

Markscheme

May 2021

Economics

Standard level

Paper 1

11 pages

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Section A

Microeconomics

1. (a) Explain how the price mechanism reallocates resources when there is a decrease in the supply of a good.

[10]

Answers may include:

- definitions of price mechanism, resources, supply
- diagram to show how a decrease in supply leads to a reallocation of resources
- explanation of how a decrease in supply shifts the supply curve left, creates excess demand at the original price, incentivizes producers to increase price, provides signals and incentives to consumers to change their consumption patterns, switches demand to less expensive goods and causes a reallocation of resources
- examples of goods where a decrease in supply has affected the allocation of resources.

Assessment Criteria

Part (a) 10 marks

Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>There is little understanding of the specific demands of the question.</i>	1–3
	Relevant economic terms are not defined. There is very little knowledge of relevant economic theory. There are significant errors.	
2	<i>There is some understanding of the specific demands of the question.</i>	4–6
	Some relevant economic terms are defined. There is some knowledge of relevant economic theory. There are some errors.	
3	<i>There is understanding of the specific demands of the question.</i>	7–8
	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.	
4	<i>There is clear understanding of the specific demands of the question.</i>	9–10
	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.	

- (b) Evaluate the view that the threat to sustainability, caused by economic activity requiring the use of fossil fuels, is best addressed through the use of carbon taxes.

[15]

Answers may include:

- definitions of sustainability, carbon taxes
- diagram to illustrate the use of carbon taxes, showing a shift of the supply curve to the left, reflecting the value of the negative externality (or any other relevant diagram)
- explanation that the use of fossil fuels generates negative externalities in production and/or consumption and therefore poses a threat to sustainability, and that this can be addressed through carbon taxes, which make the polluter pay
- examples of the use of carbon taxes and fossil fuels
- synthesis or evaluation.

Evaluation may include: possible advantages and disadvantages of the use of carbon taxes, consideration of other available policy options such as cap and trade schemes and funding for clean technologies, assessment of “best”.

A maximum of [12] should be awarded if there is not at least some reference to other policies.

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	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>There is little understanding of the specific demands of the question.</i>	1–5
	Relevant economic terms are not defined. There is very little knowledge of relevant economic theory. There are significant errors.	
2	<i>There is some understanding of the specific demands of the question.</i>	6–9
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3	<i>There is understanding of the specific demands of the question.</i>	10–12
	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.	
4	<i>There is clear understanding of the specific demands of the question.</i>	13–15
	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.	

2. (a) Explain **two** reasons why a government might impose indirect taxes. **[10]**

Answers may include:

- definition of indirect taxes
- diagram to illustrate the imposition of an indirect tax, with the supply curve shifting left, price increasing and quantity demanded decreasing
- explanation that indirect taxes may be imposed to raise tax revenue, to discourage the consumption of demerit goods, to correct negative externalities in production, trade protection, to redistribute income, eg excise taxes on luxury goods
- examples of goods on which indirect taxes are imposed.

A maximum of [6] should be awarded if only one reason is explained.

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- (b) Discuss the view that price floors are more effective than subsidies in providing assistance to producers in the agricultural sector.

[15]

Answers may include:

- definitions of price floors, subsidies
- diagrams to illustrate the use of a price floor and a subsidy
- explanation of how price floors and subsidies can both provide assistance to producers in the agricultural sector
- examples of the use of price floors and/or subsidies in practice
- synthesis or evaluation (discuss).

Discussion may include: the possible consequences of price floors, eg surpluses, inefficient allocation of resources and welfare impacts; the possible consequences of subsidies, eg on consumers, producers or the government; consideration of “more effective”.

A maximum of [12] should be awarded if there is evaluation but no consideration of “more effective”.

Assessment Criteria

Part (b) 15 marks

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Section B

Macroeconomics

3. (a) Explain how the size of the circular flow of income in an economy is likely to be affected by a decrease in the rate of interest.

[10]

Answers may include:

- definitions of circular flow of income, rate of interest
- diagram of the circular flow of income, showing a decrease in saving and an increase in investment or use of an AD/AS diagram to explain the impact of the decrease in the rate of interest on the circular flow of income
- explanation that a decrease in the rate of interest is likely to reduce saving, and increase business investment; hence a decrease in a leakage and an increase in an injection will exert an upward impact on income and output and increase the size of the circular flow of income
- examples of changes in the rate of interest affecting the circular flow of income in practice, such as the reduction of interest rates to near 0% in many countries at present.

Assessment Criteria

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- (b) Evaluate the effectiveness of fiscal policy as a means of achieving long-term economic growth.

[15]

Answers may include:

- definitions of long-term economic growth, fiscal policy
- diagram to show LRAS and/or the production possibility curve shifting to the right/outwards
- explanation of how fiscal policy can promote long-term economic growth through government spending on infrastructure, technology, R&D and human capital, tax reductions/incentives for firms to invest
- examples of the use of fiscal policy to promote long-term economic growth
- synthesis or evaluation.

Evaluation may include: the various advantages and disadvantages of fiscal policy, including both the demand- and supply-side effects on the economy, consideration of alternative (supply-side and monetary) policies.

Assessment Criteria

Part (b) 15 marks

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4. (a) Explain how aggregate demand is likely to be affected by an increase in the wealth of consumers and an increase in business confidence.

[10]

Answers may include:

- definitions of aggregate demand, wealth, business confidence
- diagram to show the AD curve shifting to the right
- explanation that an increase in the wealth of consumers may have a positive wealth effect whereby consumption increases as consumers feel richer and are more willing to spend, or can borrow more on the basis of their greater wealth; that an increase in business confidence in relation to being more optimistic about future sales and profits is likely to increase investment; and that the increase in C and I will increase AD
- examples of an increase in consumers' wealth and/or business confidence increasing AD in practice.

Award a maximum of [6] if only wealth or only business confidence is addressed.

Assessment Criteria

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- (b) Evaluate the effectiveness of monetary policy in reducing an economy's rate of unemployment.

[15]

Answers may include:

- definitions of monetary policy, rate of unemployment
- diagram to show AD shifting to the right as a result of expansionary monetary policy
- explanation of how expansionary monetary policy may help to reduce cyclical (demand-deficient) unemployment in terms of the mechanisms by which lower interest rates increase AD via the effect on consumption, investment and/or net exports
- examples of expansionary monetary policy being used in practice
- synthesis or evaluation.

Evaluation may include: the implications of monetary policy in terms of the ability to implement changes in interest rates relatively quickly and incrementally, the limited political constraints, the possible conflicts with other objectives of economic policy, time lags, the independence of the central bank, the ineffectiveness of monetary policy in relation to structural unemployment / the natural rate of unemployment, its possible ineffectiveness during a recession, the possibility that alternative policies (eg supply-side policy) may be more effective.

Assessment Criteria

Part (b) 15 marks

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