

**ECONOMICS
STANDARD LEVEL
PAPER 2**

Friday 7 November 2003 (morning)

2 hours

INSTRUCTIONS TO CANDIDATES

- Do not open this examination paper until instructed to do so.
- Section A: answer one question.
- Section B: answer one question.
- Use diagrams where appropriate.

SECTION A

Answer **one** question from this Section.

Either

Question 1

Karnataka Tourism set to gain from admissions fever¹

- 1 Being admitted to professional courses in medical, dental and engineering institutions in India is the biggest ambition of most of the academically brilliant students and their parents. Given the limited number of places available in Indian Institutes of Technology (I.I.T), there is a huge demand for admission to professional colleges – as in the State of Karnataka where thousands apply every year, not only from within the state, but also from other parts of India and even from abroad.
- 2 Despite a fee of R30 000 there is **excess demand** for places. This year, a record number of 127 343 students have applied to Karnataka’s colleges. Of these, as many as 59 299, or roughly 46.7 per cent, are from outside the state. These candidates are competing with each other for the 26 000 places in the state’s professional colleges – medical, dental and engineering.
- 3 With such large numbers of non-Karnataka students, possibly accompanied by at least one parent or adult to guide them, it is natural that there will be enormous business opportunities for the hotels, lodgings and travel operators. The state-owned Karnataka Tourism Development Corporation (KTDC) has taken the initiative to offer an elaborate and attractive package.
- 4 A spokesperson for the KTDC said, “We believe there are many **social benefits** arising from the demand for places at I.I.T and it is our intention to take advantage of them”.

[Source: adapted from *The Economic Times*, India, Sunday 6 May 2001]

¹ fever - excitement, agitation

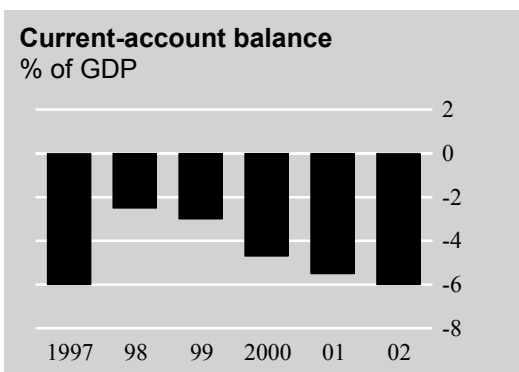
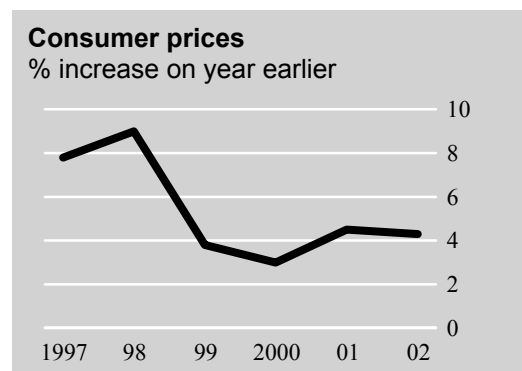
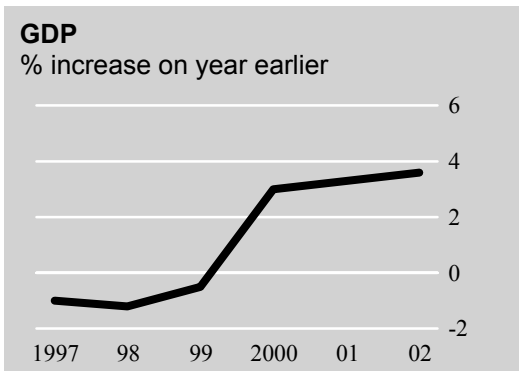
- (a) Explain the meaning of the following terms that appear in bold text in the article:
- (i) excess demand (*paragraph 2*) [2 marks]
 - (ii) social benefits (*paragraph 4*). [2 marks]
- (b) (i) Use the information in *paragraph 2* to draw a supply and demand diagram to illustrate the admissions problem at the I.I.T. [4 marks]
- (ii) With the aid of supply and demand theory suggest proposals to deal with this problem of excess demand for places at I.I.T. [5 marks]
- (c) Using the information in the article and your knowledge of economic theory, describe and explain the possible social benefits to which the KTDC spokesperson refers in *paragraph 4*. [5 marks]
- (d) Critically assess the role of I.I.T in promoting development in the Karnataka region. [7 marks]

Or

Question 2

OECD Survey, Czech Republic

- 1 According to the OECD's latest survey of the Czech Republic, structural reforms with their emphasis on supply-side measures aided a strong recovery in 2000 and early 2001 after the **recession** from 1997-99. Efforts to fight inflation through monetary policy
- 4 have also been quite successful. However, the large **current account deficit** is putting downward pressure on the exchange rate and this may be inflationary. This, along with a loose fiscal policy is posing a challenge to monetary policy in stabilizing demand in the medium term. In order to maintain its inflation targets, it is recommended that the
- 7 Czech Republic continue using supply-side measures along with fiscal tightening.



[Source: adapted from *The Economist*, 4 August 2001]

- (a) Explain the meaning of the following terms that appear in bold in the text:
- (i) recession (*line 3*) [2 marks]
 - (ii) current account deficit (*line 4*). [2 marks]
- (b) (i) Describe the relationship between the change in GDP and the current account balance between 1999 and 2001. [2 marks]
- (ii) What might account for this relationship? [3 marks]
- (c) (i) Describe the change in the Czech Republic’s consumer price level over the years 1998 to 2000. [2 marks]
- (ii) How might monetary policy be responsible for the change from 1998 to 2000? [4 marks]
- (d) Explain why “the large current account deficit is putting downward pressure on the exchange rate and this may be inflationary”. [3 marks]
- (e) Use aggregate demand/aggregate supply analysis to explain why it is recommended that the Czech Republic continue using supply-side measures along with fiscal tightening. [7 marks]

SECTION B

Answer **one** question from this section. Diagrams should be used wherever appropriate.

Question 3

- (a) Why do markets sometimes fail to set socially acceptable prices? [12 marks]
- (b) To what extent can governments overcome this form of market failure? Illustrate your answer with examples. [13 marks]

Question 4

Assess the impact of an increase in interest rates on

- (a) the balance of payments [10 marks]
- (b) the domestic economy. [15 marks]

Question 5

- (a) What are the benefits (gains) from international trade? [10 marks]
- (b) To what extent is it justifiable for governments to resort to protectionism? [15 marks]

Question 6

Evaluate the role of Foreign Direct Investment (FDI) in contributing to growth and development in Less Developed Countries. [25 marks]
