



Rewarding Learning
ADVANCED SUBSIDIARY (AS)
General Certificate of Education
2009

Economics

Assessment Unit AS 3

assessing

Module 2: The National
Economy

[ASE31]

FRIDAY 12 JUNE, MORNING



TIME

1 hour 30 minutes.

INSTRUCTIONS TO CANDIDATES

Write your Centre Number and Candidate Number on the Answer Booklet provided.
Answer Question 1 and any **one** of 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** Question 1 parts (a) and (d).

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.

You **must** answer this question.

1 The following article was written in August 2008.

Study it carefully and answer the questions which follow.

“Inflation at 16 year high”

The recently released official figures for inflation show that the Consumer Price Index (CPI) rose by 4.4% in the year ending July 2008, up from 3.8% for the year ending in June. This is more than double the Bank of England’s inflation target of 2% and the highest annual rate since 1992.

1

Food was the main culprit behind this big rise in inflation. Overall, food prices in July were up 13.7% from levels a year earlier. Bacon rose by 13%, chicken by 35% and dairy products by 19%. The price comparison website, mysupermarket.com, estimates that the average grocery bill for a family of four has risen by more than a quarter to £127 a week since summer 2007. The overall inflation rate has only been kept at 4.4% because of falling prices for luxury electronic goods such as dishwashers and fridge freezers. With the National Minimum Wage set at £5.52 per hour, it is clear that low income families will be hit hardest by the latest round of price increases.

2

Food prices have been driven up by increasing demand from fast growing Asian economies such as China, and by farmers switching grain production to biofuels rather than food.

3

Not only do these figures show the highest rate of food price inflation since 1980, they also represent another economically significant landmark. A number of interest rates have now fallen below the official measure of inflation, giving the UK negative real interest rates for the first time in 27 years. This is likely to affect economic behaviour in several ways, not least that spending will be more attractive than saving.

4

It is therefore not surprising that there is increased pressure on the Bank of England’s Monetary Policy Committee to increase interest rates. However, given that much of the inflationary pressure faced by the UK has its origins in world rather than UK markets, it is not certain that increasing interest rates will have any significant impact on this particular round of inflation.

5

The main challenge for the government is to prevent inflation having a knock-on effect on wages and creating a wage-price spiral. Hence public sector unions have been offered below-inflation pay increases: this has provoked outrage from trade unionists and led to a wave of public sector strikes.

6

One union spokesperson said, “Public sector pay and the National Minimum Wage must increase by more than the rate of inflation so that public servants and the low paid experience an increase rather than a decrease in living standards.”

7

Source: Adapted from The Times August 13th 2008. Authors Grainne Gilmore and Steve Hawkes

- (a) Explain what is meant by inflation. [3]
- (b) Using the information in paragraph 1, explain the difference between rising inflation and rising prices.
- (c) Paragraph 2 states that the current round of price rises will hit the low paid hardest. Explain why this is so. [6]
- (d) Paragraph 4 states that the UK is experiencing negative real interest rates. Explain what this means. [4]
- (e) Analyse the likely impact of negative real interest rates on the economy. [6]
- (f) Paragraph 5 states that an increase in UK interest rates may not have any significant impact on inflation. Explain why this might be true. [6]
- (g) Evaluate the view expressed in paragraph 7 that the government should increase public sector pay and the National Minimum Wage by more than the rate of inflation. [9]

Answer any **one** of Questions 2, 3 or 4.

- 2 (a) Explain what is meant by the term Gross Domestic Product (GDP). [16]
- (b) Explain any two methods by which GDP may be measured. [16]
- (c) Evaluate the view that any measure of economic welfare which is based entirely on GDP is fundamentally flawed. [16]
- 3 (a) Outline the main components of aggregate demand in an economy. [8]
- (b) Analyse the probable impact of the world financial crisis, known as the credit crunch, upon aggregate demand in the UK. [16]
- (c) Critically examine some of the policy options open to governments in dealing with the effects of this crisis. [16]
- 4 (a) Explain the main differences between the two measures of unemployment used in the UK. [8]
- (b) Explain the main causes of unemployment. [16]
- (c) Evaluate the view that in the long run only supply side policies can deliver lower unemployment without causing higher inflation. [16]