

The City School

Mid Year Examination

2016 - 2017

Class 11

ECONOMICS

Paper 2

Answer Key



1 (a) Using information from the extract, identify two indicators of improved living standards in Indonesia. [2]

- A rise in incomes/increase in purchasing power (1) improved medical care/an increase in doctors per head (1).

(b) Explain whether the extract suggests the demand for chocolate is price-elastic or price-inelastic in developed countries. [2]

- It suggests it is price-inelastic (1) as it is addictive (2).

(c) GDP was at its highest in July 16, as economy has grown continuously throughout from July 13 till July 16 and there has not been any negative growth.

[4]

(d) Calculate the rate of inflation in Indonesia in 2014. [3]

- 6.67% / 6.7% / 6.6% / 6.666666% (3)
- Correct working: $7.2/108 \times 100/115.2 - 108 \times 100/108$ or $6.67/6.7/6.6/6.666666/1.067$ or version of (2)
- 7.2 / 7.2% (1).

(e) What is the difference between real and nominal GDP growth? [4]

Real GDP refers to the rise in the productive potential of an economy that is increase in the output produced in the economy while nominal GDP refers to the rise in money GDP due to inflation

(f) Discuss whether the price of chocolate is likely to increase in the future. [5]

Up to 3 marks for why it might:

- Demand is increasing/high demand (1) as incomes are rising/population increasing (1)
- Sellers may raise price as demand is inelastic (1) market power enables producers to raise price (1)
- Supply may fall/low supply (1) due to pests and disease (1).
- Farmers may switch to other products (1).
- Farmers and farm workers may become less productive (1) becoming older (1).

Up to 3 marks for why it might not:

- Farms may be merged (1) enabling greater advantage to be taken of economies of scale (1) lowering average costs (1).
- Concerns about obesity/diabetes/health effects (1) may reduce demand for chocolate (1)
- If more producers enter the market (1). This will increase competitive pressure/increase supply which will drive down price (1)
- Up to a maximum of 2 marks for showing relevant shifts in demand and supply curves in place of statements about e.g. increase in demand.

(g) Explain reasons for rise in demand for chocolates. [4]

Rise in incomes Popularity/trend

For gaining (4) marks need to explain reasons

(h) Discuss whether an ageing population should always be regarded as an economic problem. [6]

Definition of ageing population:

- this occurs where people are living longer and therefore the average age of the population is rising (2).

Possible problems:

- a rise in the dependency ratio, i.e. the ratio of the working population to the dependent population becomes lower
- A change in the labour force; older workers may be less geographically and occupationally mobile (the retirement age is likely to go up)
- Older workers may lack the required skills/training
- A higher demand for health services
- A higher demand for welfare services
- A rise in the cost of pensions
- All of this may require taxation to be increased
- A change in the pattern of demand.

Answers which fail to address 'always' can gain no more than 5 marks.

2 (a) Explanation could include:

- There are limited/finite resources (1)
- To satisfy unlimited/infinite wants (1)
- Where choices have to be made/there is an opportunity cost (1). [3]

(b) Definition: the (next) best (1) alternative foregone/not taken (1) as a result of taking a decision/making a choice – appropriate example of choice (1). [3]

(c) Factors of production:

1. Land: natural resources available for production, e.g. oil, coal, forests, fish, farming.
2. Labour: human effort available for production/human capital, e.g. skilled/unskilled.
3. Capital: man-made physical goods used in production, e.g. machines, tools, factories (Do NOT accept money).
4. Enterprise: the role of the entrepreneur in terms of organising the other factors of production and in taking a risk in doing so.

1 mark for each correct description (4); up to 2 marks for appropriate use of examples (2). [6]

A list of 4 factors of production – 2 marks.

A list of 3 factors of production – 1 mark.

A list of 2 factors of production – no marks.

(d)

Discussion could include:

Conservation of natural resources	Use of natural resources:
<ul style="list-style-type: none">• this will avoid too rapid a depletion of resources• this is more sustainable as it takes into account the needs of future generations• a better long-term strategy	<ul style="list-style-type: none">• will raise output• will raise income and employment• but resources will be depleted/exhausted more quickly• more of a short-term strategy

A one-sided answer, which focuses on the conservation or use of resources only, can gain no more than 5 marks. [8]

3 (a) Define 'market failure'. [2]

- Where the market forces of demand and supply (1) do not achieve efficiency (1)
- When social costs are greater than social benefits (1) example of external cost e.g.

Monopoly or external benefit e.g. merit or public goods (1)

(b) Explain how government regulation may reduce market failure. [4]

- Regulation involves rules and laws (1).
- Firms may be banned (1) from producing products that create external costs (1) example such as water pollution (1).
- Firms may be fined (1) if they create external costs (1) example e.g. air pollution (1).
- Consumers may be banned from consuming products that create external costs (1) or where there are high private costs (1) some of which people are unaware of (1) example e.g. cigarettes (1)
- Consumption of some products that have external benefits (1) and/or high private benefits (1) some of which people are unaware of (1) may be made compulsory (1) e.g. primary school education (1).

(c) Analyse the effect of a decrease in resources on government economic aims.

[6]

- Fewer resources will make it more difficult to achieve economic growth (1) there will be fewer factors of production to produce goods and services (1) output may fall or rise more slowly (1).

- Fewer resources may increase costs of production (1) supply may fall by more than demand/there may be a shortage of e.g. raw materials (1) cost-push inflation may occur (1).

- Natural disasters (1) can lead to cost push inflation (1) loss of employment (1) government expenditure exceeding government income (1)

- The current account may move into a deficit/larger deficit (1) as exports may decline (1) while e.g. food may have to be imported (1).

- Destruction of factories may reduce unemployment opportunities (1) which may increase unemployment (1) but more workers may be needed to e.g. rebuild factories (1).

(d) Discuss whether the social benefits of building flood defences will exceed the social costs involved. [8]

Up to 5 marks for a discussion of why social benefits maybe greater:

- Social benefits are private benefits plus external benefits (1).
- Explain private benefits (1) e.g. greater employment, greater revenue for firms, protection of homes / reduction in high risk of flooding (up to 3)
- Explain external benefits (1) e.g. increase in house prices in the area, greater tourism, reduced cost to emergency services and benefit payments (up to 3)

Up to 5 marks for why social costs maybe greater:

- Social costs are private costs and external costs (1).
- Explain private costs (1) e.g. cost of land, raw material labour and buildings, may only be a low risk of flooding (up to 3)
- Explain external costs (1) e.g. pollution, destruction of wildlife habitats, opportunity cost of resources (up to 3).

1) Explain the concept of supply and demand (10)

2) Explain the relationship between the determinants of supply and demand (10)

3) Explain the price mechanism (10)

4) Explain the role of government in the market (10)

5) Explain the concept of equilibrium (10)

6) Explain the concept of market failure (10)

7) Explain the concept of externalities (10)

8) Explain the concept of public goods (10)

9) Explain the concept of merit goods (10)

10) Explain the concept of demerit goods (10)

11) Explain the concept of perfect competition (10)

12) Explain the concept of imperfect competition (10)

13) Explain the concept of monopoly (10)

14) Explain the concept of oligopoly (10)

15) Explain the concept of duopoly (10)

16) Explain the concept of perfect information (10)

17) Explain the concept of asymmetric information (10)

18) Explain the concept of adverse selection (10)

19) Explain the concept of moral hazard (10)

20) Explain the concept of signaling (10)

21) Explain the concept of screening (10)

22) Explain the concept of reputation (10)

23) Explain the concept of signaling and screening (10)

(c) Analyse what effect a rise in the price of apples, which are a substitute for bananas, will have on the market for bananas. [4]

1 mark for some consumers will switch from buying apples to buying bananas

1 mark for demand for bananas will decrease (this may be shown on diagram)

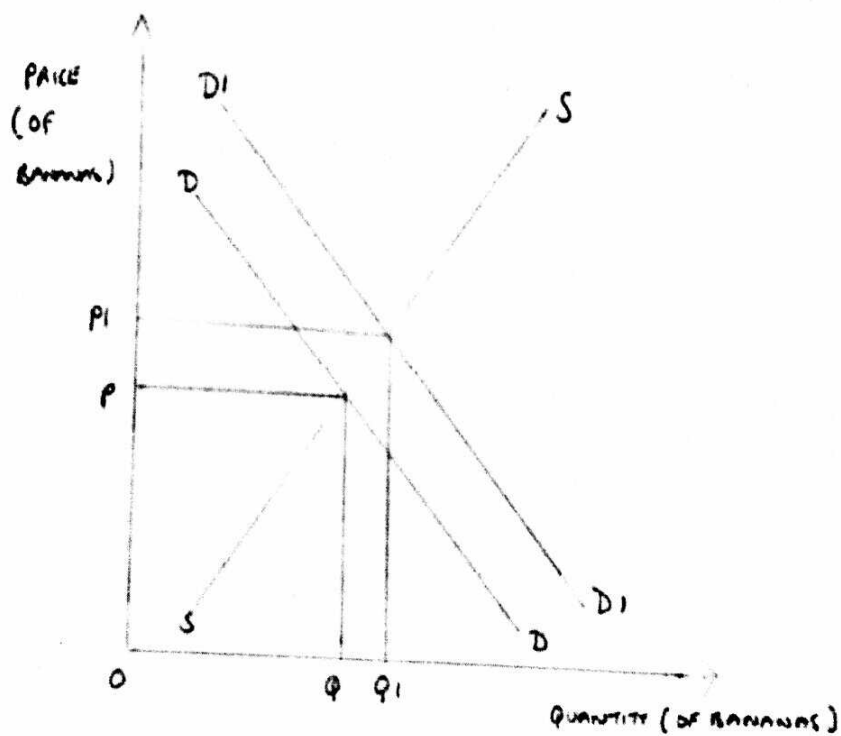
1 mark for price of banana will rise (this may be shown on diagram)

1 mark for supply of banana will rise (this may be shown on diagram)

Note: accept a diagrammatical approach for 3 marks.

Note: accept analysis of supply of bananas decreasing only if the consumer makes clear that farmers may be growing both bananas and apples.

Figure 3(c)



(d) Discuss whether a government should increase the tax on cigarettes. [8]

Up to 6 marks for why it should:

Up to 2 marks: the tax may increase government revenue (1), this would enable the government to spend more on (e.g.) education (1).

Up to 6 marks: put up price (1) to discourage smoking (1), smoking damages people's health (1) this is both for smokers and non-smokers/passive smoking (1) and so increases spending on health care (1) and reduces labour productivity (1) and reduces life expectancy (1).

Up to 3 marks: cigarettes may be imported (1), imports of cigarettes count in trade in goods component (1) and may contribute to a current account deficit (1).

Up to 2 marks: smoking causes external costs (1), e.g. air pollution (1).

Up to 6 marks for why it should not:

Up to 2 marks: demand may be inelastic (1), and so a rise in price will not have much impact on consumption (1).

Up to 3 marks: cigarettes may represent a higher proportion of spending for people with lower incomes (1) so tax may be regressive (1) and so fall more heavily on the poor (1).

Up to 2 marks: may contribute to inflation (1) as one of the products bought by consumers will rise in price (1).

Up to 3 marks: may encourage smuggling of cigarettes (1) if cigarettes are cheaper/less heavily taxed abroad (1) and reduce tax revenue (1).

Up to 4 marks: may harm domestic cigarette producers (1), if consumers switch from domestic to foreign cigarettes (1), may be an adverse effect on domestic employment (1), may also harm the balance of payments (1).

Maximum of 4 marks for a list or list-like response.

Note: a maximum of 8 marks overall.

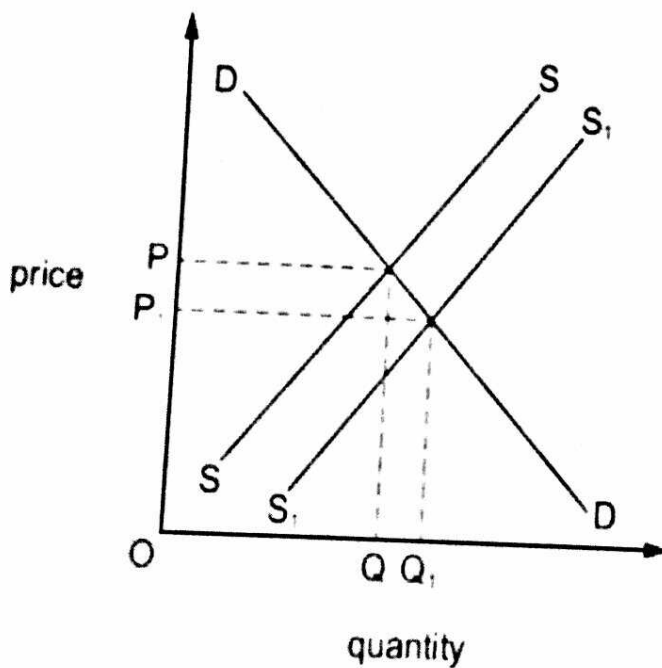
5 (a) Define 'an indirect tax'. [2]

A tax on spending / goods and services / consumption (1) the burden of the tax can be moved on to someone else (1) example (1)

(b) Explain how a cut in the rate of corporation tax could result in an increase in tax revenue. [4]

- A lower tax will increase the profit firms can keep / lower the cost of production (1) encourage them to increase output (1) increasing employment (1) pay higher wages (1) direct tax revenue would rise (1).
- Spending / consumption may increase (1) more revenue from indirect taxes (1).

(c) Using a demand and supply diagram, analyse the effect of removing an indirect tax on the market for the product. [6]



Up to 4 marks for the diagram:

- axes correctly labelled – price and quantity or P and Q (1)
- demand and supply curves correctly labelled (1)
- supply curve shifted to the right (1)
- correct equilibriums identified either by a line drawn to both axes or equilibrium points clearly identified e.g. E and E1 (1).

Up to 2 marks for written comments:

- removing an indirect tax effectively reduces costs of production (1)
- A greater supply will lower price (1).

(d) Discuss whether an increase in taxes will reduce inflation. [8]

Up to 5 marks for why it might:

- Increases in income tax (1) will reduce disposable income (1) spending may fall (1) lower demand will reduce demand-pull inflation (1).
- Increases in corporation tax (1) reduces profits firms can keep (1) reduces demand for capital goods/investment (1).
- Increases in indirect taxes (1) will reduce spending (1) lowering demand-pull inflation (1)

Up to 5 marks for why it might not:

- Consumers and firms may respond by reducing saving (1) rather than spending (1).
- Higher indirect taxes and corporation tax (1) increase costs of production / higher prices (1) may cause cost-push inflation (1).
- Higher income tax may encourage workers to press for wage rises (1) increasing costs of production (1) causing cost-push inflation (1).

6 (a) Describe how changes in the price level are measured in an economy. [5]

Award 1 mark each up to a maximum of 5 marks for describing

- use of a consumer or retail prices index
- recording of changes in prices over a period of time
- a basket of goods and services (usually about 600 products)
- use of a base year used as a 'starting point' to make comparisons over time (given the value = 100)
- weighting given to each product in the basket to reflect the percentage of average income that is spent on it
- creation of a weighted price index, multiplying the price index for different products by their weighting, to measure the change overall over a period of time

(b) Explain how a situation of 'too much money chasing too few goods' can lead to inflation. [5]

1 mark for idea of too much money; idea of monetary inflation; excessive growth of the money supply or specific mention of demand-pull inflation

1 mark for a precise definition of inflation: a sustained increase in the general level of prices over a period of time

Up to 4 marks: idea of chasing too few goods/not enough goods being produced (1) for the people who want to buy them (1), i.e. money supply has increased faster (1) than the increase in output (1), economy may be at full employment (1) prices rise (1)

Up to 2 marks for an AS/AD diagram showing shift in AD curve to right (1) and the effect on price level (1)

(c) Discuss whether fiscal policy, rather than monetary policy, is always a better way to bring down the rate of inflation in an economy. [10]

Up to 5 marks for the advantages of fiscal policy:

Up to 3 marks each for:

- an increase in taxes (1) can have a more immediate effect (1) than changes in interest rates which can take a while to have an effect in an economy (1)
- cuts in public expenditure (1) can have a major effect, given the number of people employed (1), and this can have a 'knock-on' effect in an economy (idea of multiplier effect, but candidates do not need to use that term) (1)

Up to 5 marks for the disadvantages of fiscal policy:

Up to 3 marks each for:

- there could be side-effects (1), e.g. an increase in income tax could act as a disincentive

to effort (1), leading to a reduction in output (1)

- the cuts could take a while to have an effect (1) and they could lead to an increase in

unemployment (1) and a reduction in output (1)

Up to 5 marks for the advantages of monetary policy:

Up to 3 marks each for:

- an increase in the rate of interest (1) can have a major effect by making the cost of borrowing more expensive (1), reducing the level of demand (1)
- the reduction of the money supply (1) could have a major effect by reducing the extent of liquidity in the economy (1), reducing the possibility of borrowing money (1)

Up to 5 marks for the disadvantages of monetary policy:

Up to 3 marks each for the impact of:

- a rise in the rate of interest may be limited (1), especially in the short-term (1), particularly where demand is interest-inelastic (1)
- a reduction in the money supply may take a while to have an effect (1) and banking institutions may find ways to get round the restrictions (1) making the effect very limited, especially in the short-term (1) Maximum of 5 marks for a list or list-like answer

7 (a) What is the difference between absolute poverty and relative poverty? [4]

Description:

- Absolute poverty involves a lack of basic necessities including food, housing and clothing.
- Relative poverty occurs when people have less income than other people in the country/unable to participate fully in the normal activities of their society. [4]

(b) Explain two economic advantages of a fall in unemployment. [4]

1 mark each for each of two advantages identified e.g.:

- higher output
- reduced poverty
- increase in tax revenue
- reduced government spending on benefits.

1 mark each for each of two explanations e.g.:

- more people in work will enable more products to be produced – might include a PPC with a movement from inside to on the curve
- more people in work will reduce those without an earned income and will raise tax revenue that might be spent on measures to reduce poverty
- extra tax revenue might be spent on a range of items including infrastructure and may reduce a budget deficit
- less government spending on benefits might enable a government to cut tax rates or raise spending on another area. [4]

(c) Analyse how fiscal policy may reduce unemployment. [5]

Analysis:

- A cut in taxes may increase consumer spending/investment and so increase demand for labour.
- A rise in government spending will increase total (aggregate) demand which will increase demand for labour.
- Government spending may create jobs directly in the public sector.

Up to 3 marks for an answer which focuses on either just a cut in taxes or just on an increase in government spending. [5]

(d) Discuss whether economic growth always results in higher living standards. [7]

Consideration of factors linked to growth influencing living standards e.g.:

- how extra income is distributed
- what type of products are being produced
- whether working hours are increasing
- whether working conditions are improving
- whether higher output is leading to pollution and other environmental damage
- what is happening to the size of the informal sector
- whether additional income is spent or saved.

Up to 4 marks if only three influencing factors are considered. [7]

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Paper 1

Answer Key



1	B	16	C
2	D	17	D
3	A	18	C
4	D	19	B
5	D	20	B
6	C	21	C
7	D	22	A
8	B	23	B
9	A	24	C
10	D	25	C
11	C	26	A
12	B	27	C
13	A	28	A
14	C	29	B
15	A	30	C