

Write your name here

Surname

StemUp Model Solution

Other names

Pearson Edexcel
Level 3 GCE

Centre Number

--	--	--	--	--

Candidate Number

--	--	--	--

Economics B

Advanced

Paper 1: Markets and how they work

Tuesday 5 June 2018 – Afternoon

Time: 2 hours

Paper Reference

9EB0/01

You do not need any other materials.

Total Marks

Instructions

- Use **black** ink or ball-point pen.
- **Fill in the boxes** at the top of this page with your name, centre number and candidate number.
- Answer **all** questions.
- Answer the questions in the spaces provided
– *there may be more space than you need.*

Information

- The total mark for this paper is 100.
- The marks for **each** question are shown in brackets
– *use this as a guide as to how much time to spend on each question.*
- Calculators may be used.

Advice

- Read each question carefully before you start to answer it.
- Try to answer every question.
- Check your answers if you have time at the end.

Turn over ►

P52318RA

©2018 Pearson Education Ltd.

1/1/1/1/1/1




Pearson

Answer ALL questions.

SECTION A

Read the following extracts (A to D) before answering Question 1.

Write your answers in the spaces provided.

Extract A

The gourmet confectionery brand launched by Made in Chelsea star Jamie Laing

Having dreamed of becoming a real-life Willy Wonka since he was a boy, it was almost inevitable that Jamie Laing's first entrepreneurial endeavour and start-up firm would be in the confectionery market. Jamie is related to Sir Alexander Grant, the man credited with creating the first ever digestive biscuit when an employee of *McVitie's* in 1892.

5

Looking for a gap in the sweet market, Jamie saw an opportunity in the industry and started *Candy Kittens*, a producer of gourmet, premium priced, real fruit-based, gluten free sweets.

Candy Kittens was launched in February 2014 using £500 000 in loans from family and friends. Sales revenue was £700 000 in 2015 and £1.5m in 2016. It then launched a crowdfunding campaign to raise £300 000 for expansion.

10

Candy Kittens is currently stocked in more than 1,700 stores across the UK. Its range of natural sweets is now available in *Tesco*, *Waitrose*, *Sainsbury's*, *Topshop* and *Selfridges*, as well as several independent retailers and via its website.

There were nearly two billion packs of sweets sold in the UK last year, the top selling brands being *Haribo* and *Maynards*. According to a new report, confectionery sales in the UK, which include chocolate and sweets, are predicted to grow 8.6% between 2016 and 2019, despite fears about the high levels of sugar in sweets.

15

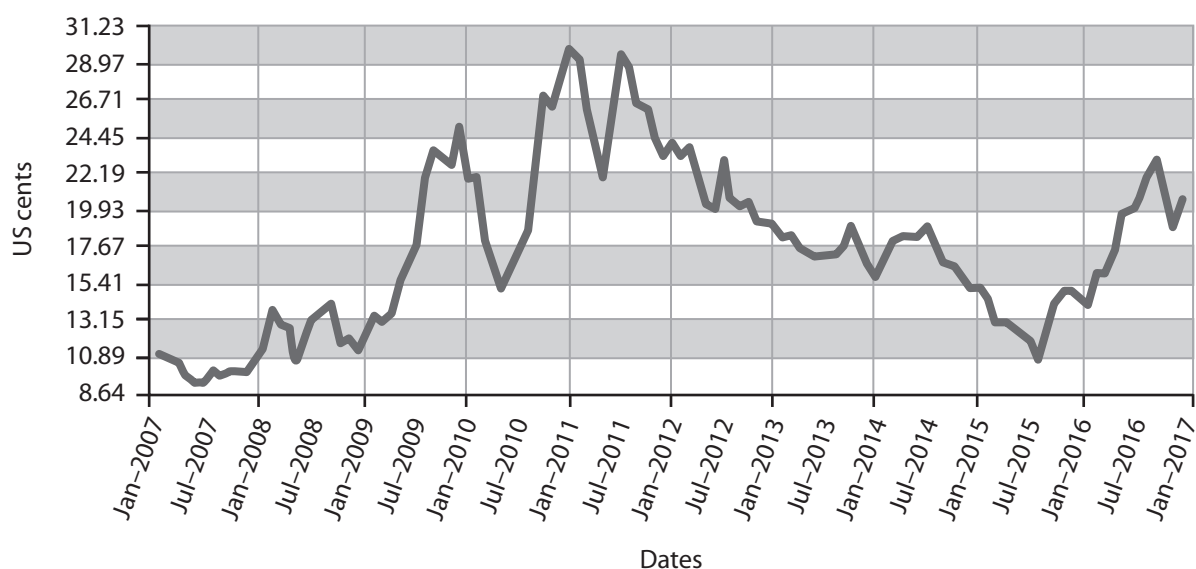
(Source: adapted from © William Reed Business Media Ltd 2017)

DO NOT WRITE IN THIS AREA

DO NOT WRITE IN THIS AREA

DO NOT WRITE IN THIS AREA



Extract B**Sugar price – US cents per pound of sugar**

(Source: © 2017 - IndexMundi)

Extract C**Half of UK start-ups fail within five years**

Research suggests that survival rates for start-up firms are lower than before the 2008 financial crisis. A start-up is a young firm that is just beginning to develop. It is usually small and initially financed by a limited number of founders or one individual.

More than half of new firms don't survive beyond five years. The top reasons given for failure include the UK tax system, a lack of bank lending and the cost of running a firm.

The biggest barrier to growth is the UK tax system, with 44% of firms citing it as their main concern; taxes include corporation tax and business rates. A further 38% stated a lack of bank lending. Other major concerns included late payments and cash flow problems.

Once their firms are up and running, owners are also struggling to plan for the long term. Some 61% of the 160 business owners surveyed said they lack confidence in their ability to achieve three years' consecutive growth.

(Source: adapted from © Copyright of Telegraph Media Group Limited 2017)

5

10



Extract D

Top five confectionery manufacturers in the UK 2015-2016

Confectionery manufacturer	Sales revenue (£)
<i>Mondelēz</i>	1 043.1m
<i>Mars</i>	648.1m
<i>Nestlé</i>	567.4m
<i>Lindt & Sprüngli</i>	127.9m
<i>Ferrero</i>	121.0m

(Source: © William Reed Business Media Ltd 2017)

DO NOT WRITE IN THIS AREA

DO NOT WRITE IN THIS AREA

DO NOT WRITE IN THIS AREA



- 1 *Candy Kittens'* sales revenue in 2016 was £1.5m. Jamie Laing is planning for an increase in sales revenue of 12% by 2019.

(a) Calculate the planned sales revenue for *Candy Kittens* in 2019. You are advised to show your working.

(4)

Planned revenue = original revenue + (original revenue × % increase)

Increase = £1.5m × 12% = £1 500 000 × 0.12 = £180 000

Planned revenue = £1 500 000 + £180 000

= £1 680 000

Planned sales revenue in 2019 = £1 680 000 (£1.68m)



According to a new report, confectionery sales in the UK are predicted to grow, despite fears about the high levels of sugar in sweets. (Extract A)

(b) Explain **one** external cost caused by the consumption of sweets.

(4)

An external cost is a cost imposed on third parties who are not involved in buying or selling the product. The overconsumption of sugar in sweets may create an external cost such as increased expenditure on healthcare.

Sugar is seen as a cause of obesity and related illnesses such as type 2 diabetes, and too much sugar can lead to tooth decay, especially amongst young people, who are big consumers of sweets.

These external costs are reflected in higher hospital and dental expenditure for the government through the NHS, which is paid for by taxpayers rather than by the consumers of sweets, so the social cost of sweets is greater than the private cost.



(c) Using Extract B, explain **one** supply factor that may have caused fluctuations in the price of sugar.

(4)

One supply factor is poor weather, such as drought or floods in major sugar producing countries like Brazil and India, which causes lower yields of sugar cane and sugar beet.

Extract B shows that the sugar price increased from approximately 11 US cents per pound in early 2009 to approximately 25 cents in early 2010, and it reached a peak of about 30 cents in early 2011 before falling back to about 11 cents in 2015.

Poor harvests are likely to have caused an inward (leftward) shift of the supply curve, which decreases the quantity of sugar and increases the price. When good weather returns, supply shifts back to the right and the price falls, and as the supply of an agricultural crop is price inelastic in the short run, these shifts cause large fluctuations in price.

DO NOT WRITE IN THIS AREA

DO NOT WRITE IN THIS AREA

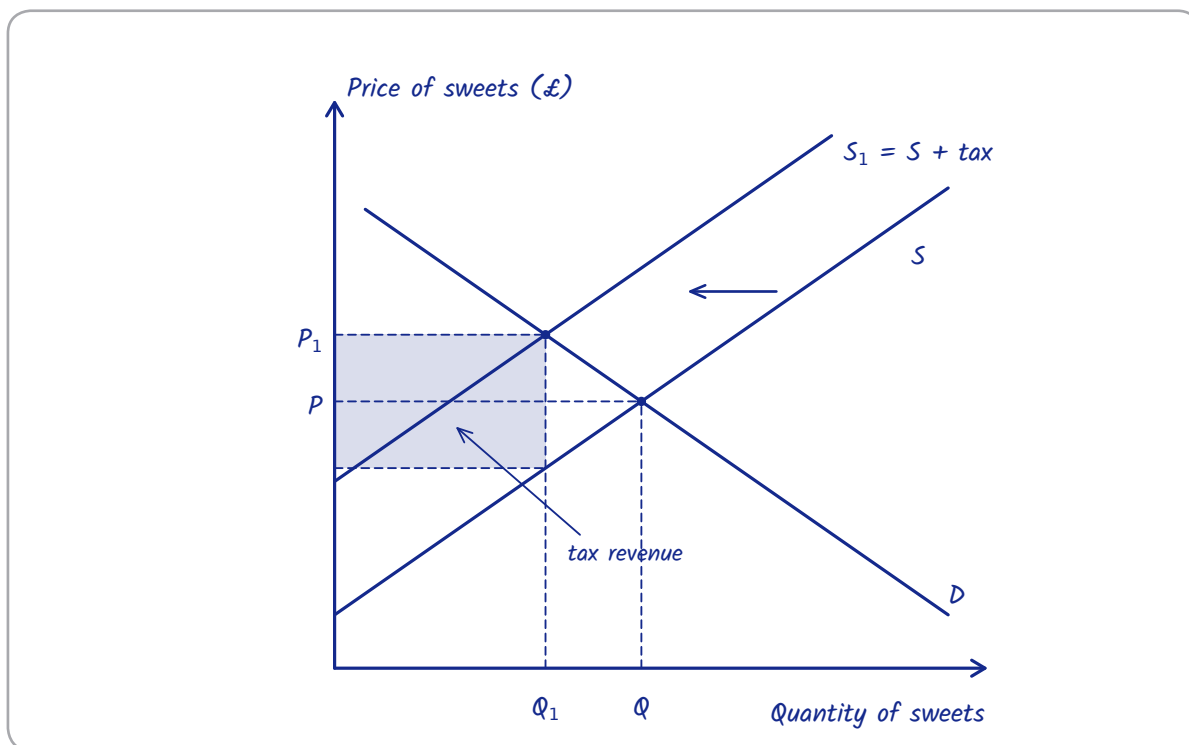
DO NOT WRITE IN THIS AREA



- (d) Research suggests that the biggest growth barrier for UK start-up firms is the UK tax system. (Extract C)

Using a supply and demand diagram, analyse the likely impact on the UK confectionery market of an increase in indirect taxes.

(6)



An indirect tax such as VAT at 20% is a tax on spending that raises firms' costs, as confectionery firms must pay it to the government on each pack of sweets sold.

This shifts the supply curve to the left (upwards) from S to S_1 , by the amount of the tax. The equilibrium moves from P, Q to P_1, Q_1 : the market price of sweets rises from P to P_1 and the quantity bought and sold falls from Q to Q_1 .

Higher costs mean that fewer sweets are produced, so firms' revenue and possibly employment in the UK confectionery market may fall. As demand for sweets is likely to be price inelastic, much of the tax is passed on to consumers as a higher price, while the shaded area shows the tax revenue for the government.

(e) Discuss the benefit that adding value brings to Candy Kittens.

(8)

Adding value is the difference between the price of a product and the cost of the inputs involved in making it. The more value a firm adds, the higher the price it can charge relative to its costs, and so the higher its profit margin per pack of sweets.

Candy Kittens has added value through its product features and benefits, as its sweets are gourmet, real fruit-based and gluten free. These features differentiate the product from mass-market competitors such as Haribo and Maynards, creating high demand from health-conscious consumers and those with a gluten intolerance.

Branding also adds value. Jamie Laing is attempting to build a brand of quality sweets, and the brand is linked to a TV personality from Made in Chelsea, which may appeal to some consumers. Candy Kittens also adds value by offering convenience, as customers can buy the sweets online through its website as well as in 1,700 stores. Together these factors make demand less price elastic and protect Candy Kittens from competitors that sell at a lower price, enabling it to charge a premium price.

However, building a brand is expensive and will mean high investment from Jamie if he is to compete with well-established brands such as Haribo. The product features of gluten free and real fruit may only appeal to a niche, small segment of the market, which restricts high volumes of sales. The premium ingredients also mean high production costs, so the value added may be smaller than expected, and the premium price charged may limit sales.

Overall, adding value is the main benefit that allows a small firm like Candy Kittens to compete, as its sales grew from £700 000 in 2015 to £1.5m in 2016, but the benefit depends on consumers continuing to value the brand enough to pay the premium price.



DO NOT WRITE IN THIS AREA

DO NOT WRITE IN THIS AREA

DO NOT WRITE IN THIS AREA

Handwriting practice lines consisting of eight horizontal dotted lines.



Jamie Laing used loans to start his firm. (Extract A)

(f) Assess the benefits of this source of finance for a new firm such as Candy Kittens.

(10)

A loan is a sum of money that is borrowed and has to be repaid, usually with interest, over a period of time. Loans come from a variety of sources, including banks, family and friends, and other individuals or firms. Jamie Laing borrowed £500 000 from family and friends to start Candy Kittens in 2014, rather than taking a bank loan.

A key benefit is that family members, such as his relative Sir Alexander Grant's family, may be willing to negotiate favourable repayment terms, such as a low or zero rate of interest or a repayment holiday until the firm is profitable, while traditional lenders such as banks will generally be less flexible. This keeps costs down and helps cash flow in the critical first years.

Jamie's business was new, with no trading record, so a bank loan may have been difficult to access, or the interest rates offered to him may have been high to reflect the risk. Extract C shows that 38% of start-ups cite a lack of bank lending as a concern, so loans from family and friends allowed Candy Kittens to start when bank finance may not have been available.

Using a loan also enables Jamie to maintain control of the firm, unlike other sources of finance such as venture capital or selling shares, where investors would own part of the firm and take a share of the profits. Once the loan is repaid, Jamie keeps all of the future profits, which matters as sales revenue more than doubled to £1.5m in 2016.

However, interest is a cost to the business, which reduces profit. Repayments have to be made regardless of the firm's cash flow position, which could be a problem for a start-up with volatile costs, such as sugar prices (Extract B). Bank loans often have to be secured against assets, which may result in a loss of personal assets if the firm fails, and more than half of new firms do not survive beyond five years.



Taking a loan from family and friends may also damage close relationships if the firm struggles to repay, and this may affect the operations and future financing of Candy Kittens. There are other sources of finance which may be more suitable, such as crowdfunding, which Jamie successfully used at a later date to raise £300 000 for expansion without taking on debt.

Overall, the benefits of the loan were significant for Candy Kittens, as it provided a large sum of £500 000 on flexible terms when bank finance was hard to obtain, while letting Jamie keep full control. The extent of the benefit depends on the repayment terms agreed and on the firm generating enough cash to repay it, so loans are most beneficial to a new firm when combined with other sources such as crowdfunding as it grows.



(g) Assess the extent to which barriers to entry may restrict the growth of Candy Kittens.

(12)

Barriers to entry are obstacles, such as high start-up costs, that prevent new firms from easily entering or growing in an industry. Barriers make a market less contestable and may include high set-up costs, high sunk costs, economies of scale, pricing strategies and strong brand names.

The largest confectionery firm, Mondelēz, with sales revenue of £1 043.1m, is likely to benefit from economies of scale, such as bulk-buying sugar and using mass production, giving it lower average costs which Candy Kittens, with sales of only £1.5m, may be unable to match. This means the large firms can sell at lower prices and still make a profit, restricting Candy Kittens' ability to grow its market share.

Firms such as Nestlé and Mars are well-established brand names with high brand loyalty. Established brands often have much larger budgets for advertising than new arrivals in a market, and they may secure the best shelf space in supermarkets. The top five manufacturers had combined sales of over £2.5bn, so they may also use pricing strategies such as predatory or limit pricing to undercut new entrants, which could force Candy Kittens out of the market or limit its growth to a small niche.

However, the barriers to entry may not be significant. Candy Kittens increased its sales revenue from £700 000 to £1.5m between 2015 and 2016, more than doubling in one year, which suggests barriers have not stopped its growth. It has succeeded in establishing its brand in the sweet market, with its products stocked in more than 1,700 stores, including Tesco, Waitrose and other major retailers.

Candy Kittens has overcome barriers through innovation and by targeting a niche segment of the market with its real fruit, gluten free sweets, so it is not competing head on with the mass-market brands. There is also no evidence of high sunk costs such as high start-up costs or high R&D in the confectionery market, as Jamie started



with only £500 000, and the market is predicted to grow by 8.6% between 2016 and 2019, leaving room for new firms to grow.

Nevertheless, the major players may have sufficient market power in the form of brand loyalty and economies of scale to protect themselves from new competitors like Candy Kittens in the long term. If Candy Kittens tries to move beyond its niche into the mass market, these barriers will become much more important.

Overall, barriers to entry restrict the growth of Candy Kittens only to a limited extent in the short run, because its differentiated product and celebrity brand let it avoid direct competition. The extent depends on how the large firms respond: if they launch their own gourmet ranges, their economies of scale and advertising budgets could seriously limit Candy Kittens' growth.



(h) Using Extract C, assess the extent to which cash flow forecasting is important to the survival of a new start-up business such as Candy Kittens.

(12)

A cash flow forecast is an estimate of the amount of money expected to flow into and out of the firm over a future period, usually month by month. Positive cash flow is essential to the survival of a firm, as it needs cash to pay suppliers, wages and loan repayments when they fall due.

Cash flow forecasting is particularly important to new start-ups, who may struggle to obtain new sources of finance when cash flow is a problem, as 38% of firms in Extract C cite a lack of bank lending. In the report, late payments and cash flow problems were among the main reasons for business failure, and more than half of new firms do not survive beyond five years. A forecast helps a start-up like Candy Kittens to spot shortfalls in cash in advance, so it can arrange an overdraft or delay spending before it runs out of cash.

Sugar prices are volatile (Extract B), rising from about 11 to about 30 US cents per pound between 2009 and 2011, which may cause difficulties in predicting cash outflows and affect the liquidity of the firm. Suppliers in the confectionery trade who do not get paid on time may stop supplying the business. Tesco and Waitrose have monopsony power and may delay payments to small suppliers such as Candy Kittens, so a forecast that plans for these delays is vital. If a firm runs out of cash and is not able to obtain new finance, it may become insolvent even if it is profitable.

However, no forecast is ever 100% accurate, and forecasting may be particularly difficult for new firms lacking experience in financial management and with no past sales data. A cash flow forecast can be affected by external factors, for example government regulation such as a sugar tax, which may make the forecast unreliable.

Other factors may be more important to the survival of start-ups. The report suggests that the biggest growth barrier is the UK tax system, cited by 44% of firms, followed



by a lack of bank lending (38%). A forecast cannot remove these problems, although it can help a firm plan for tax payments. Survival also depends on demand for the product and good management.

Overall, cash flow forecasting is very important to the survival of a start-up such as Candy Kittens, especially given volatile sugar prices and late payments from powerful supermarkets. Although cash flow forecasting is an integral part of any successful firm's management, it must be used in conjunction with other management tools, such as budgeting and securing finance, and regularly updated to be effective.

(Total for Question 1 = 60 marks)

TOTAL FOR SECTION A = 60 MARKS



DO NOT WRITE IN THIS AREA

DO NOT WRITE IN THIS AREA

DO NOT WRITE IN THIS AREA

BLANK PAGE



SECTION B

Read the following extracts (E and F) before answering Question 2.

Write your answer in the space provided.

Extract E

Cycling and walking investment strategy

The government's cycling and walking strategy aims to encourage people to cycle and walk more. The long-term goal, up to 2040, is that cycling and walking should be the natural choice for shorter journeys such as the commute to school, college or work. It aims to tackle congestion and improve physical and mental health.

5

According to a study, traffic congestion is a negative externality and could cost the UK economy more than £300bn over the next 16 years. It predicts the annual cost of congestion in the UK will rise 63% by 2030 to £21bn, with serious consequences for national and local economies, businesses and citizens. The findings from this study anticipate a significant increase in the demand for road travel across the country over the next 16 years and advises that cities need to be more innovative in their approach to tackling the gridlock.

10

Chris Boardman, the 1992 Olympic champion and policy adviser for British Cycling, said "far more ambition" was needed if the UK was to create a cycling and walking culture to rival countries like Denmark and Holland. Mr Boardman said: "The truth is that without sustained funding, this strategy won't be worth the paper it's written on."

15

Government strategy includes the ambition of doubling the number of people using bikes by 2025. To promote healthier journeys to work, the government introduced the cycle-to-work scheme in 1999, which allows employers to subsidise the purchase of bicycles by employees as a tax-free benefit. Since its introduction, over 1.1 million individuals have participated in the scheme. 2014 saw an 11.6% increase in uptake compared with 2013.

20

(Sources: adapted from © Crown copyright, Copyright © CTC 2017, 2017
© institute for employment studies and © 2017 Hemming Group)

DO NOT WRITE IN THIS AREA

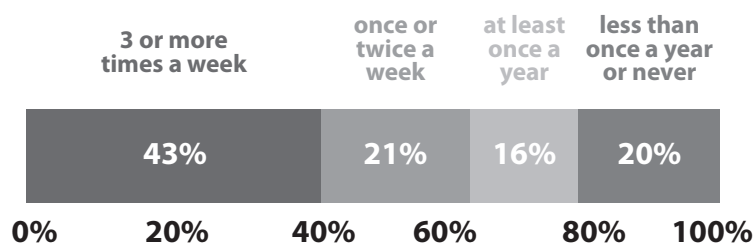
DO NOT WRITE IN THIS AREA

DO NOT WRITE IN THIS AREA

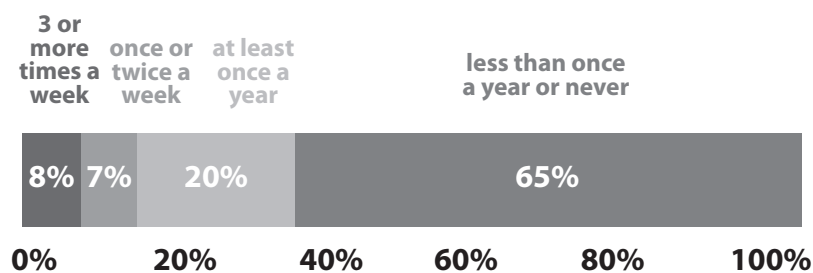


Extract F**Cycling and walking statistics (National Travel Survey, 2015)****Frequency of walking**

**64% of people aged 2+ walk for
20 minutes at least once a week.**

**Frequency of cycling**

**65% of people aged 5+ use a bicycle
less than once a year or never.**



(Source: © Crown copyright)



- 2 Evaluate the extent to which the government's cycling and walking strategy may impact the UK economy.

(20)

The government's cycling and walking strategy aims to make cycling and walking the natural choice for shorter journeys by 2040, and to double the number of people using bikes by 2025. It mainly aims to tackle congestion, which is a negative externality: a cost imposed on society, such as lost time, fuel and pollution, that is not paid for either by the producer or by the consumer of the car journey.

Consumers who take advantage of the cycle-to-work scheme benefit from financial support, as employers can subsidise the purchase of bicycles as a tax-free benefit. This lowers the price of cycling, encouraging people to use bicycles rather than cars for their commute, which may reduce congestion in the UK. Fewer cars on the road would reduce the predicted economic costs of congestion, which are expected to rise 63% to £21bn per annum by 2030, and more than £300bn over 16 years. Lower congestion means faster journeys for firms delivering goods, lowering their costs and making UK firms more competitive.

Cycling and walking can improve physical and mental health, and a healthier population puts less stress on the health service in the UK, freeing NHS resources for other uses. Healthier citizens should also improve firms' productivity, through reduced absenteeism, more people available to work and fewer sick days and benefits paid. Higher productivity could increase the UK's output and economic growth over the long term.

More bicycles bought through the cycle-to-work scheme may also benefit the UK cycle industry, raising demand for bike manufacturers, retailers and repair shops and creating more employment. The scheme appears to be popular, with over 1.1 million individuals having participated since 1999, and an 11.6% increase in uptake in 2014 compared with 2013. In addition, businesses may be unwilling to be based in an area where traffic congestion is a problem, so reducing congestion could attract firms and



investment to UK cities.

However, the impact of the strategy may be minimal. The number of people currently cycling is still very low, with 65% of people aged 5 and over riding a bicycle less than once a year or never, and only 8% cycling three or more times a week (Extract F).

Whilst the number of people joining the bicycle scheme is rising, 1.1 million participants over about 16 years is small compared with the UK workforce, so it may be insufficient to have a significant positive effect on congestion. Indeed, many of these people may not use the bicycles to cycle to work at all, but for leisure use at weekends.

Walking is already quite common, as 64% of people walk for 20 minutes at least once a week and 43% walk three or more times a week, so the scope for the strategy to change behaviour may be limited. Many journeys are also too long to walk or cycle, especially outside cities, and the weather in the UK may discourage cycling compared with Denmark and Holland.

There is an opportunity cost of government spending on the walking and cycling strategy: the money could perhaps be better invested in other schemes, such as public transport or road pricing, which may reduce congestion more effectively. Other local projects may be more successful, as the study anticipates a significant increase in the demand for road travel across the country over the next 16 years and advises that cities need to be more innovative in their approach to tackling the gridlock. If demand for road travel keeps rising, the strategy may only slow the growth of congestion rather than reduce it.

Chris Boardman argues that far more ambition is needed and that without sustained funding the strategy will not be worth the paper it is written on. This suggests that the impact depends on the level of funding for safe cycle lanes and awareness of the strategy. The benefits, such as improved health and productivity, are also long term and difficult to measure, so the effect on the UK economy in the short run is likely to be



small.

In conclusion, the strategy could have a positive impact on the UK economy by reducing the external costs of congestion, improving health and productivity and supporting the cycle industry. However, given the low current levels of cycling and the expected rise in road travel, its impact is likely to be modest unless it receives sustained funding.

Although the strategy is commendable, it depends on sufficient funding and awareness, and it may need additional measures, such as increased public awareness and other ways to combat congestion, to have a significant effect.

(Total for Question 2 = 20 marks)

TOTAL FOR SECTION B = 20 MARKS



DO NOT WRITE IN THIS AREA

DO NOT WRITE IN THIS AREA

DO NOT WRITE IN THIS AREA

BLANK PAGE



SECTION C

Read the following extracts (G to J) before answering Question 3.

Write your answer in the space provided.

Extract G

Brexit and the UK economy

When the first economic data following the June 2016 Brexit referendum was published, it showed no immediate signs of an economic collapse and the data was reassuring.

Britain's retail sales increased throughout 2016, which helped support growth and reassure businesses that were worried by the referendum result.

5

The pattern of growth continued to be broadly unaffected throughout 2016 but whilst service industries increased by 0.8%, in contrast output decreased in the other three main industrial groups of construction, agriculture and manufacturing.

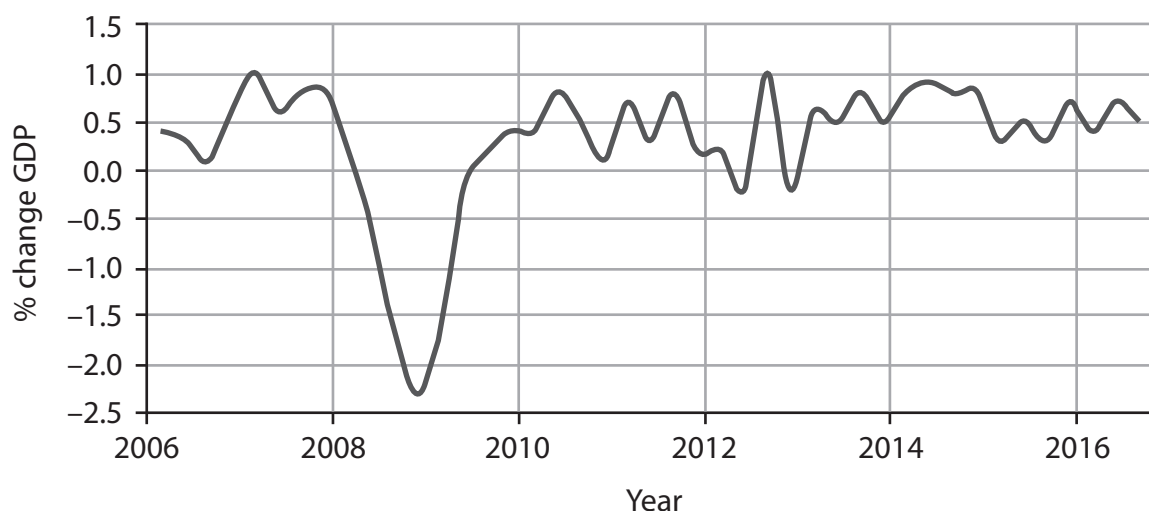
"Uncertainty around the future of the UK economy outside the European Union will continue to dampen business investment and consumer spending, as businesses hold back on hiring and making long-term investments, and as consumers postpone large spending decisions," said senior analyst Madhavi Bokil.

10

(Sources: adapted from © Telegraph Media Group Limited 2017 and © Crown copyright)

Extract H

UK GDP growth rate



(Source: © 2017 TRADING ECONOMICS)



DO NOT WRITE IN THIS AREA

Extract I

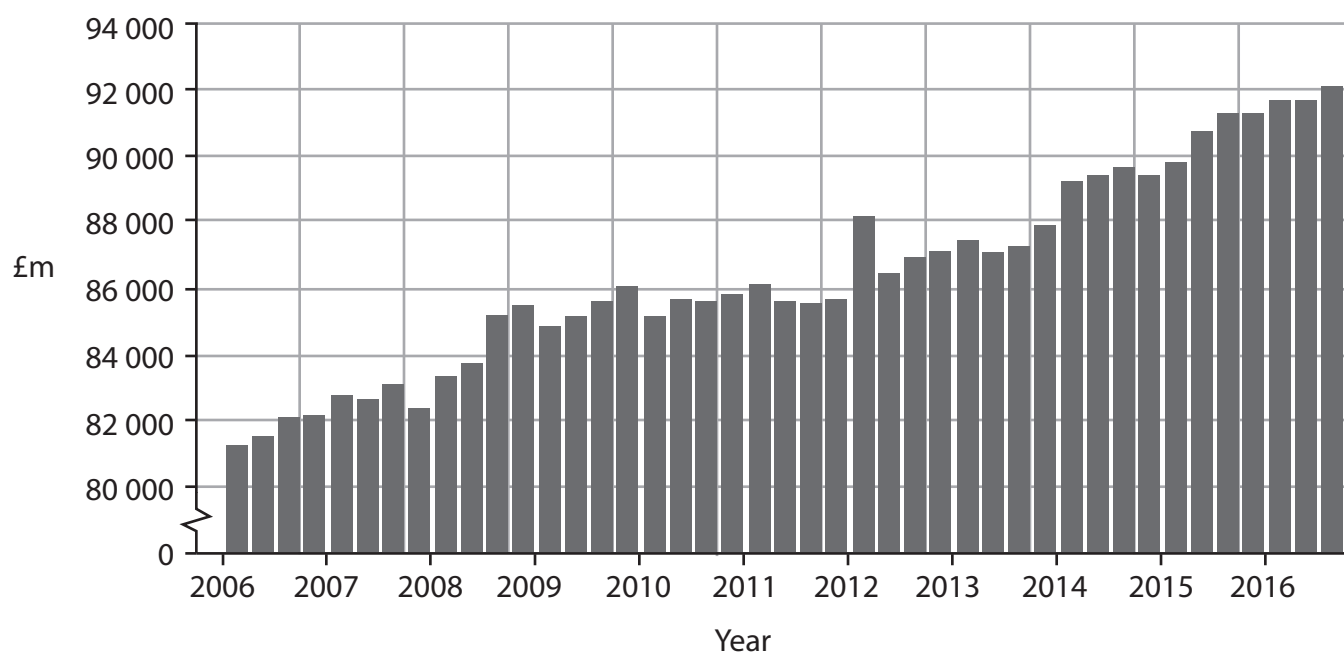
UK Bank of England interest (base) rates 2006-2016

Year	Interest (base) rate at end of year %
2006	5.0
2008	2.0
2010	0.5
2012	0.5
2014	0.5
2016	0.25

(Source: adapted from <http://www.bankofengland.co.uk/boeapps/iadb/Repo.asp>)

Extract J

UK government spending



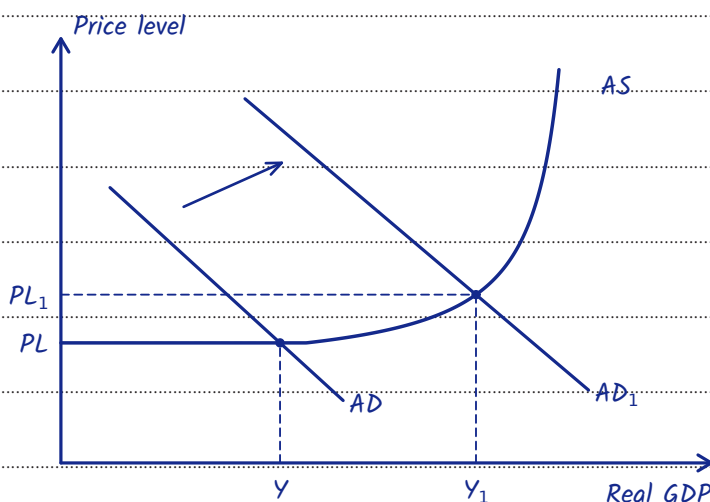
(Source: © 2017 TRADING ECONOMICS)



- 3 Using a suitable diagram, evaluate the importance of demand side policies in stimulating growth in the UK.

(20)

Demand side policies, which include monetary and fiscal policy, aim to influence aggregate demand ($AD = C + I + G + (X - M)$). To stimulate growth, expansionary monetary and fiscal policy are used to increase AD, shifting the AD curve to the right. In the diagram, an increase in AD from AD to AD_1 raises real GDP from Y to Y_1 , so output grows and jobs are created. As the economy moves closer to full capacity, the AS curve becomes steeper, so the price level rises from PL to PL_1 .



Fiscal policy uses government spending and taxation. Higher government spending injects expenditure into the economy to stimulate growth, create jobs and create a multiplier effect, as the income received is re-spent by households. Extract J shows government spending rising from about £81 000m in 2006 to about £92 000m in 2016, which may have supported this aim. Fiscal policy also involves changing taxation rates: lower income tax increases disposable income, encouraging consumer spending, which is the largest component of AD.

Monetary policy can also influence economic growth. Lower interest rates reduce the cost of borrowing for consumers and firms and reduce the reward for saving, which encourages consumption and investment and could increase AD. The Bank of England base rate was reduced from 5.0% in 2006 to 0.5% by 2010 and to 0.25% in 2016



(Extract I), which in theory should have increased consumer spending and increased growth in the UK. These policies are important during a recession or economic stagnation: the cuts helped the economy recover from the fall in GDP of over 2% in late 2008, and they may have been important after Brexit when there were concerns of an economic downturn and declining output in construction, agriculture and manufacturing (Extract G).

However, Extract H suggests that these policies had little impact on the long-term growth of the UK economy. Despite interest rates staying at 0.5% or below from 2010, quarterly GDP growth has generally stayed below 1%, and was even negative in 2012.

Extract J shows a continued increase in government spending, but again this shows little impact on growth rates. This may be because, with interest rates already close to zero, monetary policy cannot be cut much further, and confidence matters: uncertainty after Brexit will continue to dampen business investment and consumer spending, so firms and consumers may not borrow even when rates are low.

There can also be a trade-off in trying to promote growth by increasing AD, as it can cause inflation if the economy is close to full capacity. On the vertical part of the AS curve, a further shift in AD only raises the price level without increasing real output.

Some economists argue that higher government spending will not increase AD, because the government borrowing needed to finance it will crowd out the private sector by raising interest rates or reducing funds available for investment. Fiscal policy also has time lags and adds to the budget deficit and national debt.

An alternative strategy for improving economic growth is to use supply side policies, such as spending on education, training and infrastructure, which may improve productivity and efficiency in key sectors such as construction, agriculture and manufacturing. These shift the AS curve to the right, increasing the productive capacity of the economy, so long-run growth can occur without inflation, although they take a



long time to work.

In conclusion, demand side policies are important in stimulating short-run growth, especially when there is spare capacity, as in the recovery after 2009 and during the uncertainty after Brexit, when retail sales helped support growth. However, their importance is limited when interest rates are already at 0.25% and when the economy nears full capacity, and they cannot raise long-run potential growth on their own. Other factors may also affect the growth of the UK economy, such as the reactions of other countries and the remaining EU members as the UK leaves the EU. A combination of demand side and supply side policies is therefore needed to stimulate sustained growth.

(Total for Question 3 = 20 marks)

TOTAL FOR SECTION C = 20 MARKS
TOTAL FOR PAPER = 100 MARKS

Every effort has been made to contact copyright holders to obtain their permission for the use of copyright material. Pearson Education Ltd. will, if notified, be happy to rectify any errors or omissions and include any such rectifications in future editions.

