General Certificate of Education
Advanced Level Examination
June 2011

Economics ECON4

Unit 4 The National and International Economy

Thursday 23 June 2011 1.30 pm to 3.30 pm

For this paper you must have:
- an AQA 12-page answer book.

You may use a calculator.

Time allowed
- 2 hours

Instructions
- Use black ink or black 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 ECON4.
- In **Section A**, answer **EITHER** Context 1 **OR** Context 2.
- In **Section B**, answer **one** essay.

Information
- The marks for questions are shown in brackets.
- The maximum mark for this paper is 80.
- There are 40 marks for **Section A** and 40 marks for **Section B**.
- 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
  - organise information clearly
  - use specialist vocabulary where appropriate.

Advice
- You are advised to spend 1 hour on **Section A** and 1 hour on **Section B**.

Section A

Answer **EITHER** Context 1 **OR** Context 2.

EITHER **Total for this context: 40 marks**

Context 1

THE GLOBAL CONTEXT

Study **Extracts A and B,** and then answer **all** parts of Context 1 which follow.

Extract A: Macroeconomic indicators: UK and selected African economies, 2008

Economy	Real GDP growth (% change on previous year)	Real GDP growth per capita (% change on previous year)	Consumer price inflation (%)
UK	0.7	0.1	3.6
Botswana	2.9	1.8	12.6
Ghana	7.3	4.6	16.5
Mozambique	6.8	4.7	10.3
South Africa	3.1	1.3	11.5

Source: official statistics, accessed on 21 December 2009

Extract B: Living standards

Economists can generally agree on the causes of economic growth such as investment, innovation and improvements in productivity. There is greater disagreement over the consequences. An important part of the debate is the impact of economic growth on living standards. The debate has become more complex as measurement of living standards has taken on greater sophistication. GDP per capita (income per head) remains one of the basic measures.

Supporters of continued economic growth point to increased consumption possibilities, greater welfare, more support for the disadvantaged and more resources for health, education and infrastructure.

Opponents of unlimited economic growth point to the rapid depletion of exhaustible natural resources and environmental deterioration. The Copenhagen Summit of December 2009 brought the latter issue into sharp focus once again.

Various indices, such as the Human Development Index, incorporate a number of factors into their calculations in order to give as comprehensive a view of living standards as possible and to allow more accurate international comparisons. Factors include life expectancy, infant mortality and nutritional levels.

The Legatum Institute publishes a global survey annually, popularly known as a ‘prosperity index’. It brings together data on, for example, economic growth, welfare, happiness, crime and healthcare. This data is then used to rank countries.

The 2009 index ranked 104 countries. The UK was placed 12th (its best position for three years). Low scores for key public services kept it out of the top ten. All African countries were in the bottom half of the index.

However, the continent of Africa is undergoing economic change. The World Bank points to a rapid transformation in some countries. Mozambique has seen annual average growth of 8% in the last decade, Kenya has emerged as a major global supplier of cut flowers and Rwanda is developing tourism very successfully. While Lesotho is developing its clothing industry, Ethiopia is starting to manufacture footwear. Can we look to Africa for the next wave of 'emerging economies', to follow India and China? In 2009, Africa as a whole had the world's third highest rate of growth behind India and China. Africa's role as a major supplier of raw materials to China also illustrates its increasing economic links with the rest of the world.

As a result of this economic change, living standards in Africa will no doubt improve. Additionally, the living standards of developed countries, including the UK, will be affected by economic growth in Africa. Export markets for both goods and services will strengthen, as will investment opportunities, and natural resources will become more accessible.

But how long before the UK faces stiff competition from Africa in agriculture, manufacturing and service activities? No one can accurately predict the impact on the UK economy but the careful monitoring of developments in Africa will become increasingly necessary.

Source: various sources, 2010

0 1 Using **Extract A**, identify **two** significant features of the macroeconomic indicators shown for 2008. *(5 marks)*

0 2 **Extract B** (line 1) argues: 'Economists can generally agree on the causes of economic growth'.

Explain the term 'economic growth' **and** analyse **two** ways in which economic growth can be achieved. *(10 marks)*

0 3 **Extract B** (lines 33 – 34) argues that 'the living standards of developed countries, including the UK, will be affected by economic growth in Africa'.

Using the data and your economic knowledge, assess the view that living standards in the UK are likely to benefit from sustained economic growth in the economies of Africa. *(25 marks)*

Do **not** answer Context 2 if you have answered Context 1.

OR **Total for this context: 40 marks**

Context 2

THE EUROPEAN UNION CONTEXT

Study **Extracts C and D,** and then answer **all** parts of Context 2 which follow.

Extract C: Government budget balances (% of GDP): selected EU economies, 2007 to 2010

Country	**2007**	**2008**	**2009** *forecast*	**2010** *forecast*
France	−2.7	−3.4	−7.0	−7.1
Greece	−3.6	−5.0	−12.5	−12.7
Ireland	+0.1	−7.3	−12.1	−13.3
Italy	−1.5	−2.7	−5.6	−5.6
UK	−2.6	−5.1	−11.6	−13.2

Source: official statistics, accessed on 21 December 2009

Extract D: Is EU unity threatened?

Europe, and indeed much of the world, was shaken by the depth of the economic downturn from 2008. Many countries, including the UK, saw the solution to be a return to Keynesian economics and, therefore, tolerance of large budget deficits. This was coupled with significant monetary expansion, so that, in the UK for example, the Bank of England Bank Rate was cut to 0.5% in 2009, accompanied by a policy of 'quantitative easing' (increases in the money supply).

The UK pressed other EU governments to embark on fiscal expansion. Not all shared the UK's enthusiasm and, at best, wanted only a much more modest fiscal stimulus than was the case in the UK. However, events sometimes overtook such wishes. Ironically, given the scale of the UK fiscal stimulus, until the latter part of 2009 the UK was the only major economy to remain in recession. This may reflect the greater significance of the housing and financial sectors in the UK compared to other EU countries.

The fiscal position of many EU countries has given rise to concern. Italy, for example, now has a national debt (the total outstanding debt of central government) of around 120% of GDP, even though its annual budget deficit is not exceptionally large. Some countries have shown a greater determination than Italy to cut their deficits. In December 2009, for example, Ireland announced sharp cuts in public sector wages. But it is certainly not just Italy which has shown complacency. The EU's Stability and Growth Pact limits annual borrowing to 3% of GDP. EU governments are under increasing pressure to return to this target by 2014.

The short- to medium-term benefits of fiscal expansion during downturns cannot be denied. Government spending can initiate a powerful stimulus to an economy through the multiplier process. Aggregate demand therefore rises. The UK Pre-Budget Report put government spending at £676 billion. Tax cuts will give households more spending power. Coupled with cheap credit and retail price discounts, recovery can therefore be helped through increased consumption.

However, the impact of increased government borrowing arising from budget deficits across the EU is of concern amongst some economists. It may eventually force the authorities to increase interest rates, lead to ‘crowding-out’ of private sector activity and make public spending cuts and tax increases an inevitability. In the UK, for example, a VAT rate of 17.5% was restored in January 2010 following a temporary cut to 15%. Equally, the 2009 Pre-Budget Report announced an increase in National Insurance contributions.

The problem in trying to assess the impact of fiscal expansion is, of course, not knowing what might have happened without it. Certainly, some economists are quick to attribute the end of recession in France and Germany in 2009 to such fiscal loosening. Indeed, it is difficult to argue that, for any country in the EU, economic growth and employment cannot be beneficial to some extent at a time when business and consumer confidence are both at a low level.

Whether such a policy eventually causes inflation to make an unwelcome return remains to be seen. At that point, EU members may experience a greater urgency to balance budgets and reduce monetary expansion.

Source: various sources, 2010

0 4 Using **Extract C**, identify **two** significant features of the government budget balances shown for the period 2007 to 2010. *(5 marks)*

0 5 **Extract D** (lines 22 – 23) argues that government spending ‘can initiate a powerful stimulus to an economy through the multiplier process’.

Explain ‘the multiplier process’ **and** analyse its possible impact on an economy’s unemployment **and** economic growth. *(10 marks)*

0 6 **Extract D** (lines 27 – 28) states that ‘the impact of the increased government borrowing arising from budget deficits across the EU is of concern amongst some economists’.

Using the data and your economic knowledge, assess the impact on the UK economy of increased government borrowing by EU governments. *(25 marks)*

Turn over for the next question

Section B

Answer **one** essay from this section.

Each essay carries 40 marks.

EITHER

Essay 1

'The UK economy has recently been in the grip of its worst recession for 60 years.'

0 7 Explain possible reasons for an economy moving from a period of prosperity to one of recession. *(15 marks)*

0 8 Assess the contribution which supply-side reforms might make in helping avoid major recessions. *(25 marks)*

OR

Essay 2

'Inflation needs to be avoided at all costs but it is nowhere near as damaging to an economy as deflation.'

0 9 Explain how inflation is measured in the UK through indices such as the Retail Prices Index (RPI) and the Consumer Prices Index (CPI). *(15 marks)*

1 0 To what extent might it be argued that inflation is preferable to deflation? *(25 marks)*

OR

Essay 3

An economy which is enjoying rapid economic growth experiences a significant rise in the external value of its currency within a floating exchange rate system.

1 1 Explain the factors which may lead to a rise in the exchange rate of a currency within a floating exchange rate system. *(15 marks)*

1 2 Evaluate the possible macroeconomic consequences for an economy of a rise in the exchange rate of its currency. *(25 marks)*

END OF QUESTIONS

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