



General Certificate of Education
Advanced Level Examination
January 2010

Economics

ECON3

Unit 3 Business Economics and the Distribution of Income

Friday 29 January 2010 1.30 pm to 3.30 pm

For this paper you must have:

- a 12-page answer book.

You may use a calculator.

Time allowed

- 2 hours

Instructions

- Use black ink or black ball-point pen. Pencil should only be used for drawing.
- Write the information required on the front of your answer book. The **Examining Body** for this paper is AQA. The **Paper Reference** is ECON3.
- In **Section A**, answer **EITHER** Question 1 **OR** Question 2.
- In **Section B**, answer **one** question.

Information

- The maximum mark for this paper is 80.
- There are 40 marks for **Section A** and 40 marks for **Section B**.
- The marks for questions are shown in brackets.
- This paper is synoptic. It assesses your understanding of the relationship between the different aspects of Economics.
- You will be marked on your ability to:
 - use good English
 - organise information clearly
 - use specialist vocabulary where appropriate.

Advice

- You are advised to spend 1 hour on **Section A** and 1 hour on **Section B**.

SECTION A

Answer **EITHER** Question 1 **OR** Question 2.

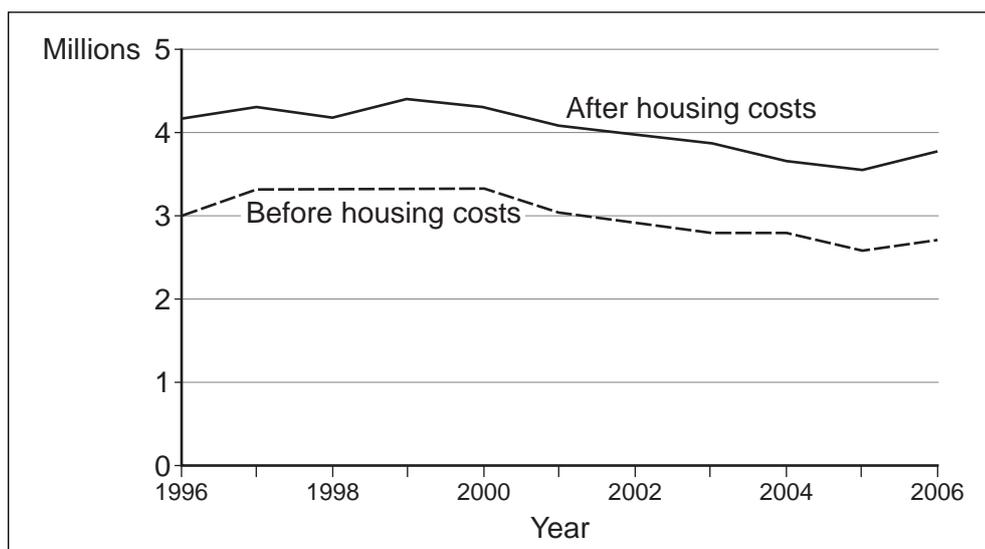
EITHER

1 THE GLOBAL CONTEXT

Total for this question: 40 marks

Study **Extracts A, B and C**, and then answer **all** parts of Question 1 which follows.

Extract A: Number of children living in poverty, UK



Source: adapted from official statistics

Extract B: Child poverty in the UK

In the mid to late 1990s, the United Kingdom suffered higher child poverty than nearly any other industrialised nation in the world. Over a period of 20 years, the proportion of children in relatively low-income households had more than doubled, and one in five families had no one in work. When the Labour Party came to power in 1997, it was estimated that more than one British child in four (nearly 5 million children) were living in households where family income was less than 60% of median (average) income after accounting for housing costs. It is considered important to allow for the impact of house rents and mortgage repayments because of the significant impact they have on the remaining disposable income of families, especially those on low incomes. In 1999, the then Prime Minister, Tony Blair, promised to halve child poverty (as measured this way) by 2010, and to eliminate it by 2020.

Children who grow up in relative poverty in the UK have poorer life chances than children from higher-income families. Every area of a child's development is affected: social, educational, personal, economic. There are long-term effects because childhood poverty tends to persist into adulthood. Children from poor families have worse school attendance records and are less likely to do well at school. They have more illnesses and are more likely to die in accidents. As adults, they are more likely to be unemployed, commit crimes, enter into abusive relationships or develop alcohol and/or drug dependencies.

Source: news reports, 2008

Extract C: Child poverty in less developed countries

Living in absolute poverty is the norm for the majority of people alive today. Almost half the world's population, over 3 billion people, live on less than \$2.50 a day. The annual total of Gross Domestic Product (GDP) of the 41 countries described by the United Nations as being 'Heavily Indebted Poor Countries' (HIPCs), which together contain 567 million people, is less than the total personal wealth of the world's seven richest individuals. Every year, the world spends on weapons more than 100 times the amount needed to put every child into school. Meanwhile, nearly a billion people worldwide are unable to read or write. While multinational companies spend millions of pounds every year marketing fizzy drinks to poorer countries, thousands of children in those countries die every day from intestinal diseases linked to a lack of clean drinking water. Meanwhile, the World Bank and International Monetary Fund have pursued policies that controversially encourage governments to privatise water supplies.	1 5 10
Child poverty is a particular problem, and the UN estimates that half the children in the world live in poverty, defined as having 'severe deprivation' in two or more of the following basic needs: shelter, sanitation, information, water, food, health or education. Economists have estimated that, if appropriately measured, the long-run economic rate of return on national investment in basic services such as primary education is greater than would be expected from stocks and shares.	15

Source: news reports, 2008

Question 1

- 1 (a) Using **Extract A**, identify **two** significant points of comparison between the number of children living in poverty before and after housing costs over the period shown. (5 marks)
- (b) Distinguish between absolute and relative poverty **and**, using the data to help you, explain why this distinction is useful when investigating poverty in the UK and in less developed countries. (10 marks)
- (c) Evaluate whether the UK government should attempt to eliminate poverty, and child poverty in particular, **or** leave the issue to market forces. (25 marks)

Turn over for the next question**Turn over ►**

Do **not** answer Question 2 if you have answered Question 1.

OR

2 THE EUROPEAN UNION CONTEXT

Total for this question: 40 marks

Study **Extracts D and E**, and then answer **all** parts of Question 2 which follows.

Extract D: Motor vehicle manufacturers supplying the EU market, 2007

Company	Market share (%)
Volkswagen (Germany)	18.3
Peugeot-Citroën (France)	13.2
Ford (USA)	10.7
General Motors (USA)	9.6
Renault (France)	9.4
Fiat (Italy)	8.8
Mercedes (Germany)	5.9
BMW (Germany)	4.6
Japanese companies	13.8
Korean companies	3.2
Others	2.5

Extract E: Mergers among car producers

In Germany, where it is estimated that one job in seven is dependent on the motor industry, the so-called 'Volkswagen Law' states that any shareholder in Volkswagen (VW) cannot exercise more than 20% of voting rights, even if their stake in the firm is bigger. In 2007, the European Union's highest court ruled that this law, protecting the car-maker VW from takeovers, was illegal. 1
5

The German Government resisted demands to scrap the VW law, but in 2008 the family-owned Porsche group took its shareholding in VW above 74%, saying that it wished to protect VW from 'foreign' takeover, anticipating that the German Government would have to back down. VW had itself completed a takeover of Sweden's Scania. The end result is a global giant that makes cars, buses and trucks, and contains not only VW and Porsche, but also Bentley, Audi, Lamborghini, Seat and Skoda. 10

At one time there were at least 20 car manufacturers in Britain alone; today, there is no single independent British manufacturer, and there are only about 20 major manufacturers in the whole world. Several well-known British brands have merged with each other or become the property of companies based elsewhere in the EU, in the USA, or as far afield as China. However, the employment and skills profiles of many British towns benefit from the fact that overseas manufacturers invest in this country in order to have unhindered access to the Single European Market. For example, since 1983 Ford has been making engines in 15

Wales which are then installed in cars at its assembly plants in Spain and other EU countries.

As well as full-blown mergers, there are many instances of cross-industry collaboration, some of which date back several decades. In 1979, for example, the then Rover Group began cooperating with Honda to produce some models using resources in both Britain and Japan. This collaboration was phased out after 1994 when Rover was taken over by BMW. Today, the Ford Galaxy, VW Sharan and Seat Alhambra (seven-seater multi-purpose vehicle models) all look remarkably similar, as they share the same basic body design and some components. The attempt by producers to benefit from economies of scale through collaboration needs to be carefully distinguished from cases of collusion. When oligopolists collude, the results can be anti-competitive and against the consumer interest.

**EU Commission estimates of minimum efficient scales (MES)
in motor manufacturing (2006)**

Product	MES as a % of production in the EU
Cars	20
Lorries	19

The tendency for the car market in Europe to become dominated by fewer, larger firms is at least partly explained by the concept of minimum efficient scale (MES). Where the MES is a large proportion of EU production, the industry will find it difficult to support many firms.

Source: news reports, 2008

Question 2

- 2 (a) Using **Extract D**, identify **two** main features of the market for motor vehicles in the EU. (5 marks)
- (b) Explain the concept of ‘minimum efficient scale’ (**Extract E**, line 30) **and** analyse its implications for the structure of, **and** barriers to entry to, the motor manufacturing industry. (10 marks)
- (c) ‘When oligopolists collude, the results can be anti-competitive and against the consumer interest’ (**Extract E**, lines 27–28).

Evaluate policies that could be used to deal with this problem. (25 marks)

Turn over for the next question

Turn over ▶

SECTION B

Answer **one** question from this section.

Each question carries 40 marks.

- 3 (a) The *British Airports Authority* (BAA), a private-sector monopolist which operates Heathrow Airport, says it needs to build a third runway. Critics say that this would cause air and noise pollution and add to global warming.

Explain why, even if this runway were profitable, an economist could argue that it would be a case of market failure. (15 marks)

- (b) A government is considering subsidising a series of high-speed rail lines in order to reduce short-haul air flights.

To what extent might cost benefit analysis be a useful method of evaluating this proposal? (25 marks)

- 4 (a) *Home Farm* is one of many small firms producing lettuces and attempting to maximise profits.

Explain the circumstances in which *Home Farm* might make supernormal profits in the short run, but only normal profits in the long run. (15 marks)

- (b) Evaluate the argument that managers controlling large companies might follow policies which do **not** necessarily maximise the profits of the owners. (25 marks)

- 5 (a) Explain why a television journalist working on the BBC's *Newsnight* current-affairs programme would usually be paid a much higher wage rate than a reporter on a local newspaper.

(15 marks)

- (b) Evaluate the view that the best way to narrow wage differentials is to increase the National Minimum Wage (NMW). (25 marks)

END OF QUESTIONS

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