



MARKSCHEME

May 2009

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) supply (paragraph 2) [2 marks]

level

0 *Wrong definition* **0**

1 *Vague definition* **1**

The idea that it is the amount supplied by producers.

2 *Precise definition* **2**

An explanation that it is the willingness and ability of producers to produce a quantity of a good.

(ii) unemployment (paragraph 4). [2 marks]

level

0 *Wrong definition* **0**

1 *Vague definition* **1**

The idea that it is the number of people out of work.

2 *Precise definition* **2**

An explanation that it is:

- people of working age (those in the labour force)
- willing and able to work
- actively seeking work
- at the current wage rate
- who are without work.

Any two of the above points would be sufficient.

- (b) **Using an appropriate diagram, explain why the supply of Australian bananas will be perfectly inelastic in the immediate to short-term period of time.** *[4 marks]*

level

- | | | |
|---|---|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <p><i>Identification of appropriate theory</i></p> <p>For drawing a correctly labelled supply diagram, where the supply curve is vertical or for providing an explanation that in the short term it is impossible for producers to respond to a change in price because the number of trees is fixed, you cannot store bananas, and banana imports are banned. (Any of these three are explanations for perfectly inelastic demand.)</p> | 1-2 |
| 2 | <p><i>Correct application of appropriate theory</i></p> <p>For drawing a correctly labelled supply diagram, where the supply curve is vertical and for providing an explanation that in the short term it is impossible for producers to respond to a change in price because the number of trees is fixed, you cannot store bananas, and banana imports are banned. (Any of these three are explanations for perfectly inelastic demand.)</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 an appropriate diagram, explain the impact of the cyclone on the price of substitute goods such as apples.** *[4 marks]*

level

- | | | |
|---|---|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <p><i>Identification of appropriate theory</i></p> <p>For drawing a correctly labelled demand and supply diagram illustrating a shift to the right/increase in demand for apples or for providing an explanation that higher prices for bananas will mean some consumers will switch to apples (a substitute), leading to an increase in demand for apples and an increase in price.</p> | 1-2 |
| 2 | <p><i>Correct application of appropriate theory</i></p> <p>For drawing a correctly labelled demand and supply diagram illustrating a shift to the right/increase in demand for apples and for providing an explanation that higher prices for bananas will mean some consumers will switch to apples (a substitute), leading to an increase in demand for apples and an increase in price.</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.

- (d) **Using information from the text/data and your knowledge of economics, evaluate a decision to impose a maximum price (ceiling price) on bananas in Australia.**

[8 marks]

Responses **may** include:

- a definition of a maximum/ceiling price.
- a correctly labelled demand/supply diagram illustrating a maximum price (ceiling price)
- it would help consumers because there will be a lower price for bananas than the current market price of \$14 per kilo (*paragraph 2*). This price will still be higher than prior to the cyclone
- the price rise for bananas will cause an increase in demand for substitute products such as apples. The imposition of a ceiling price will reduce the size of this increase in demand for substitute products
- a maximum price may reduce the cost impact on any complementary goods such as banana milkshakes/smoothies
- producers will not be happy because there will be lower revenue/lower income received for the sale of bananas (*paragraph 6*)
- impact on the market for bananas will be to create a shortage (excess demand) (*paragraph 6*)
- the shortage may cause difficulty in rationing the limited supply of bananas (*paragraph 6*)
- no impact on the supply of bananas as this is perfectly inelastic in the short run and banana imports are banned (*paragraph 7*)
- the government will receive less sales tax as this is a percentage of the price (ceiling price)
- a maximum price (ceiling price) would only have short-term effects as in 6-12 months supply would be restored
- it is possible that a parallel market for bananas may arise.

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Examiners must 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) structural unemployment (paragraph ②) *[2 marks]*

level

0	<i>Wrong definition</i>	0
1	<i>Vague definition</i> The idea that it is unemployment due to a change in the structure of the economy.	1
2	<i>Precise definition</i> Any one of the following would be appropriate: <ul style="list-style-type: none"> • long-term unemployment that is caused as a result of a fall in the demand for a particular type of labour • unemployment that occurs as a result of the changing structure of an economy resulting from changes in demand/supply and/or technology • unemployment that occurs when there is a mismatch between the skills of unemployed workers and the jobs available • unemployment that exists as a result of rigidities in the labour market. 	2

(ii) oligopoly (paragraph ③). *[2 marks]*

level

0	<i>Wrong definition</i>	0
1	<i>Vague definition</i> The idea that it is a market structure where a small number of firms dominate.	1
2	<i>Precise definition</i> An explanation that refers to any two of the following characteristics – number of buyers and sellers, type of product (usually differentiated) but could be homogeneous, with a suitable example, such as oil or cement), interdependent behavior, and barriers to entry.	2

(b) **Using an AD/AS diagram, explain how supply-side policies could affect real output in the long-run.** **[4 marks]**

level

- | | | |
|---|--|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <i>Identification of appropriate theory</i>
For drawing a correctly labelled AD/AS diagram with a movement of the LRAS showing an increase in real output or an explanation of how supply-side policies can increase real output in the long run such as by increasing the quantity and/or quality of factors of production. | 1-2 |
| 2 | <i>Correct application of appropriate theory</i>
For drawing a correctly labelled AD/AS diagram with a movement of the LRAS showing an increase in real output and an explanation of how supply-side policies can increase real output in the long run such as by increasing the quantity and/or quality of factors of production. | 3-4 |

If candidates draw a short run aggregate supply curve, then they should receive zero for the diagram, although they may gain **[2 marks]** or a suitable explanation.

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 a production possibility curve diagram, explain how the discovery of new oil reserves might affect the Russian economy.** [4 marks]

level

- | | | |
|---|---|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <i>Identification of appropriate theory</i>
For drawing a correctly labelled PPC showing a movement to the right to illustrate an increase in potential output or an explanation of how a discovery of new oil reserves can increase the potential output of the Russian economy by increasing the amount of resources available. | 1-2 |
| 2 | <i>Correct application of appropriate theory</i>
For drawing a correctly labelled PPC showing a movement to the right to illustrate an increase in potential output and an explanation of how a discovery of new oil reserves can increase the potential output of the Russian economy by increasing the amount of resources available. | 3-4 |

Candidates may explain that the oil was there already and so the factor existed and was simply not being used. The discovery and use of the oil could therefore be illustrated by a movement from a point within the PPC to a point closer to the curve, as opposed to a shift of the PPC. This may be fully rewarded, but **only** if the explanation is complete and clear.

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

For a PPC, the axes could be two alternative products, one on each axis, e.g. Good A and Good B or schools and motor cars: or two groups of products, e.g. consumer goods and producer goods. A title is not necessary.

- (d) **Using information from the text/data and your knowledge of economics, evaluate the economic performance of Russia and Poland since the 1990s.** [8 marks]

Responses **may** include:

Russia:

- has had an increase in corruption and crime due to lack of strong property rights (*paragraph 3*)
- oligopoly market structure has developed (*paragraph 3*)
- dependent on the natural resource area for its growth (has been very high) (*paragraph 3*)
- has a large current account surplus, especially with the export of oil (*Figure 1*)
- inflation rate is coming down but is still relatively high (*Figure 4*)
- income inequality has worsened (*paragraph 3*)
- unemployment is relatively low (*Figure 2*)
- growth in production is very high fuelled by the natural resource area (*Figure 3*).

Poland:

- strengthened property rights and monetary controls, privatized and modernized its private sector which encouraged economic growth, employment and income generation
- need to reform the labour market to reduce the natural rate of unemployment
- inflation has been stable, but peaked to a little over 4% in 2005 (*Figure 4*)
- current account deficit is approximately – 2% of GDP due to exports of goods and services being less than imports (*Figure 1*)
- “rigidity” of the labour market has resulted in a high rate of structural unemployment (*paragraph 2*)
- the unemployment rate in Poland, while falling is still very high (*Figure 2*)
- sustainable/steady growth (*Figure 3*).

Candidates could make a judgment on the importance of factors contributing to the economic performance of Russia and Poland or they could compare the two economies and make a judgment as to which economy has performed better, justifying their judgment.

Examiners must 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) factors of production (paragraph ③) *[2 marks]*

level

0 *Wrong definition* **0**

1 *Vague definition* **1**
The idea that they are the resources used in production.

2 *Precise definition* **2**
An explanation that they are the four types of resources used in the production process: land, labour, capital (and possibly entrepreneurship / management / enterprise).

(ii) aggregate demand (paragraph ④). *[2 marks]*

level

0 *Wrong definition* **0**

1 *Vague definition* **1**
The idea that it is total demand in an economy.

2 *Precise definition* **2**
An explanation that it is the total demand for all goods and services produced in an economy

OR

This comprises $C+I+G+(X-M)$ is also sufficient.

(b) Using an appropriate diagram, explain why the Chinese government is expected to “respond to rising inflation with one or possibly two interest rate rises” (paragraph 5).

[4 marks]

level

0 *Inappropriate answer*

0

1 *Identification of appropriate theory*

1-2

For drawing a correctly labelled AD/AS diagram indicating a shift in AD to the right **or** for explaining that the increase in aggregate demand in China has led to an increase in inflation, which has disadvantages, forcing the government to consider raising interest rates to curb inflationary pressures.

2 *Correct application of appropriate theory*

3-4

For drawing a correctly labelled AD/AS diagram indicating a shift in AD to the right **and** for explaining that the increase in aggregate demand in China has led to an increase in inflation, which has disadvantages, forcing the government to consider raising interest rates to curb inflationary pressures.

Some candidates may show a shift in the AD curve to the left indicating that the government has responded to the inflation threat by raising interest rates, which will increase the cost of borrowing and lead to reduced consumption and investment spending. While technically not correct, as this is a consequence and not the reason why the government is raising the interest rates, it can achieve full marks if drawn and explained appropriately.

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 how the effect of capital inflows from speculators “has the potential to damage the competitive position of Chinese exporters” (paragraph 5).** **[4 marks]**

level

- | | | |
|---|--|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <i>Identification of appropriate theory</i>
For drawing a correctly labelled foreign exchange diagram, showing a shift to the right/increase in demand for Chinese currency causing an increased price of Chinese currency relative to other currencies or for explaining that the increased value of the Chinese currency will make exports from China now relatively more expensive and less competitive in international markets. | 1-2 |
| 2 | <i>Correct application of appropriate theory</i>
For drawing a correctly labelled foreign exchange diagram, showing a shift to the right/increase in demand for Chinese currency causing an increased price of Chinese currency relative to other currencies and for explaining that the increased value of the Chinese currency will make exports from China now relatively more expensive and less competitive in international markets. | 3-4 |

Some candidates may draw a diagram showing a managed/fixed exchange rate and explain that since China operates this system, the exchange rate would not change and so the competitive position would be the same. This approach may be fully rewarded.

There may be different diagrams and/or labelling used to show the above, and any appropriate diagram and/or labelling may be fully rewarded. The actual currency of China, the Renminbi (also Yuan) is not referred to in the text, so the vertical axis could be as basic as exchange rate and the horizontal axis could be as basic as quantity of currency.

- (d) **Using information from the text/data and your knowledge of economics, evaluate factors that could have caused China’s inflation to increase recently.**

[8 marks]

Responses **may** include:

- a definition of inflation
- an explanation of the difference between demand-pull and cost-push inflation. Diagrams illustrating these two causes of inflation may be included
- evaluation may be in terms of short-term and long-term impacts on inflation.

An evaluation of factors which could have caused rising inflation such as:

- rising aggregate demand (consumption, investment, government spending, net exports)
- excess demand above potential growth
- external shocks, such as increased oil prices
- increased costs of electricity, water, broadband, gas (*paragraph 1*)
- higher corn prices and the impact on the cost of feed (*paragraph 2*)
- a shortage of livestock (pigs) caused by deaths due to disease (*paragraph 2*)
- declining factors of production *e.g.* arable land and water (*paragraph 3*)
- rising wage costs, now exceeding productivity growth (*paragraph 3*)
- increased government charges for the environment and land (*paragraph 3*).

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

Examiners must 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) tariff (paragraph 1) **[2 marks]**

level

0	<i>Wrong definition</i>	0
1	<i>Vague definition</i> The idea that a tariff is a form of protectionism.	1
2	<i>Precise definition</i> An explanation that it is a tax on imports.	2

(ii) foreign direct investment (paragraph 3). **[2 marks]**

level

0	<i>Wrong definition</i>	0
1	<i>Vague definition</i> The idea that it is an investment from overseas.	1
2	<i>Precise definition</i> An explanation that it is capital expenditure (long-term investment) by a company in a foreign country.	2

(b) “The price of a Honda motorbike has gone down from US\$2200 to US\$1600” (*paragraph 2*). Using an appropriate diagram, explain the impact on the quantity demanded of Honda motorbikes of a decrease in price of Honda motorbikes.

[4 marks]

level

0 *Inappropriate answer*

0

1 *Identification of appropriate theory*

1-2

For drawing a correctly labelled demand diagram showing a movement down the existing demand curve for Honda motorbikes **or** for providing an explanation that the lower price for Honda motorbikes will lead to an increase in the quantity demanded (expansion in demand) for this product in Vietnam. Demand does not increase and so the demand curve does not shift.

2 *Correct application of appropriate theory*

3-4

For drawing a correctly labelled demand diagram showing a movement down the existing demand curve for Honda motorbikes **and** for providing an explanation that the lower price for Honda motorbikes will lead to an increase in the quantity demanded (expansion in demand) for this product in Vietnam. Demand does not increase and so the demand curve does not shift.

Some candidates may show a shift in the supply curve to the right as a result of the lower tariffs and lower costs of production. This causes a movement along the demand curve. This is acceptable and can be fully rewarded. They may also draw a tariff diagram, with a falling tariff, falling price and so an increase in the demand for motorbikes.

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 how tariff cuts could put “downward pressure on inflation” (paragraph 2). [4 marks]

level

- | | | |
|---|---|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <i>Identification of appropriate theory</i>
For drawing a correctly labelled tariff diagram showing a downward shift in the S (World) plus tariff curve or for explaining that tariff cuts will reduce the cost of imported inputs or semi-finished goods in the production process (business costs), or finished goods for consumers and lead to downward pressure on inflation. | 1-2 |
| 2 | <i>Correct application of appropriate theory</i>
For drawing a correctly labelled tariff diagram showing a downward shift in the S (World) plus tariff curve and for explaining that tariff cuts will reduce the cost of imported inputs or semi-finished goods in the production process (business costs), or finished goods for consumers and lead to downward pressure on inflation. | 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.

- (d) **Using information from the text/data and your knowledge of economics, evaluate the impact of the lower tariffs in Vietnam on domestic producers, consumers and the government.**

[8 marks]

Responses **may** include:

- a tariff diagram.

Impacts on domestic producers:

- increased competition between local and foreign goods (*paragraph 2*)
- increased sales of imported goods
- decreased sales of domestically produced goods
- lower costs of production for businesses using imported inputs (*paragraph 2*)
- improvements in efficiency and allocation of resources caused by the reduction of the deadweight loss arising from the lower tariffs
- increased FDI
- increased exports.

Impacts on consumers:

- cheaper imported goods provides an increase in consumer surplus
- a wider choice of imported goods
- reduced prices for locally produced goods
- expanded consumer choice with more goods available (*paragraph 2*).

Impacts on government:

- decrease in tax revenue from tariffs, estimated to be US\$63 million per year for the first five years (*paragraph 3*)
- increased short-term unemployment
- reduced costs putting downward pressure on inflation (*paragraph 2*)
- increased economic growth
- increased revenue from the growing economy to offset the loss of tariff revenue (*paragraph 3*).

Candidates must consider the impact upon all three stakeholders, domestic producers, consumers and the government, to move beyond Level 2.

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

Examiners must 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) economic growth (paragraph ㉓) *[2 marks]*

level

0 *Wrong definition* **0**

1 *Vague definition* **1**
The idea that it is an increase in the economy.

2 *Precise definition* **2**
An explanation that it is increased real output for an economy over time (an increase in GDP). Alternatively, it may be explained as an increase in the potential output of the economy through an increase in the quantity/quality of resources.

(ii) quotas (paragraph ㉓). *[2 marks]*

level

0 *Wrong definition* **0**

1 *Vague definition* **1**
The idea that it is a limit on imported goods.

2 *Precise definition* **2**
An explanation that they are limits on the quantity (or value) of imports (set by a government).

(b) Explain how the poverty cycle acts as a barrier to economic development (paragraph 4). [4 marks]

level

- | | | |
|---|---|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <i>Identification of appropriate theory</i>
For explaining that a poverty cycle acts as a trap or barrier to economic development because it is self-perpetuating unless the cycle can be broken or for providing an example such as the cycle where low incomes perpetuate low incomes via low savings and investment. (There are many poverty cycles that may be used and, if the example is feasible, then it should be fully rewarded.) | 1-2 |
| 2 | <i>Correct application of appropriate theory</i>
For explaining that a poverty cycle acts as a trap or barrier to economic development because it is self-perpetuating unless the cycle can be broken and for providing an example such as the cycle where low incomes perpetuate low incomes via low savings and investment. (There are many poverty cycles that may be used and, if the example is feasible, then it should be fully rewarded.) | 3-4 |

(c) **Using a subsidy diagram, explain how a subsidy given by a wealthy country to its own producers, could lead to reduced income for producers in a poor African country.**

[4 marks]

level

0 *Inappropriate answer*

0

1 *Identification of appropriate theory*

1-2

For drawing a correctly labelled subsidy diagram showing that a subsidy will cause supply of the good to shift right/increase and price to fall **or** for explaining that a subsidy will increase supply of the good, reduce the price of the good, making the produce of an African country less internationally competitive which may lead to reduced income for producers in a poor African country.

2 *Correct application of appropriate theory*

3-4

For drawing a correctly labelled subsidy diagram showing that a subsidy will cause supply of the good to shift right/increase and price to fall **and** for explaining that a subsidy will increase supply of the good, reduce the price of the good, making the produce of an African country less internationally competitive which may lead to reduced income for producers in a poor African country.

Some candidates may explain that the lower priced goods in the wealthy countries may then be exported to Africa, destroying the industries in African countries by undercutting domestic prices. This is an equally good response and should be fully rewarded.

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 ways in which wealthy countries could encourage economic development in African nations.

[8 marks]

Responses **may** include at least one of the following:

- definition of economic development
- evaluation of development assistance/official assistance
- evaluation of debt relief
- evaluation of humanitarian aid
- evaluation of a fairer trade system:
 - increases trade with other nations
 - allows African nations to earn more money so they can develop their economies and pay for their own health care and education (paragraph 1)
 - reduce tariffs on processed goods (e.g. Ghana – cocoa exports) (paragraph 4)
 - reduce quotas
 - reduce subsidies which protect countries by about \$1 billion a day (paragraph 3)
 - relevant diagrams may be drawn
- an evaluation of any other relevant strategy for providing basic needs, such as foreign direct investment.

Examiners must 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
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