

Markscheme

May 2021

Economics

Standard level

Paper 2

21 pages

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Section A

1. (a) (i) Define the term *trade war* 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 trade that is seen as unfair by one country, leading to protectionism OR the idea that it is rising protectionism.	
2	<i>Accurate definition.</i>	2
	An explanation that the imposition of a trade barrier by one country can trigger a series of retaliations by (a) trade partner(s).	

- (ii) Define the term *consumption* indicated in bold in the text (paragraph ❸). [2]

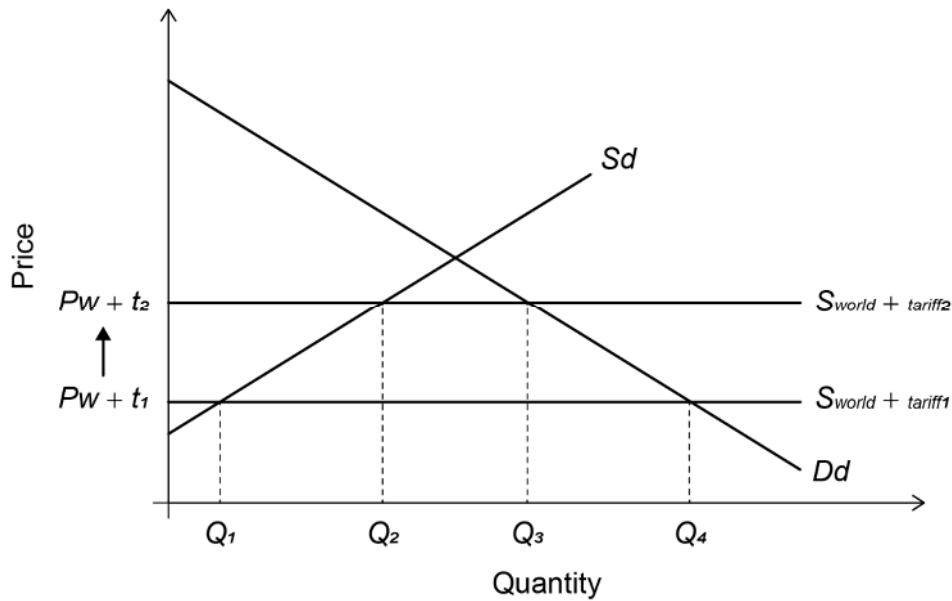
Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>Vague definition.</i>	1
	The idea that it is a component of AD OR that it is consumer spending.	
2	<i>Accurate definition.</i>	2
	An explanation that it is spending by households/people on goods (and services).	

- (b) Using an international trade diagram, explain how US tariffs could affect the export of Chinese steel and aluminium to the US (paragraph ❷). [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 an international trade diagram showing the imposition of a (or an increase in a) tariff in the US market and the world (China’s) supply ($S_{\text{world}}/S_{\text{China}}$) shifting up OR for an explanation that a tariff would increase the price of steel and aluminium and thus reduce the amount of steel and aluminium imported from China (exported to the US) from Q1Q4 to Q2Q3.	
2	<i>There is a correct diagram AND an accurate written response.</i>	3–4
	For an international trade diagram showing the imposition of a (or an increase in a) tariff in the US market and the world (China’s) supply ($S_{\text{world}}/S_{\text{China}}$) shifting up AND for an explanation that a tariff would increase the price of steel and aluminium and thus reduce the amount of steel and aluminium imported from China (exported to the US) from Q1Q4 to Q2Q3.	

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. The world supply curve may be labelled S_w , or S_{world} or S_{China} . A title is not necessary.



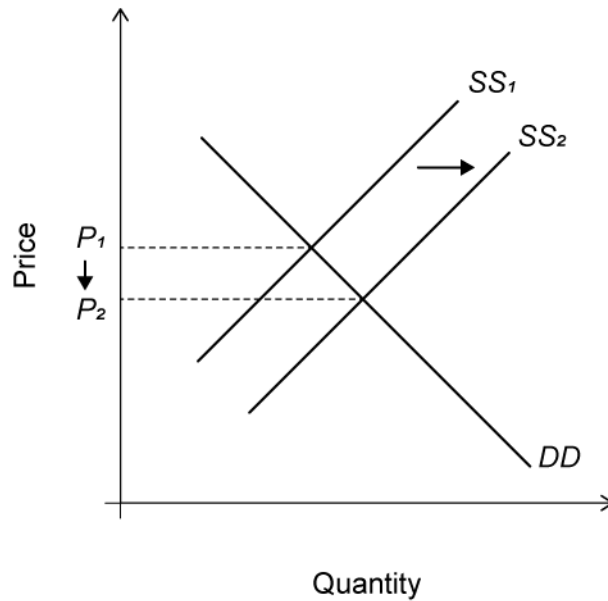
(c) Using a demand and supply diagram, explain how reduced tariffs on “imported factors of production” would affect the price of Chinese goods (paragraph 7).

[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 a demand and supply diagram showing a shift of the supply curve to the right and a decrease in price OR for an explanation that a lower tariff on imported factors of production would reduce the costs of factors of production for firms, leading to lower prices.	
2	There is a correct diagram AND an accurate written response.	3–4
	For a demand and supply diagram showing a shift of the supply curve to the right and a decrease in price AND for an explanation that a lower tariff on imported factors of production would reduce the costs of factors of production for firms, leading to lower prices.	

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

The vertical axis should be price or *p*. The horizontal axis should be quantity or *q*. A title is not necessary.



- (d) Using information from the text/data and your knowledge of economics, evaluate the impacts of free trade measures on China’s economy.

[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.

Answers **may** include:

- Definition of free trade.

Benefits of reduced tariffs:

- Lower risk of retaliation and trade war (paragraphs ② and ⑤)
- The increase in export revenue could help compensate for the decrease in consumption and combat the economic slowdown (paragraph ③)
- Greater choice and lower prices for Chinese consumers and in particular for agricultural producers, provider of medical services who may purchase foreign tractors and medical devices at a lower price (paragraph ④)
- Lower tariffs will reduce import prices leading to lower input costs for firms relying on imported components (potential increase in SRAS) (paragraph ⑦)
- Increased competition from trade and foreign firms may lead to product innovation and greater efficiency (paragraph ⑥)
- More efficient allocation of resources as US and China specialize and trade
- The current account surplus could be eroded (paragraph ①) and this may prevent currency appreciation hence benefitting exporters (but at the expense of consumers who may see their real income reduced).

Limitations of reduced tariffs:

- Lower tariffs may increase the amount of imports, which could lead to lower AD. This could lower economic growth given the current slowdown in domestic consumption (paragraph ③)
- Decreased consumption of domestic products could lead to (structural) unemployment in the manufacturing sector (paragraph ④)
- There could be an opportunity cost for the government due to the loss of tariff revenue (paragraph ①)
- More competition for Chinese car manufacturers who are currently facing an oversupply and possible impact on domestic employment in the industry (paragraph ⑤).

Any reasonable evaluation.

2. (a) (i) Define the term *current account* 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
	The idea that it is a measure of money coming into, and going out of, a country from international trade OR that it is a measure of the balance of trade	
2	<i>Accurate definition.</i>	2
	An explanation that it is a measure of the (net flow of funds from) trade in goods and services, income and transfers (flows with the rest of the world).	

- (ii) Define the term *depreciation* indicated in bold in the text (paragraph ④). [2]

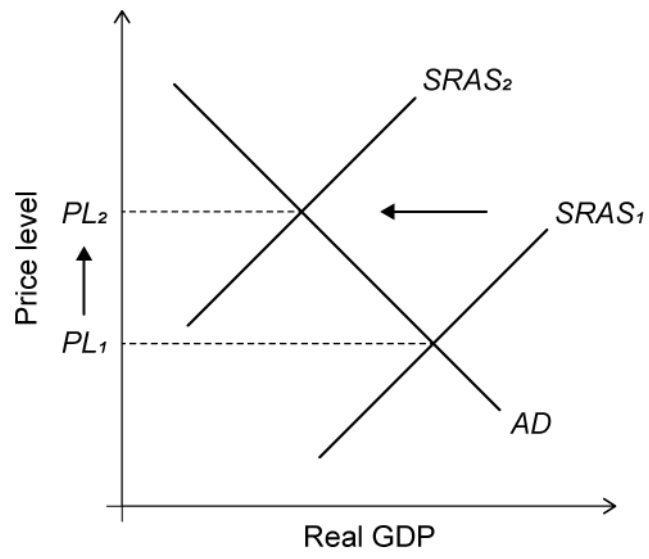
Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>Vague definition.</i>	1
	The idea that the exchange rate falls.	
2	<i>Accurate definition.</i>	2
	An explanation that it is a decrease in the value/price of one currency AND one of the following: <ul style="list-style-type: none"> • in a floating exchange rate system • due to market forces. 	

- (b) Using an AD/AS diagram, explain how an increase in oil prices “could worsen inflationary pressures” (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
	An AD/AS diagram showing a shift of SRAS/AS to the left and an increase in the price level OR an explanation that the higher price of oil would increase the cost of production and hence lead to (cost-push) inflation.	
2	<i>There is a correct diagram AND an accurate written response.</i>	3–4
	An AD/AS diagram showing a shift of SRAS/AS to the left and an increase in the price level AND an explanation that the higher price of oil would increase the cost of production and hence lead to (cost-push) inflation.	

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

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



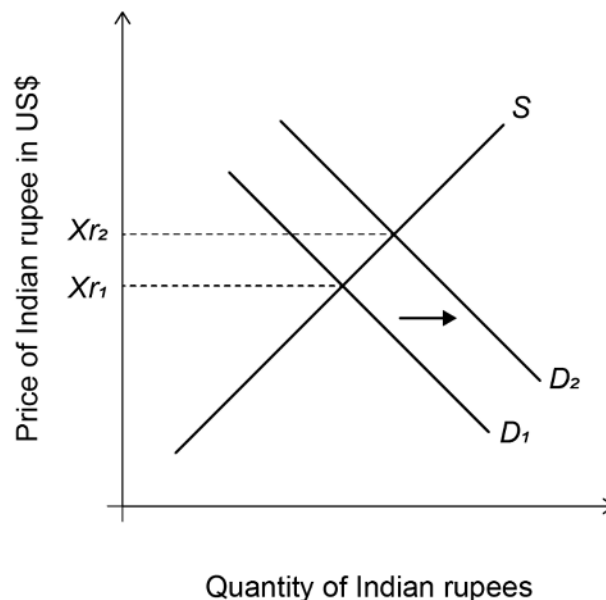
- (c) Using an exchange rate diagram, explain how higher interest rates could “protect the rupee from further depreciation” (paragraph 9).

[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
	An exchange rate diagram showing a shift of demand for the Indian rupee to the right, causing the rupee to appreciate OR an explanation that the higher interest rates would protect the rupee from further depreciation by increasing the demand for the rupee from foreigners seeking higher interest rates through saving/(portfolio) investment in India, resulting in an increase in the value of the rupee.	
2	<i>There is a correct diagram AND an accurate written response.</i>	3–4
	An exchange rate diagram showing a shift of demand for the Indian rupee to the right, causing the rupee to appreciate AND an explanation that the higher interest rates would protect the rupee from further depreciation by increasing the demand for the rupee from foreigners seeking higher interest rates through saving/(portfolio) investment in India, resulting in an increase in the value of the rupee.	

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 the (Indian) rupee in another currency, other currency/(Indian) rupee or other currency per (Indian) rupee. The horizontal axis should be quantity, or quantity of (Indian) rupee. A title is not necessary.



- (d) Using information from the text/data and your knowledge of economics, discuss the possible economic consequences on the Indian economy of a depreciating rupee.

[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

“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.

Benefits of the depreciation may include:

- The depreciation would help close the current account deficit (paragraph ①) by making imports more expensive and exports cheaper
- Exported services would become cheaper in foreign currency terms which may lead to higher demand (but will not encourage diversification of exports (paragraph ③))
- The cheaper export services might help capture other markets (in addition to US and Europe) (paragraph ③)
- Other currencies have also depreciated and hence the depreciation keeps Indian exports competitive (paragraph ⑤).

Limitations/disadvantages of the depreciation may include:

- The depreciation would make imported oil even more expensive. Given that demand is likely to be inelastic and since rising oil prices are already a contributor to the current account deficit (paragraph ②), that would worsen the deficit
- Higher prices for imported capital goods and oil would worsen cost-push inflation (paragraphs ② and ④)
- Higher prices for imported capital goods may reduce imports of such goods and slow down potential growth (paragraph ②)
- The inflation rate has risen between 2017 and 2018 (**Table 1**) and hence the depreciation would only lead to further increase in prices
- With the current high growth rate (**Table 1**), an increase in exports could lead to further demand-pull inflation.

Any reasonable discussion.

Section B

3. (a) (i) Define the term *recession* 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> The idea that it is a general slowdown in economic activity.	1
2	<i>Accurate definition.</i> An explanation that there are at least two consecutive quarters of negative economic growth/falling real GDP OR a sustained decline in economic activity.	2

- (ii) Define the term *privatization* indicated in bold in the text (paragraph ❷). [2]

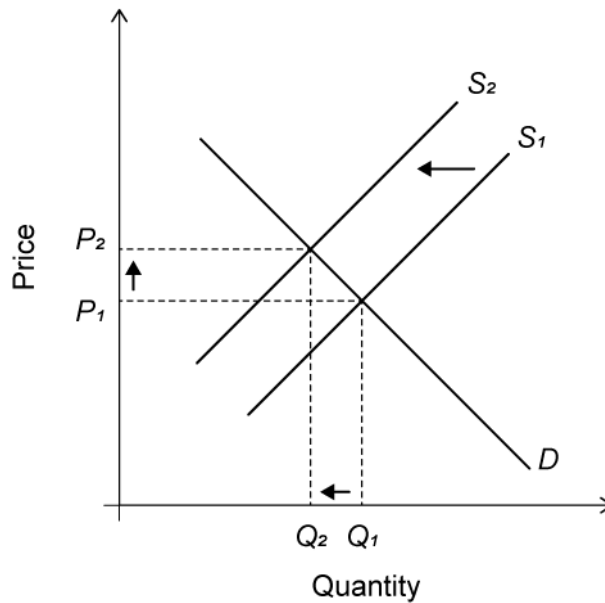
Level		Marks
0	<i>The work does not meet a standard described by the descriptors below.</i>	0
1	<i>Vague definition.</i> The idea that it is when the government no longer owns a company.	1
2	<i>Accurate definition.</i> An explanation that the government sells state-owned/public enterprises/firms/assets to the private sector.	2

- (b) Using a demand and supply diagram, explain the impact on households of “removing some subsidies on food” (paragraph ❸). [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> For drawing a demand and supply diagram with a shift of the supply curve to the left and a higher price and lower quantity OR for explaining that the reduction in food subsidies will lead to (increased costs for firms and so) a decrease in supply leading to a higher price (and lower quantity consumed) of food for households.	1–2
2	<i>There is a correct diagram AND an accurate written response.</i> For drawing a demand and supply diagram with a shift of the supply curve to the left and a higher price and lower quantity AND for explaining that the reduction in food subsidies will lead to (increased costs for firms and so) a decrease in supply leading to a higher price (and lower quantity consumed) of food for households.	3–4

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

For a demand and supply diagram, the vertical axis should be price or P. The horizontal axis should be quantity or Q. A title is not necessary.



(c) Using a Lorenz curve diagram, explain the likely impact on income distribution of “plans to encourage investment in rural areas” (paragraph 5).

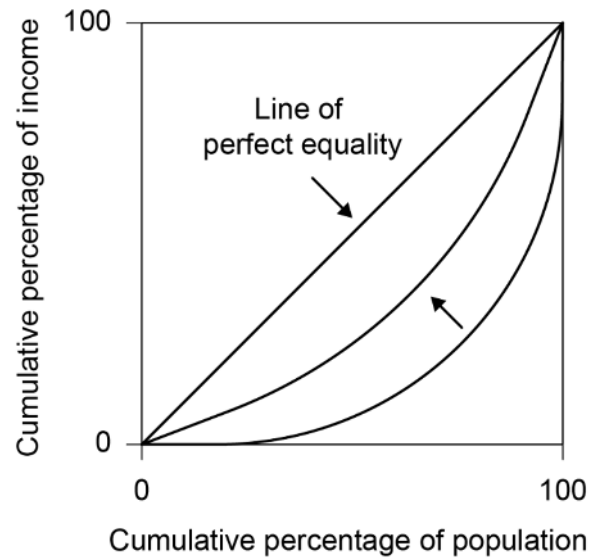
[4]

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
	A Lorenz curve diagram showing the curve moving closer to the line of perfect equality OR an explanation that plans to encourage investment in rural areas will reduce the gap with urban areas (or will raise wages/employment) making the income distribution more equal as shown by the inward movement of the Lorenz curve (or a reduction in the area below the line of perfect equality).	
2	<i>There is a correct diagram AND an accurate written response.</i>	3–4
	A Lorenz curve diagram showing the curve moving closer to the line of perfect equality AND an explanation that plans to encourage investment in rural areas will reduce the gap with urban areas (or will raise wages/employment) making the income distribution more equal as shown by the inward movement of the Lorenz curve (or a reduction in the area below the line of perfect equality).	

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

The two curves may be shown on one graph, or may be shown on two graphs. If using two graphs, it must be clear the curve after investment is closer to the line of equality than the previous one.

The vertical axis may be labelled (cumulative) % of (national) income (GDP and GNI are valid alternatives to income but wealth is not acceptable). For the horizontal axis, the label may be (cumulative) % of population/people/households. A title is not necessary. There must be a diagonal line, but it is not a requirement that it is labelled. There should be labels (or arrow) to indicate the difference between the two Lorenz curves (or direction of the change).



- (d) Using information in the text/data and your knowledge of economics, evaluate the effectiveness of market-oriented policies in achieving economic development in Angola.

[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.

Answers may include:

- Definition of market-oriented policies
- Definition of economic development.

Strengths of market-oriented policies:

- Promotes growth and creates employment and possibly higher wages by attracting foreign investment (paragraph 2)
- Devaluing the exchange rate has reduced the need for foreign exchange reserves (paragraph 3)
- Privatization may lead to competition, lower costs and lower prices and more choice for consumers (paragraph 2)
- Privatization will provide revenue to the government to pay down debt or invest in infrastructure and/or social spending
- Expanding infrastructure projects with private sector involvement encourage FDI (paragraph 2)
- Market-oriented policies may increase long run aggregate supply allowing inflation to fall below 25% (paragraph 5)
- Tax incentives in rural areas would create jobs and reduce inequalities (paragraph 5)
- Reforms of the banking sector will possibly make it easier for small-scale businesses to get loans (paragraph 2).

Limitations of market-oriented policies:

- The privatization of railways and telecommunications may lead to higher prices for consumers and more inequality
- Incentive-based policies may not be sufficient to allow for diversification since manufacturing base is small and likely underdeveloped (paragraph ① and ④)
- Stopping subsidies on food and using ad valorem taxes will raise prices causing inflation and inequality to worsen in the short term (paragraph ⑤)
- Measures to reduce public debt could worsen income inequality
- Market-oriented policies (eg more inward FDI) are unlikely to work without complementary interventionist policies such as the building of infrastructure (paragraph ④) to support diversification
- Less intervention in the exchange rate may lead to depreciation and higher prices and/or less certainty for foreign investors
- Market-oriented policies may lead to externalities
- Encouraging more inward FDI and other investment will increase private-sector debts and debt-servicing costs, leading to less income available to spend on merit goods
- Market-oriented policies tend to lead to higher inequalities (eg through lower wages).

Any reasonable evaluation.

4. (a) (i) Define the term *economic growth* 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> The idea that it is a growing economy (or an increase in GDP).	1
2	<i>Accurate definition.</i> An explanation that it is one of the following: <ul style="list-style-type: none"> • an increase in real output (over time) • an increase in real GDP • an increase in potential output. NB The term “over time” is not necessary for [2].	2

(ii) Define the term *poverty trap* indicated in bold in the text (paragraph 4). [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 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/poverty 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 lead to low levels of human capital that leads to low productivity that leads to low incomes. 	2

- (b) Using an AD/AS diagram, explain how the construction of the China–Laos railway will contribute to economic growth in Laos (paragraph 1).

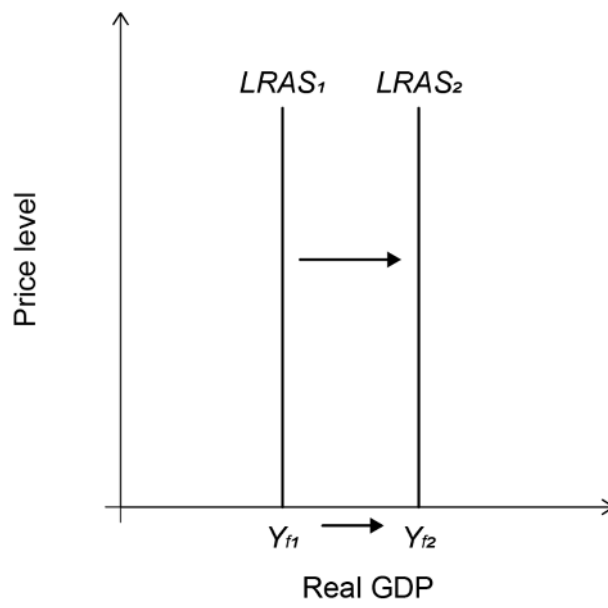
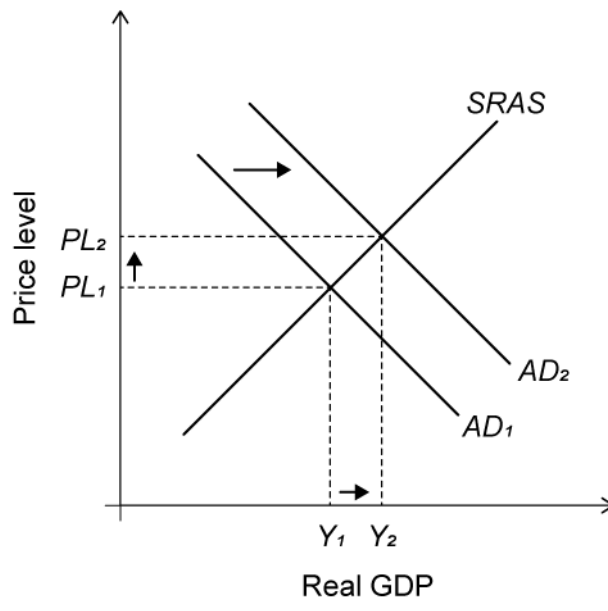
[4]

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
	<p>For an AD/AS diagram showing an increase in aggregate demand (AD) and a resulting increase in real GDP OR an explanation that the construction of the China-Laos railway would imply an increase in government spending (and/or investment and/or export revenue from trade/tourism), which would lead to greater economic activity/increased real GDP.</p> <p>Alternative diagram and explanation: For an AD/AS diagram showing an increase in LRAS and a resulting increase in potential output/GDP OR an explanation that the construction of the China-Laos railway would imply an increase in productivity/efficiency, which would lead to increased productive capacity.</p>	
2	<i>There is a correct diagram AND an accurate written response.</i>	3–4
	<p>For an AD/AS diagram showing an increase in aggregate demand (AD) and a resulting increase in real GDP AND an explanation that the construction of the China-Laos railway would imply an increase in government spending (and/or investment and/or export revenue from trade/tourism), which would lead to greater economic activity/increased real GDP.</p> <p>Alternative diagram and explanation: For an AD/AS diagram showing an increase in LRAS and a resulting increase in potential output/GDP AND an explanation that the construction of the China-Laos railway would imply an increase in productivity/efficiency, which would lead to increased productive capacity.</p>	

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

For AD/AS, the vertical axis may be price level or average price level or general price level.

The horizontal axis may be real output, real national output, real national income, or real GDP. Any abbreviation is acceptable. A title is not necessary.

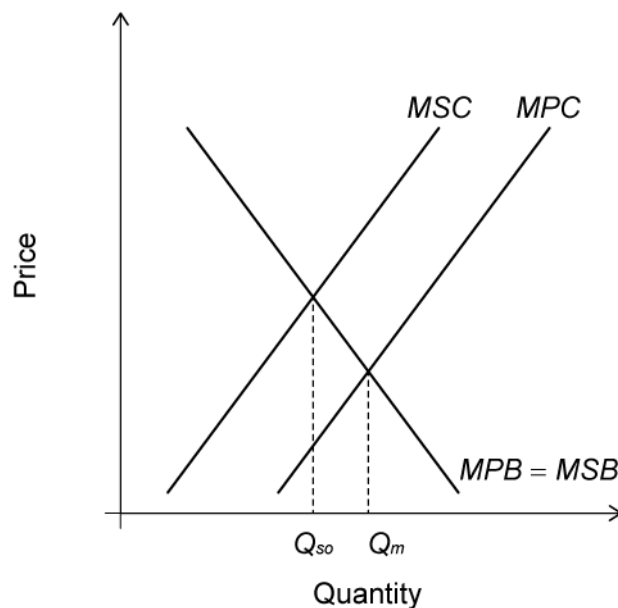


(c) Using an externalities diagram, explain why the construction of dams on the Mekong River might lead to market failure (paragraph 2).

[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 an externalities diagram showing a negative externality with MSC above MPC and overproduction taking place ($Q_m > Q_{so}$) OR for explaining that hydroelectric power 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 ($MSB \neq MSC$) • a situation where there is a welfare loss to society. 	
2	<i>There is a correct diagram AND an accurate written response.</i>	3–4
	For drawing an externalities diagram showing a negative externality with MSC above MPC and overproduction taking place ($Q_m > Q_{so}$) AND for explaining that hydroelectric power 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 ($MSB \neq MSC$) • a situation where there is a welfare loss to society. 	

Candidates who incorrectly label diagrams can be awarded a maximum of [3]. For an externalities diagram, the y axis may be labelled price or P or costs or benefits, and the x axis labelled quantity or Q.



- (d) Using information from the text/data and your knowledge of economics, evaluate the role of foreign direct investment in promoting economic development in Laos. [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.	
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	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.

Answers may include:

- definition of foreign direct investment
- definition of economic development.

Strengths of FDI/MNCs may include:

- help reduce the over-reliance on the agricultural sector (paragraph ①) where income is low
- provide employment and hence break the poverty trap (paragraph ④)
- Laos is landlocked so rail project facilitates cheaper transport of goods and services and raw materials (paragraph ①)
- potential to develop tertiary sector with tourism and exposure to “larger markets” (paragraph ②)
- foreign investment leads to economic growth (paragraph ①)
- brings efficiency and expertise/technology (paragraph ④)
- MNCs provide training
- MNCs may help finance infrastructure (paragraph ⑤)
- MNCs help generate tax revenue.

Limitations of FDI/MNCs may include:

- many of the jobs created do not go to the locals (paragraph ④)
- profits may be repatriated
- MNCs may influence local politics and taxation policies
- spending on infrastructure to attract MNCs may mean that less is spent on health and education (paragraph ⑤)
- a lot of infrastructure needs to be financed by loans to attract MNCs which may lead to debts (paragraph ⑤)
- MNCs may take advantage of less strict labour and environment protection laws
- rail project/dams may lead to negative externalities (paragraph ②).

Any reasonable evaluation.
