

# Examiners' Report

## June 2015

IAL Economics WEC04 01

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## Introduction

The entry for this paper continues to grow with just over 1,000 candidates sitting this exam.

In Section A, question 1 was the most popular choice (attempted by around 50% of candidates), followed by question 3 (35% of candidates) and then question 2 (15% of candidates). The mean scores for questions 1 and 3 were similar and in line with the average scores from the summer 2014 paper, however the mean score for question 2 was lower due to a significant proportion of the candidates who answered this question writing about a country's trade balance, rather than its terms of trade, as the question asked. Although this mistake was more common among weaker candidates, it was made by candidates at all levels. Similarly, (although to a lesser extent), question 3(a) was misread by a number of candidates. These questions were no more difficult than the others, but candidates simply did not read them carefully enough.

In Section B, the split between the two optional questions was also uneven, with around 70% of candidates attempting question 4 and 30% answering question 5. Mean scores across these two questions were roughly similar, and in line with (although slightly above) mean scores from June 2015.

The questions were generally accessible at all levels and provided some good opportunities for candidates to differentiate themselves by ability. Answering the precise question asked, integrating data with analysis, and strong evaluation remain the key ways that A-grade candidates achieve higher marks.

It is pleasing that the standard of responses was generally slightly higher than previously, and that candidates seem to have a good understanding of what is required of them when attempting this paper, including the mark distribution for each question and the four assessment objectives. Candidates are also making more consistent efforts to apply their answers to real world examples and contexts, particularly in Section A, a previous weakness that was commented upon in the January 2015 Examiner's Report. There is no evidence that candidates have problems with timing or completing the paper in the allotted time.

## Question 1

This question was generally well answered and gave candidates the opportunity to show their ability across all assessment objectives.

In response to question 1(a), all candidates were able to show an understanding of the term 'globalisation' and at least some knowledge of the idea of 'comparative advantage'. Weaker candidates were often not clear on the difference between absolute and comparative advantage, while stronger candidates could give clear definitions which were well supported with diagrammatic or numerical examples. Good answers could also give examples of what different countries may have comparative advantage in, and used these to explain specialisation and hence increased trade. All candidates could give some basic explanation of the need to trade internationally if countries specialise according to comparative advantage and understood that increased international trade was one aspect of increased globalisation. Stronger candidates were able to develop and expand on this point. Credit was given for the discussion of other likely causes of increased globalisation over the past 40 years, either as analysis or evaluation, depending on how candidates chose to present these. In evaluation, stronger candidates were also aware of the limitations of the model of the law of comparative advantage as usually presented, and could draw on real life examples of some of these to question the relevance of the concept (for example trade barriers or transport costs).

Question 1(b) was also a very accessible and generally well answered question. Pleasingly, the vast majority of candidates wrote about both the benefits and costs of globalisation to both developed and developing countries, and so addressed all aspects of the question. Stronger candidates tended to focus on more economic costs and benefits and were also able to include high level application into their responses; weaker candidates often focused more on the social (rather than economic) costs of globalisation, such as loss of cultural identity. While valid, candidates often found that they had less to write about on such issues, limiting the extent to which they could construct logical chains of economic analysis.

Indicate which question you are answering by marking a cross in the box . If you change your mind, put a line through the box  and then indicate your new question with a cross .

Chosen question number: **Question 1**  **Question 2**  **Question 3**

a)

Comparative advantage is the ability of a country to focus on its primary resources that is most advantageous compared to the rest in trade with other countries.

Theory of comparative advantage explain that for the past 40 years, the countries of the world have become more global and connected to each other this has made it easier to compare a ~~fast~~ country's comparative advantage among one another. This also makes it easier for countries to focus on their comparative ~~advantage~~ and simultaneously bridge the

gap of globalised trade. For example, let's say Italy produces a vast amount of olive oil due to its numerous olive farms and it also produces wine, meanwhile Argentina produce vast amounts of high quality wine and also olive oil. Comparing the two countries main trades we can observe that Italy has a comparative advantage at producing olive oil and ~~Argentina~~ Argentina has a comparative advantage at producing high grade wine. Thus, through globalisation and the comparative advantage theory, trade between the two countries are made easier as Italy exports imports olive oil to Argentina and Argentina imports wine to Italy. The two countries can come to an agreement and simultaneously support each others comparative advantage.

Furthermore, this explains to what extent the theory of comparative advantage increased globalisation. Based on comparative advantage a country does not have to balance as many trades as possible to globalise trade and succeed. A country could simply choose the best trade among its capabilities and use it as a comparative advantage among countries that don't have said trade as their comparative advantage.

Comparative advantage allows countries to be more connected in an era of globalisation. Thus making it easier for countries from the EU, South-East Asia and other continents to be globally connected and trade amongst one another without competing ~~at an unfair~~ without it a disadvantage when in comparison of one another.

Hence, the theory of comparative advantage explains to the extent of global trade and connectivity.



1(a): This is a relatively weak response to this question. Although it is clear that the candidate understands what is meant by 'globalisation', it is not obvious that they understand the precise meaning of 'comparative advantage'. The example given implies that comparative advantage is just producing more of something, or being able to produce more of something. The basic link between specialisation and the need to trade internationally is made, but the third paragraph is confused, and no other possible causes of increased globalisation are discussed. This is therefore a low Level 2 response, which was awarded 4 marks.

1(b): In this response, the candidate explains possible costs and benefits to both developed and developing countries, and indeed the answer is nicely balanced across all of these aspects. This response is lacking depth in some places and, particularly, it would have been strengthened by the inclusion of more application, but the variety of points explained and the evaluation content meant that it achieved a low Level 4 score and was given 16 marks.

**Indicate which question you are answering by marking a cross in the box . If you change your mind, put a line through the box  and then indicate your new question with a cross .**

Chosen question number: **Question 1**  **Question 2**  **Question 3**

~~The theory of comp~~

Question (a)

The theory of competitive advantage states that some countries are able to produce some types of goods and services with less opportunity cost. This would encourage countries to specialize into the production of a type of good where they have comparative advantage in. This country would be able to export the surplus while importing other goods from countries that have the comparative advantage in those goods. This is beneficial for all the countries involved as the total ~~amount~~ <sup>output</sup> of goods and services increases while each country has access to more types of goods <sup>which increases the standards of living</sup>. Thus, countries have significant motivation to trade between countries, so globalisation increases.

However, other factors may have been more significant towards increasing globalisation. These include the development of cheaper, easier and faster transportation around the world, as well as the creation of multinational corporations which greatly increase trade.



Comparative advantage also allows countries to increase exports of ~~its~~ <sup>their</sup> specialized goods to other countries. This increase in trade encourages the development of industries in a country as firms grow with increased revenue. These firms create more jobs with better wages for workers, so unemployment can be reduced. This also allows the government to collect greater tax revenue from income tax and corporate tax. As such, many countries would find it very beneficial to increase trade and this leads to globalisation.

It should be noted that the theory of comparative advantage does not take transportation costs into account. A country may have cheaper goods than other, but high transportation costs may mitigate the lower prices, so exports will not increase.

The theory of comparative advantage encourages globalisation because countries are able to increase their growth. By specializing in a good and exporting surpluses, exports  $X$  will increase, so  $(X-m)$  also increases. Since  $(X-m)$  is a component of aggregate demand  $AD$ ,  $AD$  also increases, thus export-led growth will increase. This growth is much faster than other types of growth.

However, barriers to trade may prevent a country's exports from penetrating foreign markets. These barriers include tariffs and non-tariff barriers, and restrict the entry of imports from another country to protect domestic employment or to prevent dumping. Thus, the exporting country is unable to increase its exports, so trade will decrease and globalisation is restricted.

### Question (b)

Globalisation occurs as global trade increases and movement of labour is also increased between countries. ~~#~~ Markets become more integrated.

Developing countries can benefit from increased globalisation as they can now export their goods to obtain revenue. Increased exports increase aggregate demand and stimulates export-led growth. The governments of these countries also collect more tax revenue which can be used to invest in development, which increases the standard of living for the population.

However, developed countries tend to implement barriers to trade to limit imports. Tariffs such as the Common Agricultural Policy will limit the ability of exports from developing countries to penetrate foreign developed markets, so they may not benefit.

Increased globalisation also allows ~~developing firms~~ firms in developing countries to have access to bigger markets. This is especially beneficial for small countries with small domestic markets. Bigger markets allow firms to expand and exploit the economies of large scale production and become more productive. ~~Firms~~ Growing firms would also increase available jobs, so unemployment will decrease.

It should be noted that ~~#~~ developing countries tend to become primary product dependent as they specialize in only a few types of goods to export. These commodities tend to be subject to volatile prices. So if prices fall, these developing countries may suffer from ~~re~~ decreased growth.



volatile prices. So if prices fall, these developing countries may suffer from ~~the~~ decreased growth.

In addition, globalisation ~~is~~ usually involves ~~that~~ Multinational Corporations that operate in developing countries. These corporations bring in foreign direct investment which fills the savings gap for these countries. According to the Harrod-Domar theory, capital accumulation is essential for growth, so as the FDI fills the developing countries' savings gap, capital accumulation increases. This stimulates growth in the country as well as increased corporate tax revenue for the government.

However, multinational Corporations tend to exploit the looser labour laws of developing countries. This may lead to the exploitation of workers which may include low wages, unsafe working environments, and long working hours. Thus, the costs ~~of~~ may outweigh the benefits.

Developed countries may benefit since they are able to import many different types of goods. The increase in the amount and diversity of available goods increases the standard of living in a developed country. ~~Importing primary products also decreases the need for low skilled labour, so~~ increasing exports <sup>to other</sup> ~~between~~ developed countries also encourages the growth in the countries.

However, a more integrated market means that a financial crisis can be transmitted quickly through many developed markets. This can lead to many developed countries to face recessions at once if a financial crisis erupts in another country.



## ResultsPlus

### Examiner Comments

1(a): This is a good response to the question which shows very clearly an understanding of both 'globalisation' and 'comparative advantage'. The link between the two concepts is clearly explained, and some other possible causes of increased globalisation are also identified. There is some good evaluative content in terms of an understanding of the limitations of the model of comparative advantage as presented. This response was therefore given a Level 4 score of 11 marks.

1(b): This is another strong response which covers a good number of points and addresses all the key aspects of the question by discussing both the costs and benefits to developed and developing countries of increased globalisation. There is a good level of depth and breadth in the points presented, and the candidate shows a good knowledge of economic concepts and theories, for example by the references to the Harrod-Domar model and savings gaps. The depth and breadth of both analysis and evaluation was sufficient to earn this response a Level 4 score of 18 marks.



## ResultsPlus

### Examiner Tip

1(a): In order to improve this answer, the candidate could have: expanded upon the explanation of comparative advantage by giving a numerical or diagrammatic example; included more application in the response, perhaps by giving examples of countries who specialise according to comparative advantage and then trade internationally; developed the explanation of another possible cause of increased globalisation.

1(b): The one major thing missing from this response is application. To improve it, the candidate needed to have included more of this, for example by giving examples of countries which have, or which might, experience of the costs and benefits identified in the answer.

## **Question 2**

This question was poorly answered by a significant proportion of candidates who chose to attempt it. The issue was not really with the answers themselves, but with candidates misinterpreting the question. Candidates of all ability levels thought that it was asking about a country's 'trade balance' rather than its 'terms of trade' and so candidates wrote essays about this concept instead, meaning that little of what they wrote was answering the question set and so could not be awarded marks. It did not seem to be the case that this was a particularly difficult topic or question - those that knew the concept of terms of trade generally managed to produce responses of a similar quality to questions 1 and 3. It is not clear whether this was because candidates had not covered terms of trade and so were not aware that it might be different to the trade balance, or due to some other reason. The fact that both part (a) and part (b) were about the terms of trade meant that candidates scored very low marks overall if they misinterpreted this concept.

Responses that did understand what the terms of trade were, were generally able to suggest a range of factors which might have explained the change in the variable that was the focus of part (a). Most candidates were able to discuss the likely effect of changes in the exchange rate, the relative inflation rate, and some aspect of production cost or productivity on the terms of trade. Stronger candidates were also often able to discuss the implications of the Prebisch-Singer Theory for the terms of trade of countries specialising in primary products, which provided an excellent answer to the question. Candidates of all ability levels did find it more challenging to evaluate these factors though.

In answer to question 2(b), stronger candidates appreciated that the effect of the change in the terms of trade would depend on whether it was the price of imports, exports or both that had caused it, and were able to discuss the likely effects of each of these on the economy. This more nuanced understanding also provided the opportunity for some good evaluation points, as did ideas of the importance of the price elasticity of demand of a country's imports and exports when discussing the effects of the change in the terms of trade on the value of a country's imports and exports and hence its net trade balance.

Indicate which question you are answering by marking a cross . If you change your mind, put a line through the box  and then indicate your new question with a cross .

Chosen question number: Question 1  Question 2  Question 3

a)

$$\text{Term of trade} = \frac{\text{Change in export price index}}{\text{Change in import price index}} \times 100$$

The term of trade of a country may worsen to several factors. One of the factors is the depreciation of a country's ~~currency~~ exchange rate. If the ~~exchange~~ value of its currency fell, the value of exports will decrease while the value of imports will increase. Hence, the term of trade will be worse off.

However, this ignores the effect of international competitiveness of goods and services. When prices are low, low exports prices will cause exports to be more competitive abroad, causing exports to increase in volume despite the decrease in price, which will cause the overall revenue to increase. Hence, the worsen of the term of trade is not necessarily bad.

\* This will decrease the ~~gover~~ nation's exports revenue.

The term of trade may also worsen due to ~~cost~~<sup>imported</sup> push inflation, assuming a nation is a commodity importer. A rise in the <sup>global</sup> prices of commodity will cause imported goods to be priced higher, causing a ~~cost~~<sup>imported</sup> push inflation and hence, a worsen of the term of trade.

Similarly, a decrease in global commodity prices will worsen the term of trade of a ~~commodity~~ exporter nation. This probably ~~explains~~ explains the decrease of 13% of Argentina's term of trade in 2012 due to low oil prices, since oil is one of Argentina's biggest export.

However, an increase in the global price of raw materials may cause a cost-push inflation. This will increase the cost of production of goods and services, which will lead to higher-priced exports and hence, <sup>an</sup> improvement in the country's term of trade. This assumes the country is an importer of commodities.

Next, a reduction in global demand for goods and services can also lead to a worsening term of trade. If the global economy is ~~and~~ experiencing a recession such as during the 2008-09 financial crisis, global demand falls as business confidence and investment falls. This will reduce the demand for exports and hence, a fall in export prices and the worsen of the term of trade.



However, this depends on the type of goods and services exported. Certain goods such as oil and the services sector are highly inelastic and have high PED. Thus, even in a global recession this type of exports will still be demanded and may not cause a deterioration in the terms of trade.



## ResultsPlus

### Examiner Comments

2(a): This response is typical of many in that the candidate has a good understanding of what the terms of trade is, but struggles to keep the whole of the response focused on this. The response starts promisingly with the terms of trade defined and then the role of the exchange rate identified correctly. In this paragraph, the candidate writes about the 'value' of imports and exports' but really means 'price'. The final paragraph on the first page is not relevant to the question, so earns no credit.

On the second page, the candidate writes about how the price of commodities will influence a country's terms of trade, and includes some good application in terms of the relevance of the oil price to Argentina's terms of trade. In evaluation, the candidate then goes on to consider the effect of a rise in commodity prices on production costs and hence prices of exports for a country which is a net importer of commodities.

On the third page, there is a weaker point presented, namely that if demand falls for a country's main exports (perhaps during a global recession), the price of that country's exports are likely to fall, worsening its terms of trade. The evaluation for this is not really correct, as it focuses on the PED of individual products, rather than the PES/elasticity of the economy's AS curve.

Overall, this response shows good knowledge, includes one stronger point about global commodity prices and two much weaker points. It was therefore felt that this response lacked the depth and breadth required to gain above a Level 3 score, and it was given a Level 3 mark of 9.

2(b): This is a much weaker response than that to question 2(a). The candidate begins by assuming that the country's current account balance will improve, without explaining why this might be the case (and indeed it only would be in the long run if the Marshall-Lerner condition were not satisfied). In the second paragraph, there is a discussion of the role of the PED of imports and exports in determining the effects of the improvement in the terms of trade, and this is correct. However, subsequently the candidate reverts to assuming that the current account balance will improve and writes the remainder of the essay about the effects of an improvement in a country's trade balance.

As it is not clear from this response that the candidate really understands the likely effects of an improvement in a country's terms of trade, and there is only the last paragraph on the first page that is really engaged with the question, this response was given a Level 1 score of 5 marks.



Indicate which question you are answering by marking a cross . If you change your mind, put a line through the box  and then indicate your new question with a cross .

Chosen question number: Question 1  Question 2  Question 3

1. Terms of trade is the measure of exchange of one good for another when two countries trade with each other. It is simply average price of exports divided by average price of imports times hundred percent. Worsening of a country's terms of trade simply means that it requires them to sell more exports to buy the same amount of imports, such as capital.

One of the factors for worsening of a country's term of trade is simply due to inflation having low inflation rate. High relative inflation rate than their trade partners will cause the cost of production to be lower. This will result in a cheaper price of goods export goods. Argentina had low inflation rates as compared to their main trading partners. This causes their export price of goods to fall and thus will worsen their country's terms of trade.

However, a fall in a country's inflation rates may not affect their terms of trade if exporters decide to maintain a higher price to increase their profit margin. This in return will not reduce the price of exports and thus will maintain the country's terms of trade.

Other than that, exchange rates also plays an important part in determining the country's terms of trade. A fall in exchange rate will cause Argentina's exports price to fall. This is simply because as people have less demand of our currency, the exchange rate will fall. Thus when exchange rate falls, it will result in a cheaper exchange in foreign currency to buy Argentina's exports. This

results in their price to become relatively cheaper.

Thus a decrease in price of exports signals a worsen in the Argentina's terms of trade.

However, ~~it depends upon the exchange rate system due to many country countries today~~ that the country holds, ~~if~~ If the country is using fixed exchange rate like China, thus the exchange rate would not cause a shock to the terms of trade of the country as the rate is fixed and stable.

In conclusion, even though ~~foreign~~ Argentina is suffering from a fall in their terms of trade, they may also gain in terms of ~~their~~ ~~income~~ improvement in their current account as exports rise and imports has fallen.

(b) ~~improvement~~ Macroeconomic objectives is basically the four most important goals which is low inflation, low unemployment, balance of payment, ~~and~~ high economic growth and two side objectives which is equality and the environment. Improvement in a country's terms of trade simply means that some amount of exports can finance more amount of imports abroad.

~~First~~ <sup>First</sup> and foremost, when ~~the~~ <sup>Taiwan's</sup> ~~country's~~ terms of trade improves, ~~because of~~ <sup>countries</sup> ~~they~~ they can import more capital goods and machinery from abroad at a cheaper price. Thus, when more spending on capital and machinery, it will lead to a higher economic growth for Taiwan as productivity increase. Thus as ~~the~~ Taiwan can increase their output of goods and ~~services~~ <sup>services</sup>, this will lead to an increase in GDP and thus will increase Taiwan's economic growth.

However, as Taiwan increases their imports and assuming that their exports remain the same, this may cause a shift in Aggregate Demand (AD) to the left. As shown on Diagram A. As <sup>real</sup> output produced ~~is low~~, falls because of

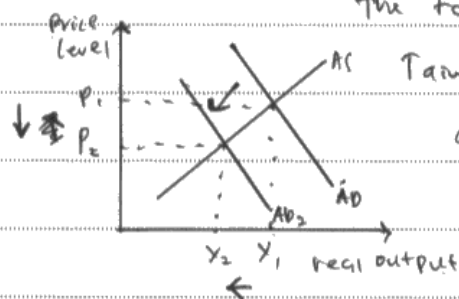


Diagram A

the fall in net exports, this will cause Taiwan to ~~suffer~~ <sup>not gain</sup> any significant changes to their economic growth as it is offset by the fall in economic growth caused by reduction on Aggregate demand.

Other than that, as ~~the~~ their terms of trade improves, Taiwan's citizen can enjoy ~~higher~~ cheaper imports. Consumers can now enjoy a more ~~wide~~ variety imported goods which offer higher quality type of goods. Furthermore, will also increase consumer choice ~~of~~ ~~and thus~~ will increase consumer utility and thus increases standard of living.

However, when exports become more expensive, ~~it~~ it will cause ~~or~~ a reduction in demand for Taiwan's exports.

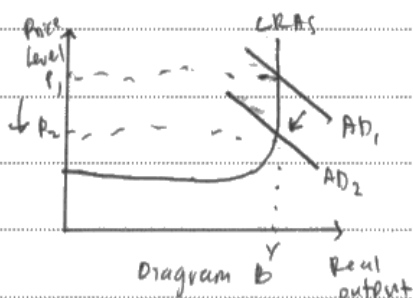
This will ~~increase~~ decrease net exports following a fall in AD.

As shown in diagram A, when output decreases from  $Y_1$  to  $Y_2$ , it will ~~help~~ cause firms to cut on ~~or~~ their production.

As labour is a derived demand, thus firms will <sup>lay</sup> ~~cut~~ off workers due to a smaller production of output. This will cause more of Taiwan's citizen to lose jobs and decrease their disposable income. This will result in lower standard of living which will also increase their unemployment level.

Moreover, an improvement in terms of trade will also reduce inflation level of their country. As export prices become more expensive and imports become cheaper, this will help to reduce the level of Aggregate demand in their economy.

Thus, following the diagram A, price level will fall from  $P_1$  to  $P_2$ , which will help to decrease the CPI level and thus ~~reduced~~ reduces inflation.



However, the fall in level of inflation for Taiwan depends upon their state of ~~recess~~ economy. If they are operating at full capacity, a fall in net exports which will cause a fall in AD, will cause a higher impact on price as <sup>shown</sup> ~~state~~ in

Diagram B. It can be seen that inflation price level had reduced greatly while real output stays at  $Y$ . Thus this will greatly result in reduced inflation and will not affect their economic growth.

In conclusion, it is largely depends upon whether ~~exports~~ <sup>net</sup> ~~and imp~~ exports represents a high proportion of GDP or not.

If the country only has net exports which is only 2% of their GDP, thus an improvement in ~~trade~~ ~~but~~ terms of trade would not affect ~~their country~~ bring a significant impact on their country's macroeconomic objectives.



## ResultsPlus

### Examiner Comments

2(a): This is a sound response to the question which shows good knowledge of the terms of trade and two factors which may have caused a worsening of it: relative inflation rates and the exchange rate. The candidate is also able to attempt to evaluate both of these factors. This response was therefore given a Level 4 score of 11 marks.

2(b): This is a good response, which considers a range of likely effects of an improvement in the terms of trade and is also able to effectively evaluate these. On the first page, third paragraph, the candidate considers the likely negative effect on the trade balance and hence aggregate demand (*ceteris paribus*). This was awarded as KAA, rather than evaluation, as this led onto the analysis on the second page. The second paragraph on the first page was therefore awarded as evaluation.

On the second page, we should note that the first paragraph analyses the likely effect of the improvement of the terms of trade on the standard of living, which is not a generally accepted macroeconomic objective and hence is not tightly focused on answering the question. The candidate does then return to relevant points however and, on the third page, presents two valid evaluative points. Given the strong economic knowledge shown, the range of points presented and the presence of some evaluative points, this response was given a Level 4 score of 18 marks.



## ResultsPlus

### Examiner Tip

2(a): In order to improve, this candidate could have tried to develop the evaluative points in more depth and/or discussed how a third factor might have caused the terms of trade to worsen.



### Question 3

As with question 2, one of the main issues encountered with responses to question 3(a) was that candidates did not answer the question, as asked. Although bold font was used to stress to candidates that the question was about reasons for income inequality between (rather than within) countries, a good number of candidates did still write essays which solely focused on the likely causes of income inequality within just one country. Such responses received some marks, but were often limited to Level 1 or 2 scores as they were really only addressing half of the question asked. It really is absolutely crucial that candidates read and re-read the question carefully and ensure that they are answering the precise question set, and not a similar one, perhaps that they have seen previously.

From candidates who understood what question 3(a) was asking them to do, some good responses were produced, often which considered the different causes of income inequality in a typical developed country as compared to a typical developing country. Here candidates could usefully discuss the different levels of government involvement to redistribute income, among other factors.

Even very able candidates did struggle to effectively evaluate their responses to this question, however. It might be useful for candidates to remember that prioritising the different factors they have analysed, with reasons, is a valid way to evaluate those factors.

Question 3(b) was perhaps something which many candidates had not considered previously, but there were some very good responses to it nonetheless. The strongest candidates appreciated that a reduction in income inequality could come about in different ways: the lower income earners could increase their earnings; or the higher income earners could see their incomes reduced, for example. In the case of the former, able candidates understood that this would likely cause an increase in the economy's marginal propensity to consume, and then to explain the varied likely effects of this. Weaker candidates tended to focus their answers on the likely effects of more equal access to social services like education and healthcare if the lower income earners received higher incomes. These points were equally valid but candidates tended to find themselves less able to develop on them, certainly in terms of developing them as different, distinct points.

Indicate which question you are answering by marking a cross . If you change your mind, put a line through the box  and then indicate your new question with a cross .

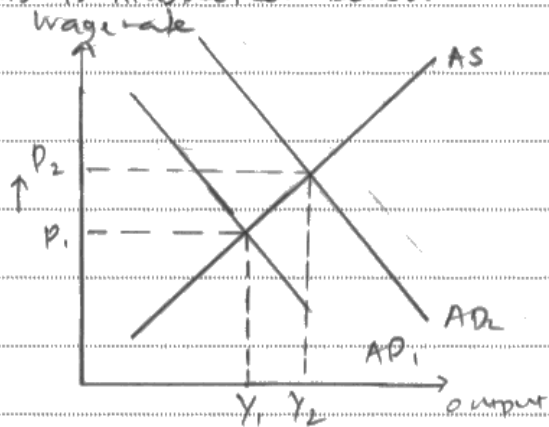
Chosen question number: Question 1  Question 2  Question 3

(a) Income is a inflow of monetary receipts that are earned by an individual. Income inequality refers to when there is a significant gap between the rich and the poor which is measured by the ~~Gini~~ Lorenz curve. ~~Many~~ There are many causes which contribute to income inequality.

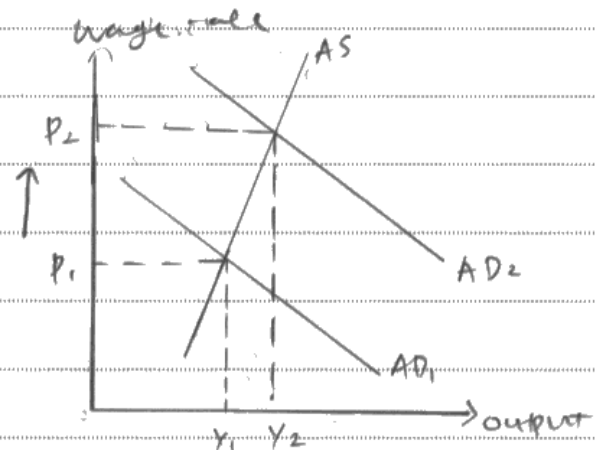


Firstly, income inequality may arise from the difference in types of jobs. For instance, a cleaner and a lawyer. ~~A cleaner~~ The demand for a cleaner to work may be ~~inter~~ inelastic whereas a lawyer ~~may be~~ is more inelastic in demand.

This is illustrated below



Demand for Cleaners.



Demand for Lawyers.

It is shown that even though a ~~big~~ ~~in~~ the ~~supply of~~ ~~of~~ ~~cleaners~~, cleaners have a small increase in wage rate when demand increase

whereas lawyers ~~it~~ will ~~increase~~ increase substantially.

This is because lawyers ~~need~~ have a higher qualification needed to become one, and also <sup>must go through years of practice</sup> firms value lawyers more as they contribute to the efficiency and productivity of a firm. Hence, income is higher in professional jobs and is increasing.

Also, another cause of income inequality is inheritance. A child born in a ~~at~~ wealthy family is better off than a child born in a poor family. This is because, ~~the~~ wealthy ~~parents~~ is likely to pass down a house in London for

instance and the child's credit balance will accumulate. This is known as the rickety down effect, as growing up. For example, Kelly Osbourne is doing well in the entertainment business and has easy access to the <sup>entertainment</sup> industry mainly due to the famous family name. Children born in Africa, or ~~East~~ Ethiopia is less fortunate ~~Furthermore~~ → as they struggle to even obtain basic needs.

Furthermore, ~~for the past~~ decade since the financial crisis in 2008, part-time jobs are seen to rise significantly. Workers are a derived demand. ~~The~~ <sup>minimum</sup> rate for part-time workers is around £4<sup>per hour</sup> and so part-time workers earn less than permanent ~~one~~ jobs. This causes ~~people~~ people working ~~part-time~~ part-time have less income and an unsustainable <sup>in</sup> flow of money causing income inequality.

However, entrepreneurs which ~~are~~ inherit a family business ~~it~~ may ~~create~~ create jobs. With the ~~over~~ overflowing of profits, this encourages them to ~~expand~~ expand their business and thus employ more workers. Although this does not significantly lighten the income inequality but workers from the third income bracket is better off ~~with~~ with a job than being jobless.

Also, it is worth noting that higher pays encourages workers to work hard without ~~as~~ a picture of a sustainable and ~~and~~ wealthy future, the worker will not be as productive and so a target is needed to motivate.

~~The~~ conclusion, income inequality can arise from many causes



3(a): This response is typical of those who misread the question and focused on likely reasons for income inequality within (rather than between) countries. As a result there is very little worthy of credit in this response. At the end of the second paragraph on the second page, the candidate does briefly contrast the USA with Ethiopia, but this is a very weak point. As a result, this response was given a Level 1 score of 1 mark.

3(b): The candidate begins the response by showing some knowledge of how income inequality might be measured, although this is not directly answering the question. The final paragraph on the first page explains a possible cause of decreased income inequality (a reduction in unemployment), not an effect of this, and hence this is not answering the question. On the second page, however, the candidate does give some possible effects, for example, an increase in consumption (although note that consumption is not an injection into the circular flow of income), and then on the third page, a resultant increase in inflation and damage to the environment. The fall in absolute poverty is not necessarily the case, but was allowed as a likely effect. The point on a fall in the crime rate is weaker. Overall, there is a selection of relevant points considered, but there is no valid evaluation, and this would be the obvious way to improve this response. A Level 3 score of 11 marks was awarded.

Indicate which question you are answering by marking a cross . If you change your mind, put a line through the box  and then indicate your new question with a cross .

Chosen question number: Question 1  Question 2  Question 3

3a) Income inequality measures the extent to which income is distributed in an uneven manner. One reason that causes income inequality between countries is the specialisation in different products. For example, those countries specializing in commodities may have a lower income than those specializing in manufacturing. This is because commodities have low <sup>relatively</sup> YED when compared to manufactured goods. When income rises, demand for commodities will change very little compared to manufactured goods like clothings. Also, commodities are low value added, they are usually at the bottom of the chain therefore jobs created are not signi not much jobs will be created. For example, Singapore has a ~~not~~ average income in China will be higher than that in Sub-Saharan

Africa countries ~~be~~ like Nigeria because <sup>about</sup> 90% of Nigeria exports are oil, while China exports manufactured goods.

Another reason may be the wealth inequality between countries. Wealth are usually in the form of stock, bonds and property. These are income generating assets. Therefore a country with more wealth can yield more income compared to ~~country~~ countries like Sub-Saharan Africa where people poverty level is high and people only earn wages.

Also, difference in development of infrastructure is a likely reason for income inequality between countries. Countries with well-developed infrastructure like airports, harbour and road infrastructure can engage themselves in more international trade and they can attract FDI better. For example Hong Kong and Singapore when compared with Sub-Saharan African countries. Sub-Saharan poor infrastructure in Sub-Saharan African countries like Ethiopia add around 30% to 40% of costs to the cost of goods. Therefore, ~~trade~~ countries who engage more in international trade may see a higher income.

However, countries with more wealth will be more vulnerable to financial crisis because they tend to involve themselves more in the financial market. Therefore, income inequality between countries may narrow during financial crisis.



Also, because commodities <sup>have</sup> low Y&D, ~~they~~ <sup>country</sup> will ~~feel less impact~~ country exporting commodities will have ~~feel less impact~~ when global income falls. Therefore, income inequality may actually decrease and terms of trade of the country exporting commodities may improve.



## ResultsPlus

### Examiner Comments

3(a): This is a sound response to the question which covers several valid points, such as specialisation in different goods, differences in wealth (a weaker point), and differences in infrastructure. There is some application, although the candidate could have included more of this if they wanted to improve the response, and on the second page there are two (although related) evaluation points. These are identified, but could have been developed in more depth. Overall, this response was given a Level 4 score of 11 marks.

3(b): This is a strong response which considers a range of possible effects and shows an excellent knowledge of economic concepts. The candidate considers the likely effects of the improvement on the marginal propensity to consume and hence the value of the multiplier, the trade balance and the budget balance. There are then three valid evaluative comments. Overall this is a good Level 4 response, which was awarded 18 marks.



## ResultsPlus

### Examiner Tip

In order to improve, the candidate needs to integrate more application into the response, and could perhaps develop the evaluative points in more depth.

## Question 4 (a)

This question was well answered, with the vast majority of candidates understanding the need to show both knowledge and application in their responses. Explanations of the meaning of the term 'free trade area' were generally sound, with stronger candidates able to add to their base definitions that there is no common external tariff in an FTA, so that although member countries agree to lower or abolish all trade barriers between themselves, each remains free to set its own barriers with non-member countries. Conversely, some weaker candidates were seemingly unaware of the different types of regional trade blocs, and gave a general definition in their response, sometimes referring to a common external tariff, the free movement of labour and capital, and other aspects only found in trade blocs exhibiting a deeper level of economic integration than an FTA. Positive marking, however, meant that such responses did usually earn the two available knowledge marks, as candidates also referred to the lowering of trade barriers between member countries too.

Application to the Extract was generally well done, with a range of relevant references credited.

(a) Explain what is meant by a 'free trade area (FTA)'. (Extract 1, line 1)

(4)

A free trade area is where a group of countries, which are usually neighbours to each other form an agreement between themselves to lower barriers of trade between them. Thus allowing easier flow of goods and services. A few examples of barriers are, quotas and tariffs.

It was estimated that the free trade area (TPP) could create annual global income gains of \$295 billion.



**ResultsPlus**  
Examiner Comments

This response earned full marks (4/4). The first, short paragraph shows sound knowledge of the meaning of the term 'free trade area' and so was awarded 2 marks; the second paragraph includes relevant reference to Extract 1 and so was awarded 2 application marks.



(a) Explain what is meant by a 'free trade area (FTA)'. (Extract 1, line 1)

(4)

A free trade area is also known as a trade bloc. Members of this FTA or trade bloc can trade amongst one another with out barriers of trade such as tariffs, quotas or embargoes. These barriers of trade may be felt when trading with countries outside of the FTA. There is also a free movement of persons within <sup>the</sup> FTA.



### ResultsPlus Examiner Comments

This response scored 2 marks out of a possible 4. The candidate shows decent knowledge and earns 2 marks for the explanation of the term 'free trade area'. Note that the final sentence about the free movement of people is not necessarily true (this is a feature of a common market, rather than an FTA), but the candidate has already secured knowledge marks by this point and responses are marked positively. However, the candidate does not earn the 2 available application marks, as there is no attempt made to relate the definition to the Trans-Pacific Partnership, or otherwise to apply it to Extract 1.



### ResultsPlus Examiner Tip

In the 4 mark data response question, there are always 2 marks available for knowledge (AO1) and 2 marks available for application (AO2). Don't forget to include an element of application to the data provided in your response so that you can also earn these latter marks. Omitting this is the most common reason for candidates not scoring full marks on the 4 mark question.

## Question 4 (b)

Candidates who read this question carefully and then answered the question, as asked, generally produced good quality responses. Those who did answer the question were almost all able to identify two types of restrictions on free trade - most commonly tariffs, quotas or subsidies to domestic firms. Stronger candidates were then able to differentiate themselves by the quality of their analysis of the effects of these restrictions; in essence we were looking for chains of reasoning to be built up explaining them, rather than a range of unconnected points to be made. For example, candidates analysing the likely effects of a tariff might explain the effect on consumer surplus, producer surplus and government tax revenue as linked steps in an explanation of the overall effect of the tariff on welfare. The strongest candidates were able to produce accurate diagrams to show the effects of the restriction (either a 'tariff diagram' or more general aggregate demand and aggregate supply diagrams) and to integrate their diagrams into their written analysis.

The four available analysis marks could be split in any way between the two types of restriction identified, i.e. an in-depth analysis of the effects of one restriction could earn all four marks, or they could be awarded as 1+3 or 2+2 across the two types of restriction. This meant that a candidate who only identified one type of restriction could earn a maximum score of 7/8. Relatively few candidates failed to identify a second type of restriction.

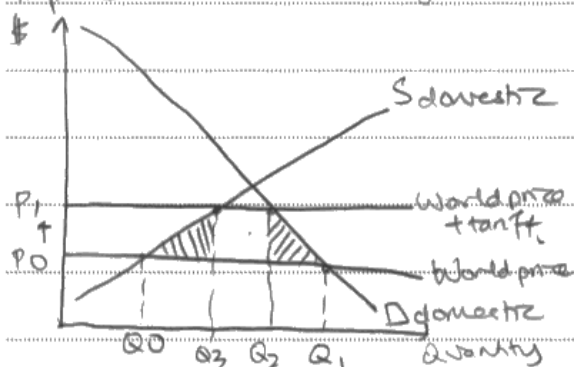
Application was the least well done skill in response to this question, with many candidates giving a purely theoretical answer with no reference to Extract 1 or the TPP.

(b) With reference to the information provided, analyse the impact of two types of restrictions on free trade.

(8)

The extract mentions that countries wish to "cut bureaucracy costs and reduce delays at borders". This ~~is a~~ ~~represent~~ ~~represents~~ ~~bureaucracy~~ costs and delays represent a restriction on free trade, as they act as non-tariff barriers. Purposeful delay and bureaucracy cost, increase to an exporting firm's <sup>total costs</sup> ~~cost of production~~. This is a restriction to trade as the increase in costs to firms is a distortion of the comparative advantage. This is because it unnecessarily increases the costs of transportation of the good to final consumers; ~~and~~ ~~therefore~~ This <sup>costs</sup> ~~artificial~~ increases would lead to ~~an~~ imports of goods to the final consumer to be at an ~~higher~~ ~~artificially~~ higher price. When cost increases lead to this translating to price increases of imports, it would mean final consumers welfare reduce. ~~and~~ Estimates show that ~~such~~ abolishing such costs would increase global ~~costs~~ ~~accord~~ to ~~\$1 trillion~~ economy by \$1 trillion, a significantly large absolute amount.

Another trade barrier, is the barrier on exports from a country for example through ~~tariff~~ tariffs or quotas. China's exports suffer from other countries' tariffs placed on Chinese goods. Tariffs are taxes imposed on imports of goods. The diagram below shows an imposition



by the USA. Assuming China is a price taker and USA a price taker. The price offered by China is at  $P_0$ . Due to the tariff, the tax on Chinese goods increases from  $P_0$

to  $P_1$ , making it less price competitive. The shaded regions show welfare losses of such an imposition.

If USA imposes a tariff on Chinese goods, prices increase from  $P_0$  to  $P_1$ , and domestic suppliers increase production from  $Q_0$  to  $Q_3$ . This leads to Also imports of Chinese goods reduce from  $Q_0$  to  $Q_4$ . The effect of price increase would also reduce total quantity of goods consumed from  $Q_1$  to  $Q_2$ .

Consumer welfare reduces, but producer welfare increases.

Also the tax collected from the tariff can be used by governments (eg to reduce budget deficit).

Both ~~Such~~ barriers would ~~reduce~~ have the effect of reducing imports which is a withdrawal from domestic circular flow of income. Also increase in spending in domestic consumption would lead to an injection to the flow. Thus this would have a net injection to ~~AD~~ aggregate demand, and multiplier effects mean the domestic economy that imposed the tariff/restriction would grow.

However the converse argument is true for those whose goods are facing the restrictions. eg China, would have less exports thus less ~~an~~ injection to flow of income. Also ~~tax~~ As such the reduction of Chinese exports may reduce inflationary and real GDP growth of Chinese goods.



## ResultsPlus

### Examiner Comments

This is an excellent response which easily received full marks (8/8). The candidate begins by making reference to the data and so secures 2 application marks. The response then goes on to identify 'purposeful delay and bureaucracy' as a type of restriction, gaining the first of the two available identification marks. The analysis of the effects of such a restriction is rather repetitive however, so earned 1 analysis mark only.

In the second paragraph, the candidate identifies tariffs as a second type of restriction and analyses the likely effects of a tariff in great detail, including a diagram in the response. This diagram is explained and good chains of reasoning are constructed. There is enough here for this candidate to be awarded 4 marks for analysis, but as there are only 3 remaining, these 3 marks were awarded.



## ResultsPlus

### Examiner Tip

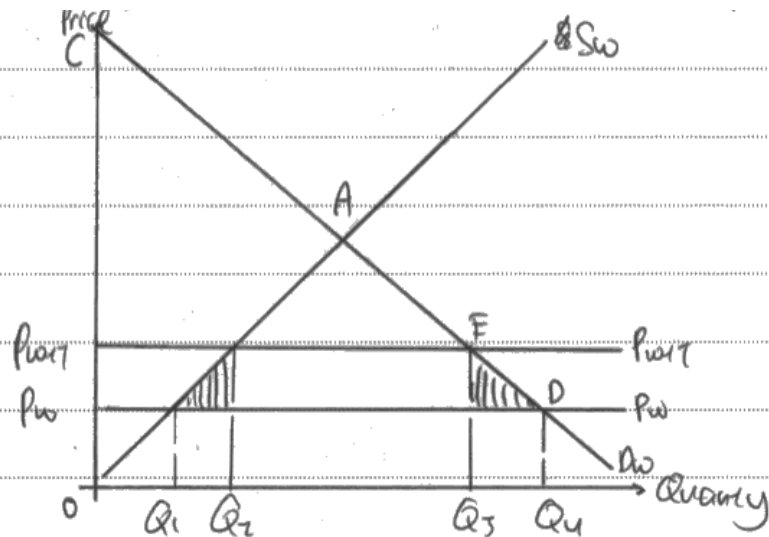
Although this is an excellent response, it is important to watch timing and not spend more time than necessary on an answer. This is only an 8 mark question so candidates are expected to produce less in response than for the 12 or 16 mark questions. In particular, the final paragraph in this response (beginning, 'However the converse argument...') is definitely extraneous as no evaluation is required in response to an 'analyse' question. This candidate had actually earned full marks by the end of the first paragraph on the second page, making the second paragraph on this page unnecessary too. This depth of analysis is very positive as long as it did not come at the expense of the candidate not having sufficient time to answer the subsequent two questions in this section.

(b) With reference to the information provided, analyse the impact of **two** types of restrictions on free trade.

(8)

Restrictions on free trade come in the form of trade protectionism which raises trade barriers in order to protect domestic industries from foreign competition.

One of the restrictions on free trade would be tariffs. A tariff is a tax on imported goods which would raise the price of the exports.



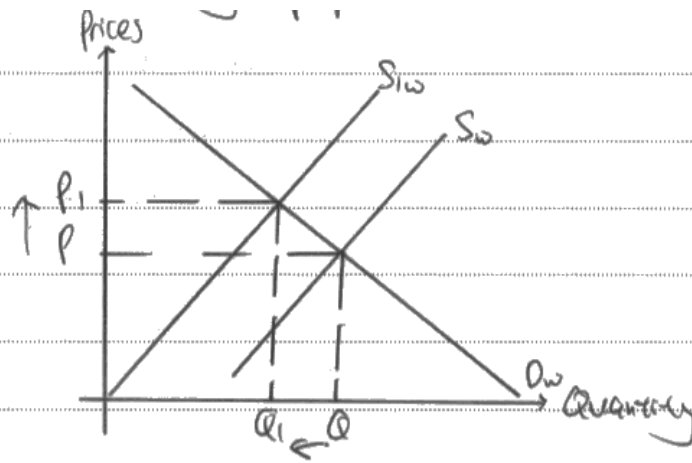
A tariff would raise the price of exports from  $P_w$  to  $P_w + T$  which would decrease the quantity supplied  $Q_1, Q_4$  to  $Q_2, Q_3$  instead. Consumer surplus would also decrease from  $CADP_w$  to  $CAEP_w + T$ .

This restriction would ~~den~~ deny access to the global markets for the world's poorest countries ~~would~~ who has yet to develop a comparative advantage yet as seen in extract 3 line 18.

However, this would depend on the magnitude of the tariff and the duration it is implemented.

Another restriction to free trade would be quotas. Quotas are a physical limit to the amount of goods imported into a country, decreasing the supply and driving up prices.





As seen in the diagram, by decreasing supply from  $Q$  to  $Q_1$ , this would increase prices from  $P$  to  $P_1$ , making the good less price competitive too.



### ResultsPlus Examiner Comments

This response earned 6/8 marks. The candidate identifies two types of restrictions on free trade (tariffs and quotas) and analyses the effects of both. 2 analysis marks were awarded for each restriction. Note that immediately above the tariff diagram, the candidate writes that tariffs raise the price of exports, rather than imports. As one country's exports are another country's imports, and the rest of the analysis is correct, the benefit of the doubt was applied here.

This response did not, however, earn the 2 available application marks, as there is no reference to the information provided. This was the most common reason for able candidates not achieving full marks on this question.

## Question 4 (c)

This proved to be a challenging question for many candidates and as such was the most effective discriminator of A-grade candidates within question 4. The vast majority of candidates were able to show some knowledge of the aim of the WTO, with weaker candidates simply identifying that it works for freer trade, and stronger candidates showing a more in-depth appreciation of the range of the organisation's aims.

In terms of the KAA (knowledge, application and analysis) marks, a basic understanding that the WTO aims for global free trade, while regional trade blocs only achieve free trade on a far more limited, regional basis tended to be a Level 1 response. Candidates who were able to explain this in more detail, either by referring to the data and/or their own knowledge so that they could apply their response to real world trade blocs and events, or by explaining additional aims of the WTO (for example, solving trade disputes, or helping to integrate developing countries into world trade - the Doha Development Agenda), were able to access Level 2 marks. Candidates who could do both of these things tended to receive Level 3 scores.

Most candidates were able to at least begin to evaluate their responses, mainly by considering the view presented in the Extract that regional trade blocs are stepping stones towards greater trade liberalisation, and that as such both trade blocs and the WTO do achieve some reduction in trade restrictions.

Many weaker candidates who obviously found this a difficult question to answer drifted away from its focus and instead wrote about the likely benefits and costs to member and non-member countries of regional trade blocs in general or the TPP in particular. This was really the response we were looking for to question 4(d), and so tended to receive very limited marks in the question.

(c) With reference to the information provided and your own knowledge, to what extent do regional trading blocs such as the TPP conflict with the objectives of the WTO?

(12)

World Trading Organisation (WTO) aims to reduce trade barriers and settle trade disputes. Thus, ~~it~~ it has conflicting objectives with trading blocs.

While there is a reduction in trade barriers amongst member countries, there are individually set ~~barriers~~ trade barriers against non member countries, such as in the case of TPP, a FTA trading bloc. This is particularly conflicting if ~~it~~ there are high tariffs set against non member countries. ~~As~~ As indicated in line 20 extract 1, costs to non-member countries may outweigh benefits of greater regional trade and investment. An example would be CET, a common external tariff imposed on other countries by the EU. This has drastically reduced trade with members and non members.

Further, WTO that aims in reducing trade disputes could have to settle trade wars if it results from implementation of trade ~~barriers~~ barriers among the countries. For example, China is under threat of protectionist measures by the USA ~~and~~. Thus, trading blocs and WTO have conflicting objectives.

~~Besides that,~~ However, the existence of trading blocs have increased trade among member countries significantly. This could be due to ~~the~~ MNC's (multinational corporations) startups in countries ~~that~~ in a trading bloc. As indicated in Extract 1 line 8, Japan has managed to attract inward foreign direct investment. These MNC's ~~would~~ ~~bring in~~ ~~take advantage~~ have immediate access to a larger market if it starts up in a member country of a trading bloc. They could export at a ~~cheaper~~ cheaper cost and thus increase incentive to expand and export across ~~the~~ borders within the trading bloc. This works in favour with the aim of the WTO.

Besides that, the trade reductions within a trading bloc enables firms in respective countries to ~~the~~ apply law of comparative advantage and specialise in goods that they have a comparative advantage in. This will lead to increase in trade as it is a ~~more~~ more viable option to trade as trade barriers are reduced. For example, Malaysia which has a comparative advantage in producing oil palms could trade with Chile which ~~is~~ has a comparative advantage in producing copper. This will lead to increase in total output and increase in consumer welfare. This would ~~be~~ make sense as both ~~these~~ these countries are in the proposal of TPP. This would then ~~conclude~~ support the aim of WTO of increasing trade.



## ResultsPlus

Examiner Comments

This response received a Level 2 mark for KAA (4 marks) and a Level 2 score for evaluation (4 marks), making a total of 8/12. The candidate begins by stating the aims of the WTO and then in the second paragraph explains the basic conflict between regional trading blocs and the WTO, (regional versus global free trade) well. The candidate integrates application to the Extract into their own knowledge and analysis.

In the third paragraph, the conflict being identified is unclear; while it is, of course, true that the WTO aims to solve trade disputes, it is not made clear why regional trading blocs would create or escalate disputes. There is therefore enough here for a low Level 2 KAA score.

In evaluation, this candidate gives two, well-developed points, earning the maximum available marks for evaluation.



## ResultsPlus

Examiner Tip

Note that in the 12 mark question, there are 8 marks available for KAA and only 4 for evaluation. This balance should be reflected in candidates' responses, with around two-thirds of the response focusing on KAA and one-third on evaluation. In this example the balance is much closer to half and half.

- (c) With reference to the information provided and your own knowledge, to what extent do regional trading blocs such as the TPP conflict with the objectives of the WTO?

(12)

With reference to extract 2, paragraph 2, line 6 to 9 the WTO is crucial for the smooth conduct of international commerce. Even the USA, he points out, has abided by the WTO judgements against it. The role of the WTO is to promote freer trade and to reduce trade barriers between nations. The establishment of the TPP conflicts with it such that they are setting up trade barriers within the 12 countries. Most of these countries are developing, if not developed countries. These countries may experience economic growth through international trade but it does not help weaker economies in third-world countries such as Bangladesh. Non-member countries will have a smaller market to export ~~an~~ as it is more

difficult to penetrate these trade barriers of the TPP.  
In line 7 to 9, this proves that "a weakened WTO would eventually lead to the biggest economies negotiating favourable deals with each other, harming the weaker economies."

With reference to paragraph 4, line 16 to 18, "The Bali agreement would do nothing to end export subsidies to farmers or to provide tariff-free and quota-free access to the global market for goods from the world's poorest countries." This can be implied that most developed countries may subsidise their farmers and this gives an unfair advantage to non-member countries who are not able to subsidise their farmers. Non-member countries will then have a declining terms of trade.

However in some cases, the TPP and WTO may come to an agreement as globalisation between these countries will rise.



### ResultsPlus Examiner Comments

The first paragraph explains the basic conflict between the WTO and regional trading blocs and makes reference to the Extract. There is enough here for a low Level 2 score for KAA (4 marks). It is not clear, however, how the second paragraph is answering the question. While the content of the paragraph is mostly correct and is referring to the Extract, it is not explaining or evaluating the conflicts between the WTO and trade blocs. No further marks can be awarded for this paragraph.

The very short, third paragraph shows that the candidate understands the need to evaluate their response to this question, but unfortunately they are unable to do so. This sentence does not really make sense, so no evaluation marks can be awarded (0 marks). This response earned 4/12 marks.



## Question 4 (d)

This appeared to be a relatively straight-forward question to answer as there was much relevant information given in the Extract. However, this was also an obstacle to weaker candidates who tended to copy out large chunks of text from Extract 1, in effect presenting these as their answer, rather than using the Extract to support their own arguments and integrating quotations into their written analysis. Although this is a data response question, and the answers to questions can often be found in the information provided, candidates must be aware that application is only one of the four assessment objectives, and so reference to the data must be combined with their own knowledge, analysis and evaluation if they are to access the higher marks. Stronger candidates were able to skilfully integrate economic analysis of likely costs and benefits with evidence from the Extract, using the data to give examples of specific countries who might experience each cost or benefit, or otherwise support their argument.

Candidates found this a relatively challenging question in which to evaluate their responses. Weaker evaluative comments focused solely on the likely costs to non-member countries which was not really answering the question: the response required mention of costs to member countries, or an assessment of the significance of the benefits to member countries. Candidates should also note that half of the available marks for the 16 mark question are awarded for evaluation, so we are looking for clear, in-depth chains of reasoning in explanation of evaluative comments, rather than just the identification of a number of different evaluative points.

(d) Assess the likely economic benefits of the proposed TPP for the countries that plan to join it.

(16)

Countries that plan to join the TPP are able to reap economic benefits such as tariff-free and quota-free access ~~to~~ with one another. Through the application of comparative advantage, each of these countries are able to specialise in their own production. Firms that are big enough to apply economies of scale (EOS) are able to pass on reduced costs onto consumers. Without tariffs, ~~the~~ price of goods and services traded are artificially cheap and more price competitive.

Consumers will then enjoy more variety of goods at a cheaper price. Standards of living will then be better off ~~and~~ and consumer welfare will rise. As some of these countries are export-driven economies such as Chile and Japan, net exports ( $x-m$ ) will then rise causing a rightward shift in AD curve. Thus, increasing real GDP and ~~causing~~ positive economic growth.

Count Huge manufacturing countries like Vietnam are able to grow even more as MNCs would want to relocate their factories in Vietnam due to cheap ~~and~~ skilled labour and cheap abundance of raw materials. These firms would want to reduce their cost of production in order to maximise profits. Vietnam will then benefit from this through gain in tax revenue, higher employment in manufacturing and public sector and economic growth.

However, in some cases where workers are now more educated and well-trained. They might result in searching for better opportunities elsewhere - This will result in a brain-drain and can be seen in developing countries like Malaysia and Mexico. This will result in firms having higher costs needed to retain workers. So profits made by MNCs may not be significantly greater as cost of production may not even fall.

In developed countries that produce these goods and services, they are not as skilled as worker compared to workers in developed countries. This means quality of the products will fall and this will reduce the attractiveness to spend on these goods and services. Due to the establishment of MNCs, they may monopolise the industry in these developing countries as ~~the~~ small local firms are not able to compete as they do not enjoy EOS. These domestic firms will be put out of business and will result in rise in unemployment. So unemployment in these countries may not even fall at all.



## ResultsPlus

### Examiner Comments

This is a good response to the question which earned 11/16 marks. The KAA content of the answer is particularly strong, and scored a Level 3 mark (7 marks), while the evaluative content was a little weaker and scored a Level 2 mark (4 marks).

The first three paragraphs analyse a range of different benefits which member countries might expect when they join the TPP. Although there is no reference to context in the first paragraph, there is in the second and third paragraphs. The candidate builds up chains of economic reasoning within each paragraph. This combination of clear understanding and explanation with good reference to context means a Level 3 mark has been awarded.

In the fourth paragraph, the candidate attempts to evaluate the response. This is a fairly weak point, partly because as an FTA the TPP will not extend to the free movement of labour between member countries, but also because the costs of a potential 'brain drain' are not really expanded upon.

The first half of the fifth paragraph is a little confused. We can assume that the candidate meant to write 'developing' rather than 'developed' as the second word of the paragraph, but still the implications of consumers substituting imported goods and services for domestically produced produce are not really explained. The second half of the paragraph is good though and nicely draws on Unit 3 knowledge to explain the possible monopolisation of markets by international MNCs.



## ResultsPlus

### Examiner Tip

To achieve a Level 3 mark for KAA, candidates should demonstrate 'appropriate reference to context throughout'. Candidates should relate each point that they make to the context of the question, either through using the data provided or their own knowledge.

(d) Assess the likely economic benefits of the proposed TPP for the countries that plan to join it.

TPP will allow a bigger market for firms <sup>and</sup> that is <sup>(16)</sup> particularly important in <sup>country with</sup> small domestic market. These firms can exploit economies of scale and reduced cost of production. Firms will pass on these reduced cost as lower prices to the consumers.

ATPP allow greater competition among member countries. Firms has less monopoly power and are forced to be more efficient and less wasteful. Firms will also become more productive. Firms not only compete price-wise but also become more innovative so consumers experience lower prices and better quality products.

The increase in FDI ~~can also~~ is also a valuable source of foreign currency. This is important for member developing countries that need to ~~import~~ finance capital goods from ~~abroad~~ overseas.

Countries are also able to become more specialise and obey the theory of comparative advantage. Members will specialise in their ~~comparat~~ goods that have a lower opportunity cost will increase total output. so <sup>the</sup> members' population can have a higher standard of living. "Vietnam could become a much bigger manufacturing hub in textiles, garments, and other industries". "Hong Kong could experience significant growth as a service and investment sector".

However, a TPP's member may experience cost push inflation if its usual trade partner is excluded from the FTA. Members have to seek more expensive ~~at~~ alternative that increases cost of production.

non-member can form <sup>their own</sup> trade bloc's ~~could~~ and have high <sup>trade</sup> barriers to against the ~~the~~ TPP members that will reduce their export and growth rate.

The benefits of joining a TPP depends on how the extend of existing trade barriers before forming. "The greater absolute gains are estimated for Japan and China" as they had high trade barriers

Effects of the Elimination of ~~trade~~ <sup>price</sup> depends on the elasticity of ~~demand and~~ imports and exports. Higher the price elasticity of imports and exports, the greater the effects.



## ResultsPlus

Examiner Comments

This response earned 9/16 marks: this was comprised of a Level 2 score for KAA (6 marks) and a Level 1 score for evaluation (3 marks).

The first three paragraphs of this response identify and explain some of the likely benefits to a country of joining the TPP. However, beyond writing 'TPP' there is no reference to context in any of these paragraphs. The depth of analysis could also be slightly improved upon, particularly in the third paragraph where the candidate only links together two sentences/stages of economic reasoning.

In the fourth paragraph, the candidate does relate the point made to two of the specific countries joining the TPP; Vietnam and Hong Kong, and uses this to evidence the point.

The candidate then moves on to evaluate the response, and a range of evaluative points are identified but not really explained or developed. If you compare the layout of the first and second pages of the answer, the length of paragraphs provide a very quick, visual comparison of the depth of analysis contained within the two sides of the argument, with the evaluative paragraphs containing one or two sentences only. This limits the candidate to a Level 1 mark for evaluation.



## Question 5 (a)

Candidates found this a relatively challenging question to answer and the mean mark for this question was significantly lower than for question 4(a). The main issue was gaining the two available knowledge marks, as most candidates were able to pick examples of current and capital government expenditure out of the Extract. There was generally a confusion between knowledge and application, with many candidates attempting to define current and capital government expenditure by giving examples of them, and then repeating this in application. For example, a good proportion of candidates wrote that government capital spending was spending on 'things like infrastructure', which earned them an application mark, rather than a knowledge mark, or similarly that government current spending was spending on 'things such as benefits'. Examples can certainly add to definitions and understanding and are a good thing to include, but only as supplementary to the general definition, not instead of it.

A small number of weaker candidates were confused between current and capital government spending and the current and capital accounts of the balance of payments.

(a) With reference to Extract 1, explain the difference between current government expenditure and capital government expenditure.

(4)

Current government expenditure are spending onto things like subsidies and salaries. Based on extract 1, introduction of new public sector saving structure is a form of current government expenditure.

Capital government expenditure are spending onto things like education, healthcare and infrastructure. Capital government expenditure can be seen in countries like Kenya and Ivory Coast.



**ResultsPlus**  
Examiner Comments

This is an example of a typical response to this question which earned 2/4 marks. Here the candidate gains both application marks, but neither of the knowledge marks. The candidate attempts to define current and capital government expenditure by giving examples of them, rather than explaining what they are more generally.

(a) With reference to Extract 1, explain the difference between current government expenditure and capital government expenditure.

(4)

Current government expenditure are spending onto things like subsidies and salaries. Based on extract 1, introduction of new public sector saving structure is a form of current government expenditure.

Capital government expenditure are spending onto things like education, healthcare and infrastructure. Capital government expenditure can be seen in countries like Kenya and Ivory Coast.



**ResultsPlus**  
Examiner Comments

This response earned 3/4 marks.

The candidate scored 1 knowledge mark for the definition/understanding of government capital expenditure as being 'spending which lasts, like investment', but did not earn a knowledge mark for the definition/understanding of government current expenditure as the response only gave examples of this.

The candidate did receive both application marks though for giving examples of each type of expenditure from the Extract.

## Question 5 (b)

This proved to be a more challenging question than might have been expected given the good number of possible causes of the slightly slower than expected economic growth given in the Extract. Weaker candidates were sometimes unable to identify possible causes, and when they were, they struggled to produce reasoned economic analysis to explain them. In particular, the fact that the 'cedi' had weakened tended to confuse weaker candidates who expected this to cause stronger growth due to it making Ghana's exports more internationally price competitive and imports relatively more expensive, (a valid evaluative point, if presented as such by candidates). Only more able candidates were able to link this depreciation to more expensive production costs and/or lower export revenues if Ghana specialises in goods with price inelastic demand, (the Marshall-Lerner condition and the 'J-curve' effect could have been brought in here).

Very few candidates showed any explicit appreciation that Ghana's economic growth had still been strongly positive: it was a fall in 'growth' that they were asked to explain, not a fall in GDP. Many candidates focused their answers on explaining why Ghana's (total) aggregate demand or (total) aggregate supply had fallen, rather than reasons why their expansion had slowed, or why individual components of aggregate demand might have fallen. This nuance was not required, but proved an effective way of A grade candidates differentiating themselves.

Evaluation also proved difficult for many candidates here.

(b) Discuss why Ghanaian 'GDP growth for 2013 is now expected to be closer to 7% than the 8% that was forecast'. (Extract 1, lines 22 and 23)

(12)

GDP growth refers to an increase in output. One of the reasons that the Ghanaian GDP growth did not achieve its targeted level of growth could be due to high rate of inflation. Extract 1 indicates that the inflation rate is at a three-year high of 11.9%. Therefore, the goods produced would be at a disadvantage as price would be less competitive ~~both~~ internationally. In turn, there would be a fall in demand causing less outputs to be produced. This would also affect the domestic market because they are not able to afford imported goods. Hence, they would have no choice but to consume less goods causing demand to fall further.

Furthermore, it could also be that the ~~the~~ Ghanaian government has accumulated a huge amount of public sector debt. ~~The~~ ~~represente~~ debt represents 50% of the country's GDP. This would usually mean that the government would have to cut spending on other areas in order to service the debt before it worsens any further. As a result, ~~it affect~~ less is being ~~spend~~ spent on the provision of healthcare and education or improvement in infrastructure. This could lead to a less skilled and unhealthy workforce which would deter growth.

~~It~~ Moreover, it may also be due to lack of foreign direct investment. It could be possible that foreigners are less confident in investing into the country because of the recent credit rating ~~of~~ ~~+~~ from B+ to B. Investors usually take into account economic stability when investing. Hence, this would deter investors from investing into Ghana which in turn prevents further growth of the economy.

However, the depreciation of the ~~the~~ currency should offset the high rate of inflation. A depreciation in the currency would mean that exports will seem artificially cheaper while imports more expensive. Therefore, there would be an increased demand from both the international and domestic market.

Also, there might be high trade barriers in ~~different~~ ~~exp-~~ ~~to~~ ~~the~~ importing countries such as tariffs or quotas.

This would either increase the cost to producers by having to pay tariffs or restrict the amount being exported. Also, in

to pay tariffs or restrict the amount being exported. Also, in developed countries such as the US, the government subsidises the agricultural produce of the farmers so it will become more price competitive. As a result, farmers in Ghana would not be able to compete at that price level.



## ResultsPlus

### Examiner Comments

This response earned 9/12 marks: comprised of a Level 3 score for KAA (7 marks) and a Level 1 score for evaluation (2 marks).

In the first paragraph, the candidate identifies one possible cause: the high rate of inflation. The response then explains that this might damage the international price competitiveness of Ghana's goods, but does not link this to the lower than originally forecast economic growth. The remainder of this paragraph is rather confused, as the candidate incorrectly writes that imported goods would become less affordable.

However, the second, third and fifth paragraphs contain additional possible causes which are explained in more detail and applied to context. Taken together, these are sufficient for a Level 3 score for KAA.

There is only one evaluative point, which is in the fourth paragraph. This is a correct point which is supported by some economic reasoning, but as there is only one evaluative comment the candidate is limited to a maximum of 2/4 marks for evaluation.

(b) Discuss why Ghanaian 'GDP growth for 2013 is now expected to be closer to 7% than the 8% that was forecast'. (Extract 1, lines 22 and 23)

(12)

This could be due Ghana government are starting to implement fiscal policy like, such as reducing government expenditure and increasing tax rate.

Reducing government expenditure indicates that lesser to public sector is not the amount of such as decrease in subsidies for firm to reduce cost of production. As government spending and investment of firms is a component of aggregate demand (AD), when government spending and investment decrease, it will shift AD to left therefore for in growth GDP growth is lesser than expected.



Lastly, Ghanaian ~~the~~ <sup>have</sup> low confidence with ~~their own~~  
the market therefore decrease spending <sup>in</sup> ~~and~~ which ~~leads~~ leads to slow growth.



## ResultsPlus

### Examiner Comments

This is an example of a response which is really explaining why Ghana may have had negative economic growth, as opposed to growth of 7% rather than the 8% originally forecast.

The candidate assumes that total aggregate demand has fallen, rather than individual components of aggregate demand falling, or not rising as quickly as had been expected.

Several possible causes of the slower than expected growth are identified - contractionary fiscal policy and low consumer confidence - but the explanations of these are really limited to the candidate identifying government spending and consumption as components of aggregate demand. The disincentive effect of higher income tax rates is not explained in relation to its possible effect on economic growth. This limits the candidate to a Level 1 score for KAA and was awarded 3 marks.

There is no attempt at evaluation, and therefore a Level 0 score of 0 marks was given for evaluation, making a total score of 3/12.

## Question 5 (c)

This was a relatively straightforward question which candidates could interpret narrowly, and write about how a cut in subsidies might improve Ghana's fiscal position, or more broadly, and analyse the likely effects of the cut in subsidies on the country's economy more generally. There were many opportunities for data reference and so most candidates were able to pick up the application marks and the identification marks. Stronger candidates were able to also gain some or all of the available analysis marks.

When considering the likely effects of the cut in subsidies, either positive effects (free market arguments) or negative effects (interventionist arguments) were rewarded, that is candidates could assume that the cut would improve competitiveness and efficiency in the fuel and utility industries and explain the positive effects of this, or they could assume that the price of fuel and utilities would rise fully by the amount of the subsidy cut and consider the possible effects of this on consumers, firms and the government.

It was pleasing to see a good number of candidates considering the possible effects of the cut in subsidies on both the supply and demand sides of the economy.

(c) Analyse the likely impact of 'cuts in fuel and utility subsidies' as a means of reducing Ghana's fiscal deficit. (Extract 1, lines 33 and 34)

(8)

Cuts in fuel and utility subsidies implies that the government is cutting back on spending. A fiscal deficit refers to government spending being greater than government revenue from taxation. Thus, a fall in government spending will lead to an ~~increase in the~~ improvement of the fiscal deficit.

When fuel and utility subsidies are taken away, industries which have been relying on these subsidies will be severely affected. Their cost of production will now increase drastically and they will have to pass this on to the consumers in the form of higher prices. Consumers have to pay higher prices for these goods and thus, experience a fall in consumer welfare.

However, this may not necessarily be the case if these industries were not overly dependent on these subsidies. If these industries were operating efficiently without the subsidies and continue to operate efficiently even with the subsidies, they would have been able to expand their capital base. Thus, the removal of the subsidy will not affect them drastically.



**ResultsPlus**

**Examiner Comments**

This response scored 4/8 marks.

This response identifies two likely impacts of the cuts in subsidies: an improvement in the fiscal deficit and a fall in consumer welfare (1+1). The second of these is explained through the effect of the cuts on production costs and hence prices. This linked explanation earned 2 analysis marks.

Note that the third paragraph is evaluative, which is not required in an 'analyse' question. There is no data reference, meaning that this response does not earn the 2 available application marks.

→ unemployment

→ decrease in  $\pm$

(c) Analyse the likely impact of 'cuts in fuel and utility subsidies' as a means of reducing Ghana's fiscal deficit. (Extract 1, lines 33 and 34)

(8)

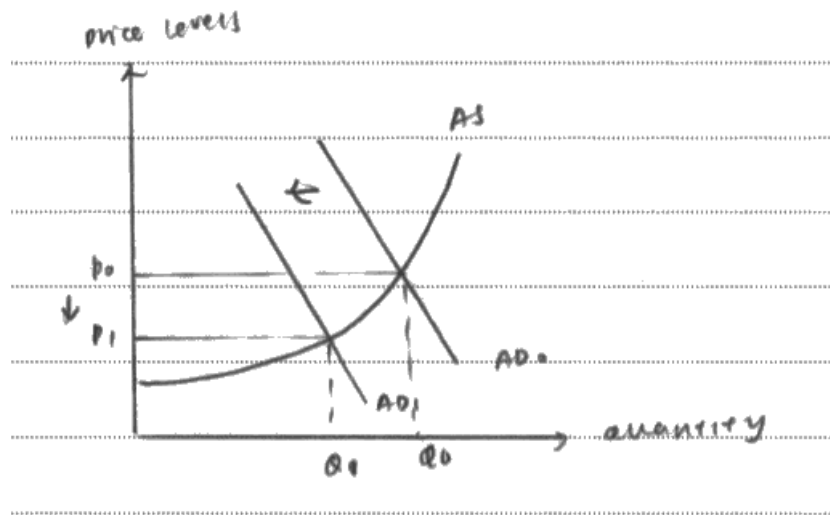
Extract 1 mentions new corporate taxes have been introduced, ~~and~~ subsidies are cut further and public sector wage bill is reduced to control the fiscal deficit.

The cut in fuel and utility subsidies will cause the cost of production of firms to increase. As such, firms will react by ~~cutting~~ <sup>reducing</sup> production and retrench workers in order to maintain profits as cost per unit has increased. This will cause ~~a fall~~ an increase in unemployment levels which leads to ~~a~~ a decrease in income levels. As disposable income reduced, consumers are likely to reduce consumer spending and saving their money in banks. This means there is a leakage in the circular <sup>flow of</sup> income, causing economic activity to slow down.

Firms will also reduce their investments as their profits have decreased. As investments in capital reduced, this also reduces the capital to labour ratio, decreasing the overall productivity of the economy.

The firm will then <sup>be</sup> unable to compete in the international market, <sup>further</sup> reducing profits of the firms. ~~As~~ This will also cause a trade deficit in the balance of payments as exports are now reduced.

As consumer spending <sup>(C)</sup> and investments <sup>(I)</sup> are ~~components~~ components of the AD. A decrease in ~~C~~ <sup>(C)</sup> and <sup>(I)</sup> will lead to a decrease in aggregate demand, reducing economic growth.



## ResultsPlus

Examiner Comments

This response begins with an attempt at data reference, however this does nothing more than repeat the question and mention tax increases which are irrelevant here. This means that the 2 available application marks were not awarded.

From this, however, the candidate does go on to identify and analyse two likely impacts of the subsidy cuts in a very good level of detail, building chains of economic reasoning. In the second paragraph, the likely effect on unemployment and hence income levels and consumption is explained (1 identification mark + 3 analysis marks), while in the third paragraph the impact on firm investment is considered (1 identification mark + 1 analysis mark). These two effects are then brought together. Therefore this response scored 6/8 marks.



## Question 5 (d)

This question worked well as a discriminator at all grades. Weaker candidates tended not to grasp the fact that the question was about 'national debt', rather than the 'fiscal deficit', and focused their responses solely on the need for the government to reduce government spending and raise taxes, and the possible effects that this might have on the economy. This tended to limit them to Level 1 or low Level 2 marks for KAA.

Stronger candidates wrote explicitly about national debt, and were able to consider more complex ideas from Unit 4 of the specification, such as the possible implications for crowding out, intergenerational equity, Ghana's credit rating and the impact on its attractiveness to inward FDI, for example.

Some very strong responses were able to show wider knowledge of contemporary economic events by suggesting that in the context of the current European sovereign debt crisis, a national debt equivalent to 50% of GDP would not be considered high, or, perhaps more relevantly, in the context of other Sub-Saharan African countries, would be unlikely to meet the requirements for the HIPC initiative and therefore may be relatively of less significance. More generally, weaker candidates found this a very difficult question to effectively evaluate their responses, while stronger candidates were able to differentiate themselves through showing this skill.

(d) Assess the significance of the size of Ghana's **public sector debt** as a proportion of its GDP.

(16)

As ~~g~~ Ghana's public sector debt increases, Ghana must take ~~most~~ austerity measures to service the debt. These measures include cutting subsidies and introducing new corporate taxes. These increases the cost of production for firms and may cause the price of goods in Ghana to increase. This leads to inflation cost push inflation. Firms may also cut back by retrenching workers which would lead to greater unemployment in Ghana. This restricts growth.

However, this depends on the government's previous expenditure on capital. If Ghana had spent enough on improving capital, the increase in productivity could lead to long term growth in Ghana, which may allow it to then service the debt.

A large public sector debt would also be a deterrent deterrent for foreign investors. Foreign investors may decide it too risky to invest in Ghana, as indicated in Extract 1, lines 9-10. Ghana's credit rating has been downgraded from B+ to B. If foreign investment stops, they will ~~take~~ withdraw their capital as well, so Ghana would be faced with a savings gap as it is unable to accumulate capital on its own, so growth is limited.

It should be noted that this would be significant as Ghana greatly relies on foreign direct investment to provide its capital. Thus a loss in investor confidence would be detrimental.

As public sector debt increases, Ghana's government will be forced to cut back on government expenditure to service the debt. This may cause the loss of jobs since many jobs are created with government spending. Thus, unemployment in Ghana will rise.

In addition, a larger public sector debt would result in a greater amount of interest payments for that debt.

If the debt and its interest become too great, Ghana may not be able to sustain it. Ghana may be stuck with servicing the <sup>sizeable</sup> interest without servicing the original debt, so the cost for of the debt keeps growing.

However, if Ghana's debt is cyclical debt and not structural debt, Ghana may be able to repay the debt when its economy experiences an upturn with greater growth.

A large public sector debt also indicates a large ~~degree~~<sup>amount</sup> of government borrowing. This may lead to a crowding out effect as the government and firms compete for the same funds. This raises interest rates for credit and may adversely affect investment spending of firms.



## ResultsPlus

Examiner Comments

This response scored 10/16 marks in total, comprised of a Level 3 score for KAA (7 marks) and a Level 1 score for evaluation (3 marks).

The candidate identifies and analyses a range of points including the likely implications for fiscal policy, and the effects on FDI and crowding out. There is some repetition of points, as the candidate comes back to the need for fiscal austerity to service the debt in three separate paragraphs. That said, there is a range of points considered and explained, with appropriate reference to context, making this response worthy of a Level 3 mark.

The evaluative content in this response is less strong. Points are identified but supported by very little, if any, economic reasoning. For example, the points at the top of the second and third pages are only identified. Additionally, the penultimate paragraph on the second page contains a confusion between national debt and fiscal deficit.

(d) Assess the significance of the size of Ghana's **public sector debt** as a proportion of its GDP.

(16)

According to the Extract, Ghana's public sector debt is 50% of its GDP. This is a relatively huge percentage of the country's overall economy & GDP. This can deter the growth rate of Ghana's economy.

With such a large debt in its hands, Ghana is unable to use ~~for~~ capital attained to improve its infrastructure ~~and so on~~ healthcare & education. This is because the government have to know use the funds to pay back creditors instead of improving its economy. This will hinder growth due to lack of human capital because education & healthcare is not prioritized. When this happens, productivity decreases and price of goods increases due to inefficiency. Consumers now have to pay for a higher priced good, decreasing their surplus & welfare. Lack of education & training will also increase the unemployment rate as they ~~are occupation~~ have no skills whatsoever to work in the market. This again ~~de~~ limits growth.

Moreover, with such a huge amount of public sector debt, MNC might not be attracted. This is because MNC are constantly searching for risk-free countries to start up their businesses. Due to its huge debts, Ghana might impose higher taxes onto both consumers & producers. This will provide the government with revenue to pay off its debt but at the risk of low investment & consumption from firms & consumers. This will limit growth again. MNCs do not prefer high tax as well due to low rate of returns.



**ResultsPlus**  
**Examiner Comments**

This response was awarded 5/16 marks, comprised of a Level 2 score for KAA (5 marks) and a Level 0 score for evaluation (0 marks).

The candidate identifies and analyses two good points as to the likely significance of Ghana's national debt, but in the second and third paragraphs there is no reference to context beyond the candidate writing 'Ghana'. For a Level 3 score for KAA there needs to be appropriate reference to context throughout the response.

There is no evaluation in this response so no marks can be awarded for evaluation. As the crossed out work on the second page was not replaced it was marked, but was not sufficient to earn any evaluation marks.



## Paper Summary

Based on their performance on this paper, candidates are offered the following advice:

- Candidates must read the questions carefully. In a number of different questions on this paper, misreading or misinterpreting the question was the biggest reason for low scores. Candidates should pay particular attention to key terms in questions, and to the use of bold font which is provided to help them to interpret questions correctly.
- In response to the 4 mark questions in Section B, candidates must be aware of the difference between a definition (knowledge) and an example (application). This was an issue particularly in question 5(a) on this paper, where candidates provided examples of government current and capital expenditure instead of defining these terms.
- Whilst it is very positive that candidates are reading the data provided in Section B carefully and attempting to use it in their responses, they should be discouraged from copying out large chunks of the data, or writing answers which predominantly contain quotations from the Extracts. Candidates should remember that application is only one of the four assessment objectives. Where an Extract contains a large amount of relevant content, candidates may need to be selective when deciding which parts to incorporate into their responses. In the higher mark questions in particular, the data should be used more to support a candidate's own knowledge, analysis and evaluation, not in place of it. Data is likely to be useful to provide evidence for a point already made, or to give examples of it. Where points themselves are taken from the data, candidates must provide their own economic analysis of them.
- In the 16 mark questions in Section B, candidates should remember that half of the available 16 marks are awarded for evaluation. Currently many candidates are not placing enough weight upon this assessment objective in their responses. Additionally, to receive higher marks for evaluation, the key is the extent to which points are developed - the chains of economic reasoning which are built - rather than the number of points which are identified.

## **Grade Boundaries**

Grade boundaries for this, and all other papers, can be found on the website on this link:

<http://www.edexcel.com/iwantto/Pages/grade-boundaries.aspx>



Ofqual  
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