

# Mark Scheme (Results) January 2008

GCE Level

## GCE Economics (6353) Paper 1

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## General Marking Guidance

- All candidates must receive the same treatment. Examiners must mark the first candidate in exactly the same way as they mark the last.
- Mark schemes should be applied positively. Candidates must be rewarded for what they have shown they can do rather than penalised for omissions.
- Examiners should mark according to the mark scheme not according to their perception of where the grade boundaries may lie.
- There is no ceiling on achievement. All marks on the mark scheme should be used appropriately.
- All the marks on the mark scheme are designed to be awarded. Examiners should always award full marks if deserved, i.e. if the answer matches the mark scheme. Examiners should also be prepared to award zero marks if the candidate's response is not worthy of credit according to the mark scheme.
- Where some judgement is required, mark schemes will provide the principles by which marks will be awarded and exemplification may be limited.
- When examiners are in doubt regarding the application of the mark scheme to a candidate's response, the team leader must be consulted.
- Crossed out work should be marked UNLESS the candidate has replaced it with an alternative response.

## 6353/01 Mark Scheme January 2008

Question Number	Answer	Mark
1(a)(i)	<p>Increase in the capital stock (2 marks) or asset build-up and replacing depreciated assets (2 marks).</p> <p><i>Other responses permitted:</i>            Accept increases in human capital (2 marks) and purchase of plant or machinery (2 marks)</p> <p>An injection into the circular flow (1 mark); new technology (1 mark); money spent on an asset (1 mark); sense of increasing future output capacity (1 mark); with a further mark allowed for some expansion of any of these concepts (1 mark).</p>	(2)

Question Number	Answer	Mark
1(a)(ii)	<p>Clear verbal comparison: e.g. rising then falling or is very high and very low/falling, is slowing (1 mark).</p> <p>Data use: 1998 24% (with margin of error 12% to 24%) AND 2001 -5% (with margin of error 5% to -7%, ); or difference 20% to 31% range (1 mark) Accept quotes from extract 1 'boom' and 'sluggish' and also accept 'negative growth' as data.</p>	(2)

Question Number	Answer	Mark
1(a)(iii)	<p>Appropriately labelled diagram with rightward shift in AD or AS or both (2 marks) If the impacts on both price level and real output are not shown then max. 1 mark.</p> <p>Transmission mechanism via AD; or the effects on AS (2 marks)</p> <p>Further analysis (2 marks) e.g. multiplier; shift in AS (or AD if AS covered above); elasticities; long run effects; analysis that the shifts in terms of price might cancel each other out (1 mark), but reinforce each other in terms of output (1 mark); data use 4.6% (1 mark)</p>	(6)

Question Number	Answer	Mark
1(b)(i)	<p>1 mark productivity definition + 2 marks valid reasons</p> <p>Definition of productivity: more output from the same inputs (1 mark). Give credit for reference to increased efficiency (1 mark) but not for increased production per se (0 marks)</p> <p>Effects of increase might include:</p> <ul style="list-style-type: none"> <li>• That this is likely to lead to economic growth or improved living standards (or equivalent answer) (2 marks).</li> <li>• Costs of production fall/efficiency increases so more profit</li> <li>• Removes inflationary pressure</li> <li>• Allow answers based on competitiveness.</li> <li>• Encourages inward investment</li> <li>• Effect on the current account</li> <li>• Shift out in the PPF/increase in productive potential</li> <li>• Effect on employment levels</li> </ul>	(3)

Question Number	Answer	Mark
1(b)(ii)	<p>Current account worsens or deficit grows (or improves if in context of productivity gap with France) (1 mark). Do not allow just 'there will be a deficit'.</p> <p>Low productivity means that exports will become less competitive (1 mark) low productivity means that imports more competitive (1 mark) (or vice versa with trade with France)</p> <p>Reference to data (1 mark) (Extract 2: Productivity is only 1.7%).</p> <p>Evaluation (2 marks) factors might include:</p> <ul style="list-style-type: none"> <li>• depends on price elasticity of demand for X and M</li> <li>• does productivity determine the current account or are other factors more important e.g. exchange rate, quality of goods and services;</li> <li>• problems in measuring productivity</li> <li>• changes will take some time to come into effect;</li> <li>• depends on the productivity growth in the main trading countries;</li> <li>• productivity IS growing therefore the opposite effects might happen, e.g. gap closing with France</li> <li>• current account might not be a problem, e.g. if there are large inflows of capital from elsewhere</li> </ul>	(6)

Question Number	Answer	Mark
1(b)(iii)	<p>For each relevant factor:</p> <p>Identification 1 mark, explanation 2 marks</p> <p>Factors might include:</p> <ul style="list-style-type: none"> <li>• relatively high value of the pound/ low value of dollar/ other relative currencies. Within the point, accept relatively <i>high interest rates</i></li> <li>• accept relatively <i>low interest rates</i>, affecting AD e.g. sucking in more imports</li> <li>• low quality of domestically produced goods or services</li> <li>• relative inflation rates</li> <li>• if related to <b>current account</b> e.g. value of the pound</li> <li>• confidence (shown in consumer spending and/or business investment)</li> <li>• price of oil/gas (UK is net oil/gas importer)</li> <li>• price of imports falling</li> <li>• real wage costs rising, government tax policy, other changes to regulations in UK makes X more expensive and M relatively cheap</li> <li>• slowdown in other countries</li> <li>• growth in UK increasing demand for imports</li> <li>• increased transfers on current account, e.g. tax to EU</li> <li>• effects of protectionism and subsidies are allowed</li> <li>• a change in the pattern of global demand for exports or imports</li> </ul> <p><i>Do not allow productivity changes per se.</i></p>	(6)

Question Number	Answer	Mark
1(c)	<p>Definition of supply side policies (1 mark), with implications for the price level and equilibrium real output - allow as diagram (2 marks).</p> <p>6 marks for policies: Outline of supply side policies with impact on balance of payments (2 x 3 marks or 3 x 2 marks) for example:</p> <ul style="list-style-type: none"> <li>• training of workers will make the UK more competitive and so exports will increase;</li> <li>• less red-tape will mean more firms invest in the UK/fewer firms leave so financial account will improve;</li> <li>• increasing competition (e.g. reducing monopoly power, privatisation) between firms will cut prices and make exporting more easy.</li> <li>• improving communications e.g. transport</li> <li>• tax incentives to enable firms to invest more or increase R&amp;D, or workers to worker more. Allow subsidies if they are shown to increase R&amp;D and new technology, not profits or just keeping businesses afloat</li> <li>• policies to increase immigration will lower costs for all firms</li> </ul> <p>MARK CAP of 4/6 for policies if not connected to current account.</p> <p>Evaluation 6 marks (2 x 3 marks or 3 x 2 marks) points might include:</p> <ul style="list-style-type: none"> <li>• failure of supply side policies (in Extract 2) show that there are problems with making supply side policies work; e.g. privatisation might not reduce monopoly power</li> <li>• time lag for the effectiveness of these policies;</li> <li>• the expense of supply side policies might have adverse effects</li> <li>• other policies - such as demand management - might be more effective, and are more generally used to correct this type of problem.</li> <li>• other things are not equal - for example, immigration might increase with or without the supply side policies; depends on growth in the rest of the world</li> <li>• Does a current account deficit matter?</li> </ul>	(15)



Question Number	Answer	Mark
2(a)(i)	<p>Weights as a measure of <b>proportion spent</b> (1 mark)</p> <p>different categories of goods taken from a survey of family expenditure (1 mark).</p> <p>Basket of goods (1 mark).</p> <p>Price survey (1 mark).</p> <p>Reference to base year (1 mark).</p> <p>Difference between CPI, RPI, or RPIX or other relevant comment about the measures in the UK e.g. housing costs (1 mark)</p> <p><b>Changes in CPI</b> (or other measure) (1 mark)</p> <p>Mark cap 3/4 marks if no specific reference to weights</p>	(4)

Question Number	Answer	Mark
2(a)(ii)	<p>For one relevant factor:</p> <p>Identification 1 mark, explanation 2 marks</p> <p>Problems of high inflation rates might include:</p> <ul style="list-style-type: none"> <li>• redistribution of incomes e.g. those on fixed incomes and creditors</li> <li>• Adverse effects of rise in interest rates which is likely to follow e.g. negative impact on GDP or employment, reducing consumer spending potential</li> <li>• Outside MPC's permitted range and therefore the MPC would have to write an open letter to the chancellor with public humiliation, loss of confidence in MPC and therefore the whole monetary policy in the UK</li> <li>• loss of international competitiveness</li> <li>• loss of confidence in the UK economy - leading to a fall in domestic and inward investment</li> <li>• erosion of the value of savings/amount lent in real terms</li> <li>• effect on nominal wages e.g. wage price spiral</li> <li>• allow shoe leather costs/menu costs up to a maximum of 2/3 (not very significant at 3% CPI)</li> </ul> <p>Do not accept a fall in GDP/unemployment rise unless linked to high inflation issues e.g. interest rates might</p>	

	rise so AD falls so GDP falls	(3)
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Question Number	Answer	Mark
2(b)(i)	<p>Reduced affordability of mortgages or increase in the cost of borrowing means that there is reduced demand for mortgages (2 marks)</p> <p>Decrease in the demand for houses (1 mark) House prices fall or rise more slowly (1 mark)</p> <p>Reward use of data e.g. £12 a month more (1 mark)</p>	(4)

Question Number	Answer	Mark
2(b)(ii)	<p>Diagram showing slowing or falling AD and/or decreasing AS (2 marks). If the impacts on <b>both</b> price level and real output are not shown then max. 1 mark.</p> <p>Transmission mechanisms (2 x 2 marks) might include via AD:</p> <ul style="list-style-type: none"> <li>• house prices</li> <li>• negative wealth effect</li> <li>• investment falls</li> <li>• increased savings/less borrowing</li> <li>• Hire purchase more expensive</li> <li>• bad debts</li> <li>• wages</li> <li>• effects via X and M</li> <li>• reduced confidence factors</li> <li>• equity release</li> </ul> <p>and via AS</p> <ul style="list-style-type: none"> <li>• increased costs to firms (AS to left/up)</li> <li>• stronger pound reduces the price of imports (AS to right/down)</li> </ul> <p>Further analysis (2 marks) e.g. multiplier; shift in AS (or AD if AS covered above); elasticities; long run effects; analysis that the shifts might reinforce each other in terms of price(1 mark), but reinforce each other in terms of output (1 mark); data use (1 mark)</p>	(8)

Question Number	Answer	Mark
2(c)(i)	<p>There are unemployed or unused (1 mark) resources (1 mark)</p> <p>There is productive potential or the economy is operating inside the PPF (2 marks)</p> <p>There is an output gap (2 marks)</p>	(2)

Question Number	Answer	Mark
2(c)(ii)	<p>2 marks for explanation about MPC consideration:</p> <ul style="list-style-type: none"> <li>• Spare capacity means that there is less likely to be inflationary pressures e.g. 'wage pressure' (line 11) (2 marks)</li> <li>• It means that there is scope to allow an increase in AD without inflationary pressure (2 marks)</li> </ul> <p>Evaluation (2 marks) points might include:</p> <ul style="list-style-type: none"> <li>• not clear that the MPC did take full account of the spare capacity, which may refer to the increasing levels of unemployment (lines 14-15);</li> <li>• many other factors to consider, and not clear how important this factor is - might involve prioritisation of factors;</li> <li>• there is evidence that full employment can co-exist with low levels of inflation.</li> <li>• Depends on elasticity of AS</li> <li>• Evidence appears to be contradictory - wages pressures and spare capacity</li> </ul>	(4)

Question Number	Answer	Mark
2(d)	<p>Aim of MPC (may be implicit) (1 mark).  Appropriate AD/AS diagram or other explanation of the working of monetary policy i.e. how interest rates affect the price level (2 marks).</p> <p>Use of evidence to suggest that interest rates should have been constant, (2 x 3 marks or 3 x 2 marks), for example:</p> <ul style="list-style-type: none"> <li>• spare capacity;</li> <li>• American-led world recession.</li> <li>• increase in banks' problems of bad debt</li> <li>• house prices have not recovered to recent rates</li> <li>• utility prices</li> <li>• slow wage growth</li> <li>• recovery has only just begun; need to keep rates constant so the process continues</li> <li>• Kern quote</li> </ul> <p><b>MARK CAP of 4/6 for factors if not connected to the data provided</b></p> <p>Evaluation 6 marks (2 x 3 marks or 3 x 2 marks) points might include:</p> <ul style="list-style-type: none"> <li>• counterarguments to justify the increase in interest rates (up to 6 marks);</li> <li>• other policies might have been better, e.g. supply side policies</li> <li>• contextual evidence in that interest rates have subsequently fallen (December 2007)</li> <li>• cannot tell which is correct as there is a time lag of two years before the full effect is felt;</li> <li>• is one quarter of a point going to make much difference?;</li> <li>• depends on what ECB and the Fed do (in the context, US rates had gone up for 14 consecutive months).</li> <li>• Elasticity of AS</li> <li>• The issue was a dilemma - recognise that the evidence was conflicting</li> <li>• Use of data e.g. threat of 3% inflation CPI</li> <li>• Relative importance of factors, e.g. what the Fed does, or how important is spare capacity</li> <li>• Validity of data issues</li> </ul>	(15)

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