BUS.IN3 The economic climate

AQA 8132 · Calculator allowed · about 55 minutes

Total Marks

Name: ________________________________ Date: ____ / ____ / ______

Answer ALL questions in the spaces provided. Show your working for any calculation: method marks are available even if your final answer is wrong. Brindlewood Furniture, used throughout this pack, is a fictional business. All interest rate and exchange rate figures in this pack are hypothetical, chosen for calculation practice only.

1 Which one of the following best describes the 'interest rate' on a bank loan?

- ☐ A) The percentage of a loan that must be paid each year as the cost of borrowing
- ☐ B) The total amount of profit a business makes in a year
- ☐ C) The number of years a business has to repay a loan
- ☐ D) The rate at which a business's sales are growing

(Total for Question 1 is 1 mark)

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2 Which one of the following best describes an 'exchange rate'?

- ☐ A) The price at which a business sells a product abroad
- ☐ B) The value of one currency expressed in terms of another currency
- ☐ C) The rate of tax charged on goods brought into a country
- ☐ D) The interest rate charged on a loan taken out in a foreign currency

(Total for Question 2 is 1 mark)

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3 State two ways a rise in interest rates could affect a business like Brindlewood Furniture.

(Total for Question 3 is 2 marks)

4 Brindlewood has an outstanding bank loan of 40,000 pounds. For this question only, assume a hypothetical annual interest rate of 4%. (This is a hypothetical rate for calculation practice only, not a statement of any current UK interest rate.)

(a) Calculate the annual interest Brindlewood would pay on the 40,000 pound loan at this hypothetical 4% rate. **(2)**

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(b) The hypothetical interest rate then rises from 4% to 6%. Calculate the new annual interest Brindlewood would pay on the same 40,000 pound loan at 6%. **(2)**

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(Total for Question 4 is 4 marks)

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5 Using your answers to question 4a and question 4b, calculate the extra annual interest cost caused by the rise from 4% to 6%. Show your working.

(Total for Question 5 is 2 marks)

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6 Explain how the extra interest cost calculated in question 5 could affect Brindlewood's profit.

(Total for Question 6 is 3 marks)

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7 Explain how a rise in interest rates could reduce demand for Brindlewood's furniture, even though Brindlewood has not changed its own prices.

(Total for Question 7 is 3 marks)

8 Brindlewood buys 11,000 euros worth of timber from a French supplier every month. For this question only, assume a hypothetical exchange rate of 1 GBP = 1.10 EUR. (This is a hypothetical rate for calculation practice only, not a statement of any current GBP/EUR exchange rate.) Calculate the sterling (pound) cost of this monthly order at this rate. Show your working.

(Total for Question 8 is 2 marks)

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9 The pound then strengthens against the euro, to a hypothetical rate of 1 GBP = 1.25 EUR: one pound now buys more euros than before. Using the same 11,000 euro monthly order, calculate the new sterling cost at this rate. Show your working.

(Total for Question 9 is 2 marks)

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10 Using your answers to question 8 and question 9, calculate the monthly saving to Brindlewood from the pound strengthening. Show your working.

(Total for Question 10 is 2 marks)

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11 Using your answer to question 10, calculate the annual saving to Brindlewood if the exchange rate stays at 1 GBP = 1.25 EUR for a full year. Show your working.

(Total for Question 11 is 2 marks)

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12 Explain why the stronger pound in question 9 benefits Brindlewood as a business that imports raw materials.

(Total for Question 12 is 3 marks)

13 Explain a risk to Brindlewood if the pound later weakens back to its original hypothetical rate of 1 GBP = 1.10 EUR.

(Total for Question 13 is 3 marks)

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14 State two other ways a change in the exchange rate could affect a business that imports raw materials, other than the cost of the materials themselves.

(Total for Question 14 is 2 marks)

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15 The stronger pound is currently saving Brindlewood 14,400 pounds a year on its timber imports (question 11), but question 13 shows this saving would be lost, and costs would rise again, if the pound later weakens. Brindlewood is considering paying a fee to fix the exchange rate on its euro purchases for the next 12 months, so its sterling cost cannot rise even if the pound weakens, but also cannot fall further if the pound strengthens more.
Recommend whether Brindlewood Furniture should fix its exchange rate for the next 12 months in this way. Justify your answer using the figures and points made earlier in this pack.

(Total for Question 15 is 9 marks)

Mark scheme · BUS.IN3 The economic climate

Question 1

- **B1** A cao
- **Answer: A**

Question 2

- **B1** B cao
- **Answer: B**

Question 3

- **B1** one acceptable effect, e.g. the cost of repaying any existing loans increases
- **B1** a second acceptable effect, e.g. customers who also have loans/mortgages have less disposable income, so demand for furniture may fall
- **Answer: Any two, e.g. higher loan repayment costs for the business; lower customer disposable income and demand.**

Question 4

- (a) **M1** 40,000 x 0.04 seen
- (a) **A1** 1,600 pounds cao
- **(a) Answer: 1,600 pounds.**
- (b) **M1** 40,000 x 0.06 seen
- (b) **A1** 2,400 pounds cao
- **(b) Answer: 2,400 pounds.**

Question 5

- **M1** 2,400 - 1,600 seen (ft from question 4)
- **A1** 800 pounds cao
- **Answer: 800 pounds.**

Question 6

- **B1** identifies the point, e.g. interest is a cost to the business, so paying an extra 800 pounds a year increases Brindlewood's total costs
- **B1** develops the point, e.g. if Brindlewood cannot raise its prices or cut other costs to match, this extra cost comes directly out of its profit
- **B1** links clearly to an outcome, e.g. lower profit leaves Brindlewood with less money to invest in the business or to pay out to its owners
- **Answer: Interest is a cost, so the extra 800 pounds a year increases Brindlewood's total costs, and if it cannot raise prices or cut other costs to match, this comes directly out of profit, leaving less money to invest or pay to owners.**

Question 7

- **B1** identifies the point, e.g. many of Brindlewood's customers also have loans or mortgages, and a rise in interest rates increases what they must repay each month
- **B1** develops the point, e.g. this leaves customers with less disposable income to spend on non-essential purchases such as new furniture
- **B1** links clearly to an outcome, e.g. Brindlewood could see fewer sales even without changing its own prices, since customer demand has fallen
- **Answer: A rise in interest rates increases customers' own loan or mortgage repayments, leaving them with less disposable income to spend on furniture, so Brindlewood could see fewer sales even though it has not changed its own prices.**

Question 8

- **M1** 11,000 / 1.10 seen
- **A1** 10,000 pounds cao
- **Answer: 10,000 pounds.**

Question 9

- **M1** 11,000 / 1.25 seen
- **A1** 8,800 pounds cao
- **Answer: 8,800 pounds.**

Question 10

- **M1** 10,000 - 8,800 seen (ft from questions 8 and 9)
- **A1** 1,200 pounds cao
- **Answer: 1,200 pounds.**

Question 11

- **M1** 1,200 x 12 seen (ft from question 10)
- **A1** 14,400 pounds cao
- **Answer: 14,400 pounds.**

Question 12

- **B1** identifies the point, e.g. a stronger pound means each pound buys more euros than before
- **B1** develops the point, e.g. so the same 11,000 euro order of timber costs Brindlewood fewer pounds, as shown by the fall from 10,000 pounds to 8,800 pounds (questions 8 and 9)
- **B1** links clearly to an outcome, e.g. this lowers Brindlewood's costs and could increase its profit, or let it lower its own prices to customers
- **Answer: A stronger pound means each pound buys more euros, so the same 11,000 euro timber order costs fewer pounds, falling from 10,000 pounds to 8,800 pounds (questions 8 and 9), which lowers Brindlewood's costs and could increase profit or allow lower prices.**

Question 13

- **B1** identifies the point, e.g. if the pound weakens, each pound buys fewer euros again, so the monthly timber order becomes more expensive in sterling
- **B1** develops the point, e.g. this would remove the 1,200 pound monthly saving calculated in question 10 and push Brindlewood's costs back up towards 10,000 pounds a month
- **B1** links clearly to an outcome, e.g. this makes Brindlewood's costs and profit harder to plan for, since exchange rates can move in either direction
- **Answer: If the pound weakens back to 1.10 EUR, each pound buys fewer euros again, removing the 1,200 pound monthly saving from question 10 and pushing the timber order's cost back up towards 10,000 pounds a month, making Brindlewood's costs and profit harder to plan for.**

Question 14

- **B1** one acceptable effect, e.g. it makes costs and profit harder to plan or budget for
- **B1** a second acceptable effect, e.g. the business may need to spend money protecting itself against future exchange rate changes, such as agreeing a fixed rate in advance
- **Answer: Any two, e.g. makes budgeting/planning harder; may require paying for protection against future rate changes (e.g. a fixed-rate agreement).**

Question 15

- **Level 1** (1-3): Makes simple, undeveloped comments about the exchange rate decision, with little or no use of the pack's figures and no clear recommendation.
- **Level 2** (4-6): Gives a developed argument for or against fixing the exchange rate, using some of the pack's figures, but does not fully weigh both sides or reach a clearly justified recommendation.
- **Level 3** (7-9): Weighs the evidence for and against fixing the exchange rate, using the saving and risk figures from this pack, and reaches a justified recommendation supported by that analysis.
- **Indicative content:**
  - For fixing the rate: question 13 shows that if the pound weakens back towards 1.10 EUR, Brindlewood would lose the 14,400 pound annual saving identified in question 11 and its costs would rise sharply; fixing the rate protects against this.
  - For fixing the rate: it gives Brindlewood certainty over its costs for a full year, making budgeting and pricing decisions easier, which question 14 identifies as a genuine benefit beyond the direct cost of materials.
  - Against fixing the rate: if the pound stays strong or strengthens further, Brindlewood would be locked into a less favourable rate than the market offers and would miss out on further savings beyond the 14,400 pounds already identified.
  - Against fixing the rate: agreeing a fixed rate normally carries its own fee or cost, which would reduce the net benefit of the saving calculated in question 11.
  - Judgement: given that the current saving of 14,400 pounds a year is significant and exchange rates are genuinely uncertain in either direction, a reasonable recommendation is that Brindlewood should fix at least part of its exchange rate exposure to protect the bulk of the saving while accepting the small cost of doing so, though a decision to stay unhedged and rely on the current strong pound is also creditable if it weighs the same evidence and reaches a justified conclusion.