



Rewarding Learning

**ADVANCED
General Certificate of Education
2012**

Economics

Assessment Unit A2 2

assessing

The Global Economy

[AE221]

FRIDAY 25 MAY, MORNING

MARK SCHEME

General Marking Instructions

This mark scheme is intended to ensure that the A2 examinations are marked consistently and fairly. The mark scheme provides examiners 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 paper, examiners will be looking for a quality of response reflecting the level of maturity which may reasonably be expected of 18-year-olds, which is the age at which the majority of candidates sit their A2 examinations.

Flexibility in marking

The mark scheme is 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. 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 18-year-old candidates. Conversely, marks should only be awarded for valid responses and not given for an attempt which is completely incorrect and 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.

Levels of response

Questions requiring candidates to respond in extended writing are marked in terms of levels of response. In deciding which level of response to award, examiners should look for the "best fit" bearing in mind that weakness in one area may be compensated for by strength in another. 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 the 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.

Marking calculations

In marking answers involving calculations, examiners should apply the “own figure” rule. 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 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 in questions which have three levels of response or the maximum for Level 3 in those which have four levels of response.

For conciseness, quality of written communication is distinguished within levels of response as follows:

Level 1: Quality of written communication is limited.

Level 2: Quality of written communication is satisfactory.

Level 3: Quality of written communication is of a high standard.

Level 4: Quality of written communication is excellent.

In interpreting these level descriptions, examiners should refer to the more detailed guidance provided below:

Level 1 (Limited): 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. There is little use of specialist vocabulary. Presentation, spelling, punctuation and grammar may be such that intended meaning is not clear.

Level 2 (Satisfactory): The candidate makes a reasonable attempt to select and use an appropriate form and style of writing, supported with appropriate use of diagrams as required. Relevant material is organised with some clarity and coherence. There is some use of appropriate specialist vocabulary. Presentation, spelling, punctuation and grammar are sufficiently competent to make meaning evident.

Level 3 (High Standard): The candidate successfully reflects 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 and coherence. There is widespread use of appropriate specialist vocabulary. Presentation, spelling, punctuation and grammar are of a sufficiently high standard to make meaning clear.

Level 4 (Excellent): The candidate successfully reflects and uses the most appropriate form and style of writing, supported with precise and accurate use of diagrams where appropriate. Relevant material is extremely well organised with the highest degree of clarity and coherence. There is extensive and accurate use of appropriate specialist vocabulary. Presentation, spelling, punctuation and grammar are of the highest standard and ensure that meaning is absolutely clear.

- 1 (a) • the pound's value in euros at the start of the period was €1.60 and at the end of the period it was €1.20. This represents a fall of 25 per cent
- the pound's value in US dollars at the start of the period was around \$1.42 and at the end of the period it was around \$1.55. This represents a rise of approximately 9 per cent
 - obviously the pound has fared much better against the US dollar than against the euro.

[2] for describing trend against euro, [1] if percentage change not calculated

[2] for describing trend against dollar, [1] if percentage change not calculated

[1] for any other relevant point, e.g. pound has performed better against dollar than euro

For narrative approach with no attempt at manipulation maximum [2]

Constrained maximum of [5] [5]

- (b) Some 66 per cent of UK trade is with the rest of the EU and a slightly lower percentage with eurozone members. Hence, any significant rise in the rate of exchange of the pound against the euro would have a major impact on the UK economy.

Issues for analysis and discussion include:

- explanation of how stronger pound causes lower import prices
- explanation of impact of lower import prices on wage settlements
- explanation of impact of stronger pound on raw material costs
- explanation of how stronger pound causes more expensive exports
- explanation of impact on aggregate demand and growth in the UK
- explanation of impact on UK employment and unemployment.

Level 1 ([1]–[3])

- candidate provides little explanation of the impact of a rise in the pound/euro exchange rate upon the UK economy
- there may be vague anecdotal assertions but little economic analysis
- quality of written communication is limited.

Level 2 ([4]–[7])

- candidate provides some explanation of the impact of a rise in the pound/euro exchange rate upon the UK economy
- there is a degree of economic analysis but this is likely to be incomplete or contain errors
- quality of written communication is satisfactory.

Level 3 ([8]–[10])

- candidate provides a clear and comprehensive explanation of the impact of a rise in the pound/euro exchange rate upon the UK economy
- there is accurate economic analysis
- quality of written communication is of a high standard. [10]

(c) A number of factors have contributed to the BRIC nations enjoying significantly higher growth rates than those of the USA and the EU.

These include:

- developed nations have significantly higher levels of tax and regulation than BRIC
- developed nations are mature economies which are showing signs of diminishing returns to investment
- some of the BRIC nations have substantial endowments of natural resources
- the USA argues that China has pegged its currency at an artificially low rate against the dollar
- BRIC nations have invested heavily in education
- examples of the free market reforms introduced by BRIC nations in recent decades
- BRIC nations have enjoyed high levels of Foreign Direct Investment (FDI) largely as a result of lower labour costs than in developed economies
- BRIC nations have suffered from the credit-crunch inspired recession much less than developed nations.

Level 1 ([1]–[3])

- candidate provides little explanation of why BRIC nations are enjoying higher levels of economic growth than the USA and the EU
- there may be some vague anecdotal points but little economic analysis
- quality of written communication is limited.

Level 2 ([4]–[7])

- candidate provides some explanation of why BRIC nations are enjoying higher levels of economic growth than the USA and the EU
- there is a degree of economic analysis though this may be superficial or contain errors
- quality of written communication is satisfactory.

Level 3 ([8]–[10])

- candidate provides a clear and comprehensive explanation of why BRIC nations are enjoying higher levels of economic growth than the USA and the EU
- there is accurate economic analysis
- quality of written communication is of a high standard. [10]

- (d) This is the view articulated by the trade union official in Source 3. He is arguing that free trade and price competition has been against the best interests of his members. Most economists would disagree with this view, arguing that free trade generally leads to an overall increase in economic welfare and higher rates of economic growth.

However, free trade has produced winners and losers and it is highly likely that organised labour is amongst the losers. Many UK firms have shifted overseas to take advantage of lower wages and cheap foreign imports have caused the closure of many UK firms.

Whilst economic welfare may have increased overall, many workers have seen no benefits and the views of the trade union official will arouse sympathy in many quarters. However, inability to compete on the basis of price alone does not mean that the UK cannot compete with emerging economies. It is possible for developed countries like the UK to be more efficient through maintaining a technological advantage. So production could take place in China but design and marketing could take place in the UK.

Issues for evaluation and discussion include:

- explanation of impact of price competition on welfare of consumers
- explanation of impact of price competition on welfare of workers and firms
- arguments for protectionism, e.g. infant industries, sunset industries
- explanation of specific impact on organised labour
- possibility of retaliation against protectionist measures
- explanation that protectionism may create domestic monopolies and a loss of efficiency
- explanation of difference between competition on price and competition in other ways.

Level 1 ([1]–[5])

- candidate provides little evaluation of the view that the UK cannot compete on price with the BRIC economies
- there will be vague anecdotal approach and no significant economic analysis
- quality of written communication is limited.

Level 2 ([6]–[10])

- candidate provides some evaluation of the view that the UK cannot compete on price with the BRIC economies
- this will be supported by relevant economic analysis though this may be superficial or incomplete
- quality of written communication is satisfactory.

Level 3 ([11]–[15])

- candidate provides in-depth evaluation and judgement of the view that the UK cannot compete on price with the BRIC economies
- this is supported by relevant and accurate economic analysis
- quality of written communication is of a high standard. [15]

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- 2 (a) A nation's balance of payments must always balance for the very simple reason that if spending takes place then the funding for it must have come from somewhere. So if the UK has a deficit on its current account then this could be financed by a surplus on the capital and financial accounts. Individual sections of the balance of payments can be in surplus or deficit but the overall balance of payments must always balance and sum to zero.

For example, a deficit on trade in goods could have been financed by borrowing from abroad which would appear as an inflow in the finance section of the balance of payments. Currently the USA has a substantial deficit on trade in goods with China. However, this is balanced by Chinese purchases of US government securities.

In the event that all recorded transactions do not balance then it is obvious that some items have been missed or wrongly valued. Hence a figure for net errors and omissions is included to ensure that the account does balance.

Level 1 ([1]–[5])

- candidate provides little explanation of why a nation's balance of payments must always balance
- there is no significant knowledge or understanding of the different sections of the balance of payments and how they are related
- quality of written communication is limited.

Level 2 ([6]–[10])

- candidate provides some explanation of why a nation's balance of payments must always balance
- there is a degree of knowledge and understanding of the different sections of the balance of payments and how they are related
- quality of written communication is satisfactory.

Level 3 ([11]–[15])

- candidate provides a clear and comprehensive explanation of why a nation's balance of payments must always balance
- there is extensive knowledge and understanding of the different sections of the balance of payments and how they are related
- quality of written communication is of a high standard. [15]

- (b) Until the financial crisis of 2008 governments had tended to ignore current account deficits on the grounds that they were easily financed by inward capital and financial flows. Thus corrective action was not taken even when the deficit was a substantial proportion of GDP. However, sentiment toward current account deficits has changed with many economists viewing large deficits as one of the causes of the credit-crunch.

Possible government responses are as follows:

- deflationary policies to reduce aggregate demand. These include contractionary fiscal and monetary policies which will reduce spending in the economy and hence the demand for imports. Success depends on a highly income elastic demand for imports and there is a downside in terms of higher unemployment and reduced growth
- depreciation of the exchange rate. One advantage of remaining outside the euro is the ability to allow the pound to fall in value. This makes UK exports relatively cheaper and UK imports more expensive. Subject to the Marshall Lerner conditions this should lead to an improvement in the balance of payments. One disadvantage of this policy is the possibility of imported inflation
- supply side policies. These should improve the balance of payments by making UK products more competitive, hence reducing imports and increasing exports. Unfortunately such policies can be socially divisive and may take a long time to have any impact on the economy.

Level 1 ([1]–[7])

- candidate provides little critical examination of the main policy options open to national governments in trying to correct a balance of payments on current account deficit
- there may be vague references to policies but these are neither explained nor developed
- quality of written communication is limited.

Level 2 ([8]–[13])

- candidate provides some evaluation of the main policy options open to national governments in trying to correct a balance of payments on current account deficit
- this evaluation will be one-sided or contain errors
- quality of written communication is satisfactory.

Level 3 ([14]–[19])

- candidate provides a significant evaluation of the main policy options open to national governments in trying to correct a balance of payments on current account deficit
- key issues are explored in some depth
- quality of written communication is of a high standard.

Level 4 ([20]–[25])

- candidate provides an extensive evaluation and judgement of the main policy options open to national governments in trying to correct a balance of payments on current account deficit
- quality of written communication is excellent. [25]

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- 3 (a)** Less Developed Countries (LDCs) differ considerably but they do have a number of economic problems which are shared to a greater or lesser extent.

These include:

- low per capita income.

However, it is important to treat these figures with some caution as the poorer the country the greater will be the proportion of output which is not traded in the market economy. Secondly, these income figures are converted to US dollars at the market exchange rate and this may be prone to significant fluctuation.

- shortage of physical capital. This includes not just factories and offices but also infrastructural capital such as roads and ports
- lower levels of human capital as measured by educational statistics
- high population growth and high dependency ratio
- health and mortality. Inhabitants of LDCs are likely to endure poorer health and have a lower life expectancy than in More Developed Countries (MDCs). This affects the quality of human capital and reduces productivity
- structure of the economy. LDCs typically have much greater dependence on agriculture than in developed nations
- poor governance and corruption
- war and the breakdown of the state
- cultural and religious attitudes which exclude women from education and the workforce.

Level 1 ([1]–[5])

- candidate shows little understanding of the main economic problems faced by Less Developed Countries
- there may be vague references to some problems but these are not explained or developed
- quality of written communication is limited.

Level 2 ([6]–[10])

- candidate shows some understanding of the main economic problems faced by Less Developed Countries
- this will be incomplete or contain minor errors
- quality of written communication is satisfactory.

Level 3 ([11]–[15])

- candidate shows a clear and comprehensive understanding of the main economic problems faced by Less Developed Countries
- quality of written communication is of a high standard. [15]

(b) In October 2010 the UK government announced a programme of deep expenditure cuts. However, the foreign aid budget was protected and indeed is scheduled to increase to £9.5 billion pounds by 2013.

Issues for analysis and evaluation include:

- explanation of opportunity cost of increasing foreign aid budget upon other areas of government spending
- possibility that foreign aid will be misused by corrupt governments
- hostility to and dangers faced by aid workers in many countries
- explanation of how aid may create dependency and hinder economic development
- explanation that the aid budget is likely to remain a small fraction of that paid in agricultural subsidies which significantly disadvantage producers in LDCs
- explanation of how increased aid may improve UK security
- explanation that much American aid goes to nations like Israel which are not LDCs
- explanation of how well-directed aid may create economic development
- explanation of how aid may reduce migration to MDCs.

Level 1 ([1]–[7])

- candidate shows little understanding of the issues involved in increasing the percentage of GDP allocated to foreign aid
- there may be some strong opinions but no significant evaluation
- quality of written communication is limited.

Level 2 ([8]–[13])

- candidate shows some understanding of the issues involved in increasing the percentage of GDP allocated to foreign aid
- there will be a degree of evaluation though it is likely to be one-sided or lack depth
- quality of written communication is satisfactory.

Level 3 ([14]–[19])

- candidate shows a clear understanding of the issues involved in increasing the percentage of GDP allocated to foreign aid
- there will be significant evaluation
- quality of written communication is of a high standard.

Level 4 ([20]–[25])

- candidate shows a clear and comprehensive understanding of the issues involved in increasing the percentage of GDP allocated to foreign aid
- there will be extensive evaluation and judgement
- quality of written communication is excellent. [25]

- 4 (a) The European Central Bank is the central bank for the 16 member states of the eurozone. It was established by the Treaty of Amsterdam in 1998 and is independent of any national government, though the central banks of member states are represented on its board.

The main function of the ECB is to control monetary policy with a view to achieving a rate of inflation of around 2 per cent. Its main instrument for this purpose is the rate of interest.

It is also responsible for managing the reserves of the eurozone and conducting foreign exchange operations to manage the value of the euro. This role was particularly important during the recent currency crisis which threatened the very existence of the euro. It has also managed the transfer of funds to countries such as Ireland and Greece which faced the possibility of leaving the eurozone because of high levels of debt.

The ECB carries out minor administrative functions such as the issue of notes and coin.

Level 1 ([1]–[5])

- candidate provides little explanation of the role and functions of the ECB
- there may be vague references to some issues but these will be confused and lack substance
- quality of written communication is limited.

Level 2 ([6]–[10])

- candidate provides some explanation of the role and functions of the ECB
- key issues will be explored though this may lack depth or contain errors
- quality of written communication is satisfactory.

Level 3 ([11]–[15])

- candidate provides a clear and comprehensive explanation of the role and functions of the ECB
- all key issues are explored with accuracy and clarity
- quality of written communication is of a high standard. [15]

- (b) Euro membership has brought both benefits and risks to its member states.

The main benefits included:

- reduced transaction costs for trade
- no currency risk for transactions within eurozone
- greater price transparency
- increased trade and tourism
- possibility of borrowing at low rates on international markets because of perceived strength of German economy.

However, there are a number of risks associated with euro membership and these culminated in the Greek sovereign debt crisis of 2010 which threatened the very existence of the common currency. The recent Irish financial crisis was partly the result of the inability of the Irish government to use interest rates as a means of controlling the housing bubble.

The main risks include:

- problems arising from common interest rate
- problems arising from inability to devalue as a means of correcting current account deficits
- problems arising from the eurozone not being an optimal currency area
- problems arising from immobility of labour between member states
- problems arising from different levels of efficiency and productivity in member states
- problems arising from lack of economic convergence amongst member states
- problems arising from failure to enforce the terms of the growth and stability pact.

However, within the eurozone there is considerable political commitment to the survival of euro and so far, richer members like Germany have been prepared to make significant fiscal transfers to weaker economies like Greece. The euro will be viewed as a failed economic experiment if it breaks up and some nations are forced to leave it. At this time (October 2010) this looks unlikely but only time will tell.

Level 1 ([1]–[7])

- candidate shows little understanding of the issues involved in judging the euro to be a success or failure
- there may be vague references to some themes but these are not properly explained
- quality of written communication is limited.

Level 2 ([8]–[13])

- candidate shows some understanding of the issues involved in judging the euro to be a success or failure
- there will be a degree of economic analysis though this is likely to be superficial or contain errors and some evaluation
- quality of written communication is satisfactory.

Level 3 ([14]–[19])

- candidate shows a clear understanding of the issues involved in judging the euro to be a success or failure
- this will be supported by accurate economic analysis and significant evaluation
- quality of written communication is of a high standard.

Level 4 ([20]–[25])

- candidate shows a clear and comprehensive understanding of the issues involved in judging the euro to be a success or failure
- this will be supported by accurate economic analysis and in depth evaluation and judgement
- quality of written communication is excellent.

[25]

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Total

80