



Oxford Cambridge and RSA

Thursday 18 May 2023 – Morning

A Level Economics

H460/01 Microeconomics

Time allowed: 2 hours



You can use:

- a scientific or graphical calculator



Please write clearly in black ink. **Do not write in the barcodes.**

Centre number

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 Candidate number

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First name(s) _____

Last name _____

INSTRUCTIONS

- Use black ink. You can use an HB pencil, but only for graphs and diagrams.
- Write your answer to each question in the space provided. If you need extra space use the lined pages at the end of this booklet. The question numbers must be clearly shown.
- Answer **all** the questions in Section A, **one** question in Section B and **one** question in Section C.

INFORMATION

- The total mark for this paper is **80**.
- The marks for each question are shown in brackets [].
- Quality of extended response will be assessed in questions marked with an asterisk (*).
- This document has **20** pages.

ADVICE

- Read each question carefully before you start your answer.

SECTION A

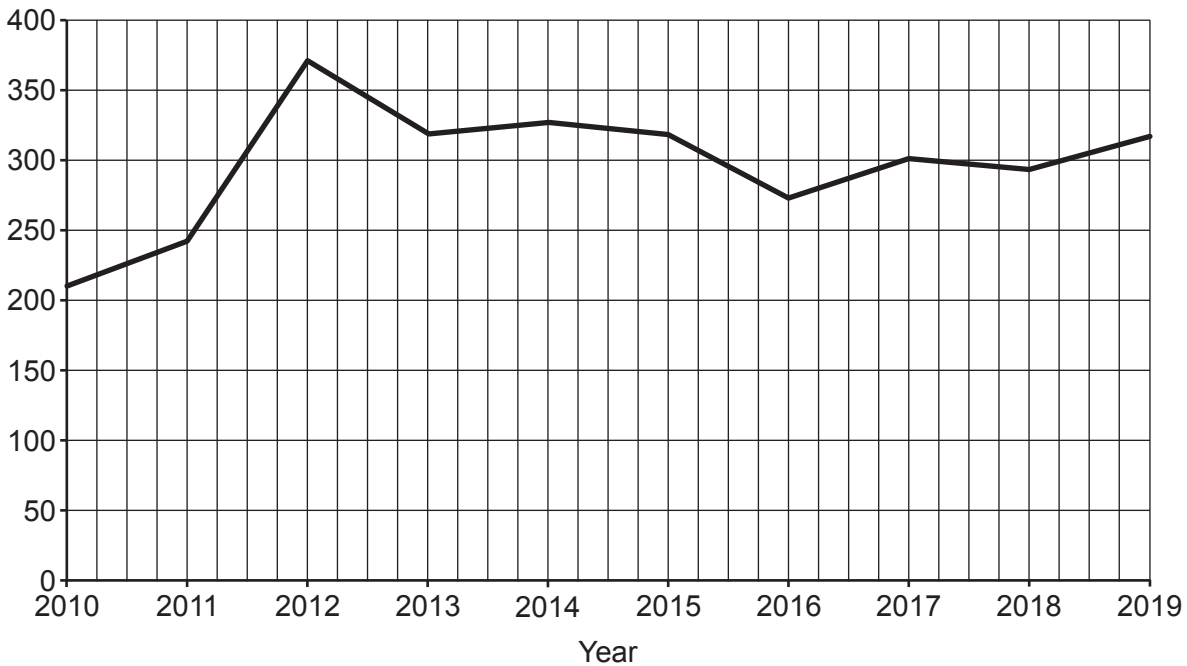
Read the stimulus material and answer **all** the parts of Question 1.

Wage differentials in the USA

Research shows the ratio of Chief Executive pay ('remuneration') to employee remuneration in the USA has increased significantly since 2010 (see **Fig. 1**). In 2019, Chief Executives at the largest 350 firms in the USA earned 320 times more than a typical employee.

Fig. 1

Chief Executive-to-employee remuneration ratio (USA), 2010–2019



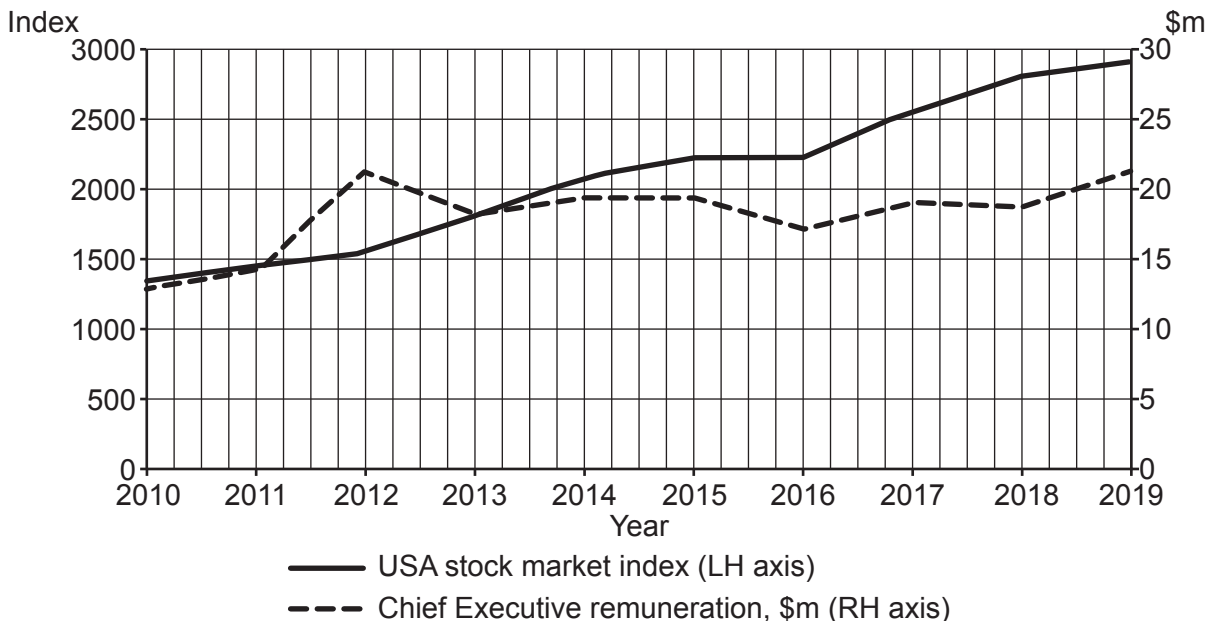
Source: Economic Policy Institute

Chief Executives earned an average of \$21 million in 2019, a 14% increase since 2018. In that year, the US stock market price index, which shows changes in the share prices of US companies also rose (see **Fig. 2**).

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Fig. 2

Chief Executive remuneration and stock market performance (USA), 2010–2019



Source: Economic Policy Institute

This growth in Chief Executive remuneration has happened while wage growth for most Americans has remained relatively low. To distract attention from their remuneration, some Chief Executives have taken a voluntary cut in salary. However, this approach is criticised as much of their remuneration comes from share options (the right to buy shares at set prices) and bonuses. Other policies that may help reduce the remuneration gap between Chief Executive and employee have been suggested, including: 10

- reinstating a higher marginal income tax rate at the very top income levels;
- setting corporation tax rates higher for firms that have higher ratios of Chief Executive-to-employee remuneration; 15
- allowing greater use of 'say on pay' which allows a firm's shareholders to vote on Chief Executive remuneration.

Society is increasingly recognising who are the essential workers. They harvest our food, stock our grocery shelves and deliver goods all over the country. They look after our children and care for us when we are ill. They are also amongst the lowest-paid workers in the country. Why is this? And, in contrast, why are relatively non-essential jobs, in such areas as entertainment and sport, so well paid? 20

The answer to these questions is not clear. The traditional economics answer would be to consider the concepts of demand and supply. Many of the essential occupations are easy to enter. For example, a cleaner might not require specialist knowledge or training. 25

A different answer could be 'scalability'. A cleaner, however skilled at their job, can only clean one building at a time. However, an entertainer can provide value to millions of people at the same time, thanks to television or the Internet. In many jobs, such as those in entertainment or sport, it is difficult to measure marginal physical productivity and so pay is set in a seemingly random way, often based on power. 30

This 'power differential' is a new area of research to explain wage differentials. This suggests that skill levels are not good predictors of wage levels, as there are big differences in wage between workers who do the same job.

In the USA, business leaders and politicians have worked together to weaken trade unions, oppose minimum wage legislation and remove labour market restrictions. Marshall Steinbaum, an economist at the University of Utah, suggests that the decline in workers' rights and bargaining power of trade unions alongside the greater power of employers is the main reasons for growing wage differentials. He says that "[The power] American bosses have to dictate take-it-or-leave-it terms to workers is the core reason our 'essential' workforce are underpaid." 35

Source: Adapted from *The Washington Post* (6/4/20) & *Pressenza* (19/8/20)

1 (a) Refer to Fig. 2.

(i) Describe the relationship between Chief Executive remuneration and stock market performance between 2010 and 2019.

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..... [2]

(ii) Explain why this relationship may exist.

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..... [2]

(b) A marginal income tax rate is one example of the marginal principle used by economists.

Explain what is meant by the economic concept of 'the margin'.

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..... [2]

(c) Explain, using an appropriate diagram, the size of economic rent relative to transfer earnings for essential workers such as cleaners. **Lines 23–25.**

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..... [4]

(d) A number of policies have been suggested to affect Chief Executive remuneration including 'Allowing greater use of 'say on pay' which allows a firm's shareholders to vote on Chief Executive remuneration,' **Lines 16–17**.

Evaluate, using evidence from the stimulus material, the extent to which greater use of 'say on pay' alone may help reduce the remuneration gap between Chief Executive and employee in the US.

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SECTION B

Answer Question 2 or Question 3.

- 2* In 2020, the Competition and Markets Authority (CMA) found that three pharmaceutical companies had taken part in an illegal agreement resulting in the price of a life-saving medicine supplied to the NHS increasing by up to 1800%. This was one of many examples investigated by the CMA where consumers were being disadvantaged by collusion and the actions of monopolies.

Evaluate, using an appropriate diagram(s), whether collusion and monopoly would always disadvantage consumers.

[25]

OR

- 3* A report for the charity Action on Smoking and Health (ASH) in January 2022 estimated that smoking in England imposed costs on the NHS totalling £2.4 billion and costs on businesses, from lost productivity, of £17.2 billion.

Evaluate, using an appropriate diagram(s), the most effective method of government intervention to reduce the negative externalities from smoking in England. [25]

Question No.

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SECTION C

Answer Question 4 or Question 5.

- 4* Flood defences are considered by economists to be public goods. The £67.4 million Ipswich tidal flood barrier is just one of the many flood defence schemes which has been completed during the government's current capital investment programme. The scheme protects 1600 homes and 400 businesses from tidal flooding.

Evaluate the case for government provision of goods and services such as the Ipswich flood defence scheme. [25]

OR

- 5* Aldi, a discount supermarket, entered the UK market for the first time in 1990. Since then it has expanded its operation and, in 2022, its market share was 9.3% making it the fourth largest supermarket in the UK.

Evaluate the importance of economies of scale to a large retailer when deciding whether to increase the size of its firm. [25]

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END OF QUESTION PAPER

ADDITIONAL ANSWER SPACE

If additional space is required, you should use the following lined page(s). The question number(s) must be clearly shown in the margin(s).

This section of the page is a large, empty area for writing answers. It consists of a vertical solid line on the left side, creating a margin, and a series of horizontal dotted lines extending across the page to the right. The dotted lines are spaced evenly, providing a guide for writing.



A large area of the page is reserved for writing, featuring a vertical solid line on the left side and horizontal dotted lines extending across the page.



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