



General Certificate of Education

Advanced Extension Award

Economics 6841

Mark Scheme

2005 examination - June series

Mark schemes are prepared by the Principal Examiner and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation meeting attended by all examiners and is the scheme which was used by them in this examination. The standardisation meeting ensures that the mark scheme covers the candidates' responses to questions and that every examiner understands and applies it in the same correct way. As preparation for the standardisation meeting each examiner analyses a number of candidates' scripts: alternative answers not already covered by the mark scheme are discussed at the meeting and legislated for. If, after this meeting, examiners encounter unusual answers which have not been discussed at the meeting they are required to refer these to the Principal Examiner.

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of candidates' reactions to a particular paper. Assumptions about future mark schemes on the basis of one year's document should be avoided; whilst the guiding principles of assessment remain constant, details will change, depending on the content of a particular examination paper.

Advanced Extension Award (AEA)

This Mark Scheme covers the Advanced Extension Award that AQA offers on behalf of all awarding bodies

June 2005

6841

AQA ADVANCED EXTENSION AWARD

Mark Scheme

Section A (Data Response Question)

Different parts of **Question 1** are marked in different ways.

Parts (a) and (b) are marked using a ‘points’ marking scheme. Candidates are rewarded for the relevant points identified and their ability to develop the points they make.

Parts (c), (d) and (e) are marked using the ‘Levels of Response Mark Band Descriptors’ given on the next page. Marks should be awarded according to whether the answer demonstrates the skills indicated in the grid on the next page. Marks are to be allocated for:

- Knowledge and Understanding
- Application
- Analysis
- Synthesis and Evaluation

When marking the candidate’s answer, the examiner must indicate where evidence of each of the four skills is demonstrated by using the following key:

K	Knowledge and Understanding
Ap	Application
A	Analysis
E	Synthesis and Evaluation

Each answer will be marked holistically and the level chosen will be the one which **best fits** the answer provided by the candidate.

The mark scheme for the individual parts of the data response question summarises the information, issues and economic ideas that candidates are likely to include in their answers.

Levels of Response Mark Band Descriptors (Question 1: Data Interpretation)		
Level 3	<p>The candidate demonstrates an in-depth knowledge and understanding of relevant economic concepts and theories throughout and applies them with precision and confidence.</p> <p>The candidate selects and uses a variety of appropriate theories and models to analyse problems and issues. An awareness of the inter-relatedness of economic ideas is shown.</p> <p>The candidate effectively synthesises complex information and ideas and constructs coherent arguments to reach well-reasoned, supported judgements and conclusions.</p> <p>The candidate is able to demonstrate the value and limitations of more complex economic concepts and theories and an understanding of the tentative nature of explanations.</p> <p>Complex information and ideas are communicated in a highly effective manner making use of the most appropriate form and style.</p>	<p>14 – 20 marks</p> <p><i>Mid-point 17</i></p>
Level 2	<p>The candidate demonstrates sound knowledge and understanding of most of the economic concepts and theories employed to help answer the question and applies them effectively.</p> <p>The candidate selects and uses appropriate theories to analyse problems and issues. An awareness of the inter-relatedness of economic ideas is shown.</p> <p>The candidate synthesises information and ideas and constructs coherent arguments to reach reasoned judgements and conclusions.</p> <p>The candidate is able to demonstrate the value and limitations of economic concepts and theories and an awareness of the tentative nature of explanations.</p> <p>Complex information and ideas are communicated effectively in an appropriate form and style.</p>	<p>10 – 13 marks</p> <p><i>Mid-point 12</i></p>
Level 1	<p>The candidate makes use of relevant economic concepts and theories but understanding is sometimes confused or incomplete. Some ability to apply economic concepts to the question is demonstrated.</p> <p>The candidate selects appropriate economic theories and shows some ability to use these theories to analyse problems and issues. However the analysis is sometimes confused.</p> <p>The candidate shows some ability to construct a coherent argument to reach judgements and conclusions.</p> <p>Some appreciation of the value and limitations of economic concepts and theories may be demonstrated but little awareness of the tentative nature of economic explanations will be shown.</p> <p>Straightforward information and ideas are expressed clearly with some appreciation of an appropriate form and style.</p>	<p>1 – 9 marks</p> <p><i>Mid-point 5</i></p>

Sections B and C (Essay Questions)

The essay questions in Sections B and C (**Questions 2 – 5**) are marked using the levels of response mark band descriptors given on the next page. Marks should be awarded according to whether the answer demonstrates the skills indicated in the grid on the next page. Marks are to be allocated for:

- Knowledge and Understanding
- Application
- Analysis
- Synthesis and Evaluation

When marking the candidate's answer, the examiner must indicate where evidence of each of the four skills is demonstrated by using the following key:

K	Knowledge and Understanding
Ap	Application
A	Analysis
E	Synthesis and Evaluation

Each answer will be marked holistically and the level chosen will be the one which **best fits** the answer provided by the candidate.

The mark scheme for the individual questions summarises the information, issues and economic ideas that candidates are likely to include in their answers.

Levels of Response Mark Band Descriptors (Questions 2 – 5: Essay Questions)		
Level 3	<p>The candidate demonstrates an in-depth knowledge and understanding of relevant economic concepts and theories throughout and applies them with precision and confidence.</p> <p>The candidate selects and uses a variety of appropriate theories and models to analyse problems and issues. An awareness of the inter-relatedness of economic ideas is shown.</p> <p>The candidate effectively synthesises complex information and ideas and constructs coherent arguments to reach well-reasoned, supported judgements and conclusions.</p> <p>The candidate is able to demonstrate the value and limitations of more complex economic concepts and theories and an understanding of the tentative nature of explanations.</p> <p>Complex information and ideas are communicated in a highly effective manner making use of the most appropriate form and style.</p>	<p>28 – 40 marks</p> <p><i>Mid-point 34</i></p>
Level 2	<p>The candidate demonstrates sound knowledge and understanding of most of the economic concepts and theories employed to help answer the question and applies them effectively.</p> <p>The candidate selects and uses appropriate theories to analyse problems and issues. An awareness of the inter-relatedness of economic ideas is shown.</p> <p>The candidate synthesises information and ideas and constructs coherent arguments to reach reasoned judgements and conclusions.</p> <p>The candidate is able to demonstrate the value and limitations of economic concepts and theories and an awareness of the tentative nature of explanations.</p> <p>Complex information and ideas are communicated effectively in an appropriate form and style.</p>	<p>20 – 27 marks</p> <p><i>Mid-point 24</i></p>
Level 1	<p>The candidate makes use of relevant economic concepts and theories but understanding is sometimes confused or incomplete. Some ability to apply economic concepts to the question is demonstrated.</p> <p>The candidate selects appropriate economic theories and shows some ability to use these theories to analyse problems and issues. However the analysis is sometimes confused.</p> <p>The candidate shows some ability to construct a coherent argument to reach judgements and conclusions.</p> <p>Some appreciation of the value and limitations of economic concepts and theories may be demonstrated but little awareness of the tentative nature of economic explanations will be shown.</p> <p>Straightforward information and ideas are expressed clearly with some appreciation of an appropriate form and style.</p>	<p>1 – 19 marks</p> <p><i>Mid-point 10</i></p>

1

Total for this question: 80 marks

- 1 (a) Explain the relationship shown in **Extract A** between the UK's public sector net cash requirement (PSNCR) and public sector net debt. *(10 marks)*

Extract A shows the PSNCR and public sector debt as proportions (percentages) of GDP. Candidates should not be penalised for explaining the relationship between absolute sizes of PSNCR and debt, though additional marks are available for stating that the data does not illustrate absolute sizes.

For candidates who:

- state the meaning of the PSNCR: **2 marks**
- relate the PSNCR to the public sector's or the government's budget deficit or to a borrowing requirement: **2 marks**
- state the meaning of the public sector net debt: **2 marks**
- state that the PSNCR is a flow: **1 mark**
- state that the public sector debt is a stock: **1 mark**
- state that a positive PSNCR (or a flow of new borrowing) increases the size of the public sector debt (or stock of debt) or state that the relationship is positive: **up to 4 marks**
- explain that this is the relationship Extract A illustrates: **up to 3 marks**
- use statistics from Extract A as evidence: **1 mark per relevant statistic, up to a maximum of 4 for statistics**

- explain that Extract A shows the PSNCR and public sector debt as proportions of GDP, and not the absolute sizes of the PSNCR and the public sector debt: **1 mark**

- explain that it is not possible to identify (directly) a relationship between changes in absolute size: **1 mark**

**Maximum of 4 marks if no attempt is made to explain a relationship
Maximum of 7 marks if no use is made of relevant statistics**

UP TO AN OVERALL MAXIMUM OF 10 MARKS

1 (b) Lines 5-6 of **Extract B** state that “serious mistakes in fiscal policy can occur if purely cyclical improvements are treated as if they were structural, or if a structural deterioration is interpreted as cyclical”. Explain this statement. (10 marks)

For candidates who:

explain that the question is referring to cyclical and structural changes in budgetary positions (deficits or surpluses), or borrowing requirements: **up to 2 marks**

explain the meaning of the cyclical component of a budget deficit (or surplus) or the borrowing requirement: **up to 2 marks**

explain the meaning of the structural component of a budget deficit (or surplus) or the borrowing requirement: **up to 2 marks**

explain a reason why a cyclical improvement in fiscal policy may occur, eg increases in tax revenues, lower spending on unemployment benefits, automatic stabiliser effects: **up to 2 marks per reason
up to a maximum of 4 marks**

explain a reason why a structural deterioration in fiscal policy may occur, eg because of an ageing population, deindustrialization, MNCs paying taxes in other countries: **up to 2 marks per reason
up to a maximum of 4 marks**

explain a reason why a mistake in fiscal policy can occur if a purely cyclical improvement is treated as if it is structural, eg the government may reduce spending on the structure of the economy when there is no case for doing so: **up to 2 marks per reason
up to a maximum of 4 marks**

explain a reason why a mistake in fiscal policy can occur if a structural deterioration is treated as if it is cyclical, eg the government may destabilise rather than stabilise the economic cycle: **up to 2 marks per reason
up to a maximum of 4 marks**

explain the statement in the context of the ‘golden rule’: **up to 2 marks**

explain at least one example of cyclical change in the economy: **1 mark**

explain at least one example of structural change in the economy: **1 mark**

Maximum of 8 marks if the answer considers only a cyclical improvement or a structural deterioration.

UP TO AN OVERALL MAXIMUM OF 10 MARKS

- 1 (c) Assess the view that “macroeconomic equilibrium is best secured through free market forces operating in competitive markets, rather than through government policies to manage aggregate demand” (**Extract C**, lines 13-15). (20 marks)

Candidates should explain how free market forces might achieve macroeconomic equilibrium, and also explain how government policies to manage aggregate demand might achieve macroeconomic equilibrium. They should then discuss the advantages and disadvantages of each method of securing macroeconomic equilibrium, before coming to a justified conclusion as to which provides the best basis for a government’s macroeconomic policy. Advantages of free market forces achieving macroeconomic equilibrium include: the automatic nature of the process; economic agents making free choices unconstrained by government interference. Disadvantages include: it may lead to market failure; the process may take too long. Advantages of government policies to manage aggregate demand achieving macroeconomic equilibrium include: stabilising inherently unstable free markets; prevention of market failure. Disadvantages include: destabilising effects; government failure; the promotion of harmful ‘big government’.

Issues, analysis and areas for discussion include:

- The meaning of macroeconomic equilibrium
- How market forces might achieve macroeconomic equilibrium
- The significance of competitive markets
- Application of relevant macroeconomic analysis, eg AD/AS analysis
- How the natural level of output, employment and unemployment may be achieved
- How policies to manage aggregate demand might achieve macroeconomic equilibrium
- Relevant discussion of fiscal policy and/or monetary policy
- Relevant discussion of supply-side policy
- Market failure arguments
- Government failure arguments
- Assessment of strengths and weaknesses of opposing arguments

Candidates should be rewarded for using diagrams to support their analysis.

Use the Levels of Response Mark Band Descriptors (Data Interpretation) to award marks for this question.

UP TO AN OVERALL MAXIMUM OF 20 MARKS

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|--|
| 1 (d) Assess the view that taxes are too high in the United Kingdom and that the government should reduce taxation as a proportion of GDP. (20 marks) |
|--|

The question does not require that the candidates use the data, but good answers are likely to make use of the information in Extract E. This shows tax revenue fluctuating between about 39% and 33% of GDP. Good answers might explain why governments impose taxes, perhaps drawing on Extract A, the disadvantages of too high an overall rate of taxation, and the disadvantages of too high a rate of income tax, and/or other taxes.

Issues, analysis and areas for discussion include:

- The reasons why government impose taxes
- Taxes used to correct market failure
- The adverse effect of taxes on incentives
- Crowding out arguments
- The disadvantages of ‘big government’
- Inefficiency and waste
- Taxation and government failure
- The optimal level of taxation
- The Laffer curve
- Consideration of particular taxes
- The effect on the UK’s competitiveness in world markets
- Assessment of strengths and weaknesses of opposing arguments

Candidates should be rewarded for using diagrams to support their analysis.

Maximum of 13 marks if the candidate has not answered both parts of the question.

Use the Level Response Mark Band Descriptors (Data Interpretation) to award marks for this question.

UP TO AN OVERALL MAXIMUM OF 20 MARKS

- 1 (e) Discuss the case **for** and **against** setting up a fiscal policy commission to assist in the implementation of fiscal policy in the UK. (20 marks)

Extract F outlines the possible role of a fiscal policy commission, and relates such a commission to the perceived success of the Bank of England's Monetary Policy Committee in controlling inflation. The Extract argues that a fiscal policy commission should *assist* the government in implementing fiscal policy, but the government would still be mostly responsible for fiscal policy. Good candidates will probably distinguish between *assistance* and *replacement* of the government's role in implementing fiscal policy. Weaker candidates may assume that the government's role completely disappears, and that the fiscal policy commission is all powerful.

An answer which considers only arguments for, or the arguments against, must be restricted to a maximum of 13 marks.

Issues, analysis and areas for discussion include:

- The meaning of a fiscal policy commission
- The functions of a fiscal policy commission
- The accountability of a fiscal policy commission
- Whether the government would set a target for the commission to hit
- Can fiscal policy be separated from political decision making?
- Discussion of the role and track record of the Monetary Policy Committee
- Government failure consideration
- Public interest versus public choice theory consideration
- EU issues such as the euro, tax harmonisation, the Stability and Growth Pact
- Assessment of strengths and weaknesses of opposing arguments

Candidates should be rewarded for using diagrams to support their analysis.

Use the Level of Response Mark Band Descriptors (Data Interpretation) to award marks for this question.

UP TO AN OVERALL MAXIMUM OF 20 MARKS

Section B: Markets and Market Failure**2**

- 2 “Government subsidies granted to firms and consumers affect the demand for different goods and services, and generally increase economic welfare.”
Discuss the case **for** and **against** using subsidies to influence the pattern of demand for goods and services. *(40 marks)*

Candidates are expected to explain that a subsidy granted to firms shifts the supply curve of the good or service rightward. They may then explain that the extent to which the quantity bought and sold increases depends on the elasticity of demand for the good. Most candidates should explain and analyse the effects of subsidies given to the producers, but the question also mentions subsidies granted to consumers. In the past, old age pensioners were given ‘butter tokens’, but candidates are not expected to know about this. In some cities, local government provides children and/or pensioners with bus passes, available either free or below the regular price. Subsidies granted to consumers cause the demand curve to shift rightward. Good answers for both scenarios may analyse and evaluate the effects on consumer surplus and producer surplus (or economic welfare). They are also likely to discuss the case for and against subsidising the provision of merit goods.

An answer which considers only the case for, or the case against, must be restricted to a maximum of 27 marks.

Issues, analysis and areas for discussion include:

- The meaning of subsidy
- The nature of subsidies granted to producers
- How consumers are affected by subsidies
- Relevant application of supply and demand analysis
- Relevant application of elasticity
- Relevant analysis of welfare gains and losses
- Relevant analysis of consumer and producer surplus
- Explanation in terms of merit goods
- External benefits and costs
- Government failure considerations
- Equity considerations
- Assessment of the strengths and weaknesses of opposing arguments

Candidates should be rewarded for using diagrams to support their analysis.

Use the Levels of Response Mark Band Descriptors (Essays) to award marks for this question.

OVERALL MAXIMUM OF 40 MARKS

3

3 Evaluate the view that a government's competition policy should be based solely on making markets contestable. (40 marks)

All candidates are expected to display a general understanding of the term *competition policy*, but they are not required to show specific knowledge, current or historical, of UK competition policy. Some good candidates may possess this knowledge and apply it in ways relevant to the question. By contrast, weaker candidates may write purely historical descriptions of UK policy. These should not be rewarded. Candidates are also expected to know the meaning of contestable markets. Good answers will consider the word *solely* in the question, perhaps arguing that, depending on circumstances, a number of strategies may be used, often as complements to each other rather than as substitutes. These include: removing entry barriers and reducing or eliminating sunk costs (both of which promote market contestability), price caps and other forms of regulation, windfalls taxes on monopoly profit, and breaking up established monopolies and preventing mergers that might create monopoly.

Issues, analysis

- The meaning of competition policy
- The meaning of market contestability
- Removal of barriers to entry
- Reduction of sunk costs
- Appreciation that different policy instruments may be used in competition policy
- Explanation and analysis of different policy instruments
- Evaluation of different policy instruments
- Discussion of the possible complementary or substitute relationship between policy instruments
- Assessment of strengths and weaknesses of opposing arguments

Candidates should be rewarded for using diagrams to support their analysis.

Use the Levels of Response Mark Band Descriptors (Essays) to award marks for this question.

OVERALL MAXIMUM OF 40 MARKS

Section C: The National and International Economy**4**

4 In 2002, the UK government estimated that the economy's trend rate of growth had increased from 2.25% a year to 2.75% a year. Evaluate the **benefits** and **costs** that might occur if a higher trend rate of growth is maintained in future years. *(40 marks)*

All candidates are expected to understand the meaning of the trend rate of growth, and to relate it to the business cycle. Good candidates may explain benefits of a higher trend growth rate in terms of virtuous circles, increased competitiveness, and the ability to increase economic welfare and standards of living. They may then go on to explain costs in terms of resource degradation (eg negative externalities such as pollution) and resource depletion (leading perhaps to exhaustion of finite resources). Some candidates may distinguish between growth and development, though this distinction is not covered by all the A Level specifications. Coverage of this distinction should be rewarded, but it is not required.

An answer which considers only the benefits, or only the costs, of a higher trend growth rate must be restricted to a maximum of 27 marks.

Issues, analysis and areas for discussion include:

- The meaning of the trend rate of growth
- The difference between the trend rate of growth and the actual rate of growth
- Diagrams to illustrate the trend rate of growth and the actual rate of growth
- Benefits of a higher trend rate of growth
- Costs of a higher trend rate of growth
- Discussion of the significance of the size of any increase
- Discussion of sustainability
- Discussion of the use of finite resources
- Relation of growth to the business cycle
- Effects of UK growth on other economies, including developing economies
- Assessment of strengths and weaknesses of opposing arguments

Candidates should be rewarded for using diagrams to support their analysis.

Use the Levels of Response Mark Band Descriptors (Essays) to award marks for this question.

OVERALL MAXIMUM OF 40 MARKS

5

5 Between 1 January 2000 and 31 December 2001, the US dollar's exchange rate rose in value against the euro by 14%. Between 1 January 2002 and 31 December 2003, the dollar's exchange rate fell against the euro by 28%.

Discuss the possible **causes** and **effects** of a change in the dollar's exchange rate against the euro.

(40 marks)

All candidates are expected to display a sound knowledge of how exchange rates are determined in a floating exchange rate system. Some candidates will also display knowledge of fixed exchange rates, but only reward such knowledge if it is used in a way relevant to the question. The question is partly about the *consequences* of exchange rate changes. The terms *overvaluation* and *undervaluation* are not used in the question, but good answers may introduce and apply the concepts. Causes of the recent fall in the dollar's exchange rate include the US encouraging capital flows out of the dollar to make American industries competitive. Consequences include, people in other countries enjoying cheap US holidays and importing oil (priced in dollars) and American food, raw materials and industrial goods at lower prices. This reduces inflation outside the USA. However, non-US firms in internationally-traded sectors suffer a loss of competitiveness, not only with the USA, but also against all countries, such as China, that have fixed their currencies against the dollar.

An answer which considers only the causes, or only the effects, of a change in the dollar's exchange rate against the euro must be restricted to a maximum of 27 marks.

Issues, analysis and areas for discussion include:

- The meaning of an exchange rate
- Relevant discussion of floating and fixed exchange rates
- The use of trade theory to explain the causes of rising or falling exchange rates
- The role of different inflation rates in causing rising or falling exchange rates
- Purchasing power parity theory and changes in exchange rates
- The role of capital flows in causing rising or falling exchange rates
- Causes of the rise and fall of the US dollar
- The effect of overvalued and undervalued exchange rates, and overshooting and undershooting
- The favourable and unfavourable effects on the USA
- The effects on the terms of trade
- The favourable and unfavourable effects on Eurozone countries
- Relevant discussion of favourable and unfavourable effects on other countries, eg non-Eurozone countries, developing economies, and countries such as China whose exchange rates have been fixed against the dollar
- Assessment of strengths and weaknesses of opposing arguments

Candidates should be rewarded for using diagrams to support their analysis.

Use Levels of Response Mark Band Descriptors (Essays) to award marks for this question.

OVERALL MAXIMUM OF 40 MARKS