



MARKSCHEME

November 2008

ECONOMICS

Standard Level

Paper 2

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In addition to the assessment criteria use the paper-specific markscheme below. Award up to the maximum marks as indicated.

1. (a) Define the following terms indicated in bold in the text:

(i) indirect taxes (paragraph ①)	[2 marks]
level	
0 <i>Wrong definition</i>	0
1 <i>Vague definition</i> The idea that it is a tax on goods.	1
2 <i>Precise definition</i> An explanation that it is an expenditure tax on a good or service that is imposed by the government.	2
(ii) price elasticity of demand (paragraph ②).	[2 marks]
level	
0 <i>Wrong definition</i>	0
1 <i>Vague definition</i> The idea that it is to do with the relationship between the price of a good and demand.	1
2 <i>Precise definition</i> An explanation that it is a measure of the responsiveness of quantity demanded to a change in the price of the good. (Candidates may give only the equation and this may be rewarded with full marks.)	2

(b) Using an appropriate diagram, explain how an indirect tax on gas is likely to affect the price and quantity of gas. **[4 marks]**

level

- | | | |
|---|---|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <p><i>Identification of appropriate theory</i></p> <p>For drawing a correctly labelled diagram, where the supply curve for gas is shifted upwards by the amount of the tax, raising the equilibrium price and lowering the equilibrium quantity or for providing an explanation of how the indirect tax increases the cost to firms, thus raising price and reducing quantity.</p> | 1-2 |
| 2 | <p><i>Correct application of appropriate theory</i></p> <p>For drawing a correctly labelled diagram, where the supply curve for gas is shifted upwards by the amount of the tax, raising the equilibrium price and lowering the equilibrium quantity and for providing an explanation of how the indirect tax increases the cost to firms, thus raising price and reducing quantity.</p> | 3-4 |

Candidates who incorrectly label diagrams cannot be rewarded with full marks.

The use of P and Q on the axes is sufficient for a demand and supply diagram. A title is not necessary.

(c) Using information from the text, calculate the value of price elasticity of demand for gas from 1975 to 1980 and from 2001 to 2006 and explain what the values signify. **[4 marks]**

level

- | | | |
|---|--|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <p><i>Identification of appropriate theory</i></p> <p>For calculating the PED for 1975 to 1980 and for 2001 to 2006 as 0.275 and 0.065 respectively or for providing an explanation of how the demand for gas was price inelastic in the first period and became even more so in the second period.</p> | 1-2 |
| 2 | <p><i>Correct application of appropriate theory</i></p> <p>For calculating the PED for 1975 to 1980 and for 2001 to 2006 as 0.275 and 0.065 respectively and for providing an explanation of how the demand for gas was price inelastic in the first period and became even more so in the second period.</p> | 3-4 |

- (d) **Using information from the text/data and your knowledge of economics, evaluate possible ways, apart from increasing the indirect taxes on gas, of reducing the demand for gas.**

[8 marks]

Responses **may** include:

- implementing road charging (toll roads) (text)
- improved public transportation (text)
- subsidies to encourage alternative transport (text)
- grants to fund research into the development of alternative fuels
- legislation relating to engine size in cars.

Candidates must evaluate at least two ways to reach level 3.

Examiners should be aware that candidates may take a different approach, which if appropriate, should be rewarded.

If there is no direct reference to the data, then candidates may not be rewarded beyond level 2.

Effective evaluation may be to:

- consider short-term versus long-term consequences
- examine the impact on different stakeholders
- discuss advantages and disadvantages
- prioritize the arguments.

Level

0	No valid discussion.	0
1	Few relevant concepts recognized. Little discussion or only basic understanding.	1-2
2	Relevant concepts recognized and developed in reasonable depth. Some attempt at application and analysis.	3-5
3	Relevant concepts developed in reasonable depth, demonstrating effective evaluation, supported by appropriate evidence or theory.	6-8

2. (a) Define the following terms indicated in bold in the text:

(i) **quotas (paragraph ③)** [2 marks]

level

- 0 *Wrong definition* 0
- 1 *Vague definition* 1
The idea that they are barriers to trade.
- 2 *Precise definition* 2
An explanation that they are import barriers that set limits on the quantity or value of imports that may be imported into a country.

(ii) **inflation (paragraph ⑤).** [2 marks]

level

- 0 *Wrong definition* 0
- 1 *Vague definition* 1
The idea that it is rising prices.
- 2 *Precise definition* 2
An explanation that it is a sustained increase in the general or average level of prices.

(b) **Using an appropriate diagram, explain how private corn sellers might be able to “manipulate prices” (paragraph ⑦).** [4 marks]

level

- 0 *Inappropriate answer* 0
- 1 *Identification of appropriate theory* 1-2
For drawing a correctly labelled diagram, where the supply curve for corn is shifted to the left and the price of corn rises **or** for providing an explanation of how corn distributors are restricting the supply of corn and thus raising its price.
- 2 *Correct application of appropriate theory* 3-4
For drawing a correctly labelled diagram, where the supply curve for corn is shifted to the left and the price of corn rises **and** for providing an explanation of how corn distributors are restricting the supply of corn and thus raising its price.

Candidates who incorrectly label diagrams cannot be rewarded with full marks.

The use of P and Q on the axes is sufficient for a demand and supply diagram. A title is not necessary.

(c) Using information from the text, explain the nature of the cross elasticity of demand for oil and ethanol. [4 marks]

level

- | | | |
|---|--|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <i>Identification of appropriate theory</i>
For explaining that cross elasticity of demand measures the responsiveness of the demand for one good to a change in the price of another good or for explaining that oil and ethanol are substitutes for each other (<i>[1 mark]</i>) and so would have a positive value of cross elasticity of demand (<i>[1 mark]</i>), since as the price of one rises, the demand for the other will also rise. | 1-2 |
| 2 | <i>Correct application of appropriate theory</i>
For explaining that cross elasticity of demand measures the responsiveness of the demand for one good to a change in the price of another good and for explaining that oil and ethanol are substitutes for each other (<i>[1 mark]</i>) and so would have a positive value of cross elasticity of demand (<i>[1 mark]</i>), since as the price of one rises, the demand for the other will also rise. | 3-4 |

- (d) **Using information from the text/data and your knowledge of economics, evaluate the government intervention in the corn tortilla market.** *[8 marks]*

Responses **may** include:

- the setting of the maximum price on corn tortillas (text) may lead to shortages and the emergence of a black market
- problems associated with enforcing the maximum price
- the increased quotas (text) will lead to an increase in imports from the US and may lead to a deterioration of the current account balance
- a fall in private sector support for the government
- reduced inflationary pressure
- a fall in the supply of corn for tortillas, since it is more profitable to sell corn for ethanol (text)
- selling at low prices in government stores (text) is likely to lead to shortages in the long-run.

Examiners should be aware that candidates may take a different approach, which if appropriate, should be rewarded.

If there is no direct reference to the data, then candidates may not be rewarded beyond level 2.

Effective evaluation may be to:

- consider short-term versus long-term consequences
- examine the impact on different stakeholders
- discuss advantages and disadvantages
- prioritize the arguments.

Level

0	No valid discussion.	0
1	Few relevant concepts recognized. Little discussion or only basic understanding.	1-2
2	Relevant concepts recognized and developed in reasonable depth. Some attempt at application and analysis.	3-5
3	Relevant concepts developed in reasonable depth, demonstrating effective evaluation, supported by appropriate evidence or theory.	6-8

3. (a) Define the following terms indicated in bold in the text:

(i) **current account deficit** (*paragraph 1*) *[2 marks]*

level

0 *Wrong definition* **0**

1 *Vague definition* **1**

The idea that it is when imports are greater than exports.

2 *Precise definition* **2**

An explanation that it is when the export revenue from goods and services is less than the import expenditure on goods and services. (Candidates may include net investment income and transfers, but this is not necessary for full marks.)

(ii) **interest rates** (*paragraph 5*). *[2 marks]*

level

0 *Wrong definition* **0**

1 *Vague definition* **1**

The idea that interest rates are the price of money.

2 *Precise definition* **2**

An explanation that interest rates are the cost of borrowing money and any second point, such as:

- usually expressed as a percentage
- an example
- the opportunity cost of current consumption.

(b) Using an AD/AS diagram, explain why “lower oil prices are a positive sign for the inflation outlook” (paragraph 6). [4 marks]

level

- 0 *Inappropriate answer* **0**

- 1 *Identification of appropriate theory* **1-2**
For drawing a correctly labelled AD/AS diagram, where SRAS shifts to the right, and the average price level falls **or** for providing an explanation of how a fall in oil prices will reduce the production costs for many firms in the economy, thus shifting their supply curves to the right and so shifting the SRAS curve to the right, which reduces inflationary pressure.

- 2 *Correct application of appropriate theory* **3-4**
For drawing a correctly labelled AD/AS diagram, where SRAS shifts to the right, and the average price level falls **and** for providing an explanation of how a fall in oil prices will reduce the production costs for many firms in the economy, thus shifting their supply curves to the right and so shifting the SRAS curve to the right, which reduces inflationary pressure.

Candidates who incorrectly label diagrams cannot be rewarded with full marks.

For AD/AS, the vertical axis may be price level or average price level. The horizontal axis may be output, real output, national output, real national output, national income, or GDP. A title is not necessary.

- (c) **Using an appropriate diagram, explain why the rising current account deficit “could have serious implications for the rand” (paragraph 4).** [4 marks]

level

- 0 *Inappropriate answer* **0**
- 1 *Identification of appropriate theory* **1-2**
For drawing a correctly labelled diagram, where the supply curve for the rand has shifted to the right, thus lowering the exchange rate **or** for providing an explanation of how the expenditure on imports leads to an increase in the demand for foreign currencies and thus an increase in the supply of the rand on the foreign exchange market, since it has to be exchanged for the foreign currencies.
- 2 *Correct application of appropriate theory* **3-4**
For drawing a correctly labelled diagram, where the supply curve for the rand has shifted to the right, thus lowering the exchange rate **and** for providing an explanation of how the expenditure on imports leads to an increase in the demand for foreign currencies and thus an increase in the supply of the rand on the foreign exchange market, since it has to be exchanged for the foreign currencies.

Candidates may take the approach of shifting the demand curve to the left, because demand for South African exports may have fallen. If this is explained correctly, then full marks should be awarded.

Candidates who incorrectly label diagrams cannot be rewarded with full marks.

The axes must be appropriate to an exchange rate market, such as exchange rate, price of rand in \$, price of rand in other currencies, or any other appropriate expression more explicit than “price”. A title is not necessary.

- (d) Using information from the text/data and your knowledge of economics, evaluate the likely effects of the “tightened interest rates” (paragraph 5). [8 marks]

Responses **may** include:

- possible fall in consumption (text/data)
- the fall in consumption may not be significant because of the strong economic confidence (text/data)
- the fall in consumption may not be significant in the short run “as monetary policy operates with a lag” (text/data)
- possible fall in investment
- possible increase in unemployment
- higher borrowing costs for firms
- appreciation of the exchange rate which is likely to worsen the growing South African current account deficit
- reduction in South African inflationary pressure
- imports would be cheaper for consumers, if the exchange rate appreciates
- imported raw materials and semi-finished goods would be cheaper for producers, if the exchange rate appreciates.

Examiners should be aware that candidates may take a different approach, which if appropriate, should be rewarded.

If there is no direct reference to the data, then candidates may not be rewarded beyond level 2.

Effective evaluation may be to:

- consider short-term versus long-term consequences
- examine the impact on different stakeholders
- discuss advantages and disadvantages
- prioritize the arguments.

Level

0	No valid discussion.	0
1	Few relevant concepts recognized. Little discussion or only basic understanding.	1-2
2	Relevant concepts recognized and developed in reasonable depth. Some attempt at application and analysis.	3-5
3	Relevant concepts developed in reasonable depth, demonstrating effective evaluation, supported by appropriate evidence or theory.	6-8

4. (a) Define the following terms indicated in bold in the text:

(i) **subsidies** (*paragraph ①*) *[2 marks]*

level

0 *Wrong definition* **0**

1 *Vague definition* **1**

The idea that it is money given to firms by the government.

2 *Precise definition* **2**

An explanation that they are a payment made by a government to a firm or industry in order to:

– reduce costs of products

or

– increase supply

or

– lower the price to consumers

or

– give domestic producers an advantage in international trade

(Candidates may only give the reasons for subsidies and this may be rewarded with *[1 mark]*.)

(ii) **income elasticity of demand** (*paragraph ⑤*). *[2 marks]*

level

0 *Wrong definition* **0**

1 *Vague definition* **1**

The idea that it is a relationship between income and demand.

2 *Precise definition* **2**

An explanation that it is a measure of the responsiveness of quantity demanded or demand to a change in income. (Candidates may give only the equation and this may be rewarded with full marks.)

(b) Using an appropriate diagram, explain the effect of the EU tariff on frozen strawberries on the European market for frozen strawberries. [4 marks]

level

- 0 *Inappropriate answer* **0**

- 1 *Identification of appropriate theory* **1-2**
For drawing a correctly labelled diagram, where the imposition of a tariff on strawberries forces up the world supply curve, reducing the quantity of imports and increasing domestic supply **or** for providing an explanation of how the tariff will force up the price in the EU, which will increase the quantity supplied domestically and reduce imports.

- 2 *Correct application of appropriate theory* **3-4**
For drawing a correctly labelled diagram, where the imposition of a tariff on strawberries forces up the world supply curve, reducing the quantity of imports and increasing domestic supply **and** for providing an explanation of how the tariff will force up the price in the EU, which will increase the quantity supplied domestically and reduce imports.

Candidates who incorrectly label diagrams cannot be rewarded with full marks.

The use of P and Q on the axes is sufficient for a demand and supply diagram. A title is not necessary.

- (c) **Using an appropriate diagram, explain the type of unemployment that Poland might experience without the strawberry tariff.** **[4 marks]**

level

- | | | |
|---|--|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <p><i>Identification of appropriate theory</i></p> <p>For drawing a correctly labelled diagram, showing a fall in demand for labour in the strawberry industry or for providing an explanation of how the type of unemployment is structural unemployment, since there has been a change in the structure of the economy, caused by cheap imports, and thus a fall in demand for labour in the strawberry industry.</p> | 1-2 |
| 2 | <p><i>Correct application of appropriate theory</i></p> <p>For drawing a correctly labelled diagram, showing a fall in demand for labour in the strawberry industry and for providing an explanation of how the type of unemployment is structural unemployment, since there has been a change in the structure of the economy, caused by cheap imports, and thus a fall in demand for labour in the strawberry industry.</p> | 3-4 |

Candidates who incorrectly label diagrams cannot be rewarded with full marks.

For a labour market diagram, the vertical axis may be wages, wage rate, or the price of labour. The horizontal axis should be quantity of labour, employment, number of workers, or simply labour or workers. A title is not necessary.

- (d) **Using information from the text/data and your knowledge of economics, evaluate a decision to increase protection in the EU strawberry industry.** **[8 marks]**

Responses **may** include:

- definition of protection
- higher prices for consumers
- welfare loss and efficiency loss/misallocation of resources
- revenue from the tariffs
- higher employment in Polish strawberry industry (text/data)
- higher costs for importers of strawberries
- higher costs of production in industries which use strawberries such as jam, yoghurt and ice cream industries (text/data)
- retaliation from China, possibly in the EU wine and cheese industries (text/data)
- possibility that other industries will lobby for protectionism, e.g. Spanish furniture makers and Belgian apple farmers (text/data)
- damaging effects on China's growth.

Examiners should be aware that candidates may take a different approach, which if appropriate, should be rewarded.

If there is no direct reference to the data, then candidates may not be rewarded beyond level 2.

Effective evaluation may be to:

- consider short-term versus long-term consequences
- examine the impact on different stakeholders
- discuss advantages and disadvantages
- prioritize the arguments.

Level

0	No valid discussion.	0
1	Few relevant concepts recognized. Little discussion or only basic understanding.	1-2
2	Relevant concepts recognized and developed in reasonable depth. Some attempt at application and analysis.	3-5
3	Relevant concepts developed in reasonable depth, demonstrating effective evaluation, supported by appropriate evidence or theory.	6-8

5. (a) Define the following terms indicated in bold in the text:

(i) infrastructure (paragraph ①) *[2 marks]*

level

0	<i>Wrong definition</i>	0
1	<i>Vague definition</i> The idea that it is to do with public services.	1
2	<i>Precise definition</i> An explanation that it involves essential facilities and services such as roads, airports, sewage treatment, water systems, railways, telephone and other utilities.	2

(ii) investment (paragraph ②). *[2 marks]*

level

0	<i>Wrong definition</i>	0
1	<i>Vague definition</i> The idea that it is spending by firms.	1
2	<i>Precise definition</i> An explanation that it is expenditure on capital equipment or that it is an injection into the economy or that it is an addition to the capital stock of the economy.	2

(b) Using information from paragraph 1 and table 1, explain why there is evidence that the demand for oil was price inelastic in 2005. [4 marks]

level

- 0 *Inappropriate answer* **0**
- 1 *Identification of appropriate theory* **1-2**
 For explaining that the price of oil has increased and oil is an important part of exports (*paragraph 1*) **or** for providing an explanation that oil prices increased and the current account balance increased (*Table 1*), indicating inelastic demand.
- 2 *Correct application of appropriate theory* **3-4**
 For explaining that the price of oil has increased and oil is an important part of exports (*paragraph 1*) **and** for providing an explanation that oil prices increased and the current account balance increased (*Table 1*), indicating inelastic demand.

(c) Using an AD/AS diagram, explain the effect that the changing current account balance is likely to have on inflation. [4 marks]

level

- 0 *Inappropriate answer* **0**
- 1 *Identification of appropriate theory* **1-2**
 For drawing a correctly labelled diagram, where the aggregate demand curve shifts to the right with the increase in $(X - M)$, thus raising the average price level **or** for providing an explanation of how the increase in AD will lead to an increase in the rate of inflation as demand in the economy increases.
- 2 *Correct application of appropriate theory* **3-4**
 For drawing a correctly labelled diagram, where the aggregate demand curve shifts to the right with the increase in $(X - M)$, thus raising the average price level **and** for providing an explanation of how the increase in AD will lead to an increase in the rate of inflation as demand in the economy increases.

Candidates who incorrectly label diagrams cannot be rewarded with full marks.

For AD/AS, the vertical axis may be price level or average price level. The horizontal axis may be output, real output, national output, real national output, national income, or GDP. A title is not necessary.

(d) **Using information from the text/data and your knowledge of economics, evaluate possible measures that the Nigerian government might employ to promote economic development.**

[8 marks]

Responses **may** include:

- a definition of economic development
- an explanation of measures that could increase economic growth, such as supply-side policies
- the use of oil wealth may be used for:
 - investment in education
 - investment in healthcare
 - investment in infrastructure
- policies to reduce corruption and ensure that public money is used for approved investment projects
- pro-poor growth strategies
- policies to attract FDI.

Candidates must explain **how** the measures that they have chosen will promote economic development in order to reach level 3.

Examiners should be aware that candidates may take a different approach, which if appropriate, should be rewarded.

If there is no direct reference to the data, then candidates may not be rewarded beyond level 2.

Effective evaluation may be to:

- consider short-term versus long-term consequences
- examine the impact on different stakeholders
- discuss advantages and disadvantages
- prioritize the arguments.

Level

0	No valid discussion.	0
1	Few relevant concepts recognized. Little discussion or only basic understanding.	1-2
2	Relevant concepts recognized and developed in reasonable depth. Some attempt at application and analysis.	3-5
3	Relevant concepts developed in reasonable depth, demonstrating effective evaluation, supported by appropriate evidence or theory.	6-8
