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 price of one currency in terms of another (2 for a clear definition; 1 for a partial idea)

2.2

- exports become cheaper (to foreigners) and imports become dearer (2 for both; 1 for one)

2.3

- a floating rate is set freely by demand and supply; a fixed rate is held at a set value by the central bank (2 for a clear difference; 1 for a partial idea)

3.1 B

- A depreciation makes exports cheaper and imports dearer

3.2

- *[8]* AO1 1 + **AO3 diagram up to 4** (demand for the currency shifts right, rate rises) + AO2/AO3 up to 3 — foreigners buying more exports must buy the currency
- demand for it rises
- with supply unchanged, the exchange rate rises (an appreciation)

3.3

- *[12]* AO1/AO2/AO3 up to 8 + AO4 up to 4. **Good:** cheaper exports and dearer imports can raise net exports, improving the current account and supporting jobs. **Bad:** dearer imports raise costs and can cause cost-push inflation; the benefit depends on the **Marshall–Lerner condition** (elastic demand) and may be slow (the J-curve). Judgement: a depreciation helps if export and import demand are elastic, but it risks inflation — its effect depends on elasticities and the cause of the fall