

# AS and A LEVEL

## *Delivery Guide*

H040/H460

# ***ECONOMICS***

Theme: Macroeconomics

Application of  
policy instruments

March 2015



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# Introduction

Delivery guides are designed to represent a body of knowledge about teaching a particular topic and contain:

- Content: A clear outline of the content covered by the delivery guide;
- Thinking Conceptually: Expert guidance on the key concepts involved, common difficulties students may have, approaches to teaching that can help students understand these concepts and how this topic links conceptually to other areas of the subject;
- Thinking Contextually: A range of suggested teaching activities using a variety of themes so that different activities can be selected which best suit particular classes, learning styles or teaching approaches.

If you have any feedback on this Delivery Guide or suggestions for other resources you would like OCR to develop, please email [resourcesfeedback@ocr.org.uk](mailto:resourcesfeedback@ocr.org.uk).

## KEY



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A Level content only



# Curriculum Content: Fiscal policy

## Macroeconomics: The application of policy instruments > Fiscal policy

- explain what is meant by the government budget
- identify the main sources of tax revenue and government expenditure in the UK economy
- distinguish between current and capital government expenditure
- distinguish between progressive, proportional and regressive taxation
- calculate average and marginal tax rates\*
- distinguish between direct and indirect taxation
- explain the features of a 'good' tax
- evaluate the relationship between the tax rate and tax revenue, including consideration of the Laffer Curve\*
- evaluate the advantages and disadvantages of a flat rate tax system
- explain what is meant by the budget position/fiscal stance
- distinguish between a budget surplus, a budget deficit and a balanced budget
- distinguish between the cyclical budget position and the structural budget position
- distinguish between an overall budget position and the budget position on current expenditure
- distinguish between a budget deficit and government debt
- explain how budget deficits can be financed
- evaluate policies to correct a budget surplus or deficit
- evaluate the consequences of government debt
- explain how automatic stabilisers work to achieve economic stability\*
- explain how discretionary fiscal policy may be used to improve macroeconomic performance
- explain how crowding out and crowding in can occur as a result of fiscal policy\*
- evaluate the effectiveness of using fiscal policy to achieve the government's macroeconomic objectives
- explain how fiscal rules can influence the behaviour of economic agents
- evaluate the effectiveness of fiscal rules.

**NB \* A-Level only**



# Thinking Conceptually: Fiscal policy

***Policies that aim to influence an economy's aggregate demand are designed either to stabilise the level of output and employment or to***

***stabilise the price level. The prime focus is thus on the short-run position of the macroeconomy. The two major categories of policy are fiscal policy and monetary policy. The term fiscal policy covers a range of policy measures that affect government expenditures and revenues. For example, an expansionary fiscal policy would be seen as an increase in government spending (or reduction in taxes) that shifts the aggregate demand curve to the right.***

## **Approaches to teaching the content**

The range of macroeconomic policy objectives, such as economic growth, full employment, the control of inflation, reaching equilibrium on the current account or the balance of payments, concerns about the environment or the distribution of income could be recapitulated. Then students could start naming and discussing various actions by the government which could then be grouped in the different categories of macroeconomic policies.

## **Common misconceptions or difficulties students may have**

Clarification may be needed on consumer expenditure and what it includes, i.e. it doesn't include welfare payments, as this would be double counting.

Students can confuse government budget deficit with a current account deficit.

**A Level  
only**

They may misunderstand the concept of national debt; it may need to be clarified that it doesn't include consumer credit debt or household debt such as mortgage debt.

The effect of fiscal policy on government's macroeconomic objectives gives students to the opportunity to discuss the demand side and supply side effects. However students must be clear on these and how changes in fiscal policy can affect short run and long run supply.

The idea of crowding out and crowding in can be challenging for many students.

## **Conceptual links to other areas of the specification – useful ways to approach this topic to set students up for topics later in the course**

The most obvious link is with monetary and supply-side policies, but fiscal policy also links to the key performance indicators: economic growth, unemployment, inflation, balance of payments as well as inequality and income distribution.

It is useful to remind students that the intention of policy makers is to put into place measures which will improve economic performance of an economy from both a micro and macro perspective.

It can be useful to get students to make these conceptual links themselves (a good revision exercise). This could be via a mind map: put fiscal policy in the centre of a page and then branch off with the links to other concepts such as unemployment or economic growth.



# Thinking Contextually: Fiscal policy

## ACTIVITIES

Fiscal policy has been high on the media's agenda since the financial crisis of 2007/08 and there is a plethora of resources on websites such as the BBC or the Guardian. In addition to the UK, the USA, Euro-zone and other countries such as Japan and China offer an international dimension to this area of macroeconomic policy instruments.

Students could look into the differing fiscal policy measures used by national governments and the consequences for rates of economic growth. China in particular offers an interesting perspective, looking at the mounting debt levels in an emerging economy with a different economic and political structure.

Different schools of thought can also be drawn upon, such as the Keynesian belief that a government should engage in deficit spending.

Discussion can also be had around the implications for countries in the Euro-zone compared to those just in the European Union. The austerity measures employed by those within the Euro-zone in order to bring down their debt levels provide both a chance to explore the concept of a fiscal straight jacket and the implications of opting to join a monetary union.



# Thinking Contextually: Fiscal policy

Activities	Resources
<p><b>Britain's public finances</b></p> <p>Even though this is a little dated now (the lecture was given in 2011) it is a great introduction to Fiscal Policy delivered by Robert Chote, Head of The Office of Budget Responsibility.</p> <p><a href="http://www.res.org.uk/view/res2011AnnualPublicLecture.html">http://www.res.org.uk/view/res2011AnnualPublicLecture.html</a></p> <p>The lecture starts at about 7 minutes into the webcast and lasts for approximately one hour. It's advisable to give students information to listen out for, such as the main sources of government revenue, the difference between progressive and regressive taxation or the difference between current and capital government expenditure.</p>	<p><a href="#">▶ Click here</a></p>
<p><b>Tax rate and tax revenue:</b> Propose a hike in the value of the top rate of tax, perhaps to 60% or even 80%. Ask students vote whether they think this would increase or decrease the tax revenue taken by the treasury. They should do this by going to either end of the room, one end of increase and the other for decrease. Count the number who voted each way. Next, having provided them with resources that discuss both the implications of a tax hike and the Laffer curve, ask them to set out the arguments for and against. Take the vote again and see how much the numbers have changed. Ask students in both camps for their main argument for their opinion and then ask for their main argument against the other opinion to create a mini debate. Ask whether any one changed their opinion and what influenced this.</p> <p><a href="http://www.telegraph.co.uk/finance/comment/jeremy-warner/10887847/Europe-is-jealous-as-Britain-resurrects-the-Laffer-Curve.html">http://www.telegraph.co.uk/finance/comment/jeremy-warner/10887847/Europe-is-jealous-as-Britain-resurrects-the-Laffer-Curve.html</a></p> <p><a href="http://www.ifs.org.uk/publications/7066">http://www.ifs.org.uk/publications/7066</a> Duration: 25 minutes</p>	<p><b>A Level only</b></p> <p><a href="#">▶ Click here</a></p> <p><a href="#">▶ Click here</a></p>



# Thinking Contextually: Fiscal policy

Activities	Resources
<p><b>Laffer curve:</b> Provide the variables (tax rate and tax revenue) and students draw them on to their mini white boards (or paper). Ask them to draw what they think the relationship would be between the two variables. This could also be done with some string/wool rather than drawing it to make it a bit different. Ask why they've chosen that relationship and ascertain how many correspond with Arthur Laffer's curve and the idea of an optimum tax rate.</p> <p>Read/watch the following afterwards:</p> <p><a href="https://www.youtube.com/watch?v=fw5rp7MfD-Q">https://www.youtube.com/watch?v=fw5rp7MfD-Q</a></p> <p><a href="http://www.laffercenter.com/the-laffer-center-2/the-laffer-curve/">http://www.laffercenter.com/the-laffer-center-2/the-laffer-curve/</a> Duration: 20 minutes</p>	<p><b>A Level only</b></p> <p>▶ Click here</p> <p>▶ Click here</p>
<p><b>If this is the answer, what is the question:</b> Create a PPT slide with various national debt: GDP percentages and ask students what the topic is. Once they've established the topic of national debt, facilitate a discussion around the causes and consequences of these levels of debt.</p> <p>The following website is useful for data collection: <a href="http://www.tradingeconomics.com/">http://www.tradingeconomics.com/</a></p> <p>The guardian data blog is often a good visual resource. Students could correlate the level of national debt over time with the course of the economic cycle and policy maker decisions and objectives.</p> <p><a href="http://www.theguardian.com/news/datablog/2010/oct/18/deficit-debt-government-borrowing-data">http://www.theguardian.com/news/datablog/2010/oct/18/deficit-debt-government-borrowing-data</a> Duration: 30 minutes</p>	<p>▶ Click here</p> <p>▶ Click here</p>
<p><b>Difference between deficits and debt:</b> This is a good opportunity for multiple choice questions. Give students various scenarios (such as a rise in unemployment and consequently a fall in income tax receipts) and they have to decide whether it would affect the cyclical or structural deficit. Duration: 15 minutes</p>	
<p><b>Once upon a time:</b> Ask students to write a short children's story to explain to a primary school pupil the difference between budget deficits and government debt and the cause of the UK's current fiscal problems. Duration: 20 minutes</p>	
<p><b>National debt is NOT.....:</b> Students choose from a variety of options (such as mortgages and credit card debt) what isn't included in national debt figures. Duration: 15 minutes</p>	



# Thinking Contextually: Fiscal policy

Activities	Resources
<p><b>Crowding in and crowding out:</b> Those wishing for further reading could read the article by Benjamin Freidman: <a href="http://www.nber.org/papers/w0284">http://www.nber.org/papers/w0284</a></p>	<p><b>A Level only</b></p> <p>▶ Click here</p>
<p><b>Fiscal Rules:</b> In small groups, students represent various firms and organisations (for example, CBI, Tesco, EDF, Toyota) or households, and consider how they would be affected by the fiscal rules. Would their behaviour (for example consumption of big ticket items or production and/or investment to expand or increase productivity) be influenced by these rules? Duration: 35 minutes</p>	
<p><b>Flat tax:</b> Read the various articles on a flat tax and write an evaluation paragraph to the following essay title: Should Britain introduce a flat rate of income tax? Justify your answer. <a href="http://www.bbc.co.uk/news/uk-politics-22575135">http://www.bbc.co.uk/news/uk-politics-22575135</a> <a href="http://www.theguardian.com/commentisfree/2012/may/22/flat-taxes-taxpayers-alliance">http://www.theguardian.com/commentisfree/2012/may/22/flat-taxes-taxpayers-alliance</a> <a href="http://www.theguardian.com/politics/2014/jul/30/tories-rich-poor-pay-31-percent-ed-balls">http://www.theguardian.com/politics/2014/jul/30/tories-rich-poor-pay-31-percent-ed-balls</a> <a href="http://money.cnn.com/2014/03/31/pf/taxes/rand-paul-flat-tax/">http://money.cnn.com/2014/03/31/pf/taxes/rand-paul-flat-tax/</a> Duration: 45 minutes</p>	<p>▶ Click here</p> <p>▶ Click here</p> <p>▶ Click here</p> <p>▶ Click here</p>



# Thinking Contextually: Fiscal policy

Activities	Resources
<p><b>Distinguish between current and capital government expenditure/progressive/proportional/regressive taxation:</b> A good opportunity for a sorting exercise. Use images to represent the types of expenditure or taxation. You could even ask your class to design the images themselves, creating your resources for you. Duration: 45 minutes</p>	
<p><b>Distinguish between budget deficit and government debt:</b> The BBC has a great video that explains the difference. <a href="http://www.bbc.co.uk/news/business-26289940">http://www.bbc.co.uk/news/business-26289940</a> and a very useful article for students to read. <a href="http://www.bbc.co.uk/news/business-25944653">http://www.bbc.co.uk/news/business-25944653</a></p> <p>The IMF has also released a video explaining the definition of debt and the difference between gross and net debt. <a href="https://www.youtube.com/watch?v=LAD1oCHCibI">https://www.youtube.com/watch?v=LAD1oCHCibI</a></p> <p>A few additional resources to further appreciate the consequences of national debt.</p> <p>Robert Preston, UK debt levels: <a href="http://www.bbc.co.uk/news/business-27116687">http://www.bbc.co.uk/news/business-27116687</a></p> <p>Further analysis of the yield on UK government bonds and gilts: <a href="http://www.bbc.co.uk/news/business-29377075">http://www.bbc.co.uk/news/business-29377075</a></p>	<p><a href="#">▶ Click here</a></p>
<p>Always an interesting resource when discussing the volume of UK national debt: <a href="http://www.debtbombshell.com/">http://www.debtbombshell.com/</a></p>	<p><a href="#">▶ Click here</a></p>



# Curriculum Content: Monetary policy

## **Macroeconomics:** The application of policy instruments > Monetary policy

- explain what is meant by monetary policy instruments/measures, such as interest rates, money supply and how exchange rates can be used to influence macroeconomic variables
- explain how monetary policy instruments/measures affect the macroeconomic performance
- explain what is meant by the liquidity trap
- explain what is meant by inflation rate targeting
- explain how inflation targeting may affect the behaviour of economic agents
- distinguish between symmetric and asymmetric inflation targeting
- explain how a central bank works to achieve its aims
- evaluate the effectiveness of using monetary policy to achieve the government's macroeconomic objectives.



# Thinking Conceptually: Monetary policy

***Monetary policy entails the use of monetary variables such as the money supply and interest rates to influence aggregate demand. The prime instrument of monetary policy in recent years has been the interest rate. Through the interest rate, monetary policy affects aggregate demand.***

## **Approaches to teaching the content**

Many of the concepts learnt in this section will have been in the media and students may be aware of things such as, the rate of inflation or the rate of interest. This can be a great help when putting across new ideas because there is some familiarity already. Use this as a springboard into discussions around how monetary policy instruments influence macroeconomic variables and macroeconomic performance. There is a lot of overlap here; you'll probably find yourself covering the first two bullet points together.

## **Common misconceptions or difficulties students may have**

Students can struggle to appreciate the time lag between a change in the rate of interest and the rate of inflation and real GDP.

Clarification may be needed on the difference between The REPO or BASE rate of interest and the difference between short run and long run interest rates.

Monetary policy instruments can be difficult, in particular quantitative easing and the increase in money supply and the liquidity trap, whereas the use of measures, such as forward guidance is relatively straightforward for most students.

## **Conceptual links to other areas of the specification – useful ways to approach this topic to set students up for topics later in the course**

This is one of the macroeconomic policy instruments that can be used by a central bank. This links in perfectly with the Financial Sector and the Role of the Central Bank. There is also the obvious link to: Economic Policy Objectives and Indicators of macroeconomic performance; inflation being a key objective for monetary policy.

Since the 2007/08 financial crisis there has been a lot of debate around whether an inflation target should be used as the sole objective for monetary policy; use this as a chance for discussion on what the target rate should be for various countries and whether there should be the use of 'forward guidance'.



# Thinking Contextually: Monetary policy

## ACTIVITIES

The specification is written purposely without a particular focus on the UK. This opens up opportunities for students to engage in a wide range of countries and perhaps compare and contrast the varying application of monetary policy. For example, the reaction of the UK, US and Euro-zone to the '07/08 financial crisis can stimulate a lot of debate around the timing of interest rate reductions and use of quantitative easing. This context can also be used when evaluating the effectiveness of monetary policy to achieve the government's macroeconomic objective. In addition a study of Japan's monetary policy would add an interesting perspective – you could ask students to research 'Abenomics'.

Japan is also a good context when explaining the liquidity trap. The Euro-zone and UK have different inflation targets, one symmetric and the other asymmetric, this can also be used to distinguish between them as well as explain how targets can influence the behaviour of economic agents.



# Thinking Contextually: Monetary policy

Activities	Resources
<p><b>Transmission mechanism:</b> Use the BOE's monetary transmission mechanism diagram to illustrate the process of altering the rate of interest and the outcome for inflation and real GDP. Cut up into a jigsaw and see whether students can fit it together. Award a prize for the quickest team.</p> <p><a href="http://www.bankofengland.co.uk/publications/Documents/other/monetary/montrans.pdf">http://www.bankofengland.co.uk/publications/Documents/other/monetary/montrans.pdf</a> Duration: 15 minutes</p>	<p></p>
<p><b>Quantitative Easing:</b> Watch the following video clip on Quantitative Easing <a href="https://www.youtube.com/watch?v=pzXEZSiDYw">https://www.youtube.com/watch?v=pzXEZSiDYw</a></p> <p>Ask students to draw their own representation of quantitative easing. Duration: 15 minutes</p>	<p></p>
<p><b>Liquidity Trap:</b> Ask students to read the two articles (one from the economist and one from the NYT) and write a short paragraph explaining the liquidity trap.</p> <p><a href="http://www.economist.com/blogs/freeexchange/2013/10/monetary-policy-2">http://www.economist.com/blogs/freeexchange/2013/10/monetary-policy-2</a></p> <p><a href="http://krugman.blogs.nytimes.com/2013/04/11/monetary-policy-in-a-liquidity-trap/?_php=true&amp;_type=blogs&amp;r=0">http://krugman.blogs.nytimes.com/2013/04/11/monetary-policy-in-a-liquidity-trap/?_php=true&amp;_type=blogs&amp;r=0</a> Duration: 25 minutes</p>	<p><b>A Level only</b></p> <p></p> <p></p>
<p><b>How a central bank works:</b> Students write questions they'd like to ask these central banks about their policy measures, pass to a partner who must answer the questions. Give time for research into the questions. Duration: 30 minutes</p>	



# Thinking Contextually: Monetary policy

Activities	Resources
<p><b>Flipped lesson:</b> Ask small groups of students to come to the lesson with prior research on a central bank. Organise this so that there is only one student per central bank. These could be, Federal Reserve, European Central Bank and Bank of England (or another central bank of their choice). Tell them that they need to have information that will help them to explain how the bank works to achieve its main target (probably an inflation target) and what monetary policy instruments have been used and what impact they've had on the macroeconomic performance.</p> <p>In the lesson they are tasked to find out about another three central banks. One or two from the group visit other groups to learn about other central banks and report back, while the rest of the group answers questions about their central bank from other groups.</p> <p><a href="https://www.ecb.europa.eu/">https://www.ecb.europa.eu/</a> <a href="http://www.bankofengland.co.uk">www.bankofengland.co.uk</a> <a href="http://www.federalreserve.gov/">http://www.federalreserve.gov/</a> Duration: 30 minutes</p>	<p><a href="#">▶ Click here</a></p> <p><a href="#">▶ Click here</a></p> <p><a href="#">▶ Click here</a></p>
<p><b>Inflation Targeting:</b> The federal reserve doesn't use an inflation target, but has been thought to be considering it. Students act as an economic advisor to the Federal Reserve and write a letter to the Head of the Federal Reserve setting out the merits and pitfalls of inflation targeting, with particular emphasis on the affect it will have upon economic agents (households, firms and the government).</p> <p><a href="http://www.imf.org/external/pubs/ft/fandd/basics/target.htm">http://www.imf.org/external/pubs/ft/fandd/basics/target.htm</a> <a href="https://www.imf.org/external/np/seminars/eng/2011/res/pdf/go2.pdf">https://www.imf.org/external/np/seminars/eng/2011/res/pdf/go2.pdf</a> <a href="http://www.ft.com/cms/s/0/4b6276f8-df95-11df-bed9-00144feabdc0.html#axzz3Dln5H1Na">http://www.ft.com/cms/s/0/4b6276f8-df95-11df-bed9-00144feabdc0.html#axzz3Dln5H1Na</a> Duration: 35 minutes</p>	<p><a href="#">▶ Click here</a></p> <p><a href="#">▶ Click here</a></p> <p><a href="#">▶ Click here</a></p>
<p><b>Effectiveness of monetary policy:</b> Ask students to draw a picture of a see-saw. Best to use A3 paper. They're to write the upsides and downsides of using monetary policy on either side of the see-saw and make a judgement on which outweighs the other by which side of the see-saw will be the 'heaviest'.</p> <p>To add another level to this they could consider the weight of each argument, i.e. the stronger the argument on either an upside or downside, the greater the impact it has on pulling down that end of the see-saw. This can be a useful exercise for them to practice making judgements on the strength of their arguments and the importance of selective analysis. Duration: 25 minutes</p>	



# Curriculum Content: Supply side policy

## **Macroeconomics:** The application of policy instruments > Supply side policy

- **explain policies which are used to increase the quality or quantity of factors of production, including:**
  - education and training
  - reforming tax and benefits
  - reducing marginal tax rates
  - National Minimum Wage legislation and promoting a 'living wage'
  - improving labour market flexibility – including consideration of the housing market
  - immigration
  - privatisation
  - deregulation
  - trade union reform
  - infrastructure investment – including consideration of transport market
  - research and development incentives
  - subsidies
- **evaluate the effectiveness of using supply side policy measures to achieve the government's macroeconomic objectives.**



# Thinking Conceptually: Supply side policy

***Supply side policy measures provide a great opportunity for students to problem solve and apply their economic toolbox early on in the topic as the subject content can be easier to access than perhaps monetary and fiscal policy. There is more that students can relate to and are perhaps familiar with from their own engagement in current affairs and experiences.***

## **Approaches to teaching the content**

This content can be easier for students to grasp and can lend itself to discussion but advise students to make full use of their economic toolbox when analysing the consequences of supply side policies.

It is advisable for students to know of real world supply side policies in order to offer examples, rather than simply offering generic, theoretical, arguments that aren't focused on a particular market or factor of production. For example, they could discuss the merits of investment into education and training (via apprenticeship schemes) rather than just supply side policies per se.

## **Common misconceptions or difficulties students may have**

Students can write in a very generalised manner; the temptation when asked to discuss the impact of supply side policy measures is to just offer theoretical arguments. Advise students to focus on types of supply side policy measures.

## **Conceptual links to other areas of the specification – useful ways to approach this topic to set students up for topics later in the course**

Supply side policies link with the production possibility curve and causes of long run economic growth. In addition discussion can be had on how supply side policies could be used to avoid major recessions when studying the economic cycle.

The topic also links with unemployment (particularly structural), labour mobility and inflation.



# Thinking Contextually: Supply side policy

## ACTIVITIES

Supply side policies are microeconomic policies with a macroeconomic impact and so can be discussed when studying labour market failure (particularly immobility) as well as macroeconomic topics.

It is good to consider: labour market and product market policies as well as public and private sector initiatives.

Keeping examples in context of the UK can be easier for students to grasp, but if you have international students this can add a very interesting dimension to discussions.



# Thinking Contextually: Supply side policy

Activities	Resources
<p><b>Carousel:</b> You'll need A3 paper for this activity and move tables so that students can sit in groups. Put students in small groups (3 to 5) and give each group a different economic problem, for example youth unemployment or skills shortages. Ask them to write down their most effective solution. Next each group moves to another station (go in a clockwise direction if possible) and analyse the offered solution, saying why the solution would be effective. Groups move again to the next station, and either add to the existing analysis or evaluate it (depending on the number of groups) Repeat this again if groups still need to evaluate. Finally, return to original station and discuss the answer plan that has been created. Duration: Depends on class size, about 35 minutes.</p>	
<p><b>Starter activity:</b> As students enter the room, give them a supply side policy which they have to match up with an economic problem. As them to explain why they chose that combination. Duration: 10 minutes</p>	
<p><b>Supply-side policy tennis:</b> Revision of various policy measures: in twos students exchange as many policies as they can; the loser is the one that can't keep going. To make it a little harder (intermediate level) they can't break eye contact. At the higher level, they lose points if they say umm/err or hesitate. Duration: 10 minutes</p>	
<p><b>Supply side policy Pictionary:</b> Students in two teams. A volunteer from each team to the front and they are shown the policy. Either use the classroom whiteboard or use large sheets of paper and students have to go to you with what they think is the answer. Obviously no talking allowed from those drawing. Duration: 15 minutes</p>	
<p><b>Presentations:</b> There is a lot of information on the internet about supply side policies. Once you've given an introduction to the polices overall allocate the various types (education and training, trade union reform etc..) to individuals or groups and ask them to produce a mini presentation on the policy, how it works and to what extent it is effective. This could make a good classroom display. Duration: 45 minutes</p>	



# Curriculum Content: Policy conflicts

## **Macroeconomics:** The application of policy instruments > Policy conflicts

- **explain the possible trade-offs which exist between policy objectives, such as:**
  - unemployment and inflation
  - growth and inflation
  - inflation and the balance of payments
  - growth and the balance of payments
  - growth and income and wealth equality
- **evaluate the consequences of conflicts between policy objectives**
- **evaluate the methods through which policy conflicts can be resolved or reduced.**



# Thinking Conceptually: Policy conflicts

***The use of one macroeconomic policy can sometimes outweigh the impact of another – leading to policy conflict between policy objectives in the short run and long run. For example, policies that promote economic growth might create unemployment or policies that improve stability might limit economic growth. Macroeconomic goals are also often in conflict with the microeconomic goals of efficiency and equity. So students should be encouraged to think through some of these conflicts and how government can best balance its priorities. It is about fine-tuning the economy to create the right conditions for it to flourish and to achieve its stated objectives.***

## **Approaches to teaching the content**

This topic can be delivered with relative student independence as the concept is largely straightforward. Lessons don't have to be didactic. An AD/AS diagram on the board with the question: how can an AD/AS diagram be used to illustrate trade-offs between policy objectives? Can generate a lot of discussion. You could challenge students to find 5 (or more) conflicts.

If you've already taught the key performance indicators they may be able to come up with many (if not all) of the conflicts. However, please refer to common misconceptions or difficulties below.

## **Common misconceptions or difficulties students may have**

Students will often find it (relatively) straightforward to recognise the conflict between short run economic growth

and inflationary pressure – especially if you use the Keynesian LRAS curve. However, they may find the conflict between inflation and BoP more challenging. If students have discussed competitiveness and international trade the conflict may be more obvious.

The least obvious will be the link between unemployment and inflation – they're likely to appreciate the demand-pull inflationary effect, but could need guidance on the cost-push effect.

## **Conceptual links to other areas of the specification – useful ways to approach this topic to set students up for topics later in the course**

Policy conflicts and in particular possible resolution to those conflicts can be taught after supply-side policies in order for the connection between long run economic growth and inflationary pressure to be made.

The conflict between economic growth, unemployment and inflation can be linked to the Phillips curve and approaches to policy and macroeconomic context – in particular, the extent to which prices and wages are flexible and the role of expectations (this links well with the expectations augmented Phillips curve).

When looking at the link between unemployment and inflation, there's the opportunity to link it to increases in the national minimum wage.



# Thinking Contextually: Policy conflicts

## ACTIVITIES

Unemployment and inflation – UK recent low inflation and falling rate of unemployment.

Argentina could be an interesting case study for the conflict between inflation rates and the BoP.

Activities	Resources
<p><b>Which is the odd one out:</b> OR images that represent policy objectives (for example growth/inflation and unemployment) and ask the class what they all have in common. OR have an image of economic growth (perhaps a busy city that would represent lots of economic activity) and put around it images of policy objectives – ask the class how they could conflict with economic growth. Duration: 10 minutes</p>	
<p><b>Philips Curve:</b> Use this to represent the trade off between unemployment and inflation. Suggest the class reads Tim Harford's book: Undercover Economist Strikes Back chapter one. <a href="http://timharford.com/books/undercovereconomist-strikes-back/">http://timharford.com/books/undercovereconomist-strikes-back/</a></p> <p>Or watches the following video: <a href="https://www.youtube.com/watch?v=k7f4L1nkHPI">https://www.youtube.com/watch?v=k7f4L1nkHPI</a></p> <p>Or listens to the following program: <a href="http://www.bbc.co.uk/programmes/b01qdzcd">http://www.bbc.co.uk/programmes/b01qdzcd</a> Depends on chosen media between 10-20 minutes</p>	<p><a href="#">▶ Click here</a></p> <p><a href="#">▶ Click here</a></p> <p><a href="#">▶ Click here</a></p>
<p><b>Hawk versus Dove:</b> To represent their own views, ask the class to draw an image that represents either a hawk or dove/hard-nosed or soft-nosed banker. Have a class vote. Duration: 10 minutes</p>	
<p><b>Inequality:</b> An interesting video on growth and inequality in America. <a href="http://anticapitalists.org/2013/03/04/wealth-inequality-in-the-usa/">http://anticapitalists.org/2013/03/04/wealth-inequality-in-the-usa/</a></p> <p>Growth and inequality in China: <a href="http://www.bbc.co.uk/news/world-asia-18935323">http://www.bbc.co.uk/news/world-asia-18935323</a></p> <p>Global inequality: <a href="http://www.bbc.co.uk/news/business-16800265">http://www.bbc.co.uk/news/business-16800265</a></p> <p>Inequality gap narrows between East and West Germany: <a href="http://www.bbc.co.uk/news/business-17037346">http://www.bbc.co.uk/news/business-17037346</a></p> <p>Inequality in Latin America: <a href="https://www.youtube.com/watch?v=5z2_SfzpcSg">https://www.youtube.com/watch?v=5z2_SfzpcSg</a></p> <p>Ask students to watch the videos and discuss the factor(s) that exacerbate (or influence) the trade-off between economic growth and inequality. Duration: 30 minutes</p>	<p><a href="#">▶ Click here</a></p>



# Curriculum Content: Approaches to policy and macroeconomic context

**Macroeconomics:** The application of policy instruments > Approaches to policy and macroeconomic context

- **evaluate debates in macroeconomic thinking concerning:**
  - the extent to which prices and wages are flexible
  - the flexibility/elasticity of aggregate supply
  - the role of expectations
- **explain why approaches to macroeconomic policy change in accordance with economic circumstances, with reference to:**
  - the Great Depression
  - Keynesian demand management in the 1970s
  - the monetarist approach in the 1980s
  - the 2007–08 financial crisis and its aftermath.

**NB. Please note that this section is relevant to the A Level only.**



# Thinking Conceptually: Approaches to policy and macroeconomic context

***The discussion so far has focused on short-run aggregate supply. However, it is also important to consider how aggregate supply can be seen in the longer term. Changes in the factors affecting aggregate supply alter the long-run potential productive capacity of the economy. Also if firms have pessimistic expectations about aggregate demand, and thus reduced their supply of output, this would lead to lower incomes because of the workers being laid off. This would then mean that aggregate demand was indeed deficient, so firms' pessimism was self-fulfilling.***

## **Approaches to teaching the content**

This topic helps to put a lot of modern day economics in context and is a great opportunity to study a bit of economic history. You may find some of your students are familiar with the Great Depression (at least on a superficial level) from their History studies. This could be an opportunity for a mini research project. The basic framework may be needed but students could use a variety of internet or book based resources to construct a timeline on the evolution of economic thought.

Because this is (initially) a knowledge based topic, it may require some direction and teacher input at the beginning to ensure students grasp the fundamental concepts of concepts such as the role of expectations and wage and price flexibility.

## **Common misconceptions or difficulties students may have**

When teaching stagflation this may be challenging for students as they can confuse inflation/disinflation and deflation.

The distinction between short run and long run aggregate supply needs to be stressed to aid understanding of the flexibility/elasticity of aggregate supply.

## **Conceptual links to other areas of the specification – useful ways to approach this topic to set students up for topics later in the course**

It is advisable to cover this topic after monetary/fiscal and supply side policies and also the key performance indicators.

The concept of elasticity of aggregate supply will be easier to grasp if you've also taught price elasticity of supply and the difference between the long run and the short run.



# Thinking Contextually: Approaches to policy and macroeconomic context

## ACTIVITIES

The approaches to macroeconomic policy can be taught in context of the causes and consequences of the policy changes. As with many elements of this section of the syllabus, this topic can be addresses from the context of a number of countries, and it is a great opportunity to contrast the different approaches of various nations.

The monetarist approach in the 1980s could be looked at in context of both America and the UK and the influence Margaret Thatcher took from Hayek as well as the Chicago School of Economics.

Activities	Resources
<p><b>Keynes versus Hayek:</b> Play the two videos and ask students to write a summary of the different economic schools of thought. <a href="https://www.youtube.com/watch?v=d0nERTFo-Sk">https://www.youtube.com/watch?v=d0nERTFo-Sk</a> <a href="https://www.youtube.com/watch?v=GTQnarzmTOc">https://www.youtube.com/watch?v=GTQnarzmTOc</a> Duration 40 minutes</p>	<p><a href="#">▶ Click here</a></p> <p><a href="#">▶ Click here</a></p>
<p><b>Timeline:</b> In groups, the class constructs a timeline of the evolution of economic thought. Encourage the inclusion of AD/AS diagrams, images, data, headlines, brief outlines of the economic circumstances and economic policy responses, the economic thinkers of the day and their opinions/conflicts.</p> <p>Some interesting books on this topic:</p> <p>New ideas from dead economists by Todd G Buchholz</p> <p>Keynes versus Hayek: The Clash that Define Modern Economics by Nicholas Wapshott (Link to the review by the Adam Smith Institute: <a href="http://www.adamsmith.org/research/think-pieces/review-keynes-hayek-the-clash-that-defined-modern-economics/">http://www.adamsmith.org/research/think-pieces/review-keynes-hayek-the-clash-that-defined-modern-economics/</a>)</p> <p>Keynes: The Return of the Master by Robert Skidelsky</p> <p>The Making of modern economics: The Lives and Ideas of the Great Thinkers by Mark Skousen</p> <p>Some additional articles on Keynes versus Hayek: <a href="http://www.economist.com/blogs/freexchange/2012/08/keynes-and-hayek">http://www.economist.com/blogs/freexchange/2012/08/keynes-and-hayek</a> <a href="http://www.economist.com/blogs/freexchange/2014/03/keynes-and-hayek">http://www.economist.com/blogs/freexchange/2014/03/keynes-and-hayek</a> <a href="http://www.bbc.co.uk/news/business-14366054">http://www.bbc.co.uk/news/business-14366054</a> Duration 45 minutes</p>	<p><a href="#">▶ Click here</a></p> <p><a href="#">▶ Click here</a></p> <p><a href="#">▶ Click here</a></p> <p><a href="#">▶ Click here</a></p>



# Thinking Contextually: Approaches to policy and macroeconomic context

Activities	Resources
<p><b>Word search:</b> How many words associated with the different approaches to macroeconomic policy can students identify. <a href="http://www.puzzle-maker.com/">http://www.puzzle-maker.com/</a> Duration 10 minutes</p>	
<p><b>Hat game:</b> In 2+ teams students are given a few small pieces of paper. On these they write either; a person, an economic policy or an event. They fold them up and put them into a container (a hat is a good option). There are three levels to the game, Level 1: Each team takes turns for a member of their group to select a piece of paper from the hat and describe it to their team. They get 30 seconds to do as many as they can. This alternates between teams and team members until all the pieces of paper have been selected. Hopefully all the team members will have a chance to participate in describing something from the hat. Count up how many pieces of paper each team went through and record their points.</p> <p>Level 2: The same process but they must use only one word to help their team members identify what is on the paper.</p> <p>Level 3: The same process but only actions can be used.</p> <p>The winning team is the one with the most points.</p> <p>Hint: the trick is to listen to both your team and the others to remember what people, events or policies are in the hat and so make it easier to identify them in level 2 and level 3. Duration 20 minutes</p>	





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