



Edexcel A - A Level Economics

Theme 4 – A global perspective

4.4 The financial sector

Worked Examples

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- The financial sector

4.4 The financial sector

Exam Style Question 1

- (a) Explain **one** role of financial markets.
- (b) Explain **one** reason why the UK central bank used quantitative easing following the Global Financial Crisis of 2008. [2]
- (c) Which **one** of the following would be the most likely cause of market failure in the financial sector? [1]
- A Banks charge higher interest rates on higher risk loans
 - B Banks do not create any external costs or benefits in their operations
 - C Banks know that the government will bear the risk of customers defaulting on loans
 - D Banks and their customers have symmetric information



4.4. The financial sector

Exam Style Question 1

Answer:

(a) Explain one role of financial markets. [2 marks]

One role of financial markets is to **mobilise savings** (1), which can then be used for **lending to businesses and individuals** so they can invest in things like new equipment or houses (1).

(b) Explain one reason why the UK central bank used quantitative easing following the Global Financial Crisis of 2008. [2 marks]

The UK central bank used **quantitative easing to increase the money supply** (1), which helped to **stimulate economic growth** during a time when interest rates were already very low and couldn't be cut further (1).

(c) Which one of the following would be the most likely cause of market failure in the financial sector? [1 mark]

Correct Answer: C – Banks know that the government will bear the risk of customers defaulting on loans

Explanation:

This is known as **moral hazard** where banks take more risks because they expect the government to bail them out if things go wrong, which can lead to market failure.

Please see the '4.4 The Financial Sector Revision Notes' pack for detailed notes.

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