

Examiners' Report
June 2012

GCE Economics 6EC02 01

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June 2012

Publications Code US032039

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Introduction

In general candidate performance was at a high level, with answers demonstrating a good grasp of the requirements of the specification. The majority of candidates knew how to recognise the evaluation command words and made a good effort at demonstrating this higher order skill.

Question 1 (a) (i)

Generally well answered. Candidates were confident on the distinction between the two categories of income, although some confused inflation with taxation.

(a) (i) With reference to Extract 1, explain the difference between real and nominal incomes.

(4)

Real income is your annual income adjusted to inflation, whilst nominal income is the actual amount of money you receive. Whilst in extract 1 nominal income increased by 2.3%, CPI increased by 4% thus seeing a real decrease.



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Examiner Comments

This answer was not the best but there was evidence that the candidate understood the difference, 2 marks and used data to demonstrate the point, 2 marks.

(a) (i) With reference to Extract 1, explain the difference between real and nominal incomes.

(4)

Real incomes are incomes which have the effects of inflation^{3*} removed. In the extract real disposable incomes are "falling by 0.8%". Nominal incomes are unadjusted by the effects of inflation and therefore show a much higher value: "earnings rising by 2.3%".

As inflation has increased by "4%" according to the CPI measures, real incomes have decreased because consumers can buy less with their ~~money~~ income.



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Examiner Comments

Identified the difference, 2 marks and used data to support the point, 2 marks.

Question 1 (a) (ii)

This question was confidently answered by most candidates, making good use of the data provided. The most popular responses focused on the inflation and unemployment figures. A minority of candidates thought disposable income meant after expenditure on mortgage payments and so referred to the impact of interest rates in their responses.

(ii) With reference to the extracts and your own knowledge, explain **two** possible causes of falling real disposable income in the UK during 2010.

(8)

Real disposable income could decrease because of rising interest rates. If there is a rise in interest rates, it means that mortgage repayments would be higher and these already take a huge amount of a worker's wages. The rising interest rates means that consumers will have to pay more money at the end of every month for their house resulting in less disposable income that they can spend on themselves. However, people with fixed mortgages may not see this effect immediately but will experience it in the long-run. Real disposable income is the money remaining after all costs of a household has been taken from a consumer's wages. Another cause of falling real disposable income is an increase in taxes. If taxes increased, it means people would have to pay more to the government to fund government spending programmes such as health care and national defence. This means that more money will be taken from a person's real ~~own~~ wages leaving them with less real disposable income. Also, if taxes on goods and capital rise as well such as VAT, it will mean the price of goods will increase and some goods may be price inelastic such as addictive goods. This means people will have to spend the extra money to buy these goods as there are not very or any available substitutes. This means they will have less money left after their expenses.



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Examiner Comments

Misunderstanding of real disposable income initially but the second cause to do with income tax earned the full 4 marks. The third point about VAT was also incorrect. The total is 4 marks.

(ii) With reference to the extracts and your own knowledge, explain **two** possible causes of falling real disposable income in the UK during 2010.

(8)

One possible cause of falling real disposable income is the high rate of CPI inflation which was at 4.0% in January 2011. Even with bonus payments included, wage increases are not able to keep pace with this high inflation - nominal wage growth was only 2.3%. This means that in real terms, workers are being paid less since the high CPI inflation is mostly caused by cost-push inflation imported from countries with high rates of economic growth.

A second cause could be the high rates of unemployment in the UK, reaching 2.53 million in January 2011 - the highest figure since 1994 - with the ILO measure. A high unemployment rate may mean that the workforce experiences falling real disposable incomes, since a person who was previously employed and is now claiming JSA is likely to have a lower income, as JSA is generally lower than wage rates. The more people unemployed, the more this pulls the average real income down. Lower incomes also can lead to a negative cycle, where consumption is lower, so firms make lower profits, so they pay their workers lower wages.

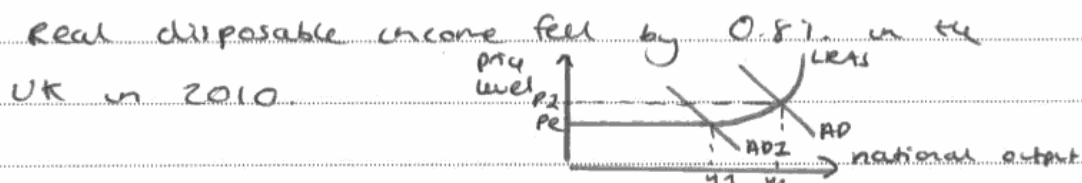


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Examiner Comments

The candidate received 2 marks for each sentence in the first paragraph, including 2 marks for data in the first paragraph. In the second paragraph 2 marks for high rates of unemployment and 2 marks for JSA is generally lower than wage rates, but full marks have already been awarded. 2 further marks could have been awarded for the last sentence.

(ii) With reference to the extracts and your own knowledge, explain **two** possible causes of falling real disposable income in the UK during 2010. (8)



~~One reason~~ for ~~one reason~~ for the falling disposable income was because of the increasing unemployment. UK unemployment was at 2.5 million in 2010. This ~~reduced~~ ~~meant~~ ~~that~~ ~~many~~ ~~were~~ ~~not~~ ~~earning~~ ~~income~~ ~~and~~ ~~lots~~ ~~of~~ ~~pay~~ ~~freezes~~ were experiencing ~~get~~ pay were ~~not~~ earning income and lots of pay freezes as a result of low aggregate demand. Therefore there was a lack of disposable income as wages fell. Due to high unemployment, wage pressure fell and producers were able to cut wages.

Another reason for the falling real disposable income was the high CPI inflation which was beyond the target of 2% (± 1). This reduced the value of disposable income as wage growth was lower than inflation rate and therefore the value of incomes fell, reducing disposable income. It also increased cost of production as ~~may~~ inflation was a result of rising commodity prices (cost push) which increased cost of production of firms, and increased unemployment, decreasing disposable income. High inflation also increased cost of living and so reduced disposable income.



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Examiner Comments

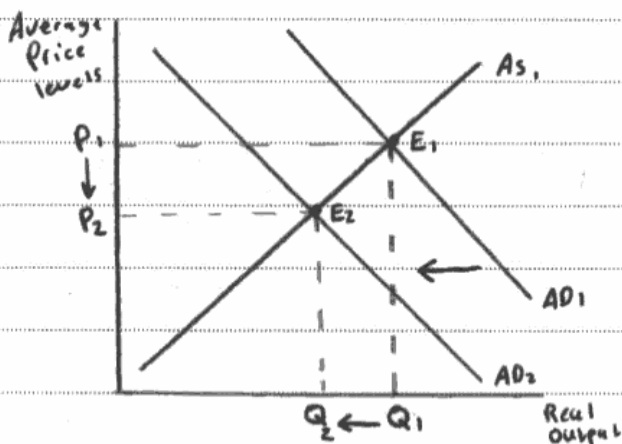
The candidate received 6 marks for the first paragraph including data reference and 4 marks for the second.

Question 1 (a) (iii)

The majority of candidates confidently drew and explained a correct AD and AS diagram. Most attempted evaluation. Evaluative comments based on the elasticity of the AS curve were the most popular and often the most successful.

(iii) Assess the likely impact of falling real incomes on the price level and equilibrium output. Illustrate your answer with an aggregate demand and aggregate supply diagram.

(12)



Falling real incomes will have a serious effect on price levels. By consumers having less disposable income to spend on consumption, AD will shift to the left from AD_1 to AD_2 . This is because

$$AD = \text{consumption} + \text{investment} + \text{Gov spending} - (\text{Exports} - \text{Imports})$$

So by decreasing consumption AD will shift inwards.

This will create a new equilibrium at the point E_2 . This new equilibrium will force price levels to fall from P_1 to P_2 . This is because firms need to reduce prices to seem more appealing as competition has increased, and real income has fallen.

The output of the economy will also suffer. At the new equilibrium at E_2 the real output of the economy will decrease from Q_1 to

Q2. This is because less consumers are demanding goods and services, therefore the total amount sold in the economy is going to decrease. The decrease in real incomes will have a very negative effect on the output of an economy.

However this will depend on the magnitude in the fall in real income. A very large fall will have an extreme effect in the short run as people dramatically try to cut back on spending. But a very small decrease is not likely to effect spending habits build up over years.

Furthermore this is assuming all other factors are equal, but in reality there will loss of other factors effecting the price levels and output. For example if the government are putting in place a fiscal policy by government spending then AD will shift outwards which would reduce the impact of the reduction in consumption. However it's unlikely to completely cancel it out as consumption makes up 60% of the UK's AD.

Or if there was a natural disaster a fall in the factors of production where decreased. As would shift in raising price levels, but would have a negative effect on real output. So there are loss of other factors which contributes to price levels and real output.



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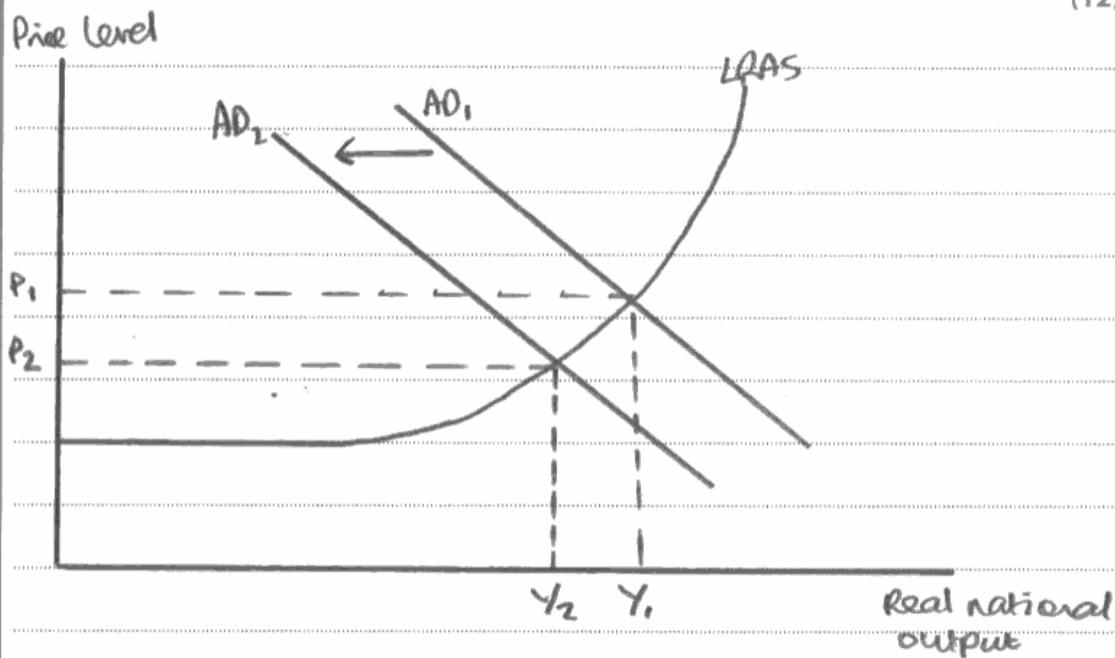
Examiner Comments

Diagram received 4 marks, decreasing consumption 2 marks and then identifies fall in Price level, 1 mark and Output, 1 mark gives the maximum of 8 KAA marks.

On the second page in the second paragraph magnitude of the fall and the explanation of spending habits building up over years is worth 4 evaluation marks and the maximum is scored. The third paragraph would have achieved 4 evaluation marks and the fourth might have achieved 2 marks.

(iii) Assess the likely impact of falling real incomes on the price level and equilibrium output. Illustrate your answer with an aggregate demand and aggregate supply diagram.

(12)



A fall in real incomes will decrease aggregate demand from AD_1 to AD_2 . This is because this will cause real national output to fall from Y_1 to Y_2 , and cause the price level to ~~decr~~ fall from P_1 to P_2 . The reason for the decrease in AD is due to less disposable income and less consumer confidence caused by the decrease in real incomes, which therefore decreases consumption, an important component of AD .

However, the extent to which there is a fall in output and the price level depends where on

^{LRAS}
the curve the AD shift occurs. If the economy is close to full employment, i.e. where LRAS is inelastic, then a decrease in AD will have a very large effect on decreasing the price level, and a much smaller effect on decreasing output. If the economy is in recession, i.e. where LRAS is elastic, then a fall in AD will have a large effect on decreasing output, but not so much on the price level.



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Examiner Comments

Diagram received 4 mark plus 2 marks for the fall in Price Level and Output, and a further 2 marks for the explanation of the fall in consumption, giving a maximum of 8 marks.

The discussion of where the economy is in the business cycle, received 4 evaluation marks.

Question 1 (b) (i)

This question was well answered by the majority of candidates. Most had clearly prepared well by revising the details of this specific area of the specification.

(b) (i) With reference to Figure 1 and Extracts 2 and 3, distinguish between the claimant count and the ILO measures of unemployment.

(6)

Claimant Count is the number of people receiving or claiming Jobseeker's allowance. They are usually aged between 18-65 years old. Also this they have to go and register in the nearby ^{Jobseeker's} post office.

ILO is measures the number of people out of work for 4 weeks and ready to work in 2 weeks through face to face interviews. ~~Also~~ ~~most~~ the age range for this is 16-65 years old.

The ILO unemployment in 2011 is about 2.5 million while the ^{total} Claimant Count is about 1.5 million. ^{Extract 8 suggests} 974,000 is the new unemployment rate for people aged between 16-24 while the 16 year olds cannot claim Jobseeker's allowance.



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Examiner Comments

This answer easily achieved full marks. 4 marks for CC (maximum 2) and 4 marks for the ILO (maximum 2) with a further 2 marks for the data at the end.

(b) (i) With reference to Figure 1 and Extracts 2 and 3, distinguish between the claimant count and the ILO measures of unemployment.

(6)

The labour force survey is a measurement taken by the ILO which involves face-to-face meetings, followed up by phone calls which classifies people as unemployed if they have been out of work for 4 weeks and are ready to start work in 2 weeks. Whereas the claimant count is a measurement taken by the government of the number of people claiming unemployment benefits such as the job seeker's allowance. However, the labour force survey figures are always much higher than the claimant count as some unemployed people may choose not to claim unemployment benefits.



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Examiner Comments

Similarly the ILO scored a maximum of 2 marks, although 4 marks were made, and the CC scored 2 marks. There was one data mark for stating the ILO was higher than the CC.

Question 1 (b) (ii)

Many candidates found this question challenging. Most focused on general reasons why the two measures differ. Only the minority of candidates explained reasons why the trend may have specifically differed after 2009.

- (ii) With reference to Figure 1 and Extracts 2 and 3, outline **two** possible reasons why the trends in the claimant count rate and the ILO measure of unemployment differ after 2009.

(8)

Figure one shows that after 2009 the ILO unemployment stayed fairly constant, beginning to slowly increase whereas the claimant count decreased.

One reason for this trend is because people that are still in full time education are not entitled to claim benefits, therefore will not be included ^{in the claimant count}, whereas in the ILO measure they are included. Extract 3 states that the unemployment level for those aged 16-24 reached 974000 in the 3 months to 2011. Therefore this is going ~~to~~ ^{all of it to} ~~be shown~~ to contribute to the ILO but not ^{the} claimant count.

Another reason why the trends differ in the two measures is because people may just say they are looking for work, and so included as unemployed by the ILO, but actually have no intention to start work. This leads to inaccurate information and a bad reflection of the number of unemployed. Whereas the claimant count is more accurate, and it has to be ~~proved~~ ^{proven} that you are entitled to get Job seekers



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Examiner Comments

Recognising the divergence in the first sentence received 2 data marks.

The first reason for the divergence got 4 marks and the second reason got 2 marks, but didn't explain why it might diverge after 2009.

- (ii) With reference to Figure 1 and Extracts 2 and 3, outline **two** possible reasons why the trends in the claimant count rate and the ILO measure of unemployment differ after 2009.

(8)

As the graph in figure 1.2 shows there is a massive surge in the unemployment for young people in 2009, and this would of course affect the two different measures.

This is as the claimant count completely excludes people from the ages of 16-18 and so doesn't include a large percentage of youth unemployment and also young people from 18-24 may not be as likely to claim anything due to them living at home or being in further education.

Also by the time that ILO is published it is six weeks out of date and particularly during an economic crisis 6 weeks can be a large fluctuation in unemployment.

One example of the two measurements differing quite vastly ILO measured a 0.1% increase in the first three months over January 2011 whereas the flat claimant count fell by 10,200 between January and February 2011.

Another possible reason for this inconsistency is a change in the regulation or process of jobseekers allowance; as the jobseeker has to go in to see an office to prove them looking for work less people are likely to do it. As when it becomes harder and more time consuming less people will do it.



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Examiner Comments

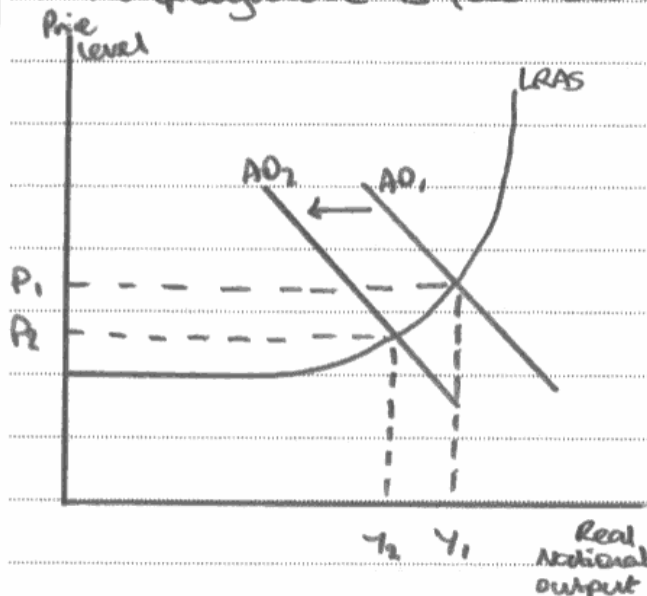
The candidate received 4 marks for the first two paragraphs. 2 for the data in the fourth and the last paragraph made it full marks.

Question 1 (b) (iii)

Most candidates were able to identify factors explaining the rise in unemployment and the majority of responses were to a reasonable standard. However many did not attempt evaluation and some of those who did were often unsuccessful.

*(iii) With reference to the information and your own knowledge, examine **two** factors which might explain the rise in UK unemployment since 2008. (12)

one factor which may have caused the recession, rise in unemployment is the recession. This would have



decreased consumer confidence, causing a fall in consumption, and decreased confidence of firms, causing a fall in investment. These both would decrease AD, causing a lower level of

output. A lower level of output is associated with lower employment, as firms need to satisfy less demand, and so cut down on costs by laying off workers. The *

The extent to which this happens depends on the magnitude of the recession, and therefore the size of the decrease in AD. The 2008 recession was a large one, and so ~~was~~ employment suffered heavily.

Another cause of unemployment * The fall in real disposable income by 0.7% in 2010 would have also

decreased AD and therefore employment.

Another cause of unemployment is the shift in comparative advantage from high wage economies such as the UK to lower wage economies such as China. Many jobs, particularly ones in the secondary sector (e.g. manufacturing) have been lost, as firms relocate to lower wage economies to cut costs. Not only does this directly cause a decrease in unemployment, but through the negative multiplier effect, more jobs will be lost, as the unemployed spend less, and a decrease in exports further decreases AD, therefore ~~the~~ output, and hence employment.

The extent to which this happened depends on how occupationally mobile the workforce is. If their skills are limited, they will find it hard to get another job, whereas if they have a broad range of skills, they will be more mobile. The size of the multiplier also affects the size of the increase in unemployment.



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Examiner Comments

Fall in confidence leading to a fall in consumption, 2 marks and investment, 2 marks leading to lower output and employment, 2 marks. Possibly another 2 marks for the diagram which adds to the explanation, as consumption and investment are separate points.

Evaluation 4 marks for the extent of the 2008 recession.

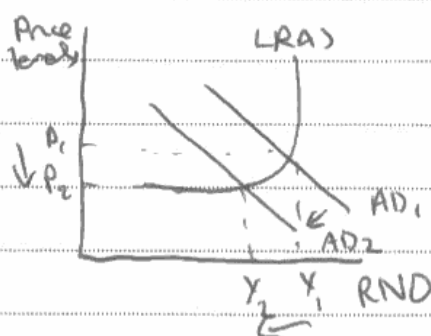
Comparative advantage would have also been rewarded 4 marks even though it is not on the syllabus at AS. This is likely to be an A2 candidate resitting the paper. 4 marks for evaluation in the final paragraph on the flexibility of the workforce.

*(iii) With reference to the information and your own knowledge, examine two factors which might explain the rise in UK unemployment since 2008.

(12)

It is shown that the information that unemployment has risen sharply in recent years in the UK. The labour force survey has suggested this amount has increased to 2.53 million whereas the claimant count suggests this figure is nearer to 1.45 million.

One possible reason for the rise in UK unemployment since the 2008 economic crisis, is the loss of consumer confidence and expectations for the future. Consumers may become less confident about the future and perhaps decide to reduce their spending and to increase the amount they save. This would represent a withdrawal from the circular flow of income, and would cause consumption in the economy to fall. This would cause AD to shift inwards. This could result



in less demand for labour since fewer consumer goods are being demanded and therefore fewer will be produced. This is due to derived demand

for labour. Unemployment will rise by the distance Y_1 to Y_2 . However the extent to which AD shifts in could depend on how much consumer confidence is affected and by how much spending falls or incomes fall. Also, the demand

for goods may fall for products which don't require labor to be produced. Therefore the demand for labor may not necessarily fall. So unemployment may not fall.

Secondly, a rise in UK unemployment may be due to the occupational mobility of workers falling. For example there may be a lack of demand for the skills needed to build houses or cars or other 'big ticket items' since as a result of the economic crisis there will be less income with which to spend on such items. Thus these workers may become structurally unemployed since they don't have the necessary skills required to take up other professions. This will reduce the mobility of workers and result possibly in long-term unemployment. However it is likely that in the long-run the occupational mobility of labor will improve as a larger proportion of 16 to 24 year olds are staying in higher education. If this is the case then the mobility to change occupations will improve and unemployment may not necessarily rise, however this will likely only occur in the long run and may not be the case after the 2008 banking crisis, as there will be many workers who wouldn't have received higher education or training to improve their mobility and ability to change professions.



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Examiner Comments

The candidate received 4 marks for falling domestic demand causing more unemployment. 4 marks for greater structural unemployment because of occupational immobility and this was well evaluated at the end, which gave 12 marks in total.

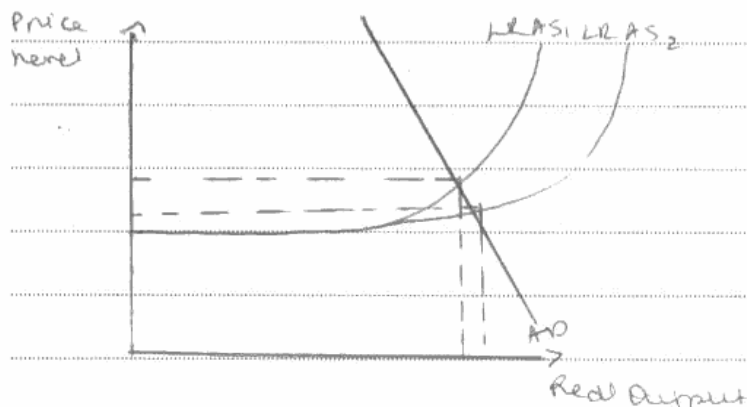
Question 1 (c)

This question was well answered by the majority of candidates. Most were able to explain suitable policies in good depth and also evaluate them by discussing their likely effectiveness or how they might clash with other macroeconomic objectives. Most answers were well structured and included an AD and AS diagram. Only a minority of candidates made direct comparisons between the policies.

* (c) Evaluate macroeconomic policies which may be used to reduce the level of unemployment in the UK.

(30)

Unemployment is defined as the ^{percentage} ~~proportion~~ of the labour force who are not employed but are seeking work. The ~~to government~~ ^{gov}. There are several macroeconomic objectives the government has to improve the economy and that includes stable balance of payments, a lower rate of inflation, a rise in GDP, price stability, improved environment and ~~to~~ full employment. A policy used by the government to improve employment is Supply Side Policy. Supply Side Policy aims to shift Aggregate Supply to the right.



The diagram shows what ~~a shift~~ a shift from LRAS₁ to LRAS₂ decreased prices

and increased output.

Supply-side policy aims to improve education and training which in the long run, it effective ~~can improve~~ reduce unemployment. Education, ~~and~~ training and remaining improves the skills of the current labour force and the future labour

forces which will make it easier for people to attain jobs as they have improved structural and occupational mobility and employment.

Supply side policies also aim to reduce income direct taxes such as income and corporation tax. Reducing ~~income~~ income taxes will increase the incentive to work as a less proportion of income will be taxed away. The multiplier effect of higher incomes will improve the circular flow of income and also improves the wealth effect in the economy.

Supply side policies also aim to make unemployment seem less attractive by ~~a~~ removing or reducing unemployment benefits to give people the incentive to work. It may also increase minimum wage to create better incentives.

To improve competitiveness it may lean towards privatisation of public firms. Improvements in competitiveness helps to decrease unemployment.

Supply side policy also aims to remove bureaucracy. The government may ease restrictions to improve competitiveness (reducing barriers to entry).

Although Supply Side policies has its aims to improve unemployment by shifting

the LRAS curve to the right, there are several factors things that may make it more ineffective. For aims such as Education and training, there is a time lag for there to take effect. In the short run it has little or no effect and a large proportion of Government expenditure is ~~now~~ being spent on improving and/or building new schools which would have an effect on Aggregate Demand. In the long run there is no guarantee that the education will give people the incentives to work as what they are being educated in may not be helpful for the economy for example someone learning golf will not be as productively efficient as someone who learnt engineering meaning that there is a high degree of risk.

In evaluation if the government ~~to~~ decide to reduce direct taxes such as income and corporation tax they will receive less government revenue. ~~in~~ reducing government expenditure (ceteris paribus, AD) meaning ~~that~~ that they can't spend as much money on granting subsidies to firms to hire more workers or money to improve infrastructure to encourage new building

encouraging new firms to enter the market and ~~to~~ less money can be spent on education or more facilities and reserves for job centres, so some of the aims within supply side policy conflict with each other. Supply side policy conflicts with Aggregate demand as a reduction in tax revenue from income and corporation tax will reduce government expenditure which reduces AD.

Moreover the 'crowding out' of the private sector to the public sector will affect and ~~harm~~ harm competitiveness.

"Grayling claimed that youth unemployment had fallen if young people in education were excluded from the figures".

- Multiplier effect
- Wealth effect.



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Examiner Comments

The candidate received 2 marks for the identification of the full employment government objective and 2 marks for the identification of a type of policy. 3 marks for the diagram as no equilibrium points bringing up the maximum of 6 for the first part of KAA.

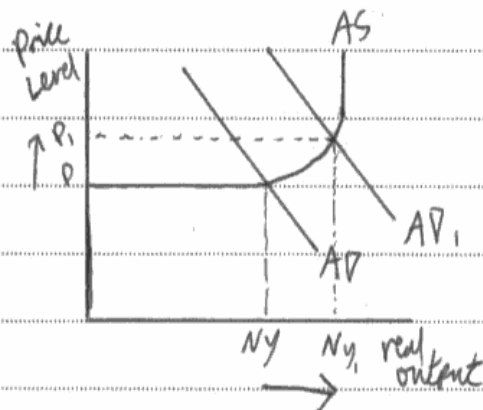
Education and training achieved 4 marks by the top of the second page and a reduction in income tax earned another 4 marks, as did the reducing benefits, which gave a maximum KAA of 18. This meant the 2 for privatisation and 2 for bureaucracy were not needed.

On the third page the top paragraph got 6 evaluation marks and the bottom one got 4 when it continued on to the fourth page. The last paragraph got the final 2 evaluation marks for raising the possibility of crowding out, which made a total of 30 marks.

*c) Evaluate macroeconomic policies which may be used to reduce the level of unemployment in the UK.

(30)

There are three types of macroeconomic policy to reduce unemployment and stimulate growth. They are fiscal policy, monetary policy and supply side policies. The fiscal and monetary policy focuses on increasing AD to increase real output, which leads to more jobs and a higher GDP, as more goods and services are consumed.



Fiscal policy increases AD by increasing government spending. ~~and/or~~ ~~increasing~~ ~~the~~ This means that the G section of AD rises, so AD also rises, causing a shift to the right from AD to AD₁, which causes output to increase NY to NY₁. An increase in ~~the~~ output causes more goods and services to be produced, increasing employment.

However, increasing government spending also increases the national debt, which means we no longer

have sustainable growth (future generations' are compromised as they have to pay it off). An increased national debt also ~~depress~~ decreases investment, as potential investors are not convinced our economy is stable enough to put their money into.

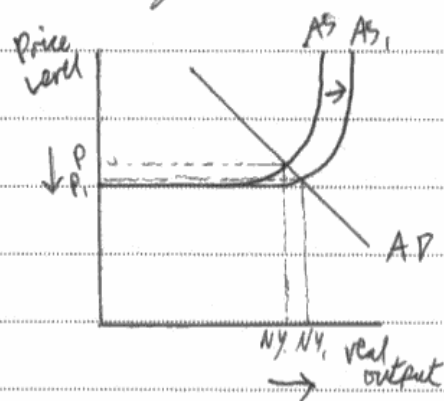
Monetary Policy works the same way as fiscal, by increasing AD to increase real output, a "demand-side" policy. However, monetary policy ~~works~~ is the manipulation of interest rates by a central bank (the Bank of England), and quantitative easing.

The BoE can lower interest rates, which makes it cheaper to borrow money from the banks, as you pay back less interest on loans etc. The increased ease of credit causes consumption to rise, which is a factor of AD, so AD increases therefore increasing real output so more people are employed. Quantitative easing is the BoE electronically printing ~~money~~ money to buy assets of ~~banks~~ banks so they have more capital to lend to consumers, increasing consumption. However, this significantly reduces the purchasing power of the pound. Demand-side policies increase inflation ($P \rightarrow P_1$) which can balance our current account, but also wipes out savings, so a lot of pensions are affected. When the rate of interest is lower than the rate of inflation, ~~as~~ savings are worth less and less each year. The UK is

Currently using monetary policy to shift AD as our interest rate is 0.5%.

~~Graph~~

Supply-side policies focus on shifting AS to increase real output, by increasing the potential productive capacity of our economy.



These are 3 policies. Increasing Incentives, deregulation and privatisation. When AS is shifted to the right to AS_1 , $NY \rightarrow NY_1$, which increases output therefore employment but $P \rightarrow P_1$, meaning price falls. Supply side policies do not create inflation and produce sustainable growth as national debt is not increased unlike fiscal policy.

Incentives work by ~~reducing~~ reducing benefits and reducing taxes. People are forced to work as they can no longer afford to live on benefits, and workers' disposable incomes increase due to lower taxes.

Deregulation is where government takes away rules and regulations which stop firms from entering the market. Although this is proven to work, it is argued that the deregulation of the finance sector caused the 2008 recession.

Privatisation is where government owned companies are sold to private sector. When a firm has government funding, they essentially have free money (tax payers money). But the private sector relies on shareholder funding, so companies make economic decisions unlike government companies. Privatisation works, as BT will show. BT was a government owned telecommunications monopoly, but was privatised. It improved efficiency and allowed competition to enter the market, causing BT to increase their quality. This allocates resources more efficiently.

Demand-side policies have lots of evidence they do not work. Unsustainable government debt and rising inflation destroying savings. Supply-side policies promised lots in the 80's, but did not deliver. There were higher growth rates in the 60's when supply-side policies weren't being used, true in the 80's. Deregulation also creates monopolies to appear, not allowing new firms to enter the market.

(Total for Question 1 = 80 marks)



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Examiner Comments

The candidate received

6 marks for the identification of policies and for the correct diagram. 4 for government spending at the bottom of the page.

The candidate received

4 marks for evaluation at the top of the second page. In the third and fourth sentences of the next paragraph a total of 4 marks were awarded. (2 marks for Quantitative easing but not needed). 4 marks for evaluation at the bottom of the page.

On the third page the diagram didn't receive any credit as already awarded the full amount. In the paragraph below 2 marks were awarded for evaluation. There were 4 marks for incentives in the bottom paragraph meaning that the maximum 18 KAA had been achieved.

The fourth page starts with a point which had potential but was unclear. 4 marks could have been awarded for a good example of privatisation's beneficial effects.

Total of 10 for evaluation, which made a total of 28.

Question 2 (a) (i)

A significant number of candidates were not able to define a recession as two consecutive quarters of negative growth. Most were able to identify negative growth (or equivalent) though. The best answers referred to the data by identifying the period of recession (i.e. Q2 2008 to Q3 2009) and quoting the range of negative growth rates (ie -0.2% to -2.25% of GDP).

(a) (i) Using the data in Figure 1, explain what is meant by a recession.

(6)

Recession is a quarterly figure of negative growth, or contraction of output. In figure 1 it is measured as a percentage, in the last quarter of 2008, ~~GDP~~ real GDP growth was just over -2.0%.



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Examiner Comments

Identified negative growth, 2 marks, but not the duration. Reference to data was not comprehensive (ie for the duration of the recession) and benefit of the doubt was given for 2 further marks.

(a) (i) Using the data in Figure 1, explain what is meant by a recession.

(6)

A recession is when there is ~~a~~ negative growth for two successive quarters. The UK experienced a recession from the second quarter of 2008 to the third quarter of 2009 (a year and a half). This is because the UK real GDP growth was at -2.25% at its lowest. In a recession, the government ~~may~~ might introduce ~~isolationist policies and~~ supply-side policies such as education and training to improve productivity and increase the LRAS curve and push the economy out of recession.



ResultsPlus

Examiner Comments

The candidate received 4 marks for the first sentence. The second sentence gathered the final 2 data marks.

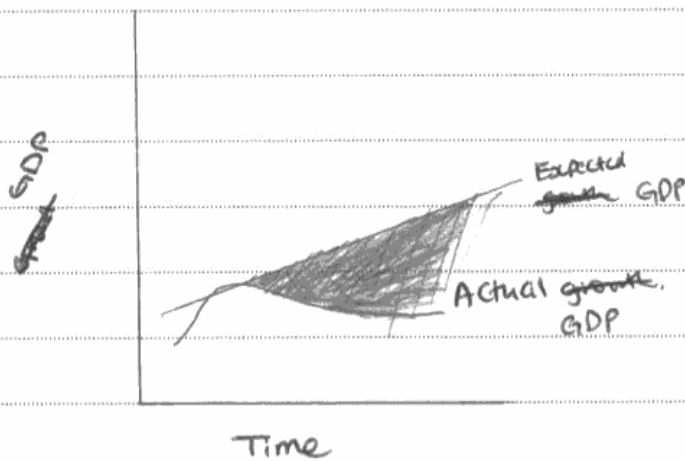
Question 2 (a) (ii)

This question proved to be challenging to some candidates. Most were able to explain what was meant by negative output gap. Diagrams varied in quality and many of those showing actual and potential GDP were not fully/correctly labelled. Many candidates found clearly linking the data to the question difficult.

- (ii) With reference to Figure 1, explain why economists might consider that a negative output gap existed in 2008–9. Use an appropriate diagram in your answer.

(8)

The U.K. government expects a growth of approximately from the economy every period. However, during 2008–2009, there was clearly a negative growth, which suggests that the economy ~~shrank~~ ^{shrank}.



The graph shows a straight line which indicates where the government wants the GDP (output) to be at. However, the negative growth during 2008–2009 suggests that the economy was not doing as well as they could have.

Negative output gap is the shaded area – the difference between actual GDP and potential GDP. As the actual GDP is below expected GDP, there is a negative output gap. If it was above, then there will be a positive output gap.



ResultsPlus

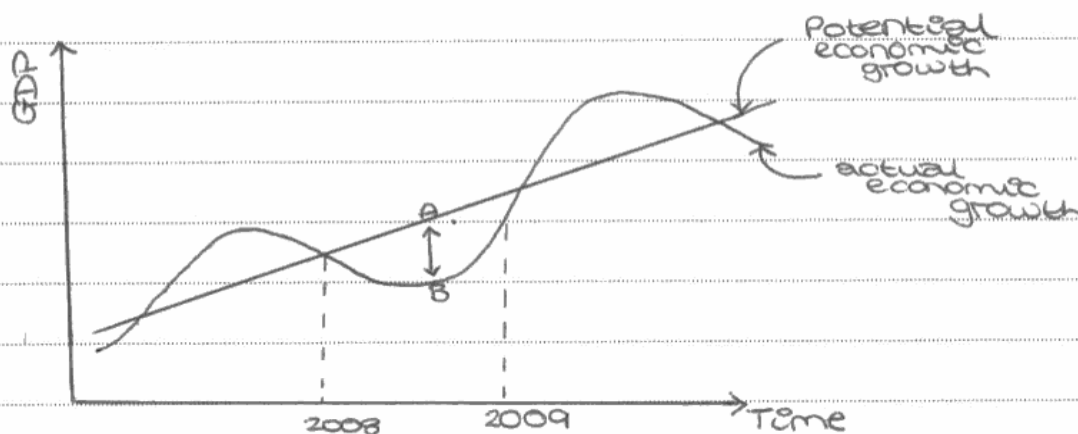
Examiner Comments

The first paragraph was given 2 data marks. The diagram was also worth 2 marks as the labelling was accurate. The final paragraph picked up the remaining 4 marks.

- (ii) With reference to Figure 1, explain why economists might consider that a negative output gap existed in 2008–9. Use an appropriate diagram in your answer.

(8)

The output gap is the difference between actual economic growth and potential economic growth.



The output gap is the distance from A to B. Economists might consider that a negative output gap existed in 2008–9 because the actual economic growth was lower than the potential economic growth.



ResultsPlus

Examiner Comments

In isolation the first sentence would have been awarded 2 marks however the final paragraph picked up all 4 explanation marks. The diagram got 2 marks but there was no reference to data.

Question 2 (a) (iii)

There were many good answers to this question, but a sizeable minority did not refer to the factors in the extract and instead discussed general reasons why AD might change, e.g. increased government spending, despite the clear reference to deflationary fiscal policy in the extract. Some felt that 'increased their borrowing further' implied consumption would be rising.

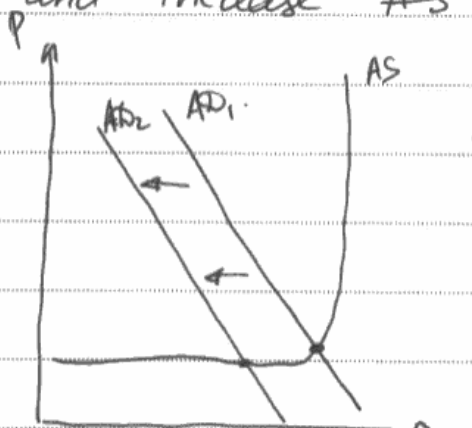
(iii) With reference to Extract 1, assess two factors likely to affect the level of aggregate demand in the UK.

(12)

AD - total expenditure on all goods & services produced in a country. There are 4 components in AD: consumption (or consumer spendings), government spendings, investments & net exports (or exports - imports)

$$AD = C + G + I + (X - M)$$

First of all, according to extract 1, there was a decrease in consumption, so now "households will have to reduce their savings and increase their borrowing further".



consumption is ~~one~~ of the biggest & most important component of AD. As there is an unstable situation in UK's economy (unstable growth, high unemployment rate, inflation) people are afraid to spend money and as a result there is a decrease in AD. (AD₁ to AD₂)

Secondly, in Extract 1 it is mentioned that "domestic substitutes for some

We is not able to produce some of products. What is more, it is said that "exports are growing, but not as strongly," which is another one indication that net export is very likely to be negative. That means that AD ~~is~~ becomes ^{if not} lower, than grows less, because ~~there~~ ^{one} is of the components - net exports - in negative or very small.

Although net exports is not ~~th~~ as important for the level of AD, as consumption, when problems with both of these factors occur as a result there may be a huge fall in AD, which will cause a decline in economic growth.



ResultsPlus

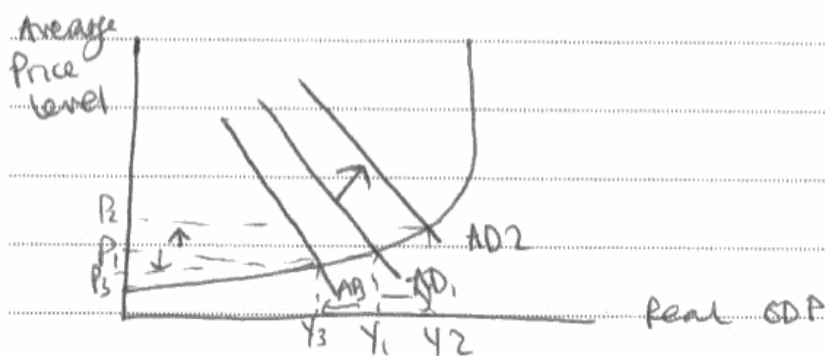
Examiner Comments

Second paragraph earned 4 marks and the third got another mark on the second page. 2 evaluation marks were awarded for the last paragraph.

(iii) With reference to Extract 1, assess **two** factors likely to affect the level of aggregate demand in the UK.

(12)

Extract one mentions the pound has depreciated by 20% plus if the pound depreciates it is lower in value. This would make imports more expensive and less price competitive. Therefore they should decrease. Exports become more price competitive and should increase. $(X-M)$ is a component of AD and therefore AD should rise from AD_1 to AD_2 , increasing the price level from P_1 to P_2 and increasing output from Y_1 to Y_2 .



however the extract says this depreciation has had virtually no impact on imports. This can be due to the UK's high MPS. This could mean demand for imports are inelastic and won't respond greatly to an increase in price.

The extract also mentions deflationary fiscal policy. This means there would be an increase in ^{taxes} income taxes and a decrease in government spending. Government spending is a component of AD and an injection in to the circular flow, therefore AD would decrease. An increase in taxes is a withdrawal and leaves consumers with less disposable income and so consumption would decrease. AD would decrease from AD1 to AD3, decreasing the price level from P1 to P3 and lowering output from Y1 to Y3.

However, the extent to which consumption falls depends on how much consumers manage to borrow to maintain their standards of living. Household debt is forecast to grow to 175% of disposable incomes.



ResultsPlus

Examiner Comments

The candidate received 4 marks for the first paragraph and only 2 evaluation marks for the second because the candidate wrote MPS instead of MPM. 4 marks for each of the two paragraphs on the second page, the latter being evaluation.

Question 2 (b) (i)

Generally candidates answered this question well. Often answers were extensive and some candidates seemed to spend too long on this question. Only the best candidates clearly made reference to the value of exports and imports.

(b) (i) With reference to Figure 2, explain why the UK current account balance in 2010 was a net withdrawal from the UK's circular flow of income.

(4)

A current account deficit is a net outflow of goods + services + net transfers from the economy UK's circular flow of income and where exports are smaller than imports (volume). In 2010 we saw the subsector of trade in goods + services at -48.5 and the total current account balance of -36.4 leaving the current account balance of GDP -2.5%.



ResultsPlus

Examiner Comments

The candidate received 2 marks for the first sentence. Nothing for the figures -48.5 and -36.4 as they didn't have £ or billions. However 2 marks for -2.5% GDP.

(b) (i) With reference to Figure 2, explain why the UK current account balance in 2010 was a net withdrawal from the UK's circular flow of income.

(4)

There was a net withdrawal in the current account of - £36.4 bn (figure 2).

The current account tracks the trade in goods and services and whether a country exports more (such as Germany) - a surplus, or imports more (UK) - a deficit.

The net withdrawal in 2010 is due to the negative trade of - £48.5 bn, that money is leaving the UK in import costs and not being replenished fully by export income - hence a net withdrawal.



ResultsPlus

Examiner Comments

Data received 2 marks in the first sentence and 2 marks for explanation in the last.

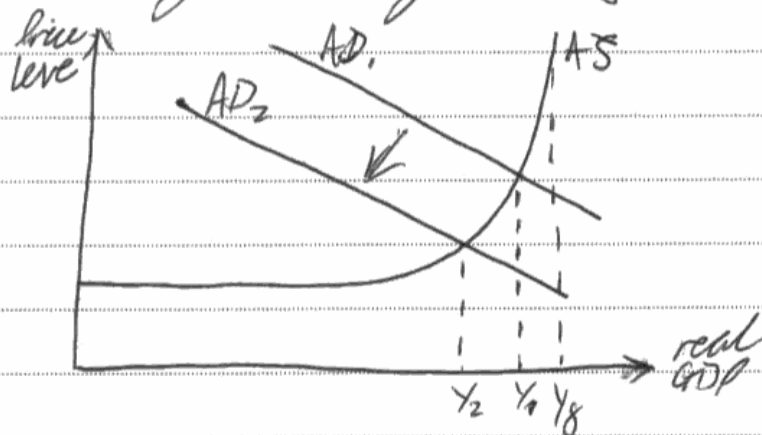
Question 2 (b) (ii)

Many candidates found this question challenging and only the minority were able to convincingly explain two problems.

(ii) Explain **two** possible problems for the UK economy of its persistent and increasing current account deficit.

(8)

The current account deficit causes a reduction in the AD as there is lower demand for UK goods and more money leaking out of the economy.



The reduction in AD ($AD_1 - AD_2$) causes a fall in GDP ($Y_1 - Y_2$) this is severe and prolonged could cause a recession effectively stunting the economy.

Unemployment is another problem, as there is less demand within the economy, less workers are wanted meaning the output gap is increased, $(Y_3 - Y_1) - (Y_3 - Y_2)$.
and
more This is particularly bad if it is prolonged as workers become unskilled and won't be able to get back into work, this means crime may increase



ResultsPlus
Examiner Comments

The candidate received 4 marks for the explanation of the recession and another 4 for unemployment.

(ii) Explain **two** possible problems for the UK economy of its persistent and increasing current account deficit.

(8)

Balance of Payments = Exports - Imports.

This affects Aggregate Demand because it is part of it.

A deficit in the current account will cause a negative

Balance of Payments and might even decrease AD

if it's big enough. This can cause recession (negative growth). A negative growth means a greater output

gap and therefore not using all the resources available,

one of which could be labour. This can cause unemployment

in the economy because the country's goods are not

competitive abroad and there is less incentive for

investment.

Unemployed people might receive Job Seekers Allowance

and due to other automatic reasons e.g. less taxation

because of lower wages and discretionary reasons such

as to increase G in order to push up AD, the

government could be spending more than what they're

receiving from taxation. This could lead to a

fiscal deficit and even an increase in national

debt.



ResultsPlus

Examiner Comments

There was enough good explanation in the first and second paragraphs to award 4 marks for each problem.

Question 2 (b) (iii)

Most candidates were able to identify two causes, although some causes were not well explained.

*(iii) Examine **two** possible causes of the "largest ever recorded trade in goods deficit in 2010" (Extract 1, lines 11-12).

(12)

A trade in goods deficit can be for a number of reasons.

The deficit means in simple terms that the UK is producing less & exporting less than it is importing and therefore not making money from imports/exports but in fact making the deficit larger.

The UK deficit can be seen to be in this position due to the fact that production and specifically the industrial part of the UK economy has subsided. We used to be massive exporters of coal, steel & other textiles right up until the later half of the 20th century but now with this reduction in industry we rely heavily on imports from abroad for the majority of our goods.

It can also be put down to the increased standard of living in the UK & the fact that consumers more & more want extravagant goods from abroad such as exotic goods that have become common in all family homes. This has meant that the trade deficit has grown larger & larger & caused a massive shift in production from goods to services in the UK. This is due to the reduction in goods production & increased cheap production from abroad making it more viable to subcontract in from overseas than to produce it ourselves.



ResultsPlus

Examiner Comments

The candidate received 4 marks for the decline of certain sectors and another 4 for the increased standard of living pulling in imports. No evaluation so the total was 8 marks.

*(iii) Examine **two** possible causes of the "largest ever recorded trade in goods deficit in 2010" (Extract 1, lines 11-12).

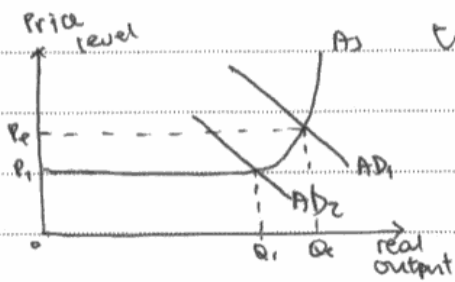
(12)

~~(current account deficit)~~
Trade in goods deficit refer to as exports is less than imports. In extract 2, it is mentioned that "the UK's exports is growing, but not as fast as other European countries". This could suggest that other countries' goods are more attractive. that could have been caused by better innovation, ~~more~~ since ~~the~~ their designs of the goods are better function than UK's goods, more people will demand for the goods from European countries even people from UK, therefore UK will experience an increase in imports from ~~other~~ ^{those} countries (M⁺) but less demand for domestic goods, hence exports falls leading to ~~current~~ ^{trade in} goods deficit.

Another reason why there's trade in goods deficit might be due to other countries ~~have~~ having a more productive workforce. As the productivity of their economy increase, the output per unit of worker increases therefore the cost ^{per unit} falls. This means those foreign producers are able to lower the price of their goods, the lower price will attract more demand and ~~hence~~ the export of those countries will increase relative to the less productive ~~workforce~~ ~~in the~~ UK. Demand will come from UK to those countries but

less demand ~~less~~ ^{TOI} UK goods, therefore resulting in import greater than exports and again trade in goods deficit.
~~a trade in goods deficit.~~

In evaluation, in the short run, ~~although~~ the trade in goods deficit will



cause AD_1 to shift to the left to AD_2 . Real output of the economy will fall from Q_e to Q_i , price level will fall from

P_e to P_i . In the long run though, because the deficit has caused price level of goods to fall (P_e to P_i), the UK's goods are now cheaper which will increase its competitiveness between others such as the European countries as cheaper price will attract more demand. The trade in goods deficit might therefore be resolved in the future.



ResultsPlus

Examiner Comments

Less attractive products from poor innovation 4 marks. Lower productivity meaning higher prices 4 marks. Evaluation 4 marks as falling domestic prices might resolve some of the issues surrounding price competitiveness in the longer run.

Question 2 (c)

Generally this question was confidently answered by the majority of candidates. Many answers included an appropriate diagram, were well structured, explained and evaluated. Some candidates focused, at least in part, on the causes rather than the benefits of growth. Often the benefit identified was explained as 'this will help us achieve more growth in the future', rather than demonstrating a true understanding of how economic growth serves us. A minority of candidates discussed at length policies to achieve growth and some candidates included points more relevant to a developing nation.

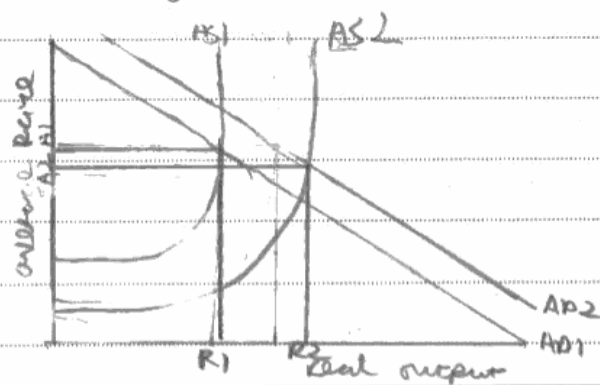
* (c) Evaluate the benefits of economic growth for the UK.

(30)

Economic growth is the increase in productive capacity in the UK over time. It is measured using GDP which is the collective incomes and ~~profits~~ revenues of individuals and firms in the economy.

one benefit of economic growth in the economy is that it allows for higher employment in the economy as firms are making higher revenues due to increased spending in the economy. ~~As~~ As more people are employed this in turn increases consumer spending further as there are more people with jobs and as a result there is more disposable income to spend on consumer goods (further increasing firm revenues). This is an example of a positive multiplier effect. Due to increased economic growth, prices will also increase as well as housing prices. This will make people feel more ~~richer~~ wealthy and will encourage them to spend more, this is known as the wealth effect.

Another benefit of economic growth is experienced by the government. Due to increases in consumer spending and higher employment as a result the government will acquire more revenue from taxation. They ~~will~~ ^{get} revenue from direct taxation such as income tax, as more people are employed it means more people are paying income tax and as a result the government's tax revenue will increase. They will also ~~get~~ ^{get} more tax revenue from ~~the~~ indirect taxation such as VAT on products. As consumption has increased more VAT tax is acquired by the government resulting in higher tax revenues to be spent on the various aspects of the economy. The money can be spent on higher education for example to make future generations a more skilled workforce causing output to increase and causing economic growth to increase further.



Due to economic growth there is an increase in aggregate demand and increase in supply as shown by the AD/AS diagram.

Although economic growth results in higher employment it also results in higher income inequality as the effects of economic growth are not experienced by all and while some workers do get a pay rise as a result of economic growth, others will see no effect. In some cases economic growth is not experienced by everyone in the economy.

The increase in consumer spending will cause an increase in prices. This in turn will cause inflation to go up which will make UK firms less competitive abroad, this will cause cheaper alternatives to be demanded causing an increase in leakages but decrease in injections ~~and~~ potentially causing a current account deficit.

Another issue is with the ~~very~~ magnitude of the rate of economic growth. Should growth rate be small the there will be no difference experienced by the economy whereas if it is a rapid growth there can be negative effects as a result such as misjudgement by the government and firms on policies for example or how much to supply. This can easily result in a misallocation of resources or so cause market failure. This could also result in a trade in goods ~~to~~ deficit if too much is demanded by the economy in terms of imports and little ~~is~~ exports occur.

There can also be an opportunity cost of what the government do with it's tax revenue. on one hand they can spend it on higher education but just go a building of a hospital. There can also be a time lag between what the government spends and the outcome of that investment.



ResultsPlus

Examiner Comments

Definition received 2 marks in first paragraph. 4 marks for employment in the second. 2 marks were awarded for asset values rising although these weren't needed.

Direct taxation revenue on the second page was awarded 4 marks and the diagram another 4 as it was just legible.

The second and third paragraphs were each awarded 4 marks for evaluation on the third page. The last page at the bottom received 2 evaluation marks for the time lag.

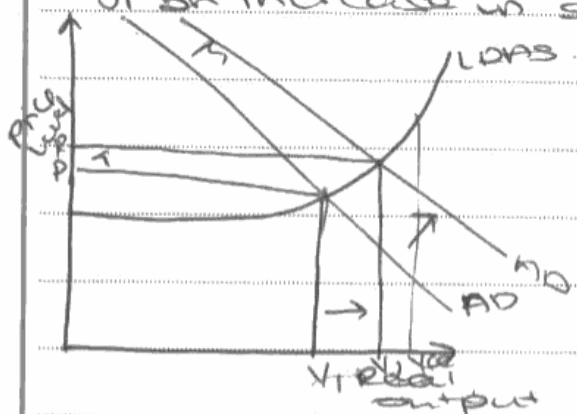
16 for KAA and 10 for evaluation which made a total of 26 marks.

*c) Evaluate the benefits of economic growth for the UK.

(30)

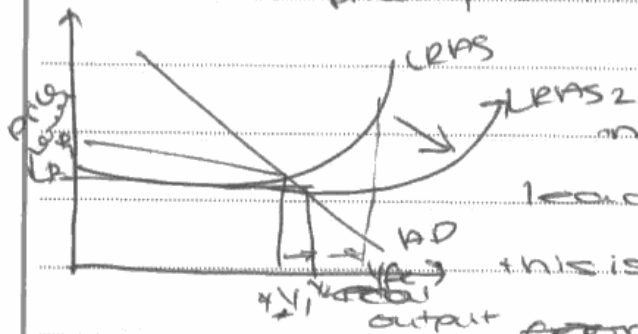
Economic growth is the sustained increase in real GDP over a few quarters. Real GDP is used as it is GDP that has been adjusted for inflation and therefore gives a true indication of the economy's growth and situation.

Economic growth can be due to a few possibilities it can be due to export led growth or due to an increase in demand or an increase in supply in the long term.



A rise in AD can lead to a rise in real output from $Y_1 \rightarrow Y_2$ and a fall in the output gap. It can also however cause

a rise in prices from $P_1 \rightarrow P_2$.



In the long run economic growth can be

led by an increase in supply this is as an increase in LRAS from $LRAS_1 \rightarrow LRAS_2$ causes

real output to rise from $Y_1 \rightarrow Y_2$ narrowing the output gap and also decreasing price levels

from $P_1 \rightarrow P_2$.

Economic growth is the main macroeconomic objective.

An A rise in economic growth can lead to many benefits. Firstly, it can lead to a decrease in unemployment. This is as, as real output increases, the ~~demand~~ ^{demand} for goods and services also increases. Due to employment being derived demand a rise in demand for other goods and services will cause a rise in the need for labour and increase employment lowering unemployment and therefore meeting a macro-economic objective of low unemployment.

If economic growth is export led growth it will also help reduce our balance of payment deficit. It has said that the £ has been depreciated by 20%. Thus making the UK economy more internationally competitiveness exports look relatively cheaper compared to other countries. Therefore more exports leading to a rise in net exports.

Also a fall in the pound will lead to an increase in hot money and FDI into the economy, leading to a fall in balance of payment deficit.

Economic growth also means incomes will rise. Therefore, more people will have higher disposable income and thus a higher living standard. People will be able to afford more luxuries those goods that are elastic goods.

It would also reduce inequality, as there is a rise in jobs so those who are actively seeking for a job will be able to find one more easily and a rise in economic growth will mean they will have very reasonable incomes probably a lot above the national minimum wage.

It will increase the productive capacity of the economy if lead by supply.

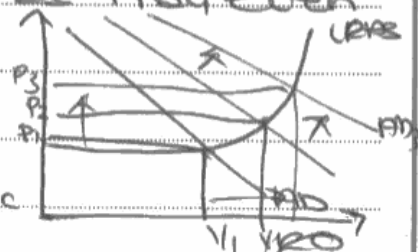
Nevertheless, a rise in economic growth does cause a lot of economic concerns

Firstly it will cause inflation as may even lead to hyper inflation. This is

is economic growth lead by demand

will mean while economic

growth is occurring inflation will be rising rapidly at a more than proportional rate this is due to the multiplier



affect. This will lead to an increase in overall prices of goods and services,
* Not meeting the target of 1.2% of CPI
It will also cause negative externalities
this is as we are polluting and using
finite resources like oil and wood.
This means, although the economy
will be growing the sustainability
of the country will be decreasing and
in the future generations will not be able
to meet their own needs.

besides, although a rise in economic
growth may lead to a rise in incomes
and therefore higher living standards
it may actually in fact cause lower standards
of living. This is as there will need
more work, so more overtime and there
fore increasing stress and reducing
living standards.

Overall economic growth in the short run
has a positive effect in the economy but in the
long run can cause many conflicts.
* set by the MPC one of the economic objectives.

(Total for Question 2 = 80 marks)



ResultsPlus

Examiner Comments

Definition 2 marks in the first paragraph and another 4 marks for the diagram further down the page.

On the second page there were 4 marks for each paragraph.

On the third page 4 marks for the higher standard of living.

The fourth obtains full marks for evaluation across three points; inflation, pollution and increased working hours.

PAPER: 80 MARKS

Paper Summary

There was an 11:9 split in favour of answering question 1, which suggests the questions were similarly popular. Question 1 had a mean score that was several marks higher than question 2.

The vast majority of the questions differentiated between candidates effectively and gave the candidates the opportunity to demonstrate their knowledge and skills. Some questions were on average less well answered, particularly 2(b)(ii) and 2(b)(iii), although there were some excellent responses to them that achieved full marks. Question 1c had a marginally higher mean than 2(c) as a number of candidates wanted to answer a question about the causes of growth rather than its benefits. However there were many excellent answers to the 30 mark essays in both questions.

Most entrants showed considerable awareness of the current state of the economy and some were truly outstanding in using this information to help them evaluate. This real interest in the economy was evident in many papers, and was easy to credit within the flexible mark scheme.

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