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Cambridge International Advanced Subsidiary and Advanced Level

MARK SCHEME for the October/November 2015 series

9708 ECONOMICS

9708/21 Paper 2 (Data Response and Essay – Core), maximum raw mark 40

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Data Response

1 (a) (i) Calculate the percentage change in the price of cereals between 2011 and January 2014. [2]

The price of cereals fell/decreased/declined **(1 mark)** by 21.8%. **(1 mark)**

Accept an answer between 21.0 and 22.0.

Accept a minus sign as indication of a fall in price.

(ii) Explain <u>two</u> possible reasons why the world price of cereals and the world price of dairy products moved in opposite directions between 2012 and January 2014. [4]

Candidates need to explain one reason why the price of cereals fell and one reason why the price of dairy products increased over the time period. The selected reasons could be suggested in the data but any 'possible' reasons are acceptable. The reasons will be based upon supply and demand, so any possible reasons for an increase in the supply and/or a reduction in the demand for cereals and a decrease in the supply and/or an increase in the demand for dairy products can score.

For an explained reason for the fall in the price of cereals. **(Up to 3 marks)**

For an explained reason for the rise in the price of dairy products. **(Up to 3 marks)**

(4 marks maximum)

Maximum of 2 marks without any reason given for the change in demand and/or supply.

(b) Explain how an economist would decide whether cereals and dairy products are substitutes. [3]

For an accurate formula of cross elasticity of demand. **(1 mark)**

For stating that if cereals and dairy products are substitutes the cross elasticity of demand will be positive. **(1 mark)**

For **explanation** of this value in terms of an increase in the price of one product will lead to a rise in demand for its substitute. **(1 mark)**

For **explanation** that the higher the value of the coefficient the closer the two products are as substitutes. **(1 mark)**

(3 marks maximum)

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(c) Use a diagram to illustrate how a subsidy will affect the price and quantity of rice produced in India. [3]

For a diagram showing the shift to the right of the supply curve. **(1 mark)**

For a fall in the price of the product. **(1 mark)**

For an increase in equilibrium quantity. **(1 mark)**

If no diagram is included, but correct description is given, award 1 mark.

If the shift of the supply curve is implied in a diagram, but not actually shown, award 2 marks.

(d) Explain a likely opportunity cost of the Indian Government's spending on the food subsidy. [2]

For a clear statement of the concept of 'opportunity cost'. **(1 mark)**

For an example of opportunity cost in terms of government expenditure e.g. reduced spending on infrastructure, education, health care. **(1 mark)**

(e) Discuss whether food subsidies are likely to solve the world's food shortages in the long run. [6]

For **understanding** of the cause of food shortages e.g. population growth, poor harvests, lack of investment in agriculture and whether subsidies are likely to solve food shortages that arise from these problems. **(Up to 4 marks)**

For **evaluative comment** on the likely effectiveness of subsidies. **(Up to 2 marks)**

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Essays

2 (a) Explain, using the concept of income elasticity of demand, how a fall in incomes affects the demand for inferior goods and necessary goods. [8]

For **knowledge and understanding** of income elasticity of demand. **(Up to 4 marks)**

For **knowledge and understanding** of what income elasticity of demand is. **(1 mark)**

For an accurate formula. **(Up to 2 marks)**

For some elaboration. **(1 mark)**

For **application** of the concept to explain how inferior and necessary goods respond to a fall in incomes. **(Up to 4 marks)**

Application to inferior goods. **(Up to 3 marks)**

Application to necessary goods. **(Up to 3 marks)**

(4 marks maximum)

(b) Discuss the policies that businesses might adopt to maintain sales when incomes are falling and consider which is most likely to be successful. [12]

When incomes are falling the demand for normal and necessary goods, to a lesser extent, will fall. Businesses need to offset this with policies to increase the demand for these goods. For example, advertising is designed to shift the demand curve to the right. A reduction in price will increase sales. Also, some businesses might switch to the production of inferior goods.

Whether policies are successful depends upon a number of factors. For example, the success of price reductions depends upon the price elasticity of demand.

For **analysis** of policies designed to maintain sales. **(Up to 8 marks)**

For **evaluative comment** on the success of the policies suggested. **(Up to 4 marks)**

3 (a) With the help of diagrams, explain how both cost-push and demand-pull inflation can be caused by a falling exchange rate. [8]

For **knowledge and understanding** and **application** showing how a decline in the exchange rate can cause cost-push inflation. **(Up to 4 marks)**

Maximum of 3 marks if no diagram.

For **knowledge and understanding** and **application** showing how a decline in the exchange rate can cause demand-pull inflation. **(Up to 4 marks)**

Maximum of 3 marks if no diagram.

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(b) Distinguish between the domestic and external consequences of inflation and discuss which are the more damaging to an economy. [12]

The internal effects of inflation include the impact upon savings and investment, the effects upon savers and lenders and the haphazard re-distribution of incomes in addition to shoe-leather and menu costs.

The external effects of inflation are principally the effects upon trade. Which is most damaging depends upon issues such as the extent to which an economy is open or closed.

For analysis of the domestic and external effects of inflation. **(Up to 8 marks)**

Up to 6 marks on internal effects.

Up to 6 marks on external effects.

For **evaluative comment** upon which is most damaging. **(Up to 4 marks)**

4 Assume, in a two-country, two-product world, that one economy is more efficient at producing both products.

(a) Explain how the efficient economy can benefit from specialisation and trade with the less efficient economy. [8]

For **knowledge and understanding** of the law of comparative advantage. **(Up to 4 marks)**

For **application** to show how each country can benefit. **(Up to 4 marks)**

(b) Evaluate the economic reasons that the less efficient economy might offer to justify protection of its industries. [12]

A number of reasons are often advanced to justify protection of domestic industries from foreign trade. These include to allow industries to decline slowly, to prevent dumping, for strategic reasons and the infant industry argument. The main reason to support protection is to allow comparative advantage to emerge. So on this basis the infant industry argument is often justified in terms of economic theory.

For **analysis** of the arguments often used to justify protectionism. **(Up to 8 marks)**

For **evaluative comment** on the justification of these arguments. **(Up to 4 marks)**

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