CAMBRIDGE INTERNATIONAL EXAMINATIONS

International General Certificate of Secondary Education

MARK SCHEME for the October/November 2012 series

0455 ECONOMICS

0455/22 Paper 2 (Structured Questions), maximum raw mark 80

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1 (a) 1 mark each of four from:

- a mainly agricultural country
- nearly a third of the population live in poverty
- the infrastructure is poor
- an increasing number of shanty towns
- millions of people moving into the cities/large scale rural to urban migration.

Note: a maximum mark of 4. [4]

(b) Possible economic reasons:

- to gain employment
- to increase wages/salaries
- to improve standard of living/quality of life
- possible promotion
- take advantage of better training
- better facilities e.g. education/health care.

Full marks can be awarded to an answer which deals with only two economic reasons in some depth. [4]

(c) Up to 3 marks for the diagram:
labels (price, quantity, demand, supply) (1)
shift of the demand curve to the right (1)
equilibriums (1)

Explanation: changes in demand would bring about a rise in the equilibrium price (1) [4]

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(d) Up to 3 marks for possible advantages to the local tribespeople who are already living on the land:
Examples
- a large profit from selling the land; may use this for e.g. education/health care/house
- may have greater employment opportunities, supplying food/materials such as sand and wood, building/working in the city
- living in the city may increase living standards, better facilities provided e.g. hospitals.

Up to 3 marks for possible disadvantages to local tribespeople who are already living on the land:
Examples
- loss of farmland, may reduce income in the long run, may become unemployed
- disruption to their traditional way of life, some pollution e.g. noise when city is built.

Up to 3 marks for possible advantages to the economy of Ghana as a whole:
Examples
- higher employment, building the city, local multiplier effect (term does not have to be used), attract FDI, higher GDP
- reduced pollution, cutting external costs
- reduced overcrowding, improving living standards.

Up to 3 marks for possible disadvantages to the economy of Ghana as a whole:
Examples
- opportunity cost of the money needed to finance the project, example
- may result in empty houses/schools etc. elsewhere, inefficient use of resources
- possible inflationary effects, higher level of activity may raise prices.

Up to 4 marks for a list-like response.

Note: maximum mark of 8. [8]

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2 (a) Land: natural resources available for production, e.g. oil, coal, forests, fish, farming
Labour: human effort available for production/human capital, e.g. skilled/unskilled
Capital: man-made physical goods used in production, e.g. machines, tools, factories (Do NOT accept money)
Enterprise: the role of the entrepreneur in terms of organising the other factors of production and in taking a risk in doing so
Only TWO factors need to be described.
1 mark for each correct description (2); 1 mark for each use of examples (2)
Note in the case of enterprise: Up to 2 marks from: organising other factors of production (1); risk bearing (1) example (1). For the example just the name of a business is not acceptable.
[4]

(b) 2 marks for an explanation of what is meant by the economic problem, i.e. limited/finite resources and unlimited/infinite wants (1) giving rise to a condition of scarcity/insufficient resources (1).

2 marks for an explanation of what is meant by opportunity cost, i.e. the benefit obtained from the (next) best alternative (1) foregone (1).

2 marks for an explanation of why opportunity cost is relevant to the allocation of resources i.e. the condition of scarcity gives rise to the need to make a choice (1) opportunity cost indicates if resources are used for one purpose they cannot be used for another purpose/ consideration of opportunity cost can result in an efficient allocation of resources (1). [6]

(c) Up to 7 marks for the case for intervention:
Examples:

- income inequality, some people will have more influence than others because of their greater buying power, there may be a shortage of basic necessities, on grounds of equity everyone should have access to education, health care and housing
- some goods will be over-consumed – demerit goods (term does not have to be used), consumers may be unaware of the harmful effects to themselves/underestimate private costs, may not take into account effects on others/external costs
- some goods will be under-consumed – merit goods (term does not have to be used), consumers may be unaware of the full benefits to themselves/underestimate private benefits, may not take into account the benefits to others/external benefits
- some goods will not be provided – public goods (term does not have to be used), not possible to make consumption dependent on payment/non-excludable
- may be information failure, consumers may not be aware what different suppliers are charging, firms may not know cheapest source of raw materials
- some markets may be dominated by a monopoly, need for regulation.

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Up to 7 marks for case against intervention:
Examples:

- free market forces can promote efficiency, firms that do not produce what consumers want may go out of business, firms that produce at high costs may go out of business, firms that produce what consumers want may enjoy high profits, firms that produce at low costs may enjoy high profits
- consumers should decide on the allocation of resources/be sovereign
- price changes signal changes in demand, automatically allocate resources, quick adjustment to changes in consumer demand
- government intervention may be slow/bureaucratic, takes time for a government to recognise need for intervention, takes time to introduce policies
- government intervention may be influenced by desire to win political support/may be corruption
- difficult to determine what are merit/demerit goods, quantity of public goods to supply
- difficult to measure external costs and benefits, so difficult to determine social costs and benefits.

Up to 2 marks for a supported conclusion.

Note: a macro approach is acceptable but if the focus is on only one aspect e.g. trade protection there is a maximum of four marks available.

Note: maximum of 10 marks. [10]

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3 (a) Up to 2 marks for a description of social costs:
- social costs are private costs plus external costs. (2)
- social costs are total costs/ costs to society. (1)

Up to 2 marks for examples:
1 mark for example of a private cost identified as such e.g. the cost of paying the wages of those building the railway.
1 mark for an external cost identified as such e.g. the damage to the land of scenic beauty.
1 mark maximum for any number of examples of costs of constructing the railway which are not identified specifically as either private and external costs. [4]

(b) Up to 3 marks for identifying reasons:
- a government will have other things to spend the money on
- a government may lack finance
- private sector funding may be more readily available
- private sector funding may be more efficient.

Up to 3 marks for explaining reasons:
- there will be an opportunity cost of using government funding
- government may already be spending more than it is raising in taxation
- private sector firms may be encouraged to invest by improving economic prospects
- private sector firms may bring expertise and may monitor project carefully to ensure low costs/high quality. [6]

(c) Up to 7 marks for advantages:
Examples:
- improvement in travel time will reduce firms' costs, make firms more internationally competitive, raise exports, increase GDP
- reduced travel time may encourage fewer people to travel by cars, reducing congestion, reducing pollution
- employment will be created during the building, reducing unemployment, raising GDP
- local 'multiplier' effect in the area (term does not have to be used), work for e.g. taxi firms, encourage firms to move into areas serviced by the railway
- train companies will benefit (1) likely to attract more passengers and so higher revenue (1).

Up to 7 marks for disadvantages:
Examples:
- disruption to farming/loss of fertile agricultural land, reduction in agricultural output
- negative impact on area of scenic beauty, reduction in tourism, reduction in GDP
- bus companies may experience lower demand, causing unemployment, structural unemployment
- high cost, opportunity cost in terms of other projects
- demand for the services of the railway may be low, price of travelling may still be higher than travelling by road, quality may still be lower.

Up to 2 marks for a supported conclusion.

Up to 5 marks for a list-like response.

Note: maximum of 10 marks. [10]

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4 (a) The four functions of money:

- a medium of exchange
- a store of value
- a unit of account
- a standard for deferred payments.

4 marks for 4 functions identified and described.
3 marks for 3 functions identified and described.
2 marks for 2 functions identified and explained or 4 functions described.
1 mark for 1 function identified and explained or 3 functions described. [4]

(b) Up to 4 marks for identification of ways:

- a relatively high rate of interest
- effective advertising/publicity/information
- extension of branch opening hours
- provision of Internet operation
- details of the financial strength of the institutions
- a compensation scheme to protect savers if a bank does collapse
- provision of more saving schemes
- increase in number of branches.

Up to 3 marks for explanation e.g.:

- a high interest rate increases the reward from saving, increases the opportunity cost of spending/discourages spending, if the rate of interest is higher than inflation there is a positive real interest rate
- advertising of saving schemes will make people more aware of e.g. range of saving opportunities
- long branch opening hours will make it easier for people to deposit savings and to gain access to savings
- internet access reduces the time taken to access savings/find out details of savings
- awareness of strength of institutions/compensation schemes will increase people's confidence in saving
- more saving schemes increase the chance of people finding one that will suit them
- more branches will bring saving schemes closer to people.

Full marks can be awarded to an answer which deals with only two ways in some depth. [6]

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(c) Possible reasons:

- demand for workers may be higher in one sector, higher demand results in higher earnings
- supply of workers may be lower in one sector, lower supply results in higher earnings
- job security may be greater in one sector, this may encourage higher supply and so lower earnings
- pensions provided by one sector may be worth more, as a result people may be prepared to work for lower earnings
- trade unions may be stronger in one sector, this will give workers stronger bargaining power, which may push up earnings
- public sector may be more likely to comply with minimum wage legislation, this could raise average earnings in the sector
- there may be more overtime available in one sector, pushing up earnings
- skill/qualifications required may be higher in one sector, reducing supply, raising earnings
- risks involved in jobs in one sector may be higher, reducing supply, raising earnings
- status of working in one sector may be higher, increasing supply, reducing earnings.

A generic answer on earnings, which doesn't clearly distinguish between earnings in the two sectors, can gain no more than 7 marks.

Up to 5 marks for a list-like response.

Note: a maximum of 10 marks. [10]

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5 **(a)** Up to 2 marks for describing the main features of a co-operative:
- it is owned by the workers/customers
- it is run for the benefit of the workers/members
- the workers/customers are often shareholders in the business
- equal voting for members
- sharing resources
- reference to limited liability

Up to 2 marks for describing the main features of a public corporation:
- it is a state-owned public enterprise/nationalised industry
- it is accountable to a government
- there are no shareholders
- may act in the public interest. [4]

(b) Co-operative
Up to 2 marks:
- operates in the private sector
- does aim to make a profit
- the profit is distributed to the workers/members
- how profit may be earned i.e. raising revenue/lowering cost.

Public corporation
Up to 2 marks:
- operates in the public sector
- does not aim to make a profit
- aim is to work in the public interest. [4]

(c) Up to 2 marks for horizontal integration:
- two (or more) firms come together that are producing similar goods/services at the same stage of production. (1)
- examples could include banks, motor car manufacturers, breweries. (1)

Up to 2 marks for vertical integration:
- two (or more) firms come together that are at different stages of production. (1)
- there could be forward vertical integration where a firm takes over another firm at a later stage of production e.g. an airline taking over a travel agency or a brewery taking over a public house. (1)
- there could be backward vertical integration where a firm takes over another firm at an earlier stage of production to secure supplies, e.g. a tyre company taking over a rubber plantation or a brewery taking over hop fields. (1)

[4]

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(c) Up to 5 marks for disadvantages:
Examples:
- may be high prices, low quality, due to lack of competition
- may be lack of innovation/product development, and so slow response to changes in consumer demand
- quantity produced may be restricted, to drive up price
- if large, may experience diseconomies of scale, raise costs of production, increase prices.

Up to 5 marks for advantages:
Examples:
- if large, may experience economies of scale, lower costs of production, lower prices
- large profits may be used to finance investment, may raise quality of products
- may avoid wasteful duplication, e.g. in the case of water supply/rail infrastructure
- a state monopoly may base decisions on social costs and benefits, increasing efficiency.

Up to 2 marks for a supported conclusion.

Up to 4 marks for a list like response.

Note: a maximum mark of 8. [8]

6 (a) Definition of inflation – 1 mark

Up to 6 marks for possible harmful effects of inflation:
- some workers, whose wages are not linked to the rate of inflation, will find that the real value of their earnings falls
- it is particularly a problem for those not in trade unions or in trade unions that are not very powerful
- borrowers tend to gain whilst lenders tend to lose (unless loans are index linked)
- those on fixed incomes tend to lose out
- there is thus a redistribution of income in an economy
- if the rate of inflation is relatively high, it can make a country's exports much more expensive abroad, making them less competitive
- menu costs, i.e. the cost of changing prices regularly
- the uncertainty that can affect investment decisions
- if the rate of inflation is very high, it can lead to hyperinflation and this can result in the collapse of a currency.

Up to 3 marks on any one harmful effect well explained.

Note: Up to 3 marks for a list-like response.

Note: maximum mark of 6. [6]

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(b) Up to 4 marks for the effect on the unemployed:
- will not be able to use skills/knowledge
- this could mean that skills/knowledge become out of date
- this will make them less employable in the future
- this could have social effects
- greater loss of income.

Up to 4 marks for the effect on the economy:
- output of the economy likely to be less
- lower GDP/economic growth
- candidates may refer to particular types of unemployment, e.g. structural rather than seasonal
- loss of tax revenue will be higher
- more will have to be spent on unemployment benefit opportunity cost.

Note: a maximum of 6 marks. [6]

(c) Up to 6 marks for reasons why may conflict:
Examples:
- high employment will increase income, this will increase spending, higher spending will increase total (aggregate) spending, which may result in demand-pull inflation.
- high employment may result in a shortage of workers, wages may be pushed up, as firms compete for workers/trade unions have greater power, causing cost-push inflation/ wage-price spiral.
- high employment may increase demand for imports, which may result in imported inflation.
- to reduce inflation/keep inflation low a government may seek to reduce total (aggregate) demand, so may e.g. raise taxes/interest rates, the lower demand will reduce output, causing cyclical unemployment.

Up to 6 marks for reasons why may not conflict:
- supply-side policies may enable an economy to have both low inflation and high employment, e.g. education will make labour more skillful/mobile, this may reduce unemployment, more skillful workers may reduce costs, and so lower cost-push inflation.
- low inflation may increase demand for exports, higher demand may increase output, this may raise employment, lower cyclical unemployment.

Up to 2 marks for a supported conclusion.

Note: maximum mark of 8. [8]

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7 (a) Definition of regional specialisation – 1 mark

Up to 4 marks for possible advantages:
- able to focus on what the region is best at producing
- output in the region should be higher
- there should be higher living standards
- economies of scale could lead to lower costs
- efficiency is likely to increase
- may gain a good reputation.

Note: maximum mark of 4. [4]

(b) There are four elements:
- trade in goods/visible balance of exports and imports
- trade in services/invisible balance of services
- income
- current transfers.

An answer which only focuses on the first two elements, i.e. the balance on trade in goods and services, can gain 3 marks. [4]

(c) Up to 2 marks for general reference to market forces:
- fall in demand for the currency
- rise in supply of the currency.

Up to 4 marks for explanation of specific reasons:
- fall in demand for exports/increase in current account deficit due to e.g. fall in quality/ inflation
- rise in demand for imports/rise in current account deficit due to e.g. higher incomes at home
- less FDI/more investment abroad due to e.g. better economic prospects abroad
- changes in hot money flows due to a fall in the rate of interest
- speculation – reduction in demand/rise in supply due to expectation currency will fall in value.

Note: maximum mark of 4. [4]

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(d) Up to 5 marks for the advantages and disadvantages of a floating exchange rate:
Examples:

- the exchange rate automatically adjusts, moving current account position to equilibrium/ eliminating deficits or surpluses
- no need for the central bank to keep reserves, foreign currencies/gold can be used for other purposes
- governments can pursue other objectives more easily e.g. changing interest rates to influence inflation
- may be instability of value which could discourage trade and investment
- may be speculation, causing movements in value which lead to current account deficits or surpluses.

Up to 5 marks for advantages and disadvantages of a fixed exchange rate:
Examples:

- may be a greater degree of certainty and stability, may promote trade and investment
- may be less speculation
- need to keep reserves, to intervene to protect the exchange rate, involves an opportunity cost
- exchange rate may not be set at an appropriate level, if too high will discourage exports, if too low, may increase import prices – causing inflation
- policies taken to maintain the exchange rate may conflict with other objectives e.g. raising the interest rate may increase unemployment/reduce economic growth.

Up to 2 marks for a supported conclusion.

Up to 4 marks for a list-like approach.

Note: a maximum mark of 8. [8]

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