

**GCE AS**

**Economics**

**January 2010**

**Mark Schemes**

Issued: April 2010



MARK SCHEMES (2010)

Foreword

*Introduction*

Mark Schemes are published to assist teachers and students in their preparation for examinations. Through the mark schemes teachers and students will be able to see what examiners are looking for in response to questions and exactly where the marks have been awarded. The publishing of the mark schemes may help to show that examiners are not concerned about finding out what a student does not know but rather with rewarding students for what they do know.

*The Purpose of Mark Schemes*

Examination papers are set and revised by teams of examiners and revisers appointed by the Council. The teams of examiners and revisers include experienced teachers who are familiar with the level and standards expected of 16- and 18-year-old students in schools and colleges. The job of the examiners is to set the questions and the mark schemes; and the job of the revisers is to review the questions and mark schemes commenting on a large range of issues about which they must be satisfied before the question papers and mark schemes are finalised.

The questions and the mark schemes are developed in association with each other so that the issues of differentiation and positive achievement can be addressed right from the start. Mark schemes therefore are regarded as a part of an integral process which begins with the setting of questions and ends with the marking of the examination.

The main purpose of the mark scheme is to provide a uniform basis for the marking process so that all the markers are following exactly the same instructions and making the same judgements in so far as this is possible. Before marking begins a standardising meeting is held where all the markers are briefed using the mark scheme and samples of the students' work in the form of scripts. Consideration is also given at this stage to any comments on the operational papers received from teachers and their organisations. During this meeting, and up to and including the end of the marking, there is provision for amendments to be made to the mark scheme. What is published represents this final form of the mark scheme.

It is important to recognise that in some cases there may well be other correct responses which are equally acceptable to those published: the mark scheme can only cover those responses which emerged in the examination. There may also be instances where certain judgements may have to be left to the experience of the examiner, for example, where there is no absolute correct response – all teachers will be familiar with making such judgements.

The Council hopes that the mark schemes will be viewed and used in a constructive way as a further support to the teaching and learning processes.



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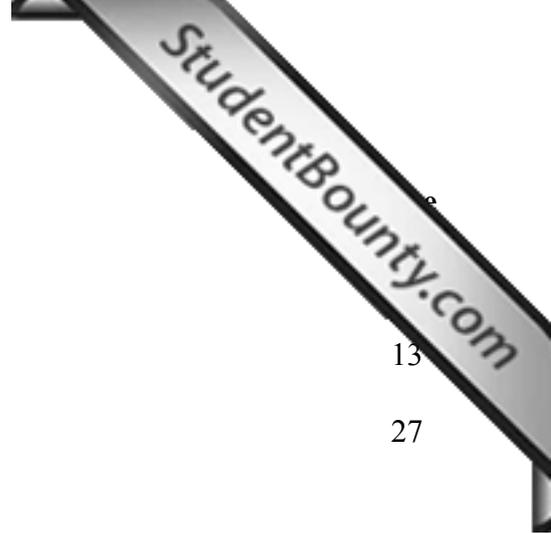
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**January 2010**

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## **Economics**

Assessment Unit A2 1

*assessing*

Module 3: Production and Competition

[A2E11]

**THURSDAY 21 JANUARY, MORNING**

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# **MARK SCHEME**

This mark scheme is intended to ensure that the A2 examination is marked consistently and reliably. The mark scheme provides markers with an indication of the nature and range of candidate responses likely to be worthy of credit. It also sets out the criteria which they should apply in allocating marks to candidates' responses. The mark scheme should be read in conjunction with these general marking instructions which apply to all papers.

### **Quality of candidates' responses**

In marking the examination papers, examiners will be looking for a quality of response reflecting the level of maturity which may reasonably be expected of an 18-year-old which is the age at which the majority of candidates sit their A2 examinations.

### **Unanticipated responses**

The mark schemes which accompany the specimen examination papers are not intended to be totally prescriptive. For many questions, there may be a number of equally legitimate responses and different methods by which the candidates may achieve good marks. No mark scheme can cover all the answers which candidates may produce. In the event of unanticipated answers, examiners are expected to use their professional judgement to assess the validity of answers and to refer for guidance to the general marking criteria that follow. If an answer is particularly problematic, then examiners should seek the guidance of the Supervising Examiner for the paper concerned.

### **Positive marking**

Examiners are encouraged to be positive in their marking, giving appropriate credit for valid responses rather than penalising candidates for errors or omissions. Examiners should make use of the whole of the available mark range for any particular question and be prepared to award full marks for a response which is as good as might reasonably be expected for an 18-year-old A2 candidate. Conversely, marks should only be awarded for valid responses and not given for an attempt which is completely incorrect or inappropriate.

### **Types of mark schemes**

Mark schemes for questions which require candidates to respond in extended written form are marked on the basis of levels of response which take account of the quality of written communication. These questions are indicated on the cover of the examination paper.

Other questions which require only short answers are marked on a point for point basis with marks awarded for each valid piece of information provided.

### **Marking calculations**

In marking answers involving calculations, examiners should apply the 'own figure rule' so that candidates are not penalised more than once for a computational error.

## Quality of written communication

Quality of written communication is taken into account in assessing candidates' responses to all questions that require them to respond in extended written form. These questions are marked on the basis of levels of response. The description for each level of response includes reference to the quality of written communication. Where the quality of candidates' economics is not matched by the quality of written communication, marks awarded will not exceed the maximum for Level 2.

## Levels of response

General descriptions of levels of response in terms of each assessment objective and the quality of written communication are given in the following table. These descriptions are intended to assist examiners in judging candidates' performance when they produce answers unanticipated by the detailed mark scheme for each question and to provide guidelines for examiners in assessing the appropriate level of response in respect of the quality of written communication.

The detailed mark schemes for each question relate these levels of response to the content of the relevant question. In deciding which mark within a particular level to award any response, examiners are expected to use their professional judgement. The following guidance is provided to assist examiners.

**Threshold performance:** Response which just merits inclusion in this level and should be awarded a mark at or near the bottom of the range.

**Intermediate performance:** Response which clearly merits inclusion in the level and should be awarded a mark at or near the middle of the range.

**High performance:** Response which fully satisfies the level description and should be awarded a mark at or near the top of the range.

**General Marketing Criteria**

<b>Level of Performance</b>	<b>Assessment Objective</b>	<b>AO1 Knowledge and Understanding</b>	<b>A02 Application</b>	<b>A03 Analysis</b>	<b>A04 Evaluation and judgement</b>
<b>BENEATH THRESHOLD</b>		There may be limitations in the candidate's grasp of theoretical principles, resulting in an excessively narrow focus on the issues involved in the question.	The candidate tends to make unsubstantiated generalisations, and superficial assumptions, lacking any real awareness of contemporary events.	The candidate is likely to confuse hypotheses with facts and does not successfully account for divergences between theoretically predicted and actual outcomes of events or decisions in a real economy.	The candidate finds it difficult to pinpoint strengths or limitations of economic models and theories in explaining real world issues and problems, or to compare and contrast alternative strategies or policy instruments.
<b>LEVEL 1</b>		The candidate makes only a limited attempt to select and use an appropriate form and style of writing. The organisation of material may lack clarity and coherence with little use of specialist vocabulary. Presentation, spelling, punctuation and grammar may be such that intended meaning is not clear.	The candidate makes valid connections between theoretical principles and real-world events.	The candidate shows ability to identify causes of economic problems and is able to relate these insights to real economies.	The candidate shows some awareness of the strengths and limitations of different economic models, theories, decisions and policies, and attempts to support observation with appropriate references.
<b>LEVEL 2</b>		The candidate shows sufficient knowledge of economic theory for the main issues involved in the question to be satisfactorily identified.			
<b>LEVEL 3</b>		The candidate makes a reasonable attempt to select and use an appropriate form and style of writing, supported with appropriate use of diagrams. Relevant material is organised with some clarity and coherence and some use of specialist vocabulary. Presentation, spelling, punctuation and grammar are sufficiently competent to make meaning evident.	The candidate relates concepts to situations and problems in real economies with some skill and can explain contemporary events while supporting conclusions with evidence.	The candidate is aware of the implications of hypotheses and distinguishes between association and causation in contemporary economic problems, offering valid suggestions as to how these may be addressed.	The candidate is able to critically examine alternative economic models, theories, arguments and policies in the analysis of economic problems and demonstrates the ability to evaluate the outcomes of economic decisions, supporting the analysis with accurate reference or relevant examples.
<b>HIGH GRADE</b>		The candidate successfully selects and uses an appropriate form and style of writing, supported with the effective use of diagrams where appropriate. Relevant material is organised with a high degree of clarity, coherence and widespread use of appropriate specialist vocabulary. Presentation, spelling, punctuation and grammar are of a sufficiently high standard to make meaning absolutely clear.			

- 1 (a) The recession has affected the profits of UK retailers in a number of ways:
- Sales revenue has fallen as consumers have cut back on spending.
  - Stores have had to slash prices in order to attract customers.
  - The recession has contributed to the fall in the value of the pound and this has increased the purchasing costs of stores which import much of their stock.
  - Some stores such as Lidl have benefited from the recession as consumers have sought out value products.
  - Food retailers have maintained sales.
  - Sellers of luxury goods such as electronics have been particularly badly hit.
  - Good candidates may use concepts such as income elasticity to explain this process.

**Level 1 ([1]–[2])**

Candidate shows little understanding of how the recession has affected the profits of UK retailers. There is no significant economic analysis and quality of written communication is limited.

**Level 2 ([3]–[4])**

Candidate shows some understanding of how the recession has affected the profits of UK retailers. There is a degree of economic analysis and quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

Candidate shows a clear understanding of how the recession has affected the profits of UK retailers. There is extensive economic analysis and quality of written communication is of a high standard. [6]

- (b) This is an example of horizontal integration.
- Horizontal integration is a merger between two firms at the same stage in the production of the same good or service.
- 2 marks for identifying merger as horizontal integration  
2 marks for explaining horizontal integration [4]
- (c) (i) A concentration ratio measures the market share of the leading firms in a particular industry. [2]
- (ii) The four firm concentration ratio is 75.1%.  
Tesco 30.7%, Asda 17.1%, Sainsbury 15.9%, Morrison 11.4. [2]
- (d) Candidates should explain what is meant by economies of scale and then proceed to identify and explain the main scale economies which would be achieved through a merger between two supermarket chains.

Issues for analysis and discussion include:

- Explanation of economies of scale.
- Purchasing economies.
- Marketing economies.
- Financial economies.
- Managerial economies.

**Level 1 ([1]–[2])**

Candidate shows at best a superficial understanding of economies of scale but these are not related to a merger between two retailers. Quality of written communication is limited.

**Level 2 ([3]–[4])**

Candidate shows some understanding of economies of scale and makes a reasonable attempt to relate these to a merger between two retailers. Quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

Candidate shows a clear understanding of economies of scale and directly relates this to a merger between two retailers. Quality of written communication is of a high standard. [6]

- (e) The issue of the market dominance exerted by large supermarkets is extremely controversial and has been the subject of a number of enquiries by the Competition Commission. The most recent report (2008) ruled that there was effective competition and that Tesco’s dominance was “not insurmountable.”

Issues for discussion include:

- Possibility of the disappearance of virtually all small independent retailers.
- Buying power of large supermarkets may affect suppliers, especially farmers.
- Consumers may be exploited if dominance becomes total and choice disappears.
- Possibility of collusion between the big chains.
- Dereliction of town centres as shoppers move to out of town sites.
- Large chains have brought prices down.
- Supermarkets have only become dominant because of consumer choice.
- Supermarkets are more efficient, partly because of scale economies

**Level 1 ([1]–[3])**

Candidate shows little understanding of the issues involved in restricting the growth of the major supermarket chains. There is no significant evaluation of the arguments and quality of written communication is limited.

**Level 2 ([4]–[7])**

Candidate shows some understanding of the issues involved in restricting the growth of the major supermarket chains. There is a degree of evaluation though this may lack depth or balance. Quality of written communication is satisfactory.

**Level 3 ([8]–[10])**

Candidate shows a clear understanding of the issues involved in restricting the growth of the major supermarket chains. There is in-depth evaluation and judgement of the arguments. Quality of written communication is of a high standard. [10]

- 2 (a) The most important feature of an oligopolistic market is that supply will be dominated by a few sellers. This will often be the result of barriers to entry and gives rise to a degree of interdependence and sometimes collusion between the firms ie the decisions of one firm have direct impact upon the profits of other firms.

Appropriate Development.

- Examples
- Causes of oligopoly.

**Level 1 ([1]–[2])**

Candidate shows little knowledge or understanding of oligopoly and there is no significant development. Quality of written communication is limited.

**Level 2 ([3]–[4])**

Candidate shows some knowledge and understanding of oligopoly and there is a degree of development. Quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

Candidate shows clear knowledge and understanding of oligopoly and there is extensive development. Quality of written communication is of a high standard.

[6]

- (b) The fact that oligopoly contains only a small number of firms makes it easy for collusive, anti-competitive pricing agreements to take place. This may be reinforced by the kinked oligopoly demand curve showing how firms with significantly different marginal costs may have the same equilibrium price. Furthermore if the industry is one with high fixed and low variable costs then competition which leads to marginal cost pricing is financially disastrous.

Issues, analysis and area for discussion include the following:

- Explanation and examples of non-price competition.
- Kinked oligopoly demand curve.
- Games theory.
- Collusion.
- Cost structures.
- Diagram.

**Level 1 ([1]–[4])**

Candidate provides little explanation of how oligopolistic market structures often lead to collusion and non-price competition. There is no significant economic analysis and quality of written communication is limited.

**Level 2 ([5]–[8])**

Candidate provides some explanation of how oligopolistic market structures often lead to collusion and non-price competition. There is a degree of economic analysis and quality of written communication is satisfactory.

**Level 3 ([9]–[12])**

Candidate provides a clear explanation of how oligopolistic market structures often lead to collusion and non-price competition. This explanation is supported by widespread use of economic analysis. Quality of written communication is of a high standard. [12]

- (c) Traditional economic theory tends to favour perfect competition above all other market structures. It leads to productive and allocative efficiency by producing the right goods in the right quantities and using the right productive methods. Other structures involve some degree of welfare loss. However this type of comparative static analysis ignores the dynamic features of markets such as economies of scale, research and development and so on. So it is too simplistic to state that oligopoly is *always* against the best interest of consumers though in many cases this will be true.

Issues for analysis and evaluation include:

- Comparison with perfect competition.
- Welfare implications.
- Productive and allocative efficiency.
- Appropriate diagram (s)
- Economies of scale.
- Research and development.
- Historical examples.

**Level 1 ([1]–[4])**

Candidate shows little awareness of issues relating to oligopoly and the welfare of consumers. There is no significant evaluation and quality of written communication is limited.

**Level 2 ([5]–[8])**

Candidate shows some awareness of issues relating to oligopoly and the welfare of consumers. There is a degree of evaluation though this may lack depth or balance. Quality of written communication is satisfactory.

**Level 3 ([9]–[12])**

Candidate shows extensive awareness of issues relating to oligopoly and the welfare of consumers. There is in-depth evaluation and judgement. Quality of written communication is of a high standard. [12]

- 3 (a) Candidates should give a brief explanation of the short run before proceeding to an explanation of marginal and average costs.

Appropriate Development:

- Explanation of short run.
- Definition of marginal cost.
- Definition of average cost.
- Marginal cost consists entirely of variable costs.
- Average cost has fixed and variable elements.

**Level 1 ([1]–[2])**

Candidate gives at best a flawed or incomplete definition of marginal and average costs. There is no significant development and quality of written communication is limited.

**Level 2 ([3]–[4])**

Candidate gives a reasonable definition of marginal and average costs though this may be incomplete or contain minor errors. There is a degree of development and quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

Candidate gives complete and accurate definitions of marginal and average costs. There is an extensive development and quality of written communication is of a high standard. [6]

- (b) The marginal cost curve shows how marginal cost changes with output in the short run. This will be determined by the returns to the variable factor(s) usually known as marginal product. This will rise initially due to the benefits of specialisation and marginal cost will fall. Eventually marginal product will start to decline due to the law of diminishing returns and marginal cost will rise. The average cost curve shows how average cost changes with output in the short run. It is the summation of average variable costs and average fixed costs. It also will fall at first due to the increase in marginal product also due to the fall in average fixed costs as these are spread over higher levels of output. The average cost curve will continue to fall after the MC curve has started to rise since the fall in AFC will for a while outweigh the rise in MC. The MC curve will intersect the AC curve from below at its minimum point.

Issues for analysis and discussion include:

- Explanation of marginal and average cost curves.
- Explanation of significance of marginal product.
- Explanation of law of diminishing returns.
- Explanation of significance of falling average fixed costs.
- Explanation of why marginal and average cost curves have different minimum points.
- Diagram.

**Level 1 ([1]–[4])**

Candidate shows little understanding of the factors which determine the shape of the firms' marginal and average cost curves. There is no significant economic analysis and quality of written communication is limited.

**Level 2 ([5]–[8])**

Candidate shows some understanding of the factors which determine the shape of the firm's marginal and average cost curves. There is a degree of economic analysis though this may contain minor errors or be incomplete. Quality of written communication is satisfactory.

**Level 3 ([9]–[12])**

Candidate shows a clear and comprehensive understanding of the factors which determine the shape of the firm's marginal and average cost curves. There is accurate economic analysis and quality of written communication is of a high standard. [12]

- (c) Traditional economic theory assumed that firms would seek to maximise profits and that this would occur where marginal cost was equal to marginal revenue. Hence the shape and position of the marginal cost and marginal revenue curves were crucial in the decision-making process. More modern analysis of firms' behaviour views corporate objectives as much more complex.

Issues for analysis and evaluation include:

- Firms may lack the information to equate marginal cost and marginal revenue
- Fear of intervention by competition authorities
- Importance of public image
- Divorce of ownership from control
- Long and short run interests of the firm
- Alternative objectives, e.g. satisficing
- Fear of take-over if profits are not maximized
- Explanation that equating MC and MR is a necessary but not sufficient condition for profit maximization.

**Level 1 ([1]–[4])**

Candidate shows little or no understanding of why firms may not aim to equate MC and MR and of what other objectives they may have. There is no significant evaluation and quality of written communication is limited.

**Level 2 ([5]–[8])**

Candidate shows some understanding of why firms may not aim to equate MC and MR and of what other objectives they may have. There is some evaluation though this may lack depth or balance and quality of written communication is satisfactory.

**Level 3 ([9]–[12])**

Candidate shows a clear understanding of why firms may not aim to equate MC and MR and of other objectives they may have. There is significant evaluation and judgement. Quality of written communication is of a high standard.

[12]

30

**Total**

**90**





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**January 2010**

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## **Economics**

Assessment Unit A2 2

*assessing*

Module 4: The International Economy

**[A2E21]**

**FRIDAY 29 JANUARY, AFTERNOON**

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**MARK  
SCHEME**

## General Marking Instructions

This mark scheme is intended to ensure that the A2 examination is marked consistently and fairly. The mark scheme provides markers with an indication of the nature and range of candidate responses likely to be worthy of credit. It also sets out the criteria which they should apply in allocating marks to candidates' responses. The mark scheme should be read in conjunction with these general marking instructions which apply to all papers.

### Quality of candidates' responses

In marking the examination papers, examiners will be looking for a quality of response reflecting the level of maturity which may reasonably be expected of an 18-year-old which is the age at which the majority of candidates sit their A2 examinations.

### Unanticipated responses

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### Positive marking

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### Marking calculations

In marking answers involving calculations, examiners should apply the 'own figure rule' so that candidates are not penalised more than once for a computational error.

### Types of mark schemes

Mark schemes for questions which require candidates to respond in extended written form are marked on the basis of levels of response which take account of the quality of written communication. These questions are indicated on the cover of the examination paper.

Other questions which require only short answers are marked on a point for point basis with marks awarded for each valid piece of information provided.

## Quality of written communication

Quality of written communication is taken into account in assessing candidates' responses to all questions that require them to respond in extended written form. These questions are marked on the basis of levels of response. The description for each level of response includes reference to the quality of written communication. Where the quality of candidates' economics is not matched by the quality of written communication, marks awarded will not exceed the maximum for Level 2.

## Levels of response

General descriptions of levels of response in terms of each assessment objective and the quality of written communication are given in the following table. These descriptions are intended to assist examiners in judging candidates' performance when they produce answers unanticipated by the detailed mark scheme for each question and to provide guidelines for examiners in assessing the appropriate level of response in respect of the quality of written communication.

The detailed mark schemes for each question relate these levels of response to the content of the relevant question. In deciding which mark within a particular level to award any response, examiners are expected to use their professional judgement. The following guidance is provided to assist examiners.

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**Intermediate performance:** Response which clearly merits inclusion in the level and should be awarded a mark at or near the middle of the range.

**High performance:** Response which fully satisfies the level description and should be awarded a mark at or near the top of the range.

**General Marketing Criteria**

<b>Level of Performance</b>	<b>Assessment Objective</b>	<b>AO1 Knowledge and Understanding</b>	<b>A02 Application</b>	<b>A03 Analysis</b>	<b>A04 Evaluation and judgement</b>
<b>BENEATH THRESHOLD</b>		There may be limitations in the candidate's grasp of theoretical principles, resulting in an excessively narrow focus on the issues involved in the question.	The candidate tends to make unsubstantiated generalisations, and superficial assumptions, lacking any real awareness of contemporary events.	The candidate is likely to confuse hypotheses with facts and does not successfully account for divergences between theoretically predicted and actual outcomes of events or decisions in a real economy.	The candidate finds it difficult to pinpoint strengths or limitations of economic models and theories in explaining real world issues and problems, or to compare and contrast alternative strategies or policy instruments.
<b>LEVEL 1</b>		The candidate makes only a limited attempt to select and use an appropriate form and style of writing. The organisation of material may lack clarity and coherence with little use of specialist vocabulary. Presentation, spelling, punctuation and grammar may be such that intended meaning is not clear.	The candidate makes valid connections between theoretical principles and real-world events.	The candidate shows ability to identify causes of economic problems and is able to relate these insights to real economies.	The candidate shows some awareness of the strengths and limitations of different economic models, theories, decisions and policies, and attempts to support observation with appropriate references.
<b>LEVEL 2</b>		The candidate shows sufficient knowledge of economic theory for the main issues involved in the question to be satisfactorily identified.			
<b>LEVEL 3</b>		The candidate makes a reasonable attempt to select and use an appropriate form and style of writing, supported with appropriate use of diagrams. Relevant material is organised with some clarity and coherence and some use of specialist vocabulary. Presentation, spelling, punctuation and grammar are sufficiently competent to make meaning evident.	The candidate relates concepts to situations and problems in real economies with some skill and can explain contemporary events while supporting conclusions with evidence.	The candidate is aware of the implications of hypotheses and distinguishes between association and causation in contemporary economic problems, offering valid suggestions as to how these may be addressed.	The candidate is able to critically examine alternative economic models, theories, arguments and policies in the analysis of economic problems and demonstrates the ability to evaluate the outcomes of economic decisions, supporting the analysis with accurate reference or relevant examples.
<b>HIGH GRADE</b>		The candidate successfully selects and uses an appropriate form and style of writing, supported with the effective use of diagrams where appropriate. Relevant material is organised with a high degree of clarity, coherence and widespread use of appropriate specialist vocabulary. Presentation, spelling, punctuation and grammar are of a sufficiently high standard to make meaning absolutely clear.			

- 1 (a) The balance of trade in goods is simply the difference between exports of goods and imports of goods, formerly known as the visible balance.

The balance of payment on current account includes:

- The balance of trade in goods.
- The balance of trade in services.
- Net income from abroad.
- Current transfers.

**Level 1 ([1]–[2])**

Candidate shows little knowledge or understanding of the difference between the balance of trade in goods and the current account balance. There is at best a superficial reference to one of the additional items which is included in the current account balance and quality of written communication is limited.

**Level 2 ([3]–[4])**

Candidate shows some knowledge and understanding of the difference between the balance of trade in goods and the current account balance. There is a reasonable explanation of at least two, or a detailed explanation of one of the additional items which are included in the current account balance and quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

Candidate shows detailed knowledge and understanding of the difference between the balance of trade in goods and the current account balance. There is a clear and detailed explanation of all of the additional items which are included in the current account balance and quality of written communication is of a high standard. [6]

- (b) The sterling trade weighted index measures changes in the value of the pound against a “basket” of other currencies. Obviously some currencies are much more important to the UK than others. For example the countries of the eurozone represent our largest trading partners. Hence the value of the pound against the euro is much more significant than the value of the pound against, for example, the Swiss franc. For this reason each currency is allocated a weighting which reflects its importance in UK trade. So the trade weighted index measures the pound’s value against a range of other currencies.

The eurozone and the USA have weightings of 65 per cent and 16 per cent respectively. In this respect it is similar to the composition of the Retail Price Index where each item is allocated a weighting which reflects its importance in the spending pattern of the “typical” household.

**Level 1 ([1]–[2])**

Candidate shows little understanding of how the value of sterling can be measured on a trade weighted basis. Quality of written communication is limited.

**Level 2 ([3]–[4])**

Candidate shows some understanding of how the value of sterling can be measured on a trade weighted basis, though this will be incomplete or contain minor errors. Quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

Candidate shows a clear and comprehensive understanding of how the value of sterling can be measured on a trade weighted basis. Quality of written communication is of a high standard. [6]

- (c) A fall in the value of the pound will make our exports cheaper for foreign buyers and make our imports more expensive for domestic purchasers. This should increase the volume of exports and reduce the volume of imports. Hence there will be an increase in the net export component of aggregate demand.

Issues for analysis and discussion include:

- Explanation of aggregate demand.
- Explanation of impact of fall in pound upon export and import prices.
- Explanation of impact upon net export component of aggregate demand.
- Diagram.

**Level 1 ([1]–[2])**

Candidate provides little analysis of how falling pound would be likely to affect aggregate demand. The key relationships are not explained and quality of written communication is limited.

**Level 2 ([3]–[5])**

Candidate provides some analysis of how falling pound would be likely to affect aggregate demand. The key relationships are explained though this may be incomplete or contain minor errors. Quality of written communication is satisfactory.

**Level 3 ([6]–[8])**

Candidate provides a clear and detailed analysis of how falling pound would be likely to affect aggregate demand. The key relationships are comprehensively explained and quality of written communication is of a high standard. [8]

- (d) There are a number of factors which might prevent the falling pound causing an increase in aggregate demand:
- Export sales might not increase because of the impact of the recession on world markets.
  - Export and import sales may not have adjusted yet because of time lags. (J curve effect)
  - The Marshall Lerner condition, with regard to the price elasticities of demand for exports and imports, may not be fulfilled.
  - Firms may adjust prices to compensate for exchange rate changes.
  - The falling pound has caused an outflow of funds from UK and exacerbated the credit crunch.

**Level 1 ([1]–[3])**

Candidate provides little analysis of why the falling pound might not stimulate aggregate demand. The key relationships are not explained and quality of written communication is limited.

**Level 2 ([4]–[7])**

Candidate provides some analysis of why falling pound might not stimulate aggregate demand. Key relationships are explained though the explanation may be incomplete or contain minor errors. Quality of written communication is satisfactory.

**Level 3 ([8]–[10])**

Candidate provides a clear and detailed analysis of why falling pound might not stimulate aggregate demand. The key relationships are comprehensively explained and quality of written communication is of a high standard. [10]

- (e) This is clearly a topical issue. The idea of buying local produce and protecting local businesses and jobs is very attractive during a recession. However it could be claimed that this is an example of a fallacy of composition in that if only one country does it then it might work but if everyone follows then not only does no one gain but there are is an overall welfare loss.

Issues for analysis and evaluation include:

- Infant industry argument for protection but is this relevant to shopping trips ?
- Strategic industry argument for protection but is this relevant to shopping trips ?
- Impact on consumer surplus and welfare of consumers by buying more expensive products in the South.
- Transfer of welfare from consumers to producers in the South if shoppers persuaded to stay at home.
- Thriving retail sector in North may employ labour from the South.
- Many of the products sold in the North are produced in the South, e.g. Jameson whiskey.
- Beneficial impact on employment and tax revenue in the South if shoppers stayed at home.
- Impact on the Republic's economy if other countries persuaded their citizens not to go shopping there.
- Experience of protectionist policies during The Great Depression of the 1930s.
- Possibility that such policies may be breach of EU or WTO rules.

**Level 1 ([1]–[3])**

Candidate shows little understanding of the economic implications of persuading southern citizens not to shop in the North. There is little economic analysis or evaluation and quality of written communication is limited.

**Level 2 ([4]–[7])**

Candidate shows some understanding of the economic implications of persuading southern citizens not to shop in the North. There is a degree of economic analysis and evaluation, though this may be shallow or contain errors, and quality of written communication is satisfactory.

**Level 3 ([8]–[10])**

Candidate shows a clear understanding of the economic implications of persuading southern citizens not to shop in the North. There is accurate economic analysis and in-depth evaluation and judgement.

Quality of written communication is of a high standard. [10]

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- 2 (a) Globalisation can be defined as the ever increasing integration of the world's local regional and national economies into a single international market (A. Anderton)

There are 5 aspects to globalisation:

- The free movement of goods and services between counties.
- The free movement of labour between countries.
- The free movement of capital between countries. This refers to both direct and portfolio investment.
- The free movement of technology between countries.
- Global marketing and creation of international brands.

**Level 1 ([1]–[2])**

Candidate shows little understanding of globalisation  
There is no significant explanations of its main features  
and quality of written communication is limited.

**Level 2 ([3]–[5])**

Candidate shows some understanding of globalisation. There is a degree of explanation of its main features, though this may be incomplete or contain minor errors and quality of written communication is satisfactory.

**Level 3 ([6]–[8])**

Candidate shows a clear understanding of globalisation and comprehensively explains its main features. Quality of written communication is of a high standard. [8]

- (b) The world recession started with the financial crisis known as the credit crunch which had its origins in the USA where banks made a number of injudicious loans to borrowers who were categorised as high risk or “sub prime”. As these loans became irrecoverable, banks became insolvent and this financial crises spread rapidly to British and eurozone banks which had bought many of these loans from their American counterparts. Many banks had to be rescued by their national governments.  
The speed and ease with which this crisis spread from the USA to banks throughout the world was in part the result of the integration of world financial markets which itself is part of the overall process of globalisation. The financial crisis rapidly became an economic crisis as the USA's demand for imports fell with a knock-on effect on European and Asian economies. The spread of a recession from the USA was also in part a consequence of globalisation.  
So the increased integration of the world's economies means that financial and economic crises are unlikely to be confined to one nation or region.

Issues for analysis and discussion include:

- Explanation of significance of integration of the world's financial markets and banking systems.
- Explanation of impact of recession on demand for exports and imports.
- Explanation of impact falling net exports upon aggregate demand in economies throughout the world.
- Explanation of impact of recession upon flows of migration.

**Level 1 ([1]–[5])**

Candidate provides little explanation of how globalisation has contributed to the spread of recession throughout the world. There is no significant economic analysis and quality of written communication is limited.

**Level 2 ([6]–[11])**

Candidate provides some explanation of how globalisation has contributed to the spread of recession throughout the world. There is a degree of economic analysis and quality of written communication is satisfactory.

**Level 3 ([12]–[16])**

Candidate provides a comprehensive explanation of how globalisation has contributed to the spread of recession throughout the world. There is clear and accurate economic analysis and quality of written communication is of a high standard. [16]

- (c) The issue of globalisation has been a controversial one for some time. Many on the political left see as it nothing more than a mechanism by which rich nations exploit poor ones whilst supporters of free markets would hail it as a vehicle for progress and prosperity.

Issues for analysis and evaluation include:

- Imports from low wage economies such as China have increased the welfare of consumers in developed nations.
- Some workers in developed economies have lost jobs as production has been switched to low wage economies.
- There has been increased prosperity in emerging economies such as China and India.
- There has been an increase in demand for food and raw materials which has driven up some prices.
- There has been a massive flow of migration to developed economies. This has depressed wages for some groups of workers.
- Industrialisation in emerging economies has been at a significant environmental cost.
- Integration of world markets and economies has facilitated the spread of the credit-crunch.

**Level 1 ([1]–[5])**

Candidate provides little meaningful evaluation of the relative costs and benefits of globalisation. There is no significant economic analysis and quality of written communication is limited.

**Level 2 ([6]–[11])**

Candidate provides some evaluation of the relative costs and benefits of globalisation, though this may lack depth or be one-sided. It is supported by a degree of economic analysis and quality of written communication satisfactory.

**Level 3 ([12]–[16])**

Candidate provides an in depth evaluation and judgement of the relative costs and benefits of globalisation. There is relevant and accurate economic analysis and quality of written communication is of a high standard. [16]

- 3 (a) A free trade area such as the North American Free Trade Agreement is a lower level of economic integration than a customs union. It simply requires that its members have free trade amongst themselves but their trading relationships with non-member states are not affected by the free trade agreement. A customs union goes one step further and requires that member states have a common external tariff against imports from countries outside the union.

**Level 1 ([1]–[2])**

Candidate shows little knowledge or understanding of the features of free trade areas and customs unions. Quality of written communication is limited.

**Level 2 ([3]–[5])**

Candidate shows some knowledge and understanding of the features of free trade areas and customs unions. Quality of written communication is satisfactory.

**Level 3 ([6]–[8])**

Candidate shows clear and extensive knowledge and understanding of the features of free trade areas and customs unions. Quality of written communication is of a high standard. [8]

- (b) Trade creation exists when consumption shifts from a relatively high cost producer to a lower cost producer. The removal of trade barriers within the customs union allows for greater specialisation and enables consumers to switch from high cost domestically produced goods to lower cost imports.  
Trade diversion exists when consumption shifts from a relatively low cost producer outside the customs union to a relatively high cost producer inside the union. There is a loss of consumer welfare as consumers now have to pay a higher price for the same product.

Issues for analysis and discussion include:

- Explanation of trade creation and how it may be achieved by joining a customs union.
- Explanation of trade diversion and how it may be a consequence of joining a customs union.
- Analysis using consumer and producer surplus.

- Benefits of specialisation.
- Appropriate diagrams.

**Level 1 ([1]–[5])**

Candidate provides no significant economic analysis of how both trade creation and trade diversion may be the result of a country joining a customs union. Quality of written communication is limited.

**Level 2 ([6]–[11])**

Candidate provides some economic analysis of how both trade creation and trade diversion may be the result of a country joining a customs union. However, this will tend to be incomplete or contain minor errors. Quality of written communication is satisfactory.

**Level 3 ([12]–[16])**

Candidate provides a clear and accurate economic analysis of how both trade creation and trade diversion may be the result of a country joining a customs union. Quality of written communication is of a high standard.

[16]

- (c) Inefficiency in a market exists when consumers buy from high cost rather than low cost producers and when production costs are not minimised. Most of the time this is the result of government intervention to protect a particular sector of the economy. The EU imposes much higher tariffs on imports of agricultural products than it does on imports of manufactured goods.

Issues for analysis and evaluation include:

- Explanation of the regime of support for European and American agriculture.
- Evaluation of arguments for this support eg need to treat agriculture as a strategic industry.
- Costs of agricultural support to taxpayers and food consumers.
- Impact of agricultural protection on third world producers.
- Experience of countries like New Zealand which have abolished government support for agriculture.
- Positive externalities from a well maintained countryside.

**Level 1 ([1]–[5])**

Candidate shows little understanding of the issues involved in removing government support and protection from agriculture. There is no significant evaluation and quality of written communication is limited.

**Level 2 ([6]–[11])**

Candidate shows some understanding of the issues involved in removing government support and protection from agriculture. There is a degree of evaluation though this may lack depth and balance. Quality of written communication is satisfactory.

**Level 3 ([12]–[16])**

Candidate shows a clear understanding of the issues involved in removing government support and protection from agriculture. There is in-depth evaluation and judgement. Quality of written communication is of a high standard.

[16]

- 4 (a) An import tariff is a tax on imported goods. It may be used to either to raise revenue for the government or to restrict imports. An administrative barrier exists when governments restrict imports on health and safety or similar grounds but where the real motive is a desire to protect domestic producers.

Appropriate development:

- Explanation of tariff.
- Appropriate diagram.
- Examples.
- Explanation of administrative barrier.
- Reasons for use of administrative barriers.
- Examples.
- Role of WTO and EU

**Level 1 ([1]–[2])**

Candidate shows little knowledge or understanding of import tariffs and administrative barriers. Definitions are seriously flawed, development is virtually non-existent and quality of written communication is limited.

**Level 2 ([3]–[5])**

Candidate shows some knowledge and understanding of import tariffs and administrative barriers. Definitions are reasonable though may be incomplete or contain minor errors. There is a degree of development and quality of written communication is satisfactory.

**Level 3 ([6]–[8])**

Candidate shows detailed knowledge and understanding of import tariffs and administrative barriers. There are flawless definitions, extensive development and quality of written communication is of a high standard.

[8]

- (b) David Ricardo who developed the model of comparative advantage in the early 19th century argued that specialising according to the concept of comparative advantage would increase the total value of world output and create higher levels of economic growth. This would still be true even when one country had an absolute advantage over another in both products. Trade could still benefit both so long as they had different opportunity cost ratios. The more efficient nation should specialise in the sector in which its advantage was most marked and discontinue production of the other item, hence free up resources for the more valuable item.

Issues for analysis and discussion include:

- Assumptions of the model of comparative advantage such as zero transport costs.
- The 2 country, 2 product model.
- Analysis showing different opportunity cost ratios.
- Analysis showing increased welfare for both consumers and producers as a result of specialisation and trade.
- Analysis of how pattern of exports and imports could be determined by comparative advantage

#### **Level 1 ([1]–[5])**

Candidate gives no significant explanation how the theory of comparative advantage might determine a country's pattern of exports and imports. There is no credible attempt at an example and quality of written communication is limited.

#### **Level 2 ([6]–[11])**

Candidate gives a partial explanation how the theory of comparative advantage may determine a nation's pattern of exports and imports. There is a credible attempt at an example though this may contain errors. Quality of written communication is satisfactory.

#### **Level 3 ([12]–[16])**

Candidate gives a clear explanation how the theory of comparative advantage may determine a nation's pattern of exports and imports. There is a well explained example and quality of written communication is of a high standard. [16]

- (c) The theory of comparative advantage is a simple model based on a number of unrealistic assumptions such as zero transport and other transaction costs. Since these conditions are unlikely to be replicated in the real world it follows that conclusions based on the theory may be flawed.

Issues for evaluation and discussion include:

- The immobility of resources.
- The time taken for adjustment may be so long as to make the process irrelevant.
- Economies of scale may create dynamic comparative advantage.
- Infant industries may grow and achieve dynamic comparative advantage.
- The gains from trade may be unevenly distributed.

#### **Level 1 ([1]–[5])**

Candidate displays little understanding of the conditions attached to the theory of comparative advantage and provides no significant evaluation of the validity of using the theory to justify free trade. Quality of written communication is limited.

#### **Level 2 ([6]–[11])**

Candidate displays some understanding of the conditions attached to the theory of comparative advantage and provides a degree of evaluation of the validity of using the theory to justify free trade. This evaluation will tend to lack depth or be unbalanced. Quality of written communication is satisfactory.

**Level 3 ([12]–[16])**

Candidate displays a clear understanding of the conditions attached to the theory of comparative advantage and provides in-depth evaluation and judgement of the validity of using the theory to justify free trade.

Quality of written communication is of a high standard.

[16]

40

**Total**

**80**



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**General Certificate of Education**  
**January 2010**

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## **Economics**

**Assessment Unit A2 3**

*assessing*

Module 5: Economic Development and  
the Environment and  
Module 6: Financial Economics

**[A2E31]**

**TUESDAY 2 FEBRUARY, AFTERNOON**

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# **MARK SCHEME**

## General Marking Instructions

This mark scheme is intended to ensure that the A2 examination is marked consistently and fairly. The mark scheme provides markers with an indication of the nature and range of candidate responses likely to be worthy of credit. It also sets out the criteria which they should apply in allocating marks to candidates' responses. The mark scheme should be read in conjunction with these general marking instructions which apply to all papers.

### Quality of candidates' responses

In marking the examination papers, examiners will be looking for a quality of response reflecting the level of maturity which may reasonably be expected of an 18-year-old which is the age at which the majority of candidates sit their A2 examinations.

### Unanticipated responses

The mark schemes which accompany the specimen examination papers are not intended to be totally prescriptive. For many questions, there may be a number of equally legitimate responses and different methods by which the candidates may achieve good marks. No mark scheme can cover all the answers which candidates may produce. In the event of unanticipated answers, examiners are expected to use their professional judgement to assess the validity of answers and to refer for guidance to the general marking criteria that follow. If an answer is particularly problematic, then examiners should seek the guidance of the Supervising Examiner for the paper concerned.

### Positive marking

Examiners are encouraged to be positive in their marking, giving appropriate credit for valid responses rather than penalising candidates for errors or omissions. Examiners should make use of the whole of the available mark range for any particular question and be prepared to award full marks for a response which is as good as might reasonably be expected for an 18-year-old A2 candidate. Conversely, marks should only be awarded for valid responses and not given for an attempt which is completely incorrect or inappropriate.

### Marking calculations

In marking answers involving calculations, examiners should apply the 'own figure rule' so that candidates are not penalised more than once for a computational error.

### Types of mark schemes

Mark schemes for questions which require candidates to respond in extended written form are marked on the basis of levels of response which take account of the quality of written communication. These questions are indicated on the cover of the examination paper.

Other questions which require only short answers are marked on a point for point basis with marks awarded for each valid piece of information provided.

## Quality of written communication

Quality of written communication is taken into account in assessing candidates' responses to all questions that require them to respond in extended written form. These questions are marked on the basis of levels of response. The description for each level of response includes reference to the quality of written communication. Where the quality of candidates' economics is not matched by the quality of written communication, marks awarded will not exceed the maximum for Level 2.

## Levels of response

General descriptions of levels of response in terms of each assessment objective and the quality of written communication are given in the following table. These descriptions are intended to assist examiners in judging candidates' performance when they produce answers unanticipated by the detailed mark scheme for each question and to provide guidelines for examiners in assessing the appropriate level of response in respect of the quality of written communication.

The detailed mark schemes for each question relate these levels of response to the content of the relevant question. In deciding which mark within a particular level to award any response, examiners are expected to use their professional judgement. The following guidance is provided to assist examiners.

**Threshold performance:** Response which just merits inclusion in this level and should be awarded a mark at or near the bottom of the range.

**Intermediate performance:** Response which clearly merits inclusion in the level and should be awarded a mark at or near the middle of the range.

**High performance:** Response which fully satisfies the level description and should be awarded a mark at or near the top of the range.

**General Marketing Criteria**

<b>Level of Performance</b>	<b>Assessment Objective</b>	<b>AO1 Knowledge and Understanding</b>	<b>A02 Application</b>	<b>A03 Analysis</b>	<b>A04 Evaluation and judgement</b>
<b>BENEATH THRESHOLD</b>		There may be limitations in the candidate's grasp of theoretical principles, resulting in an excessively narrow focus on the issues involved in the question.	The candidate tends to make unsubstantiated generalisations, and superficial assumptions, lacking any real awareness of contemporary events.	The candidate is likely to confuse hypotheses with facts and does not successfully account for divergences between theoretically predicted and actual outcomes of events or decisions in a real economy.	The candidate finds it difficult to pinpoint strengths or limitations of economic models and theories in explaining real world issues and problems, or to compare and contrast alternative strategies or policy instruments.
<b>LEVEL 1</b>		The candidate makes only a limited attempt to select and use an appropriate form and style of writing. The organisation of material may lack clarity and coherence with little use of specialist vocabulary. Presentation, spelling, punctuation and grammar may be such that intended meaning is not clear.	The candidate makes valid connections between theoretical principles and real-world events.	The candidate shows ability to identify causes of economic problems and is able to relate these insights to real economies.	The candidate shows some awareness of the strengths and limitations of different economic models, theories, decisions and policies, and attempts to support observation with appropriate references.
<b>LEVEL 2</b>		The candidate shows sufficient knowledge of economic theory for the main issues involved in the question to be satisfactorily identified.			
<b>LEVEL 3</b>		The candidate makes a reasonable attempt to select and use an appropriate form and style of writing, supported with appropriate use of diagrams. Relevant material is organised with some clarity and coherence and some use of specialist vocabulary. Presentation, spelling, punctuation and grammar are sufficiently competent to make meaning evident.	The candidate relates concepts to situations and problems in real economies with some skill and can explain contemporary events while supporting conclusions with evidence.	The candidate is aware of the implications of hypotheses and distinguishes between association and causation in contemporary economic problems, offering valid suggestions as to how these may be addressed.	The candidate is able to critically examine alternative economic models, theories, arguments and policies in the analysis of economic problems and demonstrates the ability to evaluate the outcomes of economic decisions, supporting the analysis with accurate reference or relevant examples.
<b>HIGH GRADE</b>		The candidate successfully selects and uses an appropriate form and style of writing, supported with the effective use of diagrams where appropriate. Relevant material is organised with a high degree of clarity, coherence and widespread use of appropriate specialist vocabulary. Presentation, spelling, punctuation and grammar are of a sufficiently high standard to make meaning absolutely clear.			

**Section A**

**Module 5: Economic Development and the Environment**

- 1 (a) According to some scientists, climate change is now inevitable.
- This means that any resources used in trying to prevent it are wasted.
  - It makes better sense to use resources to try to deal with the effects of climate change. This may require drastic actions such as movements of population away from areas at risk from rising sea levels.
- [2] marks for each point explained [4]
- (b) Poorer countries are likely to suffer more as a result of climate change for a variety of reasons.
- The geographical location of most of the world's poorest countries makes them more vulnerable to flooding or drought than countries in temperate zones
  - LDCs traditionally are more dependent on specialisation in a narrow range of outputs and are less flexible in their response to any form of change
  - One of the features which keeps nations in poverty is a lack of infrastructure
  - Traditional paths to development involve industrialisation; this would add to current ecological problems and is likely to be impeded by powerful nations
  - Poorer countries would have no choice but to endure consequences of whatever strategies were employed by richer ones

**Level 1 ([1]–[2])**

The candidate shows little knowledge or understanding as to why poorer countries are most at risk. Quality of written communication is limited.

**Level 2 ([3]–[4])**

The candidate shows some knowledge and understanding as to why poorer countries are most at risk. Quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

The candidate shows extensive insight into why poorer countries are most at risk. Quality of written communication is of a high standard. [6]

- (c) External costs include loss of livelihoods and increased risks of death by starvation or as a result of greater frequency of extreme weather incidents, such as gales.

Local environments may deteriorate to the point where they become uninhabitable or, as a result of higher sea levels, simply disappear.

Increasing shortages of water and energy resources could lead to political unrest and increased frequency of armed conflict.

Up to [2] marks for each point well explained, to a constrained maximum of [4] [4]

- (d) Conventionally, economists regard government intervention as the appropriate response to market failure, but when failures threaten the long-term welfare of firms, there is evidence that the most efficient firms will look for solutions, too.

Issues, analysis and areas for discussion would include the following:

- emergence and identification of markets for alternative technologies
- private development of alternative sources of energy as tax and regulation make use of carbon fuels less attractive
- increased focus on identifying future problems
- increased incentive for investment in new production techniques
- recognition that climate change will accelerate decline of some industries or some productive regions, alongside the need for adjustment to new opportunities

**Level 1 ([1]–[2])**

The candidate is able to quote Stern’s belief that there are business opportunities in the provision of new technologies, but does not develop the idea. Quality of written communication is limited.

**Level 2 ([3]–[4])**

The candidate shows some understanding that widespread market failures may result in creation of new markets. Quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

The candidate shows insight that serious disruption of existing markets imposes pressure on firms to adapt, and that profits may motivate some firms to adapt more quickly. Quality of written communication is of a high standard.

[6]

- (e) Big problems persist, but there is more than one reason to be more “cheerful” :
- ordinary people’s desire to address the problems may be increased by unease at some of the recent alternative proposals for “geo-engineering”
  - there may be less cause to fear that “greener” production in MEDCs will simply divert production to other countries when world demand is depressed
  - American apathy in the past has been a bar to progress on agreements about Kyoto targets. The new President is sensitive to a change in the public mood and has appointed a special envoy on climate change
  - existing businesses in danger of closure due to falling demand may be more motivated to switch to alternative technologies
  - attitudes to high-spending projects may have changed after the banking crisis
  - recent disruptions in supplies of “fossil” energy sources may lead to more favourable attitudes towards adoption of renewable energy

**Level 1 ([1]–[3])**

The candidate provides no significant evaluation of the merits of the proposition. Quality of written communication is limited.

**Level 2 ([4]–[7])**

The candidate identifies some causes of the new optimism and provides some evaluation of the proposition however this may be one-sided or lack depth. Quality of written communication is satisfactory.

**Level 3 ([8]–[10])**

The candidate provides an in-depth evaluation and judgement of the proposition. Quality of written communication is of a high standard. [10]

- 2 (a) The concept of sustainable economic welfare involves an attempt by economists to measure standards of living in a generally consistent way which takes account of quality of life and responsibilities for future generations.

A good answer would take account of most of the following points :

- all economists recognise the importance of material welfare; it is commonly agreed that GDP per person is an acceptable measure of this,
- allowance for other aspects of human welfare may be made by considering such factors as crime rates, family stability and social networks,
- living and working conditions are also important considerations, as are standards of justice, education and health services,
- assessments about the sustainability of national ‘lifestyle’ involve recognition that certain established systems and sets of values confer benefits which endure over time,
- valuation of negative externalities such as pollution, and the consequences of depletion of capital and other resources are important indicators of future problems.

**Level 1 ([1]–[2])**

The candidate shows little knowledge or understanding of the idea of sustainable economic welfare. Quality of written communication is limited.

**Level 2 ([3]–[4])**

The candidate shows some knowledge and understanding of the idea of sustainable economic welfare. Quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

The candidate shows extensive knowledge and understanding of the idea of sustainable economic welfare. Quality of written communication is of a high standard. [6]

- (b) The national income statistics record all incomes within an economy, after allowing for depreciation, over the period of a year. These can be measured by the income, expenditure or output methods. They are based on the “circular flow of income” model. In practice there will be some differences because of problems in gathering information. The figures are commonly used to compare performance over time and between countries.

Issues, analysis and areas for discussion would include the following:

- possible uses and users of the statistics
- the impact of self-provided goods
- climatic differences and their impact on statistics
- differences in composition of national output
- working practices and proximity to workplaces
- difficulties with currency conversion
- possible divergence in patterns of income distribution
- variations in accuracy due to different levels of efficiency in administration

**Level 1 ([1]–[4])**

The candidate provides little explanation of the problems involved in comparing economic welfare between different countries. Quality of written communication is limited.

**Level 2 ([5]–[8])**

The candidate provides some explanation of the problems involved in comparing economic welfare between different countries. Quality of written communication is satisfactory.

**Level 3 ([9]–[12])**

The candidate provides a clear explanation of the problems involved in comparing economic welfare between different countries.

Quality of written communication is of a high standard. [12]

- (c) Even in developed countries there are occasional instances of absolute poverty. Statistics which focus on positive aspects of welfare and development may conceal problems. Inequality in the distribution of income is an acknowledged defect of using GDP per person as an indicator of average welfare. This is particularly true of many African countries where small social, regional or tribal groups may enjoy disproportionate privilege. The United Nations Human Development Programme uses a two-part indicator of particular and acute need. The Human Poverty Index (HPI) concentrates on various measures of deprivation : low income in money terms; low levels of literacy and lack of educational opportunities; and poor health as measured by infant mortality and lack of access to clean water. The HPI-2 focuses on these deficiencies in more economically developed countries. This helps identify social exclusion, whether deliberate or as a consequence of cultural difference, of particular social or ethnic groups. Understanding of poverty may help target efforts of relief agencies and NGOs where it is most needed.

On the other hand, the implication above is that intervention in the domestic affairs of sovereign nations is always practicable or justifiable. Concentration on failures of development provides no useful evidence of which policies most successfully improve quality of life. Welfare measures are necessary for valid comparisons to be made for the purposes, for example, of assessing scales of contribution to international co-operative agencies.

**Level 1 ([1]–[4])**

The candidate provides no significant evaluation of the merits of the proposition. Quality of written communication is limited.

**Level 2 ([5]–[8])**

The candidate provides some evaluation of the importance of paying specific attention to the welfare of the most deprived members of any society however this may be one-sided or lack depth. Quality of written communication is satisfactory.

**Level 3 ([9]–[12])**

The candidate provides an in-depth evaluation and judgement of the proposition. Quality of written communication is of a high standard. [12]

30

- 3 (a) Benefits of a public good are not diminished by consumption. Improvements in air or water quality are experienced by the whole population; utility received by one person does not reduce the utility available to that person's neighbour. Consumption of a public good may not be denied to individuals ("free-riders") who may avoid paying for it. Clearly, also, a healthy environment is not a commodity from which anyone may be readily excluded. For this reason, development of free markets for public goods is considered unlikely, and their provision is generally seen as a responsibility of government. This is certainly the case with policing and enforcing environmental protection policies. A corollary to this is that dissenters may not refuse such environmental benefits.

**Level 1 ([1]–[2])**

The candidate does not clearly identify characteristics of a public good, nor relate them to ideas about the environment. Quality of written communication is limited.

**Level 2 ([3]–[4])**

The candidate understands some characteristics of a public good, and is partly aware of their relevance in environmental issues. Quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

The candidate demonstrates clear understanding of the relevance of characteristics of a public good in the context of the environment. Quality of written communication is of a high standard. [6]

- (b) Governments may try to limit environmental damage at the supply side through a variety of measures, which involves restrictive legislation, including licensing; taxation and subsidy; and attempts to replicate elements of a market.
- **Regulation**, e.g. banning either all production, or certain methods of production. Smoke pollution is a good example. However, regulation may be expensive to enforce and is sometimes ineffective. It can be a very blunt instrument in that it is difficult to design to avoid affecting all production and the economically efficient level of pollution is not usually zero.
  - **Tax (Pigovian)**. If correctly applied, this should shift the supply curve to the left and result in socially efficient price and output. However, there are disadvantages that :
    - it is virtually impossible to determine the “correct” level of tax in order to engineer a socially efficient supply curve,
    - it does not discriminate between “clean” and “dirty” producers,
    - it may be costly to collect and enforce.
  - **Government subsidies** (to encourage clean production methods).
  - **Tradable pollution permits**. These have the advantage of giving firms a financial incentive to cut pollution. They allow “clean” firms to sell their permits and require “dirty” firms to buy them. Problems include:
    - establishing the level of pollution which each firm is permitted,
    - difficulty of measurement and enforcement,
    - possibility of concentrating pollution in particular geographical areas.

**Level 1 ([1]–[4])**

The candidate may identify some government policies, but lacks clear insight into their intended or actual operation. Quality of written communication is limited.

**Level 2 ([5]–[8])**

The candidate shows awareness of steps available to government in limiting environmental damage, but development is inaccurate or incomplete. Quality of written communication is satisfactory.

**Level 3 ([9]–[12])**

The candidate is aware of a range of policies to limit the damage producers may cause the environment and explains with some skill their effects in theory and practice.

Quality of written communication is of a high standard. [12]

- (c) In a market economy, creating or responding to changes in patterns of demand or behaviour may not be a simple task for government planners. Many responsible observers, themselves concerned about world climate, have expressed worries that promotion of bio-fuels is an example of an ill-considered (“knee-jerk”) response to lobbying. Governments are keen to be seen to be doing something; what they may be persuaded to do may not always be constructive.

Other issues for discussion include the following:

- businesses may respond to pressure from consumers in ways that are little more than cosmetic. It might be argued that some supermarkets project an appearance of “green” concern by such devices as charging for plastic carrier bags. Consumers may satisfy themselves that they are helping the environment by supporting such shops, rather than investigating or objecting to more ecologically unfriendly practices,
- a well-known challenge to the culture of re-cycling quotes an example of the person who drives some distance to deposit a few items in the bottle bank,
- of course, there are criticisms with less validity, such as arguments that there is no point in trying to do good if most other people are doing wrong,
- there are examples of cases where public opinion has influenced business planners towards “greener” thinking, and attitudes to dropping litter or conserving energy can be changed in the long term,
- campaigners for change can influence others, at least by example,
- activities such as re-cycling can be economically justifiable; firms would not be interested in collecting glass, for example, if it were unprofitable.

Arguments that human activity may not be the sole cause of global warming, or warnings that it is already too late to reverse climate change, do not make sensible, well-informed action designed to prolong the health of the environment irrelevant.

**Level 1 ([1]–[4])**

The candidate provides no significant evaluation of relevant issues. There may be a brief, one-sided defence of environmentalist action. Quality of written communication is limited.

**Level 2 ([5]–[8])**

The candidate provides some evaluation of issues in the environmental debate, although this will typically lack depth or balance. Quality of written communication is satisfactory.

**Level 3 ([9]–[12])**

The candidate provides an in-depth evaluation and judgement of the sceptics’ point of view, and of the usefulness of private actions in support of the environment. Quality of written communication is of a high standard.

[12]

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**Section A**

**90**

**Section B**

**Module 6: Financial Economics**

- 1 (a) • The FTSE 100 index measures the average share price of the largest 100 companies on London stock market. [2]  
 • It is a weighted average with the largest companies having the greatest impact on the index [1]  
 • It is an index number with a base of 1000 in January 1984 [1]  
 Constrained maximum of [3] marks [3]
- (b) The FTSE 100 index started in January 2008 with a value of 5800. Since then it has fallen almost continuously to reach 4100 in February 2009. This is a fall of 29 %.  
 RBS shares started 2008 with a price of 340 pence. Since then it has fallen almost continuously to reach 10 pence in February 2009. This is a fall of approx 97%.  
 Obviously the fall in the RBS share price has been much greater than that for the FTSE 100  
 [2] marks for calculating the percentage fall in the share price of RBS.  
 [2] marks for calculating the percentage fall in the FTSE.  
 [1] mark for stating that the RBS share price has fallen much more than the FTSE. [5]
- (c) The main reason for the fall in the RBS share price is the magnitude of its losses which for 2008 were the largest ever recorded for any UK company. These losses were the result of a number of factors:
- A large number of loans to sub-prime borrowers in the USA, These mortgages are unlikely ever to be repaid and so will have to be written off.
  - Many of these mortgages were the result of the take over of ABN Amro.
  - Excessive borrowing to fund acquisition of banks, many of which have fallen significantly in value.
  - Excessive bonuses and salary packages to senior executives.

**Level 1 ([1]–[2])**

Candidates provide no significant explanation of the reasons for the fall in the share prices of RBS. Quality of written communication is limited.

**Level 2 ([3]–[4])**

Candidates provide some explanation of the reasons for the fall in the share price of RBS. However this will be incomplete or contain minor errors and quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

Candidates provide a clear and comprehensive explanation of the reasons for the fall in the share price of RBS and quality of written communication is of a high standard. [6]

- (d) The FSA could have taken a number of steps which would have prevented the banking crisis:
- It could have more closely supervised bank lending to ensure that it was not lending excessively to high risk or sub-prime borrowers who were unlikely to repay their loans.
  - It could have intervened to restrict the excessive salaries and bonuses paid to senior bank executives.
  - It could have prevented RBS's aggressive programme of mergers and expansion.

**Level 1 ([1]–[2])**

Candidate provides little explanation of the ways in which the FSA might have prevented the banking crisis. There may be vague assertions but little substance and quality of written communication is limited.

**Level 2 ([3]–[4])**

Candidate provides some explanation of the ways in which the FSA might have prevented the banking crisis. However this may be incomplete or contain errors and quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

Candidate provides a clear and comprehensive explanation of the ways in which the FSA might have prevented the banking crisis. Quality of written communication is of a high standard. [6]

- (e) Many UK banks have experienced severe financial difficulties and lacked the funds to repay the depositors who wished to withdraw their savings. This has led the government to either nationalise or part nationalise many banks and to guarantee the security of customers' savings. At present some 70% of RBS's shares have been acquired by the government at a cost of £20 billion

Issues for analysis and evaluation include:

- Cost to the taxpayer of the rescue packages.
- Possible domino effect, leading to the collapse of other banks, if Northern Rock and RBS had not been rescued.
- Risks involved in fractional banking.
- Failure of FSA to properly monitor UK bank lending.
- Wider impact on macro economy of a major bank collapse.
- Unique position of banks in the economy.
- Moral issue of rescuing a badly run business. If it's ok to save RBS then why not every other business in financial difficulties?

**Level 1 ([1]–[3])**

Candidate shows little understanding of the issues involved in the government granting financial support to UK banks. There is no significant evaluation of the decision and quality of written communication is limited.

**Level 2 ([4]–[7])**

Candidate shows some understanding of the issues involved in the government granting financial support to UK banks. There is a degree of evaluation of the decision, though this will lack depth or balance. Quality of written communication is satisfactory.

**Level 3 ([8]–[10])**

Candidate shows a clear understanding of the issues involved in the government granting financial support to UK banks. There is in-depth evaluation and judgement of the decision. Quality of written communication is of a high standard.

[10]

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- 2 (a) Monetary policy is the attempt by government or the central bank to influence key monetary variables in order to achieve its policy objectives such as price stability.

The key monetary variables are:

- Availability of liquidity to banking system
- Money supply
- Supply of credit
- Interest rates.

It should be noted that the central bank can only control the rate at which it lends to the banking system and not all interest rates in the economy.

**Level 1 ([1]–[2])**

Candidate shows little understanding of monetary policy. There may be vague references to terms like the rate of interest but no serious development. Quality of written communication is limited.

**Level 2 ([3]–[4])**

Candidate shows some understanding of monetary policy. There is a degree of explanation of terms like the rate of interest but this will be incomplete or contain minor errors. Quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

Candidate shows a clear understanding of monetary policy. There is a comprehensive explanation of its key features and quality of written communication is of a high standard.

[6]

- (b) The most important instrument in a contractionary monetary policy is an increase in the rate of interest. If the B of E increases its repo rate then this is likely to lead to rise in all interest rates throughout the economy. The route by which higher interest rates affect the price level is known as the transmission mechanism. Other possible policies include the over-issuance of gilts to remove liquidity from the banking system.

Issues for analysis and discussion include the impact of higher interest rates on:

- House prices
- Other asset prices such as shares
- Market for consumer durables and other interest rate sensitive items
- Investment
- Saving
- The exchange rate.

Candidates might choose to illustrate this by aggregate demand and supply analysis.

#### **Level 1 ([1]–[4])**

Candidate provides little analysis of the impact of a contractionary monetary policy on the rate of inflation. Key linkages are not explored and quality of written communication is limited.

#### **Level 2 ([5]–[8])**

Candidate provides some analysis of the impact of a contractionary monetary policy on the rate of inflation. However this will be incomplete or contain minor errors and quality of written communication is satisfactory.

#### **Level 3 ([9]–[12])**

Candidate provides a clear and detailed analysis of the impact of a contractionary monetary policy on the rate of inflation. Quality of written communication is of a high standard.

[12]

- (c) In 1997 the Bank of England was given responsibility for setting an interest rate appropriate for achieving the government's inflation target. For many years it appeared as if the Bank had been successful in meeting this target. However the recent banking crisis has led many commentators to question this success. They point out that low interest rates have fuelled an unsustainable housing boom which was the basis of the financial crisis. Perhaps the Bank should have acted earlier to deal with house price inflation rather than focusing exclusively on retail price inflation.

Issues for analysis and evaluation include:

- Bank of England should have control to prevent political manipulation of monetary policy.
- Suspicion that government may be able to exert pressure on Bank of England, meaning that political manipulation may still take place.
- Monetary policy committee of Bank of England is composed of "expert" economists who should in theory make better decisions than politicians who may lack economic expertise.
- Relative success of Bank of England in meeting the inflation target until 2008.
- Was excluding house prices from the inflation target a policy error?
- If so who was responsible?
- Governments may take a broader view when setting monetary policy and not just focus on inflation.
- Were interest rates kept too low for too long and a cause of reckless lending and borrowing?

**Level 1 ([1]–[4])**

Candidate shows little understanding of the issues involved in the setting of monetary policy. There is no serious evaluation of the proposition and quality of written communication is limited.

**Level 2 ([5]–[8])**

Candidate shows some understanding of the issues involved in the setting of monetary policy. There is a degree of evaluation of the proposition, though will lack depth or balance and quality of written communication is satisfactory.

**Level 3 ([9]–[12])**

Candidate shows a clear understanding of the issues involved in the setting of monetary policy. There is in-depth evaluation and judgement of the proposition. Quality of written communication is of a high standard. [12]

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**3 (a) The most important source of revenue for government is taxation.**

Other sources are:

- Borrowing,
- Privatisations,
- Direct sale of goods and services, e.g. passports,
- Private finance initiatives.

**Level 1 ([1]–[2])**

Candidate shows little knowledge or understanding of the main sources of government revenue. There may be a brief reference to tax but little development and quality of written communication is limited.

**Level 2 ([3]–[4])**

Candidate shows some knowledge and understanding of the main sources of government revenue and quality of written communication is satisfactory.

**Level 3 ([5]–[6])**

Candidate shows detailed knowledge and understanding of the main sources of government revenue and quality of written communication is of a high standard. [6]

**(b) Government finances are likely to be adversely affected by a recession.**

Tax revenues will fall and welfare spending will increase.

Issues for analysis and discussion include:

- Impact of recession on income tax and corporation tax.
- Impact of recession on house prices and stamp duty tax.
- Impact of recession on VAT and other indirect taxes
- Impact of recession on unemployment and welfare benefits.

**Level 1 ([1]–[4])**

Candidate provides little analysis of the impact of a recession on government finances. Key issues are missed and quality of written communication is limited.

**Level 2 ([5]–[8])**

Candidate provides some analysis of the impact of a recession on government finances. Most issues are explained though the explanation may be incomplete or contain minor errors. Quality of written communication is satisfactory.

**Level 3 ([9]–[12])**

Candidate provides a clear and accurate analysis of the impact of a recession on government finances. Key issues are thoroughly explained and quality of written communication is of a high standard. [12]

- (c) A progressive tax is one where the percentage paid in tax rises with income. To make the tax “steeply” progressive would require a large number of marginal tax rates and tax bands. This is administratively cumbersome and expensive for both tax payer and tax collector. However progressive tax systems may be justified on the basis of equity and redistribution.

Issues for analysis and evaluation include:

- Explanation of operation of progressive tax system
- Administrative costs of progressive tax system
- Disincentive effects and impact on economic growth
- Redistributive impact
- Impact on inward investment
- Possible migration of capital and skilled labour
- Historical and international examples.

**Level 1 ([1]–[4])**

Candidate shows little understanding of progressive tax systems. There is no significant evaluation of their desirability and quality of written communication is limited.

**Level 2 ([5]–[8])**

Candidate shows some understanding of progressive tax systems. There a degree of evaluation of their desirability, though this is likely to lack depth or balance, and quality of written communication is satisfactory.

**Level 3 ([9]–[12])**

Candidate shows a clear understanding of progressive tax systems. There is in-depth evaluation and judgement of their desirability. Quality of written communication is of a high standard. [12]

**Section B**

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**90**

**Total**

**180**





