Qurious

Education

2018 Edexcel Economics Paper 3
Synoptic Paper

Model Answers

This document is helpful for longer essay questions/responses. Please reference the Mark Scheme for answers to Multiple Choice questions.

Pearson
Edexcel

Examiners' Report
June 2018

GCE Economics A 9EC0 03

ResultsPlus

Question 1 (a)

Many candidates scored well on this question (mean 3.8/5), with the analysis mark being the main discriminator. For the fifth mark, candidates needed to go beyond listing characteristics of the market structure identified and instead develop the explanation, for example, by explaining interdependence or identifying price rigidity. If the candidate chose monopoly they could earn the 5 marks but they tended to be less able to talk about the process linking the market structure to the behaviour or the firms, or any other analytical process.

Over 67% of answers scored 4 or 5 out of 5, meaning that most candidates were confident in the area of market structures.

A significant number of candidates took the approach of describing a legally-recognised monopoly, either the 25% CMA figure or the more relaxed EU definition (40% of the market is unlikely to be a dominant position, Article 102 of TFEU – both definitions were equally acceptable), although the *legal monopoly* had to be clearly linked to the concept of market power or dominance rather than pure monopoly power to gain full marks. Candidates using the oligopoly approach found accessing full marks very straightforward when accompanied by a calculation of concentration ratios and a brief development of the explanation of the market structure.

Oligopoly was the most common answer – and the evidence fitted well with this approach.

(a) With reference to Figure 1, briefly explain the market structure that best describes the UK branded coffee shop market.

(5)

The UK branded coffee shop market is best described ~~[illegible]~~ oligopoly market structure, as there's a collection of firms, who have some market power, and some say within the market. The 6 firm concentration ratio is 71%, ~~and~~ which suggests there is a limited number of firms ~~at~~ who have some market power. Firms are likely to engage in ~~some~~ non-price competition, for example loyalty schemes, in order to retain customers. An oligopoly market structure will also mean the firms are producing a similar range of goods and services, however there's may be some ~~[illegible]~~ ~~price~~ product differentiation. For example, the use of branding.

ResultsPlus
Examiner Comments

This is a clear 5/5.

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Examiner Tip

Calculate the concentration ratio and if five or fewer firms have 50% of the market then you know it is oligopoly.

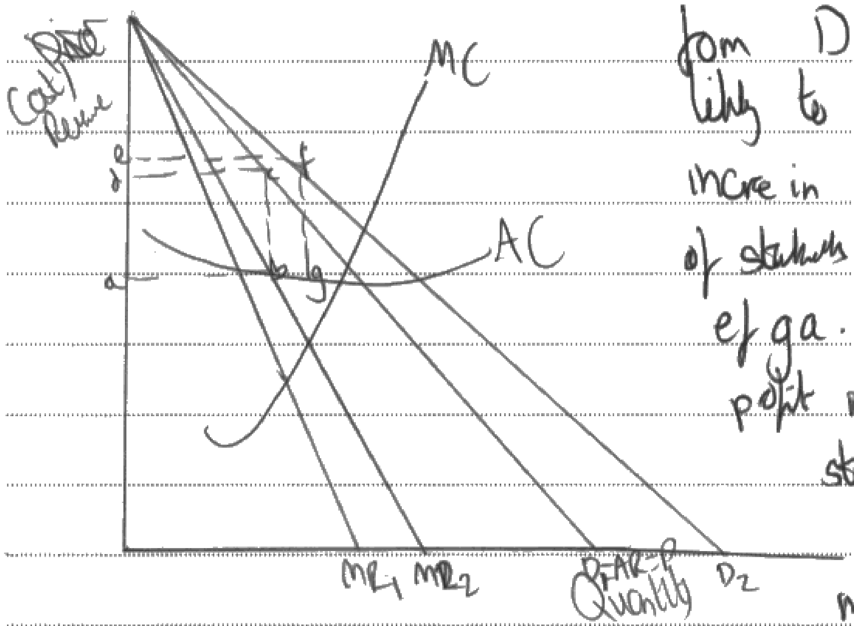
Question 1 (b)

Although there are several faults in this answer, it still gains full marks.

(b) With reference to Figure 3 and other information provided, discuss the price and non-price strategies that Starbucks may use to increase profitability.

(12)

Starbucks has 13% market share, it may try to increase its profitability by reducing the cross elasticity of demand of its products by engaging in non-price competition & non-pricing barriers. Starbucks may use a loyalty scheme which encourages repeat custom or advertise the unique qualities of its coffee beans. This should help to differentiate Starbucks from the other firms in the market. This differentiation should reduce the cross elasticity of demand between starbucks coffee and its competitors, enabling it to increase the price without causing a contraction in demand. This change in demand

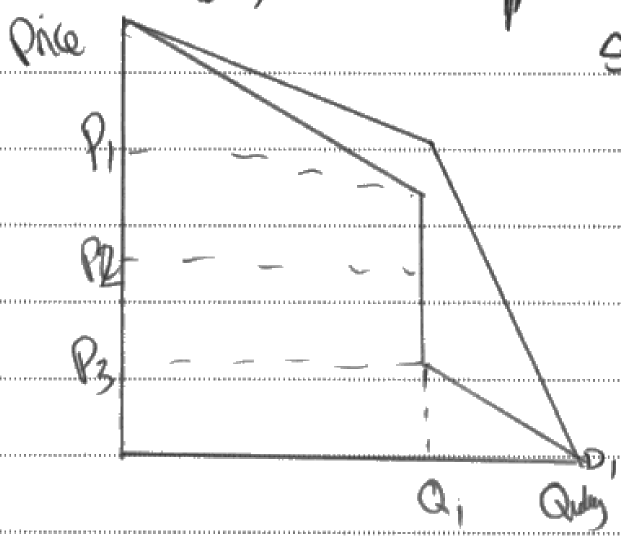


from D_1 to D_2 is likely to lead to an increase in the supernormal profit of starbucks from abcd to efga. This increased supernormal profit may be reinvested by starbucks to achieve dynamic efficiency & organic growth moving closer to productive & allocative efficiency & increasing future profitability.

However, the non-price strategy may not be successful at increasing profitability as any marketing is unlikely to take ~~cop~~ customers away from Macdonalds when offers espressos at £0.99, less than half the price of the Starbucks alternative. Moreover, other firms may also use similar non-price competition strategies which will reduce the impact of the Starbucks strategy.

In the short term starbucks may try to compete on price to increase future profitability. Starbucks may use predatory pricing, ~~to do~~ this is where starbucks takes advantage of its economies of scale & low average costs to set prices at below the average costs of smaller firms such as Pret-a manger with only 5% market share, this may lead to them reaching their long run shut down point if Average Total costs are greater than average revenue, this reduces competition in the market & allows starbucks to increase its price in the future due to less competition leading to increased profitability.

However, as the Coffee market is an oligopoly with a ~~so~~ ~~Starbucks is unlikely to be~~ CR5 of 66% so Starbucks is unlikely to use ~~p~~ price strategies to increase profitability. If starbucks chose to increase its prices, up from the £2.80 for a large latte then demand is price elastic above a set point so demand would fall drastically leading to a reduction in profits. Similarly, if Starbucks chose to reduce its price



demand is price inelastic as others follow the price fall leading to a price war & a reduction in profitability in the long run.

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Examiner Comments

This fulfils all the assessment objectives and demonstrates many of the points above.

Evaluation was often effective on this question, with better answers giving context to their answers and using the case study to help them e.g. referring to brand issues of Starbucks, and the damage to its reputation caused by the transfer pricing issues; and in evaluation, the observation in the data that the headquarters were moving from Amsterdam to London. There were good examples of kinked demand analysis, used to explain somewhat 'sticky' prices in the cases where Starbucks and Costa are charging the same price for an Espresso Double (Figure 3), which made a very effective evaluation point.

The main problem with the question was the opportunity cost, with candidates spending more than the 12-15 minutes they should allow, which was reflected in a higher than normal frequency of unfinished answers at the end of the paper.

ResultsPlus
Examiner Tip

Check the MC=MR points are extended to the horizontal axis, and if using the kinked demand curve (not required but can be used) then the angle of the MR will change after the kink to become steeper.

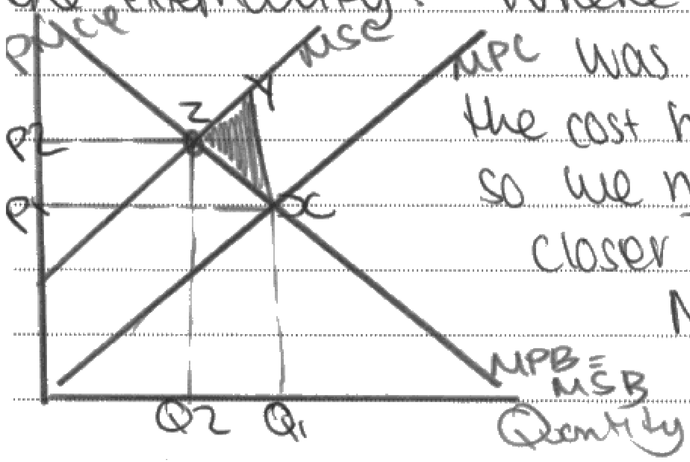
Question 1 (c)

Many candidates tried to use externalities diagrams but faced issues with the fact that negative externalities in consumption is not required for this specification in diagrammatic form. Such an approach tended to lead to confusion and was rarely fruitful, and it is advised that candidates try not to learn diagrams that are specifically not required for this exam.

(c) Examine the advantages of using an indirect tax as a means of reducing the use of disposable coffee cups.

(8)

An indirect tax is on the expenditure of a good. It is a regressive tax usually, so affects the poor more as is a higher percent of their income. One advantage of a indirect tax as means of reducing use of disposable coffee cups is that it internalises the externality. Where as intially, the UK was consuming at Q1, the cost has been internalised so we may consume closer to social optimum, Q2.



MSC represents the marginal social costs, the effects the use of disposable ~~coffees~~ cups on the third party eg CO_2. The indirect tax increases the cost of coffee within that cup, hopefully ~~[illegible]~~ decreasing the demand. It allows the negative welfare triangle, Y, X, Z, to be adressed and hopefully reduced.

However, as suggested in the extract if the increase in price changes coffee from £2.60 to £2.65 it is such a small proportion of disposable income and a small percent of the price of the good that consumers will probably still buy. Therefore, demand won't fall and instead the private costs will still increase.

Another advantage would be the revenue made to the government. An indirect tax on coffee cups would provide tax income to the government which could be used on research and development for cleaner disposable cups and towards reducing the problems already caused.

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Examiner Comments

There are many points to raise in this answer:

- definitions are not required (indirect tax) but they can help the candidate focus on the question.
- reducing the use of cups is in the question and is not therefore a benefit, but the answer is awarded for 'internalising the externality' – a clear benefit in this context.
- the diagram does not show the effect of the tax, and a shift would be an effective way to pick up a second diagram mark. However it does illustrate the social optimum issue and is therefore awarded (deadweight welfare loss area).
- The diagram shows production externalities but the discussion is not explicitly about production. However there is an oblique reference to contraction of demand so credit is given here.

There is enough here to score full marks.

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Examiner Tip

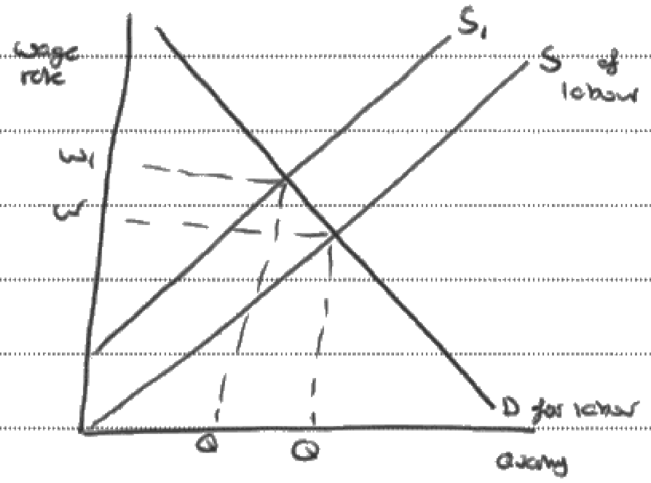
There were several other diagrammatic approaches that were valid, such as negative externalities in production as shown here, and indeed a diagram was not needed at all to gain full marks although it can be an efficient way to score two marks.

Question 1 (d)

This answer tries a range of micro and macro approaches and reaches Level 4 on two occasions. Evaluation does link to the points being made.

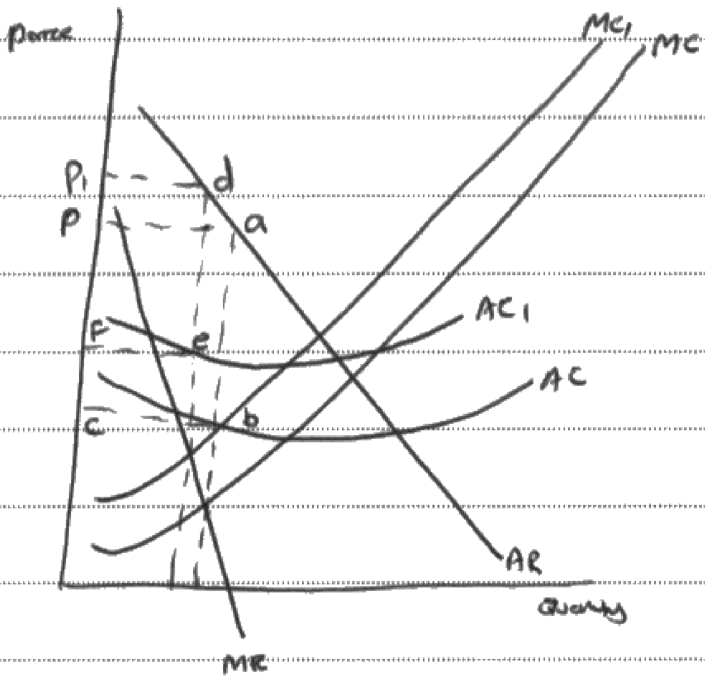
Write your answer here:

One microeconomic factor that might influence whether Starbucks chooses to expand ~~the~~ could be the supply of labour.



If there is a low supply of labour, it is likely to increase the wage rate of workers in that particular country. This could potentially be due to a low participation rate in that country, perhaps if benefits are high and income tax is high. This would increase wages for Starbucks from w to w1. As a result, this could increase their variable costs, as

(next page)

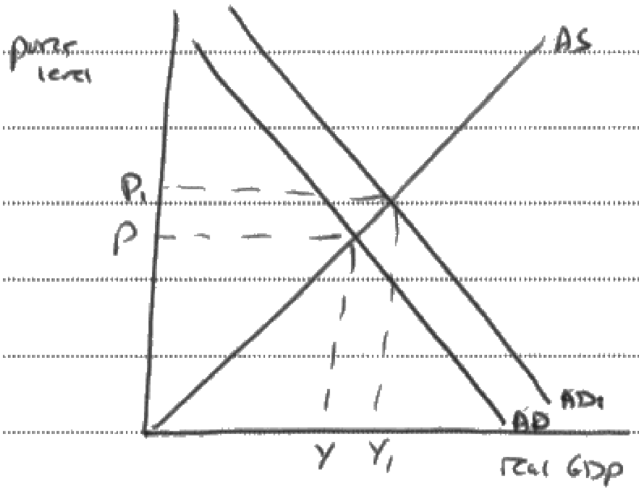


They have to pay more for workers within a country. This could increase AC, and result in a lower area of supernormal profit from pabc to area p1def. This could also raise prices from p to p1, which could be harmful to demand as prices are already above those of Costa and Greggs. The reduced area of supernormal profit could make Starbucks less dynamically efficient, and could leave them with less profit to reinvest into reusable or biodegradable coffee cups, which could cause them to lose out to rivals who may be doing so. This wage rise could also be caused by a national minimum wage, which would particularly raise costs for Starbucks due to its high amount of low skilled workers.

However the impact of this depends on how large the wages are, as only a small increase in wages abroad could be outweighed by other factors, such as less competition. As a result Starbucks may continue to pursue expansion into that particular country. Additionally Starbucks could work a way around higher wage costs, such as by moving to a more capital intensive means of production, which does not require the

~~the~~ need for as high total wage costs. This could be by developing self-serve coffee machines. Wage rates will also increase all firms in the country, and so it may not reduce the competitiveness of Starbucks.

One macroeconomic factor that may be influential could be the interest rate in a particular country. If interest rates are low, like the 0.5% ~~base rate~~ in the UK, then there may be a rise in ~~aggregate~~ consumer spending in that country, as there is less reward for saving in banks. As a result this could lead to higher sales for Starbucks in that country.



This rise in the components of 'C' and ~~a~~ 'I' could result in greater aggregate demand in the country, increasing real GDP from ~~Y~~ Y to Y_1. This could suggest that there may be higher economic growth ~~~~, which could suggest that incomes are increasing and so demand may also increase. The low interest could also ~~~~ make it cheaper for Starbucks to invest themselves into new stores or machinery.

~~~~ ~~~~ High quality infrastructure ~~~~ in a country could also be beneficial for Starbucks, as it would leave them in a better position to transport goods, and could make labour in ~~~~ the country more
~~~~

geographically mobile.

However consumer spending may not increase due to the low interest rates. If there is high unemployment and weak employment protection laws, then there could be high uncertainty amongst consumers, which could reduce consumer confidence and lower the levels of spending. ~~Additionally~~ Additionally there could be an unstable ~~[illegible]~~ financial system in the country, which could reduce the incentive for firms to invest.

This would also increase price levels from P to P1, which could ~~[illegible]~~ increase prices of suppliers in that country, making costs of production and they may have to increase prices themselves.

Overall I would say that there are more macroeconomic factors to analyse before entering a particular country, as consumer spending, exchange rates, economic growth and inflation will all have ~~this~~ impacts on Starbucks. However the microeconomic factors may be more directly concerning, if the raises costs, but there are things they can do to reduce the impacts of this, such as moving to a capital intensive means of production. Macroeconomic factors are likely to fluctuate in the long run, especially in a developing country, and so Starbucks may not be put off by slight macroeconomic differences in the short run.

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Examiner Comments

Level 4 15/16 KAA.

Level 3 evaluation – just makes Level 3, therefore 7/9 Eval.

= 22/25.

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Examiner Tip

Use diagrams and data to support your response. Evaluation must try to link to your points made.

Question 1 (e)

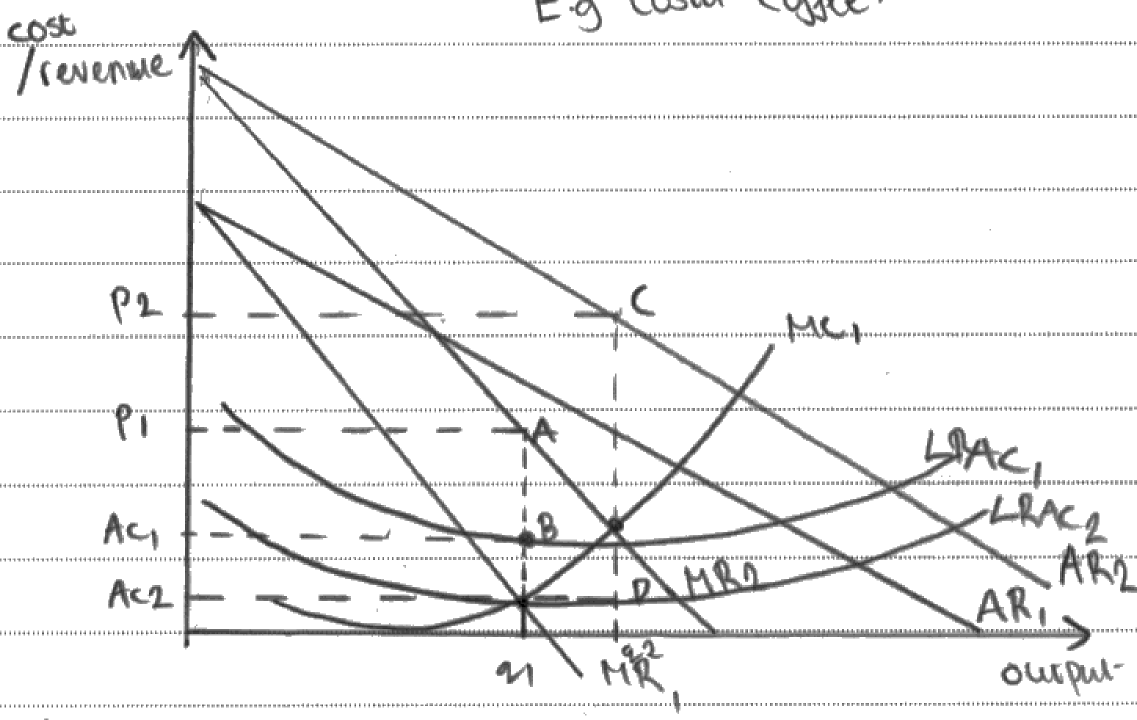
This is a wide ranging and carefully reasoned answer. It is fully applied and the diagrams are relevant.

Write your answer here:

One likely impact of increased UK demand is increased profitability. since it is an increase in demand for coffee as a whole this may lead to external economies of scale. There may be an improvement in anchillary/supporting industries such as the ~~disposa~~ multi-use cup market, this may lower long run costs of production as many coffee shops can benefit due to lower cup prices and better transportation infrastructure. ~~For example the number of coffee shops has increased from 1225~~

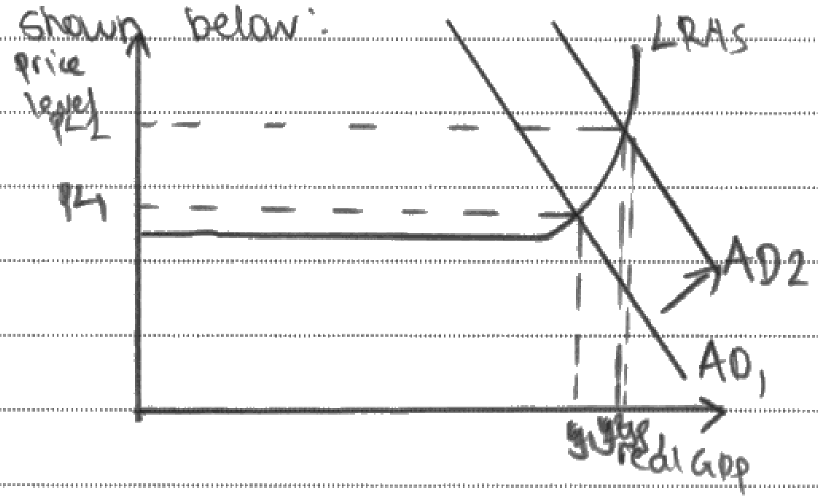
This coupled with increased consumer demand also could leads to an increase in average and marginal revenue for coffee shops, for example Starbucks in the UK has increased from 1 outlet in 1998 to 849 UK outlets currently. these impacts can be shown below:

E.g costa coffee.



This increase in average revenue and fall in long run costs of production means that quantity may increase from q1 to q2 and the fall in costs may lead to a fall from AC1 to AC2, this in turn may lead to an increase in super normal profits from (P1, A, B, AC1) to (P2, C, D, AC2). This extra profit may be reinvested which could to dynamic efficiency in the coffee industry. However, firms such as Costa coffee may not see a large increase in average revenue. The UK coffee market is quite contestable so these increases in consumer demand may result in new entrants entering the market due to low barriers to entry, this could lead to increase consumer choice and competition for large 31% market holders such as Costa and lead to a possibly more monopolistically competitive market especially on a local level, this supernormal profit may increase more for the smaller firms than the larger ones

A likely macroeconomic ~~influence~~ effect could be an increase in aggregate demand and economic growth. This increase in demand for coffee may increase consumption in the UK economy as more people will buy and consume coffee, this may increase SNP for firms as previously mentioned, this could lead to a macroeconomic effect of these coffee firms hence increasing investment, and the government may gain more tax revenues from the corporation tax of coffee firms hence allowing the government to spend more without incurring a larger fiscal deficit. This leads to a multiplied effect on AD as the initial consumption increase could lead to greater G and I, this multiplied increase on AD is shown below:



This increase in AD may lead to an increase in real GDP from Y1 to Y2 hence representing economic growth and an increase in inflation by price level rise from PL1 to PL2. Hence benefitting the UK economy, however the UK has been thought to be close to full capacity by the Bank of England due to a 'loose' labour market, as such this may not lead to significant economic growth as there is little capacity for this hence it is more likely to lead to demand-pull inflationary pressures as seen by above target inflation, this point is even more valid from a classical viewpoint as they believe the economy is always at full capacity in the long run hence it may just lead to inflation and not economic growth.

In judgement, in the short run this increase in consumer demand may increase large coffee companies e.g. Starbucks profitability, but over the long run new firms may simply enter the relatively contestable coffee market so in the long run major coffee firms may not reap the benefits. Furthermore the microeconomic effect is more considerable than the macroeconomic effect as coffee is a relatively small part of the UK economy. Weighing up the evidence, it is likely the size of the coffee sector will increase and demand-pull inflation will occur.

ResultsPlus
Examiner Comments

There are clear Level 4 passages, with carefully argued chains of reasoning, fully in context. There is a sound judgement after each piece of KAA, and a judgement at the end to consider the overall impact.

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Examiner Tip

25/25 is clearly deserved, even though the answer is not over-long or complex. Simple is good.

Question 2 (a)

This example shows how to earn full marks.

(a) Using the data in Figure 4 and other information provided, explain the likely change to Indonesia's terms of trade since 2011.

(5)

Terms of trade is how much needs to be exported in order to pay for all the imports. The fall in coal price from $125 to $50 would damage Indonesia's terms of trade as more coal now needs to be exported to generate the same revenue to purchase the imports.

$$\text{terms of trade} = \frac{\text{index of exports}}{\text{index of imports}} \times 100.$$

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Examiner Comments

The formula is not perfect (no reference to prices) but prices are discussed in the answer so the outlining of the meaning of the terms of trade is valid.

ResultsPlus
Examiner Tip

Terms of trade worsening might mean the balance of trade actually improves. Don't be caught out by these apparent contradictions. It is this kind of reasoning that makes economics a logical challenge, and therefore very enjoyable.

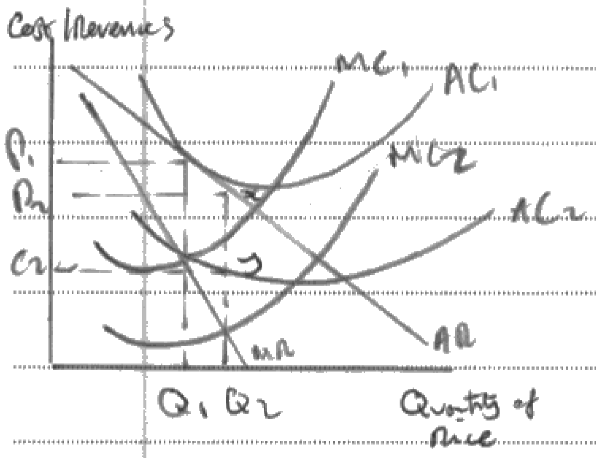
Question 2 (b)

This is a short, clear and effective answer.

(b) Examine the likely effects on the profitability of Indonesian rice farmers of the government's increased investment in dams (Extract E, lines 43-48). Use a cost and revenue diagram to support your answer.

(8)

The increased Gov investment in dams will most likely lead to a fall in variable costs for Indonesian rice farmer. This leads to both MC and AC shifting downwards for firms. Assuming farmers profit maximise, they will go from making normal profit at P1 to a super normal profit of P2, x, y, C2.



This clearly indicates an increase in profitability as farmers now have the ability to make supernormal profit, meaning they can be dynamically efficient and so can fund investment in the future, allowing the profitability to stay sustainable with a permanent reduction in costs.

However the market for rice could be considered ~~[illegible]~~ perfectly competitive, therefore in the long run, low barries to entry allows new entrants, increasing quantity supplied, lowering the price. Firms being price takers means that only normal profit can be made.

ResultsPlus
Examiner Comments

The diagram is clearly labelled. The text describes the diagram. There is a clear paragraph set apart for evaluation. This is a joy for an examiner to read.

ResultsPlus
Examiner Tip

Note that you can also score all the marks using a shift in just the FC or AC, although you must be careful not to describe a change in VC and draw just a change in fixed costs, and vice versa.

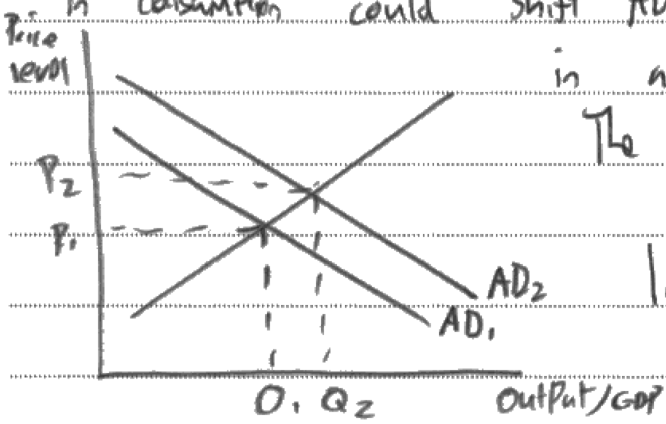
Question 2 (c)

This answers well in terms of KAA, seeing a variety of types of aid and applying them well in the context of the data on Indonesia.

(c) Discuss the benefits of aid to Indonesia.

(12)

One Benefit of Aid to Indonesia is The improved Education and Healthcare, Extract D States That Aid will allow ~~For~~ for free health care at the Point of access for the poorest 88million People. This will improve the health of the nation allowing People to Seek medical help for accidents and injuries, and reduce disease. This would ~~[illegible]~~ result in a more fit and able work force, increasing The amount of People able to work. ~~This~~ As a consequence of The The Productivity of businesses could increase as less workers will be negatively effected by injury or illness. Increased Productivity would lead to higher Profits being made by firms as more is be efficiently Produced. As a result of higher Profits wages of workers could be increased resulting ~~[illegible]~~ in a higher disposable income which could be spent within The economy. This increase in consumption could Shift AD to the Right resulting in an increase in output and The GDP of indonesia.



Improved Education could also have large Benefits for indonesia. Extract D Says That Aid allows for free Schooling up to the age of 12 and tersory eduction for Students accepted into university. An increased eduction in the indonesian Society would allow

More people to have access to higher paying jobs which require higher qualifications. With more people earning increase wages consumption would increase shifting Aggredemand to the right resulting in an increased GDP and economic growth. ~~Further more~~ A higher level of income Tax would also be able to be collect further contribution to Government Revenue. Increased Eduction could also lead to an increase in Technological and medical advances which could improve the nation health or increase Productivity.

Furthermore another Benefit of Aid to indonesia is rebuilding The damage done by The Earthquake and Tsunami in 2004 ~~The damage done~~ By Fixing This Production is able to increase and people can have access to new homes. Increased Spending on infrastucture Through a aid would also make it easier for people to commute to work

ResultsPlus
Examiner Comments

The diagram was useful, if not fully labelled, and there was Level 3 analysis throughout.

Unfortunately there is no evaluation at all – the candidate has possibly run out of time. Two good points are often better than three unjudged ones.

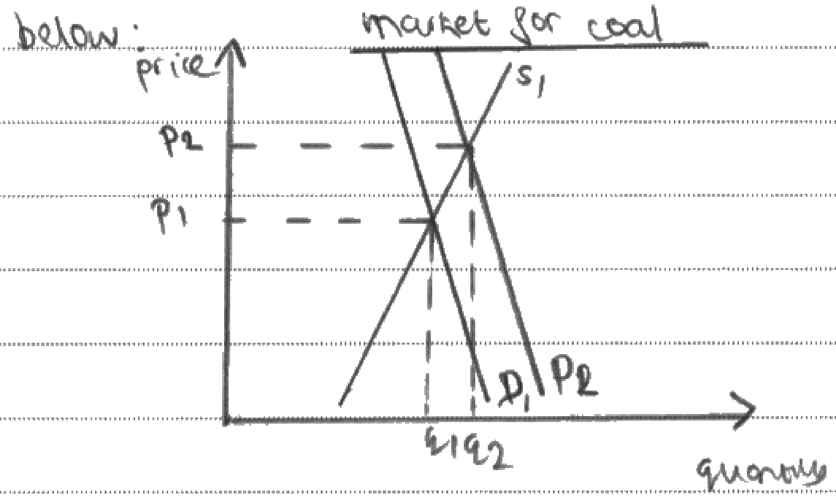
ResultsPlus
Examiner Tip

Evaluate each point as you go along, if you can, and shape your answers around the data provided.

Question 2 (d)

This response is full of data, theory and clear development of economic analysis.

One likely microeconomic effect is a lack of investment in ~~the~~ volatile commodity industries. For example coal has ~~both~~ relatively price inelastic demand and supply as a result these commodity industries can have huge fluctuations in total revenue as shown below:



For example if there was an increase in demand for coal ~~then~~, due to a country demanding more to a fill a temporary energy shortage, then price rises from p1 to p2 and quantity increases from q1 to q2 this lead to an increase in total revenue in the Indonesian coal market from ~~(PXQ)~~ TR = P×Q

∴ ($P_1 \times Q_1$) to ($P_2 \times Q_2$). This small change in demand has lead to a proportionally greater increase in price than change in quantity. These volatile prices hence lead to coal firms and commodity farmers such as rice having very uncertain incomes as a small change in demand (increase or decrease) has a huge impact on the total revenue they earn. As a result coal firms will be uncertain about the future as incomes change hence hold off on much needed investment. For example coal now sells for \$50 per tonne as opposed to \$125 in 2011. As a result this lack of investment could lead to lower supernormal profits and worse quality for consumers. Due to a lack of investment in these industries the firms may not be able to have the best capital and most efficient production methods, hence they may not be able to provide as high quality a commodity as if they had stable prices and investment, thus limiting dynamic efficiency. These volatile commodity farmers could also fall into absolute or relative poverty when the price falls. However as the Indonesian economy grows and develops the financial sector may improve and as a result there may be future markets developed for volatile commodity prices. The use of call and put options can be used in commodity markets to set a price for future delivery, this could then lead to less uncertainty in incomes for these commodity farmers / firms hence resulting in more investment, more quality and lower cost of production.

~~Anoa~~

The macroeconomic effect again is it causes a lot of uncertainty. Due to volatile commodity prices, export revenues can vary significantly e.g through lower coal prices export revenue may fall as coal is relatively ped inelastic. This fall in export prices means that there is a lower demand for the rupiah, as seen by the "30% depreciation since 2013", so the volatile commodity prices can lead to huge swings in current account position currently around "2% of GDP", and volatile exchange rates. This again leads to very volatile investment in Indonesia, investors may decide to buy the rupiah when the exchange rate is weak in the hope that it will rise in value to make a profit and sell when at its peak. This leads to a huge speculative buying and could create a market bubble for the rupiah which could lead to huge swings in aggregate demand due to currency value being a huge influence on (x-m). Indonesia may consider short term managed exchange rate in order to reduce this volatility. Furthermore the government collects tax receipts from corporation tax on these industries such as crude oil, rubber and tin, this again leads to volatile fiscal positions and could lead to overly cautious 'tight' fiscal policy from the government as they need to save some tax receipts in order to boost the economy through fiscal stimulus'. All this volatility and uncertainty can lead to huge variations in growth and development in Indonesia as when prices are high all macroeconomic indicators will be positive but when it's low these indicators will worsen. However, despite this volatility the Indonesian real GDP has grown by an average of 6% since from 2004-2014, despite the collapse in commodity prices they still had a large and respectable 4.8% growth in 2015 which was the lowest since 2009. This may be a large change, but it is still large positive growth. Furthermore through sound governance the volatility has been offset somewhat, they are fiscally tight during the boom stages of high commodity prices so they can provide huge government spending in slowdowns to offset the weak exports in low price times.

In judgement, the macroeconomic impacts are much more severe, this volatility can cause huge current account fluctuations and currency fluctuations which is really worrying for this economy, ~~research~~ this is because too high a proportion of their exports are volatile. They should consider diversification into services or the Lewis model of industrialisation to reduce the effect of external shocks. The microeconomic impact is still important but it is

offset somewhat by government provision of
dams for some volatile monies leading to investment

![ResultsPlus Examiner Comments]

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Examiner Comments

Although it seems that the answer is going to focus on causes not effects of volatility, it is soon clear that the correct focus is there, and the diagram clearly illustrates the impact of low PED on revenues. This is then clearly explained in the text ('uncertain incomes') and the data on coal prices is central to the answer. The Lewis model is used effectively and there are clear micro and macro points.

Question 2 (e)

The case study gave several supply side policies to evaluate the economic effects of, with discussion of education/healthcare, deregulation and opening up to FDI commonly used. Many candidates were then able to apply this knowledge to theoretical models, such as AD/AS, demand and supply and monopoly diagrams in order to provide in depth analysis in the context of Indonesia.

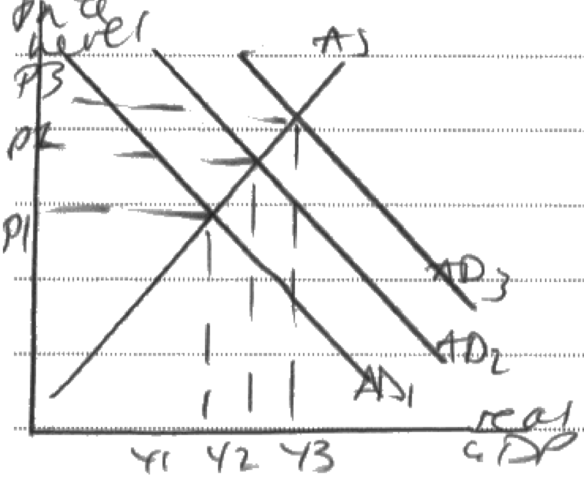
There were a surprising number of answers that shifted AD rather than LRAS. Whilst the effects of supply side policies can clearly have side effects on AD, the more coherent arguments focused on LRAS for the macroeconomic effects given. Rises in AD while of course valid (and on the mark scheme) were unlikely to be convincing when developed into a rise in inflation (given the increase in AS), and some candidates then went on to discuss the costs of inflation, including menu costs, which was highly ineffectual in the context given.

Candidates had clearly learned some downsides of supply side policies, but again the best answers would put these in the context of Indonesia (e.g. the fiscal constraint they face). Extract D clearly spelt out supply side policies (easing regulations, tax incentives and SEZs) and these formed the ideal basis for an essay. In evaluation, one of the most effective answers was to consider the social and fiscal implications of these specific measures.

This essay struggles at first to make it into Level 4 as the focus seems to be on the AD shift. However the chains of reasoning are logical, and clearly an AD shift is legitimate for interventionist supply side policies if government revenue remains constant.

Supply-side policie's are aims to increase aggregate supply and can be either market-based or interventionist.

The supply-side policies of increased levels of spending on infra-structure "will help bring foreign investment" as it's easier for firms to set up businesses and is attractive. foreign direct investment will improve the economy of Indonesia as it will create jobs for the locals who may have struggled before, thus reducing the level of unemployment in the economy. More jobs and income will generate a positive multiplier effect in the economy as it means more confidence and higher levels of spending, increasing aggregat demand to AD3 from AD, as consumer

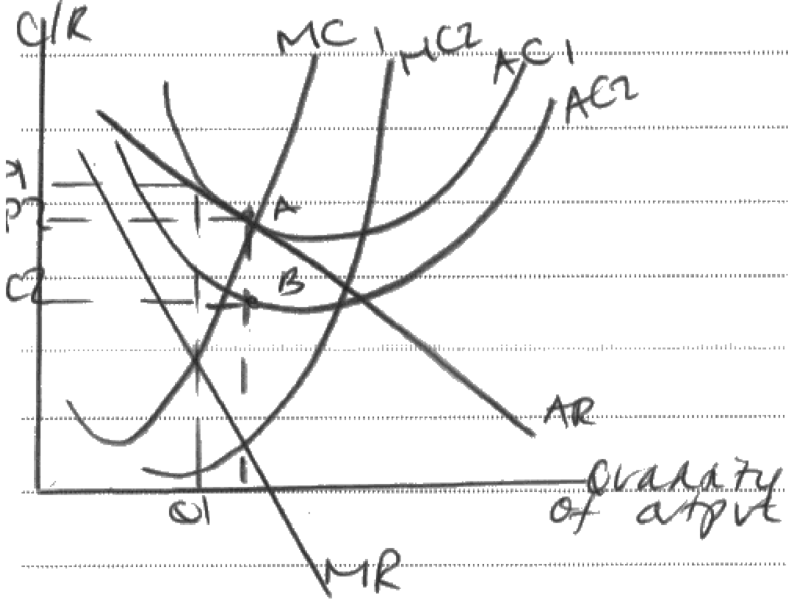


expenditure and government spending are components.

Subsequently, the level of real GDP will rise to Y3 and actual economic growth will result and as figure 5 shows, real GDP in Indonesia has risen from 4% in 2014 to 5.1% in 2016, meaning the supply-side policy of spending on infrastructure is beneficial to the economy.

However, FDI may not increase if foreign firms don't have confidence in the economy of Indonesia. They may not be willing to invest if they think it's volatile and their investments won't be safe, thus the effect of the policy will be limited.

A microeconomic effect of supply-side policies may see business growth and as extract E says, "are improving the business climate". Improved infra structure and education in Indonesia has meant "new enterprise is to flourish". Improved infrastructure may lower the average costs of firms as it's easier to transport goods and services and makes the firms more available to consumers.



The AC and MC curves shift to MC2 and AC2 as average variable costs will fall meaning a lower price of P2 and the potential to make profit of area P2C2BA. The infrastructure may have allowed firms to exploit external economies of scale, aiding in the fall in costs and benefiting the firms in the future, allowing them to grow more, which may hopefully help the growth of the economy too if there is more economic activity.

However, business growth may be very slow in Indonesia for businesses that new power plants, it still takes 200 days for its approval. This may hinder business development, meaning although the supply side policies are helpful, the time lags that accompany it may reduce their comprehensiveness and growth.

Overall, for a country like Indonesia supply-side policies are very helpful, despite the cost to the government. They are a great way of encouraging growth and improvements in aggregate supply. The effects may have been even greater if they were accompanied with demand-side policies too like low interest rates which would have borrowing cheaper, encouraging investment the development of the country.

ResultsPlus

Examiner Comments

The AD point needs clearer links, as does the FDI discussion. However the microeconomic argument is better and it is supported by a helpful diagram (Level 4). There is good context but the evaluation tails off on the micro section – time lags are underdeveloped and lose the connection with the thrust of the argument, and it feels as if they are a standard, rehearsed evaluation point that does not convince.

The final paragraph contains convincing judgement and is credited with a L3+.