CAMBRIDGE INTERNATIONAL EXAMINATIONS

GCE Advanced Subsidiary Level and GCE Advanced Level

MARK SCHEME for the October/November 2013 series

9708 ECONOMICS

9708/22 Paper 22 (Data Response and Essay – Core), maximum raw mark 40

This mark scheme is published as an aid to teachers and candidates, to indicate the requirements of the examination. It shows the basis on which Examiners were instructed to award marks. It does not indicate the details of the discussions that took place at an Examiners' meeting before marking began, which would have considered the acceptability of alternative answers.

Mark schemes should be read in conjunction with the question paper and the Principal Examiner Report for Teachers.

Cambridge will not enter into discussions about these mark schemes.

Cambridge is publishing the mark schemes for the October/November 2013 series for most IGCSE, GCE Advanced Level and Advanced Subsidiary Level components and some Ordinary Level components.

Section A

1 (a) (i) What is meant by hyperinflation? [2]

Hyperinflation is a rise in the prices (fall in the value of money) at an extremely rapid (runaway) uncontrolled rate.

For a general definition of inflation **(1)** and for an awareness of the extreme nature of the rate of the increase in the case of hyperinflation. **(1)**

(ii) Describe what happened each day to the real value of money in Zimbabwe in November 2008. [2]

It declined **(1)** by almost 50% or other quantitative statement **(1)**

(b) Explain how a government may cause hyperinflation. [4]

Governments are responsible for the quantity of money in an economy and are usually held responsible for causing inflation when the money supply is allowed to grow excessively.
The theory underpinning this approach is the quantity theory of money.

The quantity theory can be used to explain that an increase in the money supply will cause inflation. If the money supply increases excessively this could become hyperinflation.

For an explanation of the government's role in increasing the money supply excessively **(1)** and with application based on the assumptions of the model, showing that P should increase proportionately when the money supply increases. **(1)**
For the formula: $MV = PT$ **(1)** with the components accurately explained **(1)**

Other possible causes should also be rewarded e.g. excessive increases in non-funded government expenditure/excessive cuts in taxes **(1)** if developed **(1)**; if government brings in very low interest rates **(1)** if developed **(1)**.

Maximum of 3 marks if no discussion of government impact on money supply.
Maximum of 3 marks if no discussion of hyperinflation.

(c) (i) Account for the shopkeepers' treatment of cheque (check) payments. [2]

A cheque cannot become purchasing power immediately **(1)**, to counter the loss of real value due to hyperinflation the shop keeper demands a premium at twice the original cost **(1)**; for an understanding of the shopkeepers' reaction. **(up to 2 marks)**

(ii) Explain how workers and foreign investors might react to hyperinflation. [4]

For an explanation of how workers might react, e.g. why they may ask to be paid more frequently or in kind **(up to 3 marks)**.

For an explanation of how foreign investors might react e.g. why they might defer investment decisions; if investment falls **(1)** explanation of why **(1)** **(up to 3 marks)**.
The context has to be explicitly hyperinflation for 3 marks.

Must refer to both workers and foreign investors for the full 4 marks.

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(d) Discuss whether the change in Zimbabwe's current account is what would be expected when a country has the highest inflation rate in the world. [6]

For a clear understanding of the changes in Zimbabwe's current account and the reasons for this e.g. increased deficit **(1)**; rise in relative price of exports **(1)**; fall in value of exports **(1)**; fall in relative price of imports **(1)**; rise in value of imports **(1)**; leading to an **increased deficit (up to 3 marks)**.

For an explanation of the way in which the current account would be expected to change given the fact that Zimbabwe has the highest inflation rate in the world e.g. the price elasticity of exports and imports; compensatory falls in the exchange rate; any offsetting government action **(up to 3 marks)**.

A concluding statement. **(1 mark)**.

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Section B

2 In September 2011 the Kenyan government reintroduced price controls to ensure that basic commodities were sold to the citizens at reasonable prices.

(a) With the help of a diagram(s), contrast the impact of a maximum price fixed below equilibrium market price with one that is fixed above it. [8]

This is frequently tested and candidates become confused between the effects of a maximum price above equilibrium and one below.

- For an accurate diagram and explanation of the outcome when price is placed below equilibrium **(up to 4 marks)**.
- For an accurate diagram and explanation of the outcome when price is placed above equilibrium **(up to 4 marks)**.

(b) In view of the problems of allocation that might arise with effective maximum price legislation discuss how these problems might be overcome. [12]

The maximum price might cause an excess demand for the good. This raises the problem with allocation. An alternative means of allocation has to be found. In addition, problems arise in maintaining the maximum price leading to black markets etc.

- For a full analysis of the problems and policies with maximum price legislation **(up to 8 marks)**.
- For an evaluative comment on how these problems can be overcome **(up to 4 marks)**.

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3 (a) Use diagrams to explain the difference between merit goods and demerit goods. [8]

This area often causes confusion amongst students so we are looking for evidence of good understanding of the core concepts.

For knowledge and understanding of merit goods and demerit goods (3/1, 2/2, 1/3 possible splits) i.e. negative externalities (third party effects) associated with demerit goods; positive externalities associated with merit goods; better for consumer then consumer realises so good under consumed and a merit good; worse for consumer than consumer realises so good over consumed and a demerit good. **(up to 4 marks)**.

For application – diagrams showing SMC greater than PMC demerit goods; SMB greater than PMB merit goods (allowance for Q and P/Supply and Demand application see below). **(up to 4 marks)**.

With merit goods P is lower than it should be as does not reflect the true value of the good (i.e. a positive externality) and Q is under consumed in the market.

With demerit goods P is lower than it should be as the true cost is not reflected in the market (i.e. a negative externality) and Q is over consumed.

This could be shown on a demand and supply diagram but the application is unlikely to be sufficient to gain full marks unless there is a full discussion of information failure.

Note: No diagram = 4 marks out of 8 maximum

(b) Discuss whether it would be better if smoking were banned completely or whether it should be subject to an indirect tax. [12]

The approach should be to use the conceptual framework that shows the impact on price and quantity that will occur with each policy. Evaluative comment might include consideration of the correct price i.e. one that recognises all the costs. In addition the question of whether the policies would be evaded might be considered.

- For analysis of the impact of a ban on smoking (up to 6 marks) and the impact of an indirect tax (up to 6 marks) **(up to 8 marks)**.

- For evaluative judgement on the two policies in terms of their impact on consumer welfare and/or the likely effectiveness of each **(up to 4 marks)**.

If no conclusion then cap at 3 marks out of 4 maximum.

4 (a) Explain, with the help of a diagram, how a policy of expenditure dampening in an economy would affect aggregate demand, prices and output in that economy. [8]

- For knowledge and understanding of expenditure dampening (if only fiscal **or** monetary explanation then 3 marks maximum) **(up to 4 marks)**.

- For application – an accurate diagram showing how aggregate demand is affected by expenditure dampening and the impact on prices and output **(up to 4 marks)**.

A maximum of 2 marks if clearly only a micro diagram. However if there are elements of a macro diagram then if the written explanation is correctly macro based, mark out of 4 marks.

Note: No diagram = 4 marks out of 8 maximum.

(b) Discuss whether a policy of expenditure switching is more appropriate than a policy of expenditure dampening in an economy with a large balance of payments current account deficit and a high rate of inflation. [12]

Candidates should have a firm grasp of both expenditure switching and expenditure dampening and how they are expected to work to cure a deficit. In terms of appropriateness of each policy, we expect students to apply theory to make a judgment.

- For analysis of the impact of expenditure switching (6 marks maximum) and expenditure dampening (6 marks maximum) in the specific economic circumstances of a balance of payments deficit and high inflation **(up to 8 marks)**.

- For evaluative judgement on which policy is more appropriate **(up to 4 marks)**.

If no conclusion then cap at 3 marks maximum.

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