

Paper 2

Australia and its Northern Territory

The Northern Territory of Australia is a large, sparsely populated area. It relies heavily on tourism, mining, agriculture and fishing. The extraction of oil and gas and the mining of iron ore and bauxite have grown significantly in recent years. Its manufacturing is principally based on the processing of its natural resources.

The Northern Territory government publishes forecasts, which compare the economic prospects of the Northern Territory with those of Australia as a whole. The table below gives extracts from the forecasts in January 2009.

Table 1: Selected economic forecasts for Northern Territory and Australia

| | Northern Territory | | Australia | |
|--|--------------------|---------|-----------|---------|
| | 2008–9 | 2012–13 | 2008–9 | 2012–13 |
| International exports, constant price (A\$m) | 4172 | 6004 | 176 010 | 236 824 |
| International imports, constant price (A\$m) | 2718 | 2811 | 217 675 | 224 521 |
| Consumer price index, 1989–90=100 | 164.6 | 180.0 | 167.7 | 186.4 |
| Average weekly nominal earnings, A\$ | 954 | 1078 | 916 | 1050 |
| Unemployment rate (%) | 3.7 | 5.7 | 4.2 | 6.5 |
| Population aged 15–64 (thousands) | 170 | 186 | 17 456 | 18 627 |

* A\$ = Australian dollars

Question 1(a)(i)

Calculate and compare the change in the trade balance between 2008–9 and 2012–13 of the Northern Territory with that of Australia. [4]

Mark scheme

Calculate and compare the change in the trade balance between 2008–9 and 2012–13 of the Northern Territory with that of Australia. [4]

Both improved (1), Northern Territory (NT) has an increased surplus (1), Australia goes from deficit to surplus (1), supporting calculation NT A\$1454 to A\$3193, Aus A\$-41 665 to A\$12 303 (2)

Comparative points without accurate calculation can be rewarded, but the points must relate to the 'balance', not the change in imports or exports alone.

Example candidate response

| | |
|--|-----|
| Trade balance of Northern Territory (2002) $24172 - 2718 = 1454$ (surplus) | |
| Trade balance of Northern Territory (2013) $6004 - 2811 = 3193$ (surplus) ✓ | |
| Trade balance of Australia (2002) = $176010 - 217675 = (41665)$ (Deficit) | |
| Trade balance of Australia (2013) $236824 - 224521 = 12303$ (surplus) ✓ ✓ | |
| <p>In Northern Territory, there is an increase in trade surplus which shows that there is their Balance of Payment are and terms of trade are improved. Australia also improved at a greater rate ✓ comparative to Northern Territory, as proved by the figures calculate above. This shows that Australian government had made a significant improvement although Northern Territory also improved but Australia at a greater rate which is due to population ✓</p> | |
| | 2/4 |

Examiner comment

This answer gains full marks. The candidate provides an accurate calculation, although it would have been better if the balances had been shown in Australian dollars. It then goes on to make the comparative points that the balances of both areas had improved and that the balance in Australia had improved at a greater rate.

Mark awarded = 4 out of 4

Example candidate response

| | |
|---|-------------------|
| Trade balance for Northern Territory | |
| 2008-9 | Exports - imports |
| $4172 - 2718 = 1454$ | |
| 2012-13 | |
| $6004 - 2811 = 3193$ | |
| Exports increase in 2012-13 as compared to 2008-9. Trade Surplus. | |
| Australia Trade Balance | Exports - imports |
| 176010 | |
| 2008-9 | |
| $176010 - 217675 = (41665)$ | |
| 2012-13 | |
| $236824 - 224521 = 12303$ | |
| 224521 | |
| In 2008-9 Australia has made deficit but increase in exports over imports make made Surplus | 2 |

Examiner comment

This answer contains the necessary calculation, but fails to provide any comparative comment. As a result the maximum mark available is two. The question clearly asks the candidate to 'calculate and compare'. Careful reading of question requirements is essential for maximum marks.

Mark awarded = 2 out of 4

Example candidate response

change in
2(i-) trade balance of the Northern Territory =

$$(X_2 - M_2) - (X_1 - M_1)$$

$$= (6004 - 2811) - (4172 - 2718)$$

$$= 1739 \text{ m A\$}$$

percentage change =

change in trade balance for Australia =

$$(X_2 - M_2) - (X_1 - M_1)$$

$$= (236824 - 224521) - (176010 - 217675)$$

$$= +53,968 \text{ m A\$}$$

~~Both trade balances~~ ~~increased~~ ~~from 2008-9 to~~
2012-13.

percentage increase for Northern Territory

$$= \frac{6004 - 2811}{4172 - 2718} \times 100$$

$$= 219.6\%$$

percentage increase for Australia

$$= -29.5\%$$

The trade balance for the Northern Territory will increase by 219.6% from 2008-9 to 2012-2013. The trade balance for the Northern Territory will ^{keep} increasing whereas as negative trade balance for Australia will change into a positive one. The percentage increase for Australia will be -29.5% in 2012-13 as compared to the negative trade balance in 2008-09.

Examiner comment

This candidate provides a very confused calculation. In addition there is no real direct, comparative comment. There is some understanding of the meaning of 'trade balance' however and the recognition that in Australia the balance changes from a deficit to a surplus. It was considered to have sufficient understanding for one mark.

Mark awarded = 1 out of 4

Question 1(a)(ii)

Explain why exports and imports are often measured at constant prices. [2]

Mark scheme

Explain why exports and imports are often measured at constant prices. [2]

Constant prices exclude the effect of inflation (1), more accurate in real terms or shows the volume of trade.

Example candidate response

Exports and imports are measured at constant prices in order to ascertain the real growth in the trade balance without the inflation distorting the real balance. It helps the governments ~~understand~~ ^{see see} understand the increase or decrease which would help implement disequilibrium policies. ~~etc etc~~

Examiner comment

This answer gains both marks available. The idea of the 'real growth in the trade balance' and the fact that inflation distorts the real balance shows that there is clear understanding here.

Mark awarded = 2 out of 2

Example candidate response

Exports are the goods sold ~~to~~ abroad and imports are the goods bought from other countries. Using constant prices is better because there're always some changes that influence exports and imports, such as inflation, change of exchange rate. X

Examiner comment

This candidate gains a mark for the recognition that using constant prices is better because of the distorting effects of inflation and a change in the exchange rate. For a further mark the candidate needed to say a little more on why it was 'better'. This could have been for example a statement that the measurement was more accurate in real terms or that it would show the changes in the actual volume of trade.

Mark awarded = 1 out of 2

Example candidate response

Exports and imports are measured at constant prices because they don't relate to any of the other components of the economy. Exports and imports when exchanged are according to the values and price^{of their own}. They are not related to anything else.

Examiner comment

This candidate clearly does not understand the idea of 'constant prices'. An attempt is made to suggest a possible meaning, but with little success.

Mark awarded = 0 out of 2

Question 1(b)

Explain **two** additional pieces of information that would be useful in judging Australia's international financial position. [4]

Mark scheme

Explain **two** additional pieces of information that would be useful in judging Australia's international financial position. [4]

From net income, net transfers, capital account, financial account, foreign reserves, exchange rate, *terms of trade* or alternatives, identification (1), plus 1 mark for explanation of identified point (1)

Example candidate response

Australia's international financial position can be judged by ~~the balance of payment account~~ capital and financial section of the balance of payment account, which shows the capital inflows and outflows of the country. How much investment is done by the foreigners and how much investment is done abroad. For example: a Japanese motor car company setting up a factory in Australia. Or Australian government building a hospital overseas. The Capital and financial account consists of direct investment, portfolio investment flows, other reserves, acquisition/disposal of nonfinancial and nonproduced assets and capital transfer.

Australia's financial position can even be ~~just~~ judged

by the terms of trade, that is, the rate at which a country exchanges its exports for imports. ~~How~~ The quantity of imports that a country can get by a unit of exports. The formula is of ~~the~~ terms of trade is =
$$\frac{\text{Index of export prices} \times 100}{\text{Index of import prices}}$$

Examiner comment

This candidate provides two relevant and additional pieces of information that would be useful in judging Australia's international position. Both are explained with sufficient clarity and detail to ensure full marks.

Mark awarded = 4 out of 4

Example candidate response

| | |
|--|---|
| <p>The terms of trade can be used in the judging the Australia's financial position. Term of trade is the opportunity cost of ^{the goods} import export in terms of export or it is the value.</p> <p>Terms of trade = $\frac{\text{Price of Exports}}{\text{Price of Imports}} \times 100$.</p> <p>If Terms of trade is greater than 100, it is said to be favourable. If terms of trade is less than 100, it is said to be unfavourable.</p> | 2 |
| <p>The current <u>account</u> can also be used to measure the international financial position.</p> | 2 |

Examiner comment

This candidate identifies the terms of trade as an additional piece of information that would be useful in judging Australia's international financial position. The answer then goes on to explain how the terms of trade are calculated. This is worth two marks. The second piece of information identified by the candidate is the 'Current Account'. This fails to score because without elaboration, this is too vague. If the candidate had gone on to identify and explain some items within the Current Account, this would have been acceptable and would have gained further credit.

Mark awarded = 2 out of 2

Example candidate response

| | |
|--|---|
| <p>The Consumer price index shows the rate of inflation in Australia. Inflation have a very important role in the financial position of a country. The Consumer price index of Australia in 2008-9 was 167.7 and in 2012-13 was 186.4. The balance of trade ^{given} can be also be used to determine the financial international position of Australia as calculated above in the part (a).</p> | 0 |
|--|---|

Examiner comment

This candidate identifies the Consumer Price Index and the Balance of Trade as two additional pieces of information. These were not acceptable because both of these were provided in Table 1 and could not therefore be considered as 'additional'. This was a very common error amongst candidates. The most likely cause of this error was a failure to read the question requirements carefully and many candidates gained no marks here as a result.

Mark awarded = 0 out of 4

Question 1(c)

Analyse the change in average weekly earnings in Australia in real terms between 2008–9 and 2012–13. [4]

Mark scheme

Analyse the change in average weekly earnings in Australia in real terms between 2008–9 and 2012–13. [4]

For an understanding of meaning of 'real terms' (1 mark)

Real earnings will rise (1), earnings rise more rapidly than inflation (1), supporting calculation 14.6% v. 11.2% (2)

Example candidate response

The average weekly earnings in real terms would take into account inflation ~~because~~ ^{per} into consideration. The consumer price index (inflation) rose by 11.2% ($\frac{186.4 - 167.7}{167.7} \times 100$) whereas the Average weekly nominal earnings (A\$) ~~rose~~ rose by 14.6% between 2008–~~2009~~ and 2012–13, according to the forecast. So, in real terms, the average weekly earnings (A\$) rose by ~~about~~ about 3.4%. 4

Examiner comment

This concise answer was awarded full marks. The candidate starts by showing a clear understanding of the meaning of 'real terms'. An accurate calculation is then provided showing that inflation rose by 11.2% whilst nominal earnings rose by 14.6%. This was then followed by the correct conclusion that in real terms the average weekly earnings rose.

Mark awarded = 4 out of 4

Example candidate response

In the years between 2008-2009, the average weekly earning in Australia was 916A\$ which in 2012-2013 increased to 1050A\$. This change shows that as the years progressed, the ~~wage rate which can also per week~~ average weekly nominal earnings increased by 15%.

On the other hand, the ~~average~~ consumer price index shows that during the years 2008-2009, the inflation rate was 67.7% and in 2012-2013, it increased to 86.4%. Therefore there was a 28% increase in 2008-2013. This shows that prices rose at a higher rate in Australia.

Analyzing the situation of Australia, it can be said that the average weekly earnings in Australia in real terms decreased. ~~This is because as the nominal~~ Average weekly earning in Australia in real terms refers to the wage rate related to the average price level in the country. As it is shown in the table, the average price level also showed a rise in the year 2008-2013, therefore the disposable income in real terms decreases over the years. In simple words, it can be said that the amount that people earned was equal ^{or lesser than the} to the amount they had to spend ~~or might be less~~.

Examiner comment

This answer showed understanding of the meaning of 'real terms', but unfortunately the candidate was unable to use the data to perform all parts of the calculation. A mark was awarded for the correct calculation of the percentage change in nominal earnings, but there is no figure provided for the percentage increase in prices. This meant that no conclusion regarding the change in real terms could be reached.

Mark awarded = 2 out of 4

Example candidate response

Ans:- Real change = Average weekly earnings - CPI.

Change Earnings:- $1050 - 916 = 134$.

Change CPI:- $86.4 - 67.7 = 18.7$.

$\Rightarrow 134 - 18.7 = \text{As\$} 115.3$.

The real change is dependant on the average weekly earnings, less, the inflation rate. In nominal terms the earnings have increased by AS \$ 134 but at a closer look the earnings have ^{actually} increased by AS \$ 115.3 meaning that the rate of inflation has increased and the value or purchasing power of money has decreased.

Examiner comment

This candidate understands the meaning of 'real terms' and gains a mark for this, however the candidate's application and data handling skills are weak. The candidate does not grasp the distinction between absolute figures, percentages and index numbers and fails to gain any marks for the calculation.

Mark awarded = 1 out of 4

Question 1(d)

With the help of the text and the table, discuss the economic outlook for the Northern Territory.

[6]

Mark scheme

With the help of the text and the table, discuss the economic prospects of the Northern Territory. [6]

Good prospects: trade in tourism (income elastic), minerals and oil, rising surplus, relatively low inflation rate, higher real wages, growth of working population.

Poor prospects: rise in unemployment, dependence on narrow range of production, variable demand, externalities of tourism and mining, lack of sustainability of natural resources.

For the identification of points that could affect the economic prospects of the Northern Territories (2 max.)

For explanation of why the identified points are relevant to the economic prospects. (2 max.)

For comment on the economic prospects of the Northern Territories, for example a reasoned summary or conclusion. (up to 2 marks)

Example candidate response

The text ~~is~~ given ~~above~~ ^{Northern Territory of} prove that, Australia is a developing country and is specialised in manufacturing sectors ~~such as~~ ^{and primary sector} manufacturing such as extraction of oil and gas, mining ores etc. ~~And~~ ^{And} Northern Territory ~~is~~ also tourism one of ^{the} main business (service sector). ~~The~~ The table shows growth in trade balance of Northern Territory ~~from~~ between 2008-9 and ~~2010~~ 2012-13. The consumer price ~~is~~ index ~~too~~ showed as

upward slip from 164.6 to 180.0 (rise of 9.36%). The actual inflation was forecasted to be 8.0% in 2012-13 compared to 1989-90 (base year) which might decrease country's ~~economic~~ international competitiveness and attract less ^{capital} inflows from abroad. Inflation rate is considered to be high and people may lose confidence in money. So, govt. should take the figure seriously to increase country's competitiveness. The Northern Territory's earning in real terms ~~will~~ has been forecasted to increase, which could increase marginal propensity to ~~consume~~ import due to high price of domestic goods. The unemployment rose to 5.7% (4% rise from 2008-9), which could pressure govt. to provide more unemployment benefits. But labour force showed a rise of 9.4% from 2008-9 to 2012-13 which could ~~also~~ increase ~~the~~ Gross Domestic Product and output of country. Although, high dependence on natural resources will affect Northern Territory in long term as the natural resources are scarce and high dependency on them will lead to depletion of resources.

2

2

2

TWT

(5)

6

19

Examiner comment

This answer starts by describing some features of the Northern Territory economy before identifying information provided in the data that would allow a judgement to be made concerning the economic prospects of this area. The surplus on the trade balance, which is expected to grow, is identified. The candidate then provides some inaccurate estimates of the rate of inflation but goes on to explain the dangers of a high rate of inflation. Some good analysis is then provided using relevant economic concepts. The final paragraph provides a valid comment on the danger of the Northern Territories relying upon natural resources which might run out. A rather fuller comment on the future economic prospects of the region would have resulted in full marks for this answer.

Mark awarded = 5 out of 6

Example candidate response

The Northern Territory constitutes a small economy (than Australia). Its main industries lie in the primary sector. The economy relies heavily on agriculture and mining. In other definitions, it could be labelled as a developing economy. According to forecasts and suggested by the text, the mining and extraction industries are growing significantly. In the future, this development could give way to factories and structural changes in the economy, likely to shift towards the secondary sector.

Balance of Payments are satisfactory under the circumstances, with exports significantly higher than its imports. Inflation is also considerably low and stable. This means risk-taking is encouraged and business owners have confidence in the economy.

Employment is low as well, however the situation might slightly worsen according to forecasts. This may as well be structural unemployment due to businesses moving towards secondary sector industries.

2+2+0

12

12

Examiner comment

This candidate identifies and then explains two items of data that could be used to assess the economic prospects of Northern Territory. Good explanations of the inflation rate and the unemployment rate and the significance of each are provided. Marks are lost here however, because there is insufficient attention paid to an assessment of the overall prospects for the region. No comment is provided for example on whether the negative indicators might be more powerful than the positive indicators. This comment might have been supplied in a concluding paragraph in which some evaluative judgement might have been provided.

Mark awarded = 4 out of 6

Example candidate response

Northern Territory as mentioned in the passage is a populated area, which relies heavily on tourism, mining, agriculture and fishing which indicates that it has a lot of industries to earn from as well as from the extraction of oil and gas and the mining of iron-ore and bauxite. It shows a very well developed infrastructure of the Northern Territory of Australia.

According to the table 1. In 2008-9, it has an excess of exports over imports showing a positive balance of payments. Further ahead in 2012-13 its exports increased well enough, and again having a positive Balance of payments showing an increase of 1739. Consumer price Index is a

way of measuring inflation that in 2008-9 it has a CPI of 164.6 and going off a little worse in 2012-13 ~~to~~ ^{to} by an increase rate. In 2012-13 it was 180.0, indicating that inflation rate increased.

Average weekly earnings in 2008-9 was 954 which increased in 2012-13 to 1078, showing a good ~~it's~~ sign. Next is the unemployment rate, that in 2008-9 was 3.7 that rose to 5.7 in 2012-13 which is worse for Northern Territory.

Population aged about 15-64 in 2008-9 was 170 which rose to 188 in 2012-13. This factor is considered with the infrastructure of the country.

Hence the Northern Territory has well economic outlook as per the table given. Not expl

Section B.

2
6
6

Examiner comment

This candidate refers to a very wide range of economic indicators shown in the data. The answer starts with a description of the Northern Territory and then goes on to list the contents of Table 1. The weakness is that none of the indicators are used to answer the question. For example, it is stated that the unemployment rate is expected to rise from 3.7% to 5.7% and that this is 'worse' for the Northern Territory. This is clearly the case, but there is no explanation of why this is so. A simple statement that, for example, a rise in unemployment represents a waste of potential output or that the increase in unemployment benefits represents a drain on government finances would have been sufficient for a further mark here. Explanation of the points identified would have allowed an evaluative conclusion to be reached on the economic outlook of the region.

Mark awarded = 2 out of 6

Question 2(a)

Explain the role that a government should fulfil in a mixed economy.

[8]

Mark scheme

Explain the role that a government must fulfil in a mixed economy.

[8]

A mixed economy is based on private ownership, the profit motive, demand and supply etc. with a role for the government. The role is to provide the environment in which the market can operate successfully. This includes ensuring law and order, national defence, property rights and the provision of public goods and desirable merit goods. It intervenes with taxes, subsidies etc. to influence the behaviour of the private sector and markets and achieve a better allocation of resources.

For a definition of the mixed economy (2 marks)

For an explanation of the role of government in a mixed economy (6 marks)

Example candidate response

A mixed economy is a mixture of planned economy and free market economy. A planned economy is run by the government as it solely ~~make~~ makes all the decisions. However, in a free market economy the decisions are taken by the private sector and the market forces, such as demand and supply. There is very little government intervention, such as to maintain law and order. 2

A mixed economy, being a mixture of both the extreme economies, involve two sectors only, private sector and the government. Private sector is free to make decisions but government when want or feel the requirement can intervene and alter the actions of the private sector to an extent only. (2)

In a mixed economy, private sectors make private goods only. They employ the factors of production according to their wants and decide what to make and for whom to

make, themselves. However their decision is influenced by market structural forces, ~~known~~ also known as the invisible hand, demand and supply. Their aim is to maximise profit.

If the private sector is ~~exploiting~~ exploiting the consumers and charging a high price, government can intervene and apply price ceiling or if the producers are ~~being~~ exploited then price flooring can be adopted by the government.

Government collects taxes from the private sector and use them to make public goods for the people. The aim of the government is to maximise welfare so it could create job opportunities for the unemployed without putting any pressure on the private sector to employ more workers.

Government ~~can~~ can increase awareness of ~~the~~ merit goods and demerit goods and offer subsidies ~~to the producers of merit goods~~ to the producers of merit goods to increase their allocation and impose taxes on the demerit goods to decrease their allocation.

The ~~government~~ government can decide to fix the balance of payments. It has the ability to impose tariffs, place quotas on the imports to improve the balance of payment.

The government can also fix the exchange rate for a limited time as it also affects your balance of payments. If there are high imports the government can ~~devalue~~ ^{revalue} the currency, making it difficult to import and ^{instead} rely on domestic products. On the other hand if the exports are falling then the government can ~~devalue~~ the currency, making your exports cheap and demanded more.

It's the government's job to provide the country with law and order, defence. This will make the private sector secure and will concentrate on their production and will feel free to expand.

Most of times, the actions of private sector are not disturbed by the government and ~~the~~ ^{private sector} feels free to ~~to~~ produce what they

| | |
|--|---|
| want to and how. It's the private sector's choice to decide for whom to produce too. They can give subsidies to to help producers of infant industries. | 8 |
| 2+6 | 8 |

Examiner comment

This is a very full answer. The candidate starts by providing a sound explanation of the mixed economy. The answer then goes on to consider a wide range of roles that the government undertakes in a mixed economy. The comment is made that the role of the government is to maximise welfare and various types of government intervention to achieve this are explained. These include price controls, policy concerning demerit and merit goods, the provision of public goods and the need to ensure law and order so that the private sector can operate.

Mark awarded = 8 out of 8

Example candidate response

Section B.

2 a) The mixed economy consists of ~~be~~ the market economy and the Public ^{Command} ~~Economy~~ sector. The government operates in the public sector, the role of the government is to provide taxes and subsidies, nationalise industries when required, operate through a centralised economy? Provide public goods and prevent market failure through the prevention of externalities by using methods such as regulation and taxes.

The mixed economy also consists of the market economy. The price system ~~and~~ determines this economy as it helps to interpret demand and supply and help also act as a rationing method. The Market economy will usually produce Private goods and consists of thousands of firms and millions of households.

So the government has a huge role to play in the command economy of the mixed economy. However the market mixed economy also consists of the market economy which will usually undermine any government policies.

Not fully clear on 'mixed' 1+4

5

5

Examiner comment

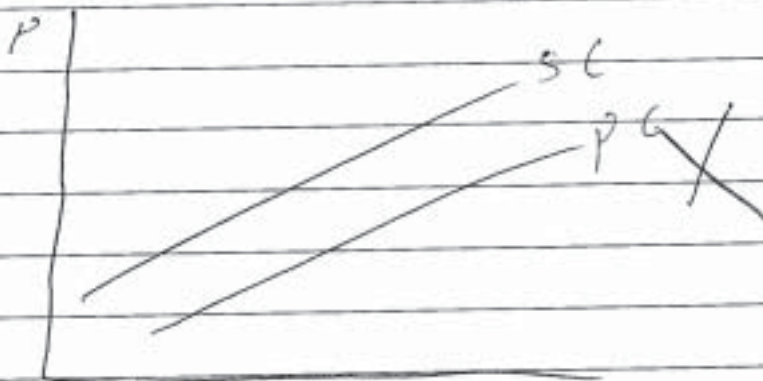
This answer starts with a rather uncertain explanation of the 'mixed economy'. It then continues with a number of reasons for government intervention, which are valid, but left insufficiently explained. The answer ends with a very confused concluding paragraph.

Mark awarded = 5 out of 8

Example candidate response

Mixed economy is defined as an economy which is controlled both by private individuals and by government. It is the most realistic type of economy in today's world as relying solely at government might make the economy inefficient and private individuals would ignore social cost.

The government should play a vital role in a mixed economy as private individuals just aim at maximizing profits which might mean that they might even provide harmful goods and ignore negative externalities.

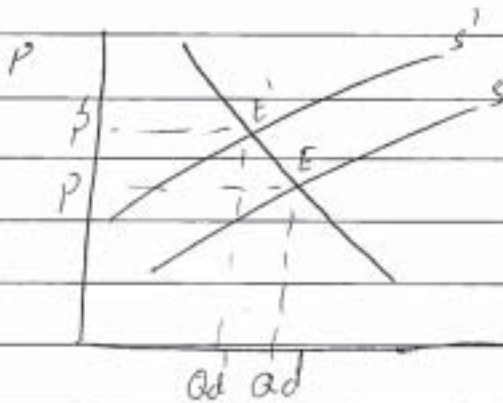


ad

The above diagram shows negative externalities as ~~social~~. Negative externalities are the harmful third party effect which might arise from business activity.



Government role should be to control the negative externalities and to provide public goods and merit goods which private individuals do not provide as it is not profitable to do so. Government can impose taxes on the goods which create negative externalities.



Imposing a tax will make the supply curve shift from S to S' and this will raise its price which will discourage people from buying it unless it has inelastic demand.

Government can also keep control on Multinationals which might be running a monopoly and exploiting the consumers. The Government can do this by maintaining strict law and order.

| | |
|---|---|
| so in my view government should keep a check and balance in the economy through taxes and subsidies rather than trying to provide all the goods itself. | 4 |
| 1+3 | 4 |

Examiner comment

This candidate produces quite a weak answer. There is no clear explanation of the meaning of the term 'mixed economy' provided at the start of the essay. The role of the government is considered very briefly and there is a limited range in the reasons for intervention considered. The structure and content of the answer are both limited and a middling mark is the result.

Mark awarded = 4 out of 8

Question 2(b)

Discuss the accuracy of the definition of public and merit goods as 'goods that must be provided by the government'. [12]

Mark scheme

Discuss the accuracy of the definition of public and merit goods as 'goods that must be provided by the government'. [12]

Public goods are non-rival and non-excludable such as street lighting. Merit goods are goods underprovided by the market system. The consumers lack full information of the consequences of non-consumption. This might include healthcare and pension provision. Although the government provides public goods because it is not possible for the market due to free riders, merit goods are supplied to a greater or lesser extent by private providers. The government also provides other goods and services which are neither public nor merit goods. The definition fits public better than merit goods but is inadequate in itself.

For an understanding of public goods and why they are provided by the government (up to 6 marks)

For an understanding of merit goods and why they are provided by the government (up to 6 marks)
(10 marks max.)

Discussion of the accuracy of the definition. (4 marks)

Example candidate response

Public goods are only provided by the government, example being light house, defence, traffic signals and roads. They have the characteristics of non-~~excludability~~^{rivalry} and non-excludability. ~~Non-excludability~~
~~Non-rivalry~~ means that consumption by one individual does not ~~at~~ reduce the amount available to others. Non-excludability means that no one is excluded from the consumption, not even those who have not paid for it.

Public goods are provided by the government as private sector is not willing to produce it.

As no one is willing to pay for it due to the non-excludability, there is no proper demand registered thus private sector is not interested in making them. ~~That~~ Non-excludability and non-rivalry gives birth to the problem of 'free-rider'. Thus the government takes the responsibility of

5 0

providing it to the ~~co~~ people.

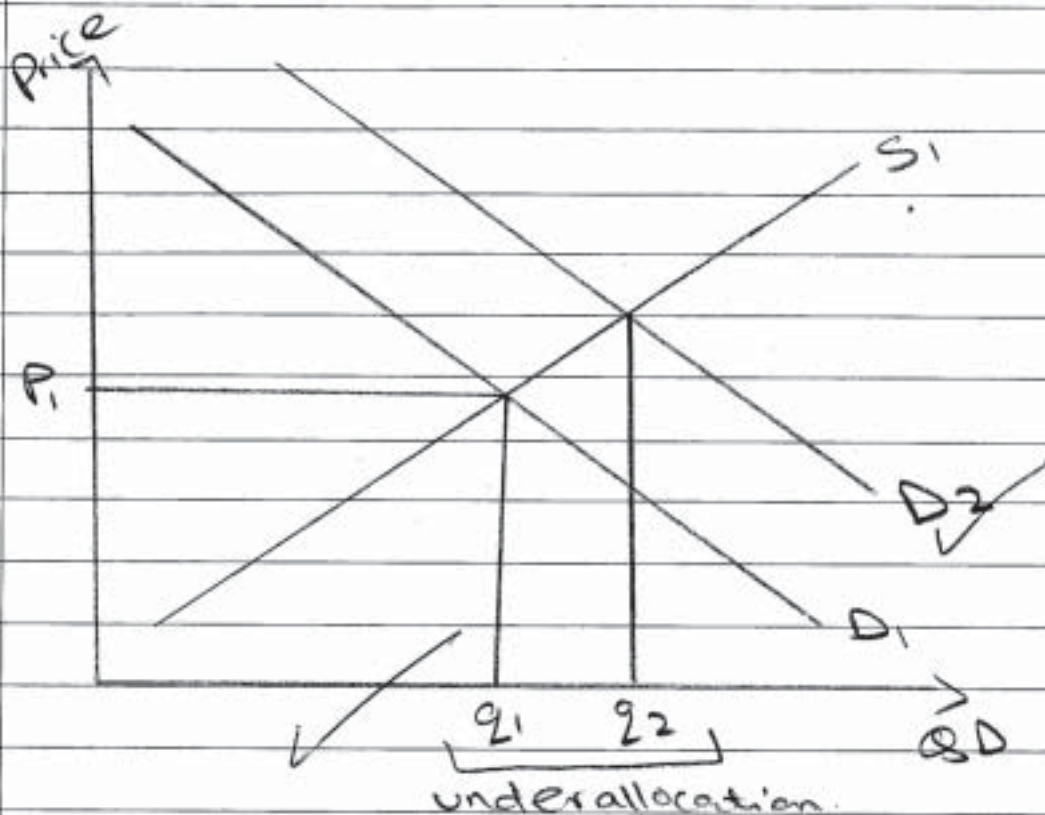
Merit goods are goods which ~~are~~ ^{more} good for the ~~hand~~ benefits than the consumer realises, thus are demanded less. There are positive externalities associated to them. Examples being, ~~the~~ education and healthcare.

Merit goods can be provided by the government but even the private sector will provide it. This is because there is a proper demand registered to it, people pay for these services and thus profits can be earned. Unlike public goods merit goods do not have non-excludability and non-rivalry associated to them. If a surgeon is operating a person, the same surgeon cannot operate another person at the same time so non-excludability is not associated to them.

If medicines are bought by an individual then the quantity ~~is~~ ~~not~~ available for others is reduced.

What government does is that it increases the awareness

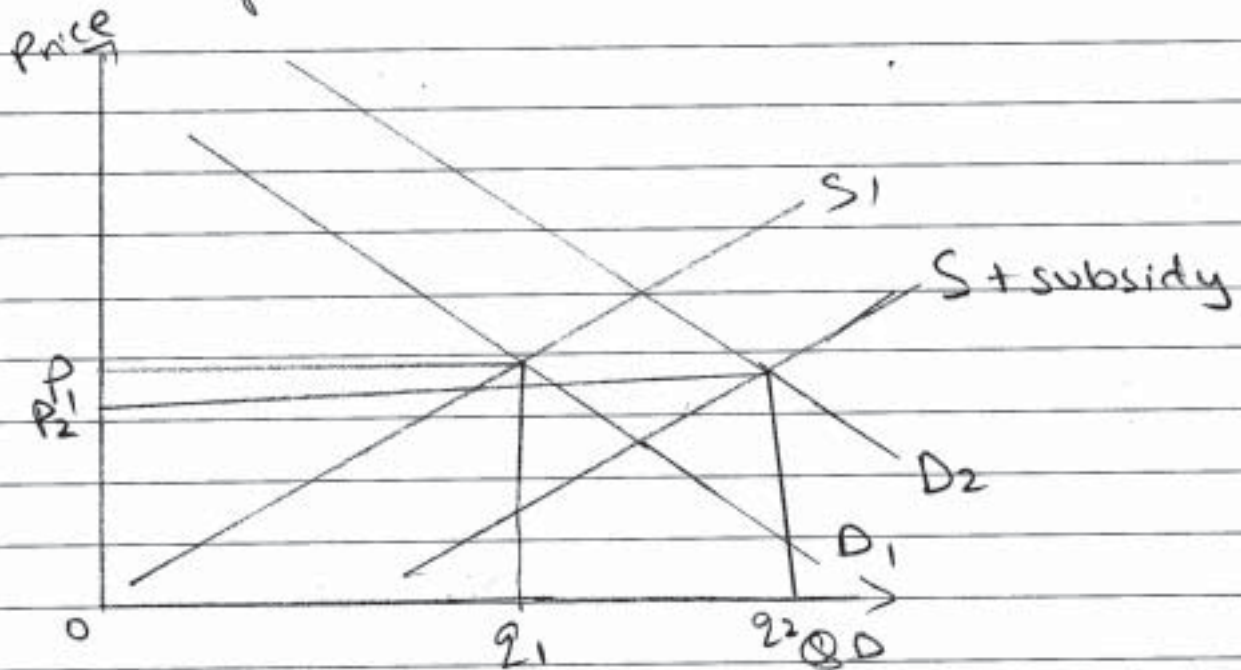
and allocation of resources ~~to~~ needed to provide merit goods.



demand of

Initially the merit goods ~~were~~ ~~demanded~~ is represented by 'D' and the supply by 'S'. Now the government thinks that they should be ~~more~~ consumed by the individuals more as they are good for them. So the government increases awareness by advertising and the demand curve shifts from D_1 to D_2 . This increases the quantity demanded from Q_1 to Q_2 . This tells that before it was underallocation of resources.

needed to produce this. Another method used to increase the ~~needs~~ allocation of resources and the product is to provide subsidies to the producer.



Before the demand had risen to D_2 and now after the subsidy the supply curve shifted ~~from~~ to rightwards. This increased the quantity consumed further and the price also came down. Now of merit goods will be consumed.

12

12

5+5+4 capped max

20

20

The government provides the public goods solely and only helps in increasing the allocation of merit goods. It does not produce them solely.

Good answer

Examiner comment

This is an excellent answer. The features of public and merit goods are each explained in sufficient depth. It is clear that the candidate has a firm grasp of each type of good and can distinguish between them. This allows the candidate to consider whether each 'must' be provided by the government. The view reached on each type of good is clear and this is confirmed in a brief conclusion.

Mark awarded = 12 out of 12

Example candidate response

A Public good has the features of being non-excludable, which means once a person has purchased a good other people will also benefit from it and of being non-rival, which means as more people consume the product the benefit provided to those people who ^{purchase} consumed the product will not be diminished. A Merit good is defined as something which provides benefit to people e.g. education, but they do not possess the right amount of information of these goods.

The government usually provides public goods such as defence, as there are not sufficient resources to produce these goods in a market economy, the features of non-excludability and non-rivalry result in the free rider problem which means consumers benefit from those goods that belong to others rather than purchase their own good. This results in insufficient resources being devoted to a product and results in market failure. The government will establish regulation to help

4 2

prevent Market failure.

Merit goods such as education usually result from the failure of information. As people are not provided enough information for the good, this usually results in underproduction of a product which means there will be a decrease in demand and reduction in supply. This will cause a build up of stocks and eventually cause the Market to fail. The government will usually provide subsidies to increase production and prevent Market failure.

So Government intervention in Public and merit goods is necessary as it helps prevent Market failure and improves the economy.

4+4+1

Reasonable and with a ref to Q in last para albeit 'hedging bets'

9
9

14

Examiner comment

This answer contains evidence of an understanding of the main features of public and merit goods and gains marks for this. It would have been awarded further marks if the question had been answered more convincingly. A crucial point has been missed. This is that the government 'must' provide public goods because the free rider problem, which is mentioned by the candidate, means that private firms cannot charge a price and as a result cannot make profits from their provision. A more assured explanation of this point would have meant that the candidate would have provided a much more convincing answer to the question set.

Mark awarded = 9 out of 12

Example candidate response

Merit Public

Public goods are basically those goods which have main two qualities in it. It should be non-excludable which means if the person benefiting from it does not have the full awareness of the benefits provided to them, secondly the good should be non-rivalry - means that the type of good which is being provided could not be provided by any other organisation. e.g. streetlights or infrastructure.

On the other hand merit goods are those goods which are

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number of the
question in
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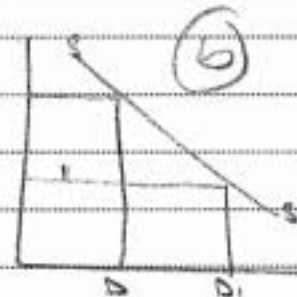
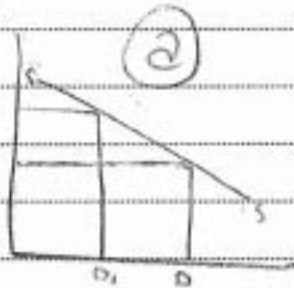
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4

* These types of goods have positive externalities.

excludable - means the person paying for the good can exclude others and get benefit alone and there are competition in the market. For example education as the person paying for the good is only benefiting from it.*

But there is another part which are demerit goods. These goods are also excludable and there is competition available. For example smoking or cigarettes. As the person paying for the pack is able to benefit but in this type of goods there are negative externalities means which have bad effects on the society or the person in long-term.



Above diagram (a) represents the ^{supply} availability of merit goods but because of the lack of awareness population is not attracted towards it and government resources are getting wasted because they are not utilized properly. Diagram

Diagram (b) represents demerit goods of which supply is constant but demand is getting higher day by day.

Next comes the "goods that must be provided by the government" the authority of providing certain types of goods like "defense", "infrastructure" and "education" must be provided by government. As the decisions made for the defense should not get into private hands because of national security. On the other hand infrastructure should be provided by government because the public as a whole is benefiting from it as the standard of living is improved which automatically increase the Gross Domestic Product (GDP) of the country. Then there is the education which must be provided by government because this which benefit the economy as there will be more advanced and educated people. Therefore the literacy rate of the country will rise. There will be more opportunities for jobs and less crimes and people would have the standard living. This will also raise the reputation of the country as there would be litered population which could represent the country in abroad.

2+0+0
Little of relevance to meow.

not related to public goods.

2

2

9

9

Examiner comment

This is a very poor answer that displays a complete lack of understanding, together with very poor exam technique. The candidate starts by stating that public goods are non-excludable and non-rival. This is correct, but it is clear from the explanation provided of each feature that the candidate has tried to learn these terms rather than understand them. This lack of understanding continues in the candidate's explanation of merit goods. It is correctly stated that these goods are excludable and that they have positive externalities, but these features are not explained sufficiently, nor are they used to answer the question about government provision. The answer then drifts into irrelevance with an explanation of demerit goods and some quite general comments on the benefits of for example education.

Mark awarded = 2 out of 12

Question 3(a)

Using economic analysis, explain the possible causes of the increase in the sales of electronic goods, such as mp3 players, in recent years. [8]

Mark scheme

Using economic analysis, explain the possible causes of the increase in the sales of electronic goods such as mp3 players in recent years. [8]

Influences have come from both the demand and supply side. Rising incomes, advertising, changing fashion and tastes have increased demand. Innovation, the introduction of new and improved products and the lowering of costs have increased supply. The fall in the price of the goods has resulted in an extension of demand. More are being sold at lower prices.

| | |
|--|---------|
| Understanding the significance of demand and supply | 2 marks |
| Explanation of demand and/or supply changes (up to 3 marks for each factor explained) | 6 marks |

Example candidate response

question in its margin

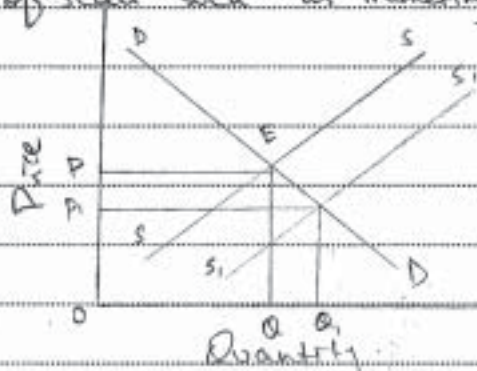
13

Q3 a)

Answer There has been a massive hype in the production and sales of electronic devices such as phones, mp3 players, iPods etc. There are innumerable reasons for this boom in the electronics industry.

Firstly, it is the taste ^{and trends} of consumers that have changed. Earlier tape recorders and CD players used to serve the purpose of mp3 players but as these are more durable, ~~of~~ better quality, ^{portable} and have a much larger storage capacity there has been an increase in production to meet the demand of the consumers. In this modern era people prefer quality ^{and} capacity the most which the mp3 players provide.

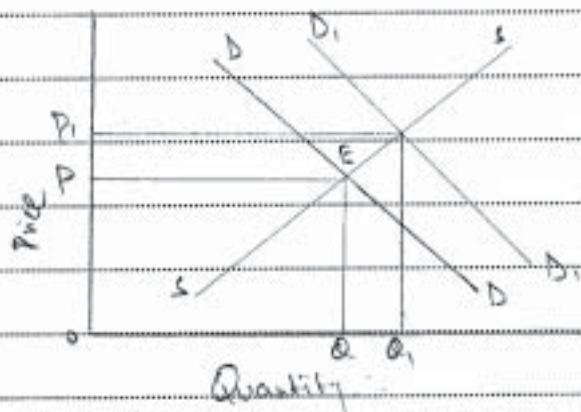
The increase in the amount of capital intensive production methods is another reason for the increase in the sales of such devices. With growing technology goods can be produced which are much more cheaper, portable and of a very high quality. Firms take advantage of economies of scale such as marketing, financial etc which ^{stem to produce goods at low prices.} ~~challenge~~



The graph shows that the equilibrium is at E with price 'P' and quantity Q. With the introduction of technology the cost of production decreases

shifting the supply curve from S to S_1 , lowering the price and causing the consumer to Demand more at Price P_1 with quantity Q_1 .

~~Mp3 players~~ Their substitutes play an important role in this hype. The substitutes for MP3 players are devices such as iPods, iPhones, mp4 players etc which are significantly cheaper. Everyone listens to music. With the tape recorder outdated, people tend to use these digital devices which are cheaper than their substitutes. An mp3 player costs around Rs. 1,500 - 2,000 while an expensive iPod costs around Rs. 8,000 - 10,000, over 5 times the price!



The graph shows that the rising prices of ~~the~~ substitutes cause a rise in demand for mp3 players with original price at P and quantity at Q the quantity rose to Q_1 causing the price to move to P_1 .

Another reason for this could be the increased spending by the people and the increase in aggregate demand. As people have more money their demands for luxuries ~~has~~ rise by a margin thus causing situations that are similar to this.

These are the major reasons for rise in sales of mp3 players. As people demand more to satisfy their wants the suppliers supply more to make large amounts of profits. ✓ 8/

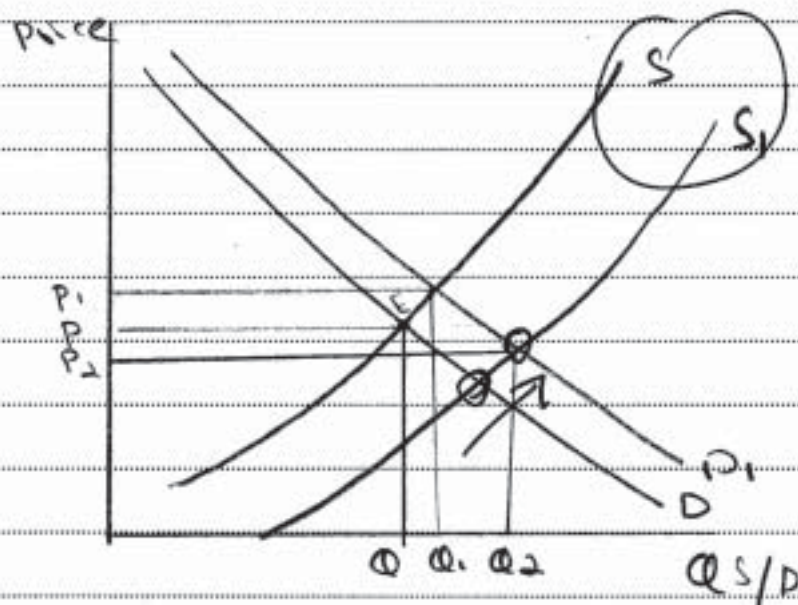
Examiner comment

This is a very good answer that displays a good grasp of the required supply and demand concepts allowing a very successful analysis of the possible causes of the increase in sales of electronic goods. Diagrams are accurate and the examples provided of a possible increase in demand and increase in supply of these products are valid and appropriate.

Mark awarded = 8 out of 8

Example candidate response

The demand for the electronic goods have caused its sales to rise. The demand of such goods ^{might have} increased because of competition, the competition between the firm led to a decrease ⁱⁿ prices of such goods. The increase in competition might have caused because of increase in demand, as Demand curve shift, the prices of the electronic goods rise, which invited new firms to enter in the market ~~and~~ which eventually increased the supply of such goods.

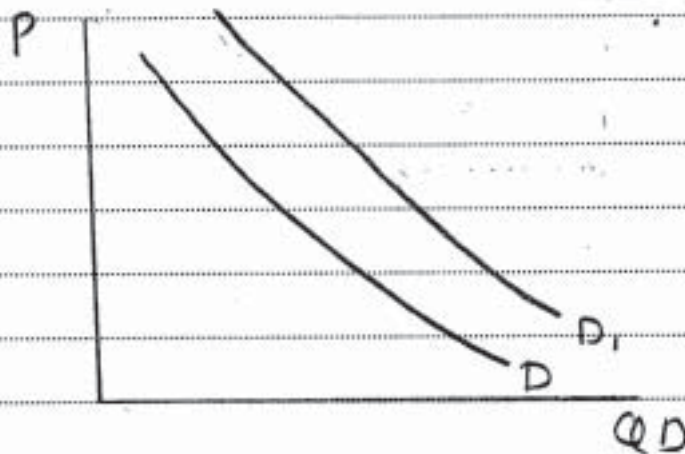


Initially, the eqb was at point E, then an increase in demand caused demand curve to shift, which increase the price to P_1 and increased Q to Q_1 . Because of higher prices, new firm entered into the market and caused supply to shift to S_1 and eqb qty to Q_2 and price to P_2 .

The increase in ^{supply} demand might have caused because of decrease in cost of production. The electronics goods are designed in countries like UK ~~and other~~ developed countries, but are sent to job assembly

in China because of cheap labour. The decrease in cost of production might ~~have~~ have caused prices to fall, which led to an increase in demand.

The increase in the sales might also have caused because of increase in ~~Advertising~~ Advertising. The Persuasive Advertising shift the demand curve ~~sightwards~~.



In recent years, the consumers preferences and tastes have changed. They are diverted more towards luxuries. So ~~and~~ a change in preference might also have caused demand to shift.

The increase in sales ~~was~~ might also have led because of an increase in the ~~income~~ income of consumers.

The state of preference of consumers might have changed, which means that the things which were ~~now~~ called luxuries ^{before} might now be necessities for consumers now.

needs application to be clearer
2+2+2

6
6

Examiner comment

This answer contains some quite valid comment on the possible reasons for the increase in sales of electronic goods. Supply and demand curves are outlined and there are suggested reasons offered for shifts in both the demand curve and the supply curves. Some of the explanation provided is incorrect however and fails to score as highly as it could.

Mark awarded = 6 out of 8

Example candidate response

1. Products are divided into two groups inelastic and Elastic products. Products like Electronic such as MP3 Player are Elastic Products.

Increase in the elasticity sales of electronic goods can be due to change in Price and Income in Price.

Price elasticity of Demand measures the degree of responsiveness of quantity demanded towards a change in Price - $\frac{\text{Percentage change in quantity demanded}}{\text{Percentage change in Price}}$ NAQ

| Price | Electronic goods demanded |
|-------|---------------------------|
| 10 | 100 |
| 8 | 150 |

AS A change in Price of electronic good will increase its sales revenue because ~~will demand~~ demand increases if prices are reduce. In Elastic products such situation will occur.

Other factor for increase in sales revenue will be high incomes because consumer spending Power will increase and they will demand for luxury.

Income elasticity of Demand measures the degree of responsiveness towards of quantity demanded towards a change in income of consumer.

$\frac{\text{Percentage change in Quantity demanded}}{\text{Percentage change in Price}}$

| | |
|--|-----|
| When income increases consumers will move towards luxury products. Income of consumer had been increase so they want to enjoy the luxury of electronic goods this increases the sales revenue for such products. | |
| Advertising can be another factor which made desire in consumer to buy the product. | |
| Sales revenue will increase in the situation when demand increases and capability to buy in high than revenue of such products will increase. | 2 |
| | 2 |
| | 0+2 |

Examiner comment

This is a weak answer. It is poorly focused and contains irrelevant material. The candidate seems aware of factors that affect sales, such as advertising and the price of the product, but there is no development of a supply and demand framework within which the answer can be delivered. As a result the candidate scores for one or two points made in a disorganised framework.

Mark awarded = 2 out of 8

Question 3(b)

Suggest **two** possible reasons why a government might increase the indirect tax on such goods and discuss, in light of these reasons, the likely effectiveness of such a policy. [12]

Mark scheme

Suggest two possible reasons why a government might increase the indirect tax on such goods and discuss, in the light of these reasons, the likely effectiveness of such a policy. [12]

Possible reasons include raising revenue to finance government expenditure, cutting the purchase of imports to help the balance of trade. It might be argued that the products are demerit goods because of the harm to hearing and disturbance to others. An indirect tax is imposed on spending and raises the price of the good. PED measures the responsiveness of demand to a change in price and affects the impact of an increase in an indirect tax. A tax will best reduce the quantity imported when demand for imports is elastic as there will be a more than proportionate fall in demand. To raise revenue it is better for demand to be inelastic so that the fall in demand is less than proportionate to the price rise. The effectiveness of internalising the negative externality will depend upon setting the tax at the appropriate rate.

For a definition of indirect tax (1 mark)

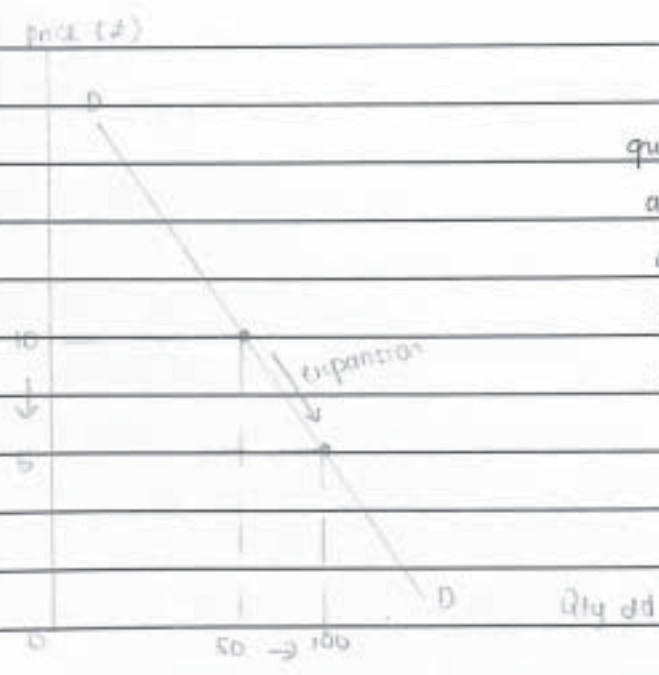
For an explanation of one reason for an indirect tax and a discussion of 'effectiveness' (up to 6 marks with 4 max. if only one element is considered)

For an explanation of a second reason for an indirect tax and a discussion of 'effectiveness' (up to 6 marks with 4 max. if only one element is considered)

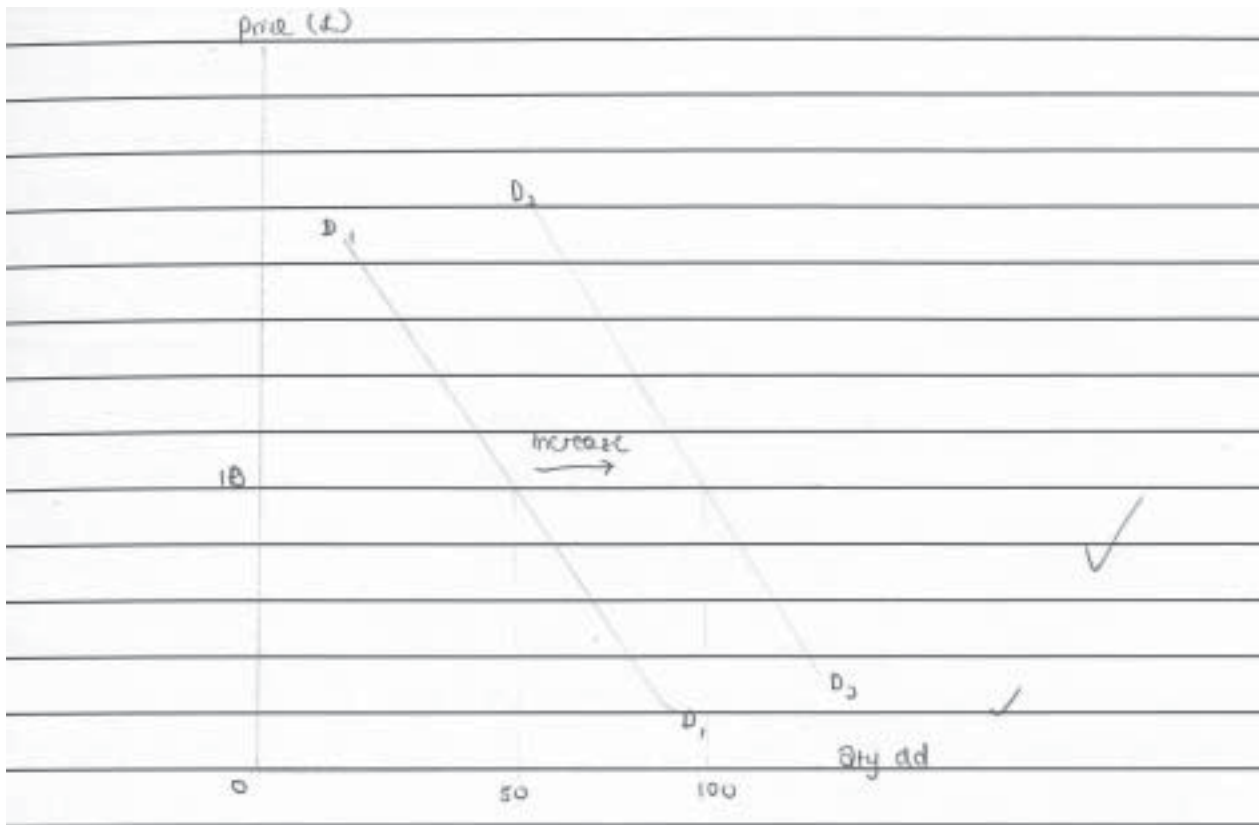
Example candidate response

3. The ~~current~~ market trend of goods and services may ~~show~~ have shown rapid changes ~~depending~~ influenced by several factors. The market interact by the forces of the demand and supply in the market. Demand is defined as the quantity demanded of a product that consumers are willing and able to buy at various prices per period of time, ^{where} ~~per~~ ^{period}. Electronic goods have seen a change in trend of demand where 50 years back, electronic devices are seen as luxury goods and recently, electronic devices are considered as one of the ^{preference} normal necessity goods especially among the young generations.

There are several factors that ^{causes} affect the ^{increase} ~~change~~ in demand sales of electronic goods. According to ~~the~~ normal law of demand, the quantity demanded will rise as price fall. ~~Dem~~ This is shown by an expansion along the ~~same~~ demand curve and it is ~~solely~~ affected by the fall in price. However, there are other factors that may affect demand. When electronic devices are concerned, the major factors that causes this increase may be the technology and change in consumer's taste ~~and~~ in favour of electronic devices. The other reason that contributes may also be ~~a~~ influence from the advertisement by the media. This factors causes a ~~the~~ parallel rightward shift in demand curve.

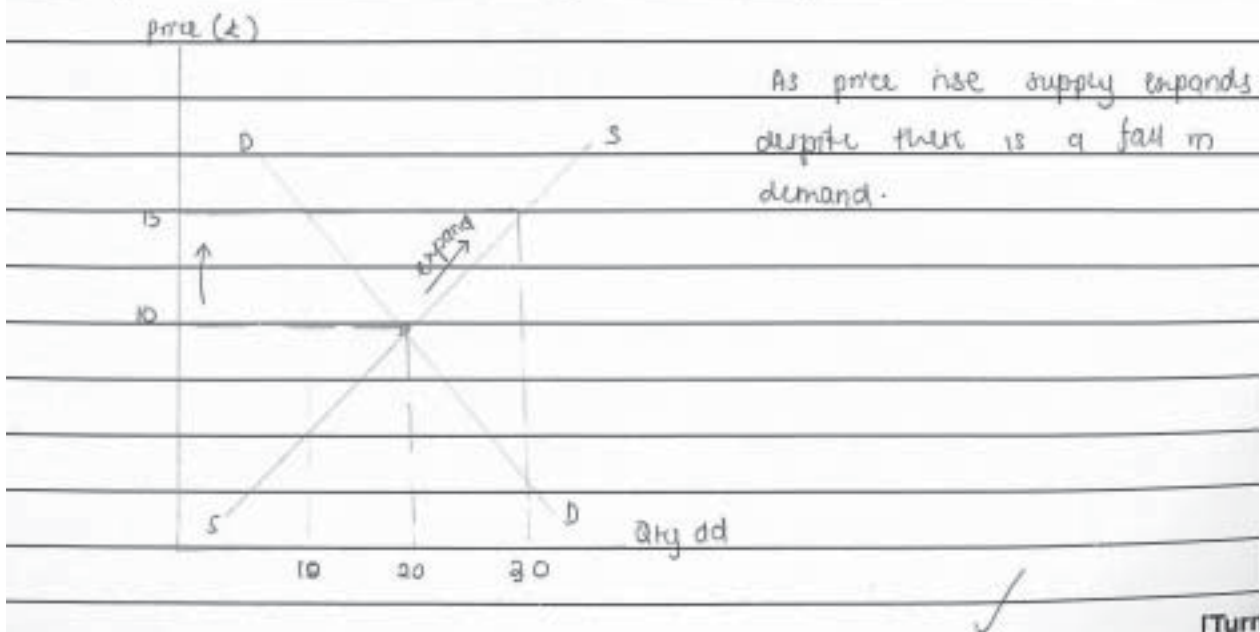


The ~~or~~ expansion of demand quantity demanded may also be affected by the price elasticity of demand. The more elastic it is the, more significant change may be observed as price fall.



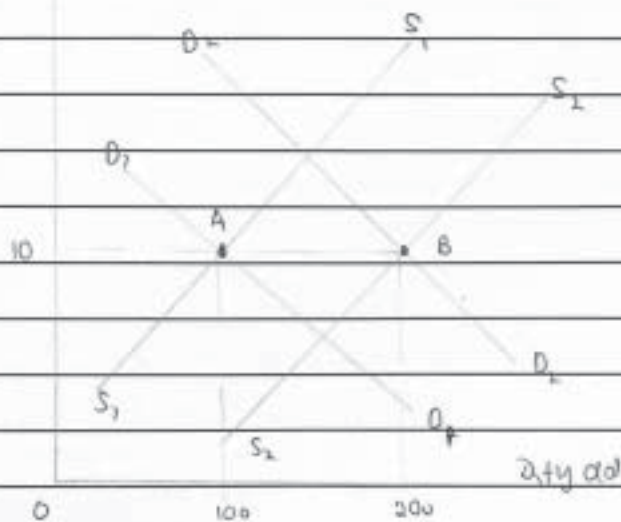
The shift in demand curve as shown by the graph is not affected by the price. But other factors such as trend, consumer price of other goods (substitute and complement), festivals and others.

Analysing the supply side of the electronic devices, the increase in supply in the market by be significant by the increase in price. This is seen by the expansion of supply curve as ~~demand~~ ^{price rises} expands. This is because a rise in price may be a form of incentive for producer to produce more.



Supply too may shift leftwards due to other reasons other than price. There may be a development in technology that occur in the electronic device market for instance, that causes supply to shift right. Supply defined as the quantity ~~of~~ of a good

Price (£)



that producers are willing and able to supply at various prices per period of time, ceteris paribus.

At point A, the initial equilibrium of the demand and supply which may be 50 years back when technology was not well developed. But as technology changes advanced and the consumer preferences favour the electronic devices, there is an increase in both demand and supply. Thus, a new equilibrium formed at point B. ✓✓

Despite the shift in ~~both~~ both curves, the price remain unchanged as it is proven there are other contributing factors other than price that effect the sales of electronic goods. This may be due to change in technology mainly and the change in consumers taste. Advertisement also contributed in this ~~to~~ drastic evolutions. Another factor from the supply side that affect the demand is the business strategy and management. For example, the new CEO of Apple corporation ^{Steve Jobs,} had managed to boost the sales of Apple product a few times more than previous years.

Government policy to encourage the usage of technology also contributed to the increase in sales of electronic

[Turn

| | | | |
|------------------|---|-------------|-------------------------|
| | goods - As the usage of information technology is encouraged | | For Examiner's use only |
| b) g) | in studies education and globalisation, government may subsidise the devices for schools and offices, which increases sales of the device. ✓ | 1 | 11 |
| | | 2 + 6 (max) | 8 |
| | | 2 + 6 | 8 |

Examiner comment

This candidate clearly identifies two reasons for the imposition of an indirect tax. Each is explained clearly. Although the second reason identified has the effectiveness of the tax examined, the first reason does not consider this aspect of the question. The question clearly states that effectiveness should be considered, so marks are lost and the mark awarded less than it could have been.

Mark awarded = 8 out of 12

Example candidate response

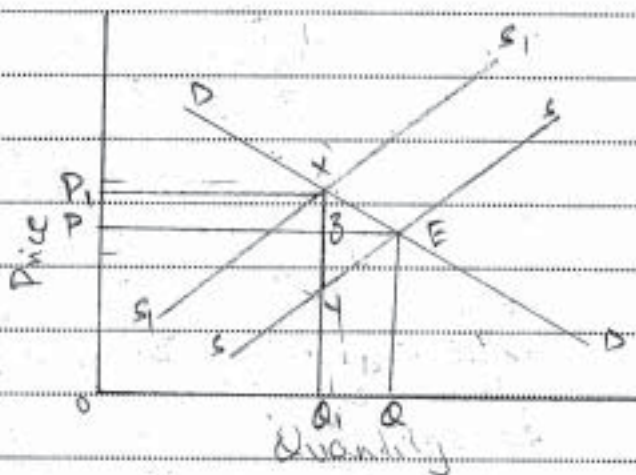
Answer - There are a number of reasons why a government may use protectionism such as high tariffs, quotas or increase the amount of indirect taxes.

Demand pull inflation is a major reason. It is defined as the rise in demand for goods which causes the prices to inflate, that is to say, too much money chasing too few goods. With a large amount of money in the hands of people their demand for luxuries tends to increase.

This type in the buying of unnecessary items causes the prices to rise thus resulting in inflation.

With the introduction of a ^{tax} ~~price~~ the prices of such goods increase. The ^{increment} ~~cost~~ of production causes the producers to reduce their supply that causes a rise in price thus lowering their quantity demanded. In addition to this, luxuries have an elastic demand. So, if the price rises the quantity demanded decreases. The people who still continue to buy such expensive luxuries pay large sums of tax to the government which adds to their revenue which can be spent on economic

development.

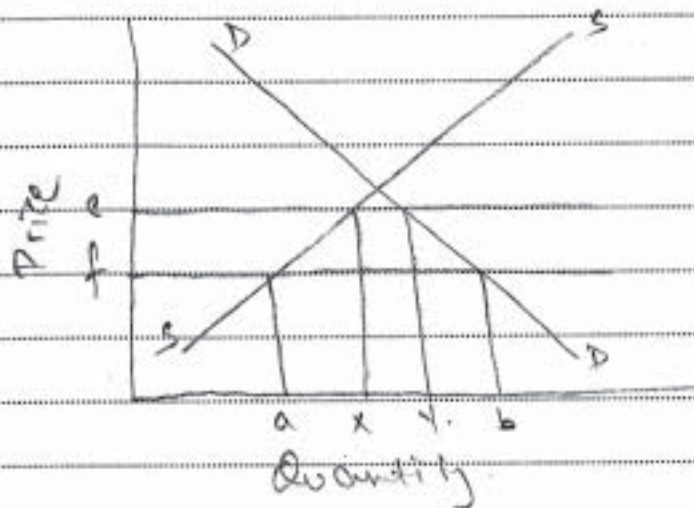


The graph shows the original quantity demanded equilibrium at E with price P and quantity Q . As a tax of XY is imposed the price rises to P_1 , reducing the quantity demanded to Q_1 . As the demand is inelastic most of the tax (XY) is borne by the ~~consumer~~ producer. XZ is by the consumer and ZY by the producer.

A balance of pay

A trade account deficit is another major reason. The trade account comprises of all the visible and invisible the imports and exports of a country. ~~As~~ If the goods ~~are~~ produced in foreign countries are cheaper and of a better quality people tend to ~~try~~ import the goods rather than consuming the local production. The increase in unnecessary imports ^{may} cause a balance of trade deficit leading to a balance of payment deficit thus depleting the countries foreign reserves. This causes depreciation of the country's currency.

or currency leading to unemployment, inflation etc. Hence, by taxes the prices rise causing the demand for goods to decrease. Those who still consume pay taxes to the government increasing their revenue, making economic development possible.



The graph shows the imports and exports getting affected. The gap between demand and supply is filled through imports. With a tax of ef the demand for imports falls to xy . This is due to rising prices.

Hence the imposition of taxes will cause a major effect to the economy. It will benefit it, making the economy prosper. $1+1+3=5$



Examiner comment

Candidates were asked to identify two possible reasons for the imposition of an indirect tax. This candidate is unclear on the possible reasons. The reference to demand-pull inflation is confused. There seems to be a recognition that indirect taxes can raise revenue, but this is not developed. Similarly, the explanation of a trade account deficit is not fully clear. In terms of effectiveness, it is correct to refer to the price elasticity of the taxed profit, but this candidate does not apply the concept successfully. The answer also fails to define or explain, 'indirect tax'.

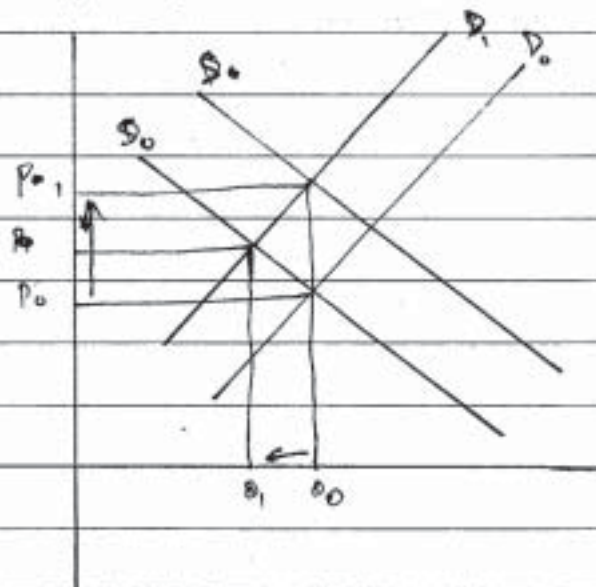
Mark awarded = 5 out of 12

Example candidate response

The Government might increase indirect taxes due to following reasons

- (i) To In order to decrease the demand of ~~the~~ such goods
 (ii) In order to prevent itself from budget deficit. Reason?

By increasing the indirect tax on firms producing such goods, firms may pass this tax to the customer and may charge high prices and hence it will reduce demand; however it also depends on the elasticity of demand of that particular good. If the good has elastic demand a small increase in price will lead to a large decrease in quantity demanded and if the product has inelastic demand a large increase in price will lead to a small increase in quantity demanded. The likely effectiveness of such a policy can be increasing investment as fewer amount of money will be spend on luxury items or this may ~~the~~ increase the saving dependig on the interest rate.



less quantity will be demanded on high prices and less will be supplied on high prices

The increase in indirect tax may result the individual with the higher disposable income at the end of month? As fewer amount of money will be spent on luxury items and this may lead to better standard of living. By increase the tax it also provides more equal dis distribution of income.

The govt may increase indirect taxes in order to achieve prevent it self from budget deficit ~~revenue~~. By increasing the ~~to~~ taxes it will limit the wants of consumer and this will reduce the aggregate demand of consumers which means imports are less and exports will be high. as well as budget and this will result in budget surplus however in a long run currency of the country may depreciate. Because continuous budget surplus will make the ^{imports} exports expensive for ~~ath~~ exports expensive and imports will be less ~~eg~~ expensive which will result in depreciation of currency.

0+2+1

Lack reengagement.

3

3

4

4

Examiner comment

This candidate identifies two valid reasons for an increase of an indirect tax, although one reason is not expressed very well. The supporting analysis is confused however and fails to answer the question set. The diagram is incorrect and there is considerable irrelevance. This suggests that the candidate lacked the necessary knowledge and understanding to attempt this question.

Mark awarded = 3 out of 12

Question 4(a)

Explain why the successful operation of the division of labour depends upon the use of money. [8]

Mark scheme

Explain why the successful operation of division of labour depends upon the use of money. [8]

Division of labour involves dividing the production process into a series of stages. This leads to more specialised outputs which are not necessarily final products. Trading these in a barter system would be difficult, inefficient and probably impossible. Money, anything that is generally acceptable as a means of payment, can act as a medium of exchange and a unit of account, so enabling trade to take place and making division of labour effective.

Understanding of division of labour and money 4 marks (one only 3 max.)
Explanation of the link between the functions of money and trade 4 marks

Example candidate response

Modern day production is based upon the principle of division of labor. Division of labor is a process which is accompanied by specialisation where the workers do that tasks they are good at. This is time saving and efficient. The division of labor has been further promoted by the use of money as a medium of exchange.

In old times when the concept of money was not introduced, people used to rely on barter system to carry out their daily transactions. A farmer would take his sack of wheat and go into the market to buy some tools in return. Barter was time and time consuming and depended upon the double coincidence of wants. It discouraged division of labor and specialisation because people only exchanged complete goods eg, A worker who specialised at making wheels couldn't exchange them for a sack of wheat, he could only get wheat if he had a whole cart not just the wheels. Thus barter discouraged division of labor.

With the advent of the use of money as

The medium of exchange, the concept of division of labor became more common. A chair manufacturer who used to make 5 chairs a day now made 20 chairs a day by employing division of labor. Workers can now do the tasks they are best at and get paid for them.

Successful operation of division of labor depends upon the use of money because money makes the process of economic transactions smooth by eliminating the double coincidence of wants. The employer does not have to pay his workers different commodities eg) if division of labor was in barter then the employer would have to reward one worker with wheat, the other with rice and so on. Whereas, now with the general acceptability of money workers can be paid simply in money because it is now a medium of exchange and a unit of account and they can buy the commodities they desire with that wage they earned.

Also the use of money as a measure of money has allowed employers to objectively measure the productivity of labor in monetary terms, whereas in barter this was not possible.

| | |
|--|------------------|
| <p>To get an accurate quantitative/measure of a labor's work.</p> | |
| <p>Thus money is essential in the successful operation of division of labor. 4+4</p> | <p>✓ 8 8</p> |

Examiner comment

This candidate explains both the division of labour and money as a medium of exchange. The answer goes on to explain how money facilitated exchange through the removal of barter and the necessity of a double coincidence of wants. This encouraged growth and the division of labour. Each concept together with the link between them is explained ensuring full marks.

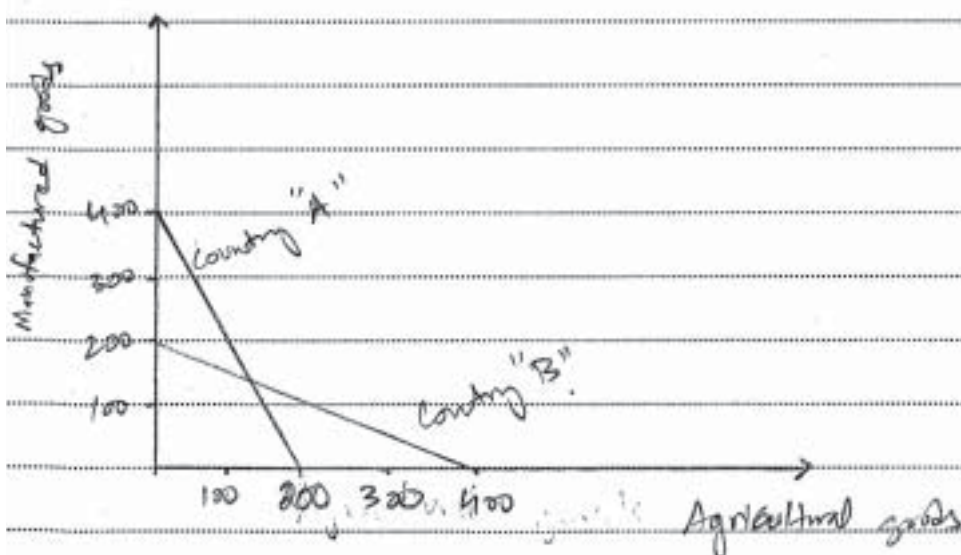
Mark awarded = 8 out of 8

Example candidate response

| | |
|----------------|--|
| <u>Q4)</u> | = (17) |
| (a) | |
| <u>Answer)</u> | <p>The use of money has a significant impact on the successful operation of an economy. Money is a medium of exchange, a method of account and a store of value. Within the economy and in the international sectors, the exchange of goods and services takes place using money. Labour is a factor of production and is very vital for production in an economy. All economies benefit from the factor endowment and the amount of resources they have for production of goods. This benefit that the economies derive can be maximized if resources are used in a way they are best suited for and this leads to specialization.</p> <p>Division of labour is a part of specialization the process to increase the productivity and thus the benefits derived from it. This also constitutes to an efficient use of resources present in an economy, as less resources are now wasted. Specialization has benefits both domestic and international. When looking from the domestic point of view, the production process increases and so does the productivity when labour is specialized. Productivity refers to the output per worker per given resources per time. For a manufacturing industry for example, if all workers work together at all stages, the process would take much longer longer time compared to each worker doing his designated task. Division of labour</p> |

also leads to labour efficiency. An old saying states that too many cooks spoil the broth. Same is the case here, if all of the work force works at each stage together, problems arise and this may affect the quality if not the quantity of the product produced.

For the international sector, the concept of division of labour and specialization is rather a vast one. This takes into account the whole country specializing to produce goods that the resources of the country are best suited for. This increases the benefits from trade and also the efficiency as ~~are~~ less resources are wasted. This phenomena can be explained using the comparative advantage theory. For two countries with fixed amount of resources, the resources might be well suited for producing one good in the market but not the other. Take for example manufactured goods and agricultural goods. Since opportunity cost ratios differ between the countries, it will be well suited for both countries to specialize in the production of the best suited good and then trade with each other to maximize the benefits. Comparative advantage is shown on the graph below.



After the production of goods by division of labour, ~~the~~ to maximize the gains, the goods are traded on the international market. For this, the main determinant is money, as it is the medium of exchange. The price of one currency in terms of another currency is referred to as exchange rate. One country purchases the goods of another country in the international market and this exchange of goods continues on a vast level leading to all the countries involved getting the benefits.

Hence it can be seen that successful operation of division of labour or in other words specialization depends upon the use of money.

5

Examiner comment

This candidate explains in some detail the division of labour and identifies this as an aspect of specialisation. Money is also identified as a medium of exchange. This scores highly. Unfortunately, the candidate scores very few marks for the second part of the mark scheme. There is very little on the link between the use of money and the growth of the division of labour and trade.

Mark awarded = 5 out of 8

Example candidate response

Section B.

4 a). Division of labour means that divide labour into each process of the production of a good. It will increase the productivity because ~~each worker will~~ of ~~not~~ no wastage of time. And it will increase the quality of the goods. But the workers may ~~not~~ feel ~~bored~~ ^{boring} because of doing the same thing ~~at~~ every day, they might lose motivation. Also, the Independence of workers are not strong, if one worker is ~~also~~ absent, ~~all the process~~ the production line will stop. Workers only have single skill, it will increase the unemployment.

Uses of money means the functions of money. First, medium of exchange ^{it will be used} when the country has the domestic and international trade.

Second, store of value, such as, saving the money in the bank.

Third, measure of value, to evaluate the value of goods and services. The last one is standard of deferred payment.

The successful operation of the ~~division~~ ^{division} of labour depends upon the use of money, because one of the ~~dis~~ disadvantages of ~~the~~ division of labour is that the workers will feel boring, then the company may increase the wage for the worker, ~~what~~ makes that is the workers will have the wage motivation and the the productivity of the company increase. This method depends upon the functions of money (measure of value and something else).

very basic

3
3

Examiner comment

This is a very poor answer that does not go far beyond a very basic grasp of the two central concepts. The candidate gives a very brief definition of the division of labour but there is little accompanying explanation or attempt to illustrate the process through examples. The answer also contains some irrelevant comment on the disadvantages of the division of labour. This is followed by a list of the functions of money. Again this is far too brief. The candidate fails to display any idea of the link between the two concepts.

Mark awarded = 3 out of 8

Question 4(b)

Discuss whether it is the behaviour of producers, consumers or governments that is most likely to cause inflation. [12]

Mark scheme

Discuss whether it is the behaviour of producers, consumers or governments that is most likely to cause inflation. [12]

Inflation is a sustained rise in the general price level and is measured by the CPI or RPI. Each of the groups can contribute to inflation although in different ways. Producers may increase prices to raise profit levels or to respond to higher import prices (cost push); consumers may increase their spending and reduce their saving raising AD (demand pull); governments may increase the money supply (monetary inflation), lower direct taxation and run budget deficits (demand pull) and raise indirect taxation (cost push inflation); they may also manipulate the exchange rate. Candidates can argue for any group although government influence may be most widespread.

For a definition of inflation

1 mark

For an understanding of different types of inflation

6 marks

Analysis of the influence of different groups

6 marks

Discussion of the relative impact of the groups

4 marks

} (10 marks max.)

Example candidate response

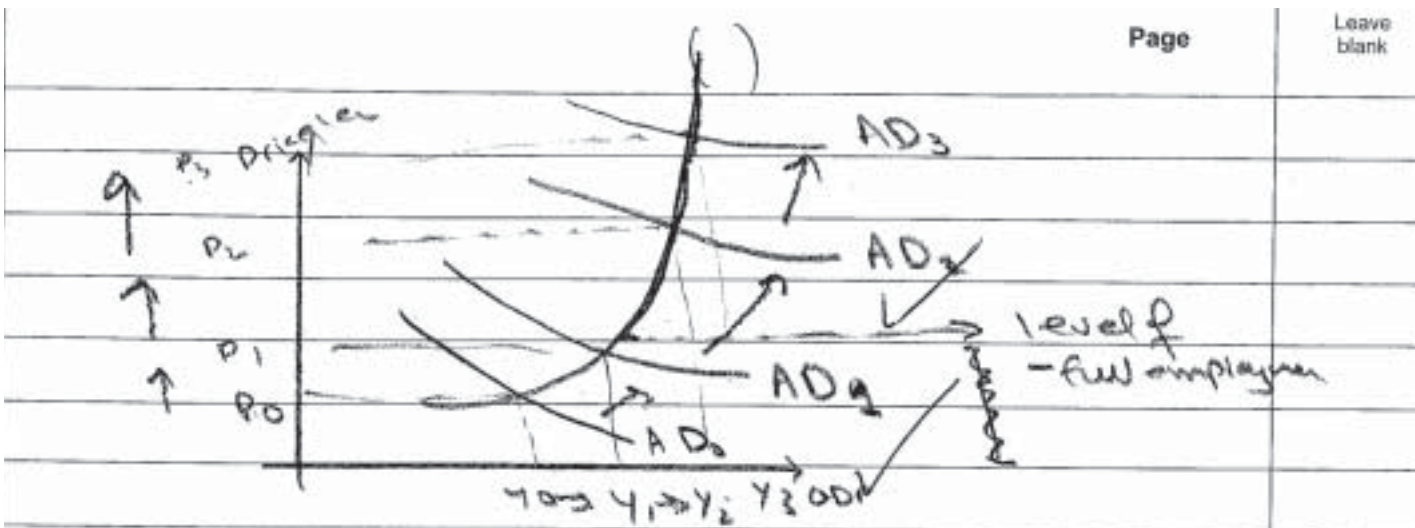
Inflation is: persistent rise in general price level - Inflation can be of different type

- 1) Galloping inflation (5% - 10%)
- 2) Walking inflation (10% to 20%)
- 3) Hyper inflation (100's and 1000's)
- 4) Creeping inflation (1% - 5%)

Inflation cause general price level to rise ~~causing~~ which can eventually cause money to lose its value of money. Inflation can be due to behaviour of producer (~~cost push~~ ^{cost push} inflation) consumer (~~cost push~~ ^{demand pull} inflation) or government (monetary inflation)

~~deflation~~

Demand pull inflation is when aggregate demand in economy rises due to increase consumer spending, increased ~~of~~ government spending or merit good, low interest rate resulting in capital investment, all these will result in increase in aggregated demand in an economy, too much export earning and little import payment. technological growth resulting in more production.

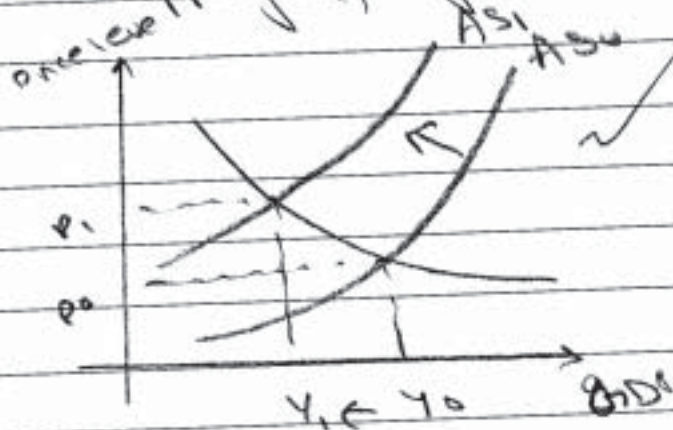


Increase in aggregate demand will result in increase in price level along with increase in National Income. However, this is only possible up till point of full employment after which increase in Aggregate demand will increase price level ~~but~~ but not National Income. Demand pull inflation is due to pattern of spending of consumers.

Cost push inflation is ~~caused~~ initiated by rising ~~cost price~~ and sustained by rising price of goods - Cost push inflation can be caused by

- (1) Increase in price of raw material (expensive cost of production)
- (2) Increase in wage rate (trade union)
- (3) Increase in price of imported raw material caused by increase in price in other countries
- (4) Cost increased due to indirect taxes.

These will result in increased cost of production and decrease in profit margin for producer who will cut back on the ~~the~~ production and supply of goods.



Decrease in supply has caused rise in price level and fall in National income and employment rate.

When inflation and unemployment coexist they are called stagflation.

This type of inflation is caused by production patterns of producer.

Monetary inflation, monetarist believe that inflation is only caused when government allows too much money supply in an economy.

According to the theory of M₁

$$M V = P T$$

M = supply of money

V = velocity of money circulation

P = Price level

T =

Monetarist believe that rate at which money changes hands is fairly constant hence

$M \propto P$

~~the~~ Price level P is directly proportional to supply of money that the govt allows. Increase in supply of money will result in increased spending, ~~a~~ aggregated demand rise, increased aggregate demand will cause prices to rise and eventually causing cost push inflation.

~~then there~~ ~~is~~ ~~no~~ ~~only~~ reason of inflation is money supply in an economy. Hence they claim that ~~is~~ only reason of inflation is money supply in an economy.

In conclusion, I would say that inflation is caused by different behaviour ~~purchase~~ of all three, producers, consumers and government, different patterns of sales and purchase and government policy interact to cause general price level to rise in an economy.

1+6+3+1

12

11

20

11

Examiner comment

This answer provides a good definition of inflation which gains credit. There is also a strong analytical framework based upon demand-pull, cost-push and monetary explanations of inflation. These gain full marks as per the mark scheme. There is also an analysis provided of the relative influence of consumers, producers and the government linked to these explanations. The candidate also concludes that it is the interaction of all three agents that causes inflation. This is an acceptable conclusion at this level.

Mark awarded = 12 out of 12

Example candidate response

b) Inflation means the continuous increase in the price levels of goods and services in the economy over time. There're three causes of inflation: demand pull inflation, cost push inflation, and money supply inflation.

Demand pull inflation is when the total demand of goods and services increase a lot, the prices of goods and services increase and then, it cause the demand pull inflation. It is the behaviours of consumer to cause inflation. The inflation will cause the cost of living increase and the living standard decrease of people. Also, the unemployment will increase. The government will using laws such as indirect tax on goods. especially the goods will inelastic demand and elastic supply, then

~~people~~ people will pay more tax and the consumption will decrease, and the demand of goods and services will decrease.

Cost push inflation is when the ~~cost~~ of production of a good or service is very high, ~~then~~ the producers will increase the price to gain more profit. Then it will cause the cost push inflation. It is the behaviour of producers to cause the inflation. ~~The inflation~~ high domestic inflation will cause the ~~exports~~ ~~more expensive~~ and imports more cheaper, then people will prefer to buy the imports instead of local produced goods. The local companies may fail. To solve this situation, the government will give a subsidy to producers to encourage the production and ~~using tax~~ ~~the~~ the cost will decrease and the price will decrease, the inflation will reduce.

Money supply is the government gives money to the consumers to encourage the consumption. It will cause the demand of goods and services increase and the prices increase. Then it will lead to ~~an~~ ^{the} inflation. It is the behaviour of the government to cause the inflation. The high domestic inflation will cause the exports less competitive, then the demand for exports decrease and the demand for imports increase, it might lead to a balance of payment deficit for the country. Then the government will take some actions to deal with balance of payment deficit and the inflation. The government may use the expenditure switching policy to reduce the ~~top~~ ~~deficit~~ ~~that~~ ~~is~~ ~~switch~~ ~~switch~~ the expenditure on imports to the local ~~product~~ companies.

Overall, I think the ~~behaviour~~ behaviours of ~~producers~~ consumers, producers and governments will ~~at~~ cause the inflation.

143 + 3

looks focus

10

10

Examiner comment

The candidate starts with a definition of inflation. This gains some credit. The answer then lists and gives a brief explanation of demand-pull, cost-push and monetary explanations of inflation. Each is generally satisfactory, although lacking in depth and reference to economic frameworks. These gain credit, but the main weakness of the answer is the limited focus on the behaviour of producers, consumers and governments. This means that a full discussion of which is most likely to cause inflation is not provided and this leads to the very weak conclusion and a disappointing mark.

Mark awarded = 7 out of 12

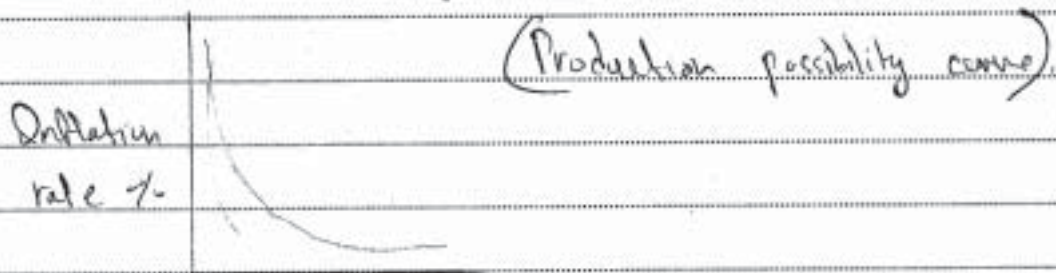
Example candidate response

Inflation is a general and persistent rise in price levels of all goods and services. Inflation can be caused by demand pull inflation, cost push inflation and monetarist view.

Our government, producers and consumers all three in a way contribute to a country's rate of inflation. Government could remove direct taxes and so people would have an increase in income leading to demand pull inflation. They could allow unbridled printing of money supplying excess money to people leading to inflation, according to the monetarist view. They could lower interest rates as well.

If the government starts encouraging borrowing and lending of money from banks that will increase demand pull inflation. Indirect taxes could be removed or lowered leading to cost push inflation.

Business could encourage inflation if they start using capital intensive methods which will lead to unemployment.



The above diagram is an production possibility curve showing how the rate of inflation and unemployment react.

If producers start giving up and stop producing goods in their country this will make companies rely more on imports worsening balance of trade and causing inflation. Companies should give more importance to home produced goods.

Therefore from the above possibilities it can be concluded that consumers, producers and government do cause inflation but they are not the only reason. If ~~inflation~~ ^{inflation} ~~decreases~~ ^{increases} in countries abroad ^{compared to our country} it our country can be saved. Expensive raw materials is also a cause to inflation. The value of money has to be controlled.

④ Producers have to pay high wages to workers when trade unions interfere hence leading to inflation again. Producers setting high prices to gain maximum profit could also create inflation.

5

1+2+1+1

5

Touches on a number of relevant ideas but does not develop these.

11

11

Examiner comment

This candidate is aware of how the government might cause inflation, but this is presented as a few isolated points and is not developed within a conceptual framework. Similarly, reference is made to producers and consumers, but without the conceptual framework, the candidate is unable to develop the answer to gain a good mark.

Mark awarded = 5 out of 12