PEARSON EDEXCEL A-LEVEL ECONOMICS B · 9EB0

ECONOMICS



EXAM QUESTION PACK

4.4 MACROECONOMIC POLICIES AND IMPACT ON FIRMS AND INDIVIDUALS

SCORE	PERCENTAGE
/837	%

STEMUP

These questions belong to Pearson Edexcel, not to us.

The examination questions and mark schemes in this pack were written and published by Pearson Edexcel. They are past assessment materials, reproduced here so that students can revise from them.

What we do not own

STEMUP is not affiliated with Pearson Edexcel and does not own, and makes no claim to own, any of the question or mark scheme material in this pack. Pearson has not endorsed, approved or been involved in the production of it. Pearson, Edexcel and the qualification titles used here belong to their respective owners and appear for identification only.

Where to find the originals

Pearson publishes its past papers and mark schemes free of charge. Always check the current specification at qualifications.pearson.com before you revise, because content and wording can change between series.

If you hold the rights to any material in this pack and would like it amended or removed, contact admin@stemup.co.uk and we will act on it.

Questions

Q1.

Use the data to support your answers where relevant. You may annotate and include diagrams in your answers.

Answer the question with a cross in the box you think is correct ☒. If you change your mind about an answer, put a line through the box ☒ and then mark your new answer with a cross ☒.

A number of business groups have signed an open letter to the UK Government asking it to commit to delivering the full High Speed 2 rail link. This will connect London to the northern cities of Manchester and Leeds at a cost of £56 billion and reduce journey times by as much as 50%.

(Source adapted from: https://www.theguardian.com/uk-news/2019/jun/22/business-heads-urge-next-pm-to-commit-to-finishing-hs2)

(a) Explain **one** likely impact of this project on aggregate supply in the UK.

(4)

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

(b) Government spending on the High Speed 2 rail link is an example of which of the following?

(1)

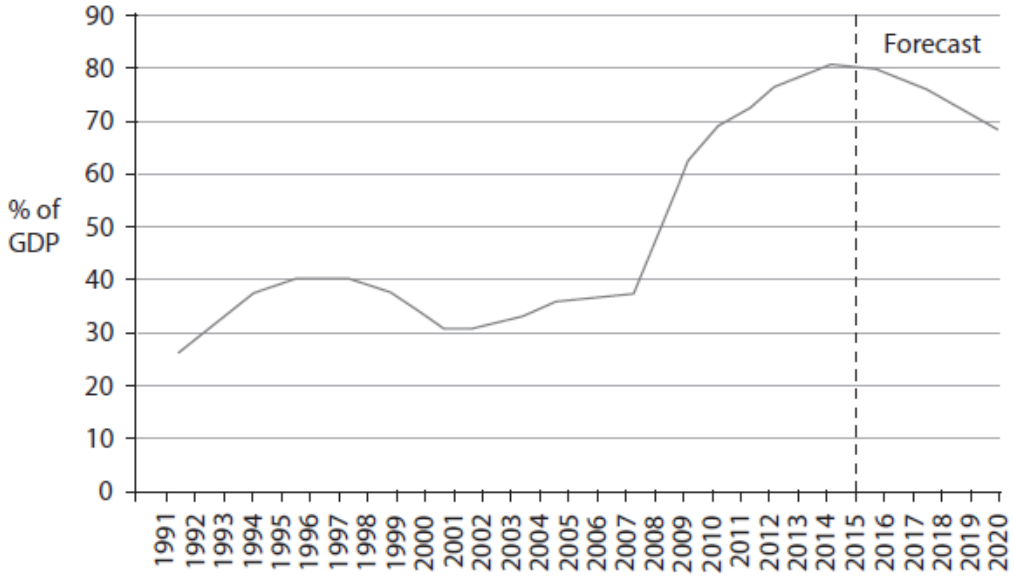
- ☒ **A** Automatic stabilisers
- ☒ **B** Capital expenditure
- ☒ **C** Current expenditure
- ☒ **D** Transfer payments

(Total for question = 5 marks)

Q2.

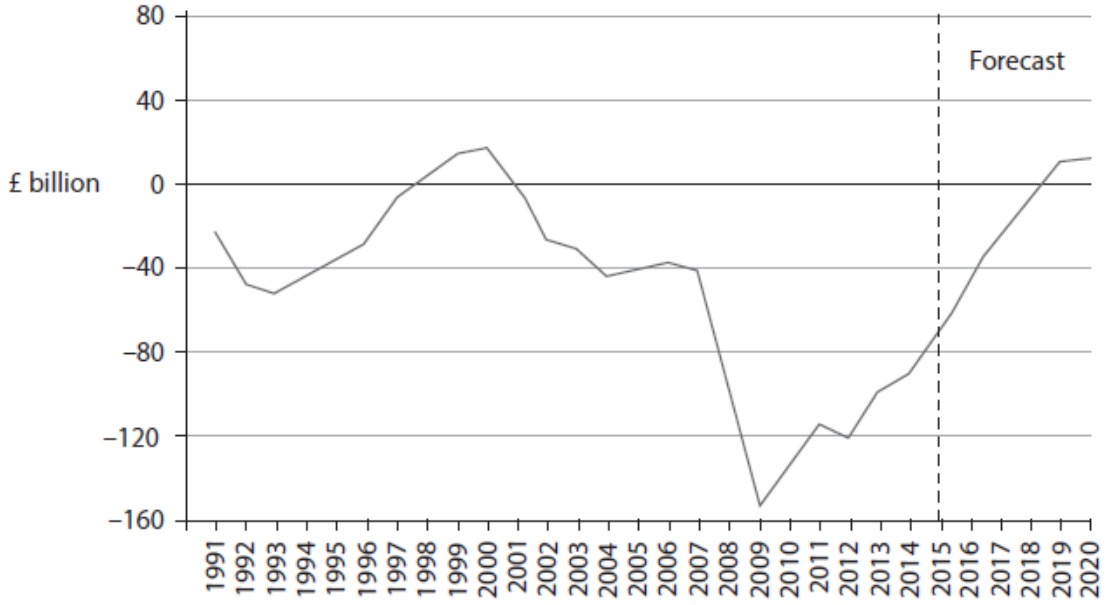
The UK economy

Figure 4: UK national debt as a percentage of GDP



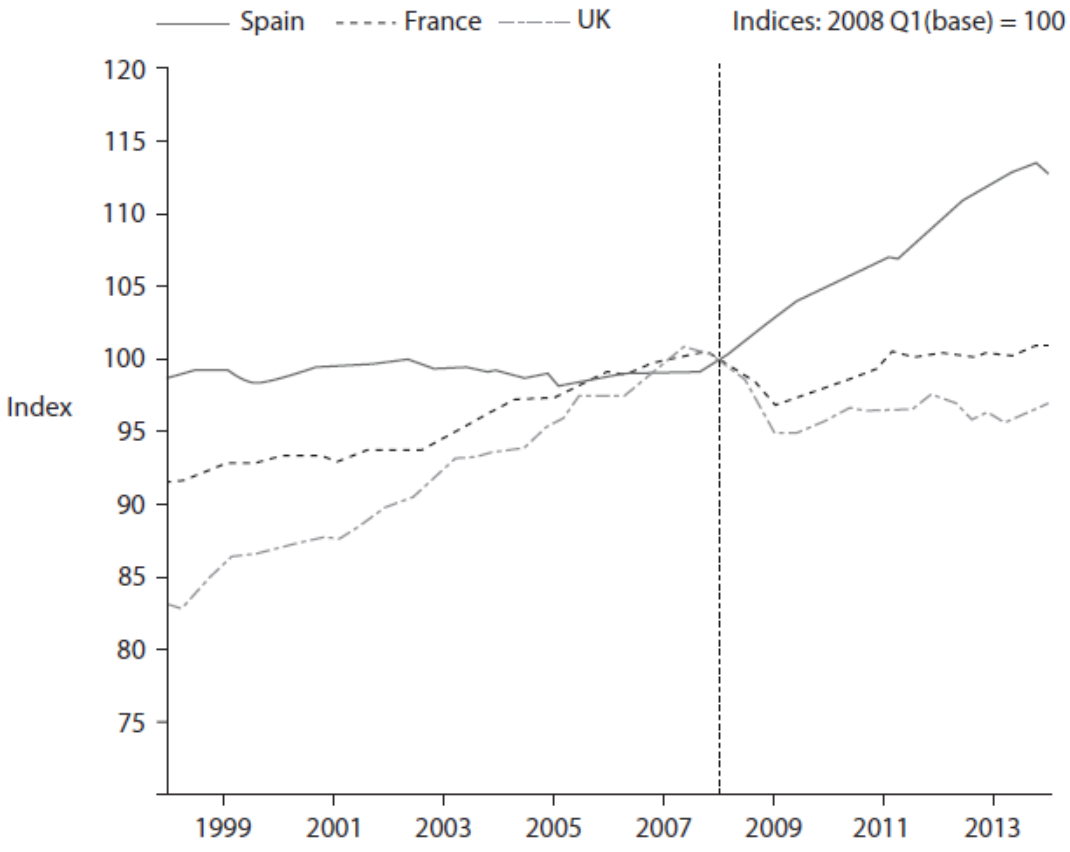
(Source: http://budgetresponsibility.org.uk/docs/dlm_uploads/BriefGuide_020511.pdf)

Figure 5: UK fiscal deficit, public sector net borrowing (PSNB)



(Source: http://budgetresponsibility.org.uk/docs/dlm_uploads/BriefGuide_020511.pdf)

Figure 6: Labour productivity per head, selected countries



(Source: http://www.bankofengland.co.uk/publications/Documents/quarterlybulletin/2014/qb14q201.pdf)

Extract C

The National Living Wage (NLW)

The Government has announced that from 2016 it will introduce a Living Wage Premium that will apply on top of the National Minimum Wage (NMW) for employees aged 25 and over to deliver a National Living Wage (NLW) for those people. The main NMW will continue to be set for all employees aged 21 and over, so that those aged 21 to 24 will continue to be subject only to that rate.

The effective minimum wage for the 25+ age group will therefore be over 13% higher in 2020 than would otherwise have been the case, and result in a 0.3% increase in wage costs overall. Further impacts on real GDP are estimated to be higher productivity (+0.3%) but lower average hours worked (-0.2%) and higher unemployment. Overall real GDP is forecast to fall by 0.1% as a result of the NLW. However these forecasts depend on estimates of the likely elasticity of demand for labour.

Academic evidence suggests that changes to the NMW since 1999 have led to only limited effects on demand for labour in the UK. The types of work that will be affected are relatively labour intensive, which may limit the scope for firms to substitute towards using capital. Firms may also be expected to shift demand in favour of the under-25s given that they will not be subject to the NLW, which all else being equal would lead to a smaller reduction in overall labour demand. Some of the reduction in employees could also be partially offset by a rise in self-employment. But increasing the NLW to a higher proportion of median earnings may lead to bigger effects than have been experienced in the past.

(Sources: adapted from http://cdn.budgetresponsibility.independent.gov.uk/July-2015-EFO-234224.pdf and http://budgetresponsibility.independent.gov.uk/)

Extract D

The productivity puzzle in the UK

Since the onset of the 2007–2008 financial crisis, labour productivity growth in the UK has been exceptionally weak. Despite some modest improvements in 2013, whole-economy output per hour remains around 16% below the level implied by its pre-crisis trend. Even taking into account possible measurement issues and changes in the size of the service sector, this shortfall is large and is often referred to as the 'productivity puzzle'.

Measures of productivity can be used to inform estimates of an economy's ability to grow without generating excessive inflationary pressure, which makes understanding recent movements important for the conduct of monetary policy. During the initial phases of the recession, companies appear to have acted flexibly by holding on to labour and lowering levels of capacity utilisation in response to weak demand conditions. But the protracted weakness in productivity and the strength in employment growth over the past two years suggest that other factors are likely to be having a more persistent impact on the level of productivity. These factors are reduced investment in both physical and intangible capital, such as innovation and training, and failings in the labour market such as immobility of labour and under-employment of skilled workers. Some economists explain this by using the concept of an output gap.

(Source: adapted from http://www.bankofengland.co.uk/publications/Documents/quarterlybulletin/2014/qb14q201.pdf)

(a) With reference to Extract D (line 18), explain the meaning of the term 'output gap'. Use an aggregate demand and aggregate supply diagram in your answer.

(5)

(b) With reference to Figures 4 and 5 and your own knowledge, examine the relationship between the national debt as a proportion of GDP and the fiscal deficit.

(8)

(c) Discuss the likely impact of the National Living Wage on the profitability of firms. Use a cost and revenue diagram in your answer.

(12)

EITHER

(d) With reference to the information provided and your own knowledge, evaluate the likely microeconomic and macroeconomic influences on the UK's international competitiveness.

(25)

OR

(e) With reference to the information provided and your own knowledge, evaluate the microeconomic and macroeconomic effects of a government policy of cutting public expenditure rather than raising taxes as a means of reducing a fiscal deficit.

(25)

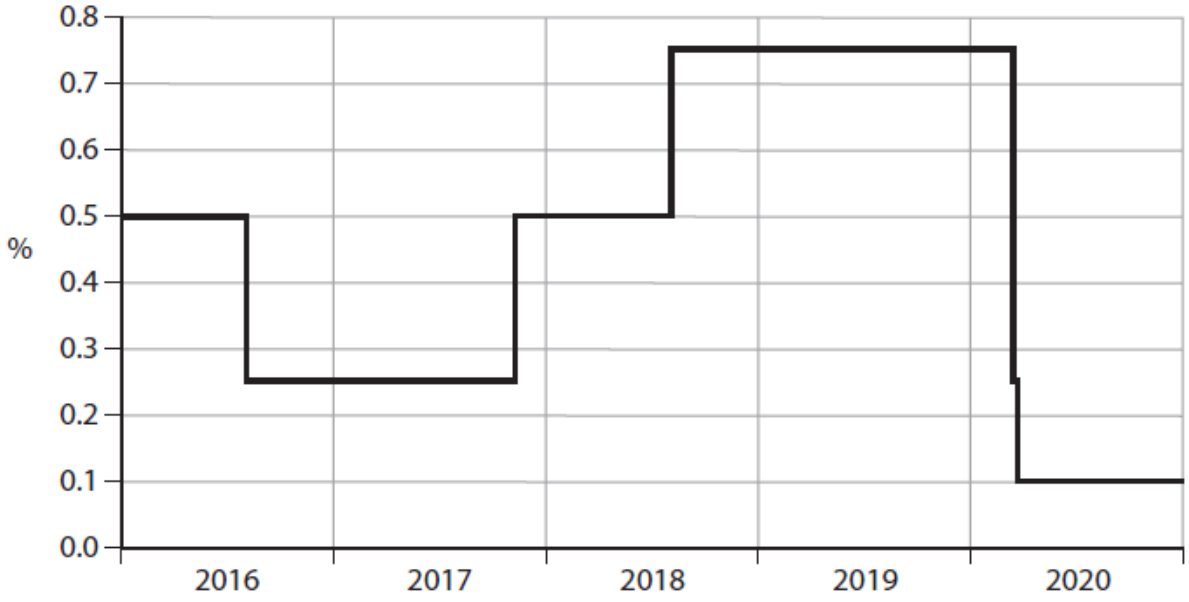
(Total for question = 50 marks)

Q3.

Some questions must be answered with a cross in a box (☒). If you change your mind about an answer, put a line through the box (☒) and then mark your new answer with a cross (☒).

Use the data to support your answers where relevant. You may annotate and include diagrams in your answers.

Bank of England base interest rate, 2016–2020



(Source: adapted from https://www.bankofengland.co.uk/monetary-policy/the-interest-rate-bank-rate)

(a) With reference to the chart above, explain the likely impact of a reduction in the base interest rate on UK investment.

(4)

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

(b) Which **one** of the following would be most likely to result from lower base interest rates?

A fall in:

(1)

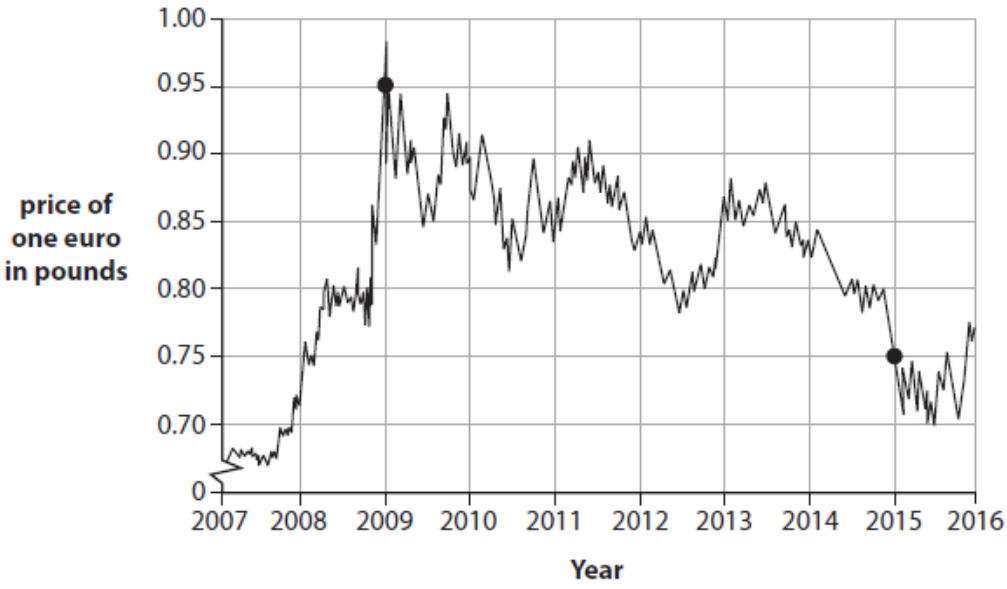
- ☒ **A** the average price of houses
- ☒ **B** the external value of the pound
- ☒ **C** the level of employment
- ☒ **D** the rate of economic growth

(Total for question = 5 marks)

Q4.

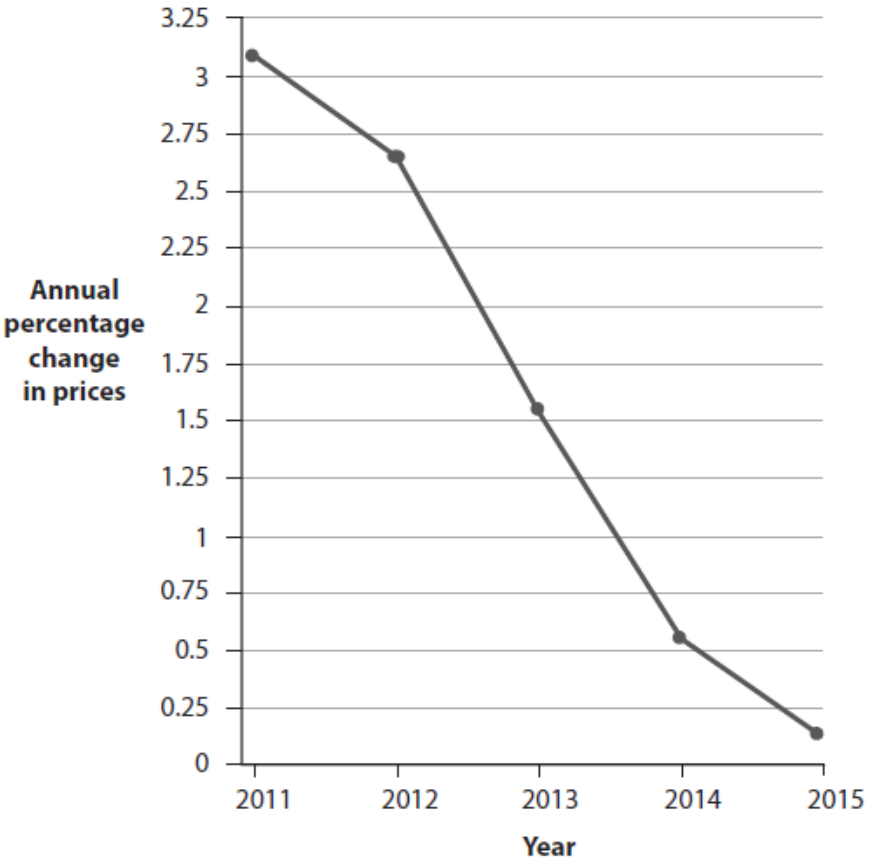
The Eurozone economy

Figure 1: Exchange rate of the euro (€) to the British pound (£)



(Source: https://www.ecb.europa.eu/stats/exchange/eurofxref/html/eurofxref-graph-gbp.en.html#)

Figure 2: Eurozone inflation rate as measured by the Consumer Prices Index (CPI)



(Source: adapted from http://www.imf.org/external/pubs/ft/weo/2015/02/weodata/download.aspx)

Extract A

European Central Bank disappoints markets with weaker than expected stimulus

Mario Draghi, president of the European Central Bank (ECB), surprised financial markets in November 2015 with a less ambitious package of monetary stimulus than many had anticipated.

The ECB cut its base interest rate by 0.1% to minus 0.3% in order to encourage private banks to lend funds to companies and households rather than deposit them at the central bank. The central bank agreed to extend its €60 billion (£45 billion) monthly bond-buying quantitative easing (QE) programme for a further six months. The ECB's €1.1 trillion QE scheme had originally been due to end in September 2016.

"We are doing more because it works," Mr Draghi said. Yet the ECB did not increase the size of its monthly asset purchases and also disappointed those expecting that it would cut interest rates more aggressively.

The euro rose almost 3% against the dollar to $1.08 after the announcement. Italian and Spanish bond yields both jumped by 0.27% to 1.62% and 1.72% respectively.

The ECB's economists reduced their inflation forecasts for the next two years. They now predict consumer prices in the Eurozone rising by just 1% in 2016 and 1.6% in 2017 – still below the central bank's ceiling of 2%. In November 2015, the inflation rate was just 0.1% and core inflation, excluding volatile items such as fuel and food, dropped to 0.9%.

Mr Draghi stressed again that monetary policy alone could not restore the Eurozone to economic health. He called for looser fiscal policy among member states to support aggregate demand and more rapid implementation of supply-side reforms. "In order to reap the full benefits from our monetary policy measures, other policy areas must contribute decisively," he said.

(Source: http://www.independent.co.uk/news/business/news/ecb-disappoints-traders-with-weaker-than-expected-stimulus-a6759786.html, 4th December 2015)

(a) With reference to Figure 1, calculate the percentage change in the value of the euro in pounds from the start of 2009 to the start of 2015.

(5)

(b) With reference to the information provided and your own knowledge, examine **two** factors which might explain the change in the rate of Eurozone inflation as shown in Figure 2.

(8)

(c) Since mid-2015 the euro has appreciated. Assess the likely impact of an appreciation of the euro on the current account of the balance of payments for Eurozone countries.

(10)

(d) Discuss the likely success of the ECB's quantitative easing programme in moving Eurozone inflation closer to 'the central bank's ceiling of 2%' (Extract A, line 17).

(12)

(e) Discuss 'looser fiscal policy' and 'supply-side reforms' (Extract A, lines 20 and 21) that may be used by governments of Eurozone countries to increase economic growth.

(15)

(Total for question = 50 marks)

Q5.

The UK has experienced a budget deficit since 2001. The government aimed to reach a budget surplus by 2019, but in 2016 this target was abandoned.

(Source: adapted from https://www.gov.uk/government/news/autumnstatement- 2016-some-of-the-things-weve-announced)

(a) Explain **one** likely reason why the 2019 budget surplus target was abandoned.

(2)

.....

.....

.....

.....

.....

.....

.....

.....

.....

(b) Explain the likely impact of abandoning the budget surplus target on the UK national debt.

(2)

.....

.....

.....

.....

.....

.....

.....

.....

.....

(c) If a government takes decisions to target a budget surplus, this is an example of:

(1)

☒ **A** contractionary monetary policy

☒ **B** discretionary fiscal policy

☒ **C** expansionary fiscal policy

☒ **D** expansionary monetary policy

(Total for question = 5 marks)

Q6.

Use the data to support your answers where relevant. You may annotate and include diagrams in your answers.

In 2018, the United States Government cut the corporation tax rate (tax on company profits)

from 35% to 21%. Income tax rates for US citizens were also reduced: for example, the top rate of income tax was cut from 39.6% to 37%.

(Source adapted from: https://www.nytimes.com/)

Evaluate the likely impact of cutting tax rates as a policy to increase economic growth.

(Total for question = 25 marks)

Q7.

Use the data to support your answers where relevant. You may annotate and include diagrams in your answers.

The European Central Bank introduced a new round of quantitative easing (QE) in March 2020, purchasing up to €750 billion of assets. The objective of this QE was to reduce the serious risks to the effectiveness of monetary policy resulting from a significant recession. The European Central Bank's target for inflation remains at 'below but close to 2%'.

(Source adapted from: https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr200318_1~3949d6f266.en.html)

Evaluate the effectiveness of quantitative easing during 'a significant recession'.

(Total for question = 2 marks)

Q8.

Use the data to support your answers where relevant. You may annotate and include diagrams in your answers.

The UK Government is planning to cut the rate of corporation tax on all pre-tax profits of companies to 17% by 2020.

(Source: adapted from https://www.ft.com/content/ 7579f124-5742-11e7-9fed-c19e2700005f)

(a) This would be an example of:

(1)

☒ **A** a contractionary monetary policy

☒ **B** an exchange rate policy

☒ **C** an expansionary monetary policy

☒ **D** a supply-side policy

(b) If a company makes £500 000 pre-tax profit in 2020, calculate how much corporation tax it will pay. Assume that the government cuts the rate of corporation tax as planned.

(2)

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

(c) Explain **one** possible reason why the revenue from corporation tax could increase if the government cuts the rate of tax.

(2)

.....

.....

.....

.....

.....

.....

.....

.....

.....

(Total for question = 5 marks)

Q9.

The UK economy

Figure 3: GDP per hour worked, nominal values at PPPs, percentage above or below UK level, 2018

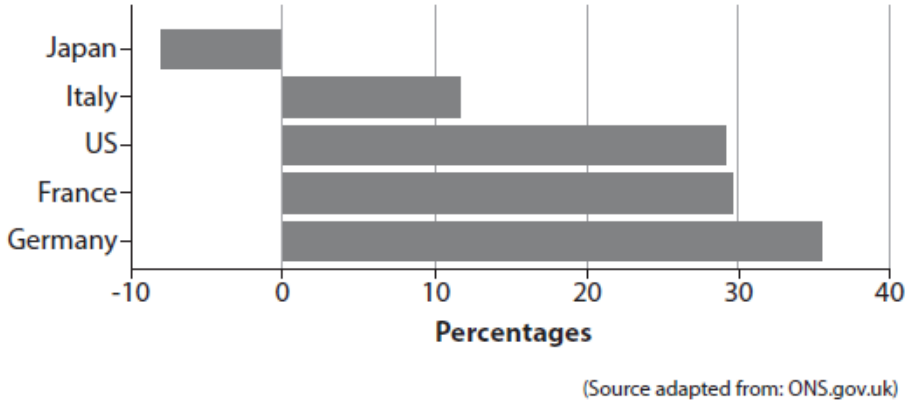
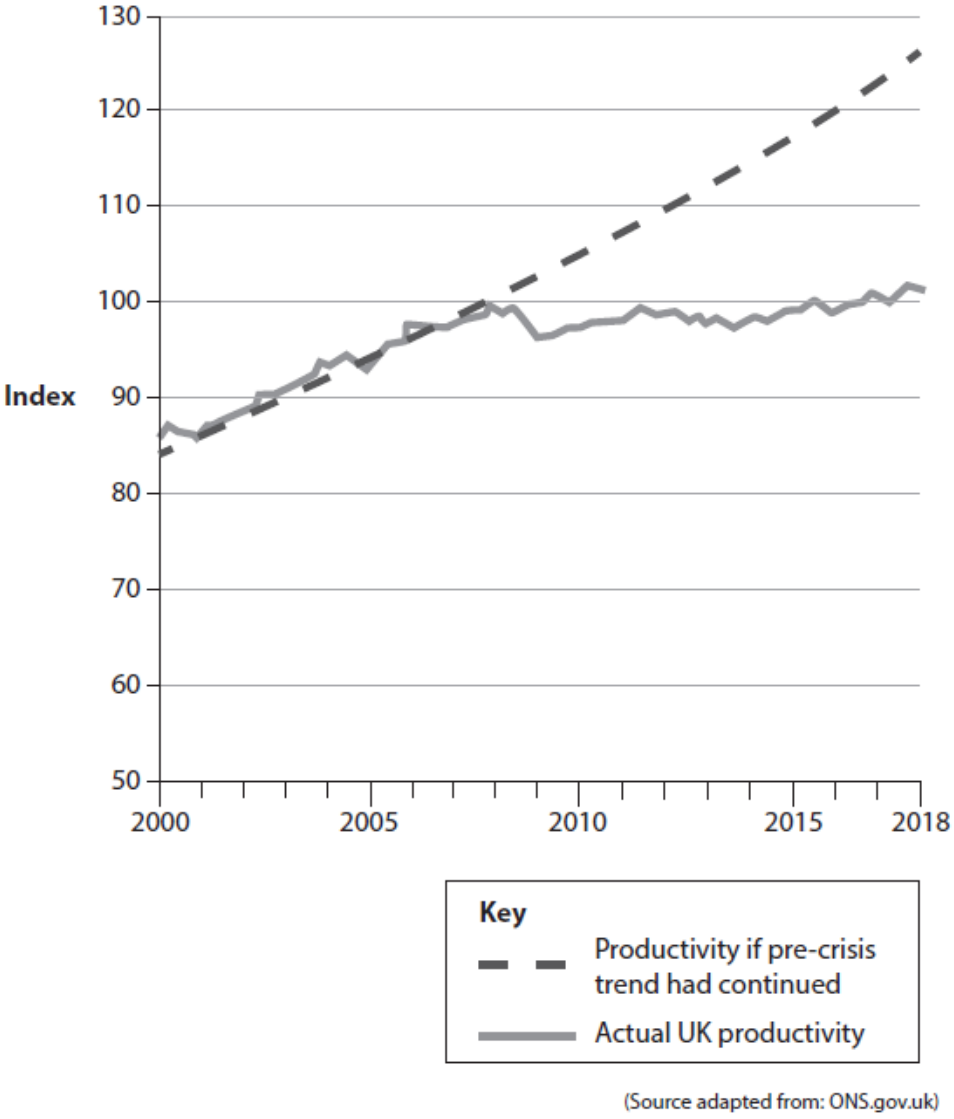
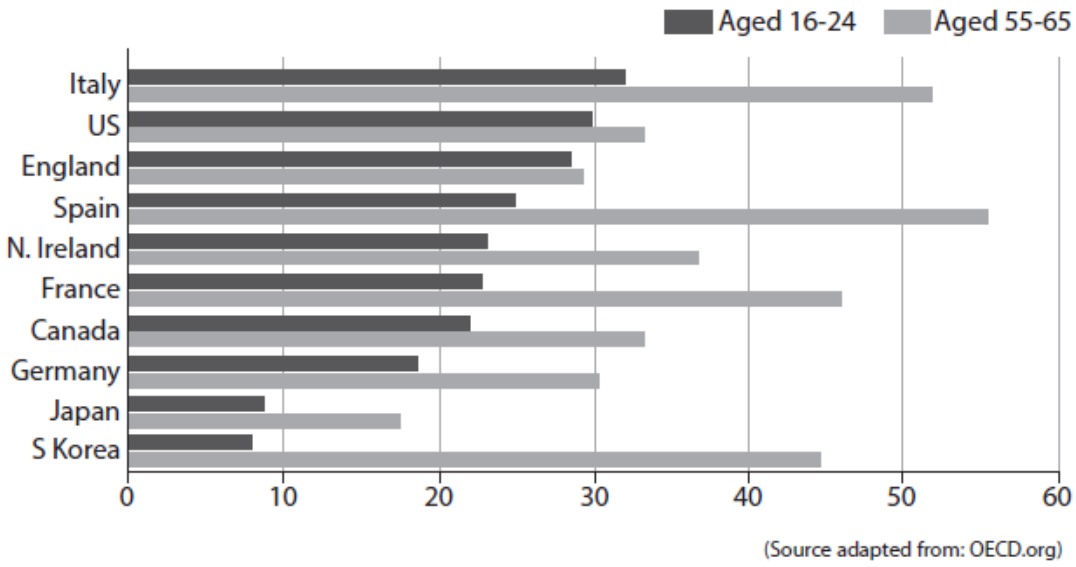


Figure 4: UK index of output per hour worked, base year 2016 = 100



(Source adapted from: ONS.gov.uk)

Figure 5: Proportion of adults with low literacy and/or numeracy skills, by age, selected countries



(Source adapted from: OECD.org)

(Figures 3, 4 and 5 Source: FT.com 2016 data published https://www.ft.com/content/6ada0002-9a57-11e8-9702-5946bae86e6d 2018)

Extract D

The end of the High Street?

Homebase, the UK's second-largest do-it-yourself (DIY) retailer, made £20–40 million a year profit up to 2016. The Australian conglomerate Wesfarmers bought Homebase for £340 million in 2016, and began to rebrand 24 stores under its own name. It scaled back on curtain, cushion and other homeware sales in favour of power tools and building materials. In 2018 Wesfarmers sold the DIY chain for £1, in the face of "extremely challenging" market conditions and excess store space. The chain was bought by restructuring specialist Hilco, which had also rescued the music chain HMV in 2013, and the stores have gone back to using the Homebase name. Over 70% of Homebase stores are currently losing money and the new owner wants to exit loss-making stores and agree to rent reductions, as sales fell 10% in 2018. Homebase has gone back to popular products and brands dropped by its previous owner Wesfarmers.

The closures will add to the mounting job losses on Britain's high streets. About 25 000 jobs have gone in the first seven months of 2018, according to analysis by an economics thinktank. A further 8 300 jobs are under threat at suppliers, with the multiplier effect meaning that GDP is £1.5 billion less than projected.

Several Marks & Spencer clothing stores closed their doors for the last time as the high-street chain pushes ahead with a transformation plan. It plans to close 100 stores by 2022. Toys R Us, Poundworld and Maplin have shut down completely, while New Look, Mothercare and Carpetright have plans to close hundreds of stores as losses rise sharply. Increasing rents and higher business rates have occurred at the same time as falling consumer confidence. Meanwhile, House of Fraser employees and pensioners are nervously awaiting more details about their future. The £90 million rescue deal by Sports Direct, the sportswear chain controlled by Mike Ashley, will protect 16 000 jobs for the time being.

(Source adapted from: https://www.ft.com/content/00d0bb9e-a6ee-11e8-8ecf-a7ae1beff35b 24 August 2018 and https://www.theguardian.com/business/2018/aug/13/homebase-close-80-stores-high-street-job-losses-mount Patrick Collinson 13 Aug 2018)

(a) With specific reference to Figure 3, explain why productivity is measured by 'GDP per hour worked, nominal values at PPPs'.

(5)

(b) Apart from literacy and numeracy skills in young workers, examine **one** reason for the trend in productivity in the UK, over the period shown in Figure 4.

(8)

(c) Discuss factors that are causing many high street retailers in the UK to close some branches or shut down completely.

Use a cost and revenue diagram to support your answer.

(12)

EITHER

(d) Evaluate possible microeconomic and macroeconomic policies which could be used to improve UK competitiveness.

(25)

OR

(e) Evaluate the microeconomic and macroeconomic effects of a decline in the literacy and numeracy skills of a country's young workers.

(25)

(Total for question = 50 marks)

Q10.

(a) Explain the difference between 'good' deflation (Extract B, line 16) and 'bad' deflation (Extract B, line 27).

(5)

(b) With reference to Figure 1 and Extract A, examine the likely reasons for the fall in oil prices since the middle of 2014.

(8)

(c) With reference to Extract A, discuss the factors necessary for the success of a cartel.

(12)

EITHER

(d) With reference to the information provided and your own knowledge, evaluate the microeconomic and macroeconomic effects of a sustained period of deflation.

(25)

OR

(e) With reference to the information provided and your own knowledge, evaluate the microeconomic and macroeconomic effects of a sustained fall in global oil prices.

(25)

(Total for question = 50 marks)

Q11.

The unemployment rate in Portugal decreased steadily from 17.5% in the first quarter of 2013 to 13.1% in the third quarter of 2014.

(a) **One** possible cause of this change in the unemployment rate is that over this period there was an increase in:

(1)

A immigration into Portugal

B aggregate demand in Portugal

C the size of Portugal's negative output gap

D the value of Portugal's trade deficit

Answer ☐

(b) Explain the likely effect of this change in the unemployment rate on Portugal's budget deficit.

(4)

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

(Total for question = 5 marks)

Q12.

The Australian government is temporarily increasing the top marginal rate of income tax by 2 percentage points. Incomes over 180 000 Australian dollars will be taxed at a marginal rate of 49%. This measure is expected to affect around 400 000 taxpayers and to raise 3.1 billion Australian dollars in revenue.

Evaluate the likely impact of this tax rise on the Australian economy.

(Total for question = 25 marks)

Q13.

(a) With reference to Figure 1, explain **one** possible cause of the forecast change in total energy use.

(5)

(b) With reference to Figure 4, examine the likely impact on the USA's circular flow of income of the trends in exports and imports of natural gas between 2000 and 2020.

(8)

(c) With reference to the information provided, discuss the likely impact of a change in the price of gas on the markets for solar energy and nuclear energy.

(12)

EITHER

(d) With reference to the information provided and your own knowledge, evaluate the possible microeconomic and macroeconomic effects on the UK economy of a decision by the government to encourage fracking.

(25)

OR

(e) With reference to the information provided and your own knowledge, evaluate the possible microeconomic and macroeconomic effects on the global economy of lower energy prices.

(25)

(Total for question = 50 marks)

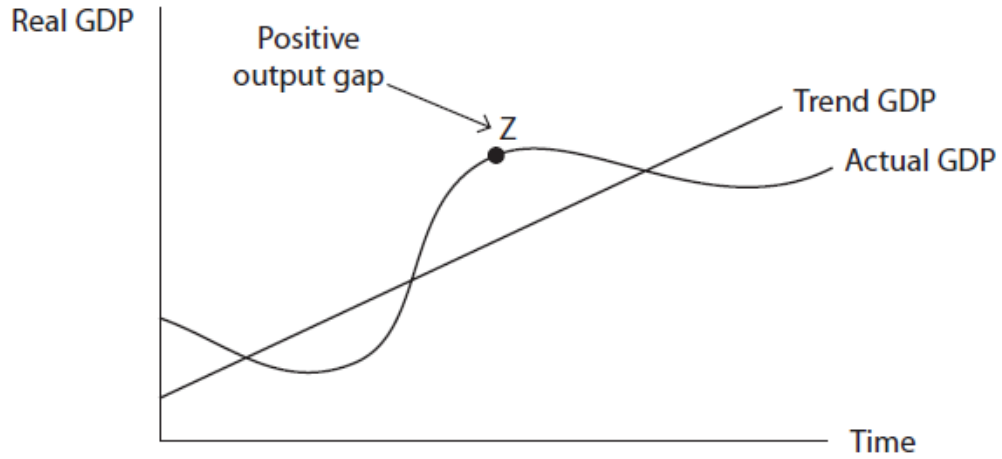
Questions

Q1.

Some questions must be answered with a cross in a box (☒). If you change your mind about an answer, put a line through the box (☒) and then mark your new answer with a cross (☒).

Use the data to support your answers where relevant. You may annotate and include diagrams in your answers.

The trade cycle



(a) At point Z on the diagram, which **one** of the following is likely to occur?

An increase in:

(1)

☒ **A** absolute poverty

☒ **B** budget deficit

☒ **C** cyclical unemployment

☒ **D** inflation

(b) With reference to the graph, explain the difference between automatic stabilisers and discretionary fiscal policy.

(4)

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

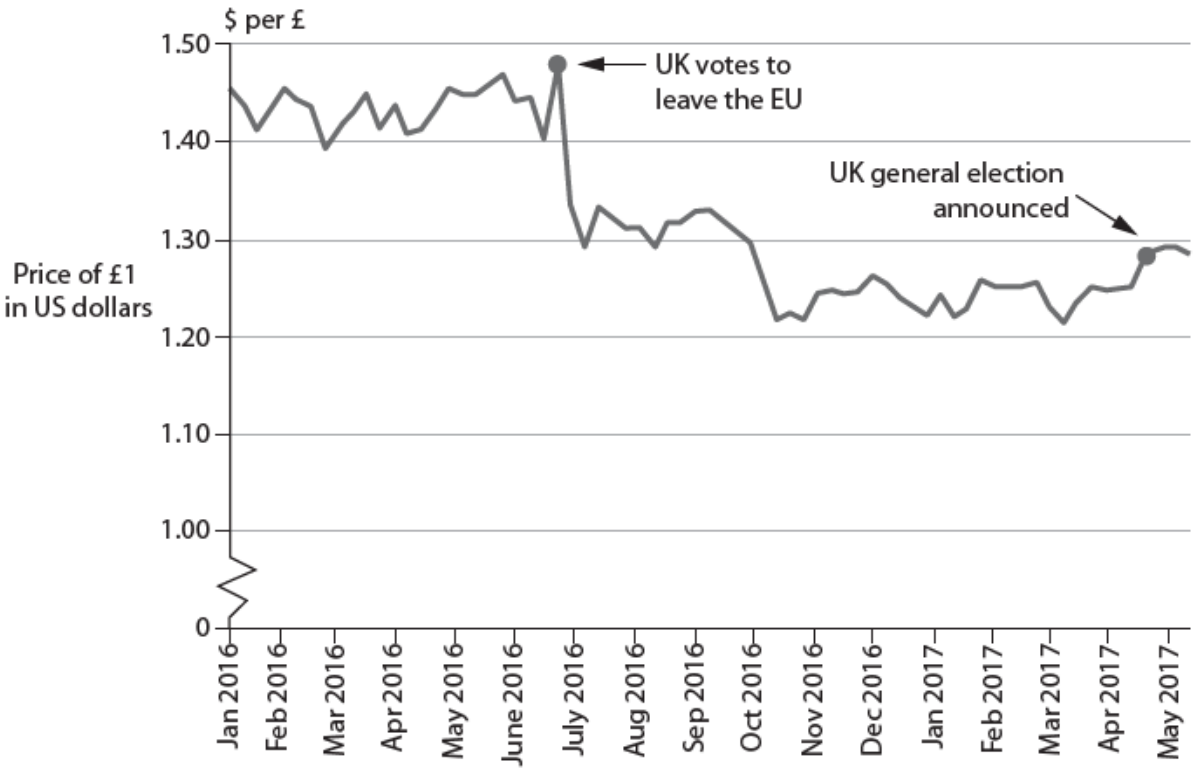
.....

(Total for question = 5 marks)

Q2.

The UK economy since the financial crisis

Figure 1: Pound sterling to US$ exchange rate, 2016-17



(Source: adapted from https://www.ft.com/content/d50ce580-3968-11e7-ac89-b01cc67cfeec)

Extract A

UK companies use forward currency market

The Norfolk-based picture frames maker Nielsen Bainbridge recently made forward contracts in the foreign exchange market to reduce the impact of currency fluctuations. The pound's post-Brexit referendum depreciation has been a test of nerve for Nielsen Bainbridge and many other importers. At present the company's suppliers are located in Europe or China. "Currency therefore has a big impact on our business and the margins we can obtain," says Ms Burdett, the Finance Director. Forward contracts enable institutions, businesses and individuals to lock in an exchange rate over a certain period of time regardless of how the rate moves during that time. Ms Burdett buys currency as soon as Nielsen Bainbridge confirms a large order as a way to fix costs. One third of UK business managers are considering shifting from EU to UK suppliers.

(Source: adapted from 'UK companies use pound strength to hedge forex risk' by Roger Blitz, Markets, © FT.com, 16 May 2017. https://www.ft.com/content/d50ce580-3968-11e7-ac89-b01cc67cfeec)

Extract B

Bank of England seeking to prevent future bank bailouts

The Bank of England has ordered big lenders in the UK to find £116 billion of funding to ensure that taxpayers will never again have to bail out the banking sector. The Bank intends to publish details of how each of the big lenders would cope in the event they find themselves in a situation similar to Royal Bank of Scotland and Lloyds Banking Group, which needed £65 billion of taxpayer bailouts during the 2008 Global Financial Crisis. This had a significant negative impact on the UK government's national debt and, many would argue, increased the need for contractionary fiscal policy. Having said that, the UK government sold all its shares in Lloyds Banking Group in 2017 and, according to the Chancellor of the Exchequer, "recovered every penny of its investment in Lloyds".

Sir Jon Cunliffe, the deputy governor at the Bank responsible for financial stability, said regulators needed to let banks fail in a similar way that traditional companies collapse. This has not been possible in the past because of the risk that savers lose their money and because a system did not exist to allow banks to be put into insolvency.

"Just like when other businesses fail, losses arising from bank failure would be imposed on shareholders and investors. This protects the public from loss and incentivises banks to operate more prudently," said Cunliffe.

(Source: adapted from 'Bank of England tells lenders to find £116bn to help prevent bailouts', by Jill Treanor, 02 October 2017, Copyright The Guardian News and Media Ltd https://www.theguardian.com/business/2017/oct/02/bank-of-england-bailouts-rbs-lloyds and 'Lloyds bank bailout repaid in full, Philip Hammond claims', by Jill Treanor, Larry Elliott, 21 April 2017, Copyright Guardian News & Media Ltd 2017 https://www.theguardian.com/business/2017/apr/21/lloyds-bank-bailout-repaid-in-full-philip-hammond-claims)

Extract C

Bank of England tells lenders to increase capital reserves

The Bank of England has told lenders they will need to build a special reserve worth £11.4 billion by the end of 2018 as it tries to make banks more resilient to the risk posed by mounting consumer debt. This reserve of assets that can be readily turned into cash is a way of forcing banks to set aside capital reserves in good times in order to keep lending to the wider economy at a steady level, even during an economic downturn. In 2017 the Bank of England told UK banks it would raise the reserve ratio, relative to all assets, from zero to 0.5% and also forecast a further increase to 1% by the end of 2017.

The move is not intended to directly reduce consumer demand for credit, which in 2017 grew by 10.3% on an annual basis, but it may well lead to banks becoming less willing to lend to consumers. Since the Bank of England has recently become increasingly concerned about consumer borrowing, including rising car loans and credit card debt, this may be no bad thing as far as the Bank of England is concerned, even if it does have a negative impact on the wider economy.

Analysts are concerned about the impact on consumer confidence of rising inflation, partly caused by a falling pound. With falling real incomes consumers could become more vulnerable to falling behind with their credit card and personal loan repayments. Despite these concerns the UK economy recently recorded the lowest rate of unemployment since 1975.

(Source: adapted from 'Bank of England tells lenders to increase capital buffers by £11.4bn' by Caroline Binham, Gemma Tetlow and Martin Arnold © Financial Times 2017 https://www.ft.com/content/9bc99294-5b1b-11e7-9bc8-8055f264aa8b)

(a) With reference to Extract A, explain the role of forward markets in currencies.

(5)

(b) With reference to Extract A and Figure 1, examine the likely impact of the change in the sterling exchange rate on the UK economy.

(8)

(c) With reference to the last paragraph in Extract C, assess the impact of a fall in real incomes on subjective happiness.

(10)

(d) With reference to Extract C, discuss the potential conflicts between macroeconomic objectives when the central bank attempts to control inflation.

(12)

(e) Discuss whether providing substantial government financial support to banks is the best policy response during a financial crisis.

(15)

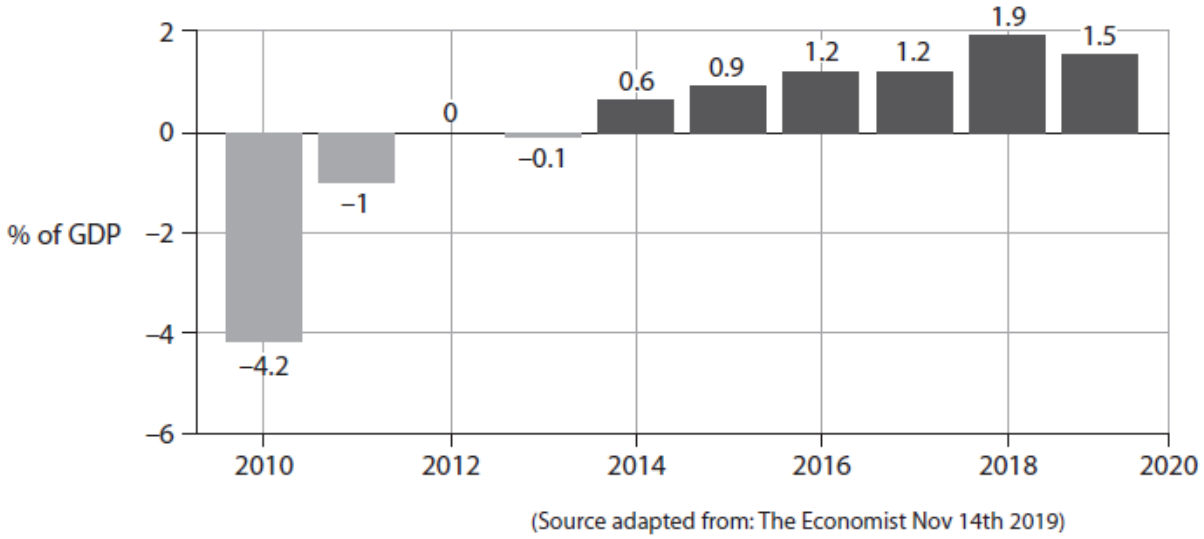
(Total for question = 50 marks)

Q3.

Read Figures 1 to 4 and extracts C and D before answering this question.

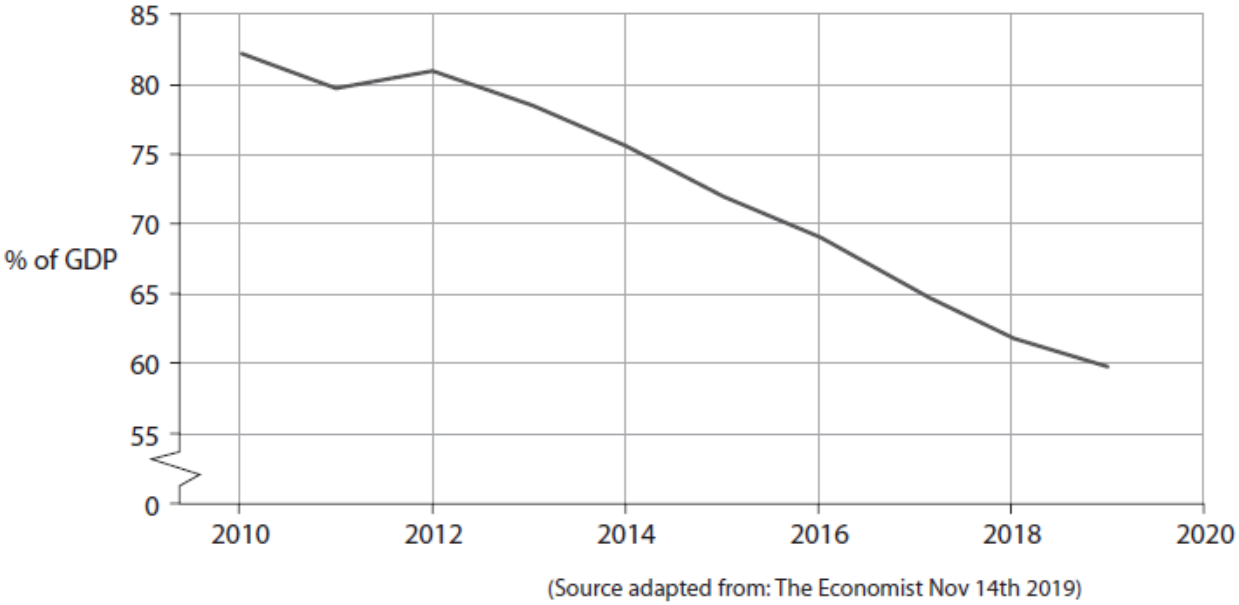
The German economy

Figure 1: German government budget balance, percentage of GDP, 2010 to 2019



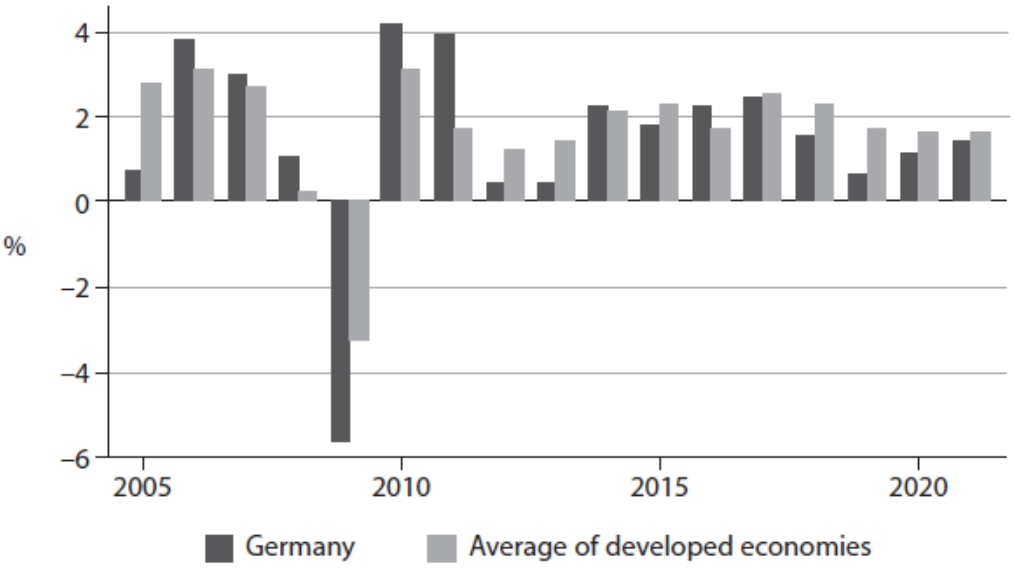
(Source adapted from: The Economist Nov 14th 2019)

Figure 2: German national debt, percentage of GDP, 2010 to 2019



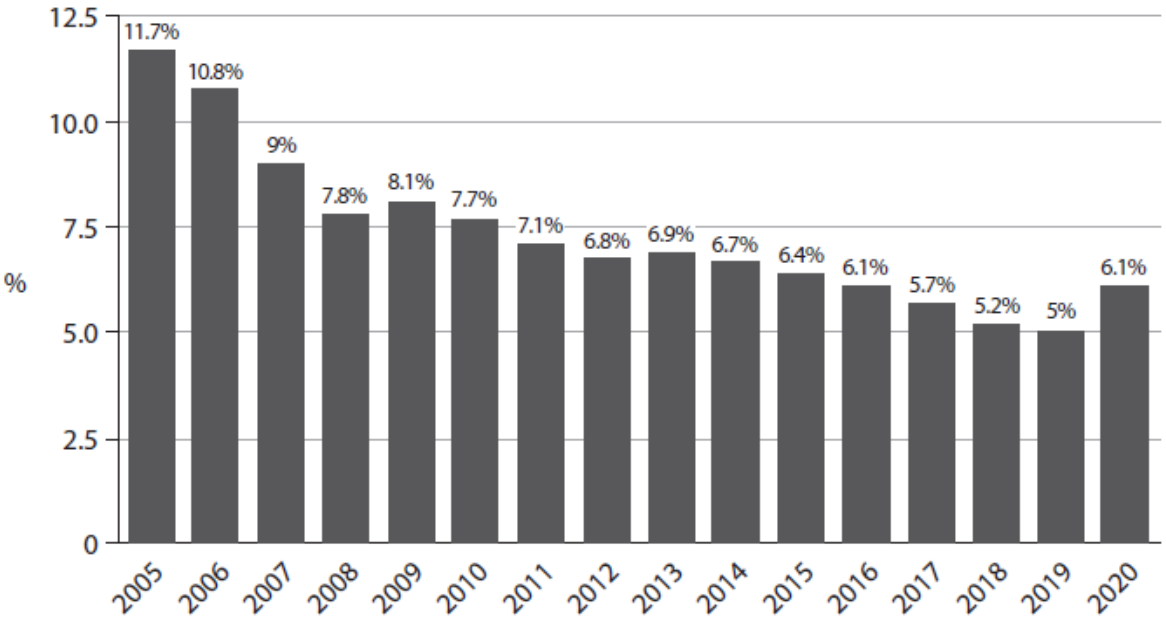
(Source adapted from: The Economist Nov 14th 2019)

Figure 3: Annual percentage change in real GDP, Germany and average of developed economies, 2005 to 2021 (forecasted data for 2020 and 2021)



(Source adapted from: IMF and German Federal Statistical Office)

Figure 4: Unemployment rate in Germany, percentage of labour force, 2005 to 2020 (2020 figure is forecasted)



(Source adapted from: bundesagentur für arbeit.de and https://www.ft.com/content/5486b247-c73e-4887-a2b2-528b23e301a6)

Extract C

Why Germany keeps to budget rules despite a slowdown in growth

Germany's economic boom is over, as it has entered recession. During the last ten years of economic growth well over 4 million jobs were created.

The fear of recession has revived a debate in Germany: should the government spend more to stimulate growth? It is written into the German constitution that the fiscal deficit cannot be greater than 0.35% of GDP, once the effects of the economic cycle have been removed. Germany's budget has been in surplus since 2014 and the government is always reluctant to increase spending which would create a deficit. In 2018, aided by booming employment and low interest costs on existing debt, the budget ran to a surplus 1.9% of GDP.

Germany's main trading partners have long been angered by German fiscal policy. The French President criticised Germany's budget and current account surpluses that "always occur at the expense of others".

Large parts of Germany's infrastructure need significant investment. As the economy has slowed, a decision to run a balanced-budget policy has become harder to defend. In wealthy regions of Germany, crumbling schools have been closed for fear of collapse, and information and mobile technology on a wide scale needs to be modernised. The World Economic Forum reported that accessibility of fibre optic broadband also "remains the privilege of the few". However, private sector firms, such as major motor manufacturers, are still willing to invest in new technology and the profitability of some of these firms, in the long run, benefits as a result.

The state development bank puts Germany's investment shortfall at €138 billion (£120 billion). Arguments for a much more expansionary fiscal policy have failed to influence government policy. Big government programmes, such as a recent package to reduce Germany's carbon emissions, are only implemented when they satisfy fiscal rules.

(Source adapted from: The Economist Nov 14th 2019 and https://www.ft.com/content/3cec4908-d164-11e9-8367-807ebd53ab77 7th September 2019 and https://www.ft.com/content/198f072e-4e42-11ea-95a0-43d18ec715f5 and https://www.ft.com/content/d89d9404-c586-11e9-a8e9-296ca66511c9 and https://www.ft.com/content/8f87c03c-93dc-11e8-b67b-b8205561c3fe)

Extract D

Germany drops to number 7 in the Global Competitiveness Index

Despite being the largest economy in the European Union, Germany's competitiveness is declining, according to the World Economic Forum (WEF). Germany dropped four places in the WEF's Global Competitiveness Index, coming in as the seventh-most competitive economy. Out of the 103 indicators used in the report, Germany received lower scores in 53 areas in 2019.

(Source: https://www.dw.com/en/germany-falls-in-global-competitiveness-ranking/a-50745071 8 October 2019)

(a) Explain **one** reason why a country such as Germany wants to avoid an increase in the national debt relative to GDP (Figure 2).

(5)

(b) Examine **two** likely effects of the forecast change in the rate of unemployment between 2019 to 2020, on firms in Germany. Refer to Figure 4 in your answer.

(8)

(c) Discuss the likely impact of investment in new technology on the profitability of firms in Germany, as described in Extract C line 20. Use a cost and revenue diagram to support your answer.

(12)

EITHER

(d) Evaluate the microeconomic and macroeconomic factors which are likely to determine the rate of economic growth in Germany relative to other developed economies.

(25)

OR

(e) Evaluate the microeconomic and macroeconomic impacts of 'a much more expansionary fiscal policy' (Extract C line 23) on the German economy.

(25)

(Total for question = 50 marks)

Q4.

In 2016 the UK Chancellor of the Exchequer announced that the government would spend an extra £23 billion on innovation and infrastructure over the following five years.

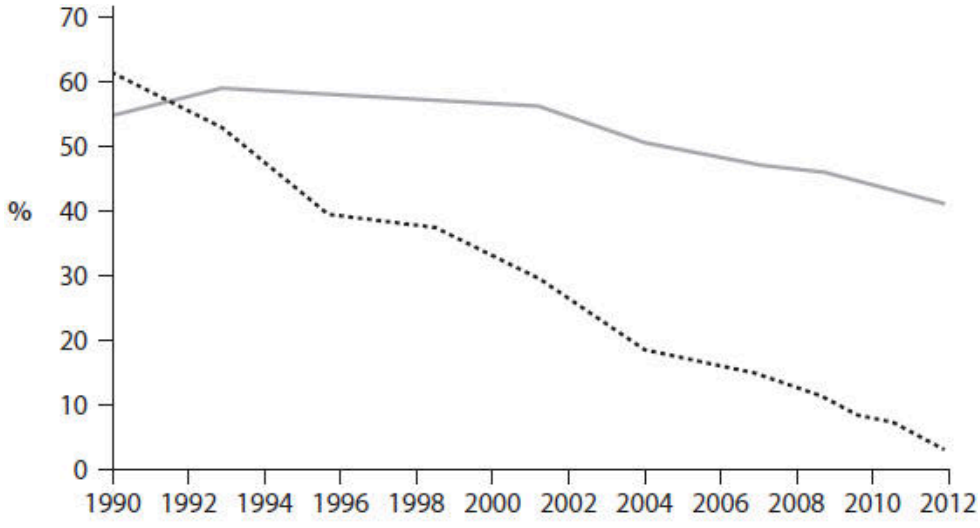
Evaluate the likely economic effects of this planned increase in government expenditure.

(Total for question = 25 marks)

Q5.

Globalisation and Inequality

Figure 1: Proportion of population in absolute poverty (US$1.90-a-day 2011 PPP)



(Source: https://openknowledge.worldbank.org/bitstream/handle/10986/25078/9781464809583.pdf)

Lessons from globalisation

Extract A

The past 25 years have seen a freeing up of trade. Capital has been free to move around the world. Formerly closed economies in Asia have been opened up and tariffs cut. In emerging economies, a billion people have been taken out of absolute poverty, but relative poverty remains a problem.

In many advanced economies globalisation has come to mean, according to the Governor of the Bank of England, "low wages, insecure employment, stateless corporations and striking inequalities". His solution to these problems is threefold: an acceptance by economists that not everybody has gained from trade and technology; a better mix of monetary policy, fiscal policy and structural reform to boost growth; and more inclusive growth. In essence, this is the same conclusion that was reached in the past when there was a fear that market forces had to be moderated to prevent capitalism from destroying itself.

The good news is that this moderation of capitalism included real policy changes: an extension of the right to vote, the growth of trade unions, the creation of welfare states, a move to more progressive tax policies, nationalisation of key sectors of the economy, and more activist demand management.

The bad news is that this process took about 100 years and was not completed until the end of the Second World War. What's more, protectionism seems to be on the increase as countries seek to protect themselves from inequalities caused by rapid globalisation.

(Source: adapted from https://www.theguardian.com/business/2016/dec/05/mark-carney-globalisation-bank-of-england-capitalism)

Extract B

Tackling inequality

Despite decades of substantial progress in boosting prosperity and reducing absolute poverty, the world continues to suffer from substantial inequalities. For example, the poorest children are four times less likely than the richest children to be enrolled in primary education across developing countries. Among the estimated 780 million illiterate adults worldwide, nearly two-thirds are women. Poor people face higher risks of malnutrition and death in childhood and lower chances of receiving key healthcare. Such inequalities result in high financial costs, limit economic growth, and generate social and political burdens and barriers.

These consequences highlight the importance of directing attention to the problem of inequality. There are other reasons to tackle inequality. Most economies are struggling to recover from the global financial crisis that started in 2008 and the subsequent slowdown in global growth. The goal of eliminating absolute poverty by 2030 might not be achieved without accelerated economic growth or reductions in inequalities within countries, especially in those with large numbers of poor. Generally speaking, poverty can be reduced through higher average growth, a narrowing in inequality, or a combination of the two. Achieving the same poverty reduction during a slowdown in growth therefore requires a more equal income distribution.

Some level of inequality is desirable to maintain an appropriate incentive structure in the economy or simply because inequality also reflects different levels of talent and effort among individuals. However, the substantial inequality observed in the world today offers great scope for reducing the gap between rich and poor. Policies to redistribute income from higher-income and wealthy households to those on lower incomes can be achieved without compromising growth, if done effectively. A trade-off between efficiency and fairness is not inevitable.

(Source: adapted from https://openknowledge.worldbank.org/bitstream/handle/10986/25078/9781464809583.pdf)

(a) With reference to the information provided, explain the distinction between absolute poverty and relative poverty.

(5)

(b) With reference to the information provided and your own knowledge, examine **two** factors that might explain the differing rates of decline in absolute poverty in East Asia and Sub-Saharan Africa.

(8)

(c) With reference to Extract A, discuss **two** macroeconomic policies, apart from protectionism, that a government could use to reduce the negative effects of globalisation.

(12)

(d) Assess the view that 'some level of inequality is desirable to maintain an appropriate incentive structure in the economy' (Extract B, lines 19 and 20).

(10)

(e) Discuss the role of the financial sector in the growth and development of developing countries.

(15)

(Total for question = 50 marks)

Q6.

Japan's budget deficit for 2017/18 is expected to be 4.6% of GDP. Its national debt is forecast to increase to above 250% of GDP by 2019.

Evaluate the impact of a large fiscal deficit and national debt on a country's economy.

(Total for question = 25 marks)

Q7.

Mozambique

Figure 2: Interest rates (bank rate of the central bank) and inflation rates of selected African countries, 2017

Selected country	Central bank rate of interest	Inflation rate (CPI measure)
Congo (D.R.)	14%	13.8%
Ghana	21%	9.1%
Kenya	10%	10.1%
Malawi	18%	21.4%
Mozambique	**21.75%**	**18.0%**
Nigeria	14%	21.1%

(Source: official government websites, and other news sources, July 2017)

Extract D

Rising debt levels in Africa

Increases in national debt have brought several African governments towards a debt-servicing crisis when the repayment of debt and interest become unsustainable. Between 2010 and 2015, many sub-Saharan countries raised debt totalling more than £20 billion. Back then, with commodity prices soaring and foreign loans available at very low interest rates, everyone agreed that borrowing was the way to grow an economy with expansionary fiscal policy. Since 2015, some African governments – beneficiaries of big debt write-offs at the start of the century – have taken to private debt markets too eagerly, leaving them with heavy repayment schedules at a time of lower commodity prices.

Until recently, the International Monetary Fund (IMF) has played down African debt concerns, pointing to better management of public resources and greater transparency. But it was shaken by Mozambique's default on more than £2 billion of secret loans used to purchase a non-existent tuna-fishing fleet, raising fears of hidden debt in other African countries with similar levels of corruption. The median level of debt in sub-Saharan Africa had risen sharply from 34% of gross domestic product in 2013 to 48% in 2017. Although that is low by international standards, analysts said debt burdens were heavier than they appeared because of most African countries' low tax base. "The real thing to look for is debt to revenue, or debt-service as a percentage of government spending," said John Ashbourne, Africa Economist at Capital Economics. In several countries, he said, debt payments were above 20% of government revenue, with an opportunity cost in terms of government spending.

(Source: adapted from African debt worries intensify as levels near tipping point by David Pilling © Financial Times 2017 https://www.ft.com/content/939808dc-b4d8-11e7-a398-73d59db9e399)

Extract E

Mozambique's economic stability is being put to the test

The economy of Mozambique, which gained independence from Portugal in 1975, has continued to under-perform. Large-scale emigration, especially of skilled workers, economic dependence on South Africa, a severe drought, a prolonged civil war and political tensions have hindered the country's development. More than half of Mozambique's 26 million people continue to live below the poverty line.

GDP growth declined to 3.6% in 2016 due to fiscal tightening and a slowdown in foreign direct investment. A weak manufacturing sector employs just 3.2% of the population, and is made up of small enterprises (90%), many of which were set up with the aid of microfinance. Traditional export earnings dropped due to depressed global demand. In addition a wide-scale drought seriously affected agricultural production. Foreign currency inflows have weakened – as large-scale gas projects were put on hold, and 14 external lenders suspended direct budget support, as a lesson to be learned from the tuna-fleet scandal. The state budget deficit was 10.7% of GDP in 2017. High interest rates have reduced aggregate demand, and import costs added to inflation following further depreciation of Mozambique's currency, the *metical*, to a new low of 100 meticals to £1.

Mozambique needs urgently to improve its investment environment and confidence in its institutions. The World Economic Forum's global competitiveness ranking placed Mozambique 136 out of 137 countries.

Longer term, Mozambique's economic prospects are promising. There has been progress in talks on restoring international confidence in the government's running of the economy, leading to a lasting and sustainable agreement between rival political groups. The development of gas fields off Mozambique's coast discovered in 2011 is set to transform the economy, coming into production in the 2020s. A rise in coal and electricity exports should help growth to increase. But in the short term, it remains uncertain whether Mozambique can deliver badly needed economic stability.

(Source: adapted from http://www.africaneconomicoutlook.org/en/country-notes/mozambiqua and https://www.chathamhouse.org/expert/comment/mozambique-s-stability-being-put-test 6 October 2017 Dr Alex Vines OBE)

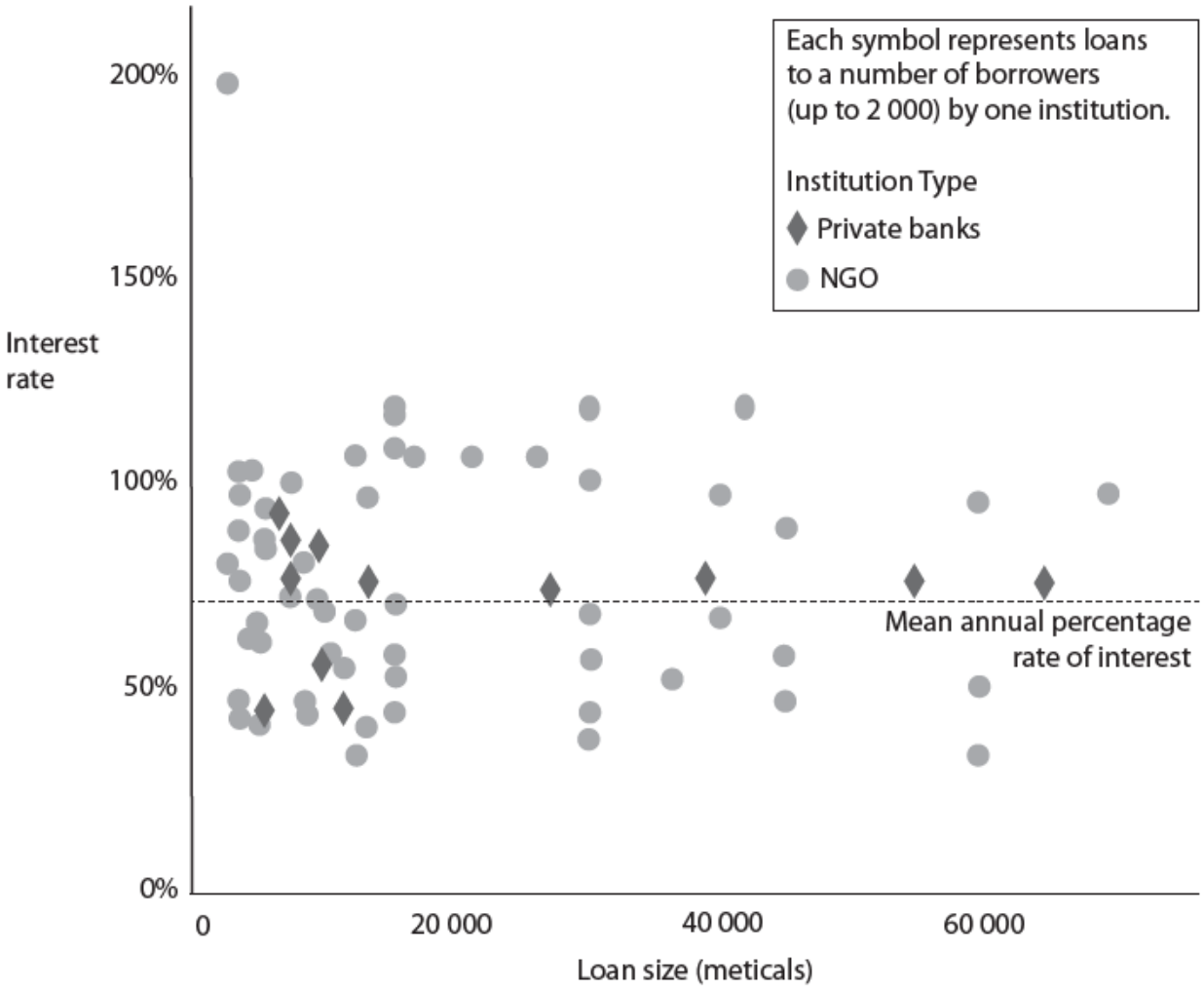
Extract F

Microfinance in Mozambique

Microfinance in Mozambique started in the late 1980s through projects initiated by international relief organisations. The sector has expanded to include many private banks and non-government organisations (NGOs), see Figure 3. This has resulted in wider use (over 100 000 borrowers) and many new business start-ups which could not have gained finance from any other source. Evidence suggests that there is unfulfilled demand for microfinance and a large potential for expansion.

(Source: adapted from http://www.mftransparency.org/microfinance-pricing/mozambique/)

Figure 3: The cost of microfinance loans in Mozambique, 2015



(Source: http://www.mftransparency.org/microfinance-pricing/mozambique/)

(a) With reference to Extract D line 21, explain why 'opportunity cost' is a problem for governments of developing countries when servicing debt.

(5)

(b) Examine **two** reasons, apart from access to finance, why 90% of the manufacturing sector in Mozambique 'is made up of small enterprises' (Extract E, line 9).

(8)

(c) Discuss whether borrowers benefit from microfinance. Make reference to Mozambique in your answer.

(12)

EITHER

(d) Evaluate the microeconomic and macroeconomic factors, apart from access to credit and banking, influencing growth and development in Mozambique.

(25)

OR

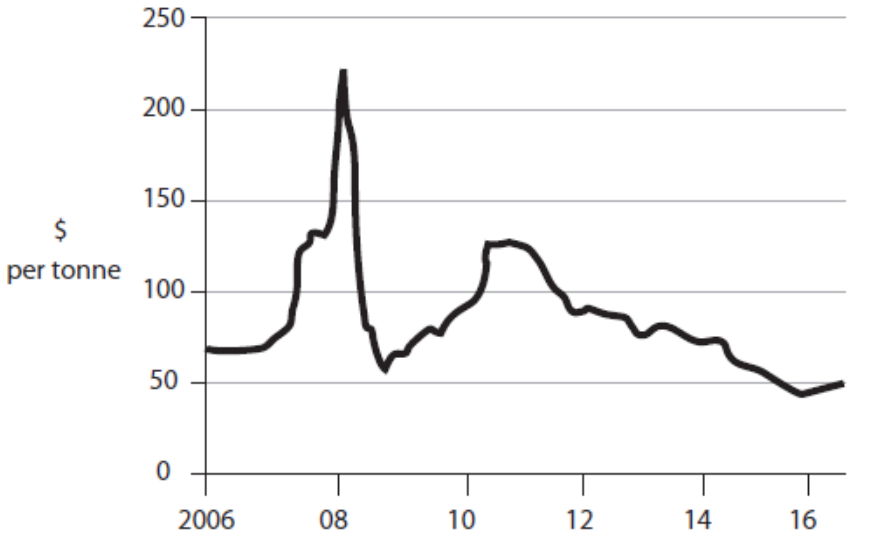
(e) Evaluate the likely microeconomic and macroeconomic effects of relatively high inflation rates in many African countries.

(Total for question = 50 marks)

Q8.

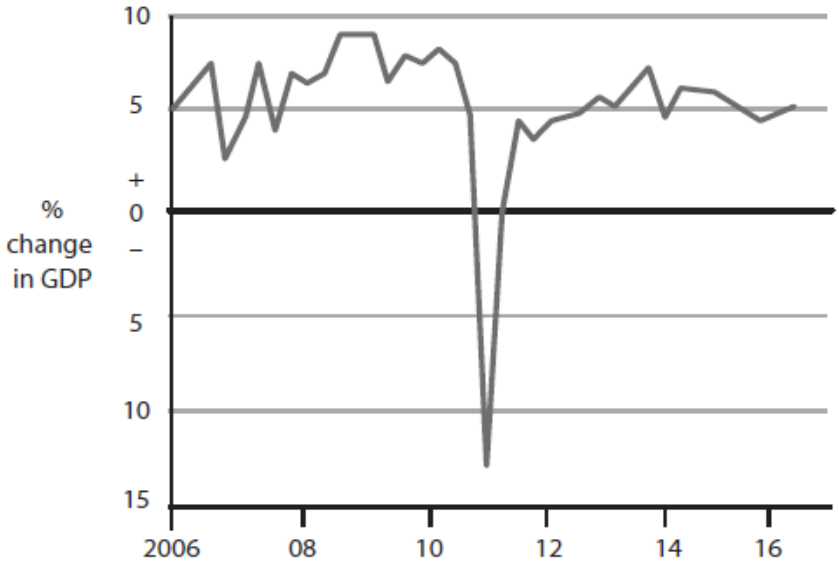
Indonesia

Figure 4: World coal prices, 2006–2016, US dollars per tonne



(Source: http://www.economist.com/news/world-week/21697025-business-week)

Figure 5: Indonesia's real GDP, annual percentage change



(Source: http://www.economist.com/news/world-week/21697025-business-week)

Extract D

Indonesia's economic outlook

The Indonesian economy is expected to grow by an average of 4.8% a year between 2017 and 2021. Joko Widodo, president of Indonesia since 2014, is increasingly confident in his role and now has enough political support to pass some of his desired supply-side reforms. His government has been aggressively trying to improve the business and investment environment by easing regulations and offering tax incentives, for example to firms investing in special economic zones.

Indonesia receives US$2.3 billion a year in overseas development aid, which is mainly spent on education and healthcare. There is also ongoing aid from international institutions and non-government organisations paying for restructuring after the 2004 Indian Ocean earthquake and tsunami, which led to the loss of over 170 000 lives and much damage to economic livelihood. Aid agencies have supported the Indonesian government in providing healthcare free at the point of access for 88 million of the poorest people, free schooling for 12 years for each child, and tertiary education for students accepted into university. There is a scheme to provide each of Indonesia's 15.5 million poorest households with a cash transfer of 200 000 rupiah (US$14.37) a month. The World Bank has approved US$800 million in infrastructure loans to Indonesia, with another US$950 million as conditional loans. The Asian Development Bank has committed itself to lending US$2 billion. In December Japan's development agency lent Indonesia US$535 million to construct two power stations.

(Sources: adapted from http://country.eiu.com/Indonesia and http://www.economist.com/news/special-report/21693404-after-decades-underinvestment-infrastructure-spending-picking-up-last)

Extract E

Indonesia's economic policies as commodity prices collapse

Indonesia is the world's fourth largest exporter of coal and the raw material accounts for 11% of its exports. Its other main exports are crude oil, palm oil, rubber and tin. Its main commodity exports tripled in value between 2000 and 2010, and as exports boomed, so did the economy. But the value of commodity exports has fallen by more than half from its peak. Coal now sells for just US$50 per tonne, against US$125 in 2011.

In the decade to 2014, Indonesia's real GDP grew by an annual average of 6%, but the collapse in commodity prices has slowed the economy. In 2015 growth was 4.8%, the slowest rate since 2009. But compared with many other commodity exporters, Indonesia is getting off lightly.

The value of the rupiah, Indonesia's currency, against the US dollar has fallen by 30% since 2013, but has since stabilised. Other emerging market currencies have depreciated even more steeply over that period. Despite the weak exchange rate, Indonesia's inflation rate has mostly remained within the central bank's target range of 3-5%. The main impact of the rupiah's fall has been to curb imports, helping limit Indonesia's current account deficit to around 2% of GDP despite weaker export earnings. A cautious fiscal policy during the boom years has allowed for a modest fiscal expansion to offset the effects of weak exports and investment. The national debt is just 26% of GDP.

Mr Widodo knows that Indonesia cannot raise its long-term growth rate if the economy remains reliant on coal. It needs a broader range of manufacturing and service industries. If new enterprise is to flourish, Indonesia must support local entrepreneurship. The labour market is inflexible. To start a business takes an average of 47 days, compared with four in Malaysia and two in Singapore. The President's supply-side policies are improving the business climate. The average number of days needed to approve a new power plant has declined from 900 to 200. The government recently revised its "negative investment list" of sectors in which foreign ownership is banned or restricted, fully opening up the rubber, film and restaurant sectors, among others. In 2015 he launched a series of measures to try to reduce government failure, including easing some regulations, streamlining licensing procedures for firms on industrial estates and providing tax incentives to invest in special economic zones.

The government has used savings from cutting fuel subsidies, worth over 4% of GDP, to fund extra capital spending. But the budget deficit still widened to 2.8% of GDP, very close to the legal limit of 3%. If public expenditure is to increase further, the government will need to raise more revenue. That will not be easy. Most workers and employers pay little or no tax. Only 27 million of Indonesia's 255 million people are registered taxpayers, and in 2014 just 900 000 of them paid what they owed, leaving it with a tax revenue to GDP ratio of around 10%. Big companies say that they are being squeezed harder by the tax authorities because they are an easier target.

Infrastructure spending will help bring foreign investment and good jobs to Indonesia as well as encouraging exports. Indonesia's infrastructure problem can be summed up as too few roads and congested ports. In the short term, infrastructure spending puts people to work and boosts demand for raw materials. In the longer term this spending offers the chance to make up for decades of neglect and underinvestment. Indonesia has plans for 65 dams, 16 of which are already under construction. In 2015 work started on the Keureuto Dam, designed to boost agricultural productivity in Aceh. Recently fields were flooded for the massive Jatigede Dam in West Java, after 20 years of delays. Once complete, the dam will irrigate 90 000 hectares of rice paddy, increasing efficiency by giving farmers two harvests a year instead of one.

(Sources: adapted from http://www.economist.com/news/special-report/21693405-secure-growth-it-needs-indonesia-must-resist-its-protectionist-urges-roll-out and http://www.economist.com/news/special-report/21693404-after-decades-underinvestment-infrastructure-spending-picking-up-last)

(a) Using the data in Figure 4 and other information provided, explain the likely change to Indonesia's terms of trade since 2011.

(5)

(b) Examine the likely effects on the profitability of Indonesian rice farmers of the government's increased investment in dams (Extract E, lines 43-48). Use a cost and revenue diagram to support your answer.

(8)

(c) Discuss the benefits of aid to Indonesia.

(12)

EITHER

(d) With reference to the information provided and your own knowledge, evaluate the microeconomic and macroeconomic effects on Indonesia of the volatility of prices of commodities such as coal.

(25)

OR

(e) Evaluate the likely microeconomic and macroeconomic effects of the supply-side policies recently introduced in Indonesia.

(25)

(Total for question = 50 marks)

Q9.

Use the data to support your answers where relevant. You may annotate and include diagrams in your answers.

According to the charity Oxfam, the combined wealth of the 62 richest people in the world is the same as the wealth of the poorest half of the world's population. The value of the combined wealth of the poorest half of the world's population has fallen by 38% between 2010 and 2016.

(Source: adapted from https://www.oxfam.org/en/pressroom/pressreleases/2016-01-18/62-people-own-same-half-world-reveals-oxfam-davos-report)

(a) Explain the distinction between income and wealth.

(2)

.....

.....

.....

.....

.....

.....

.....

.....

.....

.....

(b) Explain **one** likely reason why global wealth inequality has increased.

(2)

.....

.....

.....

.....

.....

.....

.....

.....

.....

(c) Which **one** of the following would be most likely to reduce a country's Gini coefficient?

An increase in:

(1)

☒ **A** import tariffs

☒ **B** progressive taxes

☒ **C** regressive taxes

☒ **D** value added tax

(Total for question = 5 marks)

Q10.

Markets for food and drinks high in fat, salt or sugar (HFSS)

Figure 1: UK market share of potato crisps, 2017

Firm	Brand	Size	Market share of firm	Market share of product	Price (£)
Walkers	All Walkers		*55.3%*		
	of which: *Regular Standard*	35 g		28.1%	0.45
	Regular Max	50 g		7.4%	0.63
	Sensations	40 g		2.0%	0.59
	Doritos	40 g		4.7%	0.45
	Other			13.1%	
KP	KP	50 g	*22.7%*		0.52
Tayto	Golden Wonder		*4.2%*		
		<40g		3.1%	0.38
		40g+		1.1%	0.72
Other	Other		*17.8%*		

(Source: adapted from https://academic.oup.com/restud/article/3108825/The-Effects-of-Banning-Advertising-in-Junk-Food 6 April 2017)

Extract A

The effects of a total ban on advertising of HFSS foods

Food and drinks which are high in fat, salt or sugar (HFSS) tend to be sold in highly concentrated markets. Tough new rules banning advertisements for HFSS products, such as those for confectionery, fizzy drinks and potato crisps, come into effect in July 2017 as a means to reduce consumption. The rules apply to media targeted at under-16s and will mean a major reduction in the number of advertisements children see for HFSS products in posters near schools, in films targeted at children, on catch-up television and in social media if it is directed at children.

There are three main factors that will determine the effectiveness of the intervention: first, whether advertising acts to expand the market share or steal rivals' market share. Secondly, how firms in the market adapt their behaviour in response to the ban. Thirdly, what substitute products do consumers turn to if they opted out of the targeted market.

Results from a recent survey in the UK suggest that the total quantity of crisps sold would fall by around 15% in the presence of an advertising ban, or by 10% if firms respond with price cuts, since the ban acts to make the market more competitive and firms respond to the ban by, on average, lowering their prices.

The survey showed that following a ban, consumers are more likely to switch to another junk food than to a healthy food, which (in addition to the pricing response of firms) acts to partially offset any health gains from the policy.

(Source: adapted from The Effects of Banning Advertising in Junk Food Markets, Dubois, Pierre; Griffith, Rachel, Review of Economic Studies Copyright © 2017, Oxford University Press https://academic.oup.com/restud/article/3108825/The-Effects-of-Banning-Advertising-in-Junk-Food 6 April 2017 and https://www.asa.org.uk/news/tougher-new-food-and-drink-rules-come-into-effect-in-children-s-media.html 30 June 2017)

Extract B

Taxing HFSS foods and subsidising healthy eating widens inequality

Since low-income groups spend a higher proportion of their income on food and tend to eat less healthily, they are the main targets of taxes on products that are high in fat, salt or sugar (HFSS). Subsidies on healthy food are seen as an alternative policy approach to encourage healthy eating. While data on the impact of such policies are scarce, a recent study on the distributional impacts of HFSS taxes and healthy food subsidies found that these actually widened health and fiscal inequalities. The policies tend to be regressive and favour higher-income consumers. Taxes on unhealthy food increase prices which have a greater impact on low income groups rather than higher income groups. Lower income groups prefer to buy HFSS food.

Subsidies encouraged all income groups to buy more fruit and vegetables. However, those on higher incomes proved more responsive and the average share of budget spent on healthy food actually increased for the higher income groups who were more likely to buy the subsidised healthy food and then spend the savings they had enjoyed on yet more healthy food. The diets of the higher income groups before the subsidy tended to be healthier. The choices of the higher income groups are more responsive to price changes. By contrast, lower income groups, if they responded to lower prices, often used the money saved to buy unhealthy items or something else entirely. The long-term benefits of a healthier diet are harder to grasp for consumers when information gaps exist. Often the immediate boost of a tasty treat is more appealing. Taxes and subsidies do not change that. Other strategies are needed to promote healthy eating, especially education.

(Source: adapted from Economist 5 October 2017 https://www.economist.com/news/finance-and-economics/21730033-study-suggests-lower-income-families-end-up-paying-more-their-food-taxing-fat and https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3031005 The Economic Journal September 2017 Vol 127 Issue 604)

Extract C

Tax on fatty foods in Denmark is an economic disaster

Denmark introduced a specific tax on saturated fat in October 2011. Recognised as a world-leading public health policy, it was abandoned just 15 months later having been both an economic and political disaster.

Indirect taxes of this sort are invariably regressive, disproportionately affecting the elderly and the poor. The specific tax led to prices rising on average 15% for highest-fat products, yielding a total decrease of 5% in the intake of saturated fat from products such as minced beef and cream. 80% of Danish consumers did not change their shopping habits at all. The behavioural change was economically damaging as consumers switched to cheaper brands and crossed the border to Sweden and Germany to do their shopping. Danish tax revenue fell as a result.

(Source: adapted from https://iea.org.uk/in-the-media/press-release/evidence-shows-a-fat-tax-would-hit-poorest-the-hardest 25 May 2013 and https://www.cambridge.org/core/journals/public-health-nutrition/article/effects-of-the-danish-saturated-fat-tax-on-the-demand-for-meat-and-dairy-products/984CF03634C819D50E66C7B5DC5209DA/core-reader)

(a) With reference to Figure 1 and Extract A, explain what is meant by a 'highly concentrated' market for potato crisps (Extract A, lines 2–3).

(5)

(b) Apart from changes in indirect taxes and subsidies, examine **two** causes of income inequality within a developed economy such as the UK.

(8)

(c) In Extract A, lines 15–16, it was suggested that some firms may respond to the advertising ban by cutting the prices of their products.

Using game theory and the information provided in Figure 1 and Extract A, discuss the effects **on firms** of cutting prices in an oligopolistic market.

(12)

EITHER

(d) Evaluate the microeconomic and macroeconomic effects of increased government spending on education to promote healthy eating in the UK.

(25)

OR

(e) Evaluate the likely microeconomic and macroeconomic effects of imposing a tax on HFSS foods.

(25)

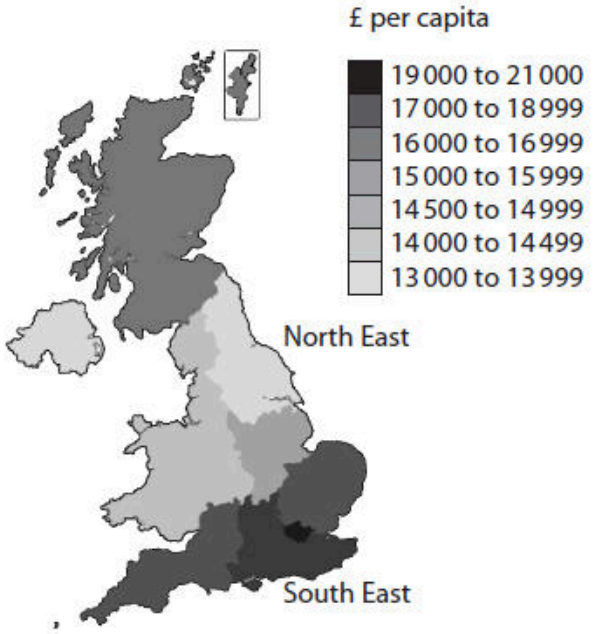
(Total for question = 50 marks)

Q11.

Read Figures 1 and 2 and the following extracts (A to C) before answering this question.

UK Government spending and inequality

Figure 1: UK regional gross disposable household income per capita, 2018



(Source: adapted from University of Sheffield/Office for National Statistics: https://www.sheffield.ac.uk/news/nr/uk-higher-regional-inequality-large-wealthy-country-1.862262)

Figure 2: UK subjective happiness by income, April 2021

Answer to the question: 'On a scale of 1–10, how happy did you feel after yesterday?' (0 = not at all, 10 = completely)

Less than £10 000	£10 000–£20 000	£20 000–£40 000	More than £40 000
7.31	7.02	7.13	7.29

(Source: adapted from https://www.ons.gov.uk/peoplepopulationandcommunity/wellbeing/datasets/incomegroupsplitestimatesonpersonalandeconomicwellbeingacrosstime)

Extract A

Regional inequality in the UK

Geographically, the UK is highly unequal in incomes. According to research from the University of Sheffield, the estimate of the Gini coefficient is 0.34. There are a number of different reasons for this. First, labour in poor places tend to develop too few skills, with a lack of education holding people back. In Rotherham in the north of England, for example, 21% of disadvantaged 18-year-olds from state schools and colleges go on to higher education compared to 41% in London. Secondly, there is a lack of infrastructure spending in northern cities compared to London. In 2017–18, 28% of public expenditure on transport – and 46% of capital expenditure on railways – was spent in London. The argument for this is that London gets a lot of public money because a lot of people take public transport. This has angered many people in the North.

These problems cannot be solved quickly. They compound each other. Just as people are rarely poor for one reason, regions do not fall behind only because they have poor transport, poor schools or poor policy making, but for all those reasons and more. Ideally, the UK would develop a bold plan for regional development that could be followed by future governments, as Germany did for its eastern part. Tera Allas of McKinsey, a consultancy firm, argues that improving education is crucial, even if the returns are not immediately obvious. It is easier to improve schools than to persuade businesses to move to a poorer part of the country.

(Source: adapted from https://www.economist.com/britain/2020/07/30/why-britain-is-more-geographically-unequal-than-any-other-rich-country)

Extract B

Public sector spending on infrastructure

Economic differences across the UK are large and have grown. The government is looking at reducing this inequality partly through spending on transport infrastructure. Public sector capital spending is due to rise from just over 2% of GDP to 3%. That amounts to around £20 billion of additional spending per year on new capital projects. The government is looking to take advantage of current low interest rates to finance the expansion without worsening its fiscal position.

The government is determined to focus this spending on the north of England, Wales and the Midlands. Planned schemes include a new Trafford Park tram line in Manchester and reopening train lines and stations closed back in the 1960s, including stations in Haxby in Yorkshire and Blyth in Northumberland. Progress has already been made in Wales with the reopening of Bow Street station near Aberystwyth. This project has taken 11 years to become a reality and cost £8m. It is estimated that it will generate a boost to the economy of £24m through boosting local trade, creating new jobs in the local area, and easing pressure on congested roads heading into Aberystwyth.

(Source: adapted from https://www.economist.com/britain/2020/01/09/the-coming-splurge-on-northern-infrastructure and https://www.wales247.co.uk/transport-for-wales-delivers-new-bow-street-station)

Extract C

Options for UK tax rises in the future

There are a number of options for raising additional tax revenue in the future. These include:

- increasing council tax on houses: this annual charge paid to local government is currently based on estimated house prices in 1991 and so is very out of date. This would negatively affect areas where house prices have risen the most since 1991
- a one-off wealth tax: a 5% tax on property and pension wealth of more than £500 000 would raise £260 billion to help pay for the global health crisis in five years, according to proposals from the Wealth Commission
- increasing corporation tax: at the 2021 Budget the Chancellor announced that the top rate of UK corporation tax would be increased to 25% by 2023. This will remain the lowest rate in the G7 group of the world's largest advanced countries, but will raise £17.2 billion in 2025–26.

(Source: adapted from https://www.telegraph.co.uk/tax/income-tax/five-tax-rises-rishi-sunak-considering-chances-happening-budget/, and https://home.kpmg/uk/en/home/insights/2021/03/tmd-corporation-tax-rate-to-increase-to-25-percent.html)

(a) Using a Lorenz curve diagram, explain how income inequality is measured using the Gini coefficient. Refer to Extract A in your answer.

(5)

(b) With reference to Figure 1 and Extract A, examine **two** likely causes of income inequality within the UK.

(8)

(c) With reference to Figure 2, assess whether an increase in real income improves subjective happiness within the UK.

(10)

(d) With reference to Extract C and your own knowledge, discuss methods the UK government could use to increase tax revenue.

(12)

(e) With reference to Extract B, discuss the benefits of an increase in infrastructure spending on the UK economy. Use an aggregate demand and aggregate supply diagram to support your answer.

(15)

(Total for question = 50 marks)

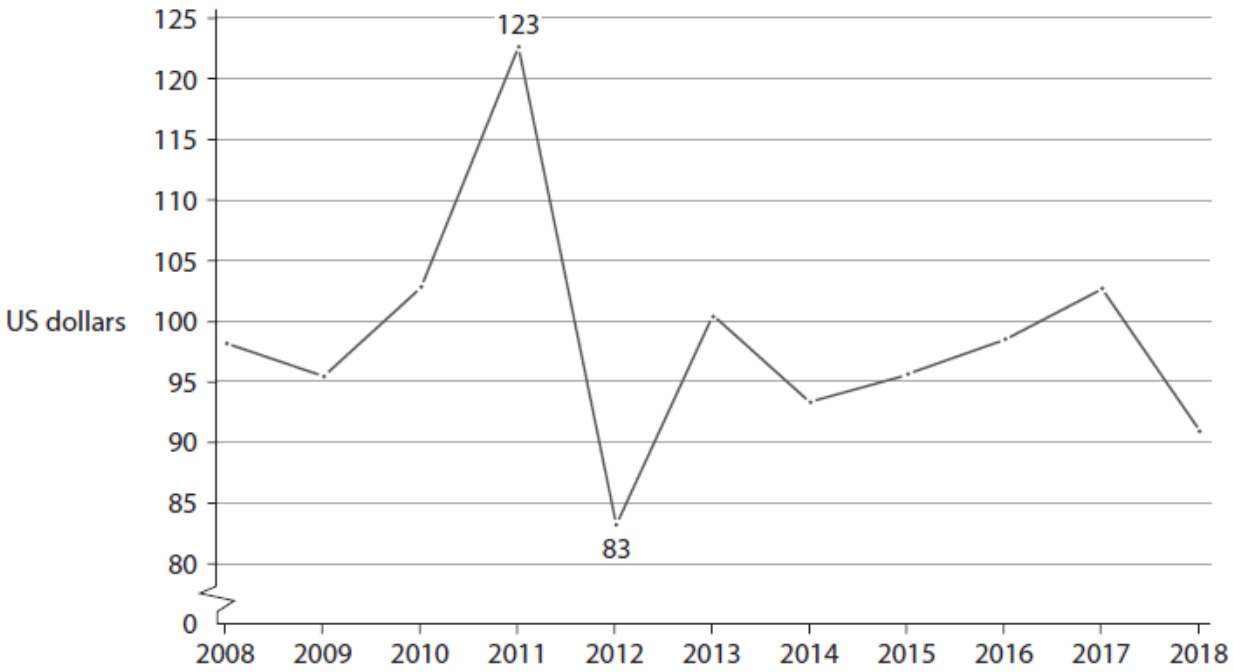
Q12.

Use the data to support your answers where relevant. You may annotate and include diagrams in your answers.

Read Figures 1, 2, and 3 and extracts A and B before answering this question.

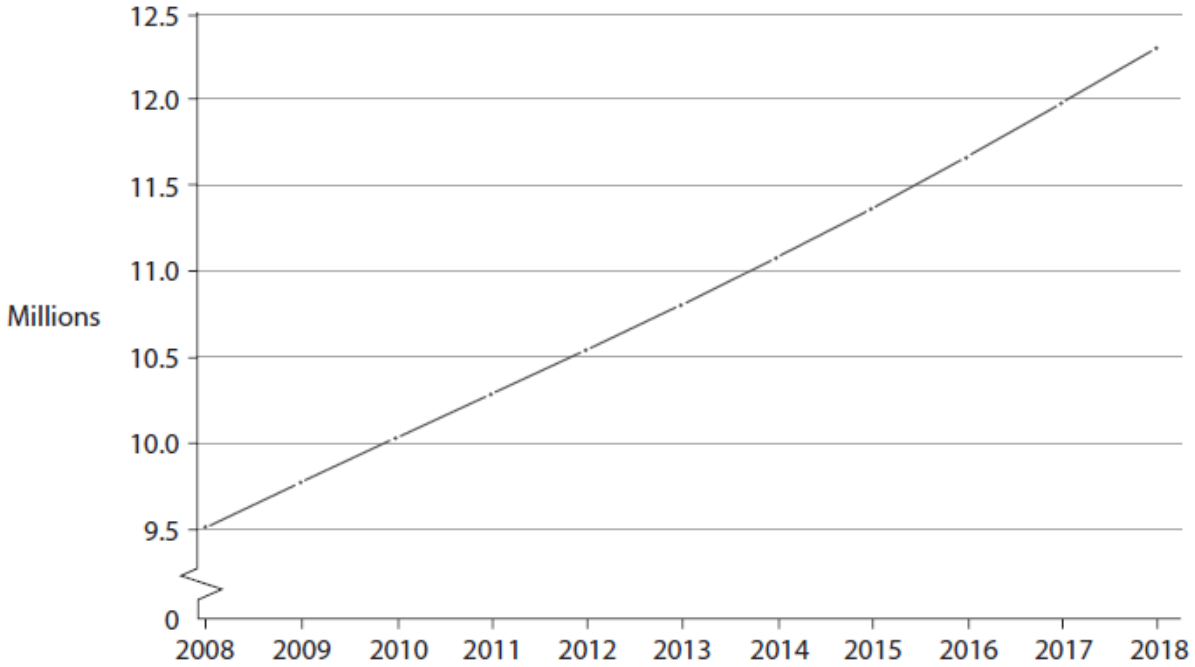
Trade and aid in Rwanda

Figure 1: Aid funding received by Rwanda (per capita, US dollars), 2008 to 2018



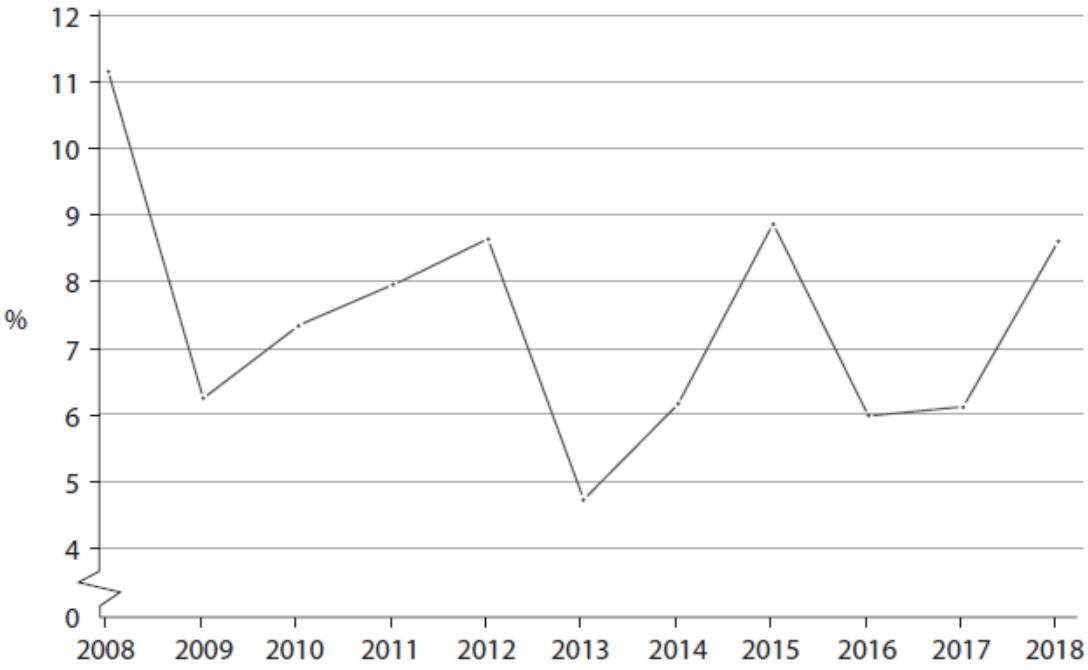
(Source adapted from: data.worldbank.org)

Figure 2: Population of Rwanda (millions), 2008 to 2018



(Source adapted from: https://tradingeconomics.com/rwanda/population)

Figure 3: Rwanda real GDP annual percentage growth rate, 2008 to 2018



(Source adapted from: African Development Bank Statistics accessed April 2020)

Extract A

Rwandan tariffs on imports of used clothing

In a market in Kigali, Rwanda's capital, an auction is under way. Sellers offer crumpled T-shirts and faded jeans; traders argue over the best picks. Everything is second-hand. A Tommy Hilfiger shirt sells for 5 000 Rwandan francs ($5.82); a plain one for a tenth of that. Afterwards, a trader sorts through the purchases he will resell in his home village. The logos hint at their previous lives: Kent State University, a rotary club in Pennsylvania, Number One Dad.

These auctions were once twice as busy, but in 2016 Rwanda's government increased import tariffs on a kilo of used clothes from $0.20 to $2.50. Now many traders struggle to make a profit. The traders are not the only ones who are unhappy. Exporters in the US claim the tariffs are costing jobs there. In March, the US President warned that he would suspend Rwanda's tariff-free access to US markets for its clothing exports after 60 days if it did not remove the tariff.

Globally, about $4 billion of used clothes crossed borders in 2016. The share from China and South Korea is growing, but 70% still come from Europe and North America. Many go to Asia and eastern Europe, but Africa remains the largest market. The trade enables poor people to afford clothes and creates retail jobs. However, governments worry that the trade undercuts their own clothing manufacturers.

Second-hand imports of clothing now dominate African markets. Researchers at the Overseas Development Institute, a British think-tank, estimate that Tanzania imports 540 million used items of clothing and 180 million new ones each year, while producing fewer than 20 million itself. African manufacturing is weak for many reasons, from ineffective privatisations to collapsing infrastructure. But second-hand clothing imports are a major factor: it is estimated that they accounted for half of the fall in employment in the African clothing industry between 1981 and 2000.

For example, a clothing factory in Kigali is operating at only 40% of capacity and employs 600 workers, down from 1 100 in the 1990s. It is hard to compete, says Ritesh Patel, its manager, when a used imported T-shirt sells for the price of a bottle of water. Instead, the company specialises in uniforms for police, soldiers and security guards, which cannot be bought second-hand.

The threatened suspension of tariff-free access to the US market would hurt Rwanda, but not very much. Last year Rwanda sold just $1.5 million of clothing to the US. Nor, with about 12 million people, is Rwanda a big market for US exports.

(Source adapted from: https://www.economist.com/finance-and-economics/2018/05/31/rwanda-refuses-to-remove-tariffs-on-imports-of-used-clothing)

Extract B

Development in Rwanda

Rwanda's strong economic growth has been accompanied by substantial improvements in living standards, with a two-thirds drop in child mortality and near-universal primary school enrolment. A strong focus on policies to encourage industrialisation and poverty reduction initiatives have contributed to significant improvements in access to services and human development indicators. Absolute poverty declined from 59% to 39% of the population between 2001 and 2014 but was almost stagnant between 2014 and 2017. The official inequality measure, the Gini index, declined from 0.52 in 2006 to 0.43 in 2017.

(Source adapted from: https://www.worldbank.org/en/country/rwanda/overview)

(a) Using the data in Figures 1 and 2, calculate the change in the level of total aid funding to Rwanda between 2011 and 2012.

(5)

(b) With reference to the information provided, examine **two** likely benefits for the Rwandan economy of the growth in the country's population.

(8)

(c) With reference to the information provided, assess the likely impact on the Rwandan economy of the change in aid received between 2017 and 2018.

(10)

(d) Discuss the likely impact on Rwandan consumers and clothing manufacturers of the increase in the tariff on imports of second-hand clothes. Use an appropriate diagram to support your answer.

(12)

(e) Discuss policies, other than import tariffs, that the Rwandan government could use to develop its manufacturing industries.

(15)

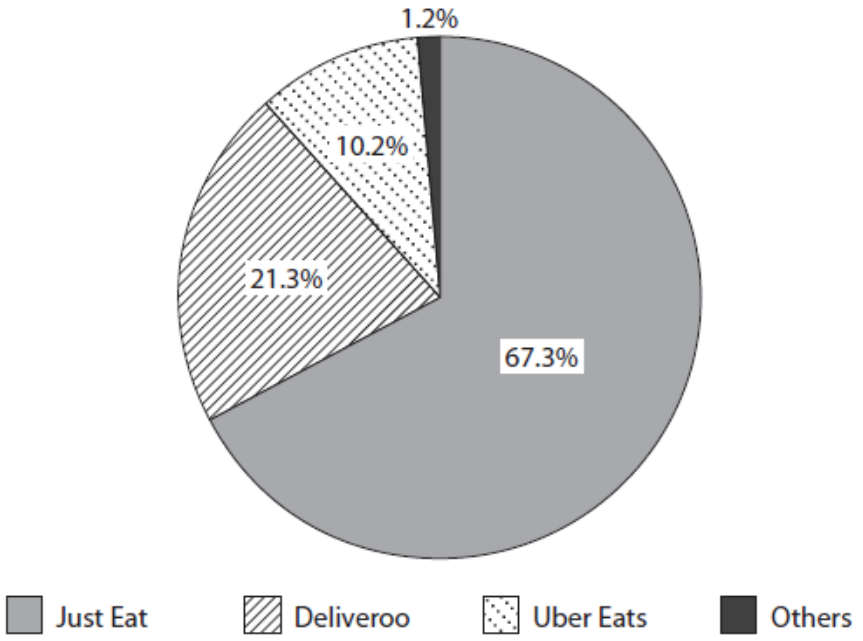
(Total for question = 50 marks)

Q13.

Read Figure 1 and the following extracts (A to C) before answering this question.

The food delivery industry

Figure 1: Market share for third-party food delivery services in the UK, 2019



(Source: adapted from https://onefourzerogroup.com/the-takeaway-takeover/)

Extract A

National Minimum Wage rises are more significant for 23 to 25-year-olds

In 2021, the National Minimum Wage main rate, also known as the National Living Wage, rose by 2.2% to £8.91, following a 6.2% rise in 2020. By reducing the age at which people are eligible for the National Living Wage to 23 in 2021, it is estimated that an additional 7.5% of 23 to 25-year-olds could get a 71p an hour pay rise. This amounts to an 8.7% increase, which may cause further financial worries for employers.

(Source: adapted from https://www.ndna.org.uk/NDNA/News/Latest_news/2020/Minimum_wages_to_rise_by_inflation_in_April.aspx)

Extract B

What is the true cost of the food delivery service?

The food delivery industry has boomed in recent years. Just Eat, Uber Eats and Deliveroo all offer very similar services – third-party food delivery firms that take up to 30% of the price of restaurant meals and deliver them to customers within a certain radius. The average spend per customer is around £15 with a £5 delivery fee, about five times more expensive than cooking at home and the same price as eating in the restaurant. Cash rich, time poor professionals increasingly turn to food delivery.

Food delivery comes with many layers of packaging. In the UK, there are 200 million meals annually with around 1.4 billion individual pieces of plastic for heat retention and protection when travelling, but does it really have to be plastic? People tend to order more food, often high in fat, sugar and salt, and don't even have to get up from their sofa.

But there are concerns that the delivery firms are exploiting employees who have no alternative. There is an issue of low pay and informal contracts. Delivery drivers are classed as 'independent contractors', and therefore not subject to some employment rights including a guaranteed minimum wage, sick pay, pensions or holiday pay. Drivers are paid either a flat hourly rate, or a fee per delivery. Factors such as delivery distance, speed, how busy it is and whether there are multiple drop-offs are all factored into how much a driver is paid. Deliveroo says its wages amount to around £10 per hour, but drivers say that during 2020 their pay has been as low as £1 per hour. Drivers are not paid extra for petrol or to maintain their vehicles. Many drivers are recent immigrants or students, who do not have property or savings to fall back on.

The government could address this with widening minimum pay legislation to contracted workers, by setting codes of practice, or by setting recommended wage targets. Furthermore, there are health and safety issues for workers. Vehicle safety checks, length of shifts and safety equipment are of concern. However, there are still people who take benefit from working flexibility.

(Source: adapted from https://www.theguardian.com/australia-news/2020/oct/25/home-food-delivery-what-is-the-most-ethical-way-to-order-in and https://digitalcommons.molloy.edu/cgi/viewcontent.cgi?article=1043&context=bus_fac)

Extract C

Integration in the third-party food delivery industry

The Competition and Markets Authority (CMA) is watching carefully to prevent any one firm having complete control of the food delivery industry. Just Eat, the market leader, agreed to merge with successful Dutch firm Takeaway.com in 2020, creating a new European leader by revenues. It also bought Grubhub in the US, with 20 million active users. Just Eat uses an aggressive pricing strategy, undercutting delivery fees below the average cost of other firms in the market, that will force them to merge in order to gain some economies of scale.

Amazon, having failed with its own delivery company Amazon Restaurants in 2018, has bought 16% of Deliveroo. The CMA took over a year to agree to the partial integration, on the argument that Deliveroo would close down without external investment. Amazon has unique expertise in marketing, increasing customer share and, most importantly, efficiency in delivering things. Food delivery is often uneconomical because a single household puts in a single order from a single restaurant at any one time. Tech companies such as Amazon can improve the business: once a meal has been ordered, an app often moves that restaurant to the top of the rankings for that neighbourhood, in the hope of getting a second and third delivery.

So why do restaurants turn to these delivery firms? The sheer volume of customers these delivery firms can hold makes it a difficult deal to turn down. But resentment from small business restaurant owners, angry at being wholly dependent on tech companies, is growing. Most restaurants would prefer that customers come in and pick up their orders themselves because they do not have to pay the 30% commission. Restaurant profit margins are small, and the effects of a 20% fall in the external value of the pound since 2016 on food costs are significant, given that over half of their food and drink is sourced outside the UK.

(Source: adapted from https://www.ft.com/content/c20f6848-3c4b-11ea-a01a-bae547046735 https://www.ft.com/content/edf8a144-a101-4ef8-80e3-7d2f1565d35c and https://www.thisismoney.co.uk/money/markets/article-8138703/Uber-set-sell-takeaway-division-rival-Deliveroo-two-years.html and https://www.ft.com/content/c20f6848-3c4b-11ea-a01a-bae547046735 and https://www.ft.com/content/bed7c4d8-28c1-11ea-9a4f-963f0ec7e134 and https://www.economist.com/1843/2021/01/26/gulp-the-secret-economics-of-food-delivery)

(a) Using the information provided, explain **one** externality that arises in the food delivery market.

(5)

(b) With reference to Extract B, examine whether the demand for delivered food is price inelastic **and** income elastic.

(8)

(c) With reference to Extract C, discuss the likely effects of increasing integration within the food delivery market.

(12)

EITHER

(d) Evaluate the microeconomic and macroeconomic effects of a depreciation of the pound. Refer to restaurants or other food delivery services in your answer.

(25)

OR

(e) Evaluate the microeconomic and macroeconomic effects of significant increases in the minimum wage. Refer to restaurants or other food delivery services in your answer.

(25)

(Total for question = 50 marks)