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ECONOMICS **9708/21**

Paper 2 Data Response and Essay **May/June 2017**

MARK SCHEME

Maximum Mark: 40

Published

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Question	Answer	Marks	Guidance
1(a)(i)	• For a diagram showing an increase in supply or a decrease in demand. (1 mark) • For an accompanying explanation giving possible reasons for the shift in supply or demand. (1 mark)	**2**	The fall in price could be caused by either an increase in supply or a decrease in demand.
1(a)(ii)	For an explanation that • the fall in the price of oil has resulted in a fall in export revenues (1 mark) • and a fall in the demand for the peso (1 mark). (2 marks maximum)	**2**	The context of the case study makes it clear that the fall in the price of oil has resulted in a fall in Colombia's export revenues. This has resulted in a fall in the demand for the peso.
1(b)	For a clear diagram of production possibility curves. (Up to 2 marks) For an explanation of the increased possibility of the production of capital goods or the development of human capital that will generate growth in the economy. (Up to 2 marks) Maximum of 2 marks if no diagram.	**4**	The prospects of the end of the rebel insurgency will allow the Colombian government to spend less on the military. Resources can be diverted to the production of capital goods or to enhanced training of labour that will shift the PPC outwards. This is the 'peace dividend'

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Question	Answer	Marks	Guidance
1(c)	For explaining how each component is affected with due reference to the data. Consumption has fallen because of the fall in incomes and the rise in taxes. (Up to 2 marks) Investment has fallen because of the fall in activity (Puerto Gaitan). (Up to 2 marks) Government expenditure has fallen because of the fall in government revenues. (Up to 2 marks) Net exports have fallen because of the fall in oil prices and export revenues. (Up to 2 marks) (6 marks maximum) (If only 3 components are explained, then 5 marks maximum)	**6**	**Candidates need to interpret the data to explain how each of the four components has been affected.**
1(d)	At least **two** factors must be explained for full marks. • For any one factor explained (Up to 4 marks) (6 marks maximum)	**6**	The relevant factors include • the price elasticity of demand for Colombia's exports and imports and whether the Marshall-Lerner condition is fulfilled. • The price elasticity of supply of Colombia's exports. • The time period under consideration; J-curve effect. • The reaction of Colombia's competitors in world trade.

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Question	Answer	Marks	Guidance
2(a)	For **knowledge and understanding** • of the meaning of a merit good (Up to 3 marks) • and a public good (Up to 3 marks). **(4 marks maximum)** For **application** showing • understanding of the reasons that profit can be made in the supply of merit goods, • but not in the supply of public goods. **(4 marks maximum)**	**8**	The goods should be distinguished through the qualities of excludability, diminishability and rejectability. The explanation should be based upon the free-rider problem that occurs in the supply of public goods.

Question	Answer	Marks	Guidance
2(b)	For **analysis** that explains: • The way in which an indirect tax is used to reduce the consumption of alcohol with due reference to the strengths and weaknesses of this approach. (Up to 6 marks) • The way in which an awareness campaign is used to reduce the consumption of alcohol with due reference to the strengths and weaknesses of this approach. (Up to 6 marks) **(8 marks maximum)** For **evaluation** that **assesses and compares** • the relative strengths and weaknesses of each approach (Up to 3 marks) • and for reaching a conclusion on which approach is likely to be most effective. (1 mark). **(4 marks maximum)**	**12**	A demerit good should be explained in terms of incomplete information of the harm that it can cause. An indirect tax is designed to reduce supply and increase price. An awareness campaign is designed to decrease demand for the demerit good. Evaluative points include the following: • the fact that the demand for alcohol might be price inelastic • the fact that an awareness campaign might be costly • the fact that an awareness campaign might take a long period to take effect

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Question	Answer	Marks	Guidance
3(a)	For **knowledge and understanding** • of the term equilibrium (Up to 3 marks) • and where it occurs in the context of the market for a normal good.(Up to 3 marks). **(4 marks maximum)** For **application** • showing how price allocates resources when there is an increase in demand. **(4 marks maximum)**	**8**	Equilibrium in a market occurs where there is 'no tendency for price or quantity to change'. In the market for a normal good, it occurs where the demand and supply curves intersect. If there is an increase in demand the demand curve will shift to the right causing an excess demand for the normal good. This will cause market forces to raise equilibrium price and quantity.
3(b)	For **analysis** that explains: • How maximum prices operate when imposed below equilibrium. (Up to 2 marks) • The difficulties that arise when maximum prices operate during a period of high inflation. (Up to 6 marks) **(8 marks maximum)** For **evaluation:** • commenting on whether difficulties can be overcome (Up to 3 marks) • and for reaching a conclusion on the likelihood that this will be successful. (1 mark) **(4 marks maximum)**	**12**	The difficulty in imposing maximum prices below equilibrium is that shortages will occur. These shortages will become more pronounced as inflation occurs unless the maximum prices are continually moved upwards. Other difficulties include the administrative costs and the extent to which the price legislation can be policed. The problems could be overcome, e.g. with rationing, but whether this will be successful depends upon a number of factors.

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Question	Answer	Marks	Guidance
4(a)	For **knowledge and understanding** • of demand-pull inflation (up to 3 marks) • and cost-push inflation (up to 3 marks) **(4 marks maximum)** For **application** • showing how a decline in an economy's exchange rate can cause cost-push inflation (Up to 3 marks) • and demand-pull inflation. (Up to 3 marks). **(4 marks maximum)**	**8**	A fall in the exchange rate will lead to a fall in the price of exports and a rise in the price of imports. This will lead to a rise in net exports and this will increase aggregate demand that could result in inflation. The rise in the price of imports will increase import prices and this might increase input costs leading to cost-push inflation.
4(b)	For **analysis** that explains: • The aims and objectives of supply side policies with appropriate examples. (Up to 6 marks) • How the methods adopted are designed to solve the problem of inflation with due reference to the strengths and weaknesses of these methods. (Up to 6 marks) **(8 marks maximum)** For **evaluation** that **assesses and compares** • the relative strengths and weaknesses of different supply side policies (Up to 3 marks) • and for reaching a conclusion on their likely effectiveness. (1 mark). **(4 marks maximum)**	**12**	Supply side policy is designed to increase the aggregate supply curve of the economy. Methods that might be adopted include • measures to increase the supply of capital goods • measures to increase the labour supply to prevent upward pressure upon costs Evaluative comment might include: • the expense of supply side policy • the fact that it might take a long time to be effective

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