

2002 June Unit 1 Mark Scheme

Key to answers

1 D 2 B 3 C 4 B 5 D
6 C 7 C 8 D 9 A 10 B

1 Answer D

either statement is factual (1). Both statements contain opinions/value judgements (1). The key words/phrases are 'should' and 'it would be a good idea' (1).

If a wrong key is selected, but the explanation shows some understanding of the difference between positive and normative statements in economics (1).

2 Answer B The PPF shows various attainable maximum combinations of output of two goods (1) when all a nation's resources are fully' employed (1). The presence of A, C and D might encourage - but do not guarantee - economic growth (1). Investment in new technology increases the quantity and quality of a nation's productive capacity (1) and enables it to produce more of both goods (1).

If a wrong key is selected, but the explanation shows some understanding of the link between investment, technology, growth and the PPF (2) or shows some understanding of the shift in the PPF and the ability to produce more of both goods (1)

3 Answer C All the countries concerned have abandoned planned economies and have since been moving towards (i.e. in transition to) a more market-based economic structure (1), thus rejecting state planning (A) and any extension of public ownership (B) (1). The difficulties of transition have encouraged speculators and others to take their money out of these economies, adding to the problems of transition (D) (1). Economic stabilisation programmes (C) have steadied the fall in real GDP and reduced the average rate of inflation to a low level (1) after a period of falling/stagnant GDP/recession and rising inflation (1).
Note that candidates are not required to specify particular economic stabilisation programmes.

4 Answer B Increased demand for a joint product (leather) increases the supply of beef, and supply

shifts from S₁ S_i to S₃S₃. The health warning against eating red meat decreases demand

for beef, and demand shifts from D_iD_i to D₂D₂. S₃S₃ and, D₂D₂ are now in equilibrium at point B.

To gain 3 marks, both shifts and the reasons for each must be made explicit.

If a wrong key is selected, but there is valid reasoning in the explanation, award marks as follows, up to a maximum of 2 marks: , Answer increase in supply (1)
decrease in demand (1)

supply rises and demand falls (1)
joint supply (1)

5 Answer D

Since $PED = \frac{\% \text{ change in quantity demanded } X}{\text{change in price } X}$ (1)

Then, (1) $\frac{600,000 - 400,000}{400,000} = 50\%$ (1)

(2) $\frac{\pounds 1-20 - \pounds 0-90}{\pounds 1-20} = -25\%$ (1)

(3) $\frac{50\%}{-2.0} = -25\%$

If a wrong answer is selected, a candidate may be awarded up to a maximum of 2 marks for identifying the PED formula or defining PED or stating that PED is elastic (1) or correctly calculating %OQd (1) and/or %OP (1).

6 Answer C

In a non-regulated market, the supply increase should find equilibrium with demand at price O_{Pi} and quantity O_G (1). Target price schemes, however, encourage overproduction (1). At price O_{Pz}, an increase in supply leads to excess supply FH (1). To restore the target price, the producers (the scheme's operators) must eliminate the excess supply of sugar by reducing its quantity from O_H to O_F (2)

If a wrong key is selected, but the explanation shows some understanding of target price schemes award up to 2 marks

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7 Answer C Comparative advantage does not mean that one country can produce more of a product than another country (1) or can produce more efficiently (1) or at a lower unit (average) cost (1). Comparative advantage is measured in terms of other goods that could have been produced, instead of sheet steel (2). In the production of sheet steel France sacrifices less of some other good than Greece (1). A correct numerical example (2).
If the wrong key is selected, but the explanation shows some understanding of the principle of comparative advantage (1) and if there is some development of the relevance of opportunity cost (1)

8 Answer D

Tax per unit = the vertical difference between supply curves or the total tax revenue = sales x (price - sales revenue): 80 units x (£7-£4) = £240 (1).

The horizontal line from the pre-tax price to the original equilibrium reveals the apportionment of tax between producers and consumers, with the producers' share below the line and the consumers' share above the line (1) (may be implicit or expressed differently)

Producers: 80 units x (£6 -£4) = £160 (1) Consumers: 80 units x (£7 -£6) = £80 (1) Correctly annotated diagram (1)

Impact of elastic demand on the incidence of taxation (1)

If a wrong key is selected, but the explanation shows some understanding of the concepts involved (and perhaps contains mathematical errors) award up 2 marks

9 Answer A

YED = % change in quantity demanded

change in income or definition (1)

Normal goods: a change in income leads to a positive change in demand (i.e., when income increases, demand increases also) (1)

Inferior goods: a change in income leads to a negative change in demand (i.e., when income increases, demand decreases) (1)

Award marks for explanatory diagrams

If a wrong key is selected, but the explanation shows some understanding of YED (1)

10 Answer B

A supply curve rests upon a ceteris paribus assumption (1). A change in any of the underlying conditions (determinants) of supply will result in a new supply curve (a shift in supply) (1). A shift to the left shows a decrease in supply (could be shown in a diagram) (1). An increase in factor costs (wages) increases production costs and decreases supply (2). Key C would bring about an increase in supply, while D is a demand determinant, and the price of tea (A) is a given (1)

If a wrong key is selected, but the answer shows some understanding of the determinants of supply (1) and of shifts in supply (1)

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11(a) Using a supply and demand diagram, analyse why there has been a continuing slump in the price of coffee' during the last two years

Diagram showing change in Quantity demanded and supplied (2)

Candidates may show two increases (shifts) in supply

An increase supply due to a rapid increase in Vietnamese output (1) and Brazil's recovery from poor harvests (1)

Failure of demand to keep pace with rising production (1)

(b) Explain why 'the price of coffee has long been subject to extreme fluctuations'

Price inelastic demand accentuates the price effect of supply shifts

Supply is relatively inelastic between harvests, and unresponsive to demand shifts

Supply is subject to weather, pests, etc. and difficult to plan or predict

Coffee growers base their supply decisions upon the price received in the previous period, leading to over-supply / under-supply and price instability (i.e. the cobweb model)

Failure of buffer stock schemes

Award up to 6 marks (3+3 or 4+2) for any two well-developed responses, particularly if illustrated with an appropriate diagram

Paragraphs 2 and 3 refer to market intervention. Why might such schemes be unlikely to succeed?

A buffer stock scheme (1) solved the problem of temporary excesses of demand or supply, but collapsed when consuming countries became unwilling to finance the build up of buffer stocks (3)

A scheme to reduce supplies (1) would fail from a lack of co-operation from some major producers (India, Indonesia, Brazil) and the inability of producers to fund the scheme (3)

Fixing the target price too high would encourage overproduction (2) and increase the costs of the scheme (1)

(c) With reference to the passage and other knowledge, examine possible measures by which the demand for coffee might be increased

It may be inferred from the text that coffee producers might exploit the recent study

that suggests that coffee is not as bad for health as once thought. Coffee might be marketed as superior alternative to other beverages - or as a product without close substitutes. Who would promote this view of coffee - an individual national producer (e.g., Brazil) or an international body of coffee producers?

Advertising campaigns might be employed to increase consumer awareness of the product. However, most advertising is by coffee processors (Nescafe, Maxwell House) rather than by producers. For many years they have promoted an image of coffee as an up-market product, thereby attempting to create brand loyalty and both increasing demand and making it more price inelastic. Such advertising may not, therefore, increase the total demand for coffee

The concept of branding is also mentioned in the text. Colombia has been successful in creating something of a market niche for its arabica coffee. This is also due to investing in technical advice and to quality control. However, increased demand for Colombian coffee may be at the expense of producers in other countries.

For each argument analysed and evaluated

(i.e. 3+3 or 4+2) 6

(Total 20 marks)

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12 (a) Discuss possible economies of scale Wimpey might be expected to gain from its take-over of McAlpine's home division.

For defining economies of scale (1)

There may be technical economies through the use of better machinery and an extension of the division of labour (although this is unlikely because site-based construction does not *offer* the same opportunities as factory production).

Managerial economies through the shedding of staff and possibly through the opportunities opened up for reorganising management structures, duties and responsibilities, etc.

Commercial economies in architectural design, land banking, the bulk purchase of bricks and other materials and subcontracting, etc.

Commercial economies in the marketing and sale of homes

Financial economies in securing market/bank funding of schemes and in raising long-term capital.

Risk-bearing economies such as the entry to the 'upmarket housing in the South East' providing greater market diversification.

(2 x 3) subject to a maximum of 2 marks for merely identifying economies of scale without application

(b) Using a supply and demand diagram, examine the likely consequences for house prices over the next 15 years of the information provided in lines 12-17.

(if there is one correct shift and one incorrect shift, up to 3 marks)

House prices will rise because the forecast increase in demand of 3.8 million houses (equivalent to 237,000 pa) (1) exceeds the current annual increase in supply (175,000 pa) (1) and even exceeds the 230,000 pa built during the 1987-1990 boom (1). Relevant reference to inelastic supply (1) The forecasts tell us nothing about the assumptions that have been made about other demand determining factors such as the level of employment and the growth of real incomes, the level of interest rates and the availability of mortgages, preferences for home ownership or renting (2).

Award up to 3 marks for the explanation

(c) Examine *one* possible reason why 'the current low level of interest rates ... has stimulated housing demand' (lines 18-19).

Very few people are able to buy a house outright. Saving would take too long. The vast majority of house buyers must borrow from a mortgage lender (bank or building society). The monthly cost of mortgage repayments (capital plus interest or interest plus endowment/ISA etc.) has a powerful influence on demand for house purchase. It is usually the largest single item in household expenditure and default risks repossession and possibly homelessness

Lower interest rates encourage a 'feel good' factor by reducing the monthly burden of debt repayment on existing mortgages and making new mortgages cheaper (unless and until offset by higher house prices).

Lower interest rates will have maximum impact upon demand if accompanied by positive economic circumstances, i.e., low unemployment and low inflation, rising real incomes and prosperity, optimistic expectations.

Lower interest rates are a disincentive for saving and encourage consumption expenditure (e.g. housing - which may also be regarded as an investment)

Award up to 4 marks for one reason if suitably developed and evaluated.

(d) Examine one factor that might be thought likely to prevent house building keeping up with the growth of demand over the next fifteen years
House building appears to be demand led and much influenced by past experience. Developers and builders suffered badly in the housing market recession of the early 1990s, and seem to be so psychologically disturbed by the events of that period that they are always cautious - and often pessimistic - about future prospects. The passage suggests that if the market is currently doing well, it can only get worse
A major factor contributing to developers' caution is the nature of housing demand. Demand is driven by short-term influences - incomes and employment, interest rates and inflation, expectations and confidence. The passage focuses primarily upon short-term interest rates (as a guide to the health of the economy and the direction of government policy) and their influence upon housing demand. When interest rates are perceived as having peaked, then rate cuts will be expected to stimulate housing demand; when interest rates are thought to have bottomed out, then rate increases will be expected to reduce housing demand. Since (i) interest rate policy has been the major tool of economic policy, leading to frequent rate changes, and (ii) most mortgages are still on a variable rate basis, then demand is likely to be volatile and

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to encourage developers' cautious attitude to undertaking new construction commitments.

Town and country planning controls over the use and development of land - through such measures as greenbelt, zoning and density controls - limit the amount of land available for house building. Encouraging redevelopment of brownfield (i.e., already used) sites, while tightening further the restrictions on the development of greenfield sites will add additional constraints upon the supply of residential building sites. There appears to be a contradiction in government policy between ensuring for the provision of sufficient future housing and making adequate provision for environmental concerns. The conflict is likely to be most apparent in the prosperous, expanding South East (4)

Award up to 4 marks for any one point if sufficiently developed and evaluated. It is likely that candidates may combine a number of different arguments, in which case award on the basis of both content and quality. A list of points without evaluation should not be awarded maximum marks. Bear in mind, however, that candidates are not required to have a detailed knowledge of the housing market, and that the passage itself is likely to provide the major source of material and information (Total 20 marks)