

X038/701

NATIONAL
QUALIFICATIONS
2010

FRIDAY, 28 MAY
9.00 AM – 11.15 AM

ECONOMICS
ADVANCED HIGHER

You should answer Section A and **two** questions from Section B.

The marks for each question are shown in the margin.



SECTION A

Read the following passage, and then answer the questions which follow on *Page three*.

The UK's Budgetary Deficit

According to the International Monetary Fund, the UK's Budget deficit as a share of GDP will be greater than any other leading economy by 2010/11, reaching well over 13% of GDP. The problem for the UK economy is not the **automatic stabilisers** or the fiscal stimulus which have occurred as a result of the recession. The real problem is the large **structural deficit** which had been growing before the recession even started. The Institute for Fiscal Studies has calculated that the structural deficit will remain at £90 billion after the recession. This is partially because tax revenues, especially those from the financial sector, have plunged.

The sustainability of the UK's budgetary position is very much a concern. The level of National Debt may reach well over 150% GDP by 2014. Future generations will have to pay a high price for the costs of the recent recession and the public finances may be a drag on economic growth for years to come. The reaction of international money markets to this situation could lead to a further fall in the value of sterling. As yet the UK government has had little difficulty funding the deficit but should the UK be viewed as a "sick" economy this may become more of a problem. If UK government debt were to lose its AAA rating this might lead to upward pressure on interest rates in the UK.

Given the continued concerns over the length of the recession and shape of the recovery, withdrawing the fiscal stimulus too early could bring the fragile recovery to a juddering halt. In the long run, coming up with the mix of tax increases, cuts in government spending and asset sales which will do least damage to the UK's economy and social fabric is going to be a major problem.

Adapted from an article in "The Economist" 29th September 2009.

	<i>Marks</i>
1. (a) Explain the following terms as used in the passage.	
(i) Automatic stabilisers (line 3).	2
(ii) Structural deficit (line 5).	2
(b) (i) Outline the fiscal stimulus taken by the UK government.	2
(ii) Explain how it should help the UK economy recover from recession.	3
(c) Explain how the rising level of National Debt could lead to a burden on future generations and be a drag on economic growth for years to come.	4
(d) Describe why a large and persistent budget deficit might lead to a fall in the value of sterling in foreign exchange markets.	3
(e) Consider the possible consequences for the UK government and the economy if the government's debt loses its AAA rating.	3
(f) "Coming up with the mix of tax increases, cuts in government spending and asset sales which will do least damage to the UK's economy and social fabric is going to be a major problem."	
Discuss the above statement in relation to reducing the budget deficit.	6
	(25)

[Turn over for Section B

SECTION B**Attempt TWO of the six questions set.****Each question carries 25 marks.**

1. The banking crisis that started in 2008 exposed weaknesses in the UK's system of financial regulation.
 - (a) Outline the weaknesses which existed in the UK's system of financial regulation. 7
 - (b) Describe changes in the UK financial regulations that have been considered to avoid a repeat of the banking crisis. 8
 - (c) Evaluate the likely effectiveness of the proposed changes in financial regulation and suggest other changes that might be considered to tighten control. 10

2. Different types of market structure bring different costs and benefits for consumers and the wider economy.
 - (a) Discuss the main differences between perfect competition and monopoly. (You must include diagrams to clarify your explanation.) 8
 - (b) Argue the case for and against the view that perfectly competitive markets are always more efficient in allocating resources than monopolistic markets. 9
 - (c) Examine the reasons why an airline is able to charge different prices to passengers for using the same flight or route. 8

3. In common with most developed countries, the UK is facing the consequences of an ageing population.
 - (a) Discuss the consequences for the economy of an ageing population. 8
 - (b) Describe measures that have been considered to deal with the economic effects of an ageing population. 8
 - (c) Analyse the likely effectiveness of these measures. 9

4. In 2008/2009 the UK experienced its worst economic recession since 1945.
- (a) Discuss the reasons why the UK economy moved into recession in 2008. 7
 - (b) Explain why the UK has been slower to recover from recession than most other developed countries. 8
 - (c) Examine the consequences of high levels of unemployment for the demand side and supply side of the UK economy. 10
5. In January 2009 the Bank of England implemented a policy of Quantitative Easing.
- (a) Explain the term Quantitative Easing and the reasons why it was introduced. 8
 - (b) Explain how Quantitative Easing is expected to influence the UK economy. 9
 - (c) Discuss the reasons why concern has been expressed about the likely effects of the policy of Quantitative Easing. 8
6. The Copenhagen climate change summit in December 2009 was a follow up to the Kyoto Protocol to prevent dangerous increases in global warming.
- (a) Explain why many economists consider that global warming is the result of market failure. (Your answer must include a diagram.) 8
 - (b) (i) Describe the main outcomes of the Copenhagen summit. 4
 - (ii) Discuss the methods that could be used to achieve a reduction in CO₂ levels. 6
 - (c) Explain why measures to reduce CO₂ levels have been criticised by emerging and developing economies. 7

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