UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS

International General Certificate of Secondary Education

MARK SCHEME for the October/November 2011 question paper for the guidance of teachers

0455 ECONOMICS

0455/23 Paper 2 (Structured Questions), maximum raw mark 80

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1 (a) Possible benefits of economic development:
- increase in standard of living/quality of life
- better educational opportunities
- improved health care
- increase in incomes
- increase in employment
- increase in output/real GDP/economic growth
- higher ranking in Human Development Index. [4]

A list-like approach can gain no more than 2 marks.

(b) Any two reasons:
- to ensure that the natural resources of natural gas and oil are extracted
- this could contribute to economic growth/encourage economic development
- taxation on this could lead to an increase in government revenue
- could help to create wealth/increase living standards
- large amount of land/supply could reduce price
- not enough resources to develop without external support. [4]

(c) Potential disadvantages:
- may be more inefficient
- will be supported by public funds and so will not be so worried about making profits
- may have less concern for the environment (indicated in item)
- may not have the necessary expertise/knowledge
- possibly too much interference from politicians
- issue of opportunity cost. [4]

A list-like approach can gain no more than 2 marks.

(d) Use of resources:
- contributes to the economic development of Peru
- leads to a higher standard of living/quality of life.

Conservation of resources:
- this will be better in the long-term
- avoids using up scarce resources too quickly
- need to be mindful of environmental impact of use/exploitation; people in Peru have been unhappy about exploitation
- idea of sustainability in terms of future generations [candidates do not need to refer to the term sustainability itself].

Answers need to get across the idea that there is a trade-off between the two; an answer which is entirely one-sided can gain no more than 5 marks. An answer which fails to make any reference to Peru can gain no more than 6 marks. [8]

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2 **(a)** Basic economic problem:
- finite/limited resources
- basic situation of scarcity
- unlimited wants
- necessity for a choice to be made. [2]

(b) Possible causes:
- reduction in price of complements
- increase in price of substitutes
- change in income
- change in tastes and preferences
- effect of advertising campaign
- climate/season.

A list-like approach can gain no more than 2 marks. [4]

(c) Diagram:
- axes (P and Q) and curves (D and S) correctly labelled (1)
- shift of the demand curve to the right (1)
- rise in both equilibrium price and equilibrium quantity (1).

Explanation of what is happening in the diagram, e.g. shift in demand curve and increase in equilibrium price and output – up to 3 marks. [6]

(d) Advantages:
- idea of invisible hand to allocate resources through price signals
- no need for government intervention to achieve this
- profit motive should lead to greater efficiency
- importance of consumer sovereignty.

Disadvantages:
- there may be market failures
- some goods may be under-consumed
- some goods may be over-consumed
- problem of externalities.

A one-sided answer can gain no more than 5 marks. [8]

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3 **(a)** Functions:

- government's bank
- lender of last resort
- issuing of notes/coins
- involvement in monetary policy, e.g. determination of interest rates
- management of the national debt
- possible involvement in exchange rate determination.

A list-like approach can gain no more than 3 marks. [6]

(b) Explanation of three of:

- means of exchange
- unit of account/measure of value
- store of value
- standard for deferred payment. [6]

(c) Reasons in favour of government support:

- the financial system is too important to be allowed to 'go under'
- money is the 'oil' in the economic system
- continued liquidity is important for both institutions and private individuals
- without that, aggregate demand will fall
- this will have a negative effect on employment and economic growth
- collapse of financial institutions would have a terrible effect on confidence in country and its economy
- this could deter inward investment.

Reasons against government support:

- government might be supporting inefficient institutions
- the 'survival of the fittest' idea suggests that weak institutions should be allowed to collapse
- the money will need to come from somewhere – public funds
- this might lead to taxes going up
- idea of opportunity cost – the alternative areas of public expenditure that the money might have gone to.

A one-sided answer can gain no more than 5 marks. [8]

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4 (a) (i) Features of a co-operative:
- owned and controlled by members
- each member has an equal share in this: one member, one vote. [2]

(ii) Any two of:
- producer
- worker
- farming
- consumer/retail
- banking/financial
- insurance
- funeral. [2]

(b) A public limited company:
- part of the private sector
- companies exist to make profit
- controlled by shareholders
- has limited liability.

A public corporation:
- part of the public sector
- may make a profit, but not necessarily the main aim
- may have objective to serve public/community interest in one way
- controlled by the state/government.

A one-sided answer can gain no more than 4 marks. [6]

(c) For a definition of monopoly – up to 2 marks.

Advantages of monopoly:
- they make abnormal/supernormal profits
- these can be used to finance research and development
- their products should therefore be in the vanguard
- such a large firm can benefit from economies of scale
- the lower costs could lead to lower prices for consumers.

Disadvantages of monopoly:
- the large profits are a reflection of the higher prices that consumers have to pay
- firm is a price maker, not a price taker
- output will be lower than in perfect competition
- there will therefore be inefficiency
- no guarantee that the lower costs will lead to lower prices
- consumer not given choice.

A one-sided answer can gain no more than 6 marks. [10]

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5 (a) Progressive tax:
- these are taxes on income, e.g. Income Tax
- they take a higher proportion of a person's income (not just a higher amount) as the income rises.

Regressive tax:
- these are taxes on spending, e.g. VAT, GST
- they take a smaller proportion of a person's income as the income rises. [4]

(b) Possible reasons:
- to finance expenditure on public goods, e.g. defence, law and order
- to finance expenditure on merit goods, e.g. education, health care
- to discourage consumption of demerit goods, e.g. tobacco, alcohol
- to discourage consumption of imports
- to support different sectors of the economy
- to reduce consumption/growth/inflation.

A list-like approach can gain no more than 3 marks.

Candidates who only give one reason can still get full marks if the answer is extremely thorough. [6]

(c) Advantages:
- taxes can be used to finance expenditure on various benefits for the less well-off
- progressive taxation is particularly useful to raise the finance as it takes an increasing proportion of income from the better-off
- taxes can be used to finance subsidies to make things cheaper
- taxes can be used to finance maximum prices
- idea of 'fairness' as a policy objective.

Disadvantages:
- the cost of the various benefits can be very large
- taxes could be too high (especially income tax)
- there is an opportunity cost here as the money used to finance benefits could have been spent on other things
- some people may decide to leave the country as a result of a high level of taxation
- the distribution of income can be so fundamentally uneven that government policies/initiatives don't really achieve very much ('tip of the iceberg').

A one-sided answer can gain no more than 6 marks. [10]

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6 (a) Exchange rate:
It is the price/value (1) at which one currency is bought and sold (1) for another currency on the foreign exchange market/it is the price of one currency (1) in terms of another currency (1).

For a specific example, e.g. £1 = $1.4, one mark. [2]

(b) Possible causes:
- changes in the demand for the currency
- to pay for more exports
- changes in the supply of the currency
- to pay for more imports
- changes in the balance of trade
- changes in interest rates
- economic/political state of the country; level of confidence
- speculation
- rate of inflation in relation to other countries.

A list-like approach can gain no more than 3 marks. [6]

(c) Current account structure:
- the trade in goods (visible balance)
- the trade in services (invisible balance)
- income
- current transfers. [4]

A list-like approach can gain no more than 3 marks.

A good answer on the visible and invisible balance only can be awarded 3 marks.

(d) Yes:
- a depreciation (or devaluation) of a currency will make exports cheaper
- and if demand is price elastic this should lead to an increase in demand
- it will also make imports dearer
- and if demand is price elastic this should lead to a reduction in demand.

No:
- price elasticity of demand may not be elastic
- the change in the currency may not have much of an effect
- any impact is likely to take a while to come into effect
- the demand for goods is dependent on many factors, not just the price of a good.

A one-sided answer can gain no more than 5 marks.

Up to 3 marks where candidates explain alternative options for solving a deficit e.g. deflation, higher taxes/import duties and higher interest rates. [8]

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7 **(a)** Net migration:
This is the difference (1) between the number of people coming into a country (immigrants) (1) and the number of people leaving a country (emigrants) (1) over a particular period of time. [3]

(b) Possible economic reasons:
- to gain employment
- to obtain a higher income/lower tax rates
- to improve standard of living/quality of life
- to benefit from improved education/health care facilities
- to improve skills/widen experience
- to follow firm, e.g. multi-national. [7]

(c) Positive effects:
- obtaining employment
- increase in standard of living/quality of life
- economy may benefit from economic growth
- government will benefit from increased revenue.

Negative effects:
- migrants may not have the necessary skills/training and cannot obtain work
- may lead to unemployment
- may lead to inflation if demand exceeds supply
- may be a burden on resources, especially if migrants locate in particular areas, e.g. housing
- similar point in relation to education
- some of the income may be sent home to relatives; leakage from the economy
- may lead to a fall in wages if supply of labour is greater than the demand.

A maximum of 6 marks for a one-sided answer. [10]

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