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CAMBRIDGE INTERNATIONAL EXAMINATIONS

GCE Advanced Subsidiary Level and GCE Advanced Level

MARK SCHEME for the October/November 2012 series

9708 ECONOMICS

9708/21 Paper 2 (Data Response and Essay – Core), maximum raw mark 40

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1 (a) Between 1995 and 2007 which country was

(i) the least successful and [1]

UK or France

(ii) the most successful in increasing the overall educational participation rate? [1]

South Korea

(b) Explain TWO possible economic reasons why the educational participation rate of 15–19 year-olds is higher than that of 20–29 year-olds as shown in Table 1. [4]

e.g. legal requirement
direct costs
opportunity costs
age – family responsibilities etc. (2 × 2)

(c) (i) What is the difference between production and productivity? [2]

Production relates to output from all factors of production (1)
OR
Production is the process of providing goods and services
Productivity is output per unit of input (often labour) (1)

(ii) Explain how education may affect labour productivity and the production possibility curve. [4]

Education results in greater skills leading to higher productivity (1)
Higher productivity leads to higher output (1)
Understanding of ppc (1) – either written or accurate diagram
Outward shift of ppc (1)

(d) Why is education considered to be an example of a merit good? [2]

EITHER
Merit goods are under-consumed because of lack of information (1)
Individuals not aware of benefits (1). In terms of long term income/career opportunities/ personal development (1)
OR
Education has positive externalities (1). Benefits to society on top of individual benefits (1). More educated labour force contributes to higher national welfare (1)

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(e) Discuss the extent to which the provision of education is different from the provision of national defence. [6]

Education is a private good but defence is a public good (1)
Explanation of (Non) excludability/(Non) rivalry/(Non) rejectability (2)
(1 mark if any 2 of the above are correctly identified but not explained)
In market economy – education under-provided, defence not provided at all (1)
Both can be totally provided by the public sector from taxation (1)
Defence can **only** be provided by public sector (1) + reason (1)
Education can be provided by public and private sectors (1)
Reason for public sector provision of education (1)
Reason for private sector provision of education (1)
Comments on contrast of provision (1)

2 (a) Explain, with the use of diagrams, the different effects on the price and quantity of a product of the removal of a subsidy and the removal of an indirect tax on that product. [8]

A subsidy is a grant to producers that lowers their costs of production. Its removal will shift the supply curve to the left and result in a higher price and a lower quantity traded.
An indirect tax, e.g. VAT or GST, is levied on goods and services and raises the cost of production. Its removal would shift the supply curve to the right and result in lower price to the consumer with a greater quantity traded.

For **knowledge and understanding** of subsidies and indirect taxes (4)

For an **analysis** of how the removal of a subsidy and indirect would affect price and quantity of a product. (4)

(b) Discuss the possible benefits and drawbacks of government subsidies to agriculture. [12]

Subsidies lower producer costs and increase output. This benefits consumers who pay lower prices and producers who receive higher incomes. This may be justified in terms of maintaining essential products, supporting lower income groups, preventing dependence on foreign suppliers, improving the balance of trade, retaining a traditional form of life and contributing to environmentally friendly activity that has positive externalities.

Subsidies have opportunity costs in terms of alternative government expenditure, may reduce the efficient allocation of resources, may encourage dependence on the state, may reduce producer initiative and may raise taxes with disincentive effects.

For **knowledge and understanding** of the impact of subsidies on costs (1) prices and output (1) (2)

For an **analysis** of the benefits (4 max.) and drawbacks (4 max.) of subsidies. (6)

For an **evaluation** of the overall impact of subsidies. (4)

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3 (a) Explain, with the use of an aggregate demand (AD) and aggregate supply (AS) diagram, the different effect of cost-push and demand-pull inflation on real output. [8]

Inflation is a persistent rise in the general price level. Cost-push is based on rising costs such as wages, raw materials, taxes and affects the AS curve. Demand-pull results when consumption, investment, government spending or exports minus imports shift the AD curve.

A shift to the right of the aggregate demand curve on an upward-sloping section of the aggregate supply curve will cause inflation and Increase real output. A shift to the left of the aggregate supply curve will also cause inflation but will reduce real output.

For **knowledge and understanding** of cost-push inflation, demand-pull inflation and real output (Max. of 2 for anyone) (4)

For an **analysis** of the effects on real output. (4)

(b) Discuss whether the effect of the rate of inflation on the exchange rate is more or less important than the effect of the exchange rate on the rate of inflation. [12]

A relatively high rate of inflation will make a country less competitive in international trade. Exports may fall, imports may rise and the current balance may worsen. International confidence in the currency may fall reducing investment and the financial flow may become adverse. There will be less demand for and increased supply of the currency and it may depreciate. A low rate of inflation may not have a noticeable effect.

Changes in the exchange rate affect the rate of inflation within an economy. A depreciating exchange rate will make imports more expensive (cost-push inflation) and exports cheaper (demand pull inflation). An appreciation will reduce inflationary pressure. Candidates may consider the extent to which each influence is the major or only influence on the other. For example inflation may be influenced by a wide range of domestic factors while the exchange rate may be significantly affected by the trade position. A decision on the importance of the two links will depend on the conditions assumed.

For **knowledge and understanding** of the rate of inflation (1) and the exchange rate (1) (2)

For an **analysis** of how the rate of inflation can affect the exchange rate (4 max.) and how the exchange rate can affect the rate of inflation (4 max.) (6)

For an **evaluation** of the importance of the influences. (4)

4 (a) Explain the different types of international economic integration. [8]

The common forms of integration are free trade areas, customs unions, and economic unions. They differ in their levels of integration. The main differences relate to common external tariffs, freedom of movement of factors of production, common currency systems and common economic policies. The different forms will reflect the intentions of the members, the similarities of members' economies and their ability to achieve common policies.

For **knowledge and understanding** of international economic integration and its main types(4)

For an **analysis** of the features of each type. (4)

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(b) Discuss the possible economic effects of a global ban on all forms of trade protection. [12]

Trade protection involves measures to restrict the flow of international trade, such as tariffs, quotas, subsidies and exchange controls. The outcome is that the domestic market faces less international competition. A ban on protection would mean free trade with greater international competition. This has the benefit of more efficient production based on comparative advantage, cheaper prices, wider choice, higher employment and greater welfare. The change might cause casualties in the short run that might justify temporary protection. The usual cases involve infant industries, sunset industries, structural adjustment, loss of government revenue and harm to the terms of trade. It has been suggested that globalisation has benefited developed countries at the expense of developing economies.

For a **knowledge and understanding** of a 'global ban on trade protection' (2)

For an **analysis** of the benefits (4 max.) and drawbacks (4 max.) of a global ban on trade protection. (6)

For an **evaluation** of the overall desirability of a global ban on trade protection. (4)

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1 (a) (i) Calculate the approximate price of sugar in January 2008. [2]

Approximate value is 11.5 US cents per pound (2).

(ii) Compare the behaviour of sugar prices with that of average food prices between January 2008 and August 2009. [3]

Similar until July 2008 (1), sugar price then rose, while average food price fell (1), sugar price rose overall, all food price fell overall (1), both fluctuated, (1)

(b) With the use of diagrams, contrast the weather explanations of the sugar price rise with the ethanol explanations of the sugar price rise. [5]

Bad weather decreases supply (1), with diagram showing leftward shift of the supply curve and rise in price (1). Ethanol use increases demand (1) with diagram showing rightward shift of the demand curve and rise in price (1). Reserve (1) for clear understanding of the quantity change in both cases.

(c) Explain the likely reaction of

(i) consumers of sugar, and
1 mark for understanding that consumers would reduce quantity demand and 1mark for some elaboration of this idea. (2)

(ii) producers of sugar
1 mark for understanding that producers would increase quantity supplied and 1 mark for some elaboration of this idea (2)

to a continual, rapid rise in its price. [4]

(d) With reference to the data, discuss the likely effects of [6]

(i) the actions of the Indian government, and

Increased supply of sugar as a result of the export ban has reduced prices of sugar in India.
This will help Indian consumers, especially the lower income groups. India's current account will be affected as sugar exports fall. Sugar farmers will reduce cultivation of sugar and this is likely to increase prices in the future. It may also lead to unemployment. Allow comment on world impact, such as new areas under cultivation. Also impact on Indian's balance of trade. (Up to 4 marks)

(ii) the actions of the Malaysian government.

A maximum price would cause an excess demand in the market for sugar in Malaysia. This would help those lucky enough to obtain sugar but would mean shortages and the problem of allocation would arise. The outcome would be queuing and black markets unless an effective rationing system could be devised. (Up to 4 marks)

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2 (a) Explain, with the help of a production possibility diagram, how the opportunity cost of producing different combinations of goods can be measured. [8]

For knowledge and understanding of the ppc and opportunity cost (Up to 4 marks. Allow 3/1 or 1/3 split). For an analysis of how the ppc can be used to measure opportunity cost (Up to 4 marks).

(b) Discuss the ease with which a planned economy may be changed into a market economy. [12]

For knowledge and understanding of planned and market economies (2).
For an analysis of the nature of the changes required to transform a planned economy into a market economy. (Up to 2 marks for identified features with implications that they need to change). (Up to 6 marks) For evaluative comment on the ease of transformation.

3 (a) Explain what determines the demand for and supply of a currency in the foreign exchange market. [8]

For knowledge and understanding of the determinants of the demand and supply of a currency in the foreign exchange market (Up to 4 marks. Allow 3/1 or 1/3 split). For analysis of how changes in these determinants impact upon the foreign exchange market (Up to 4 marks).

(b) Discuss the extent to which a decline in the value ofthe national currency (depreciation or devaluation) will improve a country's balance of trade. [12]

For knowledge and understanding of depreciation or devaluation and the balance of trade (2). For analysis of how depreciation affects the balance of trade (Up to 6 marks). For evaluative comment on the conditions for a successful outcome (Up to 4 marks).

4 (a) Explain why governments measure changes in the general price level and why they usually have more than one measure of these changes. [8]

For knowledge and understanding of anyone method of measuring changes in the general price level e.g. CPI, RPI, WPI etc (Up to 4 marks). For analysis of why it is measured and why a number of measures are needed (Up to 4 marks. Allow 3/1 or 1/3 split).

(b) Discuss whether it is better for a government to raise the economy's rate of productivity growth or to control its rate of inflation. [12]

For knowledge and understanding of inflation and productivity (2). For analysis of the effects of inflation and productivity growth (Up to 6 marks). For evaluative comment on 'whether it is better' aspect of the question (Up to 4 marks).

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1 (a) (i) Compare the price of petrol in the US and China between January 2008 and September 2009. [2]

US petrol dearer pre-October 2008 (1 mark), Chinese petrol dearer post October 2008 (1 mark), Chinese price rose while U.S. price fell (1 mark), Chinese price less volatile (1 mark)
Any two points. (2 marks total)

(ii) How does Fig. 1 confirm that it is in China rather than in the US that the price of petrol is set by the government? [2]

The stepped nature and period of stability (1 mark) suggest that it is government action rather than market forces that determine price in China (1 mark).
Allow analysis from the US view i.e. US price more volatile (1 mark), because it is subject to market forces (1 mark) (Up to 2 marks)

(b) Explain how the consumption of petrol generates externalities. [4]

Externalities affect third parties (spill-over effects) (1 mark); they can be negative externalities (1 mark). In the case of petrol they are harmful and they generate air pollution that contributes to ill-health and global warming. (up to 2 marks) (Up to 4 marks)

(c) (i) Identify two points about the PED of petrol on which the studies agree. [2]

PED of both is inelastic (1 mark) short-run PED is more inelastic than long-run PED in both cases (1 mark), both have negative value confirming expected inverse price/demand relationship, (1 mark)
Any two points. (2 marks total)

(ii) Explain why the values of the short-run and long-run PEDs for petrol are different. [4]

In the short-run the consumer has less time to respond to the price change by adjusting spending (1 mark). One further mark for elaboration of this statement (1 mark) (up to 2 marks)
In the long-run the consumer has more time to substitute cars for other forms of transport (1 mark). One further mark for elaboration of this statement (1 mark) (up to 2 marks)

(Up to 4 marks)

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(d) Discuss the possible consequences of the Chinese price fixing policy between January 2008 and September 2009. [6]

Keeping the price lower will help low income consumers, reduce inflationary pressure and keep production costs down. It may encourage waste, cause petrol producers to lose money and cause shortages. (up to 4 marks)
Keeping the price higher will reflect market pressures, encourage responsible use through less waste. It may harm consumers, especially those on low incomes.
(up to 4 marks)
Also, allow marks for stability (up to 4 marks)
General arguments concerning the efficiency of resource allocation should be credited.
(6 marks maximum)

2 (a) Explain, with the aid of a diagram, what changes will alter the amount of consumer surplus available from the consumption of a good. [8]

For **knowledge and understanding** of consumer surplus illustrated with an appropriate diagram. (Up to 4 marks. Allow 3/1 or 1/3 split).
For an **analysis** of how changes in demand and/or supply change consumer surplus through their impact upon price. (Up to 4 marks)

(8 marks total)

(b) Discuss why in many countries some services, such as education and healthcare, are supplied both by the government and private producers. [12]

For **knowledge and understanding** of private goods and merit goods. (Up to 2 marks)
For an **analysis** of government and private supply of education and healthcare.
(Allow 4/2 or 2/4 split) (Up to 6 marks)
For **evaluative comment** on government and private supply of education and healthcare.
(Up to 4 marks)

(12 marks total)

3 (a) Explain the factors that might cause a fall in a country's terms of trade. [8]

For **knowledge and understanding** of the terms of trade with illustration of a fall in the index.
(Up to 4 marks. Allow 3/1 or 1/3 split).
For an **analysis** of the factors that cause a fall in terms of trade e.g. exchange rate depreciation, relative rates of inflation etc.) (Up to 4 marks)

(8 marks total)

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(b) Discuss the view that unrestricted free trade has as many disadvantages as advantages. [12]

For **knowledge and understanding** of meaning of 'unrestricted free trade' (Up to 2 marks)
For an **analysis of the advantages** and disadvantages of unrestricted free trade (Allow 4/2 or 2/4 split) (Up to 6 marks)
For **evaluative** comment on relative strength of the advantages and disadvantages. (Up to 4 marks)

(12 marks total)

4 (a) Explain how an economy may face a deficit in its trade in goods yet have a surplus on its current account of the balance of payments. [8]

For **knowledge and understanding** of the relevant structure of the current account deficit in trade in goods and surplus on current account. (Up to 4 marks. Allow 3/1 or 1/3 split).
For an **analysis** of the offsetting inflows that create a surplus on current account. (Up to 4 marks)

(8 marks total)

(b) Discuss whether a satisfactory balance of payments, a strong exchange rate and a low rate of inflation are likely to be achieved at the same time. [12]

For **knowledge and understanding** of the targets identified. (Up to 2 marks)
For an **analysis** of the relationships between the targets. (Up to 6 marks)
For **evaluative comment** on the compatibility of the targets and likelihood of the targets being achieved at the same time. (Up to 4 marks)

(12 marks total)

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