

GCE

Economics

Unit **H460/01**: Microeconomics

Advanced GCE

Mark Scheme for June 2018

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This mark scheme is published as an aid to teachers and students, to indicate the requirements of the examination. It shows the basis on which marks were awarded by examiners. It does not indicate the details of the discussions which took place at an examiners' meeting before marking commenced.

All examiners are instructed that alternative correct answers and unexpected approaches in candidates' scripts must be given marks that fairly reflect the relevant knowledge and skills demonstrated.

Mark schemes should be read in conjunction with the published question papers and the report on the examination.

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Annotations

Annotation	Meaning
BP	Blank Page – this annotation must be used on all blank pages within an answer booklet (structured or unstructured) and on each page of an additional object where there is no candidate response.
	Tick
	Cross
	Comment
BOD	Benefit of doubt
	Level 1
	Level 2
	Level 3
	Level 4
	Effective evaluation
	Omission
NAQ	Not answered question
SEEN	Noted but no credit given
	Too vague
OFR	Own figure rule

Subject-specific Marking Instructions

INTRODUCTION

Your first task as an Examiner is to become thoroughly familiar with the material on which the examination depends. This material includes:

- the specification, especially the assessment objectives
- the question paper and its rubrics
- the mark scheme.

You should ensure that you have copies of these materials.

You should ensure also that you are familiar with the administrative procedures related to the marking process. These are set out in the OCR booklet **Instructions for Examiners**. If you are examining for the first time, please read carefully **Appendix 5 Introduction to Script Marking: Notes for New Examiners**.

Please ask for help or guidance whenever you need it. Your first point of contact is your Team Leader.

Rubric Infringement

Candidates may infringe the rubric in the following way:

- answering two questions from Section C.

If a candidate has written two answers for Section C, mark both answers and award the highest mark achieved.

USING THE MARK SCHEME

Please study this Mark Scheme carefully. The Mark Scheme is an integral part of the process that begins with the setting of the question paper and ends with the awarding of grades. Question papers and Mark Schemes are developed in association with each other so that issues of differentiation and positive achievement can be addressed from the very start.

This Mark Scheme is a working document; it is not exhaustive; it does not provide 'correct' answers. The Mark Scheme can only provide 'best guesses' about how the question will work out, and it is subject to revision after we have looked at a wide range of scripts.

The Examiners' Standardisation Meeting will ensure that the Mark Scheme covers the range of candidates' responses to the questions, and that all Examiners understand and apply the Mark Scheme in the same way. The Mark Scheme will be discussed and amended at the meeting, and administrative procedures will be confirmed. Co-ordination scripts will be issued at the meeting to exemplify aspects of candidates' responses and achievements; the co-ordination scripts then become part of this Mark Scheme.

Before the Standardisation Meeting, you should read and mark in pencil a number of scripts, in order to gain an impression of the range of responses and achievement that may be expected.

In your marking, you will encounter valid responses which are not covered by the Mark Scheme: these responses must be credited. You will encounter answers which fall outside the 'target range' of Bands for the paper which you are marking. Please mark these answers according to the marking criteria.

Please read carefully all the scripts in your allocation and make every effort to look positively for achievement throughout the ability range. Always be prepared to use the full range of marks.

Levels of response / Level descriptors	Knowledge and understanding/ Application	Analysis	Evaluation
Strong	Precision in the use of the terms in the question and applied in a focused way to the context of the question.	An explanation of causes and consequences, fully developing the links in the chain of argument.	A conclusion is drawn weighing up both sides, and reaches a supported judgement.
Good		An explanation of causes and consequences, developing most of the links in the chain of argument.	A conclusion is drawn weighing up both sides, but without reaching a supported judgement.
Reasonable	Awareness of the meaning of the terms in the question and applied to the context of the question.	An explanation of causes and consequences, which omit some key links in the chain of argument.	Some attempt to come to a conclusion, which shows some recognition of the influencing factors.
Limited	Awareness of the meaning of the terms in the question.	Simple statement(s) of cause and consequence.	An unsupported assertion.

Question		Answer	Marks	Guidance
1	(a)	<p>Explain, using evidence from the stimulus material, why higher education is a private good.</p> <p>1 mark for any characteristic of a private good</p> <ul style="list-style-type: none"> it can be provided by the private sector (1) it is excludable (1) it is rivalrous (1) it is rejectable (1) <p>1 mark for use of evidence from the stimulus material</p> <ul style="list-style-type: none"> there are private universities (1) students have to pay tuition fees (1) there are a limited number of places on various courses (1) some students do not gain the required grades (1) 	<p>2</p> <p>A01 x 1 A02 x 1</p>	
1	(b)	<p>Calculate, using information from the stimulus material, the average fixed cost of educating a university student in 2014 – 2015.</p> <p>1 mark for the identification OR understanding of fixed costs</p> <ul style="list-style-type: none"> fixed costs are the costs of providing university education which do not vary with the number of students (1) depreciation and other overheads (1) <p>2 marks for the calculation of total fixed costs</p> <ul style="list-style-type: none"> $£31.2\text{bn} \times 7.7\% (1) = £2.4024\text{bn} (1)$ <p>3 marks for the calculation of average fixed costs</p> <ul style="list-style-type: none"> $£2.4024\text{bn} (1) / 2.2\text{m} (1) = £1,092 (1)$ 	<p>3</p> <p>AO1* x 1 AO2* x 2</p>	<p>Award 1 mark for calculation of an average (ie by dividing any cost by the number of students = $x / 2.2\text{m}$)</p> <p>If a candidate identifies a valid fixed cost in their calculation they can be awarded full marks eg:</p> <ul style="list-style-type: none"> $£31\text{bn} \times 1.4\% (1) = £0.4368\text{bn} (1) / 2.2\text{m} = £198.5 (1)$ $£31.2\text{bn} \times 6.3\% (1) = £1.9656\text{bn} (1) / 2.2\text{m} = £893 (1)$ $£31.2\text{bn} \times 62.5\% (1) = £19.5\text{bn} (1) / 2.2\text{m} = £8,863 (1)$
1	(c) (i)	<p>Explain whether the information in Fig.3 on average income and on 25 – 34 year olds who had completed tertiary education shows the expected relationship between the two.</p> <p>1 mark for whether the information supports the expected relationship OR 1 mark for the expected relationship</p> <ul style="list-style-type: none"> the expected relationship is not supported by Fig. 3 / 'no '(1) it is expected that the higher the % of 25 – 34 year olds completing tertiary education, the higher the average income (1) 	<p>2</p> <p>A02* x 2</p>	

Question	Answer	Marks	Guidance
	<p>1 mark for use of supporting evidence</p> <ul style="list-style-type: none"> • USA has the highest average income but the third lowest proportion of the population completing tertiary education (1) • South Korea has the lowest income but the highest proportion 25 – 34 year olds completing tertiary education (1) • South Korea has a lower income than the USA but higher proportion of 25 – 34 year olds completing tertiary education (1) • Fig. 3. does not show average incomes for 25 – 34 year olds / Fig. 3 show the average income of both age groups (1) • Fig. 3 does not show the average income for 25 – 34 year old before completion of tertiary education (1) 		

Question			Answer	Marks	Guidance
1	(c)	(ii)	<p>Explain, using information in Fig. 3, which country is likely to have experienced the lowest increase in occupational mobility over the last thirty to forty years.</p> <p>1 mark for an understanding of occupational mobility / immobility</p> <ul style="list-style-type: none"> the ease with which workers can switch job. (1) <p>1 mark for identification of the country with the lowest relative <u>OR</u> absolute increase</p> <ul style="list-style-type: none"> USA (1) <u>OR</u> Germany (1) <p>Up to 2 marks for use of the information in Fig. 3</p> <ul style="list-style-type: none"> USA has the smallest (1) relative difference (1) of 13.4% (1) in the proportion of young people who have completed tertiary education than older people Germany has the smallest (1) absolute difference (1) of 4.2 percentage points (1) in the proportion of young people who have completed tertiary education than older people. 	<p>3</p> <p>AO1* x 1</p> <p>AO2* x 2</p>	

Question	Answer	Marks	Guidance
1 (d)	<p>Evaluate whether students will benefit from the government freezing the maximum annual tuition fee for some time.</p> <p>Level 2 (5–8 marks) Good knowledge and understanding of how and why governments intervene in markets (price controls). Good – strong analysis of the impact of freezing tuition fees. Good analysis will be in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Reasonable – Strong evaluation of the impact of freezing tuition fees, considering both sides and underpinned by appropriate theoretical analysis. Good evaluation will weigh up both sides but without reaching a supported judgement. Strong evaluation should include a supported judgement.</p>	<p>8</p> <p>AO1 x 1 AO2 x 1 AO3 x 3 AO4 x 3</p>	<p>Students will not experience a rise in the tuition fees and so their consumer surplus will not be reduced. The real cost of university education will fall over time with inflation. Students will potentially get into less debt and will be able to keep a higher proportion of their income than if tuition fees were raised. More A level students may be encouraged to go on to university. As a result, they may benefit from more choices of occupation and a higher income.</p> <p>If universities, however, do not receive more funding from the government, the quality of the education they provide may decline. They may find it difficult to attract the best lecturers and professors. Fig.1 shows that government funding has been falling which may suggest that higher tuition fees will not be replaced by more government funding. Without more funding, the number of university places may be reduced. More students may want to go to university but not all will be able to do so. Demand may increase more than supply. A freeze may act like a maximum price set below the equilibrium price, with a shortage of places developing. If the number of graduates actually declines, the wage differential between graduates and non-graduates will increase which may increase income inequality. The key influence on whether students will benefit or not will depend on whether government spending on higher education will</p>

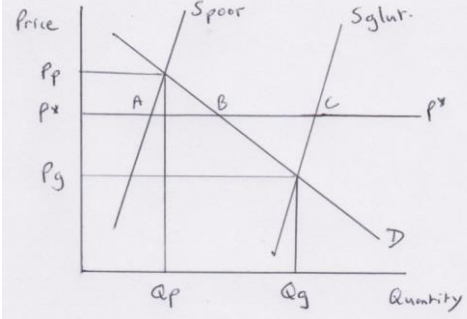
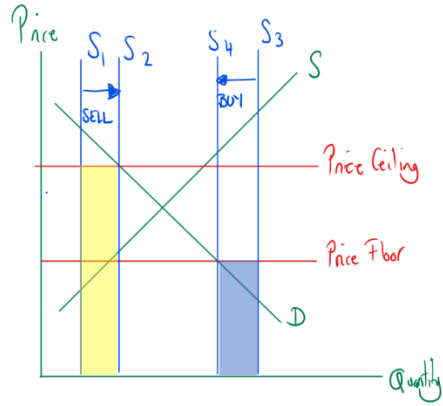
Question	Answer	Marks	Guidance
	<p>Level 1 (1–4 marks) Limited – reasonable knowledge and understanding of how and why governments intervene in markets (price controls). Limited – reasonable analysis of the impact of placing a limit on tuition fees. Limited analysis will have little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. Reasonable analysis will have correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Limited evaluation of the impact of freezing tuition fees in the form of an unsupported statement or no evaluation. 0 marks no response or no response worthy of credit.</p>		increase.
	<p>Descriptor</p> <p>Consistently meets the criteria for this level</p> <p>Meets the criteria but with some slight inconsistency</p> <p>Just enough achievement on balance for this level</p> <p>On the borderline of this level and the one below</p>	<p>Award mark</p> <p>At top of level</p> <p>Above middle and either below top of level or at middle of level (depending on number of marks available)</p> <p>Above bottom and either below middle or at middle of level (depending on number of marks available)</p> <p>At bottom of level</p>	

Question	Answer	Marks	Guidance
1 (e) *	<p>Evaluate, using evidence from the stimulus material whether a higher tuition fee should be charged to medical students than to English Literature students.</p> <p>Level 3 (9–12 marks) Good knowledge and understanding of private and external costs and benefits. Good – strong analysis of the extent it can be argued that a higher tuition fee should be charged to medical students than to English Literature students. Good analysis will be in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Good - strong evaluation of the extent to which it can be argued that a higher tuition fee should be charged to medical students than to English Literature students, weighing up both sides/comparing alternatives. Strong evaluation should include a supported judgment. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and substantiated.</i></p> <p>Level 2 (5–8 marks) Good knowledge and understanding of private and external costs and benefits. Reasonable analysis of the extent to which it can be argued that a higher tuition fee should be charged to medical students than to English Literature students. There is correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning.</p>	<p>12</p> <p>AO1 x 1 AO2 x 1 AO3 x 5 AO4 x 5</p>	<p>There are two key arguments for charging medical students more than English Literature students. One is that medical students receive a higher private benefit from their education than English Literature students. This is in the form of higher earnings. Their earnings would help them pay back loans taken out to pay the higher tuition fees. Doctors already, in effect, pay more as they are more likely than English Literature students to pay back all of their loans. The second argument is that it costs more to provide a medical degree than an English Literature degree course. More equipment and contact hours are needed. Allocative efficiency may be achieved by charging a tuition fee which reflects the marginal cost.</p> <p>However, as well as the private benefit enjoyed by the medical students, there are considerable external benefits generated. Doctors can increase the productivity of the labour force which can benefit the whole population. As the stimulus material suggests all education can bring external benefits but these benefits may vary by subject. If tuition fees are based on just private benefits arising from studying particular subjects, the demand for some courses may be below the socially optimum level. If it discourages some students applying for medical degrees, it may result in a shortage of doctors and, for example, delayed operations. Charging</p>

Question	Answer	Marks	Guidance
	<p>Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis of the case for or against private sector ownership</p> <p>Reasonable evaluation of the extent to which it can be argued that a higher tuition fee should be charged to medical students than to English Literature students.</p> <p><i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i></p> <p>Level 1 (1–4 marks)</p> <p>Limited – reasonable knowledge and understanding of private and external costs and benefits.</p> <p>Limited analysis of the extent to which it can be argued that a higher tuition fee should be charged to medical students than to English Literature students. Little evidence of reasoning that addresses the question asked. There is a lack of a clear structure.</p> <p>Limited evaluation of the extent to which it can be argued that a higher tuition fee should be charged to medical students than to English Literature students. in the form of an unsupported statement or no evaluation.</p> <p><i>The information is basic and communicated in an unstructured way. The information is supported by limited evidence and the relationship to the</i></p>		<p>lower tuition fees for English Literature degree courses may increase the number of students applying for such courses. If universities offer more places for English Literature students, the supply of graduates to the jobs undertaken by such students may increase. This may reduce the return from studying English Literature. Charging different fees will increase universities' administrative costs. More time and effort will be taken setting fees. In addition, the quality of degree courses in medicine and English Literature vary between universities. A student studying English Literature in one university may gain a better education than one studying medicine in another university. Not all students who study medicine will gain high paid jobs while some students who study creative arts gain high paid jobs. Some graduates in medicine may, for instance, go to work in medical publishing while some English Literature may become best-selling authors. In addition, it is difficult to predict which jobs will be in demand and highly paid in the future.</p> <p>Medical degrees have the potential to generate higher private benefits than English Literature degrees. They do, however, also have the potential to generate greater external benefits. Charging the same fees will not discourage students from studying medicine and, if they do later earn high incomes they will be likely to not only pay back more of their student loans but also</p>

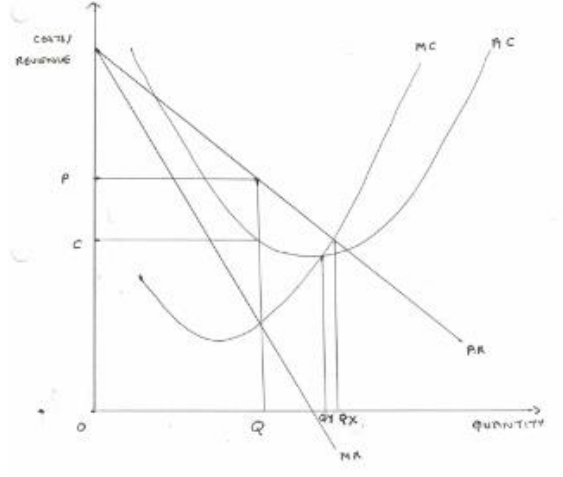
Question	Answer	Marks	Guidance
	<p><i>evidence may not be clear.</i></p> <p>0 marks no response or no response worthy of credit.</p> <p>Note: although a diagram is not required, it may enhance the quality of the answer and should be rewarded at the appropriate level.</p>		higher income tax.
	<p>Descriptor</p>	<p>Award mark</p>	
	Consistently meets the criteria for this level		At top of level
	Meets the criteria but with some slight inconsistency		Above middle and either below top of level or at middle of level (depending on number of marks available)
	Just enough achievement on balance for this level		Above bottom and either below middle or at middle of level (depending on number of marks available)
	On the borderline of this level and the one below		At bottom of level

Question	Answer	Marks	Guidance
2	<p>Governments may use buffer stock schemes to reduce the market failure caused by price instability Evaluate, using an appropriate diagram(s), the effectiveness of a buffer stock scheme in reducing market failure.</p> <p>Level 5 (21–25 marks) Good - Strong knowledge and understanding of how and why governments intervene in markets (buffer stock systems). Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Strong evaluation of how effective a buffer stock scheme is in reducing market failure considering extent and alternative and reaching a supported judgment. <i>There is a well-developed and sustained line of reasoning which is coherent and logically structured. The information presented is entirely relevant and substantiated.</i></p> <p>Level 4 (16–20 marks) Good knowledge and understanding of how and why governments intervene in markets (buffer stock systems). Strong analysis will have consistently well-developed links through a</p>	<p>25</p> <p>AO1 x 6 AO2 x 6 AO3 x 6 AO4 x 7</p>	<p>In some markets, particularly commodity markets, prices can exhibit volatility over time. This volatility may generate market failure through a high level of uncertainty. Producers find it difficult to form accurate expectations about future market conditions. This means that they are less likely to invest in ways of improving both productivity and the quality of the product. Similarly, consumers faced with volatile prices are unable to make purchasing decisions and may either delay purchasing or indulge in over consumption at low prices.</p> <p>Buffer stock schemes attempt to stabilise prices. A scheme is set up whereby excess supply is bought up to prevent prices falling below a certain level. In periods when supply is limited e.g. a poor harvest, then stocks are released on to the market in order to maintain the price. In the below diagram the price agreed to be maintained is p^*. When there is a glut year with Supply located at Sglut there is excess supply of BC. This amount is bought up by the buffer stock and stored. If supply is at Spoor there is excess demand so the AB is released by the buffer stock on to the market. This helps to maintain price.</p>

Question	Answer	Marks	Guidance
	<p>coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Good evaluation will weigh up both sides/comparing alternatives but without reaching a supported judgment. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and in the most part substantiated.</i></p> <p>Level 3 (11–15 marks) Good knowledge and understanding of how and why governments intervene in markets (buffer stock systems). Good analysis of how effective a buffer stock scheme is in reducing market failure. There is correct analysis in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Reasonable evaluation of how effective a buffer stock scheme is in reducing market failure considering extent and alternatives. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i></p> <p>Level 2 (6–10 marks) Good knowledge and understanding of how and why governments intervene in markets (buffer stock systems). Reasonable analysis of how effective a buffer stock scheme is in reducing market failure. There is correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Reasonable evaluation of how effective a buffer stock scheme is in reducing market failure considering extent and alternatives. <i>The information has some relevance, but is communicated in an unstructured way. The information is supported by limited evidence, the relationship to the evidence may not be clear.</i></p> <p>Level 1 (1–5 marks)</p>		 <p>An alternative diagrammatic approach would be explanation of a price floor and a price ceiling with a permitted band of fluctuation. Comparison of the cost of buying surplus stock and the revenue gained from releasing stock onto the market could be used to analyse how buffer stocks may be self-financing.</p>  <p>However, the setting of an agreed price may cause problems in itself as it may be set too high or too low. If the buffer stock scheme finds itself purchasing excess supply on a regular basis and not selling</p>

Question	Answer	Marks	Guidance
	<p>Reasonable knowledge and understanding of how effective a buffer stock scheme is in reducing market failure.</p> <p>Limited or no analysis of how effective a buffer stock scheme is in reducing market failure. There is little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. The relevant diagram(s) may not be present or are incorrectly labelled.</p> <p>Limited evaluation of how effective a buffer stock scheme is in reducing market failure in the form of an unsupported statement or no evaluation.</p> <p><i>Information presented is basic and may be ambiguous or unstructured. The information is supported by limited evidence.</i></p> <p>0 marks no response or no response worthy of credit.</p>		<p>from the stock, then the stocks will rise over time. This can be a costly policy and ultimately unsustainable. The cost of storing products might be a problem with some products being more expensive to store than others. Excess supply may also be dumped on other countries and have a detrimental effect on their economies. Examples from historical schemes such as the Common Agricultural Policy with its lakes and mountains could be used as examples. Commodity prices are set by global demand and supply so that individual countries are price takers. In order to prevent imports undermining the buffer stock, variable tariffs may be required. It can be argued that it is in the consumer's interest to have access to low prices in times of glut and also that guaranteeing prices to producers can result in inefficiencies and market failure.</p> <p>The extent to which buffer stock schemes reduce the market failures caused by price stability depends on the ability of individual economies to insulate themselves from price instability in global markets. This is easier when the buffer stock is co-ordinated between a groups of countries who, together, account for a high % of global production.</p>

Question		Answer	Marks	Guidance
		Descriptor		Award mark
		Consistently meets the criteria for this level		At top of level
		Meets the criteria but with some slight inconsistency		Above middle and either below top of level or at middle of level (depending on number of marks available)
		Just enough achievement on balance for this level		Above bottom and either below middle or at middle of level (depending on number of marks available)
		On the borderline of this level and the one below		At bottom of level

Question	Answer	Marks	Guidance
<p>3</p> <p>*</p>	<p>Some economists claim that the Royal Mail was more efficient when it was a monopoly. Evaluate, using an appropriate diagram(s), whether a monopoly will be efficient.</p> <p>Level 5 (21–25 marks) Good - Strong knowledge and understanding of a monopoly market structure and different types of efficiency. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Strong evaluation of whether a monopoly will be efficient. weighing up both sides/comparing alternatives and reaching a supported judgment. <i>There is a well-developed and sustained line of reasoning which is coherent and logically structured. The information presented is entirely relevant and substantiated.</i></p>	<p>25</p> <p>AO1 x 6 AO2 x 6 AO3 x 6 AO4 x 7</p>	<p>There are a number of reasons why a monopoly may be inefficient. The market power enjoyed by the firm may encourage it to restrict the quantity it sells and drive up price. The diagram shows the monopoly selling a quantity of Q. This quantity is below the allocatively efficient level of QX. The firm’s profit maximisation quantity $MC = MR$ is less than the allocatively efficient quantity where $MC = P$ (AR).</p>  <p>Lack of competition may also result in productive inefficiency. The diagram shows that the firm is producing where AC is still falling. This quantity is below the productively efficient quantity of QY where $MC = AC$. As well as a monopoly not producing at the lowest point on the average cost curve, it may also not produce on the lowest possible AC curve. This is because it may experience X-</p>

Question	Answer	Marks	Guidance
	<p>Level 4 (16–20 marks) Good knowledge and understanding of a monopoly market structure and different types of efficiency. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Good evaluation will weigh up both sides/comparing alternatives but without reaching a supported judgment. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and in the most part substantiated.</i></p> <p>Level 3 (11–15 marks) Good knowledge and understanding of a monopoly market structure and different types of efficiency. Good analysis of whether a monopoly will be efficient. There is correct analysis in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Reasonable evaluation of whether a monopoly will be efficient, considering both sides/comparing alternatives. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i></p> <p>Level 2 (6–10 marks) Good knowledge and understanding of a monopoly market structure and different types of efficiency. Reasonable analysis of whether a monopoly will be efficient. There is correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Reasonable evaluation of whether a monopoly will be efficient. considering both sides/comparing alternatives.</p>		<p>inefficiency. The lack of competition may reduce the incentive for the firm to reduce, for example, overmanning and higher than necessary stock levels. In addition, a monopoly may be dynamically inefficient. It may not feel the pressure to innovate to improve the quality of its products. Customers may not be particularly happy with the quality of the firm's product but if there are no substitutes, they may still buy it.</p> <p>It is, however, possible that a monopoly may be more dynamically efficient than a more competitive firm. This is because it may have large amount of supernormal profit. Some of this may be reinvested in new equipment embodying advanced technology and in training its workers. Knowledge that, if it has high and effective barriers to entry, it may be able to keep any extra profit generated by improving the quality of its product may encourage it to invest. While not having actual competition, a monopoly may have potential competition. New firms and firms producing other products may be trying to enter the market. This may encourage the monopoly to charge a lower price than the profit maximising price to discourage the entry of other firms into the market. As well as engaging in limit pricing, a monopoly may also raise the quality of its product to build up brand loyalty in case of the entry of rival firms. The existence of a monopoly with high barriers to entry may encourage firms outside the market to</p>

Question	Answer	Marks	Guidance
	<p><i>The information has some relevance, but is communicated in an unstructured way. The information is supported by limited evidence, the relationship to the evidence may not be clear.</i></p> <p>Level 1 (1–5 marks) Reasonable knowledge and understanding of whether a monopoly will be efficient. Limited or no analysis of whether a monopoly will be efficient. There is little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. The relevant diagram(s) may not be present or are incorrectly labelled. Limited evaluation of whether a monopoly will be efficient in the form of an unsupported statement or no evaluation. <i>Information presented is basic and may be ambiguous or unstructured. The information is supported by limited evidence.</i> 0 marks no response or no response worthy of credit.</p>		<p>develop new and better versions of the product so as to overcome barriers such as patents and brand loyalty. While price may be above marginal cost, it may still be lower in a monopoly than in a more competitive market. This is because the monopoly may be able to enjoy economies of scale. Even with a high profit per unit, a lower average cost can result in a lower price. Economies of scale are especially significant in the case of a natural monopoly. In this case, a monopoly can supply the market at a lower price than two or more firms. Fixed costs are high, so that average cost falls over a large range of output.</p> <p>Whether or not a monopoly is efficient or not is also influenced by the objectives followed by the firm. For instance, a state-owned monopoly may seek to achieve allocative efficiency. It might also be more likely to take into account social costs and benefits than a more competitive firm producing in the private sector. A monopoly is more likely to be efficient if it faces potential competition, if it produces a high output and so is able to take advantage of economies of scale and if it is seeking to be efficient.</p>

Question		Answer	Marks	Guidance
		Descriptor		Award mark
		Consistently meets the criteria for this level		At top of level
		Meets the criteria but with some slight inconsistency		Above middle and either below top of level or at middle of level (depending on number of marks available)
		Just enough achievement on balance for this level		Above bottom and either below middle or at middle of level (depending on number of marks available)
		On the borderline of this level and the one below		At bottom of level

Question	Answer	Marks	Guidance
4 *	<p>Estonia continues to increase the role of market forces in its economy. Evaluate whether operating a market economy is the best way to allocate resources.</p> <p>Level 5 (21–25 marks) Good -Strong knowledge and understanding of the market economy and resource allocation. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis.</p> <p>Strong evaluation of the contribution of whether operating a market economy is the best way to allocate resources, weighing up both sides/comparing alternatives and reaching a supported judgment. <i>There is a well-developed and sustained line of reasoning which is coherent and logically structured. The information presented is entirely relevant and substantiated.</i></p>	<p>25</p> <p>AO1 x 6 AO2 x 6 AO3 x 6 AO4 x 7</p>	<p>A market economy relies on the price mechanism to allocate resources. This is an automatic system that can allow consumers to be sovereign, determining what is produced. It signals to producers changes in consumer demand. It provides an incentive, in the form of profit, to encourage producers to move their resources to making those products experiencing an increase in demand and away from those experiencing a decrease in demand. The profit incentive can also encourage firms to be efficient. If there are a number of firms competing in the market, the one that produces at the lowest average cost, which is most responsive to changes in consumer demand and is the most innovative will earn the highest profit. Competition provides consumers with choice. This gives them the power to switch from less efficient to more efficient producers. Workers have an incentive, in the form of higher wages, to be productive. Those workers who have the skills in the greatest demand, will earn the highest wages.</p> <p>There are, however, a number of reasons why a market economy may not be the best way to allocate resources. One is that some producers may develop market power in both product and labour markets. A lack of competition may raise prices,</p>

Question	Answer	Marks	Guidance
	<p>Level 4 (16–20 marks) Good knowledge and understanding of the market economy and resource allocation. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Good evaluation will weigh up both sides/comparing alternatives but without reaching a supported judgment. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and in the most part substantiated.</i></p> <p>Level 3 (11–15 marks) Good knowledge and understanding of the market economy and resource allocation. Good analysis of whether operating a market economy is the best way to allocate resources. There is correct analysis in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Reasonable evaluation of whether operating a market economy is the best way to allocate resources. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i></p>		<p>reduce quality and make the firm or firms less responsive to changes in consumer demand. A monopsony employer may keep wages low and provide poor working conditions. Producers in a pure market economy will have no incentive to allocate resources to producing public goods. This is because they will have not be able to make consumption of the goods dependent on payment. Merit goods will be under-consumed as consumers will not be fully aware of their true benefits and because they do not take into the external benefits created. As a result of the under-consumption, merit goods will be under produced – there will not be enough resources allocated to their production. In contrast, too many resources will be devoted to producing demerit goods. They will be overconsumed as consumers will not be fully aware of their harmful effects and will not take into account the external costs they generate. Consumers and producers base their consumption and production decisions on private costs and private benefits. The failure to base decisions on social costs and social benefits will result in resource allocation being socially inefficient. It is possible that resource allocation may also be inefficient because of the immobility of factors of production. For instance, if labour is occupationally and/or geographically immobile, there may not be enough workers to make more popular products while there may also be unemployed workers. A market economy may allocate</p>

Question	Answer	Marks	Guidance
	<p>Level 2 (6–10 marks) Good knowledge and understanding of the market economy and resource allocation. Reasonable analysis of whether operating a market economy is the best way to allocate resources. There is correct analysis largely in the form of single links. These address the question but are not developed into a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis. Reasonable evaluation of whether operating a market economy is the best way to allocate resources. <i>The information has some relevance, but is communicated in an unstructured way. The information is supported by limited evidence, the relationship to the evidence may not be clear.</i></p> <p>Level 1 (1–5 marks) Reasonable knowledge and understanding of the market economy and resource allocation. Limited or no analysis of whether operating a market economy is the best way to allocate resources. There is little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. The relevant diagram(s) may not be present or are incorrectly labelled. Limited evaluation of whether operating a market economy is the best way to allocate resources in the form of an unsupported statement or no evaluation. <i>Information presented is basic and may be ambiguous or unstructured. The information is supported by limited evidence.</i></p> <p>0 marks no response or no response worthy of credit.</p>		<p>resources in a way that benefits consumers with high income. Poor consumers, however, will have less influence on what is produced.</p> <p>A market economy has a number of potential advantages including encouraging entrepreneurship and innovation but most economists accept the need for some government intervention to correct the market failure that may arise. Where economists disagree is the extent to which the government should intervene. Note: although a diagram is not required, it may enhance the quality of the answer and should be rewarded at the appropriate level.</p>

		Descriptor	Award mark
		Consistently meets the criteria for this level	At top of level
		Meets the criteria but with some slight inconsistency	Above middle and either below top of level or at middle of level (depending on number of marks available)
		Just enough achievement on balance for this level	Above bottom and either below middle or at middle of level (depending on number of marks available)
		On the borderline of this level and the one below	At bottom of level

Question	Answer	Marks	Guidance
5 *	<p>Firms usually take into account the income and cross elasticities of demand for their products when setting their prices. Evaluate whether a firm which produces a product that has positive income elasticity of demand and positive cross elasticity of demand should lower the price of the product.</p> <p>Level 5 (21–25 marks) Good -Strong knowledge and understanding of the usefulness of and significance of YED and XED to economic agents. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Strong evaluation of whether a firm which produces a product that has positive income elasticity of demand and positive cross elasticity of demand should lower the price of the product, and reaching a supported judgment. <i>There is a well-developed and sustained line of reasoning which is coherent and logically structured. The information presented is entirely relevant and substantiated.</i></p>	<p>25</p> <p>AO1 x 6</p> <p>AO2 x 6</p> <p>AO3 x 6</p> <p>AO4 x 7</p>	<p>If consumer incomes fall, demand for products with positive income elasticity of demand will experience a fall in demand. To offset this downward pressure on demand, a firm may decide to reduce the price of its product. At a time of falling incomes, this may make its product more affordable and there will be an extension of demand / rise in quantity demanded. This may result in an increase in the revenue from sales. If the product has positive cross elasticity of demand, this suggests that the product has substitutes. The higher the value of the XED, the closer the substitutes are. In this situation, lowering the price of the product may enable the firm to capture more of the market and gain an increase in revenue due to an extension of demand / rise in quantity demanded. Greater market share may enable the firm to produce more and gain economies of scale. The lower long run average cost may result in higher profit margins and enable firms to increase not just sales but also profit. and higher supernormal profits. In addition, lowering price where XED is positive may enable a firm to achieve other objectives such as sales or growth maximisation or sales revenue maximisation. In these situations, firms that produce a product that has positive income elasticity of demand and positive cross elasticity of demand may consider lowering the price of the product.</p>

Question	Answer	Marks	Guidance
	<p>Level 4 (16–20 marks) Good knowledge and understanding of the usefulness of and significance of YED and XED to economic agents. Strong analysis will have consistently well-developed links through a coherent chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct with no significant errors that affect the validity of the analysis. Any diagrams must be integral to the analysis. Good evaluation of whether a firm which produces a product that has positive income elasticity of demand and positive cross elasticity of demand should lower the price of the product which will weigh up both sides/comparing alternatives but without reaching a supported judgment. <i>There is a well-developed line of reasoning which is clear and logically structured. The information presented is relevant and in the most part substantiated.</i></p> <p>Level 3 (11–15 marks) Good knowledge and understanding of the usefulness of and significance of YED and XED to economic agents. Good analysis of whether a firm which produces a product that has positive income elasticity of demand and positive cross elasticity of demand should lower the price of the product. There is correct analysis in the form of developed links. These links are developed through a chain of reasoning which addresses the question. Any relevant diagram(s) are predominantly correct and linked to the analysis. Reasonable evaluation of whether a firm which produces a product that has positive income elasticity of demand and positive cross elasticity of demand should lower the price of the product, considering both sides/comparing alternatives. <i>There is a line of reasoning presented with some structure. The information presented is in the most-part relevant and supported by some evidence.</i></p> <p>Level 2 (6–10 marks) Good knowledge and understanding of the usefulness of and significance of YED and XED to economic agents. Reasonable analysis of whether a firm which produces a product that has positive income elasticity of demand and positive cross elasticity of demand should lower the price of the product. There is correct analysis largely in the form of single links. These address the question but are not developed into</p>		<p>There are, however, a number of reasons why a firm with positive income and positive cross elasticity of demand should not reduce price. Over time, it is more common for income to rise than to fall. If the consumer incomes are growing, demand for the product will rise without the price having to be cut. Reducing price in a bid to capture sales from rival firms may not work. If the other firms reduce their prices, market share may remain the same while profit may fall due to lower revenue. This risk of rival firms matching price cuts is more likely in oligopolistic markets where there is a high level of interdependence as illustrated by the kinked demand curve. This suggests that prices tend to be relatively stable under conditions of oligopoly where firms' behaviour can be influenced by expectations of how its competitors will react to its pricing decisions. Of course, a firm will also consider the price elasticity of demand for its product. If demand is price elastic, a fall in price will raise revenue. In contrast a price inelastic demand for its product would cause revenue to fall with a relatively small increase in sales. Even if falls in income and the belief that rival firms will not match its price cuts, there are other reasons why a firm may not cut the price of its product. To gain more revenue from a lower price, the firm has to sell more output. To do this, it may be able to sell some units from stocks that it has been holding. However, most of the extra units are likely to have to come from</p>

Question	Answer	Marks	Guidance
	<p>a clear chain of reasoning. Any relevant diagram(s) may be imperfectly labelled or not linked to the analysis.</p> <p>Reasonable evaluation of whether a firm which produces a product that has positive income elasticity of demand and positive cross elasticity of demand should lower the price of the product, considering both sides/comparing alternatives.</p> <p><i>The information has some relevance, but is communicated in an unstructured way. The information is supported by limited evidence, the relationship to the evidence may not be clear.</i></p> <p>Level 1 (1–5 marks)</p> <p>Reasonable knowledge and understanding of the usefulness of and significance of YED and XED to economic agents.</p> <p>Limited or no analysis of whether a firm which produces a product that has positive income elasticity of demand and positive cross elasticity of demand should lower the price of the product. There is little evidence of reasoning that addresses the question asked. There is a lack of a clear structure. The relevant diagram(s) may not be present or are incorrectly labelled.</p> <p>Limited evaluation of whether a firm which produces a product that has positive income elasticity of demand and positive cross elasticity of demand should lower the price of the product in the form of an unsupported</p>		<p>higher output. It is possible that increasing output may raise cost by more than it raises revenue. If this is the case, profit would fall. This may discourage the firm from cutting the price even though the product it produces has positive income and cross price elasticities of demand. It is also possible that while the firm may believe that revenue will rise by more than cost, it may not be able to increase output to take advantage of a lower price. This will be the case, if the firm is operating at full capacity. If a firm is selling all it can currently produce at the current market price, whatever effect it thinks a lower price could have on sales, it would have no incentive to lower price. A firm producing under conditions of perfect competition may have positive income elasticity of demand for its product. The products produced by other firms in the market will be perfect substitutes for the firm's product. The firm will be a price taker with the price being set by market demand and supply. It will, therefore, have no incentive to lower price as it can sell any quantity at the going market price.</p> <p>Whether a firm with positive income elasticity of demand positive cross elasticity of demand should lower its price will depend on what is happening to income, how rival firms will react, price elasticity of demand for its product, the effect of higher output on average capacity and the firm's level of capacity.</p>

Question	Answer	Marks	Guidance
	<p>statement or no evaluation. <i>Information presented is basic and may be ambiguous or unstructured. The information is supported by limited evidence.</i> 0 marks no response or no response worthy of credit.</p> <p>Note: although a diagram is not required, it may enhance the quality of the answer and should be rewarded at the appropriate level.</p>		
	<p>Descriptor</p> <p>Consistently meets the criteria for this level</p> <p>Meets the criteria but with some slight inconsistency</p> <p>Just enough achievement on balance for this level</p> <p>On the borderline of this level and the one below</p>	<p>Award mark</p> <p>At top of level</p> <p>Above middle and either below top of level or at middle of level (depending on number of marks available)</p> <p>Above bottom and either below middle or at middle of level (depending on number of marks available)</p> <p>At bottom of level</p>	

Assessment Objectives Grid

Question	AO1	AO2	AO3	AO4	TOTAL	(Quantitative Skills)
1(a)	1	1			2	
1(b)	1 (1)	2(2)			3	(3)
1(c)(i)	1(1)	1(1)			2	(2)
1(c)(ii)	1(1)	2(2)			3	(3)
1(d)	1	1	3	3	8	
1(e)	1	1	5	5	12	
2/3	6 (2)	6 (2)	6 (2)	7 (2)	25	(8)
4/5	6	6	6	7	25	
TOTAL	18 (4)	20 (8)	20 (2)	22 (2)	80	(16)

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