

Markscheme

May 2016

Economics

Standard level

Paper 1

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Use the question-specific markscheme together with the markbands. Award up to the maximum marks as indicated.

Section A

Microeconomics

1. (a) Distinguish between the effect of an increase in income and an increase in the price of a good on the demand for the good. [10]

Answers may include:

- definition of demand
- diagrams to show a movement along a demand curve and a shift of the demand curve
- explanation that an increase in price of a product will cause a movement along the demand curve and a change in income will cause a shift to the left or right
- examples of goods and services affected by price and income changes.

N.B. Specific reference to normal and inferior goods is not necessary.

Assessment Criteria

Part (a) 10 marks

Level		Marks
0	The work does not reach a standard described by the descriptors below.	0
1	There is little understanding of the specific demands of the question. Relevant economic terms are not defined. There is very little knowledge of relevant economic theory. There are significant errors.	1–3
2	There is some understanding of the specific demands of the question. Some relevant economic terms are defined. There is some knowledge of relevant economic theory. There are some errors.	4–6
3	There is understanding of the specific demands of the question. Relevant economic terms are defined. Relevant economic theory is explained and applied. Where appropriate, diagrams are included and applied. Where appropriate, examples are used. There are few errors.	7–8
4	There is clear understanding of the specific demands of the question. Relevant economic terms are clearly defined. Relevant economic theory is clearly explained and applied. Where appropriate, diagrams are included and applied effectively. Where appropriate, examples are used effectively. There are no significant errors.	9–10

- (b) Discuss the significance of price elasticity of demand for firms that produce luxury cars and firms that produce less expensive cars.

[15]

Answers may include:

- definition of price elasticity of demand
- diagram to show the relationship between price and total revenue
- explanation that for a product with inelastic demand an increase in price will increase TR and that for a good with elastic demand an increase in price will cause a decrease in TR, reference to luxury cars and less expensive cars being elastic or inelastic
- example of luxury cars and less expensive cars
- synthesis or evaluation (discuss) of the significance of price elasticity of demand.

Discussion **may** include: an assessment of whether a firm can decrease price as costs are higher for luxury cars and whether the demand for luxury cars is actually price elastic or inelastic and the demand for less expensive cars is price inelastic or inelastic, also consideration of car branding and PED, availability of finance deals. In addition discussion can be an awareness that the value of PED is not absolute for either type of car.

N.B. It should be noted that definitions, theory, and examples that have already been given in part (a), and then referred to in part (b), should be rewarded.

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

Opinions or conclusions should be presented clearly and should be supported by appropriate examples.

Assessment Criteria

Part (b) 15 marks

Level	Marks
0 The work does not reach a standard described by the descriptors below.	0
1 There is little understanding of the specific demands of the question. Relevant economic terms are not defined. There is very little knowledge of relevant economic theory. There are significant errors.	1–5
2 There is some understanding of the specific demands of the question. Some relevant economic terms are defined. There is some knowledge of relevant economic theory. There are some errors.	6–9
3 There is understanding of the specific demands of the question. Relevant economic terms are defined. Relevant economic theory is explained and applied. Where appropriate, diagrams are included and applied. Where appropriate, examples are used. There is an attempt at synthesis or evaluation. There are few errors.	10–12
4 There is clear understanding of the specific demands of the question. Relevant economic terms are clearly defined. Relevant economic theory is clearly explained and applied. Where appropriate, diagrams are included and applied effectively. Where appropriate, examples are used effectively. There is evidence of appropriate synthesis or evaluation. There are no significant errors.	13–15

2. (a) Explain **one** supply factor and **one** demand factor that might lead to a rise in the price of rented housing. **[10]**

Answers may include:

- definitions of demand and supply
- diagram to show how changes in demand and/or supply lead to an increase in the price of rented housing
- explanation of how factors causing a rise in demand, such as population and income, and/or a fall in supply for rented housing, such as costs and a fall in the housing stock, cause a rise in the price of rented housing
- examples of where increasing demand and falling supply have increased the price of rented housing.

Award a maximum of level 2 if only one supply or one demand factor is given.

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- (b) Discuss the view that price controls imposed by governments on the market for rented housing should never be used.

[15]

Answers may include:

- definitions of price controls and maximum prices or price ceilings
- diagram to show the application of a maximum price on the market for rented housing
- explanation of how a maximum price (rent) can be applied to the market for rented housing
- examples of where maximum prices in the market for rented housing have been imposed
- synthesis and evaluation (discuss) of the impact of applying a maximum price in the market for rented housing.

Discussion **may** include: the problems of applying the price controls and the development of parallel markets, the negative impact on some consumers who suffer because of a shortage of housing supply and the long-term implications on the quality of housing and allocation of resources in housing, possible differences in effects in the short and long term.

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Award a maximum of level 2 if the answer is focused on minimum prices.

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

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Assessment Criteria

Part (b) 15 marks

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Section B

Macroeconomics

3. (a) Explain how an increase in interest rates might affect the level of aggregate demand in an economy. **[10]**

Answers may include:

- definitions of interest rate and aggregate demand
- diagram to show how an increase in interest rates reduces aggregate demand, real income and price level
- an explanation of how a rise in interest rates might lead to a fall in consumption and investment which leads to a fall in aggregate demand, a rise in the exchange rate which leads to a fall in exports and subsequently a fall in aggregate demand
- examples of where a rise in interest rates has led to a fall in aggregate demand.

Assessment Criteria

Part (a) 10 marks

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- (b) Evaluate the effectiveness of monetary policy when an economy is in deep recession.

[15]

Answers may include:

- definitions of monetary policy and recession
- diagram to show how a reduction in interest rates leads to a rise in aggregate demand causing real income to move towards full employment and dealing with the recession
- an explanation of how a reduction in interest rates using monetary policy leads to a rise in consumption and investment which increases aggregate demand and cause real income to rise towards full employment and dealing with the recession
- examples of where expansionary monetary policy has been used to deal with a recession
- synthesis and evaluation.

Evaluation **may** include: the problems of applying expansionary monetary policy because consumption and investment might not respond enough to deal with the problem of the recession. Expansionary monetary policy might have negative outcomes such as inflation. Expansionary monetary policy has a different effect on stakeholders where borrowers gain and savers lose. The effect of monetary policy changes over time with aggregate demand responding more in the long term.

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4. (a) Using the Keynesian AD/AS diagram, explain why an economy may be in equilibrium at any level of real output. **[10]**

Answers may include:

- definitions of macroeconomic equilibrium and real output
- diagram to show equilibrium at different levels of real output
- explanation of equilibrium at different levels of real output, eg at full employment and less than full employment
- examples of economies operating at different levels of real output and/or of economies at different times in their history.

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- (b) Evaluate the view that increased investment is the most important factor in achieving a faster rate of economic growth.

[15]

Answers may include:

- definitions of investment and economic growth
- diagrams to show economic growth such as the Keynesian AS or LRAS shifting to the right or the PPC shifting outward or AD shifting right
- explanation of different types of investment, such as in physical capital and human capital, and the linkage between increased investment and faster economic growth
- examples of countries with different levels of investment and how this has impacted on relative growth rates
- synthesis or evaluation of the role of investment in the growth process.

Evaluation **may** include: importance of other factors which may cause economic growth, importance of the type of investment, consideration of whether higher investment causes economic growth, or whether faster growth stimulates higher investment.

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