Quick Answers

Question 1

Define trade in goods balance.

- Value of exports of goods / revenue earned from exports minus value of imports of goods / expenditure on imports of goods (2)
- Exports minus imports (1) of goods / visible items (1).

Guidance:
Accept exports (of goods) = imports of (goods) for 1 mark

Question 2

Discuss whether or not India is likely to experience a deficit on the current account of its balance of payments in the future.

Award up to 4 marks for logical reasons why it might, which may include:

- there was a deficit in 2016 and 2017 (1) and it was on an upward trend (1)
- incomes are rising / economic growth is occurring (1) and so more imports may be purchased both by consumers and by firms (1)
- it is expected that the exchange rate will rise (1) this may increase the price of exports (1) and demand for exports may fall (1) price of imports
- may fall (1) so demand for imports may rise (1)
- Indian trade restrictions may be reduced / Indian government promoting free trade (1) which may increase imports (1).
- tax rates may be cut (1) with more disposable income (1) people may buy more imports (1)

Award up to 4 marks for logical reasons why it might not, which may include:

- there may be more foreign tourists (1) if pollution declines (1)
- lower tariff on imported raw materials / imported capital goods (1) may reduce costs of production (1)

- other countries may remove their trade restrictions (1) allowing India's exports to rise (1)
- if the government does spend more on education (1) productivity may rise (1) and India's products may become more price and quality competitive (1)
- MNCs may be attracted for a number of the reasons given (1) MNCs may produce exports / import substitutes (1)
- Higher investment (1) may raise quality of exports / domestic products (1) lower price of exports (1)
- Car production is rising (1) more cars may be exported / fewer cars may be imported (1)

Question 3a

Identify the difference between an export and an import.

- An export is sold to other countries / outflow of goods and services in exchange for money / credit item in the balance of payments (1) an import is purchased from other countries / inflow of goods and services in exchange for money / debit item in the balance of payments (1)

Question 3b

Explain how a rise in the income of its main trading partners may affect a country's trade in goods balance.

- A rise in income abroad will increase the countries' ability to purchase products (1) demand for this country's exports may rise (1) particularly luxury products / products without domestic substitutes (1) exports are a credit item in the trade in goods balance (1) the trade in goods balance may improve (1) may move from a deficit to a surplus / any deficit may be reduced / any surplus may be increased (1)
- The rise in income may be the result of the countries selling more goods to this country (1) this may increase the country's imports (1) imports are a debit term (1) the trade in goods balance may move from a surplus to deficit / any deficit may become larger / any surplus may get smaller (1)

Question 4a

State two components of the current account.

Any two from:

- trade in goods
- trade in services
- primary income
- secondary income

Guidance

Any two components.
Accept exports and imports for 1 mark.

Question 4b

Analyse how a country's current account deficit might be reduced if its firms become internationally competitive.

Coherent analysis which might include:

- Being internationally competitive e.g. high productivity, low inflation, low exchange rates (max 2) increases production
  (1) reduces cost of production (1) decreases price of exports (1) increases quality of exports (1) increases demand for exports (1) increases value of exports / net exports (1)
- Imports relatively more expensive / other countries products more expensive (1) lower relative quality of imports (1) decreases imports (1)

Question 5

Discuss whether or not a reduction in a country's trade protection will reduce its current account surplus.

Level (6-8 Marks)

Why it might:

- lower tariffs will reduce price of imports
- removal of quotas may result in more imports being purchased
- removal of a ban/embargo will permit imports of the product to enter the country
- import expenditure may rise
- higher import expenditure may reduce the gap between export revenue and import expenditure

Why it might not:

- foreign firms may not have the capacity to supply more products
- demand for imports may be price inelastic
- the quality of imports may have fallen
- other countries may also reduce their trade restrictions
- the exchange rate may fall, raising exports and reducing imports
- export revenue may rise to match the higher import expenditure
- may have large surplus on invisibles

Example of Level 2 answer:

The removal of quotas and tariffs on imports will make it relatively cheaper to import into the country. More imports will come into the country reducing its current account surplus. However, a reduction in a country's trade protection will show the country's willingness to have trading partners.

As such, domestic firms will allocate more resources into producing exports at relatively lower costs and better quality so that they will be more competitive in the global economy. Other countries may be attracted to these exports and the demand for them will increase. Thus, the demand for local currency will increase, causing the current account surplus to increase. Thus, the current account surplus may increase or decrease depending on the extent of the fall in import prices and the rise in demand for exports.

Principal Examiner comment:

There is limited coverage of both sides.

Question 6

Analyse the consequences of an appreciating currency on the current account of the balance of payments of a country.

- An appreciation in the exchange rate means a rise in the value of the currency (1) higher export prices (1) lower import prices (1) increase quantity demand for imports (1) decrease quantity demand for exports (1) increase value of imports (1) decrease value of exports (1) may reduce net exports (1) current account deficit increases / current account surplus decreases (1).

Guidance

- Reward but do not expect reference to outcome will be influenced by PED

Question 7

Define a trade in services deficit.

- Imports of services being greater than exports of services (2).
- A deficit on a section of the balance of payments (1).

Question 8

Define a surplus on the current account of the balance of payments

- When the revenue from trade in goods and trade in services exported exceeds the revenue from trade in goods and trade in services imported (2)
- When the inflow from primary income and secondary income is higher than the outflow of primary income and secondary income (2)
- Exports greater than imports (1)

Question 9

Discuss whether or not an increase in a surplus on the current account of the balance of payments decreases unemployment.

Up to 5 marks why it may:

- More exports (1) means more output is needed (1) more workers will be needed (1) as demand for labour is a derived demand (1)
- A surplus means more funds flowing into the economy (1) increasing total (aggregate) demand (1) which could generate jobs (1)
- Incomes increase (1) consumption may increase (1) increasing revenue of firms (1) which could then be reinvested (1)

Up to 5 marks why it may not:

- Exports may be capital-intensive (1) using less labour to produce exports (1)
- A surplus in one country may create a deficit in another (1) other countries may not be able to continue buying exports (1) other countries may impose protectionist policies (1) to prevent future deficits (1)
- An increase in a surplus may raise the exchange rate (1) reducing net exports (1) increasing unemployment (1)

Question 10

Discuss whether or not an increase in government spending will reduce a surplus on the current account of the country's balance of payments.

Up to 5 marks for why it might:

- Higher government spending may go on imports (1) e.g. imported computers for government offices (1)
- Higher government spending on e.g. state benefits (1) will increase disposable income (1) some of this might be spent on imports (1)
- Higher government spending will increase total (aggregate) demand (1) this may cause inflation (1) reduce international competitiveness (1) reduce exports (1) increase imports (1)

Up to 5 marks for why it might not:

- Government spending on education and training / healthcare (1) may raise labour productivity (1) reduce costs of production (1) improve quality (1) increased demand for domestically produced products (1) increase exports (1) reduce imports (1)
- Government spending on infrastructure (1) may reduce transport costs (1) increasing price competitiveness (1) increasing exports (1) reducing imports (1)
- The government may subsidise domestic products (1) lowering the price of domestic products (1) increasing exports (1) reducing imports (1)

Question 11

Analyse how having some of its population working abroad may benefit an economy

- The workers may send income home (1) helping to support dependents / raise living standards of dependents (1) saving on some government benefits having to be paid (1)
- They may gain skills abroad (1) if they return they will increase the productivity of the labour force (1) may raise output / cause economic growth (1) reduce firms costs of production (1)
- The money they sent back will be an inflow of foreign currency / remittance / primary income (1) improving the current account position on the balance of payments (1)
- May reduce unemployment (1) if the workers' skills are not in demand at home (1)

Question 12

Analyse to what extent the information in Table 1 suggests that countries with current account deficits have higher inflation rates and lower economic growth rates than those with current account surpluses

- The three countries with current account deficits do have higher inflation rates (1)
- Correct identification of Columbia/Nigeria/Turkey as the three countries with a deficit (1)

- China and Germany have lower inflation (1)
- The picture is less certain in terms of economic growth (1)
- Evidence (up to 2) e.g. Columbia has a deficit but relatively high economic growth (1)
- Germany had a surplus but low economic growth (1)

Question 13

Discuss whether or not an increase in investment would reduce a deficit on the current account of the balance of payments.

Up to 5 marks for why it might:

- May lower costs of production (1) make domestic products more internationally price competitive / lower export prices (1) so increasing demand for exports (1)
- Advanced technology / more efficient production (1) may increase the quality of products produced (1) increase demand for domestically produced products (1) reducing demand for imports (1)
- Investment in labour (human capital) (1) can increase skills (1) raise productivity (1) increase quality of products (1)
- Investment abroad could increase primary income/income (1)

Up to 5 marks for why it might not:

- The investment may go on imported capital goods (1) in the short run would increase spending on imports (1)
- The investment may be in products which are not in demand abroad (1) are not substitutes for imports (1)
- In the short run investment may increase total (aggregate) demand by more than total (aggregate) supply (1) which may cause inflation (1) making domestic products less internationally competitive (1)
- Domestic products may become more competitive but net exports may not rise if offset by another change (1) e.g. import restrictions/fall in income abroad / rise in exchange rate (1)
- Investment may not be big enough to make a difference (1)

Guidance

- Each point may be credited only once, on either side of an argument, but separate development as to how/why the outcome may differ is to be rewarded.

Question 14

Discuss whether or not a reduction in a current account deficit on the balance of payments will benefit an economy.

Up to 5 marks for why it might:

- May mean that demand for imports has fallen (1) and/or demand for exports has risen (1) higher total (aggregate) demand (1) may increase GDP/create economic growth (1) reduce unemployment (1)
- Will reduce debt (1) not have to borrow as much to finance it (1)
- May cause appreciation of exchange rate (1) leading to lower inflation (1)

Up to 5 marks for why it might not:

- If the deficit is reduced by buying fewer imports of raw materials (1) and capital goods (1) may reduce GDP (1) lower exports in the longer run (1)
- If fewer imports are being purchased because of a recession (1) GDP will be falling (1)
- If fewer imports are being purchased because trade restrictions are introduced (1) there may be retaliation (1) with tariffs/quotas being imposed one exports (1)
- Higher total (aggregate) demand might lead to (demand-pull) inflation (1
- Exchange rate may appreciate (1) can reduce total demand/worsen the deficit in the long run (1)

Guidance

- Accept higher total demand on either side
- One mark if given on both sides. More marks can only be awarded if a reason why this leads to a benefit/cost is given

Question 15

Explain how a country could have a trade in goods surplus but a deficit on the current account on the balance of payments

- Trade in goods surplus means exports (of goods) exceeds imports (of goods) (1)
- trade in goods is only one part of the current account (1)
- identification of two of the three other components (1)
- there could be a larger deficit on the trade in services balance (1) example of a service item decreasing (1)
- there can be a larger deficit on income (primary) balance (1) example of an income item increasing (1)
- there could be a larger deficit on current transfers (secondary) balance (1) example of a current transfer item decreasing (1) or a combination of deficits on other items (1)
- A current account deficit means more money will be leaving than entering the country (1)