



Starters and Plenaries

for OCR AS and A Level Year 1

Macroeconomics

Second Edition, February 2022

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Teacher's Introduction

This resource is essentially an activities-only resource that has been designed to support the learning and teaching of AS and A Level OCR Macroeconomics. These useful activities will help to either switch pupils into learning mood at the beginning of the session or wind down and take learning right up to the end of the lesson. Students will build on their understanding of key terms while developing new knowledge that is integral to the specification.

There are 23 activities in this resource, which closely follow the specification order, and can be conducted as individual, group or full-class activities. Teacher's notes, plus an activity-by-activity plan, are provided at the beginning of the resource to give guidance on how to teach the content. Some of this guidance includes additional activities. Here is an example:

Spec. Area	Topic	Activity Description	Notes				Extra Resources	Assessment Objectives				Suggested Use
								AO1	AO2	AO3	AO4	
1.1 Nature of Economics	What is economics?	Activity 1 – fill in the missing words followed by a cut out and paste activity.	Individual tasks (but can be done in pairs as well, where students can compare their answers).	✓	✓		Scissors and glue.	X	X			Plenary

The starters and plenaries included are designed to help teachers prevent any breaks in students' learning by encouraging them to recap previously studied topics or begin to learn new ones. Each activity sheet should take between 10 and 20 minutes to complete. The end of the resource includes an answer sheet for students and/or teachers to use in marking.

It is hoped that this resource, as well as offering support for teaching the essential elements of the OCR examination, will help students build on any knowledge they already have.

Happy teaching!

December 2017

Update: Second Edition, February 2022

Minor updates to match 2019 specification: rearranged order of activities, removed non-specified questions and moved activities on trade, exchange rates and the economic cycle that were previously part of the A2 resource.

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* resulting from minor specification changes, suggestions from teachers and peer reviews, or occasional errors reported by customers

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Activity-by-activity Plan

Spec. Area	Topic	Activity Description	Notes	Individual	Group	Extra Resources	Assessment Objectives				Suggested Use
							AO1	AO2	AO3	AO4	
Aggregate Demand and Supply	Circular flow of income	Activity 1 – completing the circular flow of income chart and assessing the importance of withdrawals and injections.	Individual activity. Task 2 can be done in pairs for comparing results.	✓	✓		X		X		Plenary
	Circular flow of income	Activity 2 – short questions on national income.	Individual activity.	✓			X	X			Starter or plenary
	Aggregate demand (AD)	Activity 3 – short questions.	Individual activity.	✓			X	X			Plenary
	Aggregate demand (AD)	Activity 4 – short questions followed by a research task.	Individual activity.	✓				X	X	X	Starter or plenary
	Aggregate supply (AS)	Activity 5 – distinguishing between SRAS and LRAS task followed by graphical illustrations task.	Can be done individually or in pairs.	✓	✓		X	X			Plenary
	Aggregate demand and supply	Activity 6 – questions based on									

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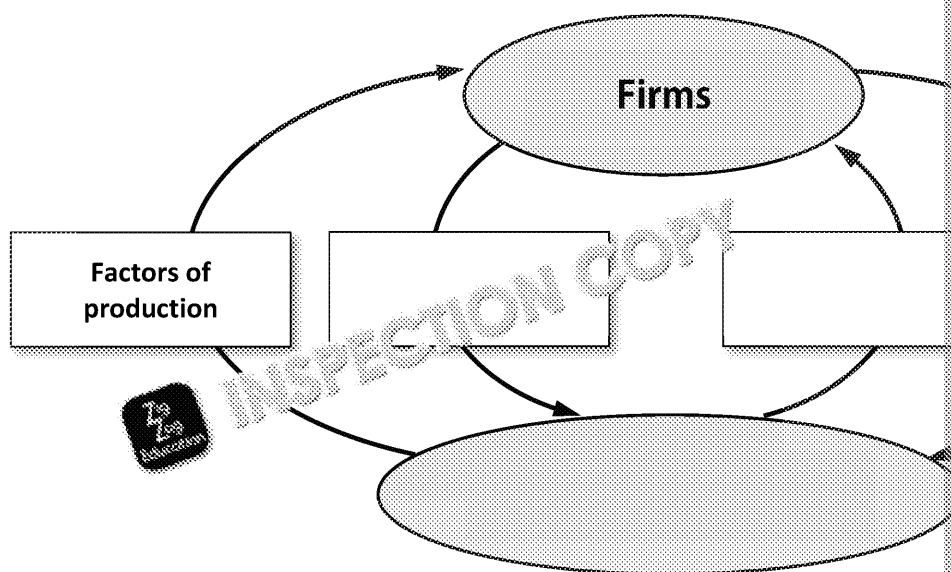


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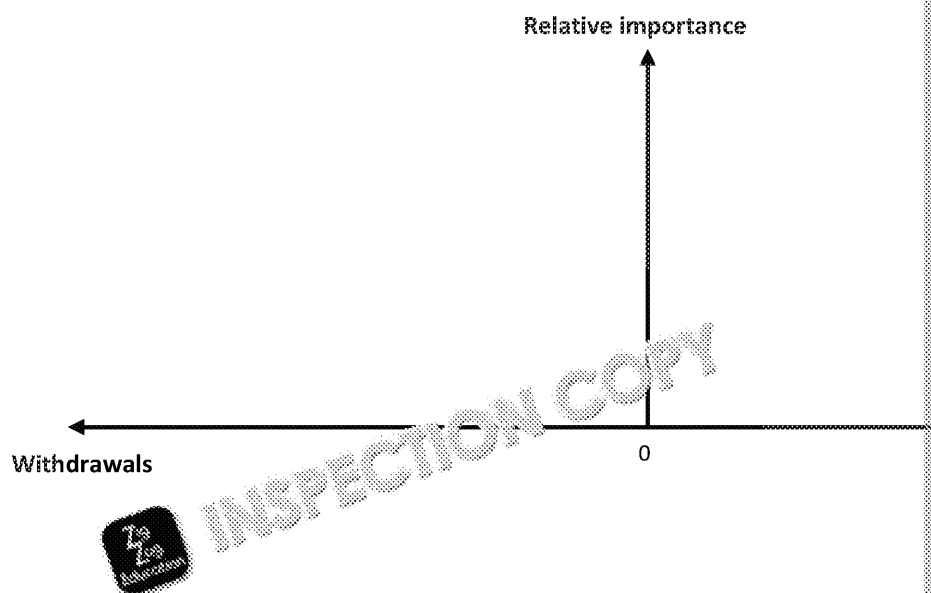


Activity 1 – Circular flow of income

1. Complete the following circular flow of income diagram.



2. On the axes below, identify three withdrawals and three injections into the circular flow. On the y-axis, suggest how important you think each response is (i.e. how it should be compared to the other two). Compare your answer with the person next to you.



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Activity 2 – Circular flow of income

1. What is meant by the national income?

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2. National income can be measured in three different ways (however, they figure). What are they? How are they calculated?

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Activity 3 – Aggregate demand (C)

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1. a) What are the components of aggregate demand?

AD =

- b) Now, briefly explain each component.

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- c) Discuss what you think the percentage of each component in the UK

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Activity 4 – Aggregate demand (C)

1. Explain how the following affect consumer spending:

a) Interest rates

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b) Wealth effects

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c)  Confidence

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2. Research what the following terms mean in economics:

- a) Animal spirits
- b) Business expectations
- c) Access to credit
- d) Government regulation



3. Now briefly explain how each of these factors will affect investment.

a) Animal spirits


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b) Business expectations

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c)  Access to credit

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d) Government regulation

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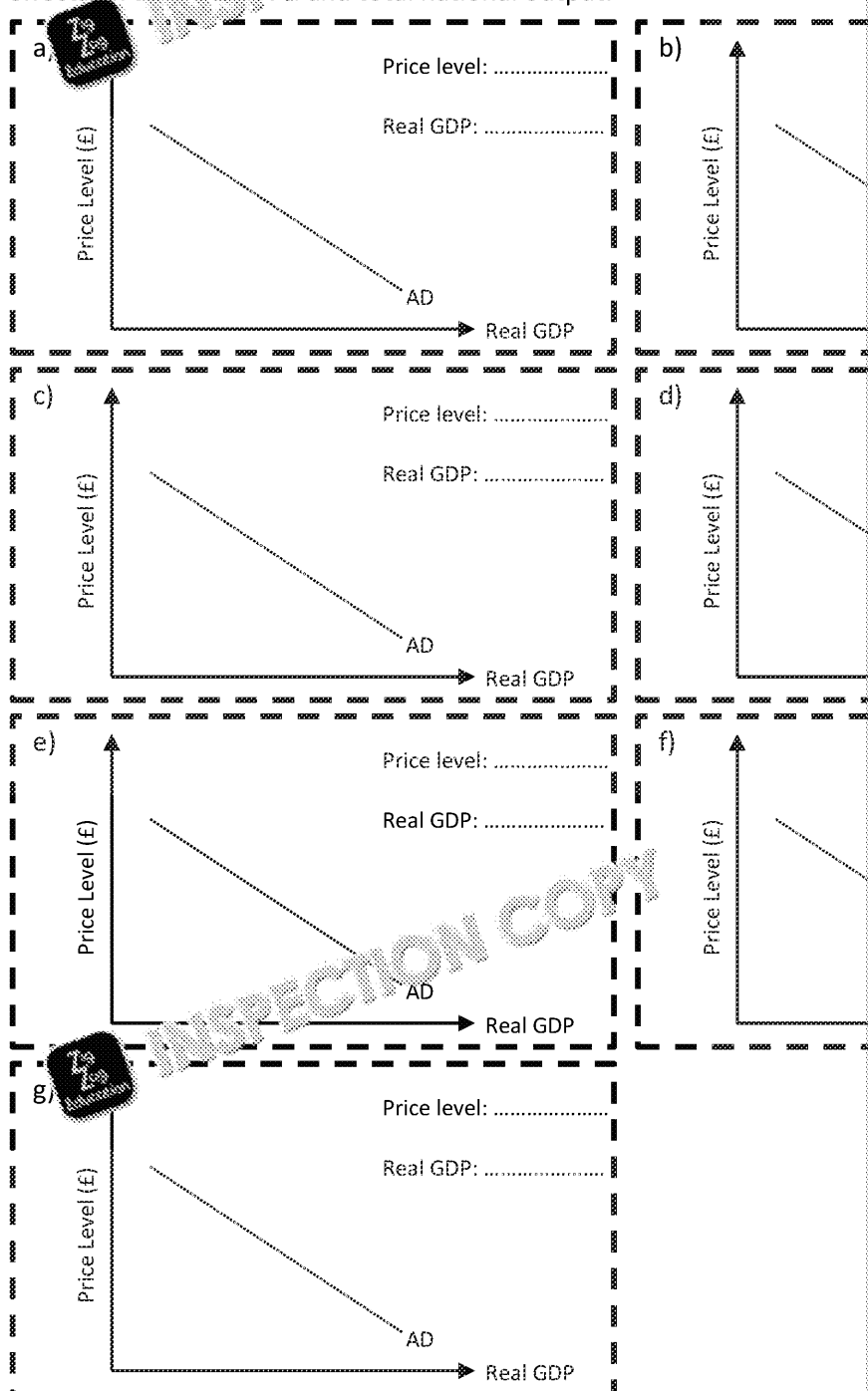
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Activity 5 – Aggregate supply

- Read the statements below and decide whether they are referring to short-run aggregate supply (SRAS) or long-run aggregate supply (LRAS).
 - Increasing tax rates affects a firm's costs.
 - Improving human capital via education and vocational training affects the economy's productive capacity.
 - Lack of competition in the industry affects AS.
 - A reduction in the price of oil is likely to lower a firm's production costs.
 - Improvements in technology improve a country's productivity.
 - If the exchange rate worsens, imports become more expensive.
 - An increase in net migration potentially increases the labour supply.

- Using the statements from Question 1, illustrate which way the curve will shift and the effects on the price level and total national output.



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Activity 6 – Aggregate demand and aggregate supply

On 23rd of June 2016, the people of Britain voted to leave the EU. A wave of uncertainty swept through the country within minutes – and economists dished out several predictions with the most frightening of them all was the possibility of another recession. However, the initial data revealed that consumers had in fact increased their spending. The British Retailers Association reported that spending in retail stores increased by 2.4% compared with last year. However, the vote did not affect the UK exchange rate. Immediately after the vote the pound fell from its 1987 31-year low of 1.36. While this has meant that UK exports appear cheaper abroad, the cost of raw materials has become more expensive.

1. a) Illustrate the above information on an AD/AS diagram.



- b) Explain what happens to inflation and real output.

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- c) Write down your predictions for.

Consumer spending:

Exchange rate:

Economic growth:




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Activity-by-activity Plan

Spec. Area	Topic	Activity Description	Notes				Extra Resources	Assessment Objectives				Suggested Use
								AO1	AO2	AO3	AO4	
Economic Policy Objectives	Economic growth	Activity 7 – questions, including definitions task and a calculation question.	Individual work. Students may swap work in pairs to mark it.	✓	✓		Calculator	X	X	X		Starter or plenary
	Economic growth	Activity 8 – discussion task followed by fill in the table task.	Pair work.		✓				X	X		Starter or plenary
	The economic cycle	Activity 9 – various types of questions, including spotting the error task.	Individual or pair work.	✓	✓				X	X		Starter
	Economic growth and development	Activity 10 – fill in the chart and definitions tasks, followed by some group research.	Tasks 1 and 2 should be done individually For task 3, split the class into groups for internet research and presentation of findings.	✓		✓	For task 3, students will need access to computers and the Internet.	X	X	X	X	Starter
	Economic growth and development	Activity 11 – definitions task followed by an evaluation question.	Tasks can be done individually or in pairs.	✓	✓			X	X	X		Starter or plenary
	Economic growth and development	Activity 12 – short question.	Tasks can be done individually or in pairs.	✓	✓			X	X			Starter or plenary

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Activity 7 – Economic growth

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1. Define the following:

- Real GDP

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- Economic growth

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2. Given that the rate of increase in the price level in the UK between 2015 and 2016 was 2.3%, and that nominal GDP was £1.7 trillion in 2015 and £1.8 trillion in 2016, calculate the real GDP in 2016.

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3. State **three** reasons why GDP and economic growth are measured.

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Activity 8 – Economic growth

1. In pairs or small groups, discuss what would lead to economic growth in the long run.


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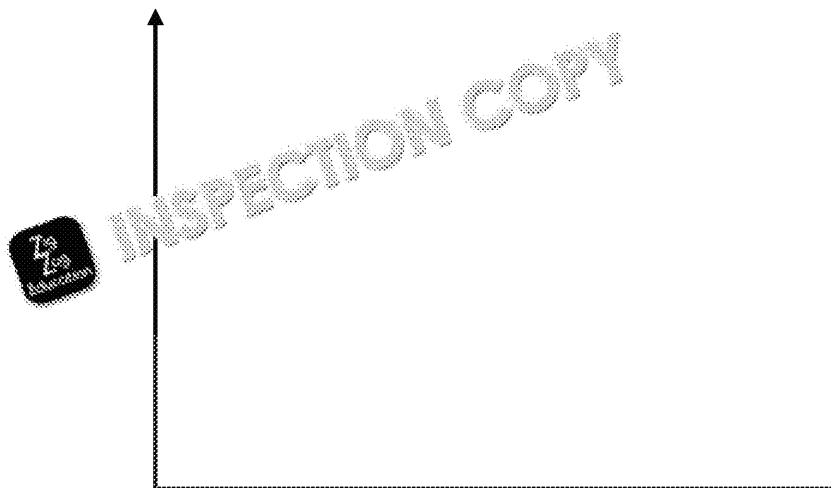
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2. Fill in the table below:

	Costs	
 Economic growth		
Recession		

3. Show economic growth using a PPF diagram.



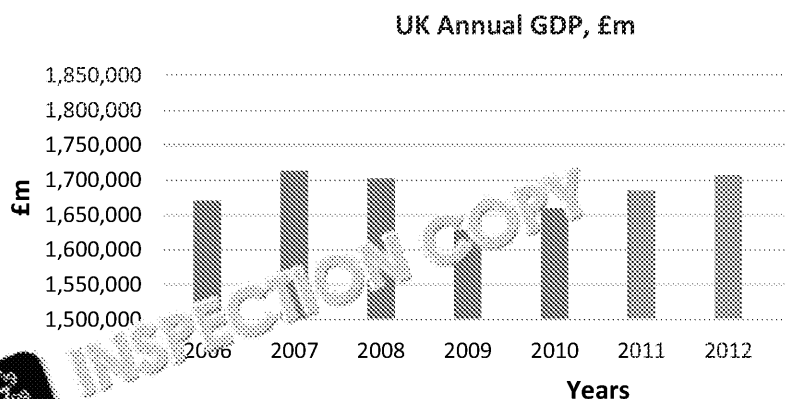
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Activity 9 – The economic cycle

1. a) Below is some data on the UK's annual growth rate between the year 2006 and 2012. Draw a trend line on the chart below:



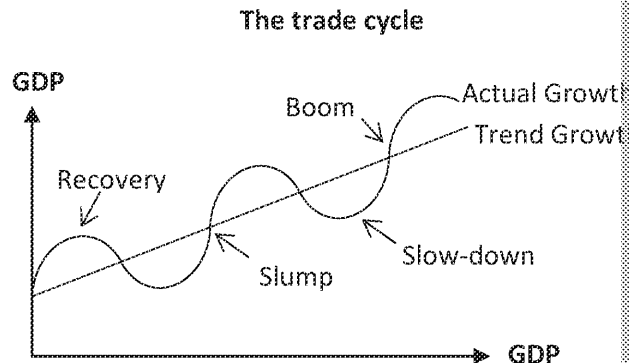
- b) Distinguish between the actual rate of growth and the trend rate

• Actual rate of growth =

• Trend rate of growth =

2. Identify what is wrong with the following and write down the correct version

- a) The trade cycle diagram.



- b) The trade cycle characteristics.

	Boom	
Economic growth	High	
Unemployment	High	
Inflation	Low	
Consumer/business confidence	High	
Government finances	Low tax revenue, low welfare spending	High
Exchange rate	Weak currency	

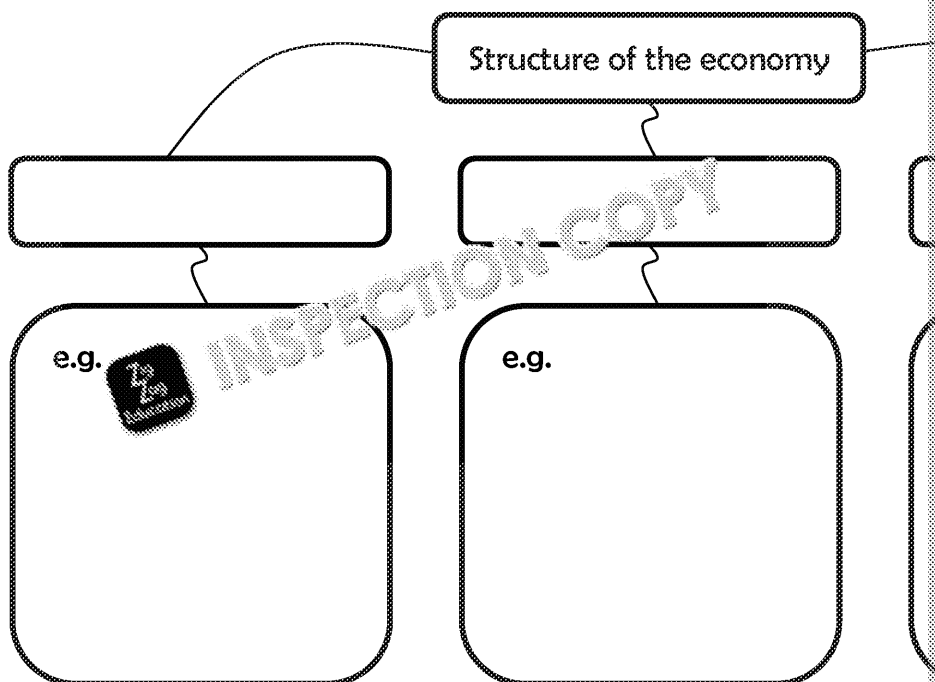
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Activity 10 – Economic growth development (1)

1. Fill in the chart below:



2. Define the following:

- Economic growth
- Economic development
- Sustainable development

3. In your groups research the following and then present your findings in a presentation to the class. It is up to you how you want to split the work within your group

Group 1	
<ul style="list-style-type: none"> Types of aid, with examples World's biggest aid donors and recipients Percentage of selected countries' GDP that is spent on overseas aid How aid helps in promoting economic growth Is aid better than trade in promoting economic growth? 	<ul style="list-style-type: none"> Types of trade agreements Benefits of the various types of trade Explain how trade promotes economic growth Is trade better than aid in promoting economic growth?

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Activity 11 – Economic growth and development (2)

1. $HDI = \sqrt[3]{V(\text{education index} + \text{life expectancy index} + \text{income index})}$

State how the various components of the Human Development Index (HDI) are calculated.

- Education index =
- Life expectancy index =
- Income index =

2. What is GNI?


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3. How good or bad is the indicator of HDI in comparing levels of development? Use the table below to answer the question.

Advantages of HDI	Disadvantages of HDI
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Activity 12 – Economic growth and development (3)

1. List and explain any three alternative indicators of development.

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Activity 13 – Employment/unemployment

1. Below is a list of the five main causes of unemployment. The task is to find an example for all causes of unemployment. The group that gets the highest number of minutes to complete this task.

- a) Structural unemployment
- b) Frictional unemployment
- c) Seasonal unemployment
- d) Cyclical unemployment
- e) Real-wage inflexibility

2. Discuss the impacts of unemployment on your assigned stakeholder and groups.

The roles are: consumers, firms, workers, government and society.

Use the following table to jot down your points.

Consumers	
Firms	
Workers	
Government	
Society	

3. What is the difference between the Labour Force Survey and claimant count unemployment?

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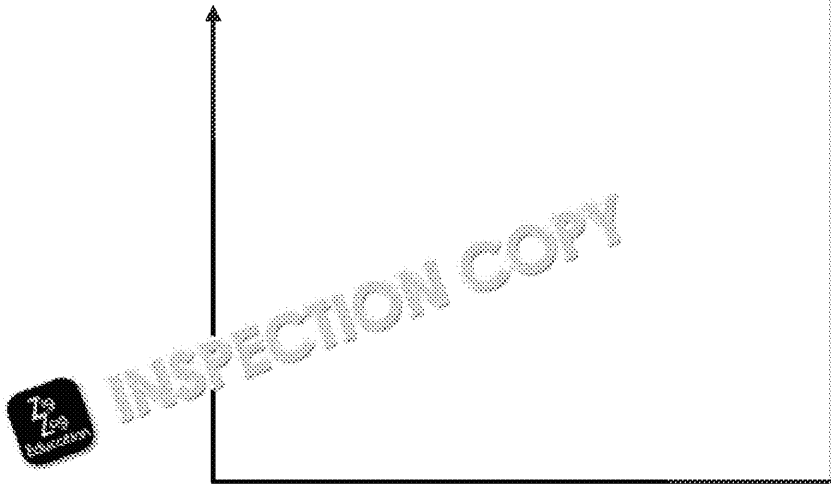
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Activity 14 – Inflation

1. On the diagram below label periods of inflation, disinflation and deflation



2. Below are three scenarios. Work out the cause of inflation each scenario

- a) Following Britain's vote to leave the EU, the UK exchange rate has devalued. £1 now buys fewer euros and US dollars. As a result all the raw materials to produce consumer goods and services have become more expensive.

.....

- b) Following a recession, the central bank of country A decided to introduce quantitative easing (QE). In simple words QE allows more money to be printed. As a result, consumer and business spending have increased, which has pushed up the price level.

.....

- c) Following a recession, the central bank of country A decided to lower interest rates. This makes saving less attractive, while making borrowing more attractive. As a result, consumer and business spending have increased, which has pushed up the price level.

.....

3. Spot the errors in the following paragraph and write down the correct version for this task.

The UK uses three methods to calculate the rate of inflation: the Retail Price Index (RPI), the Consumer Price Index (CPI). The UK calculates inflation on an annual basis, using a 'basket of goods', which includes around 150 goods and services that an average household. Each good or service is given a weightage to reflect its importance in the household. Prices of these goods are collected from 700 locations. CPI, in particular, is calculated using the Consumer and Food Survey to get data.

Once you have done that, swap your answers with the person next to you.

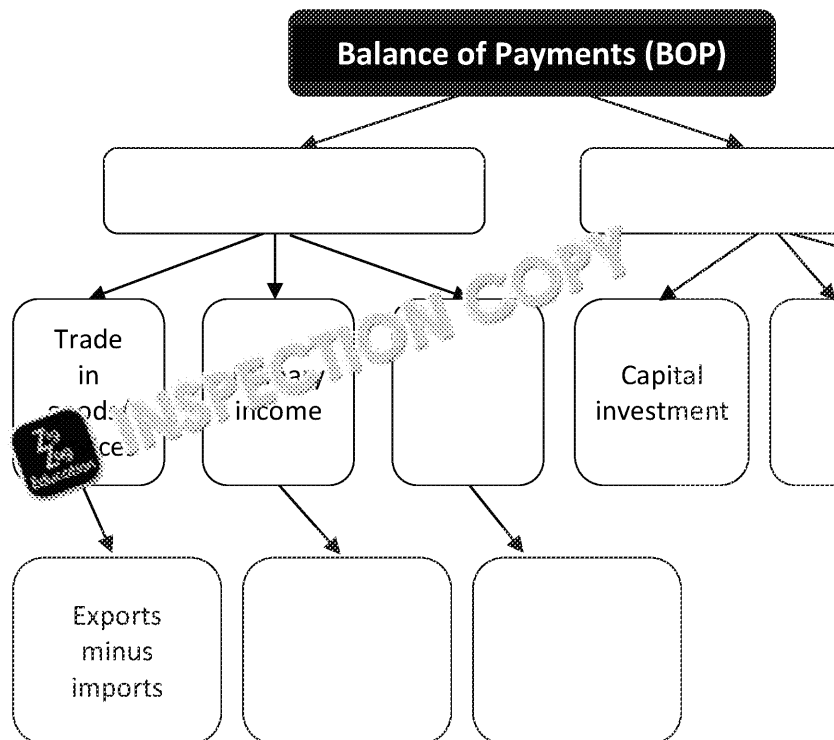
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Activity 15 – Balance of payments

1. Fill in the diagram below on the parts of the balance of payments:



2. List any three causes of current account deficit and surplus.

Causes of C/A deficit	
Causes of C/A surplus	

3. a) Identify the three main measures to reduce current account imbalance.

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- b) Now give an example for each policy.




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Activity-by-activity Plan

Spec. Area	Topic	Activity Description	Notes				Extra Resources	Assessment Objectives				Suggested Use
								AO1	AO2	AO3	AO4	
Implementing policy	Fiscal policy	Activity 16 – fill in the chart/table task followed by a graphical illustration task.	Individual work.	✓				X	X	X	X	Plenary
	Fiscal policy	Activity 17 – fill in the blanks task.	Individual or pair work.	✓	✓			X	X	X		Plenary
	Fiscal policy	Activity 18 – discussion questions.	Split class into small groups.			✓			X	X		Plenary
	Monetary policy	Activity 19 – match the keywords followed by two short questions.	Individual or pair work.	✓	✓			X		X		Starter or plenary
	Supply-side policies	Activity 20 – play a few rounds of Pictionary.	Group work. Split the class into two big groups.			✓	You will need a board for students to draw on.	X				Starter or plenary
	Policy conflicts	Activity 21 – short questions.	Individual work for task 1. For task 1b, call upon students at random and ask them to draw the diagram for any one policy conflict (i.e. AD/AS diagram illustrating high levels of growth coinciding with high inflation).	✓			Students will need a board to draw their diagrams	X	X	X	X	Starter or plenary

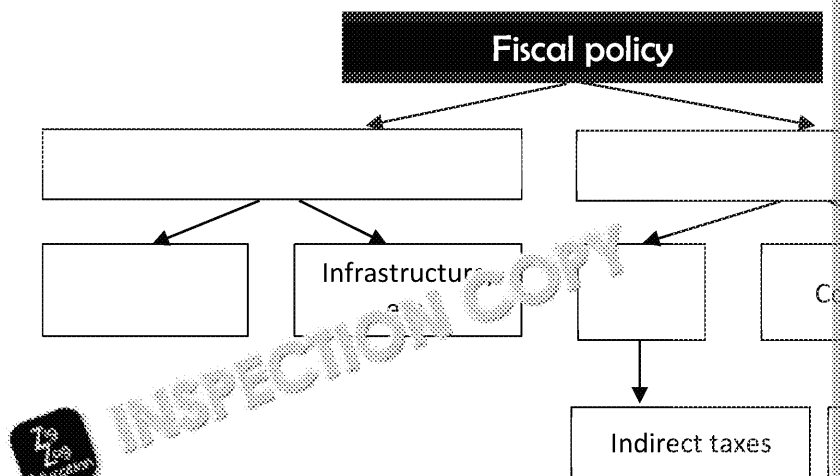
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Activity 16 – Fiscal policy (1)

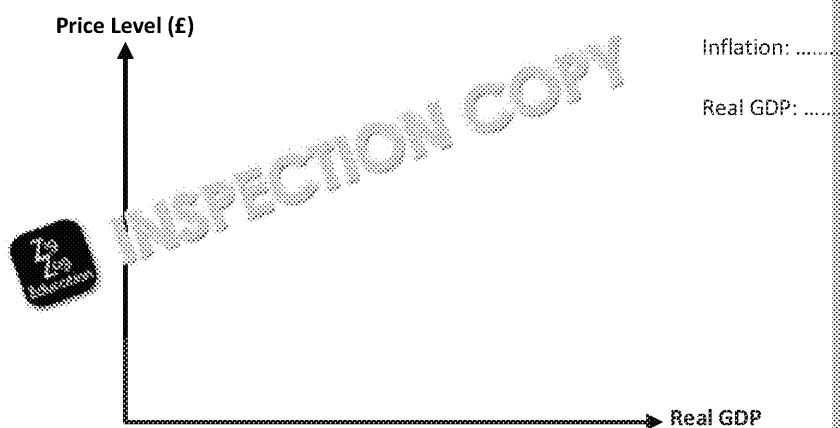
1. a) Fill in the chart below on the aspects of fiscal policy:



- b) Write down the strengths and weaknesses of fiscal policy in the table

Strengths	
Weaknesses	

2. Draw an expansionary fiscal policy diagram below and state the effect of inflation and national output.



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Activity 17 – Fiscal policy (2)

1. Fill in the blanks.

- _____ is about changes in taxation.
- _____ is the balance of government revenue.
- If government spending exceeds tax revenue, there is a _____.
- _____ is the total amount of government spending over time.
- _____ are levied directly on individuals or companies.
- _____ are levied on consumption.
- _____ refers to a system where tax rates increase as incomes increase.
- _____ refers to a system where tax rates decrease as incomes increase.
- _____ refers to a system where all taxpayers (of varying income levels) pay the same rate of tax.
- _____ refers to government expenditure on public sector wages.
- _____ refers to government expenditure on investment projects, e.g. building new railways.
- _____ deficit/surplus resulting from the economic cycle.
- _____ term deficit/surplus regardless of the economic cycle. This is overall government deficit/surplus when at full employment.
- _____ refer to automatic stabilisers, e.g. changes in government spending or taxation following changes to the economy (e.g. boom or recession).
- _____ use of fiscal policy by the government to achieve certain goals.

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Activity 18 – Fiscal policy (3)

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1. In small groups discuss the following:

a) How can budget deficits be financed?

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b) What are the $+$ and $-$ of correct budget deficits?



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2. Discuss why discretionary fiscal policy may be used.

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Activity 19 – Monetary policy

1. Match the keywords to their definitions:

Keywords
Monetary policy
Expansionary monetary policy
Contractionary monetary policy
Interest rate
Money supply
Quantitative easing (QE)
Exchange rate
Inflation targeting

Definitions
A planned target for the central bank, that is an inflation rate
The central bank buys and sells government securities in order to increase or decrease the money supply
The amount of money in circulation in the economy
About controlling the money supply in the economy, primarily to achieve a target inflation rate
Decreasing the money supply
The price of one currency in terms of another
Increasing the money supply
The cost of borrowing money

2. Explain two ways how inflation targeting can affect the behaviour of economic agents.

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3. Which of the following is an example of monetary policy?

- A) increasing the interest rate from 2% to 3% ☐
- B) increasing VAT from 27% to 30% ☐
- C) increasing spending on infrastructure ☐
- D) changing the exchange rate regime from floating to fixed ☐

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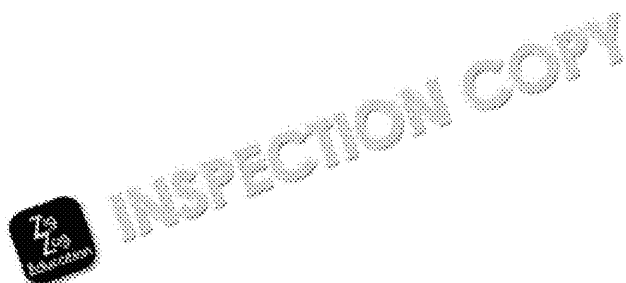
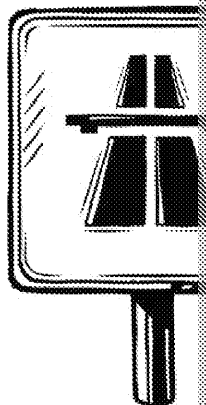
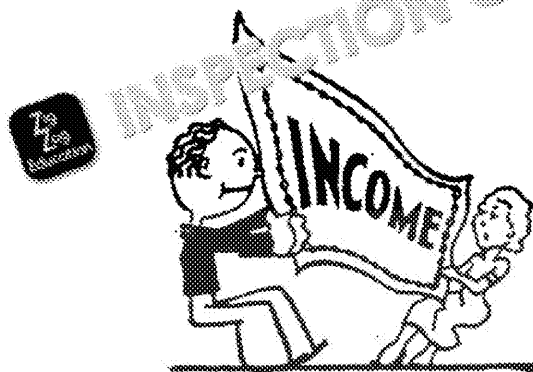


Activity 20 – Supply-side poli

1. Play a game of Pictionary (where one person from a group draws a picture and the others try to guess within two minutes). On each turn, draw pictures to represent

Groups should take turns and a different person from each group should draw. Whichever team gets the most correct answers within the allotted time of 10 minutes of correct answers (say, five) wins. The person drawing must themselves write down for the teacher to see and then begin drawing.

Remember no talking and no writing words while playing.



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Activity 21 – Policy conflicts

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1. a) List any five sets of two macroeconomic policies that may conflict with each other.

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- b) Illustrate any one of your policy conflicts on the white board using a diagram (you may use a template if you wish).



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Activity-by-activity Plan

Spec. Area	Topic	Activity Description	Notes	Individual	Group	Extra Resources	Assessment Objectives				Suggested Use
							AO1	AO2	AO3	AO4	
	International trade	Activity 22 – one short question.	Tasks may be done individually.	✓			X	X	X		Plenary
	Exchange rates	Activity 23 – some questions including true/false statements and costs/benefits analysis.	Tasks may be done individually or in pairs.	✓	✓		X	X			Plenary

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Activity 22 – International trade

1. List some of the advantages and disadvantages of trade.

Advantages	Disadvantages

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Activity 23 – Exchange rate

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1. Name the three types of exchange rate regimes.

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2. State whether the following statements are true or false:

A	Managed exchange rate is an exchange rate regime whereby the value of the domestic currency is pegged against another currency.
B	Free floating exchange rate is an exchange rate regime whereby the market mechanism determines the value of the domestic currency.
C	Under a floating exchange rate regime, a fall in the value of a currency is referred to as depreciation in the currency.
D	Under a fixed exchange rate regime, a rise in the value of a currency is referred to as appreciation in the currency.

3. Fill in the table below:

	Floating exchange rate	Fixed exchange rate
Benefits		
Costs		



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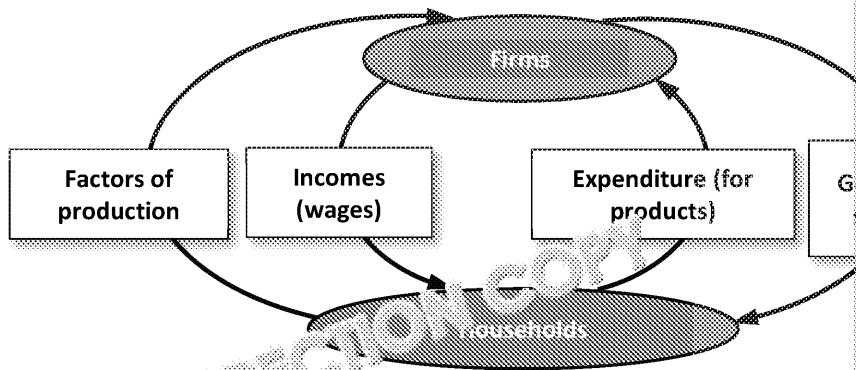
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Answers

Activity 1 – Circular flow of income (1)

1. a)



Activity 2 – Circular flow of income (2)

- National income is the value of all the goods and services produced in a country in a given period.
- Income method
 - This method adds up all the incomes of all the factors of production.
 - NI = rent (land) + wages (labour) + return (capital) + profits (enterprise).
 - Output method
 - This method adds up the total value of all the goods and services produced in a country in a given period.
 - Expenditure method
 - This method adds up all the components of AD ($C + I + G + (X - M)$).

Activity 3 – Aggregate demand (AD) (1)

- a) $AD = C + I + G + (X - M)$

b)

 - Consumer spending (C) refers to the money spent by people on consumer goods and services.
 - Investment (I) refers to the money spent by firms on factor inputs, e.g. capital equipment, to expand their businesses.
 - Government spending (G) refers to money spent by the government on public services, such as welfare payments.
 - Net exports ($X - M$) refer to goods and services sold to another country less goods and services bought from another country.

c)

AD =	C +	I +	G +	(X - M)
	60%	15%	25%	2% - 2%

Activity 4 – Aggregate demand (AD) (2)

- a) When interest rates are high, saving becomes more attractive and borrowing less so. Therefore, consumption is likely to fall. At low interest rates, the opposite happens.

b) Increases in the value of people's assets is another factor that can increase consumption. For example, if the value of someone's shares go up, as people feel wealthier.

c) Businesses and consumers may base their spending decisions on how optimistic they are about the economy. If confidence is low, consumption is likely to fall, and vice versa.
- a) High animal spirits means that consumer confidence is high. Thus, investors will spend more from higher consumer spending.

b) If business confidence is high then investors will look to invest more.

c) If credit is easily and cheaply available then investors can easily borrow the money they need to invest.

d) Excessive government regulation, e.g. high corporation taxes, is likely to put investors off investing.

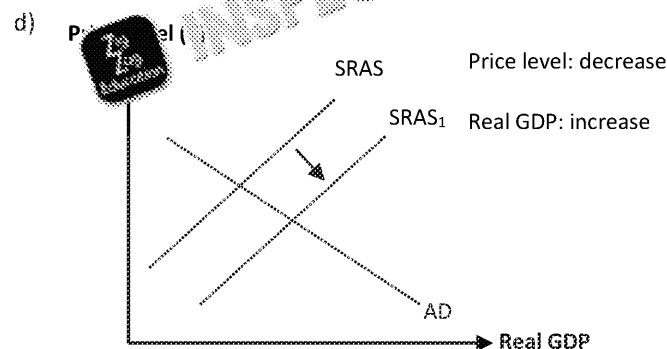
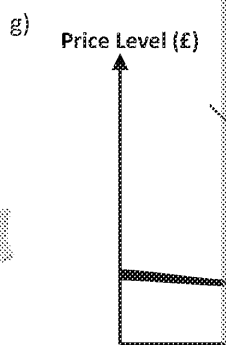
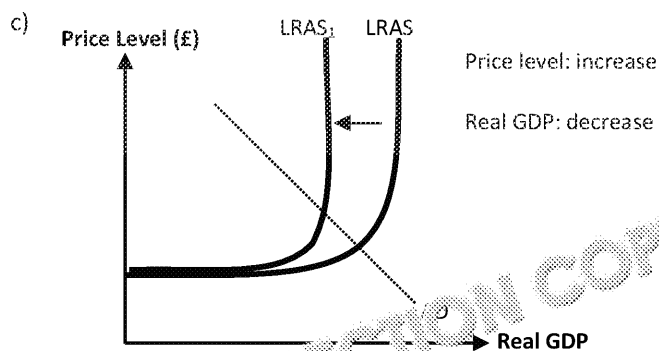
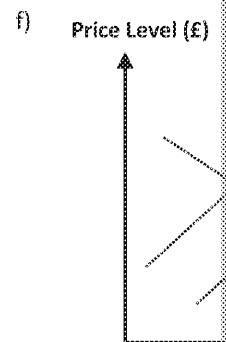
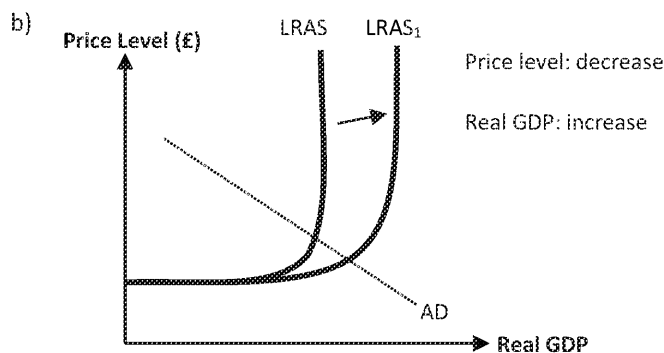
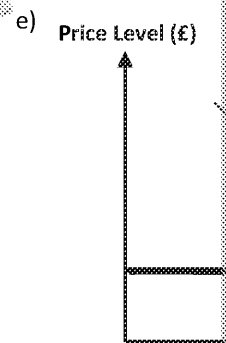
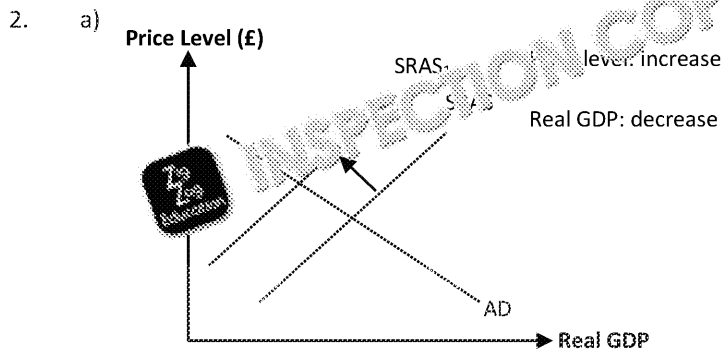
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Activity 5 – Aggregate supply

1.
 - a) Increasing tax rates affects a firm's costs. (SRAS)
 - b) Improving human capital via education and vocational training affects supply of
 - c) Lack of competition in the industry affects AS. (LRAS)
 - d) A reduction in the price of oil is likely to lower a firm's production costs. (SRAS)
 - e) Improvements in technology improve a country's productivity. (LRAS)
 - f) If the exchange rate worsens, imports become more expensive. (SRAS)
 - g) An increase in net migration potentially affects labour supply. (LRAS)



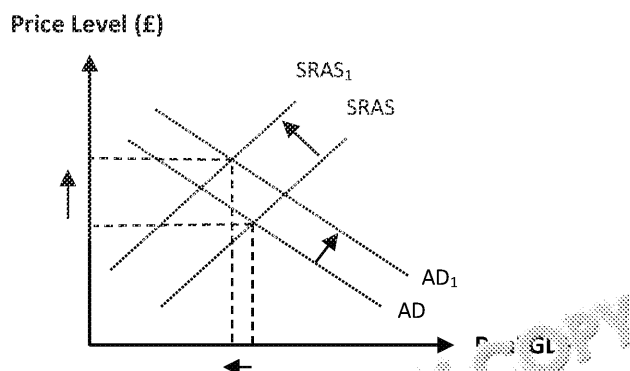
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Activity 6 – Aggregate demand and aggregate supply

1. a)



- b) An increase in demand for goods and services will shift the AD curve to the right and increase real output. However, at the same time, a fall in the exchange rate makes materials become more expensive. This translates into higher production costs. AS shifts to the left. This leads to inflationary pressure, as well as a fall in efficiency. Inflation is upward. However, the effect on real GDP depends on the size of the shifts. If an increase in the AD outweighs the decrease in AS then real output will increase. If the decrease in AS outweighs the increase in AD then real output will fall.

Activity 7 – Economic growth (1)

- Real GDP: the total value of goods and services produced by a country in a given period, adjusted for inflation.
 - Economic growth: increase in GDP (i.e. an increase in the production of goods and services).
 - Recession: an economy is said to be in recession when it experiences at least two consecutive quarters of economic growth.
- Nominal rate = $\frac{1.8-1.7}{1.7} \times 100 = 5.9\%$

Real rate = $\frac{5}{9} - 3.1 = 2.8\%$
- To evaluate a country's economic performance over time and in comparison to other countries.
 - Policies are devised based on this performance.
 - They also help other countries and/or financial institutions analyse the risk of investing in different countries.

Activity 8 – Economic growth (2)

- Short-run growth tends to come from increases in AD ($AD = C + I + G + (X - M)$).
 - Long-run growth tends to come from increases in AS.

2.

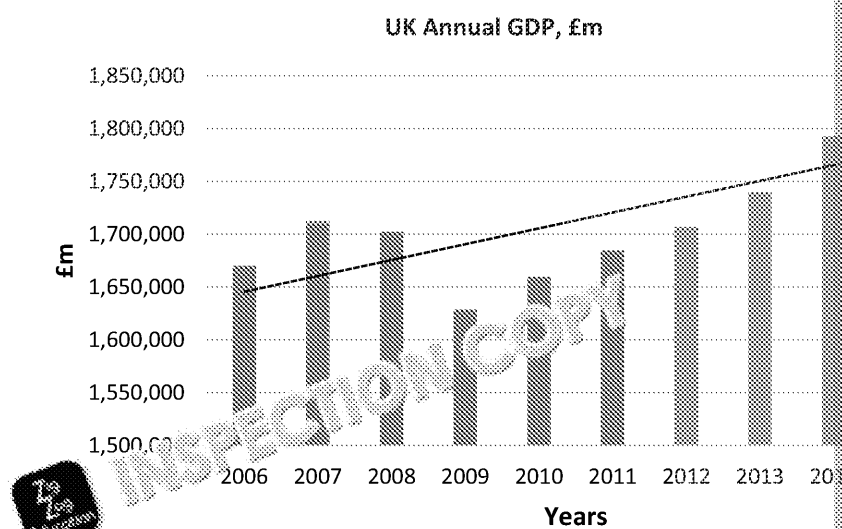
	Costs	
Economic growth	<ul style="list-style-type: none"> Inflation Trade deficit (import more expensive, exports cheaper) Increased wealth inequality Environmental degradation Unsustainable growth Can create market bubbles 	<ul style="list-style-type: none"> Higher incomes Reduced poverty Reduced unemployment More tax revenue (from public services) Less welfare spending More investment
Recession	<ul style="list-style-type: none"> Increased unemployment (redundancies) Lower incomes and profits Firms going bankrupt Increased government spending (on welfare) Lower tax revenue Lower wages Increased government borrowing 	<ul style="list-style-type: none"> Less environmental damage Reduced income inequality Currency drops Lower inflation (may experience deflation and unemployment) Creative destruction (innovations)

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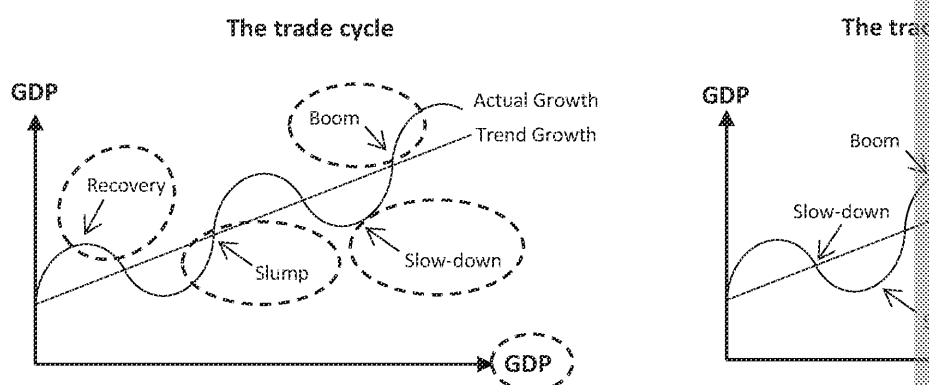
Activity 9 – The economic cycle

1. a)



- b)
- Actual rate of growth = real rate of growth measured by the GDP statistics
 - Trend rate of growth = average growth rate over time (based on past experience; this is a straight line: it ignores the effect of trade cycles.)

2. a)



b)

	Boom	
Economic growth	High	High
Unemployment	High	Low
Inflation	Low	High
Consumer confidence	High	Low
Government finances	Low tax revenue, low welfare spending	High tax revenue, high welfare spending
Exchange rate	Weak currency	Strong currency

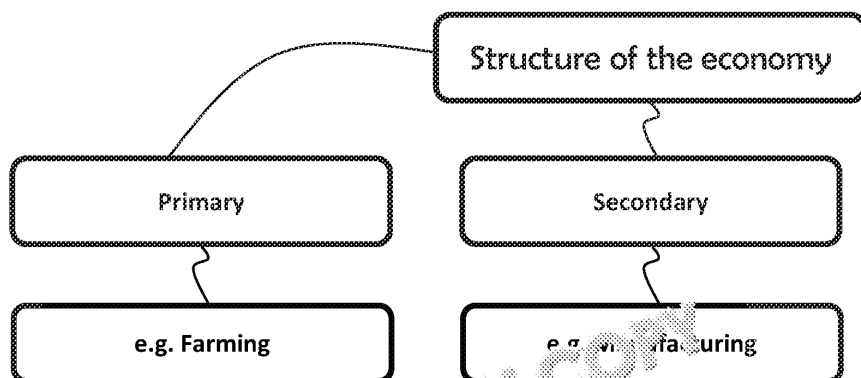
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Activity 10 – Economic growth and development (1)

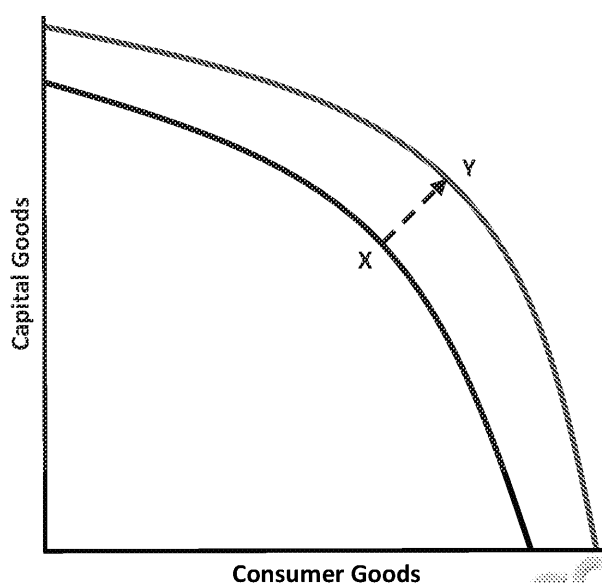
1.



2.

- Economic growth: economic growth is both a short- and long-run concept. Short-run growth is an increase in the total output of an economy produced in a given time period. Long-run growth is an increase in the productive capacity of an economy.
- Economic development: this refers to an increase in economic growth, as well as improvements in living standards, e.g. better quality education, job creation, etc.
- Sustainable development: this refers to economic development that is environmentally sustainable. It means meeting the needs of the present generation without harming the needs of the future generation. 'Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs.'

3.



Activity 11 – Economic growth and development (2)

- 1.
- Education index = average + expected years of schooling
 - Life expectancy index = Life expectancy at birth
 - Income index = GNI per person

2. $GNI = GDP + \text{net income received}$

3.

Advantages of HDI	Disadvantages of HDI
<ul style="list-style-type: none"> • Not reliant on any one measure. It is multidimensional. • Uses two measures for education. 	<ul style="list-style-type: none"> • Using averages may mask inequalities. • Certain factors are not included, e.g. income inequality, ecological sustainability.

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Activity 12 – Economic growth and development (3)

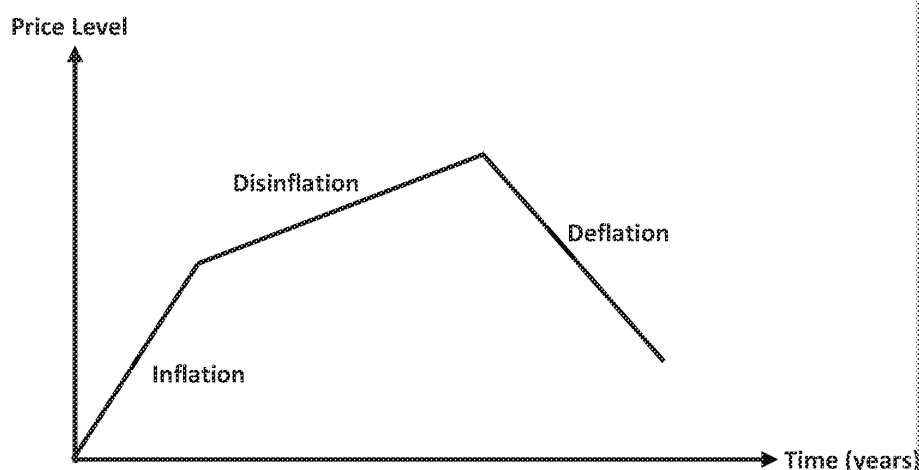
- Inequality-adjusted HDI (IHDI)
 - IHDI basically adjusts HDI for inequalities.
 - If inequality for any of the three measures (education, income, health) is lower than a country's HDI value.
 - Multinational Poverty Index (MPI)
 - This, too, is a multidimensional measure, which means it incorporates a*
 - It does not only look at poverty in terms of income but also the facilities \$2 a day. It looks at things such as sanitation, crime, water, etc.*
 - Head count ratio
 - This measure simply counts the number of poor people in a country.
 - Poverty is based on anyone earning under \$2 a day at PPP.

Activity 13 – Employment/unemployment (1)

- Labour Force Survey is a household statistical survey that is designed to calculate the count number of employment totals the number of people claiming unemployment information directly from the Department for Work and Pensions.

Activity 14 – Inflation

1.



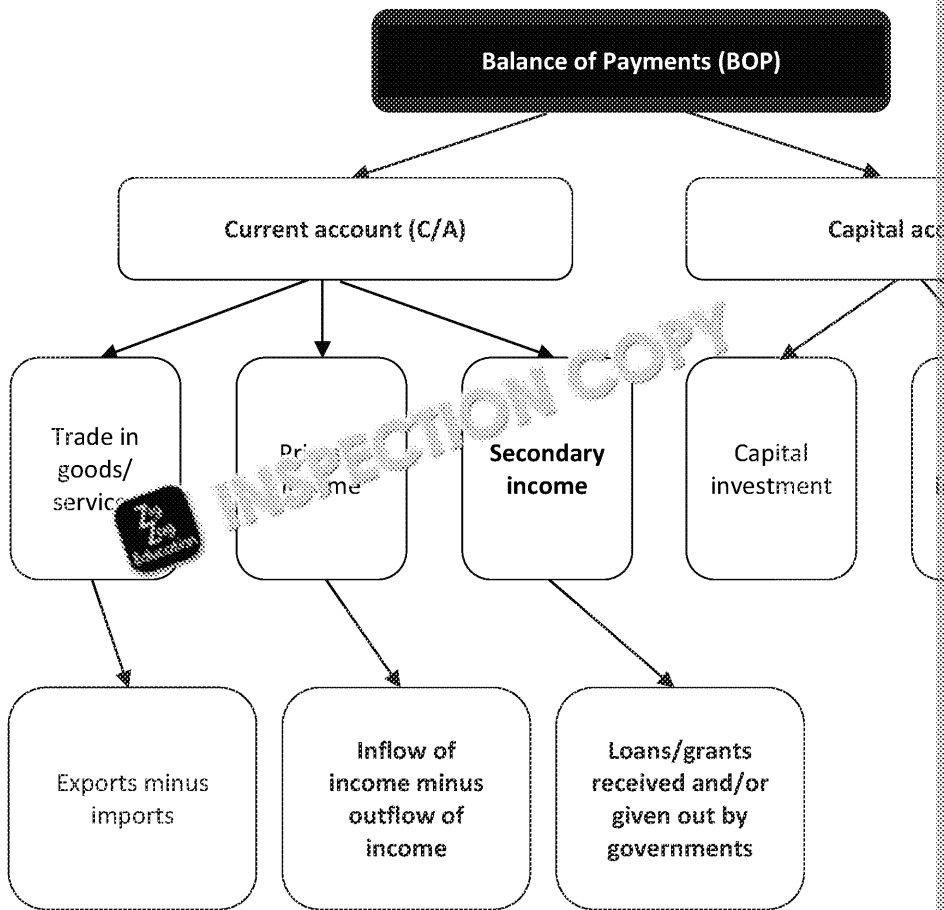
- Cost-push inflation
 - Growth in money supply
 - Demand-pull inflation
- The UK uses **three** (two) measures to calculate the rate of inflation: the Retail Price Index (CPI). The UK calculates inflation on an **annual** (monthly) basis. RPI (Both measures use a 'basket of goods', which includes **150** (700) goods and services that are representative of a household. Each good or service is given a weightage to reflect its importance to the household. These goods are sourced from **700** (150) locations. **CPI** (RPI), in particular, uses the latest data.

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Activity 15 – Balance of payments

1.



2.

Causes of C/A deficit	Causes of C/A surplus
<ul style="list-style-type: none"> • High inflation rate → cheap imports • Relatively low labour productivity → increased average cost → cheap imports • Higher exchange rate → cheap imports • High domestic growth → increased demand for imports • Growth in large economies → increased demand for imports 	<ul style="list-style-type: none"> • Protectionist measures • Low inflation → cheap exports • Lower exchange rate → cheap exports • Low domestic growth → reduced demand for exports • Relatively high labour productivity → cheap exports

3.

- Expenditure-reducing policies
 - Expenditure-switching policies
 - Supply-side policies
- Expenditure-reducing policies = increasing income tax
 - Expenditure-switching policies = trade barriers
 - Supply-side policies = spending on education and training



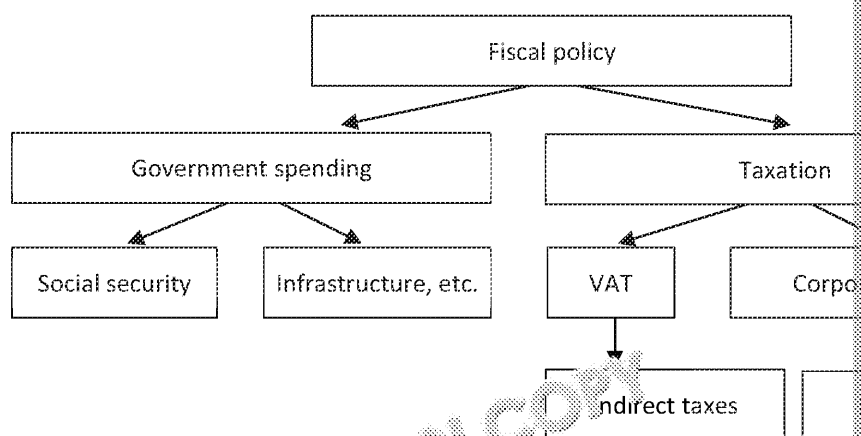
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Activity 16 – Fiscal policy (1)

1. a)

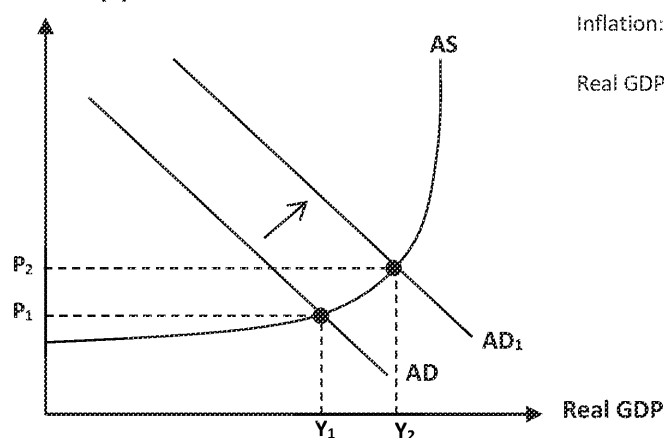


b)

Strengths	Weaknesses
<ul style="list-style-type: none"> • Government spending creates reduced poverty • Can be targeted exactly at the areas the government is trying to target • Positive multiplier effect of government spending • Can reduce market failure, e.g. through pollution tax • Government may spend on infrastructure and capital goods, which have positive effects in the long term as well. 	<ul style="list-style-type: none"> • Can cause inflation • Slow and inaccurate decision making • Raising taxes will reduce aggregate demand • Excessive government spending can lead to accumulation of debt • Spending on welfare can be a drain on the economy • Fiscal policy has a short-term effect • Government expenditure can crowd out private investment

2.

Price Level (£)



Inflation: increase

Real GDP: increase

Activity 17 – Fiscal policy (2)

- **Fiscal policy** is about changes in government spending and taxation.
 - **Government budget** is the balance between government spending and tax revenue.
 - If government spending exceeds tax revenue, there is a **budget deficit**.
 - **National debt** is the total amount of debt a country has accumulated over time.
 - **Direct taxes** are levied directly on income.
 - **Indirect taxes** are levied on consumption.
 - **Progressive taxation** refers to a system of taxation whereby tax rate increases as income increases.
 - **Regressive taxation** refers to a system of taxation whereby tax rate decreases as income increases.
 - **Flat taxation** refers to a system of taxation whereby all taxpayers (of varying income) pay the same rate of tax.
 - **Current spending** refers to government's everyday spending, e.g. on public services.
 - **Capital spending** refers to government's spending on long-term investment projects.
 - **Cyclical budget position** is a temporary deficit/surplus resulting from the economic cycle.
 - **Structural budget position** is a permanent or longer-term deficit/surplus regardless of the economic cycle.
 - **Automatic stabilisers** refer to automatic changes to government spending and taxation in response to changes in the economy (e.g. booms and recessions).
 - **Discretionary fiscal policy** refers to the deliberate use of fiscal policy by the government.

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Activity 18 – Fiscal policy (3)

1. a)
 - Financed through government borrowing
 - Governments issue bonds (loans) to investors, who may be individuals, firms or other governments
 - This is unsustainable if continued long-term, as the national debt will increase and investors will be worried about a default
- b)
 - Spending cuts
 - Increased taxation
 - Encourage/facilitate greater economic growth
2. Discretionary fiscal policy may be used for the following:
 - Lower inflation
 - Lower unemployment
 - Improve balance on the current account of the balance of payments
 - Reduce income inequality

Activity 19 – Monetary policy

1.

Keywords	Definitions
Monetary policy	About controlling the money supply in the economy to reduce inflation and volatility.
Expansionary monetary policy	Increasing the money supply.
Contractionary monetary policy	Decreasing the money supply.
Interest rate	The cost of borrowing or the reward for saving.
Money supply	The amount of money there is in the economy.
Quantitative easing (QE)	The central bank buys assets from banks to create new money and put it into the economy.
Exchange rate	The price of one currency in terms of another.
Inflation targeting	A planned target for the inflation rate, set by the central bank to inform the public.
2. Inflation targeting affects the behaviour of economic agents because it anchors expectations. Agents know that the central bank will change the interest rate if the inflation rate is above the target. If inflation is above the target the central bank is likely to *increase* the interest rate to deter household consumption and business investment. Agents take this into account and behave accordingly. Importantly, expectations of inflation determine actual future inflation. Adopting an inflation target can help manage inflation.
3. A

Activity 20 – Supply-side policies

Supply-side policies could include: education and training, research and development, deregulation, infrastructure, research, development incentives, reforming tax and benefits, reducing marginal tax rates, etc.

Activity 21 – Policy objectives

1. a) E.g.
 - Economic growth and inflation
 - Economic growth and the balance of trade (current account)
 - Economic growth and environmental protection
 - Inflation and unemployment
 - Income inequality and economic growth
- b) E.g. AD/AS diagram illustrating high levels of growth coinciding with high inflation

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2.

Policy tools	Short-run effects	
Fiscal policy	Increasing government spending is likely to create jobs and boost AD. But it will increase budget deficit.	Budget deficits increase national debt. The government can't balance the budget. If the government borrows capital, then it can invest in the economy to grow.
Monetary policy	By increasing the interest rate, inflation can be brought down because people will reduce their spending and save instead.	Reduced spending. Also high interest levels, negative growth.
Supply-side policies	Generally about large injections of government spending. Thus leading to a budget deficit.	Opportunity cost of one area (e.g. infrastructure projects) may harm the environment. The economy grows (PPF shifts outwards).

Activity 22 International trade

Advantages	Disadvantages
<ul style="list-style-type: none"> Specialisation and international trade can allow economies to consume a bundle of goods that would be outside of their PPF if they were an autarky Greater choice for consumers Cheaper goods for consumers – increase in consumer surplus Greater efficiency Firms experience economies of scale Wider market leads to higher profits Increased growth Higher standards of living Reduces monopoly power More jobs may be created Technological transfer 	<ul style="list-style-type: none"> Countries become interdependent Terms of trade may worsen – export low-value goods and export high-value goods Over-reliance on the product Countries lacking comparative advantage Unwanted goods can be imported at very low prices, which is a loss May widen the rich and poor gap Bad for 'infant industries' Environmental damage Business diversity eroded Comparative advantage may be lost (e.g. agriculture) so specialisation may be lost Structural employment issues Exploitation of workers in developing countries

Activity 23 – Exchange rates

- Floating
 - Fixed
 - Managed
- F (fixed exchange rate)
 - T
 - T
 - F (revaluation)
 - T
-

	Floating exchange rate	
Benefits	<ul style="list-style-type: none"> Automatic correction. More freedom to implement other policies domestically. 	<ul style="list-style-type: none"> No currency risk More certainty in investment. Easy to maintain
Costs	<ul style="list-style-type: none"> High currency fluctuations – uncertainty. Greater speculation. 	<ul style="list-style-type: none"> Automatic correction More freedom to implement other policies domestically.

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