

Answer EITHER Question 1 OR Question 2.

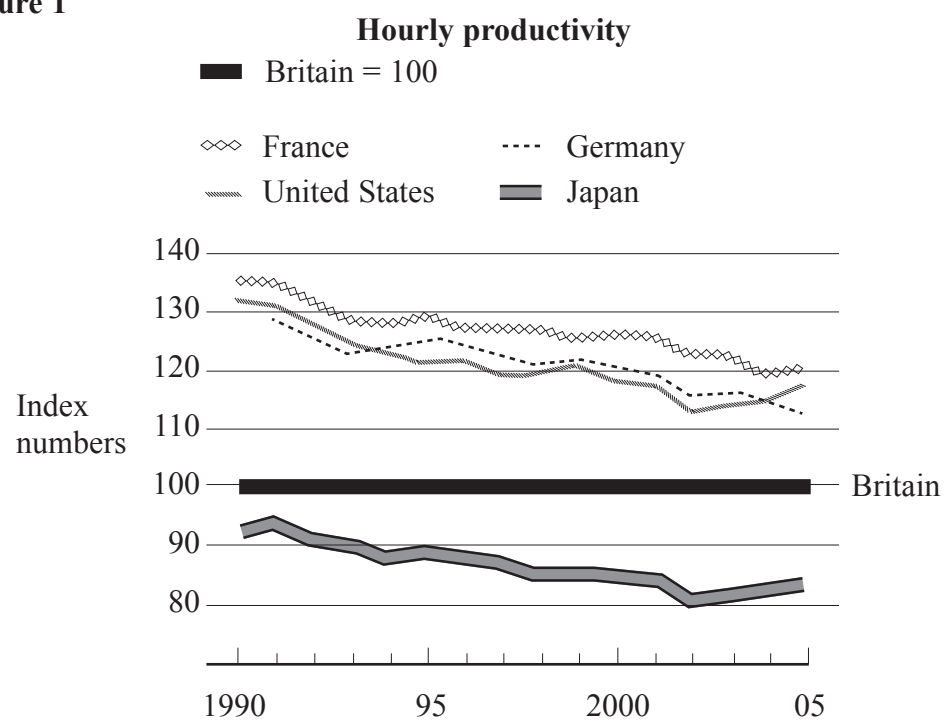
If you answer Question 1 put a cross in this box .

Question 1 **Productivity in Britain**

Extract 1

Productivity is a key area where progress has been disappointing in Britain in the last ten years. Britain's steadily growing economy, stable prices and competitive markets ought to have brought substantial gains in the past decade. Though the gap has narrowed in recent years, the differences remain large.

Figure 1



Source: ONS

The most important reason may be poor skills. Yet it is not the only one because, for example, the British workers who make cars at Honda's plant in Swindon are as productive as their equivalents in other countries. 5

Another factor is the increasing size of the government. 700,000 public-sector jobs have been created since 1997 – just over a quarter of all new jobs. Productivity in the public sector is hard to measure and often low. 10

Fairly full employment may also play a role. If almost everyone is working, less skilled and motivated people also get jobs, reducing overall productivity. That might explain some of the differential with France and Germany but not with America, which also has high employment.

Another explanation is that productivity is usually higher in businesses where employees work with machines or technology. The service sector, which is less capital-intensive, employs a bigger share of the workforce in Britain than it does in 15



Germany, for instance, but again that does not explain the gap with America.

The difference is that America has made particularly big productivity improvements in large-scale retailing whereas in Britain there are tight planning regulations restricting the size of warehouses and retail sites, and lorries have to drive on heavily congested roads. 20

Britain has a history of under investment by both business and government, especially in research and development. At the same time heavier taxes and more regulation are beginning to weigh on firms. In the past ten years the tax burden has risen from 34.8 per cent to 37.3 per cent of GDP, higher than in America, Japan or even Germany. 25
It is estimated that the direct cost to businesses of complying with government rules brought in since 1998 is more than £50 billion.

Source: adapted from *A special report on Britain 'A lost opportunity'* *The Economist* 3 February 2007

(a) With reference to Figure 1,

(i) explain what is meant by the term *hourly productivity*.

(2)

(ii) identify the change in hourly productivity, **relative to that in Britain**, in any **one** country over the period shown.

(3)



Leave blank

(b) (ii) Analyse **two** possible effects of productivity improvements on the British economy. Use an aggregate demand and aggregate supply diagram in your answer.

(6)



Leave
blank

(c) (i) Explain the concept of *full employment* (*Extract 1, line 11*).

(2)

(ii) **Apart from the effect on productivity**, analyse **one** potential problem for an economy experiencing full employment.

(4)





<p>Blank lined area for writing</p>	Leave blank
-------------------------------------	-------------



N 3 0 7 2 7 R A 0 8 2 0





<p>Blank area with horizontal lines for writing.</p>	<p>Leave blank</p>
<p>(15) (Total 40 marks)</p>	<p>Q1</p>



N 3 0 7 2 7 R A 0 9 2 0

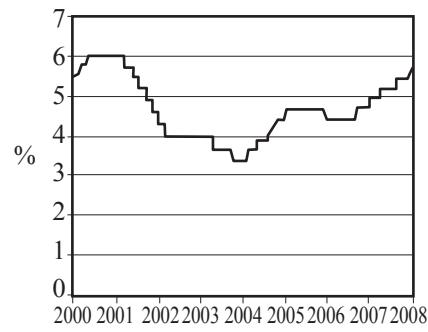


If you answer Question 2 put a cross in this box .

Question 2

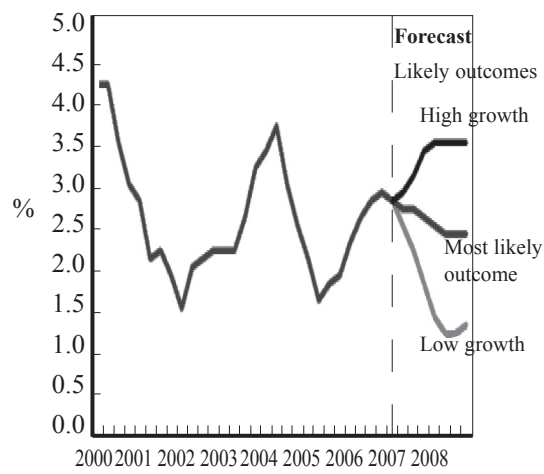
Demand management in Britain

Figure 1: The Bank of England base rate of interest



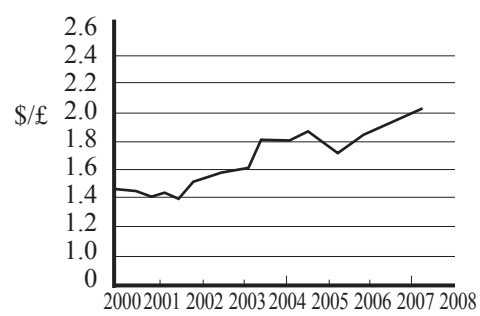
Source: Bank of England www.bankofengland.co.uk

Figure 2: GDP growth, year on year



Source: Price Waterhouse Coopers *Economic Outlook* July 2007 www.pwc.co.uk

Figure 3: The pound against the dollar



Source: Bank of England www.bankofengland.co.uk



Leave
blank

Extract 1

UK growth – likely outcomes

The most likely outcome for the UK economy is that GDP growth will remain at around 2.75 per cent in 2007 before moderating to around 2.5 per cent in 2008. This reflects the impact of tighter monetary and fiscal policy feeding through over the next year. Other factors dampening aggregate demand are the slower rate of consumer spending growth from 2.5 per cent in 2007 to 2.25 per cent in 2008, resulting from the impact of higher interest rates, high debt levels and a cooling house market. Investment is expected to remain a key driver of economic growth, although it is projected to slow down from 6.5 per cent growth in 2007 to around 3.75 per cent growth in 2008. The contribution of net trade to overall GDP growth is projected to be broadly neutral in 2007 and 2008.

Source: Price Waterhouse Coopers *Economic Outlook* July 2007 www.pwc.co.uk

Extract 2

Sterling exchange rates

The pound has once more been in the headlines, recently reaching a 26-year high against the dollar. Against the euro, which is the most significant currency for UK exporters, the pound has been stable at around the current rate since 2002 and is actually 10 per cent or so weaker than around the turn of the decade.

Andrew Sentence, member of MPC, speech: *UK monetary policy: good for business?* 10 July 2007



Leave
blank

(a) With reference to Figure 1 and Extract 1,

(i) explain the concept of *aggregate demand*.

(2)

(ii) outline **two** mechanisms by which interest rates affect the level of aggregate demand.

(4)



(iii) outline **two** sources of information, **apart from exchange rates**, used by the Bank of England’s Monetary Policy Committee when it makes interest rate decisions.

(4)

(c) Evaluate the effects of ‘tighter monetary and fiscal policy’ (*Extract 1, line 3*) on any **two** macroeconomic objectives.





<p>A large rectangular area with a thin border, containing 30 horizontal lines for writing.</p>	<p>Leave blank</p>
---	------------------------



BLANK PAGE



BLANK PAGE



BLANK PAGE

