



General Certificate of Education

Economics

ECON4: The National and International Economy

Mark Scheme

2010 examination - January series

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

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of candidates' 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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Advanced Level Economics Unit 4

General Instructions

Marks awarded to candidates should be in accordance with the following mark scheme and examiners should be prepared to use the full range of marks available. The mark scheme for most questions is flexible, permitting the candidate to score full marks in a variety of ways. Where the candidate's response to a question is such that the mark scheme permits full marks to be awarded, full marks **MUST** be given. A perfect answer is not necessarily required for full marks. But conversely, if the candidate's answer does not deserve credit, then no marks should be given.

Occasionally, a candidate may respond to a question in a reasonable way, but the answer may not have been anticipated when the mark scheme was devised. In this situation, **OR WHENEVER YOU HAVE ANY DOUBT ABOUT THE INTERPRETATION OF THE MARK SCHEME**, you must in the first instance telephone your team leader to discuss how to proceed.

Two approaches have been used in the construction of the mark scheme.

- (i) **An issue based approach.** The mark scheme for parts (a) and (b) of the data response questions and part (a) of the essay questions adopts this approach. The mark scheme lists the marks that can be awarded for particular issues (and associated development) that the candidate might include in the answer.
- (ii) **A levels approach.** This approach is used for part (c) of the data response questions and part (b) of the essay questions. The Levels Mark Scheme on the next page identifies five levels representing differences in the quality of work. A range of marks is allocated to each level. First decide the level into which an answer falls. The level chosen should be the one which **best fits** the answer provided by the candidate. It is **not** intended that the answer should satisfy every statement in the level description. Then think in terms of awarding the mid-point mark which has been identified for that level (e.g. 14 marks for Level 3). Move up or down from this notional mark by considering the extent to which the answer meets the level description overall. Strength in one skill can outweigh weakness in another. When using the Levels Mark Scheme the marker **must** identify where a particular skill is being demonstrated. The **key** to be used to identify the skill is given after the level descriptions. The question-specific mark scheme summarises the information which could be used to answer the question, but without attaching marks to particular issues.

THE LEVELS MARK SCHEME FOR A2

Level Descriptions

In part (c) of the data response questions and part (b) of the essay questions, 40% of the marks are available to award to candidates who demonstrate that they can evaluate economic arguments and evidence, and make informed judgements. An answer showing no evidence of evaluation, however good the analysis, should be awarded a maximum of 15 marks (in Level 3). The quality of evaluation should be the sole distinction between a Level 4 and Level 5 answer. As indicated below, the **Quality of Written Communication** used should be taken into account when awarding marks.

Level 1: A very weak answer

Few, if any, relevant issues are recognised. Descriptions and explanations lack clarity. Economic concepts and principles are not adequately understood or applied to the question and its context. No satisfactory analysis or evaluation. Little, if any, appreciation of the inter-relatedness of economic issues, problems and institutions. There might be some evidence of organisation in the answer but generally it fails to answer the question. Spelling, punctuation and grammar may be poor. There is little use of specialist vocabulary.

0 to 6 marks

Mid-Point 4 marks

Level 2: A poor answer but some understanding is shown

A few issues are recognised but there is only limited evidence of the candidate's ability to apply relevant economic concepts. Descriptions and explanations are sometimes hard to follow. An attempt is made to answer the question but there is little satisfactory analysis or evaluation. There is some very limited appreciation of the inter-relatedness of economic issues, problems and institutions. There is some limited logic and coherence in the organisation of the answer. The candidate demonstrates some ability to spell commonly used words and to follow the standard conventions of punctuation and grammar. Some use of specialist vocabulary is made but this is not always applied appropriately.

7 to 11 marks

Mid-Point 9 marks

Level 3: An adequate answer with some correct analysis but very limited evaluation

A few issues are recognised. The candidate has attempted to apply relevant economic concepts and ideas to the question and its context. A reasonable understanding of some concepts and theories is demonstrated. However, the evaluation of the issues, arguments and evidence is limited or superficial. There is some understanding of the inter-relatedness of economic issues, problems and institutions. There is some logic and coherence in the organisation of the answer. The candidate is generally able to spell commonly used words and usually follows the standard conventions of punctuation and grammar. Some descriptions and explanations are easy to understand but the answer may not be expressed clearly throughout. There is some use of specialist vocabulary which is applied appropriately.

12 to 16 marks

Mid-Point 14 marks

Level 4: Good analysis but limited evaluation

Several relevant issues are identified. Good understanding of economic concepts and principles is demonstrated throughout. The candidate is able to apply these concepts and principles to the context to answer the question. A clear understanding of the inter-relatedness of economic issues, problems and institutions is demonstrated. The candidate shows the ability to think as an economist making effective use of the economist's 'tool kit' of concepts, theories and techniques. There is some appreciation of alternative points of view. Satisfactory use is made of evidence and/or theoretical analysis to evaluate the issues/arguments/models identified. The candidate

demonstrates some ability to synthesise the arguments presented and come to some relevant conclusions although these might not always be based on evidence presented. Spelling is generally accurate and the standard conventions of punctuation and grammar are usually followed. The answer is well organised. Descriptions and explanations are clearly expressed. A wide range of specialist vocabulary is used with facility.

17 to 21 marks

Mid-Point 19 marks

Level 5: Good analysis and evaluation

Several relevant issues are identified. Good understanding of economic concepts and principles is demonstrated throughout. The candidate is able to apply these concepts and principles to the context to answer the question. A clear understanding of the inter-relatedness of economic issues, problems and institutions is demonstrated. The candidate shows the ability to think as an economist making effective use of the economist's 'tool kit' of concepts, theories and techniques. There is an appreciation of alternative points of view. Good use is made of evidence and/or theoretical analysis to evaluate the issues/arguments/models identified. The candidate demonstrates the ability to synthesise the arguments presented and come to conclusions which are based on the evidence presented. A clear final judgement is made. Spelling is generally accurate and the standard conventions of punctuation and grammar are usually followed. The answer is well organised. Descriptions and explanations are clearly expressed. A wide range of specialist vocabulary is used with facility.

22 to 25 marks

Mid-Point 24 marks

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.
- A** 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.

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

1 (a) Using **Extract A**, identify **two** main features of the export of goods in 2007. (5 marks)

Award one mark for each valid point made and two marks for the supporting reference to the data, up to a maximum of 5 marks.

Points might include:

- China has the largest absolute increase in exports of goods over the period (\$12bn)
- India has the smallest absolute increase in the export of goods (\$2bn)
- In terms of % increase, India has the highest % growth of exports of goods (18.2%)
- All economies with the exception of India show a similar growth in export of goods of 11 – 12%
- All economies show a quarter-on-quarter increase in the export of goods, although China's export of goods remains constant in Q3 and Q4 (\$106bn), as does that of India Q2/Q3 (\$12bn)
- India has the smallest value of exports of goods in each quarter (a range of \$11 - \$13bn)
- China has the greatest value of export of goods in each quarter (a range of \$94 - \$106bn)
- Over the whole year and across all the economies, the range of values is \$95bn (India Q1, \$11bn – China Q3/Q4, \$106bn)

Award a maximum of **1 mark** for each supporting reference to the data if the per cent sign is not used.

A maximum of **2 marks** may be awarded if the candidate simply trawls through the data.

A maximum of **2 marks** may be awarded if there is no use of statistics which support the point(s) being made.

A maximum of **4 marks** may be awarded where there is evidence of an overview (one good point is included with data) even though other parts of the answer give the impression of a few statistics chosen at random.

MAXIMUM FOR PART (a): 5 MARKS

1 (b) Extract B (lines 1-2) refers to the ‘importance of international trade in promoting economic growth’.

Explain the concept of economic growth **and** analyse **two** ways in which international trade can increase a country’s economic growth. *(10 marks)*

For candidates who:

explain the concept of economic growth, e.g.

- GDP/actual growth
- potential growth

**Up to 3 marks per definition or explanation
to a maximum of 6 marks (including diagrams)**

analyse two ways in which international trade can increase a country’s economic growth, e.g.

- encouraging the identification and development of a country’s comparative advantage (1 mark), explaining it in terms of opportunity cost (1 mark) and through the exploitation of such an advantage through specialisation (1 mark), causing output to increase (1 mark)
- facilitating the acquisition of cheap imports of energy and raw materials and being more able to pay for these through enhanced export performance
- increasing aggregate demand in the economy especially with the introduction of an export-led multiplier
- trade as a stimulus to supply-side reforms in order to strengthen an economy’s performance in world markets
- a particular reference to the way in which trade can stimulate efficiency drives which can be reflected in improvements to labour productivity
- trade as a stimulant to investment, a prime mover in achieving higher economic growth

**Up to 4 marks may be awarded for each of the chosen factors
(1 mark for identification and 3 marks for analysis)**

make relevant use of diagrams in the analysis

**Up to 2 marks per diagram
(1 mark for labelling, 1 mark for correct information shown)
to a maximum of 3 marks**

Reward references to the UK/other economies

up to 2 marks

A candidate can be awarded a maximum of **6 marks** if only one part is attempted.

MAXIMUM FOR PART (b): 10 MARKS

1(c) Extract B (lines 40-42) suggests the US and the UK may be ‘very concerned for their macroeconomic performance’ if free trade agreements lead to greater openness of their economies.

Using the data and your economic knowledge, assess the possible impact on the UK economy of greater openness to world markets. *(25 marks)*

It is hoped that candidates will be able to show an understanding of the term ‘macroeconomic performance’ and ‘greater openness’ before going on to assess the potential impact on the UK economy. Although growth may be returned to, examiners should expect both greater depth of analysis and some evaluation compared to the answer offered in response to part (b). **Where a candidate only repeats his/her answer to part (b) with limited elaboration, the mark awarded should not go beyond mid-level 2.**

Examiners should also bear in mind that the greater openness referred to could apply to other economies and not just the UK, and some candidates might develop their responses in this way.

To achieve **Level 4**, at least **two** issues should be presented and evaluated.

To achieve **Level 5**, there should, in addition, be an attempt to provide a more general evaluation of the arguments referred to, in order that a concluding judgement can be made by the candidate.

Where there is no **explicit** reference to the data, award a maximum of **20 marks**.

There must be evidence of evaluation for candidates to score more than **15 marks**.

The issues identified below are intended to provide an indication of some of the areas which might be discussed. Candidates can only be expected to consider a few of these and/or other issues in the time available.

Issues and areas for discussion include:

Introductory:

- the nature of trade restrictions
- the past progress towards free trade
- the work of GATT/WTO

Developing a response to a question:

- whether greater openness means what it implies, e.g. it might be argued by some countries that export subsidies do not count as a restriction
- the unfettered ability to exploit absolute/comparative advantages
- the particular threat of newly-emerging economies and, in particular, the BRIC economies
- the impact on UK growth
- the impact on UK inflation
- the impact on the balance of payments and the exchange rate
- the impact on UK employment

Evaluative issues:

- how restricted trade had been before the greater openness
- the strength of the economy to face the challenge presented by greater openness
- the importance of trade to the economy
- the impact perhaps being determined by the phase of the economic cycle the UK was in at the outset
- the relevance and importance of distinguishing between short and long term considerations
- the degree of openness, and hence vulnerability, to exogenous shocks

Also give credit for:

- relevant use of evidence and examples not contained in the data
- diagrams
- an overall judgement on the issues raised

USE THE LEVELS MARK SCHEME ON PAGES 4 AND 5

MAXIMUM FOR PART (c): 25 MARKS

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

2 (a) Using **Extract C**, identify **two** points of comparison in real GDP growth between the economies shown for the period 2006 to 2009. *(5 marks)*

Award one mark for each valid point made and two marks for the supporting reference to the data, up to a maximum of 5 marks. Points might include:

- all countries are similar in showing a slow-down in the rate of growth of real GDP between 2006 and 2009, eg the euro area from 2.8% in 2006 to 0.2% in 2009
- all economies over the period, with the exception of the UK in 2009, avoid negative growth of real GDP, with actual or forecast growth ranging from 0.1% in the USA and G7 economies in 2009, to 5.6% in the Asian economies, 2006/07
- the UK shows the greatest slow-down in the growth of real GDP (2.9% points), the Asian economies, the smallest slowdown (2.4 % points)
- taking the average growth of real GDP over the period, the Asian economies are the most impressive (4.6%), the major advanced economies the least impressive (1.55%)
- the actual figures for 2006 and 2007 show the Asian economies with 5.6% growth of real GDP in each year, whereas the other economies never exceed 3.0% (UK, 2007)
- the forecast figures for 2008 and 2009 show the Asian economies by far the best growth performers whereas 1.6% is the best that can be achieved amongst the other economies shown (USA in 2008)

Award a maximum of **1 mark** for each supporting reference to the data if the % sign is not used

A maximum of **2 marks** may be awarded if the candidate simply trawls through the data.

A maximum of **2 marks** may be awarded if there is no use of statistics which support the point(s) being made.

A maximum of **4 marks** may be awarded where there is evidence of an overview (one good point is included with data) even though other parts of the answer give the impression of a few statistics chosen at random.

MAXIMUM FOR PART (a): 5 MARKS

2 (b) Extract D (line 3) suggests that it is possible ‘the EU will enter recession’.

Explain the term ‘recession’ **and** analyse **two** possible causes of a recession.

(10 marks)

For candidates who:

explain the term ‘recession’, eg

- a definition, eg two successive quarters of negative GDP growth
- putting the term into the context of the whole economic cycle
- referring to the UK/EU experience
- relates to slowdowns and output gaps

**Up to 3 marks per definition or explanation to a maximum of 6 marks
(including diagrams)**

analyse two causes of a recession, eg

- an external shock such as higher oil prices (1 mark) so that more spending power has to be reallocated to oil/petrol and away from non-oil products (1 mark) and cost-push inflation erodes real income (1 mark), causing consumer demand to suffer (1 mark)
- unanticipated domestic development(s)
- damage to confidence amongst consumers, impact on consumption
- damage to business confidence, impact on investment
- housing market developments
- higher interest rates
- fiscal constraints
- loss of major overseas markets
- changes to aggregate demand

**up to 4 marks may be awarded for each of the chosen causes
(1 mark for identification, up to a further 3 marks for the analysis)**

make relevant use of diagrams in the analysis

**up to 2 marks per diagram
(1 mark for labelling, 1 mark for correct information shown)
to a maximum of 3 marks**

Reward references to the UK/other economies

up to 2 marks

A candidate can be awarded a maximum of **6 marks** if only one part is attempted.

MAXIMUM FOR PART (b): 10 MARKS

2 (c) Extract D (lines 39-40) concludes that ‘the EU, including the UK, may need to rely on an external economic stimulus to improve macroeconomic performance’.

Using the data and your economic knowledge, assess the possible effects on UK macroeconomic performance of an external economic stimulus, whether arising from other EU members or from other parts of the world. (25 marks)

It is hoped that candidates will show an understanding of what an external economic stimulus could be and then compare it to what might be expected from within the UK in terms of stimuli to, or constraints on, macroeconomic performance.

To achieve **Level 4**, at least **two** issues should be presented and evaluated.

To achieve **Level 5**, there should, in addition, be an attempt to provide a more general evaluation of the arguments referred to, in order that a concluding judgement can be made by the candidate.

Where there is no **explicit** reference to the data, award a maximum of **20 marks**.

There must be evidence of evaluation for candidates to score more than **15 marks**.

The issues identified below are intended to provide an indication of some of the areas which might be discussed. Candidates can only be expected to consider a few of these and/or other issues in the time available.

Issues and areas for discussion include:

Introductory:

- a consideration of the nature of the stimulus, e.g. lower oil prices, the recovery of the US economy, the further rapid growth of BRIC economies and their markets, rejuvenated MNC investment activity
- an understanding of the term ‘macroeconomic performance’

Developing a response to the question:

- economic growth
- employment
- prices
- the balance of payments
- the exchange rate

Evaluative comments:

- how an external stimulus relates to internal developments, eg interest rates, fiscal boost
- the ability of the UK economy to face the challenge which an external stimulus might create
- the duration of the stimulus
- whether that stimulus is having to combat equally strong external ‘deflators’ affecting the UK economy
- the strength of the stimulus
- whether or not it comes after significant weakening of the UK economy has taken place

- whether the stimulus benefits all of the EU and therefore whether the UK can also benefit, as a member, from the rejuvenation of the EU
- the possible greater significance should the stimulus arise from the remainder of the EU
- whether or not the stimulus comes at a time of overheating of the economy
- the impact on business and consumer confidence and the effects of this

Also give credit for:

- relevant use of evidence and examples not contained in the data
- diagrams
- an overall judgement on the issues raised

USE THE LEVELS MARK SCHEME ON PAGES 4 AND 5

MAXIMUM FOR PART (c): 25 MARKS

SECTION B**3****Total for this question: 40 marks**

3 (a) Explain the concept of the natural rate of unemployment **and** the factors which might determine it. *(15 marks)*

For candidates who:

Define/explain unemployment

Up to 2 marks

Define/explain the natural rate of unemployment, eg definition of the natural rate: the proportion of workers who are voluntarily unemployed when the labour market is in equilibrium, refusing opportunities for work at existing wage rates, the rate at which inflation is stable; explanation of the natural rate of unemployment, eg

- voluntary unemployment, e.g. structural, frictional, compared to involuntary unemployment
 - its relationship with stable inflation
 - the significance of unemployment being above/below the natural rate
 - the Phillips Curve
 - the labour market in equilibrium
- Up to 5 marks per feature explained
(1 mark for identification and up to 4 further marks for the explanation)**

Explain the factors determining the natural rate of unemployment, eg

- the pace of structural change in the economy (1 mark) to reflect more accurately the changing pattern of consumer demand (1 mark) so that, as consumer demand rises (1 mark), it is more likely that the supply side can respond more adequately (1 mark), providing a greater likelihood that inflation can remain stable (1 mark)
- the influences on frictional unemployment
- the incidence of seasonal unemployment
- the flexibility of wage rates
- mobility of the labour force occupationally and geographically
- welfare reform
- training and re-training
- government initiatives, eg the New Deal and Family Tax Credits

**Up to 5 marks per determinant explained
(1 mark for identification and up to 4 further marks for the explanation)**

use relevant diagrams to help the explanations

Up to 2 marks per diagram**(1 mark for labelling, 1 mark for the correct information shown) to a total of 4 marks**

A maximum of **10 marks** may be awarded if a candidate only answers one part of the question.

MAXIMUM FOR PART (a): 15 MARKS

3 (b) In May 2008, the Governor of the Bank of England spoke of the need for the UK economy to move away from spending and importing, towards saving and exporting.

Evaluate the consequences for UK unemployment if this movement were to occur.
(25 marks)

It is hoped that candidates will attempt an explanation of what the Governor means by the suggested changes and then focus on the impact of what is explained on unemployment trends in the UK.

To achieve **Level 4**, at least **two** issues should be presented and evaluated.

To achieve **Level 5**, there should, in addition, be an attempt to provide a more general evaluation of the arguments referred to, in order that a concluding judgement can be made by the candidate.

There must be evidence of evaluation for candidates to score more than **15 marks**.

The issues identified below are intended to provide an indication of some of the areas which might be discussed. Candidates can only be expected to consider a few of these and/or other issues in the time available.

Issues and areas for discussion include:

Introductory:

- the types of unemployment
- general comments on saving/spending, exporting/importing
- the general relevance of the suggested changes made to each of these, ie the potential benefits to the real economy

Developing a response to the question:

- the impact of reduced spending/slowdown in the rate of growth of spending on AD
- the impact of changes in spending on imports on AD and the current account
- the potential benefits of increased saving to the financing of investment
- the potential release of resources to the export sector for GDP and the current account
- how the suggested adjustments might be achieved and the impact of this, e.g. through changes in interest rates
- the multiplier
- short-run and long-run distinctions

Evaluation:

- the extent of any imbalance in the economy and whether it has been significant
- the extent of, and success with, the adjustment which takes place
- how enduring the adjustment proves to be
- whether or not this adjustment really will prove to be the remedy for the economy's weaknesses
- the possibility of external influences impeding the process
- placing adjustment into the context of recent UK experience

Also give credit for:

- relevant use of evidence and examples
- diagrams
- an overall judgement on the issues raised

USE THE LEVELS MARK SCHEME ON PAGES 4 AND 5

MAXIMUM FOR PART (b): 25 MARKS

4 (a) Explain how fiscal policy might be used to bring about supply-side improvements to an economy. *(15 marks)*

For candidates who:

define fiscal policy and/or supply side and/or supply-side improvements

Up to 2 marks per definition to a maximum of 4 marks

explain ways in which fiscal policy might be used with this objective in mind, eg

- a reduction in welfare benefits (1 mark), which can be related to the unemployment trap (1 mark) whereby the benefits system makes non-work financially attractive (1 mark) since wage may fall below expected benefits (1 mark) and the replacement ratio is in need of change (1 mark)
- a reduction in income tax rates/increase in tax thresholds, related to the poverty trap
- government initiatives such as the New Deal and Tax Credit system
- relevant types of government spending such as resettlement allowances, health-care, but more importantly, education and training/retraining programmes
- tax allowances on new investment
- reforms to corporation tax
- appropriate regional spending
- infra-structure

Up to 5 marks

(1 mark for identification and 4 further marks for explanation)

per aspect of fiscal policy relevant to supply-side improvements that is explained

use relevant diagrams to help the explanations

Up to 2 marks per diagram

(1 mark for labelling, 1 mark for the correct information shown)

to a total of 4 marks

MAXIMUM FOR PART (a): 15 MARKS

4 (b) The level of UK public sector spending grew from 37% of GDP in 1997 to over 45% in 2008.

To what extent do you regard such an expansion of the public sector as beneficial to the UK economy?
(25 marks)

It is hoped that candidates will be able to comment on the significance of the increase in public spending, give some indication of why this increase has taken place (e.g. a government making up for lost time having initially accepted the previous government's spending constraints, increased military spending, increased spending on health and education). Then, an evaluation of such an increase should follow.

To achieve **Level 4**, at least **two** issues should be presented and evaluated.

To achieve **Level 5**, there should, in addition, be an attempt to provide a more general evaluation of the arguments referred to, in order that a concluding judgement can be made by the candidate.

There must be evidence of evaluation for candidates to score more than **15 marks**.

The issues identified below are intended to provide an indication of some of the areas which might be discussed. Candidates can only be expected to consider a few of these and/or other issues in the time available.

Issues and areas for discussion include:

Introductory:

- the public sector
- the economic background through the period in question
- types of government spending

Developing a response to the question:

- the impact on AD
- the multiplier effect
- the possibility of crowding out
- the potential for higher taxes
- the need for higher taxes
- whether benefiting both actual and potential growth
- the danger of inflation
- the boost to consumer spending and the potential impact on the current account
- the impact on employment
- nationalisation
- merit/public goods provision
- income distribution

Evaluation:

- the ability of the economy to absorb such an increase in public spending
- the trends in the economic cycle during this period of increased spending
- the nature of the spending taking place

- the impact on the budget deficit and National Debt
- the impact on UK/EU fiscal rules
- the possible significance of government action of this nature when crises loom, e.g. the credit crunch and the need for stabilisation of the financial sector and the whole economy

Also give credit for:

- relevant use of evidence and examples
- diagrams
- an overall judgement on the issues raised

USE THE LEVELS MARK SCHEME ON PAGES 4 AND 5

MAXIMUM FOR PART (b): 25 MARKS

5 (a) Explain the factors which help determine the exchange rate of a currency.
(15 marks)

For candidates who:

define exchange rates and/or make other relevant comments, eg appreciation/depreciation, reference to exchange rate systems, a reference to the basic importance of supply and demand

Up to 2 marks per point to a maximum of 4 marks

explain relevant determining factors, eg

- trade flows (1 mark) whereby overseas demand for a country's exports creates a demand for its currency (1 mark) in order to pay for these goods/services (1 mark) while the country's demand for imports causes a selling of domestic currency to buy foreign currencies (1 mark) and it will be the relative significance of exports in relation to imports which determines the impact on the exchange rate (all other things being equal) (1 mark)
 - the type of exchange rate system and hence whether or not government intervention plays a part (candidates may only deal with government intervention without mentioning systems and this is quite acceptable)
 - investment flows
 - speculation/expectations/confidence
 - interest rates
 - the condition of the domestic macroeconomy, eg inflation and its impact on competitiveness
 - supply-side influences on competitiveness, such as productivity, and how this relates to similar developments in other country
- Up to 5 marks per determinant explained
(1 mark for identification and up to 4 further marks for explanation)**

Reward diagrams as long as they refer specifically to, and aid the explanation of, a determinant rather than simply duplicating any earlier use of supply and demand diagrams in the introduction for which credit has already been given.

Award up to 2 marks per relevant diagram (1 mark for labelling, 1 mark for the information shown). Up to 4 marks per diagram are possible for a more complex diagram (as above but a further 2 marks possible for the greater amount of information provided, e.g. intervention buying of a currency). A maximum of 6 marks can be awarded for diagrams.

MAXIMUM FOR PART (a): 15 MARKS

5 (b) In a floating exchange rate system, a currency may be subject to frequent fluctuations in its external value.

Discuss the possible economic consequences of such fluctuations for the achievement of a country's macroeconomic objectives. *(25 marks)*

It is hoped that candidates will be able to make some distinction between fixed and floating exchange rates, go on to show some understanding of what might cause fluctuations (which may or may not duplicate something included in part (a)), show an understanding of the term 'macroeconomic objectives', before relating the two issues in an evaluative discussion.

To achieve **Level 4**, at least **two** issues should be presented and evaluated.

To achieve **Level 5**, there should, in addition, be an attempt to provide a more general evaluation of the arguments referred to, in order that a concluding judgement can be made by the candidate.

There must be evidence of evaluation for candidates to score more than **15 marks**.

The issues identified below are intended to provide an indication of some of the areas which might be discussed. Candidates can only be expected to consider a few of these and/or other issues in the time available.

Issues and areas for discussion include:

Introductory:

- a floating exchange rate system
- floating v fixed
- the nature of macroeconomic objectives
- managed flexibility of the exchange rate

Developing a response to the question:

- the significance of any trend in the exchange rate, i.e. whether tending towards appreciation or depreciation over time
- the exchange rate and competitiveness impacting on export/import performance and hence the current account
- the impact on prices
- the impact on business confidence and hence investment
- the impact on employment
- the contribution fluctuations make to economic growth performance

Evaluation:

- the degree of fluctuation
- the frequency/predictability of fluctuations
- the duration of such fluctuations
- the possible relevance of what is causing those fluctuations
- the ability to prevent or control them
- the degree of instability/stability elsewhere in the economy
- whether or not these fluctuations are the only reason for government objectives not being achieved or are only one of a number of factors

Also give credit for:

- relevant use of evidence and examples
- diagrams
- an overall judgement on the issues raised

USE THE LEVELS MARK SCHEME ON PAGES 4 AND 5

MAXIMUM FOR PART (b): 25 MARKS