



General Certificate of Education
Advanced Subsidiary Examination
June 2013

Economics

ECON2

Unit 2 The National Economy

Friday 17 May 2013 1.30 pm to 2.45 pm

For this paper you must have:

- an objective test answer sheet
 - a black ball-point pen
 - an AQA 8-page answer book.
- You may use a calculator.

Time allowed

- 1 hour 15 minutes

Section A (ECON2/1)

- Answer **all** questions on your objective test answer sheet.
- Use a black ball-point pen. Do **not** use pencil.
- Do all rough work in this question paper, **not** on your objective test answer sheet.

Section B (ECON2/2)

- Answer **EITHER** Context 1 **OR** Context 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**. Each question carries one mark. No deductions will be made for wrong answers.
- There are 50 marks for **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 Which one of the following is most likely to shift the short-run aggregate supply curve to the left? A rise in
 - A money wages.
 - B government spending.
 - C the exchange rate.
 - D labour productivity.

- 2 In the short run, a fall in a budget deficit is most likely to increase
 - A imports.
 - B unemployment.
 - C interest rates.
 - D inflation.

- 3 The UK economy is in recession. The government increases its budget deficit whilst, at the same time, the exchange rate of the pound falls. These events are most likely to lead to a rise in
 - A the rate of growth of GDP and a fall in unemployment.
 - B the foreign currency price of UK exports and a rise in inflation.
 - C the price in pounds of UK imports and a rise in unemployment.
 - D labour productivity and a fall in the size of the positive output gap in the economy.

- 4 The table below shows both the unemployment rate and inflation rate for an economy between 2010 and 2012.

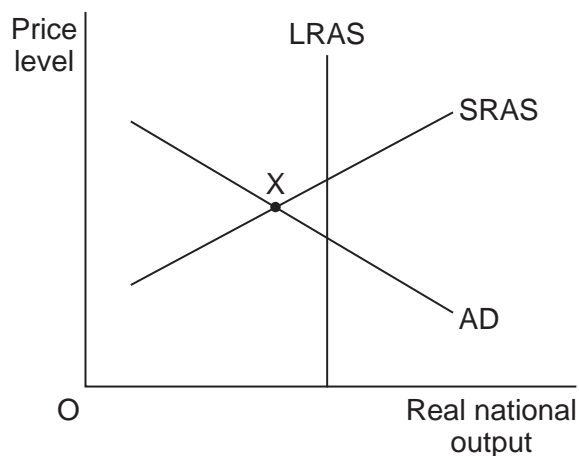
	Unemployment rate (%)	Inflation rate (%)
2010	5.3	4.0
2011	4.9	4.5
2012	4.6	4.2

Which one of the following can be deduced from the data?

- A Employment rose between 2010 and 2012.
 - B Prices fell between 2011 and 2012.
 - C There was an inverse relationship between inflation and unemployment throughout the period.
 - D The value of money fell throughout the period.
- 5 Which one of the following is a correct statement?
- A Fiscal policy can be used to affect both the level of economic activity and the pattern of economic activity.
 - B The Bank of England is responsible for fiscal policy.
 - C Fiscal policy is used only to affect the demand side of the economy.
 - D The government uses fiscal policy to control the exchange rate.

Turn over ►

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



The economy is currently operating at point X. At this point, the economy must be experiencing

- A inflation caused by excess demand.
 - B inflation caused by increasing costs.
 - C unemployment of labour.
 - D a low rate of economic growth.
- 7 Deflation is
- A a fall in the external value of the domestic currency.
 - B a fall in the rate of inflation.
 - C a loss in value of capital stock due to physical wear and tear.
 - D a rise in the real value of money over time.

- 8 The UK's balance of payments on current account is in deficit and unemployment is high. The UK Government attempts to lower unemployment by significantly increasing aggregate demand.

All other things being equal, which one of the following combinations, **A**, **B**, **C** or **D**, is now most likely to occur in the short term?

Combination	Rate of inflation	Gross Domestic Product (GDP)	Deficit on the current account of the balance of payments
A	Increases	Increases	Decreases
B	Decreases	Increases	Increases
C	Increases	Decreases	Decreases
D	Increases	Increases	Increases

- 9 The multiplier can refer to the effect of a change in the level of

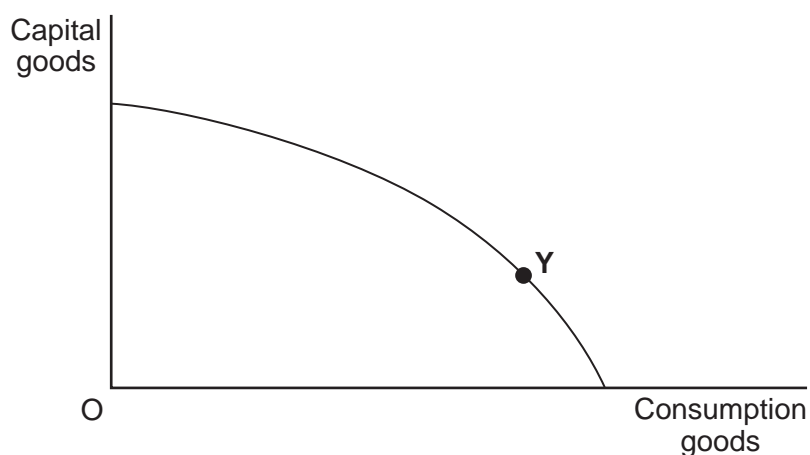
- A** aggregate demand upon imports.
- B** national income upon aggregate demand.
- C** saving upon investment.
- D** investment upon national income.

- 10 The Bank of England raises interest rates to reduce aggregate demand. Which one of the following combinations, **A**, **B**, **C** or **D**, is most likely to reduce the effectiveness of such a policy?

	Real incomes	Unemployment	Indirect taxation
A	Falling	Rising	Rising
B	Rising	Falling	Falling
C	Falling	Falling	Falling
D	Rising	Rising	Rising

Turn over ►

- 11 The production possibility diagram below shows an economy operating on its frontier, producing the combination of consumption and capital goods shown at point Y.



With no change in the position of the production possibility frontier, there is now an increase in the production of capital goods. Which one of the following, **A**, **B**, **C** or **D**, is most likely to occur because of this increase?

	Short-term change in consumption goods	Long-term change in consumption goods
A	Increase	Increase
B	Increase	Fall
C	Fall	Fall
D	Fall	Increase

- 12 A government wishing to reduce the level of unemployment through the use of fiscal policy would be most likely to
- A** lower interest rates.
 - B** decrease the size of the budget surplus.
 - C** increase interest rates.
 - D** encourage a depreciation of the exchange rate.

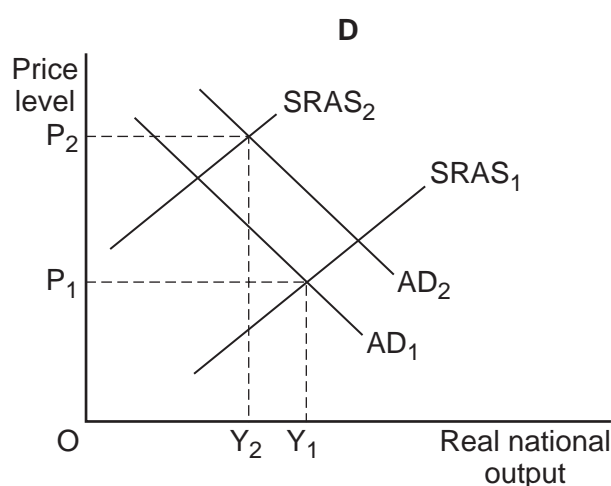
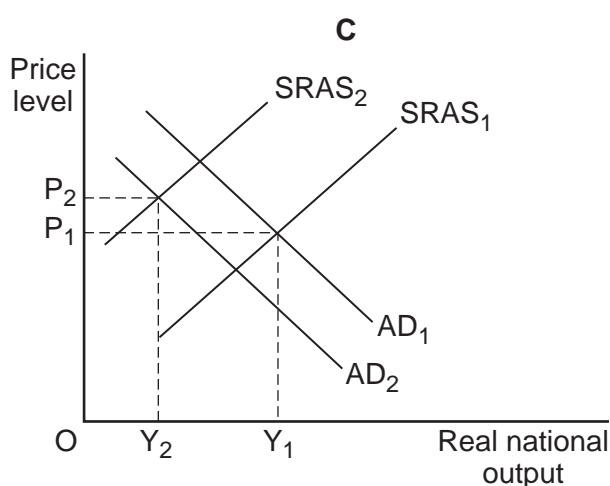
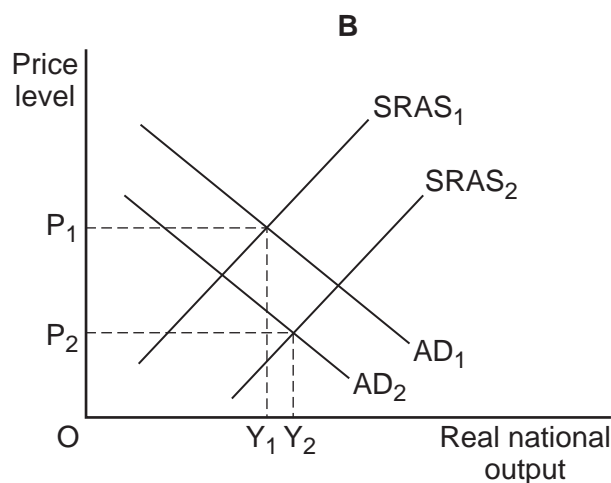
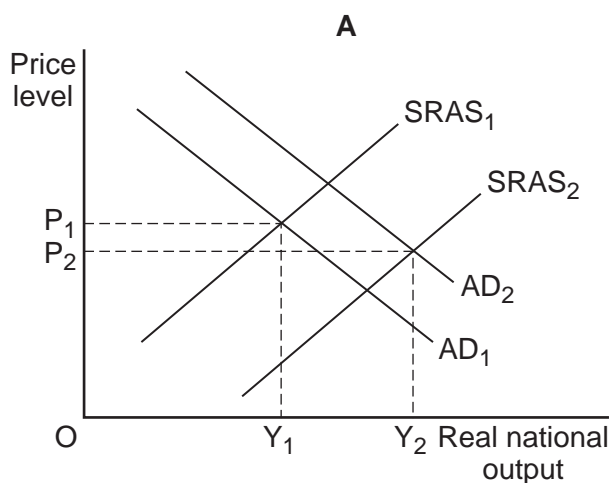
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- 13** One of the main functions of supply-side policies in the UK economy is to
- A** lower the long-run trend rate of growth of the economy.
 - B** create incentives designed to improve economic performance.
 - C** cause the rate of growth of aggregate supply to exceed the rate of growth of aggregate demand.
 - D** reduce the UK's budget deficit.
- 14** The economy is growing below its underlying trend rate and unemployment is rising. Which one of the following policies would be the best course of action to remedy the situation?
- An increase in
- A** interest rates to encourage investment
 - B** the exchange rate to increase exports
 - C** indirect taxes to raise consumption
 - D** government spending to boost aggregate demand
- 15** Which one of the following types of unemployment is best defined as 'unemployment for short lengths of time between jobs'?
- A** Frictional
 - B** Seasonal
 - C** Cyclical
 - D** Structural

16 If the world economy goes into recession, this is likely to increase unemployment in the UK because

- A the ability of other economies to supply UK industry with basic commodities will be reduced.
- B the value of goods and services exported from the UK will fall.
- C the price of oil and other raw materials is likely to rise.
- D the value of the pound will fall on the foreign exchange market.

17 The diagrams below show aggregate demand (AD) and short-run aggregate supply (SRAS) curves for an economy. AD_1 and $SRAS_1$ represent the initial position of the curves. AD_2 and $SRAS_2$ represent shifts in the position of the curves.

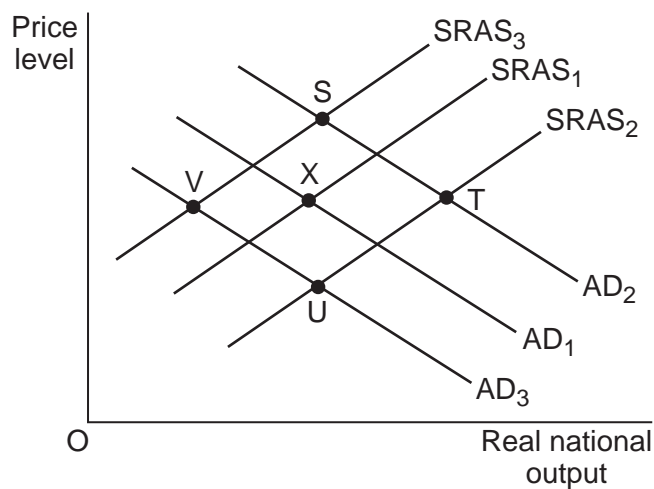
Which one of the following diagrams, **A**, **B**, **C** or **D**, indicates the effect on the economy of a general rise in wage costs and a rise in investment?



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- 18** All other things being equal, a fall in the value of the pound against the euro would be expected to affect the UK economy because it is likely to lead to
- A** an increase in aggregate demand.
 - B** a fall in raw material prices.
 - C** a rise in the euro price of UK exports.
 - D** a reduction in the rate of interest.
- 19** Which one of the following is a correct statement about monetary policy in the UK?
- A** Monetary policy is used mainly to affect the supply side of the economy.
 - B** Whenever the government uses contractionary fiscal policy, the Bank of England will use expansionary monetary policy to offset the effects.
 - C** Higher interest rates may reduce inflationary pressure but they may also reduce employment.
 - D** Monetary policy may involve the expansion of the money supply to reduce aggregate demand.
- 20** In recent years, the UK has experienced large deficits on its balance of payments on current account.
- All other things being equal, which one of the following would be most likely to reduce such deficits? A fall in
- A** aggregate supply
 - B** the exchange rate
 - C** income tax rates
 - D** labour productivity

Turn over ►

- 21 The diagram below shows the aggregate demand (AD) and the short-run aggregate supply (SRAS) curves for an economy, with the initial equilibrium being at point X.



All other things being equal, what would be the new equilibrium position following a rise in productivity and an increase in imports into the country?

- A Point S
- B Point T
- C Point U
- D Point V
- 22 The long-run trend rate of growth in an economy is declining and the economy is also experiencing an increase in its rate of unemployment. Which one of the following is likely to be most effective in dealing with these problems?
- A An expansionary fiscal policy and a restrictive monetary policy
- B A restrictive monetary policy and a restrictive fiscal policy
- C An expansionary monetary policy and additional supply-side measures
- D A restrictive fiscal policy and additional supply-side measures

-
- 23 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
- 24 A negative output gap necessarily means that the economy
- A is in recession.
 - B is suffering from demand-pull inflation.
 - C is operating inside its production possibility frontier.
 - D has a productive potential below its current level of Gross Domestic Product (GDP).
- 25 Which one of the following is a fundamental determinant of long-run aggregate supply?
- A The multiplier
 - B The output gap
 - C Real national output
 - D The institutional structure of the economy

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

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

Turn over for Section B

Turn over ►

Section B: Data Response

Answer **EITHER** Context 1 **OR** Context 2.
You are advised to spend at least 50 minutes on **Section B**.

Total for this Context: 50 marks

EITHER

Context 1

GROWTH OF THE UK ECONOMY

Study **Extracts A, B and C**, and then answer **all** parts of Context 1 which follow.

Extract A: UK index of real GDP and total employment, 2004 to 2010

	2004	2005	2006	2007	2008	2009	2010
Index of real GDP (2008 = 100)	93.3	95.2	97.7	101.1	100.0	95.6	97.3
Employment (millions)	28.48	28.77	29.02	29.23	29.44	28.96	29.04

Source: official statistics, November 2011

Extract B: Growth in 2011 is disappointing

After the severe recession of 2008/2009, it was hoped that the UK economy would stage a strong recovery in the years that followed. However, whilst the economy began its recovery in 2010, the most recent estimate of growth in 2011 is just 0.9%. Meanwhile, in the year up to November 2011, unemployment, as measured by the Labour Force Survey, has risen from 7.9% of the working population to 8.3%.	1 5
The Government's tightening of fiscal policy, designed to reduce the size of the budget deficit, clearly had an impact on growth in 2011 but this alone does not account for the low rate of economic growth. The problems in the eurozone, which affected business and consumer confidence, had an adverse effect on UK exports to Europe and on domestic consumption. However, perhaps the most important reason for low growth was the squeeze on real household disposable income. During 2011, the growth in average weekly earnings was 1.9%, whereas the CPI rate of inflation was 4.2%. The Office for Budget Responsibility says that the fall in real incomes in 2011 was the biggest reduction since the end of the Second World War in 1945. Consumer spending has never been so depressed at this stage of an economic recovery.	10 15

Source: news reports, January 2012

Extract C: Has underlying growth in the UK ground to a halt?

Many believe that the main objective of government economic policy should be to increase productivity and economic growth. The total output of the UK economy was lower in 2011 than it was in 2007. Low economic growth is usually accompanied by rising unemployment. It also makes it difficult to reduce the size of the budget deficit and to achieve an improvement in living standards. 1
5

Stimulating demand may be important but, on its own, it will not allow the UK economy to achieve a period of sustained growth. Rising demand, unless accompanied by improvements in the supply-side performance of the economy, risks higher inflation and a larger balance of payments deficit.

The UK Government has announced a number of measures to try to boost productivity and growth, such as reducing corporation tax rates, making it easier and cheaper for firms to borrow and by providing help to businesses setting up in areas of high unemployment. However, at a time when business confidence is low, it is not easy to persuade firms in the private sector to invest. There are some who believe that growth will resume only if the government takes a more active role in the economy by, for example, spending more on infrastructure projects and on improving the skills of the workforce. 10
15

Source: news reports, January 2012

0 1 Define the term 'real incomes' (**Extract B**, line 13). (5 marks)

0 2 Using **Extract A**, identify **two** significant points of comparison between the index of real GDP and total employment over the period shown. (8 marks)

0 3 **Extract C** (lines 3–4) states: 'Low economic growth is usually accompanied by rising unemployment.'

Explain why, in a period of low economic growth, unemployment is likely to increase. (12 marks)

0 4 **Extract C** (lines 1–2) states: 'Many believe that the main objective of government economic policy should be to increase productivity and economic growth.'

Using the data and your economic knowledge, discuss the difficulties that the Government is likely to encounter when attempting to boost the rate of growth of the UK economy. (25 marks)

Turn over ►

Do **not** answer Context 2 if you have answered Context 1.

Total for this Context: 50 marks

OR

Context 2

UK BALANCE OF PAYMENTS ON CURRENT ACCOUNT

Study **Extracts D, E and F**, and then answer **all** parts of Context 2 which follow.

Extract D: Summary of UK balance of payments on current account, 2005 to 2010, £ billion

Year	Balance of trade in goods and services (£bn)	Total income balance, including investment income (£bn)	Current transfers balance (£bn)	Current account balance (£bn)
2005	-42.70	21.89	-11.85	-32.66
2006	-40.73	9.50	-11.88	-43.11
2007	-42.65	21.37	-13.55	-34.83
2008	-39.12	33.14	-13.77	-19.75
2009	-25.64	20.40	-15.08	-20.32
2010	-39.68	23.04	-20.08	-36.72

Source: official statistics, November 2011

Extract E: UK trade deficit widens

Britain's trade deficit widened in November, reversing the improvement in the previous month. Although the figures were disappointing, the longer term trends show that the rebalancing of the economy is going ahead but the pace is slow and must be strengthened. The Government's aim is to rebalance the UK economy by switching demand away from consumption and government spending, financed by borrowing, towards exports and investment. Over the past 3 months, exports of goods to the European Union (EU) have risen by 1.4% and exports to non-EU countries have risen by 4.7%. However, imports of goods from countries outside the EU hit a record high. The UK has found it hard to reduce imports, despite a fall of almost 25% in the value of the pound since 2007. The surplus on trade in services has remained fairly steady. Overall, the deficit on the current account of the balance of payments is likely to be lower in 2011 than it was in 2010.	1 5 10
There have been warnings that the Government's hopes of rebalancing the economy away from domestic demand towards manufacturing and exports will be hard to achieve in 2012. With economists predicting that the eurozone is likely to go into recession and with the pound starting to strengthen against the euro, it is unlikely that there will be much, if any, growth in exports to our largest market. It is essential that UK exporters look to faster-growing markets in other parts of the world.	15

Source: news reports, January 2012

Extract F: Rebalancing the UK economy

Economic policymakers hope that UK trade with the rest of the world will help to rebalance the economy and boost aggregate demand. With little or no growth in domestic consumption and cuts in government spending, it is important that exports and investment, particularly in manufacturing, increase. Growth and employment will suffer if this change in the structure of the economy fails to materialise. 1
5

The Bank of England has concluded that the fall in the value of the pound between 2007 and 2009 has encouraged a shift towards exports and reduced the trade deficit. Compared to 2007, UK exports are now around 15% cheaper than those of our closest competitors. However, at least one member of the Bank's Monetary Policy Committee believes that the UK may need a further reduction in the sterling exchange rate to eliminate the deficit. 10

The expected slowdown in the world economy, the long-term decline in manufacturing and the over-reliance on exports of financial services make it difficult for the UK to reduce the trade deficit in the short run. Also, there has been little evidence that UK residents have switched away from buying imports towards buying domestically-produced goods. It is likely to take some time for UK manufacturing firms to expand their capacity and to penetrate new markets. Growth in the manufacturing sector will be achieved and maintained only if there are supply-side improvements in the economy. 15

Source: news reports, January 2012

0 5 Define the term 'deficit on the current account of the balance of payments' (**Extract E**, line 11). (5 marks)

0 6 Using **Extract D**, identify **two** significant points of comparison between the balance of trade in goods and services and the current account balance over the period shown. (8 marks)

0 7 **Extract E** (lines 11–12) states that 'the deficit on the current account of the balance of payments is likely to be lower in 2011 than it was in 2010.'

Explain **two** factors, **other than a fall in the value of the pound**, which might help to reduce the size of the deficit on the current account of the UK balance of payments. (12 marks)

0 8 **Extract F** (lines 1–2) states: 'Economic policymakers hope that UK trade with the rest of the world will help to rebalance the economy and boost aggregate demand.'

Using the data and your economic knowledge, assess the impact on the performance of the UK economy of a significant increase in exports and a reduction in imports of goods and services. (25 marks)

END OF QUESTIONS

There are no question printed on this page