CAMBRIDGE INTERNATIONAL EXAMINATIONS

GCE Ordinary Level

MARK SCHEME for the May/June 2013 series

2281 ECONOMICS

2281/22 Paper 2 (Structured Questions), maximum raw mark 80

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1 **(a)** limited liability
a joint stock company
name is followed by plc
a minimum number of shareholders
no maximum number of shareholders
shares can be bought and sold on a stock exchange
operates in the private sector
often run by a board of directors
legal requirement to publish financial information
a separate legal identity

Note: maximum of 4 marks. [4]

(b) size of demand/may be a local or niche market
potential benefits of economies of scale
potential problems of diseconomies of scale
extent of capital required
some firms may only have recently been established
need for personal services/attention
differences in firms' objectives/owner choice
differences in brand loyalty

1 mark for each reason explained and 1 mark each for further development

Note: maximum of 4 marks. [4]

(c) impose a maximum price
provide a subsidy
encourage new firms to enter the market
establish a publicly run firm
reduce taxes affecting firms
competition policies

Maximum of 2 marks for just identification.

Note: 4 marks may be awarded for one method well explained.

Note: maximum of 4 marks. [4]

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(d)

Disadvantages of monopolies:	Advantages of monopolies:
• they can be inefficient (either productively or allocatively efficient, but these two terms are not on the syllabus) • price will tend to be higher than in perfect competition • output will tend to be lower than in perfect competition • products may be of poor quality as a result of lack of competition • abnormal profits in the long run	• large profits can be reinvested to improve the quality of products, such as expenditure on research and development • there may be opportunities for economies of scale • this could lead to a lowering of cost and, possibly, price • avoids wasteful duplication of capital equipment

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

Note: maximum mark of 8 marks. [8]

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2 (a) land – natural resources/gifts of nature available for production, e.g. farmland
labour – all physical and mental effort of workers, e.g. teacher
capital – all man-made goods used in production, e.g. machinery
enterprise – the risk bearing and decision making function, e.g. entrepreneur or example of a function

Note: maximum of 6 marks. [6]

(b) Definition of opportunity cost: the (next) best (1) alternative foregone (1) as a result of making a decision

Diagram of production possibility curve – axes correctly labelled (1) and curve correct shape (bowed out or straight downward sloping) (1)

Explanation – idea of moving along one axis (1) has the effect of a reverse movement along the other axis (1)

Note: maximum of 6 marks. [6]

(c)

Yes	**No**
• more houses would reduce the number of homeless • the increase in supply might reduce the price of houses • making them more affordable • may improve the quality of houses • employment/multiplier effects	• the decision to build more houses will involve an opportunity cost in terms of: • the alternative use of the land • the alternative use of the money required to build the houses • the alternative use of the labour and capital involved in building the houses • may already be a surplus of houses. • some resources may not be suitable for building houses • may generate environmental costs.

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

Note: maximum of 8 marks. [8]

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3 (a) price
price of older television models/substitutes
price of complements e.g. electricity, consuls, speakers
quality
consumer tastes and preferences
income
advertising
indirect taxation, e.g. VAT
interest rates

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

4 marks may be awarded for one influence described well.

Note: maximum of 4 marks. [4]

(b) Up to 4 marks for demand and supply diagram:
- axes correctly labelled (price and quantity) (1)
- demand and supply curves correctly labelled (1)
- shift of demand curve to the right (1)
- original and new equilibrium positions identified (1)

Up to 2 marks for analysis:
- increase in income is likely to increase demand (1)
- an increase in demand will lead to a rise in price (1)
- an increase in demand will cause a rise in quantity (1)

Note: maximum of 6 marks. [6]

(c) Up to 2 marks for definition:
PED is the percentage change in the quantity demanded of a product (1) divided by the percentage change in its price (1)
Or
PED is the responsiveness of demand (1) to a change in price (1).

Up to 2 marks for expansion:
Its value can range from perfectly inelastic (1) to perfectly elastic (1) inelastic demand has a value of less than 1 (1) elastic demand has a value of more than 1 (1) and it is usually a minus figure (1) varies along the demand curve (1).

Note: maximum of 4 marks. [4]

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(d) Useful:
- it will give guidance to the firm if it is thinking about changing the price (1)
- if PED is elastic, a price reduction will increase revenue (1) additional mark for development of this point e.g. as demand will rise by more than price (1)
- if PED is inelastic, a price rise will increase revenue (1) additional mark for development of this point e.g. as demand will fall by less than price (1)

Limitations:
- may be difficult for the manufacturer to calculate accurately (1)
- may be constantly changing (1)

There are likely to be a number of competitors in the industry/the produce might be considered to be a luxury (1) and, therefore, the PED is likely to be elastic (1) unless the manufacturer can build up a strong sense of brand loyalty (1) in which case the PED will be less elastic (1).

Answers which fail to refer to the television manufacturing industry can gain no more than 4 marks.

A maximum of 5 marks for a one-sided approach.

Note: maximum of 6 marks. [6]

4 **(a)** A medium of exchange:
- money is generally accepted (1) as a means of payment for most goods and services/avoids the need for a double coincidence of wants or barter (1).

A store of value:
- people can save money because it keeps its value (1); savings enable use of money in the future (1) (idea that money will not deteriorate with time and so will be acceptable in the future, though inflation will erode its real value).

Note: maximum of 4 marks. [4]

(b) Candidates could mention:
- acts as a banker to the government
- operates as a banker to the commercial banks
- acts as a lender of last resort
- manages the national debt
- holds a country's reserves of gold and foreign currency
- responsible for issuing bank notes and coins
- implements a government's monetary policy
- controls the banking system
- interest rate manipulation

Note: maximum of 6 marks. [6]

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(c) Definition of a stock exchange – an organisation for the sale and purchase of shares (1) and other securities (1)

- provides a market for the purchase and sale of shares (1) which helps companies to raise finance (1) from a wider shareholder/investor base (1)
- this can be a very important way of providing the necessary finance for a firm to expand (1) spend on capital goods (1)
- may enable a firm to expand by buying out or merging with another firm (1)
- but not all firms will be a plc (1) for example, a private limited company will not be able to sell shares on a stock exchange (1)
- there may be other forms of gaining the necessary finance for a firm to expand (1) such as through government help and support (1) or retained profits (1) or borrowing from banks (1).

A one-sided answer, which only considers the role of a stock exchange in enabling firms to expand, can gain no more than 7 marks.

Note: maximum of 10 marks. [10]

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5 (a) rate of growth measured through change in output/real output (1)
change in GDP/real GDP/GDP per head (1)
over a period of time (usually one year) (1)
shift outwards of the production possibility curve (1)
increase in productive potential (1)

Note: maximum of 4 marks. [4]

(b) government spending could be increased, e.g. on infrastructure projects and education
direct taxation could be lowered, e.g. corporation tax on firms and income tax on workers
indirect taxation could be lowered, e.g. VAT, to stimulate demand
tariffs could be placed on imported goods to protect domestic producers

Answers which deal only with the expenditure side or the revenue side can gain no more than 4 marks

Note: maximum of 6 marks. [6]

(c) Examples of supply-side policies:
- improvements in education and training
- reforming trade unions to reduce their power and to make labour more productive
- privatisation of industries to increase efficiency
- subsidies could help to reduce supply costs and so encourage production
- cuts in direct taxes to act as an incentive to enterprise and effort
- cuts in welfare payments to increase the incentive to work

Monetary policies:
- price of money, i.e. rate of interest; this could be lowered to stimulate demand
- quantity of money, i.e. money stock; this could be increased to stimulate demand
- exchange rate, reducing value to increase competitiveness

Up to 7 marks for discussing the effectiveness of either supply-side or monetary policies.

To gain 9 or 10 marks, a conclusion has to be reached as to whether supply-side or monetary policies are likely to be more effective.

Note: maximum of 10 marks. [10]

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6 **(a)** the value is determined, like any market price, by the forces of demand for the currency and supply of the currency (candidates may refer to the appreciation or depreciation of the value of the currency)
the demand for and supply of the currency will reflect the demand for and supply of products in international trade
the demand for and supply of the currency will also be influenced by its use in investment, remittances of profits, paying interest and dividends, speculation and in terms of reserves

Note: maximum of 4 marks. [4]

(b) if the value is falling, the government will step in to buy more of the currency
if the value is rising, the government will step in to sell more of the currency
governments buy foreign currencies using reserves
the government could also increase interest rates when the value is falling
and reduce interest rates when the value is rising
reference to the mechanism by which interest rates changes affect the exchange rate

Note: maximum of 4 marks. [4]

(c) to make its exports relatively cheaper in price in foreign markets and therefore more competitive
this could lead to an increase in demand (especially if the price elasticity of demand for the goods is elastic)
to make imports more expensive which should lead to a reduction in the number of imports (assuming the price elasticity of demand is elastic)
this should lead to an improvement in a country's balance of trade in goods and services
the government might not have sufficient reserves to keep intervening in the foreign exchange market (where there is persistent downward pressure on the exchange rate)

Note: maximum of 4 marks. [4]

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(d)

Advantages of a floating exchange rate system: • the rate will be determined continually through market forces, so the government doesn't have to intervene • there is no need to hold large amounts of reserves • government is not committed to maintaining a particular external value of the currency and so can focus on other objectives Disadvantages of a floating exchange rate system: • it can fluctuate a great deal and this volatility can make it very difficult for firms to plan ahead • there can be speculative pressures on the currency	Advantages of a fixed exchange rate system: • less volatility in the exchange rate so less instability • makes planning/forecasting easier and so less uncertainty • could encourage investment/trade, having a positive effect on the economy • avoids speculative movements in exchange rate Disadvantages of a fixed exchange rate system: • requires government to hold large reserves • if the rate cannot be maintained, there will be a dramatic change in value through a devaluation

Answers which simply describe the features of the two systems can gain no more than 6 marks; to get above that, candidates do need to state to what extent one is preferable to the other.

Note: maximum of 8 marks. [8]

7 **(a)** Up to 2 marks on absolute poverty:
Absolute poverty is where people do not have access to basic items (1), such as food, shelter and clothing (1) living on less than e.g. $1.25 a day

Up to 2 marks for relative poverty:
Relative poverty is where people are poor relative to other people in the economy (1), i.e. they have access to fewer goods and services than others (1) relative poverty always exists (1)

Note: maximum 4 marks. [4]

(b) Three parts to the Human Development Index, each of which can be awarded up to 2 marks each:
- standard of living (1): GDP/GNI per capita/per head (1)
- longevity (1); life expectancy at birth (1)
- education/knowledge (1): adult literacy/enrolment in education/mean years of education/expected years of schooling (1)

Note: maximum of 6 marks. [6]

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(c) public spending on health
public spending on education
subsidies to consumers to help the poor
subsidies to producers to enable them to lower costs and prices
greater use of progressive taxation to reduce income inequalities
greater use of benefits to poor people
public spending on infrastructure to increase provision of jobs
lower interest rates to increase demand
introducing/raising a national minimum wage
encouraging more multinational companies to locate in a country, e.g. through tax holidays
government policies to promote growth and employment

Up to 6 marks for exploring how policies may reduce poverty.

Up to 7 marks for assessing policies' advantages/disadvantages.

Two policies assessed in depth could gain 10 marks.
Note: maximum of 10 marks. [10]

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