Rewarding Learning

ADVANCED SUBSIDIARY (AS)
General Certificate of Education
2009

Economics

Assessment Unit AS 2

The National Economy

[AE121]

FRIDAY 12 JUNE, MORNING

AE121

TIME

1 hour 30 minutes.

INSTRUCTIONS TO CANDIDATES

Write your Centre Number and Candidate Number on the Answer Booklet provided.
Answer **Question 1** and **one** question from **Questions 2**, **3 or 4**.

INFORMATION FOR CANDIDATES

The total mark for this paper is 80.
Quality of written communication will be assessed in all questions **except 1(d)** and **1(e)**.
Figures in brackets printed down the right-hand side of pages indicate the marks awarded to each question or part question.

ADVICE TO CANDIDATES

You are advised to take account of the marks for each part question in allocating the available examination time.

Question 1: Data Response

The following article was written in April 2008.

Study it carefully and answer the questions which follow.

"Lies damned lies and recessions"

Many economists define a recession as a period of two successive quarters of negative economic growth. However, nobody seems to know exactly where this rather silly idea originated. One theory is that it was dreamt up by advisers to American President, Lyndon Johnson, in the 1960s to enable him to claim that the economy was "OK" in spite of the fact that unemployment was rising and incomes were falling. Just so long as there had not been two straight quarters of falling output he could state that the economy was doing just fine! 1

The following example shows just how meaningless the standard recession definition is. Suppose an economy contracts by 5 per cent in the first quarter of the year, grows by 0.1 per cent in the next and contracts by a further 3 per cent in the third quarter. The economy will have shrunk significantly over these three quarters and there will probably have been sharp declines in employment and wages. However, technically there is no recession, which of course is absurd. Add to this the fact that the gross domestic product (GDP) figures on which growth is based are not always particularly accurate and the irrelevance of the official definition becomes even clearer. 2

By the end of 2007 the American economy was growing by a mere 0.6 per cent. Growth was only positive because of the strength of net exports (exports less imports) which had been helped by a dramatic fall in the value of the dollar. But growth at this very low rate is not sufficient to prevent unemployment from rising. Increasing population and higher productivity require the US economy to grow at 2.5 per cent annually just to maintain the existing rate of joblessness. 3

This dramatic slow down in the American economy has been exported across the Atlantic and the UK is also showing signs of slowing growth and weakening consumer confidence. This is reflected in the result of the consumer confidence survey which asks consumers how they feel about their personal financial situation and about the state of the economy as a whole in the year ahead. For example, a score of 0 means that 50 per cent of consumers are pessimistic and 50 per cent are optimistic and a score of plus 20 means that 60 per cent are optimistic and 40 per cent are pessimistic. 4

Results of Consumer Confidence Survey

	April 2007	April 2008
Personal financial situation over next 12 months	+12	0
General economic situation over next 12 months	–18	–38

Fig. 1

Rachel Joy, of National Opinion Polls (NOP) who carried out the survey said, “C
confidence is at its lowest level since 1992. With the news dominated by stories of
recession, the credit crunch, housing market collapse and future petrol and food price
it will take more than a small reduction in interest rates to alleviate the current gloomy m
of the UK consumer”.

Adapted from © The Times, 29 April 2008, Lies, damned lies and Statistics by Gerard Baker

(a) In paragraph 1 the standard definition of recession is described as “rather silly”. Explain why defining a recession as two successive quarters of negative growth is flawed. [6]

(b) Paragraph 3 states that the value of net exports has been helped by the fall in the value of the dollar. Explain why a fall in the value of the dollar is likely to increase the USA’s net exports. [8]

(c) Paragraph 3 states that unemployment in the USA will increase unless there is significant economic growth. Explain why this is so. [8]

(d) Using the information in Fig. 1, describe what has happened to consumer confidence levels in the UK between April 2007 and April 2008. [4]

(e) Fig. 1 shows that consumers are much more pessimistic about the general economic situation than about their personal financial situation. Explain why this might be so. [4]

(f) In paragraph 5 Rachel Joy states that a small interest rate cut would not alleviate the gloomy mood of the UK consumer. Critically examine some of the policies which governments and central banks could use to increase consumer spending during a period of economic slowdown. [10]

Essays:

Answer **one** from **Questions 2, 3 or 4**.

2 "Bank of England misses inflation target"

(a) Explain what is meant by the rate of inflation. [10]

(b) Analyse the main causes of inflation. [15]

(c) Evaluate the view that it is wrong for the Bank of England to concentrate solely on the control of inflation at the expense of other important economic objectives. [15]

3 "Government aims to increase economic activity"

(a) Explain what is meant by the economic activity rate. [10]

(b) Analyse the factors which influence an economy's rate of economic activity. [15]

(c) Critically examine some of the policies which a government could adopt in order to increase an economy's rate of economic activity. [15]

4 "Supply side policies unpopular with trade unions"

(a) Explain what is shown by the short run aggregate supply curve. [10]

(b) Analyse the factors which might lead to a rightward shift in the long run aggregate supply curve. [15]

(c) Evaluate the impact of strong supply side policies upon economy and society. [15]

THIS IS THE END OF THE QUESTION PAPER