



MARKSCHEME

May 2011

ECONOMICS

Standard Level

Paper 1

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

1. (a) Explain the roles of market forces and government in allocating resources in a mixed economy. [10 marks]

Answers **should** include:

- definitions of market forces, resources and mixed economy
- an explanation of the terms market forces, resource allocation and mixed economy
- an explanation of the role of price as a signal and as an incentive in the process of resource allocation
- use of supply and demand diagrams to illustrate resource allocation
- the role of the public sector
- the provision of public and merit goods by the government.

Answers **may** include:

- an explanation of the economic problem in terms of scarcity, choice and opportunity cost
- use of production possibility curve diagrams
- other aspects of the public sector, *e.g.* nationalized industries
- how taxation influences resource allocation, *e.g.* externalities
- consideration of the impact of government on the labour market, *e.g.* minimum wage.

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

Assessment Criteria

Part (a) 10 marks

Level		Marks
0	Completely inappropriate answer.	0
1	Little understanding of the specific demands of the question. Very little recognition of relevant economic theory. Relevant terms not defined. Significant errors.	1–3
2	Some understanding of the specific demands of the question. Some recognition of relevant economic theory. Some relevant terms defined. Some errors.	4–6
3	Understanding of the specific demands of the question. Relevant economic theory explained and developed. Relevant economic terms defined. Few errors. Where appropriate, diagrams included.	7–8
4	Clear understanding of the specific demands of the question. Relevant economic theory clearly explained and developed. Relevant economic terms clearly defined. No major errors. Where appropriate, diagrams included and explained. Where appropriate, examples used.	9–10

- (b) **Evaluate the extent to which market forces should be used to lessen the problem of environmental pollution.**

[15 marks]

Answers **may** include:

- a definition of environmental pollution as a negative externality of production or consumption
- examples of environmental pollution
- use of a MSC/MSB diagram to illustrate the problem of resource misallocation
- consideration of alternatives to market forces *e.g.* through the use of government legislation and regulations
- the advantages and disadvantages of government regulation
- consideration of government use of market intervention policies, such as taxation, subsidies and tradable permits
- the advantages and disadvantages of government use of market based policies
- international cooperation among governments
- consideration of complete reliance on market forces, *i.e.* no government intervention, relying on the signalling and incentive functions of price to solve the problem
- the advantages and disadvantages of complete reliance on market forces
- examples of different approaches.

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.

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

Assessment Criteria**Part (b) 15 marks**

Level		Marks
0	Completely inappropriate answer.	0
1	Little understanding of the specific demands of the question. Very little recognition of relevant economic theory. Relevant terms not defined. Significant errors.	1–5
2	Some understanding of the specific demands of the question. Some recognition of relevant economic theory. Some relevant terms defined. Some errors.	6–9
3	Understanding of the specific demands of the question. Relevant economic theory explained and developed. Relevant economic terms defined. Few errors. Where appropriate, diagrams included. An attempt at evaluation.	10–12
4	Clear understanding of the specific demands of the question. Relevant economic theory clearly explained and developed. Relevant economic terms clearly defined. No major errors. Where appropriate, diagrams included and explained. Where appropriate, examples used. Evidence of appropriate evaluation.	13–15

2. (a) **Using appropriate diagrams, explain how a reduction in income tax could affect both aggregate demand and aggregate supply in an economy.** *[10 marks]*

Answers **should** include:

- a definition of income tax
- a definition of aggregate demand
- a definition of aggregate supply
- an explanation of a reduction in income tax increasing disposable income, consumption and thus AD
- use of an AD/AS diagram showing shift of AD to the right
- an explanation of the possible linkage between a reduction in income tax, incentives to work and the level of output
- use of an AD/AS diagram showing shift of an AS curve to the right (upward sloping or vertical AS curve is acceptable).

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- (b) **“The lower the level of both direct and indirect taxation, the better.”**
Evaluate this view.

[15 marks]

Answers **may** include:

- a distinction between direct and indirect taxation
- lower taxation and greater use of market forces to allocate resources
- lower taxation and greater consumer choice
- lower indirect taxation and lower prices
- an explanation of what is meant by “better” in an economy
- supply-side arguments in relation to lower direct taxation (company and personal), incentives and LRAS
- relative international rates of taxation and investment by MNCs
- taxation as a means of raising revenue and financing government spending, *e.g.* on merit and public goods
- problem of budget deficits if taxes are low
- taxation as a means of discouraging consumption of demerit goods/dealing with the problem of negative externalities
- taxation as a means of influencing the distribution of income/consideration of progressive and regressive taxation
- taxation as a means of regulating AD, *e.g.* use of higher taxes to reduce AD and demand-pull inflation.

Examiners should be aware that the tax regimes of countries vary widely and that candidate responses might reflect this.

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.

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

Assessment Criteria

Part (b) 15 marks

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3. (a) **Using a diagram, explain the factors which might cause a depreciation of a country's exchange rate.**

[10 marks]

Answers **should** include:

- a definition of exchange rate
- a definition of depreciation of an exchange rate
- use of an exchange rate diagram showing depreciation either by supply shifting rightward and/or demand shifting leftward
- an explanation of the factors that may cause the above shifts of S and D and the resulting depreciation:
 - trade flows (balance of trade and balance on current account)
 - capital account movements
 - decreases in interest rates
 - explanation of impact of inflation.

Answers **may** include:

- explanation of impact of speculation
- explanation of impact of use of foreign currency reserves.

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- (b) **“A depreciation of a country’s exchange rate will always have a beneficial effect on the performance of its economy.” Evaluate this view.** *[15 marks]*

Answers **may** include:

- an explanation of impact of depreciation on export and import prices, the demand for exports and imports and thus AD
- an explanation of “the performance of its economy” in terms of growth, employment, inflation and the balance of payments
- an evaluation of impact on growth, *e.g.* positive impact, particularly if exports are significant
- an evaluation of impact on employment, *e.g.* jobs created in export industries and import-substitution industries
- an evaluation of impact on inflation, *e.g.* cost-push effect if a country imports raw materials. Demand-pull effect if it is an exporting country
- an evaluation of impact on the balance of payments
- an appreciation that the responsiveness of demand to a change in price is significant.

N.B. Examiners should be aware that consideration of the Marshall-Lerner condition and J-curve is not required as they are higher level extension topics but can still be rewarded.

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.

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Assessment Criteria

Part (b) 15 marks

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4. (a) **Explain the main features of market-led strategies used to achieve economic development in less-developed countries (LDCs).** *[10 marks]*

Answers **should** include:

- a definition of economic development
- a definition of less-developed countries (LDCs)
- an explanation of market-led strategies such as:
 - trade liberalization/low levels of protectionism
 - an emphasis on private enterprise rather than state intervention
 - a floating exchange rate
 - encouragement of FDI
 - privatization
 - use of supply-side policies
 - flexible labour markets.

Answers may include references to recent/current examples of market-led strategies.

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Assessment Criteria

Part (a) 10 marks

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- (b) **Evaluate the view that economic development in less-developed countries (LDCs) can best be achieved through market-led strategies rather than interventionist strategies.**

[15 marks]

Answers **may** include:

- an explanation of interventionist strategies, *e.g.* in terms of the state playing an active role in the management of the economy, economic planning, protectionism exchange controls, nationalization
- use of PPC diagrams to illustrate development
- the advantages of market-led strategies, *e.g.* in terms of more efficient resource allocation along the lines of comparative advantage, benefits of MNCs, benefits of free trade, flexible labour and capital markets, greater consumer choice, a reduction in government budget deficits
- the disadvantages of market-led strategies, *e.g.* in terms of market failure, increased likelihood of structural unemployment, problems of MNCs, problems of structural adjustment programmes, greater wealth and income inequality, problems of capital outflows, the greater vulnerability of countries to international economic crises
- the advantages of interventionist strategies, *e.g.* in terms of greater diversity of economic activity, supply-side improvements as a result of investment in health care and education and training, protectionism allowing industry a breathing space to grow, a more equal distribution of income and wealth, less inequality between rural and urban sectors, higher levels of employment
- the disadvantages of interventionist strategies, *e.g.* in terms of possible growth of the public sector and government spending, inability to benefit from the gains from free trade, inefficient resource allocation, growth of inefficient monopolies, drawbacks of planning
- after consideration of market-led and interventionist strategies, factors favourable to development regardless of strategy may be suggested, *e.g.* absence of corruption.

N.B. This question, as the markscheme indicates, is particularly broad, so a very wide range of answers is possible. Only some of the above points can be expected within the time allowed.

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.

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Assessment Criteria

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