3.5 Economic Influences on Business: Interest Rates and Exchange Rates: 10-minute Pack

AQA 7132 · Calculators not allowed · about 10 minutes

Total Marks

Name: _____ Date: ____ / ____ / _____

Answer ALL questions in the spaces provided. Show your working for every calculation. Use UK examples where asked.

1 Which one of the following best describes an 'exchange rate' as relevant to a UK firm buying inputs from abroad?

- ☐ A) The price in sterling for one unit of a foreign currency
- ☐ B) The tariff charged on imported goods
- ☐ C) The domestic VAT rate charged on imported inputs
- ☐ D) The profit margin a firm earns on exports

(Total for Question 1 is 1 mark)

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2 Define the term 'interest rate' in the context of business borrowing, and give one immediate effect on a firm when interest rates rise.

(Total for Question 2 is 2 marks)

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3 State two ways a rise in UK interest rates can affect consumer spending by households in the UK, referring to mortgage borrowers and savers.

(Total for Question 3 is 2 marks)

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4 Explain one advantage to a firm of using a natural hedge, where possible, to manage currency risk. Apply your explanation briefly to a firm that both invoices customers in euros and pays suppliers in euros.

(Total for Question 4 is 3 marks)

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Mark scheme · 3.5 Economic Influences on Business: Interest Rates and Exchange Rates: 10-minute Pack

Question 1

A cao **B1**

Answer: A

Question 2

definition: the percentage cost of borrowing or return on saving per year **B1**

effect: firms face higher interest payments on variable-rate debt or new loans, increasing costs **B1**

Answer: Interest rate is the percentage cost of borrowing or the return on saving per year; if interest rates rise firms face higher interest payments on variable-rate debt, increasing their costs.

Question 3

higher mortgage or loan payments reduce disposable income for borrower households **B1**

higher interest on savings makes saving more attractive, so households may cut spending **B1**

Answer: Higher mortgage payments reduce disposable income for borrowers; higher returns on savings make saving more attractive so households may cut current spending.

Question 4

identifies advantage: offsets currency inflows and outflows so net exposure is reduced **B1**

develops the point: reduced need for financial hedging lowers direct hedging costs and administrative complexity **B1**

applies to the firm: if euro receipts from customers roughly match euro payments to suppliers, exchange rate moves have smaller net impact on sterling profits **B1**

Answer: A natural hedge offsets currency inflows and outflows reducing net exposure; this lowers the need for costly financial hedging and administrative work, and for a firm that both invoices and pays in euros, exchange rate movements affect net cash flows less if receipts and payments broadly match.

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