

AS Unit 3 Managing The Economy 04 June Mark Scheme

Question 1

(a) (i) Investment is the change in the UK's capital stock. Accept answers such as "the purchase of plant and machinery by firms". Also allow investment in human capital. 2 marks

Answers referring only to investment as a component of AD, or as an injection into the circular flow, or just as new technology, 1 mark.

The graph shows a fall in business investment since 2001 (1 mark).

Identifying fall from £30 bn to just under £27 bn (1 mark), calculating the gap £3.5 bn or the percentage change, just over 10%, (1 mark). Observing the slight upward movement at the end of the series (1 mark) 3 marks

(a) (iii) Allow (2 marks) for a correctly labelled diagram showing a leftwards shift of AD and marking in the old and new level of output, Statement of impact on AD - it falls (1 mark). Correct conclusion about the resulting fall in the equilibrium level of output, (1 mark) possible multiplied contraction or long run effect on AS (1 mark)

A maximum of (3 marks) if the candidate has only analysed a shift in the AS curve. 5 marks

(b) (i) Use of interest rates (1 mark) impact on AD (1 mark). A rise in interest rates may reduce C, I, (X-M). Discussion of at least one transmission mechanisms. A fall in interest rates may increase C, I, (X-M). If both directions considered (4 marks) otherwise (3 marks). Also award: inflation target in terms of RPIX or CPI (1 mark), plus details of 2.5% plus or minus 1%, or 2.0% plus or minus 1% (1 mark). Consideration of a wide range of macro economic variables (1 mark). 6 marks

(b) (ii) The data show fairly robust levels of consumer confidence in 2002 compared to late 2001. (2 marks) Alternatively, a focus on the *fluctuating nature of confidence* (2 marks).

Significance for inflationary pressure (1 mark) appropriate change in interest rate (1 mark).

Reward at least one evaluative point up to (2 marks): other things are not equal (e.g. house prices), significance of C in AD, possible lack of reliability of a confidence survey.

6 marks

(b) (iii) Identifying relevant indicator (1 mark) Explanation of significance for inflation target (2 marks). Candidates may draw from the wide variety indicators considered by the MPC in its monthly meetings e.g. exchange rate, oil prices, unemployment, predicted movement of the RPIX, etc.

Do not allow investment, consumer confidence, stock market prices or house

prices. 3 marks

(c) Allow nine marks for analysis, reserving six marks for evaluation. Share prices have fallen and house prices are rising (1 mark). Both need to be identified for one mark.

Impact of fall in share prices: either effect on wealth/confidence and therefore consumption/investment and therefore AD. (3 marks) To gain the full three marks a transmission mechanism must be fully explained.

Impact of rising house prices: wealth/confidence increases therefore consumption and therefore AD (3 marks). To gain the full three marks a transmission mechanism must be fully explained.

Diagram to show either (or both) of these effects, which must show the old and new equilibrium price level for full marks (2 marks) 9 marks

Evaluation marks should be reserved for candidates who are able to argue more fully. For example:

Assessment of the conflicting influences on AD

House prices are more significant for C than share prices

The importance of elasticity of AS (size of output gap) to the impact on the price level.

Understanding that other things are not equal, e.g. the fiscal position, world prices.

The data is demand side: what is happening on the supply side?

Only award evaluation marks if the argument is directed to the question e.g. do not award a simple statement that "other things are not equal".

6 marks

Allow any two evaluative points up to 3 marks each (or three less developed evaluation points up to 2 marks each).

CAP: Candidates must consider the consequences of the conflicting influences on AD of share prices falling/house prices rising to achieve more than 4 out of 6 for evaluation.

Please write CAP if applied. Total Marks for Question 1: 40

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Question 2

(a) (i) Measures whether people have been actively seeking work and are available to take up a job (2 marks) Also award: reference to number of households surveyed (1 mark), telephone survey (1 mark), the measure includes over 16s etc. (1 mark) 2 marks

(a) (ii) The graph shows a rise in average earnings throughout 2002 (1 mark), identifying some appropriate figures for the earnings growth rate - must be from the correct scale (1 mark) the level of earnings are accelerating towards the end of the graph (1 mark). 3 marks

(a) (iii) Rise in average earnings should increase C in AD. Shift of AD to the right, higher equilibrium level of output (3 marks). AD/AS diagram showing increase in AD and rise in the equilibrium level of output (2 marks). 5 marks

(b) A high exchange rate will tend to make UK exports uncompetitive (1 mark) and imports more attractive (1 mark). Resulting fall in exports (hence output) (1 mark) leading to lost jobs in manufacturing (1 mark). Also award an explanation based on (X-M) in AD. Reserve (2 marks) for at least one evaluative point: other things may not be equal e.g. low productivity may be more significant, the quality of product or reductions in labour costs may compensate, the pound has been strong for some time so surviving firms may be adapted to it, exports may be to high value added markets so unaffected by the exchange rate change, 6 marks

Output per worker (3 marks). If reference only to increasing efficiency of workers (1 mark) Award no marks if candidate confuses productivity with *production*. 3 marks

The narrowing of the productivity gap should reduce the relative cost of production of UK exports, thus raising their competitiveness (3 marks). Consequent rise in exports and fall in imports should improve the current account (3 marks).

Further disaggregation e.g. visibles and invisibles (1 mark) 6 marks

(d) Allow nine marks for analysis, reserving six marks for evaluation. Definition of supply side policy (e.g. shifting AS curve to right or attempt to raise potential output or capacity) (1 mark) Diagram showing shift in AS with the change in real output illustrated (2 marks)

Consideration of specific supply side policies: 2 fully developed 3 marks each or 3 less fully developed 2 marks each.

Extending the scope of the market e.g. privatisation, deregulation

Measures to increase labour market flexibility e.g. union legislation, changes in minimum wage or eligibility for benefits Policies to raise physical or human capital e.g. education

Policies to raise incentives e.g. changes to the tax system or Measures to promote technological change e.g. tax breaks for R& D

Measures to increase resources e.g. relaxation of immigration controls, encouraging FDI Trade liberalisation
9 marks

Evaluation marks should be reserved for candidates who are able to critically examine the use of such policies.

Consideration of the significance of the economy being near to full employment i.e. that expansionary demand management policy can now be effective without adverse inflation (or trade balance) consequences.

Any critical awareness of the potential costs or limitations of the specific supply side policies discussed
6 marks

Allow any two evaluative points up to 3 marks each (or three less developed evaluation points up to 2 marks each).

CAP: Candidates must consider the consequences of the economy being *near to full employment* to achieve more than 4 out of 6 for evaluation

Please write CAP if applied. Total Marks for Question 2: 40