

AS ECONOMICS

Paper 2 The National Economy in a Global Context

Insert

DO NOT WRITE ANY ANSWERS IN THIS INSERT. YOU MUST ANSWER THE QUESTIONS IN THE ANSWER BOOKLET PROVIDED.

CONTEXT 1: INFLATION

Questions 21 to 26

- **Extract A:** UK inflation rate (%), measured by CPI, January 2018 to December 2020
- **Extract B:** Achieving the inflation target of 2%
- **Extract C:** Are very low interest rates good for the economy?

CONTEXT 2: INTERNATIONAL TRADE

Questions 27 to 32

- **Extract D:** UK monthly balance of trade in goods and services (£million), November 2017 to October 2020
- **Extract E:** The trade balance: an overlooked objective of government macroeconomic policy?
- **Extract F:** Should the trade balance receive more attention?

Context 1

Total for this context: 50 marks

INFLATION

Extract A: UK inflation rate (%), measured by CPI, January 2018 to December 2020



Source: ons.gov.uk, February 2021

Extract B: Achieving the inflation target of 2%

For over 40 years, the control of inflation has been one of the main objectives of government macroeconomic policy. It is widely believed that price stability helps to create the conditions for all the other objectives to be achieved. Stable prices mean firms and individuals have more confidence. Consequently, there is likely to be more investment and consumption, more jobs are created, and everyone benefits as the economy grows. On the other hand, high inflation can be disruptive. Firms may postpone expansion plans, workers may ask for large wage increases, and already-high inflation can quickly get out of control. With this in mind, the government sets the target rate of inflation that the Bank of England's Monetary Policy Committee (MPC) has to achieve. The MPC uses monetary policy to control inflation. Given that the price level is affected by demand-side and supply-side factors, both domestically and from all over the world, this is not an easy task.

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In 2020, the pandemic caused long periods of reduced economic activity. As expected, unemployment increased and inflation fell. Oil prices tumbled in response to falling global demand and this helped to reduce firms' costs of production. In the UK, government policy, such as the temporary reduction in VAT, an indirect tax, from 20% to 5%, also helped to reduce inflation.

15

Source: News reports, December 2020

Extract C: Are very low interest rates good for the economy?

The 2% inflation target is not only designed to protect the economy from the harmful effects of high inflation but also to prevent the economy from experiencing a period of deflation. As 2020 drew to a close, there was evidence of some inflationary pressures. It was reported that the average UK house price had risen by 7.6% in the year to November 2020. The completion of a UK–EU trade deal provided a confidence boost, and the FTSE 100 Index of leading shares reached its highest value since March 2020. However, deflationary factors were also in evidence. The UK pound sterling appreciated to its highest level against the US dollar since April 2018. Overall, output was not expected to recover to its previous peak until 2022.

5

The MPC has continued to implement very loose monetary policy to support the economy. Bank Rate remained at an all-time low of 0.1%, and there were further injections of money via the quantitative easing scheme. This should encourage consumption and much needed investment. In addition, the cost of government borrowing remained low, crucial at a time when the budget deficit and national debt were increasing considerably.

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However, there are disadvantages of low interest rates. They have the potential to create inflationary pressure. Pensioners and others who rely on their savings to provide a source of income may lose out. Low interest rates encourage more consumer debt which might lead to instability in the future. Tempted by cheaper borrowing, some firms might make poor investment decisions, leading to a misallocation of resources. It remains to be seen whether very low interest rates are good for the economy.

15

Source: News reports, December 2020

Turn over for Context 1 questions**Turn over ►**

Context 1: – Questions 21 to 26

- | | |
|---|---|
| 2 | 1 |
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 Define 'deflation' **Extract C** (line 2). **[3 marks]**
- | | |
|---|---|
| 2 | 2 |
|---|---|

 The original price of an overnight stay in a hotel room is £180 including VAT. Calculate the new price of an overnight stay, following the reduction in VAT referred to in **Extract B** (line 15). **[4 marks]**
- | | |
|---|---|
| 2 | 3 |
|---|---|

 Use **Extract A** to identify **two** significant features of the inflation rate over the period shown. **[4 marks]**
- | | |
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Extract B (lines 14–15) states: 'In the UK, government policy, such as the temporary reduction in VAT, an indirect tax, from 20% to 5%, also helped to reduce inflation.'
- Draw an AD/AS diagram to show the impact of a reduction in indirect taxation on real national income and the price level in an economy. **[4 marks]**
- | | |
|---|---|
| 2 | 5 |
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Extract B (lines 7–9) states: 'With this in mind, the government sets the target rate of inflation that the Bank of England's Monetary Policy Committee (MPC) has to achieve.'
- Explain **two** factors considered by the Bank of England's MPC when setting Bank Rate. **[10 marks]**
- | | |
|---|---|
| 2 | 6 |
|---|---|

Extract C (lines 18–19) states: 'It remains to be seen whether very low interest rates are good for the economy.'
- Use the extracts and your knowledge of economics to assess the view that very low interest rates are good for the UK economy. **[25 marks]**

There are no extracts printed on this page

Turn over for Context 2

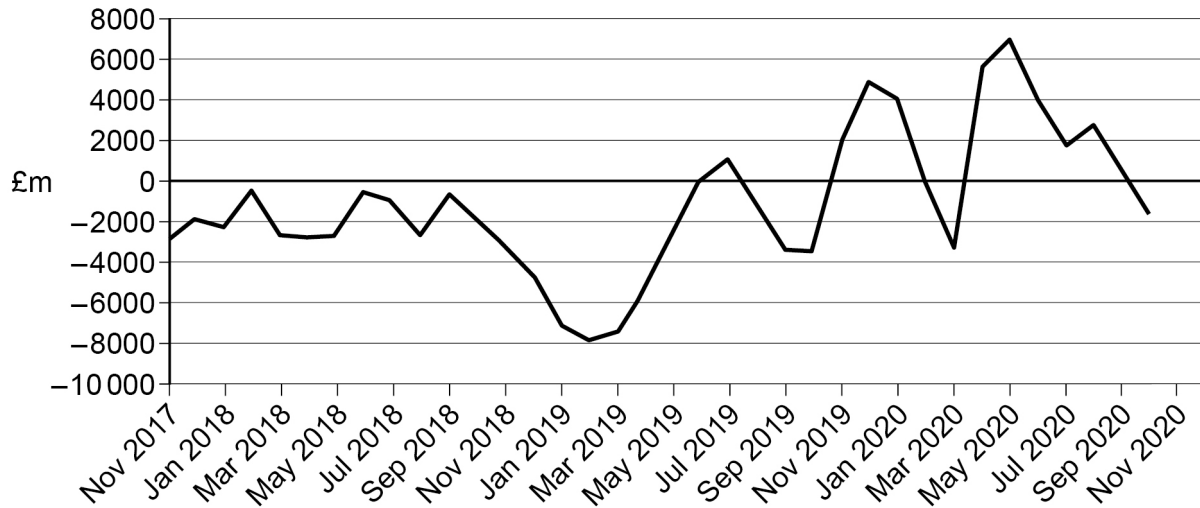
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Context 2

Total for this context: 50 marks

INTERNATIONAL TRADE

Extract D: UK monthly balance of trade in goods and services (£million), November 2017 to October 2020



Source: ons.gov.uk, February 2021

Extract E: The trade balance: an overlooked objective of government macroeconomic policy?

The importance that governments attach to the various objectives of macroeconomic policy varies over time. However, the achievement of a satisfactory balance of trade in goods and services is often the one that receives the least attention. Governments and media headlines tend to focus on unemployment, inflation and economic growth. Recent favourable trade balances, such as the £8.2 billion surplus achieved in the 12 months to October 2020, have largely been overlooked.

5

But why? An improving trade balance could signal good news for an economy. An increase in exports should help to reduce unemployment. There is likely to be a positive multiplier effect and economic growth should increase. An increase in output will reduce spare capacity, firms feel more confident, and the accelerator theory suggests that investment should rise.

10

However, this is not always the case. Changes in the trade balance are often linked to changes in the economic cycle. For example, in the year to July 2020 the balance of trade in goods deficit improved. This was not because the value of exports increased, but because the value of exports fell by a smaller amount than the fall in the value of imports. The value of exports fell by £31.6 billion to £321.6 billion. The larger decrease in the value of imports was mainly due to falling demand for machinery, transport equipment and fuels due to the inactivity caused by the pandemic. As the economic recovery gets underway, the balance of trade in goods might deteriorate again.

15

Source: News reports, December 2020

Extract F: Should the trade balance receive more attention?

Many economists believe that the trade balance reflects the strength or weakness of a country's international competitiveness in terms of the price and quality of the goods and services exported. International trade is also affected by fluctuations in the exchange rate, the rate of inflation and the level of economic activity in other economies. Some of these factors can be beyond the government's control.

5

However, there is a great deal that can be done to improve the balance of trade in goods and services. Government supply-side policy can have a direct influence, via changes to corporation tax and industrial policy, to provide incentives for exporting firms to increase investment. Increased and better-targeted spending on education and training should help to improve human capital. Highly skilled workers are capable of producing cutting-edge, high-quality goods and services which are sought after in the global marketplace. Firms themselves have a role to play, by being dynamic, innovative and constantly seeking productivity improvements. If the inflation rate remains low, and appropriate policies are adopted, the UK economy should reap the benefits from an improvement in its balance of trade in goods and services.

10

15

Source: News reports, December 2020

Turn over for Context 2 questions**Turn over ►**

Context 2: – Questions 27 to 32

- 2 7** Define 'economic recovery' **Extract E** (line 17). **[3 marks]**
- 2 8** In the year to July 2020, the deficit in the balance of trade in goods was £105 billion. Calculate the value of imports of goods for the year to July 2020, using the information in **Extract E** (lines 12–15) to help you. **[4 marks]**
- 2 9** Use **Extract D** to identify **two** significant features of the balance of trade in goods and services over the period shown. **[4 marks]**
- 3 0** **Extract E** (lines 4–6) states: 'Recent favourable trade balances, such as the £8.2 billion surplus achieved in the 12 months to October 2020, have largely been overlooked.'
- Draw an AD/AS diagram to show the effect of an improvement in the balance of trade in goods and services on real national income and the price level in an economy. **[4 marks]**
- 3 1** **Extract F** (lines 1–2) states: 'Many economists believe that the trade balance reflects the strength or weakness of a country's international competitiveness'.
- Explain how a fall in a country's international competitiveness may affect economic growth in the economy. **[10 marks]**
- 3 2** **Extract F** (lines 6–7) states: 'However, there is a great deal that can be done to improve the balance of trade in goods and services.'
- Use the extracts and your knowledge of economics to evaluate policies that may be used to achieve a sustained improvement in the UK's balance of trade in goods and services. **[25 marks]**

END OF QUESTIONS

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Please write clearly in block capitals.

Centre number

Candidate number

Surname _____

Forename(s) _____

Candidate signature _____

I declare this is my own work.

AS ECONOMICS

Paper 2 The National Economy in a Global Context

Monday 22 May 2023

Morning

Time allowed: 1 hour 30 minutes

Materials

For this paper you must have:

- the Insert
- a calculator.

Instructions

- Use black ink or black ball-point pen. Pencil should only be used for drawing.
- Fill in the boxes at the top of this page.
- Answer **all** questions in **Section A**.
- Answer **either** Context 1 **or** Context 2 in **Section B**.
- You will need to refer to the Insert provided to answer **Section B**.
- You must answer the questions in the spaces provided. Do not write outside the box around each page or on blank pages.
- If you need extra space for your answer(s), use the lined pages at the end of this book. Write the question number against your answer(s).
- Do all rough work in this book. Cross through any work you do not want to be marked.

Information

- The maximum mark for this paper is 70.
- The marks for questions are shown in brackets.
- No deductions will be made for wrong answers.

For Examiner's Use	
Section	Mark
A	
B	
TOTAL	



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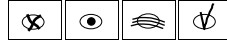
Section AAnswer **all** questions in this section.Only **one** answer per question is allowed.

For each question completely fill in the circle alongside the appropriate answer.

CORRECT METHOD



WRONG METHODS



If you want to change your answer you must cross out your original answer as shown.



If you wish to return to an answer previously crossed out, ring the answer you now wish to select as shown.

**0 1**

Which one of the following is an injection into the circular flow of income?

[1 mark]**A** Consumer expenditure**B** Exports**C** Imports**D** Wages**0 2**

In which one of the following situations is an increase in aggregate demand most likely to result in higher inflation?

[1 mark]**A** Household savings are increasing**B** Mortgage interest rates are high**C** Resources are fully employed**D** Unemployment is rising

0 3**Table 1** shows the Consumer Price Index (CPI) for an economy over a period of time.**Table 1**

Year	CPI
2008	110
2011	108
2014	116
2017	124
2020	130

Which one of the following can be concluded from **Table 1**?**[1 mark]**

- A** The price of a representative basket of goods rose throughout the period.
- B** The rate of inflation from 2011 to 2014 was the same as from 2014 to 2017.
- C** The standard of living reached its highest level in 2020.
- D** The value of money rose between 2008 and 2011.

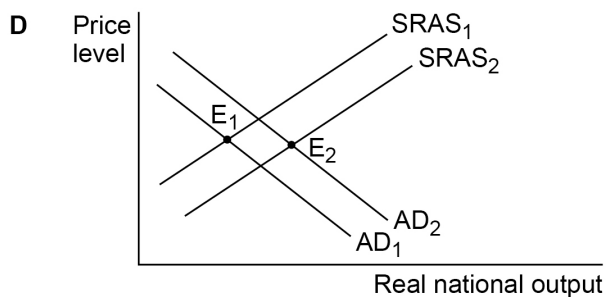
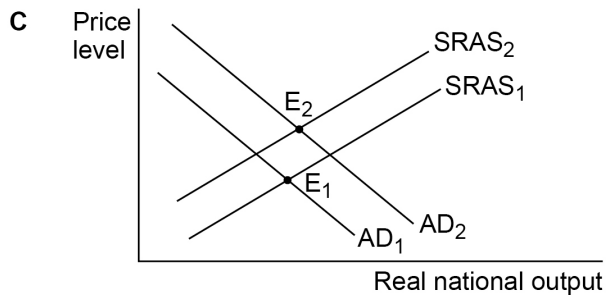
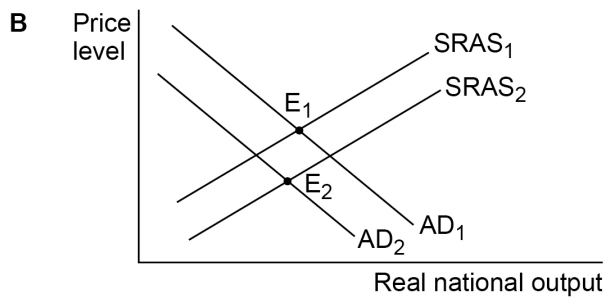
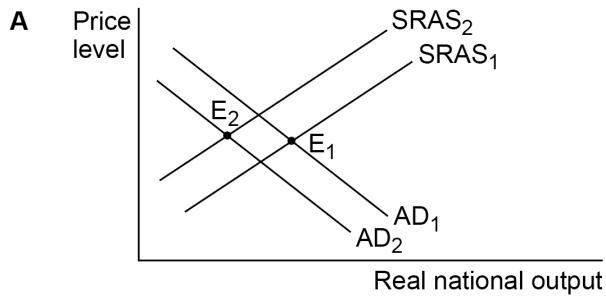
Turn over for the next question**Turn over ►**

0 4

A government decides to increase the minimum wage at a time when the rest of the world is coming out of recession. These events cause short-run aggregate supply (**SRAS**) to shift from **SRAS₁** to **SRAS₂** and aggregate demand (**AD**) to shift from **AD₁** to **AD₂**.

If the initial macroeconomic equilibrium is **E₁**, which one of the following diagrams shows the correct new equilibrium **E₂**?

[1 mark]



0 5

Which one of the following is a direct tax?

[1 mark]

- A Corporation tax
- B Fuel tax
- C Import tax
- D Vehicle tax

0 6

Table 2 shows the components of a country's national income in 2021.

Table 2

	£bn
Consumer expenditure	22
Investment	10
Government expenditure	8
Exports	11
Imports	9

It can be concluded from the data in **Table 2** that aggregate supply in 2021 must have been

[1 mark]

- A £21bn.
- B £40bn.
- C £42bn.
- D £60bn.

Turn over ►



0 7

Which one of the following is most likely to be used to identify a phase of the economic cycle?

[1 mark]

A Firms' capacity utilisation

B Structural unemployment

C The economy's productive potential

D The exchange rate

0 8

An economy has a low rate of economic growth and high unemployment.

Which one of the following sets of policies would be most likely to increase growth and reduce unemployment whilst avoiding a rise in inflation?

[1 mark]

A A cut in income tax and lower interest rates

B Higher interest rates and an appreciation in the exchange rate

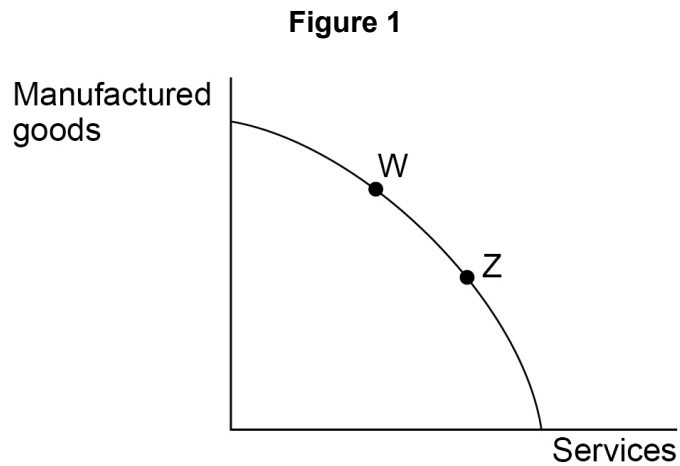
C Higher welfare benefits and an increase in the money supply

D Increased expenditure on training and an investment subsidy



0 9

Figure 1 shows the production possibility curve for an economy producing services and manufactured goods.



The economy moves from point **W** to point **Z**. It can be concluded that

[1 mark]

- A** imports of manufactured goods have risen.
- B** the international competitiveness of services has increased.
- C** the pattern of economic activity has changed.
- D** unemployment in manufacturing has increased.

Turn over for the next question

Turn over ►



1 0

Table 3 shows the planned change in government spending, the size of the output gap and the size of the multiplier in four economies, W, X, Y and Z.

Table 3

	Change in government spending (£bn)	Output gap (£bn)	Multiplier
W	-80	+100	1.25
X	-150	-225	1.5
Y	+200	+350	1.75
Z	-300	+150	2

All other things being equal, in which one of the economies, W, X, Y or Z, will the planned change in government spending eliminate the economy's output gap?

[1 mark]

- A** W
- B** X
- C** Y
- D** Z

1 1

A government wishing to reduce inflation through the use of fiscal policy could

[1 mark]

- A** cut government borrowing.
- B** decrease income tax.
- C** raise interest rates.
- D** reduce the budget surplus.



1 2

Table 4 shows the percentage change in real GDP in an economy in the four years 2016 to 2019.

Table 4

Year	Change in real GDP (%)
2016	4.2
2017	3.1
2018	2.6
2019	1.1

Over the period 2016 to 2019, which one of the following can be concluded from **Table 4**?
[1 mark]

- A** Aggregate demand decreased
- B** Real national income increased
- C** Structural unemployment increased
- D** The inflation rate decreased

1 3

The national debt is the sum of all past and current borrowing, less repayments, undertaken by

[1 mark]

- A** firms and government.
- B** firms, government and households.
- C** government.
- D** households and firms.

Turn over ►



1 4

Which one of the following is most likely to be an instrument of industrial policy?

[1 mark]

- A** An increase in manufacturing productivity
- B** Government grants for firms with growth potential
- C** Higher investment by firms in research and development
- D** Investment by firms in artificial intelligence

1 5

An economy experiences a low trend rate of economic growth, no output gap and a fall in total hours worked. In these circumstances, which one of the following combinations of events is most likely to occur?

[1 mark]

	National output	Cyclical unemployment	Labour productivity	
A	Falling	Absent	Increasing	<input type="radio"/>
B	Falling	Present	Decreasing	<input type="radio"/>
C	Rising	Absent	Increasing	<input type="radio"/>
D	Rising	Present	Decreasing	<input type="radio"/>

1 6

The UK economy experiences a change in its foreign exchange rate from £1 = \$1.60 to £1 = \$1.75.

Which one of the following is the most likely effect on the UK economy?

[1 mark]

- A** A decrease in employment
- B** A fall in the budget deficit
- C** A reduction in productivity
- D** Higher raw material prices



1 7

An economy is experiencing deflation and high employment.

The most likely cause of this situation is a

[1 mark]

A deficit on the balance of payments.

B government budget surplus.

C negative demand-side shock.

D positive supply-side shock.

1 8

Which one of the following is an example of a contractionary fiscal policy designed to reduce inflation while, at the same time, minimising the negative impact on the economy's potential for long-run economic growth?

[1 mark]

A A decrease in the budget deficit and replacement of a sugar tax with a tax on savings

B An increase in interest rates and replacement of food subsidies with subsidies for innovation

C An increase in the budget surplus and a switch from spending on pensions to spending on new airports

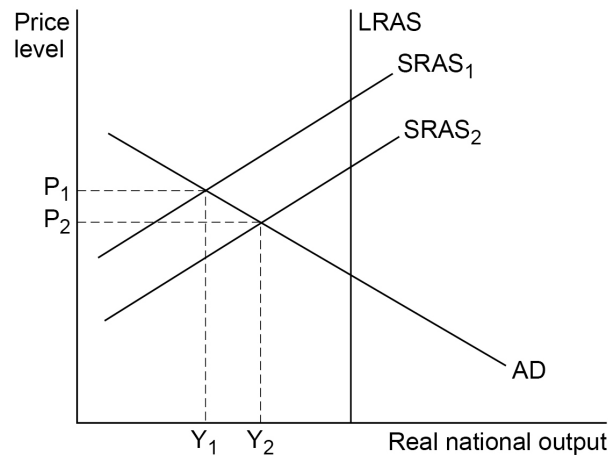
D Restrictions on bank lending and a switch from spending on arts degrees to spending on apprenticeships

Turn over for the next question

Turn over ►

1 9

Figure 2 shows the aggregate demand curve (**AD**), short-run aggregate supply curves (**SRAS**) and long-run aggregate supply curve (**LRAS**) for an economy.

Figure 2

The short-run aggregate supply curve shifts from **SRAS₁** to **SRAS₂**. Which one of the following is the most likely cause of the resulting increase in real national output?

[1 mark]

- A** An increase in bank lending to households
- B** An increase in government expenditure
- C** Productivity rising faster than money wages
- D** The action of the multiplier

2 0

Which one of the following is most likely to result in an increase in exports from the UK economy? An increase in

[1 mark]

- A** inflation in other countries.
- B** productivity in other countries.
- C** UK incomes.
- D** UK interest rates.

20

END OF SECTION A

Section B

Look at the Insert and choose to answer **EITHER** Context 1 **OR** Context 2.

Answer **EITHER** Questions 21 to 26 in the spaces below

OR

Questions 27 to 32 on pages 24 to 32 of this answer booklet.

There is a total of 50 marks for either context.

Shade the circle below to indicate which context you have answered.

Context 0 1

Context 0 2

CORRECT METHOD



WRONG METHODS



EITHER

Context 1

Total for this context: 50 marks

INFLATION

Use the Insert provided to study **Questions 21 to 26** and **Extracts A, B and C**, and then answer the questions in the spaces which follow.

2 1 Define 'deflation' **Extract C** (line 2).

[3 marks]

Turn over ►



2	2
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The original price of an overnight stay in a hotel room is £180 including VAT. Calculate the new price of an overnight stay, following the reduction in VAT referred to in **Extract B** (line 15).

[4 marks]



2 3

Use **Extract A** to identify **two** significant features of the inflation rate over the period shown.

[4 marks]

Feature 1 _____

Extra space _____

Extra space _____

Turn over for the next question

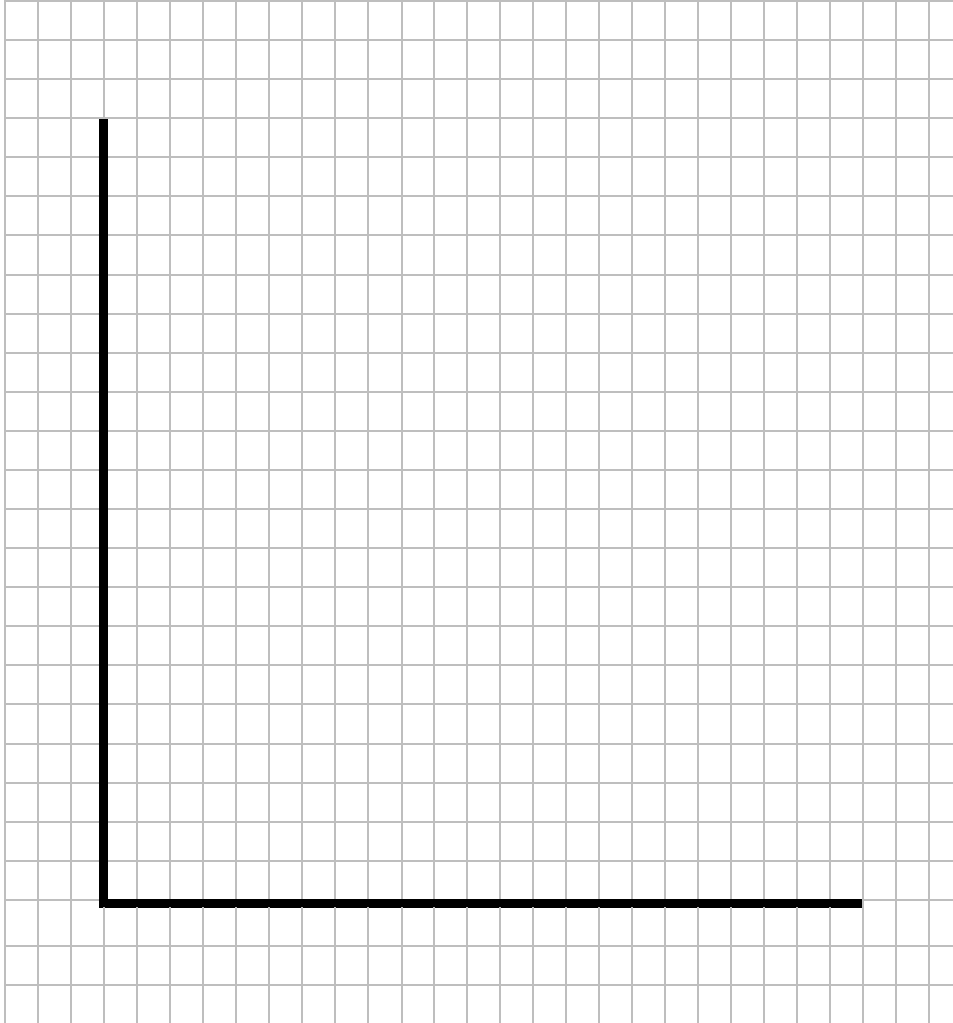
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2 4

Extract B (lines 14–15) states: ‘In the UK, government policy, such as the temporary reduction in VAT, an indirect tax, from 20% to 5%, also helped to reduce inflation.’

Draw an AD/AS diagram to show the impact of a reduction in indirect taxation on real national income and the price level in an economy.

[4 marks]

2 6

Extract C (lines 18–19) states: ‘It remains to be seen whether very low interest rates are good for the economy.’

Use the extracts and your knowledge of economics to assess the view that very low interest rates are good for the UK economy.

[25 marks]

Turn over ►



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outside the
box*

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Do **NOT** answer Context 2 if you have answered Context 1.

OR

Context 2

Total for this context: 50 marks

INTERNATIONAL TRADE

Use the Insert provided to study **Questions 27 to 32** and **Extracts D, E and F**, and then answer the questions in the spaces which follow.

2 7 Define 'economic recovery' **Extract E** (line 17).

[3 marks]

2 8 In the year to July 2020, the deficit in the balance of trade in goods was £105 billion. Calculate the value of imports of goods for the year to July 2020, using the information in **Extract E** (lines 12–15) to help you.

[4 marks]



2 9

Use **Extract D** to identify **two** significant features of the balance of trade in goods and services over the period shown.

[4 marks]

Feature 1 _____

Extra space _____

Feature 2 _____

Extra space _____

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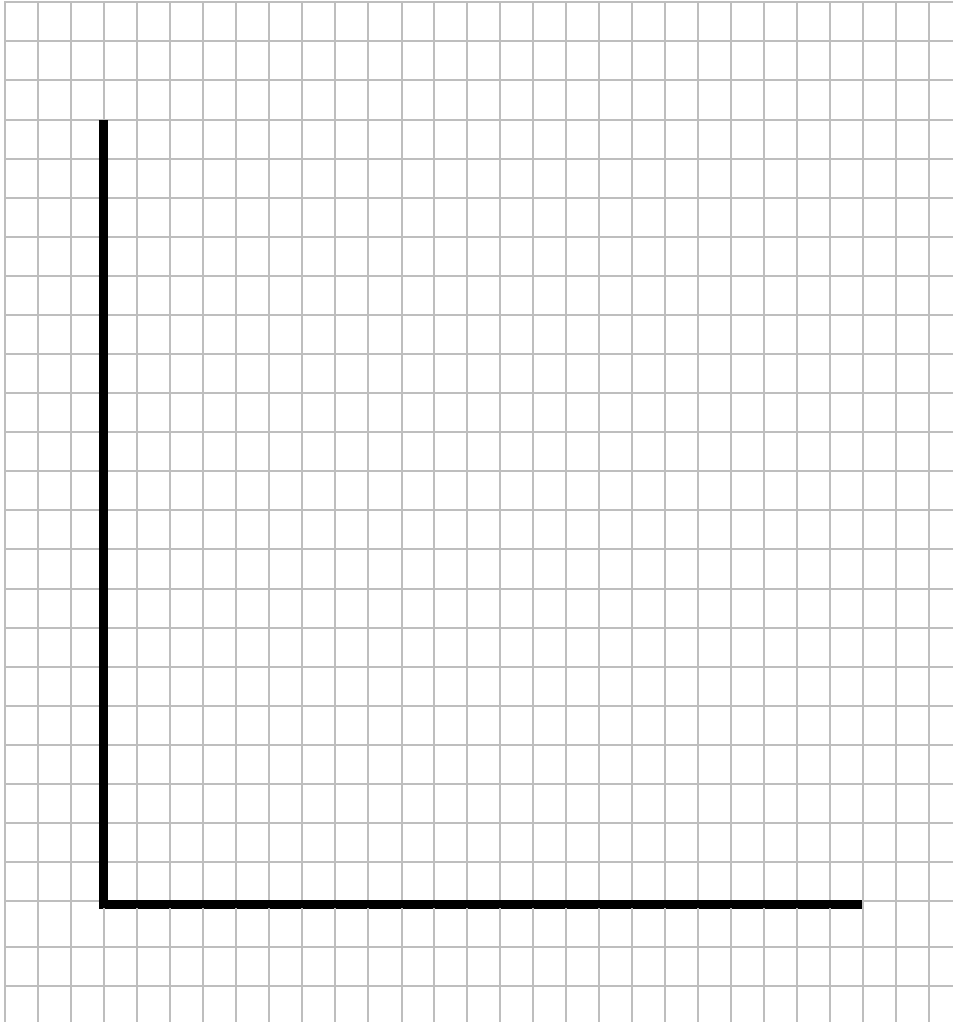
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3 0

Extract E (lines 4–6) states: ‘Recent favourable trade balances, such as the £8.2 billion surplus achieved in the 12 months to October 2020, have largely been overlooked.’

Draw an AD/AS diagram to show the effect of an improvement in the balance of trade in goods and services on real national income and the price level in an economy.

[4 marks]

3 **1**

Extract F (lines 1–2) states: ‘Many economists believe that the trade balance reflects the strength or weakness of a country’s international competitiveness’.

Explain how a fall in a country’s international competitiveness may affect economic growth in the economy.

[10 marks]

Turn over ▶

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ANSWER IN THE SPACES PROVIDED**



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Question number	Additional page, if required. Write the question numbers in the left-hand margin.
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