

Markets, Consumers and Firms: Questions and Answers

Theme 1 for Edexcel AS and A level Economics B

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Introduction

Many students taking this course will sit the '8ECO/01' AS exam after one year, which is the main focus of this material. Others will wait for '9ECO1/01' at A level after two years, which also examines additional content from theme 3 'The Global Economy'.

The questions in 9ECO/01 have a similar format to 8ECO/01 and there will be sample questions in Anforme's text for 'The Global Economy'. The AS questions in Markets, Consumers and Firms also provide a good introduction to the approach at A level.

We know this because the exam board has been more open and specific about these exams than ever before. We have a clearer idea of what to expect.

The good news is that it will not be necessary to be a genius to do well at these exams. Students who are prepared, organised and methodical can do well. Avoiding silly mistakes achieves more than trying for brilliant, dazzling answers.

8ECO/01 Structure

This exam follows the standard approach in the subject area of allocating a minute to earn each mark with a little added thinking time. There are 80 marks and 90 minutes in total. Three sections have 30, 30 and 20 marks. The first two sections (A and B) will have roughly a page of data (or 'stimulus material') and 5 questions each. Our first example is on page 5 of Markets, Consumers and Firms. Section C has its own data and just one question for the 20 marks. There are examples on pages 66 and 116 of Markets, Consumers and Firms

Expect sections in the data response questions to have 2, 4, 4, 8 and 12 marks. As you might expect, the amount required increases with the mark allocation, though even the 12 mark questions need not take more than 10-15 minutes to do well. The progression in questions involves the skills or 'assessment objectives' in the course.

On 20 mark section C questions, expect 4 marks each for knowledge and application, 6 each for analysis and evaluation. How this works should be clearer when you look at sample answers later.

Assessment Objectives

Examiners will be looking for four identified skills. The first of these is **knowledge and understanding**. This boils down to a good grip on the economic jargon and concepts in the course and understanding of how they work and influence behaviour. The 2 mark questions will normally ask for definitions, often asking "What is meant by...", so they are just testing knowledge and understanding.

Command words with 4 mark questions can include 'explain', 'calculate' or 'illustrate'. These move on from knowledge to also test **application** and/or **analysis**. Application frequently entails the use of examples from the evidence with the question or taken from prior knowledge.

Questions will often specify 'with reference to the evidence' (or similar), requiring use of the evidence material. Failure to do this means the loss of application marks. Where the question wording is more general, examples from the evidence or from elsewhere can be used. Knowing an economic formula is one thing, taking the right numbers from data and making a calculation is application.

Building an explanation using step by step logic is analysis, and is generally the target when the command word is 'explain'.

There will probably only be a couple of steps in a four mark 'explain' question in this paper, in a simple sequence of cause and/or effect. The 'illustrate' command asks for a diagram, most likely to be a supply and demand diagram in this theme.

The 8 and 12 mark questions will test all four skills, adding **evaluation** to the previous three. Typically, an 8 mark question will have 2 marks for each skill. The 12 mark questions are likely to have 2 each for knowledge and application, plus 4 each for analysis and evaluation.

Evaluation is essentially judgement. Good judgement has some balance and sees two sides to an argument. 'Balance' is a word that pops up regularly on evaluation mark schemes and does as much as anything else to separate successful students from others who don't do as well.

There is a similarity between good evaluation and the trial process in court, where there are three distinct steps. First the prosecutor makes the 'guilty' case, then the defence has their say, then a judge or jury reaches a verdict. This is a lot to ask for the 2 evaluation marks on an 8 mark question. For this reason, expect schemes for 8 mark questions to emphasise balance, stressing that the minimum for evaluation marks is to show that there are two sides. Going on to develop a small 'judgement' point (or contrast or comment on relative significance) should guarantee both evaluation marks.

Where there are 4 evaluation marks on 12 mark questions, we have moved on to a position where some judgement will definitely be required and balance will simply be a first step towards that.

Section C questions have 20 marks and target extended writing or a brief 'essay'. This should not be frightening and 20 minutes should be enough to produce a sound answer. One key here is to ensure that all four skills are covered. With 4 marks each for knowledge and application, more than one use of relevant knowledge and of examples or references to the evidence should be made.

With 6 marks each for analysis and evaluation, more is expected than on previous questions. There should be convincing chains of logic developing more than one line of thought. As a very rough guide, one brief but convincing item of analytical development is probably worth 2 marks.

Similarly, a brief but sound item of evaluation is probably worth 2 marks. Mark schemes for sample 20 mark questions refer to "A full awareness of the validity and significance of competing arguments, leading to nuanced and balanced comparisons, judgements or conclusions". This sounds a bit frightening, but what it comes down to is scope for use of judgement in addition to a final conclusion.

Having built an argument, for example, answers could move on to a 'however' sentence on the lines of 'this depends on' or 'this is important because'. These give some 'nuance' and take us into validity or significance territory. There are some examples of this identified in the sample answers.

Some examiners find it useful to consider various types of development as evaluative. These can include:

- **Comments on significance**, e.g. 'a marginal change in income might be most significant to people on low incomes'.
- **Identifying necessary conditions**, e.g. 'price increases only increase revenue if demand is price inelastic'.
- **Judging probability**, e.g. 'If Volkswagen rig emissions tests it is probable that some other firms have also found ways to improve their emissions data'.
- **Distinguishing between short and long run**, e.g. 'loans can cost more than share issues in the short run but once paid off the lenders have no long run claim on profits'.
- **Separating private and public interest**, e.g. 'inoculations against contagious disease give a private benefit of protection to individuals and a public benefit from reduced risk to others'.
- **Identifying required extra information**, e.g. 'to know whether labour is a fixed or variable cost we need information on the terms and conditions of employment'.

Health Warnings

There are no perfect answers in this subject area. Answers from different perspectives and constructed in different ways can be equally convincing.

The possible answers which follow reflect one possible approach.

The questions in 'Markets , Consumers and Firms' focus on a small part of the specification, often just one chapter, questions in exams are likely to be wide ranging.

The proportion of calculation questions in the book is lower than the 15% of exam marks which will be linked to quantitative skills. These skills might sometimes include interpretation of numerical data as well as calculation.

Mark schemes and examiner reports from 'real' papers give the best guide to examiner thinking and priorities.

For convenience, evidence and questions are reproduced with the possible answers which follow.

Health spending (page 5)

Country	Average life expectancy (Years)	Share of income spent on health (%)
Brazil	74	9.3
India	66	4.0
Japan	84	10.1
South Africa	56	8.8
United Kingdom	82	9.4
United States	79	17.9

Source: World Bank

The data in the table above shows relatively long life expectancy in the United Kingdom, suggesting a relatively healthy population in an important respect. The share of the nation's income (technically Gross Domestic Product or GDP) spent on health is similar to some of the other countries shown, though more than double the Indian figure and little over half of the United States figure.

The data shown is positive (or provable) but it would be dangerous to leap to generalisations about links between spending and life expectancy. South Africa's lower life expectancy, for example, is influenced by a problem with HIV/AIDS which is less prevalent in the other countries shown. One of the factors contributing to long life expectancy in Japan is a healthier diet and so less obesity.

It is tempting to make the normative statement that everyone should have unlimited treatment as health is so important. However, using resources for health has an opportunity cost and keeping pace with growing demand would be very difficult. Many developed countries have a growing proportion of elderly people. Old people require more health care. Expectations are rising: more people now want cosmetic surgery to improve their appearance, for example. Medical advances make more new and expensive treatments available: Kadcylla, a new drug for breast cancer treatment, costs £90,000 per patient.

Questions

1. What is meant by 'normative statement'? (2 marks)
2. Give an example of a positive statement from the above passage, and explain why it is positive. (4 marks)
3. Briefly explain one possible reason why new drugs are very expensive. (4 marks)
4. Discuss two possible causes of the variations shown in spending on health. (8 marks)
5. Assess the opportunity cost of increasing UK health spending to keep up with demand and the trade-offs involved when health spending is limited. (12 marks)

Health spending (page 5)

Answers

1. What is meant by 'normative statement'? (2 marks)

Normative statements are based on opinions or personal judgements rather than evidence. A statement containing 'should' is probably normative, for example.

Comment: Brief, accurate definitions are enough. A small example or development might secure the second mark, if a definition is slightly incomplete.

2. Give an example of a positive statement from the above passage, and explain why it is positive. (4 marks)

The first statement in the evidence is that 'the data in table one shows relatively long life expectancy in the UK'. This is a positive statement because it is based on evidence which can be tested. As the table shows, countries such as South Africa (56) and India (66) have a lower life expectancy than people in the UK.

Comment: Analytical link word

3. Briefly explain one possible reason why new drugs are very expensive. (4 marks)

There are both demand and supply based reasons for new drugs being expensive. For supply, the research, testing and development of new drugs is a very expensive process and many lines of research fail. The firms which spend this money want to recover their costs and make a profit. With prices as high as the £90,000 per patient for Kadcycla, the quantity sold is unlikely to be high so testing and development costs can only be spread over a limited output.

Comment: As above

4. Discuss two possible causes of the variations shown in spending on health. (8 marks)

The tabulated data shows the share of income spent on health. The USA has the highest income of the country's listed and health takes the highest share of income, so total U.S. spending on health must be significantly higher. One reason is that Americans, many of whom have private Medical Insurance, demand very high standards of care. They are willing to spend a large amount on insurance or treatment, perhaps partly because they can afford to. It is likely that food, shelter and other basic necessities take most income in the poorest countries listed. So, for example, many Americans have expensive dental treatments to get even, white teeth, whereas most Indians have minimal or no dental work.

It could also be that cultural factors simply made U.S. and UK citizens less healthy than Indians, so needing more care. Many rich countries have unhealthy diets and obesity problems, with high rates of heart disease. The Indian diet and lifestyle could be healthier so they need less treatment. However, Japan has the longest life expectancy, the second highest health spending and relatively high income. It is not simply the case that richer countries have less healthy citizens.*

There are probably many different factors involved in determining the level of health spending. Both of the factors identified could play a part but they don't give a full picture.

*Comment: *marks an example of an evaluative point.*

5. Assess the opportunity cost of increasing UK Health spending to keep up with demand and the trade-offs involved when health spending is limited. (12 marks)

An increase in health spending means using more scarce resources for Healthcare. Most UK Health spending is controlled by the government. Spending more on health could be funded by reducing other areas of public spending such as defence and education. The opportunity cost would then be the lost services in these areas.

As an alternative to this, the government could raise more money by extra taxation or by charging for more NHS services. For example, some people favour making a charge for GP appointments. If the government raises taxes or charges, this passes the cost to taxpayers or patients rather than to other government departments. These people would have to consume or save less as the opportunity cost.

Governments can borrow, in a sense passing the cost to future generations if the debt is not repaid for many years. However, the present UK government is determined to reduce their deficit by cutting spending and/or raising taxes. This makes additional borrowing difficult.

Growing demand from the ageing population, higher expectations (e.g. for cosmetic surgery) and the increasing availability of new and expensive treatments means that it would be difficult for total spending to keep up with all the possibilities. This means accepting limits to health spending and some prioritisation in what is done. The most likely outcome is a blend of cuts elsewhere in government expenditure, some additional taxation and some limits on health spending. Thus the opportunity costs would be the loss of whichever other services were cut, some fall in private consumption and some trade-offs within health spending. Extra spending in one area means reductions elsewhere.

Comment: a little analysis of options then an attempt at judgement of likely outcome.

Suma (page 10)

Suma is a vegetarian wholefoods wholesaler based in Leeds, specialising in healthy, natural, organic and Fairtrade foods. From modest beginnings 40 years ago, the organisation has moved to bigger premises several times to allow expansion. It now employs around 150 people and has sales revenue of more than £34 million per year. The business was well placed to gain from growing interest in healthy eating. Its approach to business has also proved very successful.

Suma is an equal opportunity, fully democratic workers' cooperative. All the members/employees have the same hourly rate of pay. Members are multi-skilled, bringing flexibility to the business and variety to each person's work. General meetings decide policy and direction. An elected management committee oversees the fulfilment of plans. An emphasis on ethical behaviour and working for sustainability has always been important to Suma

Questions

1. What is meant by sales revenue? (2 marks)
2. Explain what ethical behaviour entails. (4 marks)
3. Identify one strength and one weakness of Suma having just one pay rate. (4 marks)
4. Discuss the importance of profitability to Suma. (8 marks)
5. Assess likely objectives of a workers' cooperative, other than profit. (12 marks)

Answers

1. What is meant by 'sales revenue'? (2 marks)

Sales revenue is the total of income a business receives from its products.

Numerically, Revenue = Price X Quantity.

Comment: Brief answers are sometimes sufficient. There is no need to fill the ruled lines in a question and answer booklet

2. Explain what ethical behaviour entails. (4 marks)

Behaving ethically means doing what is right rather than simply being selfish. For example, Suma focuses on healthy food, sustainability and democratic management rather than simply on profit. This involves considering the interests of a range of stakeholder groups and the wider community.

3. Identify one strength and one weakness of Suma having just one pay rate. (4 marks)

Having a single pay rate will strengthen people's feeling of belonging to the business, perhaps creating an atmosphere of unity, and this could possibly improve the job satisfaction and motivation of workers. A disadvantage is that where specialist skills are required, accountancy skills for example, accepting a job with Suma would mean being paid far less than other members of their profession. This might make it difficult to attract able professional staff.

Comment: 'Identify' requires little or no explanation.

4. Discuss the importance of profitability to Suma. (8 marks)

Suma is described as a very successful business with revenue of more than £34 million a year. However, the evidence makes no mention of profitability and focuses on objectives such as equal opportunity, ethical behaviour and sustainability. The structure of the business, as a cooperative, means that there are no shareholders who expect dividends.

The growth of the business has presumably been funded in part by reinvesting profits for developments such as moving to bigger premises. This suggests that profits are important to Suma, but as a means to an end rather than as an objective. Without profits, the business could not have grown to employ 150 people and to distribute healthy, natural, organic and fair trade foods so widely.

A business which had no concern for profitability, and continually ran at a loss, could not last for long unless it was an indulgent hobby for rich owners. Any objectives are likely to involve the continued existence of the business, which requires avoidance of losses as a minimum. Most objectives are easier to achieve in a business with profits and a secure financial footing.

The source of the evidence on Suma is not given, but it reads like the type of information the company would produce about itself. The failure to mention profits could be a conscious choice which allows the business to stress its ethical nature. In reality, Suma could well see profit as an important part of running the business successfully.

5. Assess likely objectives of a workers' cooperative, other than profit. (12 marks)

A workers' cooperative such as Suma is controlled by its workers. In this case they have general meetings to decide policy and direction. This means that the objectives will be set after discussion between members. Members are likely to see their own security and working conditions as one priority. Security involves the continued existence and success of the business, which should keep them realistic about how much they can pay themselves, how many hours they work and how generous employee welfare provisions can be.

Ethics and social objectives are important in this case. Members evidently gain satisfaction from distributing healthy foods, working for sustainability and supporting the Fairtrade movement. People like to feel that they are doing something worthwhile. Customer satisfaction is likely to be important, both as an aspect of behaving ethically and because repeat business will help Suma to thrive.

It could well be that the management committee is concerned with the detail of issues such as cost efficiency and market share, as they are relevant to the survival and growth of the business. Other members are likely to accept the committee's decisions on this unless they feel their incomes and working conditions are under threat.

There is unlikely to be a single overriding objective for a workers' cooperative. Employee welfare is likely to have a higher priority than in some types of business and return on investment might have a lower priority. Suma is typical of many cooperatives in emphasising ethical business, sustainability and social objectives. Realistically, though, such considerations are unlikely to have higher priority than survival of the business and providing a continuing livelihood for members of the cooperative.

Comment: looking at relative importance is one way to assess.