



Rewarding Learning

ADVANCED SUBSIDIARY (AS)
General Certificate of Education
January 2012

Economics

Assessment Unit AS 2

The National Economy

[AE121]

WEDNESDAY 18 JANUARY, MORNING



TIME

1 hour 30 minutes.

INSTRUCTIONS TO CANDIDATES

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

INFORMATION FOR CANDIDATES

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

ADVICE TO CANDIDATES

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

Question 1: Data response

The following article was written in **August 2010**.

Study it carefully and answer the questions which follow.

UK inflation rate remains above target

Measures of UK Inflation, 2008–2010

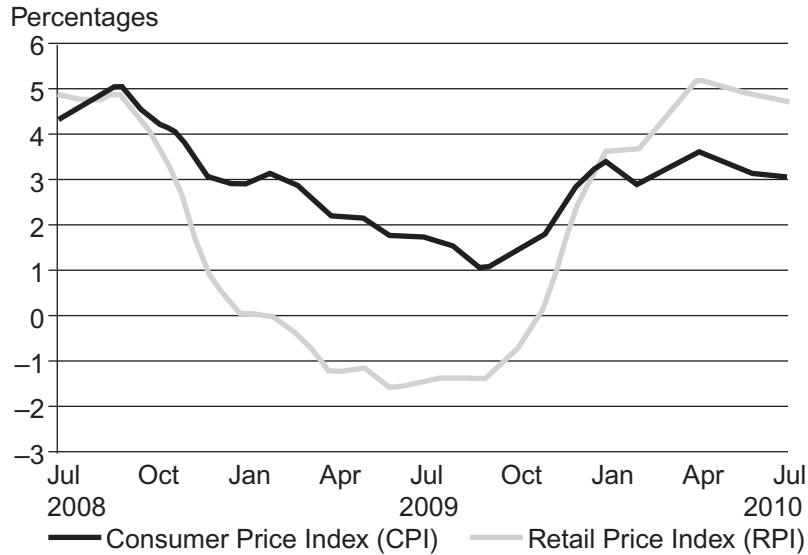


Fig. 1

The government’s target measure of annual inflation, CPI, was 3.1 per cent in July 2010, down from 3.2 per cent in June. This modest fall still left the rate of inflation significantly above the target level of 2 per cent which the Bank of England is charged with achieving. Another measure of inflation, the RPI, showed a similar pattern. In the year to July 2010, RPI annual inflation was 4.8 per cent, down from 5.0 per cent in June. The slight easing in inflation came from a variety of sources but many of them stem from a rise in the value of the pound. For example, petrol prices fell by 0.7 pence per litre between June and July this year and clothing and footwear prices are down by 4.9 per cent this year.

1

Although CPI and RPI produce significantly different outcomes, these measures of inflation are compiled in a broadly similar manner. Both are concerned with the change in the price of baskets of goods and services. However, the contents of the baskets are slightly different, for example, the RPI includes a range of housing-related costs which are excluded from the CPI. The indices also differ slightly in terms of the nature of the households which are included in the survey.

2

Not only is UK inflation above the government’s target, it is also significantly above that of our major trading partners. As an internationally comparable measure of inflation, the CPI shows that the UK inflation rate in June was above the figure for the European Union. The UK rate was 3.2 per cent, whereas the EU’s as a whole was 1.9 per cent.

3

This stubbornly high rate of inflation means that the Monetary Policy Committee of the Bank of England is under considerable pressure to raise interest rates. At its meeting in August 2010 one member, Mr Andrew Sentance, voted for a rise, and many independent economists are concerned that the inflation target may become an irrelevancy if it is continually missed. One said that the Bank of England should increase rates, irrespective of the impact on other macroeconomic variables such as unemployment and growth.

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- 1 (a) Using **Fig. 1**, compare the trends in CPI and RPI inflation rates between July 2008 and July 2010. [6]
- (b) Explain why the CPI and RPI inflation rates differ. [8]
- (c) Explain why a rise in the value of the pound helps to reduce the UK rate of inflation. (Paragraph 1) [8]
- (d) Apart from the exchange rate, analyse other possible causes of the difference between UK and EU inflation rates. [8]
- (e) Critically examine the view that the Bank of England should pursue its inflation target, irrespective of the impact on other macroeconomic objectives. (Paragraph 4) [10]

Essays:

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

2 “Happiness more important than growth!”

- (a) Explain the difference between Gross Domestic Product (GDP) and Gross National Product (GNP). [10]
- (b) Compare the income and expenditure methods of measuring an economy's Gross Domestic Product. [15]
- (c) Evaluate the view that government should focus on improving the quality of life of its citizens rather than simply trying to achieve economic growth. [15]

3 “Balanced budgets are best”

- (a) Explain what is meant by the term fiscal policy. [10]
- (b) Using aggregate demand and supply analysis, explain the likely impact on an economy of an expansionary fiscal policy. [15]
- (c) Critically examine the view that a government should always aim to balance its budget. [15]

4 “Lower wages the key to job-creation”

- (a) Outline the two methods by which unemployment is measured in the UK. [10]
- (b) Analyse the main causes of unemployment in the UK. [15]
- (c) Evaluate the view that long-term unemployment can only be eliminated by reductions in wages and benefits. [15]