Solutions

Marking: **K** = knowledge, **App** = using the data or case, **An** = analysis (explaining each step: cause, then effect), **Ev** = evaluation (a judgement with a reason). In calculations, **M1** is for the method and **A1** for the answer. Longer answers are marked in levels: the top level needs clear analysis **and** a judgement with a reason.

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

2.1

- $1/(0.1 + 0.2 + 0.2)$
- **2**

2.2

- $30/40$
- **0.75**

3.1

- a deflationary gap: total spending is too low to reach full-employment output, so there is unemployment (K)
- an inflationary gap: total spending is greater than full-employment output (K)
- output cannot rise further, so the extra spending pushes up prices (An)

3.2

- if injections are greater than withdrawals, more money enters the flow than leaves, so income rises (An)
- if withdrawals are greater, income falls (An)
- only when they are equal is there no pressure for income to change (K)

3.3

(a) $k = 1/0.2 = 5$; $20 \times 5 = \$\mathbf{100}$bn

(b) the \$20bn becomes income for builders and suppliers (An); they spend 80% of it, \$16bn, which becomes someone else's income (An); this is spent again, \$12.8bn, and so on, each round smaller (An); the total of all rounds is 5 times the first spending (An)

(c) points to include:

- the MPC may fall if people save more because they are worried about jobs (An)
- some spending goes on imports, and taxes take part of each round (An)
- if the economy is near full capacity, prices rise instead of output (An)
- higher government borrowing may raise interest rates and reduce private investment (crowding out) (An)
- the full effect takes time (An)
- judgement: the rise is likely to be smaller than \$100bn, especially in an open economy near capacity (Ev)

Levels: **top** (6–8) clear analysis, each step explained, and a judgement with a reason; **middle** (3–5) some analysis, judgement weak or missing; **bottom** (1–2) relevant points, little explanation.