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OCR
Oxford Cambridge and RSA

AS LEVEL
Exemplar Candidate Work

ECONOMICS

H060
For first teaching in 2015

Component 2
Macroeconomics

Version 3

www.ocr.org.uk/economics

Contents

Introduction

We produced a 20-mark extended response question for AS Macroeconomics (H060/02) and asked students to answer it.

The sample answers in this resource have been extracted from original candidate work to maintain their authenticity.

To facilitate different ways for using this resource, you will find the student answers twice, once without and then with examiner comments and marks.

Please note that this resource is provided for advice and guidance only and does not in any way constitute an indication of grade boundaries or endorsed answers.

Oxford Cambridge and RSA

…day June 20XX – Morning/Afternoon

AS Level in Economics

H060/02 Macroeconomics

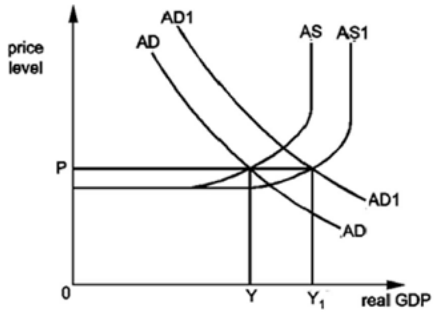
PRACTICE MARK SCHEME

MARKING INSTRUCTIONS

Descriptor	Award mark
On the borderline of this level and the one below	At bottom of level
Just enough achievement on balance for this level	Above bottom and either below middle or at middle of level (depending on number of marks available)
Meets the criteria but with some slight inconsistency	Above middle and either below top of level or at middle of level (depending on number of marks available)
Consistently meets the criteria for this level	At top of level

Levels of response – Level descriptors

<table>
<tr><th></th><th>Knowledge and understanding/ Application</th><th>Analysis</th><th>Evaluation</th></tr>
<tr><td>Strong</td><td rowspan="2">Precision in the use of the terms in the question and applied in a focused way to the context of the question.</td><td>An explanation of causes and consequences, fully developing the links in the chain of argument.</td><td>A conclusion is drawn weighing up both sides, and reaches a supported judgement.</td></tr>
<tr><td>Good</td><td>An explanation of causes and consequences, developing most of the links in the chain of argument.</td><td>A conclusion is drawn weighing up both sides, but without reaching a supported judgement.</td></tr>
<tr><td>Reasonable</td><td>Awareness of the meaning of the terms in the question and applied to the context of the question.</td><td>An explanation of causes and consequences, which omit some key links in the chain of argument.</td><td>Some attempt to come to a conclusion, which shows some recognition of the influencing factors.</td></tr>
<tr><td>Limited</td><td>Awareness of the meaning of the terms in the question.</td><td>Simple statement(s) of cause and consequence.</td><td>An unsupported assertion.</td></tr>
</table>

Question			Answer	Marks	Guidance
1	*		Evaluate the extent to which monetary policy is always able to both stimulate economic activity and achieve price stability. **Level 4 (16–20 marks)** **Good** knowledge and understanding of monetary policy, economic activity and price stability. **Strong** analysis of the link between monetary policy, economic activity and price stability. A relevant and accurately drawn and labelled diagram is provided and linked to the analysis. **Strong** evaluation including a supported judgement on whether monetary policy will always stimulate economic stability and achieve price stability. There is a well-developed line of reasoning which is clear and logically structured. The information presented is entirely relevant and substantiated. **Level 3 (11–15 marks)** **Good** knowledge and understanding of monetary policy, economic activity and price stability. **Good** analysis of the link between monetary policy, economic activity and price stability. A relevant and accurately drawn and labelled diagram is provided and linked to the analysis. **Good** evaluation on whether monetary policy will always stimulate economic activity and achieve price stability. There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and in the most part substantiated. **Level 2 (6–10 marks)** **Reasonable** knowledge and understanding of monetary policy, economic activity and price stability. **Reasonable** analysis of the link between monetary policy, economic activity and price stability. A relevant diagram is provided and linked to the analysis. **Reasonable** evaluation on whether monetary policy will stimulate economic activity and achieve price stability but without considering whether this will always be the case. There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.	20 (AO1 ×3 AO2 ×4 AO3 ×6 AO4 ×7)	*Indicative content* Use and interpretation of an AD/AS diagram:  Reasons why monetary policy may stimulate economic activity and achieve price stability: • Interest rates influence private sector investment which can influence both the demand and supply side of the economy and therefore stimulate growth while achieving price stability. • When changes to the rate of interest are gradual and can be factored in to decisions made by firms and households. • When the central bank is transparent about their decision making and firms and households believe that the central bank is credible. Reasons why monetary policy may not stimulate economic activity and achieve price stability: • Through the Fisher equation of exchange, money supply has a direct influence on rates of inflation – monetary policy measures which increase money supply will result in inflationary pressure and not achieve price stability. • Quantitative Easing didn't stimulate economic growth in the UK or the Eurozone in the way that was expected. • Decreasing the rate of interest will (through the transmission mechanism) stimulate economic activity (on the demand side) but it will also create demand-pull inflationary pressure. • Large/unexpected changes in the rate of interest can create uncertainty and can reduce economic activity/cause a slowdown in economic growth. Credit, where appropriate, knowledge/analysis of other, relevant factors.

Question			Answer	Marks	Guidance
			Level 1 (1–5 marks) **Limited** knowledge and understanding of monetary policy, economic activity and price stability. **Limited or no** analysis of the link between monetary policy, economic activity and price stability. A diagram is included which is less than perfect. **Limited or no** evaluation. The information is basic and communicated in an unstructured way. The information is supported by limited evidence and the relationship to the evidence may not be clear.		Possible routes into evaluation: • Monetary policy isn't **always** the able to stimulate activity and achieve price stability. Needs to be used alongside supply side policies. • Ability of central bankers/policy makers to anticipate the factors influencing the price level. • The time lag between a change in the rate of interest, change in economic activity and rate of inflation. • Will monetary policy affect short run and long run economic growth? • Price stability – if inflation rates are fluctuating, but within the inflation band (assuming one is used by the central bank) then is this price stability? • Depends on what is causing inflation rates to change – are demand or cost pressures the strongest? • In the current economic climate how much interest rates are changed needs to be considered. • Supply side policies need to be used alongside monetary policy.

CANDIDATE RESPONSE

"The UK continues to have record low interest rates, the Bank of England has held interest rates have been held at 0.5% since March 2009. During this period of low interest rates economic activity has gradually recovered whereas inflation rates have fluctuated from highs of 5.1% (CPI) to even a short period of deflation."

Evaluate the extent to which monetary policy is always able to both stimulate economic activity and achieve price stability [20 marks]

Candidate D – UNANNOTATED

Monetary Policy is the attempt by government or a central bank to manipulate the money supply, the supply of credit, interest rates or any other monetary variables, to achieve the fulfilment of policy goals such as price stability and economic activity.

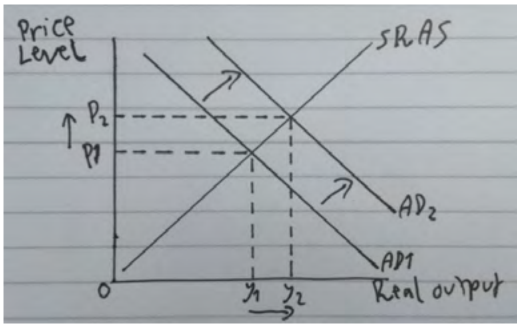
Monetary policy consists of three main instruments to achieving the policy goals which can be manipulated; interest rates are the main instrument of monetary policy in the UK. Interest rate is the price of money, determined by the demand and supply of funds in a market where there are borrowers and lenders. Secondly is money supply which is the entire stock of currency in a country's economy at a particular time. This can be manipulated by the central bank by the use of quantitative easing by effectively printing more money (or doing so electronically) which can also largely help to increase inflation to the target rate if needed. Finally is the exchange rate which is the value of one currency in terms of another currency. The Bank of England are limited in what they can do to manipulate the exchange rate as it relies on market forces apart from instances of buying up large amounts of foreign currency.

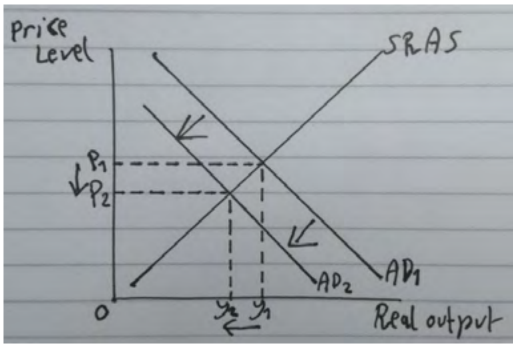
There are two types of monetary policy, firstly expansionary monetary policy which is used to increase economic activity, this type is usually employed when there is a negative output gap with the aim of increasing economic growth in the short run, increasing employment and increasing inflation (towards the target of 2%). By the Bank of England deciding to decrease interest rates to discourage saving and increase spending and investment, therefore there is increasing aggregate demand and economic activity. If firms invest more in themselves then through the multiplier effect there will be a more than proportionate increase in real national output and economic growth.

Whereas contractionary monetary policy which by increasing interest rates is used to decrease inflation in the economy and slow down an overheating economy in a positive output gap by encouraging saving from both households and firms, also increasing the cost of borrowing which consequently reduces consumption and investment.

Both expansionary and contractionary monetary policy could be used by the Bank of England to increase or decrease inflation to the current target level of 2%. Therefore also achieving better price stability by decreasing the fluctuations and changes in general price level of goods over time.

Candidate D – UNANNOTATED





However there are also risks with monetary policy as by decreasing interest rates there is a risk of increasing inflation too much (through demand-pull inflation) which will create more problems in the economy such as an overheating economy. On the other hand by increasing interest rates there in a risk of decreasing unemployment and a decrease in economic growth as households and firms save instead of invest, this could also be bad for the economy and could lead to a recession.

As in the above diagram it is evident that expansionary monetary policy can be used to shift AD from AD1 to AD2. This would have an effect of expanding the economy from y1 to y2, therefore increasing economic activity. However there will be a trade off as the price level rises from P1 to P2.

In the above diagram it can be seen that contractionary monetary policy can shift AD from AD1 to AD2. This would have a negative effect of contracting the economy from y1 to y2 and decreasing AD but it would decrease the price level from P1 to P2 encouraging economic activity.

In recent decades monetary policy has been regarded as the main instrument of demand management within the UK economy. As the interest rate is currently only 0.5%, it has been impossible to follow an expansionary monetary policy by reducing interest rates. Instead the Bank of England has largely used quantitative easing, pushing more money into the economy to encourage economic activity through investment and consumption increasing aggregate demand.

Monetary policy does have limitations as interest rates and their fluctuations have no effect on inflation if it is caused by cost-push inflation, this means that monetary policy is in fact not solving the problem of price stability and so the worth of monetary policy can only go so far. Expansionary monetary policy is not guaranteed results and if it is not having the required affect, then it is not an effective policy for managing demand. There are also time lags with monetary policy as it takes time for a change in interest rates to have an effect on the economy. It is important to take into account that monetary policy does not help with long run economic growth and is only effective in stimulating economic growth in the short run before the supply side policies can be implemented to achieve long run economic growth.

By using monetary policy to stimulate economic activity this can have a negative effect on the price level by increasing it through demand-pull inflation thus contradicting the use of this policy, as well as the vice versa when trying to achieve price stability it could result in slowing economic activity which is not solving the problems and is another negative of monetary policy.

However, there are other options for achieving economic activity and price stability such as government intervention to reduce demand-pull inflation by increasing available goods or subsidising and investing in firms to reduce cost-push inflation. Also expansionary or contractionary fiscal policy can be used by manipulating government expenditure and taxation to achieve economic activity and price stability.

In conclusion, it is evident that monetary policy is a good policy measure to help stimulate economic activity and achieve price stability to a certain extent. It can allow the Bank of England to manipulate the interest rates, money supply and the exchange rate to achieve the desired effect however there are sometimes problems associated with using monetary policy as it does not always completely solve the problem and can instead cause more problems. Therefore it would be best used alongside supply side policies in the long run and other demand side policies in the short run such as fiscal policy, this can allow economic activity and price stability without the consequences that monetary policy alone will bring.

CANDIDATE RESPONSE

"The UK continues to have record low interest rates, the Bank of England has held interest rates have been held at 0.5% since March 2009. During this period of low interest rates economic activity has gradually recovered whereas inflation rates have fluctuated from highs of 5.1% (CPI) to even a short period of deflation."

Evaluate the extent to which monetary policy is always able to both stimulate economic activity and achieve price stability [20 marks]

Candidate D – ANNOTATED

Monetary Policy is the attempt by government or a central bank to manipulate the money supply, the supply of credit, interest rates or any other monetary variables, to achieve the fulfilment of policy goals such as price stability and economic activity.

Good knowledge of monetary policy

Monetary policy consists of three main instruments to achieving the policy goals which can be manipulated; interest rates are the main instrument of monetary policy in the UK. Interest rate is the price of money, determined by the demand and supply of funds in a market where there are borrowers and lenders. Secondly is money supply which is the entire stock of currency in a country's economy at a particular time. This can be manipulated by the central bank by the use of quantitative easing by effectively printing more money (or doing so electronically) which can also largely help to increase inflation to the target rate if needed. Finally is the exchange rate which is the value of one currency in terms of another currency. The Bank of England are limited in what they can do to manipulate the exchange rate as it relies on market forces apart from instances of buying up large amounts of foreign currency.

Further development of their knowledge of monetary policy

There are two types of monetary policy, firstly expansionary monetary policy which is used to increase economic activity, this type is usually employed when there is a negative output gap with the aim of increasing economic growth in the short run, increasing employment and increasing inflation (towards the target of 2%). By the Bank of England deciding to decrease interest rates to discourage saving and increase spending and investment, therefore there is increasing aggregate demand and economic activity. If firms invest more in themselves then through the multiplier effect there will be a more than proportionate increase in real national output and economic growth.

Further knowledge of monetary policy and analysis of the impact of a reduction in the rate of interest. There is also knowledge of inflation demonstrated.

Whereas contractionary monetary policy which by increasing interest rates is used to decrease inflation in the economy and slow down an overheating economy in a positive output gap by encouraging saving from both households and firms, also increasing the cost of borrowing which consequently reduces consumption and investment.

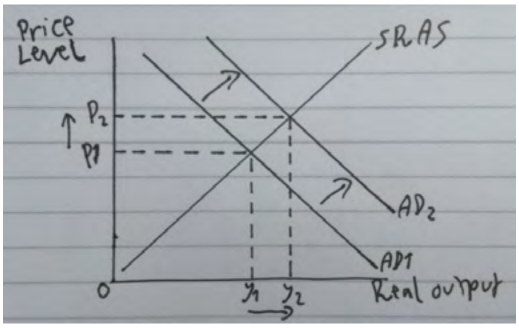
Both expansionary and contractionary monetary policy could be used by the Bank of England to increase or decrease inflation to the current target level of 2%. Therefore also achieving better price stability by decreasing the fluctuations and changes in general price level of goods over time.

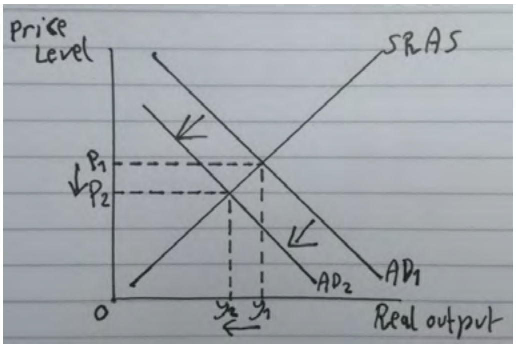
Some reasonable analysis of how monetary policy can be used to achieve price stability.

Candidate D – ANNOTATED (cont)

However there are also risks with monetary policy as by decreasing interest rates there is a risk of increasing inflation too much (through demand-pull inflation) which will create more problems in the economy such as an overheating economy. On the other hand by increasing interest rates there in a risk of decreasing unemployment and a decrease in economic growth as households and firms save instead of invest, this could also be bad for the economy and could lead to a recession.

As in the above diagram it is evident that expansionary monetary policy can be used to shift AD from AD1 to AD2. This would have an effect of expanding the economy from y1 to y2, therefore increasing economic activity. However there will be a trade off as the price level rises from P1 to P2.





Analysis of the drawbacks of using monetary policy, this develops the analysis demonstrated so far.

In the above diagram it can be seen that contractionary monetary policy can shift AD from AD1 to AD2. This would have a negative effect of contracting the economy from y1 to y2 and decreasing AD but it would decrease the price level from P1 to P2 encouraging economic activity.

Diagrams are included which are accurately drawn and (largely) accurately labelled. They are linked to the analysis.

In recent decades monetary policy has been regarded as the main instrument of demand management within the UK economy. As the interest rate is currently only 0.5%, it has been impossible to follow an expansionary monetary policy by reducing interest rates. Instead the Bank of England has largely used quantitative easing, pushing more money into the economy to encourage economic activity through investment and consumption increasing aggregate demand.

This is a limited evaluative point on the downsides of using monetary policy. Reasonable evaluation.

Monetary policy does have limitations as interest rates and their fluctuations have no effect on inflation if it is caused by cost-push inflation, this means that monetary policy is in fact not solving the problem of price stability and so the worth of monetary policy can only go so far. Expansionary monetary policy is not guaranteed results and if it is not having the required affect, then it is not an effective policy for managing demand. There are also time lags with monetary policy as it takes time for a change in interest rates to have an effect on the economy. It is important to take into account that monetary policy does not help with long run economic growth and is only effective in stimulating economic growth in the short run before the supply side policies can be implemented to achieve long run economic growth.

Evaluation is developed here – the candidate has picked up on the need for supply side policies and the time lags inherent in the use of monetary policy as well as the different causes of inflation which may not be able to be controlled by the central bank.

By using monetary policy to stimulate economic activity this can have a negative effect on the price level by increasing it through demand-pull inflation thus contradicting the use of this policy, as well as the vice versa when trying to achieve price stability it could result in slowing economic activity which is not solving the problems and is another negative of monetary policy.

However, there are other options for achieving economic activity and price stability such as government intervention to reduce demand-pull inflation by increasing available goods or subsidising and investing in firms to reduce cost-push inflation. Also expansionary or contractionary fiscal policy can be used by manipulating government expenditure and taxation to achieve economic activity and price stability.

This is stronger evaluation as alternative policy measures are suggested. However, it could have been even better if there was discussion about using these policies alongside one another.

Candidate D – ANNOTATED (cont)

In conclusion, it is evident that monetary policy is a good policy measure to help stimulate economic activity and achieve price stability to a certain extent. It can allow the Bank of England to manipulate the interest rates, money supply and the exchange rate to achieve the desired effect however there are sometimes problems associated with using monetary policy as it does not always completely solve the problem and can instead cause more problems. Therefore it would be best used alongside supply side policies in the long run and other demand side policies in the short run such as fiscal policy, this can allow economic activity and price stability without the consequences that monetary policy alone will bring.

The candidate has done well to highlight the need for various policy measures, not just monetary. However, the judgement is a little vague. There is some support for the judgement but it could be more clearly expressed.

Level 4 **17 marks**

Examiner's summary comments

Level 4 (16–20 marks)

Good knowledge and understanding of monetary policy, economic activity and price stability.

Strong analysis of the link between monetary policy, economic activity and price stability. A relevant and accurately drawn and labelled diagram is provided and linked to the analysis.

Strong evaluation including a supported judgement on whether monetary policy will always stimulate economic stability and achieve price stability.

There is a well-developed line of reasoning which is clear and logically structured. The information presented is entirely relevant and substantiated.

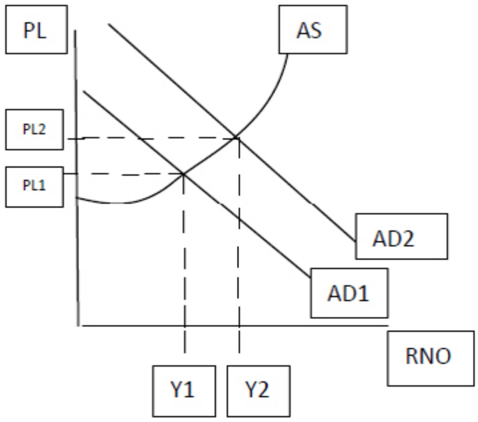
CANDIDATE RESPONSE

"The UK continues to have record low interest rates, the Bank of England has held interest rates have been held at 0.5% since March 2009. During this period of low interest rates economic activity has gradually recovered whereas inflation rates have fluctuated from highs of 5.1% (CPI) to even a short period of deflation."

Evaluate the extent to which monetary policy is always able to both stimulate economic activity and achieve price stability [20 marks]

Candidate E – UNANNOTATED

Monetary policy in the UK is controlled by the bank of England and is comprised of 3 controls, interest rates (which can be used to increase or decrease savings and spending currently at 0.5%), QE (quantitative easing) and finally exchange rates although the MPCV cannot directly control them. Monetary stability means stable prices and confidence in the currency. Stable prices are defined by the Government's inflation target, which the Bank seeks to meet through the decisions taken by the Monetary Policy Committee (MPC). Economic activity is the production, distribution and consumption of commodities this is usually in an economy because it means there is more money in the circular flow of income and could lead to the multiplier effect occurring.



A reduction in interest rates (expansionary monetary policy) by the Bank of England will increase aggregate demand because saving is discouraged, new borrowing and spending is encouraged and confidence and investment will increase eventually leading to the multiplier effect. The effect of the increase in aggregate demand on real output and the price level depends upon the elasticity of aggregate supply. But due to people having a greater disposable income economic activity will increase. However when lowering interest rates a large amount of demand pull inflation may occur which may mean price stability will decrease and may over-stimulate aggregate demand beyond the capacity of the economy to respond in the short run.

As shown by the diagram due to a shift in AD= C + I + G + (X-M) to the right from AD1 to AD2. The price level of the UK economy has increased from PL1 to PL2 and real national income has increased from Y1 to Y2. In this instance reducing the interest rates would help achieve economic activity but may not help achieve price stability. However it can be argues that to achieve price stability in a period of low inflation like the UK is in now a low interest rate could stimulate price stability.

When increasing interest rates (contractionary policy) the opposite will happen AD will decrease PL will fall meaning disinflation could occur and employment will fall. When using and contractionary MP the economy is likely to be in a boom stage of the economic cycle. Increasing interest rates would mean more people would save and inflation will decrease.

Since the bank of England can operate separately from the pressure of the government (operational independence), it allows them to make the best decisions based on how the economy is doing at a particular time. It also avoids public choice theory.

A big advantage of using MP (monetary policy) compared to fiscal policy or supply side policies is that interest rates can be adjusted on a monthly basis, which contrasts with discretionary fiscal policy which cannot be adjusted at such regular intervals. Meaning if economic activity needed to be increased it can be done quickly and effectively. However, when increasing interest rates there can be a time lag associated with it meaning it could take up to a year to change consumer spending or saving, but usually it can have a large effect on consumer confidence.

One major downside with MP is that it is only a short term measure so if used to stimulate economic activity and achieve price stability it may have to be used alongside other policies to carry the progress on into the long term.

Monetary policy also has many conflicting goals such as between inflation and reducing interest rates to expand the money supply and stem rising unemployment rates during a recession, for example, could spark future inflation if monetary policy remains expansionary for too long. In this way it is possible to argue that monetary policy is now more effective and is more likely to promote both economic activity and price stability because the central bank isn't just trying to hit the inflation target (2% CPI), it is also trying to manage economic growth and unemployment rates (this was seen with the recent policy of forward guidance). The best monetary policy seeks to strike a balance between these short- and long-term goals.

When looking at MP to stimulate economic activity and achieve price stability it can be an effective policy to use. However it is only a short term measure so if price stability is to be kept and economic activity is to be thriving then this policy may have to be use alongside fiscal policy to achieve long term success. MP is very good at changing consumer confidence but has serious time lags which could mean the effect of the policy is delayed. Overall I cannot say whether it is always effective in stimulating economic activity and achieving price stability.

CANDIDATE RESPONSE

"The UK continues to have record low interest rates, the Bank of England has held interest rates have been held at 0.5% since March 2009. During this period of low interest rates economic activity has gradually recovered whereas inflation rates have fluctuated from highs of 5.1% (CPI) to even a short period of deflation."

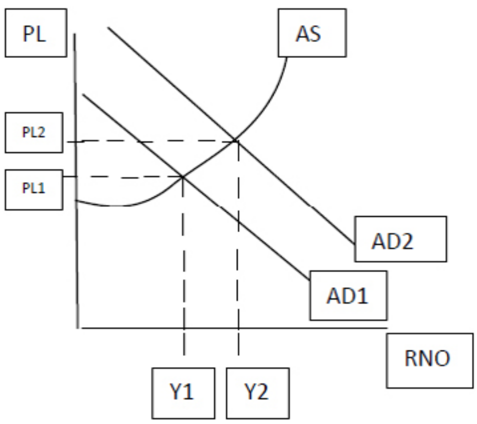
Evaluate the extent to which monetary policy is always able to both stimulate economic activity and achieve price stability [20 marks]

Candidate E – ANNOTATED

Monetary policy in the UK is controlled by the bank of England and is comprised of 3 controls, interest rates (which can be used to increase or decrease savings and spending currently at 0.5%), QE (quantitative easing) and finally exchange rates although the MPCV cannot directly control them. Monetary stability means stable prices and confidence in the currency. Stable prices are defined by the Government's inflation target, which the Bank seeks to meet through the decisions taken by the Monetary Policy Committee (MPC). Economic activity is the production, distribution and consumption of commodities this is usually in an economy because it means there is more money in the circular flow of income and could lead to the multiplier effect occurring.

Good knowledge of monetary policy and economic activity. Their knowledge of price stability could have been developed with greater knowledge of the macroeconomic objective.

A reduction in interest rates (expansionary monetary policy) by the Bank of England will increase aggregate demand because saving is discouraged, new borrowing and spending is encouraged and confidence and investment will increase eventually leading to the multiplier effect. The effect of the increase in aggregate demand on real output and the price level depends upon the elasticity of aggregate supply. But due to people having a greater disposable income economic activity will increase. However when lowering interest rates a large amount of demand pull inflation may occur which may mean price stability will decrease and may over-stimulate aggregate demand beyond the capacity of the economy to respond in the short run.



Some reasonable analysis of the influence monetary policy can have on the rate of inflation. There is some evaluation on the degree of spare capacity. They could have explored the idea of short and long run further here.

As shown by the diagram due to a shift in AD= C + I + G + (X-M) to the right from AD1 to AD2. The price level of the UK economy has increased from PL1 to PL2 and real national income has increased from Y1 to Y2. In this instance reducing the interest rates would help achieve economic activity but may not help achieve price stability. However it can be argues that to achieve price stability in a period of low inflation like the UK is in now a low interest rate could stimulate price stability.

An accurately drawn and labelled diagram which is linked to the analysis.

When increasing interest rates (contractionary policy) the opposite will happen AD will decrease PL will fall meaning disinflation could occur and employment will fall. When using and contractionary MP the economy is likely to be in a boom stage of the economic cycle. Increasing interest rates would mean more people would save and inflation will decrease.

This doesn't take the argument any further which is a shame.

Since the bank of England can operate separately from the pressure of the government (operational independence), it allows them to make the best decisions based on how the economy is doing at a particular time. It also avoids public choice theory.

This evaluation could have been explored in more depth, a missed opportunity but still, is does hint at the need for a credible central bank.

A big advantage of using MP (monetary policy) compared to fiscal policy or supply side policies is that interest rates can be adjusted on a monthly basis, which contrasts with discretionary fiscal policy which cannot be adjusted at such regular intervals. Meaning if economic activity needed to be increased it can be done quickly and effectively. However, when increasing interest rates there can be a time lag associated with it meaning it could take up to a year to change consumer spending or saving, but usually it can have a large effect on consumer confidence.

Evaluation of the time lag inherent in the transmission mechanism. This helps to develop the standard of evaluation in the whole essay.

Candidate E – ANNOTATED (cont)

One major downside with MP is that it is only a short term measure so if used to stimulate economic activity and achieve price stability it may have to be used alongside other policies to carry the progress on into the long term.

Monetary policy also has many conflicting goals such as between inflation and reducing interest rates to expand the money supply and stem rising unemployment rates during a recession, for example, could spark future inflation if monetary policy remains expansionary for too long. In this way it is possible to argue that monetary policy is now more effective and is more likely to promote both economic activity and price stability because the central bank isn't just trying to hit the inflation target (2% CPI), it is also trying to manage economic growth and unemployment rates (this was seen with the recent policy of forward guidance). The best monetary policy seeks to strike a balance between these short- and long-term goals.

There is more evaluation in this paragraph. The candidate recognises that the Bank of England now considers more than just the rate of inflation when making its monthly interest rate decisions.

When looking at MP to stimulate economic activity and achieve price stability it can be an effective policy to use. However it is only a short term measure so if price stability is to be kept and economic activity is to be thriving then this policy may have to be use alongside fiscal policy to achieve long term success. MP is very good at changing consumer confidence but has serious time lags which could mean the effect of the policy is delayed. Overall I cannot say whether it is always effective in stimulating economic activity and achieving price stability.

There is some judgement here but it isn't supported and so isn't strong evaluation.

Level 3 **12 marks**

Examiner's summary comments

Level 3 (11–15 marks)

Good knowledge and understanding of monetary policy, economic activity and price stability.

Good analysis of the link between monetary policy, economic activity and price stability. A relevant and accurately drawn and labelled diagram is provided and linked to the analysis.

Good evaluation on whether monetary policy will always stimulate economic activity and achieve price stability but the judgement hasn't been supported.

There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and in the most part substantiated.

CANDIDATE RESPONSE

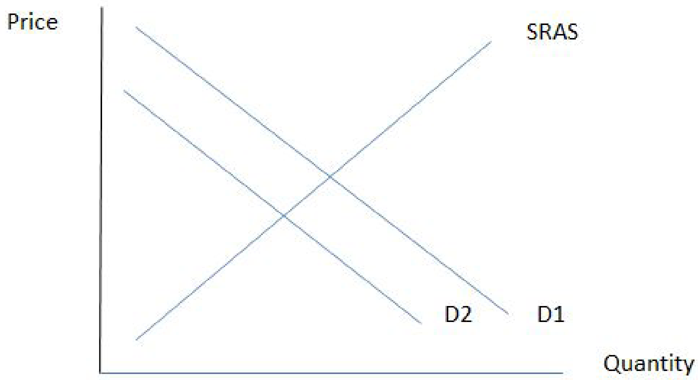
"The UK continues to have record low interest rates, the Bank of England has held interest rates have been held at 0.5% since March 2009. During this period of low interest rates economic activity has gradually recovered whereas inflation rates have fluctuated from highs of 5.1% (CPI) to even a short period of deflation."

Evaluate the extent to which monetary policy is always able to both stimulate economic activity and achieve price stability [20 marks]

Candidate F – UNANNOTATED

Governments use monetary policy to affect the economy and help to get economic growth. Monetary policy is changing the interest rate. Changing the interest rate will affect aggregate demand, if you increase the interest rate you will have less aggregate demand because consumers will have less money to purchase goods and services which will mean that there are fewer injections into the economy.

Firms will want to save their income, because the bank will give them a better interest rate and so they won't hire as many people and this could mean there are more people without a job and so there is less money being spent – a downward spiral. With fewer injections there will be a shift to the left of aggregate demand and a reduction in both prices and output as shown by the diagram below.



However, the opposite is true; decreasing the interest rate will result in an increase in the economy as people have more money to invest which is a component of aggregate demand and so an increase in the economy will make prices go up. If prices go up people are more concerned about what they can buy and may think that saving is a good idea. This could make the economy get smaller.

If the government could get the interest rate just right and not change it too much, or change it so that people know what is going on, they'd feel happier and be more likely to spend and save in a more predictable way. It is important that the economy doesn't change a lot too often as this makes people nervous and foreign firms won't want to invest into the UK as they won't know what will happen next and will be worried about whether they'll get their money back or not.

The recent recession was an example of people getting nervous and not wanting to spend their money, this is why the UK now has a very low interest rate of 0.5%, the government wants to help people and businesses to grow and increase jobs. This has led to more growth but hasn't led to much increase in prices; in fact, the UK has zero inflation at the moment which is not what theory would suggest.

Some economists think that it is better to increase supply as well as increase demand and that way there can be economic growth as well as not increasing prices. However, these take time and not everyone wants to be trained so they may not be as helpful as expected.

CANDIDATE RESPONSE

"The UK continues to have record low interest rates, the Bank of England has held interest rates have been held at 0.5% since March 2009. During this period of low interest rates economic activity has gradually recovered whereas inflation rates have fluctuated from highs of 5.1% (CPI) to even a short period of deflation."

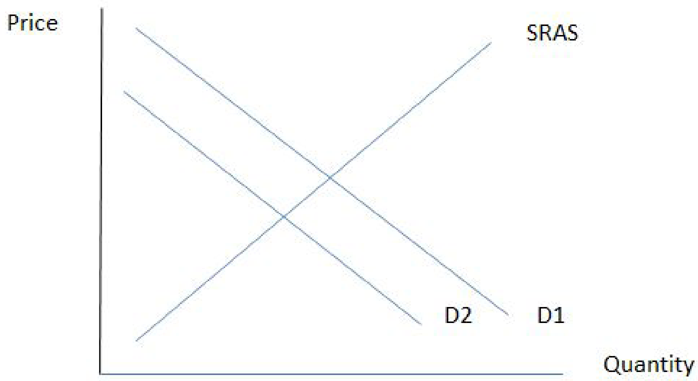
Evaluate the extent to which monetary policy is always able to both stimulate economic activity and achieve price stability [20 marks]

Candidate F –Annotated

Governments use monetary policy to affect the economy and help to get economic growth. Monetary policy is changing the interest rate. Changing the interest rate will affect aggregate demand, if you increase the interest rate you will have less aggregate demand because consumers will have less money to purchase goods and services which will mean that there are fewer injections into the economy.

Firms will want to save their income, because the bank will give them a better interest rate and so they won't hire as many people and this could mean there are more people without a job and so there is less money being spent – a downward spiral. With fewer injections there will be a shift to the left of aggregate demand and a reduction in both prices and output as shown by the diagram below.

There is muddled analysis of the effect of monetary policy and an incomplete and inaccurately labelled diagram.



However, the opposite is true; decreasing the interest rate will result in an increase in the economy as people have more money to invest which is a component of aggregate demand and so an increase in the economy will make prices go up. If prices go up people are more concerned about what they can buy and may think that saving is a good idea. This could make the economy get smaller.

This is simplistic and limited in both analysis and knowledge.

If the government could get the interest rate just right and not change it too much, or change it so that people know what is going on, they'd feel happier and be more likely to spend and save in a more predictable way. It is important that the economy doesn't change a lot too often as this makes people nervous and foreign firms won't want to invest into the UK as they won't know what will happen next and will be worried about whether they'll get their money back or not.

The candidate is trying to evaluate the idea of transparency and confidence but it is limited evaluation.

The recent recession was an example of people getting nervous and not wanting to spend their money, this is why the UK now has a very low interest rate of 0.5%, the government wants to help people and businesses to grow and increase jobs. This has led to more growth but hasn't led to much increase in prices; in fact, the UK has zero inflation at the moment which is not what theory would suggest.

There is some knowledge of the real world which is nice to see (encourage students to provide this in their essays where possible) but, again, it is limited analysis – more descriptive/assertion.

Candidate F – ANNOTATED (cont)

Some economists think that it is better to increase supply as well as increase demand and that way there can be economic growth as well as not increasing prices. However, these take time and not everyone wants to be trained so they may not be as helpful as expected.

Again, the candidate is trying to evaluate. They realise that there is the need for both sides of the economy to be addressed but haven't explored this with any use of economic models, concepts of theories.

There is no real conclusion and no judgement, therefore limited evaluation.

Level 1 **5 marks**

Examiner's summary comments

Level 1 (1–5 marks)

Limited knowledge and understanding of monetary policy, economic activity and price stability.

Limited analysis of the link between monetary policy, economic activity and price stability. A diagram is included which is less than perfect.

Limited evaluation.

The information is basic and communicated in an unstructured way. The information is supported by limited evidence and the relationship to the evidence may not be clear.

The small print

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