

Economics

Advanced GCE **A2 7812**

Advanced Subsidiary GCE **AS 3812**

**Combined Mark Schemes
And Report on the Units**

June 2005

3812/7812/MS/R/05

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Advanced Subsidiary GCE Economics (3812)

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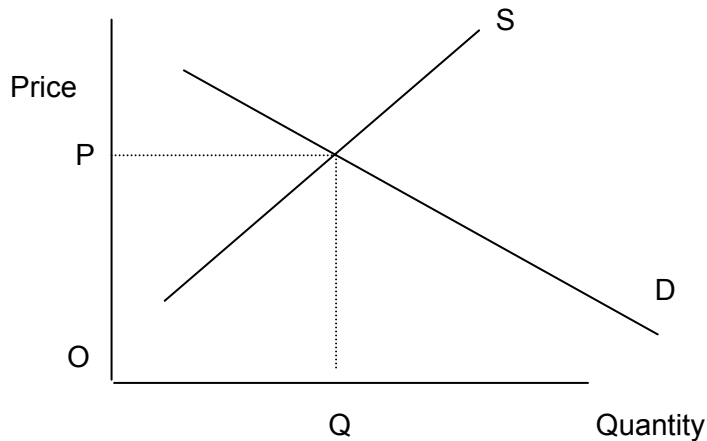
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**Mark Scheme 2881
June 2005**

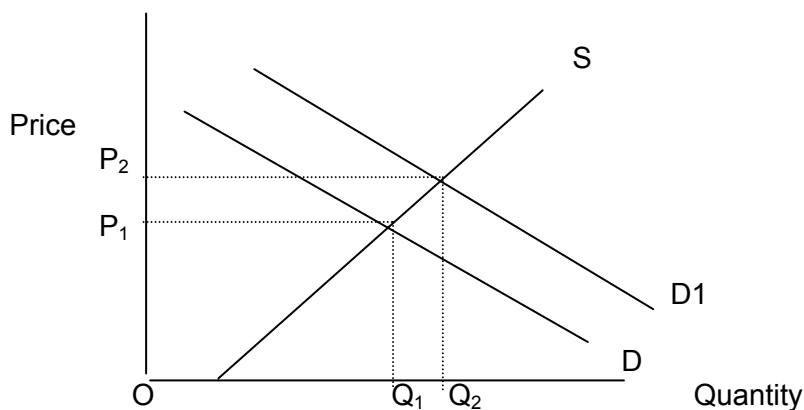
- a) 'Prices are ... determined by the market'. Draw a diagram to show what this means. [4]



Correct axes – 1 mark.
 Downward sloping demand curve – 1 mark.
 Upward sloping supply curve – 1 mark.
 Correct equilibrium price – 1 mark.

Ignore any shift of demand: mark what is correct.

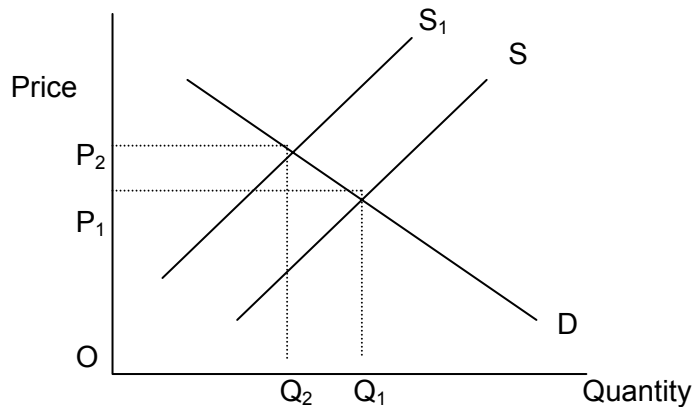
- (b) (i) With the aid of a diagram, explain how the market for take-away food in Bradford might be affected by a successful advertising campaign for take-away food. [4]



Shift to right of D – 1 mark. Successful advertising campaign – 1 mark.
 Increase in quantity demanded – 1 mark.
 Increase in equilibrium price – 1 mark.
 Elaboration of both price and quantity changes – 1 mark.
 Extent of price change will depend on extent of shift to D,
 Increase in demand – 1 mark.

A diagram without words can get no more than 3 marks.

- (ii) With the aid of a diagram, explain how the market for take-away food in Bradford might be affected by an increase in the cost of ingredients used in take-away food products. [4]



Supply curve will shift left (1) as a consequence of increase in input costs (1).
 Quantity demanded/supplied will fall – 1 mark.
 Price charged will increase – 1 mark.
 Price change will depend upon the extent of the shift of Supply – 1 mark.
 Elaboration of both price and quantity changes – 1 mark.
 A diagram without words can get 3 maximum.

- (c) Researchers at a local college have estimated that the income elasticity of demand for take-away food in Bradford is + 1.5.

- (i) Explain what this estimate means. [2]

For an understanding of YED – 1 mark.
 For an explanation of the sign e.g. normal/superior luxury good – 1 mark.
 For an explanation of size e.g. elastic – 1 mark.
 Numerical explanation incorporating implicit understanding - 2 marks.
 Price elasticity – zero: can only get numerical explanation marks once.

- (ii) Comment on its business significance to take-away food shop owners. [4]

As incomes in Bradford increase (or decrease), the demand for curry will increase (or decrease) – 1 mark.
 The change in demand for curry will be half as much again as the change in income – 1 mark.

Commentary – given generally rising incomes, this is a good sector of business to be in (1). There could be future possibilities for expansion (1).
 Comment on data accuracy is relevant.

One comment elaborated but recognising longer term aspect of income elasticity – 2 marks.

(d) **If a take-away food shop grows in size, it can benefit from economies of scale.**

(i) **Define the term 'economies of scale.'** [2]

For correct definition which recognises

- falling average cost
- over a long run period of time
- due to increased scale of operation i.e. all factors change

1 mark for general idea e.g. falling unit costs as output increases or similar –
1 mark.

(ii) **Identify and explain one example of an economy of scale that might be of benefit to a take-away food shop.** [3]

Various possible examples including

- bulk buying of ingredients
- change in scale of operation e.g. purchase of nearby competitor
- increased use of technology
- financial economies
- division of labour
- external economies

1 mark for identification of a source of economies of scale. 2 marks for a clear understanding of benefits **in terms of lower long run average costs or increased scale of operation**. 1 explanation mark for an answer that does not make increases in scale clear.

(e) **Owners of take-away food shops do not always maximise profits. Explain two reasons why this might be the case.** [6]

Other likely reasons/objectives include

- sales revenue maximisation
- sales maximisation
- satisficing, including social and cultural reasons and/or keeping shareholders happy
- breaking even/avoiding losses
- unable to establish correct cost/revenue figures.
- firms are inefficient and so costs are high
- could attract new firms who would compete away profits
- if a monopoly, no need to maximise profits.

1 mark for recognition plus 1-2 marks for an explanation/elaboration in each case.

Must explicitly or implicitly relate answer to one of the objectives.

- (f) (i) Explain two characteristics of monopolistic competition. [4]

Any two of the following characteristics

- few (no) barriers to entry
- large number of small firms due to low barriers to entry
- differentiated products
- non-price competition
- price maker
- abnormal profits only in short run
- perfect information

1 mark for identification plus 1 mark for explanation/elaboration.

- *(ii) Using the information provided, discuss the extent to which the market for take-away food in Bradford is monopolistically competitive. [12]

The aim of this question is to consider the theoretical characteristics of monopolistic competition, consider those given in the case material and to then make an evaluation as to whether theory and practice matches.

From the evidence,

- there is a large number of small firms (450 – 500)
- the products are differentiated
- there are some barriers to entry (set up costs and hygiene certificates)
- there appears to be non-price competition

Relevant discussion could revolve around

- whether the barriers to entry are substantial
- role of profits
- whether firms are price makers

On balance though, the evidence supports the view that the market is monopolistically competitive.

- L4 For a discussion of the extent to which the market is monopolistically competitive. (7-12)
- L3 For an analysis of monopolistic competition, drawing upon the case material. (5-6)
- L2 For an application of knowledge of some of the characteristics of monopolistic competition to the case. (3-4)
- L1 For knowledge of monopolistic competition and/or one/a few unstructured points. (1-2)

Possible examples for levels 1-4**Level 1 (1-2 marks)**

Description – for a descriptive knowledge of monopolistic competition, not explicitly using the information provided.

Examples

- Large number of sellers
- Large number of buyers
- Few barriers to entry
- Differentiated products
- Firm is a price maker
- Normal profits earned in long run

L1 is no more than a repetition / extension of the market characteristics as set out in previous part.

Level 2 (3-4 marks)

Application – for an application of the information provided to the characteristics of a monopolistically competitive market.

Examples

- 450 – 500 small take away food shops (large number of sellers)
- each business is competing with large numbers of similar producers
- each business has its own range of curries etc (product differentiation)
- cost of starting up a take away shop is a few thousand pounds (few barriers to entry)
- food hygiene certificates (few barriers to entry)

Level 3 (5-6 marks)

Analysis – this should be achieved through using economic analysis to explain the applied characteristics of the market.

Examples

- Large number of sellers means that no one firm can influence the total market
- Product differentiation means that firms are likely to compete on a non-price basis with respect to the range and quality of their products
- Local advertising is a likely consequence of the market structure
- Barriers to entry if substantial tend to deter new firms from entering a market

Level 4 (7-12 marks)

Discussion – some discussion of the extent to which the market is monopolistically competitive.

Examples

- Profit maximisation is not necessarily an objective of the business
- Competitive prices seem likely to reduce the scope of a business to be a price maker
- All businesses and staff will require hygiene certification, so this may not necessarily be seen as a barrier to entry

- Cost of market entry is relatively modest
- No evidence of abnormal profits in short run / normal profits in long run
- Given importance of barriers to entry, on balance, the market appears to fit the model of monopolistic competition.

The last point should put an answer towards the top of the L4 range.

It is important that appropriate evidence underpins any overall conclusion on the 'extent' aspect.

	(a)	(b)(i)	(b)(ii)	(c)(i)	(c)(ii)	(d)(i)	(d)(ii)	(e)	(f)(i)	(f)(ii)	TOTAL
AO1 Target: 13-14	1	1	1	2		2	1	2	2	2	14
AO2 Target: 13-14	3	2	2				2	2		2	13
AO3 Target:9		1	1		2			2	2	2	10
AO4 Target: 9					2					6	8
Specification	5.1.2		5.1.2		5.1.2		5.1.3	5.1.3		5.1.3	

Mark Scheme 2882
June 2005

(a) (i) Define the term negative externality. [2]

This is where social cost exceeds private cost (2 marks).

Where the price paid by consumers does not reflect the full social cost of their actions (2 marks).

A cost imposed upon a third party (1 mark) as a result of a decision or production/consumption (1 mark) for which they are not compensated for (1 mark).

A negative externality is where there is a third party / spillover effect (1 mark) arising as a result of a production / consumption decision (1 mark).

1 mark for the simple statement that it is an external cost or that it is a cost/negative effect which is imposed upon a third party.

1 mark for a relevant example.

(ii) Using the extract, identify and explain one negative externality that may result from the building of the dam. [3]

1 mark for identification of a possible example such as destruction of habitats, loss of land, loss of beauty of the Three Gorges and the impact on the 1.5 million people relocated. Relevant examples arising from dam construction which are not explicitly mentioned in the extract are valid.

Up to 2 marks for an explanation that introduces clear economics. For example, explicit reference to social costs exceeding private costs or clear reference to a cost being imposed upon a third party.

1 mark for basic idea that this is a bad effect imposed upon someone. Accept implied understanding of external costs or social cost exceeding private cost which is not clear for 1 mark.

1 mark only for explanation which involves no more than a simple definition.

(iii) Using the extract, identify and explain one positive externality that may result from the building of the dam. [3]

1 mark for identification of possible positive externalities such as increased economic growth, cheaper electricity to local residents or the possible reduction in flooding that the government claim will result. Relevant examples arising from dam construction which are not explicitly mentioned in the extract are valid.

Up to 2 marks for an explanation using clear economics. 2 marks where reference is made to social benefit exceeding private benefit or as to why there is a third party benefit.

1 mark for the basic idea that it is a benefit received by those outside of the decision making process or vague/ implied idea of social benefit exceeding private benefit.

1 mark only for explanation which involves no more than a simple definition.

(b) Define the terms productive, allocative and Pareto efficiency. [6]

Productive efficiency. Up to 2 marks for a correct definition including:

Where production takes place at the lowest point of the average cost curve or at the point of minimum efficient scale (2 marks)

Where production occurs with $MC=AC$ (2 marks)

Where production uses as few scarce resources as possible (2 marks)

Production takes place on the PPF (2 marks). Accept a diagram showing this

Where maximum output is achieved (1) from the minimum number of resources (1).

1 mark for a vague idea that goods are produced cheaply or at a lower cost or production takes place at minimum cost.

Accept diagram of long run average cost (2 marks).

Allocative efficiency. Up to 2 marks for a correct definition including:

Where the firm produces at $P=MC$ (accept $AR=MC$) (2 marks)

Where the firm uses resources (1) to produce goods which consumers want (1).

For a basic idea that production takes place which makes the best use of resources (1 mark).

For vague idea that it is producing those goods which consumers demand but lacks any reference to resources (1 mark).

Vague idea that it involves using resources in their most efficient way (1 mark).

Pareto efficiency. Up to 2 marks for a correct definition including:

A situation where it is impossible to make one person better off (1 mark) without making someone else worse off (1 mark). Complete statement gains 2 marks.

Where an economy is productively and allocatively efficient (2 marks). Alternatively, 1 mark can be gained from each separate part:

- Where the economy is productively efficient / produces at minimum AC / is producing at a point along the production possibility curve (1 mark)
- Where the economy is allocatively efficient / producing where $P = MC/MSC$ (1 mark).

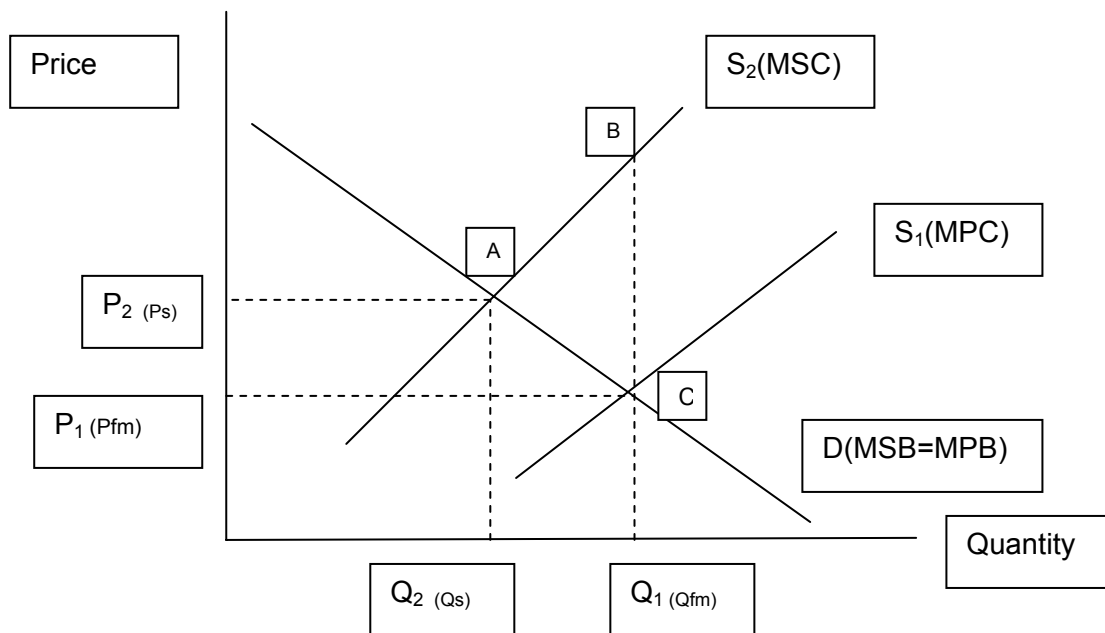
- (c) Using a diagram, analyse how the existence of negative externalities leads to market failure. [10]

A basic diagram is required showing the free market supply curve (or MPC) lying to the right of society's supply curve (or MSC). Either supply and demand or MSC/MPC approach is acceptable. (Max of 2 marks for non S&D diagram showing $SC > PC$.)

A maximum of 6 marks are available for a correct diagram:

P_1Q_1 = free market equilibrium
ABC = area of welfare loss

P_2Q_2 = society's desired equilibrium



- 1 mark for both axes (allow P/Q) OR if MSC/MSB used accept cost/output**
- 1 mark for original supply curve/MPC (accept PC)
- 1 mark for original demand curve
- 1 mark for original equilibrium clearly labelled
- 1 mark for showing society's supply curve to the left of free market supply
- 1 mark for new equilibrium (higher price and lower output in free market)
- 1 mark for identifying the correct area of welfare loss

Up to a maximum of 6 marks are available for a correct explanation, including:

In a free market, firms only take in to account their private costs (1 mark) and therefore ignore external costs (1 mark). This means that S_2/MSC lies to the left of S_1/MPC or that the free market supply curve is to the right of society's supply curve (or that $MSC > MPC$) (1 mark).

This means that the price charged (in a free market) will be lower than otherwise (1 mark) which results in over consumption/over production (1 mark).

Allocative inefficiency arises (1 mark) as too many scarce resources are used up in production (1 mark). This represents a misallocation of resources (1 mark).

** Only give mark for axes labelled cost/benefit vs output if $SC > PC$ curves used.

(d) One policy the Chinese government could use to encourage families to relocate is to give a subsidy to companies constructing new homes away from the dam.

(i) State two costs and two benefits of using a subsidy in this way. [4]

1 mark each for identification of costs up to a maximum of 2 marks:

- the financial cost of the subsidy (increased cost of the dam project)
- the opportunity cost of increased spending in terms of reduced expenditure elsewhere or higher taxes
- the environmental damage caused by the building of new homes or any other possible negative externality which may arise
- possible increased inefficiency caused by over reliance upon subsidies.

1 mark each for identification of benefits up to a maximum of 2 marks:

- increased custom/business for builders/increased work or revenue for firms/firms face lower costs
- reduced unemployment in areas where the housing is to be built/increased economic growth in the region (possible multiplier effects)
- increased supply of new houses
- houses may be cheaper (lower prices)/greater incentive for people to move.

(ii) Comment on the likely effectiveness of this policy. [5]

Up to 2 marks for simple analysis (simple subsidy diagram worth up to 2 marks).

A subsidy will work because it will lower costs of production (1 mark), increase supply/output (1 mark), reduce price (1 mark) and possibly increase the quantity demanded of housing (1 mark).

Up to 3 marks for discussion / comment on why subsidies may not work:

- It depends upon how the subsidy is used. Builders may not pass on subsidy in terms of lower prices, thus having little/no effect on demand. Likewise, builders may use most of the subsidy simply to increase profit.
- A subsidy will not work as local residents are bitter about losing their land and will not move or they are simply too old and incapacitated to relocate.
- With many residents unwilling or unable to move, reducing the price of the homes will have little effect on demand. In other words, demand is inelastic.
- The effect may well depend upon the size of the subsidy. Too small and there may be no real effect. In other words, what size should the subsidy be?
- The subsidy may be effective in terms of providing more houses but there will be a wider impact in terms of environmental damage/external costs.
- Time lags are involved – the policy will take a long time to have effect because houses cannot be built overnight. Supply is likely to be inelastic.
- Won't remove the cost/inconvenience of moving so may prove to be ineffective.

One point which is well developed can gain up to three marks.

- * (e) **In deciding whether to build the dam, the Chinese government could have used cost-benefit analysis. Discuss how cost-benefit analysis could be applied in the case of the building of a dam, such as the Three Gorges. [12]**

For a level 4 answer, candidates will be expected to comment upon some of the problems of using CBA in this context.

Possible evaluation could include measurement issues and the difficulties of placing monetary values on external costs and benefits such as the loss of scenery. Likewise, candidates could consider political interference which means that the results of CBA could be ignored. (The article implies that there is strong government support for the scheme which means that this criticism may be well founded.) Other possible comment involves the problems of deciding what costs and benefits to include (this implies a value judgement) and the problems of measuring future costs and benefits.

For level 3 responses, candidates will be expected to analyse what use CBA is. The simplest way to do this would be to say that the government weighs up total costs and benefits and goes ahead only if benefits exceed costs (i.e. there is an overall net benefit).

An answer that simply lists what costs and benefits would be measured receives a maximum of 4 marks for application only.

Level 4	A discussion of the possible problems of using CBA in this situation.	7-12 marks
Level 3	Analysis of the use of CBA in building the dam but lacking any clear discussion/comment on problems.	5-6 marks
Level 2	Application of knowledge of CBA to the construction of the dam by looking at what costs/benefits would be measured.	3-4 marks
Level 1	Basic knowledge of what CBA is, lacking any relevant application to the building of the dam.	1-2 marks

Possible valid level 4 responses include:

- Measurement issues and the difficulties of placing monetary values on external costs and benefits, such as the loss of the scenery.
- The possibilities of political interference which means that potentially the results of CBA could be altered/ignored if the government want to go ahead with the project (the article implies that there is strong government support for the scheme).
- What costs and benefits should be included? (this implies a value judgement).
- The difficulties of taking in to account future costs and benefits.
- The costs of conducting CBA may be prohibitive, outweighing any benefits (in other words it is an expensive procedure).

Possible level 3 responses covering analysis include:

- The government will decide whether or not to go ahead with the project based upon a comparison of social benefits and social costs. If $SB > SC$ then they will go ahead with the project, otherwise they should not do so. Clear reference to social costs and social benefits but lacking any discussion (for level 4) will gain 6 marks.
- The government will go ahead with the project only if benefits exceed costs. If there is no discussion then this answer gains 5 marks.

Possible level 2 responses covering application include:

- Good application of what the costs and benefits of building the Three Gorges Dam are is sufficient to gain 4 marks
- Basic application of either the costs or the benefits of building the Three Gorges Dam will receive just 3 marks.

Specification Grid

	(a)(i)	(a)(ii)	(a)(iii)	(b)	(c)	(d)(i)	(d)(ii)	(e)	TOTAL
AO1 Target: 13-14	2	1	1	6	2			2	14
AO2 Target: 13-14		2	2		4	4		2	14
AO3 Target: 9					4		2	2	8
AO4 Target: 9							3	6	9
Specification section	5.2.2	5.2.2	5.2.2	5.2.1	5.2.2	5.2.3	5.2.3	5.2.3	

**Mark Scheme 2883
June 2005**

(a) (i) Define the term 'exchange rate' (line 8). [2]

- 1 mark for price/rate/value of a currency.
- 1 mark for how exchange rate is determined.
- 1 mark for comparison against another currency.
- 1 mark for example.

(ii) Define the term 'injections' (line 9). [2]

- 2 marks for additions to AD/spending.
- 1 mark for reference to the circular flow.
- 1 mark for reference to autonomous additions.
- 2 marks for I+G+X.
- 1 mark for money entering the economy.
- 1 mark for each example.

(b) (i) Using the information in the passage, calculate the value of imported goods in 2002. Show your working. [2]

- 1 mark for £220bn.
- 1 mark for correct working in words or figures or for trade balance=exports-imports or other appropriate versions.

(ii) Using examples, explain two ways in which UK consumers may benefit from international trade. [6]

- 1 mark for each of two benefits identified e.g. higher living standards, more choice, lower prices, better quality.
- 1 mark for each of two limited explanations of benefits e.g. higher standards of living due to higher output, lower prices due to more competition.
- 1 mark each for each of two further elaboration's e.g. higher output due to specialisation, more competition forces firms to keep costs and prices lower.
- 1 mark for each example.

**(c) Using Figure 1:
(i) state what is meant by macroeconomic equilibrium; [1]**

- 1 mark for a situation where AD=AS.
- 1 mark for a situation where injections=leakages/withdrawals.
- 1 mark for situation where output is unchanged/no pressure for output to change.
- 1 mark for situation where price level is unchanged/ no pressure for price level to change.
- 1 mark for reference to P/Y or P1/Y1.

(ii) explain two factors that might have caused the shift in the aggregate supply curve from AS to AS1; [6]

- 1 mark for each of two causes identified e.g. improved technology, better training, increase in labour force, investment, fall in raw material costs, fall in wage rates.
- 1 mark for each basic explanation e.g. better training increases the productivity of labour.
- 1 mark for each further elaboration e.g. higher productivity increases the productive potential of the economy/increases AS/increases output.

4 marks maximum if explaining factors causing a decrease in AS.

(iii) analyse two policy measures that the UK government could use to move aggregate demand from AD to AD1. [8]

1 mark for each of two policy measures identified e.g. increase in government spending, decrease in income tax, cut in interest rates, increase in tariffs.

1 mark for elaboration on each policy – eg government spending is a form of fiscal policy or interest rate change is a form of monetary policy.

Up to 3 marks each for each explanation of how two measures should increase AD.

For examples in the case of a decrease in income tax.

1 mark for it will increase disposable income.

1 mark for increased disposable income will raise consumption.

1 mark for consumption is a component of aggregate demand.

1 mark for higher consumption is likely to stimulate investment.

1 mark for reference to the multiplier effect.

6 marks maximum if explaining measures to reduce AD.

(d) (i) What is meant by the Claimant Count measure of unemployment? [2]

1 mark for based on those claiming /receiving unemployment benefit.

1 mark for a measure of those out of work and willing and able to work.

1 mark for reference to any relevant group of people who are actively seeking work which is excluded from the measure.

1 mark for reference to job seekers' allowance.

(ii) Comment on two difficulties of measuring unemployment. [4]

1 mark for problem of deciding who is unemployed.

1 mark for reference to those falsely claiming benefit.

1 mark for reference to the existence of unemployed people not entitled to receive benefit.

1 mark for changes in eligibility rules.

1 mark for ILO/Labour Force Survey is based in a sample.

1 mark for a sample measure may not be representative.

1 mark for ILO measure takes time to compile.

1 mark for ILO measure is costly.

1 mark for any development of how each difficulty affects the figures.

(e) Discuss the economic consequences of inflation. [12]

Comments may include the consequences will depend on its rate, its relative rate, whether it is stable or not, whether it has been anticipated or not, whether it is of a demand-pull or cost-push nature, there may be benefits as well as costs.

Consequences may include shoe leather costs, menu costs, administrative costs, inflationary noise, arbitrary redistribution of income, adverse effect on the balance of payments, possible boost to consumption and production, increase ease of adjusting real wage rates.

Level 4 For a discussion of the consequences of inflation with some appropriate evaluation. (7-12)

Level 3 For an analysis of the consequences of inflation. (5-6)

Level 2 For an understanding of the consequences of inflation. (3-4)

Level 1 For a description of the consequences of inflation. (1-2)

Possible examples for levels 1-4**Level 1 (1-2 marks)**

Description of inflation.

Examples

- Inflation is a sustained rise in the general price level
- A low and stable inflation rate is a government macroeconomic objective
- The government's target rate for inflation is 2% as measured by the CPI
- Inflation is measured by the CPI/RPI/RPIX

Level 2 (3-4 marks)

Understanding – in this case the identification of some of the consequences of inflation.

Inflation can cause a number of problems including shoe leather costs, menu costs, administrative costs, inflationary noise, arbitrary redistribution of income, fiscal drag and an adverse effect on the balance of payments.

Level 3 (5-6 marks)

Analysis – in this case, this would involve an explanation of some of the costs of inflations.

Example

Inflation can have a number of adverse effects on an economy. One is that it gives rise to menu costs. As the price level rises, firms have to spend time and effort changing price labels and prices in catalogues.

Firms may also experience shoe leather costs and higher administrative costs. During periods of high inflation, firms cannot afford to leave money lying idle. They have to seek out the financial institutions offering the highest rate of interest and constantly check that the interest they are receiving is above the rate of inflation. In addition, staff time has to be

devoted to adjusting firms' accounts, renegotiating contracts with suppliers and negotiating wage rises with employees.

Both firms and households may experience inflationary noise. Inflation makes it difficult for firms and households to assess changes in relative prices. This may mean that they buy from more expensive sources and so inefficiency is caused. There can also be an arbitrary redistribution of income with some groups gaining and some groups losing as a result of inflation. For instance, lenders tend to lose and borrowers tend to gain as the nominal rate of interest does not usually rise in line with inflation, causing the real rate to fall. Workers with strong bargaining power are likely to be able to gain wage rises at least in line with inflation, if not above, whilst those with weak bargaining power may experience cuts in real wages.

The government may receive a gain from inflation at the expense of taxpayers as a result of fiscal drag. This occurs when the Chancellor of the Exchequer increases tax thresholds only by inflation or less, so that as pay rises, more people are taxed at higher rates.

In addition to the internal costs that inflation can impose, there is also the adverse effect it can have on the country's external trade position. Inflation may result in a country exporting less and importing more and a worsening of its current account position.

Level 4 (7-12 marks)

Evaluation – this involves making judgements and, in this case, discussing what influences the significance of the costs and/or recognising that as well as imposing costs, inflation may also give rise to some benefits.

Examples

- If a country's inflation rate is higher than that of its rivals, its products will become less price competitive. Demand for exports will fall whilst demand for imports will rise and so there is likely to be an adverse effect on the balance of payments.
- If inflation has been anticipated, it will make it easier for economic agents to take action to offset its effects. For example, tax brackets and pensions can be raised in line with inflation, workers can seek wage rises in line with inflation and savers can seek an appropriate rate of interest.
- As well as having harmful effects, inflation may also have some benefits. A low and stable level of demand-pull inflation may encourage a rise in output. This is because firms, seeing higher demand and rising prices, are likely to anticipate higher profits.

Specification Grid

Target	(a)(i)	(a)(ii)	(b)(i)	(b)(ii)	(c)(i)	(c)(ii)	(c)(iii)	(d)(i)	(d)(ii)	(e)	Total
AO1 13-14	2	2		2		2	2	2		2	14
AO2 13-14			2	2	1	4	2		1	2	14
AO3 9				2			4		1	2	9
AO4 9									2	6	8
Total	2	2	2	6	1	6	8	2	4	12	45
Subject Content Reference	5.3.1	5.3.2	5.3.1	5.3.4	5.3.2	5.3.2	5.3.3	5.3.1	5.3.1	5.3.3 5.3.1	

Mark Scheme 2884
June 2005

- 1 (a) (i) **Using Table 1, identify the group which was most disadvantaged between the years 1993 and 2000.** [1]
- Women with low qualifications in high unemployment areas.
Only 'women with low qualifications' is 0, but 1 mark if suitably qualified.
- (ii) **From the article, identify a measure which indicates the scale of the 'hidden army'.** [1]
- Any valid measure of the 'economically inactive' but must be a measure.
- (iii) **Suggest two benefits which might result from reducing the scale of the 'hidden army'.** [2]
- 1 for each of two possible valid benefits – eg reduced government expenditure on welfare payments, increased GDP, boost to depressed regions. [Accept reduction of government expenditure on unemployment benefit.]
- (b) **Explain what is meant by:**
- (i) **the quality of jobs being created (line 6);** [2]
- 1 for identification of low quality jobs (part-time, low-paid or both) and 1 for explanation linked to varying quality of jobs.
- (ii) **detached from the labour market (line 12).** [2]
- 1 for identification as those with poor qualifications and 1 for explanation, linked to nature of work/demands of employers.
- NB: Same mark allocation – 1 for identification, plus 1 for explanation – if a candidate answers in a different (eg more general) but valid way, for both (i) and (ii).
- (c) (i) **Explain how the existence of a 'hidden army' is an example of labour market failure.** [2]
- 1 for mere statement that 'hidden army' are not employed, which constitutes a labour market failure. Must be linked to the meaning of market failure for 2 marks.
2 for explanation of hidden army as a market failure, in terms of economically inactive people not being able to be wage-earners, contributing to output.
- (ii) **Comment on why government help in paying for childcare (line 27) has helped to reduce labour market failure.** [4]
- 1 for linking non-employed lone parents to labour market failure. 1 for explaining how government help in paying for childcare has reduced market failure by attracting lone parents into work.
2 for valid comment – eg comparing the benefits to the cost of the childcare.

[N.B. Must include comment on possible policy downside for more than 3 marks in total.]

- (iii) **Discuss the possible impact of policies aimed to reduce the size of the 'hidden army'.** [6]

Explanation/identification of appropriate policies – eg education and training. Explanation of possible beneficial effects of such policies, in terms of additional output, and living standards, greater equality in distribution of income, etc. Consideration of possible problems or disadvantages – eg are the people involved capable of being appropriately trained? ability of government to provide appropriate training? extra government spending?

L2	For evaluative discussion.	3-6
L1	For explanation of at least one possible impact.	1-2

[N.B. Maximum of 4 marks if answer considers only beneficial effects.]

- 2 (a) **Explain how provisions of the EU Social Charter affect the supply of labour in the UK.** [10]

Meaning of 'supply of labour in UK' – both in total, and in different occupations. Identification of main provisions of the EU Social Charter – aim of harmonisation of working conditions, with rights in the areas of trade union representation and industrial action, consultation and participation, equal treatment, minimum wages, maximum working time, minimum holiday entitlement, redundancy. Explanation of consequences for UK labour supply (though with opt-outs).

L3	For explanation of a range of consequences.	7-10
L2	For understanding of at least one effect.	4-6
L1	For knowledge of EU Social Charter.	1-3

- (b) **Discuss the view that full implementation of the EU Social Charter would make the UK labour market too inflexible.** [15]

Meaning of 'flexible' labour market, and explanation of its benefits. Explanation of effects of full implementation of EU Social Charter (from (a)), in terms of reduced labour market flexibility, and the disadvantages of this. Evaluation, in terms of 'too inflexible', assessing on the other hand the advantages too of full implementation.

L4	Discussion weighing benefits against disadvantages of full implementation, focusing on 'too inflexible'.	9-15
L3	Analysis of consequences in terms of inflexibility.	6-8
L2	Application of effects of implementation.	3-5
L1	Knowledge – a few descriptive points only.	1-2

3 So-called ‘fat cat pay’ for some top executives is inevitable in a market economy; all workers have to be paid the rate for the job.

(a) Explain the factors underlying the determination of wages in a market economy. [10]

Interpretation of ‘market economy’, and of ‘relative wages’. Explanation of wage determination in terms of supply and demand for labour. Factors underlying demand in different occupations, in particular MPP and product prices. Factors influencing supply – eg skills and qualifications, non-monitory not advantages.

L3	For explanation of a range of both supply and demand – side influences.	7-10
L2	For understanding perhaps only basic supply and demand analysis, or only one-side influences.	4-6
L1	For knowledge of factors influencing wages.	1-3

[N.B. Maximum of 4 marks if only basic Supply and Demand analysis used. Maximum of 6 marks if only one side of Supply & Demand analysis used to explain wage determination.]

(b) Discuss the view that any government attempt to interfere in the process of wage determination is bound to create more problems than it solves. [15]

Explanation of reasons why a government may wish to ‘interfere’ – on fairness/equity grounds; to improve the functioning of the labour market; to counteract excessive power (of employers or employees/trade unions); as a major employer. Identification of possible methods of ‘interference’ – eg minimum wages, action to reduce ‘fat cat pay’, limitation of public sector pay. Explanation of possible consequences – workers not being paid the ‘rate for the job’, for example – in terms of inefficient allocation of resources, distribution of income, incentives, etc. Evaluation, weighing of benefits and disadvantages of government ‘interference’.

L4	Discussion, weighing benefits and disadvantages.	9-15
L3	Analysis, either of reasons for, or of effects of, government interference.	6-8
L2	Application of knowledge only, to government involvement in wage determination.	3-5
L1	Knowledge - a few descriptive points only.	1-2

[N.B. Policies aimed to reduce ‘fat cat pay’ are not required: any policy on influencing relative wages is acceptable.]

- 4 (a) **Explain the main features of the behaviour of firms which operate in an oligopolistic market.** [10]

Meaning of oligopoly – small number of competing firms. Main characteristics – interdependence, price-makers, differentiated products, barriers to entry. Main features of behaviour of firms – collusion (open/tacit), price leadership, price stability and non-price competition, price wars.

- | | | |
|----|--|------|
| L3 | For explanation of the market structure and of a range of typical firms' behaviour. | 7-10 |
| L2 | For understanding, perhaps focusing on market structure, or at most one type of behaviour. | 4-6 |
| L1 | Knowledge – a few descriptive points only. | 1-3 |

[N.B. Use of Kinked Demand Curve is not required, though could enhance the quality of explanation of price stability if used.]

- (b) **Discuss the extent to which firms in the UK TV broadcasting industry behave as oligopolists.** [15]

Identification of the 'firms' competing in the UK TV broadcasting industry. Explanation of their different objectives, and of the way they 'behave'. Identification and explanation of ways in which behaviour can be categorised as oligopolistic – eg competing over market share, non-price competition (eg programme quality (range), collusion (eg scheduling), charges for advertising. Identification and explanation of other aspects of behaviour – eg different objectives and method of funding of BBC.

- | | | |
|----|--|------|
| L4 | Discussion, weighing behaviour of firms with oligopoly, focusing on "extent to which". | 9-15 |
| L3 | Analysis of behaviour of firms in the industry. | 6-8 |
| L2 | Application of knowledge only, on firms in the TV broadcasting industry. | 3-5 |
| L1 | Knowledge - a few descriptive points only. | 1-2 |

[N.B. Maximum of 8 marks if no reference to oligopolistic behaviour. Maximum of 12 marks if no reference to ways in which the behaviour differs from that expected in oligopoly.]

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Q1										Q2,3,4			
	a(i)	a(ii)	a(iii)	b(i)	b(ii)	c(i)	c(ii)	c(iii)	Total	(a)	(b)	Total	TOTAL
A01	1	1				1	1		4	3	2	5	9
A02			2	1	1				4	3	3	6	10
A03				1	1	1	1	2	6	4	3	7	13
A04							2	4	6		7	7	13
									20			25	45

Q1 - 5.4.1 +5.4.4

Q2 - 5.4.4

Q3 -5.4.3 + 5.4.4

Q4 - 5.4.2

**Mark Scheme 2885
June 2005**

Section A

1 (a)

- (i) Identify and explain two private costs which might result from the Crossrail scheme. [4]

1 mark x 2 for identifying private costs of the scheme e.g. costs of construction of the new line, costs of maintaining and running it over its estimated life.

Up to 2 marks for explanation of why such costs are private costs i.e. paid for by those imposing them. One of examples explained well can gain 2 marks.

- (ii) Identify and explain two possible external benefits, which might result from the Crossrail scheme. [4]

1 mark x2 for identification of external benefit e.g. reduced road and tube congestion, regeneration of poorer parts of London, new jobs.

Up to 2 further marks for explanation of why such benefits are external i.e. received by a third party who does not pay for them. One such benefit explained well can gain 2 marks.

- (b) Outline why public-private finance is necessary to fund a major project such as Crossrail. [2]

1 mark for simple idea e.g. that combination required for such a large financial commitment or clear understanding of what PPP involves.

2 marks for an elaboration for e.g. covering both of the above or could consider social desirability of a project as well as rate of return.

- (c) In order to conduct a feasibility study (Extract 1, line 10), estimates of demand would be necessary. Comment on the problems likely to be faced by economists when estimating the demand for Crossrail. [4]

Up to 2 marks for explanation of forecasting and its inherent problems applied to Crossrail e.g. in terms of estimated future demand through market research or extrapolating trends which may lack accuracy.

Up to 2 marks for further discussion e.g. does not exist already, will need surveys of customer need, construction may boost demand, need to assess journey purpose.

- (d) Discuss whether cost-benefit analysis would be an appropriate decision-making tool to use when considering whether to proceed with projects such as Crossrail. [6]

1-2 marks for knowledge/explanation of cost-benefit analysis with or without specific application to Crossrail.

3-4 marks for discussion of CBA without specific application.

5-6 marks for an assessment of the appropriateness of CBA for projects such as Crossrail e.g. provides a long and wide view including possible externalities such as reduction in traffic elsewhere such as the M25; are the estimates likely to accurate? Demand difficult to predict it could provide framework for further enquiry.

Section B

2 (a) Explain the main problems associated with monopolies. [10]

Explanation of why monopolies produce at a lower output and charge higher price compared to a more competitive market – possible use of a diagram but not required. Consideration of price discrimination. Inefficiency – both productive and allocative with explanation. Possible consideration of X-inefficiency. The key is the explanation of why these are problems perhaps via market failure in comparison to more competitive markets.

Level 3 For an explanation of the problems associated with monopoly. 7 – 10

Level 2 For an understanding of the problems associated with monopoly. 4 – 6

Level 1 For knowledge of the problems associated with monopoly. 1 – 3

(b) Discuss the possible impact of greater regulation on the local bus industry in the UK. [15]

Needs consideration of performance of a more regulated local bus industry; analysis of effects, specific examples beneficial. Will barriers be erected following regulation? Were other barriers removed? E.g. an economy of major groups; can new firms enter the market? Will the market become less contestable and more/less efficient; e.g. in terms of increased bus mileage, costs, patronage, rural services, safety concerns and employment conditions. Regional issues should be rewarded.

Level 4 For an evaluation of the impact of greater regulation on the local bus industry in the UK. 9-15

Level 3 For an analysis of the impact of greater regulation on the local bus industry in the UK. 6 – 8

Level 2 For an application of the impact of greater regulation/deregulation of the local bus industry. 3 – 5

Level 1 For some knowledge of knowledge of regulation/deregulation. 1 - 2

3 (a) Explain the determinants of demand for the main modes of freight transport.

[10]

Knowledge of main modes of freight transport; nature of derived demand for all freight in general linked to increases in GDP but also consideration of influences on demand affecting modal choice e.g. convenience, cost, speed, reliability etc and how this will differ according to the goods being transported.

Level 3 For an explanation of determinants of demand for the main modes of freight transport. 7-10

Level 2 For an understanding of the determinants of demand for the main modes of freight transport. 4 – 6

Level 1 Knowledge of the determinants of demand for the main modes of freight transport. 1 – 3

(b) Discuss the extent to which recent trends in freight transport are sustainable.

[15]

Definition of sustainability. Trends in freight transport demand – increasing but road increasing share and third party logistics an increasing share of that. Rail more sustainable – more efficient use of resources – than road. Similar comparison between sea and air although trend in airfreight growth small in comparison to road. Logistics companies making increasing use of rail and offer more than just haulage; greater organisation may bring economies and more efficient use of resources. Emphasis should be applying concept of sustainability to freight transport.

Level 4 For an evaluation of the extent to which recent trends in freight transport are sustainable. 9-15

Level 3 For an analysis of whether recent trends in freight transport are sustainable. 6-8

Level 2 For an application of knowledge of sustainability as applied to freight transport. 3-5

Level 1 For some knowledge of recent trends in freight transport and/or sustainability. 1-2

- 4 Following the introduction of the congestion charge in London in 2003, there have been suggestions for a more widespread introduction of road user charging in other UK cities.**

(a) Explain the economic basis for road user charging in cities. [10]

Explanation of congestion as a symptom of market failure in terms of excess demand because the price of roads is too low i.e. free. This is particularly relevant at peak times in cities. Roads are quasi-public goods rather than public goods and can be charged for. Consideration of the negative externalities associated with congestion and hence a misallocation of resources.

Level 3 For an explanation of the economic basis for user charging in cities. 7 – 10

Level 2 For an understanding of the economic basis for user charging in cities. 4 – 6

Level 1 For knowledge of the economic basis for user charging in cities. 1 - 3

(b) Discuss the likely impact on businesses of widespread road user charging in UK cities. [15]

Widespread user charging could imply more urban schemes. Charges would internalise the externalities and reduce market failure. But charges would need to reflect the monetary value of the marginal external cost caused which would mean variable charges according to place and time of day in order to be efficient. Practical difficulties in how this would be implemented and resentment of another tax burden increasing business costs. Possible loss of business in area where charges are higher. On the positive side, funds could be hypothecated and used to improve roads, rail or public transport; other taxes e.g. on fuel or licenses could be cut to reduce tax burden.

Very topical, expect many other equally valuable responses.

Level 4 For an evaluation of the likely impact on businesses of widespread road user charging in UK cities. 9 -15

Level 3 For an analysis of the likely impact on businesses of widespread road user charging in UK cities. 6 – 8

Level 2 For application of knowledge of the likely impact on businesses of widespread road user charging in UK cities. 3 – 5

Level 1 For some knowledge of the impact of road user charging in the UK. 1 - 2

Specification Grid

	Question 1					Question 2		Question 3		Question 4		Total
	(a)(i)	(a)(ii)	(b)	(c)	(d)	(a)	(b)	(a)	(b)	(a)	(b)	
AO1 (Target 9)			2		1	3	2	3	2	3	2	8
AO2 (Target 9)	2	2				3	3	3	3	3	3	10
AO3 (Target 13-14)	2	2		2	1	4	3	4	3	4	3	14
AO4 (Target 13-14)				2	4		7		7		7	13
												45

Subject Content Reference	5.5.3	5.5.3	5.5.1	5.5.3	5.5.3	5.5.2	5.5.1+5.5.4	5.5.4
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Quality of Written Communication embedded in Section B mark scheme: see general introduction to mark scheme.

**Mark Scheme 2886
June 2005**

Section A

1 (a) Explain how the production of oil may affect São Tomé's

- production possibility curve and

Move it outwards or diagram (1), result of increased resource (1), may affect shape/slope or diagram (1), alternatively may move towards ppf or diagram (1), fuller use of resources (1), 3 marks max.

- current account on the balance of payments.**[4]**

Help via oil export revenue (1), reduced oil import spending (1) worse via import of oil equipment (1), ipd flows (1), shipping costs (1) conclusion (1) 3 marks max.

(b) Explain one possible reason why the values of GNP per head (US\$) are so different from those for GDP per head (ppp US\$). **[2]**

Understanding of national and domestic different or ppPs different to nominal \$ (1), explanation of either point (1).

(c) Use the information provided to explain whether São Tomé is a typical developing country. **[4]**

Typical features include low HDI and GNP per head, reliance on primary products and aid and a colonial background. Less typical resource potential, adult literacy and life expectancy. Credit comment on no typical developing economy.

1 mark per clarified point with both sides for 4 marks.

(d) Explain two ways in which multinational companies might help develop its oil resources. **[4]**

MNCs will undertake extraction (1), will provide the expertise (1), technology and equipment (1), provide funds (1), have links to markets (1) São Tomé lacks the ability to exploit on its own (1). Identification 1 mark, explanation 1 mark.

(e) Use the information provided to comment on the lessons São Tomé might learn from the development experiences of Equatorial Guinea and Gabon. **[6]**

Oil exploitation raises GDP per head, which could be the basis for development. This has not led to equal growth in GNP (profit repatriation). The data suggest that the oil producers do little better than São Tomé does without oil. This is shown by HDI figures. This reflects poor use of resources, poor governance and inequality. Wealth appears to be channelled into conspicuous consumption, suggests inequality and may be unsustainable. Traditional life styles are undermined, foreign values imported and the oil industry may generate externalities. In fact the government was deposed within six months of the article. It is essential that windfalls are managed appropriately and used toward development targets and that suitable policies are introduced. Candidates may be familiar with Nigerian experience.

Analysis of problems 2 marks, judgement of implications 4 marks.

2 (a) Explain Lewis' model of structural change within developing economies. [10]

Lewis' model suggests two sectors, a traditional rural subsistence sector and a modern, urban industrial sector. In the former labour has zero marginal productivity and can transfer to the industrial sector. Higher urban wages based on higher productivity will attract labour from agriculture. The reinvestment of profits would continue this transfer until surplus rural labour disappeared. The model assumes surplus agricultural labour, a competitive labour market and the operation of diminishing returns. It indicates the process by which developing economies may progress.

L3 For explanation of the model's operation. (7-10)

L2 For understanding of the model's features. (4-6)

L1 For knowledge of the model. (1-3)

(b) Discuss whether the achievement of developed status means a country has solved its basic economic problems. [15]

A developed economy is assumed to be in a stronger position than a developing economy. The fundamental economic problem will always remain based on scarce resources and unlimited wants. Developed economies face economic problems which differ in extent (e.g. higher gdp per head and higher life expectancy) and in nature(e.g. more environmental difficulties rather than material living standard issues) to those found in developing economies. Governments may not succeed in managing their economies to achieve all of their targets simultaneously. In the way that developing economies are individual in nature so are developed economies. The term-developed economy hides many dissimilarities and differentiated development will exist among developed economies. This can be highlighted by the use of examples. Strong level 4 answers may consider the meaning of developed and make use of examples.

L4 For discussion of the changing nature of problems. (9-15)

L3 For analysis of the success with problems. (6-8)

L2 For application of knowledge to the case of developed and developing economies. (3-5)

L1 For knowledge of basic economic problems. (1-2)

3 (a) Explain the relevance to developing economies of

- changes in the terms of trade and

The terms of trade relate the price of exports to the price of imports. They are a prime influence on the ability of countries to benefit from trade. Developing economies have experienced worsening terms of trade from falling prices of primary goods and rising prices of manufactures. This has worsened their standards of living.

- infant industries. [10]

Infant industries are those which have not developed sufficiently to benefit from their comparative advantage and gain international competitiveness from economies of scale. This is the position for developing economies in some areas of manufacturing where low cost labour is an advantage. To aid development infant industries must be promoted. Protection is justified in this case. Similar protection by developed economies creates an obstacle for developing economies.

- L3 For explaining the relevance to developing economies. (7-10)
- L2 For understanding of the link to developing economies. (4-6)
- L1 For a knowledge of one/both concepts. (1-3)

(b) Discuss whether or not a reduction in the barriers to international trade will help developing economies. [15]

Free trade indicates the absence of barriers such as tariffs, quotas subsidies etc. Benefits of trade arise from comparative advantage. These benefits include increased revenue, higher employment, faster growth and more choice. Economies of scale can be achieved. There should be more efficiency on a world and national scale. This can contribute to higher levels of development. One major problem faced by developing economies is the lack of access to the markets of developed economies, this would be overcome with free trade. More open trade may not benefit developing economies if they have uneven bargaining strength, lose their own domestic markets or lack factor mobility to respond to the new situation. A strong level 4 answer may establish the underlying theory.

- L4 For a discussion of the overall impact of free trade. (9-15)
- L3 For an analysis of the effect of free trade. (6-8)
- L2 For application of knowledge of developing economies. (3-5)
- L1 For knowledge of barriers to trade. (1-2)

4 (a) Explain how the current position of developing economies has been determined by their colonial backgrounds. [10]

Colonisation was common in Africa and Asia by UK, France and other European states. Dependency theory explains an outcome in which the developing economy comes to rely on developed countries to stimulate their growth. Critics of colonisation cite reliance on primary production, a captive market, trade on disadvantageous terms and low standards of living for the colony. It is argued that this pattern is little different today. Local enterprise may have been stifled and resources exhausted for short-term profit. Against this can be set the introduction of technology, the establishment of economic and political institutions, the promotion of education and the creation of trade links with preferential terms. At independence some developing economies were relatively prosperous. This has not necessarily been maintained subsequently e.g. in Africa. Other ex-colonies e.g. Malaysia and Singapore have progressed rapidly after independence.

- L3 For explaining the impact of colonisation. (7-10)
- L2 For understanding the features of colonisation. (4-6)
- L1 For knowledge of the current position of developing countries and/or colonisation. (1-3)

(b) Discuss why help from non-governmental organisations (NGOs) is often more welcome in developing economies than official aid from foreign governments. [15]

Non-governmental organisations include voluntary organisations and charities, they include Oxfam, World Vision and The Ford Foundation. They provide support on a small, more focused scale and with a minimum of conditions. Help often takes the form of skilled personnel. They often work in the most needy areas. Their total contribution has grown rapidly in recent years and is often based on humanitarian motives. Official aid is government help on concessional terms (lower interest rates or longer repayment) but may come with conditions. This is the case with tied aid, which may require purchases from the donor country. There is also a history of misuse and political obligations may be incurred. Its level is low and major aid is concentrated on a relatively narrow range of economies.

- L4 For a discussion of the relative benefits of the two sources. (9-15)
- L3 For an analysis of the differences in the two sources of help. (6-8)
- L2 For application of knowledge to the needs of developing economies. (3-5)
- L1 For knowledge of NGOs and/or aid. (1-2)

Specification Grid

	Question 1					Question 2		Question 3		Question 4		TOTAL
	(a)	(b)	(c)	(d)	(e)	(a)	(b)	(a)	(b)	(a)	(b)	
AO1 Target : 9	2	1		2		3	2	3	2	3	2	10
AO2 Target: 9	2	1				3	3	3	3	3	3	9
AO3 Target: 13-14			2	2	2	4	3	4	3	4	3	13
AO4 Target: 13-14			2		4		7		7		7	13
												45

Subject Content Reference	56.1	56.1	56.2	56.4	56.2	56.3	56.1	56.4	56.5	56.2	56.5
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Quality of Written Communication embedded in Section B mark scheme: see general introduction to mark scheme.

Mark Scheme 2887
June 2005

Section A

1 How well is the UK doing?

- (a) Define what is meant by the current account of the balance of payments. [2]

The current account is a statement of the value of exports minus the value of imports for both goods and services.

- 1 mark for value of exports and imports,
- 1 additional mark for reference to both goods and services
- 1 mark for investment/income
- 1 mark for current/transfers
- 1 mark for record of transactions between UK and rest of the world.

- (b) With reference to Table 1:

- compare the UK's balance of trade in goods with its current account balance; [2]
- explain the reason for this difference. [2]

- (i) Britain is in deficit on both accounts (1 mark) and the deficit is worse for the trade balance (1 mark). Negative (1).
- (ii) Service sector income is in surplus (1). Indicative of our relative disadvantage in the trade of goods (1). Indicative of our relative advantage in trade in services. Investment income in surplus (1). Current transfers in surplus (1).

Up to 2 marks for recognition of differences between current account and trade balance.

Up to 2 marks for comment on UK

- (c) (i) What relationship would an economist expect between the rate of unemployment and the balance of trade in goods? [2]

It could be argued that unemployment decreases total domestic demand and hence the demand for imports falls (1). This will lead to an improvement in the balance of trade in goods. Rise in U leads to improvement in B of T – a positive relationship (1). Alternatively others may argue that a rise in exports and hence improvement in the balance of trade will cause an increase in total domestic demand and hence a fall in unemployment (1). Thus improvement in B o T and fall in U – a negative relationship (1). Accept any logical answer – only one side expected. 1 mark for stating relationship (positive/negative). 1 mark for elaboration.

- (ii) To what extent does the data in Table 1 for the UK and Japan support this expected relationship? [2]

The data shows UK has a deficit and unemployment of 4.8% whilst Japan has surplus and U of 5.2%. Thus U is roughly the same but for one country there is a deficit and for the other a surplus. This does not appear to give support for any relationship U and BoT. If pushed could argue that lower U seems to cause a deficit on BoT (a negative relationship but expect an evaluative comment that this is not a convincing conclusion).

1 mark for comment on data. Both unemployment and B of T data to be mentioned. Extra mark needs to refer to the data. Not enough to say it does or doesn't support the relationship.

1 mark for explanation of the data.

Up to 2 marks for evaluative comment on whether the data supports the expected relationship identified in part (i).

(d) Table 2 indicates that the pound sterling appreciated against the US dollar between 14 January 2003 and 14 January 2004.

(i) Explain two possible causes of this change in the value of the pound sterling. [4]

Possible reasons include:

- *a trading surplus/increase in trading surplus in goods and services on trade with US*
- *a reduction in the trading deficit with the USA*
- *a weak dollar caused by the US's massive B of P deficit with the rest of the world eg due to armed forces commitments*
- *net inflow of funds in to the UK from the USA*
- *Increase in demand for £*
- *Decrease in supply*
- *Relative increase in interest rates*
- *Decrease in relative inflation*
- *Speculative flows*

1 mark for identification (x 2)

1 mark for elaboration (x 2)

Reference to USA/dollar needed or relative values – must link to USA context.

(ii) Discuss whether a continued appreciation of the value of the pound sterling against the US dollar would improve or worsen the UK's current account balance. [6]

A continued appreciation of the pound against the dollar would mean that exports become more expensive and imports less expensive. Evaluative comments may be along the lines - if the Marshall-Lerner conditions hold this would cause a worsening of the balance of payments on current account but if it doesn't then it won't. Alternatively it could be argued that the BoP could worsen unless there is lower inflation in the UK or UK's competitiveness improved for some other reason.

L2 For evaluative comment 3-6

L1 For analysis explaining effect of continued appreciation 1-2

Development of M-L involves questioning whether it will hold to be top L2.

Section B
Answer one question

2 (a) Explain the possible causes of a rise in the rate of inflation. [10]

There are a number of different approaches to this question and candidates should refer to any one from the following: Keynesian demand-pull, monetarist or cost-push explanations. Well-labelled diagrams or other tools of analysis (e.g. an equation such as that used to explain the Quantity Theory of Money $MV=PT$) should be used to explain a cause of the rise in the rate of inflation.

- L3 For an explanation of possible causes of a rise in the rate of inflation. Max 8 if only one cause explained. 7-10
- L2 For application of appropriate theory relevant to a rise in the rate of inflation. 4-6
- L1 For knowledge of a possible cause of inflation. 1-3

(b) Discuss whether control of the rate of inflation should be the most important macroeconomic policy aim of the UK government. [15]

Candidates should identify the main macroeconomic policy aims of the UK government. The discussion should be set in the context of the current macroeconomic climate in the UK. It could be argued that control of inflation makes it easier to achieve the other macroeconomic policy targets. This should be supported by reference to relevant macroeconomic theory. Too high an interest rate (the main policy weapon to reduce inflation) might, however, cause problems and make it more difficult for the UK to achieve its macroeconomic policy aims.

- L4 For a discussion of the current state of the UK economy which questions whether control of inflation should currently be the key macroeconomic policy aim. 9-15
- L3 For analysis that supports the discussion of whether the rate of inflation should be controlled. 6-8
- L2 For application of knowledge of macroeconomic policy aims and or attempts to control the rate of inflation. 3-5
- L1 For knowledge of the macroeconomic policy aims or knowledge of the current state of the economy without applying one to the other. 1-2

3 (a) Explain the reasons why the level of investment in an economy might rise.

[10]

There are a number of potential factors that might affect the level of Investment in an economy, these might include interest rates, expectations about the future of the economy, the MEI and so on. A rise in investment might be caused by a reduction in interest rates (but this is dependent on the slope of the MEI curve), on improved outlook for future prosperity and on government policy such as taxation on both corporate profits and on incomes which influence future demand.

- L3 For an explanation of the rise in the level of investment. Max 8 if only one cause explained. 7-10
- L2 For application as to why the level of investment in an economy might rise. 4-6
- L1 For knowledge of the determinants of investment. 1-3

(b) Discuss whether an increase in investment will always lead to an improvement in the performance of the UK economy.

[15]

Economic performance can be judged by a number of factors: unemployment, inflation, balance of payments and economic growth. An increase in I will shift the AD curve to the right as it is an increase in injections, this will have large effect on Y and hence unemployment especially if the AS curve is horizontal but a small effect as the vertical section is approached. The impact on inflation will be the opposite. The candidates should also discuss the impact on the balance of payments via more imports (and possibly less exports due to increase inflation). The effect on long-run growth will also depend on the possible effect on the AS curve which may shift right as the PPF curve moves out causing long-term growth whilst reducing the inflationary impact.

- L4 For discussion with relevant evaluation of the impact on a wide range of factors that are used to judge economic performance. 9-15
- L3 For analysis that supports the effect of an increase in investment. 6-8
- L2 For application of knowledge of increased investment to the various components of economic performance. 3-5
- L1 For knowledge of the effect of increase in investment. 1-2

- 4 (a) **Using a diagram, explain how a reduction in the rate of income tax could affect aggregate supply in an economy.** [10]

A reduction in income tax rates may affect the incentive to work and thus affect the supply of labour thereby causing a shift in the AS curve (increase or decrease). People are more willing to seek work as the after tax reward from work has increased and the opportunity costs of leisure has risen. The AS curve will shift to the right. AS curve could also shift to the left if people work less.

- L3 For an explanation of the effect of a reduction in tax rates, to include a correct diagram. 7-10
- L2 For application of the effect of reduction in tax rates on AS – through an unexplained diagram. 4-6
- L1 For knowledge of how a reduction in the rate of income tax could affect aggregate supply. 1-3

- (b) **Discuss whether a reduction in the rate of UK income tax is likely to improve or worsen the performance of the UK economy.** [15]

Economic performance can be judged by a number of factors: unemployment, inflation, balance of payments and economic growth. Candidates are expected to recognise that a reduction in the income tax rate may cause both the AD and AS curves to shifts. The effects will depend on the slopes of both the AD and AS curves and the extent to which these curves shift which in turn depends on how close the UK economy is to full employment

- L4 For a discussion of the likely impact of tax cuts on economic performance. 9-15
- L3 For an analysis of how tax cuts affect impact on economic performance. 6-8
- L2 For application of how tax cuts affect economic performance. 3-5
- L1 For knowledge of the effect of cut in tax rates or on the factors that are used to judge economic performance. 1-2

	Question 1						Question 2		Question 3		Question 4		TOTAL
	(a)	(b)	(c)(i)	(c)(ii)	(d)(i)	(d)(ii)	(a)	(b)	(a)	(b)	(a)	(b)	
AO1 Target 9	2				2		3	2	3	2	3	2	9
AO2 Target 9		4					3	3	3	3	3	3	10
AO3 Target 13-14			2		2	2	4	3	4	3	4	3	13
AO4 Target 13-14				2		4		7		7		7	13
													45

Subject Content Reference	5.7.2	5.7.2	5.7.3	5.7.2 5.7.5	5.7.2 5.7.5		5.7.1 5.7.3 5.7.4	5.7.3 5.7.5	5.7.2 5.7.3 5.7.4, 5.7.5	
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Quality of Written Communication embedded in Section B mark scheme: see general introduction to mark scheme.

Mark Scheme 2888
June 2005

- 1 Using Extract 1, compare the taxation of tobacco products in the UK with that in Spain and Ireland. [6]**

Synoptic knowledge

Section 5.2.3 Making choices and the impact of government intervention on market outcomes and economic efficiency.

The way governments intervene in markets through taxation.

The general principle in marking responses should be to award 1 mark for an overall comparison of each indicator + up to 2 further marks for valid quantifications.

UK duty per pack of 20 is

- *higher than in Spain and Ireland (accept 'highest') 1 mark*
- *40% higher than in Ireland (1)*
- *over 4 times higher than in Spain (1)*

UK revenue from excise duty on manufactured tobacco is

- *higher than in Spain and Ireland (accept 'highest') 1 mark*
- *40% higher than in Spain (1)*
- *or over 6 times higher than in Ireland (1)*

UK revenue from excise duty as a percentage of GDP is

- *lower than in Spain and Ireland (accept 'lowest') 1 mark*
- *30% lower than in Spain (1)*
- *more than 50% lower than in Ireland (1)*

Where candidates compare taxation between UK and only one of Spain and Ireland (eg between UK and Spain or UK and Ireland) marks can only be awarded where quantified comparisons are given. Effectively this caps such responses to a maximum of 3 marks.

(b) Analyse why governments tax tobacco products.

[9]

Synoptic knowledge

Section 5.2.1 - Economic efficiency within competitive markets

The conditions for the efficient allocation of resources including the concepts of allocative and productive efficiency.

Section 5.2.2 - Why markets may not work efficiently

The causes and consequences of why markets may not work efficiently. The market failure of negative externalities.

Section 5.2.3 - Making choices and the impact of government intervention on market outcomes and economic efficiency

The way governments intervene in markets to correct market failure through taxation. The impact of this intervention on markets.

Section 5.1.2 - Competitive markets and how they work

Demand. Supply. Price elasticity of demand. Market equilibrium.

Outline of content

This question can be approached in two ways, as signalled in the introduction: as a way of raising revenue; as a means of correcting market failure. Either approach is acceptable and can gain full marks. Differentiation should be in terms of the quality of economic analysis of the reasons. In the case of the revenue raising objective there must be reference to PED for Level 3 marks to be awarded. In the case of correcting market failure, explicit use of terms such as social and private costs is expected, the consequent market failure and the way in which taxation corrects this failure. Diagrams will inevitably assist candidates in adopting an analytical approach.

Level 3

For an analysis of why governments tax tobacco products.

[7 – 9]

At this level it is expected that candidates will analyse the nature of the market failure(s) caused by tobacco consumption and show how taxation of tobacco products corrects the market failure.

Alternatively, the inelastic nature of the demand for tobacco products will be analysed and the link between inelastic demand and revenue from tobacco taxation made explicit.

Level 2

For an application of knowledge and understanding of why governments tax tobacco products.

[4 – 6]

At this level it is likely that candidates will understand a range of reasons why governments tax tobacco products (eg externalities, demerit goods etc) and make use of economic terminology. The link to why taxation corrects such market failures, however, will not be made explicit.

Level 1

For a description of why governments tax tobacco products.

[1 – 3]

At this level general descriptive statements can be expected. So candidates will recognise that governments want to reduce smoking, that smoking is linked to illness or that there is a concern about the effects of passive smoking. Explicit use of economic terminology, however, will not feature in responses at this level.

- 2 **Comment on the likely effectiveness of government regulation, such as Ireland's ban on smoking in work places, to correct market failure associated with negative externalities (Extract 2).** [10]

Synoptic knowledge

Section 5.2.1 - Economic efficiency within competitive markets.

The conditions for the efficient allocation of resources including the concepts of allocative and productive efficiency.

Section 5.2.2 - Why markets may not work efficiently.

The market failure of externalities.

Section 5.2.3 - Making choices and the impact of government intervention on market outcomes and economic efficiency.

The way governments intervene in markets through regulation. The impact of this form of intervention. The ways in which governments might create rather than remove distortions.

Outline of content

*This question seeks an understanding of the advantages and disadvantages of regulation as a method of reducing negative externalities. The focus need not be on bans, given the references to other forms of government regulations in both the Introduction and the Extracts. Whatever form of regulation candidates choose, however, the analysis and commentary must be in terms of correcting market failure associated with negative externalities. The effectiveness of government regulation should be analysed using the economist's toolkit of concepts (especially those related to economic efficiency). Reference could be made to: the force of law; issues of enforcement and fines; extent of negative externalities; revenue issues; government failure. Commentary could be in terms of **relative** effectiveness (ie compared to market based solutions). A reasoned judgement is required for the highest marks in L4.*

Level 4

For a commentary on the likely effectiveness of government regulations to correct the market failure associated with negative externalities. [8 – 10]

To get into this level candidates should recognise the reasons why government regulation is likely to be effective and the factors which limit its effectiveness. A commentary which examines the costs of regulation in terms of its impact on the leisure sector should be credited in this level. For example, it could be argued that regulation may well deliver benefits in terms of reduced negative externalities but at the cost of lost revenue and jobs ie a cost benefit approach.

Level 3

For an analysis of the likely effectiveness of government regulations to correct the market failure associated with negative externalities. [5 – 7]

At this level it is expected that issues related to effectiveness of government regulation will be approached using economic concepts. The responses in this level will be one-sided, however.

Level 2

For an application of knowledge and understanding of the likely effectiveness of government regulations to correct the market failure associated with negative externalities. [3 – 4]

Typical responses in this level will lack fully developed conceptual underpinning and / or look at the effects of regulation rather the effectiveness. Alternatively, concepts will be recognised but not explained or developed.

Level 1

For a description/knowledge of the likely effectiveness of government regulations to correct the market failure associated with negative externalities. [1 – 2]

This level should be awarded to responses are likely to be expressed in very general terms, with no explicit economics.

- 3 The European Commission (EC) has proposed ending the subsidy on growing tobacco in the EU (Extract 3).
Comment on the likely microeconomic and macroeconomic effects if this proposal were to be implemented. [15]**

Synoptic knowledge

Section 5.1.1 - Managing scarce resources – the reasons for choice and its impact

Concept of opportunity cost

Section 5.1.2 - Competitive markets and how they work

Demand. Supply. Market equilibrium.

Section 5.1.3 - Firms and how they operate

Revenue of firms.

Section 5.2.1 - Economic efficiency within competitive markets

Allocative and productive efficiency.

Section 5.2.2 - Why markets may not work efficiently

Causes and consequences of market failure. Unequal distribution of income and wealth.

Section 5.2.3 - Making choices and the impact of government intervention on market outcomes and economic efficiency

The way governments intervene in markets through subsidies. The impact of this form of intervention. The ways in which governments might create rather than remove distortions.

Section 5.3.1 - Government macro-economic policy objectives and indicators of national economic performance

The meaning of GDP.

Section 5.3.2 - Aggregate demand and aggregate supply: the determinants of output, employment and prices

An awareness of the multiplier process.

Section 5.3.4 - Structure and essential determinants of international transactions

Nature and benefits of trade. Free trade and protectionism. Reasons for, and methods and consequences of, protectionism.

Outline of content

This question allows candidates to employ both micro and macro-economic concepts. Analysis of effects should be at the market level, using demand and supply; at the firm level, with reference to revenue, profit, size of farms, and at the macro level, through a consideration of regional multiplier effects (poorest regions of the EU) and the impact on trade. Efficiency gains could be explored. Opportunity cost of subsidies – alternative uses of money (anti-smoking campaigns / health interventions). Accept analysis based upon standard subsidy diagram ie removal of subsidy will raise prices and reduce production. Technically, the price of raw tobacco is determined by the world price which is unaffected by the EU subsidy. Removal of this subsidy, therefore, will not affect the market price in the EU ie the tobacco regime operates as a 'deficiency payments' system.

Commentary could be in terms of alternatives to subsidy of tobacco – other crops, direct income payments, rural development programmes. Nature and size of effects. Relative importance of each effect. Reduced government failure – joined up policy.

Level 4

For a commentary on the likely microeconomic and macroeconomic effects if this proposal were to be implemented. [10 – 15]

At this level candidates will make explicit judgements on the effects they have identified.

Level 3

For an analysis of the likely microeconomic and macroeconomic effects if this proposal were to be implemented. [5 – 9]

At this level, candidates will use the economist's toolkit of concepts, theories and techniques to explain the effects identified.

Level 2

For an application of knowledge and understanding of the likely microeconomic and macroeconomic effects if this proposal were to be implemented. [3 – 4]

Effects will be understood but underlying concepts will not be developed beyond a statement of an implicit recognition.

Level 1

For a description/knowledge of the likely microeconomic and macroeconomic effects if this proposal were to be implemented. [1 – 2]

At this level responses will be very general. Some responses at this level will do little beyond a description or knowledge of the mechanics of subsidies.

Responses which consider only the microeconomic or macroeconomic effects of subsidy removal should be limited to a maximum mark in the middle of the relevant level. For example, an analysis of the microeconomic effects only is limited to a maximum mark of 7.

4 Discuss the case for greater tax harmonisation in the EU (extracts 4, 5 and 6). [20]

Synoptic knowledge

Section 5.1.3 - Firms and how they operate

Costs. Revenue.

Section 5.2.1 - Economic efficiency within competitive markets

Allocative and productive efficiency.

Section 5.2.3 - Making choices and the impact of government intervention on market outcomes and economic efficiency

The way governments intervene in markets through taxation. The impact of this form of intervention. The ways in which governments might create rather than remove distortions.

Section 5.3.1 - Government macro-economic policy objectives and indicators of national economic performance

Meaning of GDP, employment/unemployment, balance of payments, growth.

Section 5.3.2 - Aggregate demand and aggregate supply: the determinants of output, employment and prices

Constituents of, and influences on, AD and AS. How AD/AS analysis can be used to illustrate macroeconomic problems and issues.

Section 5.3.3 - The application of macroeconomic policy instruments

The nature and impact of fiscal policy.

Section 5.3.4 - Structure and essential determinants of international transactions

The pattern of trade.

Section 5.8.1 - The 'New Europe'

A perspective on integration over the past 10 years or so. The meaning and nature of integration. Forms of integration (nature of economic unions) and the barriers to the free movement of goods, services and factors of production.

Section 5.8.2 - The SEM and EMU

The SEM – removal of non-tariff barriers. Distinction between an economic and monetary union. Macroeconomic policy implications of a monetary union. Future prospects.

Outline of content

Largely requiring a macroeconomic analytical framework, although some scope for microeconomic analysis in terms of firm location decisions and mobility of goods and labour. Case for in terms of efficient operation of EU's SEM. Avoidance of problems of tax competition (investment decisions, tax avoidance, costs of compliance with different regimes). Discussion could be in terms of questioning extent and significance of problems. Loss of fiscal sovereignty. Importance of tax harmonisation in eurozone. Case of Ireland (convergence with EU, in part due to success in attracting FDI. Other factors in location decisions – productivity and unit labour costs).

Level 4

For a commentary on the case for greater tax harmonisation in the EU. [12 – 20]
At this level candidates will recognise that there are two sides to the argument over tax harmonisation in the EU. An approach which recognises the pros and cons of tax harmonisation, therefore, should be placed in this level. The extent of the explanation and development of the two sides should be used to determine the mark in this level. Responses which do not then go on to consider the significance of the arguments for and against tax harmonisation should be limited to a maximum mark of 16. For the very highest marks in this level (>18) an evaluative conclusion is expected.

Level 3

For an analysis of the case for greater tax harmonisation in the EU. [5 – 11]
Responses in this level will not recognise problems, limitations of the case for or the arguments against it. They will, however, make explicit use of economic concepts to explain the case for.

Level 2

For an application of knowledge and understanding of the case for greater tax harmonisation in the EU. [3 – 4]
Candidates in this level will have a broad awareness of the reasons why tax harmonisation is thought to be a benefit in the EU. The nature of responses will signal an implicit recognition of economic concepts, but this will not be developed towards an analysis of the issues.

Level 1

For a description/knowledge of the case for greater tax harmonisation in the EU. [1 – 2]
Candidates at this level will produce answers which owe more to general knowledge than to economics.

Specification Grid

Assessment objectives	Question 1		Question 2	Question 3	Question 4	TOTAL
	(a)	(b)				
AO1	3	3	2	2	2	12
AO2	3	3	2	2	2	12
AO3		3	3	5	7	18
AO4			3	6	9	18
TOTAL	6	9	10	15	20	60

Report on the Units

June 2005

Chief Examiner's Report

General Comments

This report contains comments from Principal Examiners on the performance of candidates in the June 2005 examinations.

Below please find some general comments covering wider issues for the delivery and assessment of the specification as a whole.

Candidate entries for the specification are growing at a steady rate, particularly at AS level. At A2, units 2884 and 2885 continue to attract a good number of re-sit candidates at this sitting.

In general, the Principal Examiners are very positive about candidate performance as their individual reports indicate. Teachers should be congratulated on this outcome.

The following points are intended to be constructive and should be noted for future examinations.

- i) In unit 2886 especially, but in other A2 optional units to a lesser extent, Principal Examiners have noted an increasing tendency for some candidates to reproduce rote learned material as their answer to structured essay questions. This is unlikely to gain many marks. Candidates should be reminded (as you always do!) that it is important to write to the point or focus of the question at all times.
- ii) On similar lines, again as previous reports have stressed, the directive words are there for a specific purpose, namely to direct candidates as to the skill level that is being examined in a particular question. In the AS examinations for instance, the 'comment' directive word was not well understood or appreciated by many candidates in their answer to part (c) (ii) on 2881 and part (e) on 2883. All that was required here was a sentence or two of reasoned opinion on the point of the question. On the A2 optional units, 'discuss' is rather different, inviting candidates to give relevant arguments for and against the point of the question. This is essential for the award of a level 4 mark.
- iii) A small number of candidates continue to confuse micro and macro terms which are similar. The most common of these is the misuse of demand and supply (micro) as against aggregate demand and aggregate supply (macro).
- iv) Could I please ask you to respectfully bear in mind the following administrative points and bring them to the attention of candidates in future examinations;
 - For A2 optional modules, to put the choice of questions answered on the front page of the answer booklet.
 - When using loose sheets, to number these and attach them to the answer booklet with a treasury tag.

The Market System (Written Examination) (2881)

General Comments

This was the fifth sitting of the unit as a one hour examination with a structured examination answer booklet. It was taken by around 5800 candidates, a slight increase on June 2004.

On the surface, this seemed a straightforward question paper. Although there were no questions on section 1, all topics were clearly within the scope of the specification and in part (f), the style of question and approach was consistent with that used on some previous question papers. For many candidates though the paper was by no means as straightforward as it might have appeared to teachers. This was probably due to the specific combination of topics rather than to any of the questions being above the scope of AS. Consequently, unlike previous examinations, smaller numbers of candidates recorded marks of 36 and above. At the bottom end, there were rather more scripts from candidates who were obviously not sufficiently well prepared.

The content of the case study was a loose adaptation of an article that appeared in the food section of the Daily Telegraph. It was an accessible topic, with no evidence that any particular group of candidates were disadvantaged in any way. The content was easily comprehended and there were no problems of timing evidenced in the examination scripts. Candidates seem to have adapted well to the answer booklet.

Parts (a) and (b) should have provided most candidates with 12 marks. This was so in many but by no means all cases. Thereafter, for parts (c), (d) and (e), answers were extremely variable with no real pattern emerging either within or between Centres which was unusual.

As in previous examinations, but to a rather lesser extent this time, candidates scoring the highest marks normally got a good mark on (f)(i) and a level 4 mark on (f)(ii). There were though candidates who struggled somewhere in parts (c) to (e) but then did well on both aspects of part (f). All in all, the outcome was that rather more scripts than usual were assessed as being in the range 28-35 marks.

Comments on Individual Questions

- (a) This was a simple opening question, as asked on an earlier question paper. Most candidates as expected got four marks. Many though over elaborated, believing the question to be more difficult than was the case. For example, demand and supply curves were unnecessarily shifted and a written explanation provided. Both were not required. A surprising number of candidates only put a demand curve on their diagrams; others got the supply and demand curves the wrong way round or did not label axes correctly.
- (b) (i) Another well answered question. Most diagrams were well drawn, with a shift to the right of the demand curve and a correct explanation of the outcome. In some cases, diagrams did not show the supply curve. This resulted in meaningless old and new equilibria. Such answers usually gained one mark for the shift of demand and a further mark for explanation. In a small number of cases, the new equilibrium position was wrongly indicated. Very few candidates failed to show the shift of demand.

- (ii) Although the skill requirement was identical to that in (b)(i), this question was not as well answered. A common error was to shift supply to the right and not to the left or to not show any shift at all on the diagram. In some cases, the demand curve was excluded, so making the two equilibrium positions wrong. Only a handful of candidates shifted demand rather than supply or saw the change being of a movement along supply.
- (c) (i) This was where some candidates started to become unstuck! A very common error was to explain price and not income elasticity of demand. Where income elasticity was understood or seemingly understood, candidates sometimes struggled to explain what +1.5 meant. Two marks could be obtained very easily for saying take-away food in Bradford was a normal (or superior) good and that the estimate indicated that income elasticity was elastic. Some candidates wrote answers that were too long, spending time laboriously explaining what was meant by income elasticity of demand rather than what was explicitly meant by the estimate of +1.5.

(ii) This part was not well answered. Few candidates gained full marks. Even where income elasticity was understood, there were few answers that indicated how a business might be able to use the data provided, particularly from a longer term standpoint. Another equally acceptable comment was to question the accuracy of the data that had been collected in arriving at the estimate. A further problem was that in some answers, material included in (c)(i) was repeated in this answer. Where this was identical (e.g. an increase in income leads to an increase in demand for take-aways), marks were only awarded once.
- (d) (i) Over the years, questions on economies of scale have not been particularly well answered. Yet again this was the case. Few candidates were able to give a correct definition that referred to falling average/unit costs as the scale of a business increases. Where understanding was limited, candidates often obtained a mark for falling average costs but struggled to understand what an increase in the scale of operation actually meant. There was, therefore, a disappointing lack of basic knowledge here.

(ii) To some extent, the errors referred to in (d)(i) re-surfaced here in many answers. In some cases, candidates who had answered the previous part correctly fell down on this part by providing explanations that did not incorporate the scale aspect specifically. Most candidates were able to quote a type of scale economy although this was often not well explained. In some cases, the explanation did not match the identification. A few candidates confused marketing economies, purchasing economies and bulk buying. To sum up, far too many answers to this question were written in vague applied terms. There is a need, therefore, for teachers to stress that a knowledge of economics must be incorporated into applied material for a good mark.

- (e) This was another question where candidate knowledge was weak and where many answers lacked economic terminology. The point behind it was for candidates to explain two alternative objectives to that of profit maximisation. Arguably, the wording of the question could have been clearer: 'Explain two alternative objectives for the owners of take-away food shops'. Many candidates interpreted the question in this way and usually gained good marks. Typical responses were that of satisfying (as implied by the information provided), sales maximisation or revenue maximisation. A few very good answers referred to the practical difficulties of actually identifying the profit maximisation point in a small business.
- (f) (i) This question was reasonably well answered although not all candidates who gave a correct characteristic of monopolistic competition were able to explain it. A common error was for candidates to give two of the characteristics of monopoly rather than monopolistic competition. Where this occurred, their answer to (f)(ii) was also invariably wrong.
- (ii) This style of question has been asked on previous question papers. Consequently, many candidates seemed well prepared as to how to produce a good answer that contained relevant discussion for a level four mark. The best answers usually contained mature economic analysis applied to the information provided. Four main types of answer were forthcoming. These were:
- Answers where candidates wrote entirely about monopoly and not monopolistic competition. If the answer consistently stated that the market structure was 'monopoly', then this had to receive no marks. If it said the market structure was 'not monopoly' then a mark of up to four was awarded.
 - Answers where the information provided was applied to some of the characteristics of monopolistic competition and where the conclusion was that this was a monopolistically competitive market. These answers usually got four marks.
 - Answers which provided application as above but then discussed the extent of barriers to entry in the form of hygiene certificates for a business and its employees. These answers were usually assessed at the lower end of the level 4 range.
 - The best answers considered other characteristics of monopolistic competition as well as few barriers to entry. Whether firms were price makers or price takers or whether they maximised profits, for example, were discussed. Some candidates wrote about whether the market structure might even display some of the characteristics of perfect competition, disputing the nature of barriers to entry and product differentiation. Such answers, therefore, provided clear evidence of the evaluation skill that has to be demonstrated for a very good mark.

2882: Market Failure and Government Intervention

General Comments

The overall standard of the performance was very pleasing with many outstanding scripts being a delight to mark. Out of the 7600 candidates sitting the paper, few received marks in single figures whilst many candidates excelled, clearly having a rigorous understanding of negative externalities and market failure.

Whilst it is extremely pleasing to see candidates performing well, lessons can still be learnt in terms of examination technique as many candidates continue to throw marks away needlessly because they have not read and understood the question clearly.

Comments on Individual Questions

(a)

- (i) This question was well answered with many candidates clearly well versed in a definition of negative externalities in terms of social costs exceeding private costs. A minority of candidates provided only simple definitions, but illustrated these with relevant examples, such as passive smoking. Where this approach was taken then both marks could still be gained.
- (ii) Despite good answers to a(i), many candidates only received one mark here for identifying an example without any relevant explanation. Candidates would be well advised to apply their economics more clearly; for example, by explaining how the negative externality would lead to social costs exceeding private costs or how it would represent a third party effect. With three marks available for such a question, the use of economic terms and concepts is clearly vital in order to gain full marks. Surprisingly, only a minority of candidates managed to achieve this.
- (iii) Once again, many answers failed to apply relevant economics in explaining why the stated examples are positive externalities.

(b)

The answers to this question were very pleasing with many candidates gaining all six marks for clear, concise definitions of the types of efficiency. Common mistakes were to confuse productive and allocative efficiency and also to define Pareto efficiency incorrectly as the situation where it is possible to make one person better off without making others worse off. Unfortunately, such a response gained no marks as it was in fact defining a situation of Pareto inefficiency. Nevertheless, it was very satisfying to see so many good answers with candidates clearly being taught clear, concise definitions and learning them well.

- (c) Whilst it is not unusual to see a ten mark diagram question on the paper, this question deviated from the norm in that it required candidates to analyse how negative externalities would lead to market failure. This proved to be a good discriminator, with many very good diagrams gaining the maximum six marks but fewer candidates being able to explain how the existence of such externalities would lead to market failure.

The best answers focused upon the price charged in the free market being too low and the resulting overproduction leading to allocative inefficiency and a misallocation of resources. Unfortunately, such answers were few and far between with too many candidates trying to analyse how such negative externalities could be solved through government intervention. Such answers gained no credit on this question.

Yet again candidates are well advised to focus upon answering the question which has been set and not to try re-writing the question to suit their knowledge. Not only does this waste valuable time but also candidates invariably gain no credit for their efforts.

- (d) (i) On the whole this question was well answered with many candidates able to identify the increased cost to the government of subsidies and some developing this further in terms of opportunity cost issues. Relevant benefits such as lower house prices and increased custom for builders were frequently identified. Unfortunately, in a few cases, more able candidates seemed to struggle, trying to develop over elaborate answers, whilst missing the basic costs/benefits to the government of introducing subsidies.
- (ii) The responses to this question were a little disappointing with many answers confusing the issue of subsidies with that of compensation being paid to homeowners. Most importantly, the key instruction word 'comment' was often ignored, at significant cost to the candidate. Where such a word appears it is very important that answers provide a reasonable opinion of the particular situation.

Better answers provided simple analysis of the possible gains from subsidies in terms of lower costs of production and price cuts and then moved on to relevant comment/evaluation. Some excellent responses included the possibilities of firms not passing on the full value of subsidy to consumers and also the difficulties posed by inelastic demand or supply. Candidates would be advised to focus in more detail on the limitations of different forms of government intervention.

If one lesson can be learnt from this examination, it would clearly be the need to respond appropriately to the directive words in the question; in this case to put forward relevant arguments.

- (e) On the whole this question was well answered which is perhaps not surprising given the number of times it has appeared on past question papers.

That said, similar problems continue to arise in applying CBA. First of all, candidates continue to confuse the terms external and social cost which are clearly not the same. Secondly, many fail to see the use of CBA and do not fully understand how it helps with the decision-making process. Candidates should understand simple analysis in terms of proceeding with projects only where the social benefit exceeds the social cost.

Nevertheless, many excellent answers gained full marks for introducing several points of very mature evaluation, beyond the basic problem of placing monetary values on external costs and benefits. Such answers referred to the problems of looking into the future, the issue of what costs and benefits to include, the cost of such an investigation and also the possibility of political interference with governments overruling results of CBA in order to go ahead with projects that they want. Indeed, it was a pleasure to read many outstanding answers to this question from candidates who were clearly well prepared.

2883: The National and International Economy

General Comments

This paper elicited a range of performance from excellent to weak. The strong candidates answered the questions set, made good use of macroeconomic analysis and made an evaluation in their answers to questions (d)(ii) and (e). As in previous sessions, time did not appear to be a factor and most candidates attempted all the questions.

Generally, however, candidates appeared to find this a challenging paper. There was some evidence that candidates were not devoting enough attention to the words in the questions, particularly the directive words.

A significant number of candidates, with perhaps a less clear understanding of macro issues, relied on a micro approach to answer questions (c)(ii), (c)(iii) and (e).

A smaller proportion of candidates gained high marks on the last question than in the previous sessions. This was largely due to a failure to address the question directly and a failure to evaluate.

Comments on Individual Questions

- (a) (i) This was generally well answered.
- (ii) This was reasonably well answered, but a number of candidates seemed somewhat confused between injections and leakages and gave saving, taxation and imports as examples of injections.
- (b) (i) Most candidates understood how to work out the value of imported goods but it was disappointing to see so many numerical mistakes with candidates concluding that £186bn + £34bn is, for instance, £120bn, £200bn or £202bn.
- (ii) There were a number of good answers to this question. The most popular benefits identified were a lower price and increased choice. Better candidates explained how benefits arise from international trade. Some candidates, however, made no reference to how UK consumers would benefit and a few only considered one way. A disappointing number of candidates concentrated on the benefits of a high exchange rate rather than on the benefits arising from trading products internationally.
- (c) (i) This question elicited a mixed response. Some candidates defined equilibrium in micro terms and others as a balanced budget or as a trade balance. A few appeared to have no understanding of the concept of equilibrium.
- (ii) This question discriminated well. Good answers identified a possible cause and then explained how it could increase aggregate supply. A disappointing number of candidates explained factors that would cause a movement along the aggregate supply curve by means of increases in aggregate demand. Others, again, adopted a micro approach and explained factors that could lead to an increase in the supply of one firm or one industry.

- (iii) Some excellent answers were given to this question and, indeed, it was the best answered question with a significant number of candidates showing a well developed ability to analyse appropriate policy measures. A number of candidates, however, answered in micro terms and some analysed policy measures designed to increase aggregate supply. There was some evidence of candidates confusing fiscal and monetary policies. A few of the better candidates evaluated, at some length, the policy measures although this was not required.
- (d) (i) A number of candidates stated that the UK Claimant Count measures everyone receiving state benefits, without indicating that it is based on those receiving unemployment related benefits. A few candidates appeared to be completely unaware of the Claimant Count.
- (ii) Most candidates did not pick up on the word 'comment'. They identified two difficulties but failed to comment on how these difficulties affect the unemployment figures.
- (e) A disappointing number of candidates struggled with this question. Some of the logic offered was simplistic; for instance: 'Inflation causes prices to rise, so people cannot afford to buy goods and services, so aggregate demand falls and the country moves into recession.' Indeed, in many answers, candidates made assertions, e.g. inflation causes unemployment/rise in the exchange rate/fall in the exchange rate without explaining why. They then went on to discuss the consequences of rising unemployment/change in the exchange rate. Others devoted their attention to assessing the effects on policy measures without linking them to the consequences of inflation and some gave detailed explanations of the causes of inflation; again, without explaining how these may affect the consequences. Indeed, many candidates seemed to be answering a different question. Even in the case of those candidates who did answer the question directly, a significant number failed to evaluate.

Recommendations

The main recommendations arising from this examination for future candidates are to:

- Read and follow the directive words carefully
- Pay particular attention to all the words in the questions
- Use macroeconomics and not microeconomics analysis
- Answer the specific question set
- Evaluate, where appropriate, as directed by the 'comment' directive words.

2884: Economics of Work and Leisure

General Comments

The total number of candidates again showed a small increase, and the generally pleasing standard of the scripts was maintained from previous sessions. Many candidates demonstrated a good grasp of relevant economic theory, as well as an impressive ability to apply it in the particular areas of the 2884 specification which the questions required. Many answers also demonstrated an encouraging awareness of recent developments in the UK labour market and in television broadcasting.

There was no evidence that candidates were unusually hampered by a time constraint, nor were there more than a handful of scripts containing a rubric infringement. The general standard of written communication was, perhaps, slightly better than in the recent past.

The data in question 1 did not seem to present any particular difficulties for candidates, and most were able to have a decent stab at most of the part-questions: though, perhaps, it was slightly more common than usual for candidates to do themselves less than full justice as a result of a failure to answer the precise question asked. In Section B, Questions 3 and 4 were both very popular, and often well answered; in each case, part (a) was on a central theme of the specification, and part (b) a clear, if challenging, application of it. However Question 2 attracted less than 1% of candidates; no doubt this reflects the fact that its topic has not featured previously on a 2884 paper.

Comments on Individual Questions

- 1(a)
- (i) A majority of answers correctly identified women with low qualifications in high unemployment areas, though a surprising number did not.
 - (ii) Less well answered: quite a few candidates failing to identify a measure as such, even though there were several mentioned in the text from which to choose.
 - (iii) Answers were generally good, with a wide range of valid possible benefits suggested.
- (b) The main problem in both parts was a failure to respond to the instruction to “explain”. Thus quite a number of candidates – though still a minority – failed to do more than identify what the article was referring to – part-time or low-paid jobs for (i) and those with poor qualifications for (ii). To “explain” requires rather more than this; and many candidates did indeed develop their answers further, most commonly by a comparison with higher-quality jobs in (i) and by reference to changing demands of employers in (ii) – though the examiners, of course, accepted any other valid further development which made clear that the phrase was fully understood

- (c) Answers to part (i) varied considerably, with the weaker ones tending to say merely that a “hidden army” represented unemployment, which is a market failure; for the full two marks, it was necessary to go further, by explaining briefly what labour market failure actually involves. Most answers to part (ii) were able to score two marks by an explanation of how the policy worked, but only a minority went much further, whereas the instruction word “comment” required this – ideally by some consideration of the wider benefits and costs of introducing the policy. Finally, part (iii) generated a wide range of answers. The weaker ones tended to offer a little more than a list of possible policies; more often, answers explained how a number of policies might work to achieve the stated objective. The best possible effectiveness of the stated policies, often via some form of cost-benefit analysis. It should also be stressed that, for a question such as this, it is not the number of different policies which a candidate identifies which matters; in this case, two relevant policies would certainly suffice. The quality of an answer would instead be judged on the quality of the consideration of their impact.
- 2 Only a handful of candidates attempted this question. Amongst them the better answers showed a good knowledge of the EU Social Charter in (a) though not all then went on to link its provisions to the supply of the labour in the UK. In (b), the crucial issue was that of labour market flexibility, and one or two answers did indeed recognise this, gaining good credit for a consideration of their interpretation of the Social Charter’s advantages and disadvantages in terms of its provisions’ implications for labour market flexibility or otherwise. The most important weakness demonstrated was to answer not in terms of the Social Charter but rather in terms of the UK’s membership of the EU in general and its implications for free movement of labour. Such answers were given credit using the “own figure” rule, when linked to the UK labour supply in (a) or labour market flexibility in (b), but of course, it was not possible to score high marks in such a case.
- 3 This was a very popular question, and many answers clearly showed that candidates had been well prepared for such a central topic, part (a) in particular. Thus, candidates often began with an explanation in terms of basic supply and demand analysis, and then went on to consider the factors underlying each separately. Weaker answers either went no further than or merely itemised a series of relevant factors – skills, trade unions, product demand, labour/capital substitutability, etc. – without putting such factors within any overall framework. Answers to (b) showed greater variation in quality. There were some excellent essays, which explained a couple of relevant policies and the rationale behind them, and then went on to evaluate them in terms of whether or not they might achieve their avowed objectives and any undesirable incidental consequences they might have. It was of course, not necessary for an answer to pick up on the “fat cat” pay theme in the prompt to the question; some did, very successfully. Quite a few candidates chose this question to produce their standard answers on the effects of introducing a minimum wage; this was not irrelevant, of course, though only the better ones of this type expressed their discussion in terms of an answer to the actual question asked. Other candidates chose to use progressive taxation as their policy focus, often with little link to the issue of wage determination itself.

- 4 Again this was very popular, and many answers to (a) in particular were of high quality. Such answers tended to begin with characteristics of oligopoly, and then to explain several main features of firms' behaviour in such a market structure. Weaker responses generally concentrated largely on characteristics, or tended to list rather than explain aspects of behaviour. Answers to (b) quite often demonstrated a very impressive ability not only to summarise the main features of the structure of the UK television broadcasting industry and of the behaviour of firms within it, but also to relate this to the explanation produced in (a). Thus discussion within good answers tended to argue that the industry demonstrates many features which approximate to that of classical oligopoly, but that there were other types of behaviour which certainly did not; for example, as a result of the state ownership and non-profit-maximising objectives of the BBC. Weaker answers were of two main types: some concentrated almost exclusively on describing the industry, with little or no reference to the economics of market structure; whereas others made points about market structure in largely theoretical terms, with minimal linkage made to the television industry in the UK.

2885: Transport Economics

General Comments

The question paper was appropriate to the candidates for whom it was intended and was of a similar standard to previous 2885 papers although part (b) of all essay questions required more thought and application than in previous examinations. Overall the standard of the performance of the candidates was good although the mean raw mark was slightly down compared to last year reflecting the above point. Scores on Section A were good although the main failing of candidates, again, was their inability to apply economic concepts in context in this case to the proposed Crossrail scheme .

Most candidates had been adequately prepared for the examination although as in previous sessions there was disparity in such preparation between centres.

There were some examples of rubric error (mainly answering all of Section B) although the vast majority of candidates divided their time usefully. Unfortunately very few candidates opted for Question 3 in Section B although those that did scored well. The majority of candidates (approximately 60%) answered Question 4 in Section B.

A good number of candidates used appropriate diagrams to support their understanding of theory although candidates should be reminded that diagrams should only be used if they add to the written answer, are incorporated in the text, and if the candidates are sure of their accuracy.

Again one significant problem for some candidates is that they do not focus on the directive word in the question. Explain frequently was interpreted as discuss, particularly in Question 2a, and in Question 1a many candidates made little attempt to explain the private costs or external benefits identified.

Comments on Individual Questions

- Q 1)** Generally well answered but there were a number of candidates who did not understand the concept of private costs. Candidates must also remember to apply their knowledge particularly in transport contexts.
- 1)**
- (a)** There were many disappointing responses to a basic AS concept applied in an A2 context. Many candidates confused private costs with external costs and therefore related to noise, the environment rather than wages, maintenance, raw materials etc. Only a very few were able to explain such costs as private costs as they were paid by those imposing them. Credit was given in both this and the next question for implicit understanding.
 - (i)**

Report on the Units taken in June 2005

- (a) This question was well answered with the majority of candidates being able to explain explicitly or implicitly the external benefits which might result from the cross-rail scheme referring to jobs gained, the regional multiplier and reduced congestion on both the underground lines or roads.
 - (ii)
 - (b) Most candidates were able to identify the need for public and private finance due to the large sum involved but many could not elaborate appropriately in terms, for example, of reducing risk and increasing efficiency,
 - (c) The majority of candidates could identify some factors that might affect future demand. However some weaker candidates concentrated on CBA or PED and as a result missed the point of the question regarding the problems of forecasting future demand. Stronger candidates discussed the significance of the project being unique and the possibility of unforeseen events influencing demand.
 - (d) This question discriminated well with the weaker candidates recycling notes on CBA. Many candidates failed to apply their answers to Crossrail or a similar project, and so were limited to 4 marks. A disappointing number also confused CBA with COBA. However there were many good answers that indicated a sound understanding of whether CBA was an appropriate tool for decision making for the Crossrail scheme with good examples of relevant costs and benefits, both private and external, and discussion of difficulties for example in assigning monetary values to externalities and the subjective nature of the assessment.
- 2)
- (a) The vast majority showed a good understanding of the main problems of monopolies in terms of price and output. The better candidates developed explanations in terms of the lack of productive and allocative efficiency in comparison to more competitive markets. Some very good answers analysed not only X inefficiency but dynamic inefficiency. The major weakness for many candidates was that diagrams were often inaccurate, incomplete or not used to help written explanations.
 - (b) The answers to this question were very varied. Most were able to explain the benefits of a deregulated market in terms of contestability supported with knowledge of its historical context. However only a minority were able construct clear evaluative arguments supported by analysis to explain the benefits and costs that re-regulation may bring. The main problem for the weaker candidates is that they did not understand that regulation is not necessarily concerned with renationalisation or subsidies.
- 3)
- (a) This was not a popular question. Of those attempting it, most were able to demonstrate an understanding of the main influences of the demand for different modes of freight transport. Good answers explained the importance of the product being transported in modal choice. The best also emphasised the importance of derived demand in influencing demand for freight transport.
 - (b) There were some very good answers where candidates gave a precise definition of sustainability, demonstrated awareness of current trends in freight transport and then made appropriate judgements relating the current trends to sustainability.

- 4) (a) A very popular question that discriminated well. On the whole it was well answered with the vast majority understanding or explaining the basis for road user charging. Stronger answers used sophisticated diagrams showing the divergence between marginal private cost and marginal social cost as a result of congestion to explain market failure and the need to internalise external costs via road user charging. Some, however, lacked focus on congestion and concentrated on road user charging being used to combat pollution.
- (b) Candidates clearly focused on the question and a substantial majority attempted to apply and/or analyse the impact of road user charging on businesses. The question discriminated well in terms of the breadth and depth of relevant economic analysis used in reaching appropriate judgements. Some candidates focused on specific businesses and others on geographical applications such as the location of industry. Where there was clear economic reasoning in reaching judgements, e.g. contrasting the benefits to businesses in terms of reduced congestion with the problems of increasing costs, candidates were able to reach Level 4. Others compared the effects on businesses within and outside a charging zone and others analysed possible macroeconomic impact on businesses.

2886: Economics of Development

General Comments

Candidates seemed to find this year's paper somewhat more challenging with fewer very high scoring scripts. There were nevertheless many signs of interest and ability shown by the candidates. The data response question contained rather more text than in some years. This seemed to affect the candidates' approach, which relied more on copying of the text than selective use. This weakened the responses. The format of the data should not alter the skills which are employed to respond. The impression continues that some candidates are hampered by their restricted essay writing techniques. In these cases they often show sound knowledge but are unable to deploy it effectively. The key seems to be the ability to provide a logical structure within which the essay can develop. Candidates would benefit from spending more time thinking about the purpose of the particular way the question is framed. Accurate knowledge of terms remains essential; this was clearly demonstrated in the case of the terms of trade and non-governmental organisations. While Economics teachers are no doubt grateful for the higher profile that Bob Geldof and Bono have given issues in development economics, candidates should be encouraged to bring a more objective approach to their analysis of problems, rather than simply quoting from press statements.

Comments on Individual Questions

- 1(a) Candidates scored well on this question. They indicated that the production possibility curve would move out and usually linked this to the increase in resources from oil exploration. Weaker answers did not explain the reason. Most answers included a diagram. An improvement in the current balance was usually anticipated, although some answers used insufficiently accurate terms, such as increase or change. Explanation usually referred to increasing exports although some references were made to reduced oil imports. Full marks were common.
- (b) This question proved difficult for candidates. An explanation of either the national/domestic distinction or the purchasing power parity element would have been sufficient. There was confusion about the impact of imports and exports, the relevance of income inequality, the relevance of the exchange rate and the position of foreign workers. The second mark required applying the distinction to developing economies rather than leaving it in principle.
- (c) High marks were generally scored through reference to production patterns, levels of GDP per head and HDI, literacy and longevity data. Full marks required that elements for and against the proposition were identified. The strongest responses clarified the relevance of the data selected. Some answers only made the comparison to the other countries in the data, therefore assuming that they must be typical. The 'typical' element of the analysis was sometimes ignored. Credit was available for the comment that there were difficulties with the concept of a typical developing economy.

- (d) This question provided few difficulties. Candidates usually concentrated on the supply of finance, capital, technology or expertise. Weaker responses tended to identify rather than explain the significance of the MNC's contribution.
- (e) The answers here disappointed. There was too much direct copying of the extracts. The significance of what had happened needed to be brought out. This could have taken the form of examining the consequences of the trend (e.g. the impact of the decline in agriculture upon the balance of trade and sustainability) or the actions which might be introduced to avoid the potential harm (e.g. the use of oil revenue to subsidise agricultural production). The decline in agriculture and the danger of growing inequality were the most commonly considered issues.
- 2 The question required an elaboration of the Lewis model of structural change and an evaluation of the nature of economic problems at different stages of development.
- (a) This was a popular question. The Lewis model was well-known, with candidates able to supply varying degrees of detail, including diagrams. The problem was that a significant number of candidates felt compelled to write a wider answer which looked at criticisms of the model. This was not required and only gained credit when it drew out assumptions which had not been previously mentioned. Weaker answers believed the model to be a far more comprehensive model of economic development than is actually the case.
- (b) There were some extremely impressive responses which recognised the inability to solve all problems and the likelihood of the nature of the problems changing. Other candidates missed the need to consider developed countries, instead writing about and quoting examples of countries which continue to be considered developing. The term 'basic economic problems' was not usually taken in its classic sense but as any type of important, economic problem. This did not prevent some credit being gained. The strongest answers were able to make reference to continuing problems in, for example, Japan and USA to support their analysis.
- 3 The question required an analysis of the significance of the terms of trade and infant industries for developing economies and an evaluation of the impact of wider free trade on their economic development.
- (a) This part did not yield high scores. As in previous examinations the terms of trade was not known in its technical sense. Candidates confused it with trade barriers, the balance of trade and general conditions of trade. Answers along these lines could score very little. Those who were familiar with the idea often wrote comprehensive answers, which recognised the declining terms of trade faced by developing countries. The error of assuming that worsening terms of trade must mean a worsening balance of trade was evident. Infant industries were better understood, although their significance as contributors to economic development was not usually stressed. The definition of an infant industry as one which employed child labour was a diversion.

- (b) There was sound awareness of the issues involved in the removal of barriers to trade. The weakness, however, was to assert the benefits or drawbacks rather than to detail them. References to comparative advantage, for example, would have underpinned the case for the removal of barriers. Some impressive answers referred to the attitudes of developed countries in thwarting progress to free trade and the experience of the newly industrialised economies in pursuing development. It was surprising that some answers did not clarify the forms that barriers to trade may take or see any links to the content of the first part of the essay.
- 4 The question required an analysis of the effect of colonisation on economic development of the colonies and an evaluation of non-governmental organisations, assistance and government foreign aid.
- (a) Few candidates were able to offer comprehensive accounts of the effects of colonisation. Most answers tended to be one-sided, with the majority seeing the effects as harmful. The style of writing tended to be journalistic. A more structured approach would have been beneficial. Few responses described the range of aspects of the economy which were shaped by colonisation, tending to stop at primary production and trade patterns. Rather a lot of attention was given to post colonisation problems, which stemmed from later developments.
- (b) There were many answers which revealed an awareness of the contrasts between the activities of NGOs and governments. These referred to, among other things, conditionality, focus and motivation. Good marks were awarded for this approach, particularly when supported by recent examples. Some significant errors were made by candidates. The inclusion of the World Bank, IMF and multinational companies within the NGO sector was not accepted, neither was the implication that aid was given on commercial terms. As might be expected the case for NGOs was often overstated but did show a clear knowledge of the scope of their activities. Candidates wrote with some enthusiasm on this topic.

2887: The UK Economy

General Comments

The examination attracted an entry of around 1600 candidates and was felt to be appropriate for all candidates studying economics at this level. Only a very small percentage of candidates failed to answer all of the questions which suggested that they were not under undue time pressure

The quality of scripts varied widely and in some cases the application and analysis of relevant economic theory was disappointing. However there were many very strong candidates who demonstrated a perceptive grasp of economic concepts and a mature ability to apply them to specific questions. These candidates tended to reflect on the case material and were well drilled in identifying the key trigger words in the questions. Their analysis usually focused around AS/AD diagrams and they were able to apply these concepts effectively in discussion.

The weaker candidates demonstrated only a limited grasp of conceptual material and little appreciation of the subtle relationships in the macro economy. They tended to use diagrams sparingly, axes were often labelled in a micro context and they usually failed to focus specifically on the question being asked.

In the middle the vast majority of good, solid candidates produced a set of sound answers and appeared to be well drilled in how to tackle certain topics and how to respond to certain trigger words. However they often lacked the mental agility to produce answers which had a spark of individual insight or the flexibility to develop their own ideas.

The data response was found to be quite challenging for some candidates and this question was often the key discriminator rather than the essays. Marks were dropped on what appeared to be the more straightforward elements and candidates failed to use the case material effectively in their answers.

In general part (a) of the essays was very well answered with a significant number of candidates achieving 10 marks. These candidates had an excellent knowledge of the subject matter and their answers were well written.

In part (b) most candidates are now familiar with the correct approach to evaluate effectively and consequently it was encouraging to see so many achieving Level 4. However, it is also evident that many candidates have had this skill taught to them and the "token gesture" evaluation is becoming increasingly the norm. This is a challenge for teachers in the future because it could be argued that a real appreciation and intuitive insight into the subject is being neglected for the sake of the model examination answer.

Comments on Individual Questions

- 1 Fewer candidates than expected achieved over 15 marks for this question and only a very small percentage achieved full marks. In some respects this is because of the rigorous way that the mark scheme was enforced on certain questions this year. It was felt that, at this level, candidates should take more care in answering the specific question, and consequently, there was less flexibility in the range of answers that were acceptable. There is also evidence of candidates being less adept at thinking on their feet when responding to data not previously seen and perhaps being more thoroughly prepared to answer certain predicted questions.
- (a) Almost all candidates were awarded full marks for this question. A common error was to focus on definitions of the balance of payments rather than the current account and to explain the meaning of deficits and surpluses.
- (b) (i) Most candidates achieved full marks by recognising that both accounts were in deficit and comparing the size of the deficit in each. Stating that the accounts were negative was acceptable. However a problem sometimes arose if they referred to the accounts as being negative because the comparison would often state that the trade balance was larger than the current account
- (ii) Most candidates realised that the reason was that the current account included the trade in services and this would achieve one of the marks. To obtain the second mark candidates needed to state that the UK has seen a growth in its service sector or has a comparative advantage in this sector, or that the UK had experienced a decline in manufacturing. Consequently, the second mark was awarded less frequently.
- (c) (i) Most candidates were able to come up with a logical relationship between unemployment and the balance of trade. Any relationship was acceptable and the second mark was awarded for the explanation.
- (ii) Most candidates used the data effectively to show that the relationship did not appear to be supported. If candidates had stated that they expected the trade balance to improve as unemployment increased they needed to state that the data supported the relationship weakly. This was because there was very little difference between the unemployment rates in the UK and Japan. A limited number of candidates compared the UK to Germany or the USA.
- (d) (i) Most candidates gave two sound reasons why the pound might appreciate but fewer linked the explanation to the USA or the dollar. It was deemed necessary to do this because in Table 2 the pound had depreciated against the Euro. Therefore, if a candidate had stated that an increase in interest rates in the UK would attract hot money and push up the value of the pound, one mark was awarded. To obtain the second mark they needed to mention that it was relative interest rates or that Americans would now invest in the UK. In many cases substitution of "Americans" for "foreigners" was all that was needed.

- (ii) Most candidates realised that a continued appreciation of the pound would lead to an increase in imports and a decrease in exports and were awarded at least two marks. The commentary required a detailed explanation of the Marshall-Lerner condition and a suggestion why the elasticity may or may not be above one. In addition, reference to the J-curve or another reason why UK competitiveness might change was usually enough to achieve full marks. Some candidates used the correct analysis for an appreciation of the pound but then focused on depreciation for their commentary.
- 2** Question 2 was the most popular essay question but it was felt that this was a poor choice for many of the candidates. The candidates who focused on Question 3 or 4 tended to give much better answers for part (b) than those who answered Question 2. Overall the standard of essays was encouraging with many candidates clearly planning their answers in advance and constructing well thought out and logical answers. However a surprising number of candidates failed to use AS/AD analysis effectively in part b) of the essays. In some cases a descriptive approach was taken when diagrams would have enhanced the quality of their arguments and this was disappointing.
- (a) There were many very good answers analysing in detail the causes of inflation and referring to demand-pull, cost-push and the monetarist approach. Level 3 required candidates to explain why demand or costs could increase and most gave excellent answers here. A minority of candidates made little or no reference to the specific theories of inflation. They relied, usually, on an implicit understanding of demand-pull inflation by explaining shifts in the AD curve and if this was well executed it was deemed to be sufficient for Level 3.
- (b) In part (b) the standard approach was to list the macroeconomic policy objectives examine each briefly and make an assessment of their importance relative to the control of inflation. Better candidates recognised the tension and potential conflicts between the objectives and would usually move into Level 4. It was important that candidates focused on the question which was whether inflation was the most important aim. It was necessary for answers to explore whether the conflicts actually existed and whether there were circumstances when the theoretically predicted result would not occur. This required a more intuitive approach and reference to the current state of the UK economy. This was found to be beyond the ability of many of the candidates.
- 3(a)** Most answers matched the mark scheme, although some candidates looked at other practical factors that affect foreign direct investment and globalisation. These were also credited. There were a number of excellent answers with candidates showing a particularly high level of understanding of the link between interest rates and investment. A limited number of candidates were clearly confused about the meaning of investment and focused on savings, bank accounts and stocks and shares.

- (b) Excellent answers used AS/AD analysis effectively to examine the potential consequences of investment on the performance of the UK economy. Although the answers tended to focus heavily on AD rather than AS, the candidates were able to develop sound commentary on why investment can be beneficial to the economy and also the situations when it might be problematic. These answers tended to conclude with the observation that, in the first instance, it depends on the state of the economy. It was noticeable that some candidates wanted to demonstrate their understanding of the more complex analysis too early in their answers. Candidates should be encouraged to develop answers and not to be afraid of using simplistic AD/AS diagrams to make basic points at the start. This will enhance the quality of their answers overall as more evaluative commentary can be introduced and it avoids over elaboration, which can disguise the point they are actually trying to develop.
- 4(a) This part was very well answered by the majority of candidates who attempted it. They recognised the incentive effect of reducing the level of income tax and were able to illustrate it effectively using a diagram. Some candidates focused too heavily on the AD effect and failed to shift the AS curve. This type of answer could still achieve Level 3 as long as explicit reference was made to the AS curve and it was shown that there would be an extension of supply and more would be produced.
- (b) This was a very similar question to part (b) of Question 3 and the same type of analysis and commentary was expected. As a result the vast majority of candidates also answered this question very well. Again, the focus tended to be on shifting the AD curve which was surprising given that most candidates had explained in part (a) that the AS curve would shift. When both AD and AS were shifted it was important that candidates made the distinction between time periods. Weaker answers tended to take a descriptive approach and failed to use diagrams to illustrate the points that they were making.

Unit 2888: Economics in a European Context

General comments

Centres are to be congratulated in the way in which they have prepared their candidates to sit this stimulating and challenging paper. The synoptic themes of taxation and subsidy were generally well understood. In particular, candidates seemed well prepared for the question on tax harmonisation. That candidates were well versed in the arguments on each side of this contemporary debate was pleasing, given that this was the first time that this important economic issue in the European context had been tested. The focus on the economics of market failure and government intervention was clearly one which was accessible to candidates and which produced responses which were confidently underpinned by use of the economist's toolkit of concepts, theories and techniques. In contrast, the economics of regulation (the focus of Question 2) proved difficult for all but the best.

Improvements in performance on this paper seem to be more to do with Centres' enhanced confidence and skill in preparing candidates than to any perceived easing of the synoptic challenge. Evidence of this was found in the responses to Question 1 (b) which contained much accurate, focused and insightful economic analysis. There was also a greater awareness of the evaluative demands of the questions set, with the exception of Question 3. In the final question it was rare to find responses which did not warrant a Level 4 mark as the case for tax harmonisation was balanced by the case against. More sophisticated evaluation through the weighting of arguments, the consideration of scale and significance and the ability to offer considered judgements in concluding paragraphs, whilst better than in the past, are still the hallmarks of the very best candidates sitting this paper. This report gives detailed guidance on how these higher order skills may be developed by candidates sitting future synoptic examinations.

If there is one continuing weakness amongst the majority of candidates it is the handling of economic data. As emphasised in almost every report on this Unit, the first question on the paper should be an opportunity for all to access full marks. The relative ease of the skill assessed is signalled by directive words such as **describe**, **summarise** or **compare**. In this session, Question 1 (a) required a comparison of the data on tobacco taxation in Table 1. It did not require candidates to **explain** differences in the taxation of tobacco, to **analyse** reasons why countries tax tobacco products differently or to **assess** the consequences of such different excise duties. Many responses, however, offered much that the question did not call for and, consequently, failed to score marks for what was required. As in previous reports the guidance which is offered is for short, succinct statements which capture the key features of the data. In this case, comparative statements like higher and lower could gain up to three of the six marks available for this question. To access the highest marks, examiners expect some degree of data manipulation. In this session the opportunity to quantify the differences in taxation of tobacco products was missed by a significant majority of candidates.

Comments on individual questions

Question 1

- (a) Many responses to this question went beyond the simple comparison of tobacco taxation asked for. Explanations of the data, though insightful, gained no marks and wasted much time. The lack of focus on the question set accounted for the paucity of full mark responses. Some candidates compared tobacco taxation in Spain with that in Ireland, completely ignoring the UK. Others compared the UK with Spain and then with Ireland but not with both. Poor data handling skills also made it difficult for even the best candidates to access all the marks available. Three marks were available for simple comparisons, such as the UK's excise duty and revenue was *higher* than Spain and Ireland's and the revenue's share of GDP *lower*. Additional marks were awarded for explicit quantification of these differences, which candidates appeared reluctant to offer. The ability to handle data is an important part of the economist's toolkit and one that many candidates need to be given practice at.
- (b) This question was handled well by the majority of candidates, who displayed confidence and skill in the analysis of reasons for the taxation of tobacco. Candidates generally sought to explain either reasons related to market failure or to revenue raising objectives, with the best covering both of these reasons. As a result there were many Level 3 marks awarded. Differentiation in Level 3 focused on the extent to which candidates developed their analysis of the reason(s) offered. For example, where the nature of market failure was well explained and then linked to the way in which taxation of tobacco corrected this, full marks were awarded. The revenue raising objective was generally less well analysed. The importance of price inelastic demand was often recognised but not fully explained. Level 2 answers typically described the negative externalities of smoking without analysing the resulting market failure or analysed **how** governments tax tobacco products rather than **why**.

Question 2

This question proved to be the most difficult one for the majority of candidates, despite the fact that questions on regulation have featured prominently in Market Failure and Government Intervention AS examination papers recently. The weakest candidates had very little, if any, knowledge or understanding of what government regulation is. These candidates often wrote at length about taxation, repeating much of what they had said in the previous question. Better candidates understood that regulation was a form of intervention based on the command-and-control, rather than the market-based, approach. Of those who understood this there were few who could use the economist's toolkit to analyse and evaluate the **effectiveness** of regulation in correcting the market failure caused by negative externalities. Many wrote at length about the **effects** of regulation instead of its effectiveness. Much of what was written was descriptive and based on general knowledge rather than economic knowledge. It was common to read that the Irish ban on smoking would not be effective since people would still smoke at home. The best answers first used the economics of market failure to show how, in theory, the ban should reduce the demand for tobacco to the optimal. They then showed an critical understanding that the effectiveness of regulation in general depended on the extent to which it could be enforced and policed, whether the benefits of regulation in terms of reducing negative externalities outweighed the costs and, in a handful of cases, whether bans were economically efficient compared to other 'solutions' to market failure. Many of these issues were touched upon in the stimulus material. It is expected that candidates will have considered them in the light of the economics they have studied, rather

than just regurgitate extract material or assert arguments without analysing or evaluating them. It was surprising how many candidates assumed that regulations would be obeyed as a matter of course and without enforcement – under-age drinking must, then, not be the problem that politicians believe it to be!

Question 3

The evaluative demands of this question were not always appreciated by many candidates. There was some very good material offered on the effects of removing the subsidy on tobacco production, but not much in the way of commentary. Centres should encourage their candidates to think about the scale and significance of what they write about in order to access Level 4 marks. This may simply be a matter of thinking about the context of the economic relationships identified. For example, if candidates argue that the removal of subsidies will reduce output and increase unemployment they should comment on this in terms of how reliant farmers are on subsidies, the degree of factor mobility in the industry and the importance of farm income within the regions affected. Similarly, when arguing that subsidy removal raises the price of tobacco, candidates should think of the extent to which the market price of raw tobacco is determined by domestic supply or by imports. These issues give the basis for the evaluative comments expected for Level 4 marks. In addition, candidates could question whether the effects identified could be made less significant by measures designed to make the transition to subsidy free farming easier.

Nevertheless, the question provided a good degree of differentiation. At the bottom end there were some who analysed the impact of subsidy removal by shifting the shifting the demand curve rather than the supply curve. Others explained in great detail the Common Agricultural Policy, its history, buffer stock schemes, target prices and the implementation of subsidies rather than their removal. In Level 2, there was a descriptive understanding of some of the likely effects often drawn directly from the stimulus material. In Level 3 some candidates were unsure which effects were microeconomic and which were macroeconomic. Better candidates in this level clearly distinguished the effects using the analytical frameworks of demand and supply and Aggregate Demand and Aggregate Supply. The standard subsidy diagram featured in many answers, but only better candidates used it to analyse the effects of subsidy **removal**. The best candidates in this level produced excellent diagrams incorporating both subsidy removal and the importation of raw tobacco based on the deficiency payments scheme which operates in this sector.

Question 4

Despite the obvious fact that a question on tax harmonisation had clearly been anticipated by candidates and Centres, this question provided good discrimination. The requirement to discuss the case for tax harmonisation was well understood by the vast majority of candidates and this opened up access to Level 4 marks. Most candidates got into Level 4 of the mark scheme by setting the case for the harmonisation of taxes alongside the case against. Differentiation, then, focused on the extent to which this discussion was developed and underpinned by economic analysis.

Weaker responses could identify points for and against tax harmonisation but struggled to offer a coherent and detailed explanation or analysis. At worst such responses were little more than a list of points.

To progress through Level 4 it was expected that argument such as the distortion of flows of FDI would be explained and its significance commented upon. All examiners felt that there

was too much assertion on both sides of the debate and too little economic analysis. Such analysis would have allowed more candidates to then engage in evaluative discussion of the competing claims. For example, an analysis of labour mobility issues might have led more to question whether labour mobility in the EU is really affected by differences in income tax rates or by other factors. Similarly, low rates of corporation tax may distort flows of FDI, but there are many other factors involved in the location decisions made by multinational companies. The extent to which flows of FDI have a bearing on macroeconomic performance could also have been questioned. Alternatively, the role of FDI in the different economies of the enlarged EU-25 could have been profitably explored by candidates.

Where such judgements were made explicit and developed, candidates were awarded marks in the higher end of Level 4. Those whose discussion ended with a genuine evaluative conclusion, weighting the various arguments in the debate, were awarded the very highest marks.

The number of candidates who went on 'automatic pilot' and produced a standard account of the virtues of closer integration without showing how tax harmonisation would help or who only stated the case for tax harmonisation was pleasingly small. In this respect, as in many others, performance on this paper continues to improve.

**Advanced Subsidiary (3812) and Advanced (7812) GCE Economics
June 2005 Assessment Session**

Unit Threshold Marks

Unit		Maximum Mark	a	b	c	d	e	u
2881	Raw	45	33	29	25	21	18	0
	UMS	90	72	63	54	45	36	0
2882	Raw	45	33	29	25	22	19	0
	UMS	90	72	63	54	45	36	0
2883	Raw	45	34	30	26	22	19	0
	UMS	120	96	84	72	60	48	0
2884	Raw	45	33	30	27	24	22	0
	UMS	90	72	63	54	45	36	0
2885	Raw	45	33	29	26	23	21	0
	UMS	90	72	63	54	45	36	0
2886	Raw	45	30	27	24	22	20	0
	UMS	90	72	63	54	45	36	0
2887	Raw	45	32	28	25	22	19	0
	UMS	90	72	63	54	45	36	0
2888	Raw	60	46	41	36	31	28	0
	UMS	120	96	84	72	60	48	0

Specification Aggregation Results

Overall threshold marks in UMS (i.e. after conversion of raw marks to uniform marks)

	Maximum Mark	A	B	C	D	E	U
3812	300	240	210	180	150	120	0
7812	600	480	420	360	300	240	0

The cumulative percentage of candidates awarded each grade was as follows:

	A	B	C	D	E	U	Total Number of Candidates
3812	22.7	43.4	61.8	77.0	88.2	100.0	5222
7812	31.6	61.1	81.4	93.2	98.3	100.0	4317

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