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Examiners' Report
June 2011

GCE Economics 6EC04 01

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Introduction

REPORT ON 6EC04 JUNE 2011

General Comments

This was the second 6EC04 paper from the new specification launched in September 2008. The structure of the paper requires candidates to answer one essay question, divided into two parts, from a choice of three (worth 50 marks) and one data response question, divided into five parts, from a choice of two (also worth 50 marks).

Most candidates completed the paper in the time available but there was evidence that some candidates did not spend enough time on the last part of the data response question.

The paper appeared to be accessible for most candidates and differentiated well. The mean mark and standard deviation was lower than last year. The main explanation for the lower mean mark is that the essays were more challenging than last year, especially the part b sections.

Once again it was pleasing to see some superb responses which demonstrated breadth and depth of knowledge and understanding combined with a rigorous analysis and evaluation of the issues. In these answers it was evident that candidates answered the questions in context and had read beyond the syllabus. Such scripts are not only a credit to the candidates themselves but also to their teachers whose inspiration and sound teaching must have played a crucial role.

Some candidates struggled to express their views precisely and accurately. This is significant for the essays and those parts of the data response questions with an asterisk. The quality of written communication is judged on the candidate's ability

- to present an argument and conclude on the basis of that argument
- to organise information clearly and coherently
- to use economics vocabulary appropriately
- to use grammar, spelling and punctuation appropriately

Section A: Essay Questions

The most popular question was number 3 followed by question 1, with question 2 being the least popular. Question 1 on the fiscal deficit provided an opportunity for those candidates who had studied the recent financial crisis to use their knowledge and understanding to good effect.

Similarly, question 2(a) enabled candidates to apply case study material appropriately to explain causes of absolute poverty while question 3(b) allowed students to make reference to the current problems facing several Eurozone countries.

In weaker responses there was frequently a failure to answer directly the question set; little knowledge about recent economic events; an inability to construct an argument and a lack of detailed analysis.

Section B: Data Response Questions

In Section B (data response) question 5 was more popular than question 4.

Question 4 provided an opportunity to use economic analysis in the context of Sub-Sahara Africa and there were many convincing answers. However, in parts (c), (d) and (e) there was sometimes confusion between FDI, trade and aid. The concept of economic development was not always clearly understood with respect to part 4(e).

Question 5 included questions about the WTO, exchange rates, trade imbalances and tariffs. Although the first two parts were answered quite well, the responses to parts (c) and (d) on trade imbalances were less convincing. Given the significance of these in the global economy, centres would be advised to cover this area of the syllabus carefully. It was performance on these questions which probably explains the slightly lower mean mark on question 5 as compared with question 4.

In weaker responses the data and information provided was frequently ignored or poorly understood; there was little analysis; and there was evidence of candidates not spending enough time answering the final part of the question.

Question 1

This question was the second most popular choice for candidates. The best answers to part (a) focused on the reasons for the increased size of fiscal deficits since 2008 and considered both the significance of automatic stabilisers and discretionary fiscal policy. There were various weaknesses in responses: some candidates ignored the requirement to relate their answers to a particular question; others confused a fiscal deficit with a current account deficit.

In part (b) the best responses assessed the implications of cutting public expenditure and of raising taxes. There was some very good analysis and evaluation of the Laffer curve. Weaker answers contained superficial analysis and/or only considered the effects of one of the two options. Some of these seemed to think that raising taxes would reduce aggregate demand but cutting public expenditure would not.

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Put a cross in the box indicating the question from Section A that you have chosen (☒).
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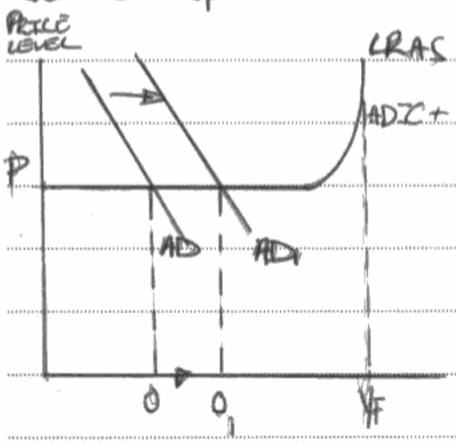
Chosen Question Number: **Question 1** ☒ **Question 2** ☐ **Question 3** ☐

a)

A fiscal deficit is when a government's expenditure is larger than its income through tax revenues ie. It spends more than it earns.

Since the financial crisis, many countries such as Greece and Portugal as well as the UK have found themselves with large budget deficits and this is due to a number of reasons. ~~and~~ The country I have chosen is the UK.

One of these is the reintroduction of expansionary fiscal policy, Keynesian economics in a bid to boost aggregate demand (AD) after the slump in 2008.



The diagram shows how, a boost in government spending (G↑), a component of AD should result in an increase in AD to AD, creating a new higher output of O. One example of this in the UK was the scrappage scheme introduced by the

government which gave subsidies on new cars in a bid to boost demand in the new car market. Policies such as these however mean that government spending increased massively despite, in the case of the scrappage scheme half the cost being met by the manufacturer.

Another way in which the UK attempted to boost demand which created a substantial rise in its fiscal deficit was to cut VAT temporarily to 15%.

The cut aimed to reduce prices of many goods and encourage consumers to purchase more, however, this ~~meant~~ 2.5% reduction meant that the governments tax revenues were severely reduced again increasing the fiscal deficit.

Reduced tax revenues and greater spending on welfare benefits were another reason for the rise in the UK's fiscal defecit since 2008.

As a result of the financial crisis and drop in demand many firms were forced to make massive redundancies. When Woodworths went into administration for example, many previous employees found themselves unemployed.

This then means, if they cannot find immediate employment that they would not be paying income tax. Their marginal propensity to consume would also fall as their disposable income falls meaning they pay less ~~direct tax~~ indirect tax like VAT.

Ultimately, they may find themselves on welfare benefits like Job Seekers Allowance and all of these mean that the government not only finds its tax revenues reduced but the welfare bill increased. This is something we have seen as unemployment reached levels not seen since the early 1990's and is a factor which may explain why ~~f~~ the UK's fiscal deficit has increased substantially.

Overall, I believe that the most important factor as to why the UK has seen in fiscal deficit rise since 2008 is the spending undertaken by the UK government in a bid to boost aggregate demand. Policies like the scrappage scheme and the cut in VAT proved to be very expensive for the government. However, the effects of these may well help reduce the deficit in the future.

b)

The large fiscal deficits suffered by many countries ~~after~~ since 2008 have meant many, notably in the Eurozone have had to introduce austerity measures, which aim to reduce fiscal deficits.

The UK government, for example, has opted to cut public expenditure as its main tool for reducing the deficit instead of raising taxes.

An argument in favour of this is that by reducing spending and the size of the public sector the private sector can take over in many ~~sectors~~ areas of the economy.
Were this to happen the size of the economy should not fall but instead increase as the private sector, driven by the profit motive can be more efficient and competetive.
An example of the private sector taking off from the public sector is in prisons, such as in Birmingham where, for the first time the private sector has entered the industry.
Reducing the size of government, theory suggests should also be more effective as a means of reducing the fiscal deficit because it reduces 'crowding out.' where

the government is an obstalle to investment. and so a growing private sector should, it is hoped, increase the levels of investment in Britain which have been low.

However, critisms of this include the fact that, as the private sector has been relatively small compared to some other developed nations like the USA there are doubts as to whether the private sector will be able to replace the public sector cutbacks so quickly.

The case for cutting public expenditure over tax raises could also be supported by the fact that, were taxes to rise then consumption, the largest component of AD, would fall creating a bigger drop in consumer demand than a reduction of government spending.

A rise in taxes would ~~ted~~ mean that those in work pay more toward the government meaning their disposable income falls. This would result in consumers spending less, weakening growth and possibly requiring greater government expenditure to boost demand as a result of cyclical unemployment for example. However, government expenditure is still a component of AD and large reductions in spending can still have the same effects should AD fall.

A case ~~for raising taxes~~ to cut the deficit that states that raising taxes instead of reducing expenditure is that those who are on low incomes or benefits are the most reliant upon government spending. This means that they could find themselves with less money as a result of government cutbacks. ~~Reduced~~ Limits on housing benefit are an example of this.

If these people, the number of whom have grown recently as unemployment and inflation rises, have their marginal propensity to consume reduced then again, this could reduce AD.

Falling AD would be a particular worry to the government at this time as growth is very weak with 0% rate over the last 2 quarters.

However again, should taxes rise then in the case of income tax the incentives to work are reduced raising the welfare bill and the rise in VAT to 20% may reduce consumption. The effects though are dependent

on the price elasticity of demand.
Ultimately, I believe that of the two taxes should be raised as a means of cutting the deficit. I think that the government should use public expenditure to boost AD, create employment which would then in turn reduce the fiscal deficit.

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Examiner Comments

(a) There is a good explanation of two aspects of discretionary fiscal policy followed by the impact of the financial crisis on government tax revenues and expenditure. There is some evaluation of these polices. Awarded 16/20 i.e. a Level 4 response.

(b) There is a consideration of a reduction in 'crowding out'; and also of the impact of higher taxes on those on low incomes and on incentives to work. The second point about higher taxes reducing consumption is less convincing because aggregate demand would also be reduced following a reduction in government expenditure. This answer was awarded 18/30 (Level 3 response)

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Examiner Tip

In part (a), knowledge of recent economic events marked out the best answers from the mediocre because these reponses usually considered both automatic stailisers and discretionary fiscal policy.

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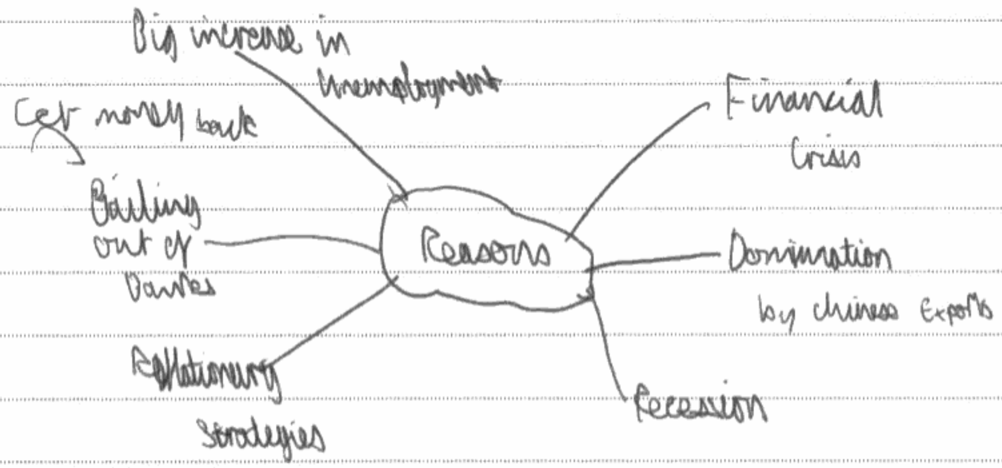
Chosen Question Number: **Question 1** ☒ **Question 2** ☐ **Question 3** ☐



Many countries ~~have~~ now have substantial fiscal Deficits which is the gap between Government spending and ~~tax~~ Revenue.

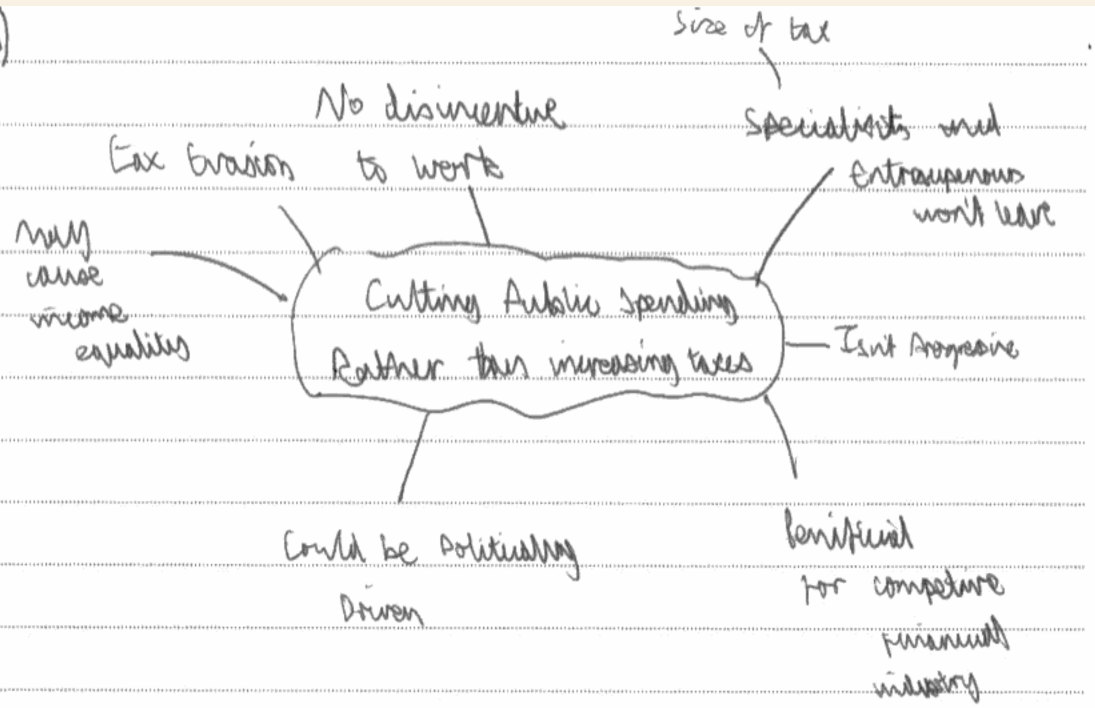
One of the reasons this has occured since 2008 is the Big increase in unemployment this has caused big automatic stabiliser adjustments. Due to the fall in number of people employed the Government has recieved much less tax revenue. In the same way unemployment has risen which has lead to a big increase in Gov. spending. This automatic stabiliser issue should help the economy grow again as it is a ~~cons~~ form of G which is a component of ag. AD. But over this short time period this is likely to effect ~~it has~~ caused very significant changes in the fiscal balance of the governments books and may be the biggest factor.

Another reason why there has been such an increase in fiscal deficits around the world has been caused by the reflationary strategies governments have been using. Many countries have cut taxes and boosted spending in order to prevent further recession. Especially in the UK where the government cut VAT in order to try and increase spending is a big fiscal loss in tax revenue. As the cut from 17.5% to 15% was fairly significant it may have had quite a large effect on fiscal deficit. These tax cuts may be good for the fiscal deficit in the long run however as they both cause growth and with extra consumption can help and stop deflation.

One big effect on the public finances especially in 08/09 was the banking collapse which lead to the governments having to take state ownership of banks. This meant the government, especially in the UK, ~~so~~ spent a lot of money ~~on~~ saving banks such as Lloyds and ~~Nat~~ Northern Rock. This move however may have saved ~~the~~ ~~&~~ an even bigger fiscal deficit had the banks been allowed to crash, if the government also invested alot of money in these banks when share prices where relatively cheap, therefore ~~this than~~ once confidence fully returns to the Banking sector, which it will, the Government will be able to ~~privatise~~ sell off the Banks and help the fiscal balance in the future.

The ~~borro~~ Increases of fiscal deficits around the World have been very large and are seen as unsustainable. Fortunately for the UK and other countries a like it seems likely these huge deficits may be short term and some of the things causing deficits now, may lead to surpluses in the future.

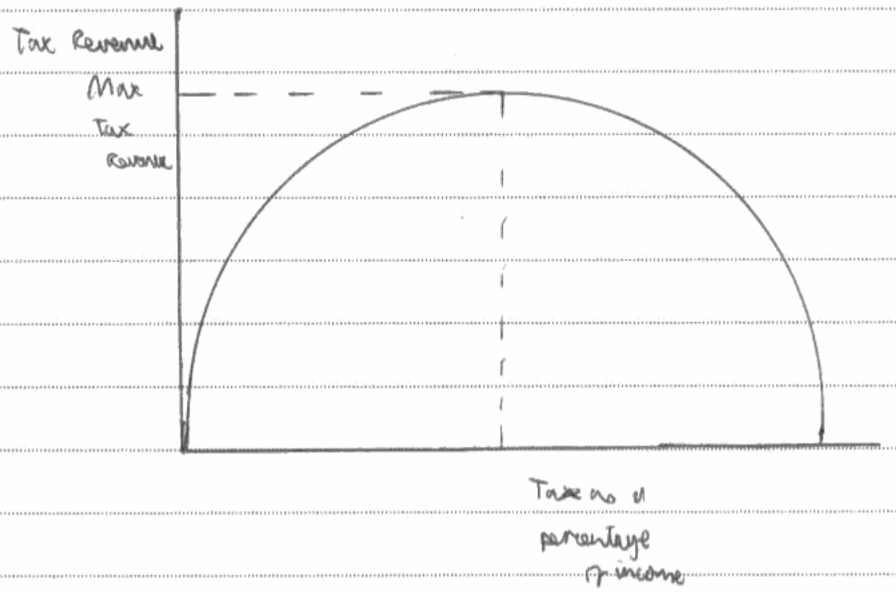
b)



In the UK at the current time aswell as around the World. The Government are trying to cut down their fiscal deficit by Reducing public spending which is how much the Government spends on things like, the NHS and Education by a greater extent than of which they are increasing taxes

By ~~incre~~ reducing public spending rather than taxes you are much less likely to push away high earners and specialists which are leading the Economy forward. By increasing taxes especially top level tax on high earners you are giving these people an incentive to move to another country were they can make more money. This is a big worry for Governments as they do not want a brain drain like of what they saw in Eastern Europe during the 1970's. However this reason depends both very much on the level of the tax and the incentive for people to move abroad. For example in the UK we have the strongest financial sector in the World or at least the biggest a small increase in tax is unlikely to push high earners away. Preventing big losses in tax revenue.

Another advantage of ~~cutting~~ not raising taxes is that it prevents ~~any~~ extra disincentive to work and by ~~increases~~ reducing spending on things like unemployment ~~and~~ benefits you are likely to increase incentive for people to get jobs. These two things are very important for increasing overall tax revenue. One big issue with increasing something like income tax is shown here by the Laffer curve.



This shows that to bigger increase in tax can actually cause a fall in tax revenue. The problem with the curve however is its difficult to tell whether we are anywhere near the maximum point. The issue with unemployment benefits is also this although it may ~~reduce~~ reduce the fiscal deficit by decreasing unemployment benefits initially. There aren't many jobs going at the moment and by reducing peoples income they may spend less and tax revenue could fall as a result.

~~[illegible]~~ One of the big disadvantages of this ~~[illegible]~~ tactic however is the large effect it has on the ~~the~~ poor. By reducing spending you are likely to hit the poor very hard through cuts on benefits, family allowance and many public services. This big reduction in living standards and income for the poor is likely to ~~do one~~ have a very negative effect on the fiscal deficit. As they spend much less and people lose their jobs and a negative multiplier puts the stability of the economy at risk again

What has become evident over the past year is just how damaging public spending cuts to the local government has been for other businesses. By cutting local council budgets naturally the government initially saves money, however not only intended ~~[illegible]~~ workers of the council have lost their job. With state sector being so big it has meant the cuts have very much damaged many businesses that rely on contracts from the local council, therefore even more people have lost their jobs, reducing ~~tax~~ tax revenues and increasing their spending. However looking to the future the size of the state sector in the UK is unsustainable and therefore by cutting it you are actually not just saving money initially but in the long term aswell.

Its clear what the government objective is at the moment and that is to cut the fiscal deficit while achieving export ~~led~~ led growth. Now to achieve the latter and gain tax revenue through it the government must allow our export businesses to become more ~~efficient~~ competitive by increasing taxes you are not going to achieve that. The UK must keep its top workers and corporation tax must not cause our products to be more expensive. If you let the private sector boom that may be the best way out of the fiscal deficit.

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Examiner Comments

(a) The answer identified and explained three factors which accounted for the rise in the UK's fiscal deficit, namely, expansionary fiscal policy; the imapct of rising unemployment on public finances and bank bailouts. Although brief evaluative comments were included, the most impressive one related to bank bailouts. Level 4: 16/20
(b) Several valid points were included i.e. disincentive effects of higher taxes; incentive effect of cutting unemoployment benefits; impact on inequality; and the impact of public spending cuts on local authorities. There is a little evaluation on the second and fourth points so this answer was just awarded a level 4 mark - 22/40

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Examiner Tip

Stronger and more detailed evaluative comments could have enabled the candidate to score a higher mark on both parts.

Question 2

Part (a) of this question was relatively straightforward and many candidates referred to case study material which they had studied. A weakness was that some responses made no reference to a specific country and an alarming number of answers referred to Africa as a country.

Part (b) proved to be quite challenging but the best responses discussed the meaning of development and then considered the extent to which a reduction in absolute poverty was necessary for economic development. The main weakness was the absence of a discussion of the meaning of economic development.

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Chosen Question Number: **Question 1** ☐ **Question 2** ☒ **Question 3** ☐

~~2a) Absolute poverty is a problem in~~

[PLAN] ~~DRC~~

- Corruption - Civil war
- Drought & bad weather - AIDS

2a) Absolute poverty is a problem throughout Sub-Saharan Africa, but particularly in the Democratic Republic of the Congo (DRC) where the issues of corrupt governments, civil war, drought and AIDS are severe. *

Most importantly of these factors is the corruption. The corrupt government means that any AID to help DRC will be diverted into the hands of those in power, so little progress will be made. The corruption of the government also means that should the IMF or World bank wish to offer ~~support~~ a system of investments in DRC, such as the microfinance investments seen in Bangladesh, it would be difficult as few banks and organisations are willing to lend to a country known for corruption. ~~and~~ ~~as~~ The cumulative effect of these factors means it is impossible to help the DRC out of their situation ~~and its~~

Civil war has torn the DRC apart for decades, particularly since the split from The Republic of The Congo. It has been deemed unsafe to travel there by the Foreign Office due to the constant volatility. Civil ~~w~~ war has a detrimental impact on countries, namely because ~~resources~~ there is an opportunity cost in diverting resources from improving infrastructure, education and healthcare to equipping itself with weaponry. Additionally, war comes with a human cost, ~~as~~ and as the body count rises, the workforce decreases, meaning the country becomes less and less productive, relative to other countries. On top of this factor, resources ~~&~~ such as primary product - which many subsaharan countries are dependent upon, are likely to get damaged in the warfare, limiting the ~~ext~~ extent to which trade can be executed.

Drought is also a limit to which primary products can be enabled, since the bad ~~who~~ weather results in a limit to the harvests. This is the least significant factor out of the four, as Western ~~Aid~~ aid programmes can help establish an irrigation system, although the effectiveness of aid is constantly debated as it may lead to aid-dependency, where a country is no longer self-sufficient because of the constant reliance ~~of~~ on overseas aid.

AIDS, the final ~~ex~~ factor, is a considerable factor on ~~po~~ absolute poverty in ~~the~~ Democratic Republic of the Congo. AIDS, again, results in a reduction of the workforce as they become too sick to work, thus reducing productivity. It also puts a strain on the already underdeveloped healthcare system, and a lack of ~~e~~ sexual education further increases the likelihood that AIDS will continue to spread. In the case of AIDS, Western aid is less possible because it is an incurable disease spread ~~throughto~~ throughout developing countries, so would significantly place burden upon ~~the~~ the Western ~~e~~ economies.

Overall, the Democratic Republic of the Congo is in a particularly volatile position and many ways of helping them out are littered with disadvantages and costs.

* Absolute poverty occurs when a country's level of poverty falls below the limit set. It is a subjective level, ~~pa~~ decided by factors such as % of people with access to clean water, % of people with basic levels of living standards, % of ~~,~~ literate people, life expectancy, child morbidity etc.

~~2b)~~

PLAN → define economic development

→ ~~explore~~ YES:

~~necessary for~~ helps trade, opp cost & comp adv.

less likely to need aid, ~~more~~

No:

→ "right wing analysis" ~~needed for~~ mess up mkt forces

→ would need to be proven to be continueable

→ not sustainable?

→ may import heavily

2b) Economic development refers to the progress in economies at meeting the needs of ~~their~~ people and how successful they are at attaining a substantial standard of living. ~~Reduce~~ Reducing the number of people in absolute poverty will only be sufficient at achieving economic development to a limited extent because it is difficult to prove whether such a level of development can be sustained by governments, as well as the external costs to the environment, and also there is the right-wing view of the cost to market forces.

If countries rely on aid to bring them out of absolute poverty, they may then become aid-dependent, meaning it becomes difficult for the level of economic development they have now achieved to be sustainable. They may end up borrowing beyond their means to finance the standard of living, especially if incentives and equipment is not ~~&~~ put in place to encourage entrepeneurial progress, which would lead to higher exports and aid the country into further developments. If this is not ~~put~~ implemented, as said before, the country may begin a system of borrowing and spending beyond their means, and if we look at the pattern into which ~~a~~ Greece has fallen (although it was never a developing country), the likelihood is that the overseas lenders are unlikely to see a their ~~return~~ loan ~~be~~ repaid, and so with the country in absolute poverty, ~~&~~ if they default on their loans they risk falling into a cycle of poverty once again.

~~&~~ Environmentally, reducing the number of people in absolute poverty may not be sustainable. With the development and industrialisation of Chindia (China + India), the impact is that there is increasing negative impact on the environment, as resources such as oil and animal stocks are depleted, which ~~is a~~ leads to a reduction in overall world development. With the Chindia development, the increasing demand ~~for~~ for resources has also led to questions being raised as to how ~~sufficient~~ sustainable this is, and whether the increasing demand from newly developed countries will lead to famine in developing countries, and as more countries develop, the likelihood of this being the case increases.

The right-wing analysis of this also disagrees with an entire reduction in absolute poverty as it will "adversely affect market forces." This argument suggests that countries in absolute poverty are likely to be primary product dependent ~~as~~ and once they develop, they will become less likely to export and more likely to import, and this will be detrimental to Western countries - for example Bolivia's supply of lithium is highly used in hybrid and electric cars, so it would be problematic. This analysis however is slightly misguided, however, as it suggests that entirely, as imports rise, exports fall when this has not been the case for China.

However, evaluatively, a reduction in ~~human~~ absolute poverty would lead to a reduction in the extent to which these countries would require aid. If they no longer need stocks of food, or medicinal and financial help, developed countries will benefit financially from not having to divert some of their GDP to foreign aid and thus could focus more on their domestic economy.

Additionally, a reduction in absolute poverty may lead to an increase in a country's production. ~~e~~ If the increased production is in a good where they have a comparative advantage, there is a likelihood that global trade will improve and all economies involved will see the benefit in GDP terms.

Conclusively, while the benefits of reducing absolute poverty are considerable, reducing it alone would be ~~definitely~~ definitively insufficient, so a system of regulations and requirements - such as requirements to reform, are required.

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Examiner Comments

(a) Four relevant causes of absolute poverty related to the Democratic Republic of the Congo are considered: corruption; civil war; drought and AIDs. However, there is only a little evaluation in relation to drought and AIDs. Level 4: 16/20

(b) This answer was poorly related to the question. However, some credit was given for comments on over-dependency on aid and impact on environmental sustainability. Just Level 2: 12/30.

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Examiner Tip

In part (b), it is important to explain the possible links between a reduction in absolute poverty and economic development and also why these links may not be very strong.

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Chosen Question Number: **Question 1** ☐ **Question 2** ☒ **Question 3** ☐

a) Absolute poverty is when a population of a country is experiencing poverty, with low standards of living and other poor ~~ssi~~ factors. Uganda is an African country that for a while has been struggling with the problem of absolute poverty, three of the main causes being, primary product dependancy, government ~~dept~~ debt and corruption within the government.

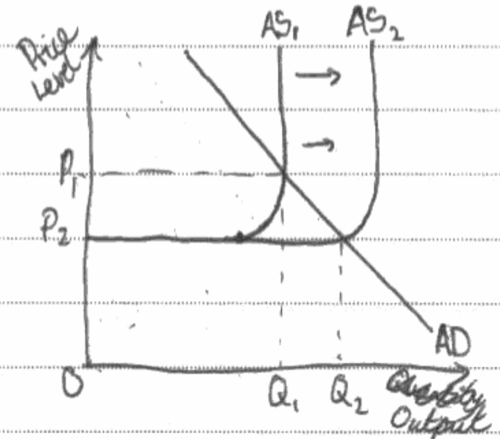
Primary product dependancy occurs when a countries economy relies solely on one product, in most cases a raw material, to provide income to a country. Uganda relies mainly on the production of coffee beans, as it is one of the highest net exporters of this product in the world. Relying on one product can lead to poverty because of the fluctuations in the price of the product, and the elasticity of demand for the product. Price fluctuations are usually uncontrolable as they are caused by the quality of harvest each year, a poor harvest can lead to higher prices, so a decrease in demand. Whereas a good harvest would lower prices, yet increase demand. Either situation could cause absolute poverty in a country, high prices mean less demand and less ~~income~~ imports whereas low prices and high demand can lead to other countries investing in the industry and exploiting the low costs. However, this all depends on the price elasticity of demand for the product. If the demand ~~products~~ for a product is price inelastic, then changes in price would not ~~not~~ lead to a change in demand and therefore absolute poverty. Unfortuately for Uganda, coffee is relatively price elastic so primary product dependancy has caused absolute poverty.

Another cause of absolute poverty is government debt. If over the years, a government has failed, debts can increase as the country needs to borrow more. This could be one of the ~~case~~ causes in Uganda, ~~as~~ because the government is poorly structured and inefficient. Public spending is no longer focused on improving the economy, but on repaying ~~to~~ debts. this can lead to poor public services including education and therefore absolute poverty. On the other hand, government debt may not always lead to poverty, as demonstrated in countries such as the UK and USA. If a government borrows money and invests it wisely, it would be in debt in the short run, but an increase in productivity caused by the investment would increase government revenue through taxes. This means in the long-run, government debt can help improve a country.

Also, corruption of the government can lead to poverty in a country. In Uganda, it is well known that the government is corrupt and ~~may~~ does not fuction efficiently. Corrupt government may set high taxes, so to improve their ~~tax~~ wealth, but in the long term they may seriously damage the rest of the population. The corrupt Ugandan government does not focus on the needs of the country, so provides poor education and poor or non-existant healthcare, forcing the country in to absolute poverty.

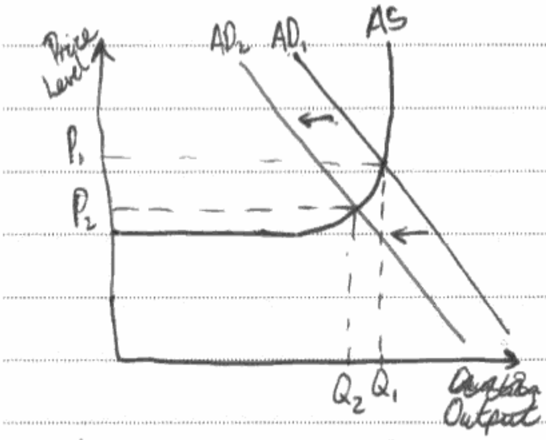
In conclusion, primary product dependancy, government debt and corruption are the main causes of absolute poverty in many countries, especially Uganda. Yet there are possible ways in which a country could prosper ~~under~~ ~~the~~ under each condition.

b) Reducing absolute poverty in a country works sufficiently to achieve economic development, especially in countries which are less developed as more progress can be made. In a less economically developed country, such as some of the african countries, a decrease in absolute poverty, through aid or other options, will majorly increase the productive potential of a country. Less poverty means a healthier, fitter and longer living population, so therefore an increase in employment. A larger workforce would shift the aggregate supply curve of a country to the right as shown below. Increasing the output ~~quantity~~ from Q_1 to Q_2. On the other hand, a healthier and larger population may lead to higher wages being demanded or a change in the availability of workers as they move from low skilled jobs into higher skilled jobs, so a possible shift to the left of the AS curve.



Another reason a reduction in absolute poverty would lead to economic development would be due to the improved infrastructure of a country. The government would no longer be focused on reducing poverty so could do infrastructure improvements such as better roads or communication. This would increase the productive capacity of the country so again would shift the AS curve to the right, as demonstrated above. However, ~~an~~ improved infrastructure could lead to increased imports, a leak from the the circular flow of income. This means the country could develop a current account deficit, leading it possibly back to poverty.

Reducing the people living in absolute poverty may not help achieve economic development. This is because people living in absolute poverty are very willing to work for small amounts of money. This attracts foreign direct investment so if wage costs increased, investments are likely to decrease. This would lead to a decrease in aggregate demand, and therefore a shift to the left on the AD diagram. This reduces the real output of the country from Q_1 to Q_2. On the other hand, the workers would become more skilled, as better education is offered in the country, which may attract investors to stay.



With less people in absolute poverty, banks would be more willing to offer loans, making finance more available to people in the country. This could be in the form of lower interest rates. Easier acess to finance, increases the AS of a country shifting the curve to the right, as demonstated earlier. However, more people would take out loans they may be unable to repay, which has considerable effects on the economy. For example, this is what caused the recent financial

crisis.
Overall, a reduction in absolute poverty is necessesary if a country wants to develop economically. The reduction can cause increases in both aggregate supply and demand, but this does not come without risks.

ResultsPlus
Examiner Comments

(a) Three causes of absolute poverty are identified and explained: primary product dependency; debt and corruption. There is good evaluation of the government debt issue. Level 4: 15/20

(b) The answer to this part focuses more on growth than to development but some valid points are made including reference to a larger, healthier workforce; improved infrastructure; increased FDI and greater willingness of banks to lend. Not all these are explained convincingly and the evaluation is rather limited. Level 3: 17/30

ResultsPlus
Examiner Tip

The introduction to part (b) should include a discussion of the meaning of economic development.

Question 3

In part (a) there was good analysis of trade creation and trade diversion in many answers. However, there was often inadequate discussion of the impact of the growth of trading blocs on the global economy. Also this question caused problems for some candidates who interpreted trading blocs as meaning methods of protectionism.

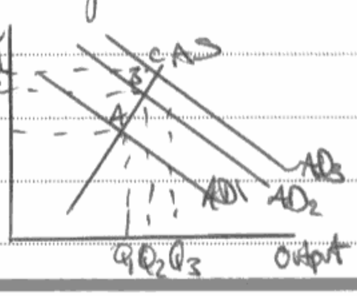
Part (b) was generally answered quite well although some focused on less impressive points such as transiition costs. Better responses considered the current crisis in the Eurozone as an argument against membership of a monetary union.

Do not use pencil. Use black ink or ball-point pen.
Put a cross in the box indicating the question from Section A that you have chosen (☒).
If you change your mind, put a line through the box (☒) and then indicate your new question with a cross (☒).

Chosen Question Number: **Question 1** ☐ **Question 2** ☐ **Question 3** ☒

3a) Trading blocs are agreements between countries to create a regional pact, to promote trade between member countries. The global economy is the trading of countries ~~to~~ across the world and to an extent this is compromised by trading blocs.

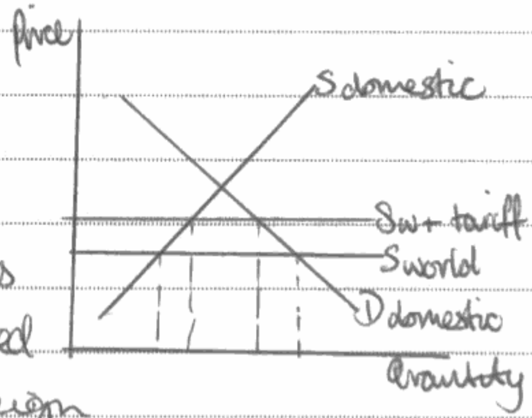
Firstly, the growth of trading blocs has increased trade and interdependancy. Interdependancy is where economies rely on each other ~~to~~ to be successful. Trading blocs give member states free movement of goods and capital, which give firms a wider market, and therefore a higher turnover and this relates to prosperity and higher GDP. This creates positive ~~~~ multiplier effects which can further increase AD to the right. This is possible due to firms having incentives to trade within blocs.



To an extent, this can

seen as global trading and trading blocs do provide members with great business benefits. However firms may not wish to supply wider than the trading bloc circle, as it has extra penalties. Across boarders in the EU or ASEAN there are no quotas or tariffs, so domestic firms may refrain going even more global, however this all depends on ~~that~~ wether the bloc is big enough initially.

Secondly, trading from outside the bloc can incur severe charges for suppliers as trading blocs agree to penalise foreign suppliers, which promotes internal growth, as foreign cheap goods get tariffed to a higher price. This is a type of protectionism as domestic firms are protected to an extent from foreign



penetration. Another form of protectionism is quotas to limit number of foreign ants entering the economy. The aim is to detract foreign firms away and to promote growth within the bloc, so this argues that the global economy is worse

off as more efficient foreign firms are restricted from trading globally as some ~~ac~~ countries enforce trading blocs to counter their trade. Trading blocs therefore segment the globe into almost teams that have to overcome obstacles to be able to enjoy global trading. This breaks down globalisation as trade links get put under strain and can create retaliation protectionism.

However this all depends on how accessible trading blocs are, ~~for~~ for example it is simple to enter the EU as a firm, they just need to merge or acquire an EU firm to then avoid the outsider penalties for trade. Also the WTO will regulate the countries and not stand for any gross unfairness in trading restrictions as it aims for a global free market.

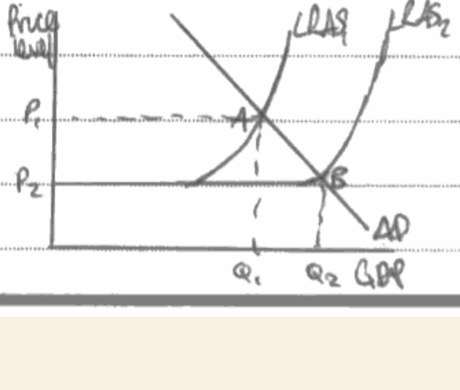
Thirdly global trading is hampered severely due to trading bloc retaliation and hostility, as ~~for~~ for example UK trade 60% with the EU, likewise the US trade alot with ~~[illegible]~~ Canada and Mexico, so firms become disincentived to become firms become disincentivised to become global due to a lack of free trade and trading partnerships are broke as

even domestic inefficient suppliers become cheaper for goods and services.

Concluding I feel regionally economies will benefit from trading ~~[illegible]~~ blocs however globally everyone would benefit to no blocs at all. then firms get a global customerbase for free, it takes just one bloc to disrupt this as others will create their own groups too.

3b) The European Union has a central bank ECB which set monetary policies for all members as a whole.

Firstly, the UK would benefit from no transaction costs between exchanging pounds to euros. This would mean the UK firms would spend less in transaction fees and shift LRAS to the right, as 60% of trade is with the EU, so to adopt the euro would make trade with other EU countries more attractive.



Lower costs in buying raw goods from the EU means firms can profit maximise

at a higher output and lower price.
However this depends on the cost to firms in the ~~[illegible]~~ short ~~[illegible]~~ run to change currency and ~~[illegible]~~ whether the benefits gained from a single currency are counteracted by negatives from the exchange rate to other trading partners like the US and China.

Secondly, the UK firms and EU firms would gain from transparancy and predictability between transactions. Currently the pound is floating in exchange rates, as is the euro, so the exchange ~~[illegible]~~ rate can fluctuate these fluctuations can slow down trade, as prices for imports/exports consistently change. Firms prefer stability as then returns on money are more accurately ~~[illegible]~~ calculatable. EU firms are more likely to invest in the UK and vice versa as investments won't fluctuate in value as there is no exchange rate to bother with if the UK adopted euro.

However the benefit lies in how volatile the exchange rates were originally normally ~~[illegible]~~ £/€ was very stable pre-recession, so trade wasn't hindered too significantly to say the benefit vastly outweighs the negatives. However during the recession £/€ has changed alot but in the LR the exchange rate is fairly stable.

Thirdly, it is arguable it would cost the UK economy alot in the LR. To join the euro we would need to surrender our independant monetary policy rights. The ability to set interest rates would be taken over by the ECB under a one size fits all rule. This would cost the UK heavily as it means we cannot target inflation at a rate of 2% ± 1% but at a stricter 2% by the ECB but the main problem arises when the UK economy is either too strong or weak and the ECB set contrasting rates. For example during the recession, we set our rates at 0.5%, the ECB at 0.75%. This allowed the UK to come out of recession, not in position like Greece currently. Greece suffered badly as they required interests lower than 0.75% to induce spending in their declining economy, but couldn't as the ECB set the rates and Germany are in a relatively strong economic boom from export led growth. The German economy would overheat from really low rates, but because of this Greece, Portugal, Ireland, and Spain are all in trouble.

Therefore this proves the cost of having the euro can outweigh the benefits, if the UK economies cycle didn't converge with Germany's.

This depends on the economic cycles of economies, which are aligned before countries join the euro to prevent these sort of problems, however as shown by the 2008 recession convergence can end up diverging during extreme downturn.

Fourthly in the short run the cost to join the euro is high. For two years the countres exchange rate needs to be ~~[illegible]~~ maintained stable. This can cost the government huge amounts when the currency depreciates and the currency needs revaluing, the ~~[illegible]~~ country may have to use up all their federal reserves to keep the ER stable. This is proven by Black Wednesday in 1992 when the UK ceased joining the euro as the cost to keep the currency in a

stable rate cost too much due to speculative
attacks and loss in confidence of the
pound as the bottom bracket was an
overvalue of the currency
However it depends on the current level
of reserves if we can afford to join and
the SR costs is less than the LR gains.
Although during our buget deficit I would
say it would be a bad choice
joining.
Concluding the costs are too much when
valuing the requirement of independant
interest rates and the cost to join
the EU. The benefits gained show no
huge gain as we trade 60% with the
EU without problems already.

ResultsPlus

Examiner Comments

(a) Although there is an attempt to relate the points to the impact of trading blocs on the global economy, they are not developed or explained in much depth. There is, however, a good evaluative comment on the accessibility of trading blocs to transantional companies. This answer was therefore deemed to be worth a top Level 3 mark of 14/20

(b) Several relevant points are made and most are evaluated e.g. absence of transaction costs; price transparency and predictability; loss of independent monetary policy (explained well) and a thin point on transition costs. This answer was therefore considered to be a Level 4 response: 24/30

ResultsPlus

Examiner Tip

In part (a), high marks were only awarded to those who examined the impact of trading blocs on the global economy since this was specifically demanded by the question.

(b) Knowledge of recent events affecting eurozone countries would provide a useful backdrop to an examination of the benefits and costs of membership on a monetary union.

Do not use pencil. Use black ink or ball-point pen.
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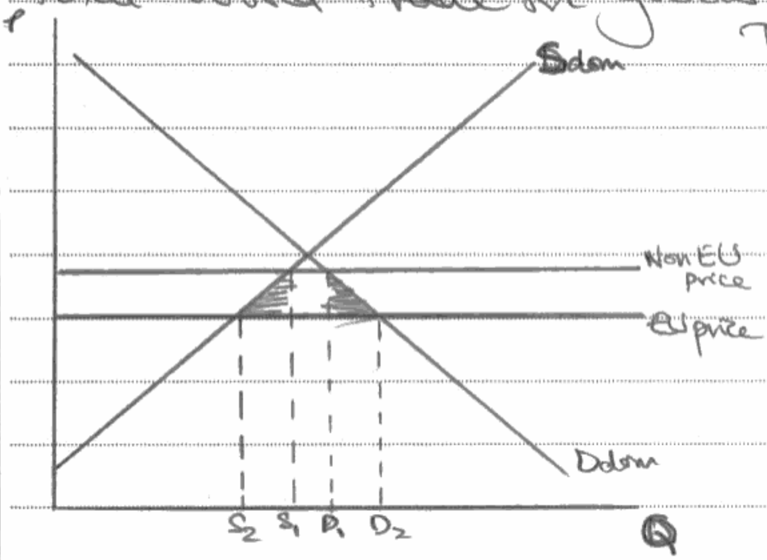
If you change your mind, put a line through the box (☒) and then indicate your new question with a cross (☒).

Chosen Question Number: **Question 1** ☐ **Question 2** ☐ **Question 3** ☒

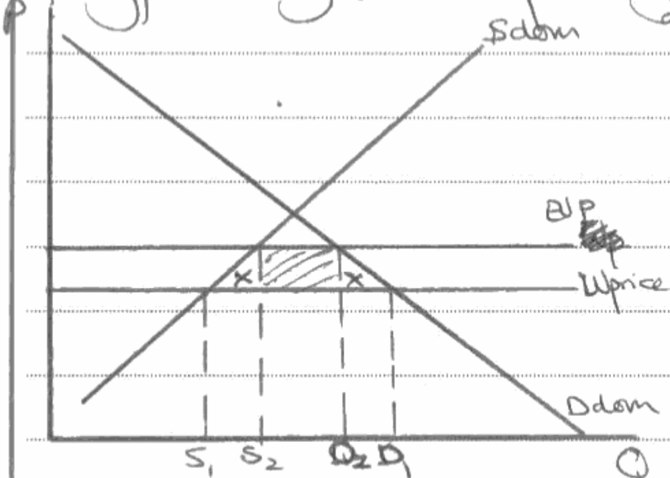
a) A trading block is a regional group of countries that practices the same preferential trading restrictions with the rest of the world. Examples of trading blocs include NAFTA and the EU.

One impact that the growth in trading blocs would have on the global economy is a further reduction in trade barriers in goods & services. There would be a growth in trade between the countries in the trading bloc. This is shown in the case of the EU27, which now accounts for 17% and 28% of the total world trade in goods and services.



This results in trade creation, as domestic consumers switch spending from a higher cost domestic source to a lower cost member source - represented by EU price. This leads to an outward shift in demand and a rise in consumer surplus. The welfare gains are represented by the shaded area. Thus, ~~an increase~~ the growth of trading blocs creates trade and improves welfare ~~as~~

However, this is not always the case as it must be considered how much trade is diverted. Trading blocs that are customs unions, like the EU, have a common external tariff taxing imports from outside the EU.



The diagram shows trade diversion as consumers switch spending from a lower ~~price~~ cost world source to a higher cost member source. Trading blocs only bring benefits if more trade is created than diverted. This also has negative effects on farmers in developing countries, as ~~their exp~~ the value of their exports decline as demand goes down. The WTO have been criticised heavily for this, and many argue that they favour developed countries over developing countries.

~~A~~ further growth in trading blocs may lead to worsening welfare in developing countries, unless developing countries create a trading bloc between themselves.

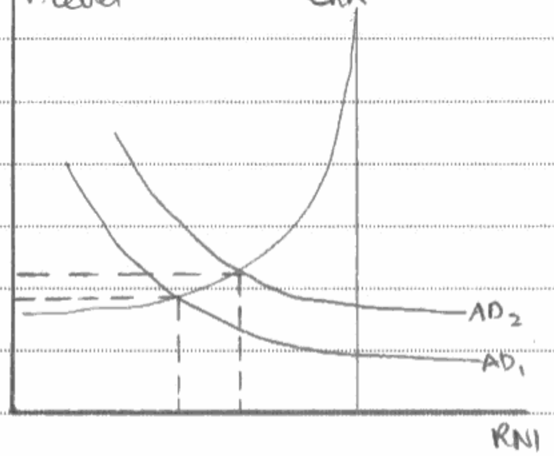
A growth in trading ~~&~~ blocs may lead to a rise in productivity. The abolishment of tariffs between member countries in the EU means that producers ~~based~~ in the EU27 now have access to a larger market as EU countries account for 7% of the worlds population. This will lead to economies of scale being able to be exploited, which in turn increases productive efficiency. ~~Large~~ Increased competition between firms may also increase productivity, as firms must find ways to be economically efficient in order to look competitive. Overall, this ~~red~~ increase in productivity means lower prices for consumers and thus, consumer welfare will increase. There is also a rise in allocative efficiency and reduction in X-inefficiency.

However, the recent recession has caused many problems within the Eurozone countries in the EU, notably Greece, Ireland and Portugal. The increased interdependence of the EU27 means that all EU countries have been impacted by this crisis and so a growth in trading blocs could be even more damaging, as it increases countries' vulnerability to external shocks.

However, a growth in trading blocs would not be the sole reason for ~~quicksp~~ quickspreading of external shocks. Even without trading blocs, the international economy is becoming more highly integrated. The recent recession is proof that every country is vulnerable to external shocks.

Overall, the most significant effect of an increase in trading blocs would be the problems of trade diversion on developing countries. It can be seen that developing countries are highly dependent on developed countries still. Therefore ~~an increa~~ a growth of trading blocs would further push them away and prevent their development

b) A monetary union is a group of two or more countries ~~practising~~ sharing a single currency. The benefits of this are that transaction costs involved in trading will decrease. A fall in the costs of trading therefore means that trade is likely to



increase, and lower prices are likely to be passed onto the consumer. Therefore members of the monetary union will see an increase in exports. Exports are an injection into the circular flow, and a multiplier effect is likely to occur as increased exports leads to increased ~~em~~ employment which may lead to increased consumption. Thus, AD will shift outwards to AD_2. Although imports are a withdrawal from the circular flow, they may lead to lower costs for ~~consum~~ businesses who are importing raw materials and thus could mean larger profits, which could be spent on further investment contributing to an increase in AD.

Membership ~~of~~ of a monetary union may also increase consumer and business confidence. Price transparency occurs as it is easier for consumers to make comparisons in prices. Their confidence will increase and thus, in theory should lead to an increase in consumption. There is reduced uncertainty within the monetary union about exchange rate and price fluctuations also. This is one ~~way~~ place in which the Euro has been successful as there has been stable prices and not too many fluctuations in exchange rate. This leads to higher business confidence, which should in theory lead to higher investment. The increase in investment and consumption will shift AD to AD_2, achieving economic growth and reducing spare capacity.

If the UK adopted the Euro, it would most likely experience these benefits. However there are also many costs. A single currency and the ECB being in control of setting interest rates means a loss of monetary policy power. For a ~~...~~ single currency to work so that 'one size fits all' the changes in interest rates must have similar effects on the membership countries. The UK, however, has 70% homeownership compared to Germany which is only 30%. Interest rate changes therefore would have a much larger impact on the UK, as homeowners ~~...~~ are most likely to have mortgages. The size of the housing market is also a lot larger in countries such as ~~...~~ Greece and Spain. The recent €110 billion bailout of the Greek economy simply ~~[illegible]~~ proves therefore that one size does not fit all. There are 17 countries in the EMU, which is far too many for it to be an optimal currency area. The euro works well for some countries (France and Germany) and doesn't work for others : the PIIGS (Portugal, Italy, Ireland, Greece and Spain) The struggle of these countries ~~during~~ due to the recession highlights that the Eurozone is not an optimal currency area and one size does not fit all.

Another cost is that there would be a loss of sovereignty on becoming a member. Though this is a more 'emotional' aspect of debating the costs and benefits of a monetary union, it is highly important to the inhabitants of a country. The UK for example is heavily interested in its history and traditions. There is already social unrest in many places due to the rise in immigration caused by being in the single market. This will only get worse if the UK adopted the ~~[illegible]~~ euro. There are many countries similar to the UK who are precious of their national identity also

However you could argue that due to globalisation, national identity is being lost anyway.

Overall, the benefits do not outweigh the costs. The recent eurozone crisis highlights this. Three countries have had to be bailed out of bankruptcy, further delaying any hope of recovery from the 2009 recession. Many countries such as Greece did not meet the convergence criteria in the first place. The UK would also not meet the EMU convergence criteria and therefore we should stay away from the Euro.

The benefits of a monetary union are far more focused on the microeconomic side, and the costs are more involved with macroeconomics. It could be argued that during the recession, macroeconomics is more important in ~~sustain all~~ getting countries through a recession. However in many ways the opposite could also be argued. ~~It is also pos~~ Overall, it is fair to say that the eurozone has failed, and though it is likely that ~~these~~ there would be costs for any monetary union, another group of countries may be more

successful in maintaining a healthy
monetary union.

ResultsPlus

Examiner Comments

(a) This is a very good answer which considers the issues of trade creation and trade diversion as well as implications for producers both within and outside the trading blocs. 19/20

(b) Again, a well structured answer which identifies and explains several relevant issues: reduction in transaction costs; price transparency; increased business confidence; loss of independent monetary policy and individual exchange rate together with evaluation and conclusions. Just level 5: 27/30

ResultsPlus

Examiner Tip

This is a good example of an answer in which economic concepts are applied accurately and knowledge about current economic issues enhances the quality of the essay.

Question 4 (a)

Although there was a clear reference in the extract about the significance of rising populations, many answers did not make the point that if the population is rising faster than GDP, then GDP per capita would fall. There was also an absence of examples in many responses.

(a) With reference to lines 18–19 of Extract 1, explain why many development economists consider that a growth rate of 6% is the minimum desirable in most African economies.

(5)

A growth rate of below 6% ~~f~~ will not be ~~th~~ able to support the huge increase of population of some areas. In the ivory coast the city of Lagos in the 3rd most rapidly growing city on earth. The ~~producti~~ growth of the economy though is only 4.5% and ~~so~~ this will ~~be able to~~ not be able to sustain the liveing standards of this country.

ResultsPlus

Examiner Comments

In this answer there is a reference to the huge increase in population and then an example is included of where economic growth is less than the rise in population. Unfortunately, there is no consideration of the impact on GDP per capita.

ResultsPlus

Examiner Tip

Include reference to the relationship between population growth and the rate of economic growth.

(a) With reference to lines 18–19 of Extract 1, explain why many development economists consider that a growth rate of 6% is the minimum desirable in most African economies.

(5)

African economies need a minimal growth rate of 6% because they have ~~huge populations~~ 'rapidly increasing populations'. Therefore, without sufficient growth to cater for this population increase, there will be huge amounts of unemployment and further problems of absolute poverty. If Growth is not as high as 6%, ~~ineo~~ GDP per capita will fall because ~~there~~ population is growing too fast, the absolute poverty will cause spread of disease because ~~there~~ they will have no shelter, sufficient diets, access to clean water or sanitation. This will act as a detterent for investors.

ResultsPlus

Examiner Comments

Answer includes reference to rapidly rising populations and the possibility of a reduction GDP per capita. However, there is no specific data reference to a country.

ResultsPlus

Examiner Tip

In questions which make reference to the information provided, it is important to include relevant data references.

Question 4 (b)

Many answers made good use of the material provided to explain why Growth rates in Sub-Saharan Africa were higher than those in Advanced Economies. Weaker answers went litlle further than identifying key factors from the extract and/or made no specific data references.

(b) With reference to Figure 1 and Extract 1, analyse why the growth rate of the Sub-Saharan African economies was higher than that of Advanced Economies between 2000 and 2010.

(8)

Sub-Saharan Africa attracted huge amounts of investment between 2000 and 2010 from countries such as the BRIC countries because they have valuable raw materials such as 'oil and gold'. Countries ~~such as Angola~~ were able to achieve economic growth because of ~~a combination of~~ FDI, ~~and exportation~~ ~~from~~ particularly from China who offered $10 billion dollars of cheap loans (microfinance) that would allow small businesses to ~~grant~~ growth leading to an increase in the overall growth rate. China also paid off debts of African countries which allows them to spend ~~this~~ the money they saved through debt cancellation ~~of~~ on other things, such as improving human capital and infrastructure, leading to further growth. This was particularly evident between 2001-02 because the GDP % changed by nearly 8% from the previous year.

There export of oil and gold also led to increases in economic growth. For example, between 2006 and 2007, Angola's oil export caused an increase in its GDP ~~by~~ to 20%.

However, ~~in the long-run this could~~ this was not the same for all African countries. The republic of Congo and Sudan had civil war which dettered investment and caused an inward shift in LRAS.

ResultsPlus

Examiner Comments

This answer identified several relevant factors including FDI, possession of raw materials, cheap loans and included appropriate data references. However, there was very little explanation of the points made. 5/8

ResultsPlus

Examiner Tip

The command word in the question is 'analyse' so it is important to develop the points raised to show their significance in explaining why the growth rate of Sub-Saharan countries was higher than that of Advanced Economies.

(b) With reference to Figure 1 and Extract 1, analyse why the growth rate of the Sub-Saharan African economies was higher than that of Advanced Economies between 2000 and 2010.

(8)

a reason why the growth rate of sub-saharan africa has been higher than that of advanced economies is the fact that many countries such as angola (oil), rely on raw materials and since these have seen a rise in demand due to the rise of the BRIC nations, growth figures for exporters of raw materials have been high. At least, in comparison with the "services industry" which are the backbone of many advanced economies.

Also, growth figures have remained above those of advanced economies during the global recession. This is due to the fact that africa's banks and stock exchange were isolated enough from the wider capital markets to escape the after shocks of the credit crunch

ResultsPlus
Examiner Comments

This answer identified two key factors: reliance on raw materials and the isolation of Africa's banks. The first point was analysed well, gaining but there was no further explanation of the second point. The data reference to Angolan oil was sufficient to gain 2 application marks. Mark 6/8

ResultsPlus
Examiner Tip

It is important to explain the significance of the points made in answering the question.

Question 4 (c)

The best answers considered a variety of benefits associated with FDI e.g. increased growth; increased employment; higher tax revenues; positive effects on the Balance of Payments and the outlined some disadvantages. However, weaker answers confused FDI with aid and debt relief.

(c) With reference to Figure 2 and Extract 2, assess the benefits of foreign direct investment in primary sector industries of countries in Sub-Saharan Africa.

(10)

FDI brings investment to Africa, this means that ~~it~~ Angola is supplying China with ~~because China is spending~~ 1.3 million barrels of oil a day China spends money on Angola to improve its infrastructure ~~and increase living standards~~ by increasing Angola's employment, thus inceasing living standards.

However, because Angola citizens doesn't have the skills to build infrastructure to jobs go the Chinese people, so unemployment stays high and living standards don't increase.

So investment stays high but develop stays lou

India has given out overall loans to Malawi of $50m for development projects. This will increase HDI as education, life expenctancy and GDP per capita increases.

However, Aid agencies consider BRICS "rogue doners" as countries like Malawi are only accumulating more dept for India. Thus, the development of Malwi will not increase as currupt government keeps the money for themselves.

ResultsPlus

Examiner Comments

Benefits of FDI are identified with brief explanation (1 + 1 marks) in the first paragarph with the inclusion of appropriate examples (2 marks). The second paragraph includes a relevant evaluative comment (2 marks). The last two paragraphs are not relevant because there is discussion about aid rather than FDI. Total: 6/10

ResultsPlus

Examiner Tip

It is important to stick to the context of the question which, in this case, is clearly about the benefits of FDI.

(c) With reference to Figure 2 and Extract 2, assess the benefits of foreign direct investment in primary sector industries of countries in Sub-Saharan Africa.

(10)

One benefit of FDI in primary sector industries in sub-Saharan Africa is that infrastructure in the countries can be improved. FDI can be invested in infrastructure, improving infrastructure that is essential for businesses to operate such as roads and telephone lines. These are particularly needed for primary sector industries as primary products need to be transported to their markets and so investment is enabling this to happen. Investment can result in the multiplier effect as more firms are likely to locate to a place where infrastructure has been improved, resulting in the multiplier effect and an increase in employment in the primary sector. This is very beneficial to sub-Saharan African countries as they have abundant supplies of raw materials, shown in Figure 2 such as oil in Brazil.

Another benefit of FDI in primary sector industries is that trade can be increased. Investment may result in more efficient production techniques as more capital equipment can be bought or new production ideas are introduced, making the goods more competitive as they can be offered at a lower price. This can increase trade leading to an increase in economic growth, particularly if improvements in productivity are made.

In evaluation, Extract 2 states that a lot of FDI is conditional e.g. equipment will be 'built or sold by Chinese companies'. This reduces the benefits of FDI as there is a cost associated with receiving the FDI.

Also, in evaluation FDI in the primary sector leaves sub-Saharan Africa 'more dependent on volatile commodities than before'. Commodities and reliance on primary products is associated with many problems such as worsening terms of trade, stated by the Prebisch-Singer hypothesis ~~which~~ which says that terms of trade for primary producers worsen as YED for manufactured products is greater and so ~~the~~ producers of primary products receive decreasing returns over time. Therefore, the benefit may be outweighed by the disadvantage as this is a very significant effect which accounts for many problems in LEDCs such as sub-Saharan Africa.

ResultsPlus

Examiner Comments

In the first paragraph there is 1 mark for identification of improved infrastructure and 2 for the subsequent analysis. 2 marks are also awarded for the example in the last sentence.

In the second paragraph, there is a mark for analysis. The last paragraph was awarded 3 evaluation marks. Total 9/10

ResultsPlus

Examiner Tip

This answer shows the importance of using the information provided to gain high marks.

Question 4 (d)

Some responses failed to focus on the benefits and problems associated with increased trade in primary products with BRIC countries. Of those which did address the question directly, many did not apply concepts such as the law of comparative advantage or include examples of countries or products to illustrate the points made.

*(d) With reference to Extract 2, evaluate the benefits to African countries of increased trade with the BRIC economies.

(12)

A benefit of increased trade to African countries with BRIC economies is that it provides them access to ~~increased~~ rapidly increasing economies whose demand is growing ~~continuously~~ ~~expont~~ exponentially as they become richer and richer resulting in increased trade and investment for the future. As a result, african companies will be able to grow at the same rate as these economies demand growing than economies of scale.

However, increased trade may not ~~mean~~ result in increased trade in the future as African countries are only trading with BRIC countries in primary products such as raw materials ~~eg~~ like copper and iron which is unsustainable as when the resources are gone african countries will not have anything left to sell and hence trade.

Furthermore, another benefit is that it would help to decrease both absolute and relative poverty within the African countries. This is because, as employment increases from greater trade, more and more people will be able to achieve a greater standard of living by affording basic neccessities and well as the government redistributing tax revenues to ~~poorer~~ the poorest in society.

This may not be the case as the income ~~as~~ created may not be redistributed properly.

ResultsPlus
Examiner Comments

The main problem with this answer is weak analysis. Two benefits are identified: increased growth and reduction in absolute poverty (2) with some analysis of the second point (1). Two examples of products are provided (2) and there is some evaluation in the second paragraph (2). Total: 7/12.

ResultsPlus
Examiner Tip

When discussing the benefits of trade, specialisation based on the law of comparative advantage would be a useful line of analysis and evaluation.

*(d) With reference to Extract 2, evaluate the benefits to African countries of increased trade with the BRIC economies.

(12)

Increased trade with the BRIC economies means that African cantries benefit from the sale of more of their exports and are able to increase the amaunt and number of their goods as demand for them increases. This means that consumers will benefit from a wider range of choice and cauntries which don't curently imports from sub Saharan Africa may decide to if they start producing different desirable products due to their increased trade with the BRIC economies.
Secondly, African cauntries may be able to benefit from economies of scale due to increased trade which they may not have been able to do beforehand. Economies of scale occur when long run average costs decrease as output increases.
However, trade with the BRIC economies may not be all beneficial for Africa. Extract 2 says that the BRIC cauntries import raw materials from poor cauntries, resulting in them diversifying their export markets but

not their industry. This would therefore lead to primary product dependency at a higher rate than before.

ResultsPlus

Examiner Comments

Two benefits are identified but not explained well (2). There is some evaluation at the end of the answer which picks the issue of primary product dependency mentioned in the extract. (2). Total 4/12

ResultsPlus

Examiner Tip

Points made should be supported by relevant analysis. For example, the first point could be developed by noting that exports are a component of aggregate demand and an injection and therefore, an increase in exports would cause a more than proportionate rise in GDP.

Question 4 (e)

There was some very good application and analysis in answers to this question both in relation to the potential benefits of aid and to problems associated with aid. However, weaknesses included an inability to relate aid to development and to a confusion between aid and FDI.

*(e) With reference to Extract 2, to what extent might aid from the 'BRIC' economies promote development in Sub-Saharan Africa?

(15)

Aid can promote development in Africa as it allows countries funds from which they can invest into reducing poverty levels of and raising living standards of the poorest in society.

However, this aid maybe tied as that given from China to African meaning that it has conditions attached to it such that governments cannot afford to redistribute aid as they have to pay debt interest payments.

Furthermore, aid can help to invest in human capital such as greater education or health facilities which can help a country to develop a more skilled and healthier nation which can be more productive.

In addition, aid can also ~~th~~ help to build infrastructure in an economy by building more roads and hospitals and schools.

ResultsPlus

Examiner Comments

Two points area identified: reduction in absolute poverty and investment in human capital (2). The latter point is developed so gaining 2 analysis marks. The second paragraph makes reference to China (1) and includes a thin evaluative comment relating to conditions attached to aid. (1). Total 6/15

ResultsPlus

Examiner Tip

This is a brief answer suggesting that the time spent answering it was insufficient. Given that the question is worth 15 marks it is important to plan time carefully.

*(e) With reference to Extract 2, to what extent might aid from the 'BRIC' economies promote development in Sub-Saharan Africa?

(15)

Aid is where is a transfer of resources from one country to another.

One way in which Aid can provide development is because it reduces absolute poverty. If the aid is pumped into the economy, then the government can use this money to help the poorer families access clean water and food. this will encourage these families to increase their living standards.

However, there is sometimes a dependency culture when related to aid. Many people from Africa may feel that they are being given enough money to access water, shelter and food, and therefore they do not feel that they need to do anything because they have what they need.

Another ~~benefit~~ way it can provide growth, is through improving human capital. In improving education and schooling, more children will be able to go to school, and therefore have a good education. this will mean that as they begin to grow up and leave school, they will have more skills and therefore gain a job. This will not only improve the skill for the workforce of these African economies, but ~~these~~ they will also be able to provide an income for their family, thus reducing poverty, and therefore increasing development within the country.

However, China are "rogue donors" and have been found giving help to "corrupt regimes". This means that all the aid that is given by China, has had no effect on the development of the country because the government has already spent it on themselves, and on the military weapons.

ResultsPlus
Examiner Comments

Reduction in absolute poverty is identified and briefly explained in the first paragraph (1 + 1). This is followed by a brief evaluative comment in the next paragraph (1). The improvement in human capital is explained in the third paragraph (1 + 2). The final paragraph includes the example of China (1) and some evaluation relating to corruption. (2). Total 9/15

ResultsPlus
Examiner Tip

A further example would have obtained another application mark.

Question 5 (a)

This question was answered well: most answers referred to the key role of the WTO in reducing trade barriers and many referred to its role in settling disputes, giving an example from the extract or from their own knowledge.

(a) With reference to Extract 1, explain the role of the World Trade Organisation (WTO).

(5)

The ~~World~~ WTO ~~a~~acts a ~~dispute~~ mediator in desputes and aims to promote free trade & economic liberalism. The case of Brasil using the WTO as a mediator between it and the USA in the case of government subsidies & loans for cotton growers. The WTO asserted its authority and declared these a breach of international law as it hindered free trade & distorted market forces. As a result of America's action retaliatory tarrifs were introduced. The WTO also helps support developing countries. Nonetheless there has been disputes over whether the organisation is simply a tool for the haves (MEDCs) against the have nots (LEDCs)

ResultsPlus

Examiner Comments

The first sentence gains 3 marks for identifying 2 key roles of the WTO. This is followed by an example relating to Brazil which gains 2 application marks. 5/5

ResultsPlus

Examiner Tip

This answer shows that the first 3 marks may be gained by a very succinct outline of the main functions of the WTO.

(a) With reference to Extract 1, explain the role of the World Trade Organisation (WTO).

(5)

The World Trade Organization (WTO) is an international commitee comprising of over 50 members. Its main role is to promote free trade and remove and review barriers to trade such as tariffs and quotas. The WTO uses consenssus voting which has proved to be promblematic in the past at resolving disputes. The role of the WTO to promote trade for developing countries is usually undermined by countries such as the USA abusing their strong economic position.

ResultsPlus

Examiner Comments

This response explains the role of the WTO in terms of promoting free trade and settling disputes but does not gain any application marks. 3/5

ResultsPlus

Examiner Tip

When there is a reference to the extract, it is important to include an example of the work of the WTO.

Question 5 (b)

This question was generally answered well and most candidates examined the effect of the undervaluation of the Chinese currency on the price of imports and on the US current account including specific data references. Better responses went on to consider other implications e.g. for employment in the US.

(b) With reference to Figures 1 and 2 and to Extract 2, analyse the effects of an undervaluation of the Chinese currency, the renminbi, for the US economy.

(8)

The udervaluation of the chinese currency, the renminbi, would affect the balance of payments, especially the current account in the US.

The high exchange rate has led to the US ~~us~~ importing a lot of goods from ~~the US~~ china. because they appear cheap in comparison to goods in the US. Importing goods is a leak from the circular flow of income, meaning that the GDP of the US is likely to decrease and also the current account deficit will increase. Since 1990, the US has accumalated $2009 billion worth of debt just from importing from China.

ResultsPlus

Examiner Comments

The marks are gained in the second paragraph for identifying two points (cheap imports and increase in current account deficit) with some explanation of the first point (2 + 1). The penultimate line gains 2 application marks for specific reference to US debt. 5/8

ResultsPlus

Examiner Tip

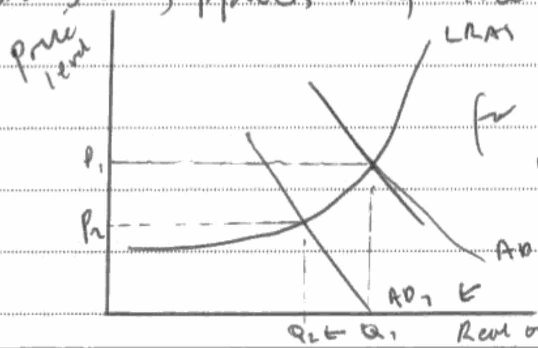
The points identified need to be explained to gain all the analysis marks.

(b) With reference to Figures 1 and 2 and to Extract 2, analyse the effects of an undervaluation of the Chinese currency, the renminbi, for the US economy.

(8)

The chinese Government undervalue their currency against the US Dollar so that the Renminbi is very cheap.
This means that the US will import lots of goods from china, which will lead to their balance of payments worsening. for example the US trade deficit to China went up from $10 billion in 1990 to $268 billion in 2008, this is a massive increase and means a large deficit

Chinas low ~~other~~ exchange rate also means there is likely to be higher unemployment in the US as domestic workers will not be able to make goods so cheap and the influx of imports will mean they will lose their jobs. for example if Ipods were made in the US for $10 but only $1 in the China, it is likely all the domestic suppliers may lose their jobs



A cheap exchange rate for china will lead to a fall in US AD, a loss of jobs and a decrease in $P_1 \rightarrow P_2$ might deflationary pressures.

ResultsPlus

Examiner Comments

In the first paragraph, the increase in imports is identified (1) and there is a specific data reference relating to the increase in the size of the US trade deficit (2). A further point relating to increased unemployment is identified (1) and explained (3) in the second paragraph. Total 7/8

ResultsPlus

Examiner Tip

It is important to use the data as this candidate has done rather than writing a purely theoretical response. 2 marks are available for a reference to the information.

Question 5 (c)

This is the first time that a question has been set specifically on the subject of trade imbalances and it proved to be quite challenging for many candidates. Nevertheless, there were some impressive responses which analysed the effects of an increase in savings on consumption, imports and on the trade balance and then went on to consider the possible link between increased savings and investment. Evaluation included comments on the size of the US trade deficit; and the possible effect of changes in the value of the dollar but such comments were relatively rare.

(c) To what extent might a higher level of savings in the USA be sufficient to eliminate trade imbalances between China and the USA?

(10)

A higher level of savings in the USA may be sufficent to elimate trade imbalances between China and the USA because if the economy as a whole starts to save more, then they are less likely going to be spending money on imports. So the trade deficit may decrease.

Also higher level of savings in the USA will encourage Chinese companies to invest in the USA as they will receive a higher amount of interest on the money they invested. This will reduce trade imbalances as it will effect the current account as it is a transaction. The current account takes into consideration trade both visable and invisable, transactions and foreign direct investment (FDI).

ResultsPlus
Examiner Comments

This answer received 2 marks for the first paragraph which identified the impact of higher savings on imports and the trade deficit. The second paragraph was not considered worthy of credit.

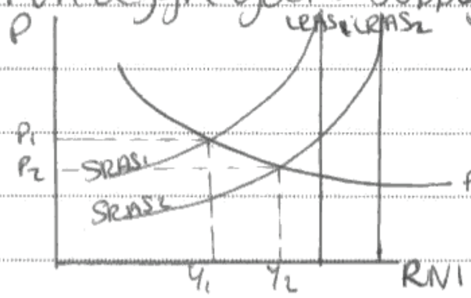
ResultsPlus
Examiner Tip

The theme of trade imbalances is mentioned in the syllabus and given its significance for the global economy, this is an area which should be studied carefully.

(c) To what extent might a higher level of savings in the USA be sufficient to eliminate trade imbalances between China and the USA?

(10)

A higher level of saving in the US will mean that people consume less, so people aren't consuming as much from abroad, ie China, so the trade deficit will decrease. The US will also have increased reserves for investment. Investment in the economy is a good thing as it may increase long run aggregate supply. ~~As~~ $LRAS_1$ to $LRAS_2$.



This will decrease inflation P_1 to P_2 and making US good more competitive and increase real national income Y_1 to Y_2.

This increase in competitiveness may mean that the Chinese buy goods and services from the US which will have a good impact on the trade imbalance. Also,

because prices are low, the Chinese may decide on the US as a tourist destination so, again, having a positive impact on the trade imbalance because the Chinese are buying more American goods.
However, this probably won't have a big enough impact because the total

ResultsPlus

Examiner Comments

In the first two sentences there is identification of the impact on consumption and its impact on the trade deficit (1 + 1). There is then good analysis of the link between savings and investment (2). The last paragraph makes a specific data reference to the US trade deficit (2) and good evaluation (3). Total 9/10

ResultsPlus

Examiner Tip

Including a specific reference to the size of the US trade deficit is a good strategy both in terms of application and evaluation.

Question 5 (d)

In the past, questions have been set on the implications of a trade deficit and many candidates interpreted this question in this way. The best responses considered the implications of both trade deficits and surpluses, examining both the reasons why each may or may not be a cause for concern. Relatively few candidates provided examples of countries with trade surpluses or deficits. In general, this proved to be a challenging question and candidates struggled to analyse and evaluate their points.

*(d) To what extent are large trade imbalances a cause for concern?

(12)

Trade ~~$~~ imbalances refer to some economies being able to run trade ~~sup~~ surpluses e.g. China, Russia and Brazil, and those economies who run trade deficits, e.g. UK, USA, India.

Trade is predominantly done between those developed ~~countries~~ economies and advanced developing economies. Very little trade takes place within developing economies e.g. African countries. This trade imbalance causes problems especially for those who struggle to trade due to a number of reasons e.g. do not have the technology or access to raw materials in the earth. Whereas trade is good for the global economy, these imbalances mean that income is not evenly spread between countries, and so the developing economies stay developing.

However, whether this is a concern for those developing or ~~¢~~ even developed countries that run trade deficits, is questionable. The US is the largest economy in the world, yet they run trade deficits, same applies to the UK economy, before the recession, we ran year on year trade deficits and still ~~adc~~ achieved GDP growth. ~~So~~ India are in the same position, they are very much against trade, they aim to develop their country through means of there domestic producers rather than trade

~~So whether these trade imbalances are of a concern I feel is relatively~~

In conclusion, I do not feel these trade imbalances ~~of~~ are of ~~an~~ a concern as there are examples of developed and developing economies who run trade deficits but still experience year on year GDP growth.

ResultsPlus

Examiner Comments

2 application marks were awarded for the examples provided in the first paragraph. The second paragraph was irrelevant but 1 identification mark was awarded for the point made in the third paragraph. Total 3/10

ResultsPlus

Examiner Tip

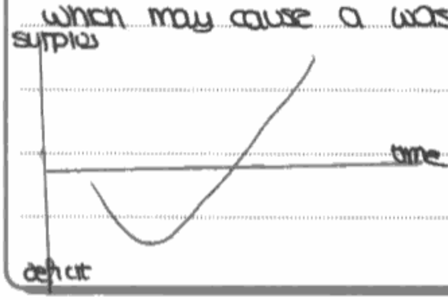
Answers could consider why trade deficits or trade surpluses are a cause for concern and then examine the counter arguments.

*(d) To what extent are large trade imbalances a cause for concern?

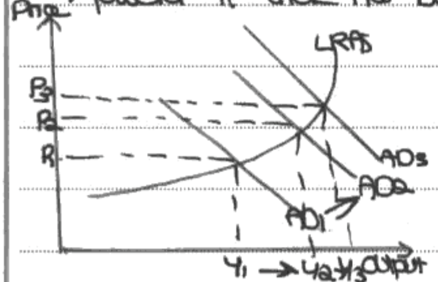
(12)

Trade imbalances are caused when a countries exports are not ~~are smaller~~ equal to their imports causing an imbalance as a surplus or deficit ~~than their imports causing a deficit.~~

This is generally seen as a large cause for concern because it implies that the economy is becoming less competitive both in price and other non-price factors. Due to this the demand for the countries goods will decrease which will then lead to a decrease in the demand for labour and an increase in unemployment. This has many negative effects which include an increase in the level of relative poverty because more people are relying on benefits or in absolute poverty if there is no welfare state. For the government this may lead to a decrease in tax revenue as corporation tax decreases as does income tax, however government spending may need to increase to pay for benefits or to try and decrease the output gap. This would then lead to a fiscal deficit which would lead to an increase in the government debt if it was sustained. Although this would depend on the time this occured for because if it was for a short time, it may just be in the time lag it takes for supply side policies to take place. This may not be as cause for concern because in a floating exchange rate the decrease in demand causes a decrease in demand for the currency. This in turn leads to the currency depreciating which may cause a worsening in the trade deficit in the short run but a surplus in the long run if the Marshall Lerner condition comes true. However, this can depend on the efficiency and competitiveness of firms.



A trade imbalance may not be a cause for concern when exports are exceeding imports because there is a high level of employment in the economy which leads to increased tax revenue and decrease in government spending, although that may depend on the level of voluntary employment. The economy will be growing in these circumstances leading to the government achieving economic growth. However if there has been little investment in the economy and it is operating at full capacity then there will be inflationary pressures which may mean the government may overshoot their inflation target., $P_1 \rightarrow P_3$.



Therefore it can be seen that a trade imbalance may be more of a problem if there is a trade deficit. Although this may depend on other parts of the balance of payments as a surplus in those areas may cancel it out. But it does indicate the economy is not competitive. A trade surplus may be positive to the economy when supported by supply side policies so there is not inflationary growth.

ResultsPlus
Examiner Comments

The second paragraph identifies a loss of competitiveness (1) as a cause for concern followed by analysis of the possible effects (2). 3 evaluation marks were awarded for the impact on the value of the currency. A further identification mark was awarded for the point about high employment being associated with a trade surplus and associated analysis (1 + 1). The last paragraph earned the 2 remaining evaluation marks. Total 10/12

ResultsPlus
Examiner Tip

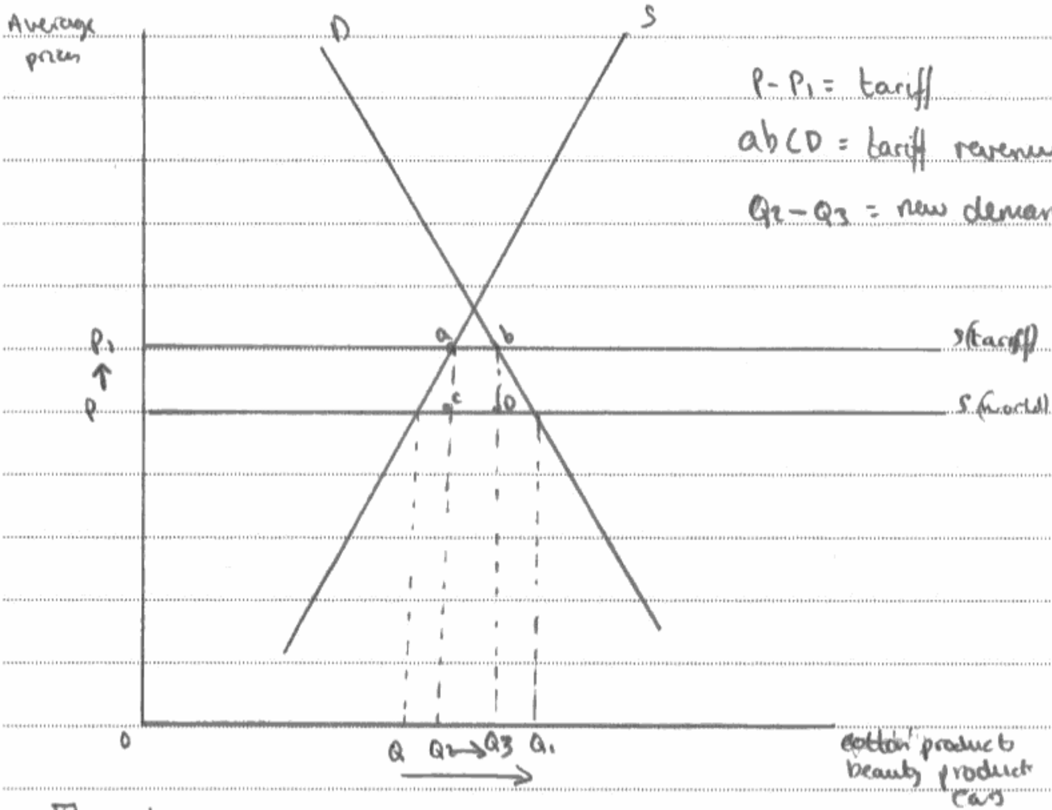
2 application marks could have been gained by giving examples of countries with larger trade surpluses or deficits.

Question 5 (e)

Most candidates were able to draw an accurate tariff diagram and many included data references from the material provided. The best responses considered the impact of tariffs by Mexico and Brazil on US producers in terms of sales, revenues, profits and possible implications for pricing and then went on to consider the implications for US consumers in terms of redundancies in US industries. Given the wording of the question, credit was given to those who interpreted the question as the imposition of tariffs by the US.

*(e) With reference to Extract 1, assess the impact of tariffs, such as those imposed by Mexico and Brazil, on US consumers and producers. Illustrate your answer with an appropriate diagram.

(15)



The tariff of $560m shown by P-P1 will create a ~~subsid~~ big amount of revenue (abcD) for Brazil which can be used for other protectionist policys such as subsidies, and also for investment in the country.

This will affect the US producers as they may ~~will~~ need to lower the price of the products so they can maintain the amount of revenue and sales they are currently earning.

This may encourage the US producers to become more cost effective and lower production costs so they still make a healthy profit even with the tariffs in place. With the tariff in place the quantity demanded falls from Q-Q1 to Q2-Q3, which is a big difference. As the price has gone up. ~~As cotton products, cars and to an extent beauty products are seen as a necessity the relative PED value will be less than 1~~, so ~~they will be inelastic which~~

The tariff introduced means that thousands of American workers may lose their jobs, this will mean ~~as~~ that consumer consumption in the US will fall as people will have less disposable income, to spend. It ~~will~~ may also encourage saving in the economy as people are losing their jobs. So the producers are also losing out on their own country's consumption aswell as some of them going out of business.

Also because Brazil are also free to impose other penalties which will then further decrease the amount of profit made by producers. They can also ignore patents that the US have, this can lead to them producing the same goods at potentially the same standard, this will yet again further cause producers to lose out, aswell as more consumers not consuming as they have lost their jobs.

ResultsPlus

Examiner Comments

The tariff diagram was awarded 2 marks. Following this there is an application mark for mentioning the revenue from the tariff to Brazil. The analysis of the effects on US producers was worth 2 marks with a further 3 marks for the analysis of the effects on US consumers. However, there is no evaluation. Total 8/15.

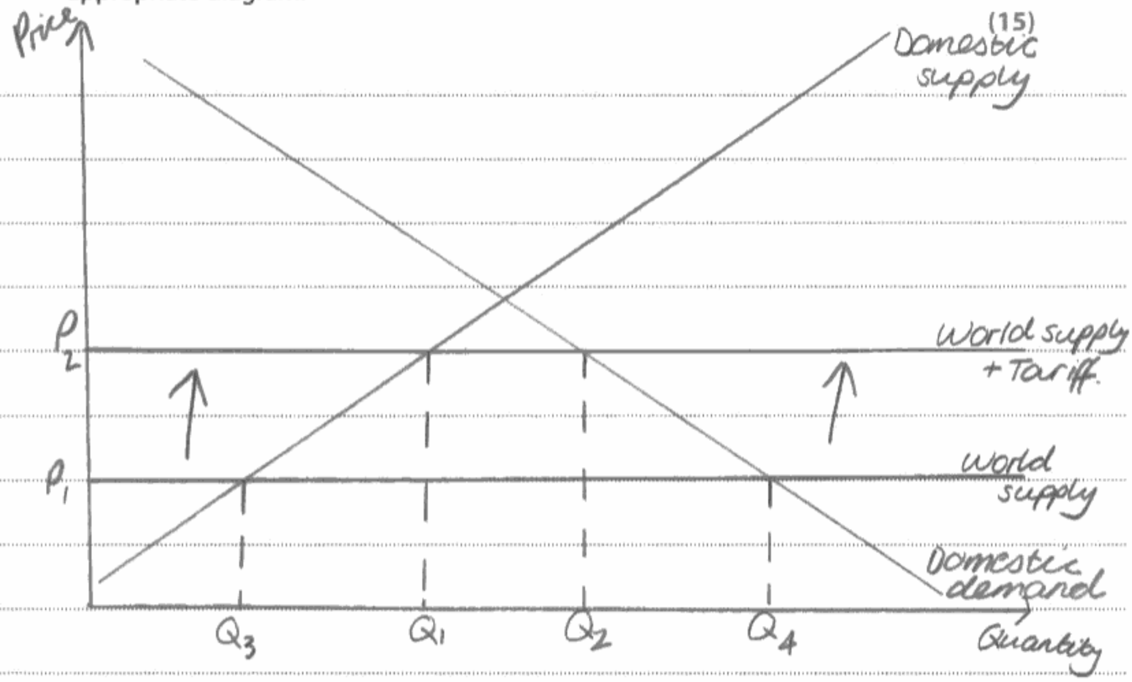
ResultsPlus

Examiner Tip

Evaluation is worth 6 marks on this question so the omission of any evaluative comments was very costly.

*(e) With reference to Extract 1, assess the impact of tariffs, such as those imposed by Mexico and Brazil, on US consumers and producers. Illustrate your answer with an appropriate diagram.

(15)



A tariff is a protectionist policy used to increase the price of exporting a good or service to a certain country or trade bloc. This comes in the form of an import tax. A tariff of \$2.4bn was imposed on US goods in Mexico and \$560m in Brazil, this will have a significant effect on US producers as these are considerable tariffs. However this depends on the proportion of goods produced are imported into Brazil and Mexico. Arguably this will not be as much as the USA's main trading partners are the EU and the UK.

The tariff reduces the amount supplied to the country (Brazil and Mexico in this case) from Q_3 ~~Q_4~~ to Q_1Q_2. This may have a significant impact on US consumers as these tariffs will result in US firms making losses of \$2.6bn and so they will be forced to make redundancies. These tariffs have resulted in 1000s of US workers losing their jobs. This of course will mean that they have no disposable income. ~~and~~ This level of unemployment is especially negative for US consumers as there are no welfare benefits available to the unemployed and so if workers are out of a job in the long run, this could result in extreme poverty. Of course this depends on the level of skill of the workers as if the US consumers are highly skilled in areas ~~of~~ that are in high demand they are likely to find another job more quickly.

US producers may face increasing problems if these tariffs are imposed for a long period of time as consumers from Brazil and Mexico may change their brand loyalties and decide to buy from other countries even if the tariffs are lifted. The significance of ~~this~~ the effect on these tariffs will also depend on how much of US exports are affected, for example it does not mention that the US technology industry will be effected by these tariffs.

ResultsPlus

Examiner Comments

2 marks for the tariff diagram; 2 for specific data references (there are at least 3 of these); 2 for analysis of the implications for US consumers/workers and 6 marks for 3 evaluative comments (at end of first page; on the impact on consumers and on producers). Total 12/15

ResultsPlus

Examiner Tip

The analysis of the effect on producers could have been developed by considering the impact on sales; profits; pricing policy.

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