

**MARK SCHEME for the May/June 2012 question paper
for the guidance of teachers**

9772 ECONOMICS

9772/03

Paper 3 (Investigation), maximum raw mark 40

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1 Transport and the environment

Evaluate the extent to which alternative sources of energy, such as biofuels, offer an effective solution to the environmental problems resulting from transport use in the UK.
[40]

Candidates should demonstrate that they understand the nature of alternative energy sources. They should demonstrate a good understanding of the environmental problems resulting from transport use, notably atmospheric emissions and their impact on health and climate. They should understand the concept of externalities and recognise the contribution alternative fuels can make to their reduction. They should use appropriate analytical tools and data to support their arguments. The wider global context is likely to be relevant when considering both the technologies themselves and their likely impact. They should reach a clear and well-supported conclusion on the extent to which alternative energy sources offer an effective solution. Candidates are likely to focus primarily on passenger transport. Those who recognise that freight transport is also part of the problem, and solution, should be rewarded. Analysis may be assisted by the use of diagrams.

Answers may include:

Knowledge and **understanding** of alternative energy sources and the environmental problems resulting from transport use.

Examples:

- Alternative energy sources, including;
 - Biofuels
 - Hydrogen
 - Electricity generated by:
 - Fossil fuels
 - Nuclear power
 - Renewables
- Negative externalities, including:
 - Atmospheric pollution
 - Visual and noise pollution
 - Blight

Application of alternative energy and environmental problems in a UK transport context.

Examples:

- Existing alternative energy technologies in the UK;
 - Biofuel (5% content of existing petrol)
 - Electric vehicles
 - Renewable electricity generation
- Transport related environmental problems in the UK;
 - Transport emissions growth
 - Emissions reduction targets
 - Health issues, including growth in respiratory illness
 - Range of other non-atmospheric externalities in context

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Analysis of the effect of alternative energy on environmental problems.

Examples:

- Use of biofuels;
 - Reduced dependence on fossil fuels
 - Potential to be renewable and reduce emissions
- Use of electric vehicles;
 - Reduced emissions in urban areas – health benefits
 - More efficient use of energy
 - Reduced noise pollution
 - Potential to use overnight electricity
- Renewable energy generation;
 - Reduced emissions on a national and global scale
 - Sustainability benefits
- Use of Hydrogen fuel cells;
 - Reduced emissions
 - Increased range and ease of use compared with electric vehicles
- Government measures to encourage use of alternative sources of energy, including;
 - Biofuel requirement in petrol (RTFO)
 - Subsidy for purchasers of electric vehicles
 - Encouragement for renewables:
 - Feed-in-Tariffs
 - Renewable Obligation
 - Renewable Energy Tariffs
 - Renewable Heat Incentive

Candidates are likely to support their analysis by referring to externalities and arguing that alternative energy sources are likely to reduce the external costs associated with transport use and move transport markets closer to the social optimum. Good candidates are likely to support their analysis with appropriate diagrams as well as relevant and recent data on, for example, the extent to which specific technologies can reduce emissions. They may also refer to the positive externalities generated by the use of government subsidy, regulation and legislation in transport energy markets.

Candidates may also use macroeconomic analysis and consider the impacts on international competitiveness, both positive and negative, of the move away from fossil fuels. They may consider the extra costs of alternative energy sources and/or the comparative advantage enjoyed by the UK in the production of renewables.

Evaluation of the extent to which alternative energy sources provide an effective solution to transport-related environmental problems.

Basic evaluation may suggest that alternative energy sources offer a potential solution but that there are many practical obstacles to their widespread use and that progress is therefore likely to be slow. Candidates may also argue that some forms of environmental problem created by transport, such as visual pollution, will be completely unaffected by alternative energy sources.

Stronger candidates are likely to deal more explicitly with the specific obstacles to each energy source and the effectiveness of relevant government policy. They are also likely to deal explicitly with the issue of credibility, in other words the extent to which the potential of relevant technologies is likely to be realised on a sufficient scale and with sufficient speed to meet emissions targets that the UK has committed to.

Evaluation of the case for electric cars is likely to consider the fact that electric cars are more expensive than petrol equivalents, thus the concept of price elasticity of demand will be useful in examining the impact of government subsidy. Income elasticity will also be relevant here when

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considering the link between the switch to alternatives by consumers and the link to economic growth. Economies of scale may also be used to argue that the relative prices of fossil-fuelled and electric cars may move closer over time. Practical issues are also likely to be relevant, such as range and charging facilities. Candidates who support their analysis with relevant data, such as the percentage of daily journeys that are within the range of electric vehicles, should be rewarded. Candidates may make the point that the emissions are simply transferred from the vehicle to the power station, although this depends on the efficiency of energy use (approx. 25% better in electric vehicle) and the way in which the vehicle is charged (particularly if it is charged at night).

The issue of electricity generation also offers considerable scope for evaluation with the issue of the practicality of renewable usage likely to be at the fore. Stronger candidates are likely to recognise that the attractiveness of renewables is closely linked to the market price of oil and gas. Political issues relating to the siting and operation of renewable energy sources, and the externalities involved therein, could be discussed, along with the even more contentious issue of nuclear power. Whilst this general discussion is very relevant to the question, candidates should not lose sight of the transport context stated in the question.

Biofuel and hydrogen use could also provide a source of discussion, particularly in terms of the energy used in their production and the extent to which their use is likely to reduce emissions overall.

Candidates may consider the wider context of transport emissions and question whether the use of alternative energy by domestic users in the UK is likely to have a significant impact on emissions. There is no obvious solution to the issue of aviation emissions, for example, and the global transportation of goods may be beyond the influence of UK consumers and legislators. The argument could also be made that the market will inevitably resolve this problem in the medium to long term as the oil price rises and price signals cause economic agents to change their behaviours. In this context, government intervention may even be harmful to the adoption of alternative fuels due to crowding-out.

Alternatively, the argument could be made that the drive toward alternative fuels masks the real problem, which is our over-use of natural resources, of which fossil fuels are but one. More fundamental lifestyle changes than the simple shift from petrol to electric cars are likely to be required to solve global resource depletion issues.

Theory and Analysis

Level 4 (18–22 marks) Mid mark 20	There is clear evidence of a thorough knowledge of the relevance of alternative energy in a transport context. A range of technologies are considered and their impact on environmental problems analysed in depth. At the top end there should be effective use of supporting theoretical concepts.
Level 3 (12–17 marks) Mid mark 15	At least two technologies are analysed, but there will be a lack of breadth or depth in some of the analysis and the answer is more likely to read as a prepared list of costs and benefits rather than a well-structured essay. Lacking critical awareness in some areas.
Level 2 (6–11 marks) Mid mark 9	Environmental costs of transport and the potential benefits of alternative energy sources are clearly understood, although the analysis may lack effective use of economic concepts and diagrams. There may be some inaccuracies or oversimplifications and/or limited critical awareness.

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Level 1 (1–5 marks) Mid mark 3	There may well be a misunderstanding of the nature of alternative energy sources and their impact on the environmental problems associated with transport use.
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Evaluation

Here follows a recap of some of the areas that might be included and a breakdown of what will be expected at the various Levels.

Issues include:

- Do the advantages of alternative energy source outweigh their disadvantages?
- Will adoption of alternative energy source in a transport context be relatively rapid and widespread?
- Can the specific obstacles related to individual technologies be overcome?
- Does the switch to electric vehicles simply displace the emissions?
- Is government intervention helpful?
- Are aviation emissions a bigger problem for which alternative energy technology has no ready solution?
- Will the market solve the problem anyway?
- Are more fundamental changes to our lifestyles required?

Level 3 (13–18 marks) Mid mark 16	Given the length of this paper, to achieve this level of evaluation there must be significant and comprehensive coverage of several relevant areas. At the top end of this Level, there will signs of real in-depth research and/or originality. In all cases there will be a clear conclusion drawn at the end that relates specifically to the set question.
Level 2 (7–12 marks) Mid mark 10	At least two relevant issues will be considered in reasonable depth but the overall scope of evaluation leaves areas unexplored and conclusions may lack any rigorous justification.
Level 1 (1–6 marks) Mid mark 4	Some of the issues that could be open to evaluation may be introduced into the discussion but there is no attempt to go further than to show an appreciation of the issue – for example, 'electric vehicles reduce emissions but are too expensive and unpopular with consumers'. There is no attempt to draw together the relevant issues in a conclusion.

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2 China and the global economy

Evaluate the extent to which China's future economic growth potential is limited by domestic supply constraints. [40]

Candidates should demonstrate their understanding of supply constraints and their impact on economic growth. They should understand the nature and extent of China's factor endowments. They should also consider the extent to which these endowments can change over time and analyse the factors that will affect future factor endowments. They should illustrate their answer with specific examples relating to individual factors. They should use appropriate analytical tools and data to support their arguments. They should be able to come to a clear and supported conclusion on the extent to which factor endowments in the present and future will place limits on economic growth. Good candidates are likely to explicitly consider the issues relevant to each factor. Analysis may be assisted by the use of diagrams.

Answers may include:

Knowledge and understanding of supply constraints and the link with economic growth.

Examples:

- Factors of production;
- Economic growth and its determinants.

Application of supply constraints in a Chinese context.

Examples:

- Land – fertile agricultural land, natural resources, energy generation;
- Labour – quantity, age profile, mobility, qualifications;
- Capital – quantity, flexibility, restrictions on movement;
- Enterprise – business culture, attitude to risk, government support.

Analysis of the influence of supply and constraints relating to supply on economic growth in China.

Examples:

Link between factor endowments and growth:

- Productive potential of the economy
- Supply-side of the economy

Supply constraints, including;

- Limited natural resources
- Limited energy resources
- Potential shortage of food
- Ageing population
- Skill shortages
- Mobility

Candidates should be rewarded for supporting their analysis with diagrams. For the higher analytical marks candidates should be able to support their answer with relevant data on, for example, the specific issues relating to individual factors.

Evaluation of the extent to which supply constraints will place limits on economic growth.

At the lower end, candidates are likely to conclude that limited resources will always place some limits on growth. Reference may be made to specific examples of limits relevant to China and the impact they may already be having on economic growth potential. There is not likely to be an explicit recognition of the dynamic nature of resource development and use.

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At higher levels candidates will recognise that this issue is more complex and has a global dimension. Examples of relevant arguments include:

- The ability of the Chinese economy to command the supply of factors from other economies, particularly raw materials. They may cite the efforts made by China to gain access to, and even control of, mineral resources in, for example, East Africa and Southern Asia.
- The ability of firms to innovate, discovering new technological solutions which ease or remove the limits placed on economic growth by depleted resources
- The ability of firms to find new reserves of natural resources and/or develop cost effective methods of extracting known reserves.
- The role of the market in making unprofitable resources and technologies more economically viable over time.

Candidates may also discuss the way in which factors are managed and developed within China, specifically:

- Energy resources, and the extent to which China can reduce its dependence on fossil fuels
- Labour shortages, and the extent to which the Chinese education system can anticipate and provide
- Lack of labour mobility and the ability of the state to direct labour resources
- The ageing population and the extent to which savings ratios may change over time.

Sustainability is likely to be a key concept in evaluation, primarily in terms of keeping Chinese growth at current levels for the foreseeable future. Candidates may consider the extent to which state planning contributes to or mitigates against sustainability.

Candidates may also consider other factors that could place limits on growth before the Chinese economy faces a shortage of factors of production. The health of the global economy, particularly global demand for Chinese exports, trade imbalances and currency wars could all be relevant in this context. Internal factors relevant to the Chinese economy could also be discussed, including resistance to full market reform and the possibility of political and social unrest.

Theory and Analysis

Level 4 (18–22 marks) Mid mark 20	The answer shows a thorough understanding of the limits within most factor markets. There will be balanced and in-depth analysis which links these limits to economic growth. At the top end of this Level, there is likely to be a clear indication of the magnitude of these limits and a timescale over which they are likely to have an effect.
Level 3 (12–17 marks) Mid mark 15	A good understanding of at least two factor markets. However, there is a lack of breadth or depth in some of the analysis and the answer is more likely to read as a prepared list of issues rather than a well-structured essay. Lacking critical awareness in some areas.
Level 2 (6–11 marks) Mid mark 9	Some understanding of the effects of supply constraints but possibly considering a narrow range of arguments or lacking clear awareness of the current context. Any analysis will be very superficial, for example, arguing that limited energy resources within China at present must place a brake on growth.
Level 1 (1–5 marks) Mid mark 3	There is little understanding of why supply constraints could place limits on Chinese growth.

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Evaluation

Here follows a recap of some of the areas that might be included and a breakdown of what will be expected at the various Levels.

Issues include:

- Will supply constraints limit growth in the Chinese economy?
- Will China be able to secure sufficient factors in global markets?
- Will exploration and technology keep pace with global demand for resources?
- To what extent will the market mechanism automatically regulate supply of scarce resources?
- Can China effectively manage its factors to ensure sustainable growth?
- Does state planning increase or decrease sustainability?
- Will other issues intervene to curtail China's economic growth?

Level 3 (13–18 marks) Mid mark 16	Given the length of this paper, to achieve this level of evaluation there must be significant and comprehensive coverage of several relevant areas. At the top end of this Level, there will signs of real in-depth research and/or originality. In all cases there will be a clear conclusion drawn at the end that relates specifically to the set question.
Level 2 (7–12 marks) Mid mark 10	At least two relevant issues will be considered in reasonable depth but the overall scope of evaluation leaves areas unexplored and conclusions may lack any rigorous justification.
Level 1 (1–6 marks) Mid mark 4	Some of the issues that could be open to evaluation may be introduced into the discussion but there is no attempt to go further than to show an appreciation of the issue – for example, 'China has limited endowment of factors so this must, at some point, place limits on growth'. There is no attempt to draw together the relevant issues in a conclusion.

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3 Expansion of the EU

Evaluate the extent to which a single market exists in the enlarged EU. [40]

Candidates should demonstrate a clear understanding of the concept of a single market. They should be familiar with the specific details of EU enlargement and the member states involved. Candidates should be familiar with the various aspects of the Simple European Market (SEM), notably goods, services, labour and capital. They should also be aware of the impacts of enlargement on each of these markets. They should use appropriate analytical tools and data to support their arguments. They should reach a clear and well-supported conclusion on the extent to which a single market exists in the EU and the extent to which enlargement has had an impact on the single market. Good candidates are likely to explicitly consider the impact on specific markets and among different groups of member states. Analysis may be assisted by the use of diagrams.

Answers may include:

Knowledge and understanding of the single market and EU enlargement.

Examples:

- The nature of the SEM and the rationale behind its creation;
- The scale and time-frame of the enlargement process and the states involved.

Application of the single market in the context of enlargement.

- The impact on goods, services, labour and capital markets of the enlargement process
- Examples of impacts on specific markets and/or member states

Analysis of the conditions required for the establishment of single markets, the process of creating such markets and the effects of enlargement.

Examples relating to conditions and the process:

- Liberalisation of markets for goods and services:
 - Removal of non-tariff barriers
 - Legal, technical and fiscal harmonisation
 - Competition policy
 - Price convergence and arbitrage
- Liberalisation of labour markets:
 - Free movement of labour
 - Regulatory harmonisation
 - Shengen Agreement
 - Wage convergence and market flexibility
- Harmonisation of capital markets:
 - Increased scale and flexibility
 - Impact on the banking sector
 - Interest rate convergence

Examples of the effects of enlargement:

- Increased size of markets
- Increased movement of some factors
- Lack of completely free movement of labour
- Increased diversity of legal, technical, regulatory and fiscal systems

Candidates should be rewarded for supporting their analysis with diagrams. For the higher analytical marks candidates should be able to support their answer with relevant data on the effectiveness of movement towards a single market prior to and following enlargement.

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Evaluation of the extent to which a single market currently exists in the enlarged EU.

Evaluation is likely to consider whether the single market has actually been achieved across all member states and in all markets. Conclusions are likely to suggest that progress has been made but that inconsistencies remain. Examples may be given to illustrate this point.

Stronger candidates are expected to consider in detail specific effects on individual markets. In the case of product markets they may wish to critically examine the extent to which price convergence has been achieved. They are likely to conclude that harmonisation of goods markets is easier to achieve than in markets for services. However, price convergence has been more apparent in some goods markets than others and candidates may discuss why this has been so, considering factors such as information, value proportional to income, price elasticity, portability, etc. Candidates may point out that harmonisation is far from being achieved in some markets even within the EU-15, for example markets for energy. They may go on to discuss the reasons for this, including political and institutional resistance. A discussion of the extent to which EU competition policy has been effective in furthering harmonisation would also be relevant here.

Candidates should also consider the extent to which the enlargement has moved the EU closer towards a true single market or further away from it. Labour markets are clearly a relevant example in this context. Enlargement has led to a more flexible single labour market for some member states, but not for others, depending on their willingness to allow access to labour markets for nationals of all new member states. Candidates may consider the extent to which, for example, increased mobility of labour has, or has not, been beneficial to individual member states. Whilst this debate is relevant, it should not be the central focus of discussion and candidates should stick to the question.

Candidates may ultimately consider the extent to which achievement of SEM is desirable and realistic. They may conclude that enlargement has had relatively little impact on a policy aim that was unlikely to be realised anyway.

Theory and Analysis

Level 4 (18–22 marks) Mid mark 20	The answer shows a thorough knowledge of the conditions required for the SEM to exist, the process involved in creating it and the effects of enlargement. There is coverage a wide range of conditions and the problems created by enlargement are thoroughly analysed using relevant economic theory. At the top end of this level there should be supporting data relevant to specific markets and member states.
Level 3 (12–17 marks) Mid mark 15	Conditions in at least two markets are analysed and some implications of enlargement considered. However, the analysis lacks breadth or depth and is more likely to read as a prepared list of advantages or disadvantages, possibly restricted to a few key issues and may generalise about the effects across all member states. Lacking critical awareness in some areas.
Level 2 (6–11 marks) Mid mark 9	Some limited appreciation of the SEM and the impact of enlargement. Likely to be general points related to a narrow range of markets. Limited critical awareness.
Level 1 (1–5 marks) Mid mark 3	There is a lack of understanding of the SEM and/or what is meant by EU enlargement.

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Evaluation

Here follows a recap of some of the areas that might be included and a breakdown of what will be expected at the various Levels.

Issues include:

- Has SEM been achieved in all markets and across all member states?
- What is the current level of harmonisation in each market?
- Which factors have limited convergence?
- To what extent has government intervention facilitated or prevented convergence?
- To what extent has EU competition policy been sufficiently robust to ensure convergence?
- Is the SEM a realistic and desirable objective?
- To what extent has enlargement increased or reduced the pace of progress towards SEM?

Level 3 (13–18 marks) Mid mark 16	Given the length of this paper, to achieve this level of evaluation there must be significant and comprehensive coverage of several relevant areas. At the top end of this Level, there will signs of real in-depth research and/or originality. In all cases there will be a clear conclusion drawn at the end that relates specifically to the set question.
Level 2 (7–12 marks) Mid mark 10	At least two relevant issues will be considered in reasonable depth but the overall scope of evaluation leaves areas left unexplored and conclusions may lack any rigorous justification.
Level 1 (1–6 marks) Mid mark 4	Some of the issues that could be open to evaluation may be introduced into the discussion but there is no attempt to go further than to show an appreciation of the issue – for example, 'SEM has not been achieved as there are still some markets which are not entirely convergent'. There is most unlikely to be any attempt to draw together the relevant issues in a discussion.

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4 The pensions crisis

Evaluate the extent to which the pensions crisis is an example of market failure and one which demands government intervention. [40]

Candidates should demonstrate an awareness of the nature and extent of the pensions crisis in the UK. They should be aware of the implications of the crisis for workers and taxpayers in the UK. Candidates should demonstrate a clear understanding of market failure and apply that understanding in the context of pensions. They should be able to analyse the nature of the market failure(s) present and the possible interventions available to the government. They should reach a clear and well-supported judgement about the extent to which the pensions crisis is a clear example of market failure and the extent to which government needs to intervene. Good candidates are likely to recognise that there are two clear aspects to this question and their conclusions may well reflect this. Analysis may be assisted by the use of diagrams.

Answers may include:

Knowledge and understanding of the pensions crisis and market failure.

Examples:

- The problem of under-provision;
- Impact of under-provision;
- The nature of market failure.

Application of market failure to the crisis.

Examples:

- Pensions as a merit good;
- The role of information failure in the market;
- Positive externalities relating to pension consumption;
- The impact of monopoly power on the pensions market;
- The influence of inequity on the crisis;
- The role of rational behaviour.

Analysis of the impact of market failure on pension provision and the methods available to government to deal with this failure.

Examples:

Impact of market failure:

- Under provision due to information failure and the existence of positive externalities;
- The impact of market power and asymmetrical information;
- Under provision among those on lower incomes;
- Under provision due to irrational consumer behaviour.

Government intervention currently in place and options for future policy:

- Information provision and consumer support;
- State pension provision;
- Role of The Pensions Regulator and the FSA;
- Compulsory pension enrolment;
- Tax incentives on pension contributions and savings;
- Means-testing of pension benefits.

Candidates who use diagrams to support their analysis should be rewarded. For the higher analytical marks candidates should be able to support their answer with relevant data regarding, for example, the extent of the problem and the specific nature and impact of intervention.

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Evaluation of the extent to which the pensions crisis is a clear example of market failure and evaluation of the extent to which government is obliged to intervene.

Basic evaluation is likely to conclude that there is at least some degree of market failure because there is clearly under-provision. There may be some discussion of the precise nature of this failure. Candidates may not explicitly deal with the second part of the question or may simply conclude that government intervention is required in order to deal with this failure and that previous intervention has clearly been inadequate.

At higher levels candidates should be able to very clearly identify the nature and extent of the market failure present. They are likely to explicitly deal with the extent to which the crisis can be explained by market failure alone or whether other factors are involved. Government failure may be suggested as an alternative cause and students who can elaborate on this point and accurately debate the nature and extent of this failure should be rewarded. At the highest level students should be able to support their conclusions with research findings. Candidates may also deal with the phrase 'clear example' in the questions and may profitably debate the extent to which the market failures identified are 'clear' or not.

Candidates may even question whether there is a crisis at all and may discuss the subjectivity of the concepts of merit goods and positive externalities. They may question the assumption that under-provision by individuals is an example of information failure and/or irrational behaviour and consider the impact of government pension provision on the rational expectations of consumers.

Stronger candidates must deal with the two parts of the question in turn. On the topic of government intervention they may discuss the extent to which government intervention has succeeded in correcting the market failure to date and enter into informed speculation about the likely success of future interventions. This debate could also be successfully linked with government failure.

At higher levels candidates are likely to deal explicitly with the extent to which the government is **obliged** to intervene. They may well question the severity of the failures concerned and their impact on both the micro and macro economy.

Theory and Analysis

Level 4 (18–22 marks) Mid mark 20	The answer shows a thorough knowledge of the crisis and a good range of market failures are dealt with in depth. The effects of policy responses are also covered and analysed in detail using appropriate concepts. At the top end candidates are likely to use data to support their reasoning.
Level 3 (12–17 marks) Mid mark 15	The answer shows a good understanding of crisis, the impact of a range of relevant market failures and the measures taken by government to deal with these failures. However, the analysis lacks breadth or depth and is more likely to read as a prepared list of advantages or disadvantages rather than a well-structured essay. Lacking critical awareness in some areas.
Level 2 (6–11 marks) Mid mark 9	There is some understanding of market failure in the context of pension provision but the analysis is superficial and likely to focus on only one aspect of market failure. Limited critical awareness.
Level 1 (1–5 marks) Mid mark 3	There is a lack of understanding of the pensions crisis and/or market failure.

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Evaluation

Here follows a recap of some of the areas that might be included and a breakdown of what will be expected at the various Levels.

Issues include:

- Is under provision caused by market failure?
- What is the nature and extent of this failure?
- What other factors are involved?
- How significant are these other factors?
- Is there evidence of government failure?
- Is this a 'clear example' of market failure?
- How subjective are the concepts of market failure?
- To what extent is government **obliged** to intervene?

Level 3 (13–18 marks) Mid mark 16	Given the length of this paper, to achieve this level of evaluation there must be significant and comprehensive coverage of several relevant areas. At the top end of this Level, there will be signs of real in-depth research and/or originality. In all cases there will be a clear conclusion drawn at the end that relates specifically to the set question.
Level 2 (7–12 marks) Mid mark 10	At least two relevant issues will be considered in reasonable depth but the overall scope of evaluation leaves areas unexplored and conclusions may lack any rigorous justification.
Level 1 (1–6 marks) Mid mark 4	Some of the issues that could be open to evaluation may be introduced into the discussion but there is no attempt to go further than to show an appreciation of the issue – for example, 'market failure clearly exists so government is obliged to intervene.' There is no attempt to draw together the relevant issues in a conclusion.