

Write your name here

Surname

Other names

Centre Number

Candidate Number

Edexcel GCE

Economics

Advanced Subsidiary

Unit 1: Competitive Markets: How they work and why they fail

Friday 18 May 2012 – Afternoon

Time: 1 hour 30 minutes

Paper Reference

6EC01/01

You do not need any other materials.

Total Marks

Instructions

- Use **black** ink or ball-point pen.
- **Fill in the boxes** at the top of this page with your name, centre number and candidate number.
- Answer **all** questions in Section A and **one** question from Section B.
- Answer the questions in the spaces provided
– *there may be more space than you need.*

Information

- The total mark for this paper is 80.
- The marks for **each** question are shown in brackets
– *use this as a guide as to how much time to spend on each question.*
- Questions labelled with an **asterisk** (*) are ones where the quality of your written communication will be assessed
– *you should take particular care on these questions with your spelling, punctuation and grammar, as well as the clarity of expression.*

Advice

- Read each question carefully before you start to answer it.
- Keep an eye on the time.
- Check your answers if you have time at the end.

Turn over ►

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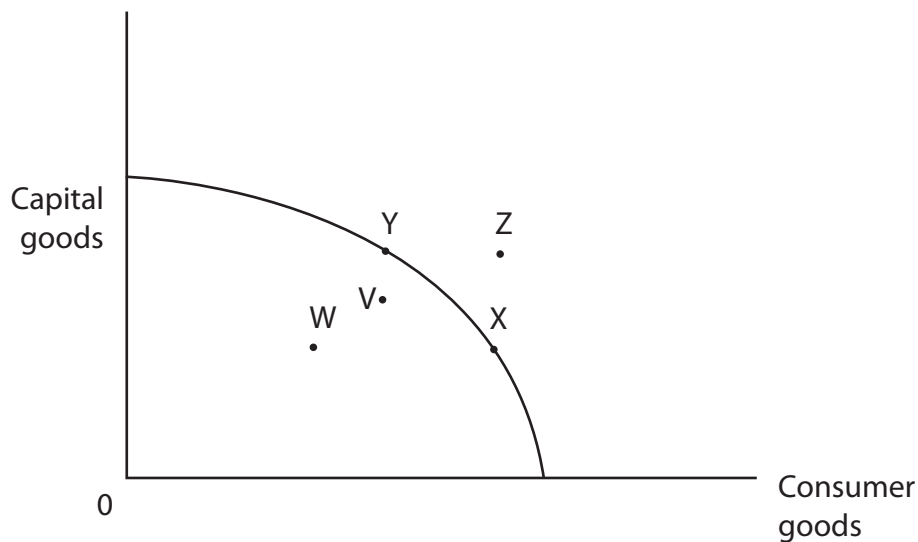


PEARSON

Section A: Answer all the questions in this section

You should spend 35 minutes on this section. Use the data to support your answers where relevant. You may annotate and include diagrams in your answers.

1



The diagram shows a production possibility frontier for an economy. Which of the following changes shows a reduction in unemployed resources?

(1)

- A** W to V.
- B** X to Z.
- C** Y to X.
- D** An outward shift of the whole production possibility frontier.

Answer

Explanation

(3)

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(Total for Question 1 = 4 marks)



2 In November 2010 the UK government increased the tax for passengers flying by aircraft (Air Passenger Duty). The tax increased from £40 to £60 per passenger flying economy class from the UK to the US.

One effect of this tax is to:

(1)

- A increase the consumer surplus for air passengers.
- B decrease the tax revenue collected if demand for flights is price inelastic.
- C increase the producer surplus for airlines if supply of flights is price elastic.
- D increase the price of air flights.

Answer

Explanation

(3)

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(Total for Question 2 = 4 marks)



3 One function of the price mechanism is to:

(1)

- A** eliminate shortages of a good by allowing its price to fall.
- B** act as a signal to firms when making production decisions.
- C** eliminate surpluses of a good by allowing its price to rise.
- D** encourage government intervention to reduce inequality.

Answer

Explanation

(3)

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(Total for Question 3 = 4 marks)



5 The table shows the demand and supply schedules for packets of shortbread biscuits. You may use the last column for your workings.

Price per packet	Quantity of packets demanded per month (000)	Quantity of packets supplied per month (000)	New quantity supplied per month (000)
£2.00	200	160	
£2.10	180	180	
£2.20	160	200	
£2.30	140	220	

As a result of an increase in the baking costs for producing packets of shortbread biscuits, supply decreases by 40 000 packets at all prices. The new equilibrium price is: (1)

- A £2.00
- B £2.10
- C £2.20
- D £2.30

Answer

Explanation (3)

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(Total for Question 5 = 4 marks)



6 Market failure arises in a free market economy when:

(1)

- A** prices fall in response to an excess supply.
- B** public goods are under-provided.
- C** firms exit a market.
- D** government intervention leads to a misallocation of resources.

Answer

Explanation

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(Total for Question 6 = 4 marks)



Section B: Answer either Question 9 or Question 10.

If you answer Question 9 put a cross in this box .

Question 10 starts on page 24.

You should spend 55 minutes on this question.

9 UK Higher Education tuition fees

Figure 1: Estimated repayment of tuition fees by graduate workers

Gross annual income	Monthly repayment
Under £21 000	0
£25 000	£ 30
£30 000	£ 68
£40 000	£143
£50 000	£218
£60 000	£293

(Source: Browne report: Review of Higher Education Funding and Student Finance, 2010
© Crown Copyright)

Figure 2: UK University applications 2005-2011

Year	Number of student applications to higher education	Percentage change over previous year
2005	522 155	-----
2006	506 304	-3.0*
2007	534 495	5.6
2008	588 689	10.1
2009	639 860	8.7
2010	697 351	9.0
2011	729 376 (forecast)	4.6

*Note: between 2005 and 2006 tuition fees increased from £1 175 to £3 000 per annum

(Source: UCAS Analysis and Research - http://www.ucas.com/about_us/stat_services/stats_online/data_tables/datasummary)



Extract 1 University tuition fees increase up to a maximum of £9,000 a year

Universities minister David Willetts announced an increase in tuition fees from £3,290 to a maximum of £9,000 a year in England by 2012. Three quarters of English universities intend to set the maximum tuition fees of £9,000, and 95% plan to charge more than £7,000. This will help to balance out an 80% cut in government funding to university undergraduate courses.

5

Increasing the contribution made by graduates strengthens the link between what the student gains from education and what they pay back. It encourages universities to compete for students who will now directly fund the courses. Universities may be forced to improve teaching standards and become more efficient. Students should still gain financially: the return on a degree has been estimated at an additional £160,000 over a working lifetime compared to a non-graduate with A Levels. However, graduate unemployment reached a 17 year high at 8.9% in 2010.

10

Many students will take out student loans to pay their fees and living expenses. These loans will only be repaid once graduates' income rises above £21,000 a year, at a rate of 9% of their income above this level. For students from low-income families, there are grants of up to £3,250 per year, and bursaries from universities will also be available.

15

A world class university education system is vital for attracting investment and increasing labour productivity, ensuring long term wealth and prosperity. It also generates earnings from large numbers of overseas students.

20

(Source: Adapted from 'University tuition fee limit rises to £9 000'; by Hazel Barker, Sky News online, 3rd November 2010 © 2011 BskyB and Jeevan Vasagar, Guardian, 22nd November 2010 © Guardian News & Media Ltd 2010)

Extract 2 Higher university fees are unfair to students from low-income families

Research conducted in 2010 by the University of Leicester indicated that students from low-income families are more likely to be put off from applying to higher education than better-off students. The research involving 730 A Level students found that an increase in tuition fees from £3,290 to £7,000 would reduce the number of applications from low-income households by 14% compared to a reduction of 9% for better-off households.

5

The research also revealed a differing impact on the types of institutions and courses. Applications to the most prestigious universities would not be affected but the new universities would suffer a significant fall in applications. Furthermore, applications for Medicine and Law would hardly be affected but there would be a big fall in numbers applying for Arts and Humanities courses. The tuition fees increase could lead to a reduction in the number of universities and range of courses on offer. There are fears that some 36 000 university places could be lost in 2012.

10

However, most A Level students still intend to apply to university, suggesting a genuine appreciation of the benefits from a higher education degree.

15

(Source: © University of Leicester 20 September 2010)



- (a) With reference **to the titles** of Extract 1 and Extract 2, distinguish between positive and normative statements. (4)
- (b) With reference to the information provided and your own knowledge, explain the opportunity cost of higher education to students. (6)
- * (c) Evaluate the likely private benefits and external benefits of university education. Illustrate your answer with an appropriate diagram. (14)
- (d) With reference to Extract 2 and using price elasticity of demand calculations, assess the likely impact on *student applications* of an increase in tuition fees from £3,290 to £7,000. (10)
- * (e) Discuss the possible economic effects of an increase in university tuition fees on the market for higher education. (14)



(a) With reference **to the titles** of Extract 1 and Extract 2, distinguish between positive and normative statements.

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* (c) Evaluate the likely private benefits and external benefits of university education. Illustrate your answer with an appropriate diagram.

(14)

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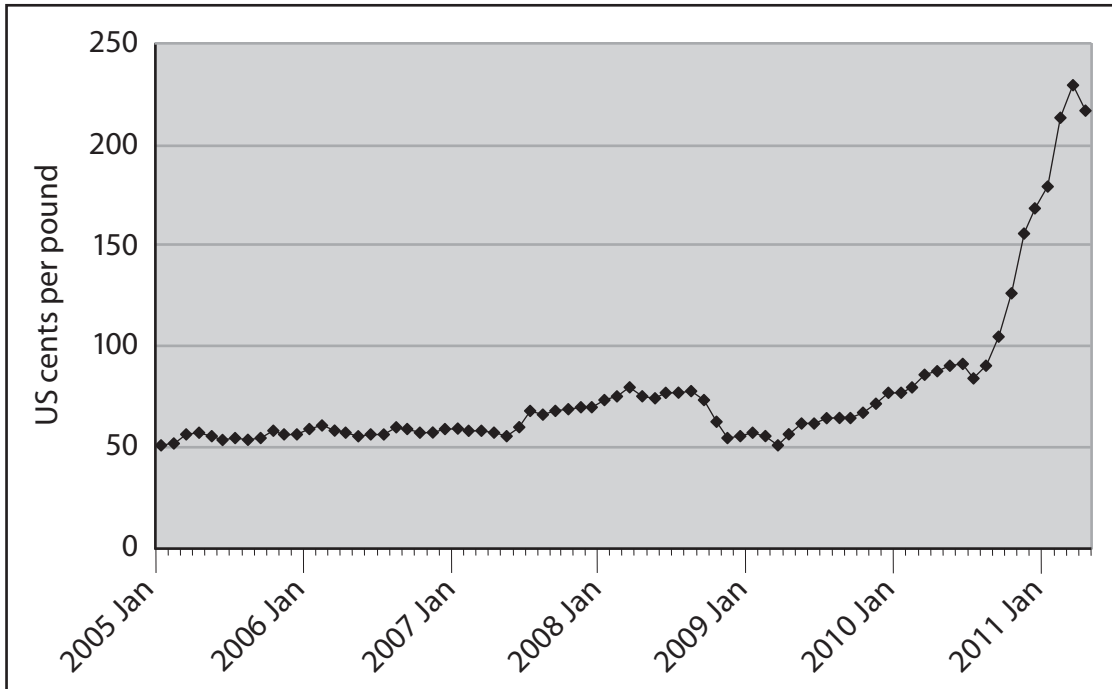
Handwriting practice area with 20 horizontal dotted lines.



If you answer Question 10 put a cross in this box .

10 The price of cotton

Figure 1: Cotton prices 2005-2011 (US cents per pound in weight)



(Source: World Economic Outlook Database © 2011 International Monetary Fund)

Extract 1 Rising cotton prices

The price of cotton more than doubled in 2010 after crops in China and Pakistan were hit by floods. This was made worse by the Indian Government's ban on cotton exports. World supply of cotton fell from 107 million bales in 2009 to 101 million bales in 2010. A bale of cotton weighs 500 pounds and can make 1200 t-shirts. Stocks of cotton are at their lowest level for five years. At the same time, speculators have bought up large quantities of cotton in the hope of making profits.

5

Farmers have responded to rising prices by devoting more land to cotton. In the right conditions, cotton crops take 100 days to reach maturity. World supply is forecast to increase to 117 million bales in 2011.

Cotton is the most important textile for making clothing. However, demand for synthetic materials is increasing as manufacturers look for alternatives.

10

(Source: adapted from 'Cotton price rise will hit clothing warns Next', James Hall, The Telegraph, 4th November 2010 © Copyright Telegraph Media Group Limited 2010)



Extract 2 The impact of rising cotton prices on clothing retail stores

Lord Wolfson, chief executive of retail clothing store Next, warned that the soaring price of cotton could lead to clothing prices rising by almost 10% in 2011. The retailer, which has more than 500 stores and 2.6 million online and catalogue shoppers, blamed 'what appears to be a speculative bubble' for the expected price rises.

Lord Wolfson stated that 'we have not seen clothing prices rise for nearly twenty years, so it's going to be very difficult to know how consumers will respond to a price increase'. Other stores such as Debenhams and Marks & Spencer also predicted higher clothing prices in 2011. Previously, prices had been kept down by firms relocating production facilities to Asia. 5

Next's share price in November 2010 was more than 20% higher than in November 2009. This reflected a successful diversification into home furnishings such as cushions, curtains and furniture. However, analyst Katharine Wynne, at Investec, cut her full-year profit forecasts for Next from £560m to £542m and cancelled her 'buy' recommendation on the retailer's shares. 10

(Source: adapted from 'Next forecasts 10% rise in clothes prices', Julia Finch, The Guardian, 4th November 2010 © Guardian News & Media Ltd 2010)

Extract 3 Genetically modified (GM) cotton farming in India

The use of genetically modified cotton seed is widespread in India. It is used to prevent disease, increase crop yields and used to kill the pink bollworm, a mite which eats cotton seed. However, in 2009, scientists found that the bollworm had developed resistance to the modified version of the seed.

Consequently, the anticipated increase in crop yields has not materialised. However, the costs to farmers of buying and using GM seeds have increased – they require more fertiliser and twice as much water compared to traditional seeds. Farmers are not allowed to harvest seeds for the next crop but are forced to buy fresh supplies from Monsanto, the producer of this GM seed. There is now a genuine fear of a lack of bio-diversity resulting from the use of GM crops. 5 10

(Source: adapted from 'Monsanto and Indian Farmer suicides', by Ralph Stone, © The Berkley Daily Planet, 6th December 2010.)



- (a) With reference to Figure 1 and Extract 1, outline why the price of cotton more than doubled in 2010. Use a demand and supply diagram in your answer. (6)
- (b) Referring to cross elasticity of demand, explain the likely relationship between the price of cotton and the demand for synthetic materials used in making clothing (Extract 1, lines 10–11). (4)
- (c) With reference to Extract 1, discuss the factors that are likely to influence the price elasticity of supply of cotton. (10)
- * (d) With reference to Extract 2, evaluate the likely effects of the increase in the price of cotton on retail clothing firms such as Next. (14)
- * (e) With reference to the concepts of private costs and external costs, assess the possible economic effects of 'the use of genetically modified cotton seed' (Extract 3, line 1) Use an appropriate diagram in your answer. (14)



(a) With reference to Figure 1 and Extract 1, outline why the price of cotton more than doubled in 2010. Use a demand and supply diagram in your answer.

(6)

Dotted lines for writing the answer.



(b) Referring to cross elasticity of demand, explain the likely relationship between the price of cotton and the demand for synthetic materials used in making clothing (Extract 1, lines 10–11).

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*(e) With reference to the concepts of private costs and external costs, assess the possible economic effects of 'the use of genetically modified cotton seed' (Extract 3, line 1) Use an appropriate diagram in your answer.

(14)

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(Total for Question 10 = 48 marks)

TOTAL FOR SECTION B = 48 MARKS

TOTAL FOR PAPER = 80 MARKS

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