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General Certificate of Education

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## Economics

### Assessment Unit A2 2

*assessing*

### Module 4: The International Economy

[A2E21]

FRIDAY 29 JANUARY, AFTERNOON

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A2E21

#### TIME

1 hour 40 minutes.

#### INSTRUCTIONS TO CANDIDATES

Write your Centre Number and Candidate Number on the Answer Booklet provided.  
Answer Question **1** and any **one** of Questions **2**, **3** or **4**.

#### INFORMATION FOR CANDIDATES

The total mark for this paper is 80.  
Quality of written communication will be assessed in all questions.  
Figures in brackets printed down the right-hand side of pages indicate the marks awarded to each question or part question.

#### ADVICE TO CANDIDATES

You are advised to take account of the marks for each part question in allocating the available examination time.

You **must** answer this question.

- 1 The article below was written in January 2009.

Study it carefully and answer the questions which follow.

## Trade deficit worst ever

The UK deficit in trade in goods soared to £8.3 billion in November 2008, the highest since records began. Of course, this is only part of the UK current account balance and was partly offset by a surplus in trade in services of £3.9 billion. The most recent figures for the current account balance relate to the third quarter of 2008 and show a deficit of £7.7 billion.

1

These figures will have come as a shock to those analysts who had been predicting that the fall in the value of the pound would give a boost to exports and generate an export-led recovery in the economy. In spite of the pound's 23% fall on its trade-weighted index against a basket of other currencies, the value of our exports was down by 6% from October 2008.

2

Commenting on this, Hetal Mehta, senior economic adviser to The Ernst and Young Item Club, said, "The impact of weaker sterling is being completely dwarfed by a collapse in world demand. Given the extent of the depreciation in the pound in the last few months, today's figures are hugely disappointing".

3

Of course the falling pound's failure to provide this stimulus to net exports may just be a matter of timing. With the world awash with unsold stocks, it may take a considerable period before changes in the relative prices of exports and imports have any significant impact on volumes.

4

Indeed, some analysts believe that the plunge in the value of sterling, far from creating a recovery in the economy, has actually deepened the recession. Lack of confidence in the pound has led to a massive outflow of funds from UK banks, which have then found it even more difficult to provide credit to hard-pressed businesses and consumers.

5

The falling pound has also created massive problems for the economy of the Irish Republic and this is particularly true of the tourism and leisure sectors. Failte Ireland's chief executive, Shaun Quinn, estimates that the tourism industry has already lost over 20,000 jobs, and that visitors from Britain are down by 5 per cent. In addition, large numbers of shoppers are crossing the border to buy goods in Northern Ireland. Irish finance minister, Brian Lenihan, described the loss of revenue as huge and that it had made it "very, very difficult" when framing his recent budget. Dublin's Lord Mayor, Eibhlin Byrne, urged shoppers not to go north. She said, "These are critical times. People need to be aware that when they make the decision to go north they are taking their spending out of the city and there will be repercussions".

6

However, a leading economist poured scorn on this appeal to economic patriotism. He described it as nothing more than old fashioned protectionism, “if every country told its citizens not to buy imports then we would be repeating the mistake of the 1930s, making the recession longer and deeper for everyone”.

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- (a)** Explain the difference between the balance of trade in goods and the balance of payments on current account. [6]
- (b)** Explain how the value of the pound can be measured on a “trade-weighted” basis. [6]
- (c)** Analyse how in theory a falling pound could give a stimulus to aggregate demand in the UK. [8]
- (d)** Explain why the falling pound does not appear to be giving this expected stimulus. [10]
- (e)** Critically examine the view of Eibhlin Byrne that citizens of the Republic of Ireland should not make shopping trips to Northern Ireland. [10]

Answer any **one** from Questions 2, 3 or 4.

- 2 (a) Explain what is meant by globalisation. [16]
- (b) Analyse how globalisation has contributed to the rapid spread of recession from one country to another. [16]
- (c) Critically examine the view that the costs of globalisation outweigh its benefits. [16]
- 3 (a) Explain the difference between a free trade area and a customs union. [8]
- (b) Analyse how a customs union may cause both trade creation and trade diversion. [16]
- (c) “Agricultural protectionism by developed countries is the most important source of inefficiency in world trade and should be abolished.” Critically examine this view. [16]
- 4 (a) Explain the difference between tariffs and administrative trade barriers. [8]
- (b) Analyse how the theory of comparative advantage might determine a country’s pattern of international trade. [16]
- (c) “The theory of comparative advantage is based on so many unrealistic assumptions that it cannot be used to justify free trade.” Evaluate this view. [16]

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**THIS IS THE END OF THE QUESTION PAPER**

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