

2005 Economics

Advanced Higher

Finalised Marking Instructions

These Marking Instructions have been prepared by Examination Teams for use by SQA Appointed Markers when marking External Course Assessments.

Marking Instructions
Economics Advanced Higher

Detailed marking instructions/guidelines

In the essay questions in particular it is not necessary for candidates to include all the points listed. Candidates are expected to demonstrate a thorough appreciation of the topic and a sound understanding of the economic issues under discussion. Marks should not be allocated on rigid point-scoring basis, but on the overall quality of the answer.

Candidates who use appropriate examples and show evidence of up to date knowledge of the question being answered should be rewarded accordingly.

Advanced Higher: Marking Scheme

Marks

Section A

1.	<p>Inefficient allocation of resources – Factors of production are not used in the best way or location to maximise economic welfare (output).</p> <p>Differentials – Proportionate differences in pay between one grade of worker and another.</p> <p>Low Pay Commission – Statutory body that advises the UK Government on the level and scope of the NMW.</p>	3
2.	<ul style="list-style-type: none"> • To achieve ‘fair’ wage levels • Protect public sector workers • Compensate members for the rise in the cost of living (for example in housing, transport, gas and electricity) 	3
3.	<p>Recent increases have been significantly above the rate of inflation (four times) and the general level of wage increases (double)</p> <p>Sharp increases in other costs – fuel, rates and cost of compliance with new regulations.</p> <p>Reduce competitiveness of manufacturing.</p>	3
4.	<p>Large employers are likely to be well known and with a reputation to protect who may pay more and often offer better terms of employment than some small firms who may use and exploit cheap (sweated) labour.</p> <p>The economy in general will benefit from higher AMD, the multiplier effect and the extra tax revenue generated by the spending and earnings of those paid the higher NMW. Reduced benefits and credits paid to the low paid.</p>	2 2
5.	<p>Labour market is tighter in some areas because of the difficulty in recruiting labour and therefore wage rates are forced higher</p> <p>Costs of living, especially for housing and transport, are higher in London and SE England</p>	2
6.	<p>(a) Diagram drawn to show Supply in excess of Demand if the wage rate is fixed above the equilibrium wage. The diagram should also show potential unemployment on the x axis.</p> <p>(b) There is no such thing as a single labour market. Suitable examples needed to demonstrate the fixed nature of the labour supply in the short run in a given occupation. ‘People are not bananas’ because they are not all the same! Depends on current employment levels. Firms may ‘hoard’ labour. Past experience = 1</p>	4 3
7.	<p>Migrant workers may be happy to accept the NMW (or less?) that may be much higher than that paid in their country of origin</p> <p>Fill gaps in key shortage areas where UK workers are unwilling to work or where there are skills shortages</p>	3
		(25)

Section B

Marks

1.	(a)	Rising oil prices	
		Reasons include	
		<ul style="list-style-type: none">• The high rate of economic growth in 2004 (highest in 30 years)• The rapid growth of China and its demand for oil• Speculation leading to the hoarding of stocks• Disruptions to supply in Iraq, Venezuela, Nigeria• Reluctance by OPEC to increase supply• Low levels of reserves in the USA• Absence of new major discoveries since 2000 (Kazakhstan)• Problems caused by adverse weather conditions, for example hurricane Ivan in the Gulf of Mexico• Uncertainty created by the conflict between the Russian government and Yukos that could reduce supply	8
	(b)	High oil prices reduce disposable income because the demand for oil is relatively price inelastic and therefore cuts the level of AMD. This is subject to a multiplier effect nationally and internationally. Oil prices are likely to be passed in the form of higher production costs and in increases in domestic fuel and transport prices. The US economy is more oil dependant than most and also represents 25% of world GDP.	6
	(c)	Factors to be considered include	
		<ul style="list-style-type: none">• Oil prices have fallen (how much? – check position in May 2005!)• OPEC increasing supplies• A higher price brings forth a higher supply both from existing producers and new or marginal suppliers.• World is less oil dependant than in the past because of greater efficiency and attempts to diversify the sources of energy, especially in the USA.• World inflation under closer scrutiny and control than in the past• The real price of oil is still much lower than in 1979 (about \$80 a barrel in real terms).• The importance of Russia on the supply side; the world’s largest producer is keen to use oil to establish its influence on the world economy.• Value of the dollar.	11
		NB Candidates who suggest that we are too complacent about the effect of higher prices should be rewarded if they support this view with clearly constructed arguments.	(25)

2. (a) Microeconomic reforms refer to the supply side changes that helped to improve productivity in the ‘Thatcher years’. These include trades union reform, privatisation, deregulation of the labour and other markets, cuts in direct taxation and an emphasis on education and training.
 Macroeconomic revolution refers to the operational independence of the Bank of England removing monetary policy from the political arena and establishing tried and tested methods of putting the economy on ‘cruise control’ using an inflation target as the base control. 8
- (b) Success in recent years owed more to luck than judgement?
 The benefits of cheap products from Asia, especially from China, are endangered by inflationary trends in Asia.
 The public finances may be getting out of control and taxes may need to be increased.
 Higher commodity prices.
 Changing exchange rates making UK exports to the USA less competitive.
 Wage pressures have been subdued, can this continue?
 Many firms face higher production costs that they may be forced to pass on as higher prices.
 Other members of the G7 expected to perform much better, especially Japan.
 The uncertainty caused by the house price boom leading to a bursting of the bubble.
 Can competitiveness be maintained if service industry firms begin to outsource to cheaper locations?
 Slow productivity growth in manufacturing and the public sector. 9
- (c) **Benefits include**
 Higher living standards, employment levels and productivity gains.
 Ability to use the growth surplus to develop health, education, transport or housing without needing to raise tax rates.
 Develop a wider range and better products.
 Mood of confidence encourages entrepreneurial initiative and enterprise.
 Opportunity to cut poverty without reducing the income levels of the more affluent.
 More leisure time to enjoy the fruits of economic success.
- Costs include**
 Depletion of economic resources.
 Social costs including pollution, congestion and noise.
 Current living standards may suffer in the pursuit of higher levels of capital investment.
 Inflationary pressures may be unavoidable if shortages develop in some factor markets.
 Crime, vandalism, stress and depression associated with hectic urban life. 8
- (25)**

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|----|---|------|
| 3. | <p>(a) Present arrangements for pensions will not generate sufficient income to meet the needs of pensioners in the future.</p> <p>Causes include
 People living longer.
 The poor performance of the Stock Market and other financial markets yielding lower returns than anticipated.
 The closure of many private sector firms pensions schemes to new entrants.
 Lower interest rates to the detriment of pensioner savings.
 A falling birth rate increasing the dependency ratio.
 Some would blame higher taxes causing higher costs in the management of pension schemes.
 It is considered that the share of pension payments as a percentage of GDP must rise from 10% to about 16% in the next 50 years.
 Large numbers of people especially the low paid have little or no private pension provision.
 The fall in the relative value of the state pension in the last 25 years.
 Low savings ratio in the UK.</p> | 8 |
| | <p>(b) The Pensions Commission has suggested that four options demand closer examination.
 Pensioners become even poorer relative to average income.
 Higher taxes and National Income Contributions.
 Higher levels of private saving, that might be made compulsory.
 Higher average retirement ages for both men and women.
 The Pensions Commission will submit a full report in autumn 2005, but has indicated that a combination of the above options is likely to be recommended.
 Extend the number of year's service to qualify for the full pension scheme.
 Tax breaks to encourage larger families, but this will take a long time to be effective and it may not work anyway!
 Schemes in other countries (eg Australia).</p> | 10 |
| | <p>(c) Inaction will mean that pensioners are consigned to even greater poverty in the future.
 People might become readier to save for retirement without compulsion, although this seems unlikely.
 Equity yields, stock markets prices and interest rates may all rise and reduce the problem.
 Compulsory retirement ages are abandoned as in many other countries giving people a choice of how their living standards will fare in their declining years.
 Good candidates will observe that the situation is much worse in France and Italy where the retirement age is much lower.
 Immigration likely to increase size of the working population,
 Potential for (increased) pressure on the public finances.</p> | 7 |
| | | (25) |

Marks

4. (a) Candidates should show an awareness of the fall in value of the dollar, nearly 50% against the value of the euro (early December 2004) since 2001, but also that the current level is a return to the exchange rate of the early 1990s.
The twin Budget and current account deficit – some figures required
US complacency about the deficits encouraging speculation against the dollar.
Uncertainty about the likely response of the holders of US dollars, especially Japan and China when their savings are in effect falling as the dollar falls in value.
Realisation that correcting the deficits will require a substantial fall in the value of the dollar because the deficits are rising so rapidly.
Political uncertainty about the USA's role in the world and its commitment to 'defence' expenditure. **9**
- (b) UK products will become less competitive with USA leading to lost orders and jobs.
Cheaper holidays for UK citizens, but more expensive for Americans coming to the UK.
Since many commodities, in particular oil, are priced in dollars raw material prices will fall.
The rising euro will assist the competitiveness of UK products in most EU markets (candidates are expected to be aware that sellers of US dollars often buy euros).
Lower cost-push inflation.
The recovery of the yen and the euro because of improved prospects in other countries.
Low interest rates. **6**
- (c) USA is in effect exporting its deficit to other countries holding dollar reserves accumulated when goods are sold to the USA.
Many countries in the Americas and Asia use the dollar in addition to or instead of their own currency.
China and other countries peg their own currency to the dollar; this may be unsustainable especially for China who has large dollar reserves and a large trade surplus. Will the renminbi retain the fixed rate against the dollar?
A serious attempt to deal with the US trade deficit would lead to a recession there and throughout the world because of the sharp fall in demand that would take place.
A falling US dollar will reduce competitiveness of products from other countries. **10**
- NB As this is a difficult question, candidates who write intelligently about the role of the dollar in the international economy should be awarded high marks. **(25)**

5. (a) The ability to produce any good or service anywhere in the world, using raw materials, components, capital and technology from anywhere, sell the resulting output anywhere and place the profits anywhere (Peter Jay).
It should be stressed that globalisation is not a new phenomena. 3
- (b) **Benefits include**
Establishment of a truly world wide economy without barriers because of freer trade and the application of modern technology.
Wider range of goods and services available.
Greater competition reducing prices and improving quality and efficiency.
Better allocation of economic resources (specialisation and comparative advantage).
Enables firms to achieve economies of scale.
Opportunities for developing countries to increase living standards.
- Costs include**
Jobs may be lost to other parts of the world.
Exploitation of poorer countries and their citizens and a widening gap between rich and poor.
Environmental and safety standards suffer.
Increased power of MNE's.
Remote decision-making, many people powerless to influence their lives.
'Brain drain' from poorer countries to the developed nations. 12
- (c) Very few regulations exist and they are often ignored by the rich nation when it suits them.
The WTO tries to ensure that the rules of free trade are observed (What about EU farm prices and the CAP and American protectionist measures?).
Voting patterns on the IMF and the WTO are based on economic size and terms can be dictated to the poorer debt ridden nations.
Few countries meet the UN aid recommendation (0.7% of GNP).
Need to reform international institutions to make them more sympathetic to the poor countries of the world. Suggestions might include: human rights declarations related to employment rights; transfer pricing and the use of profits generated in one country not being invested in another; genuinely competitive practices; redistribution of resources to the poorer countries; greater priority for development aid; legal limits to the influence of MNE's.
Growth of the ethical consumer.
Is China an example to the developing world?
No credit for references to Competition Commission and other domestic bodies. 10
- (25)**

6. (a) The scale of the NHS should be mentioned (cost approaching £100 billion and 1.2 million employees) and candidates should make it clear that they know about the large increase in real NHS spending since 2000.
- Attempts to increase the amount of private sector provision by the use of tax breaks (much smaller in the UK than in comparable countries)
 - GP fund-holders.
 - Hospital trusts and boards.
 - Encouragement of competition through the publication of waiting lists and consultant performance indicators.
 - Performance monitoring to improve value for money.
 - Creation of larger and or specialised hospitals .
 - To reward productivity by clinicians (rather than quality).
 - To give patients more choice of hospital and medical practitioner.
 - To make use of underused capacity in other parts of the country or even in other countries.
 - Contracting out some non-medical functions, for example catering and laundry.
 - Attempts to promote a healthier life style, encouraging healthy eating and exercise, limitations on smoking in public places etc.
- (b) Concern about the rising cost of health care.
- Attempts to improve the quality of service. Since medical provision is usually free at the point of delivery to find market-based principles to allocate scarce resources when faced by a potentially unlimited demand.
 - The rising costs associated with advances in medical techniques and equipment.
 - To make fuller use of medical facilities (why not 24/7?).
 - Shortage of suitably trained medical personnel.
 - The consequences of an ageing population.
 - To reach EU levels (as % of GDP) of expenditure on health provision
 - To cut waiting lists and other indicators of unsatisfactory levels of consumer welfare.
 - Healthier population will make fewer demands on the NHS.

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- (c) **Benefits might include**
Greater productivity (shorter waiting lists).
Lower costs.
People respond to market incentives of higher pay and better promotion prospects.
A healthier population and some conditions treated earlier to the gain of the individual and the economy as a whole.
Better value for money for the Exchequer making funds available for financing other activities.
More patient choice.
- Costs might include**
Poorer quality of service.
Less personal service.
Greater bureaucratic structure.
Conflict with consultants and health unions.
Concerns with competition and efficiency might make these a higher priority than patient care.
Less choice for patients as hospitals and GP surgeries are merged into larger units often remote from the patient's home.
- NB Much of the new money has gone towards the payment of higher salaries and better working conditions; this might be viewed as an advantage or a disadvantage.

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(25)

[END OF MARKING INSTRUCTIONS]