidate demonstrates the ability to **APPLY** knowledge and **CRITICAL UNDERSTANDING** to problems and issues.
- A** Where the candidate demonstrates the ability to **ANALYSE** the problem using appropriate economic ideas.
- E** Where the candidate **EVALUATES** and makes judgements about the significance of various issues and arguments.

EITHER

26 PRODUCTIVITY

Total for this question: 50 marks

26 (a) Define the term 'labour productivity' (Extract B , lines 1-2). (5 marks)
--

For an acceptable definition (eg, output per worker per period of time, output per person employed, total output divided by the number of people employed) **5 marks**

NB Full marks should be awarded to a candidate who demonstrates a clear understanding of the term 'labour productivity' even if the definition is not exactly the same as the three acceptable examples quoted above)

If the definition is incomplete, marks may be broken down, for example as follows:

How much people can produce in a given amount of time **4 marks**

Output produced for every input used **3 marks**

A measure of output (or the amount produced) **2 marks**

A measure of efficiency **2 marks**

Candidates who confuse productivity with production can be awarded **up to 2 marks**.

This mark scheme does not allow examiners to award 1 mark for a point. Examiners must award either 0 or 2 for each point made by the candidate.

MAXIMUM FOR PART (a): 5 MARKS

26 (b) Using **Extract A**, identify **two** main features of the annual rate of growth of UK labour productivity for the period 2002 to 2007. **(8 marks)**

Award up to 4 marks for each valid point (two marks for identification and two marks for supporting reference(s) to the data). These include:

- the volatility of the data from late 2003 (ranging from a high of 3.1% to a low of around 0.5%)
- the highest rate of growth was in mid-2004 at over 3%
- the lowest rate of growth was about 0.5% in mid-2005
- for the period overall, the rate of growth of labour productivity rose from just under 1% in 2002, to almost 3% in the first quarter of 2007
- 2002 to the end of 2003 and mid-2005 to mid-2006 are periods of increases in the rate of growth of labour productivity, e.g. from under 1% of growth in 2002 to almost 3% rate of growth at the end of 2003
- mid-2004 to mid-2005 is the longest period of decline in the rate of growth of labour productivity from just over 3% to under 1% rate of growth
- the values are positive throughout the period
- the rate of growth of labour productivity gives the appearance of being cyclical and lies within the range of 0 and 3% of growth

Where a candidate quotes percentage figures, allow a margin of error of 0.2 percentage points either way in relation to the figures given above.

Where a candidate persistently confuses the rate of growth of labour productivity with the absolute level of labour productivity, e.g. labour productivity over the period increased from 1% to 3%, labour productivity award a **maximum of 4 marks**.

Up to 4 marks may be awarded if there is no use of statistics to support the points made or if candidates simply trawl through the data

Up to 6 marks may be awarded where there is evidence of an overview being taken, even though parts of the answer give the impression of a trawl through the data.

Where a candidate has included more than two points, award marks to the best two points.

MAXIMUM FOR PART (b): 8 MARKS

26 (c) Extract B (line 6) suggests that ‘international studies provide explanations for differences in labour productivity’.

Explain **two** determinants of labour productivity.

(12 marks)

For candidates who:

For relevant definitions, other than labour productivity

2 marks

explain determinants of labour productivity, e.g.

- investment in new machinery in a particular industry (2 marks), will usually mean fewer breakdowns (2 marks), allowing labour to feel more confident of having the expected production time and finding use of new equipment more rewarding (2 marks) and so being able to produce more per production period (2 marks)
- technological progress arising from R&D programmes
- pay incentives, e.g. bonuses for exceeding production targets, profit sharing
- moving resources from less productive to more productive uses
- a more enterprising business culture whether or not government inspired
- the rate of growth of employment when compared to the rate of growth of output
- improved working practices, e.g. multi-skilling, job satisfaction programmes
- the macroeconomic climate (as long as candidates explain the relevance of this to productivity, e.g. greater business confidence to invest in new equipment)
- investment in human capital

up to 8 marks (2 + 6) per reason explained.

Within the 8 marks, up to 4 marks (2 marks for curve/axes labelling, 2 marks for the information shown) for use of relevant diagrams accurately drawn.

It would be quite legitimate for candidates to write in terms either of factors bringing an increase or a decrease in productivity.

If candidates explain more than two determinants award marks to the best two explanations.

While reference to the data should be given due credit, candidates who do not go beyond simply copying from Extract B when explaining a determinant, should be awarded a maximum of **2 marks**.

MAXIMUM FOR PART (c): 12 MARKS

26 (d) Using the data and your economic knowledge, assess the importance of higher labour productivity in bringing about improvements to UK macroeconomic performance. **(25 marks)**

In this part of the question, candidates will need to demonstrate that they are able to evaluate issues and arguments to support a conclusion if they are to be awarded **more than 13 marks**.

Candidates who make a genuine attempt at evaluation should be well rewarded. *For this question they might comment on the extent of any improvement; what impact this might have on the productivity gap; that we cannot put too much weight on any one factor but must see productivity as part of a wider picture; the extent to which productivity improvements are cancelled out by a rising rate of inflation and/or an appreciating exchange rate; productivity improvements become meaningless if we cannot sell any extra output in world markets for whatever reason, eg recession or poor quality.*

A maximum of **21 marks** should be awarded if there is no **explicit** reference to the data.

Issues and areas for discussion:

- definition of macroeconomic performance
- components of the macroeconomy
- economic growth
- price level
- employment/unemployment
- the balance of payments on current account assuming improved productivity benefits unit costs
- labour productivity and how it might affect one or more of the above components
- the productivity gap
- the UK experience
- the significance of the rate of inflation
- the significance of exchange rate trends
- the significance of macroeconomic conditions in the UK's overseas markets
- the significance of the rate of growth of AD
- better productivity being unable to disguise the deindustrialisation that has taken place in the UK
- the importance of considering in which sectors of the economy the greatest improvements in productivity are taking place
- the extent of any improvement in labour productivity
- the dangers of isolating, and putting significant weight upon, just one factor such as labour productivity

The issues identified above are intended to provide an indication of some of the areas which might be discussed. Candidates can only be expected to consider a few of these issues in the time available.

Also give credit for:

- Use of diagrams
- Relevant use of the data
- Reference to the UK and/or other economies
- Real world examples

USE THE LEVELS MARK SCHEME ON PAGES 5 AND 6

MAXIMUM FOR PART (d): 25 MARKS

TOTAL FOR THIS QUESTION: 50 MARKS

OR

27 HOUSEHOLD SAVINGS

Total for this question: 50 marks

27 (a) Define the term 'savings' (**Extract F**, line 1).

(5 marks)

For an acceptable definition (eg Income minus consumption ($S = Y - C$), the portion of income that is not spent, the portion of income that is not passed on around the circular flow of income) **5 marks**

Another acceptable definition is the amount of money held by households in financial institutions such as bank, i.e savings as a stock

NB Full marks should be awarded to a candidate who demonstrates a clear understanding of the term 'savings' even if the definition is not exactly the same as the acceptable examples quoted above)

If the definition is incomplete, marks may be broken down, for example as follows:

For stating that savings is a withdrawal from the circular flow of income **2 marks**

For stating one or more examples of savings **2 marks**

Acceptable examples of savings include:

- funds deposited in a bank account
- funds deposited in a building society account
- purchase of shares
- purchase of government securities
- funds put into a pension scheme
- funds put into a life assurance policy

Reward any other reasonable examples but do not reward the purchase of real assets such as property, antiques, vehicles and consumer durables.

This mark scheme does not allow examiners to award 1 mark for a point. Examiners must award either 0 or 2 marks for each point made by the candidate.

MAXIMUM FOR PART (a): 5 MARKS

27 (b) Using **Extract D**, identify **two** main features of the UK household savings ratio for the period 2004 to 2007. **(8 marks)**

Award up to 4 marks for each valid point (two marks for identification and two marks for supporting reference(s) to the data). These include:

- the savings ratio fluctuates over the period with a range of values from 2.1% to 6.3%
- both 2004 and 2006 see an overall decline in the savings ratio, e.g. in 2004 from 4.5% to 3.7%
- 2005 is the only year to see a sustained increase in the savings ratio, from 4.6% to 6.3%
- for the period overall the values ranged from 4.5% to 3.2%
- Both 2005 and 2006 see the highest value for the savings ratio of the period (6.3%)
- 2007 sees the lowest value (2.1%)
- the values are positive throughout the period
- 2006 sees the biggest change in the ratio (from 6.3% to 3.9%) suggesting some volatility in the ratio, 2004 the smallest (3.1% to 4.5%)

Where a candidate quotes percentage figures, allow a margin of error of 0.2 percentage points either way in relation to the figures given above.

Where a candidate persistently confuses a rise/fall in the savings ratio with a rise/fall in household savings, award a **maximum of 4 marks**.

Up to 4 marks may be awarded if there is no use of statistics to support the points or if candidates simply trawl through the data.

Up to 6 marks may be awarded where there is evidence of an overview being taken, even though parts of the answer give the impression of a trawl through the data.

Where a candidate has included more than two points, award marks to the best two points.

MAXIMUM FOR PART (b): 8 MARKS

27 (c) Extract E (lines 1-2) states that ‘the rate at which households are saving has plunged to the lowest level in almost half a century’.

Explain **two** determinants of saving by households.

(12 marks)

For candidates who:

For relevant definitions, other than savings

2 marks

explain determinants of household saving, e.g.

- a rising rate of interest (2 marks) which creates a higher opportunity cost of consumption over savings (2 marks), in that more interest income can now be gained from saving (2 marks), as institutions such as banks and building societies follow any increase in bank rate set by the MPC (2 marks)

- family income within a household

- a rising rate of interest means higher monthly payments for those with variable-rate mortgages and less income to use at their discretion for consumption or saving

- a changing tax burden affecting disposable income and the ability to save

- changing expectations, e.g. the greater threat of redundancy causing people to increase savings

- the rate of inflation influencing the real value of savings and causing households to adjust their decisions over saving

- to finance future consumption, e.g. a new car or a house

- the attraction or otherwise of savings schemes offered by financial institutions or by government

- the attractiveness of pension schemes or, as in recent years, severe doubts about their track-record

up to 8 marks (2 + 6) per reason explained.

Within the 8 marks, up to 4 marks (2 marks for curve/axes labelling, 2 marks for the information shown) for use of relevant diagrams accurately drawn.

It would be quite legitimate for candidates to write in terms either of factors bringing an increase or a decrease in savings.

If candidates explain more than two determinants award marks to the best two explanations.

While reference to the data should be given due credit, candidates who do not go beyond simply copying from Extract E when explaining a determinant should be awarded a maximum of **2 marks**.

MAXIMUM FOR PART (c): 12 MARKS

27 (d) Extract F (lines 7-8) argues that ‘the potential significance of household savings for UK macroeconomic performance needs to be recognised’.

Using the data and your economic knowledge, evaluate the significance of household savings for UK macroeconomic performance. (25 marks)

In this part of the question, candidates will need to demonstrate that they are able to evaluate issues and arguments to support a conclusion if they are to be awarded **more than 13 marks**.

Candidates who make a genuine attempt at evaluation should be well rewarded. *For this question candidates might comment on the need to draw a distinction between the short run (changed savings decisions affecting AD) and the long run (changed savings decisions affecting the rate of growth given the impact on investment); domestic savings not having the significance they might once have had for investment because of much greater FDI; in practice, changes in household savings don't seem to have had a major impact on the UK's growth performance or it is difficult to isolate savings as a factor when considering changes in the macroeconomic performance of the UK.*

A maximum of **21 marks** should be awarded if there is no **explicit** reference to the data.

Issues and areas for discussion:

- the savings ratio
- the UK experience
- the division of household income into consumption and saving
- definition of macroeconomic performance
- components of macroeconomic performance
- economic growth
- prices
- employment/unemployment
- the balance of payments on current account
- how savings might affect the above components
- the need to draw a distinction between the short run (changed savings decisions affecting AD) and the long run (changed savings decisions affecting the rate of growth given the impact on investment)
- domestic savings not having the significance they might once have had for investment because of much greater inward investment from overseas
- in practice, changes in household savings don't seem to have had a major impact on the UK's growth performance or it is difficult to isolate savings as a factor when considering changes in the macroeconomic performance of the UK.

The issues identified above are intended to provide an indication of some of the areas which might be discussed. Candidates can only be expected to consider a few of these issues in the time available.

Also give credit for:

- Use of diagrams
- Relevant use of the data
- Reference to the UK and/or other economies
- Real world examples

USE THE LEVELS MARK SCHEME ON PAGES 5 AND 6

MAXIMUM FOR PART (d): 25 MARKS

TOTAL FOR THIS QUESTION: 50 MARKS