

National Junior College
SH2 Preliminary Examinations for General Certificate of Education Advanced Level
Higher 1

ECONOMICS

8823/01

Paper 1

2 September 2019

3 hours

Additional Materials: Answer Booklet

READ THESE INSTRUCTIONS FIRST

Write down all the necessary information on the front page of the answer booklet.

Write in dark blue or black pen.

You may use an HB pencil for any diagrams, graphs or rough working.

Do not use staples, paper clips, glue or correction fluid.

DO **NOT** WRITE IN ANY OF THE MARGINS.

Answer **all** questions.

The number of marks is given in brackets [] at the end of each question or part question.

This document consists of **7** printed pages and **1** blank page.

Answer **all** questions.

Question 1: Climate Change

Figure 1: Food Price Index



Source: *Food and Agriculture Organisation*

Extract 1: Global food prices continue to fall despite climate concerns

When El Nino wreaked havoc on the world's population during 2015, causing floods in Southeast Asia and rains in Brazil, it also damaged crops, especially sugar and palm oil. In October, prices shot up, particularly for sugar. However, the rise was a rare exception – international prices for most foods, including sugar and dairy, have been falling for the past four years.

Meanwhile, the Food and Agricultural Organisation (FAO) continues to stress that food security remains a great concern. People in some 33 countries, with the majority in Africa, may face food shortages. Instead of producing crops for food, farmers produce fuel from crops like corn in the United States (US) due to heavy government subsidies. The International Energy Agency estimates that global production of biofuels met about one third of the 900,000-barrel-per-day increase in worldwide demand for oil. The Gates Foundation, founded by Bill Gates, recently announced \$306 million in subsidies to boost agricultural yields in the developing world, with nearly \$165 million to replenish depleted soils in Africa and to equip and train farmers. Numerous countries, from Argentina to Russia, have erected minimum price levels on exports to try to shore up domestic food supply.

Source: Adapted from *Financial Times*, 14 January 2016

Extract 2: Global food prices around two-year high as meat, dairy and wheat prices climb

International food prices soared to around two-year highs during June, fueled by higher prices for wheat, meats and dairy products such as butter. Analysts say stronger global demand for

meat is helping to keep prices strong. Beef is one of the fastest-growing meat categories in Asia, and the US last month returned to shipping supplies to the Chinese market for the first time in 13 years. The opening of US beef sales to China could make it a multibillion-dollar market to American producers within a few years. Beef demand in China has grown due to a rise in household incomes and a taste for more Western foods.

In the US market, the barbecue-grilling season has helped spur demand and helped support recent prices for meats. "Supplies still appear ample to meet demand and that is probably going to lead to moderation in prices." said Bill Lapp, president at Advanced Economic Solutions in Omaha.

Source: *CNBC*, 6 July 2017

Extract 3: Food and farming policies 'need total rethink'

A big meeting in London will look at how reforms could help halt species extinction and meet climate goals. The campaigning organisation, Compassion in World Farming (CiWF) warns that "there will be catastrophic impacts for life on Earth unless there is a global move away from intensive farming".

Farming contributes to climate change through the release of methane (a major greenhouse gas) from the production of livestock animals. The aim would be to properly integrate objectives such as food security, climate change, animal welfare and human health – so one is not pursued at the expense of the other.

Source: *BBC News*, 5 October 2017

Extract 4: Singapore to impose carbon pricing in move to cut greenhouse emissions

Carbon pricing such as a carbon tax could be based on average emissions for production of an item. "A carbon price would send appropriate price signals to encourage changes in energy consumption, provide market incentives for the adoption of energy-efficient technologies and low-carbon solutions, and stimulate growth in green industries. But a carbon price will incur costs, including affecting Singapore's competitiveness. Its overall impact will have to be studied." said National Climate Change Secretariat.

The petroleum refining, chemicals and semiconductor sectors made up the bulk of greenhouse emissions in Singapore. Shell, together with five other European oil majors such as BP and Statoil, said they would discourage high-carbon options and help to stimulate investments in the right low-carbon technologies. ExxonMobil has said that it is supportive of a carbon tax.

Source: *The Straits Times*, 17 February 2017

Extract 5: China unveils an ambitious plan to curb climate change emissions

China released plans to start a giant market to trade credits for the right to emit planet-warming greenhouse gases. The nationwide market would initially cover China's vast, state-dominated power generation sector. China's announcement could also disappoint those who were hoping the long-promised emissions market would cover the country's broader economy. China's booming car culture, its industrialising agriculture sector and its huge chemical complexes, cement factories and steel mills are also big emitters.

Under emission markets, power companies and others effectively pay the right to pollute beyond a government-mandated limit. Those that cut their emissions could sell permits to pollute to dirtier companies, ideally at a healthy price. So far, such efforts have been underwhelming. Markets in Europe and at the provincial level in China have faltered because the authorities issued too many credits to existing polluters. That gave companies little reason to buy credits, or to cut their own emissions and sell the credits. China was likely to issue many credits starting early next year in response to domestic political pressures, and then gradually tighten annual allocations to force up the price.

Having them trade with each other might help the central government figure out more rules to regulate trading in less regulated sectors, and also to identify which companies are the most efficient at reducing emissions. Kelly Sims Gallagher, a professor of environmental policy at Tufts University, said the Chinese government was right to be cautious by starting with just the electricity sector. “It’s important to realise you can’t do that overnight,” Ms. Gallagher said.

Source: *New York Times*, 19 December 2017

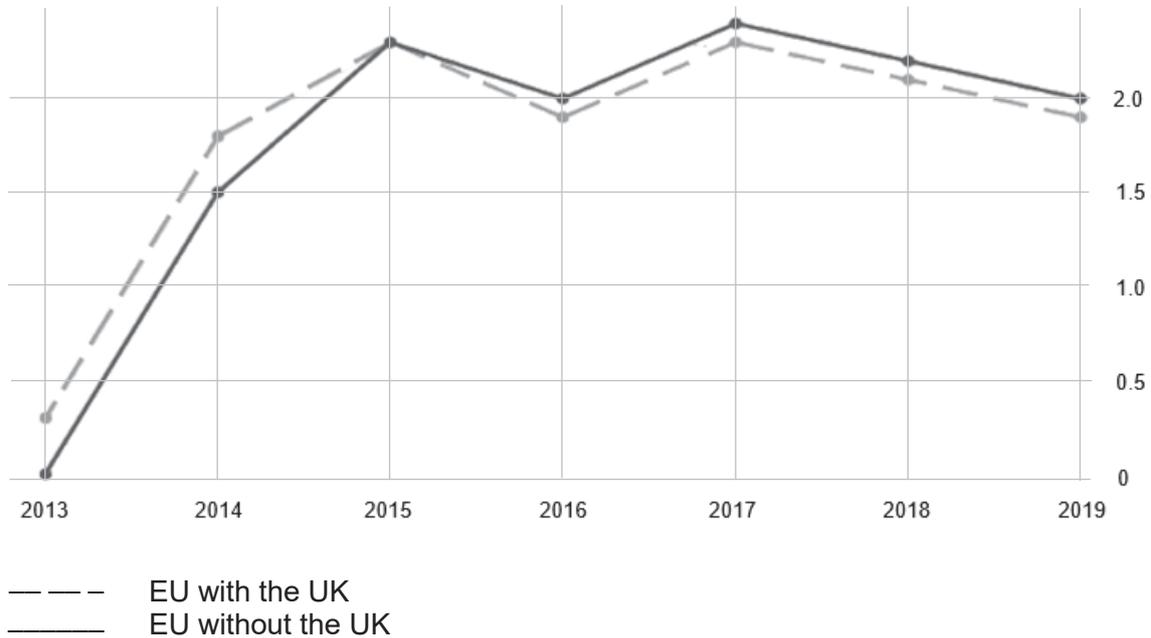
Questions

- (a) Using Figure 1, describe the trend of global food prices during the period 2014–2017. [1]
- (b) With reference to Extract 1:
- (i) Explain how the heavy government subsidies in the production of crops for biofuel affects the market for crops for food in the US. [4]
- (ii) Explain the assertion that the impact of El Nino has caused the prices of crops to shoot up. [2]
- (c) Using **two** demand factors and a relevant elasticity concept, explain the “moderation in beef prices” (Extract 2). [6]
- (d) With the aid of a diagram, explain why the market might fail in the case of intensive farming. [5]
- (e) Explain and comment on the view that the implementation of a carbon tax will incur costs, including affecting Singapore’s competitiveness. [8]
- (f) Explain and evaluate the effectiveness of carbon emission-trading scheme in reducing rising greenhouse emissions in China. [7]
- (g) Discuss whether a provision of subsidies to boost agricultural yields in the developing world is the best policy to overcome food shortages. [12]

[Total: 45]

Question 2: Brexit and the European economy

Figure 2: Economic growth rate in the United Kingdom (UK) and European Union (EU)



Source: *Financial Times*

Extract 6: Austerity has strangled Britain

In a statement, the Office of Budget Responsibility (OBR) said it expects growth to slow "as public spending cuts intensify and Brexit-related uncertainty continues to bear down on activity."

Since the eurozone crisis, many governments have turned to austerity. Across Europe, and in Britain, they have tried frantically to cut their spending, to repay debts as a result of the crisis. Austerity has not only damaged the European economies, but threatens future growth. There is a long list of investments that governments should be making, such as strengthening infrastructure, transport and communications, investment in education and in families.

In this election, it is the Labour party that is advocating the kind of economic plan that is right for the UK. The party proposes to finance its plans on carefully thought-out proposals based on taxing the higher-income group and ensuring that corporations pay what they should. The evidence shows that these actions will not slow down growth but will help strengthen the UK economy.

Source: *The Guardian*, 7 June 2017

Extract 7: UK economy lags behind G7 after 2017 growth rate cut

Gross Domestic Product (GDP) growth slowed to a quarterly 0.4% from a previous estimate of 0.5%, wrong-footing economists and reducing 2017 growth as a whole to 1.7%, its lowest since 2012. The downgrade of the full-year and fourth-quarter growth rates raised questions about the strength of the economy as the Bank of England prepares to raise interest rates.

The country has relied heavily on the unexpectedly robust global economy to sustain its economic growth while consumers have been squeezed by higher inflation caused by the fall in the pound after the Brexit vote.

The UK is a net importer of energy, meaning the fall in the value of the pound makes commodity purchases more expensive. In February, the UK's inflation rate jumped to 2.3%, its highest level since September 2013, on the back of higher fuel costs, especially transport fuels. The retail petrol prices have been increasing, off the back of the OPEC and non-OPEC pact from November 2016 to cut back crude oil production.

Despite a possible boost to manufacturing exports, the depreciation of the pound since the Brexit vote must reflect expectations of slower growth for the UK economy in the next few years and beyond. The latest GDP data suggest that the economy remains in a fragile state and does not need to be cooled with another rate rise as soon as May.

Source: Adapted from *Reuters*, 22 February 2018

Extract 8: UK wage growth picks up as unemployment rate falls again

UK wage growth has started to edge up amid signs that the lowest level of unemployment since the mid-1970s may be increasing workers' bargaining power, which can be attributed to the robust global economy. But despite the additional jobs and the acceleration in wage growth, living standards remain under pressure because wages have failed to keep pace with inflation, which stood at 2.6% in June.

A tighter labour market is seen as strengthening the hand of the Bank of England's monetary policy committee, who are pressing for an increase in interest rates. The availability of jobs in the UK continues to attract workers from overseas, but the rate of increase had slowed over the past year.

Source: *The Guardian*, 16 August 2017

Extract 9: Germany's biggest Brexit boon

The biggest economy in Europe is a ticking demographic time bomb. The number of Germans approaching retirement is growing strongly. The inevitable result of buoyant businesses and retiring baby boomers will be a growing shortage of skilled workers. Almost 20% of German firms also said that a shortage of labor is currently limiting their production – the highest value ever recorded. Job openings have been difficult to fill in some professions, such as in engineering, software and health care. Companies can try to attract migrants to fill the jobs.

During the eurozone crisis, Britain benefitted from a surge of young and well-educated European workers who were struggling to find jobs. But after last year's Brexit referendum, net migration of EU citizens to Britain fell sharply.

With Germany's comparatively old population, retiring baby boomers, growing economy and reasonably flexible labour market and immigration conditions, it has the most to gain as Brexit changes the patterns of migration within the EU.

Source: *Centre for European Reform*, 11 December 2017

Extract 10: Brexit will hit Germany's car industry

Economists say a combination of tariffs and new regulations would result in fewer sales for German businesses, especially for its £26 billion car industry.

If the UK leaves the EU without a trade agreement in place, it will fall back on the World Trade Organisation rules to deal with other countries. The UK will be treated as a "third country" – alongside the United States, Japan and Australia – which carries a strict set of quality regulations and customs duties. This would mean the EU's standard export tariff of 10% would probably be applied to German car manufacturers.

Source: *Express*, 1 November 2017

Questions

- (a) Using the data in Figure 2, compare the economic growth rate in the EU with the UK and EU without the UK over the period 2015–2019. [2]
- (b) Explain how government spending can boost the UK economy and comment on the appropriateness of taxing the higher-income group and the corporations to finance the government spending. [6]
- (c) With reference to Extract 7:
- (i) With the aid of a diagram, explain the effect of the cutback in crude oil production on inflation in the UK. [5]
- (ii) Assess the validity of the view that the UK economy 'does not need to be cooled with another rate rise'. [9]
- (d) Explain why living standards in Britain has been under pressure despite the acceleration in wage growth. [3]
- (e) With reference to Extract 10, explain whether consumers or the German car manufacturers are likely to bear a greater burden of the tariffs. [8]
- (f) Discuss the likely impact of Brexit on economic growth in the UK and Germany. [12]

[Total: 45]

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Question 1**Suggested Answers:**

(a)	Using Figure 1, describe the trend of global food prices during the period 2014-2017. [1] Global food prices decreased from 2014 to 2017. [1]
(b)	With reference to Extract 1:
(i)	Explain how the heavy government subsidies in the production of crops for biofuel affects the market of crops for food in the US. [4]
	<ul style="list-style-type: none"> • Government subsidies in the production of crops for biofuel such as corn will increase the supply of crops for biofuel. • Crops for biofuel and crops for food are substitutes in production. • As more resources are used to produce crops for biofuel, the supply of crop for food decreases. • The fall in supply of crops for food leads to an increase in price and a fall in equilibrium quantity.
(ii)	Explain the assertion that the impact of El Nino has caused the prices of crops to shoot up. [2]
	<ul style="list-style-type: none"> • The demand for crops is price inelastic due to a high degree of necessity to consume crops as food to survive. • This leads to a more than proportionate increase in the prices of crops, causing the prices of crops to shoot up.
(c)	Using two demand factors and a relevant elasticity concept, explain the “moderation in beef prices” (Extract 2). [6]
	<ul style="list-style-type: none"> • The two demand factors that caused an increase in demand for beef are changes in taste and preference towards the consumption of beef and also an increase in income. • The increase in demand due to the two factors cause an increase in beef prices. • As mentioned in Extract 2, there is ample supplies of beef. This suggests that there is adequate stock. • This means that the price elasticity of supply of beef is greater than one. • The increase in demand, will bring about a moderation in beef prices.
(d)	With the aid of a diagram, explain why the market might fail in the case of intensive farming. [5]
	<ul style="list-style-type: none"> • Intensive farming results in climate change. Such third party effects is known as negative externalities which impose an external cost to the society. • This results in a divergence between the marginal private cost (MPC) and the marginal social cost (MSC) of farming. • Referring to Figure 1, the free market equilibrium output is Q_M where the marginal private cost is equal to marginal private benefit ($MPC=MPB$).

- The social optimal output is Q_S where $MSB=MSC$. Hence, there is an overproduction of $Q_S Q_M$ of farmed animals.
- This results in a deadweight loss of area abc.

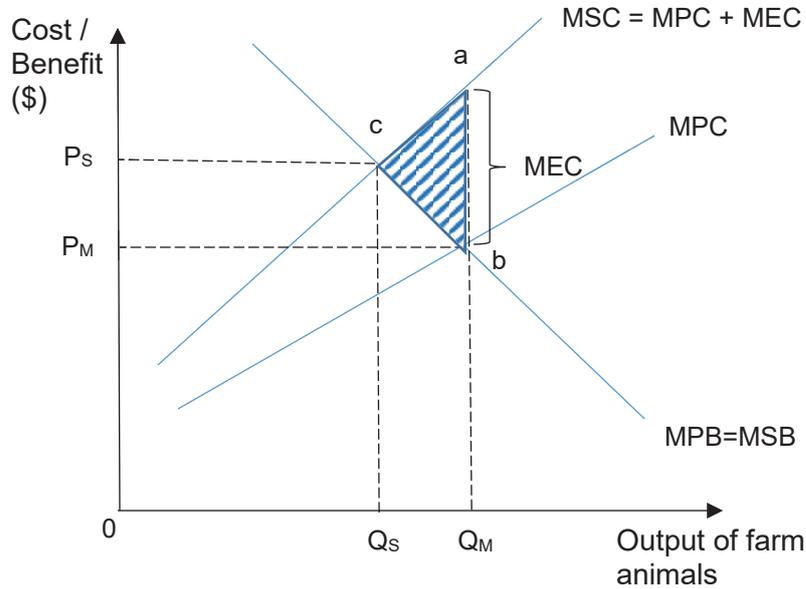


Figure 1: Market for farmed animals

(e) Explain and comment on the view that a carbon tax will incur costs, including affecting Singapore's competitiveness. [8]

Body 1: Explain how a carbon tax affects Singapore's export competitiveness

- The imposition of a carbon tax is considered an indirect tax on the producers. It shifts the supply curve leftward in a parallel manner assuming it is a specific tax.
- The equilibrium price of the good increases from P_0 to P_1 .
- Suppose that good A is one of the goods for exports and the other exports also face an increase in price, it leads to an increase in price of exports in general, which will affect the price competitiveness of exports in the global market.



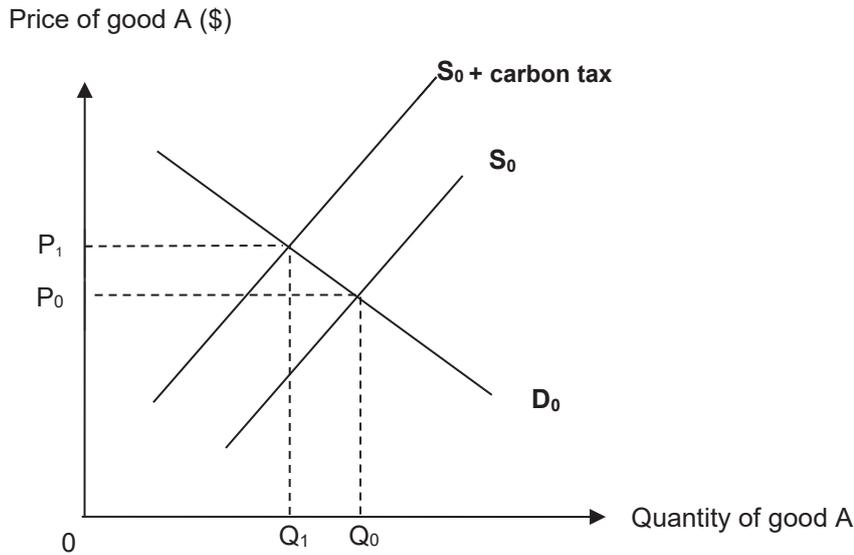


Figure 2: Market for Good A

Body 2: Explain how a carbon tax affect Singapore competitiveness in terms of foreign direct investment

- With an increase in cost of production, foreign investors might be deterred from investing in Singapore in terms of setting up new companies and investing to expand existing companies in Singapore.

Body 3: Comment on how a carbon tax might not affect Singapore's export competitiveness

- More investment could be made in green industries to reduce the level of carbon emissions.
- With the reduction in carbon emissions, these firms that successfully adopt energy efficient technologies would not experience a significant increase in cost of production, thereby reducing the risk of losing export competitiveness due to a price increase.

Body 4: Comment on how a carbon tax might not affect foreign direct investment

- The investment in green industries might attract similar companies from overseas to invest in Singapore due to rising demand for such products and services.
- FDI might increase instead of decrease which means Singapore's competitiveness is unlikely to be negatively impacted.

(f)	Explain and evaluate the effectiveness of carbon emission-trading scheme in reducing rising greenhouse emissions in China. [7]
	<p><u>Introduction:</u></p> <ul style="list-style-type: none"> • China is implementing carbon trading scheme gradually and it is now imposed on state-dominated power generation sector in the short run.

	<ul style="list-style-type: none"> China has plans to roll out the scheme further to cover more sectors in the long run since the large emitters of greenhouse gases include car, agriculture, chemical, cement and steel industries. <p><u>Body 1: Explain emission-trading scheme</u></p> <ul style="list-style-type: none"> The system of tradable permits is a combination of command-and-control and market-based system of resolving externalities. Each firm is given a permit to produce a given level of pollution. If the firm produces less pollution than what they are legally permitted to produce, the firm is given a credit. This credit can then be sold to another firm, allowing the other firm to exceed its original limit. The polluting firms internalise the externality of pollution as there is an opportunity cost of polluting. <p><u>Body 2: Evaluate the effectiveness of carbon emission-trading scheme in reducing rising greenhouse emissions in China</u></p> <ul style="list-style-type: none"> The main advantage of tradable permits is that the government can simply determine the total amount of permitted discharge according to the ability of the environment to absorb the pollutants; it can do this without any knowledge of the specific costs and benefits of individual firms. The market in tradable permits can then allocate the reduction in pollution to where it can achieve at least cost. However, critics have argued that the tradable permits system which gives firms a “right to pollute” is not morally right. Firms which find that the costs of the permits is lower than their abatement costs (costs of eliminating pollution), would buy more permits to pollute. As such, these firms might not have the incentive to reduce pollution. Another issue of this system is deciding how to allocate the permits to firms. If there are many polluting firms, regulators would be concerned about the administrative costs. If there are too many credits, companies have little reason to buy credits, or to cut their own emissions.
(g)	<p>Discuss whether a provision of subsidies to boost agricultural yields in the developing world is the best policy to overcome food shortages. [12]</p>
	<p><u>Introduction:</u></p> <ul style="list-style-type: none"> The concern on the possibility of facing food shortages in 33 countries have led to non-profit organisations such as the Gates Foundation and governments to react to resolve it. Food shortages occur as quantity demanded outweighs the quantity supplied at the original price levels. According to Extract 1, a provision of subsidies to boost agricultural yields in the developing world include both funds to replenish soils in Africa as well as to equip and train farmers. <p><u>Thesis:</u> <u>Subsidies to replenish soil is effective to overcome food shortages</u></p> <ul style="list-style-type: none"> The provision of subsidies to boost agricultural yields is considered an indirect subsidy paid to the farmers. These subsidies help to reduce the cost of production by providing funds to replenish soils.

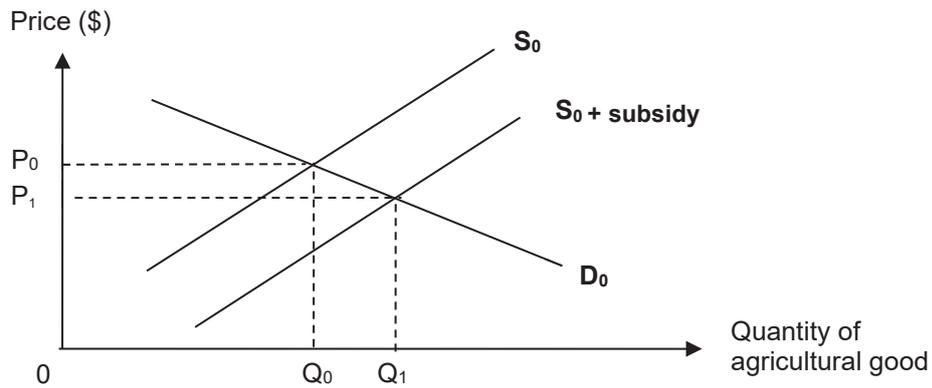


Figure 3: Market for agricultural goods

- With reference to Figure 3 above, the supply curve shifts downwards by the full amount of the indirect subsidy from S_0 to $S_0 + \text{subsidy}$.
- The increase in quantity of agricultural goods reduces the food shortage faced by developing countries.

Anti-Thesis

Limitations of subsidies

- The limitation of using subsidies to resolve food shortages is that it is often difficult to assess the exact amount of subsidies to be provided.
- If the subsidies provided is insufficient due to a lack of funds, then it might only temporarily solve the problem by reducing the price of soil or cost of production.

Thesis

Subsidies to equip and train farmers is effective to overcome food shortages

- By providing equipment and training to farmers, the cost of production decreases leading to an increase in supply.
- Hence quantity of agricultural goods will increase, reducing food shortages effectively.

Anti-Thesis

Limitations of equipping and training

- The effectiveness of education on new ways of farming with the help of equipment depends on the receptiveness of the farmers and the effect is only seen in the long run.

Anti-Thesis

Minimum price levels on exports to try to shore up domestic food supply is effective

- In a free market without government intervention, the free market equilibrium price and quantity determined by the free market forces of demand D_0 and supply S_0 would be at P_0 and Q_0 respectively, as shown by Figure 4.

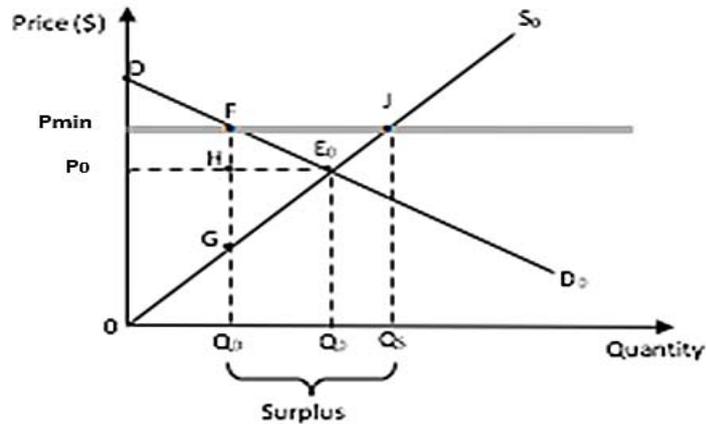


Figure 4: Effects of a Price Floor on exports

- Given that the price floor is set at P_{min} which is above the free market equilibrium price P_0 , a surplus of $Q_S Q_D$ exists as the corresponding quantity supplied at Q_S is larger than the quantity demanded at Q_D (also the quantity transacted).
- These surpluses are not exported and thus sold in the domestic market, increasing the supply of domestic supply of agricultural goods. The increase in supply will help to alleviate the food shortages.

Overall Evaluation:

- Whether a provision of subsidies to boost agricultural yields in the developing world is the best policy to overcome food shortages depends on time period. (students can compare long run and short run needs)

Mark Scheme

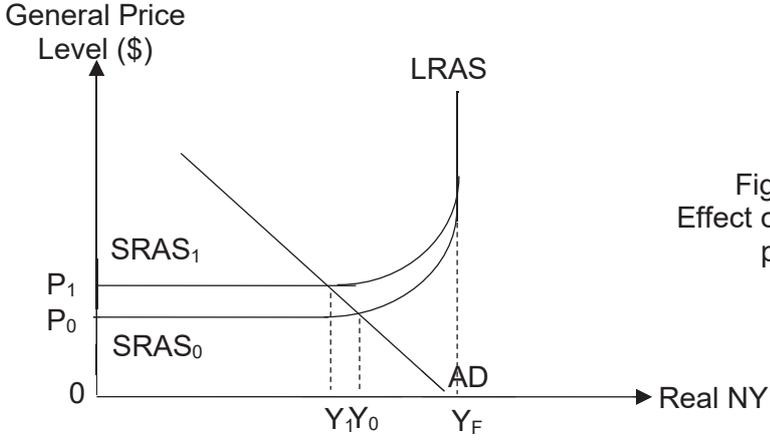
<p>L3 7-9 marks</p>	<p>For an answer that demonstrates knowledge and understanding with excellent application and analysis:</p> <p>Excellent breadth that considers the following economic concepts in explaining multiple and balanced perspectives, viewpoints, relationships and factors. MOST points chosen should be of relevance and significance in answering the question.</p> <p>Excellent depth in economic analysis that reflects the following in MOST explanations. Accurate use of economic concepts, clear elaboration, and precise use of economic terminologies, language and phrasing.</p> <p>The answer should also be supported by: Well-labelled and well referred to diagram(s) / Tool(s) of analysis drawn with precision (where appropriate). Evidence(s). Logical structure.</p>
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	<p>L2 4-6 marks</p>	<p>For an answer that demonstrates knowledge and understanding but lacks application and analysis:</p> <p>At least GOOD breadth that considers the following economic concepts in explaining multiple and balanced perspectives, viewpoints, relationships and factors. MOST points chosen should be of relevance and significance in answering the question.</p> <p>At least GOOD depth in economic analysis that reflects the following in MOST explanations. Accurate use of economic concepts, clear elaboration, and precise use of economic terminologies, language and phrasing.</p> <p>The answer should also be supported by: Well-labelled and well referred to diagram(s) / Tool(s) of analysis drawn with precision (where appropriate). Evidence(s). Logical structure.</p>	
	<p>L1 1-3 marks</p>	<p>For an answer that demonstrates knowledge but lacks understanding, application and analysis:</p> <p>INSUFFICIENT breadth that considers the following economic concept(s). Point(s) chosen may be of relevance but may not be of significance in answering the question.</p> <p>INSUFFICIENT depth in economic analysis that may reflect the following: Lack of accuracy in the use of economic concepts, lack of clarity in elaboration, and lack of precision in the use of economic terminologies, language and phrasing.</p>	
	<p>E2 2-3 marks</p>	<p>For an evaluation that contains:</p> <ul style="list-style-type: none"> ➤ A synthesis of earlier economic arguments to arrive at relevant judgements/decisions (i.e. answer the question). ➤ Well-explained criteria-based evaluative comments supported by accurate and clear analysis to provide fairness in views. ➤ A good summative conclusion. 	
	<p>E1 1 mark</p>	<p>For an evaluation that contains:</p> <ul style="list-style-type: none"> ➤ Relevant but unexplained evaluative judgement(s)/ statement(s) i.e. evaluative judgement(s)/statement(s) not supported by analysis or ➤ A relevant conclusion. 	

Question 2

Suggested Answers:

(a)	Using the data in Figure 2, compare the economic growth rate in the EU with the UK and EU without the UK over the period 2015–2019. [2]
	<ul style="list-style-type: none"> • From 2015 to 2019, the economic growth rate in the European Union with and without the UK decreased. [1] • However, the economic growth rate in the European Union without the UK is consistently higher than that with the UK. [1]
(b)	Explain how government spending can boost the UK economy and comment on the appropriateness of taxing the higher-income group and the corporations to finance the government spending. [6]
	<p><u>Explain how government spending boosts economy</u></p> <ul style="list-style-type: none"> • Government spending (G) can increase aggregate demand (AD), since it is a component of AD. • Real national output is increased. • Therefore, there would be economic growth. <p><u>Comment on appropriateness of taxing those at the top and the corporations to finance spending</u></p> <ul style="list-style-type: none"> • The Labour party’s plans of taxing the higher-income bracket and corporations to finance government spending may lead to a decrease in consumption and investment. • Therefore, government spending may end up merely replacing the spending on consumption and investment, with no added impact on the economy. • However, it is appropriate to fund the fiscal spending using taxes on those with higher income and firms in order for greater inclusivity in economic growth.
(c)	With reference to Extract 7:
(i)	With the aid of a diagram, explain the effect of the cutback in crude oil production on inflation in the UK. [5]
	<ul style="list-style-type: none"> • The cutback in crude oil production causes the price of oil to rise. • As the price of oil, which is imported from the Middle East increases, there will be an increase in cost of production across the UK economy, leading to a fall in short-run aggregate supply (SRAS) from $SRAS_0$ to $SRAS_1$ in Figure 1. • Well-labelled and referred to diagram

	 <p style="text-align: right;">Figure 1: Effect of rise in oil price</p> <ul style="list-style-type: none"> As such, price levels increase from P_0 to P_1, leading to inflation.
(ii)	<p>Assess the validity of the view that the UK economy 'does not need to be cooled with another rate rise'. [9]</p>
	<p><u>Introduction:</u></p> <ul style="list-style-type: none"> A rate rise refers to an interest-rate based monetary policy which is usually carried out when an economy is running at full capacity, with demand-pull inflation. An interest rate rise is implemented to curb inflation. <p><u>Explain interest-rate policy using indirect transmission mechanism</u></p> <ul style="list-style-type: none"> When money supply is decreased from MS_0 to MS_1, as shown in Figure 2 below, the interest rate increases from r_0 to r_1.



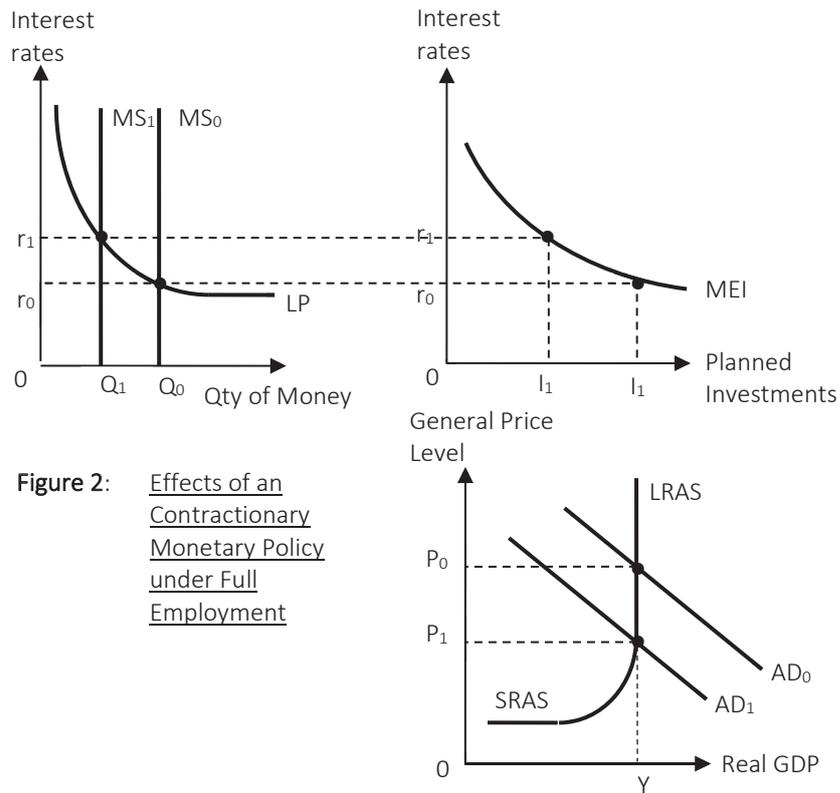


Figure 2: Effects of an Contractionary Monetary Policy under Full Employment

- As interest rate rises, the cost of borrowing rises. Therefore, the rate of return from investments fall, leading to a fall in planned investments from I_0 to I_1 .
- As investment (I) falls, aggregate demand (AD) falls from AD_0 to AD_1 , since I is a component of AD .
- Hence, real national output falls and the general price level falls from P_0 to P_1 , easing demand-pull inflation.

The economy does not need to be cooled with a rate rise

Slowing GDP in the UK

- The GDP in the UK slowed even with robust global economy, indicating that the economy could fall into a recession should there be an interest rate rise.
- Aggregate demand (AD) will fall since C and I fell, causing the real output to fall.
- Given the weak economy in the UK, this could lead to an even greater slowdown in the economy or a recession.

The economy may need to be cooled with a rate rise

Explain demand-pull inflation in the UK

- The fall in the value of the pounds led to a fall in prices of exports in foreign currency. Therefore, export revenue will increase since demand for exports

		<p>increase, as seen from Extract 7 where manufacturing exports are likely to gain from the depreciation.</p> <ul style="list-style-type: none"> • Net exports increase and thus, AD increases, leading to increases in real national output. <p><u>Evaluative conclusion:</u> <u>Root cause of inflation</u></p> <ul style="list-style-type: none"> • Whether an increase in interest rate is required depends on the root cause of inflation in the UK. <p><u>Mark Scheme</u></p> <table border="1" data-bbox="336 745 1372 1420"> <tr> <td data-bbox="336 745 472 1420" style="text-align: center;"> <p>L2 4-6 marks</p> </td> <td data-bbox="472 745 1372 1420"> <p>For an answer that demonstrates knowledge and understanding with excellent application and analysis:</p> <ul style="list-style-type: none"> ➤ Excellent breadth that considers the following economic concepts in explaining multiple and balanced perspectives, viewpoints, relationships and factors. MOST points chosen should be of relevance and significance in answering the question. ➤ Excellent depth in economic analysis that reflects the following in MOST explanations. ➤ Accurate use of economic concepts, clear elaboration, and precise use of economic terminologies, language and phrasing. <p>The answer should also be supported by:</p> <ul style="list-style-type: none"> ➤ Well-labelled and well referred to diagram(s) / Tool(s) of analysis drawn with precision (where appropriate). ➤ Evidence(s). ➤ Logical structure. </td> </tr> </table> <table border="1" data-bbox="336 1451 1372 1957"> <tr> <td data-bbox="336 1451 472 1957" style="text-align: center;"> <p>L1 1-3 marks</p> </td> <td data-bbox="472 1451 1372 1957"> <p>For an answer that demonstrates knowledge and understanding but lacks application and analysis:</p> <ul style="list-style-type: none"> ➤ At least GOOD breadth that considers the following economic concepts in explaining multiple and balanced perspectives, viewpoints, relationships and factors. MOST points chosen should be of relevance and significance in answering the question. ➤ At least GOOD depth in economic analysis that reflects the following in MOST explanations. ➤ Accurate use of economic concepts, clear elaboration, and precise use of economic terminologies, language and phrasing. <p>The answer should also be supported by:</p> </td> </tr> </table>	<p>L2 4-6 marks</p>	<p>For an answer that demonstrates knowledge and understanding with excellent application and analysis:</p> <ul style="list-style-type: none"> ➤ Excellent breadth that considers the following economic concepts in explaining multiple and balanced perspectives, viewpoints, relationships and factors. MOST points chosen should be of relevance and significance in answering the question. ➤ Excellent depth in economic analysis that reflects the following in MOST explanations. ➤ Accurate use of economic concepts, clear elaboration, and precise use of economic terminologies, language and phrasing. <p>The answer should also be supported by:</p> <ul style="list-style-type: none"> ➤ Well-labelled and well referred to diagram(s) / Tool(s) of analysis drawn with precision (where appropriate). ➤ Evidence(s). ➤ Logical structure. 	<p>L1 1-3 marks</p>	<p>For an answer that demonstrates knowledge and understanding but lacks application and analysis:</p> <ul style="list-style-type: none"> ➤ At least GOOD breadth that considers the following economic concepts in explaining multiple and balanced perspectives, viewpoints, relationships and factors. MOST points chosen should be of relevance and significance in answering the question. ➤ At least GOOD depth in economic analysis that reflects the following in MOST explanations. ➤ Accurate use of economic concepts, clear elaboration, and precise use of economic terminologies, language and phrasing. <p>The answer should also be supported by:</p>
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		E2 2-3 marks	<p>For an evaluation that contains</p> <ul style="list-style-type: none"> ➤ A synthesis of earlier economic arguments to arrive at relevant judgements/decisions (i.e. answer the question). ➤ Well-explained criteria-based evaluative comments supported by accurate and clear analysis to provide fairness in views. ➤ A good summative conclusion.
		E1 1 mark	<p>For an evaluation that contains</p> <ul style="list-style-type: none"> ➤ Relevant but unexplained evaluative judgement(s)/ statement(s) i.e. evaluative judgement(s)/statement(s) not supported by analysis or ➤ A relevant conclusion.
(d)	<p>Explain why living standards in Britain has been under pressure despite the acceleration in earnings growth. [3]</p> <p>Inflation rate increased by more than wage growth rate. Thus, there is lower purchasing power, resulting in lower material standard of living.</p>		
(e)	<p>With reference to Extract 10, explain whether consumers or the German car manufacturers are likely to bear a greater burden of the tariffs. [8]</p> <ul style="list-style-type: none"> • The imposition of tariffs leads to an increase in cost of production. Thus, price increases, ceteris paribus. • Since the purchase of cars take up a relatively large proportion of income, the PED value is likely to be greater than 1. • Cars are manufactured goods, which can be produced via automation through a short time period. This means that the PES value is likely to be greater than 1. • Although both PED and PES values are greater than 1, PED value is likely to be higher than that of PES because German cars are substitutable by cars from other manufacturers which are not impacted by tariff changes. <p><i>Note: any other logical explanations can be accepted</i></p> <ul style="list-style-type: none"> • Therefore, the German car manufacturers will bear the greater burden of it. 		
(f)	<p>Discuss the likely impact of Brexit on economic growth in the UK and Germany. [12]</p> <p><u>Introduction:</u></p> <ul style="list-style-type: none"> • Economic growth is the increase in real national income or GDP over a period of time. It consists of both actual and potential growth. 		

- Actual growth is the actual increase in real output or equilibrium national income, which can be due to an increase in aggregate demand or short run aggregate supply.
- Potential growth is the rate of increase in potential output or productive capacity shown by an increase in the long run aggregate supply.

Impact of Brexit on economic growth in the UK

Positive impact on the UK

- The fall in the value of the pounds lead to a fall in prices of exports in foreign currency. Therefore, export revenue will increase since demand for exports increase.
- AD increases from AD_0 to AD_1 as shown in Figure 3, leading to an increase in real national output from Y_0 to Y_1 via the multiplier process.
- This increases the actual growth of the economy.

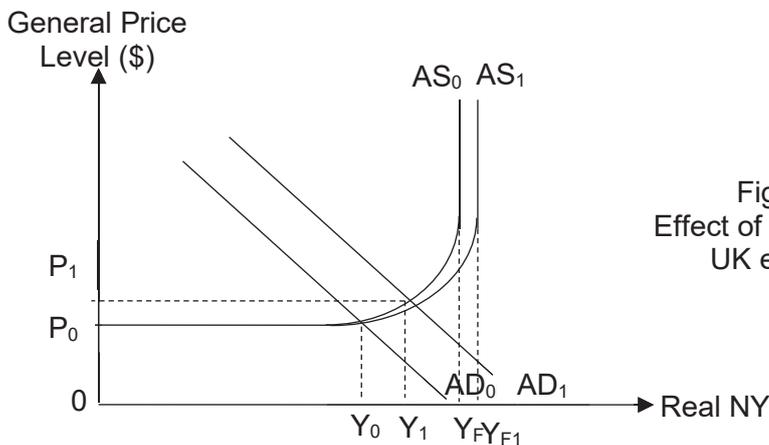


Figure 3:
Effect of Brexit on the
UK economy

Negative impact on the UK

- Brexit-related uncertainty may lead to a fall in C and I as economic outlook is uncertain.
- Consumers are unwilling to spend on consumption while businesses are unwilling to spend on investment since the future is uncertain.
- These lead to a fall in AD, which can offset the increase in AD due to net exports. Thus, AD may increase by a smaller extent from AD_0 to AD_1 .
- Actual growth will slow down, assuming that the economy is not at full employment level.

Impact of Brexit on economic growth in Germany:

Positive impact on Germany

- With Brexit causing the UK to lose its appeal in attracting skilled immigrants, there can be an increase in migration to Germany and hence, quantity of skilled labour.
- Therefore, productive capacity is increased.

- AS shifts right from AS_0 to AS_1 in Figure 4 as a result and both potential and actual growth are increased.

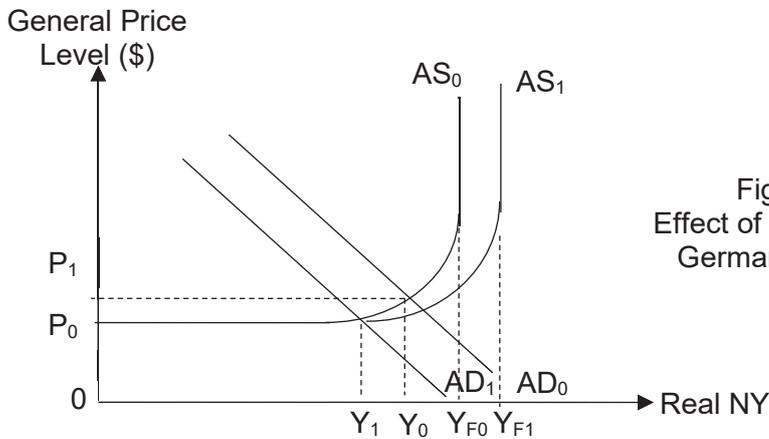


Figure 4:
Effect of Brexit on the
German economy

Evaluative conclusion:

- For the UK, whether Brexit ultimately positively impacts the economy is dependent on the extent of increase and decrease in AD.

Mark Scheme

<p>L3 7-9 marks</p>	<p>For an answer that demonstrates knowledge and understanding with excellent application and analysis:</p> <ul style="list-style-type: none"> ➤ Excellent breadth that considers the following economic concepts in explaining multiple and balanced perspectives, viewpoints, relationships and factors. MOST points chosen should be of relevance and significance in answering the question. ➤ Excellent depth in economic analysis that reflects the following in MOST explanations. ➤ Accurate use of economic concepts, clear elaboration, and precise use of economic terminologies, language and phrasing. <p>The answer should also be supported by:</p> <ul style="list-style-type: none"> ➤ Well-labelled and well referred to diagram(s) / Tool(s) of analysis drawn with precision (where appropriate). ➤ Evidence(s). ➤ Logical structure
<p>L2 4-6 marks</p>	<p>For an answer that demonstrates knowledge and understanding but lacks application and analysis:</p> <ul style="list-style-type: none"> ➤ At least GOOD breadth that considers the following economic concepts in explaining multiple and balanced perspectives,

		<p>viewpoints, relationships and factors. MOST points chosen should be of relevance and significance in answering the question.</p> <ul style="list-style-type: none"> ➤ At least GOOD depth in economic analysis that reflects the following in MOST explanations. ➤ Accurate use of economic concepts, clear elaboration, and precise use of economic terminologies, language and phrasing. <p>The answer should also be supported by:</p> <ul style="list-style-type: none"> ➤ Well-labelled and well referred to diagram(s) / Tool(s) of analysis drawn with precision (where appropriate). ➤ Evidence(s). ➤ Logical structure. 	
	L1 1-3 marks	<p>For an answer that demonstrates knowledge but lacks understanding, application and analysis:</p> <ul style="list-style-type: none"> ➤ INSUFFICIENT breadth that considers the following economic concept(s). Point(s) chosen may be of relevance but may not be of significance in answering the question. ➤ INSUFFICIENT depth in economic analysis that may reflect the following: ➤ Lack of accuracy in the use of economic concepts, lack of clarity in elaboration, and lack of precision in the use of economic terminologies, language and phrasing. 	
	E2 2-3 marks	<p>For an evaluation that contains:</p> <ul style="list-style-type: none"> ➤ A synthesis of earlier economic arguments to arrive at relevant judgements/decisions (i.e. answer the question). ➤ Well-explained criteria-based evaluative comments supported by accurate and clear analysis to provide fairness in views. ➤ A good summative conclusion. 	
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