## 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**

- the nominal rate is the everyday market rate between two currencies; the real rate adjusts it for differences in prices, showing true competitiveness (2 for a clear difference; 1 for a partial idea)

**2.2**

- an average of a currency's value against all its trading partners, weighted by how much trade is done with each (2 for a clear definition; 1 for a partial idea)

**2.3**

- a depreciation is a fall in value under a floating system (set by the market); a devaluation is a deliberate fall under a fixed system (set by the central bank) (2 for a clear difference; 1 for a partial idea)

**3.1 C**

- A deliberate fall under a fixed system is a devaluation

**3.2**

- *[8]* AO1 1 + **AO3 diagram up to 4** (demand for the currency shifts left, rate falls) + AO2/AO3 up to 3 — fewer exports sold means foreigners need less of the currency
- demand for it shifts left
- with supply unchanged the exchange rate falls (a depreciation)

**3.3**

- *[12]* AO1/AO2/AO3 up to 8 + AO4 up to 4. **Fixed:** gives certainty for traders and investors and disciplines inflation — but needs large reserves and removes monetary independence. **Floating:** adjusts automatically and frees monetary policy — but can be volatile and speculative. Judgement: neither is always better — a fixed rate suits a country seeking stability and credibility, a floating rate one wanting policy freedom; it depends on the economy's needs