CAMBRIDGE INTERNATIONAL EXAMINATIONS

International General Certificate of Secondary Education

MARK SCHEME for the May/June 2014 series

0455 ECONOMICS

0455/22 Paper 2 (Structured Questions), maximum raw mark 90

This mark scheme is published as an aid to teachers and candidates, to indicate the requirements of the examination. It shows the basis on which Examiners were instructed to award marks. It does not indicate the details of the discussions that took place at an Examiners' meeting before marking began, which would have considered the acceptability of alternative answers.

Mark schemes should be read in conjunction with the question paper and the Principal Examiner Report for Teachers.

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1 (a) Why is the Angolan economy considered to be 'specialised'? [2]

1 mark each for any of the following two:

- most of its output is oil/plays a key role in the economy/country too dependent on oil/dependent on oil/most of its resources are devoted to oil
- oil production accounts for 97% of its export revenue
- provides 75% of government tax revenue
- government trying to develop other industries/diversify

Note: no marks for produces 1.9m barrels a day/large quantity of oil/specialises in oil.

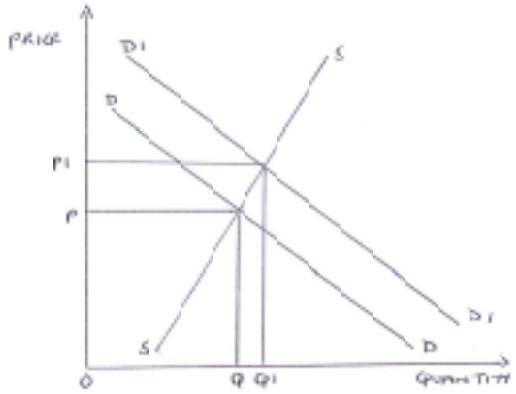
(b) Using information from the extract, explain why taxi (cab) fares were high in Luanda in 2010. [2]

1 mark for recognising there is only one firm/a monopoly.
1 mark for mentioning that the lack of competition enables firms to drive up price/firm is a price maker/price can be driven up because demand is inelastic.

(c) Using information from the extract, draw a demand and supply diagram to show what is likely to have happened to the price of diamonds in 2012. [4]

1 mark for axes correctly labelled – price and quantity or P and Q.
1 mark for demand and supply curves correctly labelled.
1 mark for demand curve shown shifted to the right.
1 mark for correct equilibriums identified either by lines drawn to both axes or equilibrium points clearly identified e.g. E and E1.

Figure 1(c)



(d) Explain why countries with a high population growth rate may have a lower average income than countries with a lower population growth rate. [3]

- May result in more dependants [1] due to rise in birth rate or fall in death rate [1].
- May mean fewer workers [1] if there is a high birth rate, there may be fewer parents in the labour force [1].
- A higher labour force may increase competition for jobs [1] may push down wages [1].
- There may not be enough vacancies [1] for increasing number of potential workers [1].
- Resources may be devoted to providing for the extra population [1] rather than expanding productive capacity [1].

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- Population may grow more rapidly than GDP/average income is GDP divided by population [1].
- Population growth may be caused by low income [1].

Note: these points may be inter-linked. 3 marks may be awarded for one reason that is well developed.

(e) Analyse whether the information in Table 1 supports the view that countries with a high population growth rate have a lower average income than countries with a lower population growth rate. [4]

- Generally the information supports the view/ supports the view. [1]
- Uganda has the highest population growth rate and the lowest real GDP per head/Kenya's population growth rate is higher than Nigeria's and its income per head is lower. [1]
- South Africa has the lowest population growth rate and the highest real GDP per head. [1]
- Angola is an exception – second in both rankings. [1]

(f) Discuss whether an increase in a country's GDP will reduce poverty in that country. [5]

Up to 3 marks for why it might:
Up to 3 marks for: may generate more tax revenue [1] which can be used on spending on benefits [1] or on measures to reduce poverty in the long run e.g. education and health care [1].

Up to 3 marks for: high GDP may increase average incomes/living standards [1] higher incomes may enable people to spend more on basic necessities [1] such spending will reduce absolute poverty [1].

Up to 3 marks for: higher output will create jobs [1] this will reduce unemployment [1] with more in work absolute poverty will fall [1].

Up to 3 marks for why it might not:
Up to 3 marks for: income may be unevenly distributed [1] and so not every one may benefit from higher incomes [1] and so relative poverty may rise [1] even if absolute poverty falls [1].

Up to 2 marks for: real GDP may not have increased [1] need to adjust for inflation [1].

Up to 2 marks for: (real) GDP per head may not have increased [1] if population has risen by more than GDP [1].

Maximum of 3 marks for a list-like response.

(g) Using information from the extract, explain <u>two</u> reasons why labour productivity is low in Angola. [4]

1 mark each for two reasons identified:
- lack of capital equipment
- subsistence farming
- lack of education/high degree of illiteracy
- poor health care.

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1 mark each for two reasons explained:

- workers will not be able to produce much if they are working with low amounts of capital
- subsistence farming tends to use poor quality resources
- poor education will mean workers are unable to work with advanced technology/will be less inventive/will lack skills
- poor health care may result in workers being off sick/being tired.

(h) Discuss whether a cut in taxes will reduce unemployment. [6]

Up to 4 marks why it might:
Up to 3 marks for: a cut in income tax will increase disposable income [1] this may increase the incentive to work [1] a greater incentive may reduce voluntary/frictional unemployment [1].

Up to 3 marks for: a cut in corporation tax will increase the profit firms can keep [1] this may encourage firms to expand [1] and so take on more workers [1].

Up to 3 marks for: a reduction in income tax and indirect taxes will increase purchasing power [1] this may increase demand [1] and so cyclical unemployment may fall [1].

Up to 4 marks for why it might not:
Up to 3 marks for: firms may not spend extra profits on expansion [1] if they lack confidence [1] that they will sell the extra output [1].

Up to 3 marks for: consumers may not spend extra income [1] if they lack confidence [1] instead they may save the extra income [1].

Up to 3 marks for: tariffs may be cut [1] which may increase imports [1] and raise unemployment, at least, in the short run [1].

Up to 3 marks for: government spending may fall [1] due to less revenue [1] and as a result cyclical unemployment may stay unchanged/increase [1].

Up to 3 marks for: higher demand may cause inflation [1] may result in workers pressing for wage rises [1] firms may make workers redundant to cut costs [1].

Up to 3 marks for: a cut in taxes on firms may encourage firms to use more capital-intensive methods (1) resulting in lower demand for labour (1) causing technological unemployment (1)

Up to 2 marks for: frictional and structural unemployment may not fall [1] if unemployed workers are still occupationally and/or geographically immobile [1].

Maximum of 3 marks for a list-like response.

2 (a) What is meant by the 'economic problem'? [2]
2 marks for wants exceeding resources or wants are unlimited/infinite whilst resources are limited/finite or 1 mark for limited resources or scarcity.

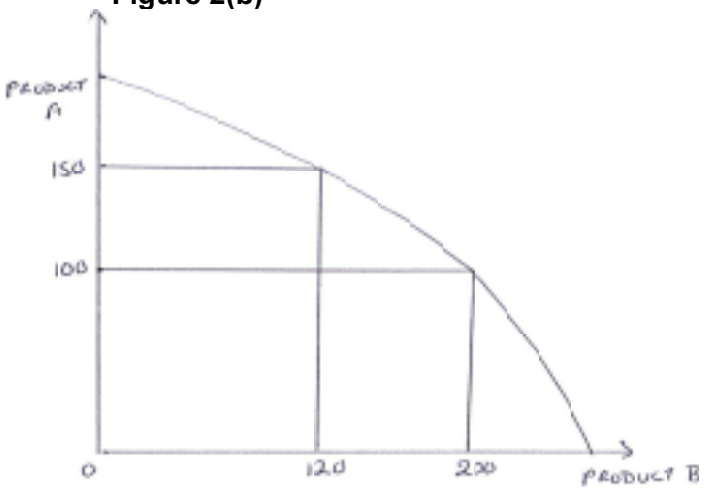
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(b) Using a production possibility curve diagram, explain why choices have to be made as to how to allocate resources. [6]

Up to 3 marks for the diagram:

- 1 mark for axes correctly labelled in terms of two different products or types of products.
- 1 mark for curve or downward sloping line – drawn to the axes.
- 1 mark for showing a trade off.

Figure 2(b)



Up to 3 marks for written comments:

- definition of opportunity cost (1)
- recognition choice arises because of scarcity (1)
- example based on the diagram: if an economy produces e.g. 200 units of B it cannot produce 150 units of Product A (1)
- recognising that if an economy chooses to allocate more resources to making one product, it has to allocate fewer resources to another product/chooses to make more of one product it has to produce less of another product (2).

(c) Explain how resources are allocated differently in market and mixed economic systems. [4]

Up to 3 marks on market economy:
1 mark for recognising that in a market economy the price system allocates resources.

1 mark for referring to the rate of demand and supply in a market economy/consumer sovereignty.

1 mark for role of the profit motive in a market economy.

1 mark for resources are allocated by the private sector/there is no government intervention.

Up to 3 marks on mixed economy:
1 mark for recognising the price system determines the allocation of some resources in a mixed economy.

1 mark for recognising that the government decides on the allocation of some resources in a mixed economy e.g. governments produce public goods, governments produce or subsidise merit goods and tax demerit goods.

1 mark for recognising there is both a private and public sector.

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(d) Discuss whether an economy would benefit from an increase in the provision of health care. [8]

Up to 6 marks for why it might:
Up to 3 marks for: likely to improve the health of workers [1] this should raise labour productivity [1] and so increase output/GDP [1].
Up to 3 marks for: possible reduction in birth rate [1] this may increase the labour force [1] and reduce dependency ratio [1].

Up to 2 marks for: likely to increase the quality of life/standard of living [1] which should increase life expectancy [1]

Up to 2 marks for: more people are likely to be employed in health care [1] this may reduce unemployment [1].

Up to 2 marks for: may make an economy a more attractive destination for FDI [1] which may provide a number of benefits e.g. advances in technology, higher employment [1].

Up to 6 marks for why it might not:
Up to 3 marks for: if resources are fully employed [1] it will involve an opportunity cost [1] e.g. fewer resources may be devoted to education [1].

Up to 3 marks for: may reduce the death rate [1] this may increase dependency ratio [1] and increase the cost of pensions [1].

Up to 3 marks for: more health care may be provided but the quality may not rise [1] population may increase by more than the extra provision [1] inefficiency may rise [1].

Maximum of 4 marks for a list-like response.

3 (a) Define 'demand'. [2]
2 marks for the willingness and ability to buy a product or 1 mark for either willingness or ability to buy.

(b) Explain <u>three</u> likely causes of increase in demand for bicycles. [6]

1 mark each for three causes identified e.g.:
- rise/fall in income (may be regarded as a normal or an inferior good)
- rise in the price of other forms of transport
- a greater desire to be fit/tastes
- rise in population size
- a successful advertising campaign

1 mark each for three explanations e.g.:
- with higher incomes, people are more able to buy bicycles
- cycling is a substitute for bus travel
- cycling is used both for transport and for leisure
- a larger population will mean there are more people to buy bicycles
- a successful advertising campaign will persuade more people to buy bicycles.

Note: accept any valid reason which would shift the demand curve for bicycles to the right but do not accept a change in price or a change in supply of bicycles.

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(c) Analyse why the demand for a product may be more price elastic in one country than in another country. [6]

1 mark for bringing out the meaning of PED or elastic demand – defined or implied.

- differences in the closeness of substitutes [1] availability of close substitutes will make demand elastic [1]
- differences in the proportion of income spent on the product [1] the higher the proportion, the more elastic demand will be [1] note: also accept average income may vary in the two countries with demand being more inelastic in the richer country
- differences in what are considered to be luxuries and what are considered to be necessities [1] if the product is considered to be a luxury, demand is likely to be elastic [1]
- differences in the price of bicycles [1] demand will be more elastic, the higher the price [1].

Note: a maximum of 3 marks for identification of reasons.

(d) Discuss whether a government should impose indirect taxes only on products with inelastic demand. [6]

Up to 4 marks for why it should:

- imposing taxes on products with inelastic demand will cause price to rise [1] demand will fall by a smaller percentage [1] and so is a good source of tax revenue [1] higher tax revenue can be spent on e.g. education and health care [1]
- a significant rise in price may be needed to reduce demand [1] of harmful products [1].

Up to 4 marks for why it should not:

- indirect taxes may be imposed on products to discourage their consumption [1] will be more successful if demand is price elastic [1] demand will fall by more than the rise in price [1] a government may want to discourage consumption of demerit goods (not necessary to use the term) [1] also may want to discourage consumption of imports [1] in practice it may be difficult to estimate PED (1).
- some products with inelastic demand are basic necessities (1) and so imposing indirect taxes on them will harm the poor (1) indirect taxes are often regressive (1).

4 (a) Describe <u>two</u> functions of a central bank. [4]

1 mark each for two functions identified e.g.:

- issuing bank notes
- banker to the government
- banker to commercial banks
- managing the national debt
- lender of last resort
- implementing monetary policy

1 mark each for two descriptions e.g.:

- influences the money supply
- operates an account for the government which enables it to receive revenue and make payments
- commercial banks' accounts at the central bank enable them to make and receive payments between each other and to withdraw money

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- issues government securities and pays interest on those securities
- will lend to commercial banks that find themselves in difficulty
- changes interest rates to control the exchange rate
- may adjust exchange rate to influence e.g. the current account position.

(b) Explain <u>two</u> types of internal economy of scale that a growing bank can enjoy. [4]

1 mark each for two types identified e.g.:
- managerial
- financial
- technical
- risk bearing.

1 mark each for explanations of the two types identified linked to banking e.g.
- a larger bank may be able to employ specialist workers such as accountants
- a larger bank may be able to sell its shares more easily and/or borrow more easily from other banks
- a larger bank may be able to use advanced technology and large scale capital equipment
- a larger bank may be able to offer a range of financial services so if one is unsuccessful, it will not have a significant impact on profits.

(c) Analyse how the spending pattern of high paid workers is likely to differ from the spending pattern of low paid workers. [4]

1 mark for high paid workers are likely to spend more in total.

1 mark for high paid workers are likely to spend a lower proportion of their income.

1 mark for high paid workers are likely to spend a higher proportion of their income on luxuries/spend more on luxuries.

1 mark for high paid workers are likely to spend a lower proportion of their income on necessities/less on necessities.

Note: accept an answer which is based on low paid workers e.g. low paid workers spend less in total.

(d) Discuss whether workers employed in banking are likely to earn more than workers employed in agriculture. [8]

Up to 6 marks for why they might earn more e.g.:
Up to 3 marks for: some bank workers are skilled workers [1] these are in low supply [1] high demand [1].

Up to 3 marks for bank workers may be difficult to replace [1] may be very productive [1] and so have inelastic demand [1].

Up to 2 marks for: bank workers may need high qualifications/better trained [1] and so have inelastic supply [1].

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Up to 2 marks for bank workers may be in a professional organisation/trade union [1] and this will give them more bargaining power [1].

Up to 6 marks for why they might not earn more e.g.:
Up to 4 marks for: some workers in banking are low skilled [1] e.g. cleaners whilst some workers in agriculture are high skilled [1] so supply of some bank workers may be higher than some agricultural workers [1] and demand may be lower [1].

Up to 3 marks for: some agricultural workers are very experienced [1] pay tends to rise over time [1] due to promotion [1].

Up to 2 marks for: agricultural workers in a rich country may earn more than workers in banking in a poor country [1] earnings vary between countries [1].

Up to 2 marks for agricultural workers in some countries may be more likely to be in a union/labour organisation (1) and so may have more bargaining power (1).

Note: the question is a general one and so candidates do not have to refer to Turkey but those answers which mention that workers in banking in Turkey may be paid more because the industry is expanding should be credited.

Maximum of 4 marks for a list-like approach.

5 (a) Define a 'multinational company'. [2]

2 marks for a company that produces in more than one country.

1 mark for any **one** of the following:
- has its headquarters in another country
- operates in more than one country
- has branches in more than one country
- is usually a PLC (but may be a state run MNC).

(b) Explain one goal a multinational company may have other than profit maximisation. [3]

1 mark for identifying a goal i.e.:
- growth/increased market share
- sales revenue maximisation
- profit satisficing
- survival
- improve the environment performance of the company.

Up to 2 marks for explaining the goal e.g.
- an MNC may try to increase its size because it will make it more difficult for other firms to buy it [1] and because the salaries and managers may be linked to size [1]
- an MNC may try to increase market share to reduce competition [1] and so gain a monopoly position [1]
- achieving a high sales revenue may enable a firm to take greater advantage of economies of scale [1] and so reduce average costs [1]
- an MNC may wish to keep shareholders happy (profit satisficing) [1] and to pursue a range of other objectives e.g. improving environmental conditions [1].

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(c) Explain why pollution is an example of market failure. [5]

Up to 2 marks for defining market failure – where the market forces of demand and supply fail to achieve efficiency.

1 mark for recognising that pollution is an external cost/harmful impact on third parties.

1 mark for mentioning that market forces do not take into account external costs.

1 mark social costs will exceed private costs.

1 mark for mentioning that market prices do not reflect social costs/are too low.

1 mark for output will be too high.

(d) Discuss whether a mine operated by the government would be more likely to benefit an economy than one operated by a foreign multinational company. [10]

Up to 7 marks for why it might:
Up to 4 marks for: more likely to take into account social costs and benefits [1] rather than base decisions on private costs and benefits [1] as it main objective may be to benefit society [1] rather than maximise profit [1].

Up to 4 marks for: may have more funds to invest [1] can use tax revenue [1] this may enable it to expand production [1] and so raise employment [1].

Up to 3 marks for: may provide better pay [1] and working conditions for workers [1] e.g. shorter working hours [1].

Up to 3 marks for; may charge lower prices to domestic firms [1] lower costs of production [1] making them more price competitive [1].

Up to 2 marks for: unlikely to take profits out of the country [1] may use some of the profits to spend on e.g. education and health care [1].

Up to 7 marks for explaining why it might not:
Up to 5 marks for: may lack competitive pressure to be efficient [1] managers of the mine may think the government will not permit the mine to go out of business [1] as it would cause unemployment [1] so costs may not be kept low [1] may be a lack of innovation [1].

Up to 3 marks for: may lack funds to invest [1] government may have low tax revenue [1] will not be able to sell shares [1].

Up to 3 marks for: may lack expertise [1] government intervention may mean that it takes time to make decisions [1] and decisions may be distorted by political factors [1].

Up to 2 marks for: may be less likely to bring in new technology than an MNC [1] technology may be more advanced in other countries [1].

Maximum of 5 marks for a list-like response.

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6 (a) What is meant by 'monetary policy'? [2]

2 marks for reference to decisions on any two from interest rates, money supply and the exchange rate.

1 mark for reference to decisions on any one of the above.

(b) Explain <u>two</u> reasons why governments aim for low and stable inflation. [4]

1 mark each for two reasons identified:
- to promote investment
- to promote international competitiveness
- to avoid lenders, workers with low bargaining power and other groups experiencing a fall in purchasing power
- to protect savers
- to prevent people losing confidence in using the currency as money
- to prevent inflation causing unemployment.

1 mark each for two reasons explained:
- low and stable inflation creates certainty/makes it easier to plan
- if inflation rate is below that of rival countries, it can increase exports/reduce imports
- if incomes rise by less than inflation, the amount that can be purchased will fall
- savers will lose if inflation rate is higher than interest rate
- may result in people resorting to barter/especially if there is hyperinflation
- inflation can result in a loss in international competitiveness/reduce spending on domestic products.

(c) Analyse how an increase in government spending may cause economic growth. [6]

An increase in government spending may result in:
- higher demand [1] which will encourage firms to expand their output [1]
- higher government spending on education (1) may raise labour productivity [1] and so increase productive potential [1]
- higher government spending on investment [1] will increase productive potential [1]
- government subsidies to firms [1] reduces costs of production [1] encourages firms to produce more [1].

Maximum of 2 marks for a list-like approach.

(d) Discuss whether a reduction in a country's unemployment rate will always benefit an economy. [8]

Up to 6 marks for why it should:
Up to 3 marks for: a reduction in unemployment is likely to increase output [1] higher output should raise living standards [1] may reduce poverty [1].

Up to 3 marks for: may improve the current account position [1] if the rise in output is due to a rise in exports [1] and exports rise by more than imports [1].

Up to 3 marks for: lower unemployment may raise tax revenue [1] e.g. from income tax [1] higher tax revenue can enable a government to spend more on education and health care [1].

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Up to 3 marks for: lower unemployment may reduce spending on unemployment benefits [1] money saved may be spent on other items [1] or tax rates reduced [1].

Up to 2 marks for: will move production point closer to the PPC [1] and reduce inefficiency [1].

Up to 6 marks for why it might not:
Up to 5 marks for: lower unemployment may cause a shortage of workers [1] this shortage may push up wage rates [1] higher wages may increase costs of production [1] higher costs can cause cost-push inflation [1] more likely to occur if the economy is operating close to full employment [1].

Up to 4 marks for: lower unemployment may increase total (aggregate) demand [1] higher demand may push up prices [1] causing demand-pull inflation [1] more likely to occur if the economy is operating close to full employment [1].

Up to 3 marks for: lower unemployment may increase a current account deficit [1] higher incomes may increase demand for imports [1] higher demand may divert products from the export to the domestic market [1].

Up to 3 marks for: a reduction in the unemployment rate does not necessarily mean fewer people are unemployed [1] unemployment may have risen if the labour force has risen [1] by more than employment [1].

Up to 4 marks for a list-like approach.

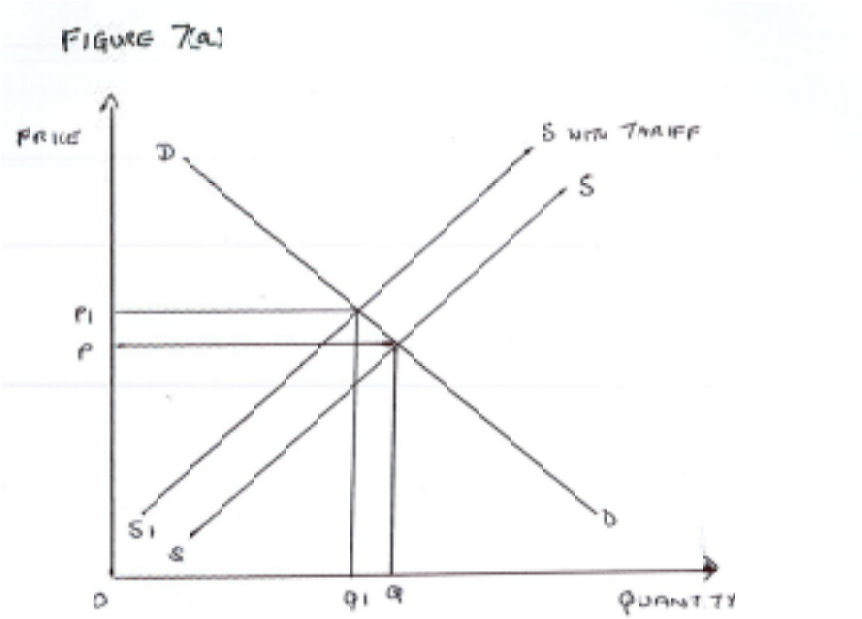
Note: accept answers which discuss the possible effects of high unemployment will always harm an economy.

7 (a) Describe how a tariff could reduce imports. [4]

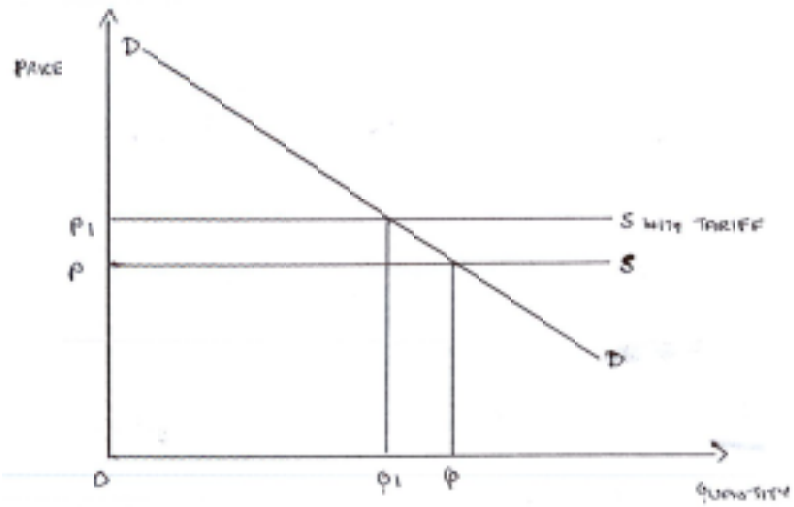
1 mark for recognising a tariff is a tax on imports.
1 mark for a tariff increases importing firms' costs of production.
1 mark for a tariff will reduce supply.
1 mark for a tariff will raise price.
1 mark for a tariff will reduce demand.
1 mark for relevant reference to PED of imports.

Note: Accept a diagrammatic approach showing supply decreasing, price rising and demand falling for 3 marks.

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OR



(b) Analyse <u>three</u> causes of a current account deficit. **[6]**

1 mark for idea of the meaning of the current account/current account deficit**.**

1 mark each for three causes identified:

- high exchange rate
- inflation
- low productivity
- high costs of production
- low quality of domestically produced products
- low incomes abroad
- high incomes at home
- protectionism abroad
- lack of protectionism at home.

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1 mark each for an analysis of three causes:

- high exchange rate would mean high export prices and low import prices
- inflation makes domestic products less price competitive
- low productivity of labour will raise wage costs/high prices of domestic products
- high costs of production e.g. raw material cost/results in high prices of domestic products
- low quality reduces demand for exports and raises demand for imports
- low incomes abroad may result in low demand for exports
- high incomes at home may lead to high demand for imports
- protectionism abroad e.g. tariffs make it difficult to export
- absence of protectionism at home may result in e.g. dumping.

(c) Discuss whether a government should always be concerned about a growing current account deficit. [10]

Up to 7 marks for why it should:
Up to 5 marks for: may indicate a poor economic performance [1] low demand for country's products [1] may be result of high inflation [1] poor quality products [1] low productivity [1].

Up to 3 marks for: will reduce total demand [1]and so may increase unemployment [1] and lower GDP [1].

Up to 3 marks for: may lead the country into debt [1] interest will have to be paid [1] this will involve an opportunity cost [1].

Up to 7 marks for why it should not:
Up to 5 marks for: may move later to a surplus [1] if imports are of raw materials [1] and capital goods [1] may be used to produce products to replace imports [1] and to be exported [1].

Up to 3 marks for: may be short term [1] especially if caused by falling incomes abroad [1] will be reduces when incomes rise [1].

Up to 2 marks for: may be a relatively small deficit [1] and/or may last for a short time [1].

Up to 2 marks for: there may be more serious macroeconomic problems [1] e.g. rising unemployment [1].

Maximum of 5 marks for a list-like response.

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