Question 2: Brexit and its impact

Suggested Answers

(a)	a) With reference to Extract 6, explain the consequences of Brexit on UK's internal economy.				
		E4P1: "businesses defer whatever spending they can as investors hate uncertainty" and "US economy has been sluggish of late"			
	E4P2: "spending on big-ticket items is likely to slump"				
	Brexit \rightarrow Increase in uncertainty / Fall in business (or invest confidence in the UK \rightarrow Fall in investment expenditure (I) as delay / shelf investment projects [2m]				
	Sluggish US economy \rightarrow American households consume less goods and services, including imports from UK \rightarrow Demand for imports fall \rightarrow UK's export revenue (X) falls [2m]				
	Brexit \rightarrow Bleak economic outlook \rightarrow UK households spend less \rightarrow Consumption expenditure (C) falls [2m]				
		I, X and C fall \rightarrow AD falls \rightarrow Unplanned accumulation of stocks / inventories \rightarrow Firms cut back on production, hiring less factors of production, including labour \rightarrow Cyclical unemployment rises \rightarrow Factor incomes fall \rightarrow Induced consumption falls \rightarrow Real national income falls by multiplies \rightarrow Negative economic growth; General price level falls [2m]			
		Expect 2 main consequences on UK's internal economy – real national income and employment should come together			
		Max 4m on how Brexit impacts the components of AD and/or AS. Max 2m on how AD and/or AS changes impacts the internal macro goals.			
(b)		Explain how the following would be affected when interest rates are cut in UK.			
	(i)	Consumption expenditure	[2]		
		Cut in interest rates \rightarrow Cost of borrowing falls [1m] \rightarrow Households borrow to buy big-ticket items \rightarrow Consumption expenditure (C) rises [1m]			
		Or			
		Cut in interest rates \rightarrow returns to savings falls [1m] \rightarrow household cut down on saving and allocate more disposable income to consumption \rightarrow C rises. [1m]			
	(11)				
	(11)	Investment expenditure	[2]		

	Cut in interest rates \rightarrow Cost of borrowing falls \rightarrow Previously unprofitable projects now become profitable [1m] \rightarrow Investment expenditure (I) rises [1m]			
(c)	Discuss whether the data is useful to assess changes in living standards in the UK from 2015 to 2017.	[8]		
	Data provided suggest that living standards in UK has fallen			
	Material standard of living has fallen Extract 4: "Some jobs will go, and wage growth will fall."			
	Extract 5: "overall inflation up to 3.1 per cent last month, with wage inflation stuck at just over 2 per cent… "; "so real pay levels have been flat."			
	Table 2: Nominal GDP per capita; trade in goods and services; average annual hours worked per worker			
	Overall inflation at 3.1% while wage inflation stuck at 2% \rightarrow rise in general price level faster than increase in wages; Nominal GDP per capita falling \rightarrow Real purchasing power reduced, negatively affecting households' ability to consume goods and services \rightarrow Less goods and services consumed			
	Current account deficit falling / Current account balance improving could be due to falling M \rightarrow Spending on imports fall			
	Non-material standard of living has fallen Table 2: Average annual hours worked per worker Rise in average annual hours worked implies a fall in leisure hours			
	Data provided suggest that living standards in UK may not have			
	Table 2: Annual GDP growth rate still positive; Gini coefficient: 0.50 \rightarrow 0.489; Unemployment rate falling			
	Material standard of living rose Real GDP growth rate still positive implies that real national income is still increasing; Falling unemployment rate implies more resources are employed \rightarrow Rise in factor income \rightarrow Rise in purchasing power \rightarrow More goods and services consumed			
	Gini coefficient falling implies a more equitable distribution of income as economy expands at a slower rate \rightarrow Inclusive growth achieved			
	Overall conclusion Even though the data provide information on how material and non- material aspects of standard of living UK may have changed from 2015 to 2017, it seems to be sending mixed signals.			
	Thus, data provided is useful to a certain extent. More information is required, for instance, data showing changes in negative externalities, literacy rates, life expectancy would be useful to ascertain whether overall living standards in the UK has risen or fallen.			

		Mark schomo				
	Levels Descriptors Marks		Marks			
		L3	For a well-developed, balanced answer that explained whether data provided is useful to access changes in living standards in UK.	5 - 6		
		L2	For a developed but 1-sided answer on how the data is OR is not useful to access changes in living standards in UK.	3 – 4		
			For an under-developed (have gaps) but somewhat balanced (2-sided) answer on whether data provided is useful to access changes in living standards in UK.			
		L1	For a descriptive / generic account (lifting of evidence from case material) of whether data provided can or cannot suggest that living standards may or may not have fallen	1 – 2		
		E	For an overall judgement on the overall usefulness of the data in accessing changes in living standards in UK.	1 – 2		
(1)	<i>(</i>)				101	
(d)	(1)	Explain the likely reason for the change observed in the value of yuan and China's foreign exchange reserves in Figures 2 and 3.			[2]	
		The value reserves	The value of yuan was weakening, and the level of foreign exchange reserves was also falling. [1m]			
		China's central bank, PBOC, could be intervening to support the yuan by selling foreign reserves to buy Chinese yuan to prevent the value of yuan from falling / depreciating further, thus resulting in the fall in the foreign exchange reserves. [2m]				
		Full 2m may be awarded if answers are similar to the 2 nd bullet as the relationship between the value of yuan and foreign exchange reserves can be inferred from the answer.				
	(ii)	With reference to the data, assess whether PBOC should 'step in to slow yuan depreciation'.			[10]	
		Whether PBOC will 'step in to slow yuan depreciation' depends on the benefits and costs of intervention. (Decision-making framework) <u>Thesis: Benefits of stepping in to slow yuan depreciation</u> Evidence				
		E6P4: "Faster declines of the yuan risk reigniting a vicious cycle where expectations for further weakness quicken capital outflows."				
	 Positive impact on China's internal economy PBOC's intervention to slow yuan depreciation will prevent further 					
L	capital outflow due to increased uncertainty \rightarrow prevents further fall					

Mark scheme				
	Levels	Descriptors	Marks	
	L3	For a well-developed explanation of both positive <u>AND</u> negative impact on China's internal <u>AND</u> external economy, with consistent application of AD/AS framework and links to China's economy.	6 - 7	
	L2	For a developed explanation of positive <u>OR</u> negative impact with consistent application of AD/AS framework, and links to China's economy. For an under-developed explanation of positive <u>AND</u> negative impact on China's	3 – 5	
		AD/AS framework or inconsistent application of AD/AS framework or inconsistent links to China's economy.		
	L1	For a descriptive / generic account (lifting of evidence from case material) of the positive and negative impact, without linking to AD/AS framework and China's economy OR For an inaccurate explanation of the positive and negative impact	1 – 2	
	E	For an overall evaluation of whether China should or should not 'step in to slow yuan depreciation'		
		Merely stating that China should / should not step in to slow yuan depreciation with NO attempt to explain	0	
		Weighing of benefits and costs with attempt to explain but inaccurate / incoherent / incomplete	1	
		Weighing of benefits and costs with attempt to explain accurately	2 - 3	
				[Total: 20]
				[10tal. 30]