Past-paper walk-through

Current account of the balance of payments ▪ 6.3

eXercise

Questions in this set

- 9708/11 N25 Q29 ▪ 1 mark
- 9708/12 N25 Q29 ▪ 1 mark
- 9708/13 N25 Q30 ▪ 1 mark
- 9708/14 N25 Q18 ▪ 1 mark
- 9708/14 N25 Q20 ▪ 1 mark
- 9708/22 N25 Q4 ▪ 20 marks
- 9708/23 N25 Q5 ▪ 20 marks
- 9708/11 J25 Q29 ▪ 1 mark
- 9708/1 23 Q21 ▪ 1 mark

Reading the mark scheme

- **B1** a mark that stands on its own – the point is either made or not.
- **M1** a *method* mark: the right approach, even if the number is wrong.
- **A1** an *answer* mark, and it usually needs its M mark first.
- **C1** a working mark on the way to the answer.
- // separates answers the examiner accepts equally.
- **ecf** = error carried forward: a later part is marked on your own earlier answer.
- **owtte** = "or words to that effect" – the wording need not match.

Question 29

9708/11 N25 ▪ Q29 ▪ 1 mark

29 What would **not** be included in the current account of the balance of payments?

A income earned outside the country that is transferred into the country

B value of food and raw materials produced and consumed within the country

C value of food and raw materials that are exported

D value of telecommunications services that are imported

Solution 29

Answer: **B**

Why

- The current account records trade in goods and services, primary income and secondary income.
- So exported food, and income earned abroad and sent home, both belong there.
- A purchase of foreign assets or shares is a *financial* account item, not a current account one.

Question 29

9708/12 N25 ▪ Q29 ▪ 1 mark

29 What is the effect of a cut in a country's income tax rates on its exports and imports?

	exports	imports
A	fall	fall
B	fall	unchanged
C	unchanged	fall
D	unchanged	rise

Solution 29

Answer: **D**

Why

- Cutting income tax raises disposable income, so consumption rises.
- Part of that extra spending goes on imported goods, so imports rise.
- Exports depend on foreign incomes and on competitiveness, so they are unchanged.

Question 30

9708/13 N25 ▪ Q30 ▪ 1 mark

30 The main export of country X is oil. The world demand for oil is price inelastic. The world supply of oil is reduced by the major oil producing countries, including country X. Imports into country X are unchanged.

What are the effects of this action by the major oil producing countries on the terms of trade and the current account of the balance of payments in country X?

	terms of trade	current account
A	increases	increases
B	increases	decreases
C	decreases	increases
D	decreases	decreases

Question 30

Solution 30

Answer: **A**

Why

- World supply of oil falls, so the world price rises.
- Demand is price inelastic, so the quantity sold falls proportionately less than the price rises.
- So total export revenue *increases* – which is exactly why producers restrict supply.

Question 18

9708/14 N25 ▪ Q18 ▪ 1 mark

18 An open economy with a government is in equilibrium at a national income of $900 million.

Households spend $700 million and save $50 million.

Firms spend $100 million on investment.

The government spends $150 million and has a balanced budget.

How much is spent on exports and imports?

Question 18

	export spending ($ million)	import spending ($ million)
A	100	100
B	100	50
C	50	100
D	50	50

Solution 18

Answer: **C**

Why

- In equilibrium, total injections equal total withdrawals.
- Withdrawals are saving, taxation and imports; injections are investment, government spending and exports.
- So work out the missing figure by setting the two totals equal – 900 of income has to be fully accounted for.

Question 20

9708/14 N25 ▪ Q20 ▪ 1 mark

20 When calculating national income by the income method, what would **not** be included?

A income from abroad

B profits of private sector businesses

C rent from the ownership of land

D transfer payments

Solution 20

Answer: **D**

Why

- The income method adds up all incomes earned from producing output: wages, rent, interest and profit.
- A transfer payment is not earned from production, so it is excluded.
- Income from abroad is added separately to get *national* rather than domestic income.

Question 4

9708/22 N25 ▪ Q4 ▪ 20 marks

4 (a) Explain three components of the current account of the balance of payments and consider the extent to which a depreciation in the exchange rate will always lead to a surplus on the current account. [8] (b) Assess the extent to which the use of supply-side policy would be the best way to reduce a deficit on the current account of the balance of payments. [12] OR

(a) (a) Explain three components of the current account of the balance of payments and consider the extent to which a depreciation in the exchange rate will always lead to a surplus on the current account. [8] **[8]**

(b) (b) Assess the extent to which the use of supply-side policy would be the best way to reduce a deficit on the current account of the balance of payments. [12] **[12]**

Solution 4

(a) Mark scheme

- Explain three components of the current account of the balance of
- payments and consider the extent to which a depreciation in the
- exchange rate will always lead to a surplus on the current account.
- Follow the point-based marking guidance at the top of this mark scheme and
- award:
- up to 3 marks for AO1 Knowledge and understanding up to 3 marks for AO2
- Analysis
- up to 2 marks for AO3 Evaluation.

Solution 4

- AO1 Knowledge and Understanding (max 3 marks)
- Knowledge and basic understanding of 3 components of the current account.
- The component must be identified by name together with a brief explanation by
- name i.e., 3 from
-
  -
- Trade in goods – the value of physical goods e.g., computers
-
  -
- Trade in services – the value of invisible goods e.g., insurance/tourism
-
  -
- Primary income – e.g., the dividend income earned from overseas

Solution 4

- investments
- ▪
- Secondary income – e.g., the income from overseas aid or worker
- remittances sent back to their own country. (3 × 1)
- AO2 Analysis (max 3 marks)
- A depreciation in the exchange rate will make exports appear cheaper and/or
- imports more expensive (1), this should increase export revenue and/or reduce
- import expenditure and lead to a surplus (1). Also other components of the
- current account may influence whether the current account goes into surplus or
- not (1). N.B. if the impact of other sections of the current account are not

Solution 4

- considered, maximum mark of 2.
- AO3 Evaluation (max 2 marks)
- Of an overall assessment of the extent to which a depreciation in the exchange
- rate will always lead to a surplus on the current account – for example,
- reference may be made to the relevance of PED values and also the value of
- other sections of the current account. Reserve 1 mark for a valid conclusion.
- 8
- AO1 Knowledge and understanding
- 3
- AO2 Analysis

Solution 4

- 3
- AO3 Evaluation
- 2
- 9708/22
- October/November
- 2025

Solution 4

(b) Mark scheme

- Assess the extent to which the use of supply-side policy would be the
- best way to reduce a deficit on the current account of the balance of
- payments.
- Use Table A: AO1 Knowledge and understanding and AO2 Analysis and Table
- B: AO3 Evaluation to mark candidate responses to this question.
- AO1 and AO2 out of 8 marks. AO3 out of 4 marks.
- Indicative content
- Responses may include:

Solution 4

- AO1 Knowledge and understanding and AO2 Analysis
- An analysis of the advantages and disadvantages of using supply-side policy
- to reduce a deficit e.g.,
-
  -
- It is likely to be more effective in the long run and less costly to the
- economy.
-
  -
- it may reduce the possibility of retaliation by other countries BUT
-
  -
- it will have an opportunity cost and is not likely to be a short-term solution.

Solution 4

- Examples of supply side policy may include:
- ▪
- Investment in education and training to improve worker productivity and
- entrepreneurship which may reduce costs and lead to increased
- competitiveness of domestic goods, therefore increasing exports and
- reducing imports
- ▪
- Export subsidies and subsidies for domestic industries competing against
- imported goods
- ▪

Solution 4

- Policies to reduce red tape and bureaucracy to encourage competition to
- reduce costs
- ▪
- Investment in infrastructure to reduce costs of production
- However:
- ▪
- They take time and can be costly, which is unlikely to reduce a deficit in
- the short term
- ▪
- Other policies such as contractionary fiscal and monetary policy may

Solution 4

- work more quickly together with protectionist policies e.g., tariffs and
- currency depreciation. These policies should be analysed in terms of their
- strengths and weaknesses in reducing a current account deficit.
- Guidance: Answers that do not refer to the policies in terms of reducing a
- current account deficit cannot gain more than a mid-Level 2 mark.
- Level 1 responses will be assertive and lacking in explanations / mainly
- descriptive and/or or mainly lacking in relevance to the question.
- Level 2 responses may contain some inaccuracies and may be one sided.
- Analysis will be explained at least in part and will be largely relevant to the
- question.

Solution 4

- Level 3 responses will consider alternative policies / concepts etc. and will
- be balanced. Explanations of points raised will be offered and will be accurate
- and relevant to the question.
- 12
- 9708/22
- October/November
- 2025
- AO3 Evaluation
- That clearly analyses both sides of the question and comes to a valid
- conclusion.

Solution 4

- Accept all valid responses.
- A one-sided response cannot gain any marks for evaluation.
- AO1 Knowledge and understanding and AO2 Analysis
- 8
- AO3 Evaluation
- 4
- 9708/22
- October/November
- 2025
- OR

Question 5

9708/23 N25 ▪ Q5 ▪ 20 marks

5 (a) Explain two reasons why an economy may have a deficit on the current account of its balance of payments and consider whether its government is likely to be concerned about this deficit.
[8]
(b) Assess whether it is better to use protectionist policies or contractionary policies to reduce a deficit on the current account of the balance of payments. [12]

(a) (a) Explain two reasons why an economy may have a deficit on the current account of its balance of payments and consider whether its government is likely to be concerned about this deficit. [8] **[8]**

(b) (b) Assess whether it is better to use protectionist policies or contractionary policies to reduce a deficit on the current account of the balance of payments. [12]**[12]**

Solution 5

(a) Mark scheme

- Explain two reasons why an economy may have a deficit on the current
- account of its balance of payments and consider whether its
- government is likely to be concerned about this deficit.
- Follow the point-based marking guidance at the top of this mark scheme and
- award:
- up to 3 marks for AO1 Knowledge and understanding up to 3 marks for AO2
- Analysis up to 2 marks for AO3 Evaluation.
- AO1 Knowledge and Understanding (max 3 marks)

Solution 5

- The current account records trade in goods and services, primary income, and
- secondary income between countries/A current account deficit occurs when the
- value of imports of goods or services, primary and secondary income exceeds
- the value of exports (1). Two marks for an accurate explanation of two
- reasons–e.g., low international competitiveness, (1) - if the country experiences
- strong domestic growth. 1
- AO2 Analysis (max 3 marks)
- An explanation of why the government is likely to be concerned at about this
- deficit. For example, a current account deficit could lead to downward pressure
- on the exchange rate, making imports more expensive and potentially causing

Solution 5

- inflation (1). Persistent deficits may reduce confidence among foreign investors,
- limiting inflows of capital needed to finance growth (1). However, the
- government may not be concerned if the deficit is temporary or caused by for
- example, high investment imports that may boost future productive capacity 1
- A max of 2 marks for either perspective.
- AO3 Evaluation (max 2 marks)
- An assessment of the extent that the government is likely to be concerned. For
- example, the level of concern will depend on the size, duration and cause of the
- deficit and how it is financed (1).
- 8

Solution 5

- AO1 Knowledge and understanding
- 3
- AO2 Analysis
- 3
- AO3 Evaluation
- 2
- 9708/23
- October/November
- 2025

Solution 5

(b) Mark scheme

- Assess whether it is better to use protectionist policies or
- contractionary policies to reduce a deficit on the current account of the
- balance of payments.
- Use Table A: AO1 Knowledge and understanding and AO2 Analysis and
- Table B: AO3 Evaluation to mark candidate responses to this question.
- AO1 and AO2 out of 8 marks. AO3 out of 4 marks.
- Indicative content
- Responses may include:

Solution 5

- AO1 Knowledge and understanding and AO2 Analysis
- Possible reasons why protectionist policies are the best way to reduce a
- deficit on the current account of the balance of payments.
- ▪
- They may reduce the value of imports, which helps to lower the current
- account deficit by limiting the outflow of money from the economy.
- ▪
- They may protect domestic industries from foreign competition, allowing
- local firms to grow and potentially increase exports in the future.
- However

Solution 5

- ▪
- They can raise prices for consumers, as tariffs or quotas make imported
- goods more expensive, reducing consumer welfare.
- ▪
- Other countries may retaliate with their own trade barriers, which could
- reduce exports and harm the economy further.
- Possible reasons why contractionary policies are the best way to reduce
- a deficit on the current account of the balance of payments.
- ▪
- They can reduce domestic demand, which lowers imports and helps

Solution 5

- decrease the current account deficit.
- ▪
- They may help control inflation by reducing spending in the economy,
- which can stabilise the exchange rate and make exports more
- competitive.
- However
- ▪
- They can slow economic growth and increase unemployment, as lower
- demand reduces output in domestic industries.
- ▪

Solution 5

- They may reduce consumer and business confidence, which can further
- decrease spending and investment, worsening the economic slowdown.
- Guidance: The assessment of both perspectives must be in the context of
- the reducing a current account deficit and not a general explanation of
- both policies.
- Level 1 responses will be assertive and lacking in explanations / mainly
- descriptive and/or or mainly lacking in relevance to the question.
- 12
- 9708/23
- October/November

Solution 5

- 2025
- Level 2 responses may contain some inaccuracies and may be one sided.
- Analysis will be explained at least in part and will be largely relevant to the
- question.
- Level 3 responses will consider alternative policies / concepts etc. and will
- be balanced. Explanations of points raised will be offered and will be accurate
- and relevant to the question.
- AO3 Evaluation
- Requires an assessment of whether it is better to use protectionist policies or
- contractionary policies to reduce a deficit on the current account of the

Solution 5

- balance of payments. For example–Protectionist policies may work more
- quickly to reduce imports and protect domestic industries, but they risk
- retaliation from other countries and higher prices for consumers. Alternatively,
- contractionary policies may take longer to reduce the deficit but may help
- control inflation, though they may slow economic growth and increase
- unemployment.
- Accept all valid responses.
- A one-sided response cannot gain any marks for evaluation.
- Accept all valid responses.
- AO1 Knowledge and understanding and AO2 Analysis

Solution 5

- 8
- AO3 Evaluation
- 4

Question 29

9708/11 J25 ▪ Q29 ▪ 1 mark

29 Primary income and secondary income are components of the current account of the balance of payments.

Which option correctly identifies an example of primary income and secondary income?

	primary income	secondary income
A	government transfers	income from profits earned abroad
B	income from profits earned abroad	dividends earned on foreign shares
C	income from profits earned abroad	government transfers
D	workers' remittances	income from profits earned abroad

Solution 29

Answer: **C**

Why

- Primary income is income earned from ownership of a factor of production abroad – wages, interest, profits, dividends.
- Secondary income is a transfer with nothing given in return – aid, remittances, gifts.
- So the test is whether something was *earned* or simply *transferred*.

Question 21

9708/1 23 ▪ Q21 ▪ 1 mark

21 A government succeeds in changing a current account deficit into a current account surplus.

Why might this current account surplus increase the country's inflation rate?

A It raises Aggregate Demand.

B It raises production costs.

C It reduces the exchange rate.

D It reduces the money supply.

Solution 21

Answer: **A**