



# **MARKSCHEME**

**November 2009**

**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 indicated. Each question is worth [10 marks].*

**1. Explain how the measurement of economic growth differs from the measurement of economic development.**

Answers **may** include:

- a definition of economic growth
- a definition of economic development
- an explanation of the differences between economic growth and economic development
- measurement of economic growth in terms of real GDP or real GDP *per capita*
- references to the various methods of National Account measurement (output, income, expenditure)
- economic development refers to sustained improvement in living standards and requires specific indicators related to *per capita* income, education and health, environmental protection, *etc.*
- economic growth as a fundamental component of economic development
- reference to the HDI as a composite measure of economic development
- other composite measures.

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

**2. Using appropriate diagrams, explain why the relative burden (incidence) of an indirect tax on the producer and on the consumer varies, depending on the price elasticity of demand for the good (product).**

Answers **may** include:

- definition of an indirect tax
- distinction between a flat rate (specific) tax and an *ad valorem* tax
- a brief discussion of burden (incidence) of an indirect tax
- definition of price elasticity of demand
- diagrammatic illustration of the imposition of an indirect tax
- explanation with reference to the diagram(s) of how the incidence of a tax varies with the price elasticity of demand
- explanation that as the price elasticity of demand value decreases the burden on the consumer would increase.

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**3. Explain the nature of competition in a non-collusive oligopoly.**

Answers **may** include:

- definition of the market structure of an oligopoly
- characteristics of the market structure with the emphasis on interdependence
- distinction between collusive and non-collusive oligopolies
- diagrammatic representation of the kinked demand curve as a description of a non-collusive oligopoly
- explanation of the kinked demand curve (with reference to the diagram) as a justification for non-price competition
- examples of non-price competition:
  - product differentiation
  - increased inducements to consumers to purchase a largely unchanged product: gifts and coupons for example
  - advertising/marketing.

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**4. With reference to the concept of the multiplier, explain how the level of national income might be affected by a new government spending project worth \$100 million.**

Answers **may** include:

- an explanation of the multiplier
- an explanation of leakages and injections
- an explanation that the government spending project is an injection
- an explanation of how the value of the multiplier is dependent upon the size of the leakages
- an explanation that the leakages are the marginal propensities to save, tax and import
- a numerical example with assumed values for the leakages
- a conclusion that national income will increase more than \$100 million.

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**5. Using an appropriate diagram, explain how a government decision to decrease income tax rates could lead to a movement along the short-run Phillips curve.**

Answers **may** include:

- an explanation of the Phillips curve: a curve showing the relationship between inflation and unemployment
- a graphical representation of the short-run Phillips curve: negative/inverse relationship between inflation and unemployment
- explanation of the graph that there is a “trade-off” between inflation and unemployment
- explanation that a decrease in income tax rates may lead to a movement up the short-run Phillips curve (assuming inflation rate is on the vertical axis)
- further explanation that a decrease in income tax rates may lead to an increase in aggregate demand and an increase in total output, leading to lower unemployment but a higher inflation rate.

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**6. Explain the differences between free trade areas (FTAs), customs unions and common markets as types of international economic integration.**

Answers **may** include:

- definition of economic integration
- FTAs are where partners abolish tariffs on trade between the member countries but each partner determines its own tariff on trade with non-partner countries
- customs unions involve intra-union free trade but have a common external tariff on all trade with non-members
- common markets are customs unions with additional provisions to encourage trade and integration through, for example, the free mobility of factors of production
- the three types show increasing degrees of economic integration
- real world examples.

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