



MARKSCHEME

May 2012

ECONOMICS

Higher Level

Paper 2

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In addition to the assessment criteria, use the paper-specific markscheme below. Award up to the maximum marks indicated. Each question is worth [10 marks].

1. Explain the differences between economies of scale and the law of diminishing returns.

Candidates **may** include:

- a definition of economies of scale
- a definition of the law of diminishing returns
- a distinction between the short run and the long run
- a distinction between fixed and variable factors of production
- an explanation of economies of scale as a long-run phenomenon
- an explanation of the law of diminishing returns as a short-run phenomenon
- use of diagrams to illustrate economies of scale
- use of diagrams to illustrate the law of diminishing returns that may be product curves and/or short run cost curves.

Candidates who incorrectly label diagrams cannot be rewarded with full marks.

Examiners should be aware that candidates may take a different approach which if appropriate, should be rewarded.

Level	Assessment Criteria	Marks
0	Completely inappropriate answer.	0
1	Little understanding of the specific demands of the question. Very little recognition of relevant economic theory. Relevant terms not defined. Significant errors.	1–3
2	Some understanding of the specific demands of the question. Some recognition of relevant economic theory. Some relevant terms defined. Some errors.	4–6
3	Understanding of the specific demands of the question. Relevant economic theory explained and developed. Relevant economic terms defined. Few errors. Where appropriate, diagrams included.	7–8
4	Clear understanding of the specific demands of the question. Relevant economic theory clearly explained and developed. Relevant economic terms clearly defined. No major errors. Where appropriate, diagrams included and explained. Where appropriate, examples used.	9–10

2. With the aid of *at least one* diagram, explain how cyclical/demand deficient unemployment may arise in an economy.

Answers **may** include:

- a definition of unemployment
- a definition of cyclical/demand deficient/disequilibrium unemployment
- use of a business cycle diagram to illustrate cyclical/demand deficient unemployment
- an explanation of demand deficient unemployment in terms of the deflationary/recessionary gap
- use of an AD/AS or ADL/ASL diagram to illustrate cyclical/demand deficient unemployment
- an explanation of the reasons for a fall in any of the components of aggregate demand, i.e. C, G, I or $(X - M)$.

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3. Explain why demand curves may not always slope downward from left to right.

Candidates **may** include:

- a definition of demand
- an explanation of a normal demand curve
- an explanation of exceptions:
 - ostentatious (Veblen) goods
 - role of expectations
 - Giffen goods
 - goods facing perfectly elastic or perfectly inelastic demand curves
- use of a diagram to illustrate an upward-sloping demand curve
- use of a diagram to illustrate a perfectly inelastic/elastic demand curve.

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4. With the aid of a diagram, explain the potential trade gains and trade losses arising from the formation of a customs union.

Candidates **may** include:

- a definition of a customs union
- explanation of potential gains:
 - benefits of specialization according to comparative advantage
 - more competition
 - economies of scale
 - lower prices
 - improved product quality
 - increased efficiency
 - trade creation
 - increased output and economic growth
 - impact on resource allocation
- explanation of potential losses
 - unequal distribution of gains
 - inferior to global free trade
 - lower output and increases in unemployment due to closure of inefficient producers
 - trade diversion
- diagram showing elimination of protectionist measures (tariff, quota or subsidy) leading to increased imports
- diagram showing increased protectionist measures (tariff, quota or subsidy) toward non-member countries, leading to a fall in imports
- AD/AS diagram illustrating economic growth arising from trade gains and reflected in an increase in AD
- diagram showing comparative advantage.

Examiners should be aware of the limited time available to candidates when marking responses to this question.

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5. Explain how a depreciation or devaluation of a country's currency could lead to an improvement in the current account of the balance of payments.

Candidates **may** include:

- a definition of depreciation
- a definition of devaluation
- a definition of current account of the balance of payments
- an explanation of a depreciation of a currency
- an explanation of devaluation
- an explanation that as depreciation/devaluation occurs import prices will rise and less imports will be purchased while more exports will be sold due to decreased prices. An improvement of the current account will result
- an explanation of the importance of elasticities and that if exports and imports are price inelastic and the sum of price elasticity of exports and imports (in absolute value) is greater than 1 then an improvement in the current account is possible.

A full explanation of the Marshall-Lerner condition or of the J-curve is not required but it should be taken into consideration when included. Based on the quality of the response, it is possible to award full marks even if the Marshall-Lerner condition is not mentioned.

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6. Explain *two* negative economic consequences of growth which may arise in a developing country.

Candidates **may** include:

- a definition of a developing country
- a definition of economic growth
- an explanation of how negative externalities may arise from production/consumption
- example(s) of negative externalities
- an explanation of impact on income distribution
- an explanation of potential resource depletion and lack of sustainability
- use of an appropriate diagram to illustrate a negative externality of production or consumption
- an explanation of the increase in rural to urban migration and the impact on cities.

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