CAMBRIDGE
INTERNATIONAL EXAMINATIONS

JUNE 2002

GCE Advanced Subsidiary Level

# MARK SCHEME

MAXIMUM MARK: 40

## SYLLABUS/COMPONENT :9708 /2

## ECONOMICS
## (DATA RESPONSE AND ESSAY (CORE))

UNIVERSITY of CAMBRIDGE
Local Examinations Syndicate

## SECTION A

**1ai) Explain the difference between the meaning of 'nominal and 'real' oil prices [2]**

Nominal = money or current value (1), real = purchasing power or without inflation (1)

**1aii) Describe the general trends in the nominal price of oil between 1970 and 1999 shown in Fig.1 [2]**

Upward 1970 – 1982 (1), downward 1982 – 1999 (1), erratic after 1986 (1). Any two aspects.

**1aiii) Using Fig1, summarise the relationship between real and nominal oil prices over the period 1970 to 1999. [2]**

Two interpretations acceptable :
Pre 1985 real prices higher (1), post 1985 nominal prices higher (1) or both move in same direction (1), but to different extent (1).

**1bi) Identify one year in which the nominal price of oil rose sharply and was subsequently maintained at the higher level. [1]**

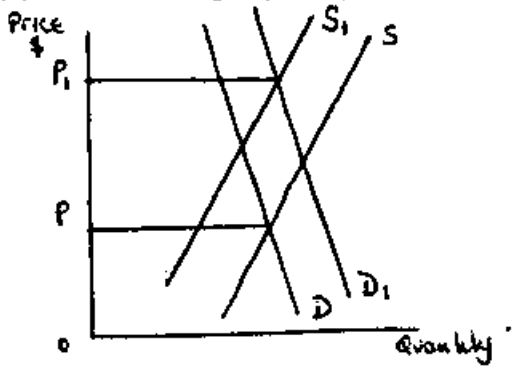
1979 (1) 1973 (1)

**1bii) Suggest two problems caused for producers by the variability of oil prices.[2]**

Unstable incomes (1), planning difficulties (1) or other acceptable problems.

**1c) Explain with the aid of a diagram how the article accounts for the sharp oil price rise in 1999. [5]**

OPEC reduction of supply (1), increase in world demand (1), diagram showing S curve to left (1), D curve to right (1), higher price (1).




**1d) Discuss the possible effects in an oil- consuming country if its government imposes an indirect tax on oil. [6]**

Effect on price, output and tax revenue linked to consumer, producer, government (4) development e.g. elasticity, tax burden (2)

## Section B

**2a) Explain, with examples, the meaning of private costs and external costs. [8]**

*Costs borne by the agent directly involved e.g. a consumer or firm are private costs. This would include the cost of purchase of goods or factor services. External costs are felt by a third party and exist when social cost exceeds private cost. Examples would be pollution and congestion.*

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|---|---|
| L3 Detailed contrast linked to social cost or use of diagram | 7 – 8 |
| L2 Understanding with examples | 4 – 6 |
| L1 Basic recognition | 1 – 3 |

**b) Discuss the role that cost benefit analysis can play in government economic policy making. [12]**

*Cost benefit allows a wider range of influences to be introduced into decision making than might be considered in commercial terms. This would allow the government to take a social view of an action. The method has difficulties in terms of inclusiveness, valuations and normative judgements but should allow a conclusion depending upon assumptions. It is often used in transport and infrastructure planning.*

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| L3 Discussion of the limitations of the method | 9 – 12 |
| L2 Understanding of its application to projects | 5 – 8 |
| L1 Knowledge of the method of cost benefit analysis | 1 – 4 |

**3a) Explain the methods a government might use to protect its national industries from foreign competition. [8]**

*Methods may be external such as tariffs, quotas and embargoes or internal such as subsidies. A long term view may be taken aiming at an increase in domestic efficiency with restructuring, training and research expenditure, devolution, supply side policy*

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| L3 Explanation distinguishing between preventing foreign competition and promoting domestic efficiency | 7 – 8 |
| L2 Explanation of the working of the methods | 4 – 6 |
| L1 Recognition of methods | 1 – 3 |

**b) Discuss whether trade protection can ever be justified. [12]**

*Protection can be supported in the short term. Arguments can include infant industry, anti dumping and orderly run down. Against this is the case for free trade based on comparative advantage. It can be argued that there are weaknesses in the application of the theory to the real world.*

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| L3 Discussion of the case for protection and free trade | 9 – 12 |
| L2 Explanation of the case for protection | 5 – 8 |
| L1 Identification of possible justifications | 1 – 4 |

**4a) Explain why a country might experience a persistent rise in its general price level.** **[8]**

*Inflation can result from cost push and demand pull influences, monetary inflation may also be treated as a distinct category. The influences at work may include import costs, wage costs and higher taxes with higher incomes and changing attitudes. Once started an inflationary spiral may develop.*

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| L3 Explanation of the interaction of various causes | 7 – 8 |
| L2 Explanation of the causes | 4 – 6 |
| L1 Recognition of the causes | 1 –3 |

**b) Discuss why reducing inflation is often the most important task for a government.** **[12]**

*Harmful effects on international competitiveness, distribution of income, market efficiency and planning capability may justify statement. Its importance to other government objectives may be explored. However the rate of inflation, its comparative level and the seriousness of other economic problems may indicate alternative emphasis.*

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| L3 Discussion of reducing inflation as the most important task | 9 – 12 |
| L2 Explanation of the harmful effects of inflation | 5 – 8 |
| L1 Recognition of harmful effects | 1 – 4 |