

Aggregate Demand — Worksheet

The AD curve · consumption and saving · investment · government expenditure · the net trade balance

Name: _____

Class: _____

Date: _____

DEFINE aggregate demand and the savings ratio · **CALCULATE** aggregate demand and the net trade balance · **DRAW** the effect of a cut in income tax on the AD curve · **ANALYSE** how a rise in the interest rate affects investment · **DISCUSS** the effects of a rise in the interest rate on aggregate demand · **EVALUATE** the effects of a cut in corporation tax on investment

Sitting 1 — Topic practice

30 marks

MULTIPLE CHOICE Task 1 — Six questions on aggregate demand

6 marks

Choose one answer for each question.

1. Which of these is part of government expenditure (G) in $AD = C + I + G + (X - M)$?

- A unemployment benefit paid to households that are out of work
- B a state retirement pension
- C interest paid on government debt
- D the salaries of teachers employed by the state

Answer:

2. A fall in business confidence reduces investment because it:

- A lowers the expected return that firms compare with the interest rate
- B raises the interest rate firms must pay on new loans
- C increases the tax firms pay on their profits
- D lowers the depreciation of the capital stock each year

Answer:

3. Istavo is a country with disposable income of \$500bn. Its savings ratio rises from 10% to 20%. Disposable income and the price level do not change, and nothing else changes. What happens to Istavo's aggregate demand?

- A AD shifts left by \$50bn at every price level
- B AD shifts left by \$100bn at every price level
- C Istavo moves along its AD curve to a lower real output
- D AD does not change, because the extra saving is lent to firms

Answer:

4. Gross investment in an economy is \$140bn and depreciation is \$160bn. It follows that:

- A net investment is positive and the capital stock is growing
- B gross investment must have been recorded incorrectly
- C net investment is negative and the capital stock is shrinking
- D aggregate demand includes only the net figure

Answer:

5. A machine costs \$500 and is expected to add \$60 a year to the firm's profit. The government pays a subsidy of \$100 towards its price. Nothing else changes. What is the firm's expected rate of return now?

- A 15%
- B 12%
- C 10%
- D 32%

Answer:

6. A country's currency moves from 5 units per US dollar to 4 units per US dollar. This means:

- A the currency has depreciated and exports are cheaper abroad
- B the currency has appreciated and exports are more expensive abroad
- C the currency has depreciated and imports are more expensive at home
- D the currency's value has not changed, because only the number fell

Answer:

DEFINE Task 2 — The meaning of aggregate demand

2 marks

Define the term aggregate demand.

aggregate demand

EXPLAIN Task 3 — Larger deposits for car loans

4 marks

In Velmora, banks used to ask car buyers for a deposit of 10% of the price. Now they ask for 25%. The interest rate on car loans has not changed.

Explain one likely effect of this change on consumption in Velmora.

CLASSIFY Task 4 — Eight changes in Kemar and the AD curve

8 marks

Kemar is a country. In each row, only the change in that row happens.

Classify each change in Kemar by what it does to Kemar's AD curve.

Key: Movement along AD · Shift to the right · Shift to the left

#	Change in Kemar	What happens to the AD curve
1	Kemar's price level rises by 4%	
2	The government cuts the rate of income tax	
3	The central bank raises its interest rate, and the price level stays the same	

#	Change in Kemar	What happens to the AD curve
4	Firms expect weaker sales in the next few years	
5	Kemar's currency falls from 6 to 8 units per US dollar	
6	A fall in the price level means the money households hold buys more	
7	Households decide to save a larger share of their disposable income	
8	The government pays firms 20% of the price of each new machine they buy	

CALCULATE Task 5 — Aggregate demand in Torvia

4 marks

In Torvia this year, households plan to spend \$420bn and firms plan to spend \$90bn on capital goods. The government plans to spend \$130bn. Exports are \$160bn and imports are \$190bn.

Calculate Torvia's net trade balance and its aggregate demand this year.

Net trade balance (\$bn)

Workings

Answer:

Aggregate demand (\$bn)

Workings

Answer:

Find the net trade balance first, and keep its sign.

ANALYSE**Task 6 — An interest rate rise and a new oven****6 marks**

Brana is a bakery firm in Dunmar. It could buy a new oven that costs \$200,000, and it would borrow the whole cost from its bank. Brana expects the oven to raise its profit by \$16,000 a year. The interest rate in Dunmar rises from 5% to 9%.

Analyse the likely effect of the rise in the interest rate on investment in Dunmar.

Knowledge — the rule a firm uses to invest, and what each part of the rule means (2)

Application — use the numbers for Brana's oven (2)

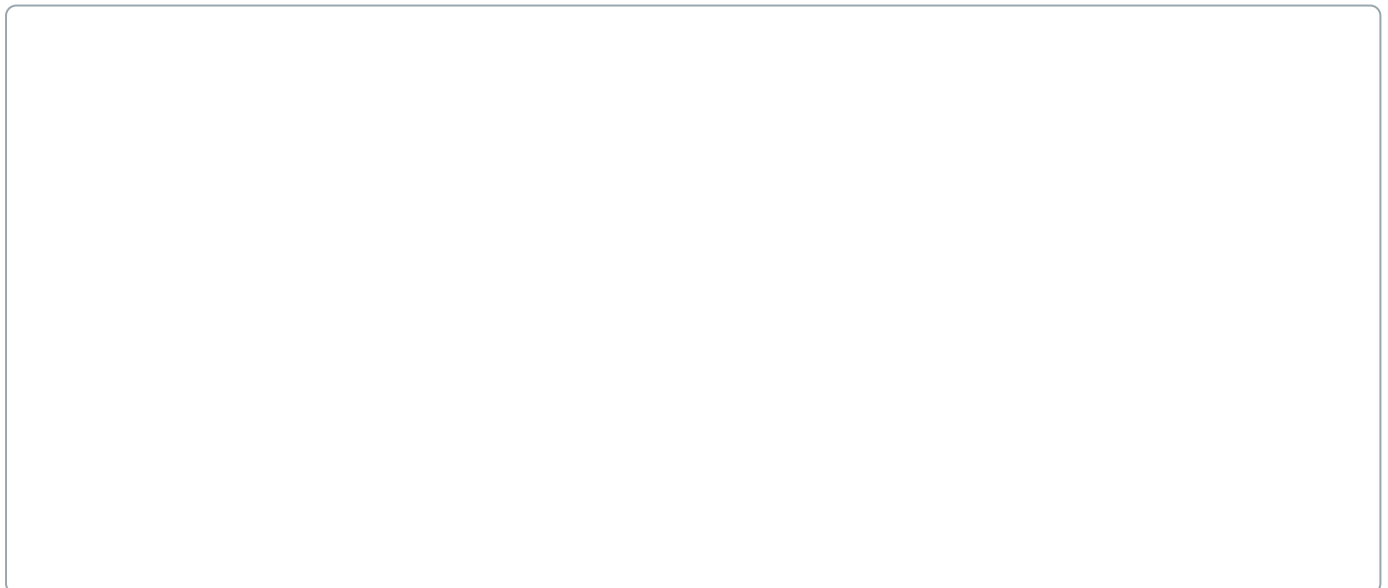
Analysis — your chain of reasoning (2)

Start with the oven, then think about all the firms in Dunmar.

Sitting 2 — Mock section**74 marks****DRAW****Task 7 — A diagram of a cut in income tax****4 marks**

The government of Mirava cuts the rate of income tax. The price level in Mirava does not change.

Draw an AD diagram to show the likely effect of the tax cut on aggregate demand in Mirava.



EXPLAIN**Task 8 — Training courses and unemployment benefit**

4 marks

Output in Pelora falls, and more people are out of work. The government spends \$2bn more on training courses for people without jobs. It also pays \$3bn more in unemployment benefit.

Explain the likely effect of these two changes on government expenditure (G) in Pelora.

CALCULATE**Task 9 — Real income and the net trade balance in Ostana**

4 marks

Real income in Ostana rises. Households spend \$60bn more, and \$15bn of this extra spending is on imports. Exports stay at \$200bn. Imports rise from \$240bn to \$255bn.

Calculate Ostana's net trade balance before and after the rise in real income.

Net trade balance before (\$bn)

Workings

Answer:

Net trade balance after (\$bn)

Workings

Answer:

EXPLAIN Task 10 — House prices and consumption in Lanova

4 marks

House prices in Lanova rise by 20% this year. Incomes in Lanova do not change.

Explain one likely effect of the rise in house prices on consumption in Lanova.

EXPLAIN Task 11 — Spending plans of a new government

4 marks

A new government in Vessa spends \$5bn more on teachers and \$5bn less on new roads. The government pays Vessa's own workers and firms for both. Nothing else changes.

Explain the likely effect of this change on aggregate demand in Vessa this year.

Source: Spending in Selvara

- 1 Selvara is a middle-income country with an open economy. In 2025, many households in Selvara feared for their jobs. Their disposable income stayed at \$800bn, but the savings ratio rose from 5% to 10%. More households now save in case they lose their jobs. Shops sold fewer cars and less furniture than in 2024.
- 2 In March 2025, Selvara's central bank raised its interest rate from 3% to 5%. Most household loans in Selvara have variable rates, so the rates on these loans rose in the same month. Banks also asked home buyers for larger deposits. Several firms said that they expected weaker sales, and they delayed plans for new factories.
- 3 The government spent more on flood protection. Selvara's two largest trading partners entered a recession in 2025. Selvara sells most of its exports to these two countries. In the same year, Selvara's currency fell from 10 to 12 units per US dollar. Figure 1 shows the components of Selvara's aggregate demand.

Figure 1: Components of aggregate demand in Selvara, 2024 and 2025

Component	2024	2025
Consumption (C)	\$760bn	\$720bn
Investment (I)	\$150bn	\$130bn
Government expenditure (G)	\$210bn	\$220bn

Component	2024	2025
Exports (X)	\$280bn	\$270bn
Imports (M)	\$300bn	\$280bn

DEFINE Task 12 — The meaning of the savings ratio

2 marks

Define the term 'savings ratio' (paragraph 1).

savings ratio

EXPLAIN Task 13 — The change in aggregate demand

4 marks

With reference to Figure 1, explain the change in Selvara's aggregate demand between 2024 and 2025.

ANALYSE Task 14 — The rise in the savings ratio

6 marks

With reference to paragraph 1, analyse the likely effect of the rise in the savings ratio on aggregate demand in Selvara.

Knowledge — consumption, saving and disposable income (2)

Application — use the numbers in paragraph 1 and Figure 1 (2)

Analysis — your chain of reasoning (2)

EXAMINE Task 15 — The fall in the value of the currency**8 marks**

With reference to the source, examine the likely impact of the fall in Selvara's currency on its net trade balance.

Knowledge — explain what a depreciation does to the prices of exports and imports (2)

Application — use two numbers or facts from the source (2)

Analysis — one chain for exports and one for imports (2)

Evaluation — say what the impact depends on (2)

DISCUSS Task 16 — The rise in the interest rate**14 marks**

With reference to the source, discuss the likely effects of the rise in the interest rate on aggregate demand in Selvara.

Knowledge — name two economic ideas that explain the effects (2)

Application — use two facts or numbers from the source (2)

Analysis — two chains of reasoning (4)

Evaluation — weigh the effects and say what they depend on (6)

EVALUATE Task 17 — A cut in corporation tax

20 marks

"The government of Marlo plans to cut the rate of corporation tax from 28% to 22%. It wants firms in Marlo to invest more." Last year, 1 in 4 firms in Marlo made a loss. Many firms in Marlo expect weak sales next year.

Evaluate the likely effects of this tax cut on investment and aggregate demand in Marlo.

Knowledge — define corporation tax, and explain two other economic ideas that you use (3)

Application — apply each idea to the facts about firms in Marlo (3)

Analysis — one chain for investment and one for aggregate demand (6)

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Write the one sentence that answers Task 17's question.



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