Solutions

Marking: **K** knowledge, **App** use of the case or data, **An** analysis (a chain of reasons: cause, then effect), **Ev** evaluation (a judgement with a reason). In calculations, **M1** is for the method and **A1** for the answer; **B1** is an independent mark.

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

2.1

spending $\dfrac{1}{0.2} = \mathbf{5}$

tax $-\dfrac{0.8}{0.2} = \mathbf{-4}$

2.2

multiplier $\dfrac{1}{0.4} = 2.5$

$\Delta Y = 2.5 \times 20 = £\mathbf{50}$bn

2.3

fiscal: (a), (e)

monetary: (b), (d)

supply-side: (c), (f)

2.4

recognition: seeing the shock in the data

implementation: deciding and acting

impact: the time for the effect to work; longer for monetary policy, while implementation is longer for fiscal

3.1

(a) $\dfrac{90}{4} = £\mathbf{22.5}$bn

(b) tax multiplier -3: $\dfrac{90}{3} = £\mathbf{30}$bn

(c) balanced-budget multiplier 1: both up by £**90**bn

(d) $\dfrac{1}{1 - 0.75 + 0.15} = 2.5$; $\dfrac{90}{2.5} = £\mathbf{36}$bn

3.2

(a) net injection $40 - 15 = 25$; $\Delta Y = 4 \times 25 = £\mathbf{100}$bn

(b) borrowing raises the demand for loans, so rates rise and private investment falls; it is small in a deep recession, when rates are low and firms are not borrowing much anyway

3.3

(a) a demand shock moves inflation and output the same way, so one policy fixes both; a supply shock raises inflation and lowers output, so raising rates cuts inflation but deepens the downturn

(b) **5–6**: for: 8% is far above target, and if wage deals start to expect high inflation it will last (An); a rate rise keeps expectations near target (App); against: the shock comes from energy prices, which rates cannot lower, and output is already falling, so unemployment rises further (An); lags mean the effect lands after the shock may have passed (Ev); judgement with a reason, e.g. a small rise with clear guidance, plus targeted fiscal help for energy bills (Ev). **3–4**: one side analysed, or both without a judgement. **1–2**: relevant points.

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