

[C038/SQP066]

Intermediate 2
Economics
Specimen Question Paper

Time: 1 hour 45 minutes

NATIONAL
QUALIFICATIONS

60 marks are allocated to this paper.

Part 1 (40 marks) Candidates should attempt **both** items.

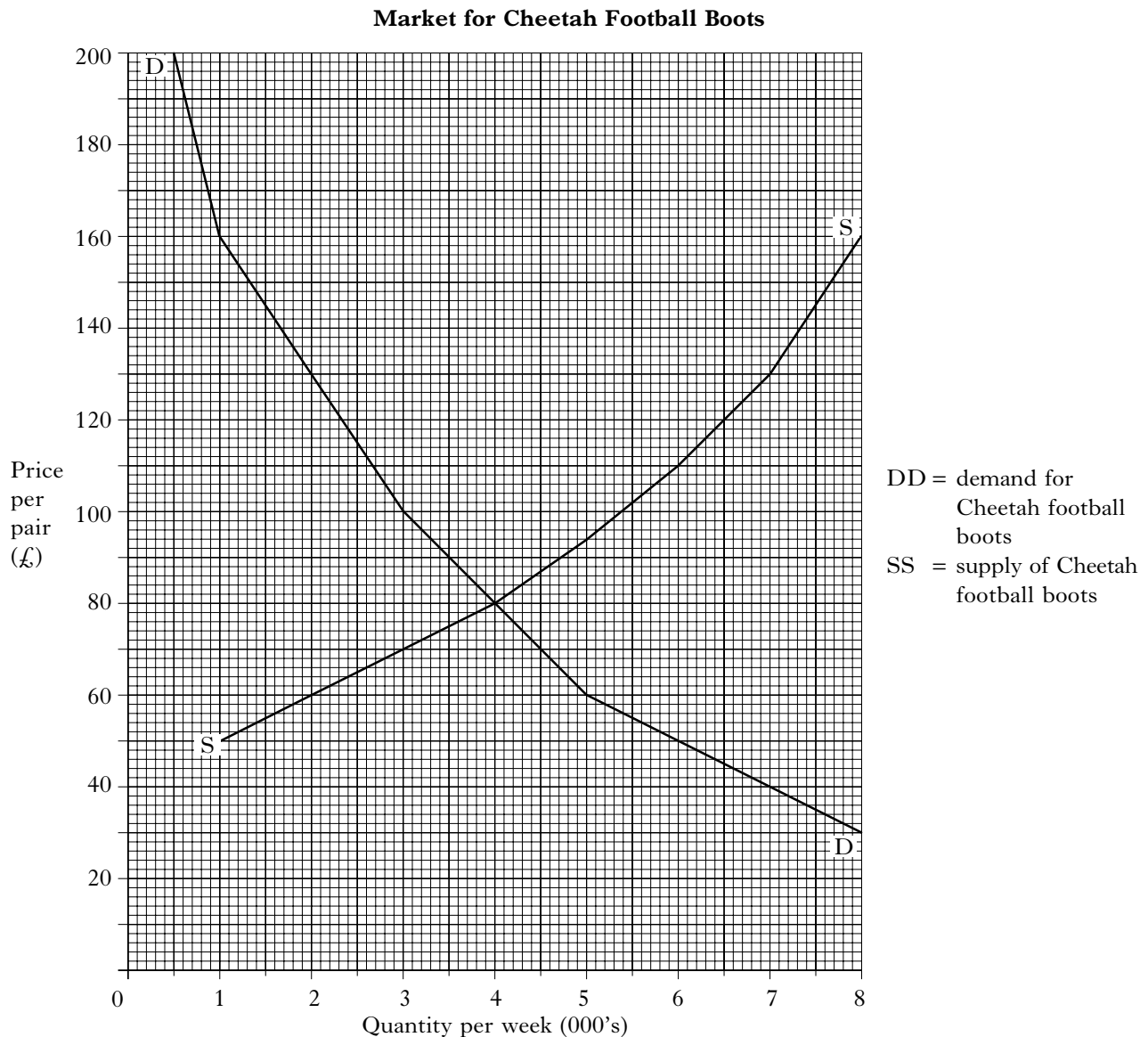
Part 2 (20 marks) Candidates should attempt **one** question.

PART 1

ITEM A

Read the information below, then answer the questions which follow.

Cheetah plc is a UK sportswear manufacturer. The following diagram shows the market for its football boots.



- | | <i>Marks</i> |
|--|--------------|
| (a) Explain what is meant by the term “ Market for Cheetah Football Boots ”. | 2 |
| (b) Calculate the total revenue per week from sales when the price is £70 per pair. | 2 |
| (c) Explain why the quantity of football boots demanded falls as the price rises. | 2 |
| (d) (i) What is meant by the term real income? | 2 |
| (ii) Explain how a rise in UK consumers’ real income might affect the demand for Cheetah football boots. | 2 |
| (e) (i) What is meant by productivity? | 1 |
| (ii) Suggest one way in which Cheetah plc could increase its productivity. | 1 |
| (iii) Explain how an increase in Cheetah’s productivity will affect the supply of its football boots. | 2 |
| (f) “Victorious Scots win World Cup.”
Explain, using a diagram, what would happen to the market for Cheetah football boots if the Scottish football team were to win the World Cup. | 3 |
| (g) The UK government decides to grant Cheetah plc a subsidy for every pair of football boots it produces. | |
| (i) Explain how this subsidy would affect the supply of Cheetah football boots. | 1 |
| (ii) Suggest two reasons why the government might grant this subsidy to Cheetah plc. | 2 |

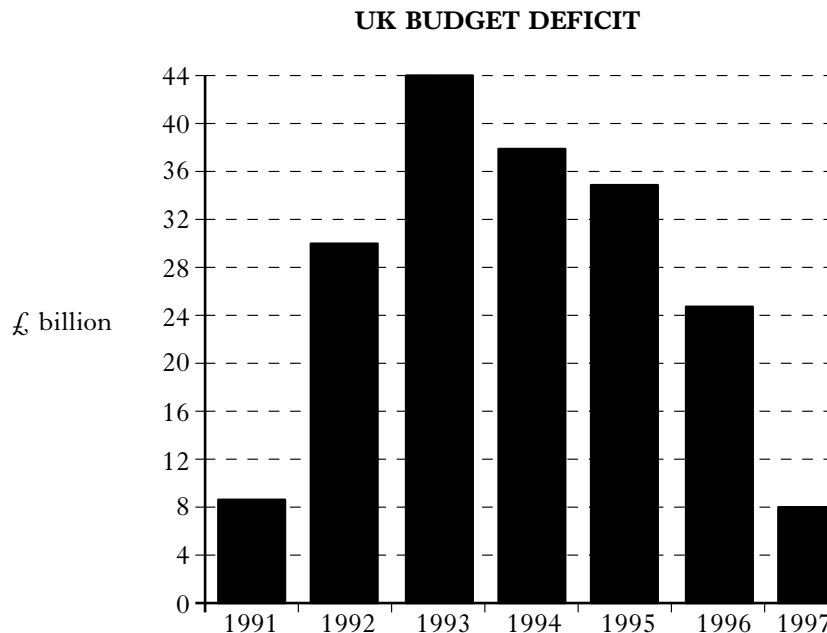
(20)

PART 1

ITEM B

Read the passage below, then answer the questions which follow.

One of the main long term aims of the UK government is to have a **balanced budget**. However, the following graph shows that the UK budget has been in deficit in recent years.



- | | <i>Marks</i> |
|--|--------------|
| (a) Explain what is meant by the term “balanced budget” (line 1). | 2 |
| (b) (i) Describe the trend in the UK budget deficit as shown in the above graph. | 1 |
| (b) (ii) In 1993 the deficit reached £44 billion. Suggest reasons for such a high deficit. | 2 |
| (c) (i) Explain, using examples, the difference between direct and indirect taxation. | 3 |
| (c) (ii) The effect of indirect taxes is often regressive. Explain what this means. | 2 |
| (d) (i) Describe two measures a government can take to reduce a budget deficit. | 2 |
| (d) (ii) Explain how these measures are likely to affect inflation and unemployment. | 4 |
| (e) Give two examples of government spending and explain why they are financed by government. | 4 |
| | (20) |

PART 2—Essay Questions

Candidates should attempt **one** question

Marks

- | | | | |
|----|-----|--|------|
| 1. | (a) | Explain what is meant by scarce resources. | 5 |
| | (b) | Explain what is meant by the term “market” in Economics. | 4 |
| | (c) | Explain, with the use of a diagram, how the price of a good in a market could rise. | 5 |
| | (d) | Using examples, explain why, in some markets, goods and services are provided by the government. | 6 |
| | | | (20) |
| 2. | | Being a member of the European Union (EU) and the single market has meant that an increasing amount of our trade is with other EU countries. | |
| | (a) | Explain what is meant by the term “single market”. | 4 |
| | (b) | Explain how UK consumers benefit from trade with our European partners. | 4 |
| | (c) | Explain why EU member countries may wish to restrict trade with countries outwith the EU. | 6 |
| | (d) | Explain what is meant by “the Euro” and describe one advantage and one disadvantage for the UK of joining the Euro. | 6 |
| | | | (20) |
| 3. | (a) | Explain the factors that can lead to an increase in unemployment in an economy. | 6 |
| | (b) | What are the effects of rising unemployment on | |
| | | (i) firms; | |
| | | (ii) the government? | 6 |
| | (c) | Suggest two policies a government can use to reduce unemployment and explain how these policies would work. | 8 |
| | | | (20) |
| 4. | | Recent natural disasters in central American countries have meant a world shortage of raw materials. This has caused raw material prices to rise, and has also caused an increase in the UK rate of inflation. | |
| | (a) | Explain, using a diagram, how a world shortage of raw materials would cause their prices to rise. | 6 |
| | (b) | Explain how an increase in the price of raw materials would affect: | |
| | | (i) UK manufacturers; | |
| | | (ii) the UK balance of trade. | 6 |
| | (c) | Other than an increase in the price of raw materials, explain two causes of inflation. | 4 |
| | (d) | Explain two policies a government could use to try to slow down inflation. | 4 |
| | | | (20) |
| 5. | | National Income statistics are used as a measurement of economic growth within a country. A major problem in Less Developed Countries (LDCs) is that growth rates tend to be very low. | |
| | (a) | Explain what is meant by the term “economic growth”. | 3 |
| | (b) | Other than the low levels of economic growth, describe the main characteristics of LDCs. | 6 |
| | (c) | Explain some of the problems which can arise when using National Income statistics to compare standards of living in different countries. | 5 |
| | (d) | Explain three measures a government could take to try to promote economic growth. | 6 |
| | | | (20) |

[END OF QUESTION PAPER]

[C038/SQP066]

Intermediate 2
Economics
Specimen Marking Instructions

NATIONAL
QUALIFICATIONS

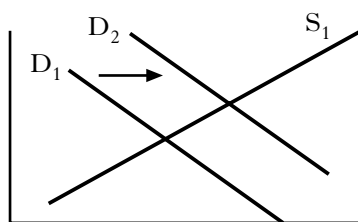
Solution

PART 1

Item A

Marks

- (a) Sum of individual demand from consumers (buyers) and individual supply by producers (sellers) of Cheetah boots. 2
- (b) $3,000 \times £70 = £210,000$ per week. 2
- (c) Simple explanation of any (or a combination) of the following:
Income effect, substitution effect or diminishing marginal utility. 2
- (d) (i) Purchasing power, the comparison of money income with changing prices (inflation). 2
- (ii) If football boots are considered a normal good, a rise in income should lead to an increase in demand ie demand curve shifts to the right.
More are bought at each price due to a rise in purchasing power. 2
- (e) (i) Output relative to input (usually explained with reference to labour, but can refer to any factor), eg output per worker. 1
- (ii) Increase in the quality of any factor, for example, train labour force to a higher standard, use more efficient technology, better working systems, economies of scale, specialisation, division of labour. 1
- (iii) —supply curve will shift to the right
—more can now be supplied at each price because of falling costs of production
—lower equilibrium price and higher equilibrium quantity
(any 2 points) 2
- (f) If Scotland win world cup, football in Scotland will become more popular. This would increase the demand for football boots, causing the demand curve to shift to the right.



- (g) (i) The supply curve will shift to the right as more can be produced at each price (as a result of the subsidy). (The equilibrium price will fall, and the equilibrium quantity will increase.) 1
- (ii) To advantage home producer over imports—maintain UK employment etc
Retaliation for foreign dumping
To encourage health through exercise
(Accept any answer which is reasonable) 2

Solution

PART 1

Item B

Marks

- (a) A “balanced budget” occurs when the government’s spending is equal to its revenue ie $G = T$. 2
- (b) (i) The UK budget deficit increased from 1991 to 1993 and then steadily decreased. 1
- (ii) The basic reason was the recession which caused G to increase at a faster rate than T .
 G increased rapidly because of the increase in unemployment; T increased much more slowly because of the slow down in demand, spending and income. Also credit references to deliberate government budget action to assist the recovery ie increases in G and cuts in taxation. 2
- (c) (i) Direct taxation is levied on income and wealth (and goes directly to the revenue authority—the inland revenue) eg income and corporation tax.
Indirect taxation is levied on spending (and is collected by an intermediary who then sends it to the revenue authority—customs and excise) eg VAT. 3
- (ii) The key idea is that a regressive tax is one that hits the poor harder than it hits the rich. In economic terms, the poor pay proportionately more than the rich. 2
- (d) (i) Straightforward question—no need for complex answers.
It can either cut its spending or increase the tax rate (income or VAT). 2
- (ii) Both these measures are likely to increase incomes and therefore demand. The increase in demand is likely to persuade producers to take on more workers (in order to meet it) and thus reduce unemployment. However the increased demand is also likely to increase inflation.
Mark on the overall quality of the explanation. 4
- (e) Look for **2** different reasons eg spending on NHS and education because of their importance to society (merit goods) is **one** reason.
Other examples include: welfare benefits and pensions—to guarantee the unemployed, the sick etc a basic standard of living; defence and law and order—to provide a uniform service for everyone; housing—to guarantee everyone a place to live. 4

PART 2—Essay Marking Scheme

Marks

1. (a) Resources are land, labour, capital and enterprise.
They are scarce because although they are limited in supply, the desire or wants for the goods they make are unlimited.

Reward actual examples of real resources.

5

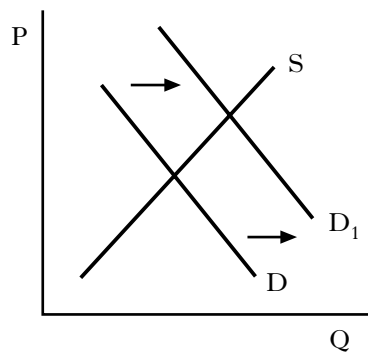
- (b) Market—any situation in which buyers and sellers are brought into contact. Not necessarily “face to face” eg telephone, internet, Stock Exchange as well as supermarkets, shops etc.

Credit candidates who mention that a market must have buyers, sellers and something to exchange.

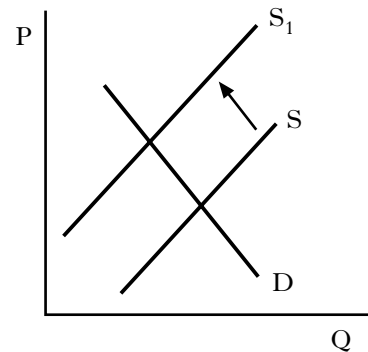
4

- (c) Explanation of either diagram would receive full marks. ie either a shortage caused by either an increase in demand or a decrease in supply.

5



OR



- (d) Examples of goods/services provided by the Government—education, health, defence, police.

Reasons for Government provision include:

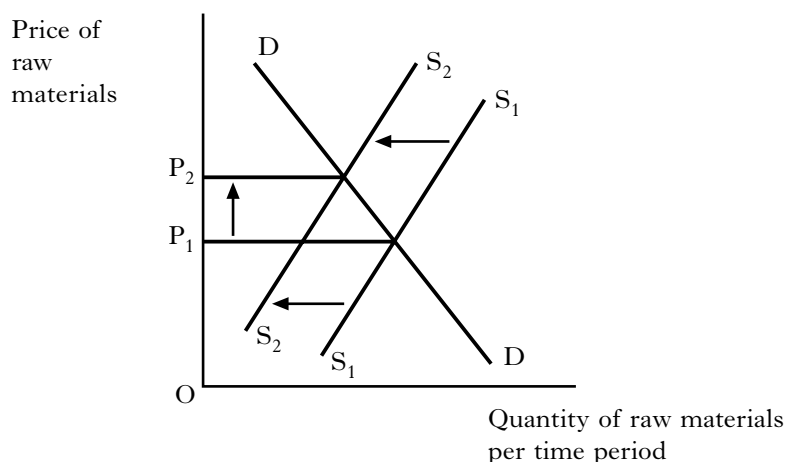
- Too important to be left to the market;
- Inability of some individuals to pay;
- Free rider (accept simple explanation of public goods);
- Lack of sufficient profit to entice private producers to supply them.

6
(20)

2. (a) A “single market” means a group of countries which act as if they were one nation as far as trading is concerned. The “single market” referred to in the question was created in January 1993 when the countries of the EU effectively became one trading market within which most of the barriers to the free movement of goods, services, people and capital, were removed. 4
- (b) This is really a question on the benefits of trade, therefore look for straightforward points such as: the increased consumer choice; access to cheaper, better quality goods (credit examples of “superior” European goods); increased competition and efficiency; reduced danger of domestic monopolies etc. Two points with explanation or four points simply stated for full marks. 4
- (c) This question concerns the reasons for trade protection which include: “infant industry” argument; protection of “essential” industries; to reduce unemployment; to improve the Balance of Trade and to prevent dumping. Credit references to the danger of retaliation. Three points with some explanation for full marks. 6
- (d) The “Euro” is the name given to the single European currency which will, eventually, become the only currency throughout (most of) the EU.
- Possible advantages of joining include: increased trade between members; no currency exchange costs; trading less risky (ER stability); lower long term inflation and interest rates; increased growth and employment.
- Possible disadvantages of joining include: loss of monetary independence; less control over fiscal policy; no control over the exchange rate; high financial costs of introducing the Euro; a common interest rate likely to be too low for the UK economy. 6
3. (a) Look for 3 factors with some development for full marks. (20)
- The factors include: lack of (overall) demand (eg during a recession), falling demand causes employers to cut output and lay off workers; changing demand patterns (eg falling demand for textiles) often caused by increased foreign competition; advances in technology (eg robot welders) can cause redundancies (at least in the short term); wage rates rising above the market clearing level (leading to workers pricing themselves out of jobs); rising costs (eg because of increased interest rates or higher exchange rates) causing a fall in competitiveness and increased redundancies. 6
- (Give some credit for references to seasonal and frictional unemployment.)
- (b) (i) Possible effects include: falling demand (because of lower incomes) and therefore reduced output and profits; increased pool of potential workers; downward pressure on wage rates. Credit any plausible answer.
- (ii) Increased spending on welfare benefits and decreased revenue from income tax and VAT. Therefore likelihood of budget deficits and increased PSBR plus possibility of tax increases. 6
- (c) Two well explained policies for full marks.
- Policies include: lower interest rates (this should increase borrowing and spending and therefore reduce unemployment); increase government spending (this should increase income and therefore demand and reduce unemployment); lower rate of income tax (this will increase disposable income and therefore increase demand and reduce unemployment); reduce VAT (this will increase real income, increase demand and reduce unemployment).
- Also credit references to supply-side policies, regional policies and government employment schemes. 8
- (20)

4. (a) A “world shortage” implies a decrease in supply. Given that world demand has not changed, the decrease in supply will result in an increase in price eg

6



- (b) (i) An increase in the price of raw materials will mean increased costs for UK manufacturers. This will force them to either increase their price or reduce their profit margins. Both actions are likely to result in reduced profits (credit references to price elasticity of demand).
- (ii) The UK Balance of Trade is likely to worsen. Dearer imported raw materials will increase our import bill (our demand for imports being price inelastic) and, if UK manufacturers increase their prices (relative to foreigners), UK export revenue will fall (demand for our exports being price elastic).
- (c) Look for two brief explanations of situations which could lead to either rising costs or excess demand in the economy. These include: increases in “other” costs eg wages, which are passed on in higher prices; decreases in taxation or increases in government spending (budget deficits) which result in increased income and therefore increased demand; cuts in interest rates which will encourage borrowing and discourage saving and therefore increase spending; a fall in the value of Sterling which will increase the price of imports.
- (d) Credit any policy likely to reduce demand or increase supply. These include: increases in taxation or reductions in government spending (budget surpluses) which reduce consumer income and therefore demand; increases in interest rates which should encourage saving and discourage borrowing and therefore reduce spending; wage restraint which should slow down cost increases; any supply-side measures.

6

4

4

(20)

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|----|-----|---|------|
| 5. | (a) | Economic growth is an increase in a country's productive capacity over time ie an increase in its ability to produce goods and services. It is usually measured by increases in GDP. | 3 |
| | (b) | Characteristics include: low productivity (because of insufficient capital, skill and education); over-population (because of high birth rates); over-dependence on agriculture (few manufacturing industries); unskilled, illiterate workforce; low life expectancy (bottom heavy population structure); heavily in debt to the first world. Any three for full marks. | 6 |
| | (c) | Problems include: lack of information (eg re population); different currencies (difficult to compare purchasing power); different income distribution; differences in hours and conditions of work; different needs (because of different climates etc). Any three for full marks. | 5 |
| | (d) | Measures include: increased spending on R and D in order to stimulate technical progress; increased spending on education and training to improve labour productivity; lower interest rates to encourage capital investment; greater specialisation and division of labour to increase efficiency; cuts in corporation tax to encourage enterprise and risk taking. | 6 |
| | | | (20) |

[END OF MARKING INSTRUCTIONS]