

AS Economics Unit 3 Managing The Economy 05 Jan MS

Q1a With reference to Figure 1:

(a)(i) Define ILO unemployment. Any 2 from the following (1 Mark each): 1. Survey/100000 people/60000 households 2. Available to work 3. Looking for work in past 4 weeks 4. More inclusive than claimant count.

(2) (a)(ii) Explain what happened to level of wages between March 2002 and March 2003.

Reference to figures (1), the level rose, but at a slower rate than in the previous year (1) 2 marks

(a)(iii) Using a carefully labelled aggregate demand and aggregate supply diagram, explain the significance of the changes in the exchange rate shown to the UK price level and equilibrium level of real output.

Reference to figures or the exchange rate has depreciated against the dollar (1). Written explanation of impact on price level and output (1) Explanation of transmission mechanism through e.g. more price competitive exports (2). Also reward Imports are more expensive + valid explanation of transmission mechanism e.g. Higher input costs (2). AD/ AS diagram showing rise in AD or shift in AS (must indicate on diagram old + new price level and output) (2 marks).

(b)With reference to Figure 2:

(6)

(b)(i) Explain the economic meaning of the term injection.

An increase in the level of money/or money into the economy (1).

Reference to I,G or X or flow of income (1). Reference to data e.g.

2002 G= £420 bn (1). (3) (b)(ii) Explain why such an injection may

lead to a more than proportional increase in the level of real output.

. Identify multiplier (1) . Initial impact on level of AD (1) . Rise in incomes of those affected (1) . These people in turn increase their consumption (1) . Extended repercussions (1) . Process dies out due to withdrawals (1) . Reward candidates with an appropriate reasoning e.g Investment in Human Capital shifts LRAS (up to 6).

Note: the development of a multiplier formula is not required but should be credited if presented.

(6)

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(c)

Refer to Figure 3. Examine the significance of the change in the oil price between 1998 and 2002 for the level of aggregate supply and hence for the equilibrium level of real output.

The graph shows a rise in oil prices (1). Impact of this on costs of production (1) causing the AS curve to shift to the left and output falling. Illustrated on diagram or through written explanation (2).

Evaluation in terms of extent, volatility, stocks, effect on AD (significance of oil, impact on UK as an oil producer) (2).

(6)

(d)

Discuss the issues which the Monetary Policy Committee might consider when seeking to achieve its inflation target.

Allow nine marks for analysis, reserving six marks for evaluation.

Explanation of inflation target + role of the MPC.

3 marks available . Identify target/2.0%/2.5% (1) . Target range +/- 1%

(1) . Use of interest rates (1) . Influencing AD (1) . Independence (1)

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Possible use of data presented: Inflation forecasts, current account impact, unemployment (drop), Economic growth rising, Government spending rising, wage growth (slowing down), exchange rate. Use of other knowledge: E.g.: House Prices, External shocks, Government Fiscal Policy etc. Any 2 points 3 marks each (1x identification) (2x explanation) or 3 points 2 marks each (1x identification) (1x explanation).

Evaluation marks could be gained from consideration of the following:

. Prioritizing the relative significance of the factors discussed. . The lagged effect of many influences on the inflation rate . Problems of switching to new measure of inflation . Uncertainty of forecasting .

Lack of data reliability Allow any two evaluative points up to 3 marks each or 3 x 2marks.

(15)

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Question 2

With reference to Figures 1, 2 and 3:

(a)(i) Define what is meant by RPIX.

Retail price index measures changes in the cost of living or inflation (1) excluding mortgage interest repayments or mortgage payments (1) Not mortgages.

(2)

(a)(ii) Explain what happened to the volume of retail sales between January 2002 and January 2003.

Grew less quickly (1) reference to data (1)

(2)

(a)(iii) Using a carefully labelled diagram, explain the likely significance of the data for Bank Lending in 2002 for the level of aggregate demand and the equilibrium level of output.

The data shows a rise in bank lending (1) likely influence on consumption (may accept investment) (1) diagram showing increase in AD (2) consequence for equilibrium level of output (1) other significant issues e.g: . Increase in price level or comment on: . Size of consumption . Time lag . Elasticity of AS . Multiplier (1).

(6)

(b)

With reference to Figure 2 assess two costs of the rise in the rate of inflation since mid 2002.

Maximum of (2) marks for each cost: identification (1) explanation (1).

Costs include: loss of international competitiveness; arbitrary redistribution of income; instability/uncertainty; menu costs; and shoe leather costs; Bank of England policy response. Reward any 1 piece of evaluation with (2) marks or (2 eval x 1 mark)

E.g.

Consequences for UK economy Size of change Inflation remains within target Relative significance of costs discussed Discussion of significance relative to other potential costs

Do not accept:

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Goods are more expensive and therefore demand is less Standard of living has fallen.

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(6)

25 (c)(i) With reference to Extract 1 define growth in real GDP (line 2).

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An increase/percentage change (1) Volume/value adjusted for inflation (1) Goods+ services/output (1)

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(3) (c)(ii) Explain the likely impact of two factors mentioned in the passage on the equilibrium level of output.

Award appropriate discussion of any two separate indicators.

Identification (1) explanation (2):

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Consumer confidence Change in tax Debt, especially mortgages Retail sales Falling Manufactured Output Possible stagflation (no repetition of definition in text) War with Iraq. Bank lending. Inflation is above target.

(6) (d) Evaluate the relative merits of fiscal policy and supply side policies in countering the risk of 'stagflation' (Extract 1, line 4).

Allow nine marks for analysis, reserving six marks for evaluation.

Definition of Fiscal Policy x1 Definition of Supply Side Policies x1

Further expansion of stagflation in terms of falling/low output and therefore unemployment x1. Do not reward repetition of definition in the text.

Identify a specific Supply side Policy x1 Explanation of Transmission Mechanism x1 Application to Stagflation x1

Identify a specific Fiscal Policy e.g. Cut Taxes x1 Explanation of transmission Mechanism e.g. rise in AD x1 Application to Stagflation e.g. Output will rise x1

Evaluation marks should be reserved for candidates who are able to critically examine the relative merits of such policies. (Candidates may evaluate either policy). . Raising AS may lead to a falling price level if AD is subdued. . Supply side policies may take some time to have their full impact. . Problems associated with Fiscal Policy e.g. Stop go cycles/Ease of change. . Cutting Income Tax + impact on both Fiscal Policy + Supply side policies . Time lags . Elasticities of AS curves . Relative merits of different Supply Side Policies. Allow any two evaluative points up to 3 marks each or 3 x 2marks

(15)

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