Centre No.						Paper Reference	Surname	Initial(s)
Candidate No.						6 3 5 3 / 0 1	Signature	

Paper Reference(s)

6353/01

Edexcel GCE

Economics

Advanced Subsidiary

Unit 3 – Managing the Economy

Friday 10 June 2005 – Afternoon

Time: 1 hour

Examiner's use only

Team Leader's use only

Question Number	Leave Blank
1	
2	
Total	

Materials required for examination	**Items included with question papers**
Nil	Nil

Instructions to Candidates

In the boxes above, write your centre number, candidate number, your surname, initial(s) and signature.
Check that you have the correct question paper.
Write your answers in the spaces provided in this question paper.
Answer **EITHER** Question 1 **OR** Question 2. Indicate which question you are answering by marking the box (☒). If you change your mind about your answer, put a line through the box (☒) and then indicate your new question with a cross (☒).

Information for Candidates

The marks for individual questions and the parts of questions are shown in round brackets: e.g. **(2)**.
There are 2 questions in this question paper. The total mark for this paper is 40.
There are 20 pages in this question paper. Any blank pages are indicated.

Advice to Candidates

You will be assessed on your ability to organise and present information, ideas, descriptions and arguments clearly and logically, taking into account your use of grammar, punctuation and spelling.
You are advised to spend the first 5 minutes reading the paper. In calculations you are advised to show all the steps in your working.

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Answer EITHER Question 1 OR Question 2.

If you answer Question 1 put a cross in this box ☒.

Question 1 The UK Economy and Changes to the Official Macroeconomic Data

Figure 1

Office for National Statistics Revisions announced October 2003	**Previous Estimate**	**Revised Figure**
Quarterly real GDP growth (second quarter) 2003, %	0.3	0.6
Annual real GDP growth, 2000, %	3.1	3.8
Balance of Payments on Current Account 2002, £bn	-9.6	-19.0

Extract 1

Britain’s top statistician was criticised by MPs this week. But Len Cook, who has run the Office for National Statistics (ONS) for three years, is used to it. His difficulties have arisen because a string of controversial statistical revisions have made the ONS look accident-prone.

There have been a number of eye-catching revisions (see Figure 1) involving an extensive rewriting of recent economic history. However, these changes are necessary as new information comes in. For example, the new second-quarter GDP growth number reflects previously unreported activity in the construction sector. Similarly, the revised current-account balance followed an investigation into tax fraud in trade with the European Union. The revisions to earlier growth estimates mainly reflected improvements in the price indices used to turn nominal GDP into real GDP.

Such revisions are vital if official figures are to reflect what is really going on in the economy. For example, accurate macroeconomic data are essential for interest rate decisions taken by the Monetary Policy Committee in seeking to achieve its inflation target. However, despite these problems, Britain’s record in providing swift and generally reliable economic figures compares favourably with that of many other countries.

(Source of Figure 1 and Extract 1: adapted from *The Economist,* 18 October 2003)

Leave blank

(a) (i) Define *annual real GDP growth*.

(4)

(ii) Explain **two** limitations of using GDP data as an indicator of changes in living standards over time.

(4)

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Leave blank

(b) (i) Explain what is meant by the 'inflation target' (Extract 1, line 14)?

(3)

(ii) Briefly assess the importance of accurate GDP growth figures for the Monetary Policy Committee in seeking to achieve its inflation target.

(4)

Leave blank

(c) (i) Outline **three** main components of the *current account* of the balance of payments.

(6)

M 2 1 5 1 3 A 0 5 2 0

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(ii) With reference to Figure 1, explain whether the current account balance represents a *withdrawal* or an *injection*.

(4)

Leave blank

(d) Using aggregate demand and supply analysis and making reference to the role of the multiplier, evaluate the effectiveness of fiscal policy to achieve a higher rate of economic growth.

Leave blank

Leave blank

(15)

Q1

(Total 40 marks)

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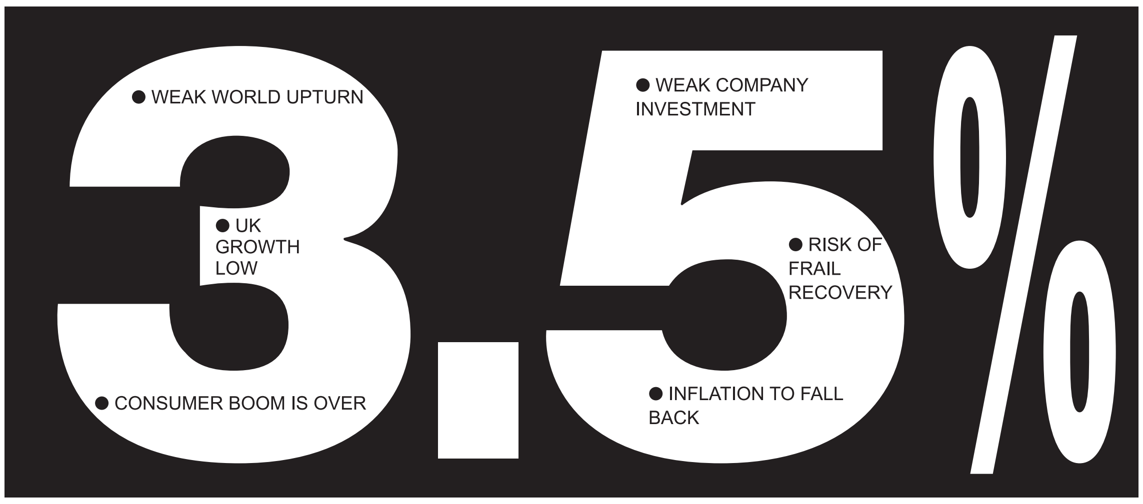
If you answer Question 2 put a cross in this box ☒.

Question 2 **A Cut in Interest Rates by the Bank of England**

Figure 1



Extract 1

British industry was handed a double boost yesterday as the Bank of England's cut in interest rates reduced the cost of borrowing for businesses and improved UK competitiveness overseas. The value of the pound fell after the Monetary Policy Committee (MPC), meeting for the first time with new Governor Mervyn King in the chair, lowered interest rates by a quarter point to a 48-year low of 3.5%.

The rate cut was welcomed by business and industry as offering a much-needed boost that would help to support the faltering economic recovery.

The MPC said that the global upturn was weaker than expected. UK growth had also been weak, consumer demand was slowing, and investment by firms remained low. The rate of inflation was within its target range. With wages under control, inflation was expected to ease further, opening up scope for lower interest rates.

Economists were divided over the chances of a further cut. But many expect that further reductions could take rates to as low as 3 per cent.

(Source of Figure 1 and Extract 1: adapted from *The Times*, 11 July 2003)

Leave blank

(a) (i) Explain what is meant by *inflation*.

(2)

(ii) Define *investment*.

(2)

Leave blank

(iii) Use aggregate demand and supply analysis to explain the likely effects of a fall in company investment on UK prices and real output.

(5)

Leave blank

(iv) Assess the significance of **two** items of information, other than those mentioned in the extract, which the Monetary Policy Committee may have considered before reaching its decision to cut interest rates.

(6)

Leave blank

(b) Explain the likely effect on inflation of the fall in the value of the pound (Extract 1, line 3).

(6)

Leave blank

(c) Outline the likely effects on income distribution of the fall in interest rates.

(4)

Leave blank

(d) Evaluate the effectiveness of monetary policy as a means of achieving price stability in the UK economy.

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(15)

Q2

(Total 40 marks)

TOTAL FOR PAPER: 40 MARKS

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