Past-paper walk-through

Fiscal policy ▪ 4.2

eXercise

Questions in this set

- 0455/11 N25 Q18 ▪ 1 mark
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Question 18

0455/11 N25 ▪ Q18 ▪ 1 mark

18 A government's spending currently equals its revenue. The government decides to decrease its spending.

What is the most likely effect of this in the short run?

A a budget deficit

B a budget surplus

C an increase in output

D an increase in tax revenue

Solution 18

Answer: **B**

Why

- A balanced budget becoming lower spending means revenue now exceeds spending – a surplus.
- Less government spending is a withdrawal from the circular flow.
- So aggregate demand falls, and with it output and employment in the short run.

Question 19

0455/11 N25 ▪ Q19 ▪ 1 mark

19 What is **not** a monetary policy measure?

A changes in income tax rates

B changes in interest rates

C changes in the exchange rate

Question 19

D changes in the money supply

Solution 19

Answer: **A**

Why

- Monetary policy uses interest rates, the money supply and the exchange rate.
- Income tax is a *fiscal* instrument, controlled by the government rather than the central bank.
- So changing income tax rates is fiscal policy, not monetary.

Question 18

0455/12 N25 ▪ Q18 ▪ 1 mark

18 A government collects the following revenue in a year.

	$m
taxes on goods	30
taxes on income	500
taxes on services	20
customs and excise duties	50

Question 18

What is the amount of indirect tax revenue?

A $30m **B** $70m **C** $100m **D** $500m

Solution 18

Answer: **C**

Why

- Direct taxes are levied on income and wealth; indirect taxes on spending.
- So taxes on income are direct, while taxes on goods, services and customs duties are indirect.
- Add the categories in each group before comparing.

Question 21

0455/13 N25 ▪ Q21 ▪ 1 mark

21 Which supply-side policy measure would most likely cause the greatest increase in labour productivity in a country?

A a decrease in the rate of corporation tax

B a reduced top rate of income tax

C improved education and training provision

D privatisation of a state-owned industry

Solution 21

Answer: **C**

Why

- Labour productivity is output per worker.
- It rises most when workers become more skilled or better equipped.
- Education and training raise it directly; a corporation tax cut works only indirectly, through investment.

Question 21

0455/11 J25 ▪ Q21 ▪ 1 mark

21 Which policy decision is most likely to cause economic growth?

A an increase in corporation tax rates

B an increase in interest rates

C an increase in the amount workers can earn before paying income tax

D an increase in the government's regulations for starting a new business

Solution 21

Answer: **C**

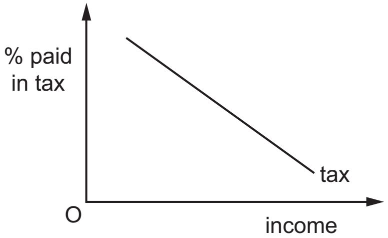
Why

- Economic growth needs aggregate demand or productive capacity to rise.
- Lower taxes, lower interest rates or more government spending all raise demand.
- Raising corporation tax or interest rates would restrain the economy instead.

Question 18

0455/12 J25 ▪ Q18 ▪ 1 mark

18 The diagram shows the percentage of income taken by a tax at different levels of income.



Which term is used to describe the tax?

Question 18

A indirect

B progressive

C proportional

D regressive

Solution 18

Answer: **D**

Why

- A tax whose *percentage* rises with income is progressive.
- One whose percentage stays the same is proportional.
- One whose percentage *falls* as income rises is regressive.

Question 18

0455/13 J25 ▪ Q18 ▪ 1 mark

18 A country's unemployment rate increased from 3.6% to 4.2% in one year.

What might be the consequences for tax revenues and welfare payments?

	tax revenues	welfare payments
A	decrease	decrease
B	decrease	increase
C	increase	decrease
D	increase	increase

Question 18

Solution 18

Answer: **B**

Why

- More unemployment means fewer people earning and paying income tax.
- So tax revenue falls.
- At the same time more people claim benefits, so welfare payments rise.

Question 18

0455/11 N24 ▪ Q18 ▪ 1 mark

18 The table shows a forecast for a government budget for year 1 and for year 2.

	year 1 $bn	year 2 $bn
revenue	50	55
spending	60	60

What does the forecast government budget for year 2 show?

A The budget deficit decreased when compared with year 1.

B The budget deficit increased when compared with year 1.

Question 18

C The budget surplus decreased when compared with year 1.

D The budget surplus increased when compared with year 1.

Solution 18

Answer: **A**

Why

- A budget deficit means spending exceeds revenue; a surplus means the reverse.
- So compare the two rows for each year.
- Then see whether the gap is widening or narrowing between year 1 and year 2.

Question 18

0455/13 N24 ▪ Q18 ▪ 1 mark

18 The table shows earnings and total income tax paid per year.

earnings $	total income tax paid $
5000	1000
8000	2000
9000	3000

Which type of tax system does this illustrate?

Question 18

A indirect

B progressive

C proportional

D regressive

Solution 18

Answer: **B**

Why

- Work out the tax as a *percentage* of earnings at each level.
- $1000/5000 = 20\%$, $2000/8000 = 25\%$, $3000/9000 = 33\%$.
- The percentage rises with income, so the system is progressive.