



2011 Economics

Advanced Higher

Finalised Marking Instructions

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Marking Instructions
Economics Advanced Higher

Detailed marking instructions/guidelines

These are not solutions

1. The appended marking instructions are guidelines only. Candidates will adopt different ways of tackling particular questions.
2. Differences of interpretation will be resolved at the Markers' meetings in May and June.
3. In essay or extended answers it is not necessary for candidates to include all the points listed in the enclosed mark schemes.
4. Candidates are expected to demonstrate a full appreciation of the topic and a sound understanding of the economic issues under discussion.
5. Marks should not be allocated on a rigid points scoring basis, but on the overall quality of the answer.

Advanced Higher: Marking Scheme

Marks

Section A

- | | | |
|----|---|---|
| 1. | (a) Derived demand. The demand for labour is determined by the level of demand for their output | |
| | (b) Inflexibility in the labour market. Workers cannot be moved occupationally and geographically with the same ease as goods and services. The wage level does not adjust to restore equilibrium in the labour market Credit reference to demand/ supply of labour not responding to market pressures. | 2 |
| 2. | Workers are conscious of price inflation and therefore demand higher wages but workers are reluctant to accept lower wages even when others are losing their jobs. Accept reference to pay freezes at times of high unemployment.etc. | 2 |
| 3. | Firms tend to hoard labour because of the costs of making workers redundant and the costs and logistical difficulties in rehiring labour when the economy recovers. Firms may have grown in efficiency prior to the recession and had less need to shed labour. Government policies which helped maintain consumer spending and therefore protected jobs, eg the car scrappage scheme or lowering of VAT. | 3 |
| 4. | Skills can be lost and good working habits sacrificed. Firms are suspicious of the attitude and commitment of the long term unemployed (LTU). LTU are usually less well qualified and may live in areas associated with high levels of unemployment. Some feel that the level of benefits can discourage active job seeking. Hysteresis. | 3 |
| 5. | Positive aspects. Bridging skills gaps in the labour market, greater competition for jobs improving efficiency, firms given wider choice of employees, lower costs for firms, and cultural diversity. Higher output and GDP. Improving dependency ratio for pensions etc.

Negative aspects. Job losses for UK workers and the cost of unemployment benefits and retraining for these UK workers, lower pay levels in certain industries, pressure on schools, housing and infrastructure in some areas.
Marks 2 + 2 | 4 |

6.	(a)	1 mark for clearly showing NMW above the equilibrium price 1 mark for clearly labelling the level of unemployment	2
	(b)	Reasons why NMW did not lead to a sharp rise in unemployment. (a) NMW has been set at a very low level. (b) Workers in many sectors already earned well above the NMW and therefore it had minimal impact. (c) High levels of economic growth led to increasing demand for labour despite NMW. (d) How accurate and reliable are unemployment statistics? (e) Growth of Part-time working. (f) Trade Union Power to prevent job losses.	3
7.		Impediments are related to the large variation in house prices between areas and problems in buying and selling houses in a depressed market with falling prices and low sales. The cost of moving house is high and unpredictable and can create high levels of stress. The rental market both private and especially public is difficult to enter when coming from outside an area. Assistance available to workers to find housing may be inadequate.	2
8.		Mention of proposals (actions) expected. Greater incentive to seek employment if benefits are cut or the rules tightened. The sharp rise in claimants for incapacity benefit in recent years is likely to be reversed if access rules are strengthened. Productivity is likely to increase and combined with greater worker participation will increase GDP, increase tax revenue and reduce social security expenditure. An alternative view might be that increased poverty, especially for low income families, might have an adverse effect on long term efficiency.	4

[END OF SECTION A]

Section B

Marks

Essay 1

1.	(a)	<ul style="list-style-type: none">• Kinked Demand Curve Theory.• Credit diagrams of Kinked Demand Curve and profit maximising output condition using this theory (2marks)• Importance of Non-Price Competition in this market structure.• Collusive Theories – Formal and Tacit Collusion.• Price Leadership.• Game Theory can be used to explain the strategic behaviour of firms. <p>At least 2 areas must be discussed for full marks but up to 8 marks can be given for 1 full explanation including diagram.</p>	9
	(b)	<ul style="list-style-type: none">• Businesses – loss of profits in SR, less competition in LR and therefore higher profit margins. Possible referral to the OFT for anti-competitive practices. Some businesses might fail. Credit examples if valid.• Consumers – lower prices in SR but less choice and higher prices in LR. <p>Consequences for firms and consumers must be covered for full marks.</p>	6
	(c)	<p>Competition Law –</p> <p>Role of OFT, Competition Commission, Regulators Enterprise Act 2002 – Price Fixing a Criminal Act Improvements – Dawn Raids, Whistleblowers' charter, Increased Penalties.</p> <p>Effectiveness – Hard to know, growing concentration in some industries, high profile successes and failures, underfunding, length of time taken for reports etc.</p> <p>Marks split 4/6 or 6/4</p>	10

Essay 2

2.	(a)	<ul style="list-style-type: none"> • Ring fencing of Education and Health Spending? • Cuts of an average of 19% of all other departments. • £81bn over 4 years. • Changes to the benefits system. • Means Testing Child Benefit. • Raising retirement age to 66 years. • Cuts in Defence. • Credit all accurate specific examples. 	4
	(b)	<ul style="list-style-type: none"> • Need to reduce the Structural Budget Deficit. • The interest burden and level of National Debt. • Intergenerational fairness. • The Financial Markets and Credit Rating of The UK. • Reducing the size of the state. • To prevent Crowding Out etc. <p>Max 3 marks per reason</p>	6
	(c)	<p>The Economy – risk of double dip, rising unemployment, negative multiplier effect, rising poverty and inequality.</p> <p>Individuals – Falling incomes, poorer public services, poverty.</p> <p>The consequences for both the economy and individuals must be mentioned for full marks.</p>	8
	(d)	<p>Disincentive effects of rising taxation, Laffer Curve, Indirect taxes are regressive, the Private Sector recovery would be worse hit. Cuts can be targeted, ideology, cuts in gov spending are “less damaging”. Cutting waste in the public sector will improve efficiency. The private sector is to be the driver of future economic growth.</p>	7

Essay 3

3. (a) (i) Rising food, gas and oil commodity prices, low £ and rising import prices. The Vat rise will push up inflation. Danger of wage-price spiral. Strength of the recovery. Gradual rise better than sharp rise in interest rates. Andrew Sentance putting forward this view. Credibility of MPC at stake. 9
- (ii) Above factors only temporary and cost-push. No risk of wage-price spiral, fear of double dip, deflationary pressures – spare capacity, weak global recovery, gov spending cuts. US QE 2. Fears of £ rising against US \$ and Euro which would diminish exports etc. Mark split 4/5 or 5/4 9
- (b) Lowering Bond Yields and LR interest rates, increasing bank deposits and therefore bank lending, increasing asset prices and wealth effect, reducing LIBOR, lowering the exchange rate and boosting exports. Increasing the money supply and the rate of inflation. 7
- (c) Impairment of Banking System, Low consumer and Business confidence, Liquidity Trap, Existing overindebtedness. Rising Savings ratio. The need to revert to a Fiscal Stimulus. Low credit availability, Time Lags. 9

Essay 4

- | | | | |
|----|-----|--|-----------|
| 4. | (a) | <p>Greece – Large budget deficit, Dishonesty re scale of deficit, corruption, poor tax system, Credit rating Agencies. Probably never met Maastricht criteria. Downgrading of Greek Government debt. Market rates were unaffordable and risk of default loomed. Estimated low growth rates in the future. Lack of international competitiveness.</p> <p>Ireland – Budget deficit not the issue. A huge property bubble which has burst – the Banking System is in deep trouble. The Banking system has a large level of Bad debt which the Irish Government guaranteed and therefore the Irish Government has had to bail out its banks. The size of the losses means that the Government requires a bail out. Credit rating agencies have also downgraded the debt of the Irish Government and interest rates on Government bonds have soared. £85 bn rescue package from EU and IMF.</p> | 10 |
| | (b) | <ul style="list-style-type: none">• Problem of bail outs and no mechanism in original treaty – German public does not want to be lender of last resort unless necessary.• Since they share the same currency risk of capital flight from debtor countries.• ECB is central bank to all countries.• Fear of contagion to other countries – Portugal and Spain.• Uncertainty has led to a fall in the value of the Euro. | 6 |
| | (c) | <p>Loss of control over monetary policy, fiscal policy and exchange rate policy. Total loss of economic and political sovereignty. Gobs cannot make decisions which might help recovery. For example no QE possible, no control over interest rate, and the strength of the Euro is driven by successful German economy which does not suit countries wanting to improve international competitiveness. On the other hand bail outs from ECB and Eurozone countries have prevented total Iceland crisis. The IMF would have required conditions as well. Is this a German takeover and do you need a United States of Europe for the euro to work.</p> | 9 |

Essay 5

5.	(a)	Effect of low exchange rate on competitiveness of Chinese exports. Effect of low currency on import prices into China. Mention of Chinese trade surplus. Form of protectionism.	6
	(b)	<ul style="list-style-type: none">• Rising prices of commodities.• Growing domestic prosperity.• Cheap Labour.• Rising productivity.• Better educated workforce.• FDI.• High savings ratio. Specific examples using a variety of emerging economies must be used for full marks.	9
	(c)	<ul style="list-style-type: none">• Lack of resources.• Natural disasters.• Poor human capital.• Poor infrastructure.• Trade barriers.• Corruption.• Dependency on Primary Production.• Wars.• Lack of developed Financial System.• Low productivity. Points must be fully developed and explained. Specific examples will be credited.	10

Essay 6

6.	(a)	<ul style="list-style-type: none"> • Size of the budget deficit. • The higher earning potential of graduates. • Unfairness to those taxpayers who have not been to university. Improve quality of universities. 	6
	(b)	<p>(i) Private Benefits – Higher earnings, 3-4 years to pursue subjects of choice, social contacts of university, occupational mobility, transferable skills, Higher employability. Social Benefits – better educated workforce, higher productivity, international competitiveness of UK, lower unemployment, higher tax take, improved public services etc.</p> <p>(ii) Fully labelled diagram showing the private marginal benefit/ Demand curve and Social Benefit curve. The vertical distance between them should be labelled as the positive externality.</p>	8 5
	(c)	<p>A graduate tax has the advantage of being progressive, the threshold would be set above a certain level of income, it would spread payment over a long time period.</p> <p>Disadvantages – There is no maximum amount, high wage earnings would pay a lot more than low wage earners. Those who leave the UK would avoid the tax. The loan system at least allows the loan to be paid off and the graduate to be free of payments. The loan system means that those on low incomes who pay most slowly will pay more interest.</p>	6

[END OF SECTION B]

[END OF MARKING INSTRUCTIONS]