GCE A LEVEL MARKING SCHEME

AUTUMN 2020

A LEVEL
ECONOMICS - COMPONENT 3
A520U30-1

INTRODUCTION

This marking scheme was used by WJEC for the 2020 examination. It was finalised after detailed discussion at examiners' conferences by all the examiners involved in the assessment. The conference was held shortly after the paper was taken so that reference could be made to the full range of candidates' responses, with photocopied scripts forming the basis of discussion. The aim of the conference was to ensure that the marking scheme was interpreted and applied in the same way by all examiners.

It is hoped that this information will be of assistance to centres but it is recognised at the same time that, without the benefit of participation in the examiners' conference, teachers may have different views on certain matters of detail or interpretation.

WJEC regrets that it cannot enter into any discussion or correspondence about this marking scheme.

GENERAL MARKING GUIDANCE

Positive Marking

It should be remembered that learners are writing under examination conditions and credit should be given for what the learner writes, rather than adopting the approach of penalising him/her for any omissions. It should be possible for a very good response to achieve full marks and a very poor one to achieve zero marks. Marks should not be deducted for a less than perfect answer if it satisfies the criteria of the mark scheme, nor should marks be added as a consolation where they are not merited.

For each question there is a list of indicative content which suggest the range of economic concepts, theory, issues and arguments which might be included in learners' answers. This is not intended to be exhaustive and learners do not have to include all the indicative content to reach the highest level of the mark scheme.

The level based mark schemes sub-divide the total mark to allocate to individual assessment objectives. These are shown in bands in the mark scheme. For each assessment objective a descriptor will indicate the different skills and qualities at the appropriate level. Learner's responses to questions are assessed against the relevant individual assessment objectives and they may achieve different bands within a single question. A mark will be awarded for each assessment objective targeted in the question and then totalled to give an overall mark for the question.

EDUQAS GCE A LEVEL ECONOMICS – COMPONENT 3

AUTUMN 2020 MARK SCHEME

1. (a)	**Using diagrams, explain the ways in which allocative and productive efficiency are efficient. [10]**	
Band	AO1	AO3
	6 marks	4 marks
3	**5-6 marks** Excellent knowledge Excellent knowledge of both allocative and productive efficiency. Each is clearly illustrated on a diagram (allow both on one diagram if clear).	
2	**3-4 marks** Good knowledge Good knowledge of both allocative and productive efficiency is shown. Detail may be lacking, perhaps being better on one than the other. Diagrams may have minor inaccuracies.	**3-4 marks** Good analysis Each type of efficiency is explained in terms of what actually makes it efficient. Strong relation back to the question.
1	**1-2 marks** Limited knowledge Learner only demonstrates a narrow knowledge of the two efficiencies and understanding is limited. Diagram(s) are weak and contain errors.	**1-2 marks** Limited analysis There is some development of what actually makes the efficiency efficient, but the explanation is not convincing.
0	**0 marks** No knowledge or understanding is present	**0 marks** No valid analysis

Indicative content:

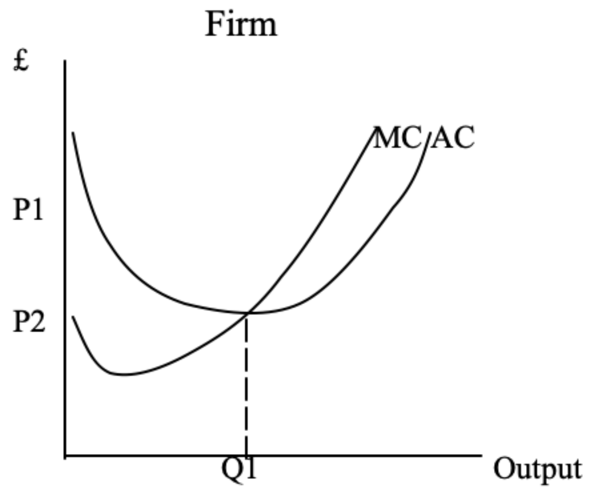
AO1/3 combined here: AO1 what the efficiency means. AO3, what is actually efficient/beneficial

Productive efficiency

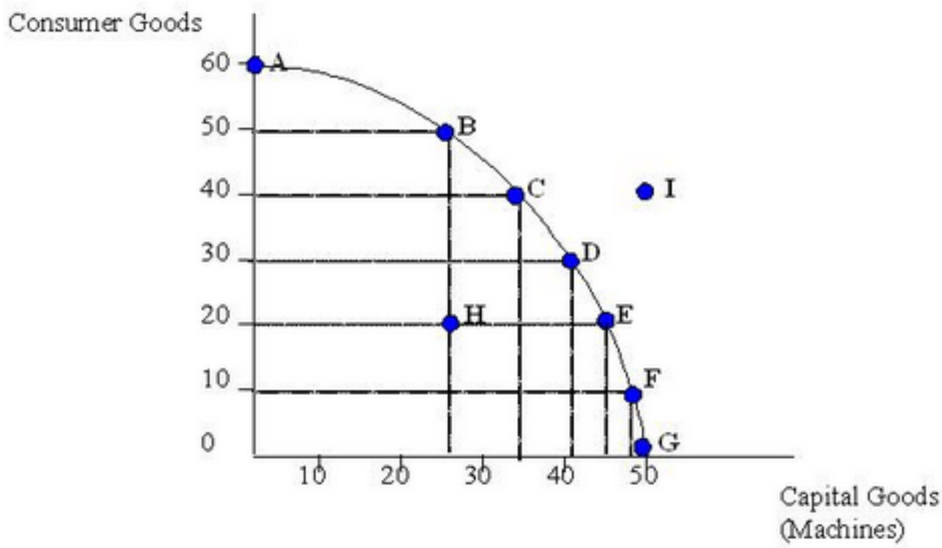
Productive efficiency means that there is efficiency in production, which has two implications:

At the level of the firm, it produces where MC=AC, the lowest point of its average cost curve. This means that productivity is maximised and that output is produced with the lowest amount of inputs. Hence an efficient output.

In the diagram, any output other than Q1 would mean that units of output would be produced at higher resource cost than necessary, therefore leading to a waste of resources and inefficiency.



Alternatively, at the level of an economy as a whole, if firms are all productively efficient, this means that an economy couldn't produce any more of one good without producing less of another again implying that output is produced at lowest unit cost. All points on a PPF are productively efficient.

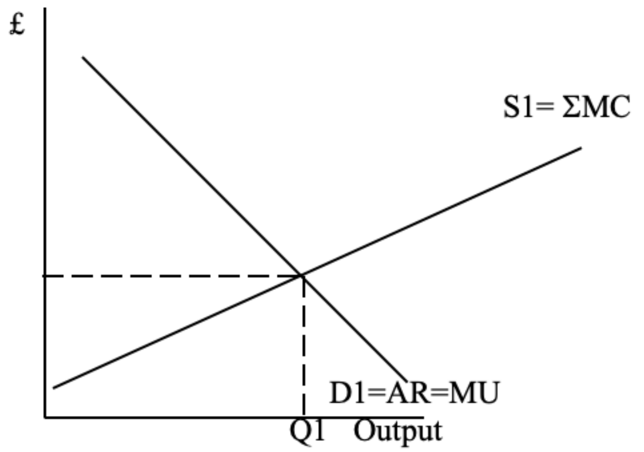


In the diagram, points A-G are all productively efficient, H is inefficient – resources are being wasted (and I is unattainable, but not relevant here).

Allocative efficiency

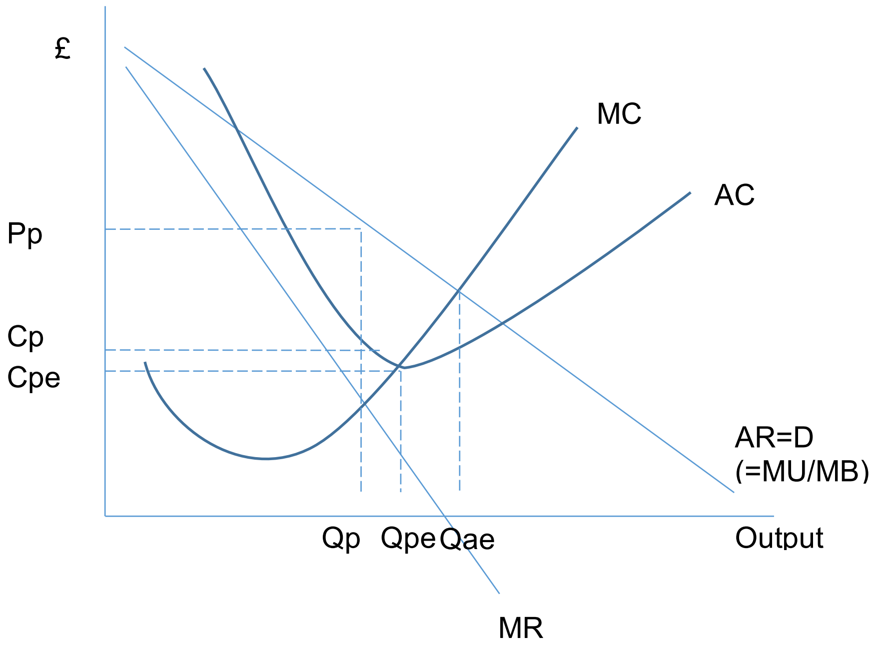
Allocative efficiency is concerned with the optimal allocation of resources, reflecting consumers' preferences such that welfare overall is maximised.

Allocative efficiency occurs technically at the price at which P/AR=MC. At this price welfare/community surplus will be maximised. They could also consider AE in the context of the of whole society and consider SMB =SMC
The price/valuation a consumer places on a product/marginal utility is equal the resource cost of producing the product (MC)



In the diagram, all units up to Q1 have MU/MB greater than MC, therefore adding to welfare, whereas all units beyond this point have the marginal cost of resources used greater than the extra benefits gained, therefore reducing welfare.

Both of these could be illustrated effectively on a single monopoly diagram, in which inefficiency could be used to illustrate what the efficiencies really mean:



1. (b) The efficiency of resources allocation in an economy would be improved by a reduction in the amount of government intervention. Discuss. [20]			
Band	AO1	AO3	AO4
	6 marks	6 marks	8 marks
3	**5-6 marks** Excellent knowledge Excellent knowledge is shown of how the presence or absence of state intervention might be beneficial in the context of resource allocation	**5-6 marks** Excellent analysis (reversible) Excellent analysis of how a reduction in the amount of state intervention would be likely to improve resource allocation. Strong chains of argument are built and answers focus on resource allocation rather than simply on the benefits of reduced state intervention.	**6-8 marks** Excellent evaluation (reversible) Evaluation points are well developed showing why a reduction in the role of the state might not be desirable in terms of resource allocation. An overall judgement draws together issues from both sides of the argument and/or there may be an integrated approach to evaluation.
2	**3-4 marks** Good knowledge Good knowledge is shown of how the presence or absence of state intervention might be beneficial in the context of resource allocation, but there may be a limited range of ideas on one side of the debate.	**3-4 marks** Good analysis Good analysis of how a reduction in the amount of state intervention would be beneficial. Strong chains of argument are built.	**3-5 marks** Good evaluation A strong two-sided answer with effective points on both sides of the argument, but which never directly answers the question set in terms of coming to a reasoned conclusion. Points are qualified and/or counterarguments are present and developed.
1	**1-2 marks** Limited knowledge Limited knowledge is shown of how the presence or absence of state intervention might be beneficial in the context of resource allocation. Points are narrow in range and development.	**1-2 marks** Limited analysis Limited analysis of how a reduction in the amount of state intervention would be beneficial. Chains of reasoning are short and lacking in range.	**1-2 marks** Limited evaluation A basic attempt is made to show that a reduction in the level of state intervention not be desirable. Points are qualified and/or counterarguments are present to a limited extent but there is little depth of explanation.
0	**0 marks** No knowledge of the benefits or otherwise of state intervention is shown	**0 marks** No relevant/valid analysis	**0 marks** No valid evaluation present

Indicative content:

AO1
There are a range of possible approaches to this question, but key points may centre around

Reduce government intervention:
Less risk of government failure
Less risk of inefficiency caused by non-market-based decisions
Less risk of inefficiency caused by state-run industries
Less danger of disincentives (Laffer curve etc.) causing misallocation of resources in terms of relocation overseas/withdrawal from the labour market/failure to maximise effort in work or education.

Don't reduce government intervention:
Government intervention is needed to correct a whole host of market failures:
Public goods
Common goods/property rights issues
Inequalities
Externalities
Information asymmetry

Privatisation has had a chequered history

AO3
A strong answer will be likely to develop a small number of the issues identified, relating back to resource allocation/misallocation for higher levels. They may well qualify as they go, starting to acquire AO4 marks if they pick a market failure and look at the case for and against intervention within it.

The key is that points are developed in terms of how government intervention may make resource allocation better or worse.

AO4
Standardly, this may contain developed counterarguments to the points made, or qualifications that show that it isn't necessarily so.

Top level AO4 will engage directly with the question which asks whether resource allocation will be improved by a reduction of state intervention – hence thoughtful answers will think about the existing level of state intervention and the areas in which reduction is anticipated to be made.

2. (a) Explain, with the aid of a diagram, why price elasticity of demand changes along a downward sloping straight-line demand curve. **[10]**		
Band	AO1	AO3
	6 marks	4 marks
3	**5-6 marks** Excellent knowledge Excellent knowledge of price elasticity of demand and how it changes along the length of the demand curve. Diagram is accurate and integrated into the text of the answer.	
2	**3-4 marks** Good knowledge Good knowledge of price elasticity of demand and how it changes along the length of the demand curve. There may be minor gaps in knowledge and understanding. Diagram is generally accurate although there may be minor errors and it may be less well integrated.	**3-4 marks** Good clear analysis Good chain of reasoning as to why price elasticity of demand varies along the length of the demand curve. The value of marginal revenue may be used to show how price elasticity of demand become less elastic as price falls. Analysis will be closely linked to the diagram which will be well integrated into the answer.
1	**1-2 marks** Limited knowledge There is a limited knowledge of price elasticity of demand and how it changes along the length of the demand curve with significant gaps in knowledge and understanding. Diagram contains significant errors or may be absent.	**1-2 marks** Limited analysis The chain of reasoning is unclear or superficial. In the analysis the diagram may not be used effectively or not at all.
0	**0 marks** No knowledge or understanding shown	**0 marks** No valid analysis

Indicative content:

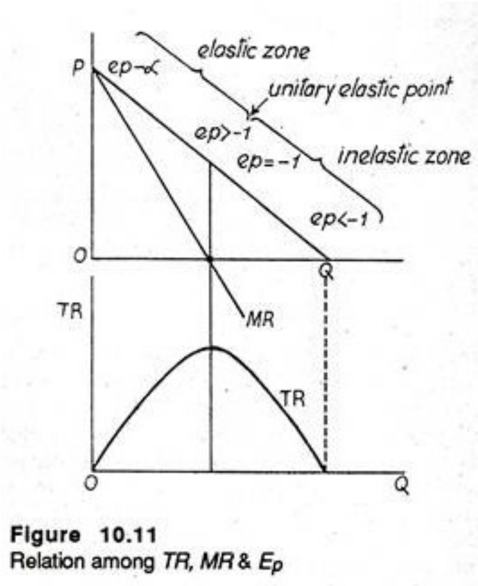
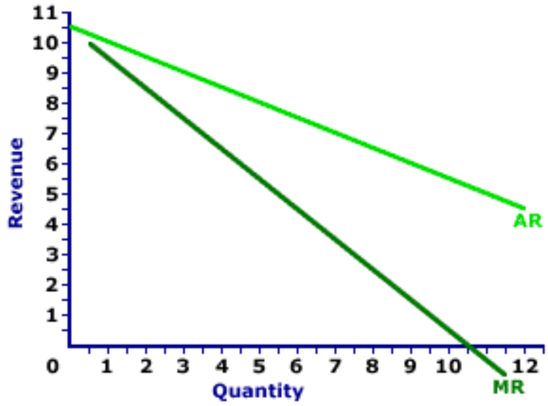
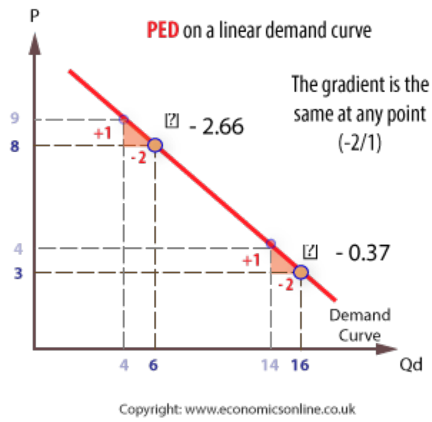


Figure 10.11
Relation among *TR, MR* & *Ep*



Understanding of price elasticity of demand.
Use of MR to show that at first as price falls demand must be elastic as MR is positive.
Beyond the mid-point as price falls demand must be inelastic as MR is negative.
When price falls for a product which is price elastic revenue rises.
When price falls for a product which is price inelastic revenue falls.
Candidates are likely to use a point elasticity approach.
A descriptive approach merely stating the points where Ped changes on the demand curve max band 2 AO1 and band 1 AO3.



<table>
<tr><td colspan="4">2. (b) Evaluate the extent to which knowledge of price elasticity of demand are important for decision making by firms and governments? Use diagrams to illustrate your answer. [20]</td></tr>
<tr><td rowspan="2">Band</td><td>AO1</td><td>AO3</td><td>AO4</td></tr>
<tr><td>6 marks</td><td>6 marks</td><td>8 marks</td></tr>
<tr><td>3</td><td>5-6 marks
Excellent knowledge

An excellent knowledge is shown of how price elasticity of demand is important for the decision-making of both firms and governments.
Accurate diagrams have been used to show the importance of price elasticity of demand. Diagrams are well integrated into the text.</td><td>5-6 marks
Excellent analysis

An excellent analysis of the importance of price elasticity of demand to firms and governments.
There is a clear line of argument showing the importance of price elasticity of demand. Both firms and governments are analysed strongly.</td><td>6-8 marks
Excellent evaluation

There is a well-balanced assessment as to the importance of price elasticity of demand looking at why it may or may not be important. Answers in this band will balance the importance of price elasticity of demand against other factors that are important in the decision making process and include an overall judgement.</td></tr>
<tr><td>2</td><td>3-4 marks
Good knowledge

A good knowledge is shown of how price elasticity of demand is important to firms and governments. However, depth of understanding across both firms and governments may be lacking.
Diagrams have some errors and may not address both firms and governments.
Diagrams may not be well integrated into the answer.</td><td>3-4 marks
Good analysis

A good analysis with a clear chain of reasoning but there be some lack of depth or breadth. Either firms or governments may only be covered superficially in the analysis.</td><td>3-5 marks
Good evaluation

Answers in this band are strong two sided approaches which in the end fail to judge the actual importance of price elasticity of demand.

Developed counterarguments are present.</td></tr>
<tr><td>1</td><td>1-2 marks
Limited knowledge

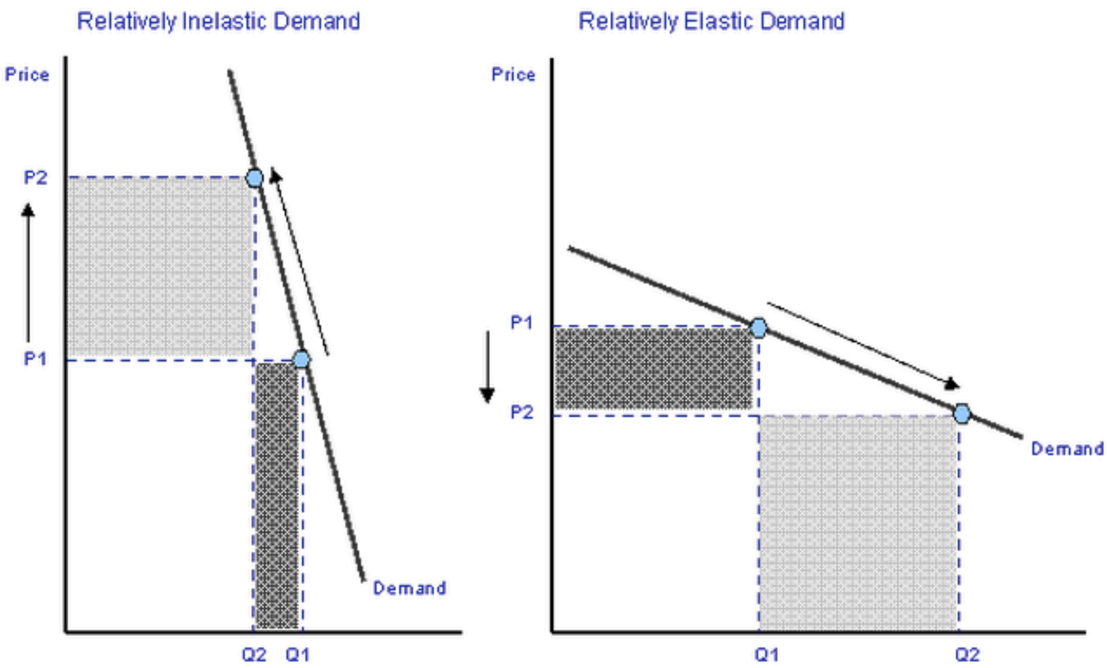
A limited level of knowledge of the importance of price elasticity of demand to firms and governments. Assertions may be made but there is no real explanation which would show a higher level of understanding.
Diagrams contain errors or may be absent.</td><td>1-2 marks
Limited analysis

Analysis of the importance of price elasticity of demand tends to be superficial for both firms and government.</td><td>1-2 marks
Limited evaluation

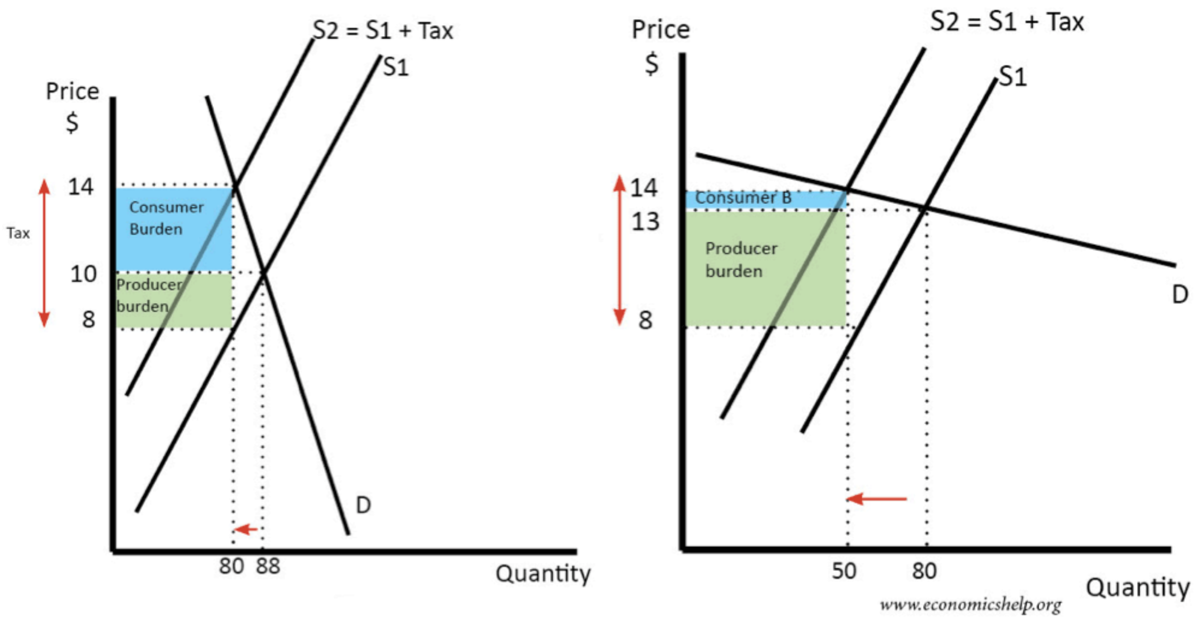
Some counter-arguments are present, but they tend to be asserted rather than analysed. Hence the depth of evaluation that is required for a higher band is absent.</td></tr>
<tr><td>0</td><td>0 marks
No knowledge or understanding shown</td><td>0 marks
No valid analysis</td><td>0 marks
No relevant evaluation</td></tr>
</table>

Indicative content:

Price elasticity of demand is important for firms when price setting if demand is price elastic revenue will rise after a price cut but if demand is price inelastic revenue will rise after a price rise.



When a government is imposing sales taxes then tax revenue will increase if demand is price inelastic but fall if demand is price elastic.
Consideration for government – impact on consumers when trying to reduce negative consumption externalities and impact on firms such as employment, output and profits.



BUT.

Knowledge of price elasticity of demand may be imperfect as it changes over the price range and as a result of changing market conditions – new entrants, state of the macro economy etc.
Other factors just as important – price is only one part of the marketing mix ie place, promotion and product.
Setting the price will depend on the objectives of firms –profit max, revenue max or sales max.
Government has other considerations when setting taxes – such as macro objectives, distribution of income and resource allocation.
Price elasticity of demand is only relevant when setting sales taxes.

<table>
<tr><td colspan="3">3. (a) Using the quantity theory of money, explain why an increase in the money supply might cause a rise in inflation. [10]</td></tr>
<tr><td rowspan="2">Band</td><td>AO1</td><td>AO3</td></tr>
<tr><td>6 marks</td><td>4 marks</td></tr>
<tr><td>3</td><td>5-6 marks
Excellent knowledge

Excellent knowledge of some version of the quantity theory in which the answer demonstrates clear understanding of its own form.</td><td></td></tr>
<tr><td>2</td><td>3-4 marks
Good knowledge

Good knowledge of some version of the quantity theory in which the answer demonstrates understanding of its own form, but there are some weaknesses on parts of it.</td><td>3-4 marks
Good analysis

Clear explanation of how an increase in the money supply could be expected to trigger an increase in the price level/inflation.</td></tr>
<tr><td>1</td><td>1-2 marks
Limited knowledge

Learner only demonstrates a narrow knowledge of any version of the quantity theory, possibly limited to knowing an equation and identifying its component elements.</td><td>1-2 marks
Limited analysis

Some explanation of the link between the money supply and inflation/the price level is made, but there are clear weaknesses in parts of the chain of argument/</td></tr>
<tr><td>0</td><td>0 marks
No knowledge or understanding is present</td><td>0 marks
No valid analysis</td></tr>
</table>

Indicative content:

AO1
There are many forms of the quantity theory, ranging from the Fisher equation to the Cambridge approach. Accept any of these that are well explained. Hence, likely formulations include:

MV=PQ or MV=PY
Where: M = money stock/money in circulation
V= Velocity of money in final expenditure/velocity of circulation
P= Price level
Q/Y= real GDP/index number of real value of final expenditures/

MV=PT
Similar to the above, with V = to the average frequency with which a unit of money is spent across all transactions and T is an index of the real value of aggregate transactions.
The Cambridge approach (courtesy of Wikipedia)

Cambridge approach [edit]

Further information: Cambridge equation

Economists Alfred Marshall, A.C. Pigou, and John Maynard Keynes (before he developed his own, eponymous school of thought) associated with Cambridge University, took a slightly different approach to the quantity theory, focusing on money demand instead of money supply. They argued that a certain portion of the money supply will not be used for transactions; instead, it will be held for the convenience and security of having cash on hand. This portion of cash is commonly represented as *k*, a portion of nominal income ($P \cdot Y$). The Cambridge economists also thought wealth would play a role, but wealth is often omitted for simplicity. The Cambridge equation is thus:

$$M^d = k \cdot P \cdot Y$$

Assuming that the economy is at equilibrium ($M^d = M$), Y is exogenous, and *k* is fixed in the short run, the Cambridge equation is equivalent to the equation of exchange with velocity equal to the inverse of *k*:

$$M \cdot \frac{1}{k} = P \cdot Y$$

Do not be too pedantic about all this.

AO3
Both sides of the standard Fisher equation (or equivalent) measure money GDP in expenditure terms. If the money stock is increased, this should therefore lead to an increase in AD. This could be direct or indirect.

Directly could be the process of printing money and supplying it to the government to spend (Zimbabwe etc).
Indirectly would be via QE.

In either case, AD should rise and if there isn't spare capacity in the economy this will then feed through to higher prices via both demand pull and cost push (higher competition for resources in factor markets) pressure.

<table>
<tr><th colspan="4">3. (b) Discuss whether a reversal of QE is likely to be economically beneficial. [20]</th></tr>
<tr><th rowspan="2">Band</th><th>AO1</th><th>AO3</th><th>AO4</th></tr>
<tr><th>6 marks</th><th>6 marks</th><th>8 marks</th></tr>
<tr><td>3</td><td>5-6 marks
Excellent knowledge

Excellent knowledge is shown of QE and/or its reversal.</td><td>5-6 marks
Excellent analysis (reversible)

Excellent analysis of how reversed QE will be beneficial in terms of helping central banks and governments to achieve their policy objectives/prevent future problems</td><td>6-8 marks
Excellent evaluation

(reversible)
Evaluation points are well developed showing why the reversal might not be desirable. An overall judgement draws together issues from both sides of the argument and/or there may be an integrated approach to evaluation.</td></tr>
<tr><td>2</td><td>3-4 marks
Good knowledge

Good knowledge of QE and/or its reversal but there may be some misunderstandings about the process.</td><td>3-4 marks
Good analysis

Good analysis of how QE will be beneficial in terms of helping central banks and governments to achieve their policy objectives/prevent future problems. The range may be a little narrow, possibly mainly centring around inflation</td><td>3-5 marks
Good evaluation

A strong two-sided answer with effective points on both sides of the argument, but which never directly answers the question set in terms of coming to a reasoned conclusion.

Developed counterarguments are present.</td></tr>
<tr><td>1</td><td>1-2 marks
Limited knowledge

Limited knowledge of QE and/or its reversal. An understanding of the process through which changes in the money supply have an effect is not demonstrated.</td><td>1-2 marks
Limited analysis

Limited analysis of how QE will be beneficial in terms of helping central banks and governments to achieve their policy objectives/prevent future problems Analysis is brief and superficial lacking both breadth and depth.</td><td>1-2 marks
Limited evaluation

A basic attempt is made to show that a reversal of QE may not be desirable. Points are qualified to a limited extent but there is little depth of explanation.</td></tr>
<tr><td>0</td><td>0 marks
No knowledge of QE/QT is shown.</td><td>0 marks
No relevant/valid analysis.</td><td>0 marks
No valid evaluation present.</td></tr>
</table>

Indicative content:

AO1
Understanding that a reversal of QE would imply the opposite of QE. Allow answers that show a strong understanding of the QE process to achieve band 3.

QT would involve the central bank beginning to resell government bonds to financial markets, removing the money received from circulation.
This would depress bond prices and tighten liquidity in markets
The fall in bond prices would both reduce the wealth of bond holders and would increase bond yields.
An increase in bond yields would be expected to have an impact on the prices (down) and yields (up) of other assets as investors rebalance their portfolios.

AO3 case for (or case against if reversed)
The merits of QE overall are unclear and opinions differ in terms of what it effects have been (some impact on growth in Japan, evidence more uncertain elsewhere). Hence it is difficult to know what the likely impacts of unwinding it are.

One criticism of QE is that it has helped to create another asset bubble in shares and housing. Reversing QE would be likely to put downward pressure on these asset prices (or at least reduce further upward growth).

Before Covid-19 it would be expected that reversing QE would have put downward pressure on inflation and with unemployment in some economies prior to 2020 clearly at or below the NAIRU, there was a clear case for anti-inflationary action. During the Covid-19 pandemic reversing QE could cause a prolonged recession.

QE has heralded an era of unprecedentedly low interest rates which has been extremely damaging to savers, those close to retirement and those trying to earn an income from savings, distorting returns towards those invested in the stock exchange and property.

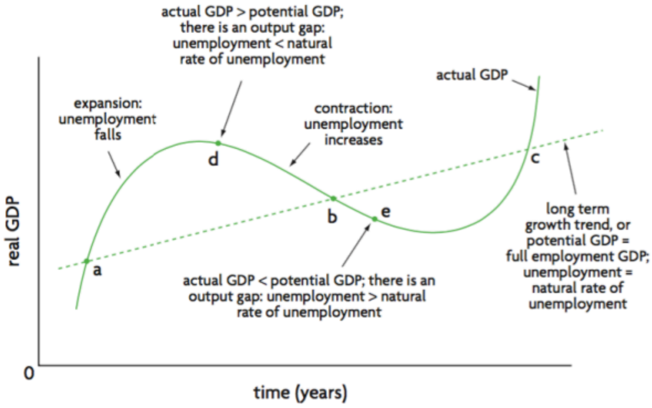
AO4 case against plus evaluation.
Rising bond yields will make government debt refinancing tricky
Not all economies are in a situation where tighter monetary policy is appropriate
Might be better to wait until interest rates have had chance to rise further before QT – give more ‘headroom for conventional monetary policy.
Much will depend on the pace at which it is done and the method
Inflation rates in many QE areas are still very low, suggesting that there is no immediate need to reverse QE.
It is unclear what the effects will be – if policy is tightened too quickly, there may be the risk of another asset price crash, putting us back to where we were in 2008 (although bank balance sheets are in principle stronger).

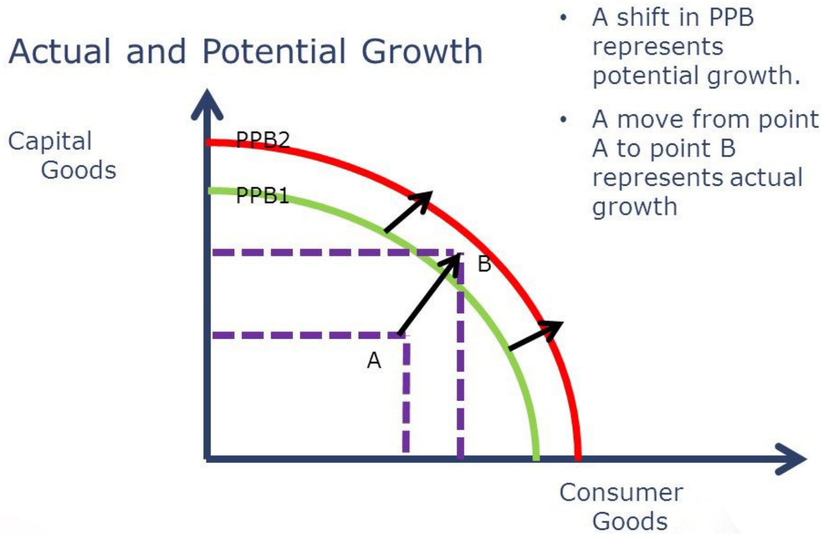
Strong AO4 will think about the title – at the present time. What is happening at the present time? How will this vary by country at the present time? What forms of QE reversal might be appropriate – certainly not all of these, but some consideration of one of these issues would be indicative of a very strong response if the other aspects of the answer are strong.
Candidates referring to the Covid-19 pandemic in their answer should be rewarded if the points made are relevant.

4. (a) With the aid of diagrams, explain the difference between actual growth and potential growth. **[10]**		
Band	AO1	AO3
	6 marks	4 marks
3	**5-6 marks** Excellent knowledge Excellent knowledge of actual and potential growth. Accurate and well annotated diagram which is integrated into the answer.	
2	**3-4 marks** Good knowledge A good knowledge of actual and potential growth but the differences between them are not shown directly no comparison between the two is present. Diagram may have minor errors and not be well integrated.	**3-4 marks** Good analysis Clear chain of reasoning is demonstrated to show the difference between actual and potential growth using the diagram effectively.
1	**1-2 marks** Limited knowledge Some knowledge of actual and potential growth is present, but the difference is unclear and only one of them has been outlined.	**1-2 marks** Limited analysis Chain of reasoning is unconvincing or superficial. Diagram is not used or used to a limited extent.
0	**0 marks** No knowledge or understanding shown	**0 marks** No valid analysis

Indicative content:

Any of the three diagrams below are acceptable.





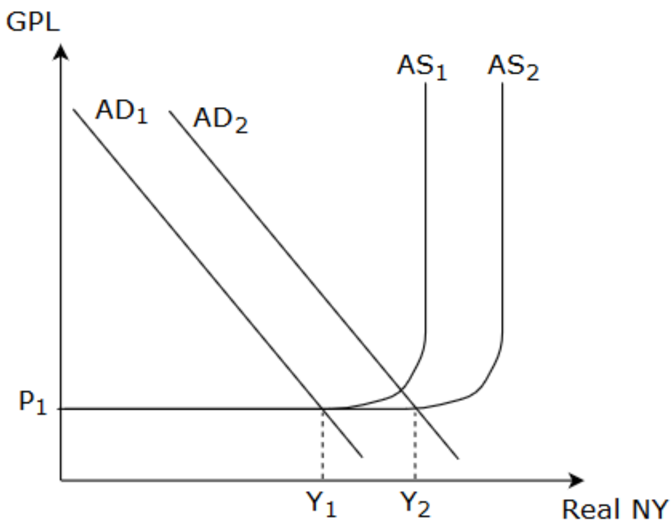


Figure 3

Actual growth is a rise in GDP when an economy moves from a point within the PPF closer to the potential output, representing an increase in AD in an economy.
Potential growth occurs when the PPF shifts to the right as a result technological change, increased productivity of resources, discovery of new resources etc, representing an increase in LRAS.
Potential GDP can only be reached by the economy when actual GDP rises to the potential level through an increase in economic activity.

4. (b) To what extent is economic growth beneficial to an economy? [20]			
Band	AO1	AO3	AO4
	6 marks	6 marks	8 marks
3	**5-6 marks** Excellent knowledge An excellent knowledge of the benefits/costs of economic growth to an economy. At least three benefits are identified with understanding shown.	**5-6 marks** Excellent analysis An excellent analysis of how economic growth benefits the economy. There is a clear line of argument as to how economic growth benefits/costs the economy.	**6-8 marks** Excellent evaluation There is a well-balanced assessment of whether economic growth might be good or bad for the economy. Answers in this band will balance the importance of economic growth against some its downsides and come to an overall judgement/conclusion.
2	**3-4 marks** Good knowledge Good knowledge of the benefits of economic growth. At least two benefits/costs are identified with understanding shown. More than two benefits may be identified but explanations are sometimes inadequate or superficial.	**3-4 marks** Good analysis A good analysis of how economic growth benefits the economy. Answer may be strong only on some benefits/costs with a limited development of others.	**3-5 marks** Good evaluation Answers in this band are strong two sided approaches which fail to judge the actual importance of economic growth. There may be a lack of a reasoned conclusion. Developed counterarguments are present.
1	**1-2 marks** Limited knowledge Limited knowledge of the benefits of economic growth. One or two benefits/costs may be identified but without sufficient explanation.	**1-2 marks** Limited analysis A limited analysis of how economic growth benefits/costs the economy. Analysis may be superficial lacking clear chains of reasoning.	**1-2 marks** Limited evaluation The answer is two sided and attempts to argue that there are benefits and downsides to economic growth but qualification is quite limited being undeveloped or superficial.
0	**0 marks** No knowledge or understanding shown	**0 marks** No valid analysis	**0 marks** No valid evaluation

Indicative content:

Benefits of economic growth.

- **Improvements in living standards:** Growth is an important avenue through which per capita incomes can rise and absolute poverty can be reduced in developing nations.
- **More employment:** Growth creates new jobs – although the pattern of employment will also change
- **The accelerator effect of growth on capital investment:** Rising demand and output encourages investment in capital – this helps to sustain GDP growth by increasing LRAS
- **Greater business confidence:** Growth has a positive impact on profits & business confidence
- **The "fiscal dividend":** A growing economy boosts tax revenues and generates the money to finance spending on public and merit goods and services without having to raise tax rates
- **Potential environmental benefits** – as countries grow richer, they have more resources available to invest in cleaner technologies. And, as nations develop, energy intensity levels fall.

Costs of economic growth.

Rapid rates of GDP growth can bring about undesirable economic and social costs – much depends on the nature/causes of growth.

Risks of higher inflation and higher interest rates

- Fast-growing demand can lead to demand-pull and cost-push inflation – this leads to a conflict between macro objectives
- The central bank may decide to raise interest rates to control inflation

Environmental effects

- More negative externalities such as pollution & waste (degradation)
- Risk of unsustainable extraction of finite resources – i.e. fast growing countries may cause a long-run depletion of natural resources

Inequalities of income and wealth

- Rapid increases in real national income can lead to a higher level of inequality and social divisions
- Many of the gains from growth may go to only a few people

An overall judgment may include discussion of whether the economic growth is occurring in an LDC or an MDC. Also the role of government is important in trying to maximising the benefits of economic growth and minimising the costs of it.

Source. tutor2u.net.

5. (a) Explain why dependency on a narrow range of primary products may damage an economy's economic development. [10]		
Band	AO1	AO3
	6 marks	4 marks
3	**5-6 marks** Excellent knowledge Excellent knowledge of the ways in which primary product dependency is damaging. Several issues are well-developed.	
2	**3-4 marks** Good knowledge Good knowledge of the ways in which primary product dependency is damaging. At least one issue is developed.	**3-4 marks** Good analysis Well-developed chain of reasoning which shows why PPD is damaging for economic development. The link to economic development is clear.
1	**1-2 marks** Limited knowledge Limited range of ways in which primary product dependency has an impact. Or Knowledge of the meaning of PPD is shown.	**1-2 marks** Limited analysis There is a link to economic development, but the chains of reasoning linking PPD to it are under-developed.
0	**0 marks** No knowledge or understanding is present	**0 marks** No valid analysis

Indicative content:

AO1
There are a range of issues that may be considered:

Price volatility may damage investment, incomes ad government finances
Over time primary product prices (especially agriculture) may fall relative to those of secondary products, worsen the terms of trade of primary exporters (Prebisch-Singer hypothesis)
Low value added generally
Risk of Dutch disease (capital flows into valuable resource sectors drive up the exchange rate and strangle other sectors)
Resource curse – economy becomes overly dependent on one sector, plus in the case of high value added products create the risk of conflict over control of resources (blood diamonds) and break the contract between the governed and those governing making maladministration and corruption more likely.
Risk of depletion leaving the economy underdeveloped and experiencing rapid decline in living standards.

AO3
Some of the ideas outlined above will be developed in the context of economic development (as opposed to economic growth). Hence there will be a link between the problem identified and the negative impact on economic development. Although definitions of economic development differ, the idea of improved living standards is central to most, with an emphasis on health and education in addition to income. A variation on this is the idea of expansion of choice, which will generally require higher income and better health and education to achieve.

5. (b)	**Discuss whether an increase in inward foreign direct investment is a good way to improve economic development for countries that are primary product dependent. [20]**		
Band	AO1	AO3	AO4
	6 marks	6 marks	8 marks
3	**5-6 marks** Excellent knowledge Excellent knowledge of how FDI might or might not be beneficial for PPD countries.	**5-6 marks** Excellent analysis (reversible) Excellent analysis with strong chains of argument about how FDI will be beneficial to countries that face PPD issues. Answer will link well to how economic development will be promoted.	**6-8 marks** Excellent evaluation (reversible) Evaluation points are well developed showing why FDI might not be desirable. An overall judgement draws together issues from both sides of the argument and/or there may be an integrated approach to evaluation, focusing on the impact on economic development.
2	**3-4 marks** Good knowledge Excellent knowledge of how FDI might or might not be beneficial for PPD countries, but there may be a limited range of ideas on one side of the debate.	**3-4 marks** Good analysis Good analysis with strong chains of argument about how FDI will be beneficial to countries that face PPD issues.	**3-5 marks** Good evaluation A strong two-sided answer with effective points on both sides of the argument, but which never directly answers the question set in terms of coming to a reasoned conclusion. Developed counterarguments are present.
1	**1-2 marks** Limited knowledge A limited knowledge of the costs or benefits of FDI, with few identified and/or little development of each.	**1-2 marks** Limited analysis Analysis is brief and superficial and is likely to lack range of ideas.	**1-2 marks** Limited evaluation A basic attempt is made to show that FDI may not be desirable. Points are qualified to a limited extent/counter-arguments are present but there is little depth of explanation.
0	**0 marks** No knowledge of costs or benefits of FDI shown	**0 marks** No relevant/valid analysis.	**0 marks** No valid evaluation present

Indicative content:

AO1

There are a range of possible effects that might be considered.

FDI useful:
Can bring expertise to allow resources better to be extracted
Links to markets in MEDCs
MNCs may build infrastructure as part of a package deal/to allow better transport/skills
May bring training to ensure that they have the staff that they need
The inflow of investment capital helps to overcome savings gaps
Local multiplier effects in terms of direct and indirect job creation
Investment may be required to allow resources to be accessed at all.
Investment may add processing ability allowing higher value added to be generated.
Investment may increase productivity in all sectors, including agriculture.

FDI of limited benefit
May bring own workforce
Profits may be repatriated
Working conditions and pay may be poor
Environmental issues
Competition with local firms may drive them out of business
Further reinforces PPD (primary product dependency)
MNCs in some countries prop up corrupt governments
May accelerate resource depletion

AO3

AO3 is reversible, and will therefore link FDI either to improvements or deteriorations in the level of economic development for PPD countries.

The key to moving up the AO3 bands will be explaining how FDI helps to tackle the problem of PPD and how in turn economic development will be raised (or how FDI will hinder the problem of PPD and how economic development will not be raised).

AO4

Standardly, this may contain developed counterarguments to the points made, or qualifications that show that it isn't necessarily so.

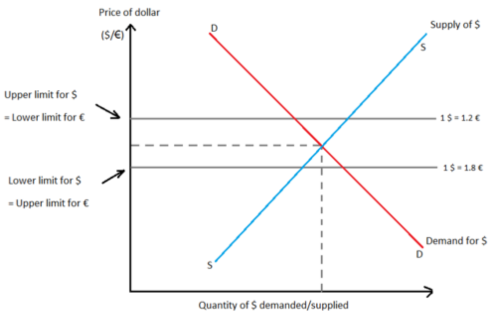
Top level AO4 will engage directly with the question which asks the extent to which FDI will raise economic development. Thoughtful answers are likely to think about the nature of FDI, the strength of the government in the country, its current level of economic development, the current level of FDI and so on; in other words, FDI may be more beneficial under some circumstances than others.

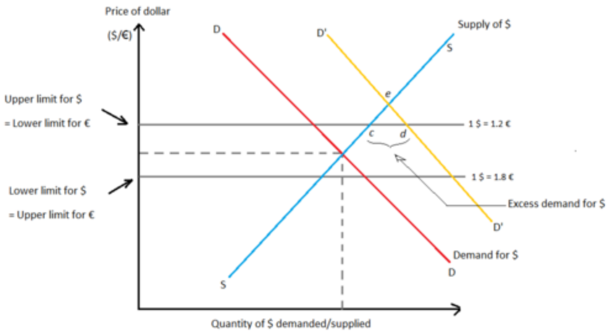
A narrow focus on the advantages and disadvantages of FDI to a LDC without reference to PPD is limited Band 2.

6. (a) **Explain, using a diagram, how an EU member could stabilise its currency against the euro prior to joining the eurozone. [10]**		
Band	AO1	AO3
	6 marks	4 marks
3	**5-6 marks** Excellent knowledge An excellent knowledge is shown of how currencies can be stabilised. More than one policy is identified. The diagram is accurately drawn, well annotated and integrated into the answer.	
2	**3-4 marks** Good knowledge A good knowledge is shown of how currencies can be stabilised. There may be a lack of detail or gaps in understanding. There may be minor errors in the diagram and it may not be well integrated.	**3-4 marks** Good analysis A good chain of reasoning is in evidence when analysing the policies that can be used to stabilise a currency. More than one policy is analysed showing a clear chain of argument.
1	**1-2 marks** Limited knowledge There is a limited knowledge of how currencies can be stabilised showing significant gaps in knowledge and understanding. The diagram may contain errors and not be integrated.	**1-2 marks** Limited analysis Analysis is superficial with a lack of clarity and the chain of reasoning is unconvincing.
0	**0 marks** No knowledge or understanding.	**0 marks** No valid analysis.

Indicative content:

Candidates will use the diagram below to show how either a change in domestic interest rates and/or use of foreign exchange reserves can be used by an EU member prior to membership of the euro zone.
The EU member will undertake to keep their domestic currency between the upper and lower limits.





Mention may be made of the convergence criteria and ERM2 which prospective Eurozone members are required to join prior to adopting the single currency. A currency in ERM II is allowed to float within a range of ±15% with respect to a central rate against the euro. EU countries that have not adopted the euro are expected to participate for at least two years in ERM II before joining the euro zone.

Band 2 maximum for only one currency stabilisation policy being mentioned.

6. (b) Discuss the possible benefits and drawbacks to EU member countries of adopting the euro. [20]			
Band	AO1	AO3	AO4
	6 marks	6 marks	8 marks
3	**5-6 marks** Excellent knowledge Excellent knowledge of the benefits and drawbacks of euro zone membership. A wide range of points are identified.	**5-6 marks** Excellent analysis An excellent analysis of the impact of euro zone membership. There is a clear line of argument shown on a wide range of points.	**6-8 marks** Excellent evaluation There is a well-balanced assessment as to relative importance of the benefits and drawbacks of euro zone membership coming to a reasoned overall judgement.
2	**3-4 marks** Good knowledge Good knowledge of the benefits and drawbacks of euro zone membership. The range of points may be more limited than in a band 3 answer. Alternatively, a fair range of points are identified but these are not well developed thus the depth of understanding is not present to allow a band 3 answer.	**3-4 marks** Good analysis A good analysis of the impact of euro zone membership. The answer may be strong on some of the effects of euro zone membership with a limited development of others.	**3-5 marks** Good evaluation Answers in this band are good two sided responses giving a full set of arguments on both sides. Evaluation at this level may lack some sophistication and lack a reasoned judgement. Developed counter arguments are present.
1	**1-2 marks** Limited knowledge Some benefits and drawbacks of euro zone membership are identified but understanding is not well demonstrated. The answer is primarily knowledge based.	**1-2 marks** Limited analysis A limited analysis of how euro zone membership will impact on an EU member. Chains of reasoning are limited and/or superficial.	**1-2 marks** Limited evaluation The answer is two sided and attempts to argue that there are benefits and drawbacks but qualification is quite limited and underdeveloped.
0	**0 marks** No knowledge or understanding shown	**0 marks** No valid analysis	**0 marks** No valid evaluation.

Indicative content:

1. Lower transaction costs

With single currency membership, there will no longer be a cost involved in changing currencies; this will benefit tourists and firms who trade with a euro zone member.

2. Price transparency

With a common currency, it will be easier to compare prices in different European countries because they would all be in Euros. This enables firms to source cheaper raw material and consumers to buy cheaper goods,

3. Eliminating exchange rate uncertainty

Volatile swings in the exchange rate can destroy the profitability of exports (e.g. a rapid appreciation). This exchange rate uncertainty undermines business confidence in investing. Therefore with a single currency business confidence should improve leading to greater trade and economic growth.

4. Improved trade

Supporters of the Euro argue that greater price and cost transparency/no exchange rates encourages intra Eurozone trade. The Single Market can only achieve its potential if there is a single currency.

4. Improvement in inflation performance

The ECB which sets interest rates for the whole Eurozone area will be committed to keeping inflation low; countries with traditionally high inflation should benefit from this greater inflationary discipline. EU inflation has been low.

5. Low-interest rates

It was hoped membership of the Euro would help reduce bond yields as there was greater security belonging to a stronger currency.

6. Inward investment

Inward investment may increase from outside the EU as firms take advantage of lower transaction costs within the EU area. Some firms have said they prefer to invest within the Eurozone area.

7. Benefits to the financial sector

The introduction of the Euro appears to have reduced the cost of trading in bonds, equity, and banking assets within the euro zone.
Source: economics.org

BUT.

Loss of independent monetary policy with a possibility of fiscal union in the long run.
Obliged to always keep to the convergence criteria.
No ability to depreciate currency when there is a recession or a negative trade deficit.
Changeover costs.
Very difficult to leave the euro zone once a member.
Depends on the extent to which the Eurozone is an optimal currency area
Depends on the flexibility of an economy's product and labour markets
Depends on the extent to which economic cycles are harmonised at the point of entry.
'One size fits all' monetary policy inappropriate across a range of economies.

Candidates who merely discuss the benefits and drawbacks of EU membership maximum band 1.