Paper 2 Section B – Improving answers activity

- **Go through these answers and improve them using the examiner's comments after each answer**
- **Make sure any new answers are in a different colour**
- **There is a link to the question paper and mark scheme below -**

https://qualifications.pearson.com/content/dam/pdf/A%20Level/economics-a/2015/specification-and-sample-assessment-materials/Economics-A-Collated-SAM.pdf

You will need to look at page 60 onwards

Economics paper 2 - Improving responses Activity

Question 6a Response 1 -

Burundi: 2.47 billion divided by 16.14 million = 153.036 (3.d.p);

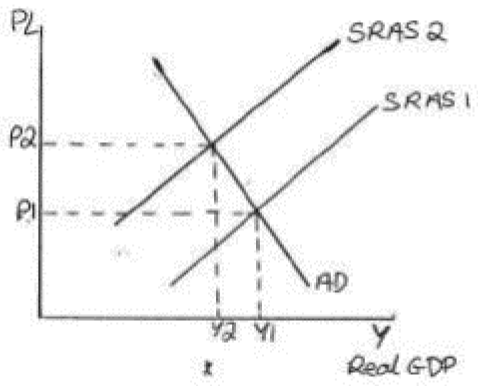
Kenya: 37.23 billion divided by 62.78 million = 593.023 (3.d.p)

593.023 divided by 153.036 = ratio of 3.88 (3.d.p)

Examiner's comments - There is an implicit understanding of GDP per capita and the calculations of GDP per capita for Burundi and Kenya are correct. However, the ratio is not calculated accurately; the figure given is for Kenya to Burundi. This response therefore gained 3 marks.

Question b) Response 2

Extract A identifies that external supply side shocks constrain economic growth in Burundi. An example of an external shock is 'climate change' and with climate change harvests and productions could be impacted. Therefore, less goods and services are produced overall. This could impact Burundi particularly as 'coffee and tea make up almost 70% of Burundi's total export earnings'. As they are landlocked, transporting items is made harder and due to their poor infrastructure anyway, costs would be very high which limits opportunities for international trade.



Lack of supply

The diagram above shows the equilibrium of supply and demand at Y1,P1. There is a lack of demand so the SRAS1 lines shifts inwards to SRAS2. Due to this the real GDP moves from Y1 to Y2, showing a decrease in the Real GDP. With price levels, P1 increases to P2, which means that prices increase and goods are less likely to be sold domestically. Another factor that constrains Burundi's growth is 'the lack of export diversity' (extract a), however have 'remained constant' (extract b). There is danger with a lack of export diversity because if the harvest is poor, it'll affect ¾ of the population and the whole country would be hit. Also, if the prices of these goods fall, there would be limited revenue for the suppliers and tax for the government who are trying to make further improvements to the country. However, the government does get money through aid to deal with some of these matters. Imports however have fallen due to inferior infrastructure. Infrastructure is key as it includes, physical mobility of labour, such as motorways, airports and train stations, which could potentially transport food, energy and water. This hinders growth as there are now higher supply costs and reduces the mobility of labour

Examiner's comments Two factors are identified in this response and there is supporting explanation of why these factors constrain growth in the context of Burundi. 6 marks are awarded for knowledge, application and analysis. However, there is no effective evaluation. This response therefore gained 6 marks. Two marks were available for evaluation in this question. The attempt to evaluate using 'aid' was not quite enough to gain the level required. The aid argument needs to be developed if it is to be an effective counter-argument.

(c) With reference to Figure 1, discuss the use of GDP data as a means of comparing living standards among the five EAC member countries.

(12)

Response 2

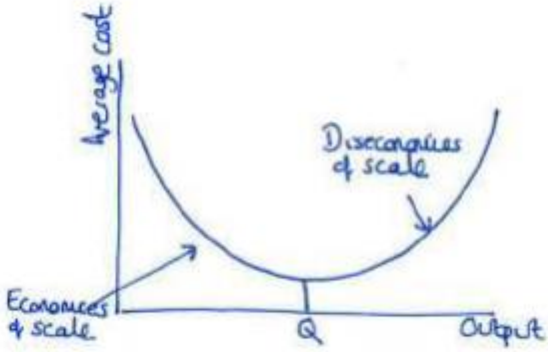
Living standards are a measure of material welfare. GDP represents the dollar value of goods and services produced by an economy in a specific time period. Figure 1 says that Kenya has the highest GDP per capita PPP and Burundi have the lowest. This means that they have lower standards of living. Many measures go into measuring living standards. For example, HDI which assesses the development of a country as well as how it impacts the growth of a country. HDI takes life expectancy, mean years of schooling and the GNI per capita into account when scoring a country. It takes all of government expenditure into accounts, such as investment projects in infrastructure and social welfare from the tax has been collected by goods and services that have been consumed. Also most of the domestic consumption of final goods and services are taken into account. It is quite a straight forward measure of living standards which makes it easier as it is internationally recognised so other countries can compare their data and know exactly what is going on. The GDP of a country can also be simply divided by the population to come up with the amount of GDP per capita which makes it more representative to different parts of the population. However, GDP data can be flawed when measuring living standards as the shadow economy isn't taken into account, as some goods and services aren't sold at market value but are still forms of trade and the products are still consumed. It doesn't show how the income is distributed amongst the population and is most likely very unequal. Also, some of the more developed counties such as Kenya and Tanzania could be experiencing externalities due to the higher levels of production, such as pollution, which could consequently have negative effects on economic welfare. We wouldn't know the quality of the goods and services produced, they could be mass produced in poor quality.

Examiner's comments This response demonstrates understanding of GDP and HDI, and the fourth paragraph explains the value of GDP as a means of comparing living standards. The last two paragraphs provide valid evaluative comments. This response gained Level 2 and 4 marks (4/8) for knowledge, application and analysis and Level 2 and 4 marks (4/4) for evaluation. The total for this response is therefore 8 marks (8/12).

(d) Assess the benefits Kenya has gained from its membership of the EAC since 2000.

(10)

Kenya is the region's largest economy. Since joining the EAC, Kenya has increased its exports to the other EAC members ($1.2 billion in 2010) [extract 2] which has led to faster economic growth for Kenya. This means that the benefits seem to be substantial. Due to rapid economic growth, Kenya should attract investment from foreigners and domestically too. People from abroad may like to set up their factories and even company headquarters in Kenya in search for the best employees for their company with specialised skills and a dedicated workforce. This would mean that unemployment in Kenya would fall, and there would be more disposable income. Furthermore, this extra income can be spent on goods and services, which comes back to the government in forms of VAT and also income tax. This would help the government improve poorer areas of Kenya and keep it constantly growing.
Economies of scale diagram



Firms can also benefits from economies of scale. As shown above, output would increase with increased demand for Kenya's products which means the average cost would also fall. However, when it reaches the point of Q or minimum efficiency scale (MES), this is the point where the product is the lowest produced and after that point the average cost increases as you produce more, leading you to diseconomies of scale. However, there could also be some costs of economic growth in Kenya. Kenya would lose import tariff revenue from the EAC counties, as they now have free trade and movement of goods. This would mean there should be higher levels of trade but they would lose out on taxes.

Examiner's comments

Three possible benefits are identified and explained with varying degrees of quality. One benefit, 'increased its exports', is briefly explained in the second sentence. There is a second benefit and linked analysis at the beginning of the second paragraph. Another benefit is identified at the beginning of the third paragraph but the explanation is rather generic. The last paragraph shows evidence of some evaluation. There is one rather brief evaluative point: 'This would mean there should be higher levels of trade but they would lose out on taxes'. This response gained Level 3 and 5 marks (5/6) for knowledge, application and analysis and Level 1 and 2 marks (2/4) for evaluation. The total for this response is therefore 7 marks (7/10).

(e) Discuss the likely costs and benefits of monetary union to the five members of the EAC.

(15)

A monetary union is when a trading bloc was a common currency, controlled by one central bank. For example most of European Union has adopted the Euro. The Euro zone is more of an important trade partner holding together many more countries than the EAC countries.

A cost of a monetary union is how they would deal with asymmetric shocks. This means that an external shock can impact different member groups of the trading bloc differently and don't have an equal effect. This can be problematic when dealing with the likes of interest rates as they would impact all member states. For example, if one country was experiencing a negative shock, e.g. Burundi, they would need lower interest rates compared to the other countries. If economic openness is increased, there should be reduced chance of an asymmetric shock having much impact.

Another possible cost would be the loss of control over the country's monetary policy. The central bank would decide upon interest rates and make a decision best for the whole trading bloc as opposed to the interests best for a specific country alone. With a common currency different problems may branch out from the interest rate problems and cause further problems. However, there could be benefits to a monetary union, as demonstrated by Kenya and Rwanda have already benefited from the EAC, they would probably benefit more than the other countries in particular Burundi with a monetary union. There wouldn't be an exchange rate risk. This could potentially mean that trade would increase, more in the trading bloc itself. Investors would also invest in these countries, as there would be free movement of goods and labour.

Another benefit of a monetary union would be that with a common exchange rate, things would be more controlled and there wouldn't be as much wage differentials. As there would be more trade, consumer surplus on the goods and services produced would increase. All members of the country would be somewhat equal and could bring the countries closer together. However, different prices may still be likely but they would reduce a big gap that currently exists.

Examiner's comments In this response two benefits and two costs have been considered in the context of the extracts provided. There is some attempted evaluation in the penultimate and last paragraphs. This response gained Level 3 and 7 marks (7/9) for knowledge, application and analysis and Level 1 and 2 marks (2/6) for evaluation. The total for this response is therefore 9 marks (9/15).

7 In 2012, it was estimated that Japan's national debt was equal to 214.3% of its GDP, and Greece's national debt was equal to 161.3% of its GDP.

Evaluate the likely impact of measures which a government could take to reduce the economy's national debt. Refer to a developed economy of your choice in your answer.

(Total for Question 7 = 25 marks)

A government could firstly impose austerity measures in an attempt to reduce the amount the country is spending in order to try and bridge the gap between the amount the country is spending and the amount that the country is generating. The impact of this would be felt on various areas of the economy. Firstly the population would be affected as the government has to make cuts to various services as the national debt means that the government cannot afford to run them in their current state. The result of this is that many people would be likely to lose their jobs, which would in turn result in these people then being productively inefficient for a short period of time as they try and find new jobs. However the negative trade off of these people losing jobs in less than the positive trade off of money being saved by not paying their wages.

Another thing the government could do to reduce the national debt would be to increase taxation. This would help to reduce the national debt as it would increase the amount of money that the collect would collect which would therefore result in the difference between the amount of the money the government generates and the amount it spends decreasing. Additionally, regarding income tax if the government were to tax the highest income earners a large amount then it would more successful for them as the amount of money that they would generate would increase. However the caveat to that can be seen in what happened with the French government when they imposed a top level taxation rate of 70% on the highest income earners. After the French government placed this tax burden the majority of the highest income earners, decided to leave the country as they were not prepared to give 70% of their tax to the French government and, due to their being very rich were easily able to move to a different country where the tax level was not so high. Thereby taxation has its benefits in the short term for reducing the national debt however its potency can be negated in the short run.

Examiner's comments This response explores two methods of reducing the national debt of a country and includes some evaluation of each. However, greater depth and breadth is required in both analysis and evaluation to secure higher marks. This response gained Level 2 and 7 marks (7/16) for knowledge, application and analysis and Level 2 and 4 marks (4/9) for evaluation. The total for this response is therefore 11 marks (11/25).

Question 8

Response 1

8 Over the past 25 years, income inequality has been increasing in many developed countries. For example, from 2007 to 2011 Spain's Gini coefficient rose by 6.0 percentage points, and Ireland's by 6.6 percentage points.

Evaluate the factors which may have caused this **increase** in income inequality. Refer to a developed economy of your choice in your answer.

(Total for Question 8 = 25 marks)

There are a number of factors that could have caused the amount of income inequality to have increased between the years of 2007 and 2011. The first of these is obviously the financial crisis which occurred in 2008. The reason for this having an impact on income inequality is that the financial crisis will have affected people in many different due to not all industries being affected and with some industries being affected at different levels. However the overarching theme is that people who may have been originally had modest incomes with modest savings maybe have been affected by the financial crisis due to the main income earner losing their job for example as was common in countries such as Spain who, even in 2014 still have very large problems surrounding the high level of unemployment. This then results in more people become poorer due to loss of income and therefore the disparity in income or the income inequality increases as there are a smaller amount of the population who are considered to be rich and a larger amount that are considered to be poor, due to the financial crisis.

Another reason as to why income disparity has increased between the years of 2007 and 2011 is due to difference between the rise in prices, or inflation, and the rise of wages. Despite the fact that during the years of 2007 and 2011 inflation was fairly low, the amount by which wages rose was even less with the majority of workers having wage freezes throughout this period, mostly brought on by the economic problems caused by the financial crisis. This therefore causes more disparity in the income earned by the population as it is clear to see that not everyone will be affected by this. The "mega-rich" will always keep on getting rich no matter what the state of the economy, which therefore leaves a small minority who are unaffected by these economic problems. However the majority of the population are not immune to changes in the economic welfare of the country therefore when the economy of the entire country does not do well then their incomes will suffer as a result. Therefore meaning that the gap between the incomes of the richest and the poorest will increase and the amount of people who fit into each category with less people being in the "rich" category" and more people being in the "poor" category due to their rise in wages not keeping up with the rise in prices meaning that they are becoming steadily worse off, year after year.

Examiner's comments This answer explores two reasons for the increase in inequality but there is no effective evaluation. The addition of a Lorenz curve would have supported the analysis. This response gained Level 2 and 8 marks (8/16) for knowledge, application and analysis and 0 marks for evaluation. The total for this response is therefore 8 marks (8/25). The evaluation could include a discussion of the Global Financial Crisis and recession as reasons why we would have expected inequality to reduce, and suggest reasons why this did not in fact do so. This is a rich area for using recent knowledge of important economic events.