Economics

AS / A Level | AQA | 7135/7136

2015 specification
first exams in 2017 (2016 for AS)

Data Response Case Studies Volume 2 (2023)

for AS / A Level Year 1 AQA Economics

3.2: Macroeconomics

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POD 12146

Contents

Teacher's Introduction

The case studies in this series are designed to support students as they study AS / A Level Year 1 Macroeconomics. These case studies cover the AQA specification perfectly, and are designed as real-world contexts to complement the theoretical content of the module.

> **Remember!**
> Always check the exam board website for new information, including changes to the specification and sample assessment material.

Each case study contains:

- **Contextual information:** this is the body text of the case studies, providing the relevant information, facts and figures.
- **Data:** each case study contains data presented in a graphical format.
- **Use the data questions:** for each case study, students are presented with questions set in response to the data presented. Answers are included.
- **Test your knowledge questions:** for each case study, students are presented with questions designed to mimic short-answer examination questions. Answers are included.
- **Extended-response question:** for each case study, students are presented with a question designed to mimic long-answer examination questions. Possible answers are included in summary form.

This resource is designed to be useful to students of all abilities. Students of the highest ability require up-to-date contextual information for use in examination, while for lower-ability students these case studies may complement class activity and help to ground theoretical content in real-world contexts.

These case studies are designed to be up to date for 2023 and provide as contemporary a snapshot of economic discussion as possible. However, it is likely that some themes which are relevant and topical at the time of teaching may not be included. It is therefore advised that these examples are used in tandem with the study of the most recent themes.

I hope this resource can contribute towards an engaging and rewarding learning environment. Best of luck with your teaching!

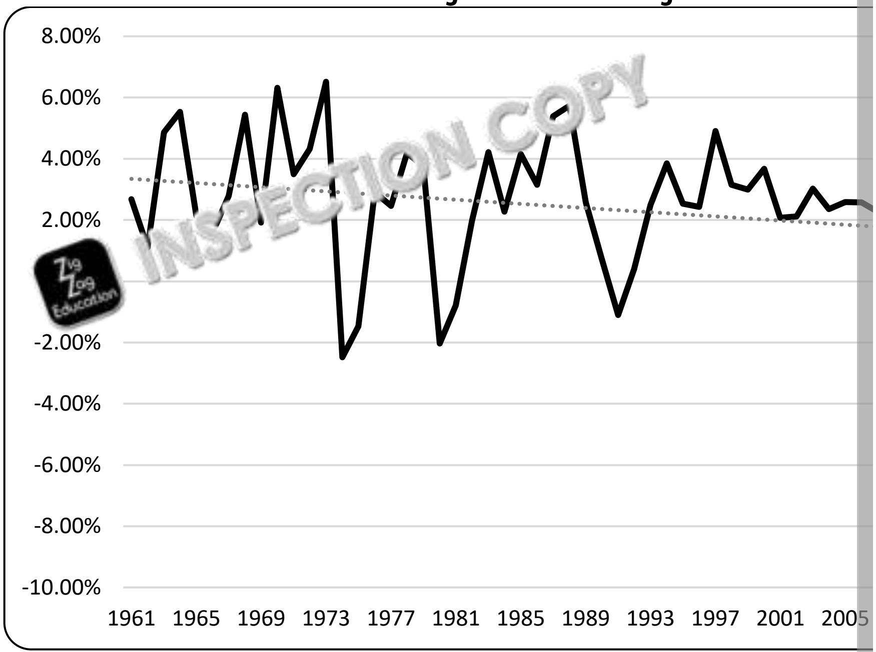
April 2023

Economic growth: in permanent de

Economic objectives; Economic growth

Perhaps the primary measurement of performance in macroeconomics is economic g
amount of economic activity that has taken place in an economy over a year, and the
activity is increasing. **Figure 1** shows the annual percentage of economic growth in th

Figure 1: Annual UK growth



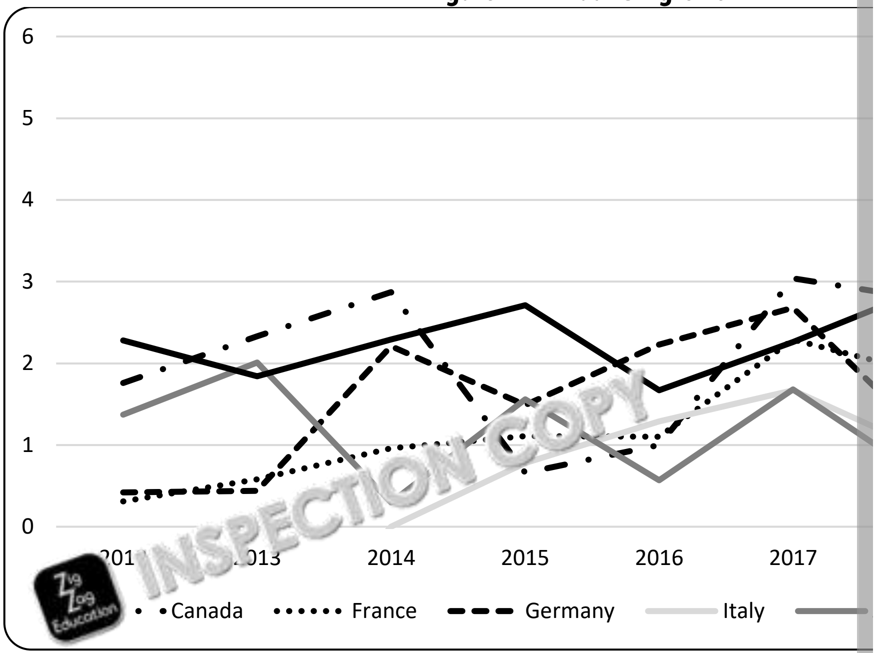
Since the global financial crisis of 2007 to 2009, economic growth in the UK has rem
historically gross domestic product would frequently exceed 3% growth over a year, a
this high has not been achieved since 2003 (with the exception of the post-pandemic
during the 2010s, economic growth averaged out at just under 2%.

At the same time, the depth of recessionary periods has become more acute. By mos
UK's economy had not truly recovered from the financial crash before it was plunged
coronavirus pandemic.

There are a number of possible reasons for these trends. Some economists argue tha
of investment over the last decade which has led to low levels of productivity, and cre
growth. Others argue that the UK in particular has become more unequal in recent ye
consumption and suppresses growth.

However, others still point out that the stagnation is not unique to the UK, and can be
economies. **Figure 2** (overleaf) shows the growth rates across the other G7 highly ind
2012 and 2019 (before the coronavirus pandemic hit). It shows that economic growth
board in the ... after the global financial crisis, and the UK – while not the best per
the most slu

Figure 2: Annual G7 growth



Measuring and forecasting growth is key to making decisions on fiscal policy. Expans
part of sustaining or resuming economic growth. However, critics argue that predicti
notoriously difficult, so basing spending decisions on forecasts is a risky move. This i
globalised economy, in which interconnected national economies are more vulnerabl
economic contagion.

Use the data

1. Briefly describe how Figure 1 would change if nominal GDP figures were used GDP figures.

2. The UK's GDP in 2019 was $2.83 trillion. The economy shrunk by 9% in 2020 What is the UK's GDP at the end of 2021?

Test your knowledge…

1. Define real GDP.

2. Explain **two** alternative measures of economic growth and how they differ fr

Extended-response questi

1. 'Once …tion size and inflation are accounted for, GDP is a good measure succes… economy is.' With reference to the UK economy, evaluate this

Inflation returns: rising prices in a slowi

Economic objectives; Inflation and deflation

Until the 2020s, inflation had become something of a historical phenomenon, associa
The 1990s, 2000s and 2010s had seen inflation brought down to manageable levels,
throughout much of the 2010s. Yet following the exogenous shock of the coronavirus
spike in gas prices caused by the Russian invasion of Ukraine, inflation made a drama

Figure 1: UK inflation

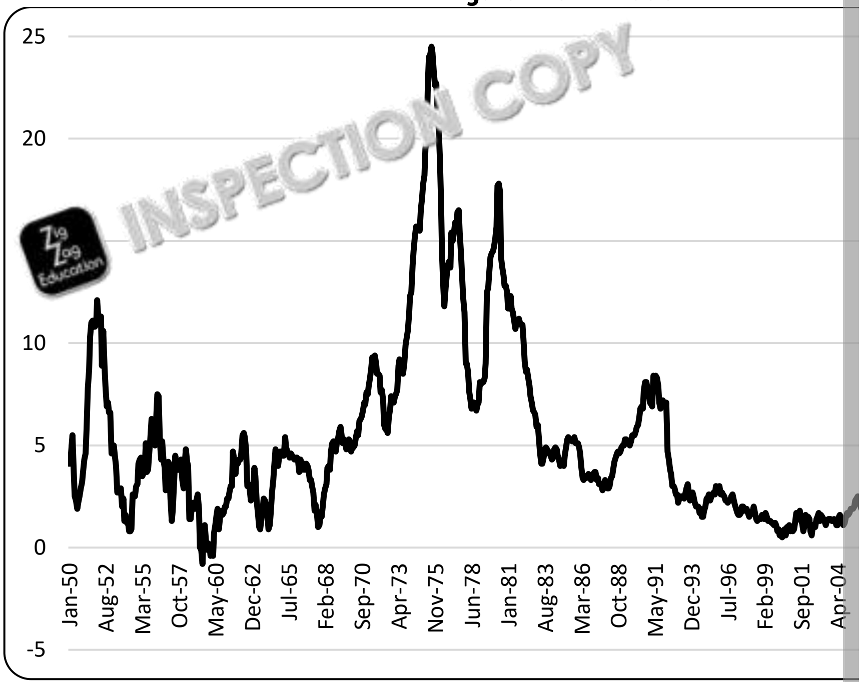


Figure 1 shows that in 2022 inflation exceeded 10% for the first time since 1981, acc
Index. The CPI measures a basket of everyday goods, such as groceries, clothing and
rate at which prices are increasing.

But the CPI is not the only measure used to capture inflation. The Retail Price Index usually records a higher figure of inflation as it includes in its basket of goods the cost of mortgages, interest payments and council taxes. Therefore, while the CPI recorded an inflation rate of 10.1% in July 2022, the RPI measured inflation at 12.3%.

Under these circumstances, macroeconomic orthodoxy tells us to raise interest rates in order to stem rising inflation. However, rising interest rates have the effect of slowing demand across the economy, and if growth is already low, it can potentially trigger a recession.

This is precisely what happened on 4th August 2022, when the Bank of England annou
rates rise for [illegible] years – an increase of 0.5% – alongside gloomy predictions of a sus
By making this decision, the Bank is essentially prioritising reducing inflation over an
growth. This is a reversal of what had become the norm in macroeconomic policy: co
growth had become the main focus.

It is wise for policymakers to therefore be cautious when relying on measurements of
lead to highly damaging results across the economy.

Use the data

1. In 2022 UK inflation reached its highest level in how many years?
2. In what year did the UK last experience deflation?

Test your knowledge...

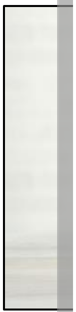
1. Explain why the UK stopped using the Retail Price Index as its official measur
2. Give **two** examples of deflationary policies.

Extended-response question

1. Using a suitable diagram, explain how commodity prices can cause inflation.

Full employment or underemploym

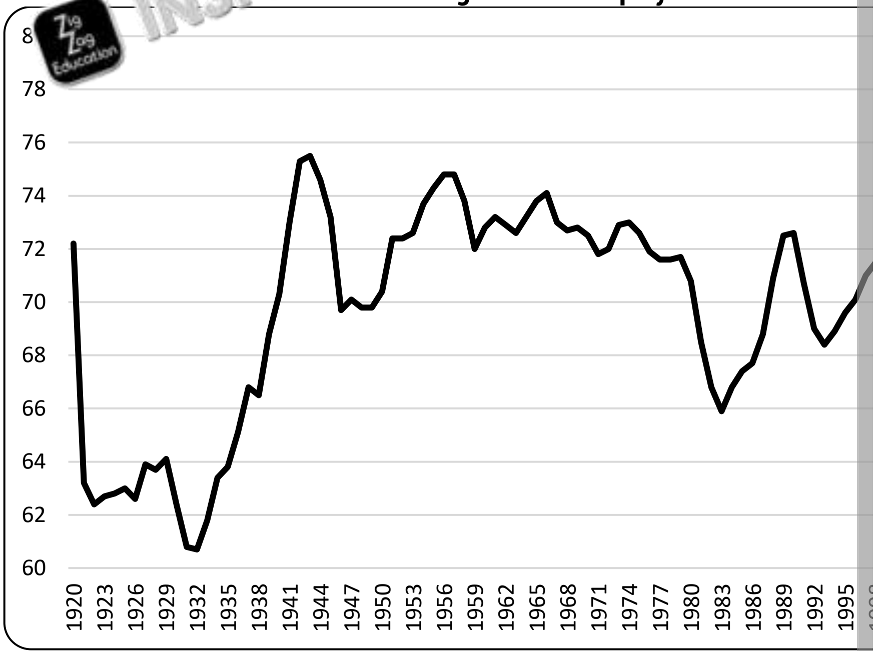
Economic objectives; Employment and unemployme



Unemployment can be one of the most persistent and damaging economic problems. Some Eurozone countries, such as Spain and Italy, have experienced eye-watering levels of youth unemployment since the financial crisis of 2008 – leading to fears of a 'lost generation'.

The UK was also buffeted by a spike in unemployment following the crash, as shown in **Figure 1**, but since then a rather different story has played out. The UK's employment rate has consistently grown to the highest it has ever been – peaking at 76.5% in 2020. Even the impact of the coronavirus pandemic had only a minimal effect on the record high employment trend.

Figure 1: UK employment



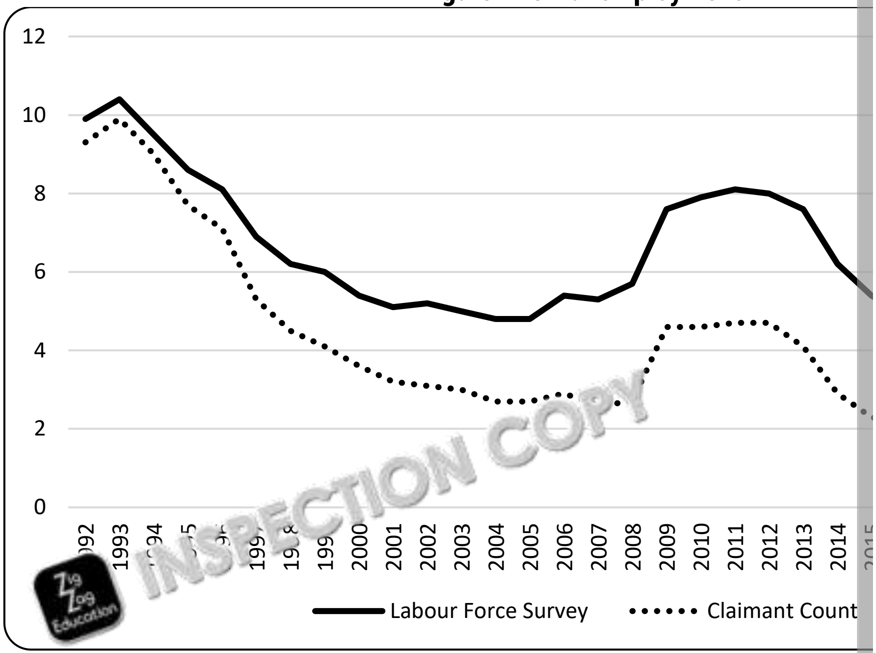
The figures look impressive on the surface, but they don't appear to tell the full story. record highs, poverty has been increasing, productivity stagnating and real wages fal

One answer is that, while more people are in work than ever before, their jobs are less remunerated than in previous eras. We can see a correlation between the rise in empl a relaxation of labour rules in the economy in order to encourage more 'flexible' worki implementation of a more flexible labour market was intended to restore profitability as well as reduce what were then rising levels of unemployment.

Reforms to employment policy between 2010 and 2015 included removing restrictior permitting more flexible employment contracts, reducing regulation around the hiring making claims for unfair dismissal more difficult, removing the compulsory retiremen enforcement around employment rights. In 2013, the Department for Business Innova labour market as 'one of the most lightly regulated labour markets in the world'.

While boosting employment figures, this approach also risks creating underemploym would like to work more hours than are available to them. Flexible labour is utilised p and social care sectors, though present across the economy. **Figure 2** demonstrates a measures, after the new flexible labour rules were introduced.

Figure 2: UK unemployment



Underemployment may be preferable to unemployment statistically, but it can place a
government finances than secure work, as workers on low wages or with few hours ar
from the welfare system.

Use the data

1. Using Figure 1, identify the year which saw the previous highest recorded lev employment prior to 2020. Can you explain why this might be?

2. Using Figure 2
   a. Explain why the Claimant Count measure of unemployment is usually lo Labour Force Survey measure.
   b. Explain why this is not the case in 2020 and 2021.

Test your knowledge…

1. Explain why the unemployment rate could be considered misleading.

2. Figure 1 shows a rise in unemployment numbers dur he financial crisis of two types of unemployment that are likely to ha e aken effect during this ti

Extended-respons uestion

1. Explain   causes of unemployment.

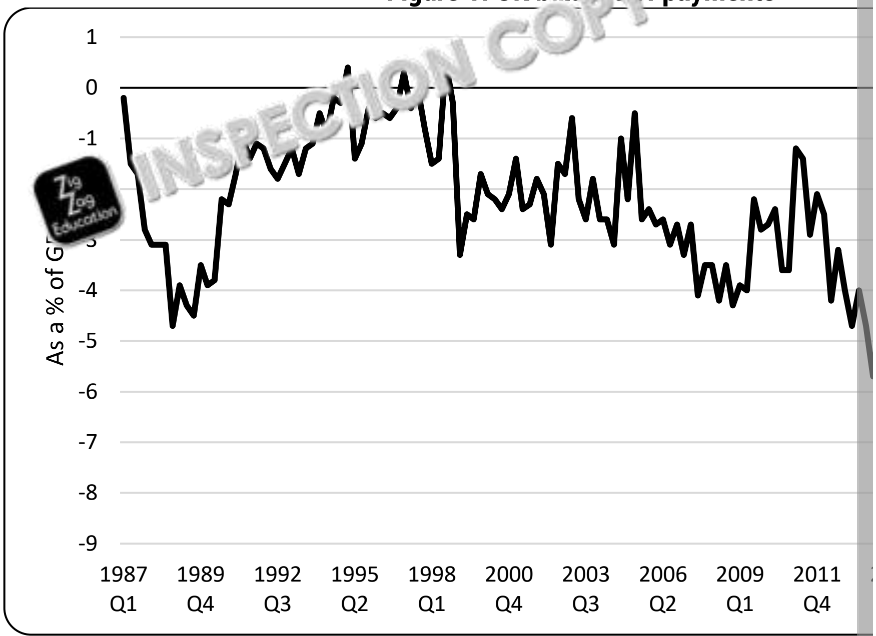
'The kindness of strangers' – running a large cur

Economic objectives; Macroeconomic indicators

In early 2022 the UK posted its largest recorded current account deficit by a large ma
Statistics reported a deficit of £51.7 billion – the equivalent of 8.3% of the nation's e

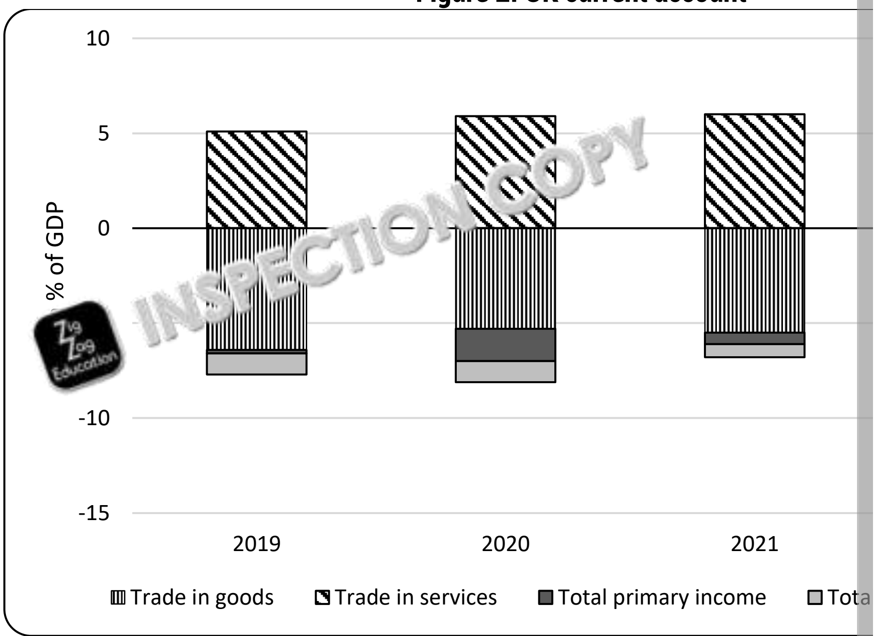
The figure sounds alarming – it is not normal for developed economies to run such la
payments current accounts. But when we look at **Figure 1**, we see that it was only thr
posted its first current account surplus for more than 20 years. So what's going on?

Figure 1: UK balance of payments



The balance of payments current account is chiefly influenced by the extent of impor
economy. However, it also counts inflows and outflows of primary and secondary inc
recent years is broken down in **Figure 2**. The current account can often be volatile be
the currency, which reduces demand for exports and makes imports cheaper, thus cr
The same dynamic is true of a deficit, only the other way round.

Figure 2: UK current account



Current account deficits are not inherently 'bad' in the same way that running current
inherently 'good'. Developing countries may wish to run a current account deficit to i
to improving their productivity in the future. Conversely, countries that rely too heavi
trouble if the price of their commodity falls unexpectedly. In this sense, neither a defi
desirable or problematic.

The problem, however, can be the size of th
over a period of time, and governments are
amounts to maintain them, then this could
payments which disrupt the functioning of
could then spook lenders and make it harde
low rates of interest, which in turn exacerba

Historically, the UK has rarely had a probler
history of repayment on debts and as such
But past performance is not always a guarantee of future success. Former Bank of En
in 2016 that the UK has for a long time relied on 'the kindness of strangers' to keep it

If the UK is borrowing so much that it no longer looks like a stable investment, then thos

Use the data

1. Using Figure 2
   a. Which of the components of the current account appears to be steadies
   b. Which of the components of the current account has contributed most t

2. If the UK's current account deficit in Q1 2022 was £51.7 billion, and this is eq
   GDP, then what was the UK's overall GDP figure in Q1 2022?

Test your knowledge…

1. Explain what is meant by 'total primary income' and 'total secondary income

2. Explain the effect on the current account balance if the value of UK investme
   abroad increased.

Extended-response question

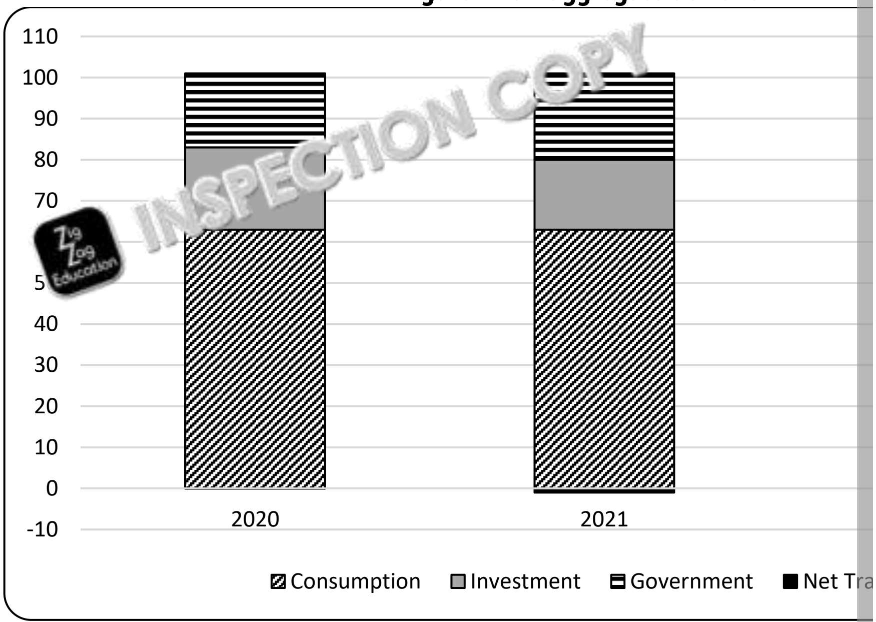
1. Evaluate the effectiveness of investing in one of the UK's export sectors as a
   the current account deficit.

Collapsing consumption during the coronavi

The determinants of aggregate demand

The response to the spread of the coronavirus pandemic had a profound effect on the large parts of the economy closed, and consumers confined to their households, aggr unprecedented extent. This is because the largest component of aggregate demand i that consumption represents 63% to 64% of the UK's total GDP.

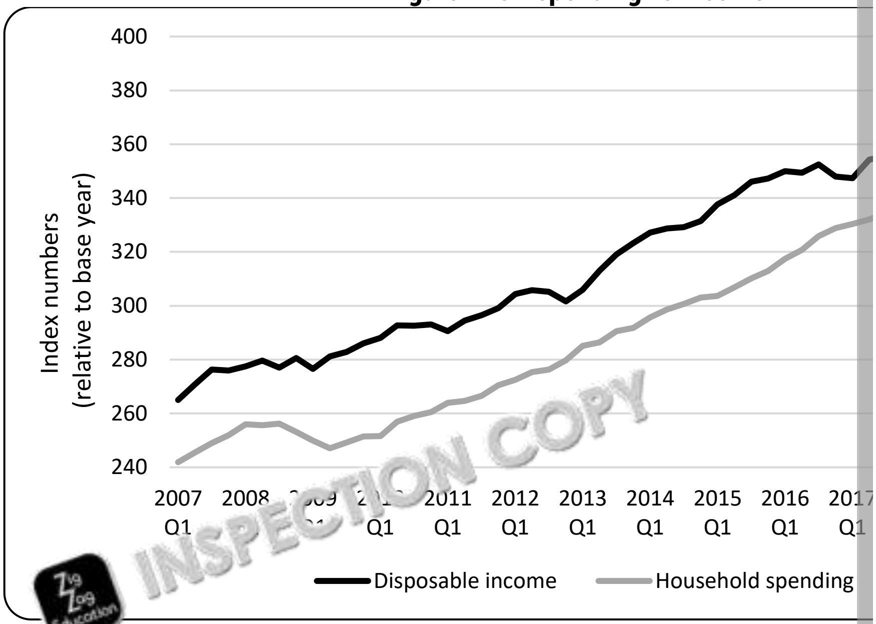
Figure 1: UK aggregate demand



Government intervention during the crisis sought while consumption fell. The main way the governm furlough scheme. This ensured that employed pe value of their wages while they were unable to wo gatherings. In addition, the government also incre unemployed people received through the Univers also reducing barriers to access.

The effect of these interventions can be seen in F spending – or consumption – decreases dramati 2020, disposable income reduces only by a relati

Figure 2: UK spending vs income[1]



However, despite the collapse in consumption overall, some sectors of the economy gr
Essential retail was one beneficiary – in particular supermarkets. As these were some o
open, and one of the few outside activities people were permitted to engage in, footfall

Another beneficiary was online retail. With people forced to stay home, a large amoun
previously take place on high streets moved online. The share of sales conducted onl
30%, in the first months of the pandemic. However, overall sales over the same perio

After the height of the pandemic, household sales rebounded, though, as **Figure 2** sh
2020 levels, demonstrating that reduced consumer confidence remained across the

Use the data

1. Is the data in Figure 1 in real or nominal terms?

2. Take a look at Figure 2. What might account for the small reduction in dispos second quarter of 2020?

Test your knowledge...

1. What is the formula for aggregate demand?

2. Using an AD curve, show the effect of a fall in the rate of VAT.

Extended-response question

1. Explain the relative importance of interest rates and consumer confidence in aggregate demand.

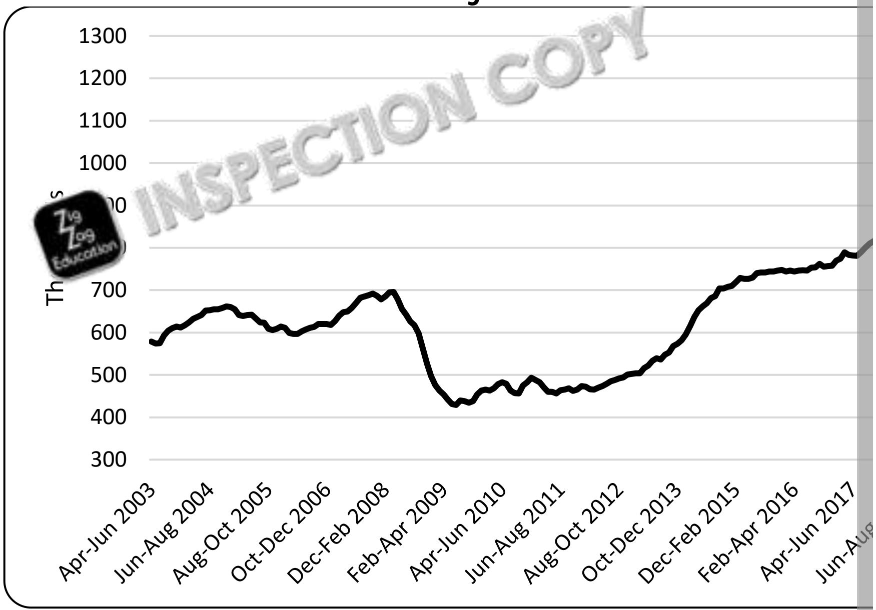
[1] Source: **https://www.niesr.ac.uk/wp-content/uploads/2022/02/UK-Economic-Outlook-Winter-2022.pdf**

Aggregate supply: tightening labour

The determinants of aggregate supply

At the onset of the coronavirus pandemic, faced with a deeply uncertain economic ou
macroeconomy stopped hiring. The result was a collapse in job vacancies, seen in **Fi**
unemployment was prevented by the introduction of the furlough scheme, many spec
high unemployment once the pandemic passed and furlough payments were conclud
opposite happened.

Figure 1: Job vacancies

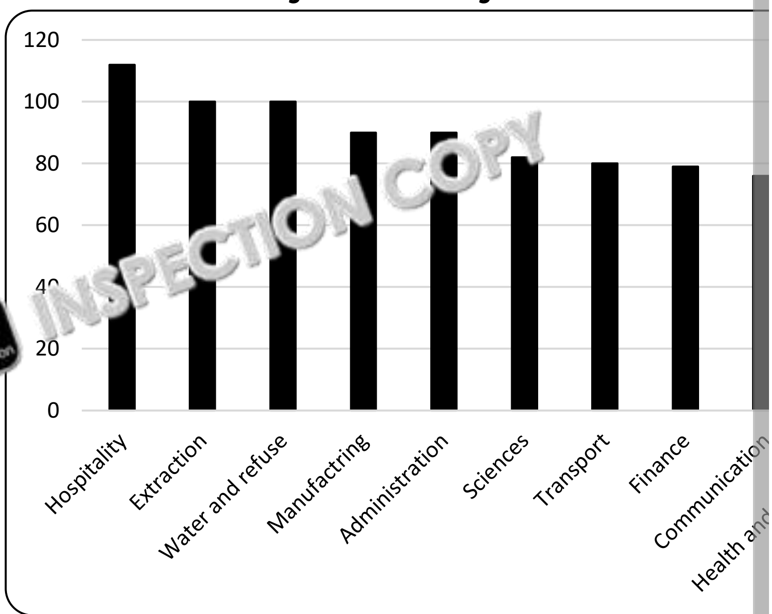


By summer 2020, the number of job vacancies across the economy had almost doubl
pandemic levels, and had reached historic highs. So what happened?

Well, there are a number of factors. Many older workers saw the pandemic as an opp
reducing the overall supply of labour. Many foreign-born workers returned to their ho
pandemic, and may have been less tempted to return to the UK once it was outside o
decreasing labour supply.

In addition, most vacancies were in low-paid or insecure jobs – positions less likely to tempt younger workers back into the labour market. **Fig** shows the industries in which vacancies became the most widespread.

Figure 2: Percentage increase in vacancies



[2] Source: **https://commonslibrary.parliament.uk/how-has-the-pandemic-affected-industries-and-labour-in-**

One high-vacancy industry that caught particular attention in 2021 was road freight. pandemic, a significant shortage of HGV drivers led to supply problems all over the ec

This can be partly attributed to the globa shortages had become commonplace thr economy due to workers being sick with the virus's spread. In addition, the econo pandemic severely disrupted supply chai reorganise their businesses, and changed many more people buying online, more d

But there are also issues specific to the U driver shortage. The industry was already drivers prior to the pandemic, in part due to the work's poor remuneration and unsoci also heavily reliant on 'just-in-time' supply chains, which minimise storage costs but any kind of disruption.

Use the data

1. What macroeconomic phenomena can we expect from a sudden tightening of as seen in Figure 1?

2. Explain **three** reasons why the hospitality industry may have experienced the following the pandemic.

Test your knowledge...

1. Using a suitable diagram, demonstrate the impact of increased demand for la aggregate supply.

2. State and explain two other factors that can increase LRAS, aside from demographic/migration changes.

Extended-response question

1. Using information from the extract and your own knowledge, evaluate the ec a country encouraging higher levels of migrant workers.

Constructing the multiplier: high-speed r

Aggregate demand

The idea of the multiplier effect in economics is quite simple in theory. When there is
economy (such as through government spending, or through spending by foreign tou
economy can be greater than the size of the initial injection. This is because when o
they then spend that money, which increases the income of others, and so on, until th

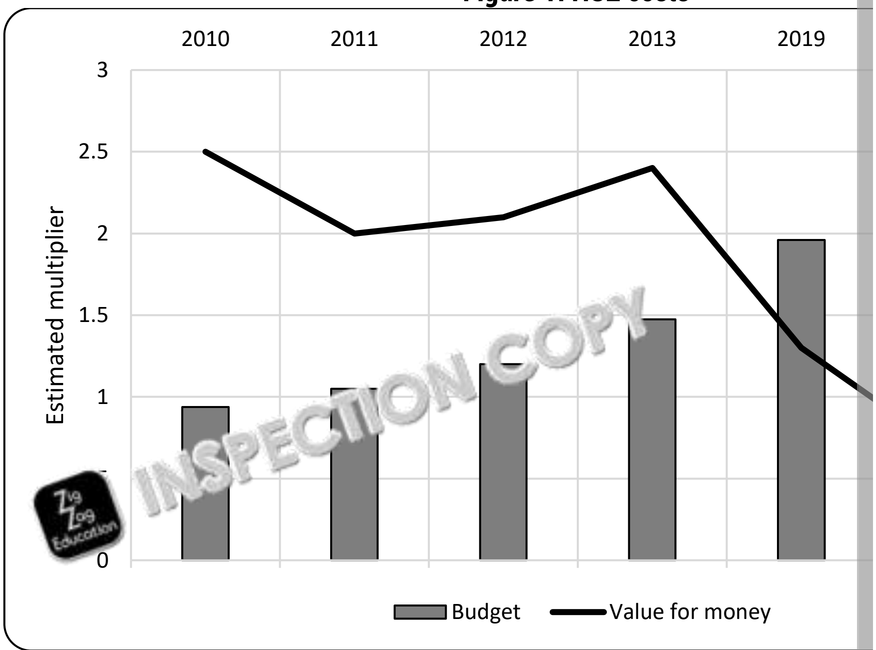
With economic growth and productivity remaining stubbornly low in the UK economy, the focus of policymakers has shifted to how big public investments can help to get the economy moving. One such large investment is the High Speed 2 railway line between London, Birmingham and Manchester.

Some economists believe that transport infrastructure will help to stimulate economic growth and productivity. There are a number of reasons to believe this. Firstly, reduced travel times will allow firms to access more skilled workers for a larger pool of labour. Secondly, greater interconnectedness of ci
services outside of their immediate area more easily. And thirdly, some firms would h
marketplace than previously, meaning their customer base will expand.

In addition, the government claims that 'HS2 stations can act as a multiplier or accele
plans.' This is because the footfall produced by commuters will increase commerce i
business and demand for housing.

However, other economists disagree with this analysis. **Figure 1** highlights how the e
increased considerably across multiple government reviews, from an estimation of £3
At the same time, the black line tracks the estimated multiplier arising from the proje
as costs rose.

Figure 1: HS2 costs[3]

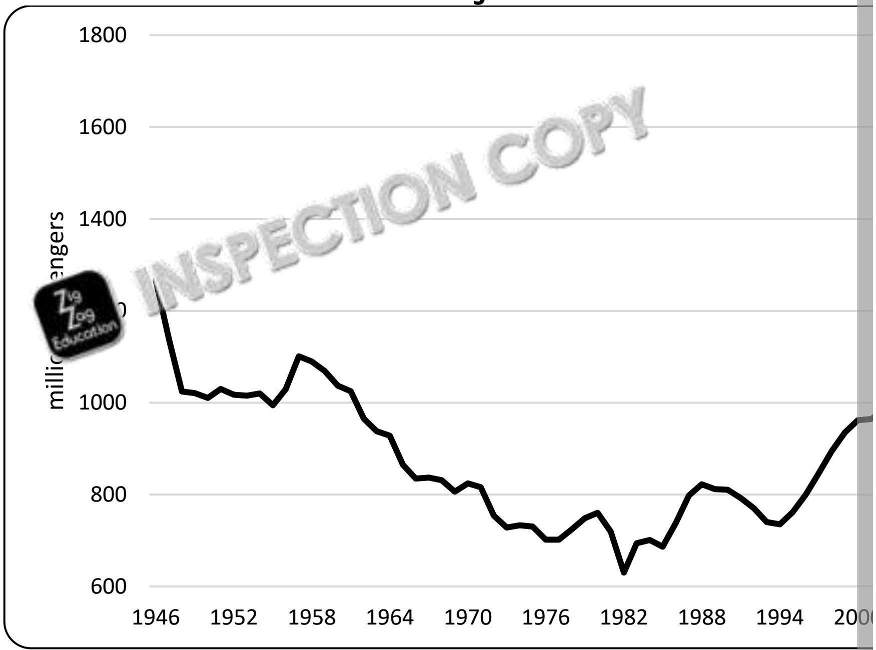


[3] Data **https://www.instituteforgovernment.org.uk/explainers/high-speed-2-costs data**

In Lord Berkeley's unofficial 2020 report on HS2, he estimates that the multiplier for t
0.6, which he regards as 'poor value for money'. This stands in contrast with initial pr
produce benefits worth more than twice its costs.

Supporters of HS2 argue that the project is not just about providing value for money,
the UK's railways. **Figure 2** highlights how rapidly increasing passenger numbers on t
capacity is likely to become a necessity in the years ahead.

Figure 2: Rail demand[4]



The government predict that demand for rail journeys will continue to increase at an a
Since 1994 rail demand has increased on average by almost 5% every year, making 2

Use the data

1. Figure 1 outlines specific estimations of multipliers that have been produced a analyses of HS2. Give three reasons why it is notoriously difficult to make accu
2. The estimated multiplier of HS2 in 2011 was 2. Calculate how many billion po generate at this point in time.

Test your knowledge...

1. Use a diagram to explain why an increase in government spending is expecte to inflation.
2. What is the most important variable in determining the size of the multiplier

Extended-response question

1. Suppose a government wanted to help the economy out of recession by raisi greater government spending. Using your knowledge of injections, withdraw multiplier, evaluate the likely effectiveness of this policy.

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4 Data **https://dataportal.orr.gov.uk/statistics/usage/passenger-rail-usage/table-1220-passenger-journeys/**

5 **https://publications.parliament.uk/pa/ld201415/ldselect/ldeconaf/134/13410.htm**

The 'golden era' of growth

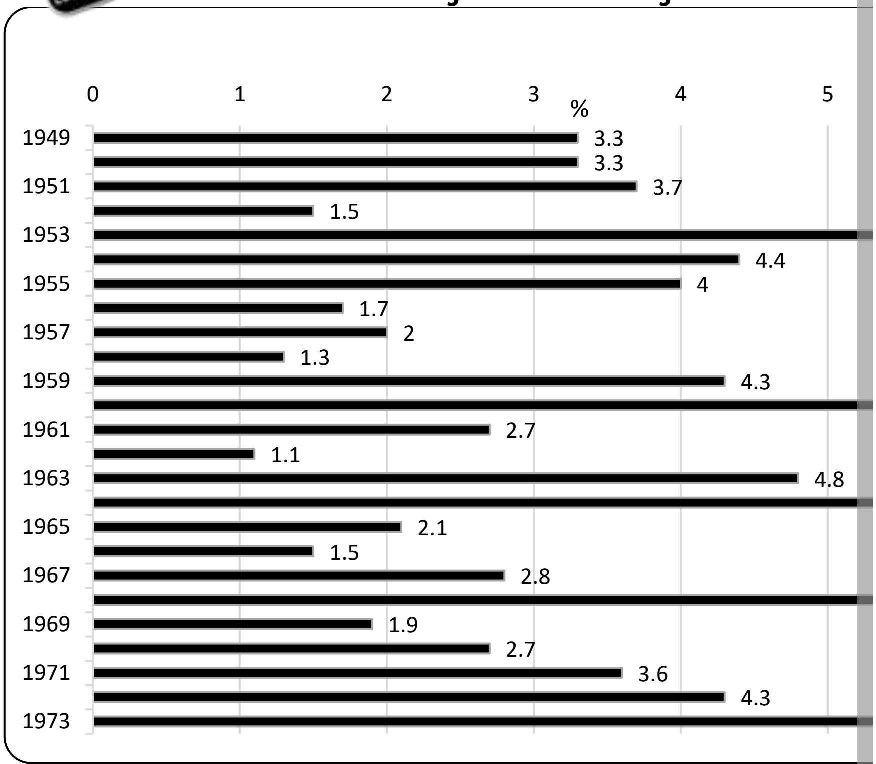
Economic growth and the economic cycle

Between the late 1940s and early 1970s, the UK economy experienced an unpreceder
often referred to as the 'golden era' of British economic expansion. During this period
regularly exceeded 3% as Britain was rebuilt following the destruction of the Second V

The strong growth figures were accompanied by significant improvements in living standards as consumer goods became cheaper, wages rose, jobs were widely available, the welfare state emerged and slums were cleared to make way for modern housing. In 1957 Prime Minister Harold Macmillan famously declared that British people had 'never had it so good'.

Figure 1 shows the exceptionally strong run of growth figures to which the 'golden era' corresponds.

Figure 1: UK annual growth

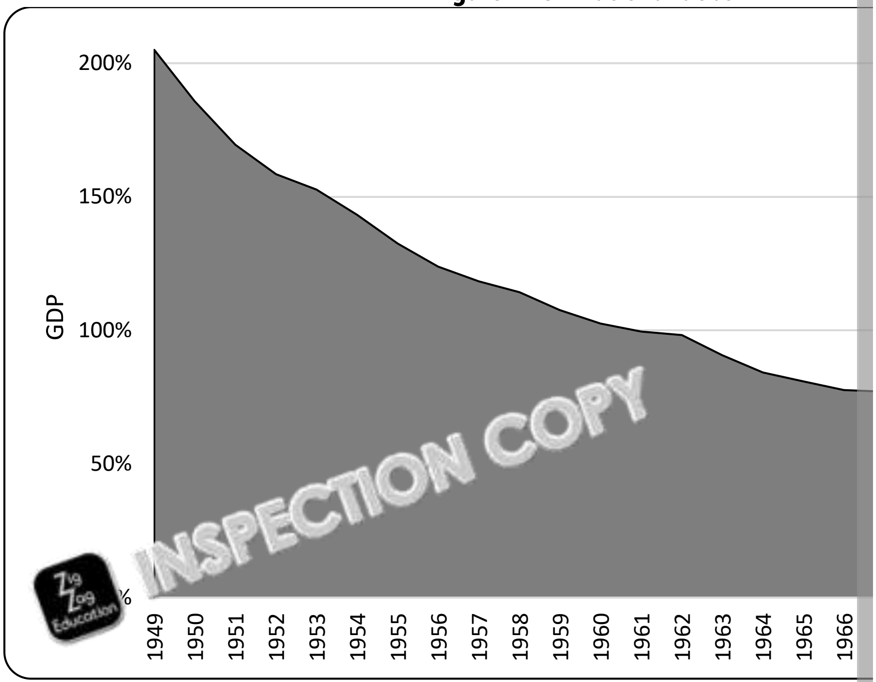


There were a number of reasons why the UK was able to sustain such a long period o
be regarded as the level of job creation associated with post-war reconstruction, and
entering the UK from Commonwealth nations.

The golden era can be regarded as having come to an end when the economy entered
response to international events. Since then the UK has not experienced such a prolo
with the economy slipping into recession on a more regular basis.

One major advantage of this 'golden era' of growth was that it helped to substantially
had accrued while fighting the Second World War. **Figure 2** traces the reduction of na
of 1949–1973. It shows that, following the war, debts were more than 200% of GDP,
50% in just over 20 years.

Figure 2: UK national debt



The Office for Budget Responsibility highlights how 'in nominal terms, debt increased GDP increased by more than 1,200 per cent in the same period. This reduced the debt level to less than 50 per cent of GDP.'[6]

This conforms to a discretionary fiscal policy approach which seeks to be a counterva During periods of expansion, high taxes and low public spending should in theory pro financial reserves needed to cut taxes and increase spending in recessionary periods.

Use the data

1. Explain why the trend in Figure 2 can be attributed to sustained economic gr

2. Using Figure 1, estimate the average annual GDP growth rate of the UK over

Test your knowledge...

1. What is the alternative to 'discretionary fiscal policy'?

2. Using a suitable diagram, explain the difference between short-run and long- economic growth.

Extended-response question

1. Explain the costs and benefits of economic booms.

[6] https://obr.uk/box/post-world-war-ii-debt-reduction/

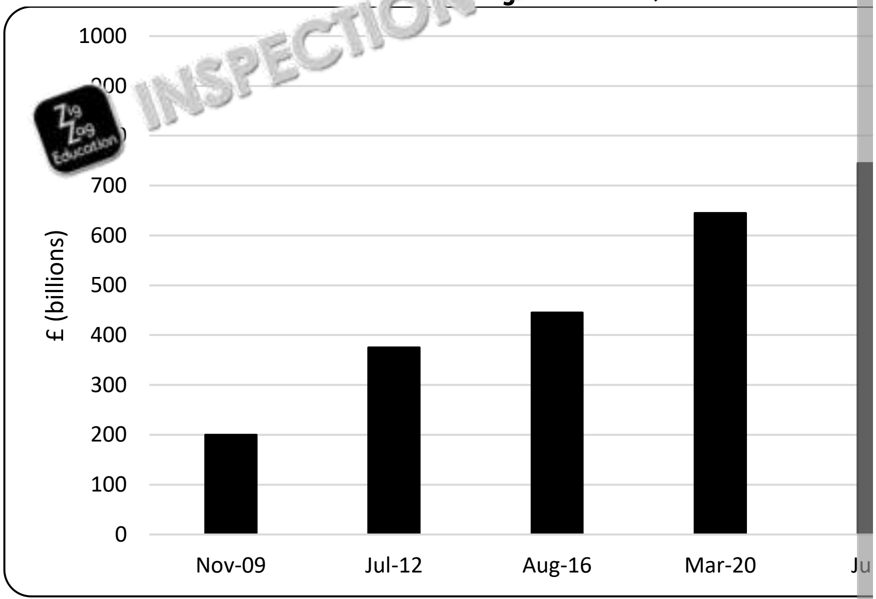
Quantitative easing: the evolution of mon

Central banks and monetary policy

Following the financial crisis of 2007/08, the Bank of England adopted a new form of
quantitative easing, or QE. QE expands the money supply, and does so through the ce
Most of the debts purchased belong to the government, and are also known as gilts. E
money that the bank has created, the money supply expands.

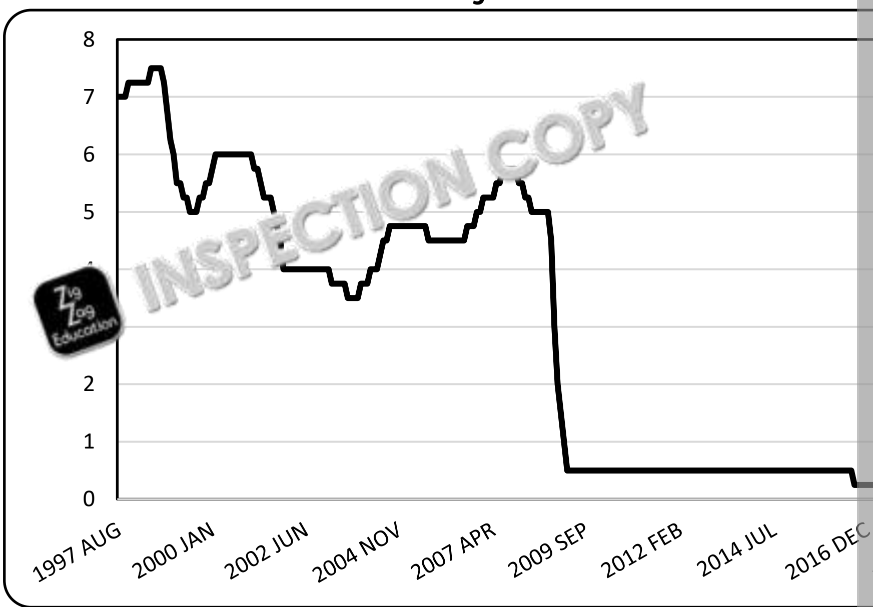
The process of QE was repeated again on two occasions in the 2010s when deflation
And it was rapidly expanded during the coronavirus pandemic, partly as a means to h
crisis. **Figure 1** demonstrates the cumulative cost of QE after each major injection to

Figure 1: BoE QE[7]



QE has been used to achieve multiple monetary and fiscal aims. It was initially introd
tool to try to increase persistently low inflation, as interest rates could not be lowered
in the Bank of England was that the money entering the national income would help t
encourage banks to lend in a weaker economic environment. **Figure 2** shows how far
lowered interest rates in this period.

Figure 2: Interest rates



[7] **https://www.bankofengland.co.uk/monetary-policy/quantitative-easing**

There is no consensus among economists as to how successful this was. Inflation mostly remained below the Bank's 2% target, but some argue that QE helped to prevent more damaging deflation. QE was also criticised at the time for increasing levels of wealth inequality in the UK by inflating the price of assets, such as housing.

QE was subsequently used in 2016 with the aim of stabilising markets following the UK's decision to leave the EU. And during the coronavirus pandemic crisis, large amounts of QE took place alongside high levels of government borrowing, which were required for high-cost fiscal interventions such as the furlough scheme.

Initially planned as a short-term and one-off interventi[illegible] has become a major po[illegible] alongside the setting of interest rates. Since 20[illegible], [illegible] Bank of England has started t[illegible] accrued during the several rounds of [illegible] such a process remains subject to c[illegible] macroeconomic impact.

Use the da[illegible]

1. Which is the single biggest injection of QE highlighted by Figure 1?

2. Explain why the Bank of England may have started offloading its QE debts in [illegible]

Test your knowledge...

1. Give **two** reasons why the UK inflation rate might have been falling (Figure 1)

2. Explain why deflation might be damaging for an economy.

Extended-response question

1. Assess the effectiveness of lowering interest rates to stimulate economic gro[illegible]

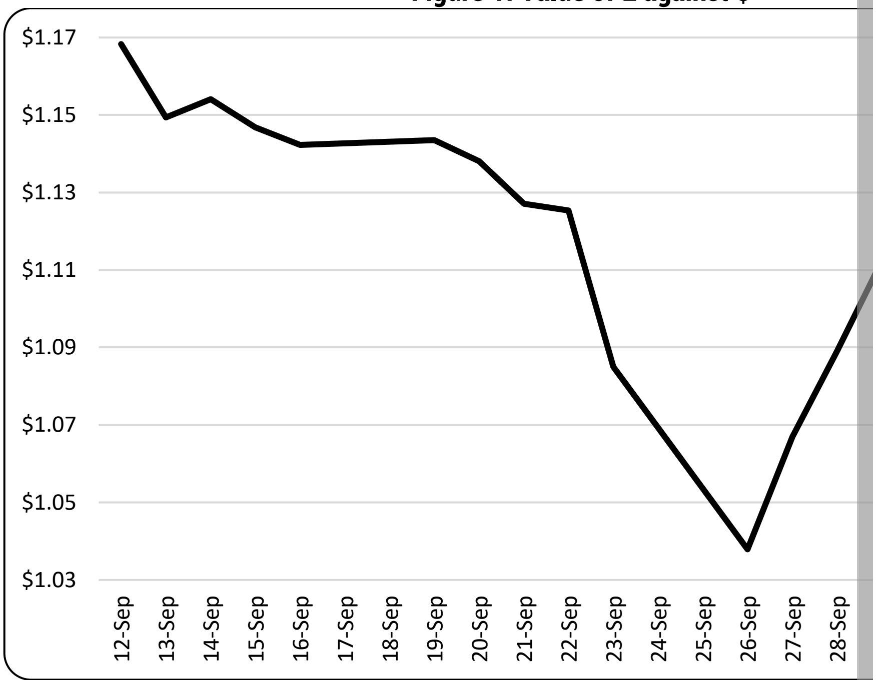
Fiscal misadventure: Truss's tax ga

Central banks and monetary policy

In September 2022, the recently elected British Prime Minis Kwasi Kwarteng announced a range of large public spendin to £100 billion was announced to cover the energy costs of followed by a further £45 billion worth of tax cuts, intended range of individuals and businesses and generate economic Responsibility, responsible for explaining how public expend permitted to issue any public information about how the mo be raised.

The reaction of financial markets to the latter announcemen devastating. Traders, spooked by the enormous unfunded sp doubt whether Britain would be able to continue paying off its debts, and lost confide governance. As a result, many started selling their UK financial commitments. This re of the British pound, seen in **Figure 1** against the US dollar.

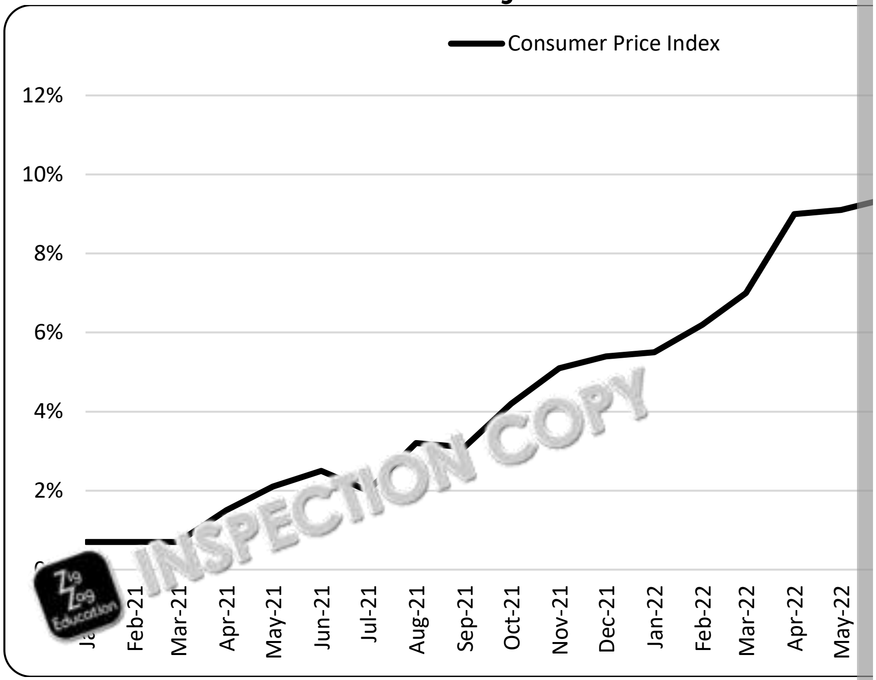
Figure 1: Value of £ against $



At the same time the price of government debt – its value on bond markets – also fel source of investment in government debt is pension funds, so as the bond market be pensions start to be put at risk. Eventually the Bank of England stepped in when pens about to collapse. The central bank spent £65bn buying government debt, which help and also restored some of the pound's value.

But the emergency intervention by the central bank also added to the inflationary pres economy, highlighted in **Figure 2**. The prospect of large interest rate rises severely af many homeowners relying on low interest rates in order to keep up with their paymen offers were withdrawn at the peak of the crisis.

Figure 2: Inflation



Eventually, the political pressure that resulted from this combination of financial scar reverse their expensive policies, and ultimately pushed them both out of office. But it important maintaining the confidence of financial markets is to the functioning of a n boundaries of plausible macroeconomic policies lie.

Use the data

1. The pound started 2022 at a value of $1.35. How much of its value had it lost

Test your knowledge…

1. Identify **two** factors which influence the Monetary Policy Committee's decisi
2. Explain **two** consequences of a currency depreciation.
3. Using a suitable diagram, explain how tax cuts could generate economic grov

Extended-response question

1. Explain the increasing role of the central bank in managing the UK economy.

Expansionary fiscal policy: eat out to

Fiscal policy; Aggregate demand

The hospitality industry was among the worst affected sectors of the UK economy during the coronavirus pandemic crisis. With the population forced into their homes, bars, restaurants and cafes had virtually no means to generate revenues which could cover their core maintenance costs, and many ended up in a perilous financial position.

As the spread of the virus appeared to dissipate during summer 2020, the government launched an unusual fiscal stimulus policy to support the industry. The 'eat out to help out' scheme subsidised food and soft drinks in hospitality venues by 50% every Monday to Wednesday for the whole of August. **Figure 1** shows the increasing popularity of the scheme over the course of the month, based on the money spent by the government.

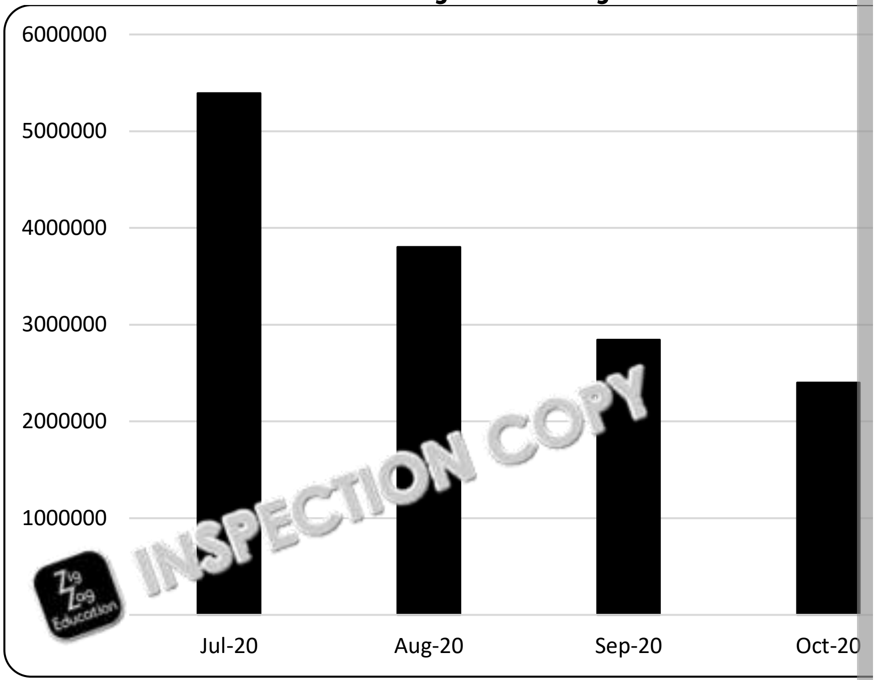
Figure 1: Subsidised meals

The overall cost of the scheme was £840 million, significantly greater than the £500
government. The aim of the government was to boost overall aggregate demand in th
recessionary pressures as the UK left lockdown. The government were anxious that p
public spaces, and demand would continue to be suppressed due to the public having
to save.

Research conducted by the London School of Economics, or LSE, suggests that the sch
aggregate demand relative to the costs involved. The LSE concluded that it did not boo
designated discount periods, and there was no evidence to suggest that it encouraged

However, the government argues that the scheme was effective at keeping strugglin
prevented them from laying off staff, by providing them with much needed revenue. I
scheme helped to reduce the cost of furlough, given that the hospitality industry was
subsidies wages during the pandemic. **Figure 2** (overleaf) shows the number of empl
and November 2020.

Figure 2: Furloughed workers



In addition, some studies found that the scheme may have contributed to the increas virus. Increased transmission meant that restrictions on social gatherings began to b mid-September, less than two weeks after the scheme ended.[8]

Use the data

1. What does the take-up of the scheme indicated in Figure 1 tell us about the p for the services provided by the hospitality industry?

2. Take a look at Figure 2. Does it indicate that the 'eat out to help out' scheme r employees furloughed?

Test your knowledge...

1. Explain how expansionary fiscal policy correlates to the economic cycle.

2. Give **two** examples of supply-side policies which could result in supply-side in

3. Show the effect of fiscal stimulus on AD using a Keynesian AD/AS diagram.

Extended-response question

1. Evaluate the effectiveness of using demand-side policies to stimulate econom

[8] **https://cep.lse.ac.uk/textonly/_new2014/news/releases/2021_02_10_i394.pdf** LSE study

Indirect taxation: Hospitality's VAT h

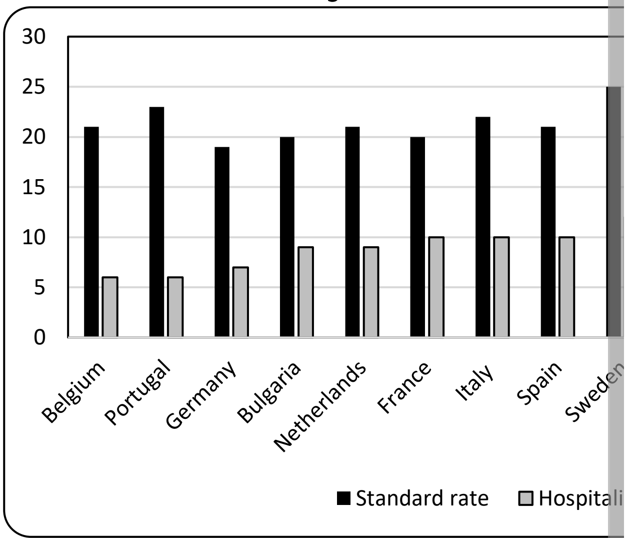
Fiscal policy

At the height of the coronavirus pandemic crisis in July 2020, the UK government made the decision to give the hospitality and tourism sector a 15% cut in value added tax (VAT), a duty on goods. Whereas the standard rate of VAT is 20%, government would reduce this rate to just 5%. This would be to help support a sector that was particularly hard hit by the closure of large parts of the consumer economy. A lower rate of VAT remained in place for the industry until March 2022.

The VAT cut enabled providers to choose either lowering their prices or retaining the extra 15% of sales for themselves. Some pubs chose to reduce the price of their alcoho did not apply, and recoup those losses by raising their food prices, in the hope that

While these measures were temporary, many in the hospitality and tourism sector bel should be lowered permanently. One reason for this is that many other European cour domestic hospitality sectors, as seen in **Figure 1**. In addition, the industry is highly pr large employer.

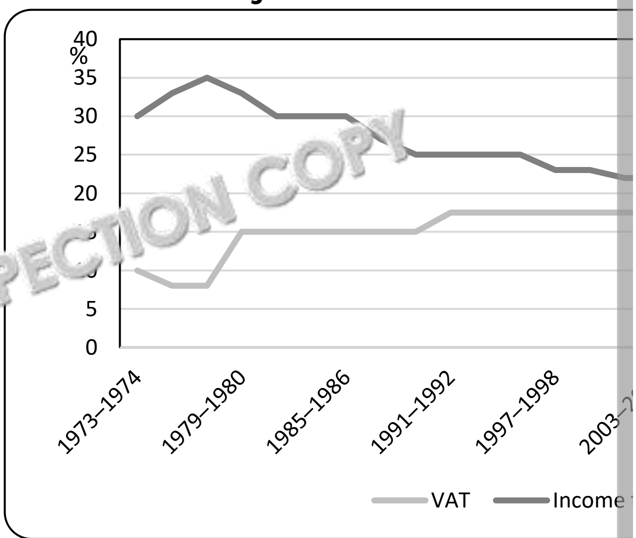
Figure 1: VAT rates across E



However, VAT exemptions are controversial and their economic benefits contested. Critics point to the increased administrative costs of such schemes, and argue that instead of offering a range of special reduced rates, the economy would be better off with a lower standard rate.

VAT was first introduced in the UK in 1973 at a rate of 10%. In 1978, VAT generated 7% of the UK's revenue – this figure had more than doubled by the 2000s, making it a key source of government revenue. But higher prices also suppress consumer demand, which in turn can mean less employment and lower profits – all of which reduce government revenue in the long run. **Figure 2** shows how income tax has fallen as VAT has increased.

Figure 2: Historic UK rates of VAT a



[9] Source: **https://www.ukhospitality.org.uk/blogpost/1721400/392803/VAT-Rates-for-Hospitality--Leisure**

Use the data

1. What is the median VAT rate of the 14 European countries in Figure 1, and h compare to the UK?

2. Give **two** reasons for trends of taxation displayed in Figure 2.

Test your knowledge...

1. Explain why the hospitality and tourism sector is price sensitive.

2. Using a diagram, explain the welfare loss ass ciа e with VAT on hospitality

Extended-respons

1. Explain sts and benefits of indirect taxation.

Answers

Economic growth: in permanent decline?

Use the data

1. Nominal GDP figures do not account for the effect of inflation, so GDP figures appear positive in the UK). Therefore, the GDP growth figures would be higher (also the rec Visually, the graph would appear to have shifted up.

2. The economy shrunk by 9% in 2020 – 9% of 2.83 is 0.25. 2.83 – 0.25 is 2.58. The econ 2.58 is 0.18. So 2.58 + 0.18 = 2.76. The answer is $2.76 trillion.

Test your knowledge...

1. GDP is the total value of output (or goods and services) produced in an economy (wit the effect of inflation has been removed.
   Award 1 mark for a corr[illegible] for a partially correct definition, 3 for correct defi

2. One alternative measure is gross national product (GNP), which measures total dome GDP, but includes property income received from foreign nations. Unlike GDP, G foreign multinational corporations. Another alternative measure is gross national inc nation's total income, rather than output as with GDP. GNI is the sum of all the mone who are domestically resident.
   Award 1 mark for identifying each alternative measure, and 1 further mark for explai

Extended-response question

1. GDP measures the total value of output in an economy. When you adjust for popula inflation (real GDP) this can give a good impression of the *size* of an economy. Howe compare the *success* of different economies, many important factors are omitted:
   - **Living standards**. It can be more informative to adjust GDP using the concept o account for different living standards in different countries (PPP should be clear Accounting for living standards tends to narrow the perceived gap between rich are usually relatively cheap in poorer countries.
   - **Inequality**. Even per capita GDP figures give no indication of the distribution of experience rapid economic growth, but this would not benefit the general popu to a small elite.
   - **Negative externalities**. GDP only measures the total value of output, it doesn't 'bad' output. Economic growth may come hand in hand with environmental da of land for commercial purposes.
   - **Happiness**. Having a higher average standard of living does not guarantee that end up working excessively long hours and spend less time with their families. wealth increases happiness up to a point – but increasing wealth beyond that p This is notoriously difficult to measure, however.

   Strong answers must include reference to the UK economy such as the respondent's information and data included in the case study.

   In your answer you could also make reference to 'composite' indicators such as the H of factors before comparing countries' performance (with respect to economic devel that GDP does not account for the size of the 'black economy' (unrecorded or illicit e greatly [illegible]n countries. A good answer should explain at least two or three of th

Preview of Answers Ends Here

This is a limited inspection copy. Sample of answers ends here to stop students looking up answers to their assessments. See contents page for details of the rest of the resource.