

Markscheme

November 2017

Economics

Standard level

Paper 2

22 pages

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

Section A

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

Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>Vague definition.</i>	1
	An explanation that it is any one of the following: <ul style="list-style-type: none"> • a form of economic integration / trade bloc / common market • a common currency • common central bank • common interest rates (monetary policy). 	
2	<i>Accurate definition.</i>	2
	An explanation that it is any two of the following: <ul style="list-style-type: none"> • a form of economic integration / trade bloc / common market • common market • a common currency • common central bank • common interest rates (monetary policy). 	

- (ii) State **two** functions of a country's central bank (paragraph ④). [2]

Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	For stating any one of the following responsibilities: <ul style="list-style-type: none"> • regulator of commercial banks • banker to the government • control of interest rates • control of money supply • implementing monetary policies • maintenance of price stability • control of exchange rate policy • holder of foreign exchange reserves • provider and printer of notes and coins • promoting full employment. 	1
2	For stating any two of the following responsibilities: <ul style="list-style-type: none"> • regulator of commercial banks • banker to the government • control of interest rates • control of money supply • implementing monetary policies • maintenance of price stability • control of exchange rate policy • holder of foreign exchange reserves • provider and printer of notes and coins • promoting full employment. 	2

- (b) Using an exchange rate diagram, explain how Denmark’s central bank is maintaining the fixed value of the Danish krone against the euro (paragraph ⑥).

[4]

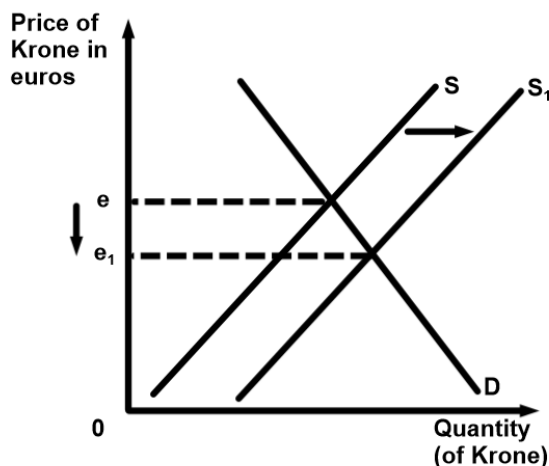
Level		Marks
0	The work does not meet a standard described by the descriptors below.	0
1	There is a correct diagram or an accurate written response.	1–2
	For drawing a correctly labelled exchange rate diagram with a shift of the supply curve of the Danish krone to the right and a fall in the exchange rate or for an explanation that the central bank is supplying Danish krone to buy euros, thus increasing the supply of the Danish krone on the foreign exchange market and bringing the value of the Danish krone back to the fixed rate.	
2	There is a correct diagram and an accurate written response.	3–4
	For drawing a correctly labelled exchange rate diagram with a shift of the supply curve of the Danish krone to the right and a fall in the exchange rate and for an explanation that the central bank is supplying Danish krone to buy euros, thus increasing the supply of the Danish krone on the foreign exchange market and bringing the value of the Danish krone back to the fixed rate.	

An alternative explanation would be that the central bank has been cutting interest rates (paragraph ⑥), which will encourage Danish people to save abroad, increasing the supply of the krone and bringing the value of the krone back to the fixed rate.

Another alternative approach would be to illustrate and explain how the demand for Danish krone has decreased because of the central bank cutting interest rates, reducing foreign saving in Danish banks, and bringing the krone back to the fixed rate.

Candidates who incorrectly label diagrams can be awarded a maximum of [3].

For an exchange rate diagram, the vertical axis may be exchange rate, price of Danish krone in euros, EUR/Danish krone or euros per Danish krone. The horizontal axis may be quantity or quantity of Danish krone.



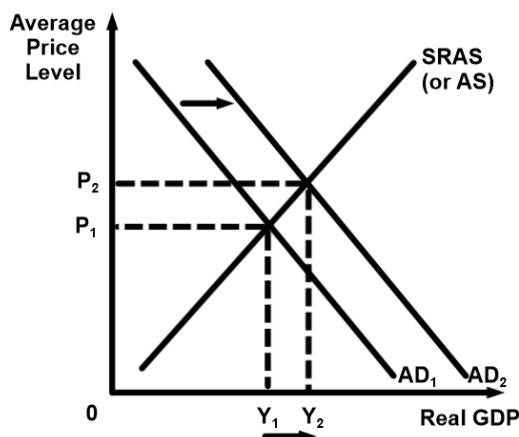
(c) Using an AD/AS diagram, explain how the interest rate cuts made by Denmark's central bank might affect the Danish economy (paragraph 6).

[4]

Level		Marks
0	The work does not meet a standard described by the descriptors below.	0
1	There is a correct diagram or an accurate written response.	1–2
	For drawing a correctly labelled AD/AS diagram showing an increase in AD with an increase in real GDP and an increase in the average price level or for one of the following explanations: <ul style="list-style-type: none"> • lower interest rates may lead to an increase in AD because of an increase in consumption (or investment) and that this would lead to an increase in real GDP and an increase in the average price level • lower interest rates may lead to an increase in AD because of a fall in the exchange rate and a rise in exports and that this would lead to an increase in real GDP and an increase in the average price level. 	
2	There is a correct diagram and an accurate written response.	3–4
	For drawing a correctly labelled AD/AS diagram showing an increase in AD with an increase in real GDP and an increase in the average price level and one of the following explanations: <ul style="list-style-type: none"> • lower interest rates may lead to an increase in AD because of an increase in consumption (or investment) and that this would lead to an increase in real GDP and an increase in the average price level • lower interest rates may lead to an increase in AD because of a fall in the exchange rate and a rise in exports and that this would lead to an increase in real GDP and an increase in the average price level. 	

Candidates who incorrectly label diagrams can be awarded a maximum of [3].

For AD/AS, the vertical axis may be price level, average price level or APL. The horizontal axis may be real output, national output, real GDP, national income, Y or GDP. A title is not necessary.



- (d) Using information from the text/data and your knowledge of economics, evaluate the decision to maintain the fixed value of the Danish krone against the euro.

[8]

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 meet a standard described by the descriptors below.</i>	0
1	<i>Few relevant concepts are recognized.</i>	1–2
	There is basic knowledge/understanding.	
2	<i>Relevant concepts are recognized and developed in reasonable depth.</i>	3–5
	There is clear knowledge/understanding. There is some attempt at application/analysis.	
3	<i>Relevant concepts are recognized and developed in reasonable depth.</i>	6–8
	There is clear knowledge/understanding. There is effective application/analysis. There is synthesis/evaluation, supported by appropriate theory and evidence.	

Command term

“Evaluate” requires candidates to make an appraisal by weighing up the strengths and limitations. Opinions and conclusions should be presented clearly and supported with appropriate evidence and sound argument.

Arguments for maintaining the fixed value **may** include:

- greater certainty
- businesses able to plan ahead with certainty about predicted costs of imported factors of production
- exporters benefit from the fixed (low) value of the Danish krone (paragraph ❶); letting it float would lead to a higher value (paragraph ❷) and would harm exporters by making their products less competitive. This may lead to unemployment since exports are very important to the Danish economy. It could be an “economic catastrophe”. (paragraph ❸)
- high level of confidence from outside investors and international credit rating agencies will make it easier to attract foreign investment (paragraph ❹)
- if the central bank continues to be able to defend the Danish krone, speculators may decide to stop buying it up, thereby stopping the upward pressure (paragraph ❺).
- according to the central bank, there will be no difficulty in maintaining the peg (paragraph ❻)
- belief that the ability to print krone will enable the government/central bank to continue to intervene to defend the peg (paragraph ❼).

Arguments against the fixed value **may** include:

- the arrangement might fail, and the central bank may have to break the peg, despite what it says (paragraph 7)
- the speculators may continue to buy up the Danish krone, assuming that at some point the central bank will be unable to maintain the peg (paragraph 5)
- if the central bank does keep printing money to maintain the peg (paragraph 7), it may lead to demand-pull inflation (monetarist explanation of inflation)
- the central bank may be sacrificing domestic monetary policy options to maintain the peg (paragraph 6)
- perhaps the peg no longer represents the best value for the Danish krone and that it is now under-valued against the euro
- other countries could argue that the value of the Danish krone is at an artificially low level, making their exports more competitive than they should be, and leading to retaliation
- accumulating foreign reserves is a waste of financial assets (paragraph 6).

Any reasonable evaluation.

2. (a) (i) Define the term *current account deficit* indicated in bold in the text (paragraph ❶).

[2]

Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>Vague definition.</i>	1
	The idea that it is when the flow of money from trade in goods and services is negative. OR The idea that imports exceed exports.	
2	<i>Accurate definition.</i>	2
	An explanation that it is when the net flow of money from trade in goods and services and income flows and/or transfers is negative. OR An explanation that the outflows of money from trade in goods and services, income flows and/or transfers are larger than the inflows of money.	

- (ii) List **two** functions of the World Trade Organization (paragraph ❷).

[2]

Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	One function is stated or two functions are partially stated (see Level 2 for functions).	1
2	A clear understanding demonstrated by listing two of the following functions of the WTO: <ul style="list-style-type: none"> • to set and enforce rules for international trade • to provide a forum for negotiating trade liberalization • to monitor further trade liberalization • to resolve trade disputes • to increase the transparency of decision-making processes • to cooperate with other major international economic institutions involved in global economic management • to help developing countries benefit fully from the global trading system. 	2

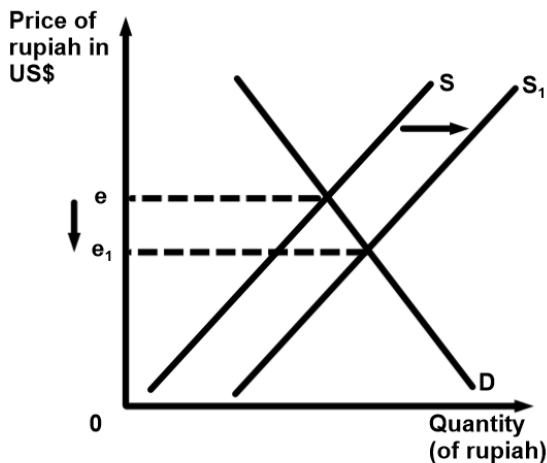
- (b) Using an exchange rate diagram, explain how Indonesia's current account deficit has weakened the rupiah against the US dollar (paragraph 1).

[4]

Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>There is a correct diagram or an accurate written response.</i>	1–2
	For drawing a correctly labelled exchange rate diagram with a shift of the supply curve to the right and a fall in the value of the Indonesian rupiah against the US dollar or for an explanation that a current account deficit involves an increase in the supply of the currency to buy the excess imports and thus causes the currency to fall in value.	
2	<i>There is a correct diagram and an accurate written response.</i>	3–4
	For drawing a correctly labelled exchange rate diagram with a shift of the supply curve to the right and a fall in the value of the Indonesian rupiah against the US dollar and for an explanation that a current account deficit involves an increase in the supply of the currency to buy the excess imports and thus causes the currency to fall in value.	

Candidates who incorrectly label diagrams can be awarded a maximum of [3].

For an exchange rate diagram, the vertical axis may be exchange rate, price of Indonesian rupiah in US\$, US\$ / Indonesian rupiah or US dollars per Indonesian rupiah. The horizontal axis may be quantity or quantity of Indonesian rupiah. A title is not necessary.



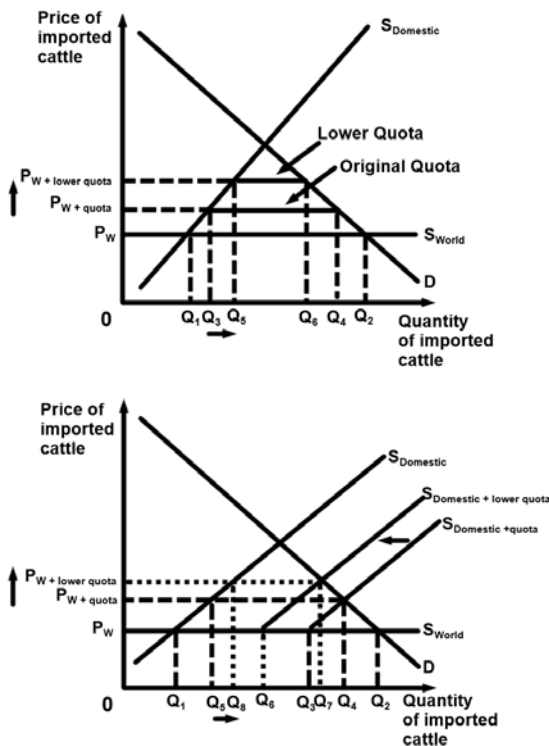
(c) Using an international trade diagram, explain how reducing the quota for cattle imports will affect the price and domestic production of cattle (paragraph ②).

[4]

Level		Marks
0	The work does not meet a standard described by the descriptors below.	0
1	There is a correct diagram or an accurate written response.	1–2
	For drawing a correctly labelled trade diagram, with a decrease in the quota, a fall in the level of imports and an increase in the price (with an increase in the quantity supplied by domestic producers) and an increase in domestic production or for an explanation that a decrease in the quota will result in a fall in the imports of cattle, and thus an increase in the price and an increase in the quantity of cattle that the domestic cattle producers are willing and able to supply.	
2	There is a correct diagram and an accurate written response.	3–4
	For drawing a correctly labelled trade diagram, with a decrease in the quota, a fall in the level of imports and an increase in the price (with an increase in the quantity supplied by domestic producers) and an increase in domestic production and for an explanation that a decrease in the quota will result in a fall in the imports of cattle, and thus an increase in the price and an increase in the quantity of cattle that the domestic cattle producers are willing and able to supply.	

Candidates who incorrectly label diagrams can be awarded a maximum of [3].

The use of P and Q on the axes is sufficient for an international trade diagram. A title is not necessary.



- (d) Using information from the text/data and your knowledge of economics, evaluate the use of trade protection in Indonesia.

[8]

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 meet 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 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. Opinions and conclusions should be presented clearly and supported with appropriate evidence and sound argument.

Responses may include:

- an explanation of trade protection (tariffs, quotas and other non-tariff barriers to support domestic producers)
- reference to diagram in part (c).

Justification for trade protection:

- may reverse the effects of the slowdown in economic growth (paragraph ❶) by reducing demand for imports (net export component of AD will increase)
- reduced imports will reduce the current account deficit (paragraph ❶) and prevent the Indonesian rupiah from falling further
- may act as a way to practice import substitution and diversify its economy away from the dependence on commodity exports (paragraph ❶)
- trade protection will prevent imports of “low-quality imported goods” but not imports of raw materials, so that domestic manufacturers who use imported raw materials will not be damaged and may become more competitive (paragraph ❸)
- level playing field argument – Indonesia’s average tariff in the past was well below others. “Indonesia had been too open to imports of consumer goods in the past” and it is simply a correction (paragraph ❹).

Arguments against trade protection:

- higher prices hurting consumers (paragraph ⑥)
- welfare loss, loss of efficiency (paragraph ⑥)
- may invite retaliation from trading partners, such as China
- may be seen as hypocritical that Indonesia is seeking freer trade (eg with the UK) while also increasing trade protection (paragraph ⑤)
- may be difficult to attract foreign direct investment (paragraph ⑤) if the government is pursuing interventionist policies such as higher levels of protection (paragraph ②)
- allows Indonesian firms to remain uncompetitive (paragraphs ① and ⑥)
- will not solve the underlying problem of “crumbling infrastructure and excessive regulations” and possibly delay necessary structural reforms (paragraph ⑥).

Any reasonable evaluation.

Section B

3. (a) (i) Define the term *investment* indicated in bold in the text (paragraph ❸). [2]

Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>Vague definition.</i> The idea that it is buying machinery.	1
2	<i>Accurate definition.</i> An explanation that it is any addition to the capital stock of the economy or that it is expenditure/spending by firms on capital.	2

- (ii) Define the term *multinational corporations (MNCs)* indicated in bold in the text (paragraph ❹). [2]

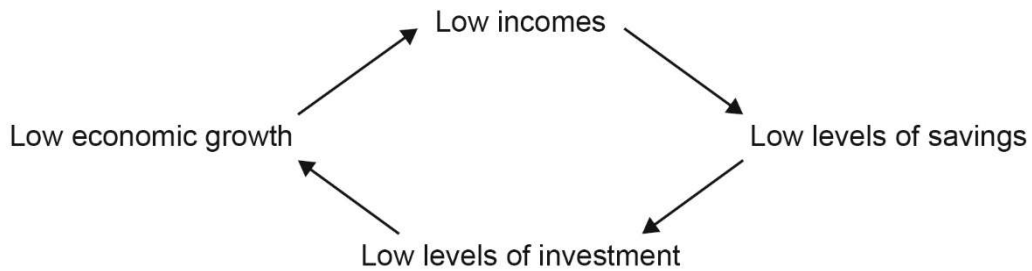
Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>Vague definition.</i> The idea that it is a company that invests in other countries.	1
2	<i>Accurate definition.</i> For an explanation that it is a company that has productive units in more than one country or that it is a company that carries out foreign direct investment in another country.	2

(b) Using a poverty cycle diagram, explain how investment from abroad might “break the poverty cycle” (paragraph 4).

[4]

Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>There is a correct diagram or an accurate written response.</i>	1–2
	For drawing a poverty cycle, including investment, that starts and ends in an indicator of poverty or for an explanation that investment from abroad will reduce the investment gap (paragraph 3) and break the poverty cycle.	
2	<i>There is a correct diagram and an accurate written response.</i>	3–4
	For drawing a poverty cycle, including investment, that starts and ends in an indicator of poverty and an explanation that investment from abroad will reduce the investment gap (paragraph 3) and break the poverty cycle.	

Example of poverty cycle (any cycle, including investment and starting and ending with an indicator of poverty, is acceptable):



- (c) Using data from **Figure 1**, explain why there is a difference between Ethiopia’s HDI world ranking and its GNI per capita world ranking.

[4]

Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>The written response is limited.</i>	1–2
	For explaining that the HDI is a composite index and that GNI per capita is one of the components or for an explanation that the lower ranking for GNI per capita (201) must mean that one or more of the other components (life expectancy, mean years of schooling, or expected years of schooling) must be relatively stronger than other countries to account for the higher HDI ranking (173).	
2	<i>The written response is accurate.</i>	3–4
	For explaining that the HDI is a composite index and that GNI per capita is one of the components and for an explanation that the lower ranking for GNI per capita (201) must mean that one or more of the other components (life expectancy, mean years of schooling, or expected years of schooling) must be relatively stronger than other countries to account for the higher HDI ranking (173).	

- (d) Using information from the text/data and your knowledge of economics, evaluate the possible impact on the Ethiopian economy of the foreign direct investment from China.

[8]

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 meet a standard described by the descriptors below.</i>	0
1	<i>Few relevant concepts are recognized.</i>	1–2
	There is basic knowledge/understanding.	
2	<i>Relevant concepts are recognized and developed in reasonable depth.</i>	3–5
	There is clear knowledge/understanding. There is some attempt at application/analysis.	
3	<i>Relevant concepts are recognized and developed in reasonable depth.</i>	6–8
	There is clear knowledge/understanding. There is effective application/analysis. There is synthesis/evaluation, supported by appropriate theory and evidence.	

Command term

“Evaluate” requires candidates to make an appraisal by weighing up the strengths and limitations. Opinions and conclusions should be presented clearly and supported with appropriate evidence and sound argument.

Responses **may** include:

- definition of foreign direct investment.

Strengths:

- fills the savings/investment gap (paragraph ③), which should lead to economic growth
- provides employment in the economy (paragraph ⑥), leading to higher levels of consumption, raising living standards
- should improve the infrastructure in the economy (paragraph ⑤), resulting in an increase in LRAS
- should improve R&D, providing access to technology (paragraph ⑤), resulting in an increase in LRAS
- should improve electricity provision (paragraphs ③ and ⑤), resulting in an increase in LRAS, and improvement of living standards of households
- provides education and training (positive externality of consumption), resulting in an increase in LRAS
- direct effect of the investment on AD
- can reduce the dependence on agriculture (paragraph ②), increasing diversification (paragraph ③)
- provision of tax revenue for the government which may be used to finance development objectives
- industrial zone should lead to higher value-added economic activity (paragraph ⑥).

Limitations:

- worries about the trade imbalance (paragraph ⑦)
- over-use of resources (paragraph ⑦) may lead to negative externalities of production
- capital-intensive production methods may not provide much employment, but this is not the case in shoes (paragraph ⑥)
- local producers may be negatively affected
- jobs may be filled by Chinese people
- MNCs may be politically powerful and able to negotiate tax breaks, contributing lower income to the government
- dependence upon MNCs/FDI causes vulnerability if these firms/countries change policy.

Any reasonable evaluation.

4. (a) (i) List **two** components of the Human Development Index (HDI) (paragraph ②). [2]

Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	One component is stated.	1
	Any one of the following measures: <ul style="list-style-type: none"> • life expectancy (at birth) • mean years of schooling (for those aged 25 years and above) • expected years of schooling (for a child of school entrance age, capped at 18 years of age) • GNI per capita or GDP per capita. 	
2	Two components are stated.	2
	Any two of the following measures: <ul style="list-style-type: none"> • life expectancy (at birth) • mean years of schooling (for those aged 25 years and above) • expected years of schooling (for a child of school entrance age, capped at 18 years of age) • GNI per capita or GDP per capita. 	

(ii) Define the term *economic growth* indicated in bold in the text (paragraph ③). [2]

Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>Vague definition.</i>	1
	The idea that it is a growing economy or an increase in GDP.	
2	<i>Accurate definition.</i>	2
	An explanation that it is one of the following: <ul style="list-style-type: none"> • an increase in the real value of output (over time) • an increase in real GDP • an increase in potential output / productive capacity. 	

N.B. The term “over time” is not necessary for [2].

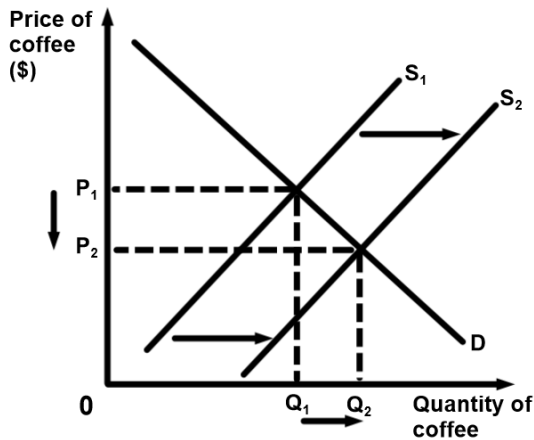
- (b) Using a demand and supply diagram, explain how the market for coffee in Papua New Guinea could be affected by improved irrigation (paragraph 9).

[4]

Level		Marks
0	The work does not meet a standard described by the descriptors below.	0
1	There is a correct diagram or an accurate written response.	1–2
	For drawing a correctly labelled demand and supply diagram showing an increase in supply (a shift of the curve to the right) a fall in price and an increase in quantity or for an explanation that improved irrigation increases the supply of coffee, lowering the price and increasing the quantity.	
2	There is a correct diagram and an accurate written response.	3–4
	For drawing a correctly labelled demand and supply diagram showing an increase in supply (a shift of the curve to the right) a fall in price and an increase in quantity and for an explanation that improved irrigation increases the supply of coffee, lowering the price and increasing the quantity.	

Candidates who incorrectly label diagrams can be awarded a maximum of [3].

The use of P and Q on the axes is sufficient for a demand and supply diagram. A title is not necessary.



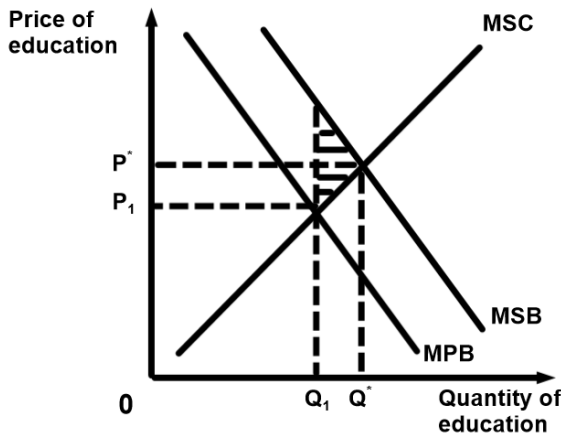
(c) Using an externalities diagram, explain why the introduction of free education for girls corrects a market failure (paragraph 1).

[4]

Level		Marks
0	The work does not meet a standard described by the descriptors below.	0
1	There is a correct diagram or an accurate written response.	1–2
	For drawing a correctly labelled externalities diagram showing an MSB curve to the right of the MPB curve and indicating under-provision of education and/or welfare loss (potential welfare gain) or for an explanation that education for girls will be under-provided in a free market and that the provision of free education will correct this, either by shifting the MSC curve to the right or by shifting the MPB (demand) curve to the right.	
2	There is a correct diagram and an accurate written response.	3–4
	For drawing a correctly labelled externalities diagram showing an MSB curve to the right of the MPB curve and indicating under-provision of education and/or welfare loss (potential welfare gain) and for an explanation that education for girls will be under-provided in a free market and that the provision of free education will correct this, either by shifting the MSC curve to the right or by shifting the MPB (demand) curve to the right.	

Candidates who incorrectly label diagrams can be awarded a maximum of [3].

The vertical axis may be price, but could be costs or benefits. The horizontal axis is quantity. A title is not necessary.



- (d) Using information from the text/data and your knowledge of economics, evaluate the role of foreign aid in contributing to economic development in Papua New Guinea.

[8]

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 meet 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 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. Opinions and conclusions should be presented clearly and supported with appropriate evidence and sound argument.

Responses may include:

- definition of economic development
- identification of types of aid *eg* bilateral, tied, grant aid, soft loans, emergency relief, emergency financial relief, NGO aid.

Possible positive outcomes:

- assistance for women and children crime victims (paragraph ❶)
- immunizations for young children to protect them from diseases, increasing the quality/quantity of future labour (paragraph ❶)
- provision of free education for girls, pre-school and early learning (paragraph ❶)
- training for the next generation of PNG police officers improves security and may attract FDI (paragraph ❶)
- benefits of aid which is targeted to improve elements of the HDI (paragraph ❷)
- aid can contribute to economic growth (paragraph ❸) which might then be used to achieve development objectives.

Possible negative outcomes:

- “a lot of aid money being spent but it is making very little difference” (paragraph ①)
- problems associated with corruption leads to poor functioning of institutions (police, justice, health, education, governance) hindering the effectiveness of the aid (paragraph ③)
- problems associated with aid dependency leads to long-term risk when foreign aid falls (paragraph ④)
- NGO aid may allow the government to ignore its development responsibilities (paragraph ④)
- problems associated with lack of effectiveness in improving life expectancy (paragraph ②).

N.B. To reach level 3, candidates must direct their responses to the issue of promoting economic development, rather than write in general terms about aid.

Any reasonable evaluation.
