

GCE

Economics

Unit **F582**: The National and International Economy

Advanced Subsidiary GCE

Mark Scheme for June 2015

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All examiners are instructed that alternative correct answers and unexpected approaches in candidates' scripts must be given marks that fairly reflect the relevant knowledge and skills demonstrated.

Mark schemes should be read in conjunction with the published question papers and the report on the examination.

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Annotations

Please annotate **every** response, even if no credit is given.

| Annotation | Meaning |
|---|---------------------------|
|  | Tick |
|  | Cross |
|  | Unclear |
| BOD | Benefit of doubt |
| C | Comment |
| EE | Effective evaluation |
| L1 | Level 1 |
| L2 | Level 2 |
| L3 | Level 3 |
| L4 | Level 4 |
| NAQ | Not answered question |
| SEEN | Noted but no credit given |
| TV | Too vague |
| REP | Repeat |

Highlighting is also available to highlight any particular points on the script.

'SEEN' to be inserted on every blank page.

| Question | | Answer | Mark | Guidance |
|----------|-----|--|------|--|
| 1 | (a) | <p>Define the term 'price level'.</p> <p>Two marks for: the average prices/general level of prices of products in an economy (or country)/ average prices of products produced in an economy. One mark for: average prices/general prices/prices in general/prices in the economy/where AD=AS.</p> | 2 | <p>Up to two marks.</p> <p>Note: not accepting value, cost or a micro approach.</p> |
| | (b) | <p>Describe one reason why a consumer prices index may provide an inaccurate estimate of inflation.</p> <p>One mark for identification of a reason, e.g.:</p> <ul style="list-style-type: none"> • people moving away from products that have become relatively more expensive • does not include price of housing (although CPIH does include owner occupiers' housing costs) • buying products at cheaper outlets • improvements in quality • weights not reflecting purchases • basket not representative/only a selection of products included • purchases being made in the informal economy • there may be sampling errors • there is a time delay <p>One mark for explanation e.g.:</p> <ul style="list-style-type: none"> • consumers may switch to relatively cheaper versions of some products • people spend a relatively large proportion of their income on housing • there may be short-term changes in the outlets from which people may buy • a rise in the quality of products will mean the same products are not being compared | 2 | <p>One mark for a correct identification, plus a further one mark for a description.</p> <p>Must be based on the inflation rate affecting the whole economy. Not giving CPI may not reflect price rises for different groups and in different regions.</p> |

| Question | | | Answer | Mark | Guidance |
|----------|-----|-----|--|------|---|
| | | | <ul style="list-style-type: none"> weights are revised each year – the delay may mean that the products do not reflect what is now being purchased sampling errors may be included in the Integrated Household Survey/Family Expenditure Survey or sampling errors may arise due to inaccurate information being given to the people carrying out the survey prices in the informal economy may be significantly different to those in the formal economy by the time the figure is published, it may not reflect the inflation that people are experiencing | | |
| 2 | (a) | (i) | <p>Using information in the case study, calculate in US\$ by how much spending on health care exceeded spending on education in Argentina in 2011.</p> <p>Two marks for: US\$20.25bn.</p> <p>One mark for :</p> <ul style="list-style-type: none"> correct working: i.e. US\$42.75bn – US\$22.50bn <p>or for</p> <ul style="list-style-type: none"> spending on health care US\$42.75bn and spending on education US\$22.50bn <p>of for</p> <ul style="list-style-type: none"> US\$20.25m/US\$20.25. | 2 | <p>Up to two marks.</p> <p>Need \$ sign, bn and correct figure for both marks</p> |

| Question | Answer | Mark | Guidance |
|----------|---|------|---|
| | <p>(ii) Using information in the case study, explain two reasons why government spending in Argentina may increase in the future.</p> <p>One mark each for each of two relevant reasons identified:</p> <ul style="list-style-type: none"> • in an attempt to reduce unemployment • to promote economic growth • to cope with an ageing population • Increased ability to spend more due to higher tax revenue • to reduce the current account deficit • to improve living standards • to increase investment • to cut costs of production • to keep pace with inflation <p>One mark each for each of two relevant explanations:</p> <ul style="list-style-type: none"> • higher government spending may reduce cyclical/structural unemployment • the government may engage in expansionary fiscal policy to raise aggregate demand and so increase output. • as people live longer there will be more demand for health care and the cost of state pensions will rise. • higher government spending on education may raise the quality of products produced • continued economic growth/lower unemployment/higher wage rates will increase incomes and spending which, in turn, will raise direct and indirect tax revenue which can be spent • a government may increase its spending on, for example, subsidies to domestic firms to increase their international price competitiveness | 4 | <p>One mark for each correct identification, up to a maximum of two identifications, plus a further one mark for each of two explanations.</p> <p>Note: explanation must be linked to reason e.g. no marks for 'may spend more on education' if not linked to e.g. promoting economic growth.</p> |

| Question | Answer | Mark | Guidance |
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| | <ul style="list-style-type: none"> • to raise living standards, a government may increase its spending on health care for example • to encourage more investment, a government may directly spend on capital goods or provide subsidies to firms • to cut costs of production a government may finance training or provide subsidies for capital equipment • rising prices will increase the cost of government purchases | | |
| (b) | <p>Comment on whether higher government spending will always increase inflation.</p> <p>Up to three marks for analysis:</p> <p>Why it might:</p> <ul style="list-style-type: none"> • government spending is a component of aggregate demand $(C+I+G+(X-M))$/injection into the circular flow • higher government spending will increase aggregate demand/result in more money in the circular flow • may result in a multiplier effect • higher aggregate demand may result in demand-pull inflation <p>Up to three marks for evaluation:</p> <ul style="list-style-type: none"> • some forms of government spending may raise both aggregate demand and aggregate supply • higher spending on education and/or health care may raise labour productivity • higher aggregate supply can reduce inflationary pressure • it will depend on the initial state of economic activity • it will depend on whether it is financed by higher taxation | 6 | <p>Note: a candidate cannot access the evaluation marks without any analytical underpinning clearly linked to the question.</p> <p>Up to three marks may be gained for one evaluative point well made, e.g. if the government increases its spending on training, aggregate supply may rise in line with aggregate demand, thereby ensuring that it does not cause a rise in the price level.</p> <p>Note: if second bullet point mark has not been awarded a mark can be given for a diagram that shows AD shifting to the right.</p> <p>Note: The question is concerning whether it will increase inflation and not by how much. Therefore, no marks for just stating that it will depend on the size or duration of the increase in government spending.</p> |

| Question | | Answer | Mark | Guidance |
|----------|-----|--|------|---|
| | | <ul style="list-style-type: none"> • if the higher AD is matched by higher AS, there may be no impact on inflation • if the higher spending raises aggregate supply by more than it raises aggregate demand, it may reduce inflation | | |
| 3 | (a) | <p>Using Fig. 1, compare the trend in unemployment rates of Argentina and the USA between 2007 and 2012.</p> <p>Indicative content:</p> <ul style="list-style-type: none"> • Argentina's unemployment rate has a downward trend • USA's unemployment rate rose over the period • Argentina's unemployment rate starts above that of the USA and finishes below that of the USA • There is a greater change in the unemployment rate of the USA • the USA experiences an upwards trend between 2007 and 2009 and then a downward trend • Argentina's unemployment fluctuated between 2007-9 and then had a downward trend • Both countries experience a downward trend after 2009/10 • The decrease after 2009 is at a similar rate in both countries • For most of the period USA unemployment rate is higher than Argentina's/from 2009 USA unemployment is higher than Argentina's (vice versa for Argentina's lower than USA) • Over the period, the range of unemployment rates has been greater in the USA/more volatility in unemployment | 4 | <p>Allow four marks for four comparisons but also allow a mark for development of one comparison, e.g.</p> <ul style="list-style-type: none"> • Argentina's unemployment rate fell by approximately 1.8% points or 21.18% over the period. • USA's unemployment rate rose by approximately 3.7% points or 80.43% over the period. • Argentina's unemployment rate is approximately 3.9% points or 84.78% higher than that of the USA at the start of the period. • USA' unemployment rate is approximately 1.6% points or 23.88% higher than that of Argentina's at the end of the period. <p>So a candidate may gain full marks by making four separate comparisons or developing two comparisons.</p> <p>Note: do not accept a pedestrian approach i.e. a year by year approach.</p> |

| Question | Answer | Mark | Guidance |
|----------|--|------|---|
| (b) | <p>Comment on whether an increase in employment in a country will increase investment in that country.</p> <p>Up to three marks for analysis.</p> <ul style="list-style-type: none"> • higher employment may increase incomes • higher incomes may increase consumer expenditure/people spend more • higher consumer expenditure/higher demand for goods and services may encourage firms to expand their output • any resulting higher consumer expenditure/economic growth may attract FDI • higher consumer expenditure may increase profits • higher profits will provide funds for investment/increase the incentive to invest • to increase output firms may increase their spending on capital goods • higher employment may push up wage costs • higher wage costs may encourage firms to replace workers with capital goods • Higher employment may increase firms' confidence • Up to three marks for evaluation • firms may have spare capacity so they will be able to produce more without undertaking investment • firms may lack confidence • firms may wait to see if demand continues high • higher incomes may not result in increased spending on domestically produced products. • If the higher employment does raise wage rates this may discourage FDI • other factors influence investment | 6 | <p>Note: a candidate cannot access the evaluation marks without any analytical underpinning clearly linked to the question.</p> <p>Up to three marks for one evaluative point well developed e.g. firms may have unused or underused capital equipment which can be brought into use if aggregate demand increases. As a result firms may not purchase new capital equipment.</p> |

| Question | | Answer | Mark | Guidance |
|----------|-----|--|------|---|
| 4 | | <p>Explain why a government would want to prevent a decrease in aggregate supply.</p> <ul style="list-style-type: none"> • it would reduce productive capacity (1) • lower real GDP/reduce economic growth (1) • raise the price level/cause inflation (1) • it may lower employment/raise unemployment (1) <p>One mark for the development of any of the above points linked to why a government would want to prevent this.</p> | 2 | <p>Up to two marks.</p> <p>One mark for each correct point up to a maximum of two</p> <p>OR</p> <p>Two marks for one point developed</p> |
| 5 | (a) | <p>Define the term 'protectionism'.</p> <p>Two marks for: protection of domestic industries from foreign competition.</p> <p>One mark for: protect domestic industries/trade restrictions/barriers to trade/reduce imports.</p> | 2 | <p>Up to two marks.</p> <p>It is one mark for who is being protected (domestic industries/products) and what they are being protected from (i.e. foreign competition/imports)</p> |
| | (b) | <p>State three non-tariff methods of protection.</p> <ul style="list-style-type: none"> • quotas • embargoes/sanctions • voluntary export restraint (VER) • red tape/quality standards/regulation/legislation • subsidies • competitive devaluation | 3 | <p>One mark for each correct identification up to a maximum of three identifications.</p> <p>Accept: requiring buyers of books having to turn up at airports.</p> |

| Question | | Answer | Mark | Guidance |
|----------|-----|---|------|---|
| 6 | (a) | <p>State three components of the current account of the balance of payments.</p> <ul style="list-style-type: none"> • trade in goods • trade in services • income/primary income • current transfers/secondary income | 3 | <p>One mark for each correct identification up to a maximum of three identifications. Accept:</p> <ul style="list-style-type: none"> • investment income or profit, interest and dividends for income • transfers, net transfers of transfer payments and receipts for transfers • services or invisibles for trade in services • goods or visibles for trade in goods <p>Note: 1 mark in total for exports and imports (net exports) or trade balance.</p> <p>No marks for an individual item in a component e.g. banking, tourism – too vague</p> |
| | (b) | <p>Analyse two causes of an increase in a current account deficit of the balance of payments.</p> <p>One mark each for each of two causes identified:</p> <ul style="list-style-type: none"> • a higher exchange rate • higher costs of production • a reduction in the quality of domestically produced products • a rise in domestic prices/inflation • fall in incomes abroad • higher incomes at home • an increase in a net outflow of income arising from previous investment in other countries • a reduction in trade restrictions | 6 | <p>One mark for each correct identification up to a maximum of two identifications, plus up to a further two marks for each of two analytical responses.</p> <p>NB further marks can only be awarded for analysis.</p> <p>Note: a maximum of two marks for each cause that is answered in wholly static terms e.g. a high exchange rate means high export prices/low import prices and so low demand for exports/high demand for imports.</p> <p>Note: an answer that has a static element but is largely dynamic e.g. a high exchange rate increases export prices and so lowers demand for export/increases demand for imports can gain 3 marks</p> |

| Question | Answer | Mark | Guidance |
|----------|--|------|--|
| | <p>Up to two marks each for the analysis of two causes:</p> <ul style="list-style-type: none"> • higher exchange would raise export prices and lower import prices. This may reduce demand for exports and increase demand for imports • higher costs of production will mean that export prices rise relative to import prices. This may mean demand for exports falls and demand for imports increases • a reduction in quality will reduce international competitive-ness. It will discourage foreigners from buying exports and will encourage domestic citizens to purchase imports. • lower incomes abroad will reduce the ability of foreign citizens to purchase all products. Some of these products may be the country's exports • if the country's prices are increasing/there is inflation its products may become less internationally price competitive which could lead to an increase in spending on imports and a reduction in export revenue • higher incomes at home are likely to increase consumer expenditure. Some of this may be spent on imports. In addition, domestic firms may divert some products from the export to the home market • if foreign direct investment and portfolio investment into the country have exceeded the outflow of investment in the past, income in the form of profit, interest and dividends may be flowing out of the country now • a reduction in trade restrictions will worsen the current account position if e.g. removing a tariff on imports leads to a rise in expenditure on imports. | | <p>Note: a good answer could gain full marks by analysing the impact of a cause on exports and imports or just exports OR imports.</p> <p>Note: a maximum of 1 mark for a rise in imports and/or fall in exports.</p> <p>Note: remember to accept relevant causes which relate to any part of the current account.</p> |

| Question | | Answer | Marks | Guidance | |
|----------|--|--|-------|---|--|
| | | | | Content | Levels of response |
| 7 | | <p>Discuss whether a reduction in taxation will always increase a country's economic growth rate.</p> <p>This question requires a discussion of the possible effectiveness of a reduction in taxation in increasing a country's economic growth rate. Answers may consider how households and firms will respond to such a reduction, which types of tax are cut and possible adverse side effects.</p> <p>A reduction in taxation may increase the disposable income of households and firms. This may result in a rise in consumer expenditure and investment. The resulting increase in AD may lead to a rise in real GDP/actual economic growth. Lower taxation may increase the incentive to work and so increase output. It may also shift out the AS curve by attracting foreign direct investment. Answers should evaluate whether such a reduction will be effective in increasing a country's economic growth rate.</p> <p>Examples of possible Level 4 answers:</p> <ul style="list-style-type: none"> • a reduction in income tax may have little impact on consumer expenditure and so on aggregate demand if workers are pessimistic about the future and save the extra disposable income. • a reduction in indirect tax may not have much effect if firms experience a rise in other costs of production. • a reduction in taxation may increase AD but this may not occur if government spending is also cut | 18 | <p>Note: a maximum of 8 marks for an answer which discusses the effect of an increase in taxation on a country's economic growth rate.</p> <p>If awarding Level 4, indicate lower band Level 4 with L4 and higher band with EE.</p> <p>For 16 – 18 marks, a discussion must have some depth to the discussion on the factors influencing whether the reduction will always be effective.</p> <p>For 13 – 15 marks, a discussion which does evaluate in terms of the effectiveness linked to the impact on aggregate demand.</p> <p>Complex ideas have been expressed clearly and fluently, using a style of writing appropriate to complex subject matter. Sentences and paragraphs, constantly relevant, have been well structured, using appropriate terminology. There may be few, if any errors of spelling, punctuation and grammar.</p> | <p>Level 4 [13 – 18]</p> <p>For a discussion of whether a reduction in taxation will increase a country's economic growth rate.</p> <p>Note: evaluation must be supported by relevant analysis.</p> <p>For 16 – 18 marks, the discussion must:</p> <ul style="list-style-type: none"> • make supported judgements as to why a reduction in taxation might be expected to increase the economic growth rate but why this may not always be the case • must have at least two well developed, relevant evaluative points • must be based on strong and relevant analysis and evaluation. <p>For 13 – 15 marks, the discussion:</p> <ul style="list-style-type: none"> • must be two-sided • must discuss the effects of a reduction in taxation on either AD or AS and link these to the economic growth rate • must be based on preceding analysis which must focus on the actual question set. |

| Question | | Answer | Marks | Guidance | |
|----------|--|--|-------|--|--|
| | | | | Content | Levels of response |
| | | <ul style="list-style-type: none"> the effect will depend on what the tax revenue was used for. If less taxation results in less spending on education and health care, aggregate supply may decrease and so potential economic growth may be reduced higher consumer spending resulting from a reduction in taxation may go on imports, possibly creating economic growth abroad rather than at home higher aggregate demand may not increase real GDP if the economy is already operating at full capacity and does not increase aggregate supply a cut in the lower bands of income tax may have more impact on consumer spending as the poor spend a higher proportion of their income a cut in income tax may encourage people to work fewer hours. This would reduce aggregate supply. A reduction in tariffs may increase spending on imports, lower aggregate demand and reduce economic growth <p>Answers should analyse the effects of such a reduction.</p> <p>Examples of possible Level 3 answers:</p> <ul style="list-style-type: none"> a decrease in income tax rates or coverage will increase disposable income. Higher disposable income may increase consumer expenditure which will raise AD. Higher AD may increase real GDP | | <p>Show where Level 3 has been awarded with L3.</p> <p>If awarding Level 3, 2 or 1 show where the highest level has been gained.</p> | <p>Level 3 [9 – 12] For an analysis of how a reduction in taxation may increase real GDP and/or productive potential.</p> <p>Note: an AD/AS diagram may be rewarded if it is explained.</p> |

| Question | Answer | Marks | Guidance | |
|----------|---|-------|--|--|
| | | | Content | Levels of response |
| | <ul style="list-style-type: none"> • a decrease in corporate tax rates may increase the ability and willingness of firms to invest. Higher investment may increase both AD and AS. Higher AD and AS may raise real GDP and potential economic growth • lower direct tax rates may attract workers and investment from abroad. If so AD and AS will increase • lower income tax may increase the incentive to work. This may lead to both higher output and higher AD • lower indirect taxes would reduce costs of production and so increase AS, raising productive potential • lower taxes on imports may reduce firms' costs of production which may increase AS, raising productive potential • lower taxes may reduce government expenditure as less tax revenue so aggregate demand may decrease reducing real GDP. <p>Answers should recognise some of the effects of a reduction in taxation. Examples of possible Level 2 answers:</p> <ul style="list-style-type: none"> • it may increase consumer expenditure/AD • it may increase investment/AS • it may increase the incentive to work • it may reduce government spending • it may increase imports | | <p>For 11 + marks, there must be some depth of analysis, covering two or three effects.</p> <p>For 9 – 10 marks, there may be some lack of depth, covering just one or two effects in sufficient detail.</p> <p>Relatively straightforward ideas have been expressed with clarity and fluency. Arguments are generally relevant, though some may stray from the point of the question. There will be some errors of spelling, punctuation and grammar and these are unlikely to be intrusive or obscure meaning.</p> <p>For 7 – 8 marks, the answer should recognise at least three or four effects.</p> <p>For 5 – 6 marks, the answer should recognise one or two effects.</p> | <p>The analysis must focus on the actual question set bringing out the effects on the economy of a reduction in taxation.</p> <p>For 11 – 12 marks, there should be analysis of three effects or well developed analysis of two effects.</p> <p>For 9 – 10 marks, there should be undeveloped analysis of two effects or somewhat undeveloped analysis of one effect.</p> <p>Note: analysis may be from either side.</p> <p>Level 2 [5 – 8] For an application of knowledge and understanding of the effect of a reduction in taxation.</p> <p>To gain 8 marks, there should be identification of four effects of the reduction in taxation, or two effects with a hint of explanation</p> |

| Question | | Answer | Marks | Guidance | |
|----------|--|---|-------|---|---|
| | | | | Content | Levels of response |
| | | <ul style="list-style-type: none"> • a relevant diagram showing either AD or AS shifting to the right and real GDP/national output increasing • unsubstantiated statements on likely outcome <p>These answers will show awareness of the terms. Examples of Level 1 answers:</p> <ul style="list-style-type: none"> • economic growth involves an increase in real GDP • economic growth involves an increase in productive potential • economic growth may be caused by an increase in aggregate demand • economic growth may be caused by an increase in aggregate supply • taxation is a payment to the government. • direct taxes are taxes on income • indirect taxes are taxes are spending • the burden of an indirect tax can be passed on to the consumer | | <p>Some ideas have been expressed in an appropriate context. There are likely to be errors of spelling, punctuation and grammar, some of which may be noticeable and intrusive.</p> <p>For 3 – 4 marks, there will be good knowledge of economic growth and/or taxation.</p> <p>For 1 – 2 marks there will be some awareness of the meaning of economic growth or taxation.</p> <p>Some simple ideas have been expressed. There will be errors of spelling, punctuation and grammar that will be noticeable and intrusive. Writing may lack legibility.</p> | <p>on at least one of these.</p> <p>To gain 7 marks, there should be identification of three effects or at least one with a hint of explanation on this.</p> <p>To gain 6 marks, there needs to be identification of two effects.</p> <p>To gain 5 marks, there needs to be identification of one effect.</p> <p>Level 1 [1 – 4] For knowledge and understanding of economic growth and/or taxation.</p> |

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