



MARKSCHEME

November 2008

ECONOMICS

Higher Level

Paper 2

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In addition to the assessment criteria use the paper-specific markscheme below. Award up to the maximum marks as indicated. Each question is worth [10 marks].

1. Explain how the three basic economic questions would be answered in a free market economy and in a centrally-planned economy.

Candidates **may** include any of the following:

- explanation of a free market economy and a centrally-planned economy
- what to produce?
 - in a free market economy, decided by consumer sovereignty/demand
 - in a centrally-planned economy, decided by the central planners, based upon their view of what is appropriate
 - some candidates may include the availability of appropriate resources as a determinant of what can be produced in both types of economy
- how to produce?
 - in a free market economy, decided by cost of production and attempts to minimize unit costs of production/maximizing profit
 - in a centrally-planned economy, decided by the central planners based upon desired production targets
- for whom to produce?
 - in a free market economy, decided by income/ability to pay
 - in a centrally-planned economy, determined by perceived needs in the view of the central planners.

If a candidate deals with only one question, then the candidate may not be rewarded beyond level 2.

If a candidate deals with only two questions, then the candidate may not be rewarded beyond level 3.

If a candidate deals with all three questions reasonably, then the candidate should be rewarded in level 4.

Examiners should be aware that candidates may take a different approach, which if appropriate, should be rewarded.

2. Using diagrams, explain the difference between the short-run and long-run profit maximizing positions of a firm in monopolistic competition.

Candidates **may** include any of the following:

- the characteristics of monopolistic competition
- an example of monopolistic competition, *e.g.* food, clothing, restaurants
- a diagram illustrating a short-run profit maximizing position, *e.g.* abnormal profits or losses
- an explanation of the short-run profit maximizing position
- a diagram illustrating the long-run profit maximizing position, *i.e.* normal profits
- an explanation of the long-run profit maximizing position and how it differs from the short-run profit maximizing position.

If a candidate deals with only one position, *i.e.* short-run or long-run, then the candidate may not be rewarded beyond Level 2.

Candidates who incorrectly label diagrams cannot be rewarded with full marks.

Examiners should be aware that candidates may take a different approach, which if appropriate, should be rewarded.

3. Explain how the burning of fossil fuels (*e.g.* coal) by industries could create a market failure and a threat to sustainable development.

Candidates **may** include any of the following:

- a definition of market failure
- burning fossil fuels may create pollution, which is an example of market failure
- negative externality (of production)
- a diagram illustrating the negative externality
- effects on third parties, *e.g.* air pollution and the effects on health or global warming
- definition of sustainable development
- the creation of pollution will compromise the ability of future generations to enjoy air quality.

Some candidates may approach the question by referring to negative externalities of consumption. If done appropriately this should be rewarded.

Examiners should be aware that candidates may take a different approach, which if appropriate, should be rewarded.

4. Explain *two* ways a government can reduce its natural rate of unemployment.

Candidates **may** include any of the following:

- a definition of the natural rate of unemployment
- a diagram to explain the natural rate of unemployment (*e.g.* LRAS, LRPC, labour market diagram)
- a statement that the natural rate of unemployment can be reduced by policies
- an explanation of two policies and how these will reduce the natural rate of unemployment – these may include:
 - reduction in income taxes
 - reduction in corporation taxes
 - reduction in trade union power
 - reduction or elimination of minimum wages
 - reduction in unemployment benefits
 - deregulation
 - privatization
 - education and training
 - research and development aid
 - provision of infrastructure
 - improved information.

If a candidate deals with only one policy, then the candidate may not be rewarded beyond level 2.

Examiners should be aware that candidates may take a different approach, which if appropriate, should be rewarded.

5. Using a diagram *or* a numerical example, explain how the concept of comparative advantage determines which goods or services a country should export.

Candidates **may** include any of the following:

- explanation of the law of comparative advantage
- opportunity cost and specialization
- an appropriate diagram
- explanation of the diagram
- a numerical example of comparative advantage
- explanation of the numerical example
- an explanation that a country should specialize in, and export, goods in which it has a comparative advantage.

Examiners should be aware that candidates need to give only a diagram **or** a numerical example. Candidates may give both, but this is not necessary for full marks.

Candidates who incorrectly label diagrams cannot be rewarded with full marks.

Examiners should be aware that candidates may take a different approach, which if appropriate, should be rewarded.

6. Using the Harrod-Domar growth model, explain how a country can increase its rate of economic growth.

Candidates **may** include any of the following:

- an explanation of the model in terms of the importance of saving and investment in increasing the rate of economic growth
- a diagram showing a shift in the PPC
- a statement of the equation, *i.e.* rate of growth of GDP = $\frac{\text{savings ratio}}{\text{capital/output ratio}}$
- an explanation of the rate of growth of GDP
- an explanation of the savings ratio
- an explanation of the capital/output ratio (productivity of capital)
- an explanation that the rate of growth of GDP may be increased either by increasing the savings ratio or by reducing the capital/output ratio.

Examiners should be aware that candidates may take a different approach, which if appropriate, should be rewarded.
