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Economics
Standard level
Paper 1

Wednesday 2 November 2016 (afternoon)

1 hour 30 minutes

Instructions to candidates

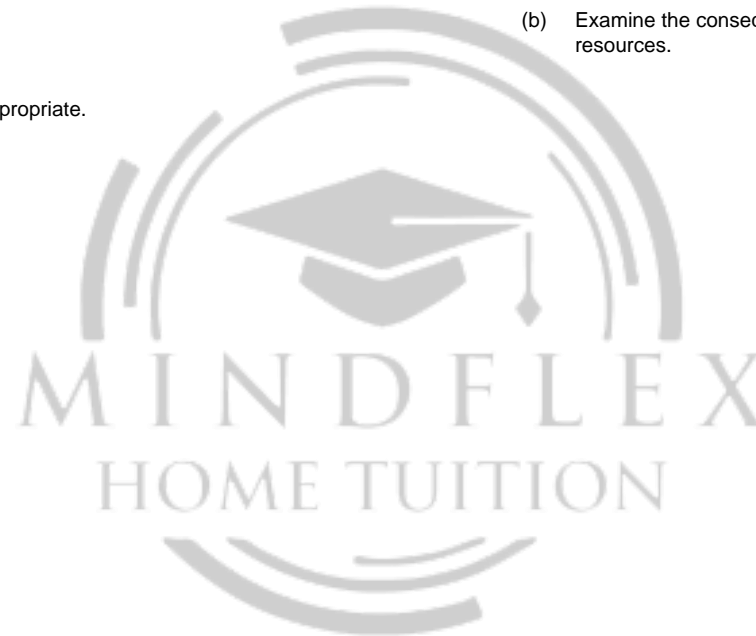
- Do not open this examination paper until instructed to do so.
- You are not permitted access to any calculator for this paper.
- Section A: answer one question.
- Section B: answer one question.
- Use fully labelled diagrams and references to examples where appropriate.
- The maximum mark for this examination paper is **[50 marks]**.

Section A

Answer **one** question from this section.

Microeconomics

- Using a production possibilities curve (PPC) diagram, explain why choices have to be made in all economies. [10]
 - Discuss the view that governments should not intervene in housing markets. [15]
- Explain why changes in the price of goods and services may lead to changes in resource allocation. [10]
 - Examine the consequences of the lack of a pricing mechanism for common access resources. [15]



Section B

Answer **one** question from this section.

Macroeconomics

3. (a) Explain how the Lorenz curve and the Gini coefficient are used to measure income inequality. [10]
- (b) Discuss the view that the best way to achieve greater equity in the distribution of income in a country is to use a progressive tax system. [15]
4. (a) Explain what effect an increase in interest rates might have on unemployment. [10]
- (b) Evaluate the effectiveness of fiscal policy as a tool to reduce unemployment. [15]

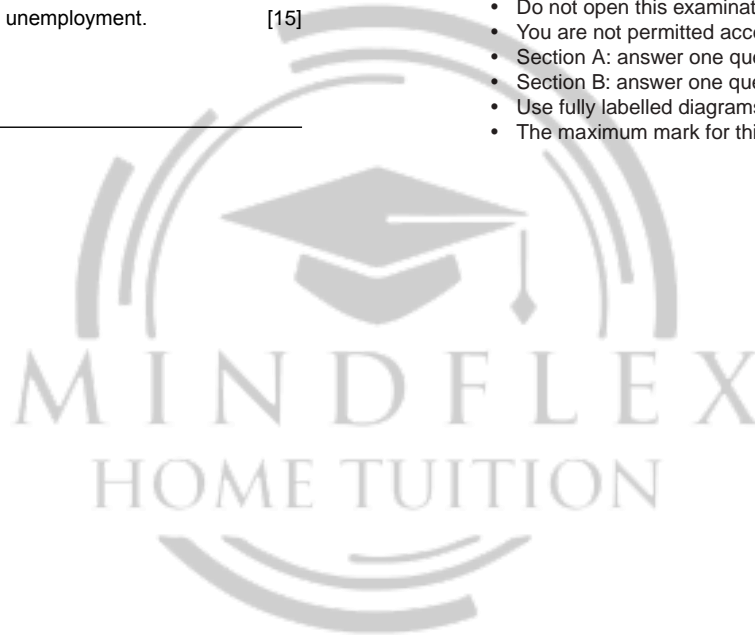
**Economics
Standard level
Paper 2**

Thursday 3 November 2016 (afternoon)

1 hour 30 minutes

Instructions to candidates

- Do not open this examination paper until instructed to do so.
- You are not permitted access to any calculator for this paper.
- Section A: answer one question.
- Section B: answer one question.
- Use fully labelled diagrams and references to the text/data where appropriate.
- The maximum mark for this examination paper is **[40 marks]**.



Section A

(Question 1 continued)

Answer **one** question from this section.

1. Study the extract below and answer the questions that follow.

New Zealand dollar overvalued

- ❶ The New Zealand finance minister said the exchange rate of the New Zealand dollar (NZD), is "unsustainably high; it is somewhere between 10% to 15% overvalued".
- ❷ The NZD had been near its record high against the US dollar before weakening last week on slower inflation figures and a fall in dairy prices. The NZD has gained about 6% so far this year.
- ❸ However, the finance minister said that New Zealand exporters had developed strength because of the high currency. "New Zealand is actually in reasonably good shape," he said. "We have had an export sector operating with a strong exchange rate now for five or six years and that has had an impact on efficiency."
- ❹ An economist said recently that the central bank might consider intervening in the currency market to achieve a **depreciation** in the value of the NZD.
- ❺ The Reserve Bank (central bank) governor raised the official interest rate for the fourth time this year to 3.5% at a time when other major economies have their rates at record low levels.
- ❻ He said that, "Encouragingly, the economy appears to be adjusting to the **monetary policy** tightening that has taken place since the start of the year. It is important that inflation expectations remain contained. This interest rate increase will help keep future average inflation near the 2% target and ensure that the economic expansion can be sustained".
- ❼ New Zealand's economy is expected to grow at an annual pace of 3.7% over 2014. New Zealand government figures showed a monthly trade (in goods) surplus of \$247 million in June 2014 compared to \$371 million in June 2013. The annual trade (in goods) balance turned to a surplus of \$1.2 billion from a deficit of \$819 million a year earlier.
- ❽ Global demand for New Zealand dairy products has been a key support for the country's exports over the past 18 months, though prices have dropped this year with increased supply.

[Source: adapted from "NZ dollar unsustainably high", *The New Zealand Herald*, 23 July 2014;
"Dollar dives after reserve bank lifts rate to 3.5pc", *The New Zealand Herald*, 24 July 2014;
and "NZ dollar slides to six-week low after rate hike", *The New Zealand Herald*, 24 July 2014]

- (a) (i) Define the term **depreciation** indicated in bold in the text (paragraph ❹). [2]
- (ii) Define the term **monetary policy** indicated in bold in the text (paragraph ❻). [2]
- (b) Using an exchange rate diagram, explain how the increase in the official interest rate to 3.5% is likely to affect the value of the New Zealand dollar (paragraph ❺). [4]
- (c) Using an AD/AS diagram, explain how "monetary policy tightening" may affect a country's inflation rate (paragraph ❽). [4]
- (d) Using information from the text/data and your knowledge of economics, discuss the possible economic consequences of an overvalued New Zealand dollar on the New Zealand economy. [8]

(This question continues on the following page)

2. Study the extract below and answer the questions that follow.

(Question 2 continued)

- (a) (i) Define the term *interest rates* indicated in bold in the text (paragraph 1). [2]
- (ii) Define the term *inflation* indicated in bold in the text (paragraph 2). [2]
- (b) Using an exchange rate diagram, explain how speculation is contributing to the rising value of the British pound (paragraph 1). [4]
- (c) Using an appropriate diagram, explain why it is possible that "British firms producing exported goods that have few substitutes have reported no reduction in export revenue despite the appreciation" (paragraph 3). [4]
- (d) Using information from the text/data and your knowledge of economics, discuss possible consequences of the appreciation of the British pound. [8]

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(This question continues on the following page)

Section B

(Question 3 continued)

Answer **one** question from this section.

3. Study the extract and data below and answer the questions that follow.

Ecuador sees 2014 trade deficit falling with new import rules, but at what cost?

- ❶ In the period from January to May 2014, Ecuador posted a trade surplus of US\$483 million, moving from a deficit of US\$626 million one year before.
- ❷ The government has been implementing an import-substitution policy to reduce the trade deficit. On 4 December 2013, Ecuador's Foreign Trade Committee established new quality control measures for the importation of 293 items, including cosmetics, toys, toothpaste, meat and cereals. In order for goods on the list to be imported a certificate needs to be obtained, ensuring that the products meet quality control standards. There are up to 13 steps to be taken before a product may enter as a result of the excessive regulations holding up the certificates.
- ❸ The import-substitution policy also involves a move to provide support to domestic industries. The president firmly believes in the benefits of sheltering **infant industries**. He has complained about imports such as coconut water, banana puree or cornflakes, which he believes could be produced by domestic industries, supported by appropriate policies. In addition, he points out that Ecuador is a top exporter of fine aroma cocoa, but imports approximately US\$25 million worth of chocolate per year. Other measures to protect domestic industries include anti-dumping measures and higher tariffs on raw materials and capital equipment that are available in Ecuador.
- ❹ In the month since this intervention started, different businesses have begun to feel both the advantages and disadvantages. Pica, one of the largest companies in the plastic industry, has taken advantage of the policy. The reduction in the importation of certain products has allowed them to increase their own production.
- ❺ In contrast, Toni Industries, one of the most important dairy businesses in the country has suffered. It has complained that cornflakes, which the company uses as a **complementary good** to one of its key products, could not get through customs because it did not have the quality control certificate.
- ❻ Many industry analysts and economists argue that closing off imports will isolate the country and create a false sense of competitiveness. They are also concerned that the government seems to be assuming that other countries will not react. Some argue that the government should seek to create incentives for investment, like tax benefits, or legal security, which would allow the entry of new competitors into the Ecuadorean markets.

Table 1: Selected exports and imports for Ecuador, January to May 2014

Exports	Export revenue (US\$ billion)	Imports	Import spending (US\$ billion)
Crude oil	5.74	Raw materials	3.20
Bananas	1.12	Capital goods	2.68
Shrimp	1.09	Consumer goods	2.01
Flowers	0.34		

[Source: adapted from www.reuters.com, 21 January 2014; www.panampost.com, 20 January 2014; www.latinvex.com, 19 March 2014 and www.blogs.wsj.com, 14 July 2014]

- (a) (i) Define the term *infant industries* indicated in bold in the text (paragraph ❸). [2]
- (ii) Define the term *complementary goods* indicated in bold in the text (paragraph ❹). [2]
- (b) Using an AD/AS diagram, explain how moving from a trade deficit to a trade surplus would affect real GDP in Ecuador, *ceteris paribus*. [4]
- (c) Using a definition of the term *ceteris paribus*, explain why it is necessary to include this assumption in part (b). [4]
- (d) Using information from the text/data and your knowledge of economics, evaluate Ecuador's import-substitution policy as a means of achieving economic growth and development. [8]

(This question continues on the following page)

4. Study the extract below and answer the questions that follow.

(Question 4 continued)

Ghana to seek help from International Monetary Fund

- 1 Ghana has said it will seek financial aid in the form of a loan from the International Monetary Fund (IMF) to help stop the rapid decline in the value of the cedi, Ghana's currency, and close a large **budget deficit**. Ghana's transformation from one of Africa's fastest growing economies to the home of the world's worst-performing currency has become a concern. The exchange rate depreciated by 40 % against the US dollar in 2014. The fall in the currency has led to increases in the price of consumer goods such as sugar and fuel; inflation is at an unacceptable 15 %.
- 2 Despite being a major exporter of gold, oil and cocoa, Ghana's current account deficit has risen sharply to 12 % of its gross domestic product (GDP). This is partly due to a rapid increase in demand for imports and falling gold prices. Additionally, oil revenues have not been as strong as expected.
- 3 The government is also struggling with a wide budget deficit, which stood at 10 % of GDP last year. Ghana's good reputation for fiscal responsibility has worsened considerably as the government tripled salaries for police officers and soldiers.
- 4 It is expected that the news of talks with the IMF will be positively received in international financial markets. The finance minister has said the step would help to stabilize the currency, to bring domestic prices under control, and also to restore investors' confidence in Ghana's economy.
- 5 A Ghanaian spokesperson noted that the IMF would insist on the government introducing measures to tackle inflation and reduce its budget deficit. The IMF says that Ghana needs to tighten its budget immediately, by reducing public sector wages, lowering subsidies and increasing taxes. The IMF is likely to demand a limit on borrowing and perhaps some privatization of power and water companies.
- 6 Earlier this year, problems in the economy had led to nationwide protests, with thousands of workers across the country protesting in the streets about the rise in the cost of living. The country's largest trade union says the government has been mismanaging the economy. In response to the protests, a government minister said that the government would work very hard to achieve **economic development** to make life easier for the working people of Ghana but that all Ghanaians would have to make "some sacrifices for the economy to recover".

- (a) (i) Define the term *budget deficit* indicated in bold in the text (paragraph 1). [2]
- (ii) Define the term *economic development* indicated in bold in the text (paragraph 6). [2]
- (b) Using an exchange rate diagram, explain how the large current account deficit may have affected the value of the Ghanaian cedi. [4]
- (c) Using an AD/AS diagram, explain how the falling value of the Ghanaian cedi may have contributed to inflation. [4]
- (d) Using information from the text/data and your knowledge of economics, discuss possible consequences of International Monetary Fund (IMF) financial aid on Ghana's economic growth and development. [8]

[Source: adapted from <http://news.yahoo.com>, 3 and 4 August 2014; <http://online.wsj.com>, 3 August 2014 and www.bbc.com/news, 24 July 2014 and 4 August 2014]

(This question continues on the following page)



Markscheme

November 2016

Economics

Standard level

Paper 2



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

Section A

1. (a) (i) Define the term **depreciation** indicated in bold in the text (paragraph 4). [2]
- | Level | Marks |
|--|-------|
| 0 <i>The work does not reach a standard described by the descriptors below.</i> | 0 |
| 1 <i>Vague definition.</i>
The idea that the exchange rate/value (price) of a currency falls. | 1 |
| 2 <i>Accurate definition.</i>
An explanation that it is a decrease in the value (price/exchange rate) of one currency plus one of the following: <ul style="list-style-type: none"> • due to a change in market forces • in a floating exchange rate system. | 2 |
- (ii) Define the term **monetary policy** indicated in bold in the text (paragraph 6). [2]
- | Level | Marks |
|---|-------|
| 0 <i>The work does not reach a standard described by the descriptors below.</i> | 0 |
| 1 <i>Vague definition.</i>
The idea that is to do with interest rates (or money supply). | 1 |
| 2 <i>Accurate definition.</i>
An explanation that it is any two of the following: <ul style="list-style-type: none"> • demand-side policy • changes in interest rates • changes in money supply. | 2 |

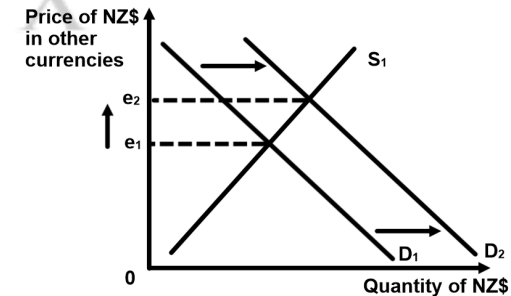
- (b) Using an exchange rate diagram, explain how the increase in the official interest rate to 3.5% is likely to affect the value of the New Zealand dollar (paragraph 9). [4]

- | Level | Marks |
|---|-------|
| 0 <i>The work does not reach a standard described by the descriptors below.</i> | 0 |
| 1 <i>There is a correct diagram or an accurate written response.</i>
For drawing a correctly labelled exchange rate diagram, showing a shift of the demand curve for the New Zealand dollar to the right or for an explanation that when the interest rate rises, people abroad will wish to save more in New Zealand financial institutions, and so demand for the currency will increase and the value of the currency will rise (appreciate). | 1-2 |
| 2 <i>There is a correct diagram and an accurate written response.</i>
For drawing a correctly labelled exchange rate diagram, showing a shift of the demand curve for the New Zealand dollar to the right and for an explanation that when the interest rate rises, people abroad will wish to save more in New Zealand financial institutions, and so demand for the currency will increase and the value of the currency will rise (appreciate). | 3-4 |

Candidates may offer an alternative explanation that, because of the interest rate increase, there might be an increase of "hot money" inflows, leading to the shift in the demand curve. This may be fully rewarded.

Candidates who incorrectly label diagrams can be awarded a maximum of [3].

For an exchange rate diagram, the vertical axis may be exchange rate, price of NZD in other currencies, or other currency per NZD. The horizontal axis should be quantity or quantity of NZD. A title is not necessary.



(c) Using an AD/AS diagram, explain how "monetary policy tightening" may affect a country's inflation rate (paragraph ④). [4]

Level

0 *The work does not reach a standard described by the descriptors below.*

1 *There is a correct diagram **or** an accurate written response.*

For drawing a correctly labelled AD/AS diagram, showing a shift of the AD curve to the left **or** for an explanation that monetary policy tightening (increasing interest rates and/or reducing the money supply) should reduce consumption and/or investment, components of AD ($C+I+G+[X-M]$), lowering the inflation rate (inflationary pressure) in the economy.

2 *There is a correct diagram **and** an accurate written response.*

For drawing a correctly labelled AD/AS diagram, showing a shift of the AD curve to the left **and** for an explanation that monetary policy tightening (increasing interest rates and/or reducing the money supply) should reduce consumption and/or investment, components of AD ($C+I+G+[X-M]$), lowering the inflation rate (inflationary pressure) in the economy.

Marks

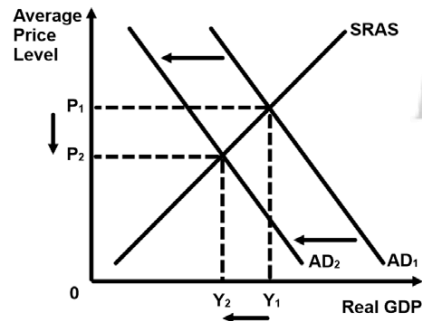
0

1-2

3-4

Candidates who incorrectly label diagrams can be awarded a maximum of [3].

For AD/AS, the vertical axis, the label may be Average (General) Price Level, APL or Price level. For the horizontal axis, real output, real national output, real income, real national income, real GDP or real Y. A title is not necessary.



(d) Using information from the text/data and your knowledge of economics, discuss the possible economic consequences of an overvalued New Zealand dollar on the New Zealand economy. [8]

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

Do not award beyond Level 2 if the answer does not contain reference to the information provided.

Level

0 *The work does not reach a standard described by the descriptors below.*

1 *Few relevant concepts are recognized.*
There is basic knowledge/understanding.

2 *Relevant concepts are recognized and developed in reasonable depth.*
There is clear knowledge/understanding.
There is some attempt at application/analysis.

3 *Relevant concepts are recognized and developed in reasonable depth.*
There is clear knowledge/understanding.
There is effective application/analysis.
There is synthesis/evaluation, supported by appropriate theory and evidence.

Marks

0

1-2

3-5

6-8

Command term

Discuss requires candidates to offer a considered and balanced review that includes a range of arguments, factors, or hypotheses. Opinions or conclusions should be presented clearly and supported by appropriate evidence.

Responses may include:

Inflation rate:

- the current inflation rate seems to be reasonable near 2% target (paragraph ④)
- a strong dollar will lower the cost of imported raw materials, semi-finished goods, and finished goods, reducing inflationary pressure.

Employment:

- in the short run, export prices will rise and import prices will fall, leading to reduced employment in both export industries, as demand for exports falls, and domestic industries, as people buy more imports
- the export sector is used to high exchange rates and remains competitive, so employment rates may not be as badly affected in export industries (paragraph ④).

Economic growth:

- the expected growth rate is 3.7% (paragraph ④) – reasonably high for a developed country
- a fall in net exports would lead to lower AD and so a fall in growth rates
- firms are efficient and competitive (paragraph ④), so economic growth may not be so badly affected
- possible intervention by the central bank to depreciate the currency (paragraph ④) to prevent net exports from decreasing and slowing economic

Current account balance:

- a high exchange rate could lead to a fall in net exports and so a movement towards a current account deficit
- exporters seem to be coping with a high exchange rate (paragraph ③) and so net exports may not be affected greatly on the export side
- the effect may be greater on the import side
- there is a present trade in goods balance surplus of \$1.2 billion (paragraph ⑦)
- overvalued NZD may begin to harm New Zealand dairy products which is a key export (paragraph ⑧).

Any reasonable discussion.

2. (a) (i) Define the term *interest rates* indicated in bold in the text (paragraph ①). [2]

Level

0 *The work does not reach a standard described by the descriptors below.* Marks
0

1 *Vague definition.* Marks
1
The idea that it is a payment for a loan.

2 *Accurate definition.* Marks
2
An explanation that it is **one** of the following:
• the price or cost of borrowed money
• the price of credit (or the percentage paid on borrowed money)
• the reward for saving.

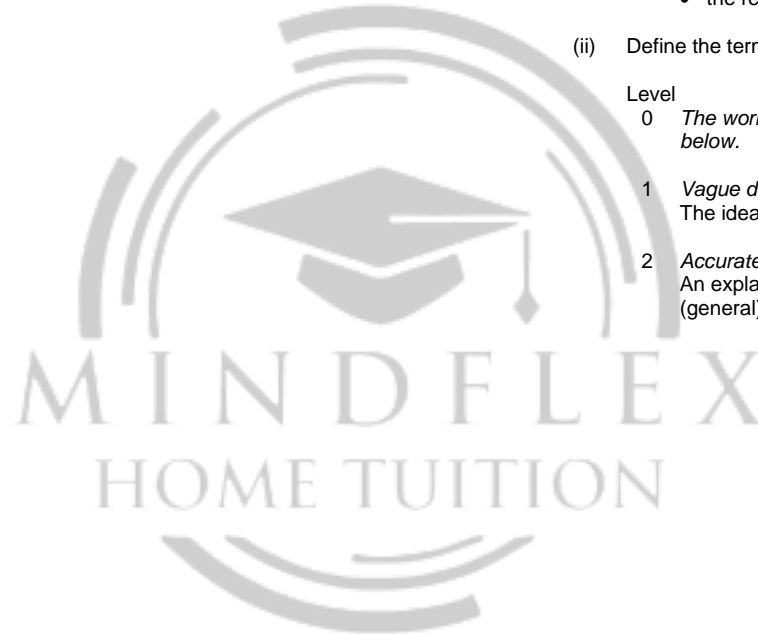
(ii) Define the term *inflation* indicated in bold in the text (paragraph ②). [2]

Level

0 *The work does not reach a standard described by the descriptors below.* Marks
0

1 *Vague definition.* Marks
1
The idea that it is an increase in prices in the economy.

2 *Accurate definition.* Marks
2
An explanation that it is a sustained increase in the average (general) price level in the economy.



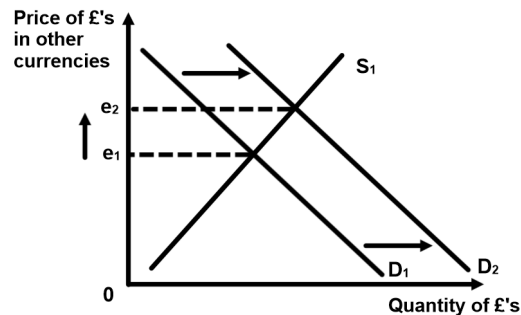
(b) Using an exchange rate diagram, explain how speculation is contributing to the rising value of the British pound (paragraph ❶). [4]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is a correct diagram or an accurate written response.</i> For drawing a correctly labelled exchange rate diagram showing an increase in demand and the appreciation of the British pound or for an explanation that speculators are anticipating that the pound will rise in value in the future and thus have been buying more British pounds, leading to appreciation.	1-2
2 <i>There is a correct diagram and an accurate written response.</i> For drawing a correctly labelled exchange rate diagram showing an increase in demand and the appreciation of the British pound and for an explanation that speculators are anticipating that the pound will rise in value in the future and thus have been buying more British pounds, leading to appreciation.	3-4

Candidates might explain that speculators are anticipating an increase in interest rates in the future, which would give a higher return on future savings, so are demanding British pounds now. This alternative approach should be fully rewarded.

Candidates who incorrectly label diagrams can be awarded a maximum of [3].

For an exchange rate diagram, the vertical axis may be exchange rate, price of British pound in other currencies, or other currency per British pound. The horizontal axis should be quantity or quantity of British pounds. A title is not necessary.



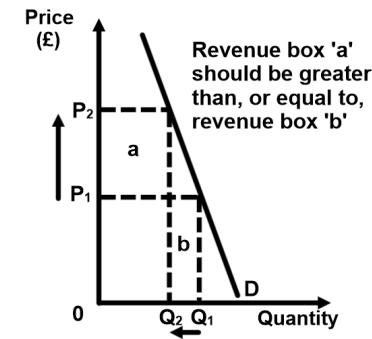
(c) Using an appropriate diagram, explain why it is possible that "British firms producing exported goods that have few substitutes have reported no reduction in export revenue despite the appreciation" (paragraph ❷). [4]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is a correct diagram or an accurate written response.</i> For drawing a correctly labelled diagram showing a demand curve, with a price increase and a decrease in quantity, and revenue boxes showing an increase in export revenue or for an explanation that since these firms produce goods with few substitutes, the demand is inelastic, and so when price increases due to appreciation, the total revenue increases.	1-2
2 <i>There is a correct diagram and an accurate written response.</i> For drawing a correctly labelled diagram showing a demand curve, with a price increase and a decrease in quantity, and revenue boxes showing an increase in export revenue and for an explanation that since these firms produce goods with few substitutes, the demand is inelastic, and so when price increases due to appreciation, the total revenue increases.	3-4

Candidates may explain that the demand is unit elastic and so when the price increases due to appreciation, the total revenue will remain the same ("no reduction in export revenue"). If the diagram is also correct, this approach may be fully rewarded.

Candidates who incorrectly label diagrams can be awarded a maximum of [3].

The use of P and Q is sufficient for a demand and supply diagram. A title is not necessary.



- (d) Using information from the text/data and your knowledge of economics, discuss possible consequences of the appreciation of the British pound. **[8]**

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

Do not award beyond Level 2 if the answer does not contain reference to the information provided.

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Few relevant concepts are recognized.</i> There is basic knowledge/understanding.	1–2
2 <i>Relevant concepts are recognized and developed in reasonable depth.</i> There is clear knowledge/understanding. There is some attempt at application/analysis.	3–5
3 <i>Relevant concepts are recognized and developed in reasonable depth.</i> There is clear knowledge/understanding. There is effective application/analysis. There is synthesis/evaluation, supported by appropriate theory and evidence.	6–8

Command term

Discuss requires candidates to offer a considered and balanced review that includes a range of arguments, factors, or hypotheses. Opinions or conclusions should be presented clearly and supported by appropriate evidence.

Responses may include:

- a strong British pound will lower the cost of imported raw materials, semi-finished goods, and finished goods, reducing inflationary pressure
- in the short run, export prices will rise and import prices will fall, leading to reduced employment in both export industries, as demand for exports falls, and domestic industries, as people buy more imports
- impact on tourist sector in the UK (paragraph ②)
- impact on British tourists going overseas (paragraph ②)
- in markets where demand is inelastic, export revenue may not fall (part (c)) (paragraph ③)
- British firms are losing out to foreign competitors (paragraph ③) as goods and services are relatively more expensive
- a fall in net exports would lead to lower AD and so a fall in growth rates
- impact on British firms' profits
- a high exchange rate could lead to a fall in net exports and have an impact on the current account
- the impact of cheaper fuel on household budgets (paragraph ④).

Any reasonable discussion.

Section B

3. (a) (i) Define the term *infant industries* indicated in bold in the text (paragraph ③). **[2]**

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Vague definition.</i> An explanation that they are any one of the following: <ul style="list-style-type: none"> • they are new industries • which do not benefit from economies of scale • that need protection to compete with imports. 	1
2 <i>Accurate definition.</i> An explanation that they are any two of the following: <ul style="list-style-type: none"> • they are new industries • which do not benefit from economies of scale • that need protection to compete with imports. 	2

- (ii) Define the term *complementary goods* indicated in bold in the text (paragraph ③). **[2]**

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Vague definition.</i> The idea that they are goods that are related to each other.	1
2 <i>Accurate definition.</i> An explanation that they are goods that are consumed with each other (joint demand) or that they are goods that have negative cross price elasticity of demand.	2

(b) Using an AD/AS diagram, explain how moving from a trade deficit to a trade surplus would affect real GDP in Ecuador, *ceteris paribus*. [4]

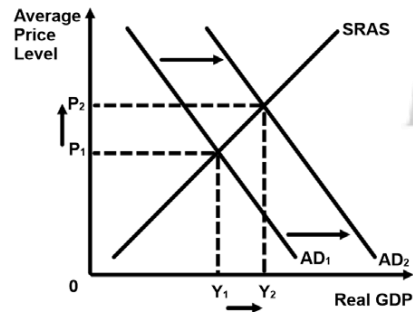
Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is a correct diagram or an accurate written response.</i> For drawing a correctly labelled AD/AS diagram showing a shift in aggregate demand to the right and an increase in real GDP or for an explanation that moving from a trade deficit to a trade surplus would involve an increase in net exports, a component of aggregate demand, and thus an increase in AD and an increase in real GDP.	1-2
2 <i>There is a correct diagram and an accurate written response.</i> For drawing a correctly labelled AD/AS diagram showing a shift in aggregate demand to the right and an increase in real GDP and for an explanation that moving from a trade deficit to a trade surplus would involve an increase in net exports, a component of aggregate demand, and thus an increase in AD and an increase in real GDP.	3-4

(c) Using a definition of the term *ceteris paribus*, explain why it is necessary to include this assumption in part (b). [4]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is a correct definition or an accurate written response.</i> For an explanation that <i>ceteris paribus</i> means "all other things being equal" (or any other reasonable explanation) or for an explanation that net exports may have increased, but any of the other components of AD may have fallen and so Ecuador's aggregate demand may not have increased.	1-2
2 <i>There is a correct definition and an accurate written response.</i> For an explanation that <i>ceteris paribus</i> means "all other things being equal" (or any other reasonable explanation) and for an explanation that net exports may have increased, but any of the other components of AD may have fallen and so Ecuador's aggregate demand may not have increased.	3-4

Candidates who incorrectly label diagrams can be awarded a maximum of [3].

For AD/AS, the vertical axis may be Average (General) Price Level, APL or Price Level. The horizontal axis may be real output, real national output, real income, real national income, real GDP or real Y. A title is not necessary.



- (d) Using information from the text/data and your knowledge of economics, evaluate Ecuador's import-substitution policy as a means of achieving economic growth and development.

[8]

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

Do not award beyond Level 2 if the answer does not contain reference to the information provided.

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Few relevant concepts are recognized.</i> There is basic knowledge/understanding.	1-2
2 <i>Relevant concepts are recognized and developed in reasonable depth.</i> There is clear knowledge/understanding. There is some attempt at application/analysis.	3-5
3 <i>Relevant concepts are recognized and developed in reasonable depth.</i> There is clear knowledge/understanding. There is effective application/analysis. There is synthesis/evaluation, supported by appropriate theory and evidence.	6-8

Command term

Evaluate requires candidates to make an appraisal by weighing up the strengths and limitations.

Responses **may** include:

- explanation of import-substitution:
- policy to replace imports with domestically produced goods
- elements of an import-substitution policy may include any measures to support domestic producers (eg tariffs, quotas, subsidies, administrative barriers)
- explanation of economic growth
- explanation of economic development.

Possible strengths:

- reduction in imports means a reduction in import spending, which will reduce the trade deficit and contribute to economic growth
- increased real GDP (may refer to diagram in part (b))
- increase employment, which may contribute to economic growth and development
- Ecuador has moved from trade deficit to trade surplus so its policy seems to be effective (paragraph 1)
- Ecuador's exports are largely primary products, and so import-substitution may be necessary for Ecuador to diversify and/or produce products with more value-added such as chocolate (Table 1 and paragraph 2)
- it is important that countries have the right to set and enforce product standards to protect their people from below-standard products (paragraph 3)
- firms like Pica may be able to increase output, thereby achieving economies of scale; this may allow it to become an exporter and further help Ecuador's trade balance (paragraph 4), thereby resulting in economic growth; possible job creation and breaking of poverty cycle for those with jobs
- any policies to support domestic producers may be seen as interventionist supply-side policies, which will increase long-run aggregate supply (paragraph 4).

Possible weaknesses:

- the government may not be able to correctly identify the industries that will be able to compete with imports
- domestic products are likely to be more expensive than imports, which is harmful to consumers; impact on low income earners will be significant
- producers like Toni Industries will have to buy from more expensive domestic producers, which increase costs of production (paragraph 5)
- higher tariffs on capital equipment and raw materials will feed through to higher costs of production leading to (cost-push) inflation (diagram) (paragraph 5)
- allows domestic producers to remain less efficient than foreign producers (paragraph 6)
- less choice of consumer goods
- misallocation of resources
- danger of retaliation (paragraph 6).

Any reasonable evaluation.

4. (a) (i) Define the term **budget deficit** indicated in bold in the text (paragraph ❶). [2]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Vague definition.</i> The idea that it is to do with government revenue or spending.	1
2 <i>Accurate definition.</i> An explanation that it is when (planned) government spending is greater than government revenues.	2

(ii) Define the term **economic development** indicated in bold in the text (paragraph ❷). [2]

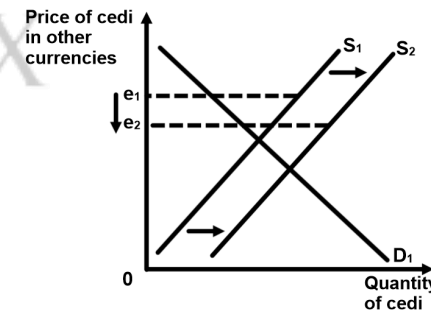
Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>Vague definition.</i> The idea that living standards improve.	1
2 <i>Accurate definition.</i> An explanation that it is a broad concept involving any two of the following: <ul style="list-style-type: none"> • improvement in standards of living • reduction in poverty • improved health • improved education • reduction in unemployment • greater equality in income distribution • environmental protection • increased freedom and economic choice. 	2

(b) Using an exchange rate diagram, explain how the large current account deficit may have affected the value of the Ghanaian cedi. [4]

Level	Marks
0 <i>The work does not reach a standard described by the descriptors below.</i>	0
1 <i>There is a correct diagram or an accurate written response.</i> For drawing a correctly labelled exchange rate diagram for the Ghanaian cedi with the supply curve shifting to the right and a fall in the exchange rate or for providing an explanation that outflows of money on the current account exceed inflows and hence there is increased selling of the Ghanaian cedi that will result in downward pressure on the currency (depreciation of the currency).	1-2
2 <i>There is a correct diagram and an accurate written response.</i> For drawing a correctly labelled exchange rate diagram for the Ghanaian cedi with the supply curve shifting to the right and a fall in the exchange rate and for providing an explanation that outflows of money on the current account exceed inflows and hence there is increased selling of the Ghanaian cedi that will result in downward pressure on the currency (depreciation of the currency).	3-4

Candidates who incorrectly label diagrams can be awarded a maximum of [3].

For an exchange rate diagram, the vertical axis may be exchange rate, price of cedi in other currencies, or other currency per cedi. The horizontal axis should be quantity or quantity of cedi. A title is not necessary.



- (c) Using an AD/AS diagram, explain how the falling value of the Ghanaian cedi may have contributed to inflation.

[4]

Level

0 *The work does not reach a standard described by the descriptors below.*

1 *There is a correct diagram **or** an accurate written response.*

For drawing a correctly labelled AD/AS diagram showing a fall in short-run aggregate supply and an increase in the average price level **or** for explaining that a fall in the value of the cedi will result in an increase in the cost of imported factors of production and therefore a fall in short-run aggregate supply, resulting in (cost-push) inflation.

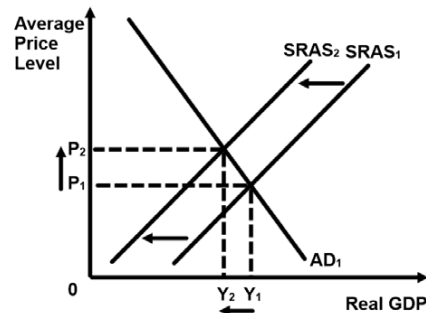
2 *There is a correct diagram **and** an accurate written response.*

For drawing a correctly labelled AD/AS diagram showing a fall in short-run aggregate supply and an increase in the average price level **and** for explaining that a fall in the value of the cedi will result in an increase in the cost of imported factors of production and therefore a fall in short-run aggregate supply, resulting in (cost-push) inflation.

Candidates might explain that the falling cedi results in increasing net exports (X-M) due to cheaper exports and more expensive imports, which increases AD causing demand-pull inflation. This alternative approach should be fully rewarded.

Candidates who incorrectly label diagrams can be awarded with a maximum of [3].

For AD/AS, the vertical axis may be Average (General) Price Level, APL or Price level. The horizontal axis may be real output, real national output, real income, real national income, real GDP or real Y. A title is not necessary.



- (d) Using information from the text/data and your knowledge of economics, discuss possible consequences of International Monetary Fund (IMF) financial aid on Ghana's economic growth and development.

[8]

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

Do not award beyond Level 2 if the answer does not contain reference to the information provided.

Level

0 *The work does not reach a standard described by the descriptors below.*

1 *Few relevant concepts are recognized.*
There is basic knowledge/understanding.

2 *Relevant concepts are recognized and developed in reasonable depth.*
There is clear knowledge/understanding.
There is some attempt at application/analysis.

3 *Relevant concepts are recognized and developed in reasonable depth.*
There is clear knowledge/understanding.
There is effective application/analysis.
There is synthesis/evaluation, supported by appropriate theory and evidence.

Command term

Discuss requires candidates to offer a considered and balanced review that includes a range of arguments, factors, or hypotheses. Opinions or conclusions should be presented clearly and supported by appropriate evidence.

Responses may include:

- an explanation of the differences between economic growth and economic development
- an explanation of the links between growth and development
- an explanation of the sources of economic growth (eg improvements in the quality and quantity of physical and human capital, institutional reform).

Possible positive consequences:

- falling cedi may be limiting economic growth; financial aid from the IMF may be necessary to stop the cedi from falling further (paragraph 1)
- if the cedi appreciates, it may reduce inflation
- any improvements in the economy may improve investor confidence, which will lead to more investment (FDI and portfolio investment) which will contribute to economic growth (paragraph 2)
- the financial aid will force the government to reduce the budget deficit which is acting as a deterrent to investment (paragraph 3)
- the financial aid will force the government to fight inflation which will help economic growth (paragraph 4)
- if investment and growth pick up, there will be more leeway for the government to be able to afford to finance spending on development objectives, although this may only be possible over the longer term.

Possible negative consequences:

- the impact of IMF conditions of reduced government spending, a reduction in subsidies, privatization and a wage freeze on development (paragraph 9)
- opportunity costs of servicing the debt
- IMF aid may be mismanaged (paragraph 9) which will have no impact on development
- the “sacrifices” (paragraph 9) Ghanaians have to make will be anti-developmental.

Any reasonable discussion.

Discussion **may** include more general consideration of the nature of aid, growth and development and relationships between them.

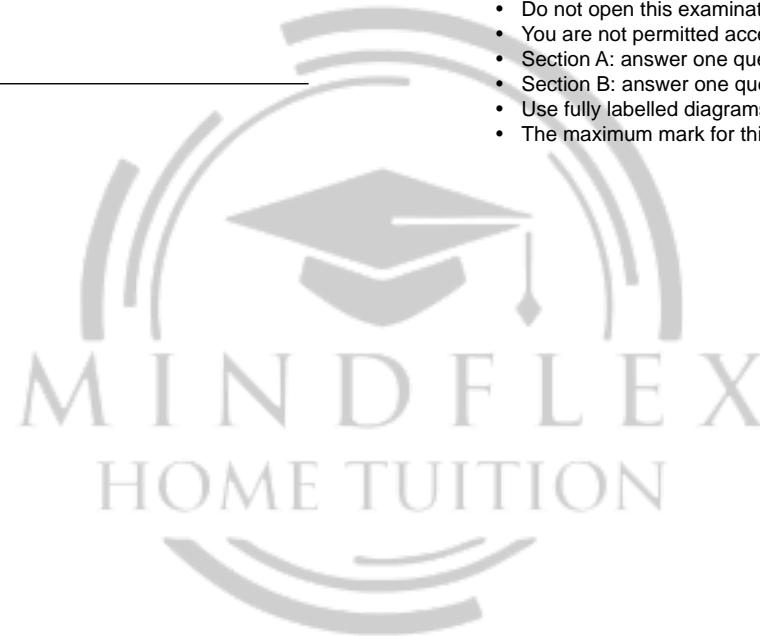
Economics
Standard level
Paper 1

Wednesday 1 November 2017 (afternoon)

1 hour 30 minutes

Instructions to candidates

- Do not open this examination paper until instructed to do so.
- You are not permitted access to any calculator for this paper.
- Section A: answer one question.
- Section B: answer one question.
- Use fully labelled diagrams and references to examples where appropriate.
- The maximum mark for this examination paper is **[50 marks]**.



3 pages

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