Solutions

Marking: **K** knowledge, **App** application to the case, **An** analysis (a developed chain of reasoning), **Ev** evaluation (a justified judgement); calculations earn **M1** for the method and **A1** for the answer.

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

2.1

- $(126 - 120) \div 120 \times 100$
- $=$ **5** %

2.2

- the pension stays at \$800 while **prices rise** (K)
- so it buys fewer goods: the pensioner's **real income** falls (An)

2.3

- $0.6 \times 10 + 0.4 \times 5 = 6 + 2$
- $=$ **8** %

3.1

B

3.2

(a)

- $(120 - 60) \div 60 \times 100$
- $=$ **100** %

(b)

- oil is an input for **transport**, energy and plastics (K)
- firms' **costs of production** rise (An)
- to protect profits, firms raise their **prices** (An)
- as many prices rise together, the general price level rises; workers then ask for higher wages, pushing costs up again (App)

(c) a developed chain, for example:

- if prices rise faster than in other countries, the country's goods become **dearer** abroad (K)
- foreign buyers switch to cheaper rivals (An)
- **exports** fall, so manufacturers sell less (App)
- they cut output and jobs (An)
- the current account may worsen as exports fall and imports look cheaper (An)

(d) deflation worse: (An)

- people **delay** spending as they expect lower prices, so demand, output and jobs fall
- the real value of **debts** rises, so borrowers struggle; firms cut wages; hard for interest rates to fix

inflation worse: (An)

- high inflation erodes savings and fixed incomes; harms exports; very high inflation destroys trust in money
- mild deflation from cheaper technology can raise living standards

judgement: (Ev) for example, persistent deflation is usually more harmful than low inflation because it can lock an economy into falling demand; but rapid inflation is worse than mild deflation, so the aim is low, stable inflation.

Level 3 (6–8): both sides analysed and a justified judgement. Level 2 (3–5): one side analysed or both explained. Level 1 (1–2): simple points.