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Centre Number					Candidate Number				
Candidate Signature									

General Certificate of Education
January 2003
Advanced Subsidiary Examination



ECONOMICS **ECN2/1**
Unit 2 Part 1 Objective Test: The National Economy

Friday 17 January 2003 Morning Session

In addition to this paper you will require:

- an objective test answer sheet;
- a blue or black ball-point pen;
- the question paper for Part 2 (ECN2/2).

You may use a calculator.

Time allowed: 1 hour 30 minutes for papers ECN2/1 and ECN2/2 together

Instructions

- Use a blue or black ball-point pen. Do **not** use pencil.
- Fill in the boxes at the top of this page.
- Answer **all** questions.
- For each question there are four alternative responses. When you have selected the response which you think is the best answer to a question, mark this response on your objective test answer sheet. If you wish to change your answer to a question, follow the instructions on your objective test answer sheet.
- Do all rough work in this book, **not** on your answer sheet.

Information

- The maximum mark for this paper is 25 marks.
- Each question carries one mark. No deductions will be made for wrong answers.

Advice

- You are advised to spend no more than 30 minutes on paper ECN2/1.
- Do not spend too long on any question. If you have time at the end, go back and answer any question you missed out.
- Make sure that you hand in **both** your answer sheet **and** this question book at the end of the examination.

OBJECTIVE TEST QUESTIONS

You are advised to spend no more than 30 minutes on these questions.

Each item consists of a question or an incomplete statement followed by four suggested answers or completions. You are to select the most appropriate answer in each case.

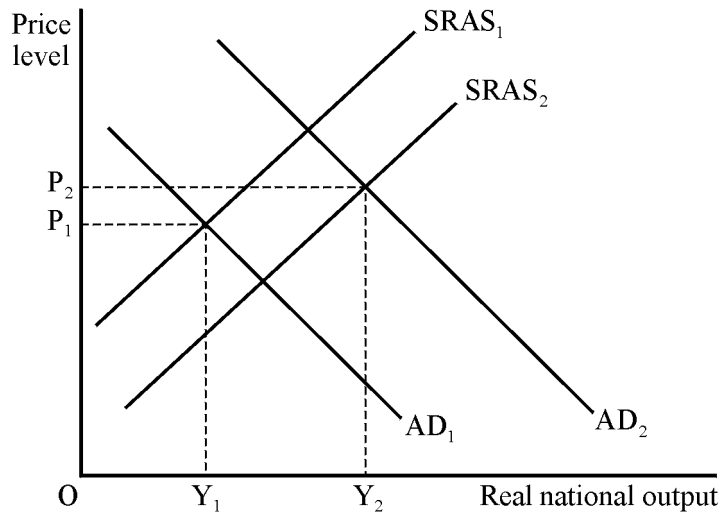
- 1 Which one of the following is most likely to lead to an increase in aggregate demand? An increase in
 - A savings.
 - B imports.
 - C government tax revenue.
 - D investment.

- 2 All but one of the following are usually regarded as objectives of macroeconomic policy. Which is the **exception**?
 - A Increasing the trend rate of economic growth.
 - B Achieving equilibrium on the current account of the balance of payments.
 - C Increasing the output of the financial services industry.
 - D Achieving full employment.

- 3 A recession is said to occur in the UK economy when
 - A the current account of the balance of payments is in deficit for more than two years.
 - B real national output falls for two successive quarters.
 - C nominal national income falls but real national income continues to grow.
 - D the growth of output of manufacturing industries slows down.

- 4 All other things being equal, an increase in the productivity of labour in an economy will lead to
 - A an increase in the price level.
 - B a rightward shift of the aggregate supply curve.
 - C an increase in the rate of growth of the labour force.
 - D a decline in the level of aggregate demand.

- 5 The diagram below shows an economy initially in equilibrium producing an output of Y_1 at a price level of P_1 .

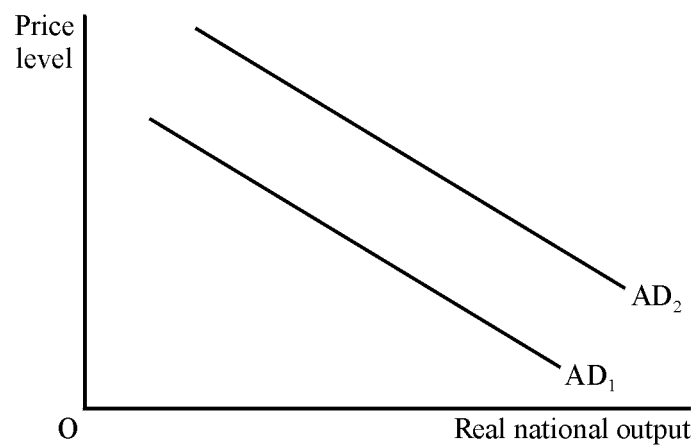


Which of the following is likely to have increased the equilibrium level of output from Y_1 to Y_2 and the price level from P_1 to P_2 ?

- A A cut in taxation and a fall in raw material prices.
- B A cut in taxation and a rise in raw material prices.
- C An increase in taxation and a fall in raw material prices.
- D An increase in taxation and a rise in raw material prices.
- 6 All other things being equal, which of the following is most likely to lead to an increase in the size of the UK's current account deficit on the balance of payments?
- A A fall in the exchange rate.
- B A fall in consumer spending.
- C A reduction in income tax rates.
- D A fall in the rate of inflation.
- 7 A large increase in borrowing by consumers is most likely to lead to a
- A rise in imports into the UK.
- B rise in exports from the UK.
- C fall in the rate of inflation.
- D fall in employment.

Turn over ►

- 8 Other things remaining constant, an initial increase in aggregate investment expenditure will lead to an even larger increase in national income. This statement refers to
- A an increase in the savings ratio.
 - B the multiplier process.
 - C the use of fiscal policy.
 - D the economy's underlying trend rate of growth.
- 9 Which one of the following statements accurately defines monetary policy? It is a policy concerned with
- A the direct control of prices and incomes.
 - B the control of taxation and government spending.
 - C the control of interest rates or money supply.
 - D managing the government's budget.
- 10 The diagram below shows aggregate demand in an economy.



All other things being equal, the increase in aggregate demand from AD₁ to AD₂ could be explained by

- A an increase in tax rates.
- B a decrease in welfare benefits.
- C an increase in the exchange rate.
- D a decrease in the rate of interest.

- 11 “In December 2001, it was predicted that between 1997 and 2004 the level of welfare benefits would rise by £32.5 billion (a 35% increase) to a record £125 billion per year.” (*Independent*, 26 December 2001).

All other things being constant, this rise in welfare benefits would be most likely to lead to

- A a budget surplus.
 - B increased exports from the UK.
 - C increased imports into the UK.
 - D a cut in taxation.
- 12 The table below shows productivity in various countries in 2000.

Productivity: GDP per hour worked (UK = 100)	
France	124
USA	122
Germany	110
Switzerland	104
Sweden	102
UK	100
Canada	98
Japan	83

From the table it can be concluded that in 2000

- A Japan had the lowest output.
- B Germany’s output per hour worked was 10% greater than the UK’s.
- C France had the highest level of GDP.
- D economic growth was occurring in all the countries.

Turn over ▶

- 13 Which one of the following statements about an economy's output gap is **not** correct?
- A There is an output gap when national income is greater than it would be if the economy always grew at its trend rate of growth.
 - B There is an output gap when national income is less than it would be if the economy always grew at its trend rate of growth.
 - C An economy's output gap can be positive or negative.
 - D The output gap measures the extent to which an economy's national output is less than that of competitor countries.
- 14 Which of the following is most likely to shift the short-run aggregate supply curve to the right?
- A A fall in money wages.
 - B A reduction in government spending.
 - C A fall in the exchange rate.
 - D A decrease in the productivity of labour.
- 15 Which one of the following is **not** a component of aggregate demand?
- A Investment.
 - B Exports.
 - C Government expenditure.
 - D Savings.
- 16 "When the economy is doing well, or is predicted to do well, interest rates are increased to make borrowing more expensive."
- The policy measure described above is an example of
- A supply-side policy.
 - B monetary policy.
 - C budgetary policy.
 - D fiscal policy.

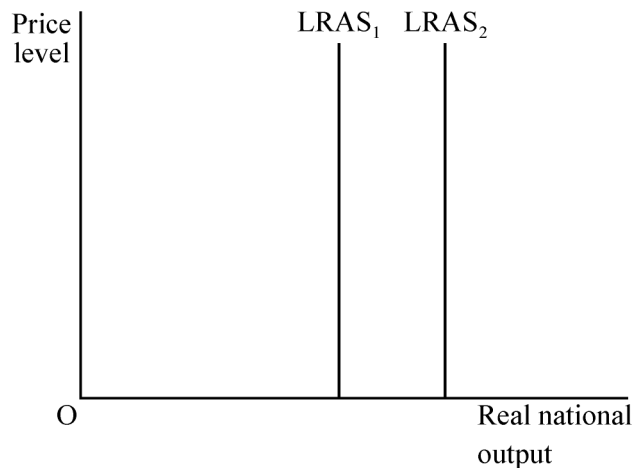
- 17 An economy's short-run aggregate supply curve is upward sloping. Following an increase in aggregate demand, what is most likely to happen to inflation and unemployment in the short run?

	Inflation	Unemployment
A	increases	increases
B	decreases	increases
C	decreases	decreases
D	increases	decreases

- 18 "There are more people in work than at any time since records began and these people are seeing their pay rise at more than twice the rate of inflation." (*Independent*, 22 June 2001)

The above extract implies that

- A the population was declining.
 B real income was rising.
 C inflation was falling.
 D the exchange rate was rising.
- 19 The diagram below represents two possible long-run aggregate supply curves, LRAS₁ and LRAS₂.



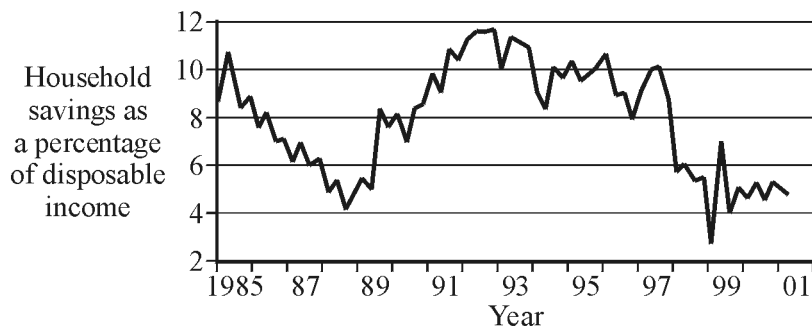
The shift to the right in the LRAS curve is most likely to have been caused by an increase in

- A the quantity of exports supplied to overseas markets.
 B interest rates.
 C expenditure on education and training.
 D household consumption.

Turn over ▶

- 20** The major objective of the monetary policy being pursued by the Bank of England is to achieve
- A** a target rate of inflation.
 - B** a higher rate of economic growth.
 - C** full employment.
 - D** equilibrium on the current account of the balance of payments.
- 21** The government is concerned that, without any change to its current economic policy, the rate of growth of the economy will fall below its trend rate. Which of the following policy changes is most likely to prevent this from happening?
- A** An increase in interest rates.
 - B** A reduction in the level of the state old age pension.
 - C** An increase in government expenditure.
 - D** A reduction in the target for the rate of inflation.
- 22** Which one of the following is most likely to lead to a rise in investment?
- A** A rise in imports.
 - B** A rise in the rate of interest.
 - C** A rise in the level of company profits.
 - D** A fall in the growth rate of aggregate demand.
- 23** In August 2001 the Monetary Policy Committee (MPC) of the Bank of England continued the trend of falling interest rates by cutting the base rate from 5.25% to 5%. One justification for this might have been the MPC's concern over
- A** increasing evidence of a recession in UK manufacturing.
 - B** an increase in the rate of growth of labour productivity.
 - C** an increase in the rate of inflation.
 - D** increasing activity in the housing market.

24 The diagram below shows the savings ratio for the UK economy between 1985 and 2001.



Source: *Financial Times*, 18 December 2001

It can be concluded from the data that

- A total household savings were lower in 2001 than in 1985.
 - B household disposable income and saving both increased between 1989 and 1992.
 - C there must have been a boom in the economy in 1997-2000.
 - D households saved a greater proportion of their disposable income in 1995 than in 2001.
- 25 Which of the following policies is most likely to lead to an increase in output and employment without increasing the rate of inflation?
- A Expansionary fiscal policy.
 - B Expansionary monetary policy.
 - C Supply-side policies.
 - D Policies to boost exports.

**QUESTION 25 WAS THE LAST
QUESTION ON THE PAPER**

**ON THE ANSWER SHEET
IGNORE ROWS 26 TO 50**

END OF TEST

General Certificate of Education
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Advanced Subsidiary Examination



ECONOMICS **ECN2/2**
Unit 2 Part 2: Data Response: The National Economy

Friday 17 January 2003 Morning Session

In addition to this paper you will require:

- an 8-page answer book;
- the question paper for Part 1 (ECN2/1).

You may use a calculator.

Time allowed: 1 hour 30 minutes for papers ECN2/1 and ECN2/2 together

Instructions

- Use blue or black ink or ball-point pen. Pencil should only be used for drawing.
- Write the information required on the front of your answer book. The *Examining Body* for this paper is AQA. The *Paper Reference* is ECN2/2.
- Answer **EITHER** Question 1 **OR** Question 2.

Information

- The maximum mark for this paper is 35.
- Mark allocations are shown in brackets.
- You will be assessed on your ability to use an appropriate form and style of writing, to organise relevant information clearly and coherently, and to use specialist vocabulary, where appropriate. The degree of legibility of your handwriting and the level of accuracy of your spelling, punctuation and grammar will also be taken into account.

Advice

- You are advised to spend at least 1 hour on paper ECN2/2.

Answer **EITHER** Question 1 **OR** Question 2.

EITHER

1 TARGETS OF MACROECONOMIC POLICY

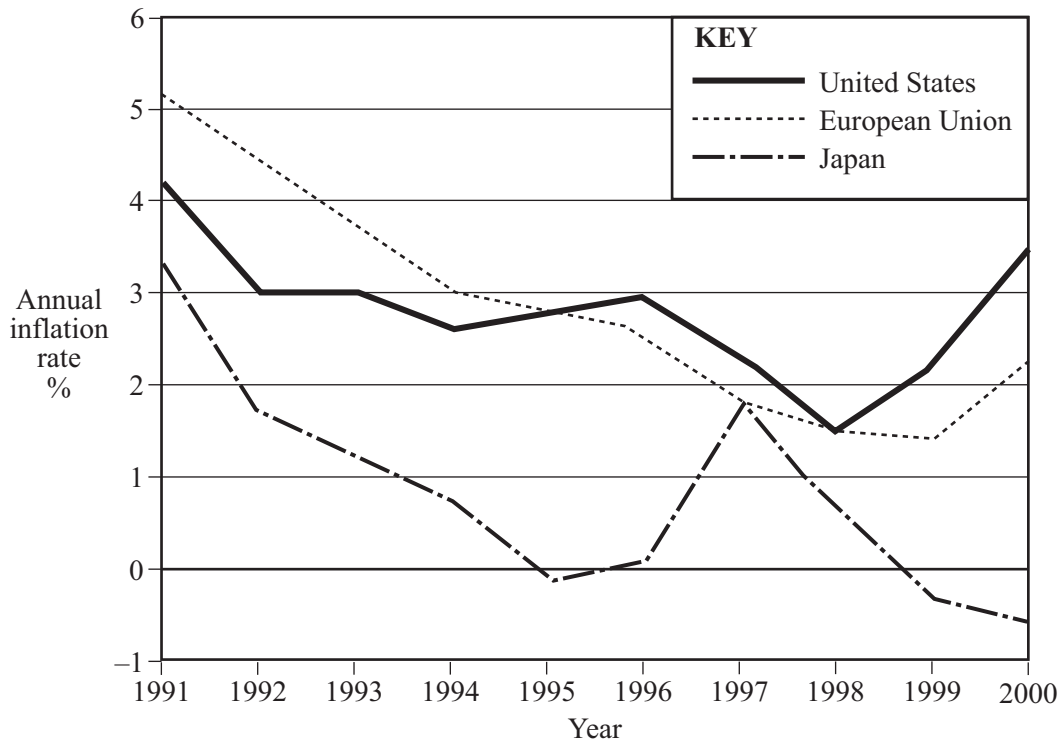
Total for this question: 35 marks

Study **Extract A**, and then answer **all** parts of Question 1 which follows.

Extract A

Macroeconomic policy is used to influence one or more economic variables, namely 1
economic growth, full employment, the balance of payments and the rate of inflation. These
are not always seen as compatible. For instance, policy aimed at providing a high rate of
economic growth and low levels of unemployment may run the risk of pushing the rate of
inflation above acceptable levels, or of leading to a deficit on the current account of the 5
balance of payments.

Inflation in selected advanced economies



Inflation would occur if the rate of growth of gross domestic product moved above its long-term potential rate of growth at a time when there was no spare capacity in the economy. The current account would be likely to deteriorate if demand was greater than the economy's ability to supply that demand. The excess demand would have to be filled by extra imports or by potential exports being shifted to the domestic market. However, supply-side policies are often used to try to increase the long-term potential rate of growth.

10

The modern trend in demand management in the United Kingdom, as well as in many other developed countries, has been to focus on the rate of inflation as the main economic target. The shift in emphasis to controlling inflation has meant that monetary policy has increasingly taken the prominent role in economic management in the United Kingdom over the last quarter of a century or so. The shift towards targeting inflation in preference to growth and full employment, targets which dominated the post-war years in the UK, has also meant a shift away from the use of fiscal policy as the main method of controlling aggregate demand. Changes in government spending and taxation have been increasingly used as a means of redistributing income and to introduce supply-side changes designed to make the economy more flexible.

Monetary policy is used to stimulate or slow the economy in the short run so that the economy is kept as close as possible to its long-term potential rate of growth and inflation is kept close to its target.

Source: adapted from The United Kingdom Economy Explained, a CD ROM produced by HSBC

Question 1

- (a) Using the graph, compare the rates of inflation in the European Union, the USA and Japan between 1991 and 2000. (5 marks)
- (b) Explain how aggregate demand can be controlled by the use of:
- (i) monetary policy; (5 marks)
 - (ii) fiscal policy. (5 marks)
- (c) Assess the view that policy aimed at achieving a high rate of economic growth will inevitably lead to inflation and a deficit on the current account of the balance of payments. (20 marks)

TURN OVER FOR THE NEXT QUESTION

Turn over ►

OR

2 THE IRISH ECONOMY**Total for this question: 35 marks**

Study **Extracts B and C**, and then answer **all** parts of Question 2 which follows.

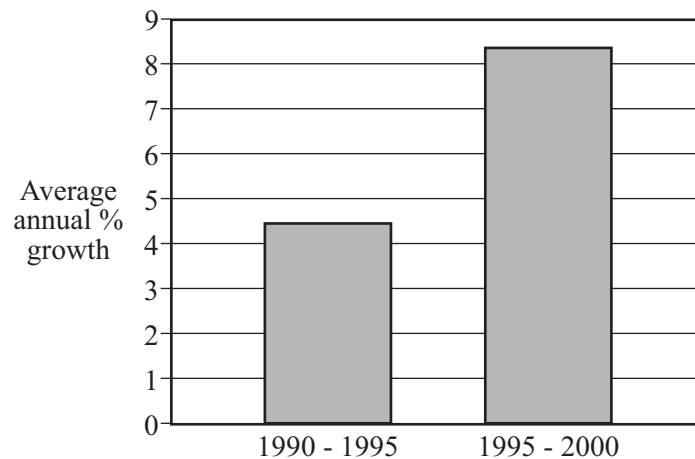
Extract B

Figure 1 below shows the growth in real Gross National Product (GNP) for the Irish economy between 1997 and 2000. The Central Statistical Office estimates that real GNP will grow by 6% in 2001.

Figure 1

Year	Change in Real GNP (%)
1997	9.4
1998	7.9
1999	8.2
2000	10.4

Source: *Economic Bulletin*, November 2001 (www.irlgov.ie)

Extract C**Figure 2: Annual average growth in real GNP**

A key factor in expanding the growth potential of the Irish economy in the 1990s was the rapid increase in the labour supply. For centuries, Ireland had “too much” labour and not enough jobs. What made the last decade different was that the combined benefits of improved access to the European Union market, and increased foreign investment in Ireland, raised the demand for goods and services produced in Ireland, while Irish productivity was greatly increased by investment in human capital.

1

5

The large inflow of young people into the labour force was supplemented by the rapid rise in the female labour supply. In addition, over the last five years substantial immigration of skilled labour has expanded the productive capacity of the economy.

In the medium term, the increase in employment will be significantly slower than over the last decade. In the 1990s, there was a considerable improvement in competitiveness, which expanded the demand for Irish products and led to a rapid increase in employment. This was achieved through moderate wage growth and a resulting rise in profits. However, with the economy currently close to full employment, this situation has changed dramatically. Wage rates are now rising rapidly relative to competitors. In our forecast for the economy, it is assumed that, between 2000 and 2005, market circumstances will lead to more moderate wage inflation, and that the growth in productivity, while slower than in the late 1990s, will still greatly exceed that of Ireland's competitors.

Source: Economic and Social Research Institute Medium-Term Review, 2001-2007 (www.esri.ie)

Question 2

- (a) Using **Figures 1 and 2**, describe the growth of the Irish economy between 1990 and 2000. (5 marks)
- (b) Explain **three** factors that have contributed to the rapid growth of the Irish economy. (10 marks)
- (c) Assess the possible effects of a continuation in the rapid growth of average wages for the performance of the Irish economy. (20 marks)

END OF QUESTIONS

THERE ARE NO QUESTIONS PRINTED ON THIS PAGE

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