AQA

ASSESSMENT and
QUALIFICATIONS
ALLIANCE

General Certificate of Education

Economics (Advanced Extension Award) 6841

Mark Scheme

2006 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

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June 2006 **6841**

AQA ADVANCED EXTENSION AWARD ECONOMICS

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	The candidate demonstrates an in-depth knowledge and understanding of relevant economic concepts and theories throughout and applies them with precision and confidence. 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. The candidate effectively synthesises complex information and ideas and constructs coherent arguments to reach well-reasoned, supported judgements and conclusions. 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. Complex information and ideas are communicated in a highly effective manner making use of the most appropriate form and style.	**14 – 20 marks** *Mid-point 17*
Level 2	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. The candidate selects and uses appropriate theories to analyse problems and issues. An awareness of the inter-relatedness of economic ideas is shown. The candidate synthesises information and ideas and constructs coherent arguments to reach reasoned judgements and conclusions. The candidate is able to demonstrate the value and limitations of economic concepts and theories and an awareness of the tentative nature of explanations. Complex information and ideas are communicated effectively in an appropriate form and style.	**10 – 13 marks** *Mid-point 12*
Level 1	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. 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. The candidate shows some ability to construct a coherent argument to reach judgements and conclusions. 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. Straightforward information and ideas are expressed clearly with some appreciation of an appropriate form and style.	**1 – 9 marks** *Mid-point 5*

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	The candidate demonstrates an in-depth knowledge and understanding of relevant economic concepts and theories throughout and applies them with precision and confidence. 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. The candidate effectively synthesises complex information and ideas and constructs coherent arguments to reach well-reasoned, supported judgements and conclusions. 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. Complex information and ideas are communicated in a highly effective manner making use of the most appropriate form and style.	**28 – 40 marks** *Mid-point 34*
Level 2	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. The candidate selects and uses appropriate theories to analyse problems and issues. An awareness of the inter-relatedness of economic ideas is shown. The candidate synthesises information and ideas and constructs coherent arguments to reach reasoned judgements and conclusions. The candidate is able to demonstrate the value and limitations of economic concepts and theories and an awareness of the tentative nature of explanations. Complex information and ideas are communicated effectively in an appropriate form and style.	**20 – 27 marks** *Mid-point 24*
Level 1	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. 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. The candidate shows some ability to construct a coherent argument to reach judgements and conclusions. 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. Straightforward information and ideas are expressed clearly with some appreciation of an appropriate form and style.	**1 – 19 marks** *Mid-point 10*

Total for this question: *80 marks*

1
(a) 'Profit maximisation requires a firm to produce the level of output at which marginal revenue
equals the marginal cost of production, and to set the price accordingly' (**Extract A**, lines 1-2).

(i) Explain why a firm may decide **not** to use the MR=MC rule when choosing levels of output and
setting prices.

(10 marks)

Reasons for not using the MR=MC rule include: firms having objectives other than profit
maximisation; the conflict between short-run and long-run profit maximisation; lack of accurate
information about costs; lack of accurate information about revenues; other pricing rules such as the
cost plus pricing rule are more practical.

For candidates who:

explain why profit is maximised when MR=MC: **2 marks**

illustrate this in a particular market structure (e.g. perfect competition):   **2 marks**

provide a very basic statement of a reason for not using the MR=MC rule: **2 marks**
develop the explanation of the reason: **up to further 5 marks**

explain an advantage of an alternative way of setting prices: **2 marks**

explain that the MR=MC rule is best regarded as a necessary condition for profit
maximisation rather than as a practical pricing rule: **2 marks**

draw a relevant diagram: **up to 2 marks per diagram**
                                                           Maximum of 3 marks for diagrams

**Explanation of two or more reasons why a firm may decide not to use the MR=MC rule can earn
full marks.**

UP TO AN OVERALL MAXIMUM OF 10 MARKS

1

(a) (ii) Outline **one other** example of the use of marginalist principles in economic decision-making.
(10 marks)

The MR=MC rule is just one of a number of examples of application of the underlying assumptions in neoclassical economic theory that economic agents are optimisers, and that in order to optimise (or maximise), an economic agent must undertake the relevant activity up to the point at which the marginal private benefit received equals the marginal private cost incurred (MPB=MPC). Likewise, to maximise the public interest (social interest), a government should undertake a particular activity up to the point at which marginal social benefit equals marginal social cost (MSB=MSC). Full marks can be earned for an explanation of one of these principles, or, more narrowly, of a specific application of a marginalist principle e.g. $MRP=MC_L$, MU of the wage = MU of leisure time, MU=P (though the latter is not on all the A Level specifications).

Reward also answers which outline examples such as the marginal propensity to consume or to import, the marginal rate of taxation, and the marginal efficiency of capital.

For candidates who:

make a basic statement of a relevant example: **2 marks**

explain the example: **Up to 8 marks**

make any other relevant point: **1 mark per point, up to a maximum of 3 marks**

draw a relevant diagram: **Up to 2 marks per diagram**
Maximum of 3 marks for diagram

UP TO AN OVERALL MAXIMUM OF 10 MARKS

1

(b) If a firm charges a different price to each consumer, it 'captures the entire consumer surplus and substantially increases profits' (**Extract C**, line 12). Assess the significance of this statement from the point of view of both firms **and** consumers. *(20 marks)*

Very good answers might draw on the sentence in Extract C immediately before the statement in the question which states that the marginal revenue curve becomes identical with the demand curve when each and every customer is charged the maximum price he or she is prepared to pay. Candidates might explain the implications of this sentence, namely that all the consumer surplus is transferred to the firm or firms engaging in price discrimination. This boosts profit and producer surplus. Firms benefit but consumers suffer. Good answers may explain that *some* consumers benefit from prices that are lower than those charged in the absence of price discrimination. An answer that explains both arguments and provides a fully justified reasoning, possibly with an accurate diagram, should earn full marks, even if only one form of price discrimination is discussed. However, reward answers that argue that in some forms of price discrimination, some, but not all, consumer surplus is transferred. Knowledge of technical terms, such as first and third degree price discrimination, is not needed for full marks.

Restrict the mark to a maximum of 10 if the answer fails to assess the point of view of consumers as well as the point of view of firms (or vice versa).

Issues, analysis and areas for discussion include:

* Relevant focus on the issue posed by the question;

* Understanding and application of the theory of price discrimination;

* Understanding of consumer surplus;

* Understanding of how price discrimination transfers consumer surplus into profit, and thus benefits firms;

* Understanding of how most but not all consumers may suffer;

* Circumstances in which price discrimination may produce a result different from that in the statement.

Also give credit for:

* Relevant use of data and/or candidate's knowledge;

* Relevant use of evidence;

* Overall assessment.

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

1

  (c) Charging lower prices for alcoholic drinks in a 'happy hour' (**Extract C**, line 7) is a form of price discrimination.

   Discuss the economic case **for** and **against** the government banning 'happy hours'.

(20 marks)

This question aims to widen discussion away from a narrow answer based solely on the case for and against price discrimination, and thus on the case for banning or permitting price discrimination. Good answers are of course likely to address this issue, but are likely also to address market failure versus government failure arguments, and in particular issues stemming from the fact that alcoholic drink may be deemed to be a demerit good.

Answers that consider only price discrimination issues (or which consider other issues but completely ignore the effects of price discrimination) should be restricted to a maximum mark of 13 (top of Level 2).

Issues, analysis and areas for discussion include:

- Application of the theory of price discrimination;

- Alcoholic drink as a demerit good;

- Market failure issues;

- Government failure issues;

- Arguments for and against government intervention in and regulation of markets.

Also give credit for:

- Relevant use of data and/or candidate's knowledge;

- Relevant use of evidence;

- Overall assessment.

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

1

(d) Using the data and your economic knowledge, discuss the case for providing goods and services, such as water, the internet and roads, free at the point of use. *(20 marks)*

The question provides three prompts (water, the internet and roads) which are mentioned in lesser or greater detail in the data. While candidates do not have to use all the prompts (and can use examples that are not mentioned in the data), the question does require candidates to use the data. Answers which make no use or hardly any use of the data should be restricted to a maximum mark of 13 (top of Level 2).

Good answers may develop the prompts provided by Extracts D and E. Extract D argues that in the case of the internet, capacity is abundant and the marginal cost of supply is zero or close to zero. Extract E discusses the negative congestion externalities imposed on other road users when a motorist decides to drive on an already congested road. This links to the capacity issue mentioned in the context of the internet.

Answers restricted to standard text bookish discussion of public goods and/or merit goods without reference to the issues in the data should not earn more than 9 marks (top of Level 1). However, an answer that focuses on just one of the prompts, for example road pricing in central London, can reach Level 3, provided the analysis and evaluation are good.

Issues, analysis and areas for discussion include:

- The functions of prices in markets;

- Prices, resource allocation and economic efficiency;

- Market failure issues;

- Capacity, congestion, and the marginal cost of supply to additional customers;

- Government failure issues;

- Equity issues.

Also give credit for:

- Relevant use of data and/or candidate's knowledge;

- Relevant use of evidence;

- Overall assessment.

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

SECTION B: Markets and Market Failure

2

In 2005, the United Kingdom government was urged to provide significant financial assistance to try to ensure the survival of the Rover car company in the UK.

Discuss the case **for** and **against** a government intervening in the market economy to support manufacturing industries or firms.   *(40 marks)*

Good answers will consider the advantages of leaving production and resource allocation to market forces, but also circumstances in which market failure may occur. The best answers will focus on the advantages and disadvantages of government intervention to save companies in manufacturing and other industries from collapsing, rather than on market failure in general.

An answer which considers only the case for, or the case against, must be restricted to a maximum of 26 marks.

Issues, analysis and areas for discussion include the following:

- The international competitiveness of manufacturing companies;

- Deindustrialisation issues;

- 'Level playing field' issues;

- Productivity issues;

- Types of financial assistance;

- The opportunity cost of financial assistance;

- Issues relating to propping up losers versus picking winners;

- Facilitating structural change in the economy;

- Comparative advantage and other trade theory issues;

- Globalisation issues.

Also give credit for:

- Relevant use of the prompt and the candidate's knowledge;

- Relevant use of evidence;

- Overall assessment.

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

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3 Plumbdown District Council is proposing to change the way in which refuse collection is financed in its area. Instead of being paid for out of local taxation, it is proposing to charge separately for the service. Households wanting to have their rubbish collected will have to pay an annual fee to a private waste collection company. A 25 per cent discount will be available to households which separate paper, plastics, glass and garden rubbish from general household waste. Households which do not pay the charge will have to find alternative ways of disposing of their rubbish.

Evaluate the case **for** and **against** this proposal. *(40 marks)*

Charging prices may make households economise in the production of rubbish. But garbage or rubbish can be regarded as a public 'bad'. If local authorities charge for refuse removal, households may dump rubbish to evade having to pay. The resulting social costs may exceed those occurring when the service is provided at zero price. When evaluating the case for and against the proposal, candidates may consider one or more of the following approaches: (i) there should be free provision for the removal of *all* types of rubbish; (ii) there should be free provision only if households separate types of rubbish; (iii) different prices should be charged for the removal of different types of rubbish; or (iv) there should be a standard price charged for removal of *all* types of rubbish.

An answer which considers only the case for, or the case against, must be restricted to a maximum of 26 marks.

Issues, analysis and areas for discussion include the following:

- Market failure arguments;

- Signalling, incentive and allocative functions of prices;

- Government failure arguments;

- Administrative costs of intervention;

- Consideration of a range of pricing (and non-pricing) options;

- The opportunity cost of free provision.

Also give credit for:

- Relevant use of the candidate's knowledge;

- Relevant use of evidence;

- Overall assessment.

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 In the light of the UK economy's recent economic performance, discuss the case **for** and **against** using fiscal policy as well as monetary policy to manage the level of aggregate demand.

(40 marks)

The main discriminators will be the abilities to show an understanding of (i) how fiscal and monetary policy can be used to manage aggregate demand; (ii) how fiscal policy is no longer used in this way (apart from through the use of automatic stabilisers); (iii) whether fiscal policy would be successful if used to manage aggregate demand; (iv) the for and against issues; and (v) an evaluation of the success of monetary policy used in this way, in the light of the UK's recent economic performance. Good answers should consider the implications of the words 'as well as' in the question.

An answer which considers only the case for, or the case against, must be restricted to a maximum of 26 marks.

Issues, analysis and areas for discussion include the following:

- Understanding of the UK's recent economic performance;

- The meaning of aggregate demand;

- Knowledge of demand management policies;

- How monetary policy and fiscal policy can manage demand;

- Discretionary policy versus non-discretionary policy e.g. the use of automatic stabilisers;

- The Bank of England's track record in implementing monetary policy;

- The Treasury's track record in implementing fiscal policy;

- How fiscal policy has been used in a supply-side rather than a demand-side way;

- The importance of other factors e.g. the impact of globalisation.

Also give credit for:

- Relevant use of the candidate's knowledge;

- Relevant use of evidence;

- Overall assessment.

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

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5 In recent years, the United Kingdom's current account deficit on the balance of payments has reached record levels, but the current account has not generally been regarded as an important problem for UK economic policy makers.

Discuss whether current account imbalances pose serious problems, both for individual countries **and** for the global economy. *(40 marks)*

Good answers should link understanding of the meaning of a current account deficit with a problem or problems that a deficit may pose. For a particular country, problems might relate to the country's industries being uncompetitive in international trading, and/or to conflicts and trade-offs with mutually exclusive internal policy objectives. Very good answers should relate problems (and lack of problems) to capital flows financing a current account deficit, and to whether the exchange rate is fixed or floating. Good answers should consider current account surpluses as well as deficits. They may also discuss the global effects of current account imbalances in the context of the US deficit and the surpluses on current account enjoyed by Asian countries such as Japan and China.

An answer which considers only an individual country, and not the global economy (or vice versa), must be restricted to a maximum of 26 marks

Issues, analysis and areas for discussion include the following:

- Understanding the meaning of, and the items in, the current account;

- Understanding the meaning of current account deficits, surpluses and imbalances;

- Understanding that for the global economy, the current account must exactly balance, and that one country's surplus is another country's deficit;

- Relating the current account to capital flows and methods of financing a deficit;

- Relating the current account to trade theory e.g. comparative advantage;

- Relating the current account to exchange rate regimes (floating and fixed);

- Explaining a particular problem or problems that a current account deficit may pose;

- Identifying, distinguishing and discussing national versus global problems and implications.

Also give credit for:

- Relevant use of the candidate's knowledge;

- Relevant use of evidence;

- Overall assessment.

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