



A-LEVEL ECONOMICS

ECON4/Unit 4: The National and International Economy
Mark scheme

2140
June 2014

Version 1.0 Final

Mark schemes are prepared by the Lead Assessment Writer and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation events which all associates participate in and is the scheme which was used by them in this examination. The standardisation process ensures that the mark scheme covers the students' responses to questions and that every associate understands and applies it in the same correct way. As preparation for standardisation each associate analyses a number of students' scripts: alternative answers not already covered by the mark scheme are discussed and legislated for. If, after the standardisation process, associates encounter unusual answers which have not been raised they are required to refer these to the Lead Assessment Writer.

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of students' reactions to a particular paper. Assumptions about future mark schemes on the basis of one year's document should be avoided; whilst the guiding principles of assessment remain constant, details will change, depending on the content of a particular examination paper.

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AQA ADVANCED LEVEL (A2) ECONOMICS
LEVELS OF RESPONSE MARK SCHEME
FOR USE WITH QUESTIONS 03, 06, 08, 10 AND 12 ONLY

| A2 LEVELS OF RESPONSE | AO1 KNOWLEDGE and UNDERSTANDING of theories, concepts and terminology | AO2 APPLICATION of theories, concepts and terminology | AO3 ANALYSIS of economic problems and issues | AO4 EVALUATION of economic arguments and evidence, making informed judgements |
|---|--|--|---|--|
| Level 5 22-25 marks (mid-point 24) Good analysis and good evaluation | Good throughout the answer with few errors and weaknesses | Good application to issues Where appropriate, good use of data to support answer | Relevant and precise with a clear and logical chain of reasoning Good awareness of the inter-relatedness of economic issues | Good with a clear final judgement |
| Level 4 17-21 marks (mid-point 19) Good analysis but limited evaluation OR Reasonable analysis and reasonable evaluation | Good throughout the answer with few errors and weaknesses Good throughout much of the answer with few errors and weaknesses | Good application to issues Where appropriate, good use of data to support answer Some good application to issues Where appropriate, some good use of data to support answer | Relevant and precise with a clear and logical chain of reasoning Good awareness of the inter-relatedness of economic issues Largely relevant and well organised with reasonable logic and coherence Some awareness of the inter-relatedness of economic issues | Limited but showing some appreciation of alternative points of view Reasonable, showing an appreciation of alternative points of view |
| Level 3 10-16 marks (mid-point 13) Reasonable, including some correct analysis but very limited evaluation | Satisfactory but some weaknesses shown | Reasonable application to issues Where appropriate, reasonable use of data to support answer | Reasonably clear but may not be fully developed and is perhaps confused in places with a few errors present Quite well organised with some logical development | Superficial, perhaps with some attempt to consider both sides of the issue(s) |
| Level 2 4-9 marks (mid-point 7) Weak with some understanding | Limited and some errors are made | Partial application to issues with some errors Where appropriate, limited use of data to support answer | Partial but confused at times, lacking focus and development Limited logic and coherence | A very basic and simplistic attempt is made which is unsupported by analysis |
| Level 1 0-3 marks (mid-point 2) Very weak | Weak with a number of errors | Little, if any, application to issues Where appropriate, no use of data to support answer | Poor and lacking clarity and focus | No relevant evaluation |

THE KEY TO BE USED WHEN USING THE LEVELS MARK SCHEME

- D** Where a particular economic term is correctly **DEFINED** in order to help the candidate to answer the question properly.
- I** Where a relevant **ISSUE** is raised by the candidate.
- K** Where the candidate demonstrates **KNOWLEDGE** of recent developments or features of the economy which help enhance the candidate's response to the question. This should also be used where the candidate quotes relevant examples.
- Ap** Where the candidate demonstrates the ability to **APPLY** knowledge and **CRITICAL UNDERSTANDING** to problems and issues.
- An** Where the candidate demonstrates the ability to **ANALYSE** the problem using appropriate economic ideas.
- E** Where the candidate **EVALUATES** and makes judgements about the significance of various issues and arguments.

Synoptic Assessment

All questions in this unit are synoptic. Therefore, candidates will need to demonstrate that they are able to think as an economist and to use effectively the economist's 'tool kit' of concepts, theories and techniques.

They should demonstrate that they:

- understand the inter-relatedness of many economic issues, problems and institutions;
- understand how certain economic concepts, theories and techniques may be relevant to a range of different contexts;
- can apply concepts, theories and techniques in analysing economic issues and problems and in evaluating arguments and evidence.

QUALITY OF WRITTEN COMMUNICATION

Quality of Written Communication (QWC) will be assessed in Questions 03, 06, 08, 10 and 12 only.

Candidates will be assessed according to their ability to:

- ensure that text is legible, and that spelling, grammar and punctuation are accurate, so that meaning is clear
- select and use a form and style of writing appropriate to purpose and complex subject matter
- organise information clearly and coherently, using specialist vocabulary when appropriate.

No specific marks are awarded for QWC.

However, examiners should take into account QWC when determining the mark to be awarded for an answer. This means an answer could be taken either up (for exceptional QWC) or down (for very poor QWC) by 1 mark (and no more).

1 THE GLOBAL CONTEXT**Total for this Context: 40 marks**

- 01** Using **Extract A**, calculate the difference between the annual average value of RPI and the annual average value of CPI for the years 2005 to 2008, and identify **one** other significant comparison between the RPI and the CPI for the period 2004 to 2011.
[5 marks]

The calculation

| | |
|--|----------------|
| For the correct answer (1.00 percentage point). The 'unit', (per cent or %) must be shown. Do not penalise if 'point' is not stated. | 3 marks |
| For the correct answer without a unit shown | 2 marks |
| Any other answer between 0.9 and 1.1 (inclusive) irrespective of decimal places, with unit shown | 2 marks |
| Any other answer between 0.9 and 1.1 (inclusive) irrespective of decimal places, without unit shown | 1 mark |
| For showing the correct method but arriving at a wrong number, e.g. $\frac{(2.8+3.2+4.3+4.0)}{4} - \frac{(-2.1 + -2.3 + -2.3 + -3.6)}{4} = \text{wrong number}$ | 1 mark |

Identifying one significant feature of the period specified

| | |
|--|----------------------|
| For identifying a significant comparison (1 mark) and providing relevant and accurate supporting data (1 mark) with units (1 mark). | Up to 3 marks |
| For a 'trawl' through the numbers, or for simply providing an item of data seemingly chosen at random with no clear significance. | 0 marks |

Examples of significant comparisons include:

- The RPI is always greater than the CPI except for 2009, eg in 2011, RPI is 5.2%, CPI, 4.5%
- Only the RPI has a negative value (deflation) and this occurs in 2009 with a value of -0.5%
- CPI is at its lowest at 1.3% in 2004; RPI is at its lowest at - 0.5% in 2009

MAXIMUM FOR PART 01: 5 MARKS

02 **Extract C** (lines 12–13) states that the Quantity Theory of Money ‘predicts a direct relationship between increases in the money supply and increases in the price level’.

Explain the term ‘price level’ **and** analyse how increases in the money supply of an economy may bring about increases in the price level in that economy.

[10 marks]

Explanation

| | |
|--|--|
| For defining the price level, eg the average level of prices of all goods and services in an economy; for defining inflation, eg a general sustained rise in the price level, or the rate of inflation, eg the change in average prices in an economy over a given time period. A definition of inflation on its own and not linked to price level is not credited. | Up to 2 marks per point ensuring that any definition is not also credited as part of the analysis |
| For linking the definition of price level to the RPI and/or CPI. | Up to 2 marks |
| For explaining the basic principle of indices. | Up to 2 marks |
| For explaining that a price index such as the RPI calculates the average price level for the average household. | Up to 2 marks |
| Any other valid point relating to the price level, indices etc. | Up to 2 marks |

Maximum of 4 marks for the explanation

Analysis

Award marks for each step in a logical chain of reasoning

| | |
|---|--|
| For explaining the Quantity Theory of Money, eg reference to the Fisher equation (1 mark) from which the theory is developed, explaining the components of the Fisher equation (1 mark) , and developing the idea that the velocity and transactions are held constant (1 mark) leading to the central principle of the theory that inflation is caused solely by increases in the money supply (1 mark) through processes such as QE (1 mark) . | Up to 5 marks |
| Reference to monetarism/monetarists and the basic argument that inflation is demand–pull in nature and the idea that increases in money supply lead to increases in AD and to increases in the price level. | Up to 5 marks |
| Reference to the Monetary Transmission Mechanism (the term may not be explicitly used because it does not feature in the specification). For example, reference to the impact of increases in money supply on the rate of interest charged by high street institutions to consumers and businesses, and hence the impact on AD. | Up to 5 marks |
| Low interest rates lowering the exchange rate, causing import prices to rise, perhaps causing higher costs for firms and hence higher inflation. | Up to 5 marks |
| Any other valid analysis, eg rising MS and falling interest rates raising expectations about future inflation. | Up to 5 marks |
| Use of appropriate diagrams, eg a diagram showing the impact of money supply increases on the rate of interest; AD/AS diagrams. | Up to 2 marks per diagram (1 mark for labelling, 1 mark for correct information shown) to a maximum of 3 marks. |
| Reference to the UK economy | 1 mark per reference up to a maximum of 2 marks |

A candidate can be awarded a maximum of **6 marks** if only the analysis is attempted. (If only the explanation is attempted, candidates are restricted to **4 marks**).

MAXIMUM FOR PART 02: 10 MARKS

03 **Extract B** (lines 15–16) argues that ‘An increasing global inflation problem could have serious consequences for all aspects of UK macroeconomic performance including the balance of payments and employment.’

Using the data and your economic knowledge, discuss the possible impact on the UK balance of payments given an increasing rate of inflation throughout the global economy.

[25 marks]

In this part of the question, candidates will need to demonstrate that they are able to evaluate issues and arguments to support a conclusion if they are to be awarded **more than 15 marks**.

Where there is no **explicit** reference to the data, award a maximum of **21 marks**.

| | | |
|----------------|---|--|
| Level 5 | Good analysis and good evaluation | 22 to 25 marks <i>Mid-point 24 marks</i> |
| Level 4 | Good analysis <u>but</u> limited evaluation OR Reasonable analysis <u>and</u> evaluation | 17 to 21 marks <i>Mid-point 19 marks</i> |
| Level 3 | A reasonable answer including some correct analysis but very limited evaluation | 10 to 16 marks <i>Mid-point 13 marks</i> |
| Level 2 | Weak with some understanding | 4 to 9 marks <i>Mid-point 7 marks</i> |
| Level 1 | Very weak | 0 to 3 marks <i>Mid-point 2 marks</i> |

| | |
|--|--|
| Introduction | <ul style="list-style-type: none"> • Definition of inflation • Global experiences of inflation • UK inflation and the scenario of ‘worsening inflation’ • The balance of payments and its various parts. |
| Developing the response to the question (Application) | <ul style="list-style-type: none"> • Low inflation for achieving economic stability and sustained growth Extract B (lines 2 & 3) • Reference to energy costs and primary commodity prices Extract B (lines 12 & 13) • The brake on hesitant recovery Extract B (lines 21 & 22) • The dangers of loose monetary policy in the UK Extract C (lines 7–11) • The breeding of ‘uncertainty’ Extract C (line 11) • Disruption to trade and investment flows (Extract B lines 19 & 20) • Cost-push inflation • Demand-pull inflation • AD/AS analysis • Balance of payments • Competitiveness. |

| | |
|------------------------------|---|
| Analysis | <ul style="list-style-type: none"> • The notion of 'impact' • Measurement of impact in the context of the balance of payments • World commodity prices increases and the UK import bill • UK competitiveness given the authorities' success or failure in controlling inflation • The impact of imported inflation on future balance of payments' performance • Inflation, the UK exchange rate and the balance of payments • The impact of global inflation on the macroeconomy of other countries and how this will inevitably impact on the UK's balance of payments • Investment flows and the capital account. |
| Evaluation | <ul style="list-style-type: none"> • Is the problem in almost every part of the global economy and what, therefore, is the relevance of this to the UK balance of payments? • Is the problem one experienced by the UK's major trading partners? • 'Increasing inflation' but is the deterioration still from low initial levels of inflation? • UK inflation compared to inflation amongst our trading partners • A worsening, but still mild, inflation as a stimulant to the world of business, to investment, and the impact on the capital account • An inflation scenario which still compares favourably to the prospect of deflation for the balance of payment • The severity of any anti-inflation policies pursued by other governments which may impact on global demand for UK goods and services • The impact on the current account of success or failure in UK authorities' attempts to deal with any national problem of inflation. <p><i>Examiners should note that, for some of the weaker or average candidates, parts of the above represent quite sophisticated evaluation and so it is important to ensure that more basic evaluation is adequately rewarded where a genuine effort has been made to display that skill.</i></p> |
| Also give credit for: | <ul style="list-style-type: none"> • Reference to the UK/other economies • Diagrams • An overall judgement on the issues raised. |

It will only be possible for candidates to consider a few of the above. They may also discuss other issues not mentioned above.

**USE THE DETAILED LEVELS MARK SCHEME ON PAGES 4 & 5
FOR FURTHER CLARIFICATION**

MAXIMUM FOR PART 03: 25 MARKS

2 THE EUROPEAN UNION CONTEXT**Total for this Context: 40 marks**

- 04** Norway's annual average GDP growth has been 2.75% over the past 40 years. Using **Extract D**, calculate in \$US billions, to the nearest whole number, what Norway's GDP at current prices would be in 2012 assuming an annual growth rate of 2.75%, and identify **one** significant feature of the data in **Extract D** for the period 2008 to 2011.

[5 marks]**Calculation**

| | |
|--|----------------|
| For the correct answer (\$314 bn). The 'unit', (\$ bn) must be shown. | 3 marks |
| For the correct answer without \$ and/or bn shown | 2 marks |
| Any other answer between 313 and 315 (inclusive) irrespective of decimal places, with unit shown | 2 marks |
| Any other answer between 313 and 315 (inclusive) irrespective of decimal places, without unit shown. | 1 mark |
| For showing the correct method but arriving at a wrong number, ie $306 + \frac{2.75}{100} \times 306 = \text{wrong number}$ | 1 mark |

Identify one significant feature:

| | |
|---|----------------------|
| For identifying a significant feature (1 mark) and providing relevant and accurate supporting data (1 mark) with units (1 mark). | Up to 3 marks |
| For a 'trawl' through the numbers, or for simply providing an item of data seemingly chosen at random with no clear significance | 0 marks |

Significant features include:

- The highest GDP value is shown for Germany: \$3205bn in 2011
- The lowest GDP value is shown for Norway: \$264bn in 2009
- All the economies show a reduction in GDP at current prices from 2008 to 2009, eg France falls from \$2191 bn to \$2171 bn

MAXIMUM FOR PART 04: 5 MARKS

05 **Extract E** (lines 12–14) points out that UK trade with the EU has created 3.5m jobs in the UK ‘either within the export sector or, more widely, through the operation of an export-led multiplier’.

Explain the term ‘export-led multiplier’ **and** analyse **two** possible economic reasons for an increase in UK exports to the EU.

[10 marks]

Explanation

| | |
|--|---|
| For defining exports and/or the multiplier | Up to 2 marks per point ensuring that any definition is not also credited as part of the analysis |
| For a basic explanation of the link between the multiplier and AD. | Up to 2 marks |
| For use of an arithmetical example | Up to 2 marks |
| For explaining export-led multiplier, eg the impact of a growing export sector on other sectors of the economy, for example, as those employed in the export sector spend their incomes on goods and services; those businesses in the export sector demanding machinery and technology from other businesses outside the export sector. | Up to 4 marks Award one mark for each step in a logical chain of reasoning |
| For use of relevant diagrams, eg AD/AS | Up to 2 marks but not additional to the maximum of 4 marks for the explanation if this maximum has been awarded. Diagram: 1 mark for labelling, 1 mark for correct information shown |

Maximum of 4 marks for the explanation

Analysis

Award marks for each logical link in the chain of reasoning. For example:

| | |
|--|---|
| An improvement in the macroeconomy of the EU (1 mark) to which over half of UK exports are sold (1 mark). Fiscal policy may loosen in the EU (1 mark), so that consumers' disposable incomes rise and hence their demand for UK goods and services (1 mark). Equally, unemployment may fall in the EU (1 mark) allowing average incomes to rise and hence consumer demand for UK exports (1 mark). | Up to 5 marks |
| UK productivity increases lowering unit costs | Up to 5 marks |
| UK/EU relative inflation rates are favourable to the UK. | Up to 5 marks |
| Quality of UK goods and services | Up to 5 marks |
| The exchange rate of the £ against other currencies | Up to 5 marks |
| Changing comparative advantage favouring the UK | Up to 5 marks |
| Any other valid analysis | Up to 5 marks |
| Use of appropriate diagrams, eg AD/AS, comparative advantage. | Up to 2 marks per diagram (1 mark for labelling, 1 mark for correct information shown) to a maximum of 3 marks. These marks can be in addition to analysis marks |
| Reference to the UK economy | 1 mark per reference up to a maximum of 2 marks |

In the analysis, only allow a maximum of **5 marks** in total for references to rising demand for UK exports caused by the revival of the EU economy, ie it is not valid to regard, for example, looser fiscal policy in the EU as separate to rising incomes and award (max) 5 marks for each. Both relate to EU economic revival and demand.

A candidate can be awarded a maximum of **6 marks** if only the analysis is attempted. (If only the explanation is attempted, candidates are restricted to 4 marks).

Award a maximum of **8 marks** if a candidate analyses only one reason.

Where a candidate analyses more than two reasons, award marks to the best **two**.

MAXIMUM FOR PART 05: 10 MARKS

06 **Extract E** (lines 1–2) states: ‘In recent years, growing disenchantment with the EU has led to calls for the UK to leave the organisation’.

Do you agree with the view that the UK economy would benefit if the UK left the EU?
Justify your answer using the data and your economic knowledge.

[25 marks]

In this part of the question, candidates will need to demonstrate that they are able to evaluate issues and arguments to support a conclusion if they are to be awarded **more than 15 marks**.

Where there is no **explicit** reference to the data, award a maximum of **21 marks**.

| | | |
|----------------|---|--|
| Level 5 | Good analysis and good evaluation | 22 to 25 marks <i>Mid-point 24 marks</i> |
| Level 4 | Good analysis <u>but</u> limited evaluation OR Reasonable analysis <u>and</u> evaluation | 17 to 21 marks <i>Mid-point 19 marks</i> |
| Level 3 | A reasonable answer including some correct analysis but very limited evaluation | 10 to 16 marks <i>Mid-point 13 marks</i> |
| Level 2 | Weak with some understanding | 4 to 9 marks <i>Mid-point 7 marks</i> |
| Level 1 | Very weak | 0 to 3 marks <i>Mid-point 2 marks</i> |

| | |
|--|--|
| Introduction | <ul style="list-style-type: none"> • Reference to the history of the EU • The history of UK membership of the EU • Changing views about membership over time • The nature of the EU, for example, as a customs union/single market • The possible criteria for making a decision. |
| Developing the response to the question (Application) | <ul style="list-style-type: none"> • The estimated total cost to UK of membership Extract E(lines 4 & 5) • UK Budget contributions Extract E (line 6) • The Single European Market Extract E (lines 14 & 15) • Foreign direct investment Extract E lines (15 & 16) • The EEA Extract F (lines 3–5) • The example of Norway as a non-member of the EU Extract F • Trade theory • AD • Economic growth |

| | |
|------------------------------|---|
| Analysis | <ul style="list-style-type: none"> • The notion of economic benefit • Economic growth • Employment • Balance of Payments • Exchange rate • Prices • CAP • SEM • CET • The euro • The EEA. |
| Evaluation | <ul style="list-style-type: none"> • The uncertainty surrounding the future outside the EU • Whether a comparison with just one other economy (Norway) is helpful • To what extent, if at all, would trade be affected? • Could the UK re-establish former economic links, for example, with the Commonwealth or is this a myth from non-existent halcyon days? • The difficulty of assessing in a truly objective and precise way the various costs and benefits • The possible UK support for membership to foster and maintain economic ties with the EU in contrast to strong opposition to political ties and loss of national sovereignty • The possible changing views about membership as enlargement of the EU continues • Support for membership increasingly tempered by a fear that the UK will become embroiled in the euro crisis financially when the UK is outside the Eurozone • ‘Sitting on the fence’ has limitations; should the UK fully embrace all aspects of the EU and become ‘full Europeans’ including adoption of the euro? • The possibility of the UK joining the EEA or even NAFTA instead. <p><i>Examiners should note that, for some of the weaker or average candidates, parts of the above represent quite sophisticated evaluation and so it is important to ensure that more basic evaluation is adequately rewarded where a genuine effort has been made to display that skill.</i></p> |
| Also give credit for: | <ul style="list-style-type: none"> • Reference to the UK/other economies • Diagrams • An overall judgement on the issues raised. |

It will only be possible for candidates to consider a few of the above. They may also discuss other issues not mentioned above.

**USE THE DETAILED LEVELS MARK SCHEME ON PAGES 4 & 5
FOR FURTHER CLARIFICATION**

MAXIMUM FOR PART 06: 25 MARKS

SECTION B

Essay 1

Total for this essay: 40 marks

In July 2012, the Office for Budget Responsibility concluded that UK Government measures to cut the budget deficit have improved the UK's long-term economic prospects.

07 Explain possible economic reasons why a government might prefer to cut government spending to reduce a budget deficit rather than raise taxes.

[15 marks]

For defining/explaining:

- budget or budget deficit
- fiscal policy
- government spending
- taxes or taxation.

**Up to 2 marks per
definition or explanation
to a maximum of 4 marks**

For explaining why a government prefers to cut government spending rather than raise taxes:

Award 1 mark for each step in a logical chain of reasoning.

| | |
|--|----------------------|
| Direct taxes are taxes on household and corporate income (1 mark) and include income tax and corporation tax (1 mark in total for examples) . Raising direct taxes will reduce household disposable income (1 mark) and reduce the profits of companies (1 mark) . This may affect incentives to work and to take risks (1 mark) and hence adversely affect the economy's supply side (1 mark) however higher direct taxes may allow for lower indirect taxes (1 mark) such as VAT or excise duties (1 mark in total for examples) | Up to 8 marks |
| The impact of indirect taxes on the rate of inflation. | Up to 8 marks |
| The impact of taxes on wage demands. | Up to 8 marks |
| The impact of tax rises on household demand for goods and services building on the effects of a tighter fiscal policy to a degree not intended by the government. | Up to 8 marks |
| The distinction between capital, current and transfer spending which the government can use to limit the impact on different groups in society, eg maintaining spending on the NHS and welfare. | Up to 8 marks |
| Cuts in capital spending, eg infrastructure, can go unnoticed for some time in a way that increases in taxation often cannot. | Up to 8 marks |
| Spending cuts can avoid cutting spending on supply-side improvements such as education and training so continuing to lay stronger foundations for recovery. | Up to 8 marks |
| The relative distributional effects of tax rises v spending cuts. | Up to 8 marks |
| Any other valid reason. | Up to 8 marks |

| | |
|--|--|
| Use of diagrams to help support explanations, eg Laffer Curve, the relationship between tax revenue and spending and how it may change over time, AD/AS. | Up to 2 marks per diagram (1 mark for labelling, 1 mark for correct information shown) to a maximum of 4 marks. |
| Reference to the UK and/or other economies. | 1 mark per reference to a maximum of 2 marks |

In answers with reasons have been merged into one answer which does not distinguish reasons clearly, award up to 15 marks.

MAXIMUM FOR PART 07: 15 MARKS

08 To what extent would you agree, if at all, that the implementation of a budget deficit reduction programme will improve the UK's long-term economic prospects? Justify your answer.

[25 marks]

In this part of the question, candidates will need to demonstrate that they are able to evaluate issues and arguments to support a conclusion if they are to be awarded **more than 15 marks**.

| | | |
|----------------|--|--|
| Level 5 | Good analysis <u>and</u> good evaluation | 22 to 25 marks <i>Mid-point 24 marks</i> |
| Level 4 | Good analysis <u>but</u> limited evaluation OR Reasonable analysis <u>and</u> reasonable evaluation | 17 to 21 marks <i>Mid-point 19 marks</i> |
| Level 3 | A reasonable answer including some correct analysis but very limited evaluation | 10 to 16 marks <i>Mid-point 13 marks</i> |
| Level 2 | Weak with some understanding is shown | 4 to 9 marks <i>Mid-point 7 marks</i> |
| Level 1 | Very weak | 0 to 3 marks <i>Mid-point 2 marks</i> |

| | |
|---|---|
| Introduction | <ul style="list-style-type: none"> • The budget and budget deficit • The recent UK experience • Short term v long term • The notion of improvement in economic prospects. |
| Developing the response to the question (application and analysis) | <ul style="list-style-type: none"> • Short-term gain versus long-term gain • International credit-agency ratings for the UK and their possible significance • Interest rates and quantitative easing – short term benefit, long-term inflation? • The importance of stabilising the economy • Recession in the short term but the possible long-term weakening of the economy • The contrast with the 'Keynesian solution' • Economic growth • Inflation/deflation • Cost-push inflation at a time of 'austerity' creating problems in the long term • Competitiveness and the balance of payments on current account • Long-term prospects for employment/unemployment • Cyclical and structural unemployment. |

| | |
|------------------------------|--|
| Evaluation | <ul style="list-style-type: none"> • The severity of reductions in the deficit • The period of time over which so-called fiscal austerity lasts • What is reasonable to consider as ‘long term’ when referring to ‘long-term economic prospects’? • How the budget deficit is achieved • Whether the improvement in long-term prospects fully compensates for short-term problems arising from the reductions in the deficit • Does the alternative ‘Keynesian solution’ really hold water under scrutiny? • Are international credit ratings really that significant? • Long term prospects may improve on one measure, eg inflation, but suffer on another measure, eg growth • The possible self-defeating nature of deficit reduction, ie efforts to reduce a deficit can bring about an increase as the economy worsens <p><i>Examiners should note that, for some of the weaker or average candidates, parts of the above represent quite sophisticated evaluation and so it is important to ensure that more basic evaluation is adequately rewarded where a genuine effort has been made to display that skill.</i></p> |
| Also give credit for: | <ul style="list-style-type: none"> • Reference to the UK/other economies • Diagrams • An overall judgement on the issues raised. |

It will only be possible for candidates to consider a few of the above. They may also discuss other issues not mentioned above.

**USE THE DETAILED LEVELS MARK SCHEME ON PAGES 4 & 5
FOR FURTHER CLARIFICATION**

MAXIMUM FOR PART 08: 25 MARKS

Essay 2**Total for this Essay: 40 marks**

'When the exchange rate of a country's currency causes problems, it may be down to free market forces, but government intervention might be to blame.'

09 Explain **three** possible determinants of a country's exchange rate against other currencies.

[15 marks]

| | |
|--|---|
| <p>For:</p> <ul style="list-style-type: none"> • defining exchange rate • defining appreciation/depreciation, revaluation/devaluation • the distinction between various exchange rate systems. | <p>Up to 2 marks per definition or explanation to a maximum of 4 marks</p> |
| <p>For explaining three determinants of a country's exchange rate Award 1 mark for each step in a logical chain of reasoning For Example:</p> | |

| | |
|---|-----------------------------|
| <p>Trade flows will affect an exchange rate (1 mark). If exports increase (1 mark) so too will the demand for the currency of the exporting country by overseas buyers (1 mark). This will cause the exchange rate to appreciate. Equally, if imports into a country increase (1 mark), so too will the supply of that country's currency (1 mark), causing the exchange rate to depreciate (1 mark).</p> <p>Note to Examiners: While it is possible for a candidate to write only about exports or only about imports and the impact of either of these on the exchange rate to earn up to 7 marks, do not reward exports and imports as separate points (ie what would then be up to 14 marks) if both are clearly being dealt with as two separate determinants by the candidate.</p> | <p>Up to 7 marks</p> |
| <p>Investment flows</p> | <p>Up to 7 marks</p> |
| <p>Competitiveness</p> | <p>Up to 7 marks</p> |
| <p>Government involvement in FOREX</p> | <p>Up to 7 marks</p> |
| <p>Interest rates and hot-money flows</p> | <p>Up to 7 marks</p> |
| <p>Expectations</p> | <p>Up to 7 marks</p> |
| <p>Confidence</p> | <p>Up to 7 marks</p> |
| <p>External factors such as strong US or Eurozone recovery or an economic shock such as an international banking crisis.</p> | |
| <p>Any other valid determinant</p> | <p>Up to 7 marks</p> |

| | |
|---|--|
| <p>Use of diagrams to help support explanations, eg supply of, and demand for, a currency or for exports and/or imports</p> | <p>Up to 2 marks per diagram (1 mark for labelling, 1 mark for correct information shown)</p> <p>Up to 4 marks (2 + 2) can be awarded for a more complex diagram, e.g. showing the 'dirty floating' process.</p> <p>A maximum of 6 marks for diagrams given the nature of this question</p> |
| <p>Reference to the UK and/or other economies</p> | <p>1 mark per reference to a maximum of 2 marks</p> |

Award a maximum of **7 marks** if only one determinant is explained, a maximum of **10 marks** if only two are explained.

An additional point is that, because the question requires a candidate to identify 3 distinct determinants, a candidate should not simply explain in terms of two categories, supply and demand, but should identify clearly, and explain, three specific determinants within these two categories. If this is not done, award up to **10 marks** for the answer as a whole.

If the expected approach is adopted (ie distinct and specific determinants such as those cited above) but more than three determinants are considered, reward the best three.

MAXIMUM FOR PART 09: 15 MARKS

10 Assess the importance of a floating exchange rate to a country trying to achieve a period of macroeconomic stability. **[25 marks]**

In this part of the question, candidates will need to demonstrate that they are able to evaluate issues and arguments to support a conclusion if they are to be awarded **more than 15 marks**.

| | | |
|----------------|--|--|
| Level 5 | Good analysis <u>and</u> good evaluation | 22 to 25 marks <i>Mid-point 24 marks</i> |
| Level 4 | Good analysis <u>but</u> limited evaluation OR Reasonable analysis <u>and</u> reasonable evaluation | 17 to 21 marks <i>Mid-point 19 marks</i> |
| Level 3 | A reasonable answer including some correct analysis but very limited evaluation | 10 to 16 marks <i>Mid-point 13 marks</i> |
| Level 2 | Weak with some understanding is shown | 4 to 9 marks <i>Mid-point 7 marks</i> |
| Level 1 | Very weak | 0 to 3 marks <i>Mid-point 2 marks</i> |

| | |
|---|--|
| Introduction | <ul style="list-style-type: none"> • Exchange rate • Floating exchange rate • Other exchange rate systems • Macroeconomic stability. |
| Developing the response to the question (application and analysis) | <ul style="list-style-type: none"> • Automatic adjustment under a floating exchange rate • The significance of automatic adjustment for macroeconomic stability • Interest rates determined by domestic conditions but nevertheless impacting on the exchange rate • Speculation and its impact • Global economic shocks • Economic growth and stability • The exchange rate and prices • The exchange rate and the balance of payments on current account • The exchange rate and employment • A floating exchange rate and business confidence • The possible significance of intervention by the authorities in an era of managed flexibility • Other factors which are more effective in achieving stability |

| | |
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| Evaluation | <ul style="list-style-type: none"> • The likelihood of automatic adjustment occurring efficiently or at all • Whether other conditions potentially able to secure stability can counteract any destabilising effect of a floating exchange rate or will it be vice versa? • The extent of changes to an exchange rate under a floating system • The impact of economic shocks making it very unlikely that stability can be achieved whatever the exchange rate system in operation • The preparedness of a government to intervene to influence an exchange rate in order that macroeconomic stability can be achieved • In reality, how long is 'a period of macroeconomic stability' expected to be? • Are changes in an exchange rate, within reason, really relevant to achieving macroeconomic stability? • The need to recognise that a floating exchange rate may help to stabilise one aspect of the macroeconomy, eg prices, but not do a great deal for another aspect, eg economic growth. <p><i>Examiners should note that, for some of the weaker or average candidates, parts of the above represent quite sophisticated evaluation and so it is important to ensure that more basic evaluation is adequately rewarded where a genuine effort has been made to display that skill.</i></p> |
| Also give credit for: | <ul style="list-style-type: none"> • Reference to the UK/other economies • Diagrams • An overall judgement on the issues raised. |

It will only be possible for candidates to consider a few of the above. They may also discuss other issues not mentioned above.

**USE THE DETAILED LEVELS MARK SCHEME ON PAGES 4 & 5
FOR FURTHER CLARIFICATION**

MAXIMUM FOR PART 10: 25 MARKS

Essay 3

Total for this Essay: 40 marks

‘Economic shocks can bring with them significant consequences for macroeconomic performance, as the UK knows only too well.’

- 11** Using at least **one** example of each, explain how demand-side and supply-side shocks might harm a country’s economic growth.

[15 marks]

| | |
|---|---|
| <p>For:</p> <ul style="list-style-type: none"> Defining economic shock, eg what maybe an unexpected event or one that at least some had predicted which affects an economy either positively or negatively (it is anticipated that the majority of candidates will see shock in negative terms because of the reference to ‘harm’ and this should not be penalised. Please make sure that credit is not given where the preamble to the question is simply copied out, ie an economic shock is something which can have significant consequences). Distinguishing a demand-side shock from a supply-side shock, perhaps with examples, such as the euro crisis, the ‘credit crunch’; oil price increase or a natural disaster. Defining economic growth, eg an increase in real GDP or an increase in productive capacity. Distinguishing between actual and potential growth. | <p>Up to 2 marks per definition or explanation to a maximum of 4 marks</p> |
|---|---|

For explaining the impact of demand-side and supply-side shocks on economic growth:

Award 1 mark for each step in a logical link chain of reasoning. Do not credit the choice of shock if already credited in the introduction

| | |
|--|-----------------------------|
| <p>Supply: A significant increase in global oil prices (1 mark) will impact on an economy having to import most or all of its oil from the international market (1 mark), causing the SRAS curve to shift to the left (1 mark). Higher oil prices will lead to higher unit costs (1 mark) and hence higher prices (1 mark) and hence cost-push inflation (1 mark). The impact of inflation on real incomes will affect AD (1 mark). Demands from labour for higher wages will worsen the inflation problem (1 mark). Inflation will cause an increase in unemployment and eventually cause economic growth to falter (1 mark) so that stagflation becomes a real possibility (1 mark).</p> | <p>Up to 9 marks</p> |
| <p>Supply: A significant increase in prices of primary commodities generally and/or food prices.</p> | <p>Up to 9 marks</p> |
| <p>Supply: A major war/significant natural disaster/a series of devastating terrorist attacks around the world in major economies. (Reward these as just one example of a shock to a maximum of 9 marks).</p> | <p>Up to 9 marks</p> |

| | |
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| Demand: The severity of the Eurozone crisis | Up to 9 marks |
| Demand: An unanticipated and sudden downturn in emerging economies such as India and China. | Up to 9 marks |
| Demand: credit crunch/crisis in major financial markets | Up to 9 marks |
| Any other economic shock explained which potentially harms growth | Up to 9 marks |
| Use of diagrams to help support explanations, eg AD/AS showing shifts of AD and/or AS, micro supply and demand diagrams, PPF | Up to 2 marks per diagram (1 mark for labelling, 1 mark for correct information shown) to a maximum of 4 marks |
| Reference to the UK and/or other economies | 1 mark per reference to a maximum of 2 marks |

If only one shock in total is explained, and therefore only the demand side or the supply side is considered, a maximum of **10 marks** may be awarded.

MAXIMUM FOR PART 11: 15 MARKS

12 Evaluate the likely impact of world economic growth **both** on the UK economy **and** on individuals in the economy.

[25 marks]

In this part of the question, candidates will need to demonstrate that they are able to evaluate issues and arguments to support a conclusion if they are to be awarded **more than 15 marks**.

Candidates who do not address both parts of the question must be awarded a maximum of **16 marks** (top-Level 3).

| | | |
|----------------|--|--|
| Level 5 | Good analysis <u>and</u> good evaluation | 22 to 25 marks <i>Mid-point 24 marks</i> |
| Level 4 | Good analysis <u>but</u> limited evaluation OR Reasonable analysis <u>and</u> reasonable evaluation | 17 to 21 marks <i>Mid-point 19 marks</i> |
| Level 3 | A reasonable answer including some correct analysis but very limited evaluation | 10 to 16 marks <i>Mid-point 13 marks</i> |
| Level 2 | Weak with some understanding is shown | 4 to 9 marks <i>Mid-point 7 marks</i> |
| Level 1 | Very weak | 0 to 3 marks <i>Mid-point 2 marks</i> |

| | |
|---|--|
| Introduction | <ul style="list-style-type: none"> • Economic growth • The standard of living • The recent global experience. |
| Developing the response to the question (application and analysis) | <ul style="list-style-type: none"> • How world economic growth is likely to be achieved • The importance of ensuring that growth is sustainable • Recognition that the impact could be positive or negative in net terms <p>The UK economy:</p> <ul style="list-style-type: none"> • Aggregate demand • Changes to the incentive to invest and the possible impact on such things as productive capacity • Aggregate supply • Inflation • The environment • The ability to sell overseas and hence the impact on exports • Imports • The balance of payments on current account • The prospects for inward/outward FDI • World growth causing changes to wealth creation in the UK • Employment/unemployment • The impact of world commodity prices. |

| | |
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| | <p>The individual in the UK:</p> <ul style="list-style-type: none"> • Trend in average income (income per head) • Distribution of income • A possible sharpening of the “haves and have-nots” distinction • Consumption patterns • The wealth effect associated with rising asset prices in a period of growth • Choice of jobs • Quality of life • Quality of life measures such as the HDI and the “happiness index”. |
| Evaluation | <ul style="list-style-type: none"> • The extent of world economic growth • World economic growth from what starting point, eg years of stagnation? • The importance of considering where in the world growth is taking place and the bearing this may have on the UK economy • The UK’s capability to participate in the growth process and in its rewards • The possibility of the UK economy importing the downside of world growth, eg inflation and a deteriorating environment, without enjoying the benefits, eg more jobs and more spending power • It is easier to measure the economic impact on the individual, ie income per head, than it is to measure changes to the quality of life • What of the individual who has the wrong skills or qualifications to allow occupational mobility or cannot become geographically mobile? • Short term v long term impact for both the individual and the economy • Does the UK economy enjoy higher demand without giving due attention to its supply-side? • Is sufficient attention given to the environment both from the individual’s point of view and that of the UK economy? • Whether growth elsewhere is likely to cause net economic benefit or net economic damage to the UK. <p><i>Examiners should note that, for some of the weaker or average candidates, parts of the above represent quite sophisticated evaluation and so it is important to ensure that more basic evaluation is adequately rewarded where a genuine effort has been made to display that skill.</i></p> |
| Also give credit for: | <ul style="list-style-type: none"> • Reference to the UK/other economies • Diagrams • An overall judgement on the issues raised. |

It will only be possible for candidates to consider a few of the above. They may also discuss other issues not mentioned above.

**USE THE DETAILED LEVELS MARK SCHEME ON PAGES 4 & 5
FOR FURTHER CLARIFICATION**

MAXIMUM FOR PART 12: 25 MARKS