CAMBRIDGE INTERNATIONAL EXAMINATIONS

Cambridge International General Certificate of Secondary Education

MARK SCHEME for the October/November 2014 series

0455 ECONOMICS

0455/21 Paper 2 (Structured Questions), maximum raw mark 90

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1 (a) Define 'Gross Domestic Product'. [2]

1 mark: total output

1 mark: either in/of a country/economy (1) or over a given time period (1)

Maximum of 2 marks

(b) Using information from the extract, calculate the Gross Domestic Product per head in Mauritius in 2011. [2]

Answer is US$8,700 (2)

US$11.31bn divided by 1.3 million people (1)

Correct figure, but with no reference to US$ (1)

Correct method, but inaccurate figure, (1)

Maximum of 2 marks

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(c) Discuss the extent to which economic growth is advantageous for a country. [6]

Up to 4 marks for why it may be advantageous:

Up to 4 marks: rising incomes (1) leading to increase in standard of living (1) and higher government tax revenue (1). Higher government spending on e.g. health, education, infrastructure (1).

Up to 3 marks: lower unemployment / more jobs created (1), lower government spending on unemployment benefit (1), reduction of poverty (1).

Up to 2 marks: more exports (1) improving the balance of payments position (1)

Up to 2 marks: more goods and services produced in the economy (1) giving consumers greater choice (1)

Up to 4 marks for why it may be disadvantageous:

Up to 3 marks: may cause inflation (1), higher incomes lead to greater demand (1) but output may be unable to match this increased demand (1)

Up to 3 marks: may be an increase in external costs (1), e.g. more pollution and congestion (1), this may mean economic growth is unsustainable (1).

Up to 2 marks: faster pace of work/change (1) leading to personal costs, e.g. increase in stress and suicide (1).

Up to 2 marks: if economic growth is achieved by depleting resources (1) this could threaten future economic growth (1).

Up to 2 marks: if economic growth is dependent on MNCs (1) this may lead to a number of disadvantages e.g. they may pull out in future, they may create pollution, repatriate profits, exploit workers (1).

Maximum of 3 marks for a list or list-like response.

(d) Using information from the extract, describe two functions that the stock exchange performs in the Mauritian economy. [4]

Up to 2 marks: provides for the buying and selling of company stocks (or shares / equities) (1). This is a way for companies to raise finance (1) and help people to buy stakes in companies (1)

Up to 2 marks: provides for the buying and selling of government bonds (1). This is a way for governments to raise finance (1).

Up to 2 marks: lists companies on the stock exchange (1) providing information for investors (1).

Up to 2 marks: allows trade in several currencies (1), this facilitates international trade in stocks (1)

1 mark: helps liberalise the financial services sector

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(e) Explain why governments impose taxes. [4]

Candidates could refer to:

Up to 2 marks: to raise revenue / collect money for the government (1), to provide finance for government expenditure on e.g. education (1)

Up to 2 marks: to pay for government debts (1) so reduce the deficit (1)

Up to 2 marks: to redistribute income / wealth (1) and reduce the gap between and rich and poor (progressive taxation) (1)

Up to 2 marks: part of fiscal policy (1) e.g. may raise tax to reduce inflation (1).

Up to 2 marks: raise the price of certain products (1) to discourage their consumption (1) (may refer to demerit goods but explicit reference to this term is not required).

Up to 2 marks: may increase price of imports (1) to improve the balance of payments position (1).

Maximum of 2 marks for a list or list-like response

(f) Using Table 1, calculate the percentage of the labour force in Mauritius employed in the services (tertiary) sector. [2]

Answer is 7% + 22% + 6% + 26% = 61% (2)

Correct method, but inaccurate figure (1)

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(g) Using information from the extract, explain why there has been substantial investment by foreign firms in Mauritius in recent years. [4]

Candidates could refer to:

Up to 2 marks: well-educated, skilled and multi-lingual workforce (1) which could contribute to higher productivity (1) and lower costs of production (1).

Up to 3 marks: new production techniques/advances in technology (1) which could give rise to economies of scale (1) and development/innovation of new products (1)

Up to 3 marks: political stability (1), less change (1), less likelihood of wars/riots (1) giving greater certainty for investors (1)

Up to 2 marks: membership of a common market (COMESA – Common Market for Eastern and Southern Africa) (1), very large market (1)

Up to 3 marks: relatively low rates of taxation (1), which reduces firms' costs and increases spending (1) and makes it more attractive than other countries (1)

Up to 2 marks: flat tax rate e.g. 15% corporate, value added and income taxes (1) are simple to operate and budget for (1).

Maximum of 2 marks for a list-like response or more than two undeveloped points.

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(h) Discuss whether an economy would benefit from becoming less specialised and having a greater range of different industries. [6]

Up to 4 marks for possible benefits:

Up to 4 marks: broader spread of industries (1), leading to less reliance on one or a few particular industries (1). This lowers risk (1), as demand for one type of product may fall (1), or there may be problems with supply, especially in primary sector (1).

Up to 3 marks: more industries may be linked to economic development (1) and movement in all countries from primary, through secondary, to tertiary sector (1), should lead to higher standards of living in the country (1).

Up to 4 marks for possible disadvantages:

Up to 4 marks: it may be difficult to identify which industries to develop (1) and the country may not be as efficient as other countries in producing other products/services (1). Costs are always changing, e.g. economies of scale may be overestimated and problems of diseconomies of scale may be underestimated (1) or set up costs may be high for new industries (1). If a mistake is made in the industries developed, resources will have been wasted setting up new and unprofitable industries (1).

Up to 4 marks: country may not have the appropriate resources (1). Labour may lack the skills/knowledge for the new areas (1) and there may be a lack of capital to support the new industries (1) or this could lead to over-reliance on foreign investors (1).

Up to 2 marks: Other countries may react to the development of new industries by imposing trade restrictions (1). If they do this, it will make this country's products uncompetitive (1).

Maximum of 4 marks for an indirect approach examining the benefits (2) and disadvantages (2) of specialisation.

Maximum of 3 marks for a list or list-like response.

2 All countries face the economic problem and so choices have to be made.

(a) Explain what is meant by the 'economic problem'. [2]

There are finite/limited/scarce resources (1) but unlimited/infinite wants (1) and so it is necessary for a choice to be made (1)

Maximum of 2 marks

(b) Describe the <u>two</u> main features of the factor of production, 'enterprise'. [4]

2 marks for identifying the two features:
- bringing together/combining the other factors of production (1)
- bearing risks (1)

2 marks for describing the two features:
- making a decision about how to combine/which factors to employ/whether to be labour-intensive or capital-intensive (1)
- risking own money/recognising risk/risk could include natural disasters, new competitors/change in technology/reward for the risk is profit (1)

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(c) Using a production possibility curve diagram, explain how the curve can be used to show the consequences of a change in the allocation of resources between the production of two goods. [6]

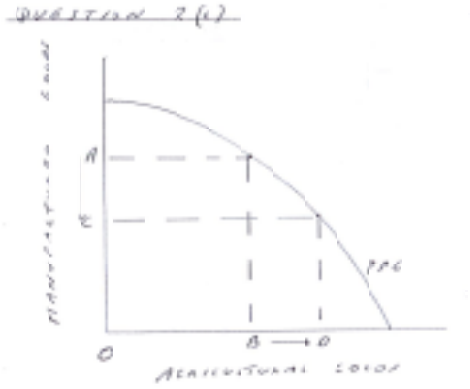


Diagram – 3 marks
- correct labelling of two axes (1)
- correct shape of curve (1)
- movement from one position on the curve to another (1)

Explanation – 3 marks
- correct explanation that as more resources are allocated to the production of one good (1), less resources can be allocated to the production of the other good (1), as there will be an opportunity cost (1)

Only reward candidates who draw shifts if it is explained that if there are more resources, it is possible to devote more resources to the production of one good without reducing the production of the other.

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(d) Discuss whether a decision by a government, with limited financial resources, to increase expenditure on education by 25% over a three year period, is likely to be an appropriate decision. [8]

Up to 6 marks for why it may be an appropriate decision:

Up to 4 marks: increase in expenditure is likely to improve the quality of education (1), this would enhance the skills/knowledge/quality of the workforce (1), leading to greater productivity (1) and a higher rate of economic growth (1).

Up to 4 marks: higher education spending should improve health (1) e.g. greater awareness of need for cleanliness/sanitation/diseases/nutrition (1), fewer days missed from work (1) and less spending on health care in the long term (1).

Up to 4 marks: more employment opportunities (1) for school leavers/graduates who are better educated (1), also for teachers and school support staff (1). Labour becomes more geographically and occupationally mobile (1), which reduces frictional and structural unemployment (1).

Up to 3 marks: educated school leavers are more likely to be innovative (1) and start new businesses (1), this will create employment (1)

Up to 3 marks: incomes will increase (1), demand/spending in the economy will increase (1), tax revenues will rise (1) (multiplier effect but this term not expected).

Up to 2 marks: education provides awareness of family planning (1), this could reduce population pressures on the economy (1)

Up to 6 marks for why it may not be an appropriate decision:

Up to 3 marks: there would be an opportunity cost involved (1), given that we are told that the government has limited resources (1). This could lead to other areas of the economy receiving less money e.g. housing, defence, transport (1).

Up to 2 marks: those benefiting from the higher education spending may emigrate (brain drain) (1), which may reduce the country's production/output/productivity (1) and increase the dependency ratio (1).

Up to 4 marks: in the short run, if mean years of schooling increase (1) the current labour supply will fall (1). The labour force may become more skilled but there may be a lack of appropriate jobs (1) and this would lead to a waste of resources (1).

Up to 2 marks: skills acquired might quickly become outdated e.g. in ICT (1) meaning more spending after 3 years will be required (1)

Up to 2 marks: it depends upon the distribution of the extra spending (1). It may only be a small minority which benefits (1) or spending may be on unproductive areas (1)

Up to 2 marks: three years could be too short (1). Education investment needs to be long-term (1)

Maximum of 4 marks for a list or list-like response.

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3 A government decides to encourage the use of public transport by the provision of a subsidy.

(a) Using a demand and supply diagram, analyse the effect of a subsidy on the equilibrium price and equilibrium quantity in such a market. [6]

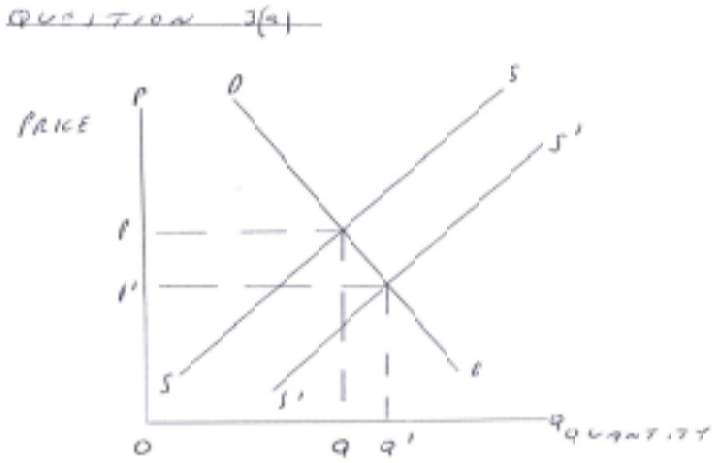


Diagram – 4 marks
- correct labelling of P, Q, D and S (1)
- shift of the supply curve to the right (1)
- decrease in equilibrium price as shown by lines or points e.g. E and E1 (1)
- increase in equilibrium quantity shown by lines or points e.g. E and E1 (1)

Explanation – 2 marks
- explanation of why supply has increased/shift of supply curve to the right (1)
- explanation of lower price and larger quantity (1)

(b) Explain what factors influence the price elasticity of demand for public transport. [6]

Up to 2 marks for a definition: Responsiveness of demand (1) to a change in price (1). Percentage change in quantity demanded ÷ percentage change in price (1)

Up to 2 marks: The price of service (1), as the price rises, demand becomes more elastic (1) (or the reverse)

Up to 2 marks: the availability of substitutes (1), e.g. if car travel is similar in price to public transport, PED is likely to be more elastic (1).

Up to 2 marks: the quality/reliability/safety/convenience of service (1) compared to alternatives e.g. car travel (1).

Up to 2 marks: the proportion of income public transport expenditure represents (1), the smaller the proportion, the less price elastic the demand (1).

Up to 2 marks: whether public transport is a necessity or luxury (1) e.g. travel to work is a necessity so demand would be less price elastic (1)

Maximum of 3 marks for a list or list-like approach.

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(c) Discuss whether transport in a country should be provided by the public sector or by the private sector. [8]

Up to 6 marks for why it should be provided by the public sector:

Up to 2 marks: public sector funds may be more available than private sector funds (1) to provide a quality service (1).

Up to 2 marks: a public sector firm can be prevented from going bankrupt (1) so there is continuity of service (1).

Up to 3 marks: a public sector firm will be more interested in providing a good service than making a profit (1) as the government is more likely to base its decisions on social costs and benefits (1) rather than just private costs and benefits (1)

Up to 2 marks: public sector will be more inclined to keep prices low (1), benefiting the poor (1).

Up to 4 marks: the government will take an overview (1) and so there is a possibility there will be a better allocation of resources between transport forms (1) e.g. promoting an integrated transport system (1) which could be more sustainable (1).

Up to 6 marks for why it should be provided by the private sector:

Up to 2 marks: a private sector firm has to make a profit to survive / profit motive (1) and so the efficiency and quality of the service is likely to be good (1).

Up to 2 marks: the potential threat of bankruptcy (1) will force it to provide a good service to stay in business (1).

Up to 4 marks: private sector firms may be in competition with each other (1), leading to greater response to consumer demand (1), pressure to keep costs low (1), and prices competitive (1)

Up to 5 marks for recognising that transport might be best provided by a combination of the two sectors.

Recognising some methods of transport may be best in the private sector e.g. car travel (1) but the infrastructure could be best provided by the public sector e.g. roads, rails (1). Using a combination of both may draw on the strengths of each (1) e.g. private sector responds quickly to competitive pressure (1) but the public sector can take a longer view (1). The public sector could subsidise (1) the private provision.

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4 Different workers can be paid vastly different amounts of money. Sometimes this can be due to the level of skill that different workers have, and sometimes it can be influenced by whether a worker is in a trade union or not.

(a) Describe <u>three</u> factors that can influence an individual's choice of occupation. [6]

1 mark for each of up to <u>three</u> factors identified e.g.:
- wage/salary/overtime payments
- working hours
- bonus/commission/profit-sharing
- job security
- skills/training/qualifications needed
- proximity to home/travelling distance
- availability of overtime work
- promotion/career enhancement prospects
- job satisfaction
- social/welfare/sport facilities
- fringe benefits
- pension scheme
- holiday entitlement

1 mark for each related description e.g.:
- skills/training/qualifications needed: means that some workers cannot apply / and others will take a long time to train/study first
- travelling distance: if close to home, saves time/reduces costs
- job security: reduces risk of unemployment/provides continuity/certainty of income for the future

(b) Explain <u>two</u> reasons why an unskilled worker is usually paid less than a skilled worker. [4]

Up to 2 marks for reasons identified:
- a lower level of demand for an unskilled worker (1)
- a relatively high supply of unskilled workers (1)

Up to 2 marks for explanations:
- lower demand because of lower efficiency/productivity/value added of the unskilled worker (1)
- higher supply because little time needed to train/study to gain the requirements needed for the job (1)

The first 2 marks can be given instead for an appropriate demand and supply diagram.

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(c) Describe what is meant by a trade union. [4]

Candidates could refer to:
- an association of workers (1)
- it engages in collective wage/salary bargaining with employers (1)
- protects and promotes other interests of its members e.g. in relation to working conditions, health and safety (1)
- will often negotiate with governments on behalf of workers (1)
- may promote training for its members (1)
- may provide help for unemployed members (1)
- may provide other benefit schemes for its members (1)

(d) Discuss whether membership of a trade union will always be beneficial for a worker. [6]

Up to 4 marks for benefits of membership of a trade union for a worker:

Up to 4 marks: better basic pay/overtime (1), a union will bargain collectively for pay/overtime (1), a union will have more power than one individual worker (1), a union can use threat of industrial action to support wage demands (1).

Up to 4 marks: better working conditions (1), e.g. better working hours/better health and safety/sick pay/pensions (1), resulting from negotiation from trade unions (1), a union will have more power than one individual worker (1), a union can use threat of industrial action to support improved working conditions (1).

Up to 4 marks for disadvantages of membership of a trade union for a worker:

Up to 2 marks: worker will have to pay a fee to be a member (1), which reduces their take-home pay/spending power (1).

Up to 3 marks: union might bring workers out on strike (1), leading to them losing potential earnings (1), and the firm may take retaliatory action, e.g. loss of benefits/restricted promotion/redundancy (1).

Up to 3 marks: prolonged strike action could force a firm to go out of business (1), leading to unemployment of workers (1), and so lower living standards of former workers (1).

Up to 2 marks: union might be closely linked with a particular political party (1), which some workers may not choose to vote for (1).

Maximum of three marks for a list or list-like response.

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5 In Pakistan, some businesses, especially sole proprietorships and partnerships, are perfectly competitive and other businesses are monopolies.

(a) Distinguish between a sole proprietor and a partnership. [4]

One mark for each characteristic and one mark for the comparison:

Sole proprietor is ownership by one person (1), whereas partnerships involve a number of owners (1).

Sole proprietor receives all the profits (1), whereas partnership divides profits between partners (1).

Sole proprietor has complete control (1), whereas in partnership control is shared between partners (1).

Difficult for sole proprietor to raise finance (1), but in a partnership it is easier to raise finance from partners (1).

Maximum of two marks if no comparisons are made.

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(b) Explain how some large firms can experience economies of scale, while others face diseconomies of scale. [6]

One mark for a definition of economies of scale and/or diseconomies of scale:

- as a firm grows in size, lead to reductions/increases in average total cost in the long run (1)

Up to 4 marks for why large firms may experience economies of scale:

Up to 3 marks: for explaining how up to <u>two</u> individual economies of scale may arise, e.g.
technical (1) large firms can employ large-scale capital equipment (1),
financial (1) large firms could raise finance more easily/more cheaply (1),
marketing (1) a large firm is able to have a wider marketing campaign (1),
buying (1) large firms can buy in bulk to reduce costs (1),
managerial (1) a large firm can employ specialised staff (1),
risk-spreading (1) diversification into different markets (1)

Up to 3 marks: for explaining how up to <u>two</u> external economies of scale may arise, e.g. ancillary services/industries (1), industries may develop to support the large firms (1), specialised labour (1), firms can recruit staff from other firms in the industry (1), infrastructure (1), firms can benefit from transport/communication links provided to support the industry (1)

Up to 2 marks: for explaining that large firms can spread fixed costs (1) over a greater amount of output (1)

Up to 4 marks for why large firms may experience diseconomies of scale:

Up to 3 marks: for explaining how up to <u>two</u> individual diseconomies of scale may arise, e.g. ineffective management (1), firm becomes too large to control and coordinate activities (1), poor industrial relations (1), greater likelihood of industrial action e.g. strikes (1)

Up to 3 marks: for explaining how up to <u>two</u> external diseconomies of scale may arise, e.g. pressure on infrastructure (1), causing congestion (1),
pollution (1), if heavy industry is concentrated in one area (1), increase in cost of production (1) because of increased competition from other firms in the industry (1)

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(c) Discuss whether a monopoly is always in the public interest. [10]

Up to 7 marks for why a monopoly may be in the public interest:

Up to 5 marks: avoids wasteful duplication of resources (1), resulting in lower costs (1), lower prices (1), significant in the case of a natural monopoly (1), e.g. water supply (1).

Up to 4 marks: a monopoly may be more likely to earn high profits (1), and may invest these (1), in research and development/advances in technology (1), resulting in new/improved products (1).

Up to 3 marks: there can be advantages of economies of scale (1), lower costs (1) could lead to lower prices (1).

Up to 2 marks: a monopoly may seek to innovate (1), in order to keep out potential rivals (1).

Up to 2 marks: monopolies are more likely to be listed on the stock exchange (1), shareholders will receive dividends from the profits (1).

Up to 7 marks for why a monopoly may not be in the public interest:

Up to 4 marks: quantity is likely to be less than in perfect competition (1), because a monopoly is likely to restrict output (1), and push up the price (1), in order to get high profit (1).

Up to 3 marks: there could be diseconomies of scale (1), higher costs (1), could lead to higher prices (1).

Up to 3 marks: because of a lack of competition (1), costs may be higher/may be more inefficient (1), and so prices may be higher (1).

Up to 2 marks: a monopoly may be less likely to innovate/invest (1), due to lack of competition (1).

Up to 2 marks: quality may suffer (1) because of a lack of competitors (1)

Maximum of five marks for a list or list-like response.

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6 Many countries experience different degrees of poverty and migration, but in all countries it can be difficult to measure living standards. (2)

(a) Distinguish between relative poverty and absolute poverty.

Relative poverty is where people have fewer goods and services/income than others in an economy (1). Absolute poverty is where people are unable to meet basic needs/living on e.g. less than US $1.25 a day (1).

(b) Explain four reasons why some developing countries experience immigration. [8]

1 mark for each of up to four reasons identified e.g.:
- wages/salaries
- employment prospects
- job security
- cost of living
- political/human rights/civil liberties
- prospect of trade union membership
- housing/accommodation provision
- working conditions
- war in other countries
- famine in other countries

1 mark for each of up to four explanations in the context of a developing country, e.g.:
- wages, although low, may be higher than neighbouring countries
- employment prospects may be higher, particularly in emerging developing economies
- job security may be higher due to legislation/regulation/faster economic growth
- cost of living may be lower, even with the same wages

Maximum 4 marks if any country is covered and the answer is not related to developing countries.

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(c) Discuss whether GDP per head is the best way to compare living standards in different countries. [10]

Up to 5 marks: Advantages of using GDP per head to measure living standards:

- takes into account the value of all that has been produced in a country (1) over a period of time (GDP) (1)
- and the size of the country's population (1)
- the information is fairly readily available (1)
- it gives an indication of the value of the goods and services available to people (1)
- income/output/expenditure is a key determinate of their living standards (1)
- the information is available on every country (1).

Up to 5 marks: Disadvantages of using GDP per head:

- accounting techniques can vary (1)
- not all income may be declared (1), if there is a significant informal/hidden economy (1)
- needs to take inflation into account (idea of real, but candidates do not need to refer to that term) (1)
- need to take into account differences in climate (1)
- composition of output may vary, e.g. defence vs. education (1)
- distribution of income may vary a great deal (1), some people in the country may have good living standards, whilst others have poor living standards (1).

Up to 5 marks: Discussion of possible alternatives, e.g. Human Development Index (HDI) and Human Poverty Index (HPI)/Multidimensional Poverty Index (MPI)

- recognising that there are other ways to compare living standards (1)
- identification of HDI (1)
- composition of HDI (1)
- HDI covers more variables than GDP (1)
- living standards are influenced by not only income but also quality of life (1), although it's wider than GDP it doesn't cover everything (1)
- examples <u>not</u> covered by HDI including water quality/pollution, number of doctors per head, internet access, school class size (1)
- for a few countries the HDI figure is unavailable (1).

Maximum of five marks for a list or list-like response.

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7 Trade protection and changes in exchange rates are two ways a country can try to reduce a current account deficit of the balance of payments.

(a) Explain what is meant by 'a current account deficit of the balance of payments'. [4]

Candidates could refer to:
- imports greater than exports (1)
- the composition of the current account in terms of trade in goods/visibles, trade in services/invisibles (1), income and/or current transfers (1) is negative
- the idea that when all these four sub-sections are added together, this will produce the current account balance (1)
- if the value of the debit items taken together is greater than the value of the credit items (1), there is a deficit (1)

(b) Analyse why the depreciation of its currency's exchange rate may lead to a reduction in a country's current account deficit. [6]

Up to 4 marks for:
- a fall in a country's exchange rate leading to cheaper prices abroad (1), leading to an increase in demand for exports (1), export revenue will increase as long as the price elasticity of demand is elastic (1), which is likely to reduce the deficit (1)

Up to 4 marks for:
- a fall in a country's exchange rate will make imports more expensive (1), leading to a fall in demand for imports (1), import expenditure will decrease as long as price elasticity of demand is elastic (1)
- this could reduce the deficit (1)

Up to 2 marks for recognising other factors influence the current account, e.g. changes in trade restrictions, changes in incomes abroad, changes in PED, changes in PES (1+1).

(c) Describe <u>two</u> methods of trade protection that a country could use. [4]

One mark for each of <u>two</u> methods identified:
- tariffs
- quotas
- subsidies
- administrative restrictions
- exchange controls
- boycott/ban/embargo

One mark for each of <u>two</u> descriptions, e.g.:
- a tariff is a tax on imports/exports
- a quota is a limit on the quantity of imports/exports

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(d) Discuss whether trade protection should always be preferred to free trade. [6]

Up to 4 marks for why trade protection may be preferred:

Up to 4 marks: protect infant/sunrise industries (1), because they can't take advantage of economies of scale/high set-up costs (1), long-run may become competitive (1) and (therefore) will no longer need protection (1)

Up to 3 marks: protect declining/sunset industries (1), to prevent a sudden rapid increase in unemployment (1), and so to allow time for retraining/reskilling (1)

Up to 4 marks: prevent dumping (1), that is selling products below cost (1), this will give advantages to consumers in the short-run (1), but in the long-run if domestic firms are driven out of business, prices rise (1)

Up to 3 marks: to raise revenue for the government (1), in a number of countries tariffs are an important source of income (1), higher government revenue could be spent to benefit the economy, e.g. spending on education and healthcare (1)

Up to 2 marks: to discourage imports (1) reducing the current account deficit (1)

Up to 4 marks for why free trade may be preferred:

Up to 4 marks: provide opportunities for specialisation (1), in products the country is good at producing (1), this would improve the allocation of resources (1) and lead to higher output (1) and so higher employment (1), and so higher living standards (1)

Up to 3 marks: encourages firms to be more competitive (1), resulting in lower costs (1), leading to lower prices for consumers (1)

Up to 2 marks: encourages more trade between countries (1), leading to a wider choice of products for consumers (1).

Maximum of three marks for a list or list-like response.

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