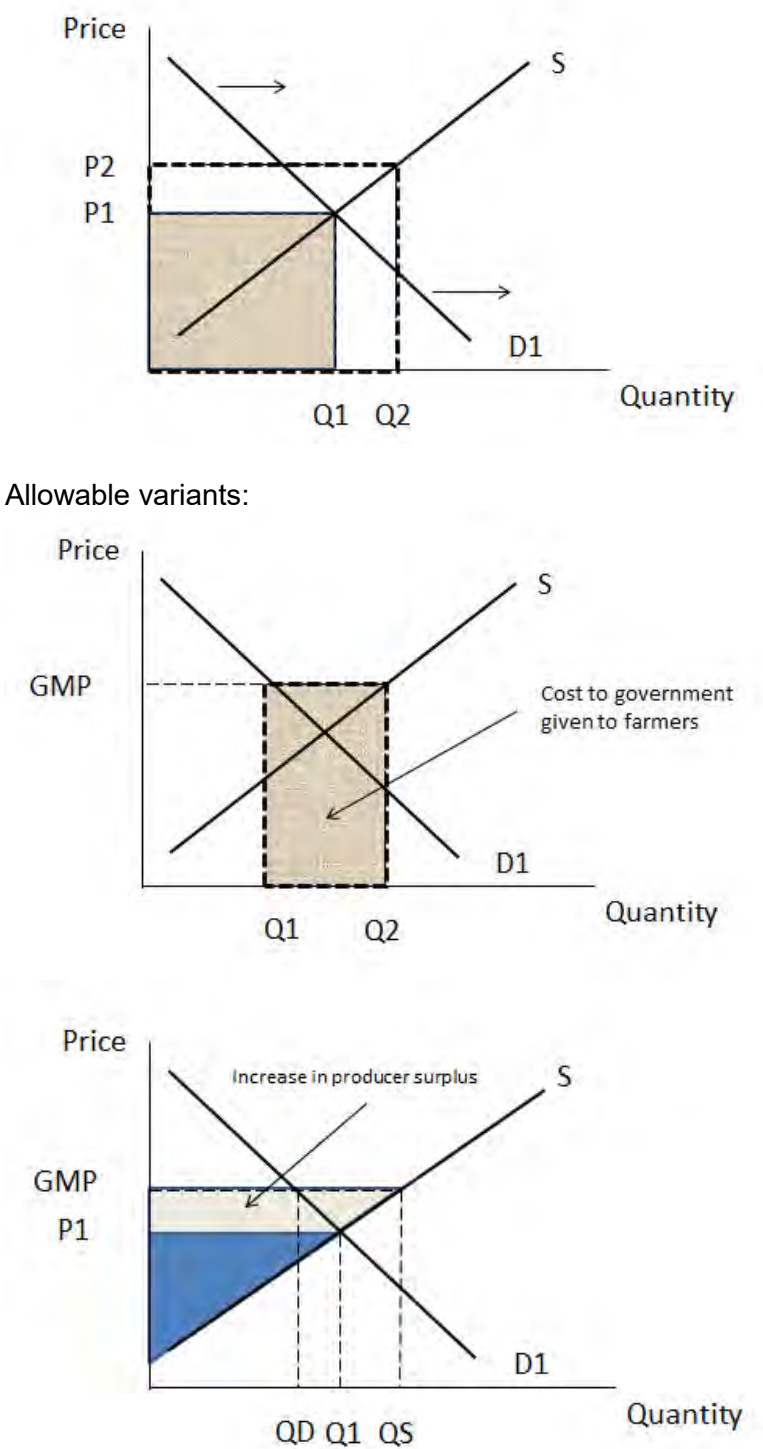


GCE ECONOMICS – EC1

Summer 2015

Question	Answer	Mark allocation	Assessment objective
General	The marks in brackets show the maximum number of marks for a point. Less well developed ideas may not be worth the full credit shown.		
1	<p>Define opportunity cost and use the data to explain what would be the opportunity cost of putting £1000 into a Tesco Instant Access Cash ISA</p> <p>Definition of opportunity cost: Value of the best alternative forgone. Good understanding = (2) Weaker understanding (e.g. not realising it is <i>best</i> alternative = (1)</p> <p>Use of data – Opportunity Cost = 2.5% at Cheshire Building Society, explained as best alternative (2 – 1+1 identification and explanation)) £23 vs £25/0.2% difference (2)</p> <p>Other examples: Not related to the data (e.g. spending the money) (1), One of the lower paying accounts = (1) All of the other accounts indiscriminately – ie they imply that they are all really the opportunity cost (1)</p>	4	AO1 2 AO2 2
2	<p>Using a supply and demand diagram, explain a possible reason for the changes in the data for the UK housing market shown between May 2012 and May 2013.</p> <p>Appropriate diagram:</p> <p>(D shifts to the right or any diagram with higher P and Q at equilibrium), correctly labelled (numbers from the data not required P1, Q1 etc. are fine) (2)</p> <div data-bbox="774 1332 1077 1601" data-label="Figure"> </div> <p>Appropriate factor: Economic recovery, continued low interest rates, weak £ leads to foreign buyers moving in, social factors (divorce rate) etc. etc. (2)</p> <p>If they simply assert that demand increases, this is not a factor and therefore if that's all the analysis that is present, they will only get diagram marks.</p> <p>Allow any plausible factor which would have shifted demand to the right.</p>	4	AO1 2 AO2 2

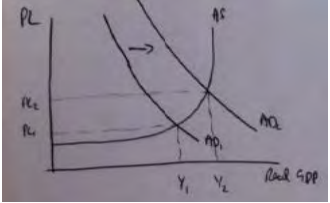
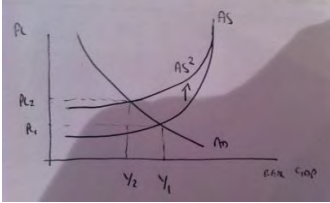
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	<p>If candidate shifts supply, then they will only be able to explain either the increase in P or increase in Q therefore max 2; 1 for the diagram and 1 for a relevant factor.</p> <p>If candidate shifts both S and D, then provided they have reason for this, and provided both P and Q increase, this is fine.</p> <p>For half-correct answers which get either Q or P right, 1 for diagram and one for appropriate factor. 2 max.</p> <p>Geographic/socioeconomic factors need to be well developed for 2</p> <p>Wealth effects based around the data are a little back to front and will probably score (1) unless there is a clear idea that there is a speculative bubble, or that prices were already rising before and this is part of a continuation.</p>											
3	<p>Using economic theory, explain the differences between goods A, B and C.</p> <table border="1" data-bbox="258 891 1141 1464"> <tr> <td data-bbox="258 891 386 1093">Level 1</td> <td data-bbox="386 891 550 1093">1-2 Marks</td> <td data-bbox="550 891 1141 1093">Candidate only defines YED and simply identifies differences between the goods without explanation or one characteristic well-explained e.g. Normal goods identified and explained only = 2.</td> </tr> <tr> <td data-bbox="258 1093 386 1294"></td> <td data-bbox="386 1093 550 1294">3-4 Marks</td> <td data-bbox="550 1093 1141 1294">Candidate correctly explains either Normal/Inferior (B vs. A/C or elastic/inelastic* (A vs. C) Or candidate identifies both key difference without explaining, and defines YED (=3)</td> </tr> <tr> <td data-bbox="258 1294 386 1464">Level 3</td> <td data-bbox="386 1294 550 1464">5-6 Marks</td> <td data-bbox="550 1294 1141 1464">Candidate correctly explains the key differences between the three goods, both Inferior/Normal and elastic/inelastic. If one explained and one identified, then this is probably 5.</td> </tr> </table> <p>*for income elastic/inelastic, allow luxury/necessity as an alternative. Hence: Income elastic/luxury because YED greater than 1. Income inelastic/necessity because YED lower than 1 For Normal/Inferior need to identify the sign and then explain the correlation in one direction.</p>	Level 1	1-2 Marks	Candidate only defines YED and simply identifies differences between the goods without explanation or one characteristic well-explained e.g. Normal goods identified and explained only = 2.		3-4 Marks	Candidate correctly explains either Normal/Inferior (B vs. A/C or elastic/inelastic* (A vs. C) Or candidate identifies both key difference without explaining, and defines YED (=3)	Level 3	5-6 Marks	Candidate correctly explains the key differences between the three goods, both Inferior/Normal and elastic/inelastic. If one explained and one identified, then this is probably 5.	6	AO1 2 AO2 2 AO3 2
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4 (a)	<p>(a) Using a diagram, explain how the guaranteed minimum price scheme was supposed to 'raise the incomes of farmers'.</p> <p>Appropriate diagram (2):</p> <p>Diagram: unused GMP diagram =1, GMP diagram used to show increase in revenue in some way = 2.</p>	4	AO1 1 AO2 2 AO3 1									

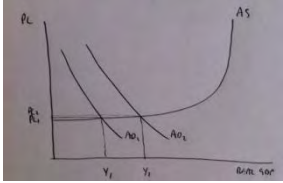
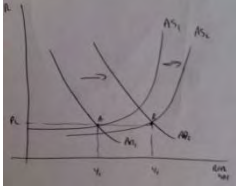
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	 <p>The first diagram shows a standard supply and demand model. The vertical axis is labeled 'Price' and the horizontal axis is 'Quantity'. An upward-sloping supply curve 'S' and a downward-sloping demand curve 'D1' intersect at equilibrium price $P1$ and quantity $Q1$. A second demand curve is shown to the right of $D1$, with an arrow indicating a rightward shift. A new equilibrium is shown at price $P2$ and quantity $Q2$. A shaded rectangle represents the area between $P1$ and $P2$ from $Q1$ to $Q2$.</p> <p>The second diagram, titled 'Allowable variants:', shows the same supply curve 'S' and demand curve 'D1'. A horizontal dashed line at price 'GMP' intersects the supply curve at quantity $Q1$ and the demand curve at quantity $Q2$. A shaded rectangle between $Q1$ and $Q2$ is labeled 'Cost to government given to farmers'.</p> <p>The third diagram shows the supply curve 'S' and demand curve 'D1'. A horizontal dashed line at price 'GMP' intersects the supply curve at quantity $Q1$ and the demand curve at quantity $Q5$. A vertical dashed line at quantity QD intersects the supply curve at price $P1$. A blue shaded triangle is formed by the supply curve, the vertical axis, and the horizontal line at $P1$. A light blue shaded rectangle is formed between $Q1$ and $Q5$ and between $P1$ and GMP. An arrow points to the blue triangle with the label 'Increase in producer surplus'.</p> <p>Explanation (2) Farmers can sell produce for a higher price than before (30-50% higher than the market price) and can sell as much as they wish to produce.</p> <p>Some explanation of how revenue will rise without reference to data or diagram = 1 Explanation of how revenue will rise with reference to data or diagram = 2.</p>		

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4 (b)	<p>Explain why the guaranteed minimum price scheme might be seen as an example of government failure</p> <p>Understanding of government failure (2): A situation in which government intervention causes a more inefficient allocation of goods and resources than would occur without that intervention (2). Government intervention wastes resources (2). Some candidates may refer to welfare loss, but this is not required (2).</p> <p>Other variations on this may well be fine - see marker notes (below) for further guidance.</p> <p>Application to the situation (2): Waste of money – only benefits rice farmers (2) when other groups are equally needy Costs of storing rice, which is then left to rot. (2) Jobs lost in rice processing – Pareto inefficiency? (2) Opportunity cost – money could have been used much more effectively elsewhere (2) Corruption/Public Choice theory (2) Government has had to reduce the minimum price, indicating that the policy was ineffective/counterproductive (2) Credit other relevant points</p> <p>The key is that the application needs to explain why resources have been misallocated.</p> <p>Marker notes:</p> <p>Government failure is the idea that governments as well as markets can cause a misallocation of resources. Governments generally intervene in markets to improve the allocation of resources, but these attempts may fail or be counterproductive.</p> <p>Ineffective policies are an example of government failure, because they use scarce resources to no end, hence using resources without improving the situation the intervention was intended to fix.</p> <p>Counterproductive policies may result in both the waste of resources implicit in a failed policy as well as a creating new problems and distortions which require further intervention. Here costs can be very great – both the resources used in the intervention and the costs of distortions created.</p> <p>Hence, government failure occurs where government intervention leads to a waste or misallocation of resources.</p>	4	AO1 2 AO2 2

Question	Answer	Mark allocation	Assessment objective
5	<p>Explain how the policies suggested by Britain’s doctors might help to correct market failure.</p> <p>Broad guidance:</p> <p>Up to 4 for good explanation of how policies work with some understanding of MF. 2 policies required for 4 (but could be 3+1) – see AO2.</p> <p>Up to 2 more marks for explaining how market failure is corrected, probably with reference to how resources are now not misallocated (but there may be other market failures that are focused on more explicitly and if well explained then 2 can be gained) – see AO3.</p> <p>AO1: Some understanding of market failure and/or an awareness that the policies might reduce obesity. 1-2 Marks.</p> <p>AO2: Candidate analyses how the policies are likely to reduce obesity: Tax will drive up the price, reducing demand. Ban on fast food near schools might encourage healthier eating. Support for weight management programmes should lead to healthier eating. Diagram might well be used. 1-2 Marks</p> <p>Top of AO2, 4 marks explains how obesity is reduced with reference to two policies, but not how market failure will be corrected.</p> <p>AO3: Candidate explains how market failure will be corrected - some sense of a misallocation of resources being corrected:</p> <p>Sugary foods and drinks are over-consumed in a free market because external costs are ignored (therefore price will be too low and equilibrium quantity will be too high). Hence:</p> <ul style="list-style-type: none"> • A tax on drinks/ban on fast food near schools will therefore reduce the equilibrium quantity closer to the optimum level, therefore correcting market failure. • Tax on sugary drinks will internalise the externality, making $PC=SC$, therefore resulting in an increase in price and a fall in equilibrium output to the optimal level. <p>Weight management programmes will tend to be under-consumed due to information gaps and present-bias/retrospective regret. Therefore an increase in the provision of such programmes should increase their uptake, again correcting market failure. 1-2 Marks for showing that misallocation of resources has been corrected.</p> <p>This level of detail isn’t necessary to get 6, but answers worth 5 or 6 marks should definitely refer to the idea that resource allocation is being improved, or that there was a problem that needed to be tackled in economic terms.</p> <p>Max 5 for one policy.</p>	6	AO1 2 AO2 2 AO3 2

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6	<p>Discuss whether the data shown on productivity will make it difficult for the UK to reduce its trade deficit.</p> <p>AO1: Candidate understands productivity and that poor productivity can make UK firms uncompetitive by raising costs/ or they understand what productivity is but don't think it really matters. AO2: Candidate makes use of the data (e.g. UK productivity is below that of the US, France, Germany and the Eurozone as a whole) to explain that this will make it hard to improve the trade position (exports likely to be weak, imports will tend to rise).</p> <p>To get 4 marks, answer needs to show a clear understanding of productivity (1), use the data (up to 2 done well) and explain clearly why the trade deficit might not improve because of the impact on costs (up to 2, needs reference to X,M for 2, but must refer to the trade balance.). Therefore up to 5 but 4 max without AO4.</p> <p>Data use = relative comparison</p> <p>AO4:</p> <p>Candidate evaluates, either by:</p> <p>1) using the data to point out that the UK's productivity performance is better than some countries (esp. Japan) and not much worse than the Eurozone as a whole. Or may note that many countries' data is not given – especially China and India, which are likely to be key markets in years to come.</p> <p>Or</p> <p>2) Explaining that other factors are important. This statement alone, however is not worth any credit. A list of 'it depends' factors should not be given any marks unless one of these factors is explained in the context of the question. These may include elasticity of demand, quality, which sectors are more important and so on.</p> <p>3) Might comment on policies which might raise productivity in the LR</p> <p>Answers which treat productivity and production as the same will not get more than 2.</p>	6	AO1 2 AO2 1 AO3 1 AO4 2

Question	Answer	Mark allocation	Assessment objective	
7	<p>With reference to the data and using an appropriate diagram, discuss whether the growth forecasts in the chart above are likely to lead to higher inflation in the UK economy.</p>	8	AO1 1 AO2 1 AO3 2 AO4 4	
	AO1, 2 and 3 - up to 4 marks			
	1-2 Marks			<p>Limited analysis</p> <p>Candidate draws a simple AD/AS diagram and asserts that an increase in AD will cause inflation/ commodity price rises will cause cost-push inflation with no explanation as to why prices might be rising.</p> <div style="display: flex; justify-content: space-around;">   </div>
3-4 Marks	<p>Reasonable analysis (Diagram not necessarily required, although see cap at bottom).</p> <p>Candidate explains how the increased AD will actually cause inflation (increased competition for scarce resources/less competition between firms due to buoyant demand or explains how rising commodity prices can feed through to the prices of final goods);</p> <p>Or</p> <p>Both types of inflation dealt with, with some development. i.e. a good theoretical explanation</p> <p>Or</p> <p>Candidate makes use of the data, explaining:</p> <ul style="list-style-type: none"> • That inflation is already close to top of target and that inflationary expectations may occur. • Global commodity prices are also on the rise • Growth is forecast to rise increasingly quickly and that the output gap will soon be closed. <p>i.e., a good applied explanation</p>			

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	<p style="text-align: center;">AO4 – up to 4 marks</p> <p>1-2 Marks</p> <p>Limited evaluation – candidate says ‘it depends on the state of the economy and draws a diagram, without any real reference to the context of the UK economy.</p> <div style="display: flex; justify-content: space-around;">   </div> <p>Or, candidate says it depends on whether AS increases and draws a diagram, again without any real reference to the UK economy.</p> <p>Or they might say it depends on other factors without really developing the ideas. Or they might assert that the forecasts might be wrong without any development</p> <p>They might do all of these, but it is still only worth 2 marks unless one of them is developed.</p> <p>3-4 Marks</p> <p>Reasonable evaluation: This will be in context (Diagram not necessarily required, although see cap at bottom).</p> <p>Hence, this is not 2 limited evaluation points; reasonable evaluation requires some sort of depth, probably the candidate adopts one of the approaches in limited evaluation, but applies it to the context/develops it fully.</p> <p>In the first case, might talk about the fact that the UK is still recovering from the credit crunch/make reference to the output gap/the fact that u/e is still high.</p> <p>In the second case, they might talk about <i>why</i> AS might be expected to rise – I recovering, SSPs, trend growth arguments.</p> <p>In the third case they might explain in detail about exchange rates, or rising productivity in other countries holding down import prices.</p> <p>The fourth case will be difficult to develop fully, but alongside other developed points, adds to the general quality of the answer.</p> <p>Cap: No diagram = 6 max. Answer is reversible, so the analysis of why inflation would occur becomes the evaluation of why it wouldn't.</p>		

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8	<p>With reference to the data, discuss whether further cuts in interest rates are likely to significantly weaken the Australian dollar.</p> <table border="1" data-bbox="240 315 1150 1128"> <thead> <tr> <th colspan="2" data-bbox="240 315 1150 349">AO1, 2 and 3</th> </tr> </thead> <tbody> <tr> <td data-bbox="240 349 352 589">1-2 Marks</td> <td data-bbox="352 349 1150 589"> <p>Limited analysis</p> <p>Candidate identifies that a fall in interest rates will cause the exchange rate to fall. Might draw a simple diagram, but no real explanation. Might assert that there will be hot money outflows, but does not explain why. Might mix up supply and demand factors.</p> </td> </tr> <tr> <td data-bbox="240 589 352 1128">3-4 Marks</td> <td data-bbox="352 589 1150 1128"> <p>Reasonable analysis.</p> <p>Candidate explains why a cut in interest rates might be expected to cause the Australian dollar to fall further. Candidate explains: Australian banks will now be less attractive to investors, causing D for A\$ to fall. Or Existing holders of A\$ may seek higher returns elsewhere, causing an outflow of short term capital (S A\$ will increase) Speculators may fear further falls in the A\$ especially as government seems determined to weaken it.</p> <p>Candidate may use a well-integrated diagram, but this is not required. 1 factor (D/S without diagram, up to 3)</p> </td> </tr> </tbody> </table> <p>Further guidance: AO1, 2 and 3 well integrated diagram is worth up to 2. Impact on D – up to 2 (needs to be fully explained for 2) Impact on S – up to 2 (needs to be fully explained for 2)</p>	AO1, 2 and 3		1-2 Marks	<p>Limited analysis</p> <p>Candidate identifies that a fall in interest rates will cause the exchange rate to fall. Might draw a simple diagram, but no real explanation. Might assert that there will be hot money outflows, but does not explain why. Might mix up supply and demand factors.</p>	3-4 Marks	<p>Reasonable analysis.</p> <p>Candidate explains why a cut in interest rates might be expected to cause the Australian dollar to fall further. Candidate explains: Australian banks will now be less attractive to investors, causing D for A\$ to fall. Or Existing holders of A\$ may seek higher returns elsewhere, causing an outflow of short term capital (S A\$ will increase) Speculators may fear further falls in the A\$ especially as government seems determined to weaken it.</p> <p>Candidate may use a well-integrated diagram, but this is not required. 1 factor (D/S without diagram, up to 3)</p>	8	AO1 1 AO2 1 AO3 2 AO4 4
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	<p style="text-align: center;">Evaluation</p> <table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 15%; vertical-align: top; padding: 5px;">1-2 Marks</td> <td style="padding: 5px;"> <p>Limited evaluation –</p> <p>Throw-away lines like: “It depends on how much interest rates are cut” are worth at most 1 mark and require some development even for that and they are not cumulative – no matter how many under-developed evaluative points they make, they will get at most 2 marks.</p> <p>Other reasonable evaluation might be long run effects. Once the exchange rate has fallen for some time, the trade balance may start to improve or further inward investment might be attracted, pushing the A\$ back up.</p> <p>Limited evaluative points will tend to be assertive rather than explained and will tend not to be in context. E.G. It depends on what happens to interest rates in other countries.</p> </td> </tr> <tr> <td style="vertical-align: top; padding: 5px;">3-4 Marks</td> <td style="padding: 5px;"> <p>Reasonable evaluation: This will be in context</p> <p>2 points with at least one point that is well applied to the case, or one fully applied point with excellent development.</p> <p>This is not 2 limited evaluation points; reasonable evaluation requires some sort of depth and will use the context. Possible angles might include:</p> <p>Interest rates have already fallen 7 times, and appear not to be having much impact. Interest rates in the US/UK/Eurozone are still much lower than 2.75% Australia may still be experiencing a commodity boom, meaning that funds will flow in regardless of the interest rate. This will also attract speculators.</p> </td> </tr> </table>	1-2 Marks	<p>Limited evaluation –</p> <p>Throw-away lines like: “It depends on how much interest rates are cut” are worth at most 1 mark and require some development even for that and they are not cumulative – no matter how many under-developed evaluative points they make, they will get at most 2 marks.</p> <p>Other reasonable evaluation might be long run effects. Once the exchange rate has fallen for some time, the trade balance may start to improve or further inward investment might be attracted, pushing the A\$ back up.</p> <p>Limited evaluative points will tend to be assertive rather than explained and will tend not to be in context. E.G. It depends on what happens to interest rates in other countries.</p>	3-4 Marks	<p>Reasonable evaluation: This will be in context</p> <p>2 points with at least one point that is well applied to the case, or one fully applied point with excellent development.</p> <p>This is not 2 limited evaluation points; reasonable evaluation requires some sort of depth and will use the context. Possible angles might include:</p> <p>Interest rates have already fallen 7 times, and appear not to be having much impact. Interest rates in the US/UK/Eurozone are still much lower than 2.75% Australia may still be experiencing a commodity boom, meaning that funds will flow in regardless of the interest rate. This will also attract speculators.</p>		
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