

OCR A-LEVEL ECONOMICS • H460

ECONOMICS



EXAM QUESTION PACK

AGGREGATE DEMAND AND AGGREGATE SUPPLY

SCORE

/259

PERCENTAGE

%

STEMUP

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Evaluate, with the use of an appropriate diagram(s), whether fiscal policy will always reduce a negative output gap.

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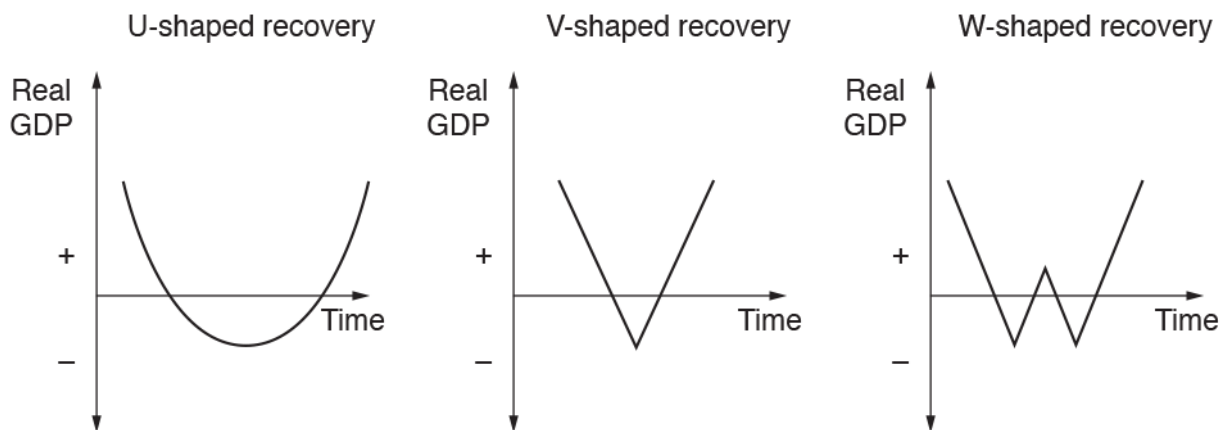
[25]

In the last two decades the Icelandic economy has experienced some significant changes in economic activity. One influencing factor has been changes in the standard rate of income tax. The rate was cut in a number of stages from 46% to 36% in 2006. Despite the lower income tax rate, government income tax revenue rose, allowing the government to spend more on the country's infrastructure. In 2009 and 2010 the income tax rate was increased.

In the period 2008 to 2011, the economy experienced a serious recession. The country's three largest banks were allowed to fail. It was the third largest bankruptcy in history and, according to the size of the economy, the biggest banking failure in history. The value of the country's stock market fell by 95%, the currency declined in value by 60%, unemployment increased by 8% and inflation rose to 12%.

From 2011 the economy has made a remarkable recovery. In 2014 its real GDP was US\$14.85bn and it grew by 4% in 2015, one of the fastest rates in Europe. Economists have developed an 'alphabet' of recoveries with the three most common types shown in Fig. 1.

Fig. 1 Different types of economic recovery



In 2015 the Icelandic government was paying back its loans to the International Monetary Fund early. It had removed capital controls and had reformed the country's financial sector. A number of the country's industries were expanding, most noticeably its tourist industry. Income from tourism can fluctuate significantly. In 2015 the total contribution of Iceland's tourist industry to the country's GDP was 23%. The impressive growth of Iceland's tourist industry was contributing to a fall in unemployment due to a rise in hotel construction, and an increase in infrastructure, although this was also putting pressure on house prices as people were buying them to rent out to tourists. In 2015 the unemployment rate was 5.3%, which was lower than in many European countries, but it was predicted to rise in 2016.

For a small country with a population of only 0.33 million in 2014, Iceland has a relatively high HDI value. Fig. 2 shows some details of the HDI values of six countries.

Fig. 2 The Human Development Index of six selected countries

Country	HDI ranking 2014	HDI value 2014	GNI per capita (US\$) 2014
Norway	1	0.944	64,992
Australia	2	0.935	42,261
Germany	6	0.916	43,918
USA	8	0.915	52,947
UK	14	0.907	39,267
Iceland	16	0.898	35,182

- 25 As Iceland's economy has grown, so has the country's aid for developing countries. In 2013, for instance, its foreign aid budget increased by 27.8%.

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Using Fig. 1, explain which type of economic recovery is likely to be most beneficial for an economy.

[3]

(b) Using information in the stimulus material, evaluate whether Iceland would be likely to experience a recession after 2015.

[8]

- 3 * Investment has fluctuated significantly in Poland in recent years. For example, it increased by 8.3% in 2008, fell by 1.5% in 2012 and grew by 5.9% in 2015.

Evaluate the extent to which the accelerator theory explains the level of investment in an economy.

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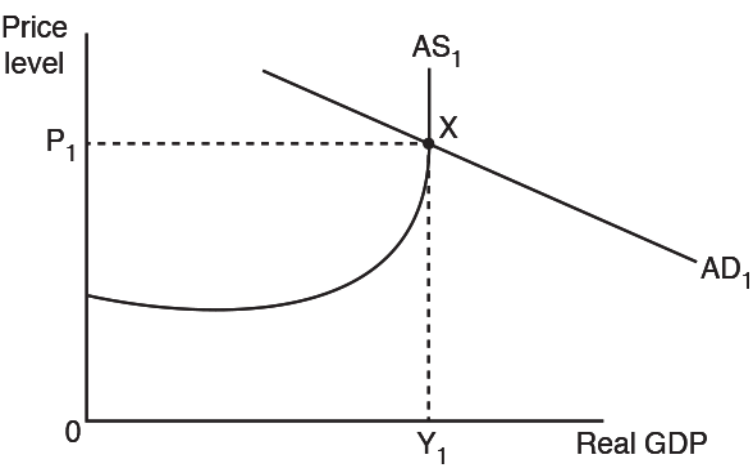
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- 4 A country's marginal propensity to import is 0.1, the marginal rate of taxation is 0.3 and the marginal propensity to consume is 0.8. What is the size of the country's multiplier?
- A 0.60
 B 0.83
 C 1.20
 D 1.67

Your answer

[1]

- 5 If an economy is operating at point X in the diagram below, which of the following best describes the impact of an increase in consumer expenditure?



	Economic Growth	Inflation	Unemployment
A	Decreases	Decreases	Decreases
B	Increases	Increases	Increases
C	Increases	Unchanged	Increases
D	Unchanged	Increases	Unchanged

Your answer

[1]

6 What is meant by the term 'negative output gap'?

- A Actual GDP is below potential GDP
- B Negative externalities resulting in over-production
- C The economy is operating beyond its production possibility frontier
- D Two consecutive quarters of negative economic growth

Your answer

[1]

7 Which of the following identifies the components of aggregate demand that are likely to be affected by an increase in household income?

	Consumption	Investment	Government spending	Net exports
A	/			
B	/	/		
C	/	/	/	
D	/	/	/	/

Your answer

[1]

8 An economy has three leakages from its circular flow of income – savings, tax and imports. Its national income multiplier rose from 2 to 2.5 between 2015 and 2018. Over this period its marginal propensity to save fell from 0.14 to 0.02 and its marginal rate of tax increased from 0.17 to 0.22. What was the change in the country's marginal propensity to import over this time period?

- A A fall from 0.19 to 0.16
- B A fall from 0.50 to 0.40
- C A rise from 0.69 to 0.76
- D A rise from 1.69 to 2.26

Your answer

[1]

9 Which of the following identifies a difference between the neo-classical and Keynesian approach to macroeconomic thinking?

	neo-classical	Keynesian
A	Aggregate supply is perfectly inelastic in the long run	There is an elastic section of the aggregate supply curve
B	Fiscal policy can affect real output in the economy	Fiscal policy cannot affect real output in the economy
C	Prices and wages are not always flexible	Prices and wages are always flexible
D	Unemployment is caused by demand side factors	Unemployment is caused by supply side factors

Your answer ☐

[1]

10 Please refer to insert **H460-03 June 2018, Olympic Games**, which can be downloaded separately and is also included with Question 31.

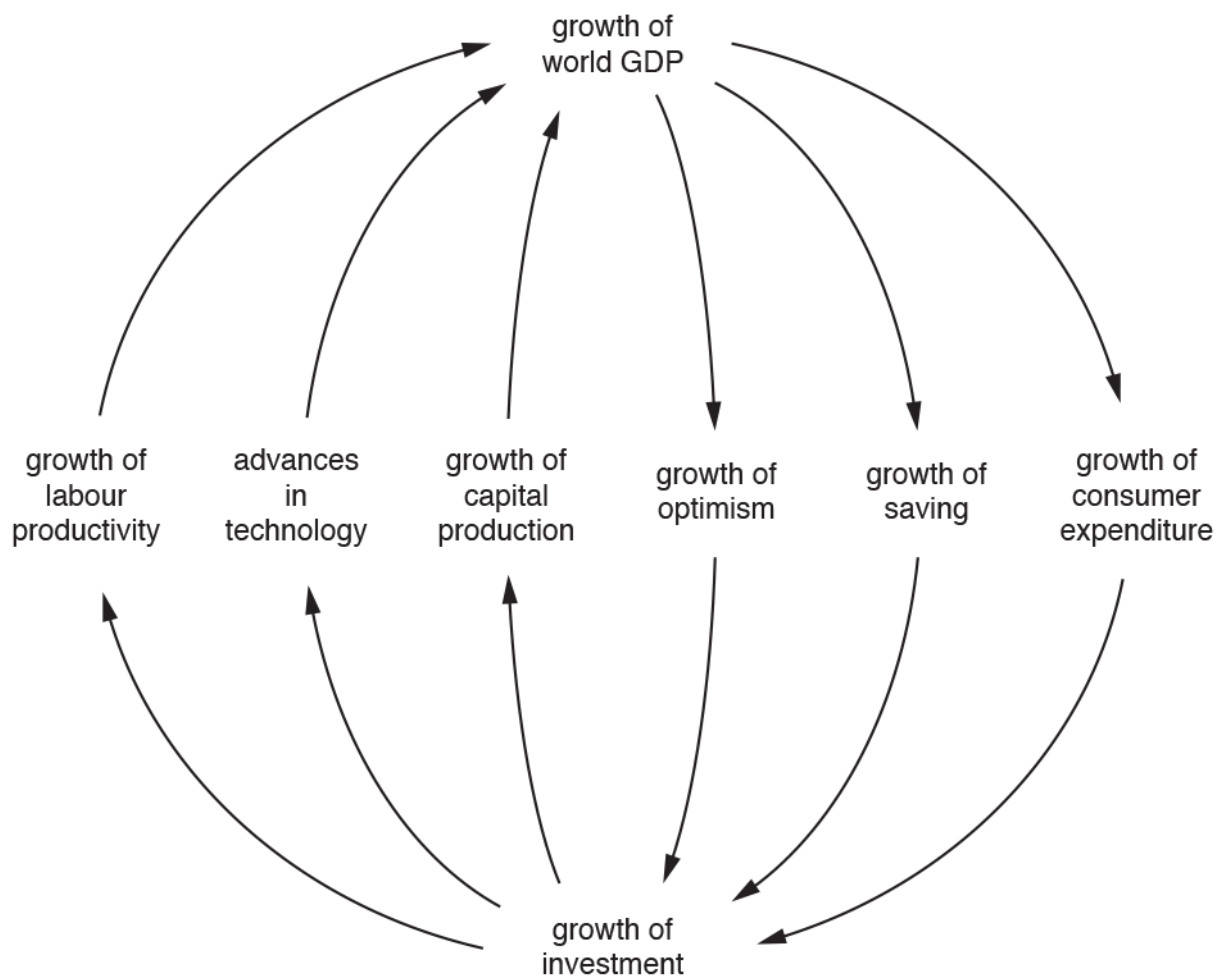
Using the data in Extract 2, explain what is meant by the multiplier effect of Olympics expenditure.

[2]

Trade wars were threatening the process of globalisation in 2018 and were restricting the ability of countries to exploit their comparative advantage and their absolute advantage. In the years before, advances in production and communication technology had lowered production and transport costs, had increased the ability of firms to move production around the world and increased the size of firms' markets.

World trade increased by 3.2% in 2017. This contributed to a growth in world GDP. Higher GDP can result in a virtuous circle as shown in Fig. 1.

Figure 1 A virtuous circle



While the benefits of globalisation are widespread, the costs are often concentrated in particular areas and among those unskilled workers who are geographically and occupationally immobile.

- 10 One of the reasons why the US government imposed tariffs on steel imported from China was to protect the jobs of US steel workers.

Some economists are also concerned that globalisation can result in governments engaging in tax competition to keep firms and skilled workers in the country and to attract foreign MNCs and

foreign skilled workers into the country. Table 1 shows government tax revenue and expenditure
15 for selected countries in 2017.

Table 1 Government tax revenue and government expenditure 2017

Country	Government tax revenue (US\$ billion)	Government tax revenue as a % of GDP	Government expenditure (US\$ billion)
China	2672	22.4	3146
Germany	1598	43.8	1573
India	249	10.2	330
Ireland	85	26.2	87
Russia	254	17.3	288
UK	984	38.4	1076
USA	3336	22.0	3991

International competition may, on the other hand, encourage governments to spend more on education, training and health care to increase productivity and so attract foreign direct investment. Table 2 shows the corporate tax rates and the foreign direct investment attracted by the same selected countries.

Table 2 Corporate tax rates and foreign direct investment 2017

Country	Average corporate tax rate (%)	Foreign direct investment per head (US\$)
China	25.0	1098
Germany	29.8	17 963
India	34.6	287
Ireland	12.5	295 400
Russia	20.0	3378
UK	19.0	30 852
USA	40.0	12 489

- 20 The UK economy is more affected by changes in the global economy than the USA. This is because it is a more open economy. The UK has a relatively high marginal propensity to import. Between 2016 and 2017, average UK household income rose from £26 300 to £27 400 while average household spending on imports rose from £4950 to £5280.

The growth of the emerging economies, including China and India, is having an impact on the UK.

- 25 For instance, Chinese steel firms have captured some of the UK's steel industry's market at home

and abroad. Indian MNCs produced more than £26 billion of goods and services in the UK in 2016 and employed more than 100 000 workers in the UK.

- (i) Using Table 1, explain which country's government made a negative contribution to the country's aggregate demand.

----- [2]

- (ii) Using Table 1, calculate Russia's GDP in 2017.

----- [2]

(b) Using information from the stimulus material, calculate the UK's marginal propensity to import in 2017.

[2]

12 * In 2018 the Australian government, concerned about the possibility of an economic downturn, used a number of policy measures intended to increase private sector investment.

Evaluate, with the use of an appropriate diagram(s), whether an increase in private sector investment will help a government achieve its macroeconomic objectives.

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[25]

- 13 * The Labour Party announced in 2014 that, if elected, it would restore the 50% income tax rate for high earners in the UK.

Evaluate, with the use of an appropriate diagram(s), whether UK macroeconomic performance would be strengthened by an increase in the top rate of income tax.

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14 What does the accelerator effect tell economists about the economic cycle?

- A A fall in injections will cause a more than proportionate decrease in real GDP
- B A fall in injections will cause a less than proportionate decrease in real GDP
- C Investment will be high when economic growth is high
- D Investment will be high when real GDP is high

Your answer

[1]

15 Which of the following represents a leakage from the circular flow of income?

- A Exports
- B Government spending
- C Investment
- D Savings

Your answer

[1]

16 How can an economy that is currently employing all its resources increase its output?

- A Improving the state of technology
- B Increasing consumption by lowering prices
- C Increasing the velocity of circulation of money
- D Redistributing income between factors of production

Your answer

[1]

17 An economy has the following leakages:

- Marginal propensity to save = 0.1
- Marginal rate of taxation = 0.2
- Marginal propensity to import = 0.2

Its government wants to raise its GDP from \$300bn to \$450bn. By how much should it increase its spending in order to achieve its objective?

- A \$15bn
- B \$60bn
- C \$75bn
- D \$150bn

Your answer

[1]

18 What is the accelerator effect?

- A An increase in aggregate demand causes a greater final change in real GDP
- B As economic growth pushes the economy towards full capacity the rate of inflation increases rapidly
- C Increases in expected demand will increase the level of investment in the economy
- D Sacrificing the production of consumer goods for capital goods in the short run can increase the rate of economic growth in the long run

Your answer

[1]

[15]

In the first decade of the twenty-first century China saw a significant increase in both income and wealth. In the current decade, however, its economic growth rate has slowed. At the start of 2016, China's president, Xi Jinping, said that the government would concentrate on supply-side reform. He mentioned that the government would no longer try to promote economic growth by just relying on fiscal and monetary policy measures. It would be placing more emphasis on long-term structural change rates rather than short-term stimulus.

In the past China has used short-term demand management to increase consumer expenditure and investment. This has led to an increase in government spending which has had implications for the country's budget position. Table 1 compares the gross domestic product (GDP), government revenue and government expenditure of the six largest economies in 2014.

Country	GDP	Government revenue	Government expenditure
China	10.4	2.3	2.4
France	2.8	1.5	1.6
Germany	3.9	1.7	1.7
Japan	4.6	1.5	1.8
UK	3.0	0.9	1.1
USA	17.4	3.0	3.5

Table 1 - GDP, government revenue and government expenditure in US\$ trillion of the six largest economies in 2014

The Chinese government is hoping that supply-side policy measures will increase the country's productivity. The UK economy has introduced a number of supply-side policy measures including deregulation, privatisation and tax cuts Fig.1 compares the UK's productivity growth with that of the six other G7 members. It shows after 2007 the gap between the actual growth in productivity and the predicted growth in productivity.

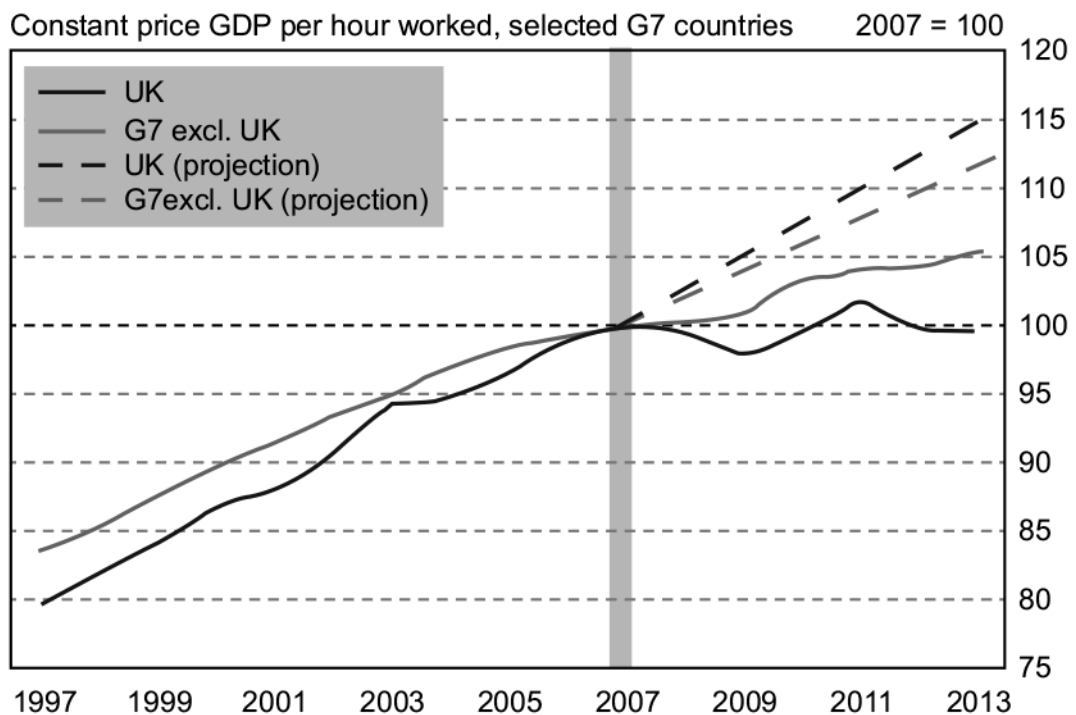


Fig. 1. A comparison of productivity growth in the UK and G7 1997 – 2013

Productivity is influenced by a number of factors including investment. In turn, there are a number of influences on investment including the level of savings. The amount of income saved varies from country to country. Some countries, including China have a relatively high average propensity to save. Others, including Denmark in recent years, have had a negative average propensity to save. Table 2 shows the average propensity to save of the G7 countries in 2014.

Country	Average propensity to save
Canada	0.05
France	0.15
Germany	0.09
Italy	0.05
Japan	0.02
UK	0.06
USA	0.05

Table 2 - The average propensity to save in the G7 countries in 2014

- (i) Using Fig.1, calculate how much greater the UK's productivity gap was than the G7's in 2013.

----- [1]

(ii) Using Fig.1, compare the trend in UK productivity and G7 productivity over the period shown.

----- [3]

(i) Explain how it is possible for a country to have a negative average propensity to save.

[2]

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For some years now the UK has had a deficit on both its budget balance and on the balance of the current account of its balance of payments. In 2015 the budget deficit fell to 4.1% of GDP. This was the lowest deficit, in percentage terms, since 2007 but it was noticeably higher than the historical average of 2.5% of GDP. In October 2016 the Chancellor of the Exchequer announced that he was abandoning the objective of achieving a budget surplus by 2020. He also said he was prepared to borrow for public sector investment in infrastructure.

Changes in the budget position can influence activity in the labour market. Fig. 1 shows the stocks of employment, unemployment, economic inactivity and migration and the flows between them. For instance, the stock of unemployment (the number of people unemployed at any particular time) is affected by flows into and out of unemployment (some people becoming unemployed while others stop being unemployed).

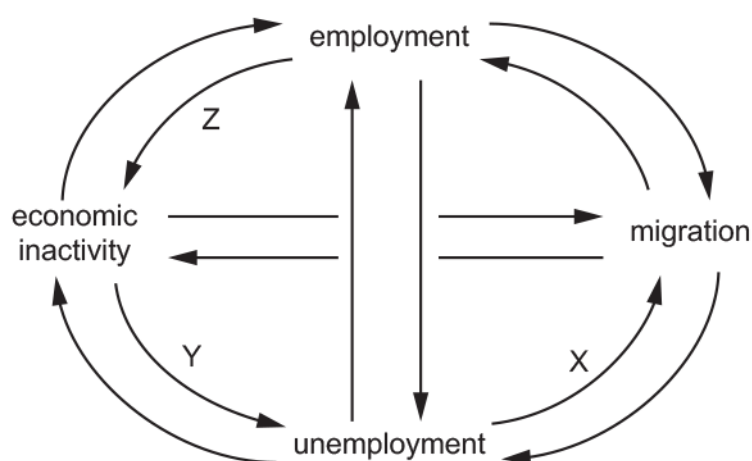


Fig. 1 Stocks and flows in the labour market

The budget position, in turn, is influenced by a range of factors including the level of economic activity, the rate of interest and any tax reforms undertaken. A number of European countries have recently introduced flat rate tax systems. Fig. 2 shows when a flat tax was introduced in a number of European countries and how the rate of income tax changed due to the introduction and the rate in 2016.

Country	Tax rate(s) before introduction (%)	Year introduced	Initial tax rate after introduction (%)	Tax rate in 2016 (%)
Estonia	16–35	1994	26	21
Lithuania	18–33	1994	33	15
Latvia	25–10	1995	25	25
Russia	12–30	2001	13	13
Georgia	12–20	2005	12	20
Macedonia	15–24	2007	12	10
Czech Republic	12–32	2008	10	10

Fig. 2 Flat rate taxes on personal income (%) in selected countries

Changes in economic activity at home and abroad, the rate of interest and the exchange rate can also influence the current account position of the balance of payments. In 2015 the UK's current account deficit was £96.2 billion. This was the largest deficit as a percentage of GDP (5.2%) since annual records began in 1948 and the largest of the G7 countries. Fig. 3 shows some details of the UK's balance of payments position in 2014.

Current account balance	−£92.9 bn
Trade in goods	−£123.7 bn
Trade in services	£89.1 bn
Secondary income	−£25.2 bn
Capital account	−£0.8 bn

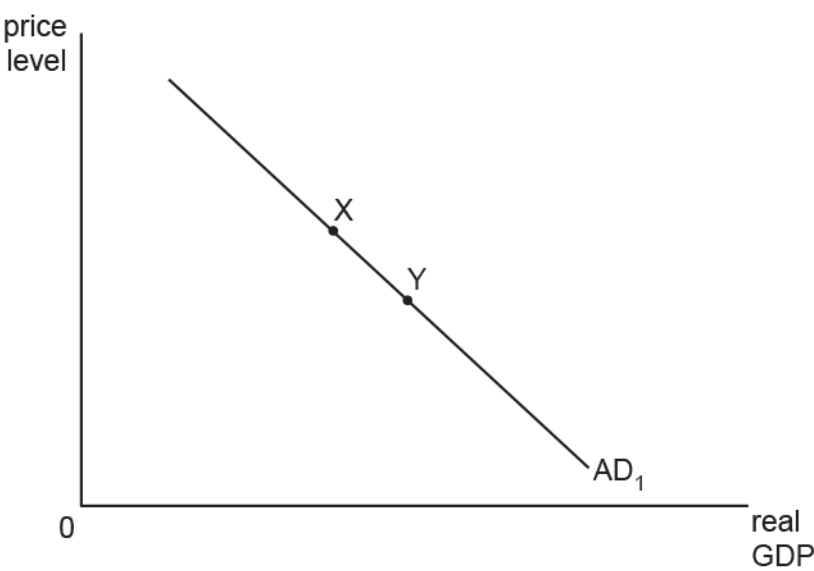
Fig. 3 Selected details of the UK's balance of payments 2014

The current account deficit has increased every year since 2011. One significant cause of this has been the rise in the deficit on primary income. Throughout the nineteenth century and the first half of the twentieth century the UK invested heavily abroad which resulted in a high yield of profits, interest and dividends. In more recent decades the UK has seen a net inflow of foreign investment. Multinational companies from a range of countries, including the USA, Germany, India and China have entered in a number of UK industries.

Identify **one** example of discretionary fiscal policy in the stimulus material and explain how it could affect aggregate demand.

[2]

22 What explains a movement from X to Y in the diagram below?



- A A decrease in corporation tax rates
- B An exchange rate depreciation
- C An increase in interest rates
- D An increase in the real value of households' wealth

Your answer

[1]

23 Use the information below to calculate the size of the national income multiplier.

Gini coefficient	0.71
Marginal Propensity to Import	0.11
Marginal Propensity to Save	0.23
Marginal Rate of Taxation	0.17
PED for exports and imports	0.42

- A 0.51
- B 1.64
- C 1.96
- D 2.94

Your answer

[1]

24 Please refer to insert H460-03 October 2020 which can be downloaded separately and is included with Q31. Evaluate, with the use of an appropriate diagram(s), whether ending austerity is likely to result in the government achieving higher levels of economic growth.

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25 * Between 2017 and 2018, households in Denmark saved more. Household saving as a percentage of disposable income rose from 5.6 to 5.9.

Evaluate, with the use of an appropriate diagram(s), whether an increase in the amount households save will harm an economy.

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26 * In March 2018 the French government announced that children would have to start school at age 3 rather than age 6 from September 2019.

Evaluate, with the use of an appropriate diagram(s), whether a fall in the compulsory school starting age will benefit an economy. [25]

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27 * In 2017 Bosnia had a significant output gap while it was estimated that Slovenia did not have an output gap.

Evaluate, with the use of an appropriate diagram(s), whether a government should always seek to reduce an output gap. [25]

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28(a) **Are we moving towards a cashless society?**

- Recent years have seen a change in both the amount consumers spend and how they make their payments. How much consumers spend is influenced by a variety of factors. These include changes in income and changes in confidence. During an economic boom, consumer expenditure is likely to be high. Indeed, an economic boom is often consumer-led. In contrast,
- 5 consumer expenditure can fall to a low level during a recession. Fig. 1 shows how consumer expenditure can vary as income changes.

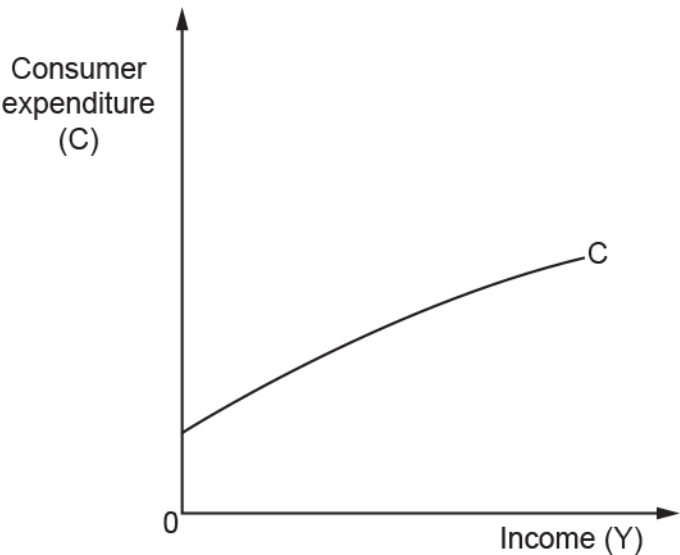


Fig. 1 The relationship between changes in income and changes in consumer expenditure

- Changes in injections and leakages can alter a country’s income. It has been estimated, for instance, that an injection of \$200m of government spending in the Swiss economy would cause a rise in GDP of \$300m.
- 10 The proportion of payments made in cash in Switzerland is declining. It is also falling in the UK. In 2005, 70% of payments in the UK were made in cash. By 2015, this had fallen to 50% and is forecast to decline to 30% by 2025. The extent to which cash is used influences the number of banknotes printed and in circulation. Fig. 2 shows the value of banknotes in circulation in the UK over a five year period.

Year	£5	£10	£20	£50	Total
2014	1 540	7 182	36 483	11 025	56 230
2015	1 601	7 371	38 912	11 788	59 672
2016	1 645	7 767	41 037	13 157	63 606
2017	1 912	8 006	43 357	15 601	68 876
2018	1 910	7 789	42 692	16 508	68 899

Fig. 2 The value of banknotes in circulation (£million) 2014 –2018

- 15 Some central banks favour ending the use of cash. One reason is because of the role that cash plays in a number of criminal activities including money laundering and drug dealing. A more significant motive is probably to enable central banks to charge negative interest rates when needed to stimulate economic activity. If people and banks can take money out of their deposits and hold them as cash, negative interest rates are likely to have less power to encourage an
- 20 increase in spending.

Negative interest rates involve commercial banks having to pay to hold deposits at the central bank. As commercial banks often have excess funds held at the central bank, a negative interest rate may encourage them to lend the funds instead. If commercial banks pass on the negative rates to their customers, people will have to pay to save. Negative interest rates would have an

25 impact on borrowing, the cost of servicing government debt and probably on the exchange rate.

A number of central banks, including the Bank of Japan, the Swiss National Bank, Denmark's National Bank and the European Central Bank (ECB) have used negative interest rates in a bid to avoid deflation. These banks received some criticism for the effect that the negative interest rates had on confidence, saving and bank profitability.

- 30 The Bank of England has yet to introduce a negative interest rate. Fig. 3 shows how the UK interest rate has changed in recent years.

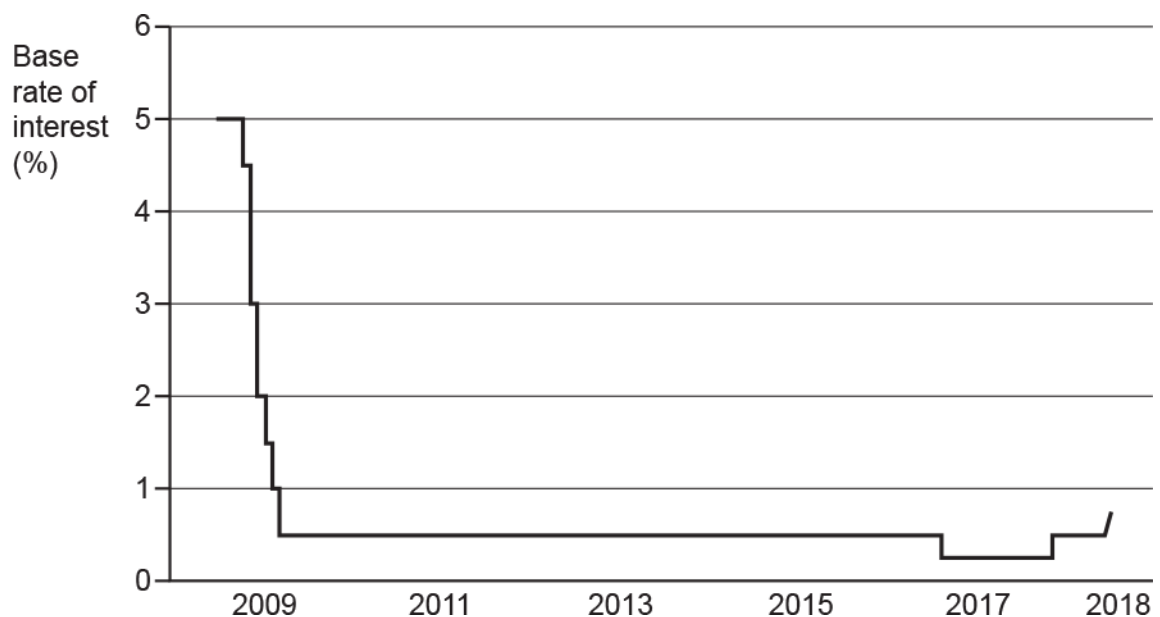


Fig. 3 UK interest rates 2009–2018

While the ECB has stopped producing its €500 note, the Bank of England has not yet scrapped any notes. Getting rid of cash is likely to affect the poor most. Nearly 1.5 million UK adults do not have a bank account and most of these are poor. Some of them are unemployed. The number of

35 people unemployed may increase during a recession. The impact on unemployment will depend

on a number of factors. These include firms' stock levels, the length of the recession, how easily firms can adjust working hours and the number of people they employ and whether the numbers in the labour force stay the same.

Using Fig. 1, explain the relationship between changes in consumer expenditure and changes in income.

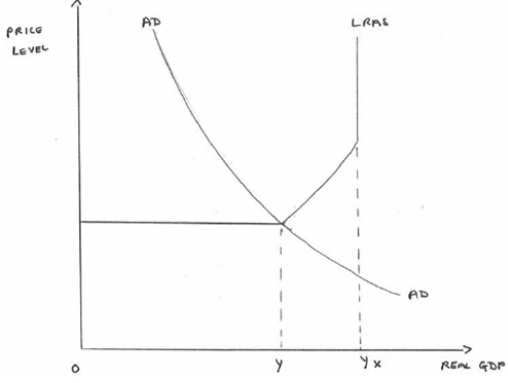
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(b) Calculate Switzerland's marginal propensity to withdraw.

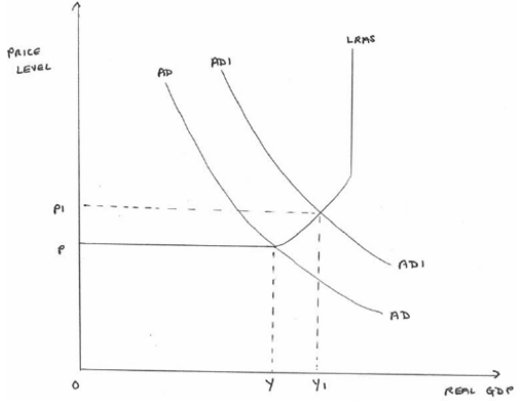
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END OF QUESTION PAPER

Mark Scheme

Question	Answer/Indicative content	Marks	Guidance
1	Evaluate, with the use of an appropriate diagram(s), whether fiscal policy will always reduce a negative output gap. Level 5 (21–25 marks) Good – Strong knowledge and understanding of fiscal policy and a negative output gap. Strong analysis of how fiscal policy may reduce a negative output gap. It will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Strong evaluation of whether fiscal policy will always reduce a negative output gap weighing up both why it might and why it might not and reaching a supported judgment. <i>There is a well-developed and sustained line of reasoning which is coherent and logically structured. The information presented is entirely relevant and substantiated.</i> Level 4 (16–20 marks) Good knowledge and understanding of fiscal policy and a negative output gap. Strong analysis of how fiscal policy may reduce a negative output gap. It will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Good evaluation of whether fiscal policy will always reduce a negative output gap weighing up both why it might and why it might not without reaching a supported	25 (AO1 x 6) (AO2 x 6) (AO3 x 6) (AO4 x 7)	<i>Indicative content</i> A negative output gap exists when actual output is below potential output. The diagram below shows that the real GDP of Y is below the potential output of YX.  A government may rely on automatic stabilisers to reduce a negative output gap. When a negative output gap increases, government spending on benefits will increase as there will be higher unemployment. Tax revenue will fall as spending and incomes may decline or rise more slowly. Higher government spending and lower tax revenue will increase aggregate demand. Automatic stabilisers, however, may not be sufficient to reduce a negative output gap and a government may decide discretionary fiscal policy. It may decide actively to increase government spending and to cut taxes. Such discretionary fiscal policy may increase aggregate demand by a multiple amount. For instance, if the multiplier is 3, an injection of extra government spending of \$20bn will cause GDP to increase by \$60bn. Lower direct taxes will increase disposable income, encouraging an increase in consumer expenditure and investment. The extra demand for consumer and capital goods will increase aggregate demand and may close the output gap as shown below.

Mark Scheme

Question	Answer/Indicative content	Marks	Guidance
	judgment. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and in the most part substantiated.</i> Level 3 (11–15 marks) Good knowledge and understanding of fiscal policy and a negative output gap. Good analysis of how fiscal policy may reduce a negative output gap. There is correct analysis in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Reasonable evaluation of whether fiscal policy will always reduce a negative output gap considering both sides. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i> Level 2 (6–10 marks) Good knowledge and understanding of fiscal policy and a negative output gap. Reasonable analysis of how fiscal policy may reduce a negative output gap. There is correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Reasonable evaluation of whether fiscal policy will always reduce a negative output gap considering both sides. The information has some relevance, but is communicated in an unstructured way. The information is supported by limited evidence, the relationship to the evidence		 It is difficult for a government to estimate the size of the multiplier so it may inject too little and so may not fully close the gap. It may also inject too much which can turn a negative output gap into a positive output gap. There is also no guarantee that lower taxes and/or increased government spending will raise demand for domestically produced products. Households and firms may not spend more if they are lacking confidence. During a recession it may be particularly difficult to reduce a negative output gap. If consumers and firms spend more they may buy imported consumer goods and services and imported capital goods. Aggregate demand may also not increase as a result of increased government spending if crowding out occurs. If a government borrows to finance extra spending, it may reduce the funds available for the private sector to borrow and may push up the rate of interest which may further discourage private sector borrowing and spending. There is the possibility that public sector spending will just crowd out private sector spending, leaving aggregate demand unchanged. Keynesian economists, however, argue that crowding in is more likely to occur than crowding out. They think that higher government borrowing and spending will raise incomes which will generate more saving. The higher saving will provide the funds for both the public and private sectors.

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Question			Answer/Indicative content	Marks	Guidance										
			may not be clear. Level 1 (1–5 marks) Reasonable knowledge and understanding of fiscal policy and a negative output gap. Limited or no analysis of how fiscal policy may reduce a negative output gap. There is little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. The relevant diagram(s) may not be present or are incorrectly labelled. Limited evaluation of whether fiscal policy will always reduce a negative output gap in the form of an unsupported statement or no evaluation. <i>Information presented is basic and may be ambiguous or unstructured. The information is supported by limited evidence.</i> 0 marks no response or no response worthy of credit. <table><tr><th>Descriptor</th><th>Award mark</th></tr><tr><td>Consistently meets the criteria for this level</td><td>At top of level</td></tr><tr><td>Meets the criteria but with some slight inconsistency</td><td>Above middle and either below top of level or at middle of level (depending on number of marks available)</td></tr><tr><td>Just enough achievement on balance for this level</td><td>Above bottom and either below middle or at middle of level (depending on number of marks available)</td></tr><tr><td>On the borderline of this level and the one below</td><td>At bottom of level</td></tr></table>	Descriptor	Award mark	Consistently meets the criteria for this level	At top of level	Meets the criteria but with some slight inconsistency	Above middle and either below top of level or at middle of level (depending on number of marks available)	Just enough achievement on balance for this level	Above bottom and either below middle or at middle of level (depending on number of marks available)	On the borderline of this level and the one below	At bottom of level		The stimulus to aggregate demand provided by expansionary fiscal policy may be offset by a global recession which may reduce the country’s exports. Neo-classical economists argue that seeking to reduce a negative output gap by increasing aggregate demand may increase output and employment in the short run but will just generate inflation in the long run. They suggest that an economy has the potential to move automatically towards the full employment level through adjustments in wages and prices. What might be needed are supply-side policy measures to ensure that market forces can operate efficiently. Automatic stabilisers are unlikely to be sufficient to reduce all of a negative output gap. Whether discretionary fiscal policy will be successful will depend on a number of factors. The larger the size of the multiplier and the greater the information about its size that the government has, the greater the chance it will have of being successful. The outcome will also depend on how households and firms respond to changes in government spending and taxation. The larger the size of the output gap, the more pessimistic households and firms are likely to be about the future and so the harder it will be to encourage them to spend more. There is also the risk that expansionary fiscal policy may just result in inflation if it causes aggregate demand to increase more than aggregate supply. Examiner’s Comments There was good use made of aggregate demand and aggregate supply diagrams, both Keynesian and Neo-classical versions, in response to this question. Again, in some cases, there were some inaccuracies and carelessness in the labelling of the diagrams. The analysis of how fiscal policy might reduce a negative output gap by changing taxes and government spending and the difference between automatic stabilisers and discretionary fiscal policy was
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					generally good. There was, however, a need for greater clarity in places. A number of candidates, for instance, appeared to confuse the likely effect of a higher disposable income on the total amount of consumer expenditure with the likely effect on the marginal propensity to consume. There was some strong evaluation shown with some particularly interesting discussion on crowding out and crowding in. It was disappointing, however, that a number of candidates lost focus and wrote about how expansionary fiscal policy would not increase output and would cause only inflation when there is full employment.
			Total	25	

Mark Scheme

Question			Answer/Indicative content	Marks	Guidance
2	a		Using Fig. 1, explain which type of economic recovery is likely to be most beneficial for an economy. The V-shaped recovery (1) this lasts a shorter time / is over quicker (1) likely to have less effect on confidence (1) less effect on unemployment / macroeconomic performance (1). The U-shaped recovery (1) more stable growth / more gradual recovery (1) more time to make adjustments/creates more certainty / gives greater confidence (1) more sustainable recovery / growth (1)	3 (AO1 x 1) (AO2 x 2)	1 mark for identifying the type of recovery Up to 2 marks relevant explanation <u>Examiner's Comments</u> Most candidates were able to interpret Fig.1 and to provide a logical explanation of the reasons why a particular type of recovery, U or V, would be most beneficial for an economy.

Mark Scheme

Question		Answer/Indicative content	Marks	Guidance
	b	Using information in the stimulus material, evaluate whether Iceland would be likely to experience a recession after 2015. Level 2 (5–8 marks) Good knowledge and understanding of the factors that will influence Iceland's future economic performance. Good – strong analysis of the future prospects of the Icelandic economy. Good analysis will be in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Reasonable – strong evaluation of the future prospects of the Icelandic economy, considering both why and why it might not experience a recession, underpinned by appropriate theoretical analysis. Good evaluation will weigh up the reasons why it might and the reasons why it might not but without reaching a strong judgement. Strong evaluation should include a supported judgement. Level 1 (1–4 marks) Limited – reasonable knowledge and understanding of the factors that will influence Iceland's future economic performance. Limited – reasonable analysis of the future prospects of the Icelandic economy. Limited analysis will have little evidence of reasoning that addresses the question asked. There is a lack of a clear structure.	8 (AO1 x 1) (AO2 x 1) (AO3 x 3) (AO4 x 3)	<i>Indicative content</i> There are a number of reasons for thinking that Iceland would not be likely to experience a recession. Its financial sector has been reformed which should make a banking collapse less likely in the future. Its economic growth has been impressive and this may have increased confidence in the performance of the economy. This may increase investment by Icelandic firms and may encourage FDI. The country's infrastructure has improved which should reduce firm's costs of production. Loans are being paid back to the IMF and capital controls have been removed. These changes may also encourage an increase in investment. It was, however, predicted that unemployment was going to rise. This could result in less spending, less output and reduced confidence. A further increase in the income tax rate could also reduce consumer spending and output. The economy's growth is also heavily dependent on the tourist industry. A slowdown or recession in other European economies could reduce Iceland's output. Whether Iceland will experience a recession will be influenced by not only what is happening in Iceland but also in the global economy. The Icelandic economy in 2015 was in a relatively good shape but it would benefit from a more diverse industrial base. Examiner's Comments Some candidates identified relevant pieces of information from the stimulus material but did not analyse and evaluate their significance. Others restricted their answers to a limited analysis of predictions on economic growth and employment. A number of candidates did not pick up on the words 'after 2015' in the question and did not show an appreciation of the information in the stimulus material of Iceland's recovery after the 2008 – 2011 recession.

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			Reasonable analysis will have correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Limited evaluation of the future prospects of the Icelandic economy, in the form of an unsupported statement or no evaluation. 0 marks no response or no response worthy of credit. Note: although a diagram is not required, it may enhance the quality of the answer and should be rewarded at the appropriate level. <table><tr><th>Descriptor</th><th>Award mark</th></tr><tr><td>Consistently meets the criteria for this level</td><td>At top of level</td></tr><tr><td>Meets the criteria but with some slight inconsistency</td><td>Above middle and either below top of level or at middle of level (depending on number of marks available)</td></tr><tr><td>Just enough achievement on balance for this level</td><td>Above bottom and either below middle or at middle of level (depending on number of marks available)</td></tr><tr><td>On the borderline of this level and the one below</td><td>At bottom of level</td></tr></table>	Descriptor	Award mark	Consistently meets the criteria for this level	At top of level	Meets the criteria but with some slight inconsistency	Above middle and either below top of level or at middle of level (depending on number of marks available)	Just enough achievement on balance for this level	Above bottom and either below middle or at middle of level (depending on number of marks available)	On the borderline of this level and the one below	At bottom of level		There was also some good evaluation, exploring how changes in confidence, the strength of Iceland’s banking sector, the country’s tourism industry and the global economy could influence the chances of Iceland experiencing a recession.
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Consistently meets the criteria for this level	At top of level														
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On the borderline of this level and the one below	At bottom of level														
			Total	11											

Mark Scheme

Question	Answer/Indicative content	Marks	Guidance
3	Evaluate the extent to which the accelerator theory explains the level of investment in an economy. Level 5 (21–25 marks) Good–Strong knowledge and understanding of the accelerator theory. Strong analysis of how changes in GDP can affect investment. It will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Strong evaluation of the influences on investment, weighing up which are the key influences and reaching a supported judgement. <i>There is a well-developed and sustained line of reasoning which is coherent and logically structured. The information presented is entirely relevant and substantiated.</i> Level 4 (16–20 marks) Good knowledge and understanding of the accelerator theory. Strong analysis of how changes in GDP can affect investment. It will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Good evaluation of the influences on investment, weighing up which are the key influences but without reaching a supported judgement. <i>There is a well-developed line of reasoning which is clear and logically structured. The</i>	25 (AO1 x 6) (AO2 x 6) (AO3 x 6) (AO4 x 7)	<i>Indicative content</i> The accelerator theory states that the level of investment depends on the rate of change of GDP. It also suggests that investment fluctuates more than consumer expenditure. During an economic boom, investment can increase dramatically with many more capital goods being purchased to expand capacity. If real GDP is constant, the only investment which takes place may be replacement investment. During a recession, net investment may be negative, with some obsolete capital goods not being replaced. There are two key reasons for thinking that changes in real GDP do play a significant role in explaining the level of investment. A rise in real GDP would be likely to increase consumer expenditure and so the quantity of goods and services purchased. This will increase the willingness and ability of firms to invest. Willingness increases as firms will expect to earn higher profits. There is more ability to invest as firms will have more retained profits to finance investment. The accelerator theory is, however, not a full explanation of investment. This is because there are other influences on investment. It is possible, for instance, that GDP may increase without there being any rise in investment. Firms may think that the increase in GDP may not last and they may be pessimistic about the future. Expectations play an important role in firms, investment decisions. Firms may be able to produce more goods and services without undertaking any investment if they have spare capacity. The level of spare capacity of the capital goods industry is operating at full capacity, firms will not be able to make more capital goods. Advances in technology may encourage firms to buy new capital goods even if GDP is not changing. More productive capital goods can increase profits by lowering costs of production. Advances in technology can also alter the relationship

Mark Scheme

Question	Answer/Indicative content	Marks	Guidance
	<i>information presented is relevant and in the most part substantiated.</i> Level 3 (11–15 marks) Good knowledge and understanding of the accelerator theory. Good analysis of how changes in GDP can affect investment. There is correct analysis in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Reasonable evaluation of the influences on investment, weighing up which are the key influences. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i> Level 2 (6–10 marks) Good knowledge and understanding of the accelerator theory. Reasonable analysis of how changes in GDP can affect investment. There is correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Reasonable evaluation of the influences on investment. <i>The information has some relevance, but is communicated in an unstructured way. The information is supported by limited evidence, the relationship to the evidence may not be clear.</i> Level 1 (1–5 marks) Reasonable knowledge and understanding of the accelerator theory.		between the value of capital goods needed to produce a given value of consumer goods and services. Lower prices of capital goods and government incentives, including cuts in corporation tax and subsidies may also stimulate a rise in investment, independently of changes in income. Changes in income is an important influence on investment but it is not the only one. Some investment is induced investment (dependent on changes in income) and some is autonomous investment (independent of changes in income). The two main influences on investment are probably changes in GDP and changes in business confidence. <u>Examiner's Comments</u> Candidates were clear about the nature of investment but there was confusion regarding the accelerator theory. These candidates wrote about how the changes in investment may affect may affect investment and GDP rather than how changes in GDP may affect investment. Other candidates wrote about how the accelerator theory can explain the level of investment in an economy but did not evaluate the extent to which it does this. Some answers tended to be rather repetitive on how higher GDP can stimulate a rise in investment. A number of the higher ability responses gave a brief numerical example and then explored a number of reasons why GDP and AD may rise but investment may not increase.

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			Limited or no analysis of how changes in GDP can affect investment. There is little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. The relevant diagram(s) may not be present or are incorrectly labelled. Limited evaluation of the influences on investment in the form of an unsupported statement or no evaluation. <i>Information presented is basic and may be ambiguous or unstructured. The information is supported by limited evidence.</i> 0 marks no response or no response worthy of credit. Note: although a diagram is not required, it may enhance the quality of the answer and should be rewarded at the appropriate level. <table><tr><th>Descriptor</th><th>Award mark</th></tr><tr><td>Consistently meets the criteria for this level</td><td>At top of level</td></tr><tr><td>Meets the criteria but with some slight inconsistency</td><td>Above middle and either below top of level or at middle of level (depending on number of marks available)</td></tr><tr><td>Just enough achievement on balance for this level</td><td>Above bottom and either below middle or at middle of level (depending on number of marks available)</td></tr><tr><td>On the borderline of this level and the one below</td><td>At bottom of level</td></tr></table>	Descriptor	Award mark	Consistently meets the criteria for this level	At top of level	Meets the criteria but with some slight inconsistency	Above middle and either below top of level or at middle of level (depending on number of marks available)	Just enough achievement on balance for this level	Above bottom and either below middle or at middle of level (depending on number of marks available)	On the borderline of this level and the one below	At bottom of level		
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			Total	25											

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Question			Answer/Indicative content	Marks	Guidance
4			D	1 (AO2)	Rationale A $MRT + MPS + MPM$ = marginal propensity to withdraw. B Correct formula for multiplier used but incorrectly specifies MPW ($MRT + MPC + MPM$) C $MRT + MPC + MPM$ D Correct: Multiplier = $1 / MPW = 1 / (0.1 + 0.2 + 0.3)$
			Total	1	
5			D	1 (AO3)	Rationale A This would be the outcome if AD shifted to the left. B There is no spare capacity so even though AD increases there will be no economic growth or reduction in unemployment. C This would be the outcome if there was significant spare capacity in the economy, meaning demand side growth would be non-inflationary. D Correct: the AD curve will shift right, however there is no spare capacity so this is simply inflationary.
			Total	1	
6			A	1 (AO1)	Rationale A Correct: a negative output gap is when an economy is producing below its trend rate of output. B This is a microeconomic concept of market failure. C This suggests a positive output gap. D This is the definition of a recession.
			Total	1	

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Question			Answer/Indicative content	Marks	Guidance
7			D	1 (AO1)	Rationale A Investment will be affected by increases in income, as firms expect rising demand and therefore better returns to investment. B Government spending will also be affected because it is likely to lead to a rise in tax revenue. C Net exports will also be affected as the demand for imports will rise. D Correct: all components of AD could be affected by an increase in income.
			Total	1	
8			A	1 (AO2)	Rationale A Correct: $0.31 + 0.19 = 0.5$ and $1/0.5 = 2$. $0.24 + 0.16 = 0.4$ and $1/0.4 = 2.5$ B This is the change in the marginal propensity to withdraw. C $1 - 0.31$ and $1 - 0.24$ D $2 - 0.31$ and $2.5 - 0.24$.
			Total	1	
9			A	1 (AO1)	Rationale A Correct: Keynesians argue an economy could operate with spare capacity in the long run. B It is the classical approach that argues the inelastic LRAS curve means fiscal policy will simply be inflationary. C Keynes argued prices and wages are sometimes 'sticky'. D Keynes proposed demand deficient unemployment could be addressed through fiscal stimulus.
			Total	1	

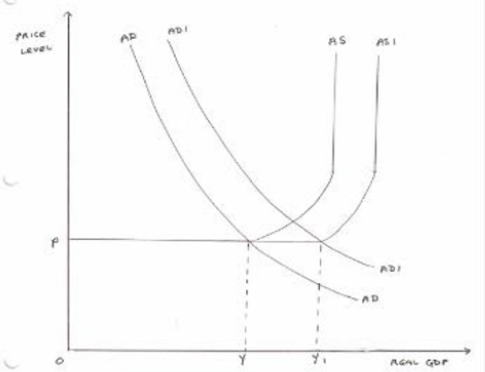
Mark Scheme

Question			Answer/Indicative content	Marks	Guidance
10			Using the data in Extract 2, explain what is meant by the multiplier effect of Olympics expenditure. <i>Award 1 mark for applying understanding of the multiplier effect:</i> Olympics expenditure leads to a greater final change in (real) GDP/output/expenditure/income. <i>Award 1 mark for appropriate use of the data:</i> A multiplier of 1.7 means for every £1 spent on the Olympics real GDP will increase by £1.70	2 (AO2 x 2)	Award answers that calculate the multiplier for Vancouver or London: Vancouver - \$7,556m x 1.7 = \$12,845m London - \$11,401 x 1.7 = \$19,382m <i>NB – this is not required for full marks.</i> <u>Examiner's Comments</u> Centres should ensure that candidates can clearly explain the multiplier and how it works. It is a concept many candidates understood but could not describe precisely and responded with an increase in GDP rather than a greater increase in GDP. Very few candidates were able to use the multiplier given in the case study to develop their answer and simply quoted the figure without applying it.
			Total	2	

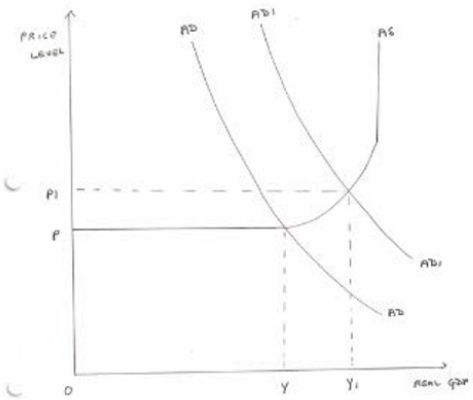
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Question			Answer/Indicative content	Marks	Guidance
11	a	i	Using Table 1, explain which country's government made a negative contribution to the country's aggregate demand. Germany (1) government tax revenue exceeded government expenditure (1).	2 (AO1 x 1) (AO2 x 1)	Germany (1) government tax revenue US\$1598bn exceeds government expenditure of US\$1573bn. (1) Or Government tax revenue was higher than Government expenditure by US\$25bn (1). Examiner's Comments A very straight forward question, which was answered correctly by the vast majority of candidates.
		ii	Using Table 1, calculate Russia's GDP in 2017. \$1 468.21bn (2). Correct working i.e. \$254bn/17.3 x 100 (1)	2 (AO1 x 1) (AO2 x 1)	Accept: \$1468bn/\$1468.2bn/\$1468.208bn. If just \$1468 or 1468bn (1) Examiner's Comments Candidates generally answered this correctly. It's worth pointing out here though, that workings should always be included, and the correct units used. In this case \$ and Billion
	b		Using information from the stimulus material, calculate the UK's marginal propensity to import in 2017. 0.3 (2). Correct working or formula: £330/£1,100 i.e. change in imports/change in disposable income (1).	2 (AO2 x 2)	Examiner's Comments Candidates generally answered this well, although there were a significant number who made no attempt. Centres could make sure candidates have further practice of these type of questions.
			Total	6	

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Question	Answer/Indicative content	Marks	Guidance
12	Evaluate, with the use of an appropriate diagram(s), whether an increase in private sector investment will help a government achieve its macroeconomic objectives Level 5 (21–25 marks) Good - Strong knowledge and understanding of investment and macroeconomic policy objectives. Strong analysis of whether an increase in private sector investment will help a government achieve its macroeconomic objectives Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Strong evaluation of whether an increase in private sector investment will help a government achieve its macroeconomic objectives weighing up both why they might and why they might not and reaching a supported judgment. <i>There is a well-developed and sustained line of reasoning which is coherent and logically structured. The information presented is entirely relevant and substantiated.</i> Level 4 (16–20 marks) Good knowledge and understanding of investment and macroeconomic policy objectives. Strong analysis of whether an increase in private sector investment will help a government achieve its macroeconomic objectives Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the	25 (AO1 x 6) (AO2 x 6) (AO3 x 6) (AO4 x 7)	<i>Indicative content</i> The reasons why it will help. An increase in private sector investment means that firms are purchasing more capital goods. This will increase aggregate demand. Investment is an injection into the circular flow of income, so there will be a multiplier effect. Aggregate demand will rise by a greater amount than the initial increase in investment. The higher demand will be likely to cause capital goods and consumer goods firms to increase their output. The country's economic growth rate may rise and unemployment may fall. In the longer run higher investment will increase aggregate supply as well as aggregate demand. This could allow an economy to grow without the economy experiencing inflation as shown in the diagram below.  As new AS capital goods are put into use, the price and quality competition of the country's products may rise. This could increase net exports and reduce a current account deficit. The reasons why it will not help If the capital goods are purchased from abroad, this may increase a current account deficit. The higher aggregate demand may also result in demand-pull inflation. If the economy is operating close to full capacity, extra demand for capital goods and consumer goods may pull up prices. The diagram below shows the rise

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	question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Good evaluation of whether an increase in private sector investment will help a government achieve its macroeconomic objectives and will weigh up both sides but without reaching a supported judgment. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and in the most part substantiated.</i> Level 3 (11–15 marks) Good knowledge and understanding of investment and macroeconomic policy objectives. Good analysis of whether an increase in private sector investment will help a government achieve its macroeconomic objectives There is correct analysis in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Reasonable evaluation of whether an increase in private sector investment will help a government achieve its macroeconomic objectives, considering both why it might and why it might not. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i> Level 2 (6–10 marks) Good knowledge and understanding of investment and macroeconomic policy objectives.		in aggregate demand from AD to AD₁, causing the price level to rise from P to P₁.  There is also the possibility that private sector investment may replace public sector demand. If private sector firms are borrowing more, this may raise the rate of interest. A higher rate of interest will increase the cost of servicing government debt. This may put pressure on the government to cut its spending. The impact on unemployment is uncertain. Firms in the private sector may be more willing than public sector firms to dismiss workers. New capital equipment may also be a substitute rather than a complement to labour. Some jobs may be lost as a result of advances in technology incorporated into new capital equipment. The effect is, however, uncertain. New technology can create new industries and new jobs. For instance, there is now a thriving games industry with games designers and testers. Possible judgment. It is generally considered that increases in private sector investment will help a government achieve its macroeconomic objectives. This is more likely if the increase is not offset by a decrease in public sector investment and if it generates extra jobs.

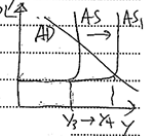
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	Reasonable analysis of whether an increase in private sector investment will help a government achieve its macroeconomic objectives There is correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Reasonable evaluation of whether an increase in private sector investment will help a government achieve its macroeconomic objectives considering both why it might and why it might not. <i>The information has some relevance, but is communicated in an unstructured way. The information is supported by limited evidence, the relationship to the evidence may not be clear.</i> Level 1 (1–5 marks) Reasonable knowledge and understanding of investment and macroeconomic policy objectives. Limited or no analysis of whether an increase in private sector investment will help a government achieve its macroeconomic objectives There is little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. The relevant diagram(s) may not be present or are incorrectly labelled. Limited evaluation of whether an increase in private sector investment will help a government achieve its macroeconomic objectives in the form of an unsupported statement or no evaluation. <i>Information presented is basic and may be ambiguous or unstructured. The information is supported by limited evidence.</i> 0 marks No response worthy of credit.		Examiner's Comments Candidates who tackled this question completed this soundly using solid economic models and were able to clearly link this back to economic objectives. The better answers analysed how an increase in private sector investment could help achieve macroeconomic objectives through an increase in AD and LRAS. Diagrams were accurately labelled and integrated into answers. Evaluation, which tended to focus on inflation, could have been improved by looking at the limitations of investment. Candidates need to take care reading the question as it clearly states increase in private sector investment not the government investing. Weaker answers tended to focus on government spending or on policies to increase private sector investment and evaluate the effectiveness of those policies. There were also candidates who had missing links in their analysis. For example, saying that private sector investment causes employment without explaining how or why, this often meant that they did not get beyond L3.

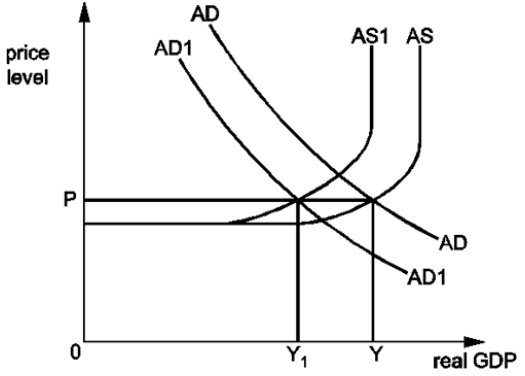
Mark Scheme

Question		Answer/Indicative content	Marks	Guidance										
		<table><tr><th>Descriptor</th><th>Award mark</th></tr><tr><td>Consistently meets the criteria for this level</td><td>At top of level</td></tr><tr><td>Meets the criteria but with some slight inconsistency</td><td>Above middle and either below top of level or at middle of level (depending on number of marks available)</td></tr><tr><td>Just enough achievement on balance for this level</td><td>Above bottom and either below middle or at middle of level (depending on number of marks available)</td></tr><tr><td>On the borderline of this level and the one below</td><td>At bottom of level</td></tr></table>	Descriptor	Award mark	Consistently meets the criteria for this level	At top of level	Meets the criteria but with some slight inconsistency	Above middle and either below top of level or at middle of level (depending on number of marks available)	Just enough achievement on balance for this level	Above bottom and either below middle or at middle of level (depending on number of marks available)	On the borderline of this level and the one below	At bottom of level		Exemplar 4 Increase in private sector investment can help a government achieve its macroeconomic objectives including economic growth, stable and low inflation, balance of payments and full employment. Firms increase investment to expand the production. In this process, there will be a higher demand of FOP (Land, labour, capital & entrepreneurship). Labour as a derived demand of production will increase. This will reduce cyclical unemployment through $D_1 \rightarrow D_2$. <i>Diagram 1: A graph showing the relationship between demand for factors of production (FOP) and production. The vertical axis is labeled 'wage' and the horizontal axis is labeled 'hour'. A downward-sloping demand curve shifts from D_1 to D_2. A horizontal supply curve is labeled S_1. The initial equilibrium is at q_1 and the new equilibrium is at q_2. The shift from D_1 to D_2 leads to a higher wage w and higher employment q_2.</i> unemployment under minimum wage (Mw) will be reduced. If there is no min wage, real wage will increase from $w_1 \rightarrow Mw$. This can help the govt to achieve full employment. As there is more employment, consumption will increase, this will increase AD as C increase. Short run economic growth is achieved by shifting $AD_0 \rightarrow AD_1$ through a multiplier effect as explained and the direct stimulation of investment (I) <i>Diagram 2: A graph showing the Aggregate Demand (AD) model. The vertical axis is labeled 'P' (Price) and the horizontal axis is labeled 'Y' (Real output). A vertical supply curve is labeled 'AS'. A downward-sloping demand curve shifts from AD_0 to AD_1. The initial equilibrium is at Y_0 and the new equilibrium is at Y_1. The shift from AD_0 to AD_1 leads to higher output Y_1 and higher price P_1.</i> the direct stimulation of investment (I) $\rightarrow$ increase from $Y_0 \rightarrow Y_1$ which is economic growth. Another advantage is through private sector investment, firms can utilise the economies of scale by increasing return to scale, which reduces the long run average cost. By firm expansion through investment, the domestic production cost can be lowered, which reduce the price of export and improves the terms of trade through a lower price in general ($TOT = \frac{\text{EXPORT PRICE}}{\text{IMPORT PRICE}} \times 100$), this can increase the export competitiveness by cost advantage and quality improvement, which improve the current acc. and the Balance of payment. Moreover, increase in net export ($X-M$) can also increase AD by ($AD_0 \rightarrow AD_1$) which improves Economic growth. Private sector investment can reduce the govt expenditure and increase government tax revenue by
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					Increase in transaction turnover, which increases the revenue and profit tax, also improves the budget position of gov't and flexibility of fiscal policy. Also investment in infrastructure can bring a long lasting effect to the AS growth. Firstly increase in investment increases firm size which increases the profit & profit tax, gov't can have more revenue to balance the budget (such as UK, 27% deficit). Gov't can save the budget and prepare for any future supply side policy such as education. Also private sector investment can bring a long lasting effect to the AS. For example, Emirates has built public aviation school which provides training of pilots in UAE, dubai. This can continuously produce skillful labor, which is a high quality FOP to shift AS to the right. This increases PLP potential output & outward shift of PPF (production possibility frontier). Shown by $(F_1 \rightarrow F_2)$, which is Economic LR growth.  In this response the candidate used a brief introduction, which clearly showed they knew what the question was asking of them. The analysis is developed with clear chains of reasoning focused on the question set, the diagrams are predominantly correct and integrated into the answer. There is use of their own knowledge which enhanced the explanation. Overall this section was awarded strong analysis and went on to be awarded strong evaluation.
			Total	25	

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13	Level 5 (21–25 marks) Good knowledge and understanding of income tax in the context of improving UK macroeconomic performance. Strong analysis of the link between a cut in the top rate of income tax and macroeconomic performance. A relevant and accurately drawn and labelled diagram is provided and is linked to the analysis. Strong evaluation, including a supported judgement, of whether UK macroeconomic performance would be strengthened by an increase in the top rate of income tax. <i>There is a well-developed and sustained line of reasoning which is coherent and logically structured. The information presented is entirely relevant and substantiated.</i> Level 4 (16–20 marks) Good knowledge and understanding of income tax in the context of improving UK macroeconomic performance. Strong analysis of the link between a cut in the top rate of income tax and macroeconomic performance would be strengthened by an increase in the top rate of income tax. Good evaluation of whether UK macroeconomic performance would be strengthened by an increase in the top rate of income tax. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and in the most part substantiated.</i> Level 3 (11–15 marks) Good knowledge and understanding of income tax in the context of improving UK macroeconomic performance. Good analysis of the link between a cut in	25 (AO1 x 6) (AO2 x 6) (AO3 x 6) (AO4 x 7)	<i>Indicative content</i> Use and interpretation of an AD/AS diagram:  • an increase in the top rate of tax may reduce the size of the country's labour force and may reduce consumer expenditure and investment • the effect will be to lower output. The impact on this price level will depend on the relative size of the two shifts. Note: also accept a diagram showing the AD and AS curves shifting to the right that is consistent with the text. Reasons why it may improve the UK's macroeconomic performance: • if the economy is operating close to full employment and aggregate supply does not decrease, a reduction in aggregate demand may reduce demand-pull inflation • a higher top rate of tax may not reduce the size of the labour force as some workers may work longer hours to maintain living standards • higher tax revenue may reduce budget deficit which may give foreign and domestic firms more confidence in the economic prospects of the country. An increase in business confidence may increase investment which, in turn, may increase international price competitiveness and economic growth

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	the top rate of income tax and macroeconomic performance. A relevant diagram is provided and is linked to the analysis. Reasonable evaluation of how a cut in the top rate of income tax may influence macroeconomic performance but without considering the extent. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i> Level 2 (6–10 marks) Good knowledge and understanding of income tax and/or macroeconomic performance. Reasonable analysis the link between a cut in the top rate of income tax and macroeconomic performance. A relevant diagram is provided, which is less than perfect. Reasonable evaluation of how a cut in the top rate of income tax may affect macroeconomic performance but without considering the extent. <i>The information has some relevance, but is communicated in an unstructured way. The information is supported by limited evidence, the relationship to the evidence may not be clear.</i> Level 1 (1–5 marks) Reasonable knowledge and understanding of income tax and/or macroeconomic performance. Limited analysis of the link between a cut in the top rate of income tax and macroeconomic performance. The diagram may not be relevant, may be inaccurate or may be missing. Limited or no evaluation.		• if any extra revenue earned is spent by the government, aggregate demand will increase. For instance, if tax revenue increases by £200bn and government spending increases by £200bn, there will be a net injection of spending into the circular flow. £40bn of the income taken in tax may have been spent, so part of the tax revenue will replace another leakage from the circular flow. An injection of government spending in such a case will be matched by a fall in leakages of £160bn, giving a net injection of £40bn • if the government spends some of the tax revenue on education, training and infrastructure projects, productivity may rise. This will increase aggregate supply and may raise the quality and price competitiveness of the country's products. A more educated and skilled labour force may attract foreign direct investment. As a result there may be actual and potential economic growth and an improvement in the country's current account position Reasons why it might not improve macroeconomic performance: • an increase in the top rate of tax may discourage some people of working age from entering the labour force • it may reduce the quantity of hours supplied by workers • investment may be reduced as foreign and domestic firms may want to be based in other countries where their top workers will be taxed less and where domestic demand may be higher • a reduction in investment will lower both aggregate demand and aggregate supply • aggregate demand may fall if the higher tax rate reduces consumer expenditure. A higher tax rate will reduce the disposable income of the rich which will lower their purchasing power. Such a fall in spending may

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			<i>Information presented is basic and may be ambiguous or unstructured. The information is supported by limited evidence.</i> 0 marks no response or no response worthy of credit.		cause GDP to fall by a multiple amount. If aggregate supply falls by more than aggregate demand, the economy may experience cost-push inflation. With less investment and the withdrawal of some possibly highly productive and innovative workers, costs of production may rise. Cost-push inflation may reduce the price competitiveness of domestic products. This combined with a possible reduction in the quality of products produced may decrease exports and increase imports. As a result the current account position of the balance of payments worsens. Credit, where appropriate, knowledge/analysis of other, relevant factors. Possible routes into evaluation: • outcome will be influenced by the level of economic activity • the effect will depend on the relative sizes and directions of the shifts of the AD and AS curves • the larger the size of the multiplier, the greater the effect is likely to be • the proportion of people who will be moved into paying the 50% income tax rate • it will depend on the other tax rates as this will influence the marginal rate of tax at the top end • it depends on the direction/influence of other policy measures.
			Total	25	

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14			C	1 (AO1)	Rationale A This is the multiplier effect. B This incorrectly specifies the multiplier effect. C Correct: When economic growth increases firms anticipate rising demand and so increase the level of investment accordingly. D The accelerator theory argues changes in investment will occur as a result of changes in output – if output is consistently high this will not spark a change in the level of investment.
			Total	1	
15			D	1 (AO1)	Rationale A This is an injection into the circular flow. B This is an injection into the circular flow. C This is an injection into the circular flow. D Correct: savings are a leakage from the circular flow.
			Total	1	
16			A	1 (AO3)	Rationale A Correct: Would result in an increase in output since it would lead to resources having greater productivity. B Has the potential to increase demand but with all resources fully employed output cannot be increased to meet the higher demand. C Has the potential to increase demand but with all resources fully employed output cannot be increased to meet the higher demand. D Has the potential to increase demand but with all resources fully employed output cannot be increased to meet the higher demand.
			Total	1	

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Question			Answer/Indicative content	Marks	Guidance
17			C	1 (AO3)	Rationale A Based on a multiplier of 10, which might be thought to be the correct answer if 1/mps is used B Based on a multiplier of 2.5 which might be thought to be the correct answer if 1/mrt + mpm is used C Correct: The multiplier is $1.0/0.5 = 2$. The government wants to raise GDP by \$150bn and so it has to increase its spending by £150bn/2 - \$75bn. D The gap between current and desired GDP.
			Total	1	
18			C	1 (AO1)	Rationale A This is the multiplier effect B This is demand-pull inflation C Correct: accelerator theory states that capital investment will increase as a result of expected increases in demand so that productive capacity can meet the demands of increased output D This illustrates the principle of opportunity cost, where a short run sacrifice in material standards of living can contribute to long run economic growth by expanding the economy's productive capacity
			Total	1	

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Question	Answer/Indicative content	Marks	Guidance
19	Evaluate the impact on the UK labour market and wider economy of the UK ending the free movement of labour with EU countries. Level 3 (11–15 marks) Good knowledge and understanding of the impact of changing immigration policy on the labour market and wider economy. Good - strong analysis of the impact of changing immigration policy on the labour market and wider economy. Good analysis will be in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Good - strong evaluation of the extent to which changing immigration policy will benefit/harm the labour market and wider economy, weighing up both sides/comparing alternatives. Strong evaluation should include a supported judgment. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and substantiated.</i> Level 2 (6–10 marks) Good knowledge and understanding of the impact of changing immigration policy on the labour market and wider economy. Reasonable analysis of the impact of changing immigration policy on the labour	15 (AO1 x 2) (AO2 x 3) (AO3 x 4) (AO4 x 6)	Guidance: • Whilst most candidates will start their answers with the negative impact of the end of free movement of labour, the reverse approach is equally valid – the benefits of ending free movement of labour can be credited as analysis if presented first. • A number of limited analytical/evaluative points can be awarded up to Reasonable, but to be awarded Good or Strong there needs to be greater depth of explanation. • Strong evaluation requires an explained judgement. An explained judgement without Good evaluation can be credited as evaluation. • Arguments for and against the benefits of free movement of labour that are not focused on the ending of free movement should not be credited – NAQ. Knowledge & Understanding: Knowledge & Understanding marks should be awarded for recognition of the costs or benefits of ending the free movement of labour that are mentioned in the case study: ◦ 2007 expansion of EU meant immigration into the UK from low wage countries spiralled out of control. ◦ High levels of immigration puts pressure on public services, pushes house prices up and depresses wages and employment opportunities for low skilled workers. ◦ UK can take control of its borders. ◦ EU immigrants are younger than native population, are more likely to work and pay taxes than claim benefits and in doing so addressing the problems an ageing population could cause the economy. ◦ Healthcare and construction rely on immigrants to fill skills shortages –

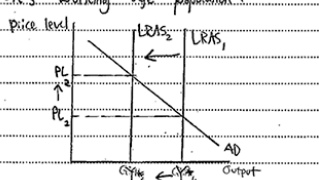
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	market or and wider economy. There is correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Reasonable evaluation of the extent to which changing immigration policy will benefit/harm the labour market or wider economy. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i> Level 1 (1–5 marks) Limited – reasonable knowledge and understanding of the impact of changing immigration policy on the labour market or wider economy. Limited analysis of the impact of changing immigration policy on the labour market or and wider economy. There is little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. Limited evaluation of the extent to which changing immigration policy will benefit/harm the labour market or wider economy or no evaluation. <i>The information is basic and communicated in an unstructured way. The information is supported by limited evidence and the relationship to the evidence may not be clear.</i> 0 marks No response worthy of credit.		immigration increases labour market flexibility. <i>Analysis and Evaluation requires candidates to go beyond what is given in the case study.</i> Analysis may include: • Labour supply decreases/becomes more inelastic, pushing wages up and increasing costs of production. • International price competitiveness falls with higher labour costs. • Less attractive place for FDI when labour costs are higher/less skilled labour force. • Productive capacity falls as a result of a smaller labour force (LRAS shifts left). • Dependency ratio increases with an ageing population. • Budget deficit may increase as a result of falling tax revenue. • Reduction in remittances as a result of less immigrant workers will improve the current account. • AD falls as a result of less consumption from immigrants, harming growth and unemployment. Evaluation may include: • Wages/employment for low skilled workers increases, reducing poverty/inequality. • Higher domestic employment reduces government spending on benefits/reduces budget deficit/allows spending elsewhere. • AD increases as a result of higher wages, improving material standards of living. • Reduction in emigration means less human capital flight. • Demand for housing will fall, decreasing prices. • Less pressure on public services can reduce the budget deficit/allow spending elsewhere.

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					• Reduces the number of people who have access to welfare benefits may reduce government spending. • Skills shortages may reduce if a points based immigration system replaces free movement. • The government can offset the effects of skills shortages caused by falling immigration by instigating supply side policy. <u>Examiner's Comments</u> Candidates used the information in Extract 2 to good effect to produce well focused answers, with only a small minority of candidates writing about the general costs and benefits of the UK leaving the EU rather than concentrating on the impact of the end of free movement of labour. The vast majority attempted to base their answers around economic theory rather than unsupported political views. It is important that candidates read the question carefully; not doing this in some cases resulted in answers that considered the advantages and disadvantages of free movement of labour with scant reference to the ending of free movement. Some candidates could have improved their answers by going beyond re-stating the information given in Extract 2, the majority used this as a springboard for detailed analysis of the impact on both the UK labour market and the wider economy. Although diagrams were not required nor necessary to achieve full marks, a number of candidates used them to good effect to support their analysis – in Exemplar 4, the candidate explains that reduced immigration will shift long run aggregate supply and follows this with an excellent chain of analysis considering the impact on inflation and the current account of the balance of payments. Equally impressive microeconomic analysis was offered by some candidates, such as shifting labour supply to the left to show an increase in wages and an explanation of the likely

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			consequences of this, or the demand curve for housing shifting to the left as a result of the population falling. Exemplar 4 Ending the free movement of labour will lead to a fall in the level of immigration into the UK. Extract 2 suggests that high levels of immigration had "pushed up house prices", suggesting that reducing this immigration will lead to a lowering of house prices, and a fall in the variation in house prices across the UK. Lower house prices will lead to an increased ability and willingness of workers to move between different regions of the UK. This will lead to an increase in geographical mobility. This will result in an increased ability of labour to respond to changes in labour market conditions (such as changing wage rate or changing demand for labour) leading to an increase in geographical labour market flexibility, (as a result of the reduced immigration). Ending the free movement of labour leading to levels of immigration will also lead to a fall in the size of the UK's working age population.  This will lead to a fall in the productive capacity of the UK and cause LRAS to shift from LRAS₁ → LRAS₂ (reducing capacity from Y₁ → Y₂). This will lead to a fall in the level of long run economic growth, leading to a fall in incomes and potentially increased unemployment. The inward shift in LRAS will also lead to an increase in the general level of prices over time from P₁ → P₂. This will lead to an increase in (cost push) inflation in the UK economy, and may also lead to lower levels of international competitiveness of UK firms, leading to a fall in the value of net exports and a worsening of the UK's current account deficit on the BOP.
	Total	15	

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20	a	i	Calculate how much greater the UK's productivity gap was than the G7's in 2013. 10% points (16% - 6%) or 166.67% (10/6)	2 (AO1 x 1) (AO2 x 1)	Do not accept 10%.
		ii	Compare the trend in UK productivity and G7 productivity over the period shown. Between 1997 and 2007 productivity was on a strong upward trend in both the UK and G7 (1) productivity grew in the UK by approximately 20% points (25%) while it grew by approximately 30% points (35%) in the G7 (1) the gap in productivity between the UK and G7 was narrowing between 1997 and 2007 (1). After 2007 productivity growth slowed in the G7 whilst it failed to grow between 2007 and 2013 in the UK (1) the UK experienced a fall in 2009 whereas there was no decline in the G7 (1) the productivity gap widened between the G7 after 2007 (1) the G7 had a smoother upward trend than the UK's/the UK's trend fluctuated more (1).	2 (AO2 x 2)	
	b	i	Explain how it is possible for a country to have a negative average propensity to save. A country would be dissaving/spending more than its income (1) either by borrowing (1) or by using accumulated wealth (1)	2 (AO1 x 1) (AO2 x 1)	Note: maximum of 2 marks.

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		ii	Evaluate to what extent the information in Table 2 can be used to compare the value of the income multiplier in France and in Japan in 2014. Level 2 (5–8 marks) Good knowledge and understanding of the income multiplier. Good – strong analysis of the extent to which the information can be used to compare the value of the income multiplier. Good analysis will be in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Reasonable – strong evaluation of the extent to which the information can be used to compare the value of the income multiplier, considering both the usefulness and the limitations of the information and underpinned by appropriate theoretical analysis. Good evaluation will weigh up both sides/comparing alternatives but without reaching a supported judgement. Strong evaluation should include a supported judgement. Level 1 (1–4 marks) Limited – reasonable knowledge and understanding of the income multiplier. Limited – reasonable analysis of the extent to which the information can be used to compare the value of the income multiplier. Limited analysis will have little evidence of reasoning that addresses the question asked. There is a lack of a clear structure.	8 (AO1 x 1) (AO2 x 1) (AO3 x 3) (AO4 x 3)	<i>Indicative content</i> The average propensity to save (aps) often provides a strong indication of the marginal propensity to save (mps). A country with a high aps is likely to have a high mps. In the absence of other leakages, the multiplier is $1/\text{mps}$. In this case if $\text{aps} = \text{mps}$, France would have a multiplier of 6.67 and Japan would have the very high multiplier of 50. The mps, however, may not be the same as the aps. For example, as an economy gets richer it may become more confident and the mps may fall. There are also other leakages – the mrt and the mpm. If Japan has a higher marginal tax rate and spends a higher proportion of extra income on imports, it may have a smaller income multiplier than France. Limited – reasonable analysis of the extent to which the information can be used to compare the value of the income multiplier. Limited analysis will have little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. Reasonable analysis will have correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Limited evaluation of the extent to which the information can be used to compare the value of the income multiplier in the form of an unsupported statements or no evaluation.

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			Reasonable analysis will have correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Limited evaluation of the extent to which the information can be used to compare the value of the income multiplier in the form of an unsupported statements or no evaluation. 0 marks no response or no response worthy of credit. Note: although a diagram is not required, it may enhance the quality of the answer and should be rewarded at the appropriate level. <table><tr><th>Descriptor</th><th>Award mark</th></tr><tr><td>Consistently meets the criteria for this level</td><td>At top of level</td></tr><tr><td>Meets the criteria but with some slight inconsistency</td><td>Above middle and either below top of level or at middle of level (depending on number of marks available)</td></tr><tr><td>Just enough achievement on balance for this level</td><td>Above bottom and either below middle or at middle of level (depending on number of marks available)</td></tr><tr><td>On the borderline of this level and the one below</td><td>At bottom of level</td></tr></table>	Descriptor	Award mark	Consistently meets the criteria for this level	At top of level	Meets the criteria but with some slight inconsistency	Above middle and either below top of level or at middle of level (depending on number of marks available)	Just enough achievement on balance for this level	Above bottom and either below middle or at middle of level (depending on number of marks available)	On the borderline of this level and the one below	At bottom of level		
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			Total	14											

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21			Identify one example of discretionary fiscal policy in the stimulus material and explain how it could affect aggregate demand. Public sector investment in infrastructure (1) would increase AD as G is a component of AD (1).	2 (AO1 x 1) (AO2 x 1)	
			Total	2	
22			D	1 (AO3)	Rationale A This is likely to cause a shift in long run aggregate supply or a shift in aggregate demand, not a movement along the aggregate demand curve. B This would cause a shift of the AD curve rather than a movement along it. C This would cause a shift of the AD curve rather than a movement along it. D Correct: As the price level decreases the real value of households' wealth increases, which increases consumption.
			Total	1	
23			C	1 (AO2)	Rationale A This is the marginal propensity to withdraw $(0.11 + 0.23 + 0.17) = 0.51$ B Calculates the multiplier by adding all terms in the table together $= 0.71 + 0.11 + 0.23 + 0.17 + 0.42 = 1.64$ C Correct: Multiplier $= 1 / \text{MPW} = 1 / (0.11 + 0.23 + 0.17) = 1 / 0.51 = 1.96$ D Calculates the multiplier as $1 / \text{MPM} + \text{MPS} = 1 / 0.11 + 0.23 = 2.94$
			Total	1	

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24	Evaluate, with the use of an appropriate diagram(s), whether ending austerity is likely to result in the government achieving higher levels of economic growth. Level 3 (11–15 marks) Good knowledge and understanding of expansionary fiscal policy and economic growth. Good – strong analysis of the impact of ending austerity on economic growth. Good analysis will be in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Good - strong evaluation of the impact of austerity on economic growth, weighing up both sides/comparing alternatives. Strong evaluation should include a supported judgment. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and substantiated.</i> Level 2 (6–10 marks) Good knowledge and understanding of expansionary fiscal policy and economic growth. Reasonable analysis of the impact of ending austerity on economic growth. There is correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of	15 (AO1 x 2) (AO2 x 3) (AO3 x 4) (AO4 x 6)	Guidance: • A number of limited analytical/evaluative points can be awarded up to Reasonable, but to be awarded Good or Strong there needs to be greater depth of explanation. • A relevant and explained diagram is required for the Analysis or Evaluation to be awarded above Reasonable. • Strong evaluation requires an explained judgement. An explained judgement without Good evaluation can be credited as evaluation. • The side of the argument presented first should be credited as Analysis, with the other side credited as Evaluation. Knowledge & Understanding: Knowledge & Understanding marks should be awarded for impacts of ending austerity that are mentioned in the case study: ◦ Greek economy collapsed because of high debt/GDP ratio. ◦ UK debt/GDP ratio was 69% in 2010 and forecast to increase to more than 100%. ◦ Austerity is crucial in promoting future economic growth and stability. ◦ Conservatives committed to increase public expenditure and cut taxes. ◦ Labour committed to public sector pay rises, green transformation fund, compensating WASPI women and building social housing. ◦ Low cost of borrowing. ◦ UK has a relatively low debt/GDP ratio. ◦ Destroys reputation of fiscal responsibility. Analysis and Evaluation requires candidates to go beyond what is given in the case study.

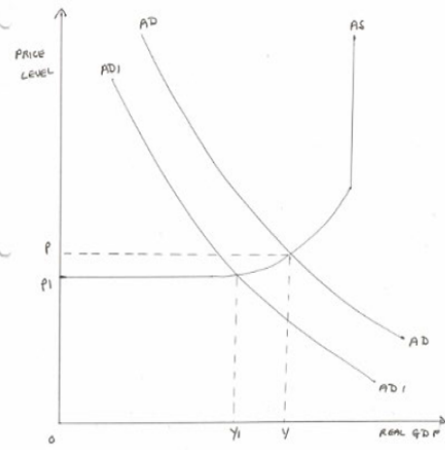
Mark Scheme

Question			Answer/Indicative content	Marks	Guidance
			reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Reasonable evaluation of the impact of austerity on economic growth. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i> Level 1 (1–5 marks) Limited – reasonable knowledge and understanding of expansionary fiscal policy and/or economic growth. Limited analysis of the impact of ending austerity on economic growth. There is little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. Limited evaluation of the impact of ending austerity on economic growth or no evaluation. <i>The information is basic and communicated in an unstructured way. The information is supported by limited evidence and the relationship to the evidence may not be clear.</i> 0 marks no response or no response worthy of credit.		Analysis may include: - Increasing public expenditure will result in AD increasing (G is a component of AD). - Tax cuts will increase consumption, increasing AD. - Increases in AD will generate economic growth. - Multiplier effect will result in further increases in consumption and investment, triggering further economic growth. - Accelerator effect may result in economic growth increasing still further. - Capital expenditure will result in productive capacity of the economy increasing – outward shift in LRAS will result in non-inflationary sustainable economic growth. Evaluation may include: - Public expenditure may crowd out private sector investment, meaning AD may not increase. - Multiplier may not be significant if leakages are large. - Depends on state of the global economy – interdependence means expansionary fiscal policy in UK may be ineffective if export markets are in recession. - Consumer and business confidence may fall if fiscal policy is not seen as credible, which could result in rising saving and falling consumption and investment. - Growth may fall in the future if future governments have to increase taxes/cut spending to pay back the debt it built up when increasing spending. - Depends on whether the capital expenditure results in economy growing enough to mean debt/GDP ratio falls despite higher levels of borrowing.

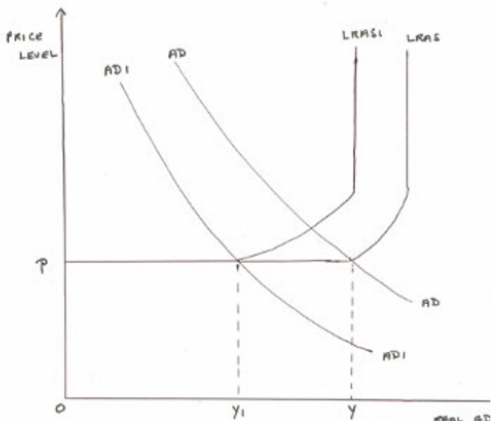
Mark Scheme

Question			Answer/Indicative content	Marks	Guidance
					<u>Examiner's Comments</u> There were several strong responses to this question which showed an impressive understanding of the debate surrounding how fiscal policy can be used to achieve economic growth, with a good use of the AD/AS model to support their responses. Candidates must make sure they read the question carefully – a small minority wrote an essay on introducing austerity rather than ending it.  Misconception Several candidates fell into the trap of offering generic analysis that ending austerity would be problematic because it is likely to cause demand-pull inflation. It is important that candidates read the extract carefully to understand the context in which the question is set – it is highly unlikely that austerity would be implemented in an environment when the economy is operating close to full capacity, which weakens this argument.
			Total	15	

Mark Scheme

Question	Answer/Indicative content	Marks	Guidance
25	Between 2017 and 2018, households in Denmark's saved more. Household saving as a percentage of disposable income rose from 5.6 to 5.9. Evaluate, with the use of an appropriate diagram(s), whether an increase in the amount households save will harm an economy. Level 5 (21–25 marks) Good -Strong knowledge and understanding of the nature of saving and macroeconomic indicators. Strong analysis of how an increase in the amount households save may affect an economy. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Strong evaluation of whether an increase in household saving will harm an economy, weighing up both why they might and why they might not and reaching a supported judgement. <i>There is a well-developed and sustained line of reasoning which is coherent and logically structured. The information presented is entirely relevant and substantiated.</i> Level 4 (16–20 marks) Good knowledge and understanding of the nature of saving and macroeconomic indicators. Strong analysis of how an increase in the amount households save may affect an economy. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any diagrams must be integral to the analysis.	25 (AO1 x 6 AO2 x 6 AO3 x 6 AO4 x 7)	<i>Indicative content</i> If households save more, they may be spending less. A reduction in consumer spending may discourage investment. This is because firms will expect to sell less and earn lower profits. As a result their incentive and ability to spend on capital goods will be reduced. Lower consumer expenditure and investment will reduce aggregate demand. If the economy is operating at less than full capacity, a decrease in aggregate demand will reduce output. The diagram shows real GDP falling from Y to Y1.  If firms are producing less goods and services, they may need fewer workers. This can result in a rise in cyclical unemployment. Some of the workers who lose their jobs may lose their skills and confidence and so may find it difficult to find other jobs when economic activity picks up. A reduction in investment would also reduce productive capacity. This again could result in a decrease in output as shown in the diagram. In this case both aggregate demand and aggregate supply decrease.

Mark Scheme

Question	Answer/Indicative content	Marks	Guidance
	Good evaluation of whether an increase in household saving will harm an economy and will weigh up both sides but without reaching a supported judgement. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and in the most part substantiated.</i> Level 3 (11–15 marks) Good knowledge and understanding of the nature of saving and macroeconomic indicators. Good analysis of how an increase in the amount households save may affect an economy. There is correct analysis in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Reasonable evaluation of whether an increase in household saving will harm an economy, considering both why it might and why it might not. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i> Level 2 (6–10 marks) Good knowledge and understanding of the nature of saving and macroeconomic indicators. Reasonable analysis of how an increase in the amount households save may affect an economy. There is correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Reasonable evaluation of whether an		 An increase in saving may, however, benefit an economy. If the economy is operating at or close to full capacity, a reduction in consumer spending may reduce inflationary pressure. A reduction in spending by households may also improve the current account position. Households may reduce spending on imports. It is also possible that domestic firms, faced with lower domestic demand, may put more effort into finding export markets. More saving may increase the funds available for investment. Banks may receive more deposits, which can be used as the basis for loans to firms to spend on capital goods. More available loanable funds may also lower the rate of interest. This will make it cheaper for firms to borrow. This could encourage them to borrow more, if they expect consumer expenditure to rise in the future. In addition, households may both save and spend more, if their incomes are rising. In this case, firms will have both the incentive to invest access to the funds to invest. Whether an increase in the amount households save will harm an economy will depend on the initial productive capacity, the initial current account position, the key influences on investment and whether income is increasing. It may be more harmful if the rise in saving is accompanied by a fall in consumer expenditure and the economy is initially operating with spare

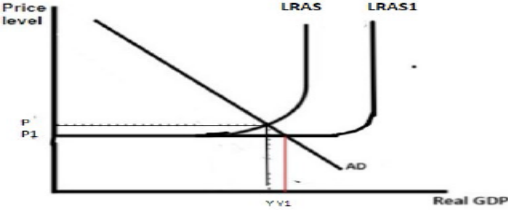
Mark Scheme

Question			Answer/Indicative content	Marks	Guidance								
			increase in household saving will harm an economy, considering both why it might and why it might not. <i>The information has some relevance, but is communicated in an unstructured way. The information is supported by limited evidence, the relationship to the evidence may not be clear.</i> Level 1 (1–5 marks) Reasonable knowledge and understanding of the nature of saving and macroeconomic indicators. Limited or no analysis of how an increase in the amount households save may affect an economy. There is little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. The relevant diagram(s) may not be present or are incorrectly labelled. Limited evaluation of whether an increase in household saving will harm an economy, in the form of an unsupported statement or no evaluation. <i>Information presented is basic and may be ambiguous or unstructured. The information is supported by limited evidence.</i> 0 marks No response worthy of credit. <table><tr><th>Descriptor</th><th>Award mark</th></tr><tr><td>Consistently meets the criteria for this level</td><td>At top of level</td></tr><tr><td>Meets the criteria but with some slight inconsistency</td><td>Above middle and either below top of level or at middle of level (depending on number of marks available)</td></tr><tr><td>Just enough achievement on</td><td>Above bottom and either below middle</td></tr></table>	Descriptor	Award mark	Consistently meets the criteria for this level	At top of level	Meets the criteria but with some slight inconsistency	Above middle and either below top of level or at middle of level (depending on number of marks available)	Just enough achievement on	Above bottom and either below middle		capacity. If a country already has a current account surplus, the need to reduce imports will be less than if it had a current account deficit. More saving may increase the availability and reduce the cost of loanable funds but if consumers are buying less of their products, firms may not want to invest. <u>Examiner's Comments</u> Question 2 was the more popular of the two options in this section and there were some very strong responses, who fully integrated correct diagrams into their responses, giving a balanced view of how increased savings may harm an economy and how increased savings may not. Context and own knowledge were also evident. The stem relating to Denmark could also be used to make a judgement. Stronger responses tended to focus on how an increase in savings would reduce consumption, and hence reduce AD and therefore lead to a fall in economic growth and then expanded that to show how it would also lead to a fall in employment. Other valid discussions explored how a fall in spending would discourage investment and lead to a fall in productive capacity and a fall in LRAS. The stronger counterbalance responses discussed how a fall in AD would lead to a fall in inflationary pressure, plus less spending may lead to less imports and improve the current account of the balance of payments. Judgements were strong when they considered the amount of spare capacity, whether incomes were also rising and whether the increase in savings from 5.6% to 5.9% was significant enough to have much of an impact.
Descriptor	Award mark												
Consistently meets the criteria for this level	At top of level												
Meets the criteria but with some slight inconsistency	Above middle and either below top of level or at middle of level (depending on number of marks available)												
Just enough achievement on	Above bottom and either below middle												

Mark Scheme

Question			Answer/Indicative content		Marks	Guidance
			balance for this level	or at middle of level (depending on number of marks available)		
			On the borderline of this level and the one below	At bottom of level		
			Total		25	

Mark Scheme

Question	Answer/Indicative content	Marks	Guidance
26	In March 2018 the French government announced that children would have to start school at age 3 rather than age 6 from September 2019. Evaluate, with the use of an appropriate diagram(s), whether a fall in the compulsory school starting age will benefit an economy. Level 5 (21–25 marks) Good -Strong knowledge and understanding of aggregate demand and aggregate supply. Strong analysis of how a fall in the school starting age will affect an economy. It will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Strong evaluation of whether a fall in the school starting age will benefit an economy, weighing up both why it might and why it might not and reaching a supported judgement. <i>There is a well-developed and sustained line of reasoning which is coherent and logically structured. The information presented is entirely relevant and substantiated.</i> Level 4 (16–20 marks) Good knowledge and understanding of aggregate demand and aggregate supply. Strong analysis of how a fall in the school starting age will affect an economy. It will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis.	25 (AO1 × 6 AO2 × 6 AO3 × 6 AO4 × 7)	For a mark at the top of each level the response should be in context. A fall in the compulsory school starting age will mean that children will start school at a younger age and therefore will have more years of schooling, should the leaving age remain the same. Analysis of how a fall in the school starting age will affect an economy might include: • A lowering of the age at which children have to start school may raise the size of the labour force due to parents being able to seek work when their children are younger, at least in the short run. • If children's skills and qualifications increase as a result of them starting their education earlier, they may go on to further education and improve the quality/skills of the labour force which could lead to a rise in the productivity of labour. If workers are more productive, the long run aggregate supply curve will shift to the right as shown in the diagram.  • The country's output would rise. A more skilled and qualified labour force is likely to experience lower structural unemployment and higher incomes. A better-quality labour force may increase net exports as a result of greater price and quality competitiveness. It may also attract multinational companies to set up in the country. As well as providing employment, MNCs may bring in new production methods and management techniques. Evaluation of whether a fall in the school starting age will benefit an economy might

Mark Scheme

Question	Answer/Indicative content	Marks	Guidance
	Good evaluation of whether a fall in the school starting age will benefit an economy, weighing up both why it might and why it might not without reaching a supported judgement. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and in the most part substantiated.</i> Level 3 (11–15 marks) Good knowledge and understanding of aggregate demand and aggregate supply. Good analysis of how a fall in the school starting age will affect an economy. There is correct analysis in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Reasonable evaluation of whether a fall in the school starting age will benefit an economy, considering both sides. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i> Level 2 (6–10 marks) Good knowledge and understanding of aggregate demand and aggregate supply. Reasonable analysis of how a fall in the school starting age will affect an economy. There is correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Reasonable evaluation of whether a fall in the school starting age will benefit an economy, considering both sides.		include: • If the government provides state education, a lowering of the school leaving age will increase government spending. This will involve an opportunity cost. This may take three main forms. The government may have to sacrifice spending on, for instance healthcare. There is the possibility that tax payers may have to bear the opportunity cost. This is because the government may raise tax rates or widen the tax base to finance the extra spending. Higher tax rates may have a disincentive effect. • It is also possible that the government may borrow to raise the finance. In this case, funds used by the government will not be available to other borrowers. Higher government borrowing could also raise the rate of interest. • Higher government spending may increase aggregate demand which may create inflationary pressure, at least in the short run. • There is no guarantee that requiring all children to start school earlier will increase their skills and qualifications. A supported judgement might include: • Until recently, the trend has been to increase the school leaving age. More countries may now consider lowering the starting age as they may consider that the benefits will exceed the costs. A lower compulsory age may improve macroeconomic performance and the quality of people's lives. • It will depend on the quality of education provided. In turn, this will be influenced by the quality of the extra resources used. • It will depend on how productive parents joining the workforce are, when their children start school early/if they join the workforce.

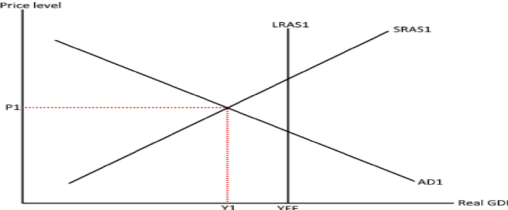
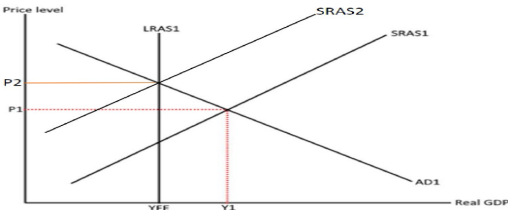
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Question			Answer/Indicative content	Marks	Guidance								
			<i>The information has some relevance, but is communicated in an unstructured way. The information is supported by limited evidence, the relationship to the evidence may not be clear.</i> Level 1 (1–5 marks) Reasonable knowledge and understanding of aggregate demand and aggregate supply. Limited or no analysis of how a fall in the school starting age will affect an economy. There is little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. The relevant diagram(s) may not be present or are incorrectly labelled. Limited evaluation of whether a fall in the school staring age will benefit an economy, in the form of an unsupported statement or no evaluation. <i>Information presented is basic and may be ambiguous or unstructured. The information is supported by limited evidence.</i> 0 marks no response or no response worthy of credit. <table><tr><th>Descriptor</th><th>Award mark</th></tr><tr><td>Consistently meets the criteria for this level</td><td>At top of level</td></tr><tr><td>Meets the criteria but with some slight inconsistency</td><td>Above middle and either below top of level or at middle of level (depending on number of marks available)</td></tr><tr><td>Just enough achievement on balance for this level</td><td>Above bottom and either below middle or at middle of level (depending on number of marks</td></tr></table>	Descriptor	Award mark	Consistently meets the criteria for this level	At top of level	Meets the criteria but with some slight inconsistency	Above middle and either below top of level or at middle of level (depending on number of marks available)	Just enough achievement on balance for this level	Above bottom and either below middle or at middle of level (depending on number of marks		
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				available)		
			On the borderline of this level and the one below	At bottom of level		
			Total			

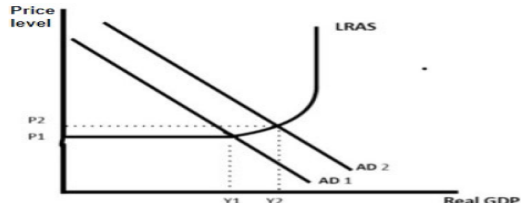
Mark Scheme

Question	Answer/Indicative content	Marks	Guidance
27	In 2017 Bosnia had a significant output gap while it was estimated that Slovenia did not have an output gap. Evaluate, with the use of an appropriate diagram(s), whether a government should always seek to reduce an output gap. Level 5 (21–25 marks) Good - Strong knowledge and understanding of output gaps. Strong analysis of why a government should seek to reduce an output gap. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Strong evaluation of whether a government should always seek to reduce an output gap, weighing up both why they might and why they might not and reaching a supported judgement. <i>There is a well-developed and sustained line of reasoning which is coherent and logically structured. The information presented is entirely relevant and substantiated.</i> Level 4 (16–20 marks) Good knowledge and understanding of output gaps. Strong analysis of why a government should seek to reduce an output gap. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis.	25 (AO1 × 6 AO2 × 6 AO3 × 6 AO4 × 7)	For a mark at the top of each level the response should be in context. An output gap is the difference between actual and potential output. A negative output gap involves an economy operating at less than its potential output. Possible analysis as to why a government should seek to reduce an output gap might include: - When an economy has a negative output gap. Output is at Y1, below the country's potential output of YFE. The existence of unemployed resources can impose considerable costs. These include loss of tax revenue, higher spending on welfare benefits, reduced living standards and a decline in workers' skills  - A positive output gap occurs when the economy produces more than the long run potential. The diagram shows macroeconomic disequilibrium, this time arising from output being above the long run potential output.  - This type of output gap will create inflationary pressure. The factors of production would be over-utilised, which could not be sustained, so the cost of production would increase (workers may be paid overtime) this

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	Good evaluation of whether a government should always seek to reduce an output gap and will weigh up both sides but without reaching a supported judgement. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and in the most part substantiated.</i> Level 3 (11–15 marks) Good knowledge and understanding of output gaps. Good analysis of it will be beneficial to reduce an output gap. There is correct analysis in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Reasonable evaluation of whether a government should always seek to reduce an output gap, considering both why it might and why it might not. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i> Level 2 (6–10 marks) Good knowledge and understanding of output gaps. Reasonable analysis of the effects of output gaps. There is correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Reasonable evaluation of whether it will be beneficial to reduce an output gap, considering both why it might and why it		would shift SRAS1 to SRAS2 which would increase the price level from P1 to P2 which would be inflationary. Evaluation of whether a government should not always seek to correct an output gap might include: • There is some debate as to whether inflation creates more harm to an economy than unemployment. • Some Neo-classical economists argue that in the case of both types of output gap, the government does not have to take action. This is because they think that the economy will move to the long run macroeconomic equilibrium by adjustments in wages and raw material prices. • In the case of a negative output gap, the higher unemployment may make workers be prepared to accept lower wages. Suppliers of raw materials may lower their prices to raise demand for their products. If wages and raw materials prices do fall, the SRAS curve will shift to the right and long run macroeconomic equilibrium will be achieved at the productive potential • In the case of a positive output gap, the SRAS curve will shift to the left. This is because workers and suppliers will demand higher wages and prices once they realise that inflation has eroded the real value of the payments they are receiving. • Keynesian economists, however, argue that output gaps are not self-correcting and can continue in the long run. In the case of a negative output gap, wages may be 'sticky' downwards. There are a number of reasons for this. One is that, despite high unemployment, some workers may resist wage costs. Employers may also be reluctant to cut wages as it may have a negative effect on workers' motivation. Their ability to cut wages will also be influenced by the length of workers' contracts. • The diagram shows that to reduce a

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	might not. <i>The information has some relevance, but is communicated in an unstructured way. The information is supported by limited evidence, the relationship to the evidence may not be clear.</i> Level 1 (1–5 marks) Reasonable knowledge and understanding of output gaps. Limited or no analysis of the effects of output gaps. There is little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. The relevant diagram(s) may not be present or are incorrectly labelled. Limited evaluation of whether it will be beneficial to reduce an output gap, in the form of an unsupported statement or no evaluation. <i>Information presented is basic and may be ambiguous or unstructured. The information is supported by limited evidence.</i> 0 marks no response or no response worthy of credit. <table><tr><th>Descriptor</th><th>Award mark</th></tr><tr><td>Consistently meets the criteria for this level</td><td>At top of level</td></tr><tr><td>Meets the criteria but with some slight inconsistency</td><td>Above middle and either below top of level or at middle of level (depending on number of marks available)</td></tr><tr><td>Just enough achievement on balance for this level</td><td>Above bottom and either below middle or at middle of level (depending on number of marks available)</td></tr><tr><td></td><td></td></tr></table>	Descriptor	Award mark	Consistently meets the criteria for this level	At top of level	Meets the criteria but with some slight inconsistency	Above middle and either below top of level or at middle of level (depending on number of marks available)	Just enough achievement on balance for this level	Above bottom and either below middle or at middle of level (depending on number of marks available)				long run negative output gap, the government would have to increase aggregate demand from AD to AD1. In this case, the government would have to trade off lower unemployment with higher inflation.  Possible supported judgements might include: • A positive output gap may be more likely to be self-correcting as it is difficult to sustain an output beyond the maximum potential for long. The higher costs that will be generated are likely to reduce output. • A government may consider taking action to reduce an output gap if it is a negative output gap which will not be self-correcting and if it is prepared to accept a higher inflation rate. • Whether a government should seek to reduce an output gap depends on the type of the output gap, whether the output gap will be self correcting and whether the measures it may take may harm its macroeconomic objectives
Descriptor	Award mark												
Consistently meets the criteria for this level	At top of level												
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			On the borderline of this level and the one below	At bottom of level	
			Total	25	
28	a		Using Fig.1, explain the relationship between changes in consumer expenditure and changes in income. Direct/positive relationship between consumer expenditure and income/rise in income results in a rise in consumer expenditure (1). The proportion of income spent falls as income rises/average propensity to consume falls as income rises (1). At low levels of income, people spend more than their income/ there is dissaving/people spend savings/benefits (1) Gradient decreases as it becomes more attractive to save (1)	2 (AO2 × 2)	Annotate with 
	b		Calculate Switzerland's marginal propensity to withdraw. 0.67 (2). Formula for the multiplier/correct working. (1)	2 (AO2 × 2)	Annotate with  Accept 2/3 with workings (2) Formula: $\Delta Y/\Delta J$ or $1/\text{mpw}$. Correct working: $\\$300\text{m}/200\text{m} = 1.5$. $1.5 = 1/\text{mpw}$.
			Total	6	