



MARKSCHEME

November 2008

ECONOMICS

Higher Level

Paper 3

*This markscheme is **confidential** and for the exclusive use of examiners in this examination session.*

*It is the property of the International Baccalaureate and must **not** be reproduced or distributed to any other person without the authorization of IB Cardiff.*

In addition to the assessment criteria use the paper-specific markscheme below. Award up to the maximum marks as indicated.

1. (a) Define the following terms indicated in bold in the text:

(i) abnormal profits (paragraph ①) [2 marks]

level

0 *Wrong definition* **0**

1 *Vague definition* **1**

The idea that revenues are greater than costs.

2 *Precise definition* **2**

An explanation that they are profits that are above the level that is sufficient to keep the firm in an industry.

(ii) product differentiation (paragraph ④). [2 marks]

level

0 *Wrong definition* **0**

1 *Vague definition* **1**

The idea that similar products are slightly different.

2 *Precise definition* **2**

An explanation that it is where a producer deliberately attempts to distinguish his/her product from those of competitors through branding or packaging or marketing.

(b) Using an appropriate diagram, explain how Apple might have thought it would lose abnormal profits due to the introduction of the Tangent MP3 player (paragraph 1). **[4 marks]**

level

0 *Inappropriate answer* **0**

1 *Identification of appropriate theory* **1-2**

For drawing a correctly labelled diagram, where the demand curve (AR) for the iPod shuffle shifts to the left, along with its MR curve, and for showing that the level of abnormal profits being made falls **or** for providing an explanation of how the competition from the Tangent MP3 player would lead to a fall in demand for iPods, reducing revenue and leading to lower abnormal profits.

2 *Correct application of appropriate theory* **3-4**

For drawing a correctly labelled diagram, where the demand curve (AR) for the iPod shuffle shifts to the left, along with its MR curve, and for showing that the level of abnormal profits being made falls **and** for providing an explanation of how the competition from the Tangent MP3 player would lead to a fall in demand for iPods, reducing revenue and leading to lower abnormal profits.

No marks should be awarded for a simple demand and supply diagram. Answers containing two diagrams representing profit before and after the introduction of the Tangent MP3 should be fully rewarded.

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

(c) With reference to the text, explain which market structure the MP3 player industry most closely represents. **[4 marks]**

level

0 *Inappropriate answer* **0**

1 *Identification of appropriate theory* **1-2**

For explaining that the market structure closely resembles an oligopoly, with reference to any of the theoretical characteristics of an oligopoly.

2 *Correct application of appropriate theory* **3-4**

For explaining that the market structure closely resembles an oligopoly **and for providing evidence from the text** relating to at least two characteristics of an oligopoly, such as non-price competition, product differentiation, interdependence, a few dominant firms, or abnormal profits.

Answers justifying an explanation that the market is a monopoly may be fully rewarded.

(d) Using information from the text/data and your knowledge of economics, evaluate the view that the government should regulate the competitive behaviour of Apple.

[8 marks]

Responses may include:

Reasons for regulation:

- protecting consumers – lower output and higher prices under monopoly
- provides more choice of products for consumers
- ensures competition from other firms
- reduces market failure
- to prevent anti-competitive behaviour such as Apple’s retaliation against stores selling the Tangent (text/data)
- to allow iPod users to play songs purchased from music stores other than iTunes (text/data).

Reasons against regulation:

- Apple may gain economies of scale which result in lower average costs
- lower prices for consumers
- more profits may lead to more research and development and thus greater choice for consumers (more new products)
- legal courts can protect property rights without government intervention.

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

If there is no direct reference to the data, then candidates may not be rewarded beyond level 2.

Effective evaluation may be to:

- consider short-term versus long-term run consequences
- examine the impact on different stakeholders
- discuss advantages and disadvantages
- prioritize the arguments.

Level

0	No valid discussion.	0
1	Few relevant concepts recognized. Little discussion or only basic understanding.	1-2
2	Relevant concepts recognized and developed in reasonable depth. Some attempt at application and analysis.	3-5
3	Relevant concepts developed in reasonable depth, demonstrating effective evaluation, supported by appropriate evidence or theory.	6-8

2. (a) Define the following terms indicated in bold in the text:

(i) **current account deficit** (*paragraph 1*) [2 marks]

level

- | | | |
|---|--|---|
| 0 | Wrong definition | 0 |
| 1 | Vague definition
The idea that it is when imports are greater than exports. | 1 |
| 2 | Precise definition
An explanation that it is when the export revenue from goods and services is less than the import expenditure on goods and services. (Candidates may include net investment income and transfers, but this is not necessary for full marks.) | 2 |

(ii) **multiplier** (*paragraph 3*). [2 marks]

level

- | | | |
|---|--|---|
| 0 | Wrong definition | 0 |
| 1 | Vague definition
The idea that national income will grow by more than any amount of money that is put into the economy. | 1 |
| 2 | Precise definition
Any of the following will be sufficient for full marks: <ul style="list-style-type: none"> • any injection into the economy will result in a larger increase in national income • an explanation that it is the ratio of the induced change in national income to the increase in the level of injections • it is the reciprocal of the marginal propensity to withdraw • it is the reciprocal of the $m_p + m_{pt} + m_{pm}$ • it is the reciprocal of $(1 - m_{pc})$. | 2 |

(b) Using an AD/AS diagram, explain why “lower oil prices are a positive sign for the inflation outlook” (*paragraph 6*). [4 marks]

level

- | | | |
|---|--|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <i>Identification of appropriate theory</i>
For drawing a correctly labelled AD/AS diagram, where SRAS shifts to the right, and the average price level falls or for providing an explanation of how a fall in oil prices will reduce the production costs for many firms in the economy, thus shifting their supply curves to the right and so shifting the SRAS curve to the right, which reduces inflationary pressure. | 1-2 |
| 2 | <i>Correct application of appropriate theory</i>
For drawing a correctly labelled AD/AS diagram, where SRAS shifts to the right, and the average price level falls and for providing an explanation of how a fall in oil prices will reduce the production costs for many firms in the economy, thus shifting their supply curves to the right and so shifting the SRAS curve to the right, which reduces inflationary pressure. | 3-4 |

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

A maximum of [1 mark] may be awarded if candidates shift only an LRAS.

(c) **Using an appropriate diagram, explain why the rising current account deficit “could have serious implications for the rand” (paragraph 4).** [4 marks]

level

- | | | |
|---|---|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <i>Identification of appropriate theory</i>
For drawing a correctly labelled diagram, where the supply curve for the rand has shifted to the right, thus lowering the exchange rate or for providing an explanation of how the expenditure on imports leads to an increase in the demand for foreign currencies and thus an increase in the supply of the rand on the foreign exchange market, since it has to be exchanged for the foreign currencies. | 1-2 |
| 2 | <i>Correct application of appropriate theory</i>
For drawing a correctly labelled diagram, where the supply curve for the rand has shifted to the right, thus lowering the exchange rate and for providing an explanation of how the expenditure on imports leads to an increase in the demand for foreign currencies and thus an increase in the supply of the rand on the foreign exchange market, since it has to be exchanged for the foreign currencies. | 3-4 |

Candidates may take the approach of shifting the demand curve to the left, because demand for South African exports may have fallen. If this is explained correctly, then full marks should be awarded.

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

(d) Using information from the text/data and your knowledge of economics, evaluate the likely effects of the “tightened interest rates” (paragraph 5). [8 marks]

Responses may include:

- possible fall in consumption (text/data)
- the fall in consumption may not be significant because of the strong economic confidence (text/data)
- the fall in consumption may not be significant in the short run “as monetary policy operates with a lag” (text/data)
- possible fall in investment
- possible increase in unemployment
- higher borrowing costs for firms
- appreciation of the exchange rate which is likely to worsen the growing South African current account deficit (text/data)
- reduction in South African inflationary pressure
- imports would be cheaper for consumers, if the exchange rate appreciates
- imported raw materials and semi-finished goods would be cheaper for producers, if the exchange rate appreciates.

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

If there is no direct reference to the data, then candidates may not be rewarded beyond level 2.

Effective evaluation may be to:

- consider short-term versus long-term consequences
- examine the impact on different stakeholders
- discuss advantages and disadvantages
- prioritize the arguments.

Level

0	No valid discussion.	0
1	Few relevant concepts recognized. Little discussion or only basic understanding.	1-2
2	Relevant concepts recognized and developed in reasonable depth. Some attempt at application and analysis.	3-5
3	Relevant concepts developed in reasonable depth, demonstrating effective evaluation, supported by appropriate evidence or theory.	6-8

3. (a) Define the following terms indicated in bold in the text:

(i) **subsidies** (*paragraph ①*) *[2 marks]*

level

0 *Wrong definition* **0**

1 *Vague definition* **1**

The idea that it is money given to firms by the government.

2 *Precise definition* **2**

An explanation that they are a payment made by a government to a firm or industry in order to:

– reduce costs of products

or

– increase supply

or

– lower the price to consumers

or

– give domestic producers an advantage in international trade

(Candidates may only give the reasons for subsidies and this may be rewarded with *[1 mark]*.)

(ii) **income elasticity of demand** (*paragraph ⑤*). *[2 marks]*

level

0 *Wrong definition* **0**

1 *Vague definition* **1**

The idea that it is a relationship between income and demand.

2 *Precise definition* **2**

An explanation that it is a measure of the responsiveness of quantity demanded or demand to a change in income. (Candidates may give only the equation and this may be rewarded with full marks.)

(b) Using an appropriate diagram, explain the effect of the EU tariff on frozen strawberries on the European market for frozen strawberries. **[4 marks]**

level

- | | | |
|---|---|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <p><i>Identification of appropriate theory</i></p> <p>For drawing a correctly labelled diagram, where the imposition of a tariff on strawberries forces up the world supply curve, reducing the quantity of imports and increasing domestic supply or for providing an explanation of how the tariff will force up the price in the EU, which will increase the quantity supplied domestically and reduce imports.</p> | 1-2 |
| 2 | <p><i>Correct application of appropriate theory</i></p> <p>For drawing a correctly labelled diagram, where the imposition of a tariff on strawberries forces up the world supply curve, reducing the quantity of imports and increasing domestic supply and for providing an explanation of how the tariff will force up the price in the EU, which will increase the quantity supplied domestically and reduce imports.</p> | 3-4 |

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

(c) Using an appropriate diagram, explain the type of unemployment that Poland might experience without the strawberry tariff. **[4 marks]**

level

- | | | |
|---|--|------------|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <p><i>Identification of appropriate theory</i></p> <p>For drawing a correctly labelled diagram, showing a fall in demand for labour in the strawberry industry or for providing an explanation of how the type of unemployment is structural unemployment, since there has been a change in the structure of the economy, caused by cheap imports, and thus a fall in demand for labour in the strawberry industry.</p> | 1-2 |
| 2 | <p><i>Correct application of appropriate theory</i></p> <p>For drawing a correctly labelled diagram, showing a fall in demand for labour in the strawberry industry and for providing an explanation of how the type of unemployment is structural unemployment, since there has been a change in the structure of the economy, caused by cheap imports, and thus a fall in demand for labour in the strawberry industry.</p> | 3-4 |

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

- (d) **Using information from the text/data and your knowledge of economics, evaluate a decision to increase protection in the EU strawberry industry.** **[8 marks]**

Responses **may** include:

- definition of protection
- higher prices for consumers
- welfare loss and efficiency loss/misallocation of resources
- revenue from the tariffs
- higher employment in Polish strawberry industry (text/data)
- higher costs for importers of strawberries
- higher costs of production in industries which use strawberries such as jam, yoghurt and ice cream industries (text/data)
- retaliation from China, possibly in the EU wine and cheese industries (text/data)
- possibility that other industries will lobby for protectionism, *e.g.* Spanish furniture makers and Belgian apple farmers (text/data)
- damaging effects on China’s growth.

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

If there is no direct reference to the data, then candidates may not be rewarded beyond level 2.

Effective evaluation may be to:

- consider short-term versus long-term consequences
- examine the impact on different stakeholders
- discuss advantages and disadvantages
- prioritize the arguments.

Level

0	No valid discussion.	0
1	Few relevant concepts recognized. Little discussion or only basic understanding.	1-2
2	Relevant concepts recognized and developed in reasonable depth. Some attempt at application and analysis.	3-5
3	Relevant concepts developed in reasonable depth, demonstrating effective evaluation, supported by appropriate evidence or theory.	6-8

4. (a) Define the following terms indicated in bold in the text:

(i) **economic growth** (*Text 1*) [2 marks]

level

0 *Wrong definition* 0

1 *Vague definition* 1

The idea that it is an increase in output.

2 *Precise definition* 2

An explanation that it is an increase in real GDP in a given time period **or** an increase in potential output, where the PPC (or the LRAS curve) shifts outwards.

(ii) **foreign direct investment** (*Text 1*). [2 marks]

level

0 *Wrong definition* 0

1 *Vague definition* 1

The idea that it is an investment by foreigners.

2 *Precise definition* 2

An explanation that it is capital expenditure by a multinational corporation in a foreign country.

(b) **With reference to the data, explain the reason for the difference in the Chinese GDP figures shown in Figure 1 and Figure 2.** [4 marks]

level

0 *Inappropriate answer* 0

1 *Identification of appropriate theory* 1-2

For noting that GDP is measured at market value in Figure 1 and adjusted for purchasing power in Figure 2 [**1 mark**] and that the GDP adjusted for purchasing power is higher than the GDP at market exchange rates [**1 mark**].

2 *Correct application of appropriate theory* 3-4

For noting that GDP is measured at market value in Figure 1 and adjusted for purchasing power in Figure 2 [**1 mark**] and that the GDP adjusted for purchasing power is higher than the GDP at market exchange rates [**1mark**] **and** for explaining that since GDP measured at market exchange rates does not take into account the relative prices of goods and services, the GDP adjusted for purchasing power in China is higher because relative prices are lower.

- (c) **With reference to the data, explain why India may have experienced economic development between 1975 and 2005.** [4 marks]

level

- | | | |
|---|---|-----|
| 0 | <i>Inappropriate answer</i> | 0 |
| 1 | <i>Identification of appropriate theory</i>
For using the data to show that the indicators (<i>e.g.</i> calorie supply, life expectancy, adult literacy and the infant mortality rate) have improved. | 1-2 |
| 2 | <i>Correct application of appropriate theory</i>
For using the data to show that the indicators (<i>e.g.</i> calorie supply, life expectancy, adult literacy and the infant mortality rate) have improved and for explaining why this means that India has experienced economic development. | 3-4 |

- (d) **Using information from the text/data and your knowledge of economics, evaluate the consequences of economic growth in China.** [8 marks]

Responses **may** include:

- negative externalities of production due to industrialisation (text)
- negative externalities of consumption due to rising incomes
- rising income inequality (text)
- rural-urban migration
- increased government revenue
- employment opportunities
- balance of payments consequences
- possible inflationary pressure
- increased consumption
- increased FDI (text)
- improved prospects for economic development (text)
- prospects of China becoming the world's major economic power (text).

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

If there is no direct reference to the data, then candidates may not be rewarded beyond level 2.

Effective evaluation may be to:

- consider short-term versus long-term consequences
- examine the impact on different stakeholders
- discuss advantages and disadvantages
- prioritize the arguments.

Level

0	No valid discussion.	0
1	Few relevant concepts recognized. Little discussion or only basic understanding.	1-2
2	Relevant concepts recognized and developed in reasonable depth. Some attempt at application and analysis.	3-5
3	Relevant concepts developed in reasonable depth, demonstrating effective evaluation, supported by appropriate evidence or theory.	6-8

5. (a) Define the following terms indicated in bold in the text:

(i) infrastructure (paragraph ❶) **[2 marks]**

level

0	<i>Wrong definition</i>	0
1	<i>Vague definition</i> The idea that it is to do with public services.	1
2	<i>Precise definition</i> An explanation that it involves essential facilities and services such as roads, airports, sewage treatment, water systems, railways, telephone and other utilities.	2

(ii) investment (paragraph ❸). **[2 marks]**

level

0	<i>Wrong definition</i>	0
1	<i>Vague definition</i> The idea that it is spending by firms.	1
2	<i>Precise definition</i> An explanation that it is expenditure on capital equipment or that it is an injection into the economy or that it is an addition to the capital stock of the economy.	2

(b) Using information from paragraph ① and table 1, explain why there is evidence that the demand for oil was price inelastic in 2005. [4 marks]

level

- 0 *Inappropriate answer* **0**

- 1 *Identification of appropriate theory* **1-2**
For explaining that oil is an essential product and so one would expect the demand to be inelastic **or** for providing an explanation of how oil prices increased and the current account balance increased by a significant amount, indicating inelastic demand.

- 2 *Correct application of appropriate theory* **3-4**
For explaining that oil is an essential product and so one would expect the demand to be inelastic **and** for providing an explanation of how oil prices increased and the current account balance increased by a significant amount, indicating inelastic demand.

(c) Using an AD/AS diagram, explain the effect that the changing current account balance is likely to have on inflation. [4 marks]

level

- 0 *Inappropriate answer* **0**

- 1 *Identification of appropriate theory* **1-2**
For drawing a correctly labelled diagram, where the aggregate demand curve shifts to the right with the increase in $(X - M)$, thus raising the average price level **or** for providing an explanation of how the increase in AD will lead to an increase in the rate of inflation as demand in the economy increases.

- 2 *Correct application of appropriate theory* **3-4**
For drawing a correctly labelled diagram, where the aggregate demand curve shifts to the right with the increase in $(X - M)$, thus raising the average price level **and** for providing an explanation of how the increase in AD will lead to an increase in the rate of inflation as demand in the economy increases.

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

(d) **Using information from the text/data and your knowledge of economics, evaluate possible measures that the Nigerian government might employ to promote economic development.**

[8 marks]

Responses **may** include:

- a definition of economic development
- an explanation of measures that could increase economic growth, such as supply-side policies
- the use of oil wealth may be used for:
 - investment in education
 - investment in healthcare
 - investment in infrastructure
- policies to reduce corruption and ensure that public money is used for approved investment projects
- pro-poor growth strategies
- policies to attract FDI.

Candidates must explain **how** the measures that they have chosen will promote economic development in order to reach level 3.

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

If there is no direct reference to the data, then candidates may not be rewarded beyond level 2.

Effective evaluation may be to:

- consider short-term versus long-term consequences
- examine the impact on different stakeholders
- discuss advantages and disadvantages
- prioritize the arguments.

Level

0	No valid discussion.	0
1	Few relevant concepts recognized. Little discussion or only basic understanding.	1-2
2	Relevant concepts recognized and developed in reasonable depth. Some attempt at application and analysis.	3-5
3	Relevant concepts developed in reasonable depth, demonstrating effective evaluation, supported by appropriate evidence or theory.	6-8
