

GCE

Economics

Advanced GCE **A2 H461**

Advanced Subsidiary GCE **AS H061**

OCR Report to Centres June 2014

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Reports should be read in conjunction with the published question papers and mark schemes for the examination.

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F581 Markets in Action

General Comments

Overall, candidates performed well in this paper and students and teachers are to be congratulated on the hard work in teaching and learning that lies behind their answers. Almost all candidates finished the whole of the paper.

Continued improvement was seen in succinctness of definitions and clarity of diagrams. The topic of Income Elasticity of Demand was handled by candidates with much more confidence than on previous occasions.

The Case Study on Airfix model production proved accessible to candidates and many took their lead from aspects of the Case Study in some of the shorter-answer questions.

Most candidates answered the essay question with less reference to the Case Study. Some excellent responses were seen, but overall there is room for further development in candidates' ability to explain **how** particular policies, such as indirect taxation, correct market failure.

Comments on individual questions

- Q1 (a)** The great majority of candidates offered a succinct, clear and familiar definition of Opportunity Cost. Those who tried to rephrase the standard definitions in their own formulations were rarely able to achieve this clarity.
- (b)** This question proved difficult for a significant minority of candidates. The Case Study offered the clearest path, with the hint that Airfix had to “make choices over which planes and other models it will produce in any year”. Answers focusing on marketing dilemmas for Airfix were rarely able to integrate this with the concept of Opportunity Cost. A frequent error was to repeat the wording as stated in the text with no development, for which no credit available
- Q2** Almost all candidates were able correctly to state two Factors of Production.
- Q3** The majority of candidates identified a viable advantage and disadvantage of Specialisation but fewer were able to explain how this advantage came about in the production process. Many answers relied on stating that production became “more efficient” which was not credited on its own without further development.
- Q4 (a)** Nearly all candidates drew a correct diagram to show Equilibrium, with accurate labelling, and thus scored full marks. A minority incorrectly labelled the horizontal axis as “quantity demanded”
- (b)** The stem of the question stated two relevant factors, one shifting the demand curve to the right and shifting the supply curve to the right. A significant minority of candidates only used one shift, and therefore lost the opportunity to gain the explanation marks for the correct changes in price and in quantity supplied and demanded.
- (c)** Here, the wording of the question excluded any taste and fashion determinant of demand (including advertising) and by asking about causes of a **shift** in demand also excluded the possibility of using a change in price. The markscheme awarded the first mark for the statement of a determinant, the second for an explanation of how this actually changes the level of demand and the third mark in each half of the question was, on this occasion, available for stating in which direction the demand curve would shift, since this is part of the answer to **how** the demand curve will shift.

- Q5 (a)(i)** The calculation of Income Elasticity of Demand seemed much more accessible to candidates than when this had been asked previously.
- (a)(ii)** Similarly, most candidates were able to offer a clear interpretation of the YED coefficient including specifying that demand was **income-elastic**. A common error was to offer an imprecise explanation that the product is inelastic/elastic and to waste a lot of time defining the term
- (b)** The stem of the question specified that demand was ‘**price-elastic**’. The markscheme therefore expected candidates to offer analysis on this basis. Many candidates defaulted to discussing price-inelastic demand and decisions to raise price, whereas correct analysis developed the strategy of reducing prices to increase revenue. Comment marks were awarded only if analysis had been credited. Some good commentary away from the formulaic reciting of the inaccuracy of estimates was seen, drawing out the importance of the size of the coefficient or looking at other factors that could affect demand. Some candidates seemed confused by being asked to discuss two types of elasticity. **Q6(a)** This question on the ‘extent to which’ negative externalities should be reduced proved very challenging. The hope was that candidates would analyse why governments intervene to correct negative externalities by identifying the economic explanation of the problem of negative externalities, that is showing some analytical awareness, and then evaluate the extent to which the Chinese government should seek to pursue this goal. A small number of very good answers were offered, but many candidates instead wrote a descriptive answer about a particular policy. This was disallowed since policies formed the core of Question 6(b) and answers could not be credited twice.
- (b)** This question did not specify a market but as in some previous examinations the previous question about China and the reference to “the negative externalities of production” offered a steer which many candidates followed, helping them apply their answers.

The highest-scoring answers were based on a clear **knowledge and understanding** of market failure and of indirect taxation which was then **applied** through reference to one or more specific policy or to a diagrammatic analysis of the imposition of an indirect tax. **Analysis** explained how the indirect tax raised price and reduced the quantity demanded and supplied (achieving Level 3 Band 1) and then went on to explain how the reduction in over-consumption or over-production worked to reduce welfare loss and to correct market failure. **Evaluation** was demonstrated in comment on such issues as the relevance of Price Elasticity of Demand, the difficulty of setting tax at the correct level, and the possibility of hypothecating tax revenues to projects working to reduce market failure. A comparison of indirect taxation with other policies also gained marks for evaluation. However, simple explanation of alternative policies without comparison of their effectiveness with that of indirect taxation added no marks, as this did not answer the question.

As in previous examinations, a large number of candidates scored Level 3 Band 1 (9 or 10 marks) by using supply and demand analysis to explain how indirect tax reduces the quantity supplied and demanded, but then moved immediately to discuss the pros and cons of indirect taxation (thus not gaining Level 3 Band 2 or Level 4) without explaining how the reduction in quantity corrects the market failure. Candidates who showed awareness of the problems of overconsumption/production were better able effectively to analyse the solution provided. Once candidates have given this explanation and passed through this threshold, many proceed to gain full marks for assured answers based on strong analysis and developed evaluation. When approaching the essay, it is important for candidates to answer the specific question posed in the paper. This can be helped by careful planning, including the

choice of the appropriate analytical tools. Teachers might encourage candidates to practice developing their skills of explaining market failure in general and in particular, as well practising following through explanations of how particular policies function in particular markets.

Advice to candidates:

- Present key definitions and formulae precisely, preferably from an OCR-approved source. Far from limiting you, clear definitions offer a guide for clear analysis.
- Practice explaining **how** remedies for market failure actually operate – analysis is all about explaining transmission mechanisms.
- Be prepared to explain how forms of government intervention referred to on the specification influence the market forces of demand and/or supply.
- With the help of teachers, practice drawing and explaining diagrams of the key concepts you have studied.
- Focus carefully on the question so that you can plan and then answer the question appropriately.
- If running on into the additional answer space, please alert the examiner by drawing their attention to this in some way.

F582 The National and International Economy

General Comments

The vast majority of candidates answered all of the questions set and there did not appear to be any timing issues. There were some excellent scripts and whilst the overall quality did vary, there were very few really weak scripts.

Most candidates wrote well constructed sentences and a pleasing proportion wrote at sufficient length, taking into account the command words. The two questions where a small number of candidates wasted some time and effort were Q5b and Q6. In the case of Q5b some candidates wrote about why Turkey might not experience rapid economic growth in the future. In the case of Q6 some candidates described the influences on consumer expenditure although they were only required to name them.

Many candidates showed a very good understanding of aggregate demand and aggregate supply analysis and an ability to apply it in answering a number of the questions. Some good, well labelled and accurate aggregate demand and aggregate supply diagrams were included in answers not only to Q8b but also to Q4 and Q5b.

A pleasing proportion of candidates sought both to analyse and to evaluate in the two comment questions. There was also some good interpretation and use of the case study material. A number of candidates, however as in previous sessions asserted points rather than explained them. When answering questions which require them to explain, analyse, comment or discuss, candidates should always keep in mind the word 'why'. It is important that candidates provide links between cause and effect and a sequence of events. In terms of questions which require evaluation, strong analytical links give more opportunity for evaluation and support that evaluation. Including terms such as it depends on the size, there may be side effects and there may be a time delay, do not constitute evaluation unless supported by underpinning analysis which clearly brings out why, for example, there may be a time delay and/or the significance of such a time delay.

Previous reports have emphasised the importance of candidates avoiding confusion between terms. On this paper a number of candidates confused the current account position with the budget position. A disappointingly high number also revealed confusion about the meaning of the term 'productivity'. This confusion has appeared on answers to questions on previous papers. On this paper it was most evident in answers to Q5b and Q8b where candidates wrote about increases in productivity when they clearly meant increases in production.

Comments on Individual Questions

Question No.1(a)

This was a straightforward, introductory question. The vast majority of candidates were able to identify three components of aggregate demand. A small number of candidates, for some reason, identified factors influencing demand for a particular product such as the price of substitutes, taste and advertising.

Question No.1(b)

Candidates coped well with this question with the majority describing equilibrium in terms of aggregate demand equalling aggregate supply. There were few micro answers which was pleasing.

Question No.1(c)

A small proportion of candidates explained how fiscal and supply-side policy measures could cause equilibrium in the macro-economy to change. A number of candidates identified inflation as a monetary policy measure. In the case of those who correctly focused on monetary policy measures, most selected changes in the rate of interest and changes in the money supply. Some of these candidates explained how the monetary policy measures could change the equilibrium in the macro-economy by affecting aggregate demand and aggregate supply. Other candidates explained how the measures would influence real GDP and/or the price level.

Question No.2

The three main differences identified were MIST countries having, on average, a lower inflation rate than BRIC countries, the MIST countries having a greater range of inflation rates than BRIC countries and a MIST country having the highest inflation rate. A small proportion of candidates did not pick up on the words 'in terms of inflation' and identified differences in unemployment rates.

Question No.3

There were some good answers to this question. These provided clear analysis based on the information in Fig.1 and some interesting evaluative points. There were some particularly strong answers which explored why caution had to be exercised in interpreting the data as the countries could have used different methods to measure inflation and unemployment. There were also some good answers which commented on how having a lower inflation rate than other countries does not guarantee a lower unemployment rate. Some candidates covered one or two evaluative points in depth whilst others covered three evaluative points more briefly. A number of candidates mistakenly sought to examine whether the countries shown had an unemployment rate that was lower than their inflation rate. Some also explained how the unemployment rate might affect the inflation rate rather than how the inflation rate might affect the unemployment rate. This was somewhat surprising as in answers to previous questions about the effects of inflation candidates have provided good analysis on how the rate of inflation can influence international competitiveness, output and employment.

Question No.4

Again there were some strong answers to this question with good analysis of how an increase in saving may reduce inflation. In these answers this was followed by pertinent evaluation including of how, for example, saving is only one of the three leakages from the circular flow and how it is unlikely to reduce cost-push inflation. There were, however, some confused statements including the misconception that an increase in saving would reduce disposable income rather than reducing the amount of disposable income available to spend. The responses to this question also included some unsupported statements including that an increase in saving will reduce aggregate demand without explaining why.

Question No.5(a)

The main reasons that candidates sought to explain were higher living standards, lower unemployment and an increase in tax revenue. Most candidates were able to identify reasons but not all explained why economic growth could, for instance, increase living standards. A small proportion misinterpreted this question and explained how economic growth could be achieved.

Question No.5(b)

This question was particularly well answered. Most candidates focused on the rise in population and the small proportion of women currently in the workforce. Good use was made of aggregate demand and aggregate supply analysis in providing the links between influences and rapid economic growth in the future. A number of candidates, however, wasted some time and effort in providing evaluation of why the influences might not result in rapid economic growth. What was more disappointing was the sexism shown in some of the comments relating to a small proportion of women currently in the workforce. Some candidates wrote that having only a small proportion of women in the workforce would mean that the quality of the workforce would be high. There was also some confusion shown in thinking that only a small proportion of the women being in the workforce meant that there was a high female unemployment rate.

Question No.6

The majority of candidates identified three relevant influences on consumer expenditure with the most frequently mentioned ones being income, the rate of interest and wealth. A small number of candidates identified influences on the demand for a particular product.

Question No.7

There was a mixed performance on this question. Some candidates identified two relevant pieces of evidence from the data whilst others identified one piece of evidence and mentioned the effect this would have on the size of the multiplier in Turkey. A number of candidates seemed unsure of the nature of the multiplier effect.

Question No.8(a)

It was pleasing that many candidates did accurately calculate Turkey's 2011 current account position. Some candidates, however, only got part way to the answer by calculating Turkey's GDP. A small number of candidates did not attempt the question.

Question No.8(b)

Candidates do not always perform well on questions on international trade but the general standard on this question was good. The main approach adopted by most candidates was to focus on an increase in net exports causing the current account of the balance of payments to move from a deficit to a surplus. They then used aggregate demand and aggregate supply analysis to examine the effects on macroeconomic performance. Evaluation tended to focus on the significance of the initial level of economic activity, the cause of any unemployment and the possible short term nature of the surplus due to the likely impact on the exchange rate. The depth of the evaluation provided varied. The strongest answers came to a supported conclusion which weighed up the most likely impact on the macro-economy.

A number of candidates provided unsupported statements. This was particularly true in terms of the significance of the size of the change in the current account position. Some candidates wrote that the outcome would depend on the size of the change without explaining why. For instance, a small change is more likely to be offset by another influence on aggregate demand and a small change may not cause aggregate demand to rise sufficiently to encourage domestic firms to take on more workers.

Some candidates, having analysed how a change in the current account position may influence the macro-economy, went on to discuss how this impact would depend on the cause of the change. This was a valid and interesting approach. Other candidates, however, stated at the start of their answer that the effect of a change in the current account position would depend on its cause but did not explain why. A number of these candidates went on to answer a different

question. For example, some candidates stated that it could be caused by an alteration in the rate of interest or an improvement in education and then analysed and evaluated the effects of a change in the rate of interest or an improvement in education.

A disappointing number of candidates wrote about whether an economy will always benefit from the budget position moving from a deficit to a surplus.

F583 Economics of Work and Leisure

General Comments

This was the only sitting of the F583 module in 2014 and as a result over 3250 candidates sat this summer's paper.

The overall impression was of an encouraging percentage of good performances especially on the essay questions. A significant number of candidates, however, were unable to apply depth and detail in their analysis of poverty in Q4(a) and as a result struggled to achieve the higher levels of analysis and evaluation in both parts of Q4. A distinction was often made between absolute and relative poverty but then neglected as part of the analysis of the causes. In contrast, the quality of diagrams produced for Q2 and Q3 was good and was often complemented by accurate and relevant analysis. There was a strong feeling that candidates understood the significance of the diagrams they produced.

Most candidates responded well to the stimulus material and showed an ability to explain, analyse and evaluate at a good level. It was encouraging to see more candidates making a strong effort to relate the material in the case study to their answers – especially when dealing with the question on contestability. It was also encouraging to see the numeracy based question handled with much greater confidence.

Contestability remains a problem for a number of candidates. There is often confusion with the concepts of perfect competition and competition. Candidates who performed well on this question focussed on areas such as different barriers to entry and exit which might exist, sunk costs and the way in which incumbent firms are influenced by the threat from potential entrants alluded to in Fig. 3.

One general observation from the examining team was the tendency not to explain in detail the point they were trying to make. Candidates should always explain why their reasons are relevant and not leave them implicit. Analysis must be relevant and explicit.

Comments on Individual Questions

Section A.

Question No.

- 1a** A very pleasing number of candidates were able to calculate the appropriate percentages but some lost marks by failing to make a comparison. There remains a small minority of candidates who simply choose not to answer such a numeracy based question.
- 1b** A significant number of candidates seemed unable to cope with the straightforward demands of this question. Marks were lost by candidates who gave vague descriptions of their chosen economy of scale. There are still candidates who fail to distinguish between costs and average costs. On the other hand good candidates were able to explain the nature of the economy of scale and how this resulted in a fall in long run average costs.

- 1c (i)** This was a question which asked the candidates to put the concept of unit labour costs into the context of a cinema. The inability of many candidates to properly define unit labour costs led on to problems when putting theory into practice. A number of candidates simply ignored the invitation to put the concept into context. There were a significant number of low scores as a result.
- 1c (ii)** Despite the problems caused by the previous question this was actually well answered with many candidates providing good two sided analysis of the implications. Candidates and centres are reminded that the evaluation mark can only be awarded when both sides of such a question have been analysed. As a result several candidates were awarded two marks or below.
- 1d** Most candidates approached the question by considering the nature of a contestable market. Unfortunately many then ignored this and wrote about market structures with emphasis on the number of firms and, in many cases, oligopoly. Most candidates found it easier to argue why the market might not be contestable but there were some very good arguments put forward to suggest the market might be contestable. Again evaluation marks could not be awarded without analysis marks on both sides.

Section B.

- 2a.** This choice of essay was selected by over 20% of candidates. It was encouraging to see good diagrams which went on to be well explained. Many candidates were able to explain why a firm would employ at the level point where the marginal cost of labour was equal to the marginal revenue product of labour. Candidates were less likely to explain why the marginal cost of labour curve was above the average cost of labour curve. Candidates were able to analyse the impact on both wages and the quantity of labour employed.
- 2b.** There was good analysis of both government intervention and other types of intervention. A large number of candidates analysed the impact of a National Minimum Wage and better candidates were able to evaluate the relative value of this as a form of intervention. Other forms of intervention were often considered with a small percentage focussing on the significance of the fact that the government itself is often a monopsonist employer. The impact of Trades Unions was used as an example of both government and non-government intervention and credited when appropriately analysed.
- 3a** This choice of essay was selected by over 20% of candidates. Many candidates were able to explain the relationship between MRP and the quantity of labour employed however there was often a lack of focus on the fact that the question asked for a consideration of changes in MRP. Better candidates analysed how changes in both MPP and changes in the price of the product produced would shift the MRP curve and as a result impact on the quantity of labour employed.
- 3b** Many candidates were able to explain the impact of various supply and demand side factors on how wages are determined. However the question asked for an analysis of wage differentials and the better candidates focussed on this aspect and were duly rewarded. Supply side factors, such as elasticity of the supply of labour, were often much more relevant in their application whilst there was less focus on wage differentials on the demand side of the question.

- 4a** This choice of essay was selected by over 50% of candidates. Candidates were often able to produce a large number of assertions about the causes of poverty but were unwilling to provide detailed analysis on why these factors caused poverty. Many candidates commenced their answers by distinguishing between absolute and relative poverty but were unable to apply this distinction to the causes of poverty identified. This combination often failed to produce a good level of analysis.
- 4b** This part of the question was answered in a much more detailed fashion with candidates able to consider and evaluate reforms to both the tax and benefit systems and also a wide variety of other policies which might be used to solve the problem of poverty. As a result there were some very encouraging answers. There was a much greater willingness to include the concepts of absolute and relative poverty in any analysis.

F584 Transport Economics

General Comments

There was a wide range in the standard of the examination scripts produced by candidates with many scripts showing clear understanding and accurate microeconomic applied to transport. The main reasons for poor performance amongst the weaker scripts were a reliance on description, insufficient focus on the question set (sometimes with good analytical understanding) and a lack of precision particularly on some of the early data response questions. Once again teachers of this unit are to be congratulated for generating enthusiasm amongst their candidates, resulting in a variety of appropriate approaches which was clearly evident from reading the examination scripts.

Comments on individual questions

Section A

1(a) (i) It was surprising how many candidates did not state a decade and instead gave a year and therefore could not be credited with a mark. The majority who stated a decade were correct.

1(a) (ii) The evidence from this question is that this topic is not a part of the specification that candidates understand well. A large number of candidates gave an example of a private benefit to motorists. Candidates who clearly stated how a third party could gain, e.g. local businesses benefitting from increased trade, were rewarded with full marks.

1(b) (i) A lack of precision was the main reason many candidates did not gain credit on this question. Many gave responses which were too vague and did not clearly state that road schemes gave a higher NPV or net social benefit than national projects and instead made comments that benefits were higher that were too simple.

1(b) (ii) Generally this question was answered well with the majority of candidates able to provide examples of two problems with CBA. The main differentiation on the question was therefore in the explanation of the problem which was often too vague e.g. 'it results in the wrong decision'. In addition there was usual confusion between CBA and COBA with candidates explaining problems of the latter.

1(b) (iii) A substantial majority of candidates gained two marks for this question by contrasting a private sector objective with a public sector objective. The third mark was then available for some development of either objective but unfortunately most candidates did not achieve this.

1(c) On the whole, this part of the question was well answered with the majority of candidates able to either define or give an example of hypothecation. Both approaches were acceptable.

1 (d) Overall this question was answered well. Only a small minority of candidates were unable to give appropriate analysis on how 'road user charging' could correct market failure. These responses gained no credit, even if they understood potential problems of the policy. When appropriate analysis was present, in terms of internalising externalities to correct for overconsumption, there was some excellent explanation of why the policy might not work. Consequently the majority of marks were 0, 4 or 5.

1 (e) This question differentiated well. Some candidates did little but repeat material from the case study and others got confused between public and private sector objectives. The better responses realised they could apply their understanding of privatisation and were able to develop why increased competition or desire for profits would raise levels of productive/allocative and dynamic efficiency before analysing why private sector provision may

not provide benefits. The most common route into this evaluation was to develop the possible loss of natural monopoly or economies of scale from smaller firms in the private sector. Alternatively, some good responses gained credit for the fact that increased competition may simply lead to service duplication and negative externalities and, therefore, allocative inefficiency and the resulting waste of scarce resources. Many very good evaluative judgements were offered, often focusing on the fact that the impact would depend on the level of public sector regulation.

Section B

Substantial numbers chose each essay with Q4 being the most popular and Q3 the least; parts (a) on each essay were very similar in the demands placed on candidates from different sections of the specifications.

2(a) The very best answers to this part of the question were able to analyse why allocative and productive inefficiency result in the short run in monopolistic competition, mainly with reference to a diagram. In addition there were many good explanations of how the pursuit of profit maximisation resulted in underproduction and excess capacity. There were also some excellent explanations of why dynamic efficiency would result from short run abnormal profits. Weaker answers either confused monopolistic competition with monopoly or perfect competition. This approach could gain some credit if there was some understanding of the different types of economic efficiency.

(b) A few candidates misinterpreted what was meant by a fall in concentration. Some other candidates suffered by offering static analysis of comparing monopoly with a more competitive market rather than a dynamic discussion of increasing competition. However there were many excellent theoretical responses analysing the impact of increasing competition on all types of efficiency and offering good judgements such as 'it depends on the level of fixed costs' or 'it is not the level of competition that determines economic efficiency but the level of contestability'. Such responses also displayed some excellent application to transport markets.

3 (a) The majority of candidates had a clear understanding of negative externalities in transport markets. The differentiation between candidates was in how they explained the impact on third parties in terms of reducing benefits, e.g. house prices of local residents falling due to noise from flight paths, or increased costs e.g. NHS costs from dealing with respiratory problems resulting from pollutants due to transport use. Credit was also given to analysis of how negative externalities resulted in market failure. Good use of diagrams was often made, but it was important that candidates clearly developed their analysis of why market failure arose in terms of explaining overconsumption and allocative inefficiency.

(b) This question produced a varied standard of responses. A large minority of candidates were unable to offer any analysis of why or how forecasting was/ was not effective in meeting the future needs and requirements of transport markets. Better responses showed some analysis of either one or both sides e.g. in terms of linking GDP/population data to transport use through derived demand or how forecasting helps government make policy decisions to achieve best use of scarce resources or how much of the data used is volatile and, therefore, unpredictable resulting in inaccurate forecasts. Often discussions were unbalanced and gained a maximum of 12 marks. When analysis had greater clarity, clearly explaining how or why forecasts were produced and why they may be unreliable or the consequences of inaccurate forecasts, a balanced discussion resulted and marks for judgements were available. Some excellent responses managed this; the most common judgement being 'that although there were inaccuracies with forecasting its best to have some data rather than none to base allocative decisions'.

4 (a) There were many excellent responses to this question with some impressive knowledge and application to the air passenger transport market. Most candidates were able to gain Level 3 and 9-15 marks. The main reason for candidates not achieving this was a reliance on description of barriers to entry rather than analysing the consequence of each barrier. The main differentiation between candidates was therefore between the different level 3 bands i.e. on the clarity and precision by which candidates analysed how specific barriers resulted in new firms being deterred from entry into the air transport market.

(b) Candidates now seem to be adept at analysing the impact of indirect taxes on equilibrium and how they could be used effectively to correct market failure. Candidates often made very effective use of diagrams. Some responses simply made use of the negative externality diagram, rather than clearly showing how an indirect tax would shift the supply curve to the left. Good answers to this part of the question were able to clearly make links to a more sustainable allocation of resources e.g. in terms of reducing consumption of non-renewable resources such as fuel. In terms of evaluation, the most popular route taken by candidates was to develop the idea of air transport having inelastic demand and the relevance of the size of the tax. As stated in previous reports, it is important to stress to candidates the need to clearly develop such evaluative points in the context of the question set. A basic list of problems of indirect taxation which are not developed and not focused clearly on the question set will not be rewarded analysis marks. However there were some excellent responses providing a balanced discussion, followed by appropriate judgements mainly linked to the need to use other policies in tandem with indirect taxation or the need for international co-operation. Some responses gave impressive judgements in terms of differentiation between different types of indirect taxation e.g. how a tax on aviation fuel would be better in achieving a sustainable outcome.

Overall, candidates would be advised to take on board the following advice:

- On the shorter earlier parts to question 1, answer the question directly, avoiding writing more than is necessary
- On the discuss and comment questions of question 1 and on both parts of the essay get straight into your answer and avoid simply setting the scene i.e. no more than a short paragraph is required to explain what the market failure is if the question is about correcting the market failure.
- When making a choice in Section B consider both parts of the question in order to maximise the overall mark; many candidates gave excellent answers to 3a but were then unable to analyse the effectiveness of forecasting.
- When analysing both sides of an issue, particularly on part b of Section B, avoid making simple statements for and against a point. Develop each of the points using the appropriate tools of economic analysis.

F585 The Global Economy

General comments

This was the first time that this unit was available only in the June sitting. There was some evidence that the spread of marks was greater than in previous June sittings.

Lower tariff questions continue to differentiate well between candidates who have good knowledge of the specification content, those whose knowledge is imprecise or inaccurate and those who answer the question set. So in Question 1 (a) (i) weaker candidates did not gain full credit because they did not fully understand what the surveillance role of the IMF involved. In Question 2 (a), knowledge of government intervention to prevent a fixed exchange rate devaluing was either absent or not linked to the demand and supply of the currency. Similarly in Question 1 (a) (ii), there was imprecise understanding of the term 'balanced budget fiscal expansion' despite this being the focus of the IMF's recommendation for the UK economy in Extract 1. Knowledge of transaction costs, price transparency and exchange rate risks was not always evident in responses to Question 2 (b). In Question 1 (b) some candidates did not focus on the **case for** fiscal expansion with a large negative output gap, despite being able to show how fiscal expansion might reduce a negative output gap.

It remains the case that candidates who perform well in Question 1 (c), Question 2 (c) and Question 3 are those who provide analysis of the key issue before providing comment or evaluation. For example:

- in Question 1 (c) strong candidates analysed how fiscal expansion conflicts with reducing the government's budget deficit;
- in Question 2 (c) strong candidates analysed how both exchange rate and internal devaluation reduced external imbalances;
- in Question 3 strong candidates analysed how international trade might raise economic development in resource rich economies.

Such analysis makes use of economic concepts to explain the link between one thing and another. It does not simply assert, but provides a reasoned chain of cause and consequence. Evaluation cannot be credited unless it is based on sound economic analysis and in all three questions must show some development to be awarded the higher marks in Level 4 of the mark scheme.

As always, there was a wide range of responses. Examiners were impressed with the quality at the top end. Such candidates showed excellent knowledge and understanding of the issues raised by the stimulus material and were able to develop arguments in depth, showing a deep understanding of contemporary debates in economics. It was evident that these candidates were easily capable of thinking as economists and marshalled concepts well to make sense of a wide range of contexts in the subject.

Comments on individual questions

Question 1 (a) (i)

This question distinguished well between candidates who understood the surveillance role of the IMF and its other roles. The most common correct responses to this question cited lending and technical assistance as roles other than surveillance. Weaker candidates did not fully understand the nature of the surveillance role of the IMF and stated, incorrectly, policy advice and conducting annual assessments of economic performance. There was also confusion about the roles of the IMF and the World Bank, with weaker candidates citing aid to developing countries as a responsibility of the IMF. Some of the core roles and responsibilities of the IMF (promoting international monetary co-operation, facilitating the expansion and balanced growth of international trade, providing exchange rate stability and assisting in setting up multilateral systems of payments) were rarely offered by candidates.

Question 1 (a) (ii)

Candidates who were able to show knowledge and understanding of fiscal expansion which did not adversely impact on the balance between government expenditure and tax receipts scored well on this question. It was not necessary for candidates to explain **how** balanced budget fiscal expansion can arise. A simple statement that increases in government spending matched by equal increases in taxation could increase economic activity was sufficient for both marks to be awarded. Weaker candidates thought that it was necessary for government expenditure to equal tax receipts and for a budget deficit to be eliminated.

Question 1 (b)

This question discriminated well between candidates who had an awareness of the nature of a negative output gap and expansionary fiscal policy and those who were able to analyse the case for expansionary fiscal policy when the output gap is large. Candidates were rewarded for their knowledge and understanding of both terms in the question. These were marks which most candidates were able to achieve. The case for fiscal expansion at a time of a large negative output gap was less well understood. Candidates who were able to identify that a large negative output gap would be associated with unemployment, a waste of resources, little inflationary pressure or a high level of spare capacity in the economy were rewarded with application marks. Analysis of the way in which fiscal expansion might remedy these issues was not always fully developed in terms of the links between higher government expenditure and / or lower taxation, aggregate demand and real GDP or employment. Weaker candidates tended to state or assert these linkages rather than explain them.

Question 1 (c)

Knowledge and understanding of both the current UK Government's Deficit Reduction Plan and fiscal expansion was generally good. Candidates who were able to show the conflict between fiscal expansion and the Deficit Reduction Plan gained marks in Level 3 of the mark scheme. This was most commonly achieved by showing how fiscal expansion, by raising government expenditure and lowering taxation, is likely to increase the budget deficit in the short run. An alternative analytical response was to show the conflicting impact on Aggregate Demand. Evaluative comment was evident in responses which explained how fiscal expansion might not raise the UK budget deficit, either through balanced budget fiscal expansion or through the impact of higher economic activity on government expenditure or taxation receipts. Developed commentary was characterised by an explanation of the different multipliers arising from higher government expenditure and higher taxation or of the impact of higher economic activity on particular forms of government expenditure and taxation receipts. Full marks were available to candidates who either made two developed comments or one comment which was well developed. In contrast, weaker responses tended to assert rather than explain the relationships

between fiscal expansion and the budget deficit. The weakest responses seen confused the budget deficit with a deficit on the current account of the balance of payments such that few, if any, marks were awarded.

Question 2 (a)

There was a wide range of ways offered to maintain a fixed exchange rate when it came under pressure. These included the anticipated policy measures of raising interest rates and direct intervention in FOREX markets, but credit was also given to measures to raise productivity, lower unit labour costs, improve the quality of exports or impose exchange controls. Any of these measures could be awarded up to two identification marks. Additional marks for each method were awarded for direct reference to the impact on either the demand or supply of the currency. Strong responses clearly identified and explained two methods, for example higher interest rates raising the demand for the currency through attracting hot money flows. Weaker responses simply identified a relevant policy measure without linking this to the demand or supply of the currency. The weakest responses wrote about ways in which a fixed exchange rate could be devalued either by lowering interest rates or by selling the currency on the FOREX markets. Such responses appeared not to understand the question set.

Question 2 (b)

Knowledge and understanding of the benefits of adoption of the euro was variable. Some candidates clearly identified lower transaction costs, greater price transparency and the elimination of exchange rate risk on trade with other Eurozone members. They were then able to explain the nature of each benefit and how it might impact on an economy adopting the euro. Less convincing answers started with the end result, higher levels of trade for example, but were unable to establish a reason why this would arise from adopting the euro. Such answers tended to score less well. The weakest answers confused the benefits of adoption of the euro with those of membership of the European Union. The best candidates clearly established a benefit (lower transaction costs), explained its nature (no need to convert currency when trading with other eurozone economies) and established a consequence for the economy (reduced cost of trade resulting in a rightward shift of AS).

Question 2 (c)

For some candidates, the lack of supporting analysis of how either exchange rate or internal devaluation can correct external imbalances resulted in marks in Level 2 of the mark scheme. Better responses were able to show how export and import prices and volumes would be affected by exchange rate devaluation. This analysis was further developed by comparison of outcomes in Iceland and Latvia and by the weaknesses of internal devaluation. Stronger candidates were then able to comment on whether exchange rate devaluation was a better approach by considering issues related to the price elasticity of demand for imports and exports and the root causes of external imbalances. Weaker candidates tended to assert rather than analyse, such that commentary was unsupported.

Question 3

An analysis of the link between international trade and economic development was the key to success in this question. Without such analysis responses were, at best, one sided in analysing the issues or, at worst, general and unsupported by any economic concepts. The latter achieved marks in Level 2 of the mark scheme whilst the former were awarded Level 3 marks. Analysis of the link between international trade and economic development for resource rich economies was most commonly shown through the impact on Aggregate Demand. Strong responses showed how an increase in exports would lead to higher AD and therefore higher real GDP. This then allowed a clear link to economic development in terms of GDP per capita, higher levels of employment and the potential for increased tax revenue to be used to increase access to

education and health care. Candidates who adopted this approach successfully used their understanding of economic development and its measurement to establish that international trade could potentially raise economic wellbeing in resource rich economies. Such analysis was a pre-requisite for access to Level 4 of the mark scheme. Without it, candidates were awarded marks in Level 2 or Level 3 depending on the extent to which there was analysis in the rest of the response. There were some responses which made use of AD / AS analysis but did not make the link to economic development. Such responses tended to simply explain how international trade could lead to economic growth, which was not the focus of the question. The best evaluation was developed beyond correct statements about why international trade might not promote economic development in resource rich economies. So, for example, many candidates pointed out that economic development might not follow if commodity prices were volatile or if, in the long run, they declined relative to other traded goods (the Prebisch-Singer hypothesis). This was basic discussion. Developed discussion gave reasons why commodity prices might be volatile (inelastic PED and PES combined with demand or supply shocks) or why commodity prices might decline in the long term (differences in YED between primary and secondary sector output). Similarly, statements about the capital intensity of resource extraction industries were awarded Band 1 marks whereas developed discussion of the implication of this for economic development were awarded marks in Band 2. In general terms, Band 2 evaluation is more about the depth of discussion than about how many points of evaluation candidates can cite in their responses. Band 2 evaluation is also a prerequisite for the award of marks in Band 3 of the mark scheme. Here examiners are looking for significant judgements which follow on from an analysis of both sides of the argument. Simple repetition of a prior argument is not sufficient. Stronger candidates were able to demonstrate good judgements by arguing that sectoral change or resource licensing / taxation, for example, may allow resource rich economies to avoid the problems of resource depletion and create more sustainable development.

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