

# X038/12/01

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NATIONAL THURSDAY, 10 MAY  
QUALIFICATIONS 9.00 AM - 11.30 AM  
2012

ECONOMICS  
HIGHER

## INSTRUCTIONS TO CANDIDATES

Candidates must attempt **both** items in Section A and any **two** questions in Section B.



## SECTION A

### ITEM A

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

#### Commodity Price Rises in 2010

Following the devastation of the Russian crop, wheat prices rose by 50%. The cost of the wheat in a loaf of bread in the UK has risen by 7 pence. All 3 major bread producers in the UK are likely to pass this on to customers.

Analysts also reported that the prices of metals were set to change further as a result of increased demand from China. Due to production problems, the prices of copper and platinum were likely to be most affected.

In previous years guaranteed minimum prices for cotton growers in the USA have resulted in overproduction. This overproduction caused the lowering of world cotton prices.

However, in 2010 rising global demand caused West African cotton prices to increase by 80%. Clothing retailers such as Primark and Next have announced that **profit margins** will come under pressure and their prices will increase. Despite this rise, cotton prices have still declined in **real terms** since the 1950s.

- (a) Define the following terms, **as used in the passage**:
- (i) “real terms”; 2
  - (ii) “profit margins”. 2
- (b) (i) Explain **one** factor that makes the demand for bread price inelastic. 2
- (ii) Explain how the total revenue of bread producers will be affected by the increase in the price of bread. 2
- (c) Draw **one** diagram to show how both production problems and China’s economic growth could cause a change in the price of copper. 3
- (d) Explain how the price of China’s imports of raw materials would be affected if the exchange rate of China’s currency were to rise. 2
- (e) Explain **one** factor that will affect the **price elasticity of supply** of copper. 2
- (f) (i) Draw a diagram to show how guaranteed minimum prices to cotton farmers in the USA can lead to the overproduction of cotton. 2
- (ii) Suggest **2** trade barriers that can be used to reduce imports and explain how they would work. 4
- (g) Explain **2** measures that companies such as Primark and Next could take to maintain profit margins without increasing retail prices. 4
- (25)**

**[Turn over**

## ITEM B

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

### After the Budget . . . The Big Questions

Scotland's Finance Secretary has revealed his **Budget**. In this, the first year of what promises to be a decade of austerity, it signals the start of a fundamental **downsizing of the Scottish state**.

After a decade in which public sector spending rose by an average of 5% per year the Scottish Budget for 2011/12 will now crunch into reverse, with spending falling by 3.9% overall. Around £1.3 billion will be cut in a single year with more to follow.

It means a pay freeze for a quarter of a million public sector workers and the loss of thousands of jobs. This measure will also help the UK Government meet its inflation target. There will be £200 million less for Higher and Further Education and 3% efficiency savings across nearly every department.

The Finance Minister has stated that the effect of budget cuts on employment can be reduced if agreement is reached on flexible working practices, eg part-time working and flexible shift patterns which will reduce costs.

The UK Chancellor has stated that he will take measures to support and encourage small and medium sized businesses. He believes this support is vital to the future health of the Scottish Economy as well as stressing the importance of Scotland continuing to attract foreign firms.

Adapted from an article in the *Sunday Herald*, 21 November 2010

- (a) Explain the following terms, **as used in the passage**:
- (i) “Budget”; 2
  - (ii) “downsizing of the Scottish state”. 2
- (b) Explain how flexible working practices can reduce the effects of budget cuts on employment. 2
- (c) Describe how the UK Government measures the rate of inflation. 3
- (d) Explain what impact the cuts in Higher and Further Education may have on the Scottish Economy in the future. 4
- (e) Explain measures the Chancellor of the UK could take to “support and encourage small and medium sized businesses”. 3
- (f) Explain how cutting the budget deficit might conflict with 2 other government economic objectives. 4
- (g) (i) Suggest 3 reasons why foreign firms might decide to locate in Scotland. 3
- (ii) Explain **one** possible disadvantage of this foreign investment to the Scottish Economy. 2
- (25)**

**[Turn over for Section B on *Pages six and seven***

## SECTION B

Attempt any TWO questions.

1. Economics has been described as the study of choice.
  - (a) Explain why the basic economic problem means that choices will always have to be made by individuals, firms and the government. 7
  - (b) Explain, using production possibility diagrams:
    - (i) productive efficiency;
    - (ii) opportunity cost. 8
  - (c) Explain how fiscal policies and the multiplier effect can be used to increase national income. 10

**(25)**
  
2. Following a recession, the UK economy experienced a period of low interest rates in 2010.
  - (a)
    - (i) Explain what is meant by a “recession”. 2
    - (ii) Describe the possible consequences of a recession for individuals, firms and government. 10
  - (b) Explain how monetary policies can assist an economy in returning to economic growth. 8
  - (c) Describe the possible impact on the UK economy of economic recovery in other EU member states. 5

**(25)**
  
3.
  - (a) Explain, using a diagram, what happens to a firm’s average total costs in the short run. 7
  - (b) Explain, using examples, what is meant by **internal** and **external** economies of scale. 10
  - (c)
    - (i) Apart from an increase in the costs of production, explain **2** other factors which can cause an increase in the rate of inflation. 4
    - (ii) Describe how a rise in the UK rate of inflation is likely to affect the Current Account of its Balance of Payments. 4

**(25)**

	<i>Marks</i>
4. (a) (i) Explain the shape of a normal demand curve.	6
(ii) Explain <b>2</b> reasons why some demand curves are abnormal.	4
(b) Describe the factors which may cause the exchange rate of sterling to fall.	8
(c) Describe the likely effects on the UK economy of a fall in the exchange rate of sterling.	7
	<b>(25)</b>
5. (a) Describe the theories of Absolute and Comparative Advantage.	8
(b) Explain the main <b>economic</b> advantages and disadvantages to the UK of membership of the European Union.	12
(c) Describe some of the uses of National Income statistics.	5
	<b>(25)</b>
6. Markets do not always allocate resources in a way that leads to the best possible outcomes. The term “market failure” has been used to describe this.	
(a) Describe <b>4</b> examples of “market failure”.	8
(b) Explain how the government intervenes to correct market failure.	6
(c) Describe the characteristics of an oligopolistic market.	5
(d) Discuss the effects on individuals of a reduction in direct taxation and an increase in indirect taxation.	6
	<b>(25)</b>

*[END OF QUESTION PAPER]*

## ACKNOWLEDGEMENT

Section A, Item A—Article is adapted from “After the budget . . . the big questions” taken from the *Sunday Herald*, 21 November 2010. Reproduced by kind permission of the Herald and Times.