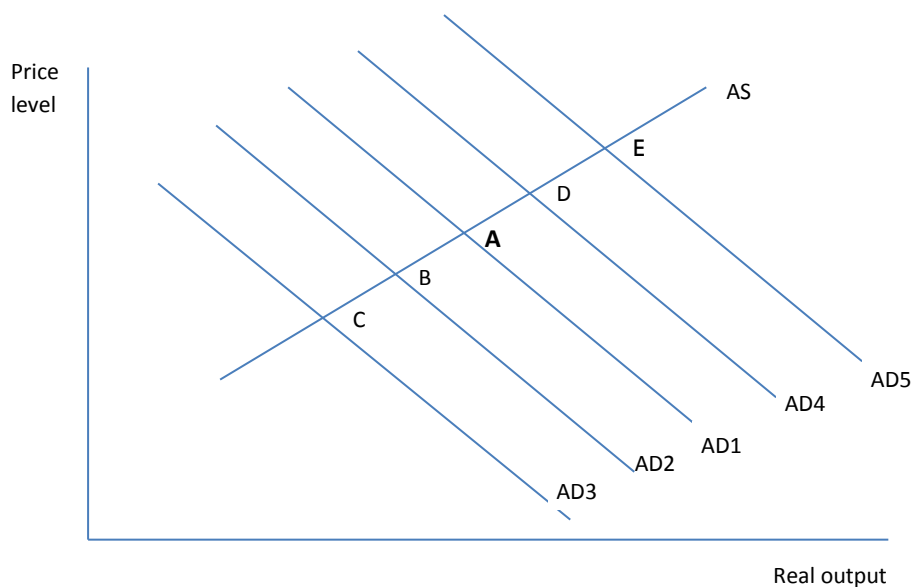


Revision on movements in the AD curve



The UK economy has been stable at equilibrium point A. At which point will the economy stabilise when each of these events occur? Think not only about the direction of the AD curve but also whether the change will be large or small. Just write the letter you think is right.

1. The Bank of England increases interest rates by 1%
2. A sharp recession hits America.
3. A new government prioritises education, boosting spending on buildings, IT and teachers.
4. With an election looming, the government brings in a 6-month cut in VAT from 20% to 15%.
5. UK firms start to invest more, following an end to trade wars between the US and China/Europe.
6. A sharp rise in the £ makes UK exports too expensive, so sales fall significantly.
7. An unexpected fall in inflation leads to a rise in consumer and business confidence.
8. The government brings in a new austerity programme, slashing public spending.

Your mark out of 8

Your estimate:

The reality:

Answers/Cribsheet

1. The Bank of England increases interest rates by 1%

- That's a sharp rise that might affect Consumption and Investment significantly, so C

2. A sharp recession hits America.

- Their downturn will hit our exports to the US. That hits our AD, but not by much (about 15% of our exports are to the US, and exports are about 25% of GDP), so B

3. A new government prioritises education, boosting spending on buildings, IT and teachers.

- Fantastic, but this wouldn't shift AD to the right by much, so it's D

4. With an election looming, the government brings in a 6-month cut in VAT from 20% to 15%.

- That would have a huge short-term effect, as people bring forward planned spending, so it's E.

5. UK firms start to invest more, following an end to trade wars between the US and China/Europe.

- AD shift to the right due to extra investment spending; but it's a small effect, so D.

6. A sharp rise in the £ makes UK exports too expensive, so sales fall significantly.

- AD falling significantly, so to C.

7. An unexpected fall in inflation leads to a rise in consumer and business confidence.

- Clearly a shift to the right, but it's hard to tell the scale, so it could be D or E. Allow either.

8. The government brings in a new austerity programme, slashing public spending.

- That cut in G sounds substantial, so AD falls to C