Please check the examination details below before entering your candidate information

Candidate surname: StemUp Model Solution

Other names:

Centre Number | Candidate Number

Pearson Edexcel International Advanced Level

Wednesday 30 October 2024

Afternoon (Time: 2 hours)

Paper reference **WEC14/01**

Economics

International Advanced Level
UNIT 4: Developments in the global economy

You must have:
Source Booklet (enclosed)

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 in Section A and Section B.
- Answer **TWO** questions in Section C.
- Answer the questions in the spaces provided
  – *there may be more space than you need.*

Information

- The total mark for this paper is 80.
- 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.
- Check your answers if you have time at the end.

Turn over ▶

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SECTION A

Answer ALL questions in this section.

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 ☒.

1 Between 2018 and 2022 New Zealand's national debt increased from $53.6 billion to $126.7 billion.

Which **one** of the following is the most likely effect of an increase in the national debt of a country?

- ☒ **A** An increase in crowding out
- ☒ **B** An increase in absolute advantage
- ☒ **C** A decrease in debt servicing costs
- ☒ **D** A decrease in the rate of inflation

(Total for Question 1 = 1 mark)

2 In 2023 the Government of Ghana removed fuel subsidies paid to fuel producers.

This is an example of which **one** of the following?

- ☒ **A** An interventionist strategy to promote economic growth and development
- ☒ **B** A reflationary fiscal policy to reduce inflationary pressures
- ☒ **C** A deflationary monetary policy to reduce inflationary pressures
- ☒ **D** A market-orientated strategy to promote economic growth and development

(Total for Question 2 = 1 mark)

3 In 2022 there was an overall deficit of $943.8 billion on the USA's balance of trade.

Which **one** of the following can be deduced from this information?

- ☒ **A** The value of consumption was lower than the value of saving
- ☒ **B** Government spending was greater than tax revenue
- ☒ **C** The value of imports was greater than the value of exports
- ☒ **D** Gross domestic investment was lower than capital flight

(Total for Question 3 = 1 mark)

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4 The table shows the maximum production possibilities for Country X and for Country Y using all available resources.

Country	Watches		Batteries
X	26 000	**OR**	13 000
Y	12 000	**OR**	12 000

Which **one** of the following can be deduced from this table?

- ☒ **A** Country X has a lower opportunity cost in the production of watches whereas Country Y has a lower opportunity cost in the production of batteries
- ☐ **B** Country Y has an absolute advantage over Country X in the production of watches and batteries
- ☐ **C** Country X has a comparative advantage over Country Y in the production of watches and batteries
- ☐ **D** Neither country will benefit from specialisation and trade

(Total for Question 4 = 1 mark)

5 In 2022 there were 10 million non-government organisations (NGOs) worldwide.

Which **one** of the following best describes the role of NGOs?

- ☐ **A** To provide loans to countries that experience temporary current account deficits on their balance of payments
- ☒ **B** To promote community-based development programmes to support economic growth and development
- ☐ **C** To maintain exchange rate stability by ensuring international monetary cooperation between countries
- ☐ **D** To set the rules for trade and to resolve trade disputes between countries

(Total for Question 5 = 1 mark)

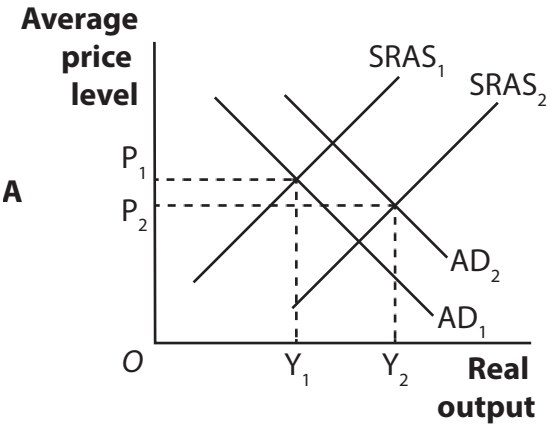
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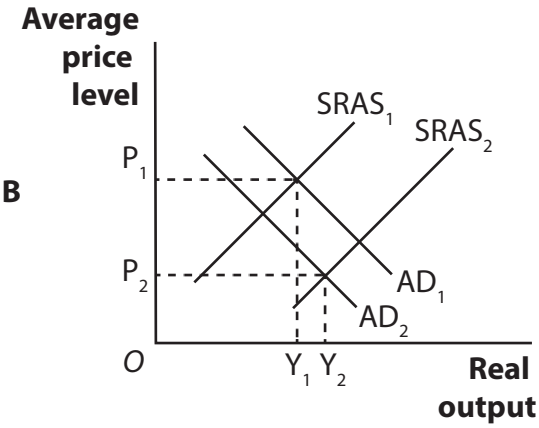
6 Which **one** of the following aggregate demand (AD) and short-run aggregate supply (SRAS) diagrams represents the likely effect of a substantial currency appreciation?

In each diagram the original equilibrium is represented by P_1 and Y_1.

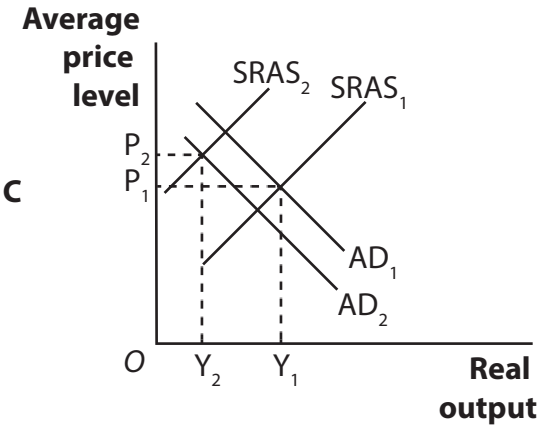
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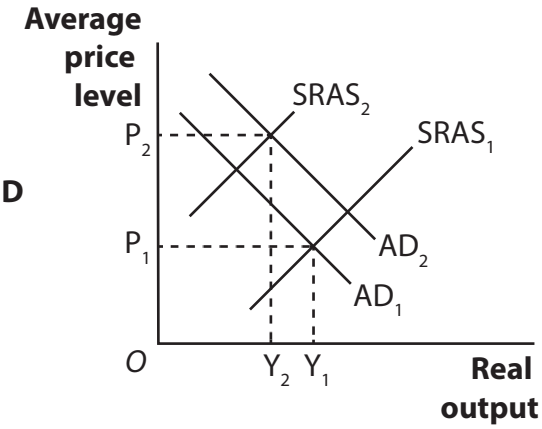
B



C



D



- ☒ **A**
- ☒ **B**
- ☒ **C**
- ☒ **D**

(Total for Question 6 = 1 mark)

TOTAL FOR SECTION A = 6 MARKS

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SECTION B

Study Figures 1, 2 and 3 and Extract A in the Source Booklet before answering Question 7.

Write your answers in the spaces provided on the following pages.

7 (a) With reference to Figure 1 and the second paragraph of Extract A, calculate the value of FDI in Vietnam in 2023. You are advised to show your working.

(2)

(b) Explain what is meant by 'absolute poverty' (Extract A, lines 10 and 11).

(4)

(c) With reference to Figure 2 and Extract A, examine **two** likely economic benefits to Vietnam of FDI inflows.

(8)

(d) With reference to Figure 3, analyse the likely impact of the change in the average monthly earnings of manufacturing employees on Vietnam's international competitiveness.

(6)

(e) With reference to the information provided and your own knowledge, discuss measures, **apart from** promoting FDI, that the Government of Vietnam might take to increase the country's international competitiveness.

(14)

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(a) With reference to Figure 1 and the second paragraph of Extract A, calculate the value of FDI in Vietnam in 2023. You are advised to show your working.

(2)

FDI in 2022 = $22.4 billion (Figure 1); FDI rose by 32.1% in 2023

FDI in 2023 = $22.4 billion × 1.321

= $29.59 billion (≈ $29.6 billion)

(b) Explain what is meant by 'absolute poverty' (Extract A, lines 10 and 11).

(4)

Absolute poverty is when a person's income is too low to meet basic necessities such as food, shelter, clothing, clean water and sanitation. The World Bank measures it as living on less than $2.15 a day, based on 2017 purchasing power parity (PPP) prices.

In Vietnam the proportion of the population living in absolute poverty fell from 9.2% in 2016 to 4.2% in 2022, a fall of 5.0 percentage points, as FDI raised national income.

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(c) With reference to Figure 2 and Extract A, examine **two** likely economic benefits to Vietnam of FDI inflows.

(8)

FDI is investment by a firm, usually a TNC, in productive assets such as factories in another country. Figure 2 shows Japan was the largest source of FDI inflows to Vietnam in 2022 at $3.4 billion, followed by Singapore at about $2.2 billion, and Extract A says Vietnam attracted 962 new FDI projects in the first five months of 2022 compared with 578 in the same period of 2021, and FDI rose by 32.1% in 2023.

Benefit 1: higher economic growth and employment. FDI is an injection into the circular flow of income. As investment is a component of aggregate demand, AD shifts right and, through the multiplier effect, real GDP rises by more than the initial investment. The TNCs moving production to Vietnam under the "China plus one" strategy need workers, so the derived demand for labour rises, unemployment falls and household incomes rise. This helps reduce absolute poverty, and higher incomes raise tax revenue that the Government can spend on infrastructure.

Benefit 2: higher productivity through technology transfer. TNCs from Japan and South Korea bring new capital, production methods and management practices, and often train local workers. This raises labour productivity and the skills of Vietnam's workforce, increasing the productive capacity of the economy, so LRAS shifts right and potential output increases, giving sustainable long-run growth. The capital inflow on the financial account also helps close the savings gap and foreign exchange gap.

However, the size of these benefits depends on the value of the multiplier and the amount of spare capacity; if the economy is near full capacity, the higher AD may mainly cause demand-pull inflation. TNCs may also repatriate profits to Japan or Singapore, which worsens the primary income balance on the current account, and if they bring their own skilled

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managers, local workers may only get low-skilled, poorly paid jobs. Weak infrastructure and high bureaucracy costs could also limit future FDI. Even so, with FDI rising by 32.1% in 2023, the benefits are likely to be significant.

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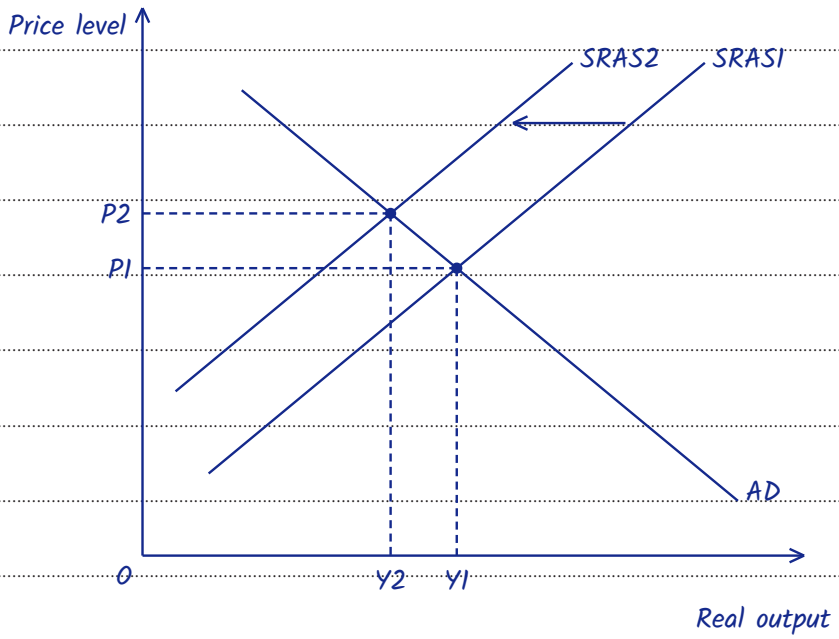
(d) With reference to Figure 3, analyse the likely impact of the change in the average monthly earnings of manufacturing employees on Vietnam's international competitiveness.

(6)

International competitiveness is the ability of a country to sell its goods and services in international markets at a price and quality that is attractive compared with those of other countries.

Figure 3 shows that average monthly earnings of manufacturing employees in Vietnam rose from about $180 in 2012 to about $300 in 2020, an increase of about $120, or roughly 67%. This is likely to reduce Vietnam's international competitiveness.

Labour is a major cost for manufacturers, so higher earnings raise unit labour costs, unless labour productivity rises by the same amount. Firms pass the higher costs on, so the price of Vietnam's exports rises. SRAS shifts left from SRAS1 to SRAS2 and the price level rises from P1 to P2.



As Vietnam's exports become relatively more expensive, foreign buyers switch to cheaper

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producers, so demand for its exports falls, especially as demand for manufactured goods is price elastic. At the same time, higher domestic prices make imports relatively cheaper, so imports rise. Net exports fall, which worsens the current account. Lower profits also leave firms with fewer funds to invest in innovation and quality, reducing non-price competitiveness too.

However, if productivity grew as fast as earnings, unit labour costs would not rise. Extract A also says unit labour costs in 2020 were still significantly lower than in China and Malaysia, so Vietnam is likely to remain competitive.

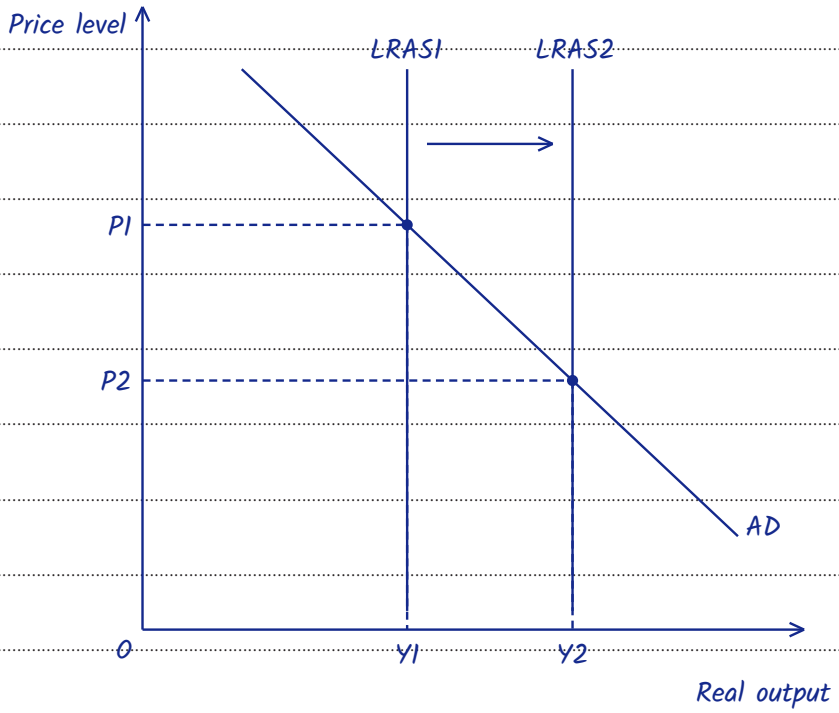
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(e) With reference to the information provided and your own knowledge, discuss measures, **apart from** promoting FDI, that the Government of Vietnam might take to increase the country's international competitiveness.

(14)

International competitiveness depends on relative unit costs, which are affected by productivity, wages and the costs of doing business, and on non-price factors such as quality and reliability. Extract A identifies weak infrastructure, high bureaucracy costs, a shortage of skilled labour and dependence on Chinese imports as threats, so the Government could use several measures.

1. Investment in physical infrastructure. Extract A says Vietnam "suffers from weak physical infrastructure, especially its electricity network". Government spending on power stations, the grid, roads and ports would reduce power cuts and transport delays, lowering firms' costs per unit and making delivery times more reliable. This raises productive capacity, shifting LRAS right from LRAS1 to LRAS2, so output can rise from Y1 to Y2 while the price level falls from P1 to P2, making exports cheaper.



2. Education and training. The economist quoted says "the challenge is the human capital", as a

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large factory may need 10 000 skilled workers. Spending on vocational training, technical colleges and apprenticeships would close the skills gap, raise labour productivity and stop wages for scarce skilled workers being bid up, so unit labour costs fall. It also improves occupational mobility, reducing the labour market inflexibility mentioned in the extract.

3. Reducing bureaucracy and deregulation. The costs of bureaucracy for businesses are high. Simplifying licences, tax filing and customs procedures, and deregulating or privatising state-owned firms, lowers barriers to entry and increases competition, so firms are forced to cut costs and become more efficient.

4. Incentives for exporters and domestic suppliers. Tax breaks, lower corporation tax or subsidies for exporters reduce costs and allow investment in new capital. Supporting domestic producers of raw materials would reduce dependence on imports from China, so supply chains are less at risk of disruption.

Evaluation. There is an opportunity cost: spending on infrastructure, education and subsidies means less for healthcare or other priorities, or higher taxes and borrowing. If the spending raises AD faster than capacity, demand-pull inflation could reduce Vietnam's price competitiveness in the short run. Infrastructure and education also involve long time lags, perhaps ten years or more before a newly trained workforce appears, so they do not help immediately.

Some measures may not be needed. The Finance Minister said infrastructure "was improving and becoming more modern", and labour "will be cheap for a long time", as unit labour costs are still well below China and Malaysia. There is a risk of government failure: subsidies may go to inefficient firms, and corruption may waste spending. Deregulation can harm workers, while

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breaking up large state firms may lose economies of scale. Competitiveness is also relative: rivals such as India and Indonesia are improving too.

Overall, education and training is likely to be the most important measure, because the skills shortage directly threatens productivity as more firms relocate, and it supports growth in higher value manufacturing. However, it works best combined with infrastructure investment and lower bureaucracy, as these address different causes of high costs.

(Total for Question 7 = 34 marks)

TOTAL FOR SECTION B = 34 MARKS

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SECTION C

Answer TWO questions from this section.

8 In 2022 an additional 2 500 trade restrictions were introduced globally.

Evaluate the likely effects of an increase in protectionist policies on the global economy.

(Total for Question 8 = 20 marks)

9 Between 2000 and 2022 globalisation was a significant factor that led to an increase in average incomes in Indonesia. However, income inequality within the country also increased during the same period.

Evaluate reasons why globalisation may lead to an increase in income inequality within a country. Refer to a country of your choice in your answer.

(Total for Question 9 = 20 marks)

10 In 2022 Pakistan's currency, the rupee, fell by 27% against the US dollar.

Evaluate factors that might cause a depreciation of the exchange rate of one currency against another currency. Refer to a developing country of your choice in your answer.

(Total for Question 10 = 20 marks)

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Write the answer to your FIRST chosen question here.

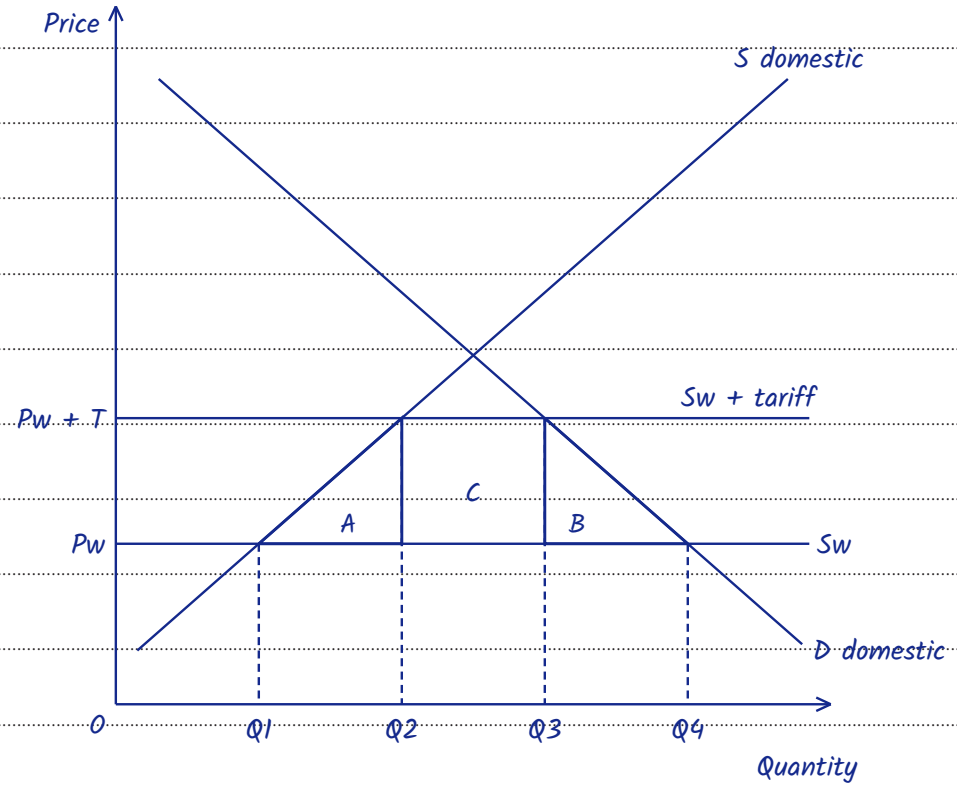
Indicate which question you are answering by marking a cross in the box ☒. If you change your mind, put a line through the box ☒ and then indicate your new question with a cross ☒.

Write the answer to your SECOND chosen question on page 22.

Chosen question number: **Question 8** ☒ **Question 9** ☐ **Question 10** ☐

Protectionism is the use of policies to restrict imports and protect domestic producers from foreign competition, such as tariffs, quotas, export subsidies, embargoes and administrative barriers. The 2 500 new trade restrictions introduced in 2022 followed the US-China trade war, in which the USA put tariffs on over $300 billion of Chinese goods and China retaliated.

A tariff raises the domestic price of an import from the world price Pw to Pw + tariff. In the diagram, domestic production rises from Q1 to Q2, domestic consumption falls from Q4 to Q3 and imports fall from Q1Q4 to Q2Q3. Consumer surplus falls; part goes to domestic producers and part (area C) is tariff revenue, but triangles A and B are a deadweight welfare loss to society.



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Effects on the global economy. First, protection distorts comparative advantage. Resources move from efficient foreign producers to less efficient domestic ones, so there is less specialisation and trade, and world output and living standards fall. The IMF estimated that trade fragmentation could cost up to 7% of global GDP in the long run.

Second, higher prices and less choice. Tariffs raise import prices and protected domestic firms face less competition, so they have less incentive to cut costs, leading to X-inefficiency. Higher costs of imported components push up firms' costs, shifting SRAS left, so there is cost-push inflation worldwide, while consumers lose access to goods that cannot be produced domestically, reducing real incomes.

Third, retaliation and trade wars. When one country imposes tariffs, others retaliate, so exports fall for everyone. Net exports and AD fall, and through the negative multiplier, global growth slows and unemployment rises in export industries. Global supply chains are disrupted, firms face uncertainty and FDI falls. In the 1930s the US Smoot-Hawley tariffs and retaliation contributed to a collapse in world trade.

Fourth, developing countries are hit hardest. Many rely on exports of agricultural goods and simple manufactures to developed countries, so barriers reduce their export earnings, growth and ability to reduce poverty, widening global inequality. There may also be trade diversion, where trade switches from the lowest-cost producer to a higher-cost one inside a trade bloc.

Evaluation. The size of the effects depends on the type and magnitude of the restrictions. 2 500 is a large number, but many may be small, targeted measures on specific products, or temporary, so their effect on total world trade of over $30 trillion may be limited. Trade wars

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may be short-lived if countries negotiate new agreements, and the WTO dispute settlement system can rule against illegal tariffs, though its appeals body has not worked since 2019, which weakens this.

There are also benefits for some economies. Infant industries in developing countries can be protected until they gain economies of scale and become internationally competitive, as South Korea did. Anti-dumping duties stop unfair competition from goods sold below cost, protecting jobs and output. Tariff revenue can be used to reduce inequality or improve infrastructure, and less long-distance trade may reduce transport emissions, a negative externality.

Much of the recent protection is also re-routing trade rather than reducing it. As firms adopt "China plus one" strategies, countries such as Vietnam and Mexico gain FDI and exports, so the global loss is smaller than it seems and some developing countries benefit. However, re-routing still adds to costs, as supply chains are no longer based purely on lowest cost.

Finally, the effects differ over time. In the short run, protection may save jobs in particular industries; in the long run, the loss of competition and dynamic efficiency, plus retaliation, is likely to reduce growth, so the costs grow.

In conclusion, an increase in protectionist policies is likely to harm the global economy overall, through higher prices, lower world output and slower growth, with developing countries suffering most. The most significant effect is retaliation, because it turns a small gain for one country into a loss for all. The size of the damage depends on whether restrictions are temporary and targeted, such as anti-dumping duties, or the start of a wider trade war, which the WTO must work to prevent.

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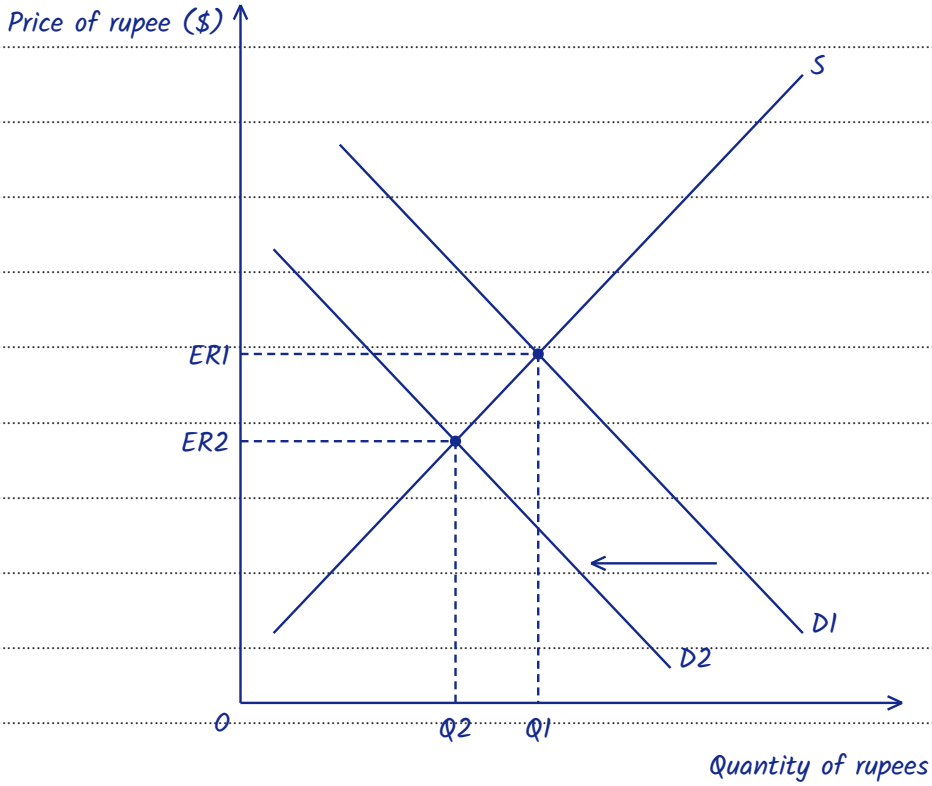
Write the answer to your SECOND chosen question here.

Indicate which question you are answering by marking a cross in the box ☒. If you change your mind, put a line through the box ☒ and then indicate your new question with a cross ☒.

Chosen question number: **Question 8** ☐ **Question 9** ☐ **Question 10** ☒

A depreciation is a fall in the value of a floating exchange rate against another currency, caused by a fall in demand for the currency and/or a rise in its supply on the foreign exchange market. In 2022 Pakistan's rupee fell by 27% against the US dollar, so each rupee bought fewer dollars and imports became more expensive.

In the diagram, a fall in demand for rupees shifts demand from D1 to D2, so the price of the rupee in dollars falls from ER1 to ER2 and the quantity traded falls from Q1 to Q2. An increase in the supply of rupees, a rightward shift of S, has the same effect on the exchange rate.



1. Relative inflation rates. Pakistan's inflation rose above 20% in 2022, far higher than in its trading partners. Its exports, such as textiles, became less price competitive, so foreign demand

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for them, and so for rupees, fell. Imports became relatively cheaper, so Pakistanis sold more rupees to buy dollars, increasing supply. Purchasing power parity theory predicts that a currency depreciates by roughly the inflation differential in the long run.

2. Current account deficit. Pakistan imports most of its oil, and oil prices rose sharply in 2022, so its import bill rose and the current account deficit reached about $17 billion in 2021/22. A persistent deficit means more rupees are supplied to pay for imports than are demanded to buy exports, so the rupee falls. Pakistan relies on primary and low value-added exports with volatile prices, which makes this worse.

3. Relative interest rates. In 2022 the US Federal Reserve raised its interest rate from near zero to over 4%. US assets became more attractive, so hot money flowed out of emerging economies like Pakistan into dollars, reducing demand for rupees and increasing their supply. The strength of the US economy meant the dollar appreciated against most currencies.

4. Confidence, speculation and debt. Pakistan's foreign currency reserves fell to only about $3 billion by early 2023, with large external debt repayments due, and it needed an IMF bailout. Political instability in 2022 and the severe floods damaged confidence. Speculators expecting a further fall sold rupees, and capital flight and lower FDI reduced demand, so expectations became self-fulfilling. The State Bank of Pakistan could not keep buying rupees to support the currency with such low reserves.

Evaluation. The factors interact, so the 27% fall was caused by a combination of them rather than one alone. However, their importance differs over time. Relative inflation and the current account mainly affect the exchange rate in the long run, while interest rates and speculation cause the large short-run movements, because daily financial flows are far larger than trade

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flows.

The current account alone is often not decisive. Many countries run deficits for years without a large depreciation if they attract enough capital inflows on the financial account. The USA has a large current account deficit but the dollar appreciated in 2022. Similarly, Japan's national debt of over 230% of GDP has not caused a collapse in the yen, because investors trust its government. What matters is confidence in the underlying strength of the economy.

Different factors matter for different developing countries. For commodity exporters such as Chile, a fall in copper prices is the key factor, whereas for Pakistan, an energy importer with low reserves, confidence and the ability to finance debt were more important. The magnitude also depends on the exchange rate regime: a country with large reserves can intervene to limit a fall, as India did in 2022, when the rupee fell by about 10%, far less than Pakistan's.

Finally, central bank policy can offset these factors. Pakistan raised its policy rate sharply in 2022 and 2023 to attract inflows and reduce inflation, but higher rates slow growth, so they may not restore confidence if investors fear default.

In conclusion, the most significant factor causing depreciation for a developing country like Pakistan is a loss of confidence, driven by low reserves, debt problems and political instability, which triggers speculation and capital flight. High relative inflation and a current account deficit create the underlying weakness, while rising US interest rates acted as the trigger in 2022. The combination, rather than any single factor, explains why the rupee fell by as much as 27%.

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TOTAL FOR PAPER = 80 MARKS

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Pearson Edexcel International Advanced Level

Wednesday 30 October 2024

Afternoon (Time: 2 hours)

Paper reference **WEC14/01**

Economics

International Advanced Level

UNIT 4: Developments in the global economy

Source Booklet

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Sources for use with Section B

The economy of Vietnam

Figure 1 Foreign direct investment (FDI) in Vietnam, $ billions, 2014–2022

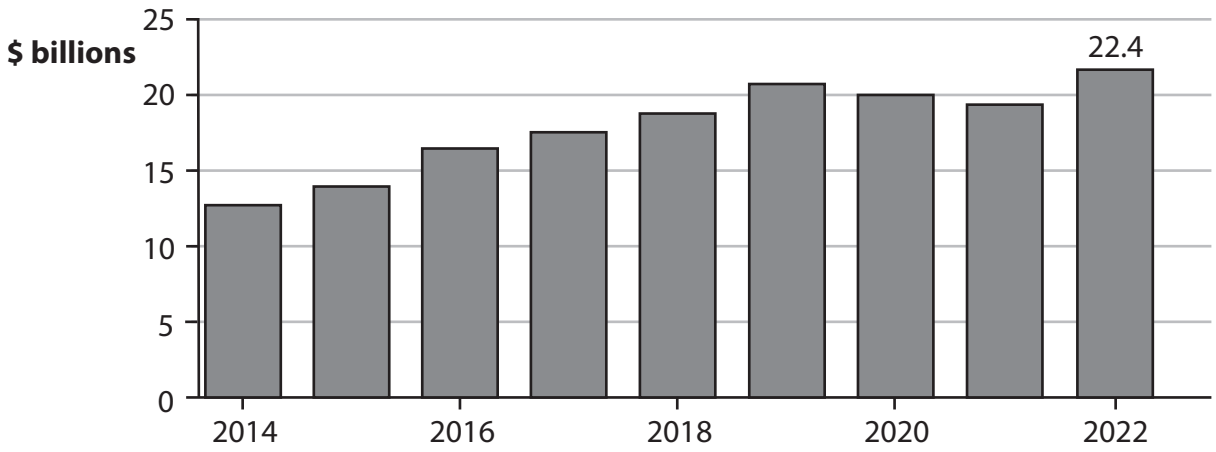
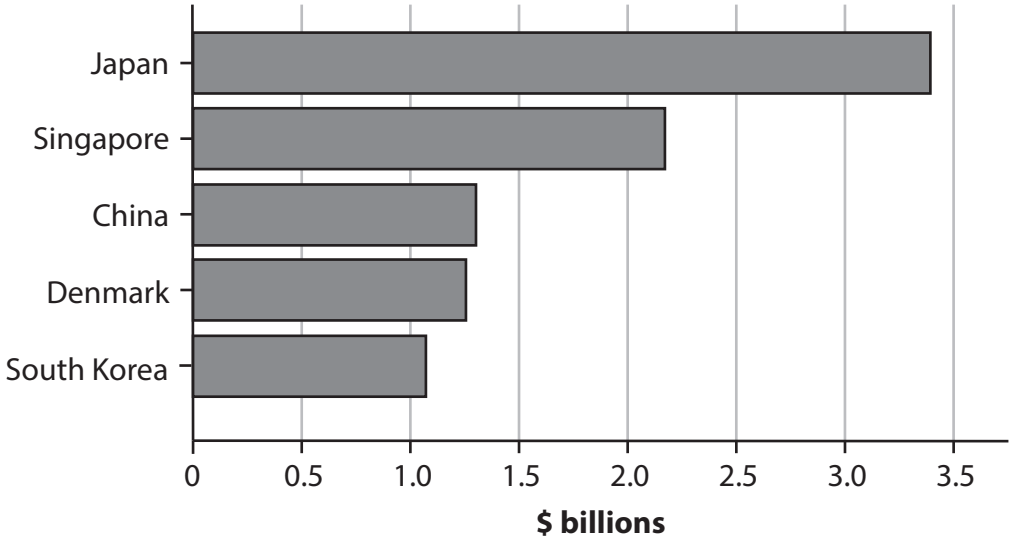
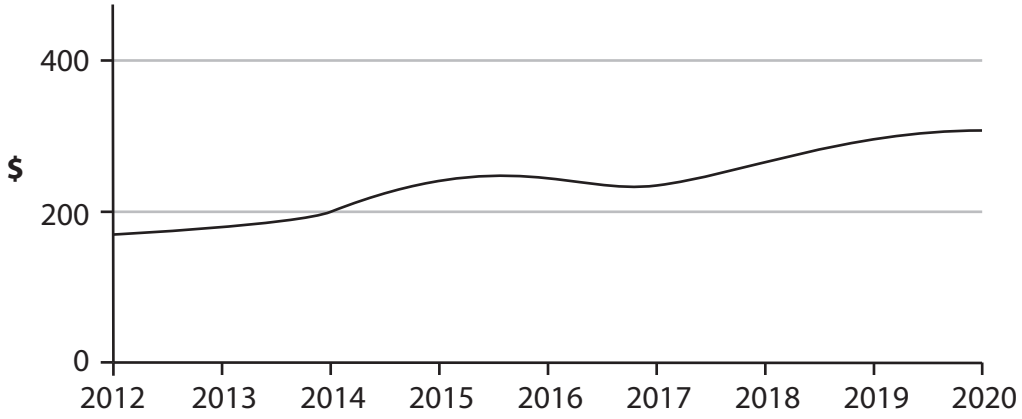


Figure 2 Largest sources of FDI inflows to Vietnam, $ billions, 2022



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Figure 3 Average monthly earnings of manufacturing employees in Vietnam, $, 2012–2020



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Extract A Economic challenges

Some of the major suppliers to global technology companies are based in Vietnam. Trade wars between the USA and China and the risks to businesses exposed by the global health crisis of 2020-22 are forcing manufacturing businesses to move out of China and to invest in Vietnam. The relocation of businesses to Vietnam is part of a growing 'China plus one' strategy aimed at expanding global supply chains.

Vietnam attracted 962 new FDI projects in the first five months of 2022. This compared with 578 projects in the same period in 2021. In 2023, FDI inflows into Vietnam increased by 32.1% compared with 2022. FDI inflows are an important source of national income for Vietnam. Between 2016 and 2022 the proportion of the population living in absolute poverty decreased from 9.2% to 4.2%.

However, there are risks and uncertainties for foreign manufacturing businesses investing in Vietnam. The country suffers from weak physical infrastructure, especially its electricity network. In addition, the costs of bureaucracy for businesses are high. This is likely to have an impact on Vietnam's international competitiveness in the long-run.

Vietnam's Finance Minister said that the country's infrastructure was improving and becoming more modern. The country has an abundant supply of labour that will be cheap for a long time. In 2020 unit labour costs in Vietnam, although higher than in 2012, were still significantly lower than in China and Malaysia.

Nevertheless, the labour market in Vietnam is becoming inflexible. If manufacturing firms continue to shift operations to Vietnam there will be a shortage of skilled labour. One economist stated, "The challenge is the human capital. If you have to build a huge factory that needs 10 000 skilled workers, they need to come from somewhere."

Vietnam remains highly dependent on imports of raw materials from China. This means that Vietnam's supply chain is at risk if there are any disruptions to the flow of imports from China.

Whatever the doubts about infrastructure, bureaucracy, labour or other issues, few economists expect 'China plus one' growth to end soon. "The gates open, FDI comes in," said one existing entrepreneur, who is planning to make further investment in Vietnam.

Acknowledgements

Figures 1, 2, 3 and Extract A adapted from: FT, https://www.ft.com/content/29070eda-3a0c-4034-827e-0b31a0f3ef11