



ADVANCED GCE
ECONOMICS
 The UK Economy

2887

Candidates answer on the Answer Booklet

OCR Supplied Materials:

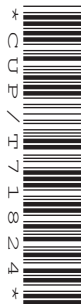
- 8 page Answer Booklet

Other Materials Required:

None

Friday 5 June 2009
Afternoon

Duration: 1 hour 30 minutes



INSTRUCTIONS TO CANDIDATES

- Write your name clearly in capital letters, your Centre Number and Candidate Number in the spaces provided on the Answer Booklet.
- Use black ink. Pencil may be used for graphs and diagrams only.
- Read each question carefully and make sure that you know what you have to do before starting your answer.
- Answer Question 1 and **one** question from Section B.
- If you need to use additional answer sheets, fasten these sheets securely to the Answer Booklet.
- Do **not** write in the bar codes.

INFORMATION FOR CANDIDATES

- The number of marks is given in brackets [] at the end of each question or part question.
- The total number of marks for this paper is **45**.
- The quality of your written communication will be taken into account in the marking of your answer to Section B.
- This document consists of **4** pages. Any blank pages are indicated.

Section A

Answer **this** question.

1

Fiscal Rules

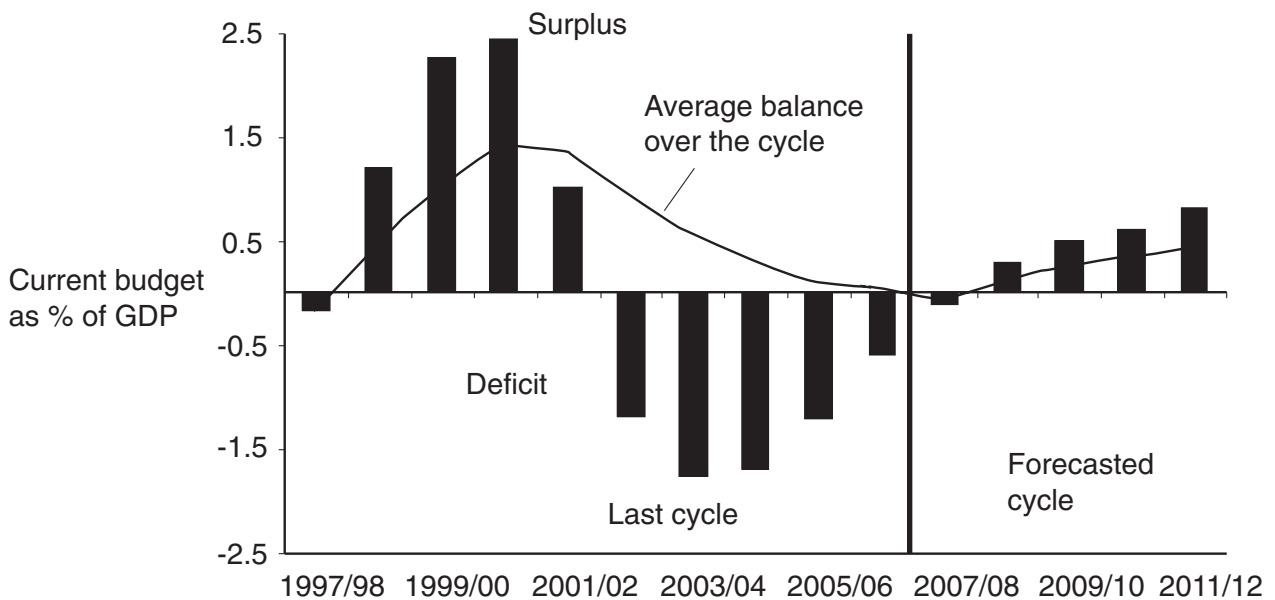
Since 1997 fiscal policy has been influenced by two basic rules:

- the golden rule;
- the sustainable investment rule.

The golden rule states that over the course of an economic cycle, the government will borrow only for investment purposes. Current spending will not be funded by borrowing over the period as a whole. In other words, the government will aim for a current budget that is balanced or a current budget surplus over the economic cycle as a whole. (See Fig. 1)

5

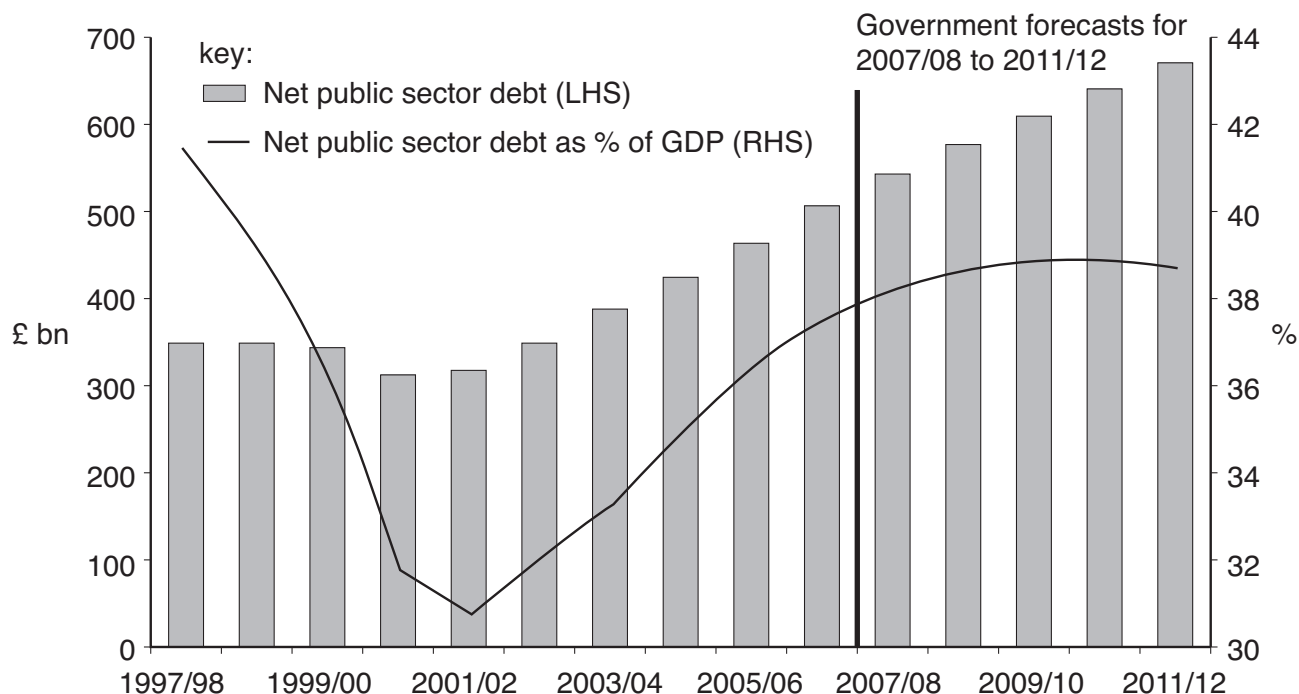
Fig. 1 Golden Rule: Current Budget Position



Denotes the end of one cycle and the beginning of the next.

The sustainable investment rule states that the ratio of public sector net debt to gross domestic product (GDP) is to be maintained at a stable level and be below 40%. This would ensure that the cost of investment is borne principally by those benefiting from it, and not imposed on future generations. (See Fig. 2) 10

Fig. 2 Sustainable Investment Rule



Denotes the end of one cycle and the beginning of the next.

According to the Treasury's 2007 Budget Report, the cycle which started in 2007/08 will have done so with a first year current budget deficit of £4 billion (compared with a forecast surplus of £1 billion in the 2006 Budget Report).

Answer **all** parts.

(a) Explain what is meant by:

- (i) the economic cycle (line 4); [2]
- (ii) current budget surplus (line 7). [2]

(b) Using an AD/AS diagram, explain the impact that a budget deficit, as indicated in Fig. 1, may have on the economy. [4]

(c) State and explain **one** benefit which the golden rule brings to macro-economic performance. [2]

(d) Using Fig. 1 and Fig. 2, comment on whether the two fiscal rules were observed during the last economic cycle. [4]

(e) Discuss whether it is possible to forecast accurately the government's budget position. [6]

Section B

Answer **one** question.

- 2** **(a)** Explain the factors that influence the current account position of the UK's balance of payments. **[10]**
- (b)** Discuss the extent to which a depreciation of sterling may help improve the UK's current account balance of payments position. **[15]**
- 3** **(a)** Explain how the distribution of income and wealth can be measured. **[10]**
- (b)** Discuss how economic policy could be used to affect the distribution of income and wealth in the UK economy. **[15]**
- 4** **(a)** Explain the significant sources of inflation currently affecting the UK economy. **[10]**
- (b)** Discuss the extent to which the control of inflation is the most important macroeconomic policy objective in the UK. **[15]**

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