



General Certificate of Education
Advanced Level Examination
June 2011

Economics

ECON3

Unit 3 Business Economics and the Distribution of Income

Friday 17 June 2011 1.30 pm to 3.30 pm

For this paper you must have:

- an AQA 12-page answer book.
- You may use a calculator.

Time allowed

- 2 hours

Instructions

- Use black ink or black ball-point pen. Pencil should only be used for drawing.
- Write the information required on the front of your answer book. The **Examining Body** for this paper is AQA. The **Paper Reference** is ECON3.
- In **Section A**, answer **EITHER** Context 1 **OR** Context 2.
- In **Section B**, answer **one** essay.

Information

- The marks for questions are shown in brackets.
- The maximum mark for this paper is 80.
- There are 40 marks for **Section A** and 40 marks for **Section B**.
- This paper is synoptic. It assesses your understanding of the relationship between the different aspects of Economics.
- You will be marked on your ability to:
 - use good English
 - organise information clearly
 - use specialist vocabulary where appropriate.

Advice

- You are advised to spend 1 hour on **Section A** and 1 hour on **Section B**.

Section A

Answer **EITHER** Context 1 **OR** Context 2.

EITHER

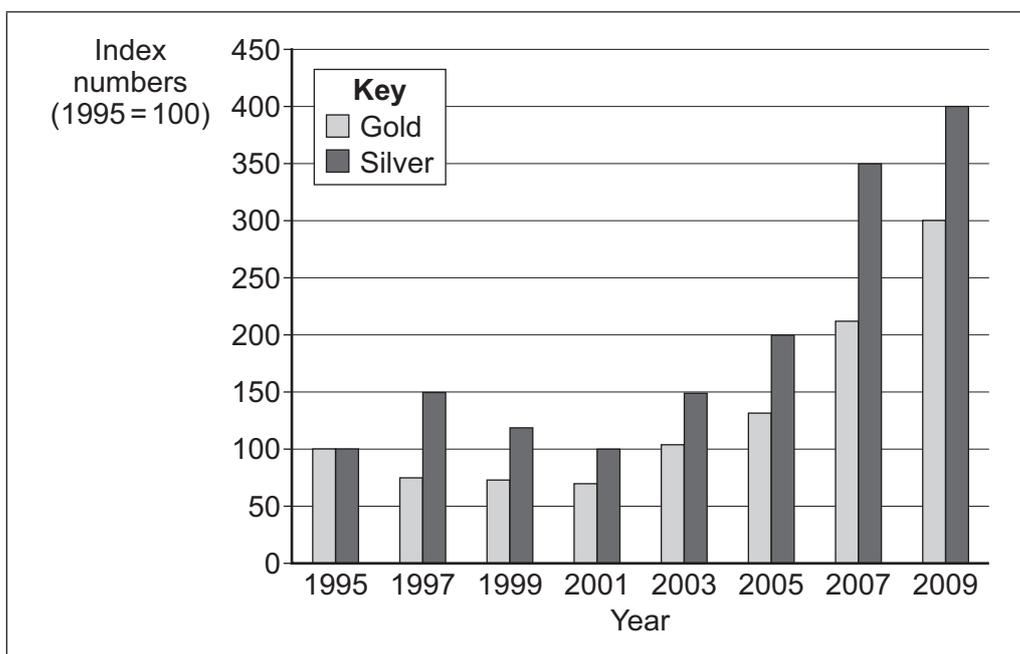
Total for this context: 40 marks

Context 1

THE GLOBAL CONTEXT

Study **Extracts A and B**, and then answer **all** parts of Context 1 which follow.

Extract A: Gold and silver, world price indices



Source: industry statistics, accessed 2010

Extract B: The recycling market

Scrap metal dealers are once again touring housing estates in their pick-up trucks obtaining steel and other metals from householders. Increased demand for steel and other metals on world markets has led to a change in the fortunes of these dealers, who are price takers.

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Recycling has become a global activity. In 2009, with gold selling internationally at well over \$1000 an ounce, there were TV adverts from companies wanting to buy unwanted jewellery. A mobile phone also contains tiny traces of precious metals which can be extracted profitably from the millions of phones discarded each year. This is done at large processing centres, usually near sea ports, and much of the recovered material is exported to factories in China. The Olympic stadium in Beijing, China, was built almost entirely using recycled steel.

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Germans, Scandinavians and Canadians are used to sorting their rubbish into different coloured bins. But instead of matching the recycling rates achieved in some countries, the UK still dumps many potentially useful materials. These include plastics, glass, paper

and metals, which are buried in landfill sites partly because there are insufficient market incentives for recycling. The UK's strong reliance on landfill indicates the existence of widespread environmental market failure. Landfill creates greenhouse gases, threatens to pollute water sources and wastes scarce resources. 15

Some critics suggest that it would be better for the UK to aim at waste reduction, eliminating unnecessary packaging and other 'bads' at the production and retail stages. The UK pressure group *Waste Watch* also suggests more reuse, for example encouraging people to buy second-hand clothes from charity shops. However, other methods, such as returnable milk bottles, are in sharp decline. 20

There are now landfill taxes and regulations which provide incentives for recycling. Households could face the prospect of fines for breaking 'bin-bag rules'. However, this may lead to unintended consequences such as illegal dumping of waste. *Waste Watch* wants national targets and other policies to promote composting because, by weight, garden and kitchen waste make up the majority of material sent to landfill. *Waste Watch* also suggests increasing the landfill tax each year and extending it to cover incineration and other waste-disposal methods. 25

Recovery is a further option. In less developed countries, some homeless people live on city rubbish dumps making a living from what they can find and sell. In the UK, market conditions are such that the metal in a 2p coin is now actually worth 3p. Some experts even predict that within ten years it will be economic to excavate landfill sites to 'mine' the tin cans and other scrap materials that have been buried there. 30

Source: news reports, 2009–10

0 | 1 Using **Extract A**, identify **two** significant points of comparison between the world price index for gold and the world price index for silver over the period shown. (5 marks)

0 | 2 Explain the term 'price taker' **and** analyse the likely effects of an increase in the world demand for scrap metals on the output **and** profits of a scrap metal dealer (**Extract B**, lines 1–4). (10 marks)

0 | 3 'The UK's strong reliance on landfill indicates the existence of widespread environmental market failure' (**Extract B**, lines 16–17).

Using the data and your economic knowledge, evaluate alternative methods of correcting market failure arising from waste disposal. (25 marks)

Turn over ►

Do **not** answer Context 2 if you have answered Context 1.

OR

Total for this context: 40 marks

Context 2

THE EUROPEAN UNION CONTEXT

Study **Extracts C and D**, and then answer **all** parts of Context 2 which follow.

Extract C: Air traffic between the UK and abroad: indices of flight and passenger numbers, 2001–2008 (2001=100)

Year	Index of number of flights	Index of passenger numbers
2001	100	100
2002	100	100
2003	96	101
2004	104	109
2005	108	119
2006	112	122
2007	115	129
2008	115	126

Source: official statistics, 2009

Extract D: *British Airways and Iberia Airlines*

Until about twenty years ago, most European countries had at least one large 'national carrier' airline which was in public ownership. When airlines were privatised, there were fears that a state-owned monopoly would simply become a private monopoly. On some routes, de-regulation took some time and it was not until 2008 that the 'Open Skies' agreement sought to eliminate anti-competitive practices among airlines flying from Europe to North America. These anti-competitive practices included denying smaller airlines the opportunity to rent landing slots (landing spaces) at major airports. 1
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In the face of greater competition from smaller, more innovative airlines such as *Virgin Atlantic* and the low-cost carriers such as *easyJet*, there has been increasing collaboration between some of the larger, traditional companies. *British Airways (BA)*, *Iberia Airlines (Spain)* and *American Airlines (AA)*, together with five other airlines, belong to *One World Alliance*, an arrangement which enables member airlines to sell seats on each other's flights. 10

With *BA* reporting a pre-tax loss of £401m in May 2009, its Chief Executive proposed a 'tie-up' with *Iberia* and *AA* which would come closer to a full-blown horizontal merger, enabling not only the marketing of flights but also joint pricing and a sharing of revenues. The proposal needed to be cleared by both EU and US anti-monopoly authorities, but it quickly failed when the European Union's Competition Commissioner objected, mainly on the grounds that it would raise prices and reduce consumer choice. 15

In October 2009, two European members of *One World Alliance*, *BA* and *Iberia*, tried again to reach a preliminary agreement for a full merger which they aimed to complete in late 2010. They claimed that a merger would be good for consumers as well as for the companies involved because duplicated European routes could be rationalised, while the routes operated in North America by *BA* and in South America by *Iberia* were complementary rather than competitive. The merger would need to be approved by the European Commission but there was a precedent because, in 2004, *Air France* was allowed to merge with Dutch airline *KLM*. 20

The merger between *BA* and *Iberia* would create Europe's biggest airline. Critics raised concerns about the new company's market share and claimed that *BA*'s dominance at Heathrow Airport would increase to even more than its existing 44% of landing slots. 25
Meanwhile, both *BA* and *Iberia* workers were planning strikes over cost-cutting proposals and pay offers. 30

Source: news reports, 2009

- 0 4** Using **Extract C**, identify **two** significant points of comparison between the index of number of flights and the index of passenger numbers over the period shown. (5 marks)
- 0 5** Explain the term 'public ownership' (**Extract D**, line 2) and analyse **two** economic reasons that could be used to support public ownership of industries such as airlines. (10 marks)
- 0 6** Using the data and your economic knowledge, evaluate the view that mergers, such as the one proposed between *British Airways* and *Iberia Airlines*, are usually 'good for consumers as well as for the companies involved' (**Extract D**, lines 22–23). (25 marks)

Turn over for the next question

Turn over ►

Section B

Answer **one** essay from this section.

Each essay carries 40 marks.

EITHER**Essay 1**

'The law of diminishing returns is an economic principle which will definitely operate at some point, whereas economies of scale are less certain.'

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 Explain how a firm's costs of production may be affected by diminishing returns in the short run and economies of scale in the long run. (15 marks)

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 Evaluate the view that firms will always try to minimise their costs and maximise their revenues. (25 marks)

OR**Essay 2**

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 'On a typical train journey, there could be as many as twenty different fares being paid by passengers travelling between the same two stations.'

Using the concept of price discrimination to help you, explain how and why this might happen. (15 marks)

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 Is price discrimination always good for producers and bad for consumers? Justify your answer. (25 marks)

OR**Essay 3**

'*The Spirit Level*, a book by Richard Wilkinson and Kate Pickett published in 2009, is subtitled: *Why More Equal Societies Almost Always Do Better*.'

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 Explain the causes of inequality in the distribution of income and wealth in the UK. (15 marks)

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 Evaluate the view that the government should rely less on market forces to determine the distribution of income and wealth in the UK and should increase its intervention to make the UK more equal. (25 marks)

END OF QUESTIONS

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