

## 2017 Edexcel Economics Paper 3 Synoptic Paper

### Model Answers

This document is helpful for longer essay questions/responses. Please reference the Mark Scheme for answers to Multiple Choice questions.

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# Examiners' Report

## June 2017

GCE Economics A 9EC0 03

Candidates performed well with this question, with a mean mark of over 3 out of 5. Most candidates could interpret the data easily, recognise a depreciation, and give good responses in a wide array of arguments. Many used a diagram to show a shift in supply or demand for the peso and consequently a fall in the value of the peso, and although a diagram was not necessary it did help candidates to think carefully about whether demand or supply was increasing or decreasing.

Many answers were centred around the fall in copper prices as illustrated in Figure 1, and the fact that Figure 2 was vertically aligned did make it very clear that there was a strong positive correlation between copper prices and the value of the peso. This was strongly backed up by the text ('weak currency' Extract A line 10, 'copper accounts for 50% of its exports' line 2).

A surprising number of candidates referred to a *devaluation* rather than depreciation, despite mentions of the 'free trade model, which is unrestricted by government interventionism' (lines 17-18) and the independent central bank (line 22). A tiny minority thought that the value of the peso was rising, but this was rare. This is a sign that most other candidates were largely well rehearsed in using exchange rate data such as this.

The most significant difference between high and very high mark answers was the ability to make a chain of reasoning or 'analysis' between the factor that changed, for example copper prices, and the demand or supply for the currency. There were many candidates that could observe copper prices had fallen but then did not make the link that the revenue of exports would therefore fall, for example by showing that the demand for exports does not increase in proportion to the price fall. Many candidates mis-stated that the demand for exports had fallen, when in fact it was the increase in demand that was slowing (in China) or worldwide oversupply, but not a fall in demand. This counter-observation was a common weakness in responses, and illustrates the importance of using the data very closely.

This is typical of a 4 out of 5 mark answer.

(a) With reference to Figure 2, explain **one** likely reason for the change in the Chile peso exchange rate between 2013 and 2015.

(5)

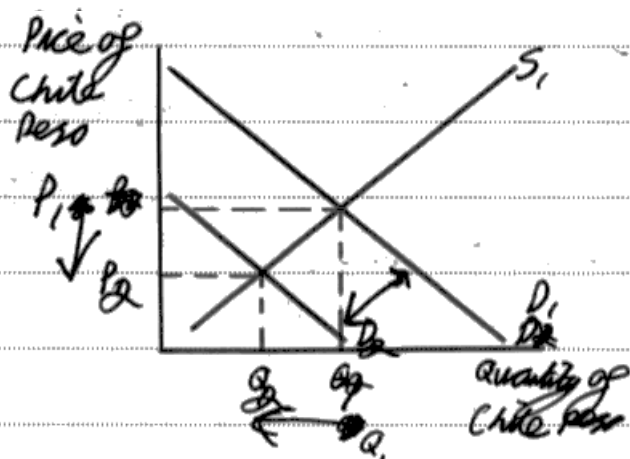
Depreciation is where the value of one currency falls against another. As shown in figure two the cost of Chile peso fell from around 0.215 to around 0.15 US dollars. This could be due to a lack of demand for exports from Chile. If there were less exports demanded, there is less demand for the currency, peso, meaning it would lose value.

## Question 1 (a)

- (a) With reference to Figure 2, explain **one** likely reason for the change in the Chile peso exchange rate between 2013 and 2015.

(5)

Between 2013 and 2015, the Chile peso exchange rate fell from approximately \$0.32 USD per 100 to approximately \$0.15 USD per 100. One reason for this fall in value may have been reduced interest rates in Chile. This would have the effect of discouraging foreign investors from undertaking foreign portfolio investment by saving in Chilean banks. As demand for Chilean pesos falls, demand for the Chilean peso falls and its price falls.



The diagram above shows how demand for Chile peso fell from  $D_1$  to  $D_2$  and consequently the price of the peso fell from  $P_1$  to  $P_2$ .



## ResultsPlus

### Examiner Comments

K Reduced interest rates  
K Less saving by foreigners  
AP ER dropped  
AP Data reference  
AN Diagram

**5/5**



## ResultsPlus

### Examiner Tip

Using a diagram can save a good deal of writing, if relevant.

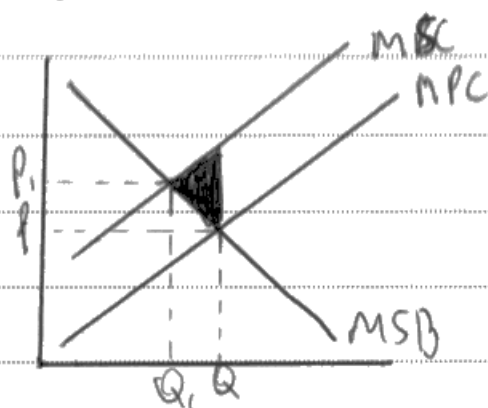
## Question 1 (b)

Brief answers can be effective.

(b) Examine the likely impact of externalities of copper mining on firms and communities within Chile.

(8)

Externalities are third party effects away from the market transaction.



As a negative externality, copper mining produces a large amount of negative externalities due to its use of natural resources and the pollution it causes.

The pollution can affect the health of local communities and as a result it can make workers sick, causing local firms to not have a full workforce. This reduces their ability to work at full capacity which can hinder ~~quantity~~ supply meeting quantity demanded.

However, copper mining provides jobs to local communities which increases the disposable income and thus the standard of living. Which in turn should keep the workforce in the community healthy so they can afford necessities.



## ResultsPlus

### Examiner Comments

K Define  
K Firms + Communities combined  
AN Development  
AN Development  
AP Diagram  
AP Diagram  
EV XB  
EV XB

**6/6 + 2/2 (8): full marks**



## ResultsPlus

### Examiner Comments

Diagrams are effective when asked for *impact*.



### Question 1 (c)

Many candidates recognised this as a question on primary product dependency and were able to explain the potential problems of this for Chile. Some used theories and extended analysis to support their explanation.

The question discriminated effectively, for many answers did not discuss copper *dependency*, but gave a more microeconomic answer focused on the issues of low prices for copper mining firms rather than the problems for Chile as a whole as a result of dependency.

The better candidates employed relative PED and PES well for analysing volatile prices and were able to use these concepts in their evaluation in addition to the analysis.

Higher-level responses included data to provide support for their argument. However, many responses failed to explain the volatility of hard commodity prices and some candidates were insufficiently focused on the context, employing unsuitable examples such as wheat or other soft commodities. The Prebisch Singer theory was also used to success for the better responses but it was rare to see it fully explained in terms of low YED for exports of primary products and high YED for imports. Answers, which did use this effectively, picked up evaluation marks by observing that copper has high YED. Other models were used including Lewis and Harrod-Domar, but these again were not always effectively employed or with the accuracy expected at this level.

The best answers focused directly on dependency and used economic theory, such as inelastic PED/PED, Prebisch-Singer and Dutch disease. Many candidates used the wine and salmon industries as counter-arguments to show that Chile is not over-dependent, while others discussed the benefits the Chilean government has reaped from high levels of tax income from copper mining, the low levels of debt and the sound financial sector.

Use of textbook theory and clear chains of reasoning are rewarded generously.

(c) Apart from externalities, discuss the problems that Chile faces as a result of dependency on copper mining.

(12)

Dependency on a product means that you rely on it to keep your economy going. Chile's dependency on copper mining has caused them many problems.

One of these is the price volatility that rely on such a primary commodity brings. As figure 1 shows copper prices have varied hugely between 2007 and 2015 with a low of around 1000 in 2008 to a high of around 9,000 in 2010. This volatility makes it hard for firms as they can't be sure of the price they get for



their products on a month to month basis. This leaves firms insecure and often reluctant to invest as they are unsure if ~~after~~ prices will fall making their investment not worthwhile. This therefore means firms are unlikely to be dynamically efficient.

However the effects of this problem may not be as large as more recently in the years 2012 to 2014 the price changes seem to be much less volatile than they were in previous years such as 2007 to 2011.

Another problem Chile faces is declining terms of trade due to their dependency on copper. This is because of the Prebisch Singer hypothesis that states primary products will increase in price less than other products over time due to having a ~~less~~ more inelastic income elasticity of demand figure. This is because when one's income rises we are more likely to buy finished products more rather than primary products. As a result of declining terms of trade people in Chile will be able to import ~~less than they could before~~ comparatively less than they could before meaning their standard of living is likely to decrease as they can't access as many goods and services as they previously did.

However this may be less of a problem for Chile compared to other countries as extract A says they do also have "strengths in tourism and high tech products". These goods are

likely to have much more elastic income elasticities of demand and therefore the terms of trade may not worsen as much as anticipated.



**ResultsPlus**

**Examiner Comments**

**KAA L3 (8):**

L3, L3+ (Prebisch-Singer)

EV L2 (4)

sustained L2 L2

**12/12**



**ResultsPlus**

**Examiner Tip**

For a 12 mark question there are only 2 levels of evaluation, two brief points or one well made point can reach the top of Level 2 evaluation.

## Question 1 (d)

This answer is not always Level 4, and at times the judgement is thin, however there was enough there for sustained L4 and L3. The answer uses the data effectively throughout, which makes it stand out as a strong answer.

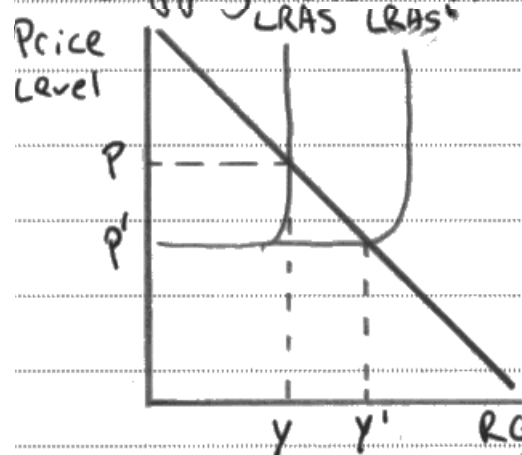
Policies growth + development

Indicate which question you are answering by marking a cross ☒. If you change your mind, put a line through the box ☒ and then indicate your new question with a cross ☒.

Chosen question number: Question 1(d) ☒ Question 1(e) ☒

Write your answer here:

One policy that could be used by the Chilean government to increase growth and development could be investment into education and training. Initially, this government spending, should as a component of AD increase AD and result in higher GDP to some extent (ceteris paribus). Spending into education and training, a Supply Side fiscal policy should result in increased aggregate supply due to staff with greater skills and qualifications.



These staff should therefore be more productive which will create the right shift in LRAS to LRAS' and the growth in Real GDP ( $Y - Y'$ ).

In terms of development, this policy should increase Chile's HDI Score by improving education standards. Literacy rates therefore, should rise.

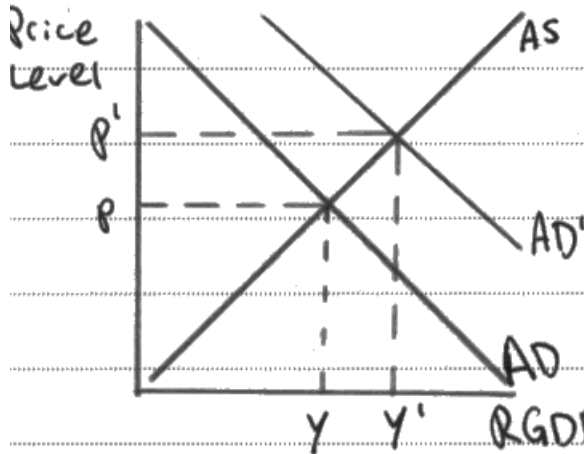
The effectiveness of Spending on education on increasing economic growth is dependent on levels of AD in an economy, a right shift in Chile's LRAS may have no effect if there is inadequate AD to result in economic growth. There are also great time lags associated with such a policy as the effects will not be felt for a generation.

Individual firms are likely to benefit from investment into education and training as the skills and qualifications of Chile's Workforce will rise. ~~Idaer~~ Higher Skilled Staff are likely to be more productive and possibly innovate, this may create new manufacturing techniques which will raise productivity further. Firms will therefore experience reductions in unit costs, enabling them to set lower prices and increase their competitiveness. Lower production costs for firms ~~may create~~ <sup>and lower</sup> prices will also increase international competitiveness which can ~~give rise~~ create a current account surplus.



However, government Spending may not be suitable for Chile due to the governments current fiscal deficit of 3% of GDP, further Spending would lead to greater government debt.

Demand Side policies such as ~~lower~~ tax rates ~~and~~ changes and manipulating ~~the~~ interest rates could also be used. Lowering interest rates could be used to boost economic growth. Lower interest rates would reduce the incentive to save money, particularly if set below inflation, this would result in a fall in the marginal propensity to save. An increase in AD to AD' would be the primary effect with RGDP rising from Y to Y', thus increasing economic



growth.

Businesses will also benefit from this policy as loan repayments will become cheaper, creating more of an incentive to borrow money. This money may be used for investment into research and development which may result in new products which will create higher profits for these firms. Lower interest rates may also reduce loan repayment costs on existing variable rate loans which will reduce Average costs.

Demand side policies have limitations, such as

the risk of <sup>demand-pull</sup> inflation as the price level rises from  $p$  to  $p'$ , this is almost inevitable in Chile due to its low levels of spare capacity. Inflation therefore will rise further above the 2-4% target range.

Demand side policies may also fail to improve inequality as only those in high positions in firms may benefit.

These policies should stimulate growth and development in Chile, however, they each have limitations. When used in conjunction, Chile's economy should prosper.

Without witnessing high inflation due to the increased spare capacity created by supply side policies. Government revenue should also rise from taxation which should help finance the fiscal spending.



**ResultsPlus**

**Examiner Comments**

L4 (growth and dev), L3+ (generic), L4 (micro macro) so 15/16

EV L3 (9)

E3-, E2, E3- informed judgement so mid level 3 8/9 eval

23/25

KAA L (15)



**ResultsPlus**

**Examiner Tip**

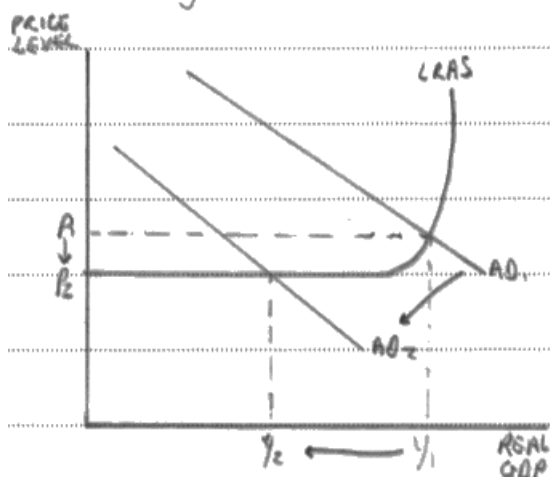
Use the context data provided as the springboard for your answer. The passages were full of fiscal, monetary and supply side policies. The evaluation was also strongly indicated in the passages.



### Question 1 (e)

This is a good answer because it is based firmly in the context provided, that of falling levels of investment in Chile.

As extract A makes clear investment in Chile is falling due to 'uncertainty' over the Prime Ministers reforms'.



A fall in the level of investment in Chile will lower aggregate demand ( $AD$ ) in the economy. This is shown in the diagram with the shift from  $AD_1$  to  $AD_2$ . This is damaging to the Chilean economy as real

GDP falls from  $Y_1$  to  $Y_2$ . This may also cause a negative multiplier effect, as a weakened economy might mean lower consumer spending, further lowering  $AD$ .

However, as shown on the diagram the fall in  $AD$  has lowered Chile's price level from  $P_1$  to  $P_2$ . This would make Chile's goods and services more internationally competitive, leading to a rise in the value of exports. This increase net exports, increasing  $AD$  and therefore, potentially, offsetting the fall in investment in the long run.

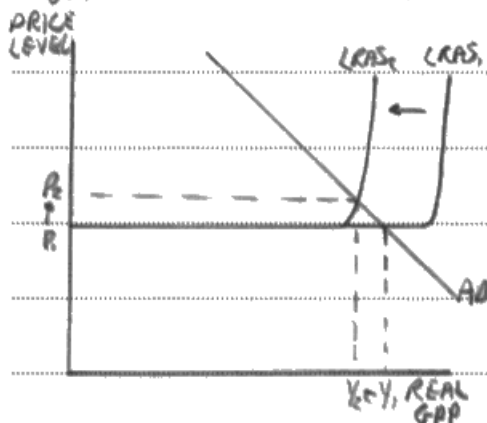
Another problem with a lack of investment for individual firms is the inability to benefit from economies of scale and more efficient production methods. By not investing in their firms,

Chile could fall behind other countries in terms of efficiency. This could lower the market share of Chilean firms, lowering profits as demand shifts to cheaper alternatives.

However, it depends on the length of time the companies hold off on investment. If it is only a short break from investing, as it becomes apparent the Prime Minister's reforms aren't too damaging, this could prevent the loss of market share and demand.

Another microeconomic effect of low levels of investment could be an increase in dividends to share holders in Chile. As firms aren't spending as much investing in firms more money may be paid to shareholders. This could lead to an increase in disposable incomes for Chilean citizens, and overall a higher standard of living.

However, the likelihood is that in a country such as Chile inequality will be high, meaning only the wealthiest will own shares. This increase in dividends could increase income and wealth inequality because rather than investment boosting wages and employment, it simply goes to the ~~at~~ already wealthy share holders.



Low investment in an economy could lead to a fall in Chile's productive capacity. This fall ~~could cause cost push~~ from LRAS, to LRAS<sub>2</sub>, could cause cost push inflation, from  $P_1$

to  $P_2$  on the price level. It may also cause a fall in real GDP from  $Y_1$  to  $Y_2$ . Overall this is damaging to ~~the~~ Chilean's economy, \*

In conclusion a fall in the level of investment is bad for Chile's economy. It may cause a fall in Real GDP due to the lower aggregate demand. ~~and~~ Furthermore the long term negatives, with the economy losing capacity and firms losing efficiency, are even worse. Chile's government should make ~~efforts~~ to increase investment and protect the economy.

## Question 2 (a)

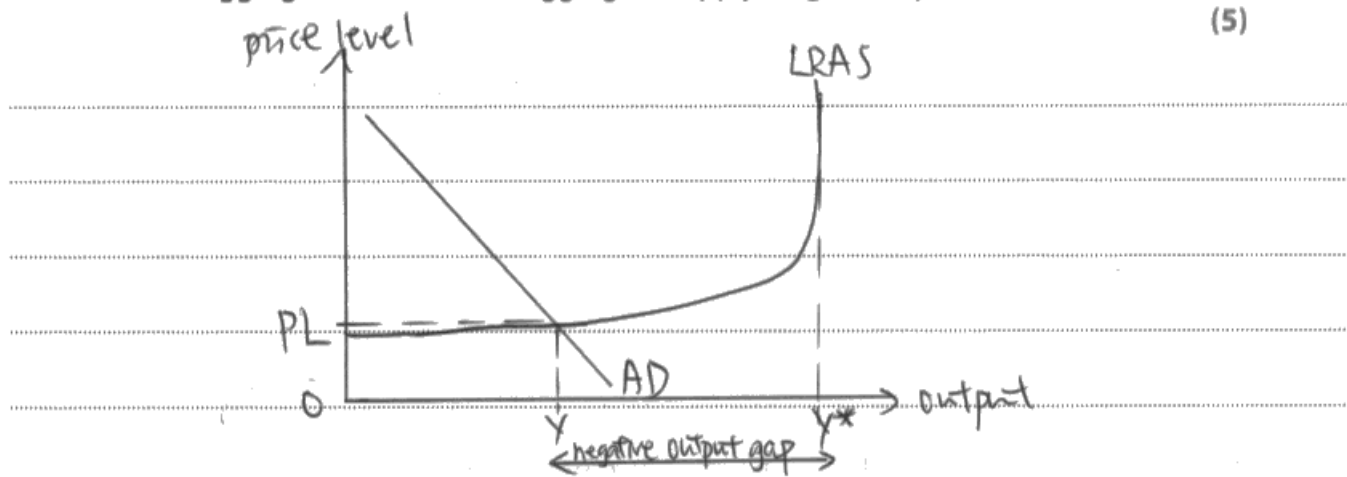
Candidates that gave a clear diagram showing an output gap and referred to the situation evident in the UK as shown by Extract D scored well on this question. An extraordinarily large number drew the output gap incorrectly as a triangle bounded by the LRAS, SRAS and AD, or just drew a shift in AD or a static AD/AS without showing full or potential output.

If candidates understood an output gap, most were able to define and show such a gap on an AD/AS diagram successfully. Many candidates failed to use the data at all and did not focus on the evidenced *negative* output gap.

This is a good example of how to earn full marks.

- (a) With reference to Extract D (line 18), explain the meaning of the term 'output gap'.  
Use an aggregate demand and aggregate supply diagram in your answer.

(5)



During recession since the onset of 07-08 financial crisis, there are reduced investment in both physical and intangible capital. This causes a fall in AD as I is one of the components. Also, immobility of labour and under-employment of skilled workers mean that AD is weak. The economy is operating below the potential capacity. There is a negative output gap.



**ResultsPlus**

**Examiner Comments**

2K: 2 clear explanation

1AN + 1AP: clear diagram showing the gap on the horizontal axis meeting the full employment level

1 AP: clear use of data – immobility of labour

5/5 marks



**ResultsPlus**

**Examiner Tip**

Short answers can be very effective. There is no need to fill all the space.



## Question 2 (b)

This was the weakest exam question in the whole exam and one that candidates struggled with the most. Firstly, most candidates could not give an accurate definition of national debt as a percentage of GDP. Often candidates got confused with the relationship between national debt and fiscal deficit. Moreover, many candidates got confused with the current account and this appeared in a large number of responses. Those candidates who were able to interpret the data and relate it to their understanding of the government's budgetary issues were able to score highly.

A higher scoring answer has some sense of the link between the stock and flow concepts of debt and deficit, and a sense of the relationship between annual figures and cumulative figures. Those answers continuing to explain how deficits and debts are related as well as how the relationship may be less clearly dependent on the changes in GDP were likely to gain both marks for evaluation, although there were many ways to achieve these evaluation marks.

Many candidates identified an understanding of the fiscal deficit and the national debt as a proportion of GDP and used the figures to demonstrate this, and this would tend to earn 4/8 marks. Few candidates made the link clear, and most were confused by the observation that at times there was a direct relationship and at other times an indirect one, as indicated by the data.

Use this response as a guide.

(b) With reference to Figures 4 and 5 and your own knowledge, examine the relationship between the national debt as a proportion of GDP and the fiscal deficit.

(8)

National debt as a proportion of GDP is the accumulation of all previous fiscal deficits that have occurred over the years within a country. The fiscal deficit is meanwhile is the amount government spending exceeds government tax revenue within a year.

There is arguably a direct relationship between the fiscal deficit and national debt as national debt is

made up of cumulative fiscal deficits. When a country is running ~~is~~ a fiscal deficit, the national debt will likely increase. When the country alternatively is running a fiscal surplus, the national debt should fall. This is shown by the fact that in the years the UK government did run a surplus, 1997 to 2001, the size of the national debt decreased as a percentage of GDP from 40% to nearly 30%.

However, it cannot be argued the fiscal deficit is the only contributor to national debt as a proportion of GDP, the size of economic growth also matters. For example if the government ran a fiscal deficit one year but economic growth was very high, it ~~may~~ would cause national debt as a proportion of GDP to fall from the previous year.



### ResultsPlus Examiner Comments

K Define deficit  
K Implicit debt definition  
AN Deficit/surplus to debt  
AN Gains two marks on mark scheme  
AP Relationship (surplus and debt)  
AP Data reference  
EV Depends on growth (strong ev)  
EV Development  
6/6 + 2/2 (8)



### ResultsPlus Examiner Tip

National debt is nothing to do with the household or external debt of a country. It is a governmental issue.

## Question 2 (c)

Many candidates recognised that the National Living Wage would increase firms' costs and lead to a rise in average and marginal costs. A good and challenging question which candidates attempted well. Most were able to give a correct diagram. Diagrams then showed a reduction in profits for the firm, but finding the new profit area lined up with the new  $MC=MR$  point was challenging for many candidates (although much easier for those who had reasoned that the change in costs was a fixed factor and therefore no change in MC).

This was often evaluated by arguing that any fall in profits may be offset by gains in productivity because of increased wages. Other excellent evaluation included the evidence that the wage increase was estimated to have a 0.3% impact on overall costs, does not affect the under-25s, depends on whether firms can pass on cost increases (often with consideration of the market power of firms and their profit levels), and effects on productivity also suggested in the data.

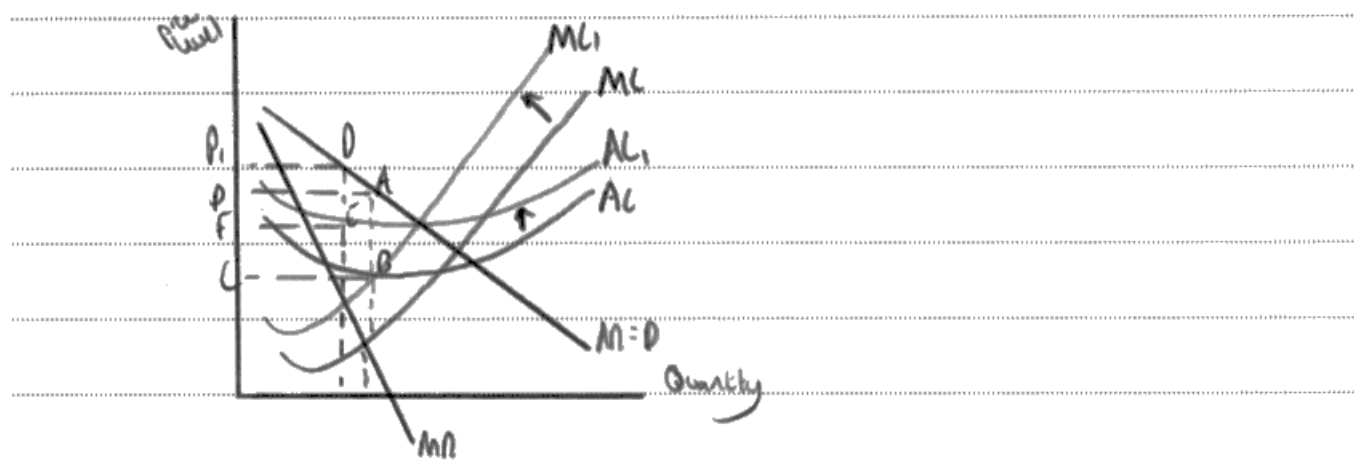
This was the question where candidates gave a large amount of evaluation to a very good standard. Candidates were able to respond well to this question perhaps as it resembled the previous syllabus Unit 3 questions. There was a tendency for the candidates to provide very long multiple evaluative points (a legacy from the 16 mark questions in 6EC03) and so perhaps spent too much time on this question.

Some candidates confused the concept of a mandatory NLW with the optional Living Wage proposed but not mandatory in some areas of the country. The passages made it clear that the NLW was a change in mandatory pay for the 25+ age group with a premium for the 25+ age group.

This diagram was one of very few that was drawn fully accurately.

(c) Discuss the likely impact of the National Living Wage on the profitability of firms.  
Use a cost and revenue diagram in your answer.

(12)



A national living wage for all employees 25 and over could lead to a rise in unit labour costs causing a rise in variable costs and consequently a rise



in both average cost for  $AC-AC$  and marginal cost for  $MC-MC$ . This could cause a fall in the Supernormal profits made by the business as seen on the diagram from  $MBC - P, DEF$ .

However in the long run firms could use the remaining supernormal profits to become dynamically efficient leading to a rise in innovation and spending on research and development leading to a fall in production costs in the long run and therefore firms allowing them to see increases in demand could potentially return to past levels of Supernormal profits.

If firms are operating in perfectly competitive markets it would be as if both  $MC$  and  $AC$  with both firms increase in labour costs will lead to both firms making a loss in the short run and if they aren't contributing to the average total costs then they may choose to shut down.

However if a firm is a capital intensive means of production then the introduction of a national minimum wage may have a relatively low

impact on  $AC$  and  $MC$  and therefore they will still be able to see normal profits in the short run.



**ResultsPlus**

Examiner Comments

KAA L3 (8):

strong KAA and diagram; no need for second KAA as diagram required

EV L2 (4):

sustained L2 ev



**ResultsPlus**

Examiner Tip

The handwriting on this script was illegible and it took some deciphering. Examiner's must be able to read responses.

## Question 2 (d)

An effective question in terms of discrimination, on which well-prepared candidates scored well, responding to the single request rather than having to look at more than one variable as in 2(e). Candidates gave a good amount of evaluation with this question.

This was a question about the factors *affecting* competitiveness, not about the *effects* of improved competitiveness. However, the advantage of this was that it made it into a question based on Year 13 work, much more in line with 2(e) in terms of difficulty, and one in which the data on productivity and the Living Wage in the passage could be used to great effect. Many answers focused on the Brexit issue, which was clearly on the minds of many candidates, but many failed to realise that at the time of the exam the UK had not actually left the EU and therefore is unable to alter independently its level of protectionism. There were some stronger answers using the prospect of Brexit, and in particular, the effect of exchange rate changes since June 2016, but it should be advised that the data provided is the best place to start in choosing points to make. Better candidates recognised this and were able to discuss both price and non-price factors that impact on competitiveness and particularly refer to the "productivity puzzle" concerning the UK.

There was a tendency to provide far too many influences at not sufficient detail but generally there were good responses with evidence based analysis and evaluation of both micro and macro. However, as with the other essays, far too many candidates offer separate influences rather than observing how a micro influence is also linked to a macro influence making their essays longer and time consuming. These responses rarely achieve higher than L3 and are often confused, fragmented and with very limited chains of reasoning. Another frequent problem was misunderstanding of the data on productivity in Figure 6, and answers and evaluation which strayed into the effects rather than the causes of competitiveness. A frequent discussion was the effects of a low exchange rate, for example, with the Marshall-Lerner condition, but it was difficult to see how this related to the question.

This starts as a narrow and repetitive response, but develops into strong L4 on the penultimate page, with some judgement at Level 3 on the final page.

A micro economic influence on the UK's international competitiveness is the low labour productivity growth in the UK compared to many other countries. The UK has almost 15% lower labour productivity per head than

Spain. This low labour productivity growth has been put down to many factors combined including reduced investment in training of human capital and lack of research and development into better production methods, immobility of labour and too much bureaucracy at the employment of new ~~workers~~ workers.

Low labour productivity means that <sup>there is</sup> ~~there is~~ less output per worker per hour compared to that of their counterparts abroad.

This increases cost of production and means that UK goods cost more to produce so the prices will be higher meaning they are less internationally competitive than many other countries.

Lack of training and investment means that the workers aren't developing new skills and new technology to improve productivity of the workforce.

There is also lack of research and development ~~in~~ into new capital intensive methods that in the long run could ~~not~~ improve productivity.



and low costs meaning the UK could become more internationally competitive.

There is also immobility of labour due to high levels of bureaucracy when employing new workers and also when firing employees. This means firms often hold onto low productivity workers instead of getting new, better employees. Because the cost of replacing employees is ~~too~~ too much and too time consuming. This means cost of production is ~~high~~ high because the current workers are inefficient, so prices are higher and less internationally competitive. However

the availability of more efficient employees may be low if there is low unemployment and the economy is reaching full employment in which case there aren't really ~~any~~ any options but to retain the less efficient workers. Furthermore there may have recently been huge amounts of spending on investment in education

and training but there are long time lags on the effects of it.

A macroeconomic influence on the UK's international competitiveness is the exchange rate and strength of the ~~A relative to~~ pound relative to other currencies, especially with the UK's main trading partners.

If there is a strong pound then UK's exports are relatively more expensive ~~to~~ compared to other countries goods as the other countries ~~have~~ to have to give up more of their currency to pay for UK exports. This makes

the UK internationally uncompetitive. However following the decision to leave the EU in 2016 the value of the pound dropped significantly, and following its slight recovery it dropped again following the June 2017 general election. This meant a weaker pound and therefore ~~at~~ UK goods and exports became internationally more competitive ~~to~~ relative to other

country's exports. This is because the country's buying UK exports ~~are~~ don't have to give up as much of their currency to ~~buy UK~~ buy UK exports.

The extent ~~that~~ to which this will improve UK's international competitiveness depends on whether the other countries that trade a lot with the UK then proceed to devalue their currency if they are operating under a fixed exchange rate to keep their ~~to go~~ exports ~~more~~ competitive or whether their currency depreciates due to shocks in their economy at the same time as in the UK.

Overall the UK's international competitiveness ~~depos~~ is influenced by many factors. The influence of exchange rates and protectionism are predominantly on influences on the finished exports whereas labour productivity is influences on the manufacturing of the



goods so a combination of increased investment in labour productivity and a relatively weak exchange rate will keep the ~~productivity of competitiveness of the~~ UK internationally competitive relative to other countries.

★ International competitiveness is the ability to compete on globally on price and non price factors in ~~markets~~ global markets



**ResultsPlus**

Examiner Comments

KAA L4 (14):

L4-, repeat, L3 (too similar), L4

EV L3 (7): E2, E3-, E3- 21/25



**ResultsPlus**

Examiner Tip

Definitions are not required (unless specifically requested in a question) but they are a useful way to keep the answer focused on the question. This candidate left the definition until the end of the final page, but the understanding was clearly there throughout the whole answer.



## Question 2 (e)

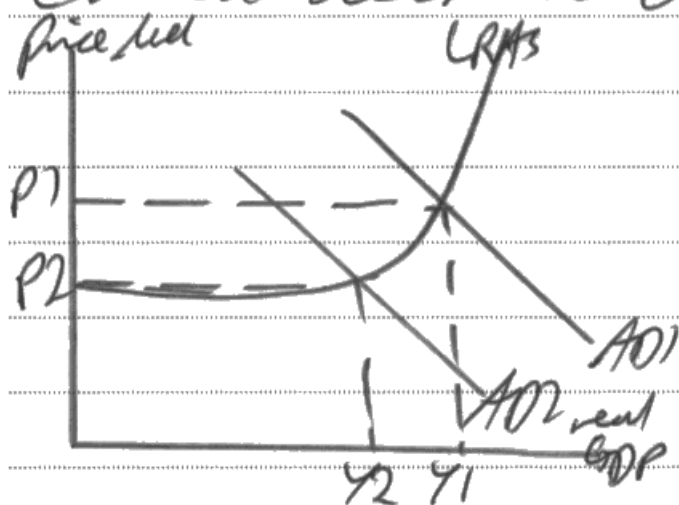
This response does actually answer the question, comparing cuts with government spending with the raising of taxes, but there are many questions left in the analysis.

Instead of increasing tax rates, reducing public expenditure may be better for the economy as it doesn't reduce incentive to work for workers, which ~~as a result~~ would be caused by an increase in income ~~the~~ tax. Therefore

it will be better as we will ~~be~~ have more incentive to work, and the work harder.

A decrease in public expenditure can mean a decrease in spending on welfare, public schools, public hospitals etc. This would really impact the poor as compared to the rich as they will be affected as they go to private schools. This will increase inequality in the economy and can increase relative poverty.

A decrease in public expenditure  
could decrease aggregate demand.



This causes deflation  
from  $P1$  to  $P2$  and  
negative actual  
economic  
growth.

Furthermore, this could lead to  
a negative multiplier effect if there  
are cuts to the NHS, as there are likely to  
be redundancies, reducing incomes and  
therefore reducing consumer spending which

will further reduce aggregate demand.

Also, not raising taxes ~~could~~ wouldn't  
cause a fall in foreign direct investment,  
although evidence of reduced government  
spending may deter possible investors from  
our country to another. This could reduce  
the possibility of jobs being created. ~~Just~~  
OB

~~Reducing public expenditure will directly reduce the level of debt, as shown in figures 4 and 5, either there was a reduction in the level of government spending (1997-2000), there was~~

Public expenditure can directly reduce the fiscal deficit, ~~but~~ where taxation is not always direct as some people ~~can~~ avoid tax. It can be seen as a safer way of reducing the deficit.

Overall, I would say that reducing the ~~def~~ fiscal deficit through reducing public expenditure is probably the best way to reduce the deficit, ~~with~~ without many micro or macroeconomic problems.

It doesn't affect the incentive of ~~workers~~ like taxes can do. I do think that it would be more beneficial if the cuts to spending wasn't on public services such as the NHS or education, it would possibly be best to cut spending on tourism, at least in the short term anyway.



## ResultsPlus

Examiner Comments

**KAA L3 (11):**

**L3, L3 (both focused on Q), L3 (developed but only G), L3 (tax); no data**

**EV L2 (6)**

**E2, E3; some judgement but not sustained E3 so top E2**

**17/25**



## ResultsPlus

Examiner Tip

Use the data. Give extended chains of reasoning. Fewer strongly argued points score better than lists of undeveloped factors.