Solutions

Economics answers are marked by **level of response** against the assessment objectives: award **AO1** knowledge, **AO2** application, **AO3** analysis and **AO4** evaluation.

Each answer shows the steps, then the **result**.

2.1

- when heavy government borrowing raises interest rates and so reduces private-sector investment (2 for a clear definition; 1 for a partial idea)

2.2

- that as the tax rate rises, tax revenue first rises but then falls, because very high rates discourage work and encourage avoidance (2 for a clear statement; 1 for a partial idea)

2.3

- any one of: it works with a long time lag; it is weak in a deep slump (a liquidity trap); it cannot fix structural problems (1)

3.1 B

- Above the revenue-maximising rate, higher tax rates lower revenue

3.2

- *[6]* AO1 1 + AO3 up to 5 — to fund a deficit the government borrows heavily
- this raises the demand for loanable funds
- the interest rate rises
- dearer borrowing means firms invest less
- public spending "crowds out" private investment, reducing the net effect on AD

3.3

- *[12]* AO1/AO2/AO3 up to 8 + AO4 up to 4. **Supply-side:** the only tool that raises capacity and productivity, giving growth *with* low inflation — but slow and costly. **Demand-side (fiscal/monetary):** quick to raise output but mainly short-run and inflation-prone. Judgement: for *long-term* growth supply-side policy should lead, supported by stable demand-side policy — the best mix depends on the time horizon and the economy's starting point