UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS

GCE Ordinary Level

MARK SCHEME for the October/November 2010 question paper for the guidance of teachers

2281 ECONOMICS

2281/23 Paper 2 (Structured Questions), maximum raw mark 80

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UNIVERSITY of CAMBRIDGE
International Examinations

1 (a) A merger occurs when two or more firms agree to join together to form a new business enterprise; there is a combining of two or more firms under one management and there is usually mutual agreement (1).

A takeover occurs through an acquisition where one company buys all, or a controlling interest, of the shares of another company; this may involve a hostile bid by one company for another and so there may be quite a lot of opposition (1). [2]

(b) Economies of scale:
- bulk-buying
- managerial
- technical, e.g. specialisation, indivisibilities, linked processes
- financial economies
- risk-bearing economies.

These are all internal economies of scale, but credit should be given for reference to possible external economies, such as availability of skilled labour or existence of ancillary firms.

The question does refer explicitly to car production; a maximum mark of 3 if a general answer with no specific reference to car production. [5]

(c) Possible reasons:
- decline in income/real income/disposable income
- prices too high
- prices uncompetitive with other producers
- possible increase in taxes on cars
- quality/reliability less than competitors
- recession/rise in unemployment/general economic conditions
- lack of advertising/poor quality of advertising
- improvement in quality of public transport/more reasonable prices (substitute good)
- rise in price of petrol/diesel (complementary good). [6]

(d) Possible reasons:
- to maintain employment
- to maintain revenue from taxes
- to avoid having to pay unemployment benefits and other forms of social security benefits
- negative regional multiplier effect (don't expect use of term multiplier)
- status/reputation of economy
- possible political reasons, e.g. don't want to risk losing votes of so many people.

Maximum of 4 marks for a one-sided view.

Candidates do not need to discuss all of these. Full marks can be obtained if just two reasons are discussed thoroughly. [7]

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2 **(a)** Possible points:
- enterprise refers to business knowledge and the ability to run a production process
- it is the quality which involves initiative to create and sell a product
- entrepreneurs organise resources to make goods and services
- they are the people who take the risks
- they are the people who take the decisions necessary to make a firm run successfully. [4]

(b) Possible ways:
- subsidies/grants
- tax incentives
- regional policy
- reskilling/retraining schemes
- encouraging investment from overseas
- road shows/advertising to encourage new entrepreneurs. [4]

(c) Diagrams:
- both diagrams correctly labelled (demand, supply, price, quantity) (1)
- shift of demand curve in one diagram (1)
- shift of supply curve in the other diagram (1).

Re-allocation of resources:
- decisions are made by individual buyers and sellers
- they act in their own self-interest
- producers aim to maximise their profits
- consumers aim to maximise their utility/satisfaction
- the price mechanism allocates resources
- this is done through the interaction of the forces of demand and supply
- there is a market-clearing equilibrium position where there is no excess demand or excess supply
- there is no government intervention. [6]

(d) Possible disadvantages of market forces:
- merit goods may be under-provided
- demerit goods may be over-provided
- public goods may not be provided at all
- externalities may not be taken into consideration
- some consumers/producers will have more power than others.

Candidates do not need to refer specifically to demerit, merit or public goods to gain full marks.

A key word in the question is **just**; a one-sided answer can gain no more than 4 marks. [6]

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3 (a) Functions:

- accepting deposits of money and savings
- helping customers make and receive payments
- making personal and commercial loans
- providing overdraft facilities
- buying and selling shares for their customers
- providing bureau de change facilities
- storing valuables in safe deposits
- financial advice.

Candidates do not need to describe all of these. Full marks can be obtained through a thorough description of just two of them. [4]

(b) A definition of the Stock Exchange can gain 2 marks.

Role of a stock exchange:

- it enables stocks and shares to be bought and sold
- it brings buyers and sellers of stocks and shares together
- this enables firms to raise finance
- it thus contributes to the growth of an economy
- it will usually have an index indicating the general value of stocks and shares and this will show how an economy is doing.

Candidates do not need to explain all of these. Full marks can be obtained through a thorough explanation of just one of them. [4]

(c) Differences in earnings between:

- male/female
- skilled/unskilled
- private/public
- agricultural/manufacturing/services.

Allow any reasonable grouping of workers, e.g. by age, union or non-union, part-time or full-time, regional, level of risk.

A description of the differences can gain no more than 4 marks. [6]

(d) Low income groups are likely to:

- spend a high proportion of their income (propensity to consume) to meet basic needs for food, clothing, housing and heating
- save a low proportion (the savings ratio) of their income because they don't usually have very much of their income left to save.

High income groups are likely to:

- spend a low proportion of their income; they will probably spend more than low income groups, but it will be a smaller proportion of their income. Much of this spending will be in relation to wants rather than needs, e.g. expenditure on luxury items
- save a high proportion of their income because they usually have quite a lot of their income left over to save.

A key word in the question is **always**; an answer which fails to take this into account can gain no more than 4 marks. [6]

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4 **(a)** A co-operative:

- a business organisation which is owned and controlled by a group of people to undertake an economic activity to their mutual benefit
- each member of a co-operative has an equal share in the ownership and control of the organisation, e.g. a co-operative retail or farming group. [2]

A public corporation:

- it is owned/controlled by a government/is in the public sector
- it is responsible for the day-to-day running of a business. [2]

(b) Demand for labour:

- a derived demand for what the labour can produce
- the higher the revenue obtained from the sales of these products, the greater the demand for labour to produce these products
- the revenue obtained from the sale of these products will need to be greater than the cost of employing the labour
- is therefore linked to the wage rate paid; idea of surplus value (don't need to use that term)
- this is why the demand curve for labour is downward-sloping
- linked to the productivity of the labour
- will be affected by demand for capital. [6]

(c) Definitions of public and private sector – up to 2 marks.

Possible advantages of public sector employment:

- greater job security
- job satisfaction, e.g. working in state community schools
- status, e.g. doctors in state community hospitals
- enhanced pension provision.

Possible advantages of private sector employment:

- improved working conditions
- better pay
- more incentives, e.g. bonuses
- stress on efficiency.

A maximum of 6 marks, inclusive of mark(s) for definitions, for an answer which deals with only one of the sectors. [10]

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5 (a) Inflation is a general (1) and sustained/persistent (1) rise in the level of prices (1) of goods and services in an economy over a period of time (1).

Any three of these four aspects can be rewarded.

For comment on reduction of purchasing power/increase in cost of living, 1 mark. [3]

(b) Possible causes:
- demand-pull
- cost-push
- monetary (excessive growth of the money supply)
- imported (as a result of international trade).

Difficult to give specific marks for each of these possible causes of inflation. Candidates can gain full marks for any two causes only. An answer which analyses only one cause can gain a maximum of 3 marks. [7]

(c) A subsidy is a payment made by a government (1) to producers (1) to help reduce their costs of production (1). [3]

Allow up to 2 marks if reference is only made to consumers.

(d) Possible advantages of subsidies:
- as a result of the subsidy, producers will tend to increase supply at every price
- as supply increases, the market price will tend to fall
- this will benefit consumers who will gain by being able to buy a product at a lower price than would otherwise be the case
- demand will expand and this will increase standards of living
- this is especially the case if it is an essential service/product.

Possible disadvantages of subsidies:
- public money is needed to finance them
- can distort competition
- can be used to support inefficient producers
- can lead to excess supply
- may not be passed on to consumers.

Accept answers that focus on subsidies being provided to consumers, e.g. in the provision of education.

A maximum of 4 marks if an entirely one-sided answer. [7]

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6 (a) Difficulties:

- it may be measured by the number of people claiming unemployment benefits, but not all countries pay these
- some people may want to work, but are not actually claiming benefits
- some people may be in employment in the hidden/informal economy, but are officially registered as unemployed
- poor data collection in rural areas
- high dependence on seasonal work.

Can gain all 3 marks for one problem well developed. [3]

(b) Possible consequences:

- the economy is under-producing compared to its potential output
- this leads to a lower rate of economic growth
- it is a waste of scarce resources
- the government loses tax revenue from income tax as fewer people are working and less revenue from VAT as there is less spending
- the government has to pay out more in the form of unemployment benefits; there is an opportunity cost of this as the money could have been spent elsewhere
- it can cause social problems, such as a higher crime rate
- workers pay higher taxes. [6]

(c) Real Gross Domestic Product:

- real – after the effect of inflation has been taken into account (1)
- gross – before depreciation/capital consumption is deducted (1)
- domestic – produced within the geographical boundaries of the country (1)
- product – the goods and services produced in a given year (1).

Alternatively, allow 2 marks for idea of output and 2 marks for explanation of real. [4]

(d) Possible differences:

- real GDP per capita
- levels of income
- life expectancy
- education/literacy rate
- access to safe water supplies and sanitation
- extent of ownership of consumer goods
- primary/secondary/tertiary proportions
- participation in international trade
- availability/use of capital
- health
- diet
- infrastructure
- distribution system
- rate of population growth/optimum population.

A maximum of 5 marks if candidates only discuss developed or developing countries. [7]

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7 **(a)** Possible factors:
- a reduction in import controls
- an increase in demand/standard of living
- the collapse of a domestic producer
- an effective advertising campaign for the imports
- exhaustion of domestic resources. [4]

(b) Possible advantages of a fixed exchange rate:
- less volatility in the exchange rate so less instability
- makes planning/forecasting easier and so less uncertainty
- this could encourage investment/trade, having a positive effect on the economy
- avoids speculative movements in exchange rate
- it could encourage tourism
- it will force a country to control its rate of inflation. [6]

(c) Possible advantages of a fall in an exchange rate:
- exports made more competitive
- this would stimulate demand for them if PED is elastic
- imports made less competitive
- this would reduce demand for them if PED is elastic
- balance of payments disequilibria can be corrected
- there is no need for the central bank to use foreign reserves to maintain a fixed exchange rate.

Possible disadvantages of a fall in an exchange rate:
- PED may not be elastic and so the effect on the balance of payments may be less than expected
- if demand for imports is inelastic, this could contribute to imported inflation.

A key word in the question is **always**; an answer which fails to take this into account can gain a maximum of 6 marks. [10]

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