3.5 Economic Influences on Business: Interest Rates and Exchange Rates: Test Pack

Total Marks

AQA 7132 · Calculators not allowed · about 15 minutes

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 the 'interest rate' set by the Bank of England and used as the base for many commercial loan rates?

- ☐ A) The tax rate applied to business profits
- ☐ B) The percentage charged on borrowing by commercial banks influenced by the Bank of England base rate
- ☐ C) The annual inflation rate measured by the Consumer Prices Index
- ☐ D) The exchange rate between sterling and the US dollar

(Total for Question 1 is 1 mark)

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2 Define 'appreciation' of a currency and give one effect on UK exporters if the pound appreciates.

(Total for Question 2 is 2 marks)

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3 Analyse the likely effects of a weakening pound from 1.30 to 1.15 EUR per GBP on a UK firm that exports handmade furniture priced in sterling at 1,000 GBP per unit and sells mainly to the eurozone. Consider price competitiveness, demand, revenue in sterling and possible firm responses. Use figures where appropriate.

(Total for Question 3 is 8 marks)

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Mark scheme · 3.5 Economic Influences on Business: Interest Rates and Exchange Rates: Test Pack

Question 1

B cao **B1**

Answer: B

Question 2

definition: appreciation is when a currency gains value relative to other currencies **B1**

effect: UK exports become more expensive for foreign buyers, likely reducing export demand **B1**

Answer: Appreciation is when a currency gains value relative to others; if the pound appreciates, UK exports become more expensive for foreign buyers, likely reducing export demand.

Question 3

identifies direct price effect: at old rate 1,000 GBP = 1,300 EUR, at new rate 1,000 GBP = 1,150 EUR, so the product is 150 EUR cheaper for euro buyers **B1**

explains that the firm's price competitiveness improves if it keeps its sterling price unchanged, because foreign buyers now pay fewer euros for the same item, which could help protect or grow sales in the eurozone **B1**

explains demand effect: cheaper price in euros could increase quantity demanded in the eurozone, adding to revenue **B1**

analyses revenue in sterling: if the firm quoted prices in euros, converting receipts means each euro now converts into more pounds, potentially increasing sterling revenue **B1**

considers firm responses: the firm could keep the euro price unchanged to boost sterling revenue and margins, or cut the euro price to gain market share while keeping sterling revenue roughly the same, with implied volume and margin trade offs **B1**

considers hedging and contractual responses: use of forward contracts, invoicing in euros, or targeting non-euro markets as ways to manage future exchange rate risk **B1**

evaluates net effect by weighing increased volume against lower unit revenue, noting outcome depends on price elasticity of demand and cost structure **B1**

applies figures to give a quantitative sense, for example unit euro price falls from 1,300 EUR to 1,150 EUR, a 11.54% change, and suggests scenarios where volume rises by less or more than 11.54% to indicate likely revenue impact **B1**

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