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OXFORD CAMBRIDGE AND RSA EXAMINATIONS

Monday 8 June 2020 – Morning

A Level Economics

H460/03 Themes in economics

Resource Booklet

Time allowed: 2 hours
plus your additional time allowance

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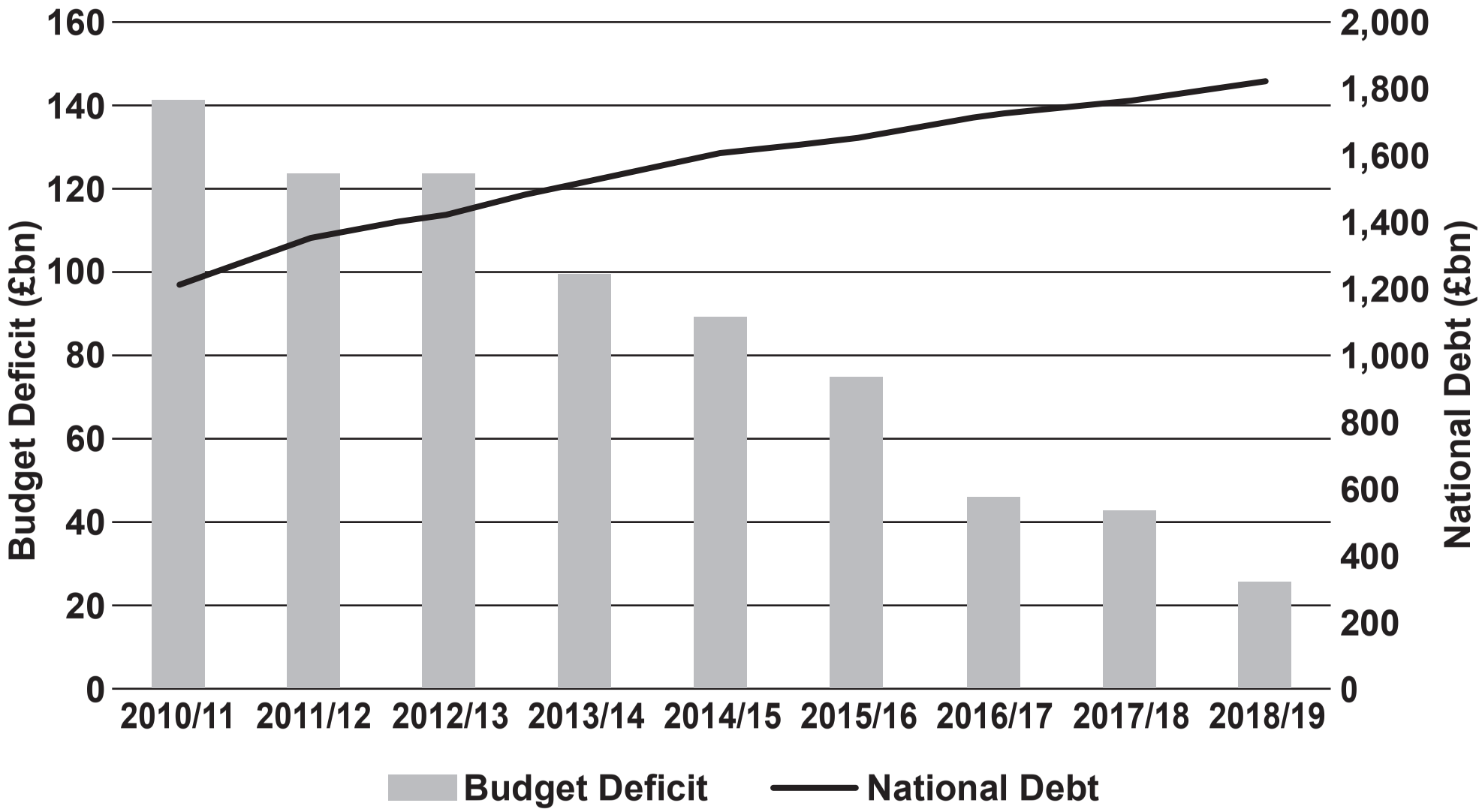
EXTRACT 1 – An end to austerity?

The commitments made by the UK's main political parties in the 2019 General Election campaign marked an end to the austerity economics that had dominated macroeconomic policy for the previous decade.

Following the global financial crisis in 2008, many of the world's advanced economies introduced a range of stimulus measures designed to promote economic recovery and end a period of recession. However, as the Greek economy began to collapse at the end of 2009, in part as a result of a national debt/GDP ratio of more than 120%, policy makers around the world began to fear their own economies were at risk because of unsustainably high levels of borrowing. With the UK's national debt/GDP ratio standing at 69% and forecast to increase to over 100% in the coming years, the Conservative-Liberal coalition came to power in 2010 to eliminate the budget deficit by implementing austerity – a deficit reduction programme focused on significant reductions in public spending and increases in tax revenue. The policy was seen to be crucial in promoting future economic growth and stability. Fig. 1.1 illustrates the impact austerity had on the size of the budget deficit and national debt.

FIG. 1.1 – UK Government's Budget Deficit & National Debt 2010–2019



However, in the 2019 General Election campaign both the Conservative government and its main challenger, the Labour Party, made significant public spending commitments that represented a significant shift away from austerity. The Conservatives promised an £11bn increase in public expenditure by 2024, including pledges to increase expenditure on the NHS, police and schools, whilst also committing to tax cuts for low paid workers. These plans were modest in comparison to the spending commitments by Labour, who pledged to increase public expenditure by £153bn. Individual policies included a 5% pay rise for public sector workers, a green transformation fund to spend on projects such as insulating 27 million homes, compensating the 'WASPI' (Women Against State Pension Inequality) women who had seen an unexpected cut to their state pension entitlements as a result of the state pension age for women being increased to match that for men and the building of social housing.

Both parties moved away from targeting to eliminate the overall budget deficit and instead sought to make a distinction between current and capital expenditure, arguing that achieving a current budget balance should be the new target. Labour committed to meeting this target within five years whilst the Conservatives aimed to achieve it in three.

Whilst the victory of the Conservative Party in the election meant the likely change in direction of macroeconomic policy was not as sharp as it might otherwise have been, it is undoubtedly the case that, after almost a decade of policy designed primarily to eliminate the budget deficit, government borrowing was set to increase. Whilst some economists point

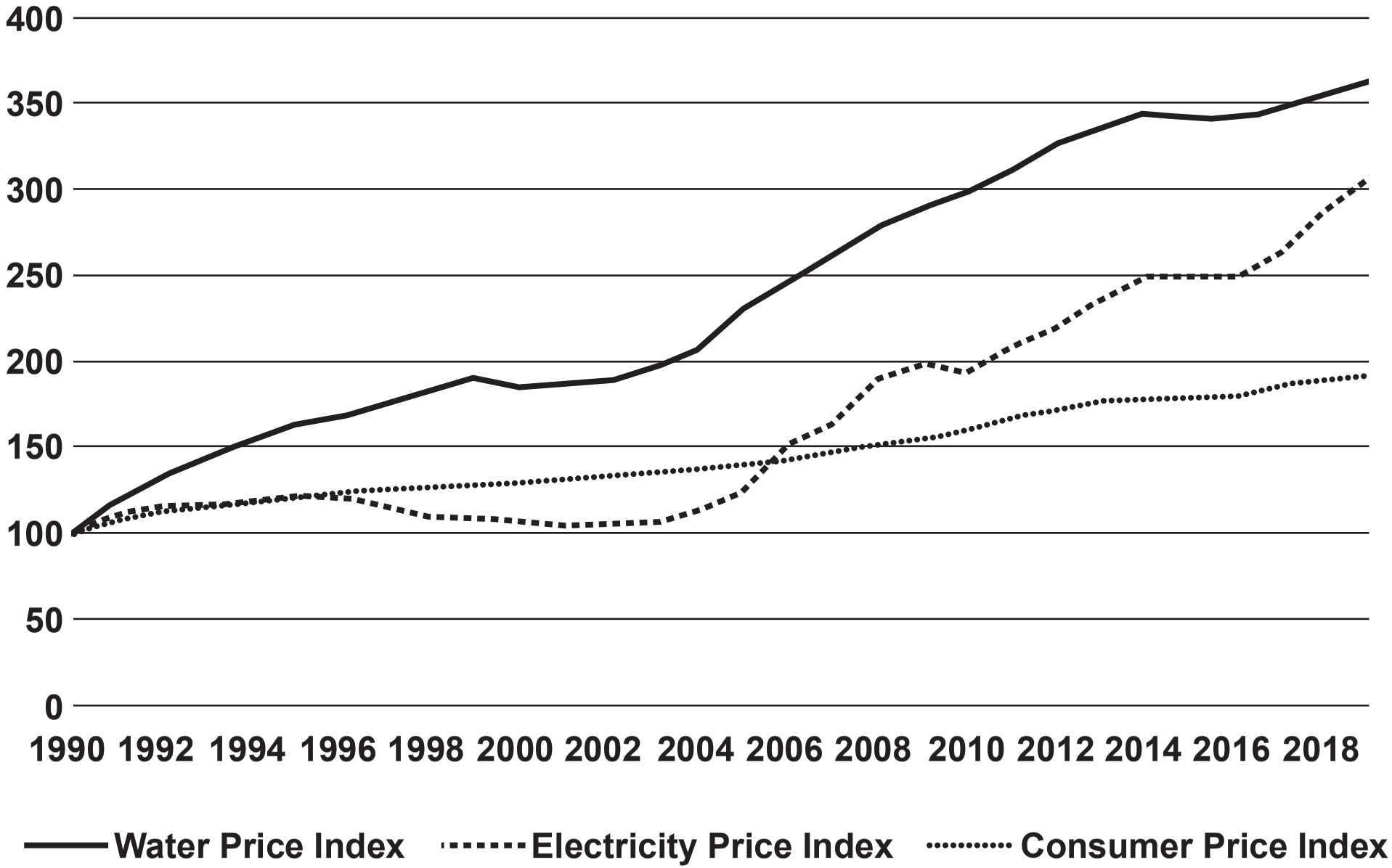
to low costs of borrowing for the government and the relatively low national debt/GDP ratio in the UK in comparison to many other developed economies as evidence that increased government spending can be justified providing it is on capital expenditure, others argue that this risks the hard-earned reputation of fiscal responsibility being destroyed. **65**

EXTRACT 2 – Ownership of public utilities

Amongst the most eye-catching proposals in the Labour Party's manifesto was its commitment to bringing a range of public utilities under government control. The proposal was to nationalise a range of key industries that had been privatised under the Conservative government in the 1980s and early 1990s, which sparked fierce debate over whether the interests of consumers would be best served by these companies operating in the private or public sector.

Two such industries are the water and electricity industry, which were privatised in 1989 and 1990 respectively. The government at the time saw privatisation as essential to boost the performance of the UK economy, arguing the discipline of the marketplace would create competition that would drive efficiency, raise revenue for the government and ultimately bring prices down for consumers. However, thirty years on, some argue privatisation has failed to achieve its stated aims. Fig. 2.1 illustrates what has happened to the price of water and electricity since privatisation.

FIG. 2.1 – Electricity, Water and Consumer Price Index 1990–2018 (Base Year 1990 = 100)



The Labour Party also argued that bringing these utilities into the public sector would enable the significant investment to occur that private firms had not been incentivised to undertake, pointing to the slow renewal of London's water mains by Thames Water and the patchy investment in universal national high-speed broadband coverage by BT as evidence of this. They suggested that the different incentives and objectives that exist between public sector and private sector firms provided a strong case for nationalisation of these private sector monopolies.

The Conservative government however argued the £170bn bill that would be incurred from nationalising the public utilities could not be justified, and that both efficiency and consumer welfare would be better served from these industries remaining in the private sector but with tighter regulation, such as the energy price caps introduced at the start of 2019.

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EXTRACT 3 – Do we need to stop flying to save the planet?

A rare area of agreement between the political parties in the General Election campaign was the need to take action to tackle climate change. Since 1970, global CO_2 emissions have increased by around 90% and the resultant impact of global warming, be it rising sea levels or more intense heatwaves, is becoming increasingly damaging to communities around the world.

In June 2019, the UK became the first major nation to pledge to have net zero carbon emissions by 2050. This was praised by environmentalists who hoped this would encourage other countries to follow the UK's lead by making similar commitments. The commitment was maintained by the Conservative Party in the 2019 General Election whilst the Labour Party went further, setting a target of net zero carbon emissions by 2030.

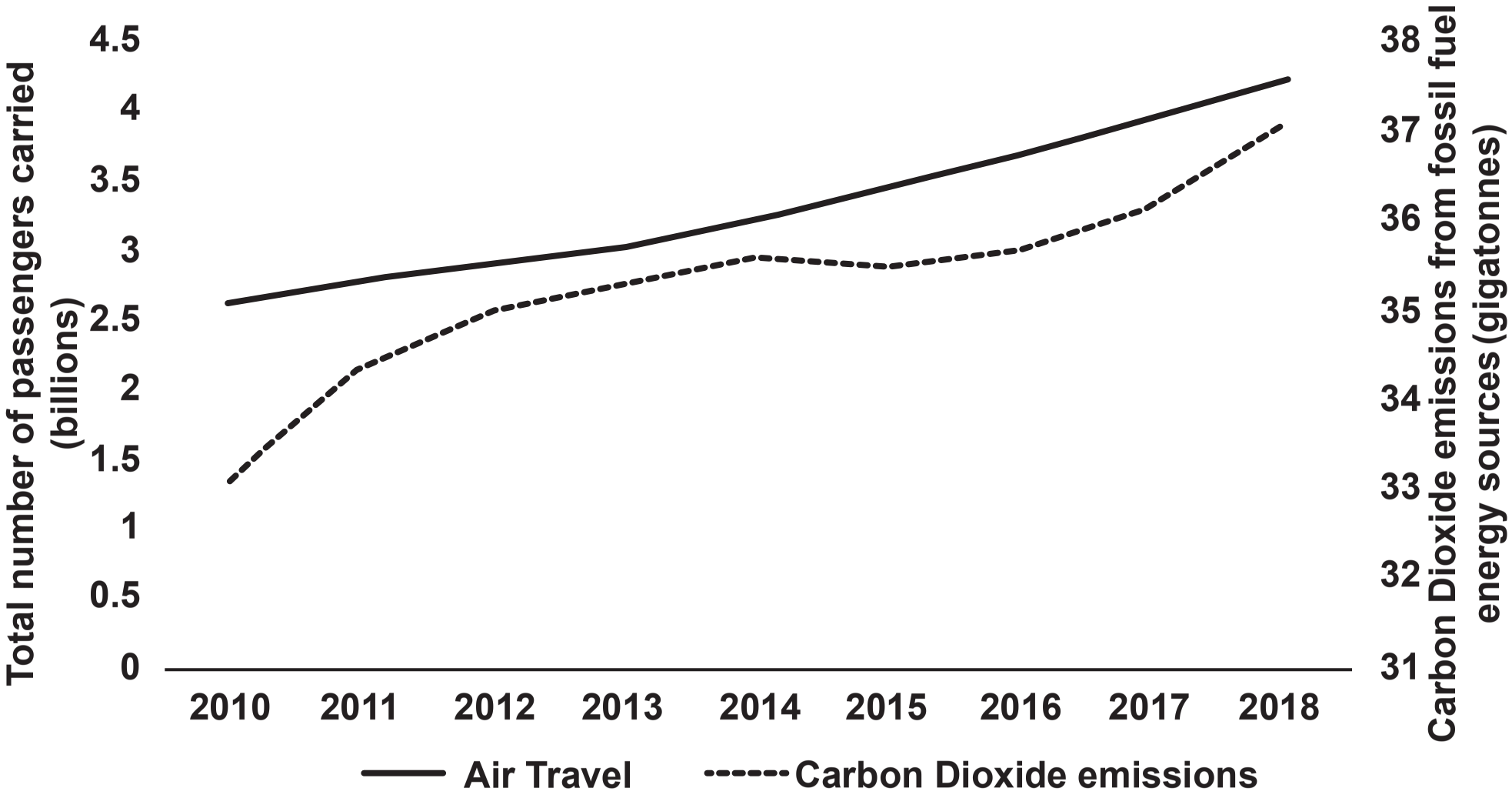
In order for these targets to be achieved, significant change will need to be seen in a number of industries. Fig. 3.1 illustrates the causes of fossil fuel emissions by sector.

FIG. 3.1 – Fossil fuel emissions by sector

Agriculture	24%
Buildings	6%
Electricity & Heat Production	25%
Industry	21%
Other Energy	10%
Transportation	14%

One of the areas most targeted for reducing emissions is the aviation sector. Increasing incomes around the world have significantly increased the demand for air travel, which has particularly harmful impacts on emissions – a journey by plane generates more than twenty times the amount of CO_2 emissions compared to travelling the same distance by train. The relationship between passenger journeys by air and carbon emissions is shown in Fig. 3.2 opposite.

FIG. 3.2 – Air passenger journeys and carbon emissions 2010–2018



A proposal made by some environmental lobbyists is for the government to legislate to limit all individuals to one return flight per year. It is argued this would help reduce the negative externalities associated with air travel and make a substantial contribution to addressing the challenge of climate change. However, business groups remain concerned about the detrimental impact such an action would have on the UK's status as a global centre of financial services, more broadly suggesting it would limit the potential gains from globalisation that are needed to generate future economic growth. Such groups argue such extreme action is not necessary when there remain less damaging alternative policy solutions to reduce global emissions.

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