



MARKSCHEME

May 2013

ECONOMICS

Higher Level

Paper 2

20 pages

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

SECTION A

1. (a) (i) Define the term *appreciation* indicated in bold in the text (paragraph ②). **[2 marks]**

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Vague definition.</i> The idea that the exchange rate rises.	1
2 <i>Accurate definition.</i> An explanation that it is an increase in the value (price) of a currency plus one of the following: <ul style="list-style-type: none"> • in terms of a foreign currency • in a floating exchange rate system. 	2

(ii) Define the term *exchange rate* indicated in bold in the text (paragraph ④). **[2 marks]**

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Vague definition.</i> The idea that it is the value (or the price) of a currency.	1
2 <i>Accurate definition.</i> An explanation that it is the value (price) of one currency expressed in terms of another.	2

- (b) Using a diagram, explain how the “increase in foreign investment in the Philippine stock market” has affected the value of the Philippine peso (*paragraph 2*). [4 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is a correct diagram or an accurate written response.</i> For drawing an accurate, labelled demand and supply diagram for the peso with the demand curve for the peso shifting to the right leading to a higher exchange rate or for an explanation that increased foreign investment means that there will have been an increase in demand for the peso and this has caused an increase in the value of the peso.	1–2
2 <i>There is a correct diagram and an accurate written response.</i> For drawing an accurate, labelled demand and supply diagram for the peso with the demand curve for the peso shifting to the right leading to a higher exchange rate and for an explanation that increased foreign investment means that there will have been an increase in demand for the peso and this has caused an increase in the value of the peso.	3–4

An alternative approach would be to illustrate a market for the US\$ against the peso, showing an increase in supply of the US\$, resulting in a fall in the value of the dollar against the peso. If drawn correctly and accompanied by a correct explanation that this means that there is an increase in the value of the peso, then this may be fully rewarded.

Candidates who incorrectly label diagrams can be rewarded with a maximum of [3 marks]. For an exchange rate diagram, the vertical axis may be exchange rate, price of peso in US\$, USD/peso, dollars per peso. The horizontal axis should be quantity, or quantity of pesos. A title is not necessary.

- (c) **Using an AD/AS diagram, explain how the Philippine peso remittances affect the national output of the Philippine economy.** **[4 marks]**

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is a correct diagram or an accurate written response.</i> For drawing an accurate, labelled AD/AS diagram showing an increase in AD/movement to the right of the AD curve or an explanation that the remittances sent to the Philippines have the effect of increasing consumption (or investment) leading to an increase in AD and therefore leading to an increase in national output.	1–2
2 <i>There is a correct diagram and an accurate written response.</i> For drawing an accurate, labelled AD/AS diagram showing an increase in AD/movement to the right of the AD curve and an explanation that the remittances sent to the Philippines have the effect of increasing consumption (or investment) leading to an increase in AD and therefore leading to an increase in national output.	3–4

An alternative approach would be to illustrate an increase in the long run aggregate supply with the explanation that remittances used to finance construction will increase capital in the economy and therefore lead to an increase in the LRAS. If this is correctly illustrated and explained, full marks may be awarded.

Given the information in the text, candidates may explain the effect of a **fall** in remittances on the national output. If correctly illustrated and explained, this approach may be fully rewarded.

Candidates who incorrectly label diagrams can be rewarded with a maximum of **[3 marks]**. For AD/AS, the vertical axis may be price level, average price level, or general price level. The horizontal axis may be real output, national output, real national output, national income (Y), or GDP. Any appropriate abbreviations such as APL, GPL, RNO, or RNY are allowable. A title is not necessary.

- (d) **Using information from the text/data and your knowledge of economics, discuss the likely impact of an appreciating currency on the performance of the Philippine economy.** **[8 marks]**

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

Do not award beyond Level 2 if the answer does not contain reference to the information provided.

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Few relevant concepts are recognized.</i> There is basic knowledge/understanding.	1–2
2 <i>Relevant concepts are recognized and developed in reasonable depth.</i> There is clear knowledge/understanding. There is some attempt at application/analysis.	3–5
3 <i>Relevant concepts are recognized and developed in reasonable depth.</i> There is clear knowledge/understanding. There is some effective application/analysis. There is synthesis/evaluation, supported by appropriate theory and evidence.	6–8

Command term

“Discuss” requires candidates to offer a considered and balanced review that includes a range of arguments, factors or hypotheses. Opinions or conclusions should be presented clearly and supported by appropriate evidence.

Responses **may** include

- identification of measures of performance, *ie* employment, stable prices, growth, current account balance
- appreciation results in a fall in the price of imported factors of production and will reduce inflationary pressure (increase SRAS)
- domestic producers will be forced to become more efficient as appreciation means that their products are less competitive in international markets and as imported goods become less expensive
- the effect of the appreciation on the current account and AD depends on the elasticities of demand for exports and imports, but the president is worried about the export sector (*paragraph 2*)
- domestic producers may have to lay off workers in order to cut costs, resulting in more unemployment
- The effect of the appreciation on the amount of remittances is unclear. It may reduce amount of remittances and thus slow down consumption and construction; or, as expected, Filipinos abroad may continue to absorb the losses themselves (*paragraph 4*).
- Some Filipinos working overseas may return to the Philippines if the value of their remittances is not worth them working away from home. This may result in increased unemployment in the Philippines and lower disposable incomes for those reliant on remittances (*paragraph 3*).

- Some high-skilled Filipinos may return the Philippines if the value of their remittance is not worth them working away from home. This will result in a more highly-skilled labour force in the Philippines, and a possible shift in the LRAS.

Any reasonable discussion that makes supported judgments/conclusions concerning the possible effects on Philippine economic performance.

2. (a) (i) **Define the term *preferential trade agreement* indicated in bold in the text (paragraph ①).** [2 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Vague definition.</i> The idea that it is an agreement that frees up trade.	1
2 <i>Accurate definition.</i> An explanation that it is a type of economic integration that removes (or reduces) trade barriers for certain products to countries that are in the agreement.	2

(ii) **State two examples of trade protection (paragraph ②).** [2 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is limited understanding.</i> Only one correct example is given.	1
2 <i>There is clear understanding.</i> Two correct examples are given, such as tariff, quota, subsidy, administrative barrier, environmental, health or safety regulations, government procurement policies, voluntary export restraints.	2

- (b) Using an appropriate diagram, explain the effect on Malaysian palm oil producers of the tariffs imposed by India (*paragraph 3*). [4 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is a correct diagram or an accurate written response.</i> For drawing an accurately labelled diagram of a tariff being imposed on Malaysian palm oil in the Indian palm oil market indicating a fall in the level of imports or for explaining that Indian tariffs on Malaysian palm oil will cause a reduction in the amount of exports that Malaysian palm oil producers will be able to sell to India.	1–2
2 <i>There is a correct diagram and an accurate written response.</i> For drawing an accurately labelled diagram of a tariff being imposed on Malaysian palm oil in the Indian palm oil market indicating a fall in the level of imports and for explaining that Indian tariffs on Malaysian palm oil will cause a reduction in the amount of exports that Malaysian palm oil producers will be able to sell to India.	3–4

Candidates who incorrectly label diagrams can be rewarded with a maximum of [3 marks]. The use of Price and Quantity for the axes is sufficient. The domestic supply curve should be labelled as “S domestic” or (S_D) and the Malaysian supply can be labelled “S Malaysia”, “ S_M ”, “S_{World}” or “ S_W ”.

- (c) Distinguish between a free trade area such as ASEAN, a customs union and a common market. [4 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>The written response is limited.</i> For an understanding that these are all types of economic integration (or trade bloc) but that there is a different level of integration in each type.	1–2
2 <i>The written response is accurate.</i> For explaining that the extent of integration increases, with reference to any two correct differences between the highest level of integration, common market, and the lowest level of integration, free trade area.	3–4

Key differences include:

- no common external tariff at lowest level
- common external tariff in customs union
- free movement of factors of production at highest level
- common policies on product regulation at highest level.

An alternative approach would be to define the three types of integration. If the definitions are correct, the answer may be fully rewarded as the distinctions between the levels will be implicit.

- (d) **Using information from the text/data and your knowledge of economics, evaluate the possible effects of this agreement on trade between India and Malaysia.** *[8 marks]*

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

Do not award beyond Level 2 if the answer does not contain reference to the information provided.

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Few relevant concepts are recognized.</i> There is basic knowledge/understanding.	1–2
2 <i>Relevant concepts are recognized and developed in reasonable depth.</i> There is clear knowledge/understanding. There is some attempt at application/analysis.	3–5
3 <i>Relevant concepts are recognized and developed in reasonable depth.</i> There is clear knowledge/understanding. There is some effective application/analysis. There is synthesis/evaluation, supported by appropriate theory and evidence.	6–8

Command term

“Evaluate” requires candidates to make an appraisal by weighing up the strengths and limitations.

Responses **may** include:

Strengths:

- trade creation (*paragraph 1*)
- greater choice and lower prices for consumers
- lower prices may reduce costs of production
- better use of comparative advantage
- increased output for Malaysia and India
- greater competition should lead to increased efficiency
- possibility of economies of scale
- increased investment linked to the agreement (*paragraph 2*) which may increase employment
- removal of technical barriers makes trade easier
- possible that tariffs will fall on Malaysia’s exports of electrical and electronic products, crude petroleum, palm oil and chemical goods, creating employment in these sectors (*paragraph 3*)
- the possibility for both countries to diversify exports as the agreement will be more extensive than the existing agreement with ASEAN (*paragraph 2*)
- less dependence on China and the US (*paragraph 1*).

Limitations:

- domestic producers may have to close down if they are not competitive
- dependency on trade within the area may be restrictive
- increased unemployment if firms that cannot compete are forced to reduce their size or close down
- possibility of trade diversion
- possible adverse effects on world trade of the appearance of regional trading blocs, compared with the multilateral agreements favoured by WTO
- structural unemployment that may result as production in the economy changes in response to freer trade
- may limit the ability of each country to support infant industries and gain comparative advantage in new areas.

Any reasonable evaluation of the relative strengths and limitations of the trade agreement.

SECTION B

3. (a) (i) **Define the term *micro-credit* indicated in bold in the text (paragraph 2).** [2 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Vague definition.</i> The idea that it is a small loan.	1
2 <i>Accurate definition.</i> An explanation that it is loan, plus one further descriptor, such as: <ul style="list-style-type: none">• micro-credit allows poor people to set up a small scale business• micro-credit is loaned to borrowers who do not have security/collateral• micro-credit contributes to the empowerment of women.	2

(ii) **Define the term *poverty trap* indicated in bold in the text (paragraph 2).** [2 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Vague definition.</i> The idea that people cannot escape from poverty.	1
2 <i>Accurate definition.</i> An explanation that it is any one of the following: <ul style="list-style-type: none">• any linked combination of factors which causes poverty to be self-perpetuating with low income as the cause• low incomes lead to low saving which leads to low investment which leads to low growth which leads to low income• low incomes leads to low levels of human capital that leads to low productivity that leads to low incomes.	2

(b) Using a diagram, explain how the use of micro-credit might affect the distribution of income in rural areas of China. [4 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is a correct diagram or an accurate written response.</i> For drawing an accurate, labelled Lorenz Curve diagram showing two Lorenz curves with an indication that there is a movement towards the line of perfect equality or for explaining that the use of micro-credit might increase the income of lower-income Chinese people, thus leading to a more equal (less unequal) distribution of income.	1–2
2 <i>There is a correct diagram and an accurate written response.</i> For drawing an accurate, labelled Lorenz Curve diagram showing two Lorenz curves with an indication that there is a movement towards the line of perfect and for explaining that the use of micro-credit might increase the income of lower-income Chinese people, thus leading to a more equal (less unequal) distribution of income.	3–4

The question does not identify a specific diagram. Alternative diagrams may be drawn and, as long as a plausible link to income distribution is explained, may be fully awarded.

Candidates who incorrectly label diagrams can be rewarded with a maximum of [3 marks]. The y-axis should be labelled “cumulative % of income” or “% of income” and x-axis should be “cumulative % of population” or “% of population”. The diagonal line should be “(line of) perfect equality” or “(line of) absolute equality”.

(c) Using a production possibility curve (PPC) diagram, explain how micro-credit schemes can affect the actual output and the production possibilities of an economy. [4 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is a correct diagram or an accurate written response.</i> For drawing an accurate, labelled PPC diagram showing an increase in production possibilities (outward shift of the PPC) or an increase in actual output (movement of a point towards the curve) or for an explanation that micro-credit may allow for an increase in the actual output of the economy or an increase in the quality and/or the quantity of the factors of production thus leading to an increase in the production possibilities (potential output) of an economy.	1–2
2 <i>There is a correct diagram and an accurate written response.</i> For drawing an accurate, labelled PPC diagram showing an increase in production possibilities (outward shift of the PPC) or an increase in actual output (movement of a point towards the curve) and an explanation that micro-credit may allow for an increase in the actual output of the economy or an increase in the quality and/or the quantity of the factors of production thus leading to an increase in the production possibilities (potential output) of an economy.	3–4

For full marks, candidates are not required to show **both** a movement towards the curve and a shift in the curve. One change, correctly explained is sufficient for full marks.

Candidates who incorrectly label diagrams can be rewarded with a maximum of [3 marks]. For a PPC, the axis could be two alternative products, one for each axis, eg Good A and Good B; or two groups of products, eg consumer goods and capital goods. A title is not necessary.

- (d) **Using information from the text/data and your knowledge of economics, evaluate the use of micro-credit in promoting economic development in economically less-developed countries.** **[8 marks]**

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

Do not award beyond Level 2 if the answer does not contain reference to the information provided.

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Few relevant concepts are recognized.</i> There is basic knowledge/understanding.	1–2
2 <i>Relevant concepts are recognized and developed in reasonable depth.</i> There is clear knowledge/understanding. There is some attempt at application/analysis.	3–5
3 <i>Relevant concepts are recognized and developed in reasonable depth.</i> There is clear knowledge/understanding. There is some effective application/analysis. There is synthesis/evaluation, supported by appropriate theory and evidence.	6–8

Command term

“Evaluate” requires candidates to make an appraisal by weighing up the strengths and limitations.

Responses **may** include:

- a definition of economic development.

Strengths of micro-credit:

- micro-credit provides a means of escaping the poverty trap (*paragraph 2*)
- micro-credit given to women allows them to improve their physical and social well-being, and gives them the opportunity to raise the standards of living for their children
- increased employment opportunities
- micro-credit gives access to people are unable to obtain loans from financial institutions as a result of having no security to offer
- micro-credit allows people to obtain a loan at a lower rate than if they borrowed from “loan sharks”
- micro-credit fosters self-reliance and the use of entrepreneurial skills through self-employment
- micro-credit is often accompanied by provision of basic skills that enable the borrowers to make better use of the loans
- micro-credit gives borrowers the opportunity to earn more income from their land (*paragraphs 5 and 6*)
- China’s state banks are now also trying to offer more access to micro-credit (*paragraph 5*).

Limitations:

- micro-credit may cause the government to feel that it no longer needs to invest in poverty-reducing programmes
- there may be insufficient regulation of the growing informal sector, resulting in new avenues for “loan sharks” to take advantage of impoverished borrowers.
- Many people who take micro-credit loans are not natural entrepreneurs and do not have appropriate business experience. This makes it quite possible that they will be unable to pay back the loans.
- businesses started with micro-credit loans are likely to remain small; while they might help individual borrowers out of poverty, this might not make a significant dent in overall poverty
- no guarantee that the use of micro-credit will lift citizens in rural China above the poverty line (*paragraph 4*)
- many remote areas remain inaccessible so it is unlikely that micro-credit will be able to be used (*paragraph 3*).

Any reasonable evaluation that assesses the relative strengths and limitations of micro-credit in contributing to economic development.

4. (a) (i) Define the term **infrastructure** indicated in bold in the text (paragraph 2). [2 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Vague definition.</i> The idea that it is (any one of the following): <ul style="list-style-type: none">• large scale public systems (services or facilities) of a country• necessary for economic activity• add to the capital stock of the economy• usually supplied by the government.	1
2 <i>Accurate definition.</i> An explanation that it is (any two of the following is sufficient): <ul style="list-style-type: none">• large scale public systems (services or facilities) of a country• necessary for economic activity• add to the capital stock of the economy• usually supplied by the government.	2

(ii) State *two* forms of development aid (paragraph 4). [2 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is limited understanding.</i> One correct example is given.	1
2 <i>There is clear understanding.</i> Two correct examples are given: <ul style="list-style-type: none">• grants• concessional long-term loans• project aid• programme aid• debt cancellation• technical assistance• humanitarian aid• multilateral aid• bilateral aid.	2

(b) Using an appropriate diagram, explain why hydropower dam projects on the Mekong River might lead to market failure. [4 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is a correct diagram or an accurate written response.</i> For drawing an accurate, labelled diagram showing a negative externality with MSC above MPC and overproduction taking place or for explaining that hydropower dam projects may be a market failure if they create external costs (or negative externalities) resulting in any one of the following: <ul style="list-style-type: none"> • a misallocation of resources • a situation where the market is operating at a level where $MSC > MSB$ • a situation where the market is operating at a level that is not socially efficient ($MSB = MSC$) • a situation where there is a welfare loss to society. 	1–2
2 <i>There is a correct diagram and an accurate written response.</i> For drawing an accurate, labelled diagram showing a negative externality with MSC above MPC and overproduction taking place and for explaining that hydropower dam projects may be a market failure if they create external costs (or negative externalities) resulting in any one of the following: <ul style="list-style-type: none"> • an misallocation of resources • a situation where the market is operating at a level where $MSC > MSB$ • a situation where the market is operating at a level that is not socially efficient ($MSB = MSC$) • a situation where there is a welfare loss to society. 	3–4

There must be two output levels shown for full marks, but there do not need to be two prices shown.

Candidates who incorrectly label diagrams can be rewarded with a maximum of [3 marks]. The vertical axis may be price, but could be costs or benefits. The horizontal axis is quantity.

(c) Explain why the Human Development Index (HDI) is considered a better measure of economic development than GNI. [4 marks]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>The written response is limited.</i> For an awareness that GNI is a measure of national income only and that HDI includes several indicators	1–2
2 <i>The written response is accurate.</i> For an explanation that economic development cannot be measured only by looking at a single indicator such as national income (or economic growth) and that the HDI is a more valid measure since it is a composite indicator that includes literacy, life expectancy and GNI per capita which are indicators for health, education and income, all of which are important for economic development.	3–4

(d) Using information from the text/data and your knowledge of economics, discuss the possible effects on the economic development of Cambodia of investment from China and the United States (US). [8 marks]

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

Do not award beyond Level 2 if the answer does not contain reference to the information provided.

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Few relevant concepts are recognized.</i> There is basic knowledge/understanding.	1–2
2 <i>Relevant concepts are recognized and developed in reasonable depth.</i> There is clear knowledge/understanding. There is some attempt at application/analysis.	3–5
3 <i>Relevant concepts are recognized and developed in reasonable depth.</i> There is clear knowledge/understanding. There is some effective application/analysis. There is synthesis/evaluation, supported by appropriate theory and evidence.	6–8

Command term

“Discuss” requires candidates to offer a considered and balanced review that includes a range of arguments, factors or hypotheses. Opinions or conclusions should be presented clearly and supported by appropriate evidence.

Responses **may** include:

- a definition of economic development
- a definition of investment
- a reference to the table noting that there has been economic development in Cambodia since 1990 but that Cambodia's level of development remains low.

Possible positive effects:

- fill the savings gap
- break the poverty cycle
- increased/improved infrastructure (*paragraph 2*) and the impact of infrastructure on economic development
- increased opportunities for employment, increasing income and raising standards of living
- improved technical and management skills and improved human capital (may be considered a positive externality of production)
- improvements in technology
- increase in tax revenue for the Cambodian government which may be used to achieve development objectives
- multiplier effect
- trust shown by US and China encourages investment from other countries
- exports which result from foreign investment may improve the trade balance and therefore the Cambodian current account
- increased economic growth may raise living standards and allow for greater access to health care and education
- The desire of the US to invest in Cambodia may be encouraging the US government to cooperate on debt negotiations. Debt relief will free up money for investment in environmental areas or education which are key for economic development (*paragraph 4*).

Possible negative effects:

- negative externalities – loss of water quality and a loss of biodiversity (*paragraph 2*)
- the motives for investment may not be consistent with Cambodia's best interests
- the infrastructure provided by Chinese and US investments may be tailored to their own needs rather than Cambodian needs
- the possibility of a loss of sovereignty for the Cambodian government to make decisions that are in the interests of the Cambodian people
- the benefits of foreign investment and economic growth may be distributed unequally amongst the Cambodian people, worsening income inequality
- capital intensive technology might not be appropriate, employing relatively few people and having little impact on domestic employment
- vulnerability if there is an outflow of foreign investment.

Any reasonable discussion of the ways that foreign investment might or might not contribute to economic development.