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Mark Scheme (Results)

January 2016

Pearson Edexcel International Advanced Level in Economics (WEC02) Paper 01 Macroeconomic Performance and Policy

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General Marking Guidance

- All candidates must receive the same treatment. Examiners must mark the first candidate in exactly the same way as they mark the last.
- Mark schemes should be applied positively. Candidates must be rewarded for what they have shown they can do rather than penalised for omissions.
- Examiners should mark according to the mark scheme not according to their perception of where the grade boundaries may lie.
- There is no ceiling on achievement. All marks on the mark scheme should be used appropriately.
- All the marks on the mark scheme are designed to be awarded. Examiners should always award full marks if deserved, i.e. if the answer matches the mark scheme. Examiners should also be prepared to award zero marks if the candidate's response is not worthy of credit according to the mark scheme.
- Where some judgement is required, mark schemes will provide the principles by which marks will be awarded and exemplification may be limited.
- When examiners are in doubt regarding the application of the mark scheme to a candidate's response, the team leader must be consulted.
- Crossed out work should be marked UNLESS the candidate has replaced it with an alternative response.

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Section A: Supported multiple choice

NB: Candidates may achieve up to 3 explanation marks even if the incorrect option is selected.

NB: Candidates may achieve up to 3 marks for explaining three incorrect options (provided three different reasons are offered and each option key is clearly rejected).

Question Number	Indicative Content	Mark
1	**Answer D** **Explanation** • Unemployment where person actively seeking work but unable to find suitable employment(1) • Budget deficit where government expenditure greater than tax receipts(1) • Reducing budget deficit either involves cutting spending(1) • Reducing deficit involves raising tax(1) • Reduced spending may reduce public/private sector jobs raising unemployment(1) • Increased income tax reduces incentive to work this raises unemployment (1) • Accurate diagram showing inward shift in AD up to 2 marks **OR** explanation that reduced government spending, falling AD will reduce real output and employment **Rejection marks:** • A incorrect because reducing net immigration may reduce supply of labour and reduce level of unemployment (1) • B incorrect as lower income tax increases incentive to work and may reduce unemployment/increases aggregate demand(1) • C incorrect as depreciation may increase demand for exports, raise AD and thus increase real output and employment (1)	**(4)**

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Question Number	Indicative Content	Mark
2	**Answer: A** **Explanation** • Example of asset purchases EG government bonds from commercial banks (1) • Definition of Monetary Policy (1) • Raises commercial bank reserves (1) • Defining/linking to quantitative easing (QE) (1) • Definition of deflation as a sustained decrease in the average price level (1) • Likely to make more funds available for lending by the commercial banks(1) • Likely to result in lower interest rates from commercial banks(1) • Increased borrowing and spending may increase AD (1) and raise average price level (1) **OR** • For correct diagram award up to 2 marks showing increase in AD and impact on price level **Rejection marks:** • **B** example of fiscal policy (1) • **C** increase in interest rates likely to reduce AD, average price level and real output (1) • **D** increase in regulation is a direct policy not monetary policy (1)	**(4)**

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Question Number	Indicative Content	Mark
3	**Answer: C** **Explanation** • Identification of increased competition as a supply-side policy/examples of policies to increase competition deregulation and privatisation (1) • Explanation of why a supply side policy might cause shift in LRAS e.g. easier market entry (1) • Increased competition likely to increase efficiency producing rise in real output (1) • Increased efficiency likely to shift LRAS right/outwards shown on diagram(1) • Explanation that lead to outward shift in LRAS (1) lower average price level and rise in real output (1) **OR** • **Correctly** annotated diagram or own diagram (outward shift in LRAS with increased real output and lower average price level labels) (2) **Rejection marks:** • **A** Increased efficiency likely to reduce average price level not increase it (1) • **B** Increased efficiency likely to reduce average price level not increase it (1) **OR** increase real output (1) • **D** Increased efficiency likely to increase real output not decrease it (1)	**(4)**

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Question Number	Indicative Content	Mark
4	**Answer: B** **Explanation** • Appreciation is a rise in value in relation to other currencies(1) **OR** Exchange rate is one currency expressed in terms of another (1) • Exports less price competitive and imports cheaper (1) • Therefore decrease in net exports (x-m) reducing AD (1) • Imports cheaper may decrease costs (inputs) for firms increasing SRAS (1) • Combined effect of these changes is to lower the average price level and increase real output (1) **Rejection marks:** • **A** is incorrect as AD likely to shift left due to falling net exports (1) • **C** is incorrect as SRAS likely to shift right due to falling costs for firms (1) • **D** is incorrect as SRAS likely to shift right due to falling costs for firms (do not reward if already awarded) **OR** for AD likely to shift left due to falling net exports (1)	**(4)**

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Question Number	Indicative Content	Mark
5	**Answer: A** **Explanation** • Identification of government spending as an injection **and** taxation as a withdrawal (1) • Definition of net injection: When government spending exceeds revenue(1) **OR** when injections exceed withdrawals from circular flow (1) • Definition of budget deficit: Where government spending exceeds tax revenues then there is a budget deficit (1) • Reference to Italy's 44 billion euro **budget deficit** (1) • Comment that deficit could be analysed as a % of GDP (1) • Deficit usually financed through government borrowing (1) • Deficit can only be reduced through lower spending and/or higher taxes to reduce net injection (1) **Rejection marks:** • **B** this does not necessarily follow as will depend upon borrowing, spending and tax receipts(1) • **C** the value of the multiplier does not depend upon the injection/depend upon value if withdrawal/leakages (it is determined independently of the injection) (1) Reward reference to MPS, MPC, MPM • **D** not a withdrawal as this would be the case if revenues exceeded expenditure (1)	**(4)**

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Question Number	Indicative Content	Mark
6	**Answer: B** **Explanation** • Definition of balance of trade in goods (I.E.value of goods exported-value of goods imported) (1) **OR** value of visible exports-value of visible imports • **DO NOT ACCEPT** X-M as Question is about trade in goods • Negative trade balance is a trade deficit in goods (1) • Each year the chart shows a deficit/negative balance(1) • Reward any calculations on the data EG % increase or decrease in the balance for a year or series of years (1) • Reward any specific data references to the size of the balance – must include unit of measurement (US$ billion (1) • Likely to reduce AD and real output (1) • Likely to depreciate currency (1) **Rejection marks:** • **A** incorrect because the chart does not show tax revenue or government expenditure it shows balance of trade in goods(1) • **C** is incorrect as the chart does not show investment (1) • **D** is incorrect because the balance of payments will always be in equilibrium/includes other items such as capital account/allow reference to other components of balance of payments (1)	**(4)**

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Question Number	Indicative Content	Mark
7	**Answer: C** **Explanation** • Definition of commodity EG raw material used in manufacturing(1) **OR** Goods traded on international commodity exchange/traded at a global price (1) • Definition of average price level **OR** real output (1) • Increased costs of production (1) • Example: oil, copper, iron, primary agricultural product (1) • Explanation that lead to inward shift in SRAS (1) higher average price level and fall in real output (1) **OR** • Accurate diagram showing left shift of SRAS (must be SRAS not LRAS) correctly labelled (up to 2 marks) **Rejection marks:** • **A** is incorrect as increase in labour productivity likely to shift SRAS right/increasing real output/fall in price level (1) • **B** is incorrect as decrease in indirect tax likely to shift SRAS right/increasing real output/fall in price (1) • **D** is incorrect as an increase in investment shifts AD right raising average price level and real output (1)	**(4)**

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Question Number	Indicative Content	Mark
8	**Answer: C** **Explanation** • Definition of inflation: sustained increase in the average price level (1) • Disinflation defined: a slowing of the rate of increase in average prices (1) • Inflation in 2011-2013 means average prices were rising in each year (1) • Data reference to specific inflation figure or figures for the years 2011-2013 (1) • Average prices were rising throughout the entire period 2000-2013 (1) • Prices were always rising even though the rate of increase varies (1) • Lower rates of inflation does not mean deflation (falling prices) just a slower rate of inflation(1) • 2011-2012/2008-2009/2012-2013 disinflation occurred (1) **Rejection marks:** • **A** incorrect because average prices were rising throughout the entire period 2000-2013 (1) • **B** incorrect because although % increase in CPI remained the same (or fell slightly) average prices still increased(1) • **D** incorrect because although inflation fell average prices still increased but at a slower rate(1**)**	**(4)**

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Question Number	Indicative content	Mark
9a		
	Knowledge and application: • definition of economic growth: annual increase in real GDP (1) • Increase in total value of output produced within the boundaries of a country(1) • Increase in productive potential (1) • Growth outward shift in PPF/PPC (1) • Negative growth inward shift in PPF/PPC (1) • PPF diagram showing outward/inward shift (1) • Measurement may be real or nominal (1) • Real growth takes into account inflation (1) • Nominal growth is monetary value and does not take into account inflation (1) • Includes output from foreign owned factors(1) • Excludes overseas output of domestic owned factors (1) • Explanation should include reference to the data/case study E.G. UK growth at 1.7% highest rate of growth (1) • Spain experiencing negative economic growth - 1.2% (1) • Negative economic growth may indicate recession (1) • France and Germany experiencing very low levels of growth(1) NB Examples do not have to relate to Western European countries to be rewarded	
		(4)

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Question Number **9b**		Mark 10
Knowledge, Application and Analysis – Indicative content		
	• UK has higher economic growth thus likely to have higher inflation as higher growth in real output • UK has lowest savings ratio compared to other countries • Implies that higher economic growth may be due to consumer expenditure forcing up AD and average prices • UK has largest current account deficit as % of GDP which may imply inflation is imported • Current account deficit may mean weaker currency therefore more expensive imported inputs • Accurate diagram showing increase in AD or decrease in SRAS causing increase in average price level	

Level	Marks	Descriptor
0	0	A completely inaccurate response.
1	1-2	Shows some awareness of reasons **or** data references
2	3-4	Understanding of reasons **or** some awareness of reasons and data references
3	5-6	Clear understanding of reasons **and** linking to data

Evaluation – Indicative content		
	Here we are looking for development and evidence of judgement as to the most significant factors • Lower investment may mean lower productivity reduces AS and, real output and causing rising average prices • Lower investment may offset rising consumption but will depend relative value of GDP components • Lower saving may mean less funds for investment • Inflation still relatively low at 1.7% (less than Bank of England target 2.0%) • Short-term higher inflation a trade-off for higher economic growth • Long-term higher inflation might reduce competitiveness and worsen current account deficit which mat reduce long term growth	

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Level	Marks	Descriptor
0	0	No evaluative comments.
1	1-2	For identifying evaluative comments without explanation
2	3-4	For evaluative comments supported by relevant reasoning

Question Number **9c**	Indicative Content	Mark
	Knowledge and application: • An injection is an inflow into the circular flow of income (1). • Injections include investment, government expenditure and exports. (1) (1 mark for any one of these) • A withdrawal is an outflow from the circular flow of income (1). • Withdrawals include savings, taxes and imports. (1) (1 mark for any one of these) • The above 4 points could be illustrated by a circular flow diagram. (up to 4 marks) • Savings defined as postponed consumption or investment (1) • Investment defined as spending on capital goods (1) • Withdrawals have contractionary effective/injections have expansionary effect (1) • **Then maximum 2 marks for data references (1 + 1):** • Specific data references from Figure 2 for savings (up to 2 marks) • Specific data references from Figure 2 for investment (up to 2 marks) • UK has lowest investment (13.9% of GDP) (1) • UK has lowest savings (12.8% of GDP) (1) • France has highest investment (19.5% of GDP) (1) • Germany has highest savings (23.1% of GDP) (1) NB Examples do not have to relate to Western European countries to be rewarded	**(6)**

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<table>
<tr><td>Question Number</td><td colspan="2"></td><td>Mark

14</td></tr>
<tr><td></td><td colspan="2">Knowledge, Application and Analysis – Indicative content</td><td></td></tr>
<tr><td>9d</td><td colspan="3">• Saving decision by people to postpone their consumption
• The savings ratio is the % of disposable income saved rather than spent - high savings ratio lowers consumption and aggregate demand
• Factors influencing savings include:
• real interest rate on savings deposits
• expectations of future income and job security
• consumer confidence
• availability of credit
• taxation of saving
• the need to save to repay debts
• to save to build up a deposit for a mortgage, pay school and university fees
• saving for retirement.
• Extract 2 refers to fall in real incomes in the UK meaning lower disposable income and less savings
• Data reference from Figure 2 such as 12.8% of GDP in UK 23.1% in Germany</td></tr>
<tr><td>Level</td><td>Marks</td><td colspan="2">Descriptor</td></tr>
<tr><td>0</td><td>0</td><td colspan="2">A completely inaccurate response.</td></tr>
<tr><td>1</td><td>1-3</td><td colspan="2">Shows some awareness of possible effects or identification of one or more points.
Definition/understanding <u>or</u> data references.
Material presented is often irrelevant and lacks organisation. Frequent punctuation and/or grammar errors are likely to be present and the writing is generally unclear.</td></tr>
<tr><td>2</td><td>4-6</td><td colspan="2">Identification and some explanation of factors identified along with some development of analysis <u>or</u> some identification of possible effects and data references.
Material is presented with some relevance but there are likely to be passages which lack proper organisation.
Punctuation and/or grammar errors are likely to be present which affect the clarity and coherence.</td></tr>
<tr><td>3</td><td>7-8</td><td colspan="2">Clear understanding and analysis of the economic impact <u>and</u> data references
Material is presented in a relevant and logical way.
Some punctuation and/or grammar errors may be found, but the writing is clear and coherent overall.</td></tr>
</table>

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Evaluation – Indicative content		
	Here we are looking for development and evidence of judgement as to the most significant factors • Short-term versus long-term causes of differences • Short-term saving may mean higher future spending by consumers and investment by firms • Structural differences in economies of the countries EG Germany and UK • Higher saving may mean more funds for investment • Reference to paradox of thrift – too high level of saving may reduce demand and cause fall in real output and average prices • Although saving as % of GDP may be relatively low, if GDP is high the value of saving may be relatively high • Possible causes of spending rather than saving (EG income and age)	

Level	Marks	Descriptor
0	0	No evaluative comments.
1	1-2	For identifying evaluative comments without explanation.
2	3-4	For evaluative comments supported by some reasoning and relevant examples.
3	5-6	For evaluative comments supported by relevant reasoning and relevant examples.

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Question Number		Mark **(14)**
Knowledge, Application and Analysis – Indicative content		
9(e)	• Current account: A measure of the flow of funds from trade in goods and services, plus other net income flows (net investment income and net transfers) • Current account surplus means deficit for other countries • If the current account is in surplus for a sustained period then: • Germany can have a deficit on capital account by building up reserves or purchasing assets in other eurozone countries or internationally(Extract 1) • The German surplus usually leads to an appreciation of the euro, which makes imports cheaper, reducing inflation, but exports more expensive, which may have a negative impact on other eurozone countries (1) • German real exchange rate is strongly undervalued compared to the rest of the Eurozone - making its goods artificially cheap, crowding out those of other eurozone countries from both eurozone and world markets • There may be increased protectionism from other countries/trade disputes within and outside of the European Union Costs or benefits can be used for KAA and the opposites for Evaluation	

Level	Marks	Descriptor
0	0	A completely inaccurate response.
1	1-3	Shows some awareness of possible effects or identification of one or more points. Definition/understanding **or** data references. Material presented is often irrelevant and lacks organisation. Frequent punctuation and/or grammar errors are likely to be present and the writing is generally unclear.
2	4-6	Identification and some explanation of factors identified along with some development of analysis **or** some identification of possible effects and data references. Material is presented with some relevance but there are likely to be passages which lack proper organisation. Punctuation and/or grammar errors are likely to be present which affect the clarity and coherence.
3	7-8	Clear understanding and analysis of the economic impact **and** data references Material is presented in a relevant and logical way. Some punctuation and/or grammar errors may be found, but the writing is clear and coherent overall.

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Evaluation – Indicative content		
	• Current account surplus can be an indication of a successful economy with high productivity • Although German surplus is negatively impacting other eurozone countries the HDI figure would suggest living standards are very high in France and Spain • German surplus is having an impact on other eurozone countries such as Spain and France Figure 1 • Low inflation would also suggest stable economy however the danger of deflation is destabilising • High levels of savings suggest growth could be export driven thus reliant upon demand for exports – thus vulnerable to low growth in target markets • High reliance upon exports can create imbalanced growth in the long-term • Impact upon rest of the eurozone can be negative and may cause rising inequality between members • Political pressures within eurozone and potential break-up of currency zone	

Level	Marks	Descriptor
0	0	No evaluative comments.
1	1-2	For identifying evaluative comments without explanation.
2	3-4	For evaluative comments supported by some reasoning and relevant examples.
3	5-6	For evaluative comments supported by relevant reasoning and relevant examples.

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Question Number	Indicative Content	Mark
10a	**Knowledge and application:** • Real wages: nominal wages minus the inflation rate (1) • Calculation 2012: -3.6% (wages) - 1.9% (inflation) (2) • Therefore, change in real wages is -5.5% (1) • If answer of between -5.38% and -5.5% (including or not including working) then award 3 marks	**(4)**

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Question Number		Mark 10

Knowledge, Application and Analysis – Indicative content		
10b	• For some years, real wages rising 2007 (0.3%), 2010 (4.3%), 2011 (1.3%) • In 2013 real wages rose by 2.2% • Therefore, consumption is likely to increase • This will cause aggregate demand to increase • With a subsequent rise in real output and the average price level. This may be illustrated with an AD/AS diagram • Higher nominal and real wages would increase the costs of firms • This would cause a leftwards shift of the SRAS curve • A rise in the price level and a fall in real output. This may be illustrated with AD/AS diagram • If AD approach is offered as KAA, the AS approach could be evaluation and vice versa	

Level	Marks	Descriptor
0	0	A completely inaccurate response.
1	1-2	Shows some awareness of reasons **or** data references
2	3-4	Understanding of reasons **or** some awareness of reasons and data references
3	5-6	Clear understanding of reasons **and** linking to data

Evaluation – Indicative content		
	• Reference to gradients of AD and/or AS curves • Significance of size of multiplier • Magnitude of wage increase (nominal and real) will determine the impact/effect • May be relatively temporary rise in wages thus the impact short-term and wages may fall in the long-term • In total over the period 2007-2013 real wages are falling-for some years, real wages are falling EG 2008 (-3.5%), 2009 (-4.2%), 2012 (-5.5%)	

Level	Marks	Descriptor
0	0	No evaluative comments.
1	1-2	For identifying evaluative comments without explanation.
2	3-4	For evaluative comments supported by relevant reasoning.

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Question Number	Indicative Content	Mark
10c	**Knowledge and application** Two costs identified (1 + 1) and for each explanation award up to 2 marks (2 + 2 marks) Costs may include: • greater uncertainty (1) and fall in business confidence (1) leading to lower investment (1) • redistribution of income (1) borrowers benefit and savers suffer (1) if the inflation rate is greater than the rate of interest (1) (Extract 2 impact on savers) • loss of competitiveness (1) of the country's exports (1) if its inflation rate is higher than that of its major competitors (1) (Extract 1 falling exports and Extract 2 impact on competitiveness) • real burden of debt (1) both public and private (1) would fall (1) (Extract 2 possible rising interest rates) • inflation may increase firms costs (1) causing profits to fall/profit margins to fall (1) if they cannot increase revenue (1) (Extract 2 weakening of currency and rising costs for firms) • real incomes could fall (1) if wage rises do not keep pace with inflation (1) thus falling living standards (1) • Inflationary spiral (1) rising prices (1) lead to rising wage demands (1)	**(6)**

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Question Number		Mark **(14)**
Knowledge, Application and Analysis – Indicative content		
10(d)	Factors might include: • Interest rates are increased to reduce AD by increasing costs of borrowing and • Interest rates are used by central banks as a component of monetary policy • Expected rate of economic growth and inflation: suggestion that this is relatively high (Extract 2) so case for increasing interest rates • PMI suggest growth rate likely to increase • Extract 2 suggest that inflation has risen from 1.75% to 2.07% July-August • Extract 2 unemployment falling • Thai dollar depreciating/decreasing in value increasing inflationary pressures • Nominal wages increased 3% in 2013 • May be an AD/AS diagram showing likely impact of rising interest rates on average price level and real output – decrease in AD with lower C + I • Arguments for may be used as KAA and against as Evaluation or vice versa	

Level	Marks	Descriptor
0	0	A completely inaccurate response.
1	1-3	Shows some awareness of the arguments for an increase in interest rates or identification of one or more points. Definition/understanding **or** data references. Material presented is often irrelevant and lacks organisation. Frequent punctuation and/or grammar errors are likely to be present and the writing is generally unclear.
2	4-6	Identification and some explanation of arguments identified along with some development of analysis **or** some identification of possible arguments and data references. Material is presented with some relevance but there are likely to be passages which lack proper organisation. Punctuation and/or grammar errors are likely to be present which affect the clarity and coherence.
3	7-8	Clear understanding and analysis of the economic arguments **and** data references Material is presented in a relevant and logical way. Some punctuation and/or grammar errors may be found, but the writing is clear and coherent overall.

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Evaluation – Indicative content		
	Evaluation might include: • Difficulty of making accurate forecasts • Fall in inflation might be short-term (real wages increased in 2013) • Inflation rate still relatively low in 2013 but extract 2 suggest inflation is rising in 2014 • Difficulty of determining impact on the exchange rate of a change in interest rates • External factors might change suddenly e.g. oil prices • Low or negative growth in wages suggest falling incomes/living standards • Low or negative growth in wages suggests that cost-push pressures are declining thus inflation may fall • Inflation rate appears to be on a downward trend - reference to data in figure 1 • Magnitude of interest rate change important (impact depends upon size of multiplier) • Short run or long run impact of interest rate rise EG lower investment reducing LRAS • Impact upon export competitiveness of currency appreciation– Extract 1 • Exports already declined (Extract 1) • Time lag between rate changes and macroeconomic effects • Impact of interest rate changes may depend upon elasticity of AS curve	

Level	Marks	Descriptor
0	0	No evaluative comments.
1	1-2	For identifying evaluative comments without explanation.
2	3-4	For evaluative comments supported by some reasoning and relevant examples.
3	5-6	For evaluative comments supported by relevant reasoning and relevant examples.

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Question Number		Mark **(14)**
Knowledge, Application and Analysis – Indicative content		
10(e)	• decline in net exports will reduce AD resulting in falling average prices and real output • downward multiplier effect upon AD • increased unemployment • falling nominal wages (and real wages depending upon inflation rate) • falling living standards • higher government spending on welfare • depreciation of currency and thus higher import prices • sustained fall may have negative long term impact upon investment • potential deflation (as inflation is already relatively low) • continued falls in nominal and real wages reducing domestic demand • growing inequality • diagram showing fall in AD as result of lower exports, lower average price level and real output AND/OR fall in AS due to higher import costs as result of depreciation • Positive effect can be used as KAA and negative effects as Evaluation or vice versa	

Level	Marks	Descriptor
0	0	A completely inaccurate response.
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3	7-8	Clear understanding and analysis of the economic impact **and** data references Material is presented in a relevant and logical way. Some punctuation and/or grammar errors may be found, but the writing is clear and coherent overall.

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Evaluation – Indicative content		
	• Potential benefits include: • depreciation of currency – meaning most successful export industries benefit from increased price competitiveness • impact will depend upon the size of the multiplier • depreciation may lead to increased domestic demand for cheaper domestically produced goods and services • Low inflation reduces uncertainty for firms which may increase investment • rebalancing of the economy towards domestic consumption • less reliant upon uncertain export markets • increased efficiency in domestic firms as they have to compete to maintain or increase global market share • decrease in exports may be offset by decrease in imports • effect may be greater in some sectors EG smartphone and petrochemicals	
Level	Marks	Descriptor
0	0	No evaluative comments.
1	1-2	For identifying evaluative comments without explanation.
2	3-4	For evaluative comments supported by some reasoning and relevant examples.
3	5-6	For evaluative comments supported by relevant reasoning and relevant examples.

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