

# Markscheme

**May 2021**

**Economics**

**Standard level**

**Paper 1**

11 pages

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## Section A

### Microeconomics

1. (a) Explain why the price elasticity of demand for primary commodities is often relatively low while the price elasticity of demand for manufactured goods is often relatively high.

[10]

*Answers may include:*

- definitions of PED, primary commodities, manufactured goods
- diagram(s) to show low (inelastic) demand for primary commodities and high (elastic) demand for manufactured goods
- explanation of low PED for primary commodities and high PED for manufactured goods in terms of the number and closeness of substitutes, degree of necessity and proportion of income spent on the good
- examples of primary commodities with a relatively low PED and manufactured goods with a relatively high PED.

### Assessment Criteria

#### Part (a) 10 marks

Level		Marks
<b>0</b>	<i>The work does not meet a standard described by the descriptors below.</i>	<b>0</b>
<b>1</b>	<i>There is little understanding of the specific demands of the question.</i>	<b>1–3</b>
	Relevant economic terms are not defined. There is very little knowledge of relevant economic theory. There are significant errors.	
<b>2</b>	<i>There is some understanding of the specific demands of the question.</i>	<b>4–6</b>
	Some relevant economic terms are defined. There is some knowledge of relevant economic theory. There are some errors.	
<b>3</b>	<i>There is understanding of the specific demands of the question.</i>	<b>7–8</b>
	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.	
<b>4</b>	<i>There is clear understanding of the specific demands of the question.</i>	<b>9–10</b>
	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) Discuss the importance of price elasticity of demand and cross price elasticity of demand for a firm’s decision making.

[15]

**Answers may include:**

- definitions of PED and XED
- diagram(s) to illustrate PED and XED
- explanation of the importance of PED estimates in terms of the impact on total revenue of price changes and the importance of XED estimates in terms of changes in the price of substitutes and complements
- examples in practice of the importance of PED for business revenue when price changes and the importance of XED when there are changes in the price of substitutes or complements
- synthesis or evaluation (discuss).

**Discussion may include:** the difficulty of obtaining reliable estimates in reality due to imperfect information, past data not necessarily being a guide to the future, the unreliability of consumer survey techniques, the problem of estimating variables that are not constant and the impact of factors other than the price of the good and the price of other goods.

Award a maximum of [9] if only PED or only XED is addressed.

**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
	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>	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 the concept of positive externalities of consumption.

[10]

Answers **may** include:

- definitions of externalities, positive externalities of consumption
- diagram to illustrate positive externalities of consumption
- explanation of positive externalities of consumption in terms of MSB being greater than MPB
- examples of positive externalities of consumption in practice.

**Assessment Criteria**

**Part (a) 10 marks**

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- (b) Discuss the view that tradable permits are more effective than taxes in reducing pollution.

[15]

**Answers may include:**

- definitions of tradable permits, taxes
- supply and demand diagram(s) to show the use of tradable permits, and/or supply shifting left due to taxes, to tackle pollution
- explanation that both methods represent market-based policies, tradable permits working via set allowances to pollute with implications for profits for over- or under-shooting, and taxes working via the effect on supply, price and quantity
- examples of the use of taxes and/or tradable permits in practice
- synthesis or evaluation (discuss).

**Discussion may include:** The advantage of tradeable permits over taxation is they create an incentive for firms to develop systems to reduce pollution and taxes just penalize all producers in a market and add to costs and the final selling price to households. The weakness of tradeable permits is the system is complicated to set up and administer and taxes are easier for a government to use.

Award a maximum of [9] if only tradeable permits **or** only tax is addressed.

### Assessment Criteria

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### Section B

#### Macroeconomics

3. (a) Explain why cyclical (demand-deficient) unemployment may occur in an economy. [10]

Answers *may include*:

- definition of unemployment, cyclical (demand-deficient) unemployment
- diagram to show cyclical (demand-deficient) unemployment
- explanation of how cyclical (demand-deficient) unemployment is caused by a fall in AD, which may arise from a fall in any or all of the components of AD (C + I + G + X – M)
- examples of cyclical (demand-deficient) unemployment occurring in practice.

#### Assessment Criteria

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- (b) Evaluate the effectiveness of interventionist supply-side policies in reducing the level of unemployment in an economy.

[15]

*Answers may include:*

- definitions of unemployment, interventionist supply-side policies
- diagram showing LRAS shifting right and/or supply of labour increasing in a labour market diagram; candidates may also show AD shifting right as a short-term effect of supply-side policies
- explanation that interventionist supply-side policies increase the quantity and quality of factors of production and thus increase the productive capacity of the economy and can be targeted at particular sectors of the economy; this may help to reduce structural unemployment in the long term and also contribute to the reduction of demand-deficient unemployment in the short term through the impact on AD
- examples of interventionist supply-side policies helping to reduce unemployment in practice
- synthesis or evaluation.

*Evaluation may include:* the importance of the type of unemployment (eg demand-deficient unemployment may be more directly reduced through expansionary monetary and fiscal policies); consideration of the effectiveness of supply-side policies (eg in terms of time lags, the ability to create employment, the impact on the government's budget deficit, opportunity cost); government investment in new technologies (eg robotics/artificial intelligence) may lead to displacement of labour.



**Assessment Criteria**

**Part (b) 15 marks**

<b>Level</b>		<b>Marks</b>
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4. (a) Explain how expansionary monetary policy could be used to close a deflationary (recessionary) gap.

[10]

Answers **may** include:

- definitions of monetary policy, expansionary monetary policy, deflationary gap
- diagrams to show a deflationary gap and how it would be closed by a shift of AD to the right and/or increasing money supply that leads to decrease in the interest rates
- explanation that by increasing the money supply/decreasing the interest rate the central bank stimulates consumption, investment and/or net export, leading to an increase in AD and return of the real GDP to its potential level
- examples of countries that have used expansionary monetary policy to close a deflationary gap.

### Assessment Criteria

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

[15]

**Answers may include:**

- definitions of monetary policy, inflation
- diagram to show AD shifting left as a result of contractionary monetary policy
- explanation of how contractionary monetary policy may help to reduce demand-pull inflation in terms of the mechanisms by which higher interest rates reduce AD via the effect on consumption, investment and/or net exports
- examples of contractionary monetary policy being used in practice or examples of inflation targeting
- synthesis or evaluation.

**Evaluation may include:** the implications of monetary policy in terms of the ability to implement changes in interest rates relatively quickly through the banking system, the possible conflicts with other objectives of economic policy, such as growth / unemployment, time lags, the independence of the central bank; the ineffectiveness of monetary policy in relation to cost-push inflation; the possibility that alternative policies (eg supply-side policies) may be more effective.

### Assessment Criteria

#### Part (b) 15 marks

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