CAMBRIDGE INTERNATIONAL EXAMINATIONS

Cambridge International General Certificate of Secondary Education

MARK SCHEME for the March 2016 series

0455 ECONOMICS

0455/22 Paper 2 (Structured Questions), maximum raw mark 90

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CAMBRIDGE
International Examinations

1 **(a) Using information from the extract, identify two examples of the factor of production 'land'. [2]**

Rivers (1) soil (1).
Allow fertilisers (1) as these may be natural fertilisers.

(b) Explain the type of exchange rate system that is referred to in the extract. [2]

A floating exchange rate system (1) determined by market forces/demand and supply (1).

(c) Using information from the extract, calculate the rise in GDP per head in India from 2012 to 2013. [3]

Increase in income per head: US$50/3.45%/3.448%/3.5%. (3)
Correct working i.e.
2012 GDP per head = US$1450. (1)
2013 GDP per head = US$1500. (1)
Maximum of 2 marks without $ sign or %
Maximum of 2 marks for different denomination of 50 e.g. 50 billion.

(d) Explain two characteristics of the USA mentioned in the extract that suggest that it is a developed country. [4]

- A low proportion of the labour force employed in agriculture/primary sector. (1) Developed countries tend to have most of their workers employed in the tertiary sector/as economies develop workers move out of agriculture/ primary sector/means a high proportion are employed in secondary and tertiary sectors. (1)
- Long life expectancy. (1) People in developed countries usually enjoy good health care systems/good nutrition/high living standards. (1)

(e) Using information from the extract, analyse two reasons why the productivity of Indian agricultural workers is likely to increase in the future. [4]

- More educated (1) and as a result are likely to be more skilled (1).
- Working with more capital (1) this will enable agricultural workers to produce more/work more efficiently (1).
- Working with more fertile soil/government subsidising fertilisers/government providing subsidies (1) this will enable agricultural workers to produce more/work more efficiently (1).

(f) Discuss whether an increase in output always reduces average cost. [5]

Up to 3 marks for why it might:
May enable firms to enjoy economies of scale (1) examples (2).
Average fixed costs fall as output rises (1) fixed costs are spread over a larger output (1).
Accept but do not expect: Increasing returns (1).

Up to 3 marks for why it might not:
May experience diseconomies of scale (1) examples (2).
Accept but do not expect: Diminishing returns/less efficient combination of resources (1)
Diagram showing economies and/or diseconomies of scale (1).

(g) Explain the cause of the example of market failure referred to in the extract. [4]

Definition of market failure (1).
Failure to take into account the external costs (1) that is the gap between social and private costs (1).
Water pollution caused by the use of fertilisers (1) third parties will suffer (1) e.g. people or animals may become sick/damage to the environment (1).
Do not expect but reward link to government failure via the government promoting use of fertilisers/subsidising fertilisers (1).
Market forces not able to work properly due to high stockpile of wheat (1) long term imbalance between demand and supply (1).

(h) Discuss whether food subsidies reduce poverty. [6]

Up to 4 marks for why they might:
A subsidy reduces the cost of production (1) increases supply (1) lowers price (1) (increase in supply and lower price may be shown on a diagram) makes food more affordable for the poor (1) the poor spend a high proportion of their income on food (1).
Food subsidies could raise the incomes of farmers (1). In some countries many farmers have low incomes themselves (1) may increase employment (1).

Up to 4 marks for why it might not:
The subsidies may not be passed on to the consumers (1) one possible reason is corruption (1).
Food prices may still be too high for the poor to afford (1).
Farmers may produce more food but it may be of a lower quality (1) it may have a lower nutritional value (1).
There is an opportunity cost involved (1) government spending on e.g. education might reduce poverty more effectively (1). There may be over-production of food (1).
If one country subsidises food it could lead to unemployment in agricultural workers abroad (1) causing their incomes to fall. (1)
Food subsidies may not be sufficient to reduce poverty (1) as poverty has many causes e.g. lack of education (1)

2 (a) Define a 'stock exchange'. [2]

An organisation/market for the sale and purchase of shares (and securities/stocks) (2).
An organisation where shares are sold/buying and selling of shares (1).

(b) Explain why some firms have survival as a short-term goal. [4]

Some firms may be making a loss/be in financial difficulties (1) they may hope to continue to produce until demand increases/grow in the future (1) and so revenue rises (1) or costs of production fall (1) so profit is again earned (1) or recession ends (1) and economic growth occurs (1).

(c) Analyse how consumers may suffer as a result of a fall in the profits firms earn. [6]

Some firms may decide to stop production (1) this may reduce competition (1) raise price (1) lower quality (1) reduce choice (1).
Some firms may reduce output (1) may lower availability of products (1).
Firms will have less funds available to put back into the firm/invest (1) spend less on research and development (1) so the quality of the product may not improve (1).
Firms may try to cut costs of production (1) may use lower quality raw materials (1) reduce quality of product produced (1).

(d) Discuss whether a decrease in wage rates and an increase in working hours will always reduce the supply of workers to a firm. [8]

Up to 5 marks for why it might:
Wage rates are a key influence on the supply of workers (1) a decrease in wages would reduce the financial return from working (1) workers may decide to switch to another firm (1) or to another occupation (1).
Longer working hours would reduce leisure time (1) this may make the job less attractive (1).

Up to 5 marks for why it might not:
Wage rates and working hours may not be better elsewhere (1) there may be a lack of job vacancies (1) during an economic downturn/recession/period of high unemployment (1).
Earnings may still be high despite a fall in wage rates (1) if e.g. bonuses/overtime payments increase (1).
Workers take into account job satisfaction (1) may stay in the job if they enjoy it (1).
Workers may stay in the job if working conditions are good, there are long holidays, good promotion chances, good pensions and good fringe benefits (up to 2).

Note: maximum of 6 marks if reference only to decrease in wages or increase in working hours.

3 (a) Define a 'monopoly'. [2]

A market with one seller/single seller/supplier/producer (2).
A price maker/a firm with market power/dominant firm/large market share/has barriers to entry (and exit) (1).

(b) Explain how a falling death rate may affect demand in a country. [4]

A falling death rate may increase the size of the population (1) this will increase demand (1).
A falling death rate may increase the average age of the population (1) demand for e.g. health care is likely to increase (1).

(c) Analyse why price can be lower in a monopoly market than in perfect competition. [6]

It can be lower if the monopoly enjoys economies of scale/perfect competition unable to enjoy economies of scale (1) examples (2) if possible to enjoy economies of scale would lower average costs (1).
It can be lower if the monopoly is subsidised (1) e.g. state owned enterprises (1).
It can be lower if the monopoly avoids wasteful duplication/perfect competition may result in wasteful duplication (1) e.g. provision of water pipes (1).
It can be lower if a monopoly keeps price low as a barrier to entry (1) making it difficult for new firms with high average costs (1) to enter the market (1).
A monopoly is a price maker/can influence price (1) a perfectly competitive firm is a price taker/unable to influence price (1).
A state monopoly may not be trying to maximise profit (1) may be trying to promote economic welfare (1) keep prices low to make the product affordable (1)

(d) Discuss whether an increase in a country's population size will cause an increase in living standards. [8]

Up to 5 marks for why it might:
If there is an increase in the labour force (1) more output can be produced (1) increasing the goods and services available/raising incomes (1) will lower the dependency ratio (1).
Market size will increase (1) which may enable firms to take greater advantage of economies of scale (1).
The higher total demand (1) may attract multinational companies to set up in the country (1).
A larger population may lead to specialisation (1) in e.g. education and health care (1).
A fall in the death rate will increase life expectancy (1) a key influence on living standards (1).
Net immigration of workers (1) may bring in new skills (1).

Up to 5 marks for why it might not:
If the birth rate falls or the death rate declines (1) there may be an increase in the dependency ratio (1).
There may be a shortage of resources (1) may put pressure on e.g. health care/housing (1).
Population may increase more rapidly than output (1) lowering GDP per head (1).
There may be external costs caused (1) e.g. congestion/pollution (1).

Reward but do not expect reference to optimum population.

4 (a) Identify two costs of unemployment. [2]

1 mark for each of two relevant costs identified e.g.:
- loss of output
- loss of income/higher poverty/lower living standards
- loss of tax revenue
- higher cost of unemployment benefits
- social costs such as decline in health
- loss of skills of workers.

(b) Explain two advantages of a sole proprietor. **[4]**

Profit incentive/all profits go to the sole proprietor (1) do not have to share with partners and/or shareholders (1).
Flexible (1) as no one else to consult/quick to make decisions (1).
Provides personal services/has personal contact with consumers (1) can pick up changes in demand/target products (1).
Low start up costs/easy to set up (1) eases entry into the market/limited legal requirements (1).
Own boss (1) no-one to take orders from (1).

(c) Analyse how a reduction in government spending may affect unemployment. **[6]**

May increase unemployment as there may be less total (aggregate) demand (1) which may cause a recession (1) leading to cyclical unemployment (1).
Lower government spending on education (1) could reduce skills/qualifications (1) increase structural unemployment (1).
Lower government spending may reduce public sector jobs (1).
Lower government spending on unemployment benefits (1) may increase the incentive to work (1) reduce frictional unemployment (1).

(d) Discuss whether a cut in corporation tax will increase economic growth. **[8]**

Up to 5 marks for why it might:
It will increase firms' incentive to expand/invest (1) as they know they will be able to keep more of any profits earned (1).
It will increase firms' ability to expand/invest (1) as they will have more funds available to spend on capital goods (1).
If firms increase their output it will directly increase real GDP (1) it will also lead to higher employment (1) which will increase total demand (1) further increasing output (1).
Multinational firms may be attracted into the country by a low rate (1) they will contribute to the country's economic growth (1).

Up to 5 marks for why it might not:
Firms may be making a loss (1) and so will not benefit from the cut (1).
Firms may be pessimistic about the future (1) may not expect to make a profit in the future (1).
Higher profits may be distributed to shareholders (1) who may spend the extra income on imports (1).
Lower tax revenue (1) may lead to a cut in government spending (1).
Multinational companies may send most of their profits abroad (1) so government revenue may not increase significantly reducing funds available to promote growth (1).
Corporation tax may have been high to start with (1) may still act as a disincentive (1).

5 (a) What is the opportunity cost of a person going to university? **[2]**

Opportunity cost is the (next) best alternative foregone (1).
The cost may be working in a job/wages (1).

(b) Explain why there may be some people unemployed whilst there are job vacancies. [4]

The unemployed may not know about the job vacancies (1).
They may lack the skills/qualifications to do the jobs (1) occupationally immobile/example of occupational immobility (1).
The jobs may be in different parts of the country (1) the unemployed may be geographically immobile (1) due to e.g. differences in housing costs (1).
They may be waiting for better paid jobs (1).
They may not be willing to work despite being registered as unemployed (1).

(c) Analyse how an increase in investment may affect unemployment. [6]

It may increase unemployment if workers and capital goods are substitutes (1) machines will replace workers (1).
Investment is a component of total (aggregate) demand (1) higher investment increases total demand (AD) (1) higher AD can reduce cyclical unemployment (1).
It may reduce unemployment if workers and capital goods are complements (1) more workers will be taken on to work with the capital goods (1).
Investment can increase labour productivity (1) this can make labour more attractive (1) can make products more internationally competitive (1) raise total demand further (1) encouraging firms to expand further (1).

(d) Discuss whether supply-side policy measures will reduce inflation. [8]

Supply-side policy measures include government policy measures designed to increase total (aggregate) supply/quality of resources/quantity of resources (1). They include government spending on education and training, privatisation, regulation, cuts in direct taxes, cuts in unemployment benefits and trade union reforms (1).

Up to 5 marks for why they might:
Supply-side policy measures may reduce costs of production (1) e.g. cuts in corporation tax will lower costs (1).
They may increase labour productivity (1) e.g. education (1). Lower costs and higher productivity will increase aggregate supply/productive potential (1) higher aggregate supply/productive potential may reduce cost-push inflation (1) allow total demand to increase without causing inflation (1).

Up to 5 marks for why they might not:
Some policy measures e.g. education spending will increase total (aggregate) demand (1) this may rise by more than total supply (1) causing demand-pull inflation (1).
The policy measures may not work e.g. privatisation may lead to private sector monopolies developing (1) these may push up prices (1).
Spending on education may not improve labour productivity (1).
Some supply-side policy measures take time to work e.g. education spending (1) by that time inflation may not be a problem or people may have got so used to inflation they act in a way that causes further inflation (1).

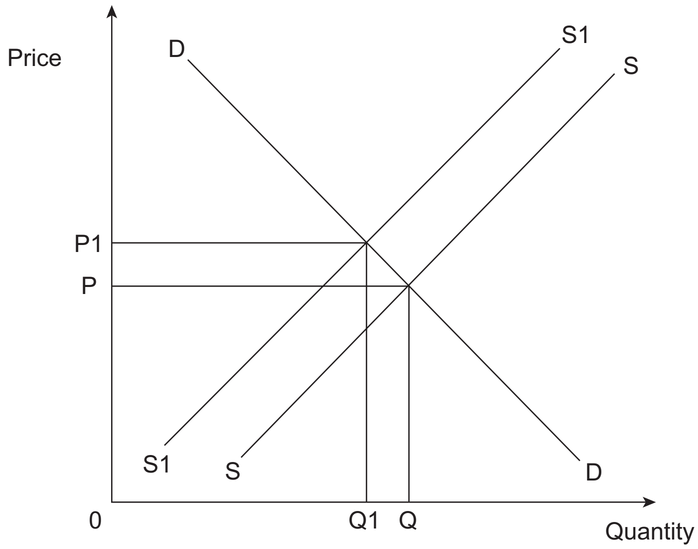
6 (a) Define an 'export quota'. [2]

A limit (1) on the quantity/value that can be exported/designed to keep products in the country/designed to keep domestic prices low (1).

(b) Explain the difference between inelastic supply and perfectly inelastic supply. **[4]**

Inelastic supply occurs when a change in price results in a smaller percentage change in supply (1) PES<1 (maybe illustrated) (1).
Perfectly inelastic supply occurs when a change in price has no effect on supply (1) PES = 0 / represented by a vertical supply curve (maybe illustrated) (1).

(c) Using a demand and supply diagram, analyse how an increase in the cost of producing smart phones will affect the market for smart phones. **[6]**



Up to 4 marks for the diagram:
- axes correctly labelled – price and quantity or P and Q (1).
- demand and supply curves correctly labelled (1)
- shift of the supply curve to the left (1)
- correct equilibriums identified either by lines drawn to both axes or equilibrium points clearly identified e.g. E and E1 (1)

Up to 2 marks for written comments:
- higher costs will discourage output/cause a decrease in supply (1)
- price will be expected to rise and quantity (traded) to fall (1)

(d) Discuss whether a country exporting its raw materials always benefits its economy. [8]

Up to 5 marks for why it might:
It will generate export revenue (1) this will appear in the trade in goods balance (1) which may improve the current account position (1).
Exporting will increase total demand (1) increasing incomes (1) leading to economic growth (1) causing a rise in employment (1).
Exporting will be more beneficial if the raw materials are highly priced (1) and in inelastic demand (1).

Up to 5 marks for why it might not:
Exporting can cause demand-pull inflation (1) as it will increase total demand (1) when an economy is operating close to full capacity (1).
Exporting raw materials enables foreign countries to compete with the country's finished products at home and abroad (1) reducing the country's finished exports (1) and increasing the country's imports of finished products (1).
Exporting raw materials may deplete raw materials (1) reducing the country's ability to produce and export in the future (1).

Up to 3 marks for possible effect on the exchange rate:
May lead to an appreciation in the exchange rate (1) may be in an advantage in that more imports can be purchased with the same volume of exports (1) may be a disadvantage as it may make domestic products less internationally competitive (1).

7 (a) How are earnings received by a country from foreign tourism recorded in the current account of its balance of payments. [2]

Positive inflow/credit item/export (1)
In trade in services / invisible balance section (1).

(b) Explain two factors that could cause an increase in foreign tourists to a country. [4]

An increase in incomes abroad (1) will increase foreigners' ability to afford holidays in the country (1).
A reduction in the country's exchange rate (1) making holidays in the country cheaper (1).
A rise in the price of holidays in other countries/lower price in domestic market (1) some people will switch to a substitute holiday/costs may be lower in the domestic market (1).
An improvement in tourist attractions in the country (1) e.g. better hotels (1)
Special events occurring in the country (1) e.g. the World Cup. (1)

(c) Analyse why workers with the same skills may be paid different wage rates. [6]

Some workers may have stronger bargaining power (1) because they are in trade unions/ in stronger trade unions (1).
Some workers may be more willing to accept lower paid jobs (1) because they e.g. regard job security to be more important (1).
The demand for workers may be different in different countries/areas/industries (1) the demand for labour may be different in the different industries/countries (1).
The supply of workers may be different in different countries/areas (1) the wage rate will tend to be higher where supply is lower (1).
Workers may be in the public or the private sector (1). In some countries, the public sector is better paid (1).
Workers may have more experience (1) may have more responsibility (1).
A group of workers may be discriminated (1) example of such a group (1).
Some workers may not be aware similarly skilled workers are being paid more (1) and so may remain in a lower paid job (1).
Overtime may be paid at a higher rate (1).

(d) Discuss how population problems in developing countries may differ from those in developed countries. [8]

Up to 5 marks for the possible problems of developing countries:
Some developing countries have a high population growth rate (1) this may put pressure on resources (1).
Some developing countries have a high birth rate (1) this increases the dependency ratio (1) and may reduce the size of the labour force (1) and may result in products/resources that might have been used to increase living standards/economic growth being used to e.g. feed the higher population (1).
Some developing countries have a high infant mortality rate (1) lower quality of life (1).
Some developing countries experience net emigration (1) may lose skilled workers (1).

Up to 5 marks for the possible problems of developed countries:
Some developed countries have a decreasing death rate/falling birth rate (1) and so an ageing population (1) increase dependency ratio (1) increase cost of pensions/health care (1).
Some developed countries experience net immigration (1) this may pressure on resources (1) may be a mismatch between skills of immigrants and job vacancies (1).

Problems may be less severe in developed countries (1) longer life expectancy/less risk of overpopulation (1).
Credit but do not expect relevant reference to the concept of optimum population.