Candidate 4 evidence

section 3

9a) • One consequence in that borrowing will become more expensive. As a result, ~~th~~ consumers will ~~leave~~ be less able to spend and especially purchase big ticket items. This ~~may~~ leads to a lower standard of living because they can afford fewer goods. This leads to a decrease in AD because of lower consumer spending. Therefore, this limits output and growth.

• ~~Add~~ There will be a higher reward for saving so individuals are more likely to save their money. Savings are a withdrawal from the circular flow of income which means that the would be a lower national income.

• Firms will also borrow less due to more expensive loans, this will reduce investment in new technology. As a result, there will be a lesser ~~less~~ increase in the productive potential of the economy. Additionaly reduced investment will lower AD as investment is a component. This further leads to lower output and growth.

• As loans are so expensive there will be fewer new businesses created. As a result, output does not increase in the economy and growth is limited. This could be countered by the government offering grants to startups.

• Increasing intrest rates will further increase mortgage repayments meaning households will have less discretionary income. This means that they can afford fewer goods and services and so will have a lower standard of living. However, most UK homes are on a fixed-rate mortgage so this may have a minimal impact.

• As firms are not investing, they will be unable to expand, as a result, they are unable to increase employment. If loan repayments

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	become too expensive, this could lead to business closures which will actually increase unemployment. This creates further issues for the government as it will have to ~~provide~~ spend more on unemployment benefits. This is particularly concerning at a time of high national debt.	
	• Increasing interest rates will lead to more demand for £s because of hot money inflows seeking favourable returns on savings. As a result, the currency strengthens. This is beneficial as the UK is still low relative to the $ and €. This means that foreign imports will be cheaper which effectively reduces inflationary pressure for consumers. However UK exports will be more expensive meaning they will see a fall in demand. This will have ~~an~~ negative impact on the current account and increase the trade deficit.	
b)	High inflation means that consumers have ~~lost dispos~~ a lower standard of living because they are unable to afford as many goods and services at higher prices. It may also increase relative and absolute poverty in the UK as food	

prices rose by 16% which meant many households could not afford basic essentials.

It has increased ~~income~~ inequality in the UK because many of the goods with highest inflation (food and energy) take up a higher proportion of spending for the poorest households. This has had a regressive effect meaning that the poorest have seen a much larger decrease in the purchasing power of their incomes than the wealthy. This has therefore widened inequality.

It has also had a harsh impact on the 'squeeze middle' who have seen a fall in the real value of their savings. As purchasing power falls, there is a negative wealth affect which decreases consumer spending. this constricts growth.

High inflation, particularly energy inflation, has increased the cost of production for many firms. As a result, they have had to make redundancies or even close down. This has increased unemployment in the UK which has had to be solved by additional government spending on transfer payments. The lack of consumer demand has further pushed firms out of the market and business shutdowns have a negative multiplier effect meaning that the loss of income from their employees ~~has~~ lessens AD further causing business failure and the shrinking of the economy.

High inflation has ~~also had some benefits.~~ meant that foreign imports have become relatively cheaper which worsens

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	the balance of payments as imports increase.	
	The government has had to increase transfer payments such as Cost of Living payments to low income, disability and pensioners households. This has worsened the UK budget deficit.	
	High inflation meant less demand for UK exports resulting in a ~~A benefit of the high inflation is that the extra demand for lower imports~~ demand for the £. This led to a depreciation in the currency. This had a later benefit of UK exports being more price competitive due to a relatively lower value of the currency.	
	~~A benefit is that~~ Inflation and the ~~may have~~ cost of living crisis may have encouraged those able to work but choosing not to into the workforce. This moves the UK closer to maximising its productive potential.	
c)	The current inflationary pressures of food inflation and energy inflation are a result of supply side factors such as problems with supply chains. Monetary policy is a demand side policy which means that it may be ineffective at tackling these supply side issues.	
	Additionally, inflation is a persistent global crisis which is unlikely to be ~~tackled~~ resolved by UK domestic policy. It is also linked to geo-political tensions which further suggests UK monetary policy will do little to improve the situation.	
	However, others may argue that ~~the~~ if the UK increases rates, other nations will follow (it has clearly been a global trend of	

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	central banks raising interest rates) and that the combined effect will lead to substantial reductions in inflation.	
	Some argue that the Monetary Policy Comittee acted too late. In 2020 signs emerged of upcoming inflation however the Bank maintained ultra-low interest rates. This suggests that they are ineffective in preventing economic crises.	
	Some argue that the increases in interest rates are too small to combat the high inflation and so will have minimal impact. However from 0.1% ~~in~~ at the end of 2021, the bank rate is now 4.5% May 2023 showing that significant steps have been taken to effectively lower the rate of inflation	
d)	Modern Monetary Theory believes that it is safe and sustainable to borrow and spend money as a government provided that they invest in projects that will generate long term growth. For example infrastructure projects. It rests on the assumption that the government cannot run out of money as it is always able to print more. It believes that investment into supply side policies is preferable to market based interventionist policies such as deregulation and privitisation. It suggests that future generations will not inherit a debt burden as traditional economists fear but that it will allow them to inherit the returns from investment in the form of greater productive potential. It believes it is not inflationary and cites the	

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	example of Japan which has debt at 240% of GDP but has	
	not experienced significant inflation.	