

Please write clearly in block capitals.

Centre number

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Candidate number

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Surname *StemUp Model Solution*

Forename(s)

Candidate signature

I declare this is my own work.

INTERNATIONAL A-LEVEL ECONOMICS

Unit 4 Economic Development and the Global Economy

Friday 21 June 2024

07:00 GMT

Time allowed: 2 hours

Materials

For this paper you must have:

- the Source Booklet, provided as an insert (enclosed)
- a calculator, which you are expected to use where appropriate.

Instructions

- Use black ink or black ball-point pen. Pencil should only be used for drawing.
- Fill in the boxes at the top of this page.
- Answer **all** questions in **Sections A, B and C**.
- Answer **EITHER** Question 15 **OR** Question 16 in **Section D**.
- You must answer the questions in the spaces provided. Do **not** write outside the box around each page or on blank pages.
- Do **not** write in the Source Booklet.
- If you need extra space for your answer(s), use the lined pages at the end of this book. Write the question number against your answer(s).
- Do all rough work in this book. Cross through any work you do not want to be marked.

Information

- The marks for questions are shown in brackets.
- The maximum mark for this paper is 90.
- You may use a bilingual dictionary for this exam.
- You may **not** use an English dictionary.

For Examiner's Use	
Question	Mark
1–10	
11	
12	
13	
14	
15	
16	
TOTAL	



J U N 2 4 E C O 4 0 1

Section A

Answer **all** questions in the spaces provided.

Only **one** answer per question is allowed.

For each question completely fill in the circle alongside the appropriate answer.

CORRECT METHOD 

WRONG METHODS    

If you want to change your answer you must cross out your original answer as shown. 

If you wish to return to an answer previously crossed out, ring the answer you now wish to select as shown. 

0 1

Which one of the following is most likely to be a **disadvantage** of globalisation for a more economically developed country (MEDC)?

[1 mark]

A A fall in labour productivity

☐

B A reduction in choice and variety of products

☐

C A rise in structural unemployment

☒

D An increase in the price of imports

☐


0 2

Table 1 shows the number of apples **or** oranges that Country X and Country Y are able to produce with a given amount of resources.

Table 1

	Apples		Oranges
Country X	16	OR	8
Country Y	8	OR	2

Using the model of comparative advantage, which one of the following terms of trade will allow both countries to benefit from trade?

[1 mark]**A** 2 apples = 1 orange☐**B** 3 apples = 1 orange☒**C** 4 apples = 1 orange☐**D** 8 apples = 1 orange☐**0 3**

Which one of the following is a function of the World Trade Organisation (WTO)?

[1 mark]**A** Arranging long-term loans for less economically developed countries☐**B** Helping countries reach agreements that lead to a reduction in tariffs☒**C** Identifying and helping to reduce risks to international financial stability☐**D** Providing short-term finance to countries with a balance of trade deficit☐**Turn over for the next question****Turn over ►**

0 4

Table 2 shows a country's nominal GDP, its population and average price index in 2021 and 2023.

Table 2

	Nominal GDP (\$)	Population	Price index
2021	60 billion	10.0 million	120
2023	80 billion	10.2 million	140

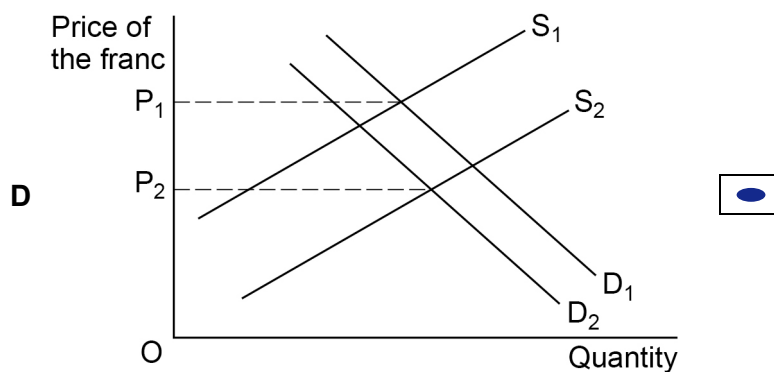
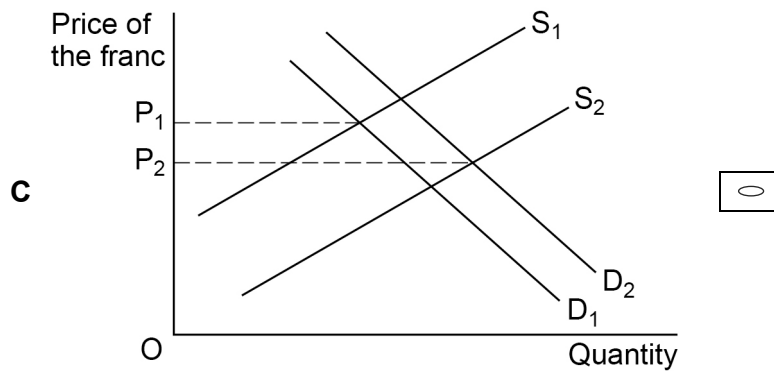
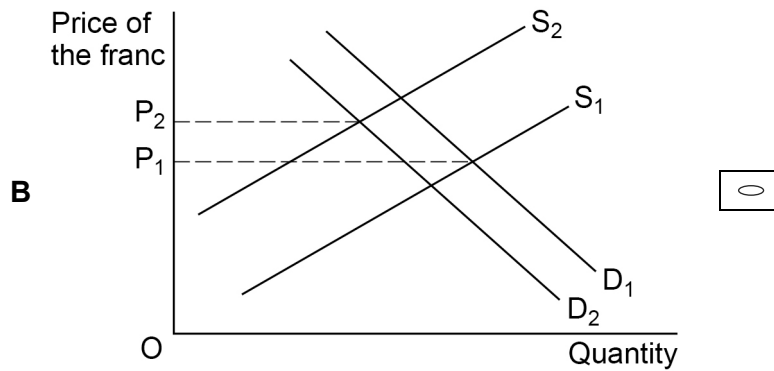
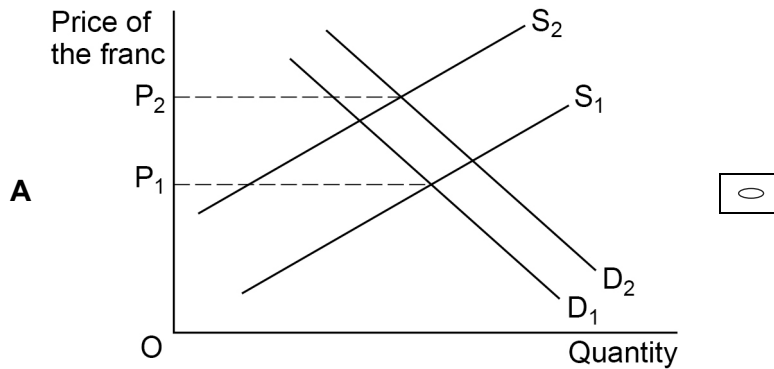
Between 2021 and 2023, the country's real GDP per head increased by

[1 mark]**A** 12.04%
☒
B 14.28%
☐
C 26.33%
☐
D 30.72%
☐


0 5

The diagrams below show the demand (D) and supply (S) of francs on the foreign exchange market. The initial price of the franc is P_1 . The country with the franc as its currency has a higher rate of inflation than other countries.

All other things being equal, which one of the following diagrams illustrates the most likely effect of the country's higher rate of inflation on the price of the franc?

[1 mark]**Turn over ►**

0 6

The government of a country decides to increase its expenditure on infrastructure by \$7 billion. The country's marginal propensity to save (MPS) is 0.15, its marginal propensity to tax (MPT) is 0.23 and its marginal propensity to import (MPM) is 0.22.

As a result of this increase in spending on infrastructure, in the short run, aggregate demand and national income will increase by

[1 mark]

A \$8.24 billion

☐

B \$11.67 billion

☒

C \$17.50 billion

☐

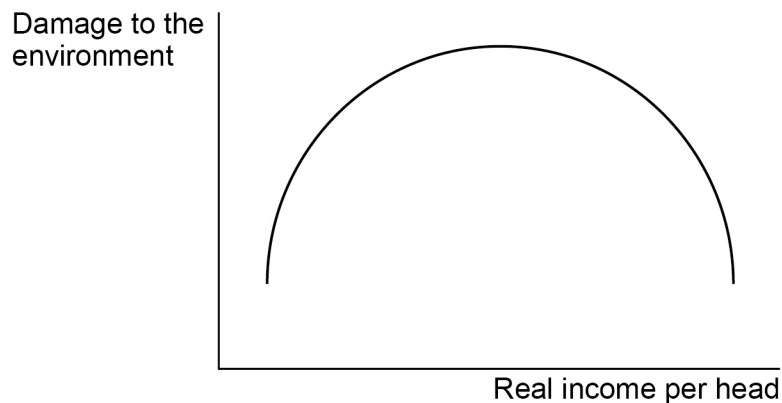
D \$46.67 billion

☐

0 7

Figure 1 shows an environmental Kuznets curve.

Figure 1



The environmental Kuznets curve suggests that

[1 mark]

A a high rate of economic growth causes more damage to the environment than a low rate of economic growth.

☐

B at high levels of real income per head, damage to the environment falls as real income per head increases.

☒

C economic development increases real income per head but also damages the environment.

☐

D there is an inverse relationship between real income per head and damage to the environment.

☐


0 8

The financial institutions in the shadow banking market

[1 mark]**A** are high risk because they borrow long term and lend short term.☐**B** are not licensed and regulated by governments or central banks.☒**C** lend to firms but not to individuals or governments.☐**D** often act as lender of last resort to commercial and investment banks.☐**0 9****Table 3** shows a summary of the balance of payments account for Greece in 2021.**Table 3**

	€ million
Balance of trade in goods	–26 719.1
Balance of trade in services	12 845.0
Primary income	368.7
Secondary income	1 233.8
Capital account	4 000.9
Financial account	7 107.6
Balancing item	1 163.1

Which one of the following is correct?

In 2021, Greece

[1 mark]**A** had a current account deficit of €12 271.6 million.☒**B** had a current account deficit of €13 874.1 million.☐**C** invested €4 000.9 million in other countries.☐**D** invested €11 108.5 million in other countries.☐**Turn over ►**

1 0

For many less economically developed countries (LEDs), remittances are an important and growing source of funds.

Which one of the following is most likely to explain why the value of remittances received by many LEDs has grown?

[1 mark]

- A** A rise in investment abroad by large transnational corporations
- B** A rise in the value of loans given to poorer countries by the World Bank
- C** An increase in the number of people living and working abroad
- D** An increase in the value of international trade in goods and services

☐☐☒☐**10**

Section B

Answer **all** questions in the spaces provided.

1	1
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In financial markets, assets such as shares, bonds and foreign currency are bought and sold.

1	1	.	1
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What is the difference between the money market and the capital market?

[2 marks]

The money market provides short-term finance, trading securities such as bills with less than a year to maturity, whereas the capital market provides medium and long-term finance, trading shares and bonds with more than a year to maturity.

Question 11 continues on the next page

Turn over ►



1 1 . 2

A firm wants to take out a loan of \$275 000 to finance the purchase of a piece of machinery.

The firm is considering two options, shown in **Table 4**.

For each option, the loan is paid back at the end of the period. The interest is calculated and paid at the end of each year.

Table 4

Option	Rate of interest	Period of loan
1	6.7%	3 years
2	5.8%	4 years

Calculate the difference between the amount of interest the firm would have to pay for Option 1 compared to Option 2.

[4 marks]

$$\text{Option 1: interest} = \$275\,000 \times 0.067 \times 3 = \$55\,275$$

$$\text{Option 2: interest} = \$275\,000 \times 0.058 \times 4 = \$63\,800$$

$$\text{Difference} = \$63\,800 - \$55\,275 = \$8525$$

Answer: \$8525 more interest is paid with Option 2 than Option 1.



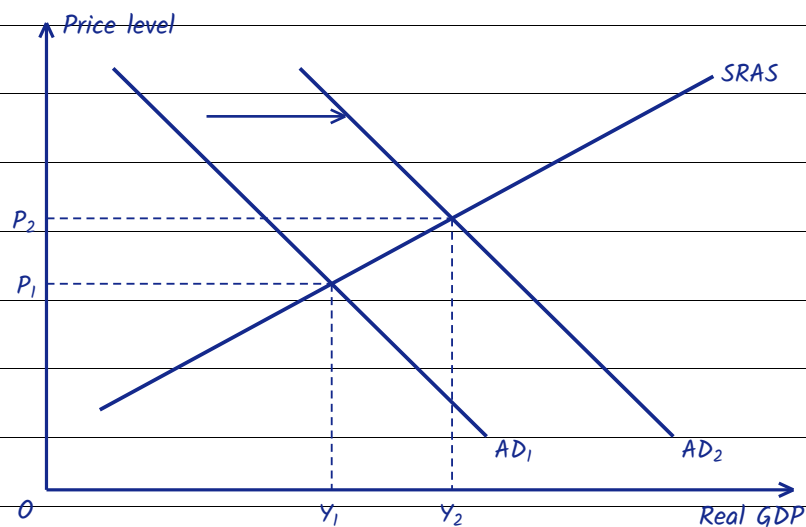
1 1 3

Explain, using a diagram, how a fall in interest rates is likely to affect a country's short-run rate of economic growth.

[4 marks]

Short-run economic growth is the annual percentage increase in real GDP, caused by an increase in aggregate demand (AD) that uses spare capacity.

A fall in interest rates makes borrowing cheaper and saving less rewarding, so households spend more on consumption, especially durables bought on credit, and firms invest more because more projects become profitable.



Lower interest rates may also cause a fall in the exchange rate as hot money flows out, making exports cheaper and imports dearer, so net exports rise. As C , I and $(X - M)$ increase, AD shifts right from AD_1 to AD_2 . Firms produce more, so real GDP rises from Y_1 to Y_2 , increasing the short-run rate of economic growth (the price level also rises from P_1 to P_2).



Section C

Look at the Source Booklet and answer **all** questions in the spaces provided.

Do **not** write in the Source Booklet.

1 2

Extract A shows the world market price of copper and the terms of trade for Chile.

1 2 . 1

Explain why the price of copper is likely to affect the terms of trade for Chile.

[4 marks]

The terms of trade measure the price of a country's exports relative to the price of its imports: $\text{index of export prices} \div \text{index of import prices} \times 100$.

Copper is Chile's main export, so its world price has a large weight in Chile's index of export prices. A rise in the price of copper raises the export price index and, other things being equal, increases the terms of trade index. This is an improvement: Chile can buy more imports with a given quantity of exports.

Conversely, a fall in the price of copper lowers the export price index, causing a deterioration in the terms of trade, so more copper must be exported to pay for the same imports.

Extra space



1 2 . 2

To what extent do the data suggest that the price of copper affected the terms of trade for Chile between 2012 and 2021?

Use the data in **Extract A** to support your answer.

[4 marks]

The data suggest that the price of copper had a strong effect. Between 2012 and 2021 the price of copper rose from US\$7962 to US\$9317 per tonne (about 17%) and Chile's terms of trade improved from 109.2 to 132.0 (about 21%), a direct relationship.

Similarly, between 2012 and 2015 the copper price fell by about 31%, from US\$7962 to US\$5510, and the terms of trade deteriorated from 109.2 to 100.0. From 2018 to 2019 the price fell from US\$6530 to US\$6010 and the terms of trade fell from 109.2 to 107.3.

However, between 2015 and 2016 the copper price fell from US\$5510 to US\$4868 (12%) yet the terms of trade improved from 100.0 to 103.1, which is inconsistent. This suggests other factors also matter, such as changes in import prices (for example oil), the prices of Chile's other exports and the

Extra space exchange rate.

Overall, the data show a strong positive correlation in most years, so the price of copper appears to be the main, but not the only, influence on Chile's terms of trade.



1 3

Extract B (line 1) states: 'Copper is the third most widely-used metal in the world but its price fluctuates.'

Explain possible reasons for fluctuations in the world market price of copper.

[12 marks]

The world market price of copper fluctuates when it rises and falls around its trend over time. Short-run fluctuations happen from month to month, while long-run fluctuations follow the economic cycle and changes in mining capacity. The price is set by the interaction of world demand and supply, so it changes when either curve shifts.

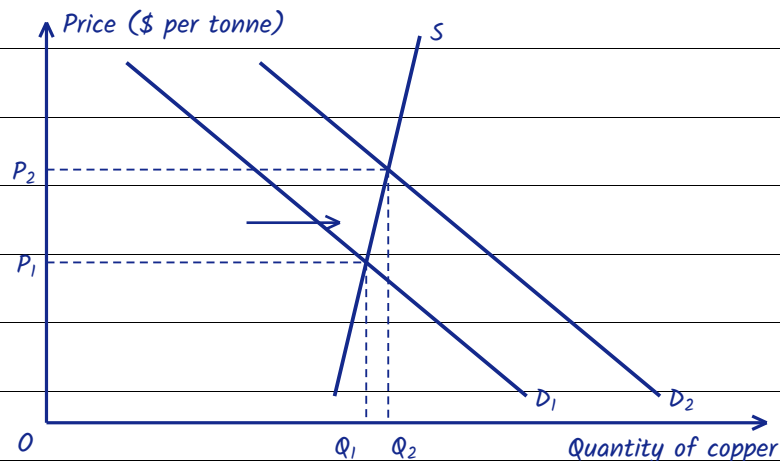
Demand for copper is a derived demand, since it is used in wiring, construction, electrical goods and vehicles. When the world economy grows strongly, especially China, which buys about half of world copper, construction and manufacturing expand and demand shifts right. Copper has a positive and fairly high income elasticity of demand, so demand rises more than proportionately in booms and falls sharply in recessions, as in 2015 when Chinese growth slowed. Government spending on infrastructure has the same effect. Policies to reduce global warming raise demand because electric vehicles, wind turbines and power grids use much more copper. Demand also depends on the price of substitutes such as aluminium: if aluminium becomes cheaper, the positive cross elasticity of demand means demand for copper falls.

Supply can shift too. New discoveries and investment in new mines increase supply, though with a long time lag, and better mining technology lowers costs. Supply falls when production costs rise, for example energy and water costs, or when output is disrupted by earthquakes in producing regions such as Chile, strikes by mine workers, falling ore grades, or environmental protests and tighter regulation. Increased recycling of scrap copper adds to supply.



These shifts cause large price changes because both demand and supply are price inelastic in the short run. Copper has few close substitutes and is a small part of the cost of final goods, so PED is low, while mines take years to open, so PES is low. In the diagram, an increase in demand from D_1 to D_2 raises the price sharply from P_1 to P_2 with only a small rise in quantity.

Speculation can make fluctuations worse. Copper is traded on commodity markets, and if dealers expect prices to rise they buy, which increases demand and makes the expectation self-fulfilling; the release of stocks or additions to stocks also change the amount available. Finally, copper is priced in US dollars, so a fall in the value of the dollar makes copper cheaper for buyers using other currencies, raising demand and the dollar price. As many of these factors change at the same time, the price of copper is volatile.



1 4

Extract C (line 5) states: 'Chile has been the world's largest producer of copper for over 30 years.'

Discuss ways in which the copper industry affects the economic development of Chile.

[25 marks]

Economic development is an improvement in living standards and welfare, including higher real income per head, better health and education, less poverty and inequality and more opportunities for people, achieved sustainably. As Extract C states, Chile has been the world's largest producer of copper for over 30 years, and copper is by far its largest export, so the industry has a major influence.

First, copper raises national income and economic growth. Investment in mines and copper exports are injections into the circular flow, raising $C + I + G + (X - M)$, so AD shifts right, and through the multiplier effect incomes rise in supplying industries such as engineering, transport, energy and construction, and in services where miners spend their wages.

Investment also adds to the capital stock and shifts LRAS to the right, increasing productive potential, as shown in the diagram. Higher real GDP per head allows more consumption of goods and services, one of the main measures of development.

Second, the industry provides jobs, often well paid, and develops skills in engineering and management. Mining TNCs and the state-owned Codelco bring capital, technology and expertise, and help fund infrastructure such as roads, ports, power and water supplies, which benefit other industries too.

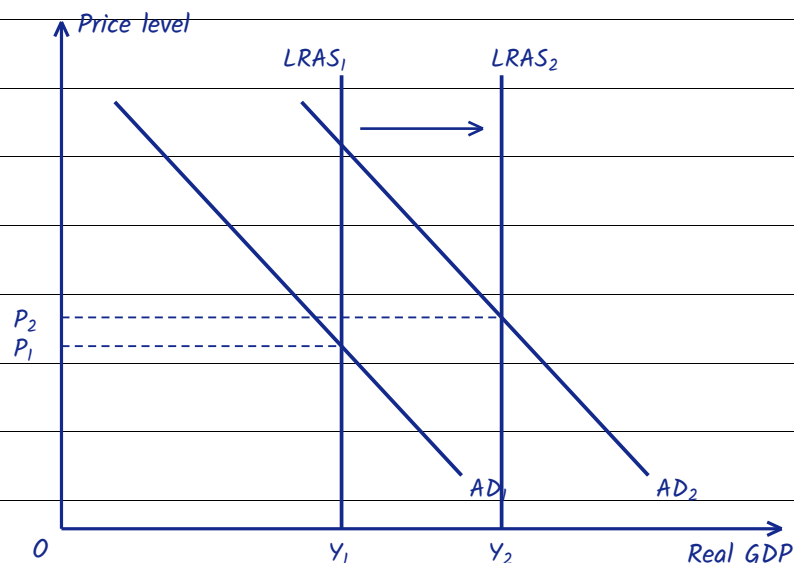
Third, copper earns foreign currency, supporting the current account and allowing Chile to import capital goods, medicines and technology it cannot produce. It also builds foreign exchange reserves, which help the central bank manage the exchange rate. Finally, the government receives tax revenue and royalties from copper firms and profits from Codelco, which can finance



spending on education, health care, pensions and anti-poverty programmes.

This improves human capital and HDI, so the gains go beyond income.

However, the impact depends on several factors. Most mines are in the north, such as the Atacama, so the benefits may be localised in particular regions, and mining is capital intensive, so it creates relatively few jobs. The



multiplier may also be small if machinery is imported and profits leave the country, because leakages from the circular flow are high. Much of the profit made by foreign TNCs may be repatriated rather than reinvested in Chile, and high wages in mining may widen inequality.

The volatility of the copper price is a serious problem. As Extract A shows, the price fell from US\$7962 per tonne in 2012 to US\$4868 in 2016. When prices fall, export earnings, tax revenue and investment fall, the peso depreciates and growth slows, making it hard to sustain long-term public spending. Heavy dependence also risks the natural resource curse and Dutch disease: in booms the currency appreciates and makes manufacturing and other exports less competitive, so the economy remains undiversified. Chile has reduced this risk with a fiscal rule that saves copper revenue in a

Turn over ►



Extra space *sovereign wealth fund during booms and spends it in slumps, so the effect depends on the quality of government and institutions.*

The importance of copper should also be kept in perspective. Services such as finance, retail and tourism account for a much larger share of Chile's GDP and employment than mining, and exports of fruit, wine and salmon have grown. Chile's development therefore also reflects stable macroeconomic policy, openness to trade and investment in education, not just copper. In the short run a copper boom raises incomes quickly, but in the long run development depends on whether copper revenue is turned into human and physical capital that will last after the mines are exhausted.

Mining also has environmental costs: it uses large amounts of scarce water, pollutes land and rivers and can harm local and indigenous communities, reducing welfare and sustainability unless firms are regulated effectively. In the long run, reserves and ore grades will decline, but demand for copper for electric vehicles and renewable energy may keep the industry valuable for decades.

In conclusion, the copper industry has made a large positive contribution to Chile's economic development, through higher incomes, foreign exchange and tax revenue, which helps explain why Chile is one of the richest countries in Latin America. However, the benefits depend on how revenue is used, whether price volatility is managed and whether the economy diversifies, for example into services. On balance, I believe its effect is positive but should be supported by policies to reduce inequality and environmental damage.



Section D

Answer **EITHER** Question 15 **OR** Question 16.

Shade the circle below to indicate which optional question you have answered.

Question 1 5 ☐Question 1 6 ☒CORRECT METHOD ☒

WRONG METHODS

**Either**

1 5

New Zealand's current account deficit increased from \$21.1 billion (6.0% of GDP) in 2021 to \$33.8 billion (8.9% of GDP) in 2022. Expenditure-reducing policies can help to reduce a deficit on the balance of payments but may damage the domestic economy.

Evaluate the advantages **and** disadvantages of using expenditure-reducing policies to decrease a deficit on the current account of a country's balance of payments.

[25 marks]**or**

1 6

Foreign aid can help poor countries grow and develop. However, this is not always the case. Foreign aid can destroy local industries and the country receiving aid may become dependent on the country or organisation providing the aid.

Evaluate the advantages **and** disadvantages of foreign aid for less-economically developed countries (LEDCs).

[25 marks]

Foreign aid is the transfer of resources to LEDCs on concessional terms. It includes grants, soft loans at below-market interest rates, technical assistance, emergency humanitarian aid and debt relief. It may be bilateral, from one government to another, or multilateral, through organisations such as the World Bank and UN agencies. LEDCs typically have low income per head, high poverty, low savings and investment, and weak infrastructure and human capital. The main advantage is that aid can fill the savings gap. In the Harrod-Domar model, growth depends on the savings ratio and the capital-output ratio. Low incomes mean low savings, so little investment, so low growth and low incomes again: a poverty cycle. Aid adds to the funds available for investment, breaking

Turn over ►

the cycle and allowing higher growth. It can also fill the foreign exchange gap, providing the foreign currency needed to buy essential imports such as capital goods, fuel and medicines without running up a current account deficit.

However, the Harrod-Domar model assumes that more investment automatically raises growth. In many LEDCs the capital-output ratio is high because of low skills, poor infrastructure and weak institutions, so extra capital adds little output. Aid may also crowd out domestic saving if governments and households save less because they expect aid to continue.

Aid can finance infrastructure such as roads, power and water, which lowers firms' costs and shifts LRAS to the right, and investment in human capital through schools, vaccinations and clean water. Healthier, better educated workers are more productive, and life expectancy and literacy rise, so aid improves development as well as growth. Technical assistance transfers knowledge and expertise in areas such as farming methods and public administration.

Humanitarian aid after natural disasters, famine or conflict saves lives in the short run when the LEDC has no means to cope. Aid can also relieve poverty directly, through cash transfers, food programmes and clean water projects that meet basic needs, which is the essence of development rather than just growth.

Debt relief, such as the Heavily Indebted Poor Countries initiative, frees government revenue for health and education.

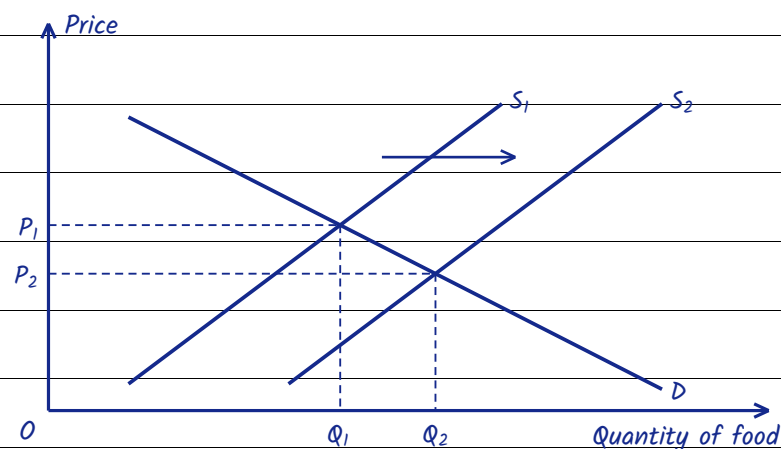
However, there are important disadvantages. Food aid can destroy local industries. In the diagram, free food aid increases the supply of food from S_1 to S_2 , so the market price falls from P_1 to P_2 . Local farmers receive lower prices and incomes, some stop farming, and domestic supply contracts, which makes the country more reliant on aid in future.

Aid may also create dependency. If governments rely on aid they may delay reforms to raise taxes or encourage enterprise, and if aid stops the projects



collapse. Tied aid, which must be spent on goods and services from the donor, often costs more than buying from the cheapest supplier and serves the donor's interests, such as exports or political influence. Aid with conditions, such as structural adjustment, may force cuts in public spending that harm the poor. Loans must be repaid with interest, often in foreign currency, so soft loans can increase overseas debt. Debt servicing means the government spends more on interest and less on capital spending, health and welfare, and a high share of export earnings is used to pay the debt rather than buy essential imports. Corruption and government failure may mean aid is stolen or wasted on prestige projects rather than reaching the poor, and aid can cause the real exchange rate to appreciate, harming exporters. Aid is also fungible: even when it funds a

Extra space school, the government may simply switch its own money to military



spending, so donors cannot be sure aid adds to development spending. The overall effect depends on several factors. It depends on the type of aid: grants, debt relief and humanitarian aid do not add to debt, whereas loans may. Untied, multilateral aid is usually more efficient than tied bilateral aid. It depends on the quality of governance: aid works best where institutions are strong and corruption is low, as in Botswana or South Korea in the past. It also depends on how aid is spent: projects in health, education and infrastructure give

Turn over ►



long-run benefits, while poorly targeted spending does not. Targeted project aid with clear outcomes, such as vaccination, is less likely to create dependency than general budget support, though it may bypass and weaken the recipient's own institutions. Conditions on good governance can reduce corruption, but harsh conditions may harm the poor. Time scale also matters, since infrastructure and education take many years to raise productivity. Humanitarian aid is almost always beneficial in the short run, but long-run development needs investment that raises productivity; aid that only funds consumption does not create self-sustaining growth. Some economists, such as Dambisa Moyo, argue that decades of aid to sub-Saharan Africa have not raised growth, while others point to large gains in health, such as vaccination programmes that have greatly reduced child mortality.

In conclusion, foreign aid has clear advantages for LEDCs, particularly in emergencies and in filling savings and foreign exchange gaps to finance human capital and infrastructure. Its disadvantages, such as dependency, debt and harm to local producers, are significant but arise mainly from poorly designed aid. On balance, the advantages outweigh the disadvantages when aid is untied, given as grants, well targeted and monitored, and used alongside trade and domestic reforms, with a clear plan for the LEDC to develop without relying on it. Where governance is weak, aid should go through trusted projects and NGOs.

END OF QUESTIONS



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ANSWER IN THE SPACES PROVIDED**



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Question number	Additional page, if required. Write the question numbers in the left-hand margin.



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ANSWER IN THE SPACES PROVIDED**

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2 8



2 4 6 X E C O 4