



ECONOMICS
STANDARD LEVEL
PAPER 2

Thursday 10 May 2001 (morning)

2 hours

INSTRUCTIONS TO CANDIDATES

- Do not open this examination paper until instructed to do so.
- Answer one question from Section A and one question from Section B.
- Use diagrams where appropriate.

SECTION A

Answer **one** question from this section.

Question 1

Read the following extract and answer the questions which follow.

Farmers to Plant Record Soybean Acres Despite Drop in Price

- (1) With prices of most crops depressed by a **big downturn in US farm exports**, growers are reducing their production of everything from corn to wheat. But farmers are switching to soybeans because a federal-government loan subsidy on this crop is far more attractive than anything Midwest farmers can get on their other commodities.
- (2) Unlike the European Union's Common Agricultural Policy which employs price support schemes, the US government has chosen various subsidies to support the nation's farmers. According to an Agricultural Department survey released last Wednesday, growers are planning to plant 1% more soybeans than last year, despite a 25% drop in price.
- (3) Three years after Congress began trying to reduce growers' dependence on subsidies, US taxpayers continue to pay billions of dollars to finance these schemes. In fact, Wednesday's report shows how government programs still heavily influence the most basic business decisions of farmers. The market's signals to farmers are still being distorted, according to Stewart Ramsey, an agriculture economist: "Farmers are planting more soybeans than we need."
- (4) Wednesday's planting survey indicates that many soybean growers plan to participate in the government loan program. As a result, some economists are projecting that federal loans on the 1999 soybean crop could cost the government roughly \$4 billion.

[Source: *Wall Street Journal Interactive Edition*, 1 April 1999]

- (a) (i) Define the term ‘subsidy’. *[2 marks]*
- (ii) Using appropriate demand and supply diagrams, briefly explain the difference between a subsidy and a price support scheme (paragraph 2). *[4 marks]*
- (b) Use a separate demand and supply diagram to explain the effects on price and output of each of the following:
- (i) the increased soybean planting (paragraph 2); *[4 marks]*
- (ii) the ‘big downturn of US farm exports’ (paragraph 1). *[4 marks]*
- (c) Using evidence from the passage, explain the decision by farmers to plant more soybeans despite collapsing prices. *[4 marks]*
- (d) “The market’s signals to farmers are still being distorted; farmers are planting more soybeans than we need.”
- Using the passage and your knowledge of economics, evaluate the effects of government intervention in agricultural markets. *[7 marks]*

Question 2

Study the items below and answer the questions which follow.

ITEM 1

CRISIS IN AFRICA

- (1) The World Bank and the International Monetary Fund have played a major role in Africa's development through their Structural Adjustment Programmes. The stated aim was to bring export-led recovery and a reduction in poverty.
- (2) However, Africa has suffered a worsening debt crisis, with looming bankruptcy. Increasingly the IMF has assumed responsibility for national budget policies, and has insisted on **strict deflationary targets**. At the same time, the World Bank has overseen moves towards **trade liberalisation** and deregulation of agricultural markets.
- (3) The IMF and the World Bank now have a chance to resolve the debt crisis which is destroying lives across sub-Saharan Africa and other developing regions. However, a new policy course will need to be charted in which reform of the heavily indebted poor countries is undertaken, along with an abandonment of the almost religious faith in the power of market forces to generate development and reduce poverty.

[Source: adapted from various newspaper articles]

ITEM 2

GUINEA BISSAU, SIERRA LEONE AND SINGAPORE

Selected indicators of development, 1995

	Guinea Bissau	Sierra Leone	Singapore
Debt service ratio (debt service as a % of exports of goods and services)	67	60	Not applicable
Adult literacy (%)	54.9	31.4	91.1
Real GDP per capita (\$)	811	625	22,604
% of labour force in agriculture	85	67	0
Terms of trade (1987 = 100)	89	92	89
Current account balance before official transfers (\$ millions)	- 41	89	15093

[Source: Human Development Report, 1998]

- (a) With reference to Item 1, briefly explain the following terms (in paragraph 2):
- (i) strict deflationary targets; *[2 marks]*
 - (ii) trade liberalisation. *[2 marks]*
- (b) With reference to Item 2,
- (i) briefly describe the debt situation of Guinea Bissau and Sierra Leone in 1995; *[2 marks]*
 - (ii) explain why their level of debt service ratio might hinder economic development. *[6 marks]*
- (c) The data provided indicates various economic problems faced by Guinea Bissau and Sierra Leone. Use your knowledge of economics to examine **two** of these problems (other than the debt service problem). *[6 marks]*
- (d) Evaluate the view that to solve the problems of less developed countries such as Guinea Bissau and Sierra Leone, it is necessary to abandon ‘the almost religious faith in the powers of market forces to generate development and reduce poverty’. *[7 marks]*

SECTION B

Answer **one** question from this section.

Question 3

- (a) Explain how, in a market economy, the price mechanism assists in the allocation of resources. *[15 marks]*

- (b) Critically evaluate how the price mechanism deals with the problem of non-renewable resources. *[10 marks]*

Question 4

- (a) With the help of examples, explain the purpose of the various supply-side policies. *[15 marks]*

- (b) Evaluate the success of these measures in countries where they have been implemented. *[10 marks]*

Question 5

Critically assess the arguments for and against the increased liberalisation of international trade. Refer in your answer to both less developed and more developed countries. *[25 marks]*

Question 6

- (a) Describe the main barriers to economic development. *[12 marks]*

 - (b) Is rapid population growth a cause or an effect of poverty? *[13 marks]*
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