

# THE NATURE OF ECONOMIC PROBLEM

- 1 Inflation and unemployment are two economic problems that governments usually have to deal with.

Explain three reasons why inflation is regarded as a serious economic problem.

## MARKSCHEME:

[6]

Explain three reasons why inflation is regarded as a serious economic problem. [6]

Up to 2 marks: increases cost of living (1), people are worse off if incomes do not rise as much as prices (1) because purchasing power will be less (1).

Up to 2 marks: this is a particular problem for those on fixed incomes (1) compared to others

who at least get some increase in their wages each year (1).

Up to 2 marks: lenders become more reluctant to lend money (1) and this can reduce the extent of liquidity in the economy/reduce investment (1).

Up to 2 marks: it can lead to uncertainty and a lack of confidence in the economic future of a

country (1), making firms reluctant to invest (1).

Up to 2 marks: if the prices of exports go up, this will make them less competitive in foreign

markets (1); this could lead to a reduction in demand and a consequent increase in unemployment (1) and may cause a current account deficit (1).

## 2 The Mints

Mexico, Indonesia, Nigeria and Turkey, known as the Mints, are four emerging economies that are predicted to grow rapidly. The four countries have relatively large populations, from 75 million in Turkey to 242 million in Indonesia in 2014. They also have high birth rates, from 17 in Turkey to 41.5 in Nigeria per 1000 people. Both income per head and the countries' Human Development Index ranking are improving. The changes, however, do not mean that everyone in the four countries is satisfied. As incomes increase, so do people's wants, and what people would like to consume exceeds the maximum output that countries are capable of producing.

Output and consumption are increasing in each of the four countries. Nigeria, for example, is predicted to be one of the world's 20 largest economies by 2020. Productivity is rising in most sectors of the Nigerian economy although it remains low in agriculture. Despite some security concerns, more multinational companies are setting up in the country, attracted by its expanding markets.

Nigeria and Turkey both had annual inflation rates above 8% in 2014. Indonesia's was 5.7% and Mexico's 5.2%. The Mexican Government had used monetary policy measures in that year to keep the inflation rate down. In August 2014 it opened up its energy market, allowing private sector firms to compete against the country's state-owned petroleum firm. It also increased spending on state-provided health care, which operates alongside private medical care.

The four countries saw fluctuations in their exchange rates in 2014. Indonesia's currency, the rupiah, changed from 10 685 per US\$ the year before to 11 450 per US\$ in 2014. Turkey's currency, the Turkish Lira, followed a similar trend.

Changes in the exchange rate can affect firms' costs of production, as can industrial action. In June 2014 Turkish trade unions organised a number of strikes seeking to gain better wages and working conditions for their members. However, the power of Turkish trade unions is limited by restrictive trade union legislation and a small membership, with only 9% of workers belonging to trade unions. This means that collective bargaining is not a key feature of Turkish labour markets and Turkish trade unions do not have much influence on economic policy.

Using information from the extract, explain how the Mints illustrate the economic problem. [2]

### MARKSCHEME:

(a) Using information from the extract, explain how the Mints illustrate the economic problem. [2]

What people would like to consume/wants (1) exceeding the maximum output the countries

are capable of producing (1).

Note. no marks for just a definition of the economic problem

3 The United Nations' World Tourism Organisation has estimated that the proportion of the world's population who have visited another country will have reached only 7% by 2020. Increasing international travel might create jobs and influence incomes. However, it would also put pressure on finite resources and would create external costs.

(a) Define 'resources'.

[2]

**MARKSCHEME:**

(a) Define 'resources'. [2]

- factors of production/inputs (1) used to produce goods and services (1)
- identification of type of factor of production – land (natural resource), labour (human resource), capital, entrepreneur (1)