General Certificate of Education
January 2007
Advanced Level Examination

ECONOMICS **ECN6**
Unit 6 Government Policy, the National and International Economy

Tuesday 30 January 2007 9.00 am to 10.30 am

For this paper you must have: • an 8-page answer book. You may use a calculator.

Time allowed: 1 hour 30 minutes

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 ECN6.
- In **Section A**, answer **all** parts of the question.
- In **Section B**, answer **one** question.

Information
- The maximum mark for this paper is 100.
- The marks for questions are shown in brackets.
- This paper is synoptic. It assesses your understanding of the relationship between the different aspects of Economics.
- You will be marked on your ability to use good English, to organise relevant information clearly and to use specialist vocabulary where appropriate.

Advice
- You are advised to spend approximately 45 minutes on **Section A** and approximately 45 minutes on **Section B**.

SECTION A

Answer **all** parts of this question.

Total for this question: 50 marks

1 UNEMPLOYMENT

Study **Extracts A, B and C,** and then answer **all** parts of Question 1 which follows.

Extract A: UK unemployment and inflation rates, 1981 – 2005

Extract A was a graph.
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Extract B: How beneficial is falling unemployment?

Unemployment can have a number of causes, both on the demand side (e.g. tax rises and higher interest rates) and on the supply side (e.g. higher unemployment benefits and rising oil prices). In recent years, however, unemployment has been falling, bringing clear benefits to both individuals and the economy. For individuals, these include higher incomes, more spending power and reduced welfare dependency; for the economy, these include the prospect of higher output and the potential benefits arising from increased tax revenue and less welfare spending.

Nevertheless, it must be remembered that a fall in unemployment and a rise in employment, resulting from an increase in low-skilled and low-paid jobs, are likely to be less beneficial than the same change occurring due to an increase in high-skilled and high-paid jobs. Also, the impact of falling unemployment on inflation must be gauged. Inflation can present problems for the macroeconomy. Economic growth, unemployment and the balance of payments may deteriorate, given the likely consequent increases in interest rates, falling business and consumer confidence, and the possible damage to competitiveness.

Source: adapted from an article by SUSAN GRANT, *British Economy Survey*, Vol 34 (1), Autumn 2004

Extract C: Can low unemployment be sustained?

At any particular moment, the number of jobs is determined by the level of household consumption, as well as by other components of aggregate demand (AD). AD is influenced by many factors, mostly outside the direct control of policymakers, although monetary policy is vital in seeking to influence it. It is important that policymakers recognise the risk of inflation accelerating as unemployment falls, especially if unemployment begins to be pushed below its natural rate.

It is true that AD will be a key determinant of the number of jobs. However, if low unemployment is to be sustained and the natural rate lowered over time, supply-side improvements to the labour market are crucial. These may include trade union and welfare reforms, improved training, increased flexibility and mobility of labour. The number of jobs will ultimately depend on the available supply of those who are ready and willing to take up jobs, and these supply-side improvements will help in this respect.

Source: adapted from an article by RICHARD LAYARD and STEPHEN NICKELL, *CentrePiece*, Vol 8 (1), Winter 2003

Question 1

(a) Using **Extract A,** compare the changes in the rate of unemployment with the changes in the rate of inflation for the period 1981 to 2005. *(4 marks)*

(b) **Extract B** (lines 1 to 3) refers to demand-side and supply-side causes of unemployment. Explain one demand-side cause **and** one supply-side cause of unemployment. *(6 marks)*

(c) **Extract B** (line 12) suggests that inflation ‘can present problems for the macroeconomy’. Analyse the possible effects of a sustained rise in the rate of inflation. *(10 marks)*

(d) Using the data and your economic knowledge, evaluate the possible effects of falling unemployment on individuals **and** on the performance of an economy. *(30 marks)*

Turn over for the next question

SECTION B

Answer **one** question from this section.

Each question carries 50 marks.

2 The 2005 Budget Statement has forecast that, for the period 2004 to 2010, the average annual borrowing by the UK government (the Public Sector Net Cash Requirement or PSNCR) would be £26 billion.

(a) Explain the likely economic reasons for government borrowing. *(20 marks)*

(b) Evaluate the possible problems for the UK economy of increased government borrowing. *(30 marks)*

3 (a) Explain the possible causes of economic growth. *(20 marks)*

(b) In recent years, eastern European countries, such as Poland, have joined the European Union (EU). New markets and business locations are developing, with resource mobility, including labour, increasing. This expansion of the EU has therefore brought opportunities for growth, jobs and investment to the UK.

Evaluate the possible impact of this expansion of the EU on UK economic performance. *(30 marks)*

4 (a) Explain the possible reasons for changes in the pattern of trade between the UK and the rest of the world. *(20 marks)*

(b) In the years 2000 to 2004, the annual average balance of payments deficit on current account for the UK was £22 billion.

Evaluate the measures which may be taken to deal with a balance of payments deficit on current account. *(30 marks)*

END OF QUESTIONS

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Extract B: Extract from ‘British Economy Survey’ 34/1, © Esterbrooke Enterprises 2004

Extract C: CentrePiece magazine is published three times a year by the Centre for Economic Performance, London School of Economics (http://cep.lse.ac.uk). This extract is taken from the article ‘Full Employment Is Not Just A Dream’ by Richard Layard and Stephen Nickell.