

Examiners' Report/ Principal Examiner Feedback

Summer 2010

GCE

GCE O LEVEL ECONOMICS (7120) Paper 01

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PE Report on Examination Paper 7120/01

General Comments

This is the final May/June examination of this specification. The new IGCSE which replaces this subject will continue to offer centres the opportunity to teach a structured specification giving candidates the opportunity to learn the basics of economics which can be used as a foundation for higher studies.

The new IGCSE consists of compulsory questions. This will probably benefit all candidates. The stronger candidates will be able to show their knowledge of all parts of the specification whilst the weaker candidates won't have to choose their questions. This summer's examination highlighted the problem of choice. Too many candidates chose questions based on the first parts of the questions and then found they had little knowledge of the later, more highly scoring parts.

As in past examinations some candidates made careless mistakes. These could be easily overcome by

- answering all parts of the question,
- learning definitions and examples,
- distinguishing between common terms e.g. trading bloc and block,
- learning demand and supply diagrams e.g. subsidies, minimum wage rate.

Centres who have been teaching this specification for many years should be confident regarding the change to the new IGCSE. Their approach and preparation has led to improved standards over the past years. Their teaching methods are sound and a positive approach to the new IGCSE will bring success in the future.

Comments on Individual Questions

SECTION A

Question 1

This question caused few problems (a) In Economics "capital" is defined as a "man made resource used to produce other goods e.g. machinery". In part (b) the other factors of production were easily identified.

Question 2

The characteristics of money are not the same as the functions of money. Some candidates wasted time by giving a list of characteristics without explaining one of them.

Question 3

Candidates are still finding the concept of price elasticity of demand difficult. They can define it but cannot distinguish between the factors affecting demand and those affecting price elasticity of demand.

(a)(i) Cigarettes are inelastic in demand (-0.4) so if price rises by 10% demand would fall and not "stay the same" as many candidates thought. In order to score maximum marks candidates needed to use the relationship between price and quantity demanded when demand is inelastic. Demand will fall by a less proportionate amount than the change in price, in this case less than 10%.

(a)(iii) The factors affecting price elasticity of demand are different from the factors affecting the demand or supply for a good or service. Too often candidates identified fashion (demand factor) and taxes (supply factor) instead of, for example, habit/addiction and the availability of close substitutes.

(b)(i) The income elasticity of demand is given as 0.06 (positive) which indicates that as incomes rise demand will rise but by a less than proportionate amount, in this case less than 10%.

Question 4

(a) A straightforward question in which the candidates were given the labels for the diagram- all they had to do was write them in the correct spaces. So why did some decide to insert different labels?

(b)(i)(ii) Economies of scale is usually a popular and well answered question in question in Section B. It was therefore surprising to find some poor responses for this question. The most common mistake occurred when candidates defined the terms instead of giving examples of one internal and one external economy of scale.

Question 5

(a) A recession occurs when a country experiences **negative** economic growth. When economic growth is positive, even if it is less than previous years, the economy is still growing. (b) Candidates were far better at answering part (ii) and referring to the data to show that unemployment rose between 2007 and 2008.

(c)(i) Structural unemployment (due to decline in demand for an industry's output) is not the same as cyclical unemployment (general fall in demand in economy). Neither is it the same as the decline in one of the sectors in an economy as a country develops e.g. the primary sector may decline and secondary and/or tertiary sector may grow. An example of a good response is shown below,

“Structural unemployment occurs when there is a fall in demand for the output of an industry. In Bangladesh the demand for jute fell. This meant that workers in the jute industry were made unemployed.”

(c)(ii) It is important that candidates don't rely on repeating the question if they want to achieve full marks. Instead of repeating Seasonal/seasons they should have referred to the “time of year”.

“Seasonal unemployment refers to workers being employed for only part of the year and at other times not having a job. E.g. in ski resorts in the winter people are employed as ski instructors but once the season is over they are unemployed for the rest of the year.”

Question 6

There were two ways of scoring maximum marks for (a). The easiest required candidates to reduce the income in 2009 by 10% (the rate of inflation) and produce the answer, \$22,500. A more complicated approach involved using the price index of 100 in 2008 and 110 in 2009 resulting in the answer, \$22727. Far too many candidates produced neither of these responses; instead they confused real income with disposable income and gave the incorrect responses, \$18,000 or \$20,000. Fortunately few found (b) difficult and most managed to score some marks in (c) for explaining why the figures showed a progressive tax.

SECTION B

Question 7

Population is always popular when it appears in this section of the paper and this question was no exception. The definitions for (a)(i) and (a)(ii) were of a high standard. However, some candidates stated the effects of an ageing population rather than two causes of an ageing population in (b). The economic consequences to the government (c)(i) and the firms (cii) enabled candidates to write at length and for most the responses were relevant. An example of a good response is given below.

7c(i) *“An ageing population places a greater burden on the government as the government will have to increase its expenditure on services such as healthcare, availability of state retirement homes and pensions. This causes an opportunity cost in expenditure on other areas such as education or training. The government will also face decreased revenue as a larger percentage of the population leaves the working age population thus reducing income tax revenue. The increased expenditure and decreased revenue would lead to a budget deficit causing the government to implement policies to try to rectify it.”*

7c(ii) *“Firms will have less workers because many of their workers will retire and less new young people will be there to replace them. The firms will have to put up their wages in order to attract more workers. Firms may start to invest in capital goods in order to keep wage costs down and production high. Firms might also have to change what they are producing due to the change in demand for goods. The demand would change because the age groups are changing e.g. a decline in the demand for toys and an increase in demand for golf clubs.”*

Question 8

The popularity of this question was probably due to parts (a) and (b) for which most candidates scored maximum marks. However, it is obvious that weaker candidates had not read or understood the following questions and their responses showed that their knowledge of localisation in (ci) was very limited. Parts (c)(ii) and (c)(iii) required candidates to identify two problems associated with localisation and how the government could overcome the problems identified. Too many candidates could not identify the problems so their responses in (c)(iii) were not worthy of any marks. The following shows how these questions should have been structured.

8c(ii) *“When there is localisation of an industry in an area that area will become congested. There will be little free space available. As demand is greater than supply, the price of land will rise making new firms unable to locate there and the local people will also be hit by this problem as houses will become more expensive. Pollution and social costs will rise in that area due to the high amount of vehicles and firms who may dump their waste into nearby rivers and lakes.”*

8c(iii) *“The government can pass laws and regulations restricting new firms from locating in overcrowded areas and not allowing existing firms to expand their businesses. The government can provide subsidies to new firms to locate elsewhere or in an assisted area thereby taking them away from overcrowded areas. . They can also improve the infrastructure and create an attractive atmosphere so that new firms will locate elsewhere. The government can also give tax holidays to firms*

locating to assisted areas, all these will attract new firms or industries to locate elsewhere and not in the localised area. The movement of firms away from an overcrowded area where industry is localised will reduce pollution. The government can also tax the industry or firms if they are polluting or harming the environment around them which will increase their costs and so encourage them to reduce pollution."

Question 9

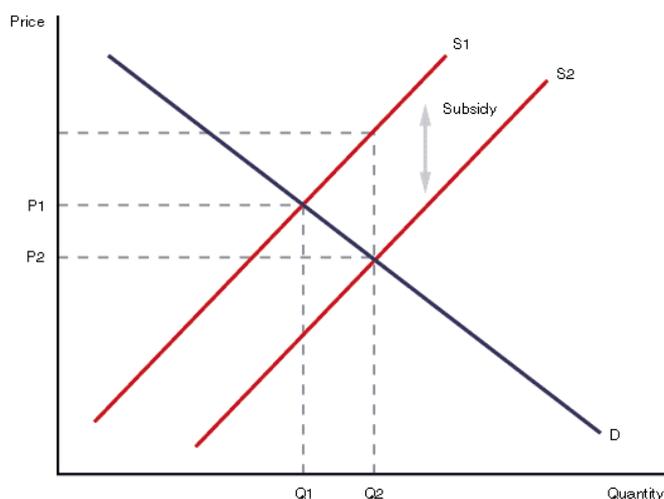
This was the least popular question in Section B. Many of the candidates who attempted it found the first definition (a)(i) difficult but were able to correctly define a mixed economy in (a)(ii).

9(a)(i) *"Prices are determined in a free market economy by the interaction of demand and supply. The equilibrium price occurs where demand is equal to supply."*

(a)(ii) *"A mixed economy combines characteristics of a planned economy controlled by the government and a free economy which is controlled by the market forces of the private sector."*

The most common mistake in the diagram (b)(i) showed the either the supply curve shifting to the left or a shift in the demand curve. The correct diagram is shown below with the explanation alongside.

9(b)(i)



The government gives firms sums of money called subsidies. This reduces the costs of production so the supply curve shifts to the right. The increase in supply reduces price and increases the quantity demanded.

There are many reasons why a government might subsidise food production in its country (b)(ii) and the most popular responses included to increase the supply of food so that it can export the surplus or to overcome poverty and starvation in the country.

The final part of this question (b)(iii) required advantages and disadvantages of subsidising food production.

9biii *"Subsidies cause domestically produced foods to increase in supply thus reducing prices hence a higher standard of living. Demand for food imports would fall and the demand for the cheaper exports would rise leading to an improvement in the balance of payments. Unemployment would fall if production increased."*

Subsidies can however lower disposable income as taxes must be increased to finance subsidies. There is an opportunity cost as less money will be available for development and it can act as a drain of money for the government. Usually a subsidy does result in the advantages mentioned and usually the advantages outweigh the disadvantages but it depends on how firms respond and how the government finances the subsidies."

Question 10

A very popular question.

The balance of trade (a) refers to visible exports - visible imports i.e. the trade in goods rather than services. A deficit is simply the value of visible imports greater than visible exports.

The majority of candidates correctly identified a variety of ways in which exports could be increased (b)(i) and imports reduced (b)(ii) ranging from the depreciation of the currency to government advice to exporters and tariffs and quotas against imports.

Despite previous reports warning of the need to differentiate between a trading bloc and a block to trade there are always some candidates who confuse the two and lose marks. A mistake in (c)(i) was compounded in their answers in (c)(ii). Fortunately some candidates produced sound responses as shown below.

10cii *"Membership of a trading bloc such as the European Union benefits Germany in numerous ways. It allows Germany to strengthen political relations and alliances between the member counties such as England and France, which ensures their political support in international matters. Germany also benefits from free trade with these counties as it does not have tariffs, quotas or voluntary export restrictions imposed against it. This means that Germany can have a greater market (non-domestic/international) for its exports without facing trade restrictions. Its firms can benefit from economies of scale. Germany also benefits from being able to export goods to member countries at a lower cost, as it will not face the added burden or strain of trade restrictions, thus improving Germany's balance of payments which may allow for further economic growth."*

Question 11

This question proved to one of the most popular. Explanations of monetary policy (a)(i) and fiscal policy (a)(ii) were usually well done but supply side policy (a)(iii) proved more difficult.

(a)(iii) Supply side policy relates to government action to increase the productive capacity in an economy. By making markets more flexible e.g. reducing the power of the trade unions and deregulation aggregate supply can be increased.

Part (b) allowed the candidates to choose two of the three policies to improve (b)(i) the level of employment in a country and (b)(ii) the level of economic growth. Choosing policies to improve the level of employment proved to be easier than increasing economic growth.

(b)(i) *"Monetary policy can improve the level of employment by decreasing interest rates. When interest rates are lowered then people save less, borrow more and therefore spend more money. When consumers spend, the aggregate demand increases and when firms invest to cope with the extra demand, they employ more*

workers to increase their output, which improves the level of employment in a country.

Fiscal policy can increase employment by increasing government expenditure and decreasing both direct and/or indirect taxes. An increase in government expenditure can increase employment directly e.g. spending government revenue on building roads or indirectly spending on education and training to improve labour mobility. Decreasing taxes, like monetary policy, will stimulate demand in the economy leading to increased employment."

Economic growth is defined as an increase in real Gross Domestic Product over a period of time NOT simply an increase in demand. Candidates scored marks if they related an increase in demand to increased production but many failed to do this! Nor is controlling inflation on its own a way of achieving economic growth!

Economic growth can be improved by Supply side policy. The government can increase competition in product and labour markets. Privatisation and deregulation increase competition which leads to increased efficiency and technological advancements which in turn lead to increased productive potential and economic growth. Supply side policies of education and training improve labour mobility which makes labour more productive leading to economic growth.

By introducing an expansionary monetary policy firms will benefit from the low rates of interest as it makes investment cheaper. Increased investment leads to economic growth, as firms are now employing more labour and capital.

Consumers will save less as there won't be much interest return on their savings and so their spending will increase. This again will increase firms' incentives to invest even more to increase supply to meet demand. Aggregate supply in the economy will increase.

Question 12

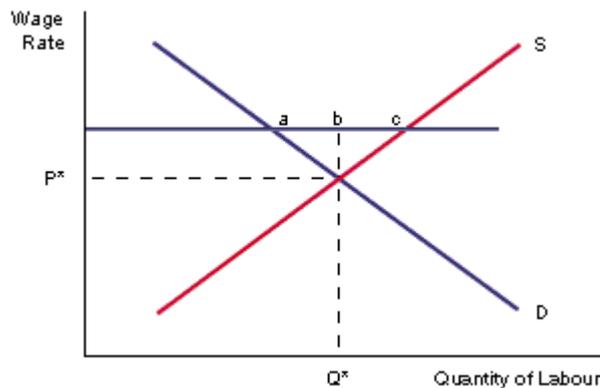
The term "working population" was misunderstood by a high number of candidates in (a). The working population = people no longer in full time education and below the retirement age. Too many candidates were unaware that the unemployed are part of the working population.

Governments may wish to increase the working population (b)(i) to overcome the problems caused by a shortage of workers e.g. high wages, low economic growth.

Ways in which a government can increase the working population (b)(ii) could include raising the retirement age, reducing the school leaving age, increasing immigration, decreasing emigration as well as ways of increasing the birth rate and decreasing death rate. Unfortunately ways of decreasing unemployment do not increase the working population as the unemployed, as stated earlier, are part of the working population.

Candidates should only have chosen this question if they were confident in their ability to draw the minimum wage rate diagram.

(c)(i) Minimum wage rate diagram



Explanation: Government imposes a minimum wage rate above the equilibrium. More workers will be willing to work at the higher wage rate but demand by firms will fall leading to unemployment.

(c)(ii) *"The minimum wage benefits poorer workers because they earn a higher income. This makes them better off and increases their standard of living. One other benefit is that workers become more motivated and become more productive and increase their output. The disadvantage is that it causes unemployment. The costs of production go up for firms as wages increase so they reduce costs by reducing their workforce. They may decide it is cheaper in the long run to replace men with machines."*

Question 13

Most candidates who chose this question showed a good understanding of and an ability to apply their knowledge of economics to the following three topics.

(a) *"Country - Sri Lanka. There are advantages of increasing the tax on petrol such as people will limit the use of cars (private vehicles). When this happens there is less pollution in the air and congestion on the roads will also fall, and breathing problems caused by emissions from vehicles will also decrease. As petrol has an inelastic demand the rise in taxation will increase government revenue. However, transport costs for firms will rise so this may lead to inflation in the country. The poor will suffer more than the rich as a petrol tax is regressive so they will probably have to sell their cars and use public transport which is considered an inferior good"*.

(b) *"The advantage to India in attracting a multinational company (MNC) to set up a factory is that the MNC creates employment which improves the living standards of the country. One other advantage is that the MNC invests a lot of money in the country and also pays tax. It also strengthens the balance of payments and the demand for Indian currency. The disadvantage is that it might take the profit to the home country which might worsen the current account balance as it is an invisible import. One of the other disadvantages is that local businesses may not be able to compete and so may go out of business thus increasing unemployment."*

(c) *"The advantage of developing the tourist industry in India is that tourism is an invisible export so the balance of payments will improve. Employment in the tourist resorts will increase. One of the other advantages is that it increases the government's revenue as tourists pay indirect taxes. The disadvantage is that it might create pollution, which is an external cost. The tourists might leave a lot of litter and destroy some of the countryside. It might also destroy the culture of India."*

Grade Boundaries - June 2010

Grade	A	B	C	D	E
Grade Boundaries	70	61	52	47	42

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