



*Rewarding Learning*

**ADVANCED**  
**General Certificate of Education**  
**2015**

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**Economics**

Assessment Unit A2 2

The Global Economy

**[AE221]**

**TUESDAY 19 MAY, AFTERNOON**

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**MARK**  
**SCHEME**

## General Marking Instructions

This mark scheme is intended to ensure that the A2 examinations are marked consistently and fairly. The mark scheme provides examiners with an indication of the nature and range of candidate responses likely to be worthy of credit. It also sets out the criteria which they should apply in allocating marks to candidates' responses. The mark schemes should be read in conjunction with these general marking instructions which apply to all papers.

### Quality of candidates' responses

In marking the examination paper, examiners will be looking for a quality of response reflecting the level of maturity which may reasonably be expected of 18-year-olds, which is the age at which the majority of candidates sit their A2 examinations.

### Flexibility in marking

The mark scheme is not intended to be totally prescriptive. For many questions, there may be a number of equally legitimate responses and different methods by which the candidates may achieve good marks. No mark scheme can cover all the answers which candidates may produce. In the event of unanticipated answers, examiners are expected to use their professional judgement to assess the validity of answers. If an answer is particularly problematic, then examiners should seek the guidance of the Supervising Examiner for the paper concerned.

### Positive marking

Examiners are encouraged to be positive in their marking, giving appropriate credit for valid responses rather than penalising candidates for errors or omissions. Examiners should make use of the whole of the available mark range for any particular question and be prepared to award full marks for a response which is as good as might reasonably be expected for 18-year-old candidates. Conversely, marks should only be awarded for valid responses and not given for an attempt which is completely incorrect and inappropriate.

### Types of mark schemes

Mark schemes for questions which require candidates to respond in extended written form are marked on the basis of levels of response which take account of the quality of written communication. These questions are indicated on the cover of the examination paper. Other questions which require only short answers are marked on a point for point basis with marks awarded for each valid piece of information provided. Some material may be included in the mark scheme for the benefit of teachers and pupils preparing for future examinations. Candidates are not expected to have provided this information. Such material is printed in the mark scheme in italics.

### Levels of response

Questions requiring candidates to respond in extended writing are marked in terms of levels of response. In deciding which level of response to award, examiners should look for the "best fit" bearing in mind that weakness in one area may be compensated for by strength in another. In deciding which mark within a particular level to award to any response, examiners are expected to use their professional judgement. The following guidance is provided to assist examiners.

**Threshold performance:** Response which just merits inclusion in the level and should be awarded a mark at or near the bottom of the range.

**Intermediate performance:** Response which clearly merits inclusion in the level and should be awarded a mark at or near the middle of the range.

**High performance:** Response which fully satisfies the level description and should be awarded a mark at or near the top of the range.

**Marking calculations**

In marking answers involving calculations, examiners should apply the “own figure rule” so that candidates are not penalised more than once for a computational error.

**Quality of written communication**

Quality of written communication is taken into account in assessing candidates’ responses to all questions that require them to respond in extended written form. These questions are marked on the basis of levels of response. The description for each level of response includes reference to the quality of written communication. Where the quality of candidates’ economics is not matched by the quality of written communication, marks awarded will not exceed the maximum for Level 2 in questions which have three levels of response or the maximum for Level 3 in those which have four levels of response.

For conciseness, quality of written communication is distinguished within levels of response as follows:

Level 1: Quality of written communication is limited.

Level 2: Quality of written communication is satisfactory.

Level 3: Quality of written communication is of a high standard.

Level 4: Quality of written communication is excellent.

In interpreting these level descriptions, examiners should refer to the more detailed guidance provided below:

**Level 1 (Limited):** The candidate makes only a limited attempt to select and use an appropriate form and style of writing. The organisation of material may lack clarity and coherence. There is little use of specialist vocabulary. Presentation, spelling, punctuation and grammar may be such that intended meaning is not clear.

**Level 2 (Satisfactory):** The candidate makes a reasonable attempt to select and use an appropriate form and style of writing, supported with appropriate use of diagrams as required. Relevant material is organised with some clarity and coherence. There is some use of appropriate specialist vocabulary. Presentation, spelling, punctuation and grammar are sufficiently competent to make meaning evident.

**Level 3 (High Standard):** The candidate successfully selects and uses an appropriate form and style of writing, supported with the effective use of diagrams where appropriate. Relevant material is organised with a high degree of clarity and coherence. There is widespread use of appropriate specialist vocabulary. Presentation, spelling, punctuation and grammar are of a sufficiently high standard to make meaning clear.

**Level 4 (Excellent):** The candidate successfully selects and uses the most appropriate form and style of writing, supported with precise and accurate use of diagrams where appropriate. Relevant material is extremely well organised with the highest degree of clarity and coherence. There is extensive and accurate use of appropriate specialist vocabulary. Presentation, spelling, punctuation and grammar are of the highest standard and ensure that meaning is absolutely clear.

- 1 (a) • The data is presented in the form of index numbers with both nations starting at a base of 100 in Q1 2010. This does not mean that American and Japanese exports were equal at that time, only that this is the figure on which all subsequent comparisons are based.
- By Q4 2012 Japanese exports had fallen by 3 per cent to 97
  - By Q4 2012 American exports had risen by 15 per cent to 115.
  - The trend in American exports has been much more consistent than for Japanese which were extremely volatile
  - The high point for Japanese exports was 109 in Q2 2012.
  - The high point for American exports was 117 in Q2 2012
  - Between Q2 2012 and Q4 2012 Japanese exports have fallen from 109 to 97. This is a fall of 12 percentage points or 11 per cent
  - Between Q2 2012 and Q4 2012 American exports have fallen from 117 to 115. This is a fall of 2 percentage points or 1.7 per cent

[1] mark for each valid point made up to a maximum of [5] [5]  
5 marks can only be awarded if there is evidence of data manipulation.

- (b) Both economic history and economic theory indicate that import controls are likely to make a bad situation even worse. However, in times of recession there will always be powerful voices raised in favour of import controls to protect local industries and employment. The current world slow-down is no exception.

Increased trade barriers would reduce the level of international trade and hence lower the net export component of aggregate demand. This would be likely to reduce the level of real GDP and lead to higher unemployment and lower living standards. There could be a world-wide recession.

Consumers would be faced with less choice, higher prices and a fall in consumers' surplus. Some local firms might gain by replacing cheap exports with more expensive domestically produced goods. This would be likely to increase producers' surplus. However overall there is likely to be a net welfare loss.

**Level 1 ([1]–[3])**

Candidate provides little analysis of the impact on the world economy of an increase in import controls. There may be a number of unsubstantiated assertions which will not be supported by relevant economic analysis. Quality of written communication is limited.

**Level 2 ([4]–[7])**

Candidate provides some analysis of the impact on the world economy of an increase in import controls. Key issues will be addressed but this may contain errors or lack depth. Quality of written communication is satisfactory.

**Level 3 ([8]–[10])**

Candidate provides a clear and comprehensive analysis of the impact on the world economy of an increase in import controls. Key issues will be addressed in depth and quality of written communication is of a high standard.

[10]

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- (c) A number of factors have contributed to the UK's success in attracting FDI. These include:

- Membership of the EU encourages inward investment as firms can locate in the UK and export to the rest of the European Union
- The level of corporation tax has been significantly reduced
- Northern Ireland in particular has a young and relatively well educated workforce
- The common language makes the UK attractive for American firms
- Firms face less regulation in the UK than in many other EU states
- The UK is not a member of the eurozone and this has given it exchange rate flexibility against the euro
- There are generous grants and other incentives
- There is a flexible market for labour.

**Level 1 ([1]–[3])**

Candidates provide little examination of why the UK is a popular destination for FDI. There is likely to be a superficial anecdotal approach with vague reference to issues like “cheap labour”. Quality of written communication is limited.

**Level 2 ([4]–[7])**

Candidates provide some examination of why the UK is a popular destination for FDI. There will be some analysis of issues such as tax and labour costs and quality of written communication is satisfactory.

**Level 3 ([8]–[10])**

Candidates provide a clear and comprehensive examination of why the UK is a popular destination for FDI. Key issues will be explained in some depth and quality of written communication is of a high standard. [10]

- (d) Immigration into the UK has become a highly contentious political issue and has in part led to the rise of UKIP. Within the EU it is not possible to restrict the movement of EU citizens but controls can be placed on immigration from outside the EU. This would have a number of economic and social impacts:

- Reduction in supply of labour and increase in wage rate
- Leftward shift in aggregate supply curve
- Reduction in demands on health and educational services
- Reduced need for translation services
- Reduced social tensions between migrants and indigenous population
- Labour shortages in key areas such as health service and premier league football
- Possibility that labour shortages and higher wages would force firms to increase investment
- Increased costs associated with tighter immigration controls

Restrictions on the international movement of capital would be difficult to police and would also have significant economic implications:

- UK is largest recipient in EU of FDI. Restrictions would cost jobs
- Many UK firms invest overseas and other nations might place restrictions on this
- Restrictions on flows of portfolio investment would reduce the risk of the spread of financial contagion between nations
- International investment allows large transnational corporations to avoid paying tax in the UK

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**Level 1 ([1]–[5])**

Candidate provides little critical examination of the proposal to restrict the international movement of capital and labour. Key issues are either not addressed or dealt with in a superficial manner. There is no significant economic analysis and quality of written communication is limited.

**Level 2 ([6]–[10])**

Candidate provides some critical examination of the proposal to restrict the international movement of capital and labour. Key issues are addressed but this will contain errors or be incomplete. There is a degree of economic analysis and quality of written communication is satisfactory.

**Level 3 ([11]–[15])**

Candidate provides an in depth critical examination of the proposal to restrict the international movement of capital and labour. Key issues are addressed in detail and there is significant economic analysis. Quality of written communication is of a high standard. [15]

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- 2 (a) Economic growth is simply an increase in a country's output of goods and services. It is usually measured by the annual increase in real GDP. It tells us nothing about the nature of the items produced or about how the proceeds of growth are distributed. Hence it is a deeply flawed indicator of the welfare of a country's citizens.

Economic development is a much broader indicator but one which has no precise definition: John Sloman says, "Development is a normative concept. Its definition will depend on the goals that the economist assumes societies want to achieve."

However most measures of development will include variables such as literacy rates, infant mortality, healthcare provision and quite often political freedom. These are incorporated in measures such as the HDI and, formerly, the ISEW.

Economic growth is relatively easy to measure. Economic development is not.

**Level 1 ([1]–[5])**

Candidate provides little explanation of the main differences between growth and development. The definitional problems of development are not addressed and quality of written communication is limited.

**Level 2 ([6]–[10])**

Candidate provides some explanation of the main differences between growth and development. However this is likely to be incomplete or contain minor errors. The definitional problems of development may be mentioned but not explained in detail. Quality of written communication is satisfactory.

**Level 3 ([11]–[15])**

Candidate provides a clear and detailed explanation of the main differences between growth and development. The definitional problems of development are fully explained and quality of written communication is of a high standard. [15]

- (b) The foreign aid budgets of MEDCs are a relatively small percentage of total GDP. The latest figure for the UK is 0.72% of GDP; for the USA this proportion is less than 0.25%. Reducing aid budgets would have only a marginal impact on total government spending. Nevertheless in times of austerity it is reasonable that every area of government spending should be examined. The high growth rates of many sub-Saharan nations has highlighted this issue.

Issues for analysis and discussion include:

- Problems of misuse of aid by corrupt governments
- Inefficient allocation of aid
- Opportunity cost of foreign aid budget upon other areas of government spending
- Hostility to and dangers faced by aid workers in many countries
- Aid may create dependency and hinder economic development
- Aid may improve security in nations where there has been a breakdown of the state such as Somalia
- Political influence which rich nations receive through aid budget
- Relative affluence of some recipient nations such as India and Nigeria
- The high levels of military expenditure by the governments of some LDCs
- High growth rates have not eliminated poverty
- The benefits of growth have not been equitably distributed in many LDCs

**Level 1 ([1]–[7])**

Candidate provides little critical examination of the view that high rates of economic growth in some LDCs provide justification for substantial cuts in the aid budgets of MEDCs. Few issues are addressed and none in any depth. Quality of written communication is limited.

**Level 2 ([8]–[13])**

Candidate provides some critical examination of the view that high rates of economic growth in some LDCs provide justification for substantial cuts in the aid budgets of MEDCs. Some issues are addressed but this will lack depth or contain errors. Quality of written communication is satisfactory.

**Level 3 ([14]–[19])**

Candidate provides an in-depth critical examination and judgement of the view that high rates of economic growth in some LDCs provide justification for substantial cuts in the aid budgets of MEDCs. Most issues are addressed in depth and quality of written communication is of a high standard.

**Level 4 ([20]–[25])**

Candidate provides an in-depth critical examination and balanced judgement of the view that high rates of economic growth in some LDCs provide justification for substantial cuts in the aid budgets of MEDCs. The major issues are addressed in significant depth and this is supported by relevant economic analysis. Quality of written communication is excellent. [25]

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- 3 (a) The exchange rate of the pound against the euro is, by and large, a freely floating one, which means it is determined by market forces with a minimum of government intervention.

Hence it will be the demand and supply for pounds and euros which ultimately determines the rate of exchange between the two currencies. The pound will rise in value against the euro if demand rises or supply falls and the euro will rise against the pound for similar reasons. A number of factors influence these market forces.

- UK purchases of imports from the eurozone creates sales of sterling and purchases of euros
- Eurozone purchases of imports from the UK will cause sales of euros and purchases of pounds
- Investment flows from the eurozone to the UK increase the demand for pounds and the supply of euros
- Investment flows from the UK to the eurozone increase the demand for euros and the supply of pounds
- Speculation can affect exchange rates
- International confidence in the economic management of the country can also affect the demand for its currency
- Use of appropriate and accurately labelled diagrams

**Level 1 ([1]–[5])**

Candidate provides little explanation of how the rate of exchange between the pound and the euro is determined. There will be superficial references to issues such as tourism but no significant economic analysis and quality of written communication is limited.

**Level 2 ([6]–[10])**

Candidate provides some explanation of how the rate of exchange between the pound and the euro is determined. There is a degree of economic analysis of issues such as exports and imports and quality of written communication is satisfactory.

**Level 3 ([11]–[15])**

Candidate provides a clear and comprehensive explanation of how the rate of exchange between the pound and the euro is determined. This is supported by relevant economic analysis and quality of written communication is of a high standard.

[15]

- (b) The issue of fixed versus floating exchange rates has been debated by economists and policy makers for many years. For almost three decades after the Second World War the world's major currencies were fixed in terms of the dollar which itself was pegged to a fixed value in gold. This was known as the Bretton Woods system and was supervised by the IMF. Member states would make deposits to the IMF which would then make loans to those countries which were facing a balance of payments deficit and downward pressure on the value of their currency. However rates were not fixed in perpetuity and could be adjusted in the long run in the event of a structural balance of payments deficit.

If a system of fixed rates were to be introduced today then the IMF would have to undertake a similar role. Today the Chinese renminbi is fixed against

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the American dollar and the members of the eurozone share a common currency. However the pound and the American dollar are allowed to float against other major currencies and against each other.

The main benefit of fixed rates is the certainty which it gives to international trade by removing currency risk from transactions.

The main disadvantage is the restriction which it places on domestic economic management. Macroeconomic objectives such as full employment become subservient to the maintenance of a fixed exchange rate.

**Issues for analysis and evaluation include:**

- Explanation of fixed exchange rates and how they are maintained
- Role of IMF in maintaining fixed rates
- Explanation of how fixed exchange rates assist in providing a stable trading environment by eliminating currency risks
- Explanation of how fixed exchange rates encourage international trade
- Explanation of how fixed exchange rates affect macroeconomic policy by forcing governments to adopt deflationary policies in order to maintain the fixed rate
- Explanation of how fixed exchange rates help to control inflation
- Explanation and evaluation of other exchange rate systems such as free floating, adjustable peg etc
- Reference to international and historical examples.

**Level 1 ([1]–[7])**

Candidate provides little explanation or critical examination of the view that the IMF should introduce a system of fixed exchange rates. There is no significant economic analysis and quality of written communication is limited.

**Level 2 ([8]–[13])**

Candidate provides some explanation and critical examination of the view that the IMF should introduce a system of fixed exchange rates. However the evaluation will be one-sided or lack depth. There is a degree of economic analysis though this will be incomplete or superficial. Quality of written communication is satisfactory.

**Level 3 ([14]–[19])**

Candidate provides a clear explanation and meaningful critical examination of the view that the IMF should introduce a system of fixed exchange rates. There is relevant economic analysis including some explanation of the role of the IMF and quality of written communication is of a high standard.

**Level 4 ([20]–[25])**

Candidate provides a clear and comprehensive explanation and in depth critical examination of the view that the IMF should introduce a system of fixed exchange rates. There is accurate and relevant economic analysis including a clear explanation of the role of the IMF and a mature judgement on the key issues. Quality of written communication is excellent. [25]

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4 (a) The current account is made up of:

- Trade in goods, including manufactured, semi manufactured and raw materials;
- Trade in services such as financial services, travel and advertising;
- Net income flows such as interest and dividends earned by foreign citizens from UK assets and dividends and interest earned by UK citizens from foreign assets;
- Net current transfers both private and official.

The total of these sections is usually a negative figure as shown below:

<i>Date</i>	<i>Trade in goods</i>	<i>Trade in services</i>	<i>Income flows</i>	<i>Current transfers</i>	<i>Overall Balance</i>
2013 Q1	-26.5 bn	20.4 bn	-6.2 bn	-2.1bn	-14.4bn

The financial account records cross border changes in the holdings of assets such as shares, government securities, buildings, land and businesses.

- When foreign citizens and businesses purchase UK assets this is an inflow of funds and when UK citizens purchase assets abroad this represents an outflow.
- Direct investment refers to the purchase of physical assets such as a factory, a farm or property. It also includes the acquisition of more than 10 per cent of the equity of a foreign firm. So when a UK citizen purchases a Spanish villa this is an outflow of funds and a debit item.
- Portfolio investment refers to changes in holdings of paper assets such as company shares or government securities. So when an American pension fund buys UK gilt-edged securities this is an inflow of funds and a credit item. This account also records changes in reserve assets.

#### **Level 1 ([1]–[5])**

Candidate provides no significant explanation of the differences between the current and financial accounts of the balance of payments and the UK balance of payments. There will at best be a vague reference to issues like exports and imports but little explanation. Quality of written communication is limited.

#### **Level 2 ([6]–[10])**

Candidate provides some explanation of the differences between the current and financial accounts of the balance of payments. However this will be incomplete or contain errors. Quality of written communication is satisfactory.

#### **Level 3 ([11]–[15])**

Candidate provides a clear and comprehensive explanation of the difference between the current and financial accounts of the balance of payments. Quality of written communication is of a high standard. [15]

- (b) The UK economy has suffered from low productivity for many decades. Our exports are uncompetitive and UK consumers increasingly buy imports rather than high priced domestic products. One solution to this is to reduce our labour costs by lowering real wages and increasing output per worker.

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This could be achieved by reducing the size of the public sector and by maintaining a public sector wage freeze. Incentives could be increased by reducing income and corporation tax rates. Tax breaks could be introduced for R and D and the introduction of new technology.

There are of course other ways in which a long term structural deficit could be addressed. These include depreciation of the pound but this is not guaranteed to succeed and may be inflationary.

**Issues for analysis and evaluation include:**

- Explanation of long term current account deficit
- How the significance of the deficit could be assessed
- Explanation of nominal wages, real wages, productivity and unit labour costs
- Labour costs and their impact on comparative advantage
- Explanation and evaluation of policies to increase productivity (supply side policies)
- Impact of de-industrialisation on the current account
- Explanation and evaluation of other policies such as depreciation of the pound and import controls.

**Level 1 ([1]–[7])**

Candidate provides little critical examination of the view that only lower wages and higher productivity can correct the persistent deficit on the current account of the UK's balance of payments. There is no significant economic analysis and quality of written communication is limited.

**Level 2 ([8]–[13])**

Candidate provides some critical examination of the view that only lower wages and higher productivity can correct the persistent deficit on the current account of the UK's balance of payments. However this will lack depth or be one-sided. There is a degree of economic analysis and quality of written communication is satisfactory.

**Level 3 ([14]–[19])**

Candidate provides a significant critical examination and judgement of the view that only lower wages and higher productivity can correct the persistent deficit on the current account of the UK's balance of payments. This is supported by relevant economic analysis and quality of written communication is of a high standard.

**Level 4 ([20]–[25])**

Candidate provides an in-depth critical examination and balanced judgement of the view that only lower wages and higher productivity can correct the persistent deficit on the current account of the UK's balance of payments. There is accurate and relevant economic analysis and quality of written communication is excellent.

[25]

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**Total****80**AVAILABLE  
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