Past-paper walk-through

Fiscal policy ▪ 5.2

eXercise

Questions in this set

- 9708/11 N25 Q1 ▪ 1 mark
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Question 1

9708/11 N25 ▪ Q1 ▪ 1 mark

1 What is an example of a normative statement?

A Indirect taxes are cheap to collect.

B Indirect taxes are taxes on income.

C Indirect taxes are unfair.

Question 1

D Indirect taxes increase inequality.

Solution 1

Answer: **C**

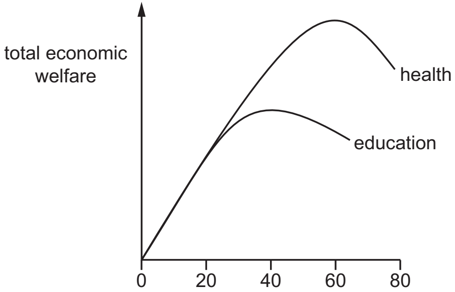
Why

- A normative statement contains a value judgement and cannot be tested against data.
- "Indirect taxes are unfair" is an opinion about what *ought* to be.
- The others are factual claims that evidence could confirm or refute.

Question 11

9708/11 N25 ▪ Q11 ▪ 1 mark

11 The graph shows the total economic welfare derived by citizens from a government's expenditure on health and education services.



Question 11

expenditure ($ billions)

If the government has $60 billion of its budget to allocate between health and education services, which allocation will give its citizens the highest level of welfare?

	health spending ($ billions)	education spending ($ billions)
A	0	60
B	20	40
C	40	20
D	60	0

Solution 11

Answer: **C**

Why

- Total welfare rises with spending but at a diminishing rate, so read the *gradient* of each curve.
- The extra welfare from the last dollar spent is the marginal benefit.
- Welfare is maximised where the marginal benefit of spending is equal in the two areas.

Question 13

9708/11 N25 ▪ Q13 ▪ 1 mark

13 What would be included in a measure of wealth?

A annual income

B benefits and pensions

C interest earned on savings

Question 13

D savings held in bank accounts

Solution 13

Answer: **D**

Why

- Wealth is a *stock* of assets held at a point in time.
- Income is a *flow* received over a period.
- So savings held in a bank account are wealth, while income, benefits and interest received are flows.

Question 6

9708/12 N25 ▪ Q6 ▪ 1 mark

6 What is consumer surplus?

A the amount of a consumer's income less the amount paid in income tax

B the amount of a consumer's income less the amount paid for goods and services

C the amount of a consumer's income received in bonuses and overtime pay

D the amount a consumer is willing to pay for a product less the amount actually paid

Solution 6

Answer: **D**

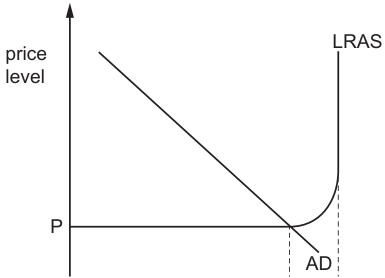
Why

- Consumer surplus is the difference between what a consumer is *willing* to pay and what they actually pay.
- It is measured as the area under the demand curve and above the price.
- It has nothing to do with income or with tax – only with the price paid against the value placed on the good.

Question 24

9708/13 N25 ▪ Q24 ▪ 1 mark

24 The diagram shows an economy in equilibrium with a real output of Y and a price level of P. The government aims to raise real output from Y to full employment (Y_{FE}) without increasing the price level in the long run.



Question 24

Which fiscal policy change is most likely to achieve this aim?

A decreasing the rate of income tax

B decreasing spending on education

C increasing the level of sales tax

D increasing welfare benefit payments

Solution 24

Answer: **A**

Why

- Raising output without raising the price level needs the *supply* side to expand.
- If only aggregate demand rises, the price level rises with output.
- So the policy must shift aggregate supply right, by adding capacity.

Question 26

9708/13 N25 ▪ Q26 ▪ 1 mark

26 Which policy is most likely to have a contractionary effect on national income?

A a reduction in income tax rates

B a reduction in interest rates

C an appreciation in the exchange rate

D an increase in government spending on transport infrastructure

Solution 26

Answer: **C**

Why

- A contractionary policy reduces aggregate demand.
- Higher taxes, lower government spending, higher interest rates or an appreciation all do that.
- Cutting income tax or interest rates would be expansionary instead.

Question 21

9708/14 N25 ▪ Q21 ▪ 1 mark

21 What is an example of expansionary fiscal policy?

A an increase in income tax

B an increase in private sector investment

C an increase in spending on public goods

D an increase in the money supply

Solution 21

Answer: **C**

Why

- Expansionary fiscal policy means the government spending more or taxing less.
- Increased spending on public goods is exactly that.
- Private sector investment is not government policy, and raising income tax is contractionary.

Question 25

9708/14 N25 ▪ Q25 ▪ 1 mark

25 An increase in interest rates is an example of which type of policy?

A contractionary fiscal policy

B contractionary monetary policy

C expansionary monetary policy

D restrictive supply-side policy

Solution 25

Answer: **B**

Why

- Interest rates are the central bank's instrument, so this is monetary policy.
- Raising them reduces borrowing and spending, so it reduces aggregate demand.
- That makes it contractionary monetary policy.

Question 25

9708/11 J25 ▪ Q25 ▪ 1 mark

25 The table shows the amount of tax paid on three different levels of income.

Which combination shows a proportional income tax system?

	tax paid on annual income of \$10 000	tax paid on annual income of \$20 000	tax paid on annual income of \$40 000
A	1000	1000	1000
B	1000	1500	2000
C	1000	2000	4000
D	[illegible]	[illegible]	[illegible]

Question 25

D	1000	2500	8000

Solution 25

Answer: **C**

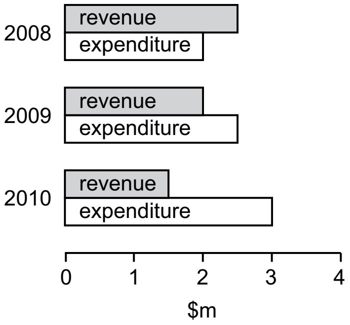
Why

- A proportional tax takes the same *percentage* of income at every income level.
- So divide the tax paid by the income in each row.
- The system is proportional where those ratios are all equal – progressive if they rise, regressive if they fall.

Question 22

9708/1 23 ▪ Q22 ▪ 1 mark

22 The diagram shows a government's revenue and expenditure for three years.



Question 22

What can be concluded from the diagram?

A A budget deficit was replaced by a budget surplus.

B A budget deficit increased.

C The economy moved from a point within its production possibility curve (PPC) to a point on it.

D The yield from taxation continuously increased.

Solution 22

Answer: **B**