

General Certificate of Education
June 2008
Advanced Level Examination



ECONOMICS **ECN5**
Unit 5 Business Economics and the Distribution of Income

Friday 13 June 2008 9.00 am to 10.30 am

For this paper you must have:

- an 8-page answer book.

You may use a calculator.

Time allowed: 1 hour 30 minutes

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 ECN5.
- In **Section A**, answer **all** parts of the question.
- In **Section B**, answer **one** question.

Information

- The maximum mark for this paper is 100.
- The marks for questions are shown in brackets.
- 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, to organise information clearly and to use specialist vocabulary where appropriate.

Advice

- You are advised to spend approximately 45 minutes on **Section A** and approximately 45 minutes on **Section B**.

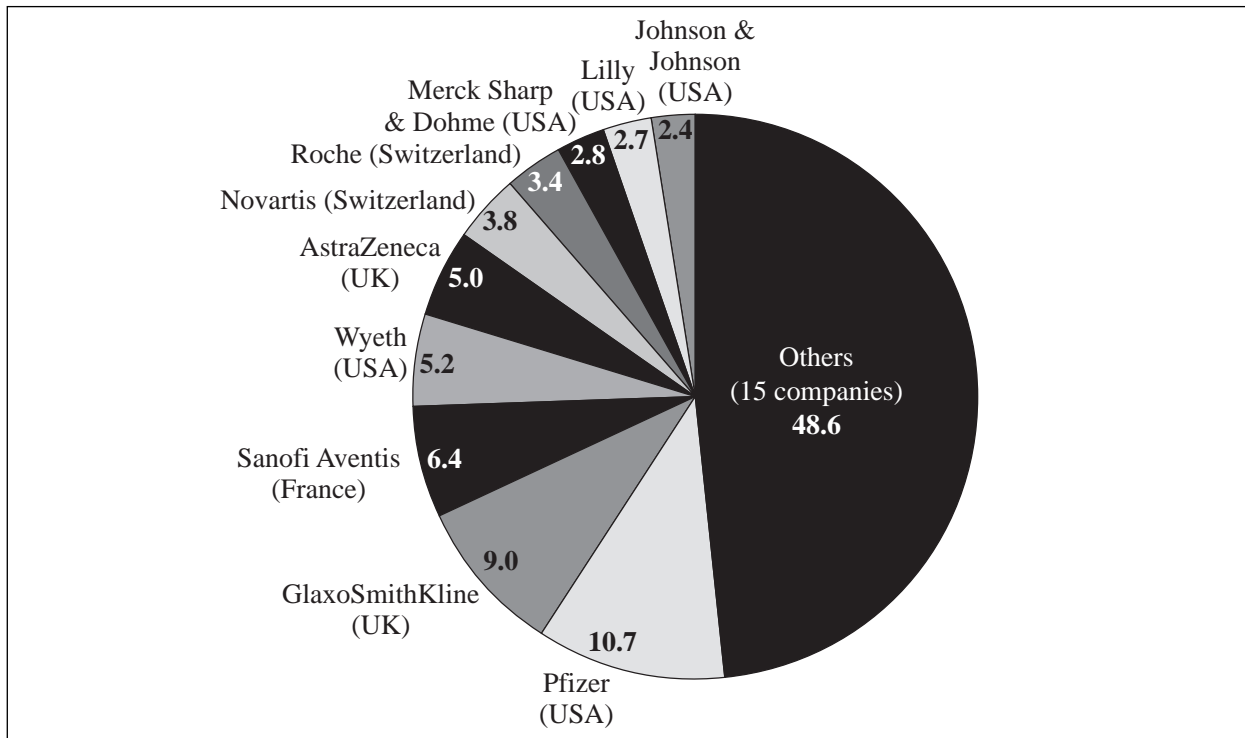
SECTION A

Answer **all** parts of this question.

Total for this question: 50 marks

- 1** Study **Extracts A, B and C**, and then answer **all** parts of Question 1 which follows.

Extract A: % market shares of manufacturing companies operating in the UK pharmaceutical (drug) market, 2004



Source: The Association of the British Pharmaceutical Industry (ABPI), accessed on 20 December 2006

Extract B: Rich countries are blocking cheap drugs for poor countries

Extract B has been removed due to third-party copyright constraints.

It was adapted from an article in The Guardian on 14 November 2006.

Source: adapted from an article by SARAH BOSELEY, *The Guardian*, 14 November 2006

Extract C: Pharmaceutical companies need patents to protect their investments in new drugs, but the investments are not always successful

| | |
|--|----------|
| Drug companies lavish fortunes on research and development (R&D), some spending well above £4 billion a year. Finding a drug takes an average of 12 years and costs £800 million, enough for three jumbo jets. Companies recoup that vast expenditure through the patent system, which allows them to charge high prices for drugs until their monopoly expires. | 1 5 |
| Without patents, drug companies would be dead. When rivals try to breach those patents, the multinational pharmaceutical companies react ferociously, bringing in lawyers and private detectives. The chairman of a leading British pharmaceutical company has argued: "If someone can come along and free-ride on my company's inventions, then why should I put money into research to improve my company's products?" | 10 |
| But even when protected by patents, investment in new drugs is not always successful. AstraZeneca (AZ), the UK's second-largest pharmaceutical company, has recently spent heavily on investing in an experimental treatment for hardened arteries. If the drug eventually reaches the market, it is likely to generate billions of pounds a year in sales for AZ. But the group's chief executive has sounded a gloomy note on the chances of success for the drug, believing it to be a very high-risk project. And if it fails, the drug will be added to AZ's many other failed investment projects. The drug's failure may lead to a collapse in AZ's share price, which will then increase the possibility of a hostile take-over. | 15 20 |

Question 1

- 1 (a) Using **Extract A**, describe **two** features of the UK pharmaceutical market in 2004. (4 marks)
- (b) '...large pharmaceutical companies in rich countries successfully restrict output and make supernormal profit' (**Extract B**, lines 8–10).
With the help of a monopoly diagram, explain this statement. (6 marks)
- (c) **Extract C** (lines 13–14) suggests that the UK's second-largest pharmaceutical company, AstraZeneca, invests heavily in research and development.
Analyse the long-term private benefits **and** costs that may be experienced by a pharmaceutical company when investing in the development of new drugs. (10 marks)
- (d) Using the data and your economic knowledge, evaluate the view that firms in industries such as pharmaceuticals and recorded music should be able to protect their market power, for example by patenting HIV drugs and through copyright protection. (30 marks)

Turn over for the next question

SECTION B

Answer **one** question from this section.

Each question carries 50 marks.

- 2** (a) Economists often assume that firms have only one objective, to maximise profit.
Explain other objectives firms may have other than profit maximisation. (20 marks)
- (b) Evaluate the view that separation of ownership from control has an adverse effect on firms' conduct **and** performance. (30 marks)
- 3** (a) Explain how the supply of labour is determined in a labour market. (20 marks)
- (b) 'Competitive labour markets lead to an unequal and inequitable distribution of income.'
To what extent does this justify government intervention in labour markets? (30 marks)
- 4** (a) Explain why externalities result in a misallocation of resources. (20 marks)
- (b) Evaluate the view that the most effective way to reduce environmental externalities is to create markets in permits to pollute. (30 marks)

END OF QUESTIONS

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