Diploma Programme
Programme du diplôme
Programa del Diploma

Markscheme

May 2019

Economics

Higher level

Paper 1

13 pages

International Baccalaureate
Baccalauréat International
Bachillerato Internacional

Use the question-specific markscheme together with the markbands. Award up to the maximum marks as indicated.

Section A

Microeconomics

1. (a) Explain the relationship between the law of diminishing returns and a firm's short-run cost curves. **[10]**

*Answers **may** include:*

- definitions of the law of diminishing returns, short run, costs of production, cost curves
- diagrams to show the effect of decreasing and then increasing marginal cost on the average total cost and on the average variable cost; marginal product increasing (total product rising at increasing rate) then decreasing (total product rising at decreasing rate)
- explanation of the relationship between (diminishing) marginal product, (increasing) marginal cost, average variable costs and average total costs
- examples of diminishing returns and their effect on short-run costs.

Assessment Criteria

Part (a) 10 marks

Level		Marks
0	*The work does not meet a standard described by the descriptors below.*	**0**
1	*There is little understanding of the specific demands of the question.*	**1–3**
	Relevant economic terms are not defined. There is very little knowledge of relevant economic theory. There are significant errors.	
2	*There is some understanding of the specific demands of the question.*	**4–6**
	Some relevant economic terms are defined. There is some knowledge of relevant economic theory. There are some errors.	
3	*There is understanding of the specific demands of the question.*	**7–8**
	Relevant economic terms are defined. Relevant economic theory is explained and applied. Where appropriate, diagrams are included and applied. Where appropriate, examples are used. There are few errors.	
4	*There is clear understanding of the specific demands of the question.*	**9–10**
	Relevant economic terms are clearly defined. Relevant economic theory is clearly explained and applied. Where appropriate, diagrams are included and applied effectively. Where appropriate, examples are used effectively. There are no significant errors.	

(b) Evaluate the view that monopoly is an undesirable market structure as it fails to achieve productive and allocative efficiency. **[15]**

*Answers **may** include:*
- definitions of monopoly, productive efficiency, allocative efficiency
- diagrams to show productive and allocative inefficiency under profit-maximizing monopoly firm, economies of scale leading to lower prices and higher output
- explanation of why the profit maximizing choices of a monopoly firm lead to productive and allocative inefficiency
- examples of inefficiencies in monopoly markets in practice
- synthesis or evaluation (evaluate).

*Evaluation **may** include:* reasons why monopoly might be desirable (*eg* possibilities of economies of scale and the case of natural monopoly, the need to innovate to maintain economic profit, ability to finance research and development). Other reasons why monopoly may be undesirable (*eg* low quality of the products and services, x-inefficiency).

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

Assessment Criteria

Part (b) 15 marks

Level		Marks
0	*The work does not meet a standard described by the descriptors below.*	**0**
1	*There is little understanding of the specific demands of the question.*	**1–5**
	Relevant economic terms are not defined. There is very little knowledge of relevant economic theory. There are significant errors.	
2	*There is some understanding of the specific demands of the question.*	**6–9**
	Some relevant economic terms are defined. There is some knowledge of relevant economic theory. There are some errors.	
3	*There is understanding of the specific demands of the question.*	**10–12**
	Relevant economic terms are defined. Relevant economic theory is explained and applied. Where appropriate, diagrams are included and applied. Where appropriate, examples are used. There is an attempt at synthesis or evaluation. There are few errors.	
4	*There is clear understanding of the specific demands of the question.*	**13–15**
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2. (a) Explain why price elasticity of demand varies along the length of a straight-line demand curve. **[10]**

*Answers **may** include:*

- definitions of demand curve, price elasticity of demand
- diagram to show differing price elasticities of demand along a straight-line demand curve
- explanation why the price elasticity of demand varies along the length of the demand curve, using the diagram, the elasticity formula and an economic rationale (*eg* when the price is higher the proportion of income spent on the good is higher)
- examples (hypothetical numerical example to support the explanation or a hypothetical example of a single good or service sold at different prices and having different price elasticities of demand).

Assessment Criteria

Part (a) 10 marks

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(b) Examine the significance of price elasticity of demand for the decision-making of firms and governments. **[15]**

*Answers **may** include:*
- definition of price elasticity of demand (PED)
- diagrams to show the relationship between PED, price changes and the total revenue of firms; the relationships between PED, the size of an indirect tax, tax incidence, quantity produced/consumed and government tax revenue
- explanations of the relationship between: PED, price changes and total revenue of firms; how PED affects government tax revenue, production/consumption and tax incidence
- examples of PED proving significant for firms and governments in practice
- synthesis and evaluation (examine).

*Examination **may** include*: the differing incidence of indirect tax on consumers and firms due to differing price elasticities, the impact of PED on the uses of tax/subsidy to address market failure, the impact of time on PED (and total revenue) when price changes, the difficulty of estimating PED values for firms, other factors affecting demand that cause a change in total revenue/tax revenue.

*Award a maximum of level 2 if the response considers **either** the significance of PED for firms **or** for governments (but not both).*

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

***NB** It should be noted that definitions, theory, and examples that have already been given in part (a), and then referred to in part (b) should be rewarded.*

Assessment Criteria

Part (b) 15 marks

Level		**Marks**
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4	*There is clear understanding of the specific demands of the question.*	**13–15**
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Section B

Macroeconomics

3. (a) Explain how a deflationary gap might occur. **[10]**

*Answers **may** include:*
- definition of deflationary gap
- Keynesian or monetarist/new classical diagram to show a macroeconomic equilibrium at a level of real output below the full employment level
- explanation of factors (events) that may depress the aggregate demand and lead to a macroeconomic equilibrium at a level of real output below the full employment level
- examples of countries that have experienced a deflationary gap.

Assessment Criteria

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(b) Using the monetarist/new classical model and the Keynesian model, discuss the view that increases in aggregate demand will inevitably be inflationary. **[15]**

*Answers **may** include:*
- definitions of inflation, inflationary, aggregate demand (AD), monetarist/new classical model, Keynesian model
- diagrams to show the impact of an increase in AD in the two different models
- explanation why in the monetarist/new classical model an increase in AD will be inflationary
- examples of cases where an increase in AD either has or has not been inflationary
- synthesis and evaluation (discuss).

*Discussion **may** include:* consideration of an increase in AD not being inflationary in the Keynesian model if the economy is operating with spare capacity, consideration of an increase in AD not being inflationary in the monetarist/new classical model if the economy is recovering from equilibrium below the full employment level of output, consideration of the impact of simultaneous improvements on the supply side of the economy as AD increases, a consideration of the word "inevitably", a consideration of the word "inflationary" in the context of the AD/AS model.

*Award a maximum of level 2 if the response considers **either** the monetarist/new classical model **or** the Keynesian model (but not both).*

Opinions or conclusions should be presented clearly and should be supported by appropriate examples.

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

Assessment Criteria

Part (b) 15 marks

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4	*There is clear understanding of the specific demands of the question.*	**13–15**
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4. (a) Explain how government spending might promote greater equity in an economy. **[10]**

*Answers **may** include:*

- definitions of government spending, equity
- Lorenz curve diagram showing a Lorenz curve shifting closer to the line of perfect income equality because of government spending to promote equity (or a subsidy diagram or an AD/AS diagram showing increasing AD and real GDP and therefore implying increased employment)
- explanation of the linkages between government spending (*eg* on merit and public goods, transfer payments and subsidies), taxation and equity
- examples of actual government spending measures (*eg* healthcare services, education, sanitation, water supplies, public parks, public transportation, old age pensions, unemployment benefits, child allowances) that have promoted equity.

Assessment Criteria

Part (a) 10 marks

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(b) Evaluate the view that government policies to promote greater equity will always have a negative effect on efficiency. **[15]**

*Answers **may** include:*
- definitions of efficiency, equity
- an AD/AS diagram to show LRAS shifting to the left (less efficiency) or to the right (greater efficiency), an externalities diagram to show government policies improving allocative efficiency, a supply and demand diagram to show welfare loss due to government policies to promote equity
- explanation of how government spending and taxation might adversely impact efficiency (*eg* through the disincentive effects of progressive taxation, transfer payments, subsidized goods and services, through the decrease in social surplus due to taxes and price ceilings)
- examples of government policies having either a negative or positive impact on efficiency
- synthesis and evaluation (evaluate).

*Evaluation **may** include*: consideration of the hypothetical trade-off between equity and efficiency, consideration of how government spending on socially desirable goods and services (*eg* health care services, education, sanitation, clean water supplies) might positively impact efficiency in the utilization of the economy's resources in the long run (*eg* through poverty reduction and human capital formation) and in the short run (*eg* through the positive impact of government spending on AD), consideration of how automatic stabilizers might improve efficiency in the utilization of the economy's resources in the short run (*eg* through the positive impact on AD during recessions), consideration of how certain kinds of government spending and taxation may increase allocative efficiency (*eg* through the increased consumption of merit goods and decreased consumption of demerit goods), government provision of merit goods may be less efficient than private provision, consideration of the word "always", consideration of the meaning of the word "equity" (*eg* the difference between equity in the distribution of income and equality in the distribution of income, equity as equality of opportunity), consideration of the meaning of the word "efficiency" (*eg* productive and allocative efficiency in microeconomics, efficiency in the utilization of the economy's factors of production in macroeconomics).

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

Opinions or conclusions should be presented clearly and should be supported by appropriate examples.

***NB** It should be noted that definitions, theory, and examples that have already been given in part (a), and then referred to in part (b) should be rewarded.*

Assessment Criteria

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