

X038/701

NATIONAL
QUALIFICATIONS
2008

FRIDAY, 23 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*.

Oil prices are going through the roof

Crude oil prices had risen from \$30 a barrel to almost \$100 a barrel by the end of 2007. In the past, a sharp rise in the price of oil has resulted in **global recession**, however, this had not happened by the end of 2007.

- Although oil remains essential to all economies, the oil intensity of **Gross Domestic Product (GDP)** today has dropped to just 15% of its level in 1970. The USA has been hit much harder by the rise in oil prices than most other developed economies. Paradoxically, UK consumers are affected less by oil price rises than consumers in other countries. Given the dependence of the world economy on the USA, the continued growth of the world economy cannot be guaranteed.
- 10 The increase in crude oil prices has been driven mainly by demand side factors. Now, however, crude oil prices are continuing to climb even as prospects for world economic growth are deteriorating rapidly. Some economists believe that as much as 20% of the cost of a barrel of oil can be blamed on speculators. Speculative buying is unlikely to ease until the price of oil exceeds \$100 a barrel. The
- 15 reluctance of OPEC to raise production to meet growing demand for oil has allowed price levels to increase.

According to BP, there are 38 years of oil reserves left in the world at current levels of consumption. However, it is predicted that demand for oil will increase from its present 85 million barrels a day to 120 million barrels a day by 2035.

- 20 Oil is a finite resource that has been running out ever since we started using it for fuel. High levels of oil prices have encouraged greater use of shale oil and the development of alternative sources of energy. Given that “necessity is the mother of invention”, we might be able to avoid the consequences of living in a world without oil.

Adapted from two articles,

1. *Oil prices are going through the roof. What will that mean for the big economies*
by Robin Pagnamenta, The Times, 10 November 2007
2. *The high price of oil is beginning to take its toll*
by Gary Duncan, The Times, 12 November 2007

1. Explain the following terms as used in the passage.
 - (a) “Global recession” (line 2)
 - (b) “Gross Domestic Product (GDP)” (lines 4–5) 2
 2. Explain why the oil intensity of GDP has dropped since 1970. 2
 3. Changes in the price of crude oil affect economies at differing rates.
 - (a) Why might the USA be affected more by increases in the price of oil than other developed economies? 2
 - (b) Why might UK consumers of petrol be affected less by increases in the price of oil than consumers in other countries? 2
 - (c) Discuss why crude oil prices of over \$100 a barrel might lead to an economic slowdown. 4
 4.
 - (a) Discuss 3 demand side factors, other than the activities of speculators, which have driven up crude oil prices. 3
 - (b) With the use of a suitable diagram, illustrate the changes which have occurred in the market for oil. 3
 5. Who are the speculators likely to be interested in the price of oil and why might they give particular attention to the market for crude oil? 2
 6. The passage suggests that the projected levels of oil consumption for 2035 are unattainable.
 - (a) Explore the viability of alternative energy sources. 3
 - (b) If “necessity is the mother of invention”, how might this affect the economic behaviour of energy supplying firms? 2
- (25)**

[Turn over for Section B

SECTION B

Attempt TWO of the six questions set.

Each question carries 25 marks.

Marks

1. There has been a marked rise in the number of migrants coming to the UK.
 - (a) Discuss the reasons for the rise in the number of migrants who have chosen to enter the UK since 2004. 7
 - (b) Analyse the economic benefits to UK citizens, UK firms and the UK economy of the rise in the number of migrants entering the UK. 9
 - (c) Analyse the economic costs to UK citizens, UK firms and the UK economy of the rise in the number of migrants entering the UK. 9

2. Because of its fall in value the President of Iran provocatively described the US dollar as “a worthless piece of paper”.
 - (a) Discuss possible reasons for the fall in the foreign exchange value of the US dollar in recent years. 10
 - (b) Discuss the effects of the fall in the value of the US dollar on
 - (i) the USA,
 - (ii) the European Union and
 - (iii) the world economy. 15

3. UK house prices rose by over 200% between 1996 and 2007, whilst the retail price index rose by only 35% over the same period of time.
 - (a) Discuss reasons why UK house prices persistently exceeded the general rate of inflation in the UK. 11
 - (b) It is widely forecast that house prices will stabilise or even fall during the course of 2008. Discuss some of the likely costs and benefits of a fall in UK house prices. 14

4. A concern of environmental economics is the problem of market failure.
 - (a)
 - (i) Explain what is meant by the term market failure. 2
 - (ii) With the use of a suitable diagram, explain how the problem of market failure will affect the efficient and sustainable use of the environment. 8
 - (b) Describe measures and initiatives which have been introduced or are under consideration throughout the world to lead to a more efficient and sustainable use of the environment. 8
 - (c) Examine the problems that have been encountered when trying to put these measures and initiatives into effect. 7

5. During the second half of 2007, the Monetary Policy Committee (MPC) of the Bank of England was reluctant to change interest rates because of conflicting pressures.
- (a) Discuss the pressures on the MPC to increase interest rates. 8
 - (b) Discuss the pressures on the MPC to reduce interest rates. 8
 - (c) Explain fully how changes in interest rates affect the UK economy through the monetary transmission mechanism. 9
6. In September 2007, the UK was hit by its first run on a bank for almost 150 years.
- (a) Explore the reasons why the Northern Rock Bank ran into financial difficulties in September 2007. 8
 - (b) Explain what measures have been considered to rescue the Northern Rock Bank and restore confidence in the UK financial markets. 9
 - (c) Discuss the possible implications of the problems in financial markets for the UK economy. 8

[END OF QUESTION PAPER]

ACKNOWLEDGEMENTS

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