



# **MARKSCHEME**

**November 2010**

**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 tax (Table 1)** **[2 marks]**

level

0 *Wrong definition* **0**

1 *Vague definition* **1**

The idea that it is a tax on a product.

2 *Precise definition* **2**

An explanation that it is a tax on expenditure. It is added to the selling price of a good or service.

**(ii) investment (paragraph 4).** **[2 marks]**

level

0 *Wrong definition* **0**

1 *Vague definition* **1**

The idea that it is spending on machines by firms.

2 *Precise definition* **2**

An explanation that it is the addition of capital stock to the economy or expenditure by firms on capital.

**(b) Using an appropriate diagram, explain how rising biofuel production may affect the market for corn (paragraph ①).** **[4 marks]**

level

- |   |  |            |
|---|--|------------|
| 0 | <i>Inappropriate answer</i>  | <b>0</b>   |
| 1 | <i>Identification of appropriate theory</i><br>For drawing a correctly labelled demand and supply diagram for corn which shows the demand for corn shifting to the right, with more being demanded and supplied at a higher price <b>or</b> for providing an explanation that corn is used for producing biofuels and so if there is an increase in the production of biofuels, then there will be an increase in the demand for corn, raising the price of corn and the quantity demanded and supplied.       | <b>1-2</b> |
| 2 | <i>Correct application of appropriate theory</i><br>For drawing a correctly labelled demand and supply diagram for corn which shows the demand for corn shifting to the right, with more being demanded and supplied at a higher price <b>and</b> for providing an explanation that corn is used for producing biofuels and so if there is an increase in the production of biofuels, then there will be an increase in the demand for corn, raising the price of corn and the quantity demanded and supplied. | <b>3-4</b> |

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 why the elasticity of supply for many commodities is low.** *[4 marks]*

level

0 *Inappropriate answer* **0**

1 *Identification of appropriate theory* **1-2**

For drawing a correctly labelled demand and supply diagram for a commodity, which shows a relatively inelastic supply curve (one which would touch the *x*-axis if extended) **or** for providing an explanation that agricultural commodities are inelastic in supply because they are crop based and so it is difficult to increase quantity supplied significantly in the short-run.

Candidates may offer a perfectly inelastic supply curve for agriculture, explaining that the crop nature of the product leads to a set quantity being produced in any time period. If this is properly explained, then it should be fully rewarded.

Candidates may write about minerals, explaining that their supply is inelastic because their sources are limited and it is difficult to discover new sources of minerals quickly. This is equally applicable.

2 *Correct application of appropriate theory* **3-4**

For drawing a correctly labelled demand and supply diagram for a commodity, which shows a relatively inelastic supply curve (one which would touch the *x*-axis if extended) **and** for providing an explanation that agricultural commodities are inelastic in supply because they are crop based and so it is difficult to increase quantity supplied significantly in the short-run.

Candidates may offer a perfectly inelastic supply curve for agriculture, explaining that the crop nature of the product leads to a set quantity being produced in any time period. If this is properly explained, then it should be fully rewarded.

Candidates may write about minerals, explaining that their supply is inelastic because their sources are limited and it is difficult to discover new sources of minerals quickly. This is equally applicable.

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.

(d) **Using information from the text/data and your knowledge of economics, evaluate Ecuador’s policy response to increasing food prices (Table 1).** [8 marks]

Responses **may** include:

- the concept of a maximum price
- a price ceiling diagram.

Possible positive consequences:

- affordable bread for consumers (Table 1)
- affordable food is a merit good
- increases the purchasing power of the urban poor (paragraph 3).

Possible negative consequences:

- reduced revenue/income for farmers as the price of bread is below the equilibrium price
- shortages of bread
- need for a rationing system
- possibility of parallel markets
- need for government intervention to increase supply
- other policy options (Table 1).

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.

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 text/data, then candidates may not be rewarded beyond level 2.

**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) **economic growth** (*paragraph 2*) [2 marks]

level

0 *Wrong definition* 0

1 *Vague definition* 1

The idea that it is a growth of economic activity in the economy.

2 *Precise definition* 2

An explanation that it is the growth of real output in an economy over time.

(ii) **sustainable development** (*paragraph 5*). [2 marks]

level

0 *Wrong definition* 0

1 *Vague definition* 1

The idea that it is related to the world's resources.

2 *Precise definition* 2

An explanation that it is development that meets the needs of the present without compromising the ability of future generations to meet their own needs.

(b) Using an appropriate diagram and the concept of elasticity, explain why “the water suppliers are able to pass on most of the increased costs to their consumers” (paragraph 4).

[4 marks]

level

0 *Inappropriate answer*

0

1 *Identification of appropriate theory*

1-2

For drawing a correctly labelled demand and supply diagram for water, which shows a relatively inelastic demand curve, a shift of the supply curve to the left, and an increase in price that covers most of the cost increase **or** for providing an explanation that because the demand for water is relatively inelastic, when costs increase and supply shifts to the left, price will increase to cover a substantial part of the cost increase.

2 *Correct application of appropriate theory*

3-4

For drawing a correctly labelled demand and supply diagram for water, which shows a relatively inelastic demand curve, a shift of the supply curve to the left, and an increase in price that covers most of the cost increase **and** for providing an explanation that because the demand for water is relatively inelastic, when costs increase and supply shifts to the left, price will increase to cover a substantial part of the cost increase.

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 why the problem discussed in the text illustrates an example of a market failure.** *[4 marks]*

level

- |   |  |            |
|---|--|------------|
| 0 | <i>Inappropriate answer</i>  | <b>0</b>   |
| 1 | <i>Identification of appropriate theory</i><br>For drawing a correctly labelled externalities diagram, which shows marginal social cost greater than marginal private cost and so more being demanded and supplied than the socially optimum level <b>or</b> for explaining that firms are creating a negative externality (of production), since the waste that they are dumping into the river is harming third parties, <i>i.e.</i> the people who use the river.       | <b>1-2</b> |
| 2 | <i>Correct application of appropriate theory</i><br>For drawing a correctly labelled externalities diagram, which shows marginal social cost greater than marginal private cost and so more being demanded and supplied than the socially optimum level <b>and</b> for explaining that firms are creating a negative externality (of production), since the waste that they are dumping into the river is harming third parties, <i>i.e.</i> the people who use the river. | <b>3-4</b> |

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

The vertical axis may be price, but could be costs or benefits. The horizontal axis is quantity. A title is not necessary.

(d) **Using information from the text/data and your knowledge of economics, evaluate the use of regulation as a solution to the market failure caused by the pollution of the Cisadane River.**

[8 marks]

Responses **should** include:

- a definition of market failure (*unless this has happened in an earlier question part*).

Responses **may** include:

- an explanation of regulation
- examples of regulation
- regulation as the most direct form of control
- problems of implementation (*paragraph 6*)
- possible alternatives *e.g.* fines (*paragraph 5*), taxes, subsidizing water producers
- reduction of Indonesia's economic growth (*paragraph 2*)
- aid to sustainable development (*paragraph 5*)
- discouraging FDI.

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.

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 text/data, then candidates may not be rewarded beyond level 2.

**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) **entrepreneurship (paragraph ①)** [2 marks]

level

0 *Wrong definition* 0

1 *Vague definition* 1  
The idea that it is a factor of production.

2 *Precise definition* 2  
An explanation that it is the factor of production involving organizing of the other factors and/or risk taking.

(ii) **monetary policy (paragraph ②).** [2 marks]

level

0 *Wrong definition* 0

1 *Vague definition* 1  
The idea that it is a policy concerned with controlling the amount of money in the economy.

2 *Precise definition* 2  
An explanation that it is a demand-side policy using changes in the money supply or interest rates to achieve economic objectives relating to inflation and unemployment.

**N.B.** Candidates may explain that it is a demand-side policy, using changes in interest rates, to shift the AD curve. This is sufficient for L2.

(b) Using an appropriate diagram, explain the likely effect of aggregate demand increasing “beyond potential output” (*paragraph 1*). [4 marks]

level

- |   |   |            |
|---|---|------------|
| 0 | <i>Inappropriate answer</i>   | <b>0</b>   |
| 1 | <i>Identification of appropriate theory</i><br>For drawing a correctly labelled AD/AS diagram which shows AD and SRAS intersecting to the right of LRAS <b>or</b> for explaining that if AD increases beyond potential output, the effect would be inflation.       | <b>1-2</b> |
| 2 | <i>Correct application of appropriate theory</i><br>For drawing a correctly labelled AD/AS diagram which shows AD and SRAS intersecting to the right of LRAS <b>and</b> for explaining that if AD increases beyond potential output, the effect would be inflation. | <b>3-4</b> |

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.

Candidates may illustrate their answer using either a Keynesian aggregate supply curve or a business cycle showing output gaps. If correctly explained they should be fully rewarded.

(c) **Using an AD/AS diagram, explain how wage increases create cost push inflation (paragraph 2).** **[4 marks]**

level

- |   |   |            |
|---|---|------------|
| 0 | <i>Inappropriate answer</i>   | <b>0</b>   |
| 1 | <i>Identification of appropriate theory</i><br>For drawing a correctly labelled AD/AS diagram, which shows a leftward shift of SRAS and higher price level <b>or</b> for explaining that wages are a cost of production and that higher wages will lead to higher production costs which will be passed on in the form of higher prices leading to cost push inflation.       | <b>1-2</b> |
| 2 | <i>Correct application of appropriate theory</i><br>For drawing a correctly labelled AD/AS diagram, which shows a leftward shift of SRAS and higher price level <b>and</b> for explaining that wages are a cost of production and that higher wages will lead to higher production costs which will be passed on in the form of higher prices leading to cost push inflation. | <b>3-4</b> |

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 the consequences for Iceland’s economy if it maintains tight monetary policies.**

*[8 marks]*

Responses **should** include:

- an explanation of tight monetary policy.

Possible positive consequences include:

- a reduction in the inflation rate (*Figure 2*)
- an appreciation of the currency, making imports cheaper.

Possible negative consequences include:

- a lower rate of economic growth (*Figure 1*)
- a worsening of the current account deficit as the exchange rate increases (*Figure 3*)
- increased unemployment (*Figure 4*)
- a fall in the growth rate of *per capita* income (*paragraph 1*)
- a reduction in the rising entrepreneurship (*paragraph 1*)
- changes in the distribution of income.

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.

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 text/data, then candidates may not be rewarded beyond level 2.

**Level**

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

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

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

level

0 *Wrong definition* 0

1 *Vague definition* 1  
The idea that they are a restriction on imports.

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) **current account surplus (paragraph 5).** [2 marks]

level

0 *Wrong definition* 0

1 *Vague definition* 1  
The idea that it is where exports are greater than imports.

2 *Precise definition* 2  
An explanation that it is where the value of exports of goods and services exceeds the value of imports of goods and services.

*N.B.* Candidates may include net income flows, but this is not necessary for full marks.

**(b) Using an appropriate diagram, explain how a western company can benefit by moving its production lines to China (paragraph 4).** [4 marks]

level

- 0 *Inappropriate answer* **0**
  
- 1 *Identification of appropriate theory* **1-2**  
 For drawing a correctly labelled demand and supply diagram for an industry, which shows a shift to the right of the supply curve **or** for providing an explanation that the lower production costs in China will lead to an increase in supply of the product and allow a firm to sell its product at a lower price (or at a higher profit).
  
- 2 *Correct application of appropriate theory* **3-4**  
 For drawing a correctly labelled demand and supply diagram for an industry, which shows a shift to the right of the supply curve **and** for providing an explanation that the lower production costs in China will lead to an increase in supply of the product and allow a firm to sell its product at a lower price (or at a higher profit).

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 a tariff diagram, explain why policy makers might choose to increase tariffs during an economic slowdown (paragraph 1).** [4 marks]

level

- 0 *Inappropriate answer* **0**
  
- 1 *Identification of appropriate theory* **1-2**  
 For drawing a correctly labelled demand and supply diagram for an industry which shows that the increase of a tariff (or even the imposition of a tariff) results in an increase in domestic output **or** for an explanation that a tariff will increase domestic production, which would help to maintain employment during the slowdown.
  
- 2 *Correct application of appropriate theory* **3-4**  
 For drawing a correctly labelled demand and supply diagram for an industry which shows that the increase of a tariff (or even the imposition of a tariff) results in an increase in domestic output **and** for an explanation that a tariff will increase domestic production, which would help to maintain employment during the slowdown.

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.



- (d) **Using information from the text/data and your knowledge of economics, evaluate the possible effects of China’s increased role in global trade.** [8 marks]

Responses **may** include:

Possible positive effects include:

- China is generating employment opportunities for Europe and the US (*paragraph 2*)
- China is becoming a powerful global buyer (*paragraph 3*)
- China supplies cheaper goods to Europe and the US (*paragraph 4*)
- China could help western companies to cut costs by moving production lines there (*paragraph 4*)
- China is becoming the world’s biggest import market (*paragraph 5*)
- China provides greater choice of products (*paragraph 6*)
- consumers gain with more choice and lower prices (*paragraph 6*)
- increased AD in countries that export to China
- a reallocation of world resources (more efficient)
- reduction in cost push inflation in countries that import factors of production from China.

Possible negative effects include:

- it may lead to protectionist policies (*paragraph 1*)
- employment may fall in western countries as firms move production to China (*paragraph 2*)
- China has a large current account surplus (*paragraph 5*) which implies that trading partners have current account deficits
- China’s purchasing of western debt, funded by the current account surplus, may be a threat to stability in some western economies
- impact on commodity prices of China’s increasing demand.

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.

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 text/data, then candidates may not be rewarded beyond level 2.

**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 2)** [2 marks]

level

0	<i>Wrong definition</i>	0
1	<i>Vague definition</i> The idea that the government provides things like roads.	1
2	<i>Precise definition</i> Any of the following: <ul style="list-style-type: none"><li>• essential facilities that add to the capital stock of the economy</li><li>• capital typically provided by government to make economic activity possible.</li></ul>	2

An answer that simply gives examples should not get any marks.  
An answer that falls just short of being precise may get full marks if supported by an appropriate example.

**(ii) bilateral aid (paragraph 5).** [2 marks]

level

0	<i>Wrong definition</i>	0
1	<i>Vague definition</i> The idea that two countries are involved.	1
2	<i>Precise definition</i> An explanation that it is aid that is given directly from one country to another.	2

(b) **Using an appropriate diagram, explain why it remains difficult for “Haitian households to break out of the poverty cycle” (paragraph 4).** [4 marks]

level

- 0 *Inappropriate answer* **0**
  
- 1 *Identification of appropriate theory* **1-2**  
For drawing a correctly labelled poverty cycle diagram, which shows a suitable circular argument beginning and ending with poverty and/or low incomes **or** for providing an explanation that there are factors that are connected that will perpetuate poverty and for describing such a series of circumstances for Haitian households.
  
- 2 *Correct application of appropriate theory* **3-4**  
For drawing a correctly labelled poverty cycle diagram, which shows a suitable circular argument beginning and ending with poverty and/or low incomes **and** for providing an explanation that there are factors that are connected that will perpetuate poverty and for describing such a series of circumstances for Haitian households.

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

(c) **With reference to Figure 1, explain why there is a difference between the Human Development Index (HDI) figures for Haiti and Madagascar.** [4 marks]

level

- 0 *Inappropriate answer* **0**
  
- 1 *Identification of appropriate theory* **1-2**  
For noting that Madagascar has a higher HDI and that the HDI includes more than just GDP *per capita*.
  
- 2 *Correct application of appropriate theory* **3-4**  
For noting that Madagascar has a higher HDI and that the HDI includes more than just GDP *per capita* **and** for explaining that education and healthcare in Madagascar are presumably better than in Haiti, thus leading to a relatively higher HDI position, despite its lower GDP *per capita*.

- (d) **Using information from the text/data and your knowledge of economics, evaluate aid as a means of achieving economic development in Haiti.** [8 marks]

Responses **may** include:

- a definition of economic development
- some types of aid.

Factors relating to the aid include:

- food aid is essential in the short-run (*paragraph 2*)
- aid is of little use if it cannot be distributed (*paragraph 2*)
- rural areas suffer more than urban areas (*paragraph 3*)
- food aid is a temporary measure (*paragraph 4*)
- development aid is critical (*paragraph 4*)
- rebuilding roads and schools (*paragraph 5*)
- importance of aid to help education and health (*Figure 1*)
- aid is no use without infrastructure and solving corruption
- other factors – institutional
- alternative of trade
- criticism of aid schemes
- discussion of the difference between multilateral and bilateral aid in the Haitian context
- evaluation of long-term aid as opposed to food aid (*paragraph 5*).

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.

There needs to be some reasoned conclusion, for the evaluation to be effective – not just a list of advantages and disadvantages. There clearly has to be evaluation of the ways that aid can or does contribute to economic development, not just a general discussion of aid.

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 text/data, then candidates may not be rewarded beyond level 2.

**Level**

0	No valid discussion.	<b>0</b>
1	Few relevant concepts recognized. Little discussion or only basic understanding.	<b>1-2</b>
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