



ECONOMICS

9772/02

Paper 2 Essays

May/June 2016

MARK SCHEME

Maximum Mark: 75

Published

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Marking criteria for Paper 2

For this paper, marks should be awarded in two categories. The first covers the knowledge and understanding of relevant economics, how this is applied and how the information/issues are analysed (Theory and Analysis) and the second covers the candidate's evaluation of the issues involved (Evaluation). Examiners should look to mark the essay holistically and decide into which relevant Levels the answer lies. The Levels will not necessarily be the same for the two categories.

Theory and Analysis

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| Level 4 (13–17 marks) Mid mark 15 | An excellent answer that shows accurate and comprehensive application of relevant theory. There will be in-depth and coherent analysis. At the top end there will be signs of real insight and/or originality, not normally expected to be seen at this level. |
| Level 3 (9–12 marks) Mid mark 11 | An answer that logically addresses the issues involved and generally shows a correct application of the relevant theory. An attempt is made to analyse and there is some depth or coherence but not necessarily both. |
| Level 2 (5–8 marks) Mid mark 7 | Some correct application of relevant theory will be shown but there may well be inaccuracies contained within the answer. An appreciation of the need to analyse may be demonstrated, but not much more than this. The answer is likely to lack any real coherence. |
| Level 1 (1–4 marks) Mid mark 3 | The answer contains something of relevance to the set question. However, theory may be misunderstood, or incorrectly applied. At this level, any analysis shown will be extremely superficial. |
| Level 0 (0 marks) | Nothing of any relevance to the set question is shown within the answer. |

Evaluation

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| Level 3 (6–8 marks) Mid mark 7 | There is in-depth, coherent, comprehensive and well-balanced evaluation. At the top end there will be signs of real insight and/or originality, not normally expected to be seen at this level. |
| Level 2 (3–5 marks) Mid mark 4 | There is a definite attempt to consider various points of view or outcomes for different economic agents or distinction between short-run and long-run consequences etc. but the coverage of these is less than comprehensive. |
| Level 1 (1–2 marks) Mid mark 2 | There is some attempt at evaluation but issues are more likely to be stated than examined. |
| Level 0 (0 marks) | There is no evidence of any evaluation whatsoever. |

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Section A

1 Evaluate whether large firms are necessarily more efficient than small firms. [25]

Candidates should be able to differentiate between large and small firms, with particular reference to market share and the ability to set price. They should also be clear in outlining what is meant by efficiency, perhaps discriminating between static and dynamic efficiency, but being clear to distinguish between productive and allocative efficiency at the very least. Good candidates might include other types of efficiency, notably technical, X-efficiency and Pareto efficiency. Candidates need to capture the ambiguity inherent in the question: in some circumstances large firms are undoubtedly more efficient, but that in many other circumstances large, profit-maximising, firms are less efficient than small firms. In order to get into Level 4, candidates need to be clear that there is no definitive answer to the question

Answers may include:

Knowledge and understanding of ways in which large and small firms can be differentiated. They should argue that for profit-maximising firms, assuming the same cost curves, large firms with price setting power will invariably be less efficient, in producing a lower output at a higher price. There will be an explanation of the equilibrium position in terms of productive and allocative efficiency. Equally, the idea of a large firm benefiting from economies of scale and actually producing more efficiently should be considered. The best candidates may focus on natural monopolies and highlight the difference between being efficient in absolute and relative terms.

Application to real life, perhaps by looking at a range of different firms, perhaps focusing on particular industries, such as utilities or the technology sector, which are characterised by large firms.

Analysis of various different equilibrium positions

Examples:

- Comparison of large firms and small firms facing the same cost curves.
- Consideration of large firms benefiting from economies of scale, possibly with reference to natural monopolies.
- An assessment of different forms of efficiency – static v dynamic, with focus on product quality, Schumpeter's notion of 'creative destruction'.
- How the pursuit of alternative objectives – sales maximisation, revenue maximisation – will have implications for efficiency.
- The possibility that large firms can be regulated effectively and thus efficiency could be greater as a consequence, perhaps with reference to RPI-X pricing or quality standards.

The best answers need to analyse the extent to which it is 'necessarily' the case that large firms are more efficient than small firms.

Evaluation of the issues involved

Examples:

- An assessment of the extent to which it is realistic for large and small firms to have identical cost curves.
- Any assessment of the extent to which firms may deviate from the price-output outcome suggested by profit maximisation and the implications of this for efficiency.
- Consideration of the extent to which large firms have contributed to significant gains in dynamic efficiency, perhaps with reference to network effects.
- An assessment of whether absolute or relative efficiency is more important.
- Evaluation of the extent to which natural monopolies exist in an economy

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Theory and analysis

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| Level 4 (13–17 marks) Mid mark 15 | <p>There is a clear understanding of the difference between large and small firms. There are likely to be two relevant diagrams, one illustrating the view that large firms are less efficient, the other the opposite position.</p> <p>At this level there may also be awareness of the fact that the extent to which the firm is efficient may depend upon its objectives. Candidates are also likely to look at specific instances of when large firms are undeniably more efficient than small firms, such as in the utilities sector or with reference to natural monopolies.</p> |
| Level 3 (9–12 marks) Mid mark 11 | <p>Candidates are likely to be able to explain that whether large firms are more efficient or not depends upon circumstance. They will draw diagrams looking at these alternatives, but at the lower end of the level there may be incomplete analysis of the implications of this. There will be awareness of different types of efficiency but at the lower end this will not be very sophisticated.</p> |
| Level 2 (5–8 marks) Mid mark 7 | <p>There is appreciation of the ambiguity in the question but there are errors or omissions in the candidate's answer. The candidate is likely to give a simplistic account of whether or not large firms are more efficient or not without any depth. The understanding of efficiency is likely to be limited.</p> |
| Level 1 (1–4 marks) Mid mark 3 | <p>Explanations and diagrams are either missing or inaccurate. The answer is likely to fail to address the set question but instead be a poor attempt to re-hash a textbook explanation of why monopolies are always less efficient than perfectly competitive firms.</p> |

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Evaluation

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| <p>Level 3 (6–8 marks) Mid mark 7</p> | <p>A good answer is likely to discuss issues such as:</p> <ul style="list-style-type: none"> • The extent to which the assumption of identical cost curves is realistic. • Evaluation of whether the profit maximisation condition is realistic and the impact of alternative objectives on the efficiency of large/small firms. • Evaluation of whether static or dynamic efficiency is more important. • An assessment of whether or not markets are characterised by ‘creative destruction’. • Evaluation of the extent to which greater efficiency of large firms is a function of their own choice or the regulatory environment in which they operate. • The possibility of ‘counter-cases’ – ie large firms in very competitive industries, small firms with significant monopoly power. <p>There will be a conclusion drawn at the end to explain the candidate’s overall view – even if this is that there is no clear-cut answer. The issue of ‘necessarily’ will be explicitly addressed.</p> |
| <p>Level 2 (3–5 marks) Mid mark 4</p> | <p>One of the above will be discussed in detail or a couple of points touched on, but only in a relatively superficial way.</p> |
| <p>Level 1 (1–2 marks) Mid mark 2</p> | <p>Whilst there might be some appreciation that evaluation could be carried out and indeed there might be the odd comment that suggests an area for potential evaluation, the point is not developed.</p> <p>For example: ‘It is clear that large firms are rarely more efficient than small firms, but when they are it is largely because they are forced to be’</p> |

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2 Evaluate the case for the government providing free access for all to museums and art galleries. [25]

Candidates are likely to start by identifying the fact that access to museums and art galleries is likely to be associated with the production of positive consumption externalities. Some may argue that they are also merit goods, and thus under-consumed in the free market. Some might attempt to assess whether there are such things as merit goods. In short, this question allows good candidates scope to focus on a wide range of economic issues that are relevant to the question. Candidates should be aware that free provision of an activity will certainly increase the quantity demanded: however, there may be different interpretations of the implications of this. The best candidates will always keep in view the various benefits and costs of providing free access to museums and art galleries before reaching some sort of conclusion, however tentative, about the desirability of such a policy. In order to get into Level 4 Theory and Analysis a candidate will be expected to consider both the case for and the case against such a policy with a degree of sophistication. Further, they should evaluate it in terms of the opportunity costs, the likelihood of government failure and the distributional issues concerned. Candidates should be rewarded for valid attempts to apply economic theory in answering the question.

Answers may include:

Knowledge and understanding of why free access to art galleries and museums generates positive consumption externalities and how providing free access might, in theory, improve the efficiency of resource allocation. Candidates should be able to categorise the goods being discussed and may refer to the characteristics of 'merit goods', and differentiate between private goods and public goods. Diagrams are likely to be drawn to illustrate why there might be market failure in this market and how free access can go some way towards correcting this. There is no definitive direction that candidates will be expected to take but there needs to be focus on the specifics of the question and not just the provision of merit goods or goods with positive externalities in general.

[NB Candidates should not be penalised for interpretations of 'merit goods' that focus on the generation of positive externalities.]

Application to museum and art gallery access. Candidates should look at the possible external benefits of consuming these goods and might consider how offering free access will change the quantity of the good demanded. Good candidates might link this to cost considerations and even utilise concepts like cross price elasticity of demand in looking at gifts/refreshment sales. They might also speculate as to how much free access might increase the costs of providing access to museums and art galleries.

Analysis of how free access will affect the market for art galleries and museums. In the vast majority of cases, providing the good for nothing to the marginal consumer might throw up a range of issues.

Examples:

- How free provision might mean that the goods move from being private goods to quasi-public goods.
- How fixing the supply of access at a particular level implies a perfectly inelastic supply curve and possible over-provision of access to these buildings.
- The equity argument of free provision: in giving free access to all, it will give low income households greater access to these facilities.
- An assessment of possible positive multiplier effects if such a move increases tourism.

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Evaluation of the issues involved

Examples:

- The extent to which the impact of providing free access will have little effect on the quantity of museum and art gallery access demanded.
- Evaluation of the extent to which the opportunity cost of providing free access is prohibitively high.
- Evaluation of the likelihood of government failure, in over- or under-providing this access, and the possible distributional implications – both within different geographic areas and between alternative cultural activities, ranging from visiting stately homes to watching football matches.
- Evaluation of the degree to which offering free access achieves the objective of getting greater numbers of people to go to museums and art galleries, or whether it is little more than a subsidy of the well-to-do.
- Consideration of whether granting free access is appropriate in this case for a number of reasons: if it were an efficient market then people who derive pleasure from going to these venues should be willing to pay for them.

Theory and analysis

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| Level 4 (13–17 marks) Mid mark 15 | There should be clear understanding of the issues raised by the question: candidates should be capable of making a case that both goods generate positive consumption externalities and that this might have implications for the type of good that they are considered to be. Good candidates will be sophisticated in their analysis of the implications of free provision and consider a range of possible outcomes from providing free access. Candidates who make intelligent use of diagrams and applied examples to support/oppose the policy should be rewarded. |
| Level 3 (9–12 marks) Mid mark 11 | Candidates should be aware of the positive externalities from free access to museums and art galleries and/or their merit good nature ; and the fact that free access might allow for an improvement in economic welfare. However, development of their arguments is likely to lack real depth and/or diagrammatic accuracy. At the bottom of the level, candidates may struggle to relate economic theory to practice with anything other than superficial reference to the question. |
| Level 2 (5–8 marks) Mid mark 7 | There might be little ability to identify the social benefits of provision and/or simplistic assertions that museum/art gallery access are merit goods. At the very bottom of the level it might be implied that given the positive externalities involved, any form of government action to encourage provision is likely to improve market outcomes. |
| Level 1 (1–4 marks) Mid mark 3 | Candidates are only able to touch upon the issue of the nature of the goods, with little, if any, sense of the market failure generated. There are likely to be no relevant diagrams. |

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Evaluation

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| <p>Level 3 (6–8 marks) Mid mark 7</p> | <p>A good answer is likely to discuss issues such as:</p> <ul style="list-style-type: none"> • Evaluation of whether there is such a thing as a merit good. • The extent of free provision is likely to ensure more/less efficient outcomes within the market, • Evaluation of the extent to which free provision will substantially increase maintenance costs and whether these outweigh any potential benefits. • Evaluation that considers that people who derive pleasure from visiting museums and art galleries should pay for this. • Evaluation of the practicalities of adopting such a scheme: will it be all-year round or only on certain weekends? Will it apply to all, irrespective of their background? • Evaluation of the distributional implications of such a scheme – is it skewed in favour of urban citizens? • Evaluation of whether state funding of museums and art galleries will make the sector less independent, more risk averse and less dynamic in attracting alternative sources of funding. <p>Candidates should be able to reach some sort of view about the introduction of a free access to museums and art galleries and credit should be given for any attempt to back this up with evidence, either appropriate data or an anecdote.</p> |
| <p>Level 2 (3–5 marks) Mid mark 4</p> | <p>One of the above will be discussed in detail or a couple of points touched on, but only in a relatively superficial way. There will be little attempt to consider the question from a culture-specific perspective.</p> |
| <p>Level 1 (1–2 marks) Mid mark 2</p> | <p>Whilst there might be some appreciation that evaluation could be carried out and indeed there might be the odd comment that suggests an area for potential evaluation, the point is not developed.</p> <p>For example: 'It is clear that providing free access to museums and art galleries is certainly good. More people will be able to attend, and this is better for society as a whole'</p> |

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- 3 A national minimum wage is self-defeating: it does nothing to reduce poverty, it increases unemployment and thus damages the very group of people it is designed to help. [25]

Evaluate this statement.

Candidates should be able to define a ‘national minimum wage’ as a legally enforceable wage floor, designed to stop wages falling below a given level. They should explain that the NMW stops the labour market from clearing and keeps wages above the free market equilibrium level. The extent to which a NMW reduces poverty is debatable: it is only received by those in work and worklessness is one of the major sources of poverty. Equally, in perfectly competitive labour markets it may be the case that a NMW does increase unemployment. Furthermore, the workers it makes redundant are likely to be ‘marginal’ workers and thus those with the lowest productivity; it may well be the case that these people are left unemployed and that over time their human capital is eroded. However, this might not be the case: a minimum wage might have markedly different effects on employment levels: in an imperfectly competitive labour market it might increase employment; if it is introduced at a time of strong growth, the impact of the NMW might be offset by increased demand for goods and services and, by definition, labour. Equally, the existence of a higher NMW than the previous equilibrium wage might encourage vulnerable members of the labour force to invest more in education and training. Thus, while most candidates may be tempted to side with the opinion expressed in the quotation, the very good candidates may be more guarded in their conclusions.

Answers may include:

Knowledge and understanding of the impact of a NMW on particular labour markets –notably perfectly competitive and imperfectly competitive labour markets. Good candidates will highlight the significance of demand and supply elasticity and the degree to which the NMW is higher than the previous equilibrium wage. Candidates should be able to define poverty and isolate the effects of the NMW on poverty – good candidates will note that definitions of poverty can differ (absolute v relative, individual v households) – and the relationship between possible unemployment and the erosion of human capital, often described as ‘hysteresis’.

Application to specific labour markets. Candidate should be able to draw accurate diagrams showing how a NMW will affect perfectly competitive and imperfectly competitive labour markets. They should be able to make meaningful comment on the implications of these outcomes for poverty and the possible impact of a NMW on the incentives of the most vulnerable to maintain their stock of human capital.

Analysis of the extent to which the effects of a NMW do correspond with those highlighted in the question

Examples:

- Whether the NMW is, on balance, likely to increase or decrease unemployment.
- Whether the NMW is likely to help tackle poverty or not – or whether it is generally a payment to second income earners in a household, thus boosting the incomes of those in the sixth and seventh decile of all income earners.
- The impact of a NMW on human capital within an economy.

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Evaluation of the issues involved

Examples:

- The extent to which the aims of the NMW correspond to the objectives seemingly highlighted by the question – maintenance of employment levels, poverty reduction and the impact on the very group of people that it is designed to help.
- The magnitude of any minimum wage effects on unemployment, poverty, and human capital formation.
- The degree to which it is wrong to see the minimum wage alone as targeting these areas and the importance of seeing its introduction within the context of government policy towards the labour market as a whole.
- Evaluation of the effects of a NMW on any economy will receive significant credit: for example, the introduction of the NMW in the UK was associated with the NICE decade and this will have lessened any detrimental effects of the NMW.

Theory and analysis

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| Level 4 (13–17 marks) Mid mark 15 | The best candidates are likely to argue that it is difficult to draw definitive conclusions about the impact of the NMW on the factors outlined. On balance, unemployment may rise, there is likely to be little effect on poverty and the impact on the people it is designed to help will depend upon how the NMW will affect them. If the rise in unemployment deters the marginal worker from participating in the labour market then human capital will be eroded, but it also increases returns to work and this might encourage more people to invest in education and training. There will be good understanding of both perfectly competitive and monopsonistic models of wage determination when a NMW exists and the strongest candidates will consider the factors that will help determine its effect on the areas highlighted by the quotation. |
| Level 3 (9–12 marks) Mid mark 11 | Candidates must be able to explain how, in theory; a NMW will affect the factors highlighted. At the top of this level candidates should develop both theory and practice At the lower end of the mark bracket, credit should be given for recognizing the complexity of the factors which affect unemployment, poverty and human capital formation. |
| Level 2 (5–8 marks) Mid mark 7 | Candidates show limited appreciation of the impact of a NMW on unemployment There are likely to be errors and omissions in candidates' answers and little awareness of the broad range of other factors that merit consideration. At the bottom of this bracket, answers are likely to generalize rather than examine how market-specific conditions are likely to be significant in determining the effects of a NMW |
| Level 1 (1–4 marks) Mid mark 3 | Candidates can only conceive of the fact that all of the outcomes highlighted must come about, but might not develop their answers appropriately. There are likely to be few diagrams, and those that are drawn are likely to be poorly explained. |

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Evaluation

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| <p>Level 3 (6–8 marks) Mid mark 7</p> | <p>A good answer is likely to discuss issues such as:</p> <ul style="list-style-type: none"> • Whether it is appropriate to view the minimum wage in the terms implied by the question – surely the minimum wage is more about taking a ‘normative’ view about what a ‘fair’ wage is? • The extent to which the introduction of a NMW has had an adverse effect upon the indicators mentioned in the quotation. • The impossibility of holding other things equal, and the difficulty in blaming the NMW alone for rising unemployment, continued poverty and the erosion of human capital. • The possibility of there being productivity gains as a result of the NMW being introduced, offsetting the perceived fall in the level of employment in a given labour market. • The extent to which perfect or imperfectly competitive labour markets are a more apt representation of the labour market. <p>Good candidates will look at a range of factors which determine the impact of the NMW on employment levels, poverty etc. before offering some assessment of the extent to which it is the NMW which is responsible for any rise in unemployment, poverty and decline in human capital formation.</p> |
| <p>Level 2 (3–5 marks) Mid mark 4</p> | <p>One of the above will be discussed in detail or a couple of points touched on, but only in a relatively superficial way. There will be little attempt to consider the relationship between marginal productivity and a variety of other factors.</p> |
| <p>Level 1 (1–2 marks) Mid mark 2</p> | <p>Whilst there might be some appreciation that evaluation could be undertaken, the point is not developed.</p> <p>For example: ‘It is difficult to blame the NMW for a general worsening in a nation’s macroeconomic performance; economies are buffeted by many different forces.’</p> |

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Section B

- 4 With reference to more economically developed countries (MEDCs), evaluate the extent to which governments should pay more attention to reducing income inequality and worry less about the pursuit of economic growth. [25]

Candidates should make an attempt to define the key terms in the question, although there may be some flexibility of definition: 'economic growth' should probably be defined with reference to real per capita GDP, and perhaps also as an increase in an economy's productive capacity; 'inequality' is usually applied to both income and wealth. However, able candidates might refer to 'inequality of opportunity'. Candidates are likely to argue that there is less of a need for MEDC countries to pursue growth alone, given that their citizens are already likely to have a relatively high standard of living. Some candidates may argue that the objective of all economies, irrespective of their level of real per capita GDP, is to improve the standard of living of their citizens and that in actual fact, pursuit of economic growth is actually the best way of promoting this. Astute candidates might consider the use of the phrase 'more attention' in the question, arguing that there is little evidence that MEDC governments pay anything other than cursory attention to reducing income inequality.

Answers may include:

Knowledge and understanding of the relationship between how rich a country is and levels of inequality. Candidates might argue that pursuit of growth alone might see a concentration of income and wealth in the hands of a relatively small section of the populace. However, others might point out the opposite: that there may be an inverse relationship between a country's income and the level of inequality. Candidates should be capable of defining inequality, with reference to either the Lorenz curve or the Gini coefficient. It should be apparent that the pursuit of macroeconomic objectives is in effect a proxy for improving economic welfare and that on this basis alone a 'disregard' for growth is unlikely to be desirable, even in MEDCs.

Application to specific MEDCs. Candidates might see increased equality as akin to a luxury good, and perhaps refer to the fact that it makes some sense for MEDCs to look beyond the promotion of economic growth and at other objectives. There might be some applied data highlighting the relationship between how rich a country is and inequality, with particular focus on what has happened to the Gini co-efficient in an MEDC such as the UK or the US.

Analysis of the relationship between how rich a country is and the level of inequality – is there any relationship; possible comment on the extent to which 'a rising tide lifts all boats'.

Evaluation of the issues involved

Examples:

- The extent to which there is any relationship between how rich a country is and its level of inequality.
- An assessment of whether any relationship between the two is causal or merely a correlation.
- Evaluation of whether or not governments can ever afford to 'disregard' growth.
- The extent to which any government is realistically going to prioritize inequality above all other macroeconomic objectives.

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Theory and analysis

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| Level 4 (13–17 marks) Mid mark 15 | There is a clear understanding of the potential for the two objectives to conflict but also enough to suggest that this is far from inevitable. Candidates should be able to demonstrate that they are able to quantify inequality. Candidates need to make substantive analysis of MEDCs. The best candidates will look at causal relationships between level of income and inequality but also be sceptical about whether governments can ever afford to ‘disregard’ the pursuit of growth. |
| Level 3 (9–12 marks) Mid mark 11 | Candidates will be able to see some sense in which there might be a trade-off between the objectives but are not able to develop explanation of it. There will be references to inequality but causal links between inequality and income will be inaccurate or incomplete. |
| Level 2 (5–8 marks) Mid mark 7 | There is an appreciation of some sort of conflict between the two objectives but little certainty in being able to quantify either value. The candidate is likely to give a simplistic, or indeed no, account of how growth can result in inequality or vice versa. |
| Level 1 (1–4 marks) Mid mark 3 | Explanations are either missing or inaccurate. The answer is likely to fail to address the issue of whether there is ever any conflict between objectives and be imprecise in defining key terms. The answer may become generalised and at the bottom of the range use little economic terminology. |

Evaluation

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| Level 3 (6–8 marks) Mid mark 7 | <p>A good answer is likely to discuss issues such as:</p> <ul style="list-style-type: none"> • An attempt to evaluate whether rich nations are more likely to have unequal distributions of either income or wealth than poorer nations. • The extent to which the relationship between how rich a country is and its level of inequality is causal or not. • An assessment of the relative importance of growth as a macroeconomic objective. |
| Level 2 (3–5 marks) Mid mark 4 | Some of the above will be discussed in detail or a couple of points touched on, but only in a relatively superficial way. The candidate may struggle to see that how rich a country is might have any meaningful relationship with inequality. |
| Level 1 (1–2 marks) Mid mark 2 | <p>Whilst there might be some appreciation that evaluation could be carried out and indeed there might be the odd comment that suggests an area for potential evaluation, the point is not developed.</p> <p>For example: ‘It is clearly the case that governments cannot disregard growth, even if growth results in growing inequality.’</p> |

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5 Evaluate whether supply-side policies alone should be used to reduce unemployment. [25]

Candidates should start by defining unemployment and then identifying that the solutions to unemployment are entirely dependent upon its causes. Broadly-speaking unemployment is caused either by insufficient aggregate demand (demand-deficient/cyclical or Keynesian unemployment) or by a range of factors that reflect supply-side issues, such as changing comparative advantage, technological change, the dynamics of people moving from job to job and labour market imperfections (structural, frictional, real wage). Thus, it is likely to be the case that a good answer would state that it is unlikely that supply-side policies ‘alone’ can reduce unemployment. Good candidates might argue, however, that if the economy is currently at the full employment level of national income, such that the number of actual jobseekers equals the number of job vacancies, then there might be a case for arguing that the premise of the question is correct. The best candidates will avoid regurgitating text book theory and develop their answers with subtlety; they will look at specific policy solutions and evaluate their effectiveness. Good candidates will refer to concrete policy initiatives, evaluate the various difficulties inherent in implementing unemployment policy and be likely to refer to recent UK experience.

Answers may include:

Knowledge and understanding of the definition of unemployment, its different causes and solutions. Candidates should appreciate that some unemployment may be a demand-side phenomenon but that there are many other supply-side causes of unemployment. They should be aware that effective policy solutions are dependent upon identifying the causes of unemployment; these may be complex. They should be capable of drawing diagrams to illustrate the different types of unemployment and the impact of suggested solutions. Candidates should examine both demand-side policies in response to demand-deficient unemployment and supply-side policies which seek to remove labour market imperfections, increase labour mobility – both occupational and geographic, and improve information flows within the market.

Application to unemployment policy. Candidates will be expected to look at demand-side solutions, via fiscal and monetary policy, and supply-side solutions. Candidates might choose to contrast the natural rate with other forms of unemployment (e.g. demand-deficient unemployment) and look at specific policy objectives such as retraining schemes, making the payment of Jobseekers Allowance conditional on being seen to ‘look for work’. Accurate reference to specific policies will be rewarded.

Analysis of the nature of unemployment and various policy solutions

Examples:

- Identifying whether the causes of unemployment are demand-side or supply-side, perhaps with reference to full employment.
- Analysis of different types of unemployment, with some candidates likely to focus on the natural rate of unemployment, and distinguishing between actual jobseekers and the labour force – perhaps highlighting that as wages rise, the natural rate is likely to fall.
- The effectiveness of policy measures adopted to tackle unemployment.

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Evaluation of the issues involved

Examples:

- The extent to which it might be difficult to distinguish between different causes of unemployment
- Issues of opportunity cost, government failure and distributional issues as they relate to specific policies to tackle unemployment.
- The time frame involved – policies to tackle unemployment may take a considerable period of time to have an effect.
- Whether or not the market will eventually resolve unemployment of its own accord.
- Whether the government might not want to reduce unemployment below a particular level because of other macroeconomic objectives.

Theory and analysis

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| Level 4 (13–17 marks) Mid mark 15 | There should be precise understanding of the different types of unemployment and the demand and supply-side solutions that this implies. The answer should move on to consider the different approaches to tackling unemployment. There should be some reference to theory and practice as regards government policy and attempts to assess the likelihood of these policies being successful. The very best candidates may highlight the distinction between the natural rate of unemployment and the rate of unemployment that actually prevails. Diagrams will be correct and some may be sophisticated in considering how to reduce the natural rate of unemployment. |
| Level 3 (9–12 marks) Mid mark 11 | There will be reasonable understanding of unemployment and its solutions. There will be analysis of how governments use both supply-side and at least one other type of policy to tackle unemployment but awareness of their effectiveness might not be made explicit. Diagrams are likely to be correct, with only minor errors. At the top of this level [11/12] the answer will begin to link different types of unemployment to appropriate solutions. |
| Level 2 (5–8 marks) Mid mark 7 | There is awareness of unemployment but little explanation of its different causes. At the lower end of this bracket answers may mention specific policy initiatives with little evidence of being able to apply them to the problems associated with reducing unemployment. Diagrams are likely to be incomplete or poorly explained. |
| Level 1 (1–4 marks) Mid mark 3 | Explanations are necessarily limited. There will be awareness of what unemployment is but little analysis of its causes.. The answer is likely to have little understanding of the use of policy instruments, and equally little reference to recent economic history. Candidates will fail to engage in any practical considerations of the effectiveness of particular types of unemployment policy. |

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Evaluation

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| <p>Level 3 (6–8 marks) Mid mark 7</p> | <p>The best answers are likely to evaluate issues such as:</p> <ul style="list-style-type: none"> • Assessment of the extent to which unemployment is a demand-side or a supply-side phenomenon, perhaps with reference to recent UK experience. • Evaluating the extent to which policy initiatives to tackle unemployment are likely to succeed and the time lags associated with these policies. • Evaluation of the possibility that in the modern economy the majority of unemployment policy is supply-side, but that the term ‘alone’ excludes possible demand-side causes. • The extent to which inaction and reliance on the market is as much of a policy choice as intervention in the market. • The extent to which reducing unemployment is a macroeconomic objective |
| <p>Level 2 (3–5 marks) Mid mark 4</p> | <p>Some of the above will be discussed in detail or a couple of points touched on, but only in a relatively superficial way.</p> |
| <p>Level 1 (1–2 marks) Mid mark 2</p> | <p>Whilst there might be some appreciation that evaluation could be carried out but the candidate will struggle to pursue it.</p> <p>For example: “Unemployment will always exist but appropriate policies to tackle it can help reduce it over time.”</p> |

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- 6 Over a twenty year period, a country has run an increasingly large balance of payments current account deficit. Evaluate the different approaches that could be taken to address this issue.

[25]

Candidates should be able to define a 'large balance of payments current account deficit'. They should recognise what this means and its implications for a nation's economy. They should be aware that solutions to this are often sub-divided into expenditure-switching and expenditure-reducing. Better candidates will appreciate that these may only be relatively short-term solutions and that in the long-term, supply-side reform may be a better solution to an economy's lack of competitiveness. Good candidates will make use of information given in the question stem – "over a twenty year period", "increasingly large" – to focus their answer on a persistent and increasing current account deficit. This implies that structural causes of the deficit are most pertinent.

Answers may include:

Knowledge and understanding of demand- and supply-side solutions to a balance of payments current account deficit. Candidates should be aware of the significance of time-lags and the importance of the relative elasticities of demand and supply for imports and exports to demand-side solutions and the longer timeframe required to implement supply-side solutions. Candidates can adopt a variety of approaches: either looking at a specific economy, likely to be the UK but any valid example should be well rewarded, using comparative analysis to consider how approaches to current account deficits vary between nations

Application to correcting a balance of payments current account deficit. Candidates should know how policy changes will affect the level of exports and imports. They should also appreciate the fact that WTO and regional economic grouping membership has implications for expenditure-switching methods of correcting a current account deficit. Some candidates might argue that a nation's mineral wealth may mean that it will be able to afford to run a deficit, or that as long as people wish to hold a nation's assets, such a deficit need not be as problematic as would first appear. However, the persistence and growth of the deficit is likely to attract comment.

Analysis of methods of solving current account problems

Examples:

- Consideration of how expenditure-reducing measures can correct a current account deficit.
- Consideration of how expenditure-switching measures can correct a current account deficit.
- Awareness that in the long-term supply-side policy is perhaps the best solution to a persistent and growing current account deficit.

Evaluation of the issues involved

Examples:

- The effectiveness of expenditure-reducing measures in tackling current account problems and their adverse consequences for other macroeconomic objectives.
- The impossibility of using many forms of expenditure-switching policies to tackle a current account deficit, given the commitment to free trade inherent in WTO membership.
- The extent to which a depreciating currency can correct current account problems and the extent to which this is desirable.
- The considerable time-lags between initiating supply-side policies and then these helping correct current account problems.

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Theory and analysis

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| Level 4 (13–17 marks) Mid mark 15 | Candidates should have an excellent grasp of what a Balance of Payments current account deficit is. They should be aware that the extent to which the current account deficit is a problem depends upon its persistence, its size, as a proportion of GDP, and its causes. They should be aware that there are, and there should be analysis of, several ways of tackling a deficit – expenditure reducing, expenditure switching and supply-side measures is perhaps the most likely subdivision to be used, though others are acceptable [eg fiscal, monetary, supply-side]. Good candidates may recognise that the ability of a nation to use expenditure switching is constrained by WTO and regional economic grouping membership. |
| Level 3 (9–12 marks) Mid mark 11 | There will be reasonable understanding of what is meant by the term ‘balance of payments current account deficit’ and different methods of tackling it. There will be some analysis of at least two categories of measures of tackling the problem but this is likely to be incomplete. |
| Level 2 (5–8 marks) Mid mark 7 | Candidates are aware that the Balance of Payments relates to a nation’s trade position but are imprecise in developing this with reference to the current account. Explanations may contain errors and omissions and little sense of structure. At the bottom of this level there will be awareness that it is one of the main macroeconomic objectives but few ideas on how to correct a ‘balance of payments current account deficit’. |
| Level 1 (1–4 marks) Mid mark 3 | Explanations are necessarily limited. There might be some awareness of what a Balance of Payments current account deficit is, but there is confusion between the account as a whole and the current account. The weakest candidates may confuse the Balance of Payments with the budget balance. The answer is likely to have no understanding of the use of policy instruments within a WTO context. |

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Evaluation

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| Level 3 (6–8 marks) Mid mark 7 | <p>The best answers are likely to evaluate issues such as:</p> <ul style="list-style-type: none"> • The extent to which a ‘balance of payments current account deficit’ is a problem. • The extent to which expenditure reducing policy can work is dependent upon the government’s other macroeconomic objectives and the level of imports and exports. • The limitations of expenditure switching policies – the issue of consumer tastes, the elasticities of demand for exports and imports. • The extent to which depreciation is wrongly seen as a cure-all for current account problems – whether or not the Marshall-Lerner condition holds, the issue of time-lags and the J-curve effect, the fact that price competitiveness is a function of both own price and exchange rates. • The degree to which WTO and membership of regional economic groupings necessarily limit the efficacy of expenditure switching policies. • The difficulties in using supply-side policy to improve the balance of payments current account deficit. |
| Level 2 (3–5 marks) Mid mark 4 | Some of the above will be discussed in detail or a couple of points touched on, but only in a relatively superficial way. |
| Level 1 (1–2 marks) Mid mark 2 | <p>There might be some appreciation that evaluation could be carried out but in general the candidate thinks that current account problems are always cured by depreciation and that external circumstances, such as WTO and regional economic grouping membership are not important in this case.</p> <p>For example: ‘A weakening dollar will always correct a balance of payments current account deficit and in the long term a nation should not worry about a deficit.’</p> |