



General Certificate of Education
Advanced Subsidiary Examination
January 2010

Economics

ECON2

Unit 2 The National Economy

Thursday 21 January 2010 9.00 am to 10.15 am

For this paper you must have:

- an objective test answer sheet
- a black ball-point pen
- an 8-page answer book.

You may use a calculator.

Time allowed

- 1 hour 15 minutes

Instructions

- In **Section A**, answer **all** questions on your objective test answer sheet.
- In **Section B**, answer **EITHER** Question 26 **OR** Question 27 in your answer book.
- Do all rough work in this question paper, **not** on your objective test answer sheet.

Section A (ECON2/1)

- Use a black ball-point pen. Do **not** use pencil.

Section B (ECON2/2)

- Use black ink or black ball-point pen. Pencil should only be used for drawing.
- Write the information required on the front of your answer book. The **Examining Body** for this paper is AQA. The **Paper Reference** is ECON2/2.

Information

- The maximum mark for this paper is 75.
- There are 25 marks for **Section A** and 50 marks for **Section B**.
- In **Section A**, each question carries 1 mark. No deductions will be made for wrong answers.
- In **Section B**, the marks for questions are shown in brackets.
- You will be marked on your ability to:
 - use good English
 - organise information clearly
 - use specialist vocabulary where appropriate.

Advice

- You are advised to spend no more than 25 minutes on **Section A** and at least 50 minutes on **Section B**.

SECTION A: OBJECTIVE TEST

Answer **all** questions in **Section A**.

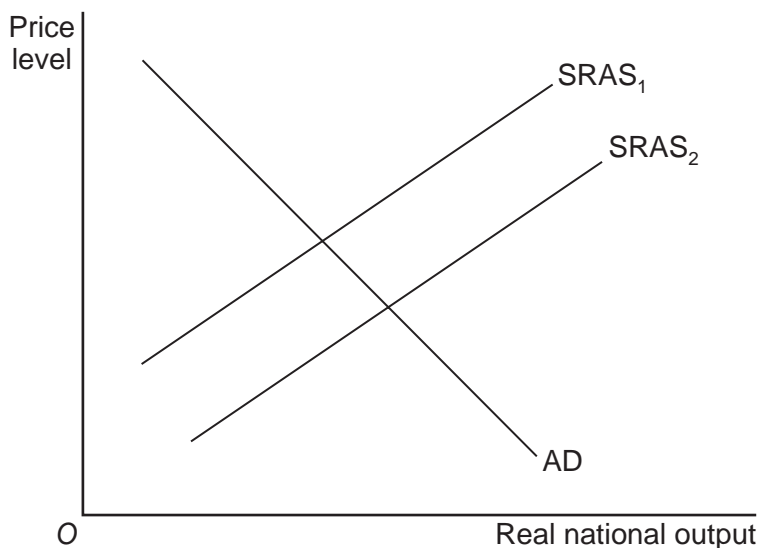
Each question carries 1 mark. No deductions will be made for wrong answers.

You are advised to spend no more than 25 minutes on **Section A**.

For each question there are four alternative responses, **A**, **B**, **C** and **D**. When you have selected the response which you think is the best answer to a question, mark this response on your objective test answer sheet. If you wish to change your answer to a question, follow the instructions on your objective test answer sheet.

- 1** In economics, investment is best defined as
- A** the flow of money into the stock of savings.
 - B** spending on capital goods in the economy.
 - C** the profit kept back by firms to finance future expenditure on new machinery and equipment.
 - D** the stock of economic resources such as factories and machinery.
- 2** A rise in the exchange rate together with a rise in taxes on household income is most likely to lead to a
- A** rise in exports and a rise in business investment.
 - B** fall in imports and a rise in business investment.
 - C** fall in exports and a rise in business investment.
 - D** rise in imports and a fall in business investment.
- 3** All other things being equal, a large rise in interest rates is most likely to lead to an increase in
- A** economic growth.
 - B** investment.
 - C** unemployment.
 - D** aggregate supply.

- 4 The diagram below shows the aggregate demand (AD) and short-run aggregate supply (SRAS) curves for an economy.



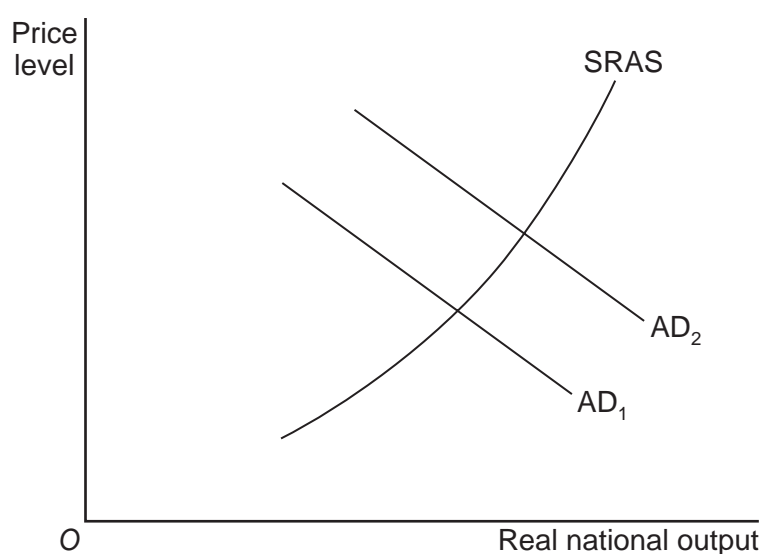
The shift of the short-run aggregate supply curve from $SRAS_1$ to $SRAS_2$ could have been caused by

- A a decrease in oil prices.
 - B an increase in employment.
 - C a decrease in the availability of credit.
 - D an increase in business costs.
- 5 All other things being equal, a government would be undertaking a contractionary fiscal policy if it reduced
- A government expenditure.
 - B interest rates.
 - C taxation.
 - D the exchange rate.
- 6 Which one of the following policies is most likely to lead to an increase in output and employment without increasing the rate of inflation?
- A Expansionary fiscal policy
 - B Expansionary monetary policy
 - C Supply-side policies
 - D Exchange rate policy

Turn over ▶

-
- 7 Which one of the following is most likely to reduce inflationary pressures in the UK economy?
- A An increase in labour productivity
 - B A fall in the value of the pound
 - C The emergence of a positive output gap
 - D A reduction in the rate of interest paid on mortgages
- 8 Which one of the following is most likely to occur in the boom phase of an economic cycle?
- A Rising national income, falling unemployment and a negative output gap
 - B Rising imports, rising profits and a positive output gap
 - C Rising consumption and investment expenditure and a negative output gap
 - D Excess demand, falling employment and a positive output gap
- 9 An increase in aggregate demand is most likely to cause inflation when
- A there are substantial unemployed resources in the economy.
 - B the government is balancing its budget.
 - C the balance of payments on current account is neither in deficit nor in surplus.
 - D actual GDP is above the productive potential of the economy.

- 10** Choosing between faster economic growth and a satisfactory balance of payments best illustrates
- A** choice between different macroeconomic policy instruments.
 - B** that the short-run aggregate supply curve is vertical.
 - C** a possible conflict between competing policy objectives.
 - D** a government sacrificing future consumption in favour of current consumption.
- 11** The diagram below shows two aggregate demand (AD) curves and the short-run aggregate supply (SRAS) curve for an economy.

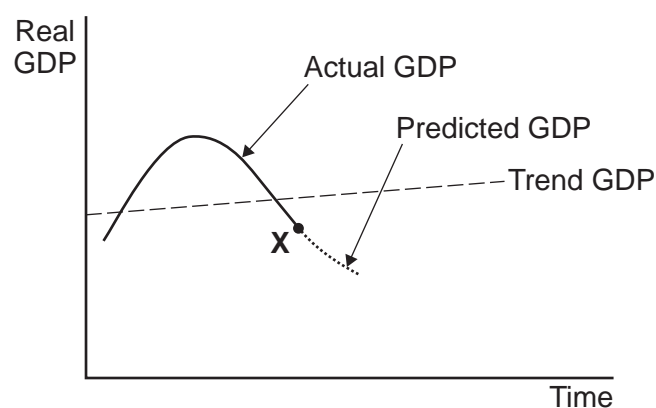


The shift in the aggregate demand curve from AD_1 to AD_2 could have been caused by an increase in

- A** imports.
 - B** labour productivity.
 - C** household savings.
 - D** the government budget deficit.
- 12** The underlying long-run trend rate of economic growth can be defined as the
- A** highest rate of economic growth achieved in the long run by an economy.
 - B** average rate of economic growth in a boom period.
 - C** rate of economic growth that can be maintained in the long run.
 - D** rate of economic growth achieved for a period of more than two quarters.

Turn over ►

- 13 All other things being equal, a fall in the exchange rate is likely to
- A increase the price of exports.
 - B reduce import prices.
 - C reduce domestic demand.
 - D increase domestic employment.
- 14 The diagram below shows actual and trend GDP for an economy over time.

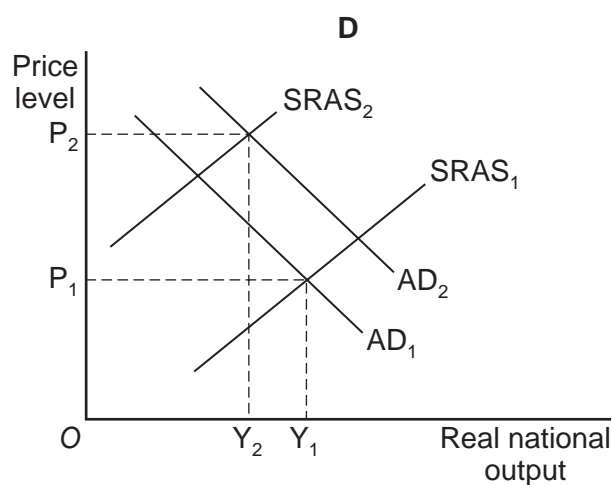
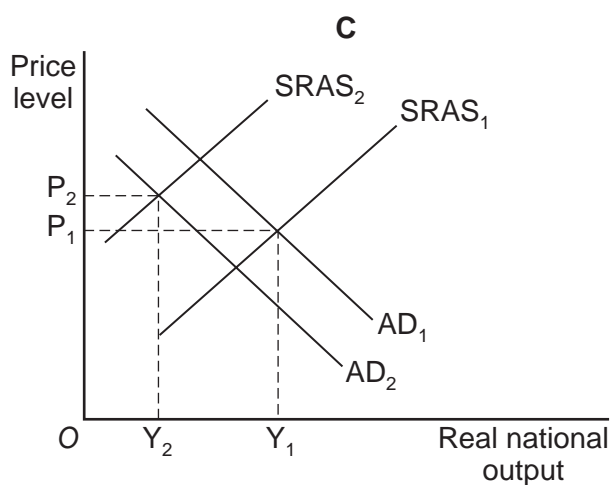
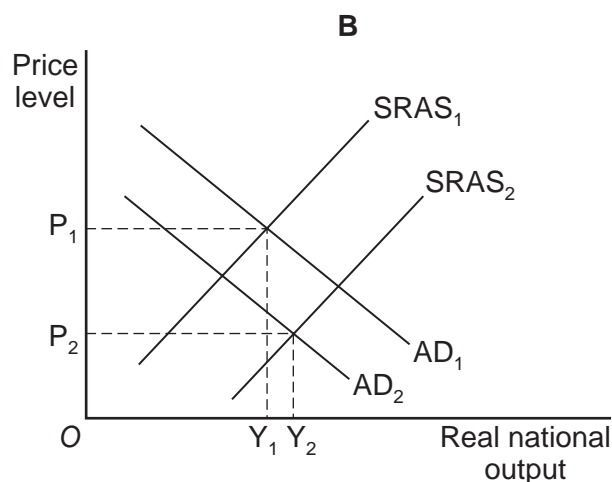
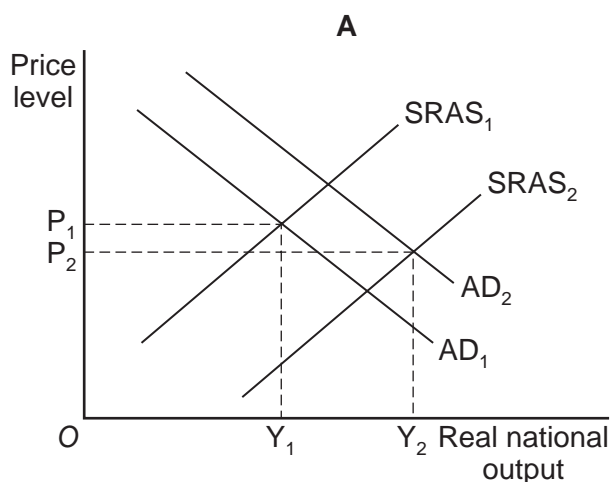


If the government is using both fiscal and monetary policies to manage the economy, what combination of policies is it most likely to implement when the economy is operating at point X?

- A Higher taxes with lower interest rates
 - B Higher taxes with higher interest rates
 - C Lower taxes with lower interest rates
 - D Lower taxes with higher interest rates
- 15 The economy is experiencing a balance of payments surplus on current account and high unemployment. Which policy is most likely to reduce both the balance of payments surplus on current account and unemployment?
- A A cut in income tax
 - B A rise in interest rates
 - C An increase in the exchange rate
 - D A fall in government spending

- 16 The short-run aggregate supply curve is drawn on the assumption that
- A investment in the economy is constant.
 - B the prices of factors of production are constant.
 - C the money supply is constant.
 - D consumption expenditure by households is constant.
- 17 The diagrams below illustrate aggregate demand and aggregate supply curves for an economy. AD_1 and $SRAS_1$ represent the initial positions of the aggregate demand and short-run aggregate supply curves. AD_2 and $SRAS_2$ represent shifts in the position of the two curves.

Which one of the following diagrams indicates the effect on the economy of a general fall in wage costs and a rise in the level of exports?



Turn over ►

- 18 In the short run, an increase in a budget deficit is most likely to reduce
- A imports.
 - B unemployment.
 - C interest rates.
 - D inflation.
- 19 All other things being equal, which one of the following is most likely to reduce a balance of payments deficit on current account?
- An increase in
- A the price level
 - B consumption
 - C productivity
 - D the money supply
- 20 The table below shows index numbers for GNP per head for two countries, X and Y, in 2005 and 2009.

	GNP per head	
	2005	2009
Country X	100	120
Country Y	100	110

From the information above, it can be concluded that

- A GNP rose faster in Country X than in Country Y.
- B GNP was the same in Country X and Country Y in 2005.
- C GNP per head was, in 2009, higher in Country X than in Country Y.
- D the rate of increase of GNP per head was higher in Country X than in Country Y.

- 21 If an economy is operating on its production possibility frontier, the most likely effect of an increase in the output of capital goods is that its rate of economic growth will
- A increase now but fall in the future.
 - B remain constant now but increase in the future.
 - C remain constant now and in the future.
 - D fall now but increase in the future.
- 22 All other things being equal, a rise in the value of the pound on foreign exchange markets is most likely to increase
- A public sector borrowing in the UK.
 - B the rate of inflation in the UK.
 - C the level of interest rates in the UK.
 - D the UK's current account deficit on the balance of payments.
- 23 A supply-side policy can be used to increase
- A interest rates.
 - B government expenditure.
 - C the mobility of labour.
 - D tax rates.
- 24 Which one of the following combinations is most likely to increase aggregate demand (AD) in the UK economy?

Combination	Government spending	Taxation revenue	Exchange rate of the £
A	Falling	Rising	Rising
B	Rising	Falling	Falling
C	Rising	Rising	Falling
D	Falling	Falling	Rising

-
- 25 All other things being equal, which one of the following is most likely to cause a simultaneous shift to the right in both an economy's short-run and long-run aggregate supply curves?

An increase in

- A the number of immigrants entering the country
- B the rate of interest
- C the rate of Value Added Tax (VAT)
- D the minimum wage rate

**QUESTION 25 IS THE LAST
QUESTION IN SECTION A**

**On your answer sheet
ignore rows 26 to 50**

TURN TO PAGE 12 FOR SECTION B

Turn over for the next question

Turn over ▶

SECTION B: DATA RESPONSE

Answer **EITHER** Question 26 **OR** Question 27.
You are advised to spend at least 50 minutes on **Section B**.

EITHER

Total for this question: 50 marks

26 TRADE, THE EXCHANGE RATE AND THE UK ECONOMY

Study **Extracts A, B and C**, and then answer **all** parts of Question 26 which follows.

Extract A: Summary of the current account of the UK balance of payments, £ billion

	2007 Quarter 4 (£bn)	2008 Quarter 1 (£bn)
Balance of trade in goods	-24.1	-22.7
Balance of trade in services	9.5	9.2
Balance of trade in goods and services	-14.6	-13.5
Income balance (including investment income)	6.9	9.0
Current transfers balance	-4.5	-3.9
Current account balance	-12.2	-8.4

Source: official statistics, accessed on 25 August 2008

Extract B: Slow growth and a falling exchange rate will affect the trade balance

The 15 economies of the eurozone (those countries that use the euro as a currency) contracted in the second quarter of 2008, experiencing growth of -0.2%. A recession in the eurozone economies will reduce UK exports and lead to lower economic activity in the UK. However, the effect of the decline in exports upon the balance of payments should be offset by a fall in foreign imports as growth in the UK slows and the sterling exchange rate falls.	1 5
The pound reached a low against the euro in April 2008 and has fallen by over 5% against the US dollar during the past month. A measure of the pound's exchange rate, the sterling exchange rate index, stood at 104.24 on the 1 January 2007 but its value closed at 91.22 on the 21 August 2008. This fall in the value of the pound will help to improve the competitiveness of UK firms and should lead to a reduction in the deficit on the balance of trade in goods and services.	10

Source: news reports, August 2008

Extract C: The UK at a standstill in the second quarter of 2008

The longest period of sustained economic growth in Britain's history has come to an end. The latest official statistics showed zero growth for the UK economy between April and June 2008. After 63 quarters (almost 16 years) of uninterrupted economic growth, the United Kingdom economy has ground to a halt.	1
Figures show that the services sector, the backbone of the UK economy, grew by just 0.2%, while manufacturing output fell by 0.8% and household spending dropped by 0.1%. City economists said it was overseas trade which had helped to prevent the economy going into recession in the first half of 2008.	5
The recent fall in the value of the pound should help UK exporters, whose goods will be cheaper overseas, but it may also add to inflationary pressures, making it more difficult for the Bank of England to cut interest rates.	10

Source: news reports, August 2008

Question 26

- 26** (a) Define the term 'balance of trade in goods and services' (**Extract B**, line 12). (5 marks)
- (b) Using the data in **Extract A**, identify **two** components of the current account that have led to the improvement in the current account balance that occurred between the fourth quarter of 2007 and the first quarter of 2008. (8 marks)
- (c) Explain the likely effect of a recession in the eurozone upon the current account of the UK balance of payments. (12 marks)
- (d) Assess the view that a fall in the exchange rate of the pound will help to improve the performance of the UK economy. (25 marks)

Turn over ▶

Do **not** answer Question 27 if you have answered Question 26.

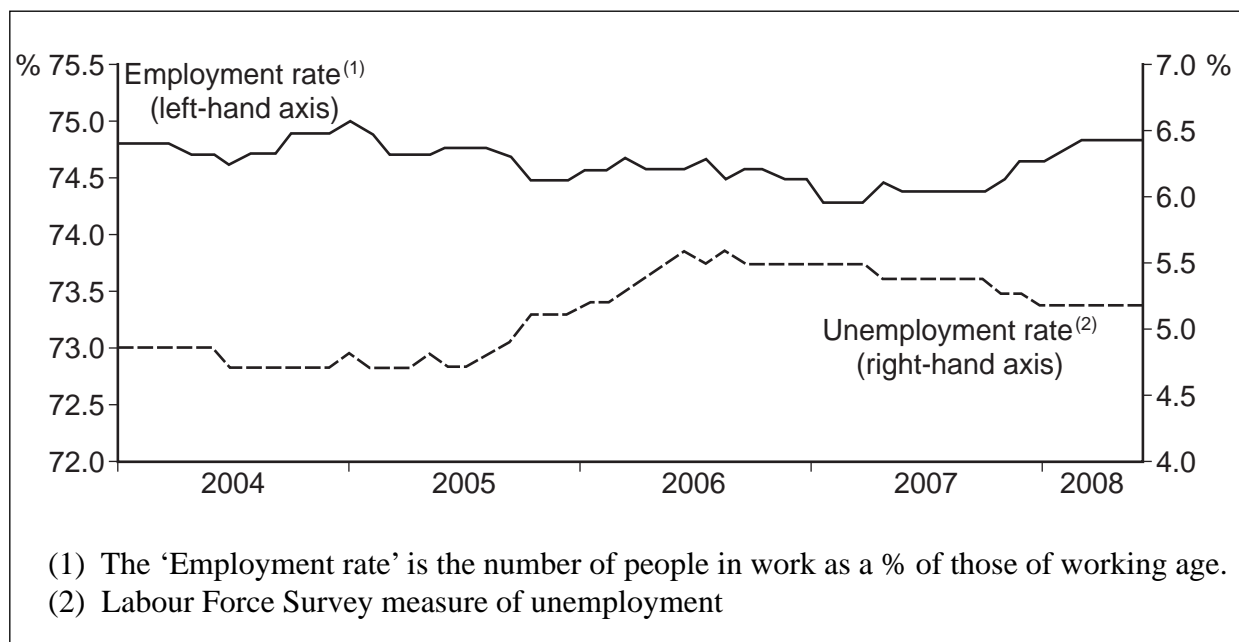
OR

Total for this question: 50 marks

27 EMPLOYMENT AND UNEMPLOYMENT

Study **Extracts D, E and F**, and then answer **all** parts of Question 27 which follows.

Extract D: Employment and unemployment rates for the UK, January 2004 to May 2008



Source: adapted from 'Economic & Labour Market Review', Vol. 2, No. 8, August 2008, www.statistics.gov.uk, accessed on 25 August 2008

Extract E: The labour market weakens

Most economists believe that a recession in the United Kingdom is inevitable.	1
The labour market is weakening, employment growth has slowed to a trickle and unemployment is rising. In June, the claimant count measure of unemployment rose by 20 100, the sixth successive monthly increase. The Labour Force Survey measure rose by 60 000 and the unemployment rate rose from 5.2% to 5.4%.	5
The number of job vacancies was also down, reflecting weaker demand conditions in the UK economy.	
The impact of the economic slowdown is becoming more widespread. Nearly every sector of the economy is affected. The credit crunch hit housebuilding and construction hard but its effects are now spreading to the rest of the economy.	10
The British Chambers of Commerce have predicted that unemployment will rise by more than 300 000 over the next two or three years, taking it close to 2 million.	

Source: news reports, July 2008

Extract F: A sustained rise in unemployment is inevitable

In recent years, the rapid increase in consumer spending provided the main contribution to the sustained growth in real GDP. However, high levels of consumer debt and falling house prices suggest that the growth in consumption in the UK is likely to fall and may even become negative.	1
Problems in the United States and the looming recession in the eurozone mean that, despite the fall in the value of the pound, United Kingdom exports are unlikely to increase sufficiently to offset the decline in domestic demand. High oil, gas and commodity prices have caused inflation to rise significantly above the 2% Consumer Prices Index (CPI) target and some economists consider it unlikely that the Bank of England will cut interest rates in the near future. A significant increase in unemployment seems inevitable and, in the short run, there is not much that a government can do about it.	5 10

Source: news reports, July 2008

Question 27

- 27 (a) Define the term 'real GDP' (**Extract F**, line 2). (5 marks)
- (b) Using **Extract D**, identify **two** significant points of comparison between changes in the employment rate and changes in the unemployment rate between January 2004 and May 2008. (8 marks)
- (c) Explain why 'weaker demand conditions in the UK economy' (**Extract E**, lines 6-7) are likely to lead to rising unemployment. (12 marks)
- (d) **Extract F** (lines 10-12) states: 'A significant increase in unemployment seems inevitable and, in the short run, there is not much that a government can do about it.'
- Evaluate alternative measures which can be used to reduce unemployment. (25 marks)

END OF QUESTIONS

There are no questions printed on this page

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