

Cambridge IGCSE® and O Level Economics Workbook Answers

● 1 The basic economic problem

- 1 The correct answer is Option B. Resources in an economy are scarce and needs and wants (of individuals, firms and governments) are unlimited. Option A states that wants are limited and resources are unlimited which is incorrect as wants are unlimited and resources limited. See pages 2–3 in the textbook for a more detailed explanation of the basic economic problem.
- 2 The correct answer is Option A. Public domain web pages are available to anybody with access to the internet. Access therefore is unlimited. The other options (running shoes, housing and tennis rackets) are all limited in supply and are therefore economic goods. See page 2 in the textbook for more examples of economic and free goods.
- 3 The correct answer is Option C. Selling and distributing olive oil is in the tertiary sector of the economy. Options A and D are in the secondary sector as both are part of the manufacturing process. Option B (growing of olive trees) is in the primary sector. See pages 5–6 in the textbook for more detailed information on the three sectors of industry.
- 4 The correct answer is Option C. To increase production of wheat from W_2 to W_1 it is necessary to decrease production of oil from O_2 to O_1 . This is because the PPF represents the maximum amount of wheat and oil that can be produced at each level of output, with all resources used efficiently. Options A and B are incorrect because to increase production of wheat it is necessary to decrease oil production. Option D requires an increase in the productive capacity of the country. See pages 7–9 in the textbook for more detailed information on PPFs.
- 5 The correct answer is Option B. It is possible to increase production within the economy without incurring an opportunity cost, i.e. it is possible to increase both production of wheat and oil without any opportunity cost. Options C and D are on the production possibility curve and therefore represent maximum output in the economy. Point E is unattainable given the current resources in the economy.
- 6 Country X could invest in machinery and/or technology and this will increase the productive capacity of the economy as more oil and wheat can be produced with the same amount of resources.

Country X could train workers to increase their skills and this may increase their productivity as workers become more efficient at producing oil and wheat.

Award 2×2 marks for stating and explaining two ways to increase the productive capacity of Country X.

See pages 132–133 and 217–218 in the textbook for more information on how to increase the productive capacity of the economy.
- 7 Examples of capital-intensive industries: car manufacturing and glass making.

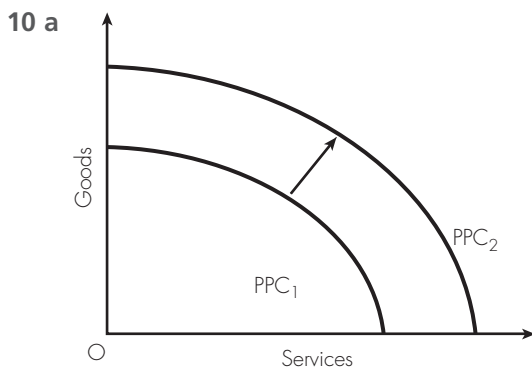
Examples of labour-intensive industries: garment manufacturing and teaching.

Award 1 mark for each relevant example of each type of industry, up to the maximum of 2 marks.
- 8 Opportunity cost is the cost of the next best alternative foregone when making a decision. For example, if a school spends money on a new sports hall, the opportunity cost might be a new science laboratory which could have been built instead. See page 7 in the textbook for a more detailed explanation of opportunity cost.
- 9 The agricultural sector has become less valuable as a percentage of GDP for Country Y because the price of goods being produced may have fallen or people may be leaving the agricultural industry. Instead, with economic development, these people have entered the manufacturing or service sector because earnings are higher in these industries.

The service sector may have increased in value due to growth in the tourism industry and related trades. For example, an increase in tourism will bring about income for the hotel industry, airlines, restaurants, retail outlets (shops) and tourist attractions.

The change in the structure of industry in Country Y could be due to economic growth caused by an increase in the tourism industry typical of a less economically developed country such as Cambodia or Laos.

Award 2 × 2 marks for stating and explaining two reasons for the change in the structure of industry.



The introduction of the internet café causes the PPF curve for the village to shift outwards, from PPC_1 to PPC_2 .

Award 2 × 1 marks for drawing and correctly labelling the axes.

Award 1 mark for drawing the original PPF curve.

Award 1 mark for drawing the new PPF curve to the right of the original PPF curve.

See pages 7–9 in the textbook for further information about production possibility curves.

- b The shift is due to the increased productivity of farmers who can now get the best price for their produce and increase yields of their crops due to improved production techniques. Existing and new businesses can communicate more easily with suppliers and customers, e.g. by using email and Skype. They can also research the market, their competitors and potentially access finance available for investment.

Award 2 × 2 marks for identifying and explaining two possible reasons for increased productivity.

2 Economic systems

- The correct answer is Option C. See page 12 in the textbook for an overview of the three main types of economic systems. Refer to Chapter 1 in the textbook for details about the basic economic problem (Option A) and scarcity (Option B). Economic agents (Option D) refers to households and firms involved in economic activities.
- The correct answer is Option B. In a mixed economy there is both a private sector (comprising of both households and firms) and a public sector (the government). See pages 17–18 in the textbook for an explanation of a mixed economy.
- The correct answer is Option B. In a planned economy, the government oversees production decisions (what, how and for whom production should take place). See page 12 in the textbook for an explanation of the various types of economic systems.
- The correct answer is Option D. In a free market economy, resources are allocated on the basis of demand and supply, e.g. highly skilled workers are paid more than those with a lack of desirable work skills. This can result in huge inequalities in income and wealth (Option D). The other options are disadvantages of operating a planned economy. See pages 14–15 in the textbook for an explanation of these disadvantages.
- The correct answer is Option C. Production takes place to fulfil people's needs and wants, irrespective of the prevailing economic system. Hence, *why* production should take place is not a fundamental economic question. See page 13 in the textbook for an explanation of why the other options are key questions that economists ask.
- Features of a planned economic system include:
 - production decisions are made by the government
 - production schedules are devised on a long-term basis
 - wage differentials are minimal
 - the economy prefers to be self-sufficient.
 See pages 13–14 in the textbook for an explanation of the above features of a planned economy.
- An explanation that prices are determined by the interacting forces of demand (consumers) and supply (producers). Prices are determined when

the demand for and supply of a product are equal (in equilibrium). See page 15 in the textbook for an explanation. An appropriate example must be provided for full marks.

- 8 a An economic system that comprises both a public sector and a private sector.

Alternatively, a combination of planned and free market economies.

See page 12 in the textbook for a definition of a mixed economy, and pages 17–18 for an explanation of mixed economies.

- b Reasons why most countries operate mixed economies include:

- misallocation of resources under a free market economy (see Chapter 5 in the textbook to read more about market failures), e.g. merit goods, demerit goods, public goods and externalities
- government intervention is required for numerous reasons, e.g. environmental protection and to redistribute income and wealth (through the tax system)
- government intervention is also required to regulate and control the activities of private sector firms in mixed economies, e.g. employment rights and anti-competitive business activities.

Award 1–3 marks for a brief explanation which shows a limited understanding.

Award 4–6 marks for an explanation which shows a good level of understanding. The use of appropriate examples should be demonstrated.

- 9 A planned economic system enables basic needs to be met for everyone in society. By contrast, production is disproportionately geared towards those with high incomes and wealth in market economies. See page 16 in the textbook for a more detailed explanation.

- 10 Arguments in favour of a free market economy, include:

- greater efficiency
- freedom of choice/more competition
- incentives to work and to innovate.

Possible disadvantages of a free market economy include:

- environmental issues
- income and wealth inequalities
- social hardship, i.e. inequalities in the distribution of income and wealth
- wasteful competition
- the existence of unregulated monopolies.

See pages 16–17 in the textbook for an explanation of the advantages and disadvantages of market economies.

Award up to 5 marks for a one-sided answer.

Award up to 8 marks for a balanced answer that considers both advantages and disadvantages of a free market economic system.

● 3 Demand and supply

- 1 The correct answer is Option A. Effective demand is used to suggest that demand is backed by both the ability and the willingness of customers to pay a certain price to buy a particular good or service. See page 20 in the textbook for further guidance.

- 2 The correct answer is Option D. If consumers become more aware of the health issues related to sugar, they are less likely to buy sugar, shifting the demand curve to the left. See pages 23–24 in the textbook to read about the differences between shifts and movements in demand.

- 3 The correct answer is Option C. Higher interest rates in China make it more expensive to borrow money to buy cars and encourage more saving rather than spending. See page 104 in the textbook

for an explanation of why an increase in interest rates will affect borrowing, spending and saving.

- 4 The correct answer is Option A. Customers who buy shampoo are likely to need conditioner too. Option C is incorrect as sugar is not jointly demanded with tea (indeed, not all tea drinkers use sugar, and it really depends on the type of tea being considered). Options B and D are examples of substitute products.

- 5 The correct answer is Option D. At \$10 per unit, supply is 21 000 units whilst demand is only 18 000 units, i.e. there is excess supply (a surplus, rather than a shortage) of 3000 units.

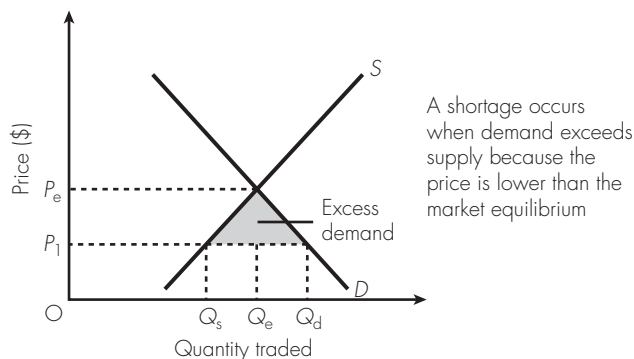
- 6 A movement along the demand curve is caused by changes in the price of a good or service.

Higher prices cause contractions in demand, whereas lower prices cause expansions in demand. However, a shift in demand is caused by changes in non-price factors that affect demand, e.g. changes in income, advertising and the price of substitute products. See pages 23–24 in the textbook for further guidance.

- 7 A normal supply curve is upwards sloping, showing a positive correlation between price and the quantity supplied. This is because at higher prices, firms are more willing and more able to supply at each given price level. See page 25 in the textbook for further guidance.
- 8 Equilibrium price occurs where demand and supply are equal, i.e. surpluses and shortages do not exist, so there is no pressure on the price to change. By contrast, disequilibrium price exists when demand and supply are not equal: there is a surplus when price is above the market equilibrium and a shortage when price is below the equilibrium.

Note: the demands of the question do not require students to draw a demand and supply diagram, although if students choose to do so they should be credited accordingly.

- 9 Excess demand occurs when demand exceeds supply because the price is lower than the market equilibrium, resulting in a shortage.



4 Price elasticity

- 1 Price elasticity of demand

$$= \frac{\text{percentage change in quantity demanded}}{\text{percentage change in price}}$$

$$PED = \frac{\% \Delta QD}{\% \Delta P} = \frac{-5}{+10} = -0.5$$
 Hence, the correct answer is Option C.
- 2 Price elasticity of demand

$$= \frac{\text{percentage change in quantity demanded}}{\text{percentage change in price}}$$

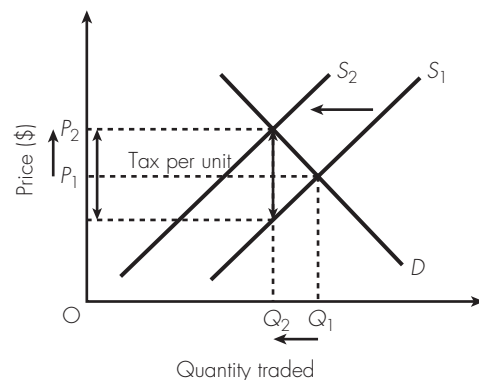
$$PED = \frac{\% \Delta QD}{\% \Delta P} = \frac{-2}{+8} = -0.25$$
 Hence, the correct answer is Option A.

Award up to 2 marks for an answer that does not include a diagram but shows understanding of excess demand.

Award up to 5 marks for a correct explanation of excess demand, with an accurately labelled diagram that shows excess demand exists at all prices below the equilibrium.

See page 31 in the textbook for an explanation of excess demand.

- 10 The imposition of a tax on suppliers causes an increase in their costs, thus shifting the market supply curve to the left from S_1 to S_2 . This raises the equilibrium price from P_1 to P_2 and subsequently reduces the quantity traded from Q_1 to Q_2 .



Imposition of a tax on oil suppliers

See page 30 in the textbook for an explanation of how the imposition of taxes affects market equilibrium.

- 3 The correct answer is Option B. Knowing the PED for a particular product enables firms to know more about how consumer spending is likely to change following a change in the price of the product. For example, if demand is price inelastic, then an increase in the price will not cause consumers to change their spending by very much due to the lack of substitutes.
- 4 The correct answer is Option B. In the short run, hairdressers could work overtime if the market

price of haircuts increased; in the long run more hairdressers could be hired. It is relatively more difficult to increase the output of organic oranges (Option D), at least in the short run. Increasing the number of season tickets (Option C) is very difficult due to the fixed capacity of the stadium (unless Real Madrid Football Club moved to larger premises in the long run). There is a finite/fixed number of original paintings by Picasso so this has the lowest value of PES. See pages 43–44 in the textbook to read more about the value of PES.

5 Price elasticity of demand

$$= \frac{\text{percentage change in quantity demanded}}{\text{percentage change in price}}$$

$$\text{PED} = \frac{\% \Delta \text{QD}}{\% \Delta \text{P}} = \frac{+15}{-25} = -0.6$$

Hence, the correct option is D.

6 a Price elasticity of demand

$$= \frac{\text{percentage change in quantity demanded}}{\text{percentage change in price}}$$

$$\% \Delta \text{QD} = \frac{8640 - 8000}{8000} = +8\%$$

$$\% \Delta \text{P} = \frac{225 - 250}{250} = -10\%$$

$$\text{PED} = \frac{\% \Delta \text{QD}}{\% \Delta \text{P}} = \frac{+8}{-10} = -0.8$$

Note: it is not necessary for students to show the formula for PED in this question.

b Students can take alternative approaches to answering this question.

The PED = -0.8 so the demand for HTC smartphones in Taiwan is price inelastic. This means it is not a good decision to reduce prices, i.e. the percentage change in quantity demanded (+8%) is less than the percentage change in price (-10%). Hence, the firm will lose revenue.

Total revenue has fallen from \$2m per week (\$250 × 8000) to \$1.944m per week (\$225 × 8640). Hence, the decision to cut prices was not a good business decision as HTC has seen a drop of \$56 000 in sales revenue per week.

Award 1–2 marks for an explanation that shows limited understanding.

Award 3–4 marks for an answer that demonstrates a good level of understanding in the context of the question. Calculations and/or the use of quantitative techniques are correct.

7 a Award up to 2 marks for an explanation that as PED = -0.55, a 10% increase in price causes demand for cigarettes to drop by only 5.5% because the demand is price inelastic.

b Factors that affect the PED for cigarettes include:

- the degree of substitution for smokers
- the degree of habits/addiction of smokers
- the proportion of a consumer's income that is spent on cigarettes
- the effectiveness of advertising, e.g. anti-smoking campaigns
- the period of time under consideration for smokers to change their habits, given price changes.

See pages 39–40 in the textbook for an explanation of how the above factors affect PED.

Award 1 mark for identifying a factor that affects the demand for cigarettes and up to 2 further marks for an explanation of the low price elasticity.

8 Award 1 mark for a correct definition of price elasticity of demand (PED).

Award 1 mark for stating that, if demand is price elastic, a reduction in price will increase revenue.

Award 1 mark for stating that, if demand is price inelastic, a reduction in price will reduce revenue.

Award up to 2 additional marks for a developed analysis, e.g. different flights have different PED at different times of the day/week/year; the effect of lower prices on profit will also depend on costs to the airline company.

9 a Price elasticity of demand

$$= \frac{\text{percentage change in quantity demanded}}{\text{percentage change in price}}$$

$$\% \Delta \text{QD} = \frac{215 - 240}{240} = -10.4\%$$

$$\% \Delta \text{P} = \frac{280 - 250}{250} = +12\%$$

$$\text{PED} = \frac{\% \Delta \text{QD}}{\% \Delta \text{P}} = \frac{-10.4}{+12} = -0.867$$

b Knowledge of PED can help Sanchez Sunglasses in several ways, for example:

- knowing the PED for its best-selling sunglasses is price inelastic (0.867), the firm can raise its price knowing that total revenue will increase, from \$60 000 (\$240 × 250) to \$60 200 (\$280 × 215)
- knowledge of PED can also inform Sanchez Sunglasses about the extent to which the firm has market power, e.g. if demand becomes more price elastic (its PED is not too far off from a value of 1.0) the firm may need to improve the marketing of its sunglasses to customers.

Accept any other reasonably explained answer in the context of Shanchez Sunglasses.

Award 1–2 marks for an answer that shows limited understanding.

Award 3–4 marks for an answer that demonstrates a good level of understanding, written in the context of Shanchez Sunglasses.

There is application of the answer from Question 9a.

10 Factors that affect the value of PES include:

- the degree of spare productive capacity
- the level of (spare) stocks

● 5 Market failure

1 The correct answer is Option C. Car parks are not an example of market failure because car parks and cars are complementary goods, with their demand and supply determined by market forces. Options A and B both have impacts on third parties who do not drive cars or produce the air pollution. Option D is incorrect because the supermarket charges higher prices than if it operated in a competitive market. See page 49 in the textbook for a definition and examples of market failure.

2 The correct answer is Option B. A tax on cars increases the cost of owning a car and therefore the demand for cars should decrease (this may of course not happen due to price or income inelastic demand for cars in some countries). Options A and C would encourage car ownership and therefore the number of cars on roads. Option D would not have a direct impact on the demand for cars.

3 The correct answer is Option D. Resources are not conserved as land is built upon to create the new airport terminal. Option A (external costs) includes traffic congestion and noise and air pollution caused by building the addition airport terminal. Option B (external benefits) includes the employment and business opportunities created which may increase standards of living and incomes in the area. Option C (opportunity cost) refers to the loss of land and the alternative projects which the government could have spent the money on.

4 The correct answer is Option C. A fall in the price of petrol would make petrol-fuelled cars more attractive than electric cars. Options A, B and D would all increase the demand for electric cars. Option A (an increase in tax) would make

- the number of producers in the industry
- the ease and cost of factor substitution, e.g. using machinery instead of labour
- the time period under consideration.

See pages 46–47 in the textbook for an explanation of how the above factors affect PES.

Award up to 2 marks for an explanation of each factor that affects PES. For maximum marks, there must be use of relevant examples.

petrol-fuelled cars more expensive. Option B (a subsidy) would make electric cars cheaper and therefore more attractive and Option D (increased advertising) should increase the demand for electric cars, assuming the advertising is successful.

5 The correct answer is Option A. Public housing funded by the government is an example of public expenditure and provides private benefits to those who are given public housing to live in. Options B, C and D all provide external benefits to society. Option B provides leisure facilities and a source of education for citizens, thus is of benefit to the general public. Option C provides the public with a park to enjoy and the plants and green space improve the natural environment. In Option D, people are trained and educated so become more occupationally mobile, thus benefiting firms. They may also train others, thus increasing the skills of a larger pool of workers.

6 Examples of goods/services provided by a government because they would otherwise be under-consumed by society include:

- health care
- education
- public libraries
- parks
- museums
- roads
- refuse/garbage collection.

Award 1 mark for each example.

See pages 56–57 in the textbook for a more detailed explanation of public versus private expenditure.

7 External costs/negative externalities include:

- negative effects of gambling, alcohol consumption and smoking in the casinos; for example, social consequences of gambling for families of people who become indebted, negative health effects of alcohol and potential anti-social behaviour caused by excessive drinking, effect of cigarette smoke on non-smokers
- loss of vegetation and green spaces due to construction of hotels and tourist attractions
- loss of local culture to casino culture as local restaurants and shops are lost to multinational chains and old buildings are demolished to make way for new hotels with casinos
- noise and air pollution caused by construction and increased traffic.

External benefits/positive externalities include:

- employment opportunities providing income for workers who then spend the income in other businesses
- higher tax revenues which may result in a greater provision of public and merit goods for the citizens of Macau
- an increase in economic growth which may lead to increased standards of living for the citizens of Macau.

Award 2 marks for identifying and explaining each example of an external cost and/or an external benefit.

See pages 49–51 in the textbook for further explanations of external costs and pages 55–56 for further explanations of external benefits.

8 Advantages of regulation and fines include:

- the fine will act a deterrent for using mobile phones on public transport
- money collected from fines can be used to fund educational campaigns to reduce mobile phone use
- travelling on public transport may become more pleasant/peaceful as there is less noise pollution
- people may arrive at work more relaxed/less stressed.

Disadvantages of regulation and fines include:

- people cannot use phones, which may reduce their productivity because, for example, they may need to make personal phones calls at work instead (which they could previously do whilst travelling to/from their workplace)

- similarly, people cannot make work-related calls so this may reduce productivity and therefore output
- people may ignore the ban, so it becomes difficult to enforce
- officials need to be employed to check whether people are following the ban on mobile phone usage on public transport and this will increase costs
- people may use mobile phones outside train carriages or bus stops and this may cause congestion and noise pollution there.

Award 1–2 marks for an answer that shows limited understanding.

Award 3–4 marks for explaining the advantages and disadvantages of a ban on using mobile phones on public transport. There may be a lack of detail and/or use of relevant examples.

Award 5–6 marks for a detailed analysis of the advantages and disadvantages of a ban on using mobile phones on public transport. There is appropriate use of terminology and use of examples.

See pages 51–52 in the textbook for a more detailed analysis of the advantages and disadvantages of using regulation and fines as a solution to market failure.

9 Social costs of the dam include:

- loss of land and damage to the environment caused by the construction of the dam
- displacement and reallocation of over 1 million people, causing disruptions to their lives and livelihood
- loss of cultures of local villages and towns.

Social benefits of the dam include:

- the production of a large amount of hydroelectric power which may lower costs and produce a reliable energy supply
- creation of jobs for the construction and management of the project.

Award 1–2 marks for an answer that shows limited understanding.

Award 3–5 marks for a balanced discussion of the social costs and benefits of the project. There may be a lack of detail and/or use of relevant examples.

Award a maximum of 5 marks if only social costs or benefits are discussed.

Award 6–8 marks for a detailed discussion of the social costs and benefits of the project. There is appropriate use of terminology and use of examples. For full marks, there must be a reasoned judgement/conclusion made.

- 10 a** Social benefits are the societal gains from the consumption or production of a good or service. For example, university education can lead to increased productivity due to increased skills and knowledge (human capital). Social benefits arise when the external benefits of an activity are greater than the private benefits.

Award 1 mark for an accurate definition.

Award 1 mark for a relevant example.

See page 55 in the textbook for more information on social benefits.

- b** An advantage of charging people for a university education is that there is no opportunity cost incurred by the government as people are responsible for the private costs of their own education.

Another advantage is that people are more likely to study hard because they are paying for their education.

Award 2 marks for identifying and explaining each advantage of charging people for a university education.

- c** A disadvantage of charging people for a university education is that people on low incomes may be unable to afford to go to university and this will discourage people from attending university.

Another disadvantage is that the high price may discourage many people from going to university and in the long term this may lower the level of skills and expertise in the economy.

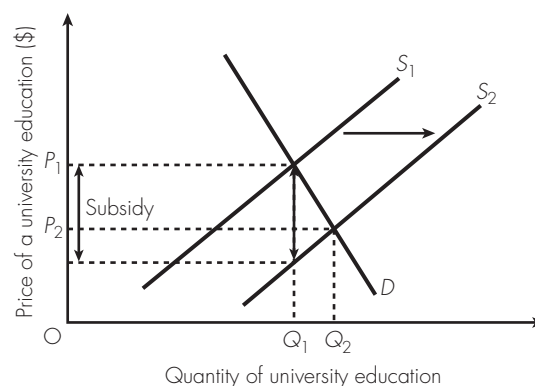
Award 2 marks for identifying and explaining each disadvantage of charging people for a university education.

- d** If a government subsidises the cost of university education, the supply curve will increase from S_1 to S_2 and the price of the university education will fall from P_1 to P_2 . Subsequently, the quantity demanded will rise from Q_1 to Q_2 .

Award 1 mark for a shift in the supply curve.

Award 1 mark for identifying the new lower price.

Award 1 mark for identifying the new higher quantity demanded/supplied.



Award 1 mark for identifying the level of subsidy.

See page 56 in the textbook for more information on the impact of governments subsidising merit goods such as education.

- e** The short-term and long-term benefits of a government subsidising university education include:
- the price of attending university will fall and therefore the demand for a university education will increase; this should result in more people going to university
 - university graduates are likely to have higher earnings and this will lead to higher consumption of goods and services in the long term which should increase GDP and therefore economic growth
 - an increase in the number of people with a university education will cause the human capital in an economy to increase in the long term and this should increase the productive capacity of the economy in the long term
 - increased consumption and productivity will increase GDP in the long term.

The short-term and long-term disadvantages of a government subsidising university education include:

- no immediate increase in human capital in the economy as it takes time to increase skills and knowledge
- a possible surplus of university graduates and therefore many unemployed graduates due to the over-consumption of university education
- the opportunity cost of the government funding university education because the money spent could have been spent on alternative programmes, e.g. health care, public housing, roads, airports or public transport.

Award 1–2 marks for an answer that shows limited understanding.

Award 3–5 marks for a balanced discussion of the short-term and long-term effects of a government subsidising university education. There may be a lack of detail and/or use of relevant examples.

Award a maximum of 5 marks if only short-term or long-term impacts of a government subsidising university education are

discussed, or if an unbalanced argument is presented.

Award 6–8 marks for a detailed discussion of the short-term and long-term effects of a government subsidising university education. There is appropriate use of terminology and use of examples. For full marks, there must be a reasoned judgement/conclusion made.

● 6 Money

1 The correct answer is Option C. Durability is a characteristic of money, not a function of money. See page 62 in the textbook for an explanation of the four functions of money: measure of value, store of value, medium of exchange and a standard of deferred payment.

2 The correct answer is Option D. Bartering (swapping) enables trade and exchange to take place in the absence of money. See page 62 in the textbook for an explanation of why Options A, B and C are problems associated with bartering.

3 The correct answer is Option D. The central bank is not involved with commercial lending of money to facilitate the growth of companies – this is the role of commercial banks and the stock exchange (see page 65 in the textbook). See pages 63–64 in the textbook for an explanation of the function of central banks.

4 The correct answer is Option C. The other options are primary functions of commercial banks. See pages 68–69 in the textbook for an explanation of both primary and secondary functions of commercial banks.

5 The correct answer is A. Stock exchanges enable institutions and individuals to buy and sell shares in listed companies (public limited companies). See pages 65–67 in the textbook for an explanation of the functions of stock exchanges.

6 Money is any commodity that can be used as a medium of exchange that is accepted for the purchase of goods and services. It must therefore be acceptable, durable, divisible and recognisable. See pages 60–61 in the textbook for a more thorough explanation.

7 Explanations could include how bank notes function as money and/or the characteristics that make bank notes suitable as money.

- Functions of money: medium of exchange, measure of value, store of value and a standard of deferred payment.
- Characteristics of money: durability, portability, scarcity, uniformity, divisibility and acceptability (as legal tender).

See pages 60–61 in the textbook for an explanation of the characteristics of money and page 62 for an explanation of the functions of money.

Award up to 2 marks for each reason that is explained clearly, up to the maximum of 4 marks.

8 Functions of a central bank include:

- responsibility for overseeing the country's monetary policies
- the sole issuer of bank notes and coins in the country
- to act as the government's bank
- to act as the bankers' bank and oversee the commercial banking sector
- being the lender of last resort.

See pages 63–64 in the textbook for an explanation of the functions of central banks.

Award up to 2 marks for each reason that is explained clearly, up to the maximum of 4 marks.

9 Functions of commercial banks include:

- accepting bank deposits of money and savings
- making advances, i.e. making personal and commercial loans
- helping customers to make and receive payments, including cheque clearance
- providing financial advice, e.g. savings and retirement plans
- credit creation, e.g. providing overdraft facilities and credit card facilities.

Other services or functions include:

- helping customers to buy and sell shares
- providing bureau de change facilities for foreign exchange
- storing valuables in safe deposit boxes in bank vaults
- internet banking facilities.

See pages 68–69 in the textbook for an explanation of the functions of commercial banks.

Note: there is no need for students to distinguish between primary and secondary functions of commercial banks in this question.

Award up to 2 marks for each reason that is explained clearly, up to the maximum of 4 marks.

10 a An initial public offering (IPO) occurs when a firm decides to 'go public' by selling its shares on a stock exchange for the first time. The IPO enables the firm to raise much-needed capital for its operations.

b Functions of a stock exchange include:

- raising share capital for businesses (\$25 billion in the case of Alibaba.com)
- facilitating company growth
- acting as a market for trading shares
- facilitating the sale of government bonds

- providing safety of transactions, boosting confidence in the trading of shares.

Award full marks for the clear identification and explanation of any two functions of a stock exchange.

Read pages 65–67 in the textbook for an explanation of the functions of stock exchanges.

c Reasons for Alibaba.com choosing to float (sell) its shares on the stock exchange in the USA include:

- the NYSE provides a platform for individuals, organisations and governments to buy shares in Alibaba.com, thus raising share capital for the e-commerce business
- the flotation of Alibaba.com shares (the main source of finance for public limited companies) can raise huge amounts of finance for the company to fund its growth
- share ownership can create much wealth for the founders, owners and investors of Alibaba.com
- the efficient functioning of the NYSE helps to create business and consumer confidence in Alibaba.com, further boosting investment opportunities.

Accept any other reasonable answer in the context of Alibaba.com.

● 7 Labour markets

1 The correct answer is Option C. Some professional footballers are rewarded because of their superior talent and skills. Option A is incorrect because the relatively short working life of a footballer is not considered when deciding upon their salary. Option B is incorrect because football is not a dangerous profession. Option D is also incorrect because, although football is seasonal, this is not considered when deciding upon salaries. See page 128 in the textbook for a list of the top-paid footballers according to *Forbes* magazine.

2 The correct answer is Option D. Public sector jobs tend to offer greater job security and a pension after retirement (although due to public sector budget cuts in many countries this may change in the future). Options A, B and C are all advantages of working in the private sector.

3 The correct answer is Option A. Unemployed workers may have a greater incentive to seek work, i.e. an increase in the NMW makes work

more attractive. Option C is an advantage to firms, whilst Option D is an advantage for the government. Option B is a possible advantage to individual firms and to the economy in general as national output should increase.

4 The correct answer is Option C. Some women work part-time or flexible hours to fit in with childcare or to look after relatives and therefore their wages tend to be lower on average. Options A, B and D are all reasons why women can earn similar wages to men. See pages 82–83 in the textbook for more information on differences in earning between male and female workers.

5 The correct answer is Option B. If a production process becomes too dependent upon a particular worker and the worker leaves the firm or is absent from work, then the production process will slow down and productivity will fall. Options A, B and D are all advantages of specialisation of labour to a firm.

6 Wage factors may include:

- wage rate or salary
- bonuses
- fringe benefits or perks
- profit-related pay
- commission earned on sales.

Non-wage factors may include:

- career prospects
- level of experience and education required
- training opportunities
- working hours
- level of responsibility
- level of challenge
- personal satisfaction gained from the job
- social environment
- level of danger.

Award 2 marks for stating and explaining each wage and non-wage factor that affects a person's choice of occupation.

See pages 71–72 in the textbook for more detailed information about wage and non-wage factors which affect a person's choice of occupation.

7 Ways a government can influence the supply of labour in an economy include:

- provision of training and education for workers to increase their skills and enable them to develop new ones
- introduction of a national minimum wage (NMW) or an increase in the NMW to encourage more people to join the workforce
- lowering welfare payments to the unemployed in order to encourage them to join the workforce instead
- raising the retirement age to increase the number of people in the workforce
- provision of childcare facilities to encourage more women to join the workforce.

Award 2 marks for identifying and explaining each way a government can influence the supply of labour.

See pages 77–80 in the textbook for more information about factors which affect the supply of labour.

8 Reasons why average earnings change over a person's lifetime include:

- earnings rise with experience and therefore people aged 35–44 years typically earn significantly more than those aged between 20–24 years, as shown in the table
- people tend to reach the peak of their career in their mid-forties and their wages tend to stay the same after that time
- people tend to retire at or around 65 years old, so their earnings fall when they reach this age, as shown in the table.

See page 73 in the textbook for more information about why earnings typically change over a lifetime.

9 Factors that might affect the demand for labour in Koh Lanta include:

- the number of tourists visiting Koh Lanta as this will impact upon the number of workers required to work in the hotel and tourism industries
- economic growth in the rest of the world will impact upon the number of tourists visiting Thailand as low growth would suggest fewer overseas trips to places like Koh Lanta, thus negatively impacting on the demand for labour
- the cost of labour in Koh Lanta will affect the demand for labour
- the productivity of workers will affect the demand for labour.

Factors that might affect the supply of labour in Koh Lanta include:

- average wages and benefits (perks) that can be earned in the tourism industry as compared to other industries
- the labour participation rate in Koh Lanta or Thailand, e.g. the number of women in the workforce, the retirement age, the school leaving age and number of full- and part-time workers in the workforce
- the availability of welfare benefits in Koh Lanta, as it may prove more attractive to claim welfare benefits rather than to work
- the seasonal nature of the work might not appeal to some workers because they need/ want to find full-time employment rather than seasonal work in the tourism industry; these workers might move to other parts of Thailand to find work
- the availability of alternative work in Koh Lanta outside of the tourism industry.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–4 marks for explaining the factors that affect the demand and supply of labour in Koh Lanta. There may be a lack of detail and/or use of relevant examples.

Award 5–6 marks for a detailed analysis of the demand and supply factors that affect the labour market in Koh Lanta. There is appropriate use of terminology and use of examples.

See pages 74–80 in the textbook for more detailed information about factors that affect the demand for and supply of labour.

10 Advantages of specialisation for someone like Frederica include:

- she becomes an expert in knitting and therefore is more efficient and productive
- the quality of her work may increase
- her expertise may gain her a reputation for producing hand-knitted garments so her work may be in great demand

- her potential earnings may increase as a result of the above.

Disadvantages of specialisation to Frederica include:

- the work may become repetitive and boring for her
- Frederica may become too specialised and if demand for hand-knitted garments decreases she will earn less income
- Frederica may lose skills or be unable to develop skills in other areas.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–4 marks for explaining the advantages and disadvantages of specialisation of labour for Frederica. There may be a lack of detail and/or use of relevant examples.

Award 5–6 marks for a detailed analysis of the advantages and disadvantages of specialisation of labour for Frederica. There is appropriate use of terminology and use of examples.

See page 86 in the textbook for more information on specialisation of labour.

● 8 Trade unions

- 1 The correct answer is Option B. If there is high demand for toys produced in the factory then there is a demand for workers to make the toys, so a pay rise may be justified. Option A is incorrect because if inflation is low in an economy then it may be difficult for the trade union to negotiate a pay rise to cover increased cost of living. Option C is incorrect because if there is a large number of people willing to work in the factory, the labour supply is high so there is no need to increase wages to keep people in the job. Option D is also incorrect because if workers become less productive there is little justification to increase their wages.
- 2 The correct answer is Option A. Increased profits in an industry may justify a wage increase as workers have clearly contributed to this. Option B is incorrect because lower productivity would increase production costs to a firm so higher pay would not be justified. Option C is incorrect because a fall in inflation suggests a fall in the cost of living and Option D suggests that there are surplus workers in the labour market willing to work; hence higher wages cannot be justified. See page 90 in the textbook for a more detailed explanation.
- 3 The correct answer is Option C. Options A, B and D are incorrect examples of industrial action.

See page 91 in the textbook for more detailed explanations of the different types of industrial action.

- 4 The correct answer is Option B. Trade unions are established to protect the rights of workers and to improve their pay and working conditions. Option A is incorrect because, although action from trade unions may increase publicity for their members, it is not their main aim. Options C and D occur if negotiations do not bring about satisfactory solutions to work-related disputes and discussions. A trade union may call its members out on strike and may cause disruption to an economy but these are not aims of a trade union. See page 90 in the textbook for a more detailed explanation of the role of trade unions.
- 5 The correct answer is Option C. Workers are working to the 'rules' of their contract. They are not committing any offences and therefore cannot face disciplinary action. Options A, B and D are all other forms of industrial action. See page 91 in the textbook for more detailed explanations of the different types of industrial action.
- 6 Collective bargaining is the process between members of a trade union (who elect a representative to meet with the management

representatives of the firm or leaders of the industry) to negotiate improved terms and working conditions on behalf of the members of the labour union. A collective voice is more powerful than each worker negotiating individually with an employer.

7 Possible reasons why trade union membership has fallen in the UK are:

- changes to legislation have reduced the powers of trade unions so less people may have joined
- some people have a negative viewpoint of trade unions and therefore have not become members
- there has been a decline in the manufacturing industry, which was typically unionised
- there has been an increase in employment in jobs which are not unionised*, e.g. jobs in the retail sector (shop workers), office work, employment in small businesses (such as hairdressers) and independent shops
- there has been an increase in part-time employment
- there has been an increase in employment in professional jobs which typically do not have a trade union as they are managed by professional organisations
- loss of jobs in the public sector, which is unionised.

*unionised = a job or trade which has a trade union to represent workers

Award 2 marks for stating and explaining each possible reason for a fall in trade union membership, up to a maximum of 4 marks.

See pages 93–94 in the textbook for more information on factors which affect trade union membership.

8 Possible reasons why more women are becoming members of trade unions include:

- more women are entering the workforce
- there is a disproportionately large number of women in low paid jobs
- there are more women in jobs with poor working conditions, so union membership becomes more desirable
- there are more women on flexible and part-time contracts who require protection from a trade union
- there is an increase in the wealth gap (the gap between rich and poor) so women wish to

attempt to achieve better pay and working conditions through union membership.

Award 2 marks for identifying and explaining each reason why more women may be joining a trade union, up to a maximum of 4 marks.

9 The main functions of trade unions include:

- bargaining with employers for pay rises and better terms and conditions of employment for their members
- ensuring equipment at work is safe to use (supported by Health and Safety legislation) and that workers are given sufficient training to enable them to perform their role at work safely
- ensuring members are given legal advice when necessary
- giving support to members when they are made redundant
- providing financial and legal support to workers who may have been unfairly dismissed or disciplined
- to persuade the government to pass legislation in favour of workers, such as legislation covering minimum wages, maximum working hours, health and safety, pension rights and the retirement age.

Award 2 marks for describing each main function of trade unions, up to a maximum of 4 marks.

See page 88 in the textbook for more information about the role of trade unions.

10 Benefits of trade unions to an economy include:

- better pay and working conditions for workers, which may lead to improved efficiency and higher productivity in the economy
- trade unions provide a channel of communication between employees, employers and governments and this may lead to better relationships between these parties; this helps to improve motivation and to reduce absenteeism at work, thus benefiting the whole economy
- if trade unions negotiate a higher minimum wage then more people may be encouraged to work and the unemployment rate may fall.

Costs of trade unions to an economy include:

- trade unions tend to ask for higher pay and better working conditions which will increase costs to businesses so fewer workers may be employed

- industrial action brought about by trade unions may cause disruptions to the economy because of working days lost or fewer hours worked.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–5 marks for a balanced discussion of the costs and benefits of trade unions to an economy.

There may be a lack of detail and/or use of relevant examples.

Award 6–8 marks for a detailed discussion of the costs and benefits of trade unions to an economy. There is appropriate use of terminology and use of examples. There must be a reasoned judgement/conclusion made for full marks.

● 9 Income and expenditure

- 1 The correct answer is Option B. Higher interest can be earned on savings, thus creating an incentive to save. Option A would reduce incentives to save as less interest is earned on savings. Option C would result in less disposable income for people as they have to pay more income tax so they would save less. Option D would encourage people to increase their borrowing and therefore they would save less. See pages 104–105 in the textbook for a more detailed explanation on incentives for saving.
- 2 The correct answer is Option B. Residential property will have a high value so the money borrowed will be paid back over a long period of time. Options A and D are current spending and therefore would not require a large amount of borrowing. It is unlikely that a bank would lend money for a holiday as there would be no security on the loan unlike on a loan for residential property, therefore Option C is incorrect. See pages 106–107 in the textbook for a more detailed explanation of motives for borrowing.
- 3 The correct answer is Option B. An increase in real wages may mean an increase in real incomes in the economy and therefore people may experience a positive wealth effect and increased standards of living. They may feel confident about borrowing and therefore borrowing increases in the economy. Options A and D would discourage borrowing due to the fall in disposable income. Option C would also discourage borrowing because the outlook for the economy is negative. See pages 106–107 in the textbook for a more detailed explanation of motives for borrowing.
- 4 The correct answer is Option D. Retired people tend to be dissaving (i.e. spending their savings) whilst borrowing will be low. Spending will represent a high proportion of their income. Option C is likely to be the pattern of a person aged 35–45 because they are saving for their retirement and likely to be purchasing property. Option A is likely to be that of a 25–35 year old because they are having to spend a high

proportion of their income as well as take advantage of borrowing opportunities. Option B could be a person nearing retirement age who is trying to save a high proportion of their income and spend little. See page 103 in the textbook for more information about patterns of spending, saving and borrowing at different stages in a person's lifetime.

- 5 The correct answer is Option A. An increase in the rate of inflation will cause a decrease in the purchasing power of money so the cost of goods and services increases which leads to lower consumption. Options B and D will lead to an increase in consumer spending. Option C should mean that people will have to spend less of their income on health care and education. See page 101 in the textbook for more information on the impact of inflation on consumer spending.
- 6 An increase in interest rates will cause spending to decrease because:
 - the cost of borrowing increases and therefore the demand for loans will fall
 - a higher cost of borrowing will cause existing repayments on loans to increase and therefore consumer spending will fall.

An increase in interest rates will cause saving to increase because:

- there is a higher return to be earned on savings
- there is a greater opportunity cost of spending.

An increase in interest rates will cause borrowing to decrease because the cost of borrowing has increased and therefore demand for loans will fall.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–4 marks for explaining how an increase in interest rates will affect spending, saving and borrowing. There may be a lack of detail and/or use of relevant examples.

Award 5–6 marks for a detailed analysis of how an increase in interest rates will impact upon spending, saving and borrowing. There is appropriate use of terminology and use of relevant examples.

7 The advantages of a high savings ratio include:

- people have funding for their retirement, so the government does not need to fund this
- people have funds for university education for their children or to support themselves if they lose their job or face an emergency; again, this means the government does not have to spend money on education and unemployment benefits
- saving a proportion of income helps to prevent demand–pull inflation caused by excessive spending
- the banks have deposits to lend to borrowers which may include individuals, firms and governments, which can contribute to economic growth.

See page 107 in the textbook for more information about the impact of a low savings ratio on an economy.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–4 marks for explaining the benefits of saving. There may be a lack of detail and/or use of relevant examples.

Award 5–6 marks for a detailed explanation of the benefits of saving to an economy. There is appropriate use of terminology and use of relevant examples.

8 Factors which affect the level of domestic spending in an economy include the following:

- Lower interest rates. See page 102 in the textbook for more information on the effect of interest rates on consumer spending.
- Lower direct and indirect taxation. See pages 186–187 in the textbook for further information on the effect of taxation on consumer spending.
- Decreasing government spending on health care, education and pensions so that people would have to spend their own money on these services.
- Level of confidence in the economy, e.g. if the economy is predicted to grow and the economic outlook is positive then confidence will be high so people will spend more. See page 102 in the textbook for more information on the effect of confidence levels on spending.

- Status attached to owning goods, e.g. if people attach status to owning designer goods or expensive cars then spending will tend to increase. See page 100 in the textbook for more information on the effect of conspicuous consumption on spending.
- If there has been an increase in wealth in the economy, e.g. if the value of property and investments has increased, people will tend to spend more. See page 100 in the textbook for more information on the effect of wealth on spending.
- Low inflation may cause people to spend more of their income. See page 101 in the textbook for more information on the effect of inflation on spending.
- The age of the population will affect spending patterns as an ageing population will have to spend their savings whereas a youthful population will have to spend a large proportion of their income. See page 103 in the textbook for more detailed information on the impact of age on expenditure patterns.
- Income levels within the economy, e.g. high income earners tend to be able to spend a higher proportion of their income on luxury goods and services whereas low income earners will spend a larger proportion of their income on necessities. See page 97 in the textbook for a more detailed explanation of expenditure patterns of low, middle and high income earners.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–5 marks for a balanced discussion of the factors which influence spending. There may be a lack of detail and/or use of relevant examples.

Award 6–8 marks for a detailed discussion of the factors that influence spending. There is appropriate use of terminology and use of examples. There must be a reasoned judgement/conclusion made for full marks.

- 9** High income earners are able to save a greater proportion of their income than low income earners. They can also afford to spend a larger amount on luxuries as well as necessities. They will not need to borrow to cover current expenditure but may find it relatively easy to borrow money to purchase property and other valuable assets because they have assets to provide security for the loans.

Middle income earners will save a smaller proportion of their income and spend a larger proportion of their income on necessities and other goods and services than high income earners. They will borrow to fund large items of expenditure, e.g. a mortgage to purchase property.

Low income earners will spend a large proportion of their income on current expenditure and may only be able to save a small proportion of their income (or in some cases be unable to save at all). They may borrow to fund large capital items of expenditure but banks may be unwilling to lend them money because they are considered to be at risk of not being able to pay back the loan.

Note that some high income earners may have high levels of borrowing and may save a small proportion of their income because they spend a large proportion of their income repaying debt and spending on luxury goods and services. Some low and middle income earners may save a larger proportion of income because they are saving up for their retirement and/or are concerned about the threat of unemployment.

See page 97 in the textbook for detailed information on different expenditure patterns of high, middle and low income earners.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–5 marks for a balanced discussion of the spending, saving and borrowing patterns of low, middle and high income earners. There may be a lack of detail and/or use of relevant examples.

Award 6–8 marks for a detailed discussion of the spending, saving and borrowing patterns of low, middle and high income earners. There is appropriate use of terminology and use of examples. There must be a reasoned judgement/conclusion made for full marks.

10 a Possible reasons people save are:

- for retirement
- to have reserves if they become unemployed
- to buy a large item of capital expenditure, e.g. a car, or to go on a foreign holiday or get married
- to fund their children's education
- to earn money on savings through interest rates.

b The proportion of income saved will vary because of:

- the age of the population, e.g. if the average age of the population is under 25 (or over 65 years old) then the proportion of saving will be lower than if the population is older because young people do not have the income to save (and retired people are spending their savings, i.e. dissaving)
- savings ratios (proportion of disposable income saved) may be higher in Mexico because people may need to save for retirement and may be concerned about the future in terms of unemployment and low business and consumer confidence
- government policies such as interest rates and taxation, e.g. in Mexico the interest rate may be high and this will encourage saving
- government's attitude to savings, e.g. a government may wish its citizens to save to fund their own pensions in retirement and may provide tax efficient schemes to facilitate this
- the amount of merit goods provided by the government, e.g. state pensions and university education; in Finland the government may provide free health care and welfare benefits for the elderly, including a state pension and hence, citizens of Finland do not need to save for these services
- the level of income of citizens will impact on the level of savings, e.g. Australian citizens may be able to save more than those in the UK because of higher income levels.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–5 marks for a balanced discussion of the reasons for the differences in savings ratios between countries. There may be a lack of detail and/or reference to the data.

Award 6–8 marks for a detailed discussion of the reasons for the differences in savings ratios between the countries. There is appropriate use of terminology, use of examples and reference to the data. There must be a reasoned judgement/conclusion made for full marks.

● 10 Business organisation

- 1 The correct answer is Option B. A private limited company can only sell shares to family and friends. Option A is a government funded organisation and therefore does not sell shares to raise finance. A public limited company (Option C) can sell shares to the general public. A partnership (Option D) cannot sell shares.
- 2 The correct answer is Option B. Firms may use internal accounting procedures to declare profits in another country with a lower tax rate than the UK (Starbucks, Amazon and Google have all been accused of tax evasion in the UK; they have tried to pay less tax in the UK by declaring profits elsewhere). Option A may be an advantage because it encourages local firms to innovate and be efficient. Option C is a reason why firms may locate in the UK and is therefore an advantage to foreign firms. Option D is an advantage of foreign firms locating in an economy.
- 3 The correct answer is Option A. Farmers might group together to have more bargaining power when they buy agricultural supplies in bulk than if each farmer bought their supplies individually. Option B is incorrect because producer co-operatives promote co-operation rather than reduce competition. Option C is incorrect because a producer co-operative is designed to reduce costs for farmers and not for farmers to form a monopoly. Option D is incorrect because the producer co-operative benefits farmers and not the wider society.
- 4 The correct answer is Option C. Co-operatives are based on the principle of being owned and run by their members with the aim of creating value for them. Option A is incorrect because a public corporation is funded by the government and provides a service for the general public. Option B is incorrect because private limited companies are obliged to make a profit for their shareholders. Option D is incorrect because, although partnerships are owned and controlled by the partners, their main aim is to produce profits.
- 5 The correct answer is Option C. Both a partnership and a sole trader have unlimited liability. Option A is incorrect because it applies to a sole trader and not a partnership. Option B is incorrect because this applies to a partnership only. Option D is incorrect because neither a sole trader nor a partnership can sell shares, not even to family and friends.
- 6 The main differences between a partnership and a private limited company include:
 - a partnership has unlimited liability whilst a private limited company has limited liability
 - a private limited company can raise money by selling shares to family and friends whilst a partnership can raise money through the partners' personal funds and bank loans
 - profits in a partnership are shared between the partners whereas shareholders in a private limited company may receive dividends from the profits of the company.

Award 2 marks for each difference identified and explained, up to a maximum of 4 marks.

See pages 110–116 in the textbook for more detailed information on partnerships and private limited companies.
- 7 The reasons an individual might buy shares in a public limited company include:
 - they receive dividends (a share of the profits) based on the number of shares they own; this is a form of income for the individuals
 - purchasing shares is a form of investment as buyers hope that the value of the shares will rise in the future so that they can make a capital gain when they sell the shares.

Award 2 marks for each reason identified and explained.
- 8 Business organisations in an economy may:
 - produce goods and services which satisfy the needs and wants of individuals in society
 - provide employment opportunities for workers and therefore an income for individuals
 - purchase goods and services from other businesses in the economy and therefore increase the earnings of other firms
 - produce goods and services which contributes to the country's GDP and economic growth
 - pay tax on profits to the government and thus contribute to government revenue
 - sell products abroad (to other countries) and therefore increase export earnings, thereby improving the current account on the balance of payments.

Business organisations in an economy may also:

- import goods and services used in their production process and this may worsen the current account on the balance of payments
- cause external costs to the economy through creating pollution, producing unhealthy/harmful products, generating litter or causing congestion in a local area
- damage the local business culture by causing closures of smaller businesses because they are large multinational firms so can sell goods more cheaply.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–4 marks for analysing the role of business organisations in an economy. There may be a lack of detail and/or use of relevant examples.

Award 5–6 marks for a detailed analysis of the role of business organisations in an economy. There is appropriate use of terminology and use of examples.

9 Negative effects of Intel's closure on Costa Rica's economy include:

- loss of jobs in Costa Rica and therefore higher unemployment
- loss of income for workers may result in lower spending and this may negatively impact on the country's economic growth
- loss of business for domestic firms that supplied Intel with goods and services, e.g. firms in the banking, marketing and transport industries
- loss of tax revenue paid to the Costa Rican government on Intel's profits
- loss of training opportunities for employees of Intel
- potential relocation out of Costa Rica for other foreign companies.

Positive effects of Intel's closure on Costa Rica's economy may include:

- more opportunities for local Costa Rican firms to attract skilled and experienced workers
- skilled and experienced workers who worked for Intel may bring their expertise to local Costa Rican firms
- Intel may have introduced new technologies to Costa Rica which local firms could use
- Intel may have trained workers and this training can be passed on and used in other domestic firms.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–5 marks for a balanced discussion of the impact of Intel's closure on the Costa Rican economy. There may be a lack of detail and/or use of relevant examples.

Award a maximum of 5 marks if only positive or negative effects are discussed.

Award 6–8 marks for a detailed discussion of the impact of Intel's closure on the Costa Rican economy. There is appropriate use of terminology and use of examples. There must be a reasoned judgement/conclusion made for full marks.

See pages 116–118 in the textbook for more detailed information on the advantages and disadvantages of multinationals.

10 a Advantages of IKEA remaining a private limited company include:

- there is no threat of a takeover as shares are not sold on a public stock market
- IKEA has privacy because it does not need to make its financial accounts available to the general public
- IKEA can remain in the control of family members and a small number of shareholders
- decision-making may be easier and there tends to be a close relationship between ownership and control.

Award 2 marks for each advantage identified and explained, up to a maximum of 4 marks.

See page 116 in the textbook for more detailed explanations of the advantages of private limited companies.

b Benefits to the Chinese economy of IKEA opening its stores in the country include:

- foreign firms bring new products and ideas to the Chinese economy which can be used/adapted by local firms
- the competition created in the furniture market may give local firms the incentive to be innovative and more efficient
- IKEA creates employment opportunities for workers in China
- IKEA pays tax on its profits earned in China
- IKEA's output adds to the GDP of China.

Disadvantages to the Chinese economy include:

- local firms may face fierce competition and lose business

- workers may wish to work for IKEA and not for local firms
- IKEA could exploit workers by taking advantage of low wages and other costs of production in China
- the jobs created may be low paid and low skilled so therefore new skills and ideas are not passed on to workers in China.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–5 marks for a balanced discussion of the impact of IKEA on the Chinese economy. There may be a lack of detail and/or use of relevant examples.

Award a maximum of 5 marks if only positive or negative impacts are discussed.

Award 6–8 marks for a detailed discussion of the impact of IKEA on the Chinese economy. There is appropriate use of terminology and use of examples. There must be a reasoned judgement/conclusion made for full marks.

See pages 116–118 in the textbook for more detailed information on the advantages and disadvantages of multinationals.

● 11 Production

- 1 The correct answer is Option C. Whilst money is an example of capital (man-made goods used to produce other goods and services), other examples include tools, machinery, vehicles, computers, factories and roads. The four factors of production are land, labour, capital and enterprise.
- 2 The correct answer is Option D. Labour-intensive production requires spending proportionately more on labour than any other factor of production. Options A, B and C require intensive use of labour whereas Option D relies on capital-intensive technologies for mass production. See page 127 in the textbook for an explanation of labour-intensive production.
- 3 The correct answer is Option B. Productivity measures how well resources are used in the production process, e.g. labour productivity measures the efficiency of the workforce in terms of output per worker. See page 130 in the textbook for an explanation of productivity and the input–output process.
- 4 The correct answer is Option A. Innovations such as tablet computers and smartphones have transformed the way many people work, for example. Innovation is an important source of productivity. See page 132 in the textbook for an explanation of innovation.
- 5 The correct answer is Option B. Factors of production are demanded for their use in the production process of creating output of goods and services. The demand for these goods and services determines the demand for the factors of production needed. See page 126 in the textbook for an explanation.
- 6 Capital-intensive production takes place when a firm spends proportionately more money on capital costs than on any other factor of production (such as land or labour). See page 129 in the textbook for an explanation and examples of capital-intensive production.
- 7 Derived demand means that labour (or any other factor of production) is demanded for the goods and services it is used to produce rather than being demanded for itself. For example, bakers are demanded for the bread they bake, not for the sake of hiring bakers. See page 74 in the textbook for an explanation of the derived demand for labour. Hence, the demand for factors of production is dependent on the demand for the goods and services which they will be used to produce. See page 126 in the textbook for an explanation of derived demand.
- 8 Productivity is a measure of how well resources are used in the production process.
Investment in human resources (e.g. training) and/or other resources (e.g. automation or more capital-intensive technologies) helps to improve the productivity of scarce resources.
See page 130 in the textbook for an explanation of productivity and how it is calculated.
Award 1–2 marks for an explanation that shows limited understanding.
Award 3–4 marks for a concise and coherent explanation that shows a good level of understanding. Relevant examples are likely to be used.
- 9 a Monthly sales per worker at Morganics Cars
= $\$284\,850 \div 5 = \$56\,970$

Monthly sales per worker at Agent Cars =
 $\$366\,440 \div 8 = \$45\,805$

Thus, the sales team at Morganics Cars is more productive as the average sales person sells an extra \$11 165 worth of cars.

Award up to 2 marks for the correct calculations and a further 2 marks for the commentary.

- b** Although Morganics Cars has higher productivity as measured by monthly sales per worker (\$56 970 compared to \$45 805 from Agent Cars), Agent Cars might be considered to be more productive as each sales staff sold a greater number of cars in the same time period.

Morganics Cars workers sold an average of 3 cars each (15 cars sold by 5 sales staff).

Agent Cars workers sold an average of 3.75 cars each in the same time period (30 cars sold by 8 sales staff).

Hence Agent Cars workers sold more cars.

Also, the data does not provide any information on the type of car being sold, e.g. Morganics Cars has an average price of \$18 990 ($\$284\,850 \div 15$) compared to Agent Cars' average price of \$12 215 ($\$366\,440 \div 30$), which might explain its higher sales volume.

Thus, the choice of measurement of productivity can determine how efficient firms are interpreted to be.

Award up to 2 marks for identifying and explaining alternative ways to measure productivity.

Award up to 2 marks for examining why it is difficult to determine the most productive firm because of alternative ways of measuring productivity.

There must be reference to the data for 4 marks.

- 10** Productivity is vital for the survival of firms because:

- a lack of productivity causes average costs to rise and thus reduces the competitiveness, profitability and survival of the firm
- high productivity helps firms to achieve economies of scale, further improving their competitiveness, profitability and survival.

Accept any other reasonable explanation of why productivity is vital for the survival of firms. Relevant examples should be used for full marks.

Award 2 marks for explaining, with an example, each reason why productivity is vital for the survival of firms, up to a maximum of 4 marks.

● 12 Costs, revenues and profits

- 1 The correct answer is Option A. Irrespective of the level of output, the manufacturer has to pay rent for the land and/or building in which it operates. Wages, overtime pay and electricity charges are all dependent on the level of output, so are classified as variable costs.
- 2 The correct answer is Option A. Fixed costs are those that have to be paid regardless of the firm's output or sales level. See page 135 in the textbook for an explanation of fixed costs.
- 3 The correct answer is Option B. Total costs consist of both fixed and variable costs. So, the total costs = fixed costs when there is no output (meaning there are no variable costs of production). Hence, the total cost line intersects the vertical axis at the value of the fixed costs. See Figure 12.3 on page 136 in the textbook for an explanation of this diagram.

- 4** $AC = TC \div Q$

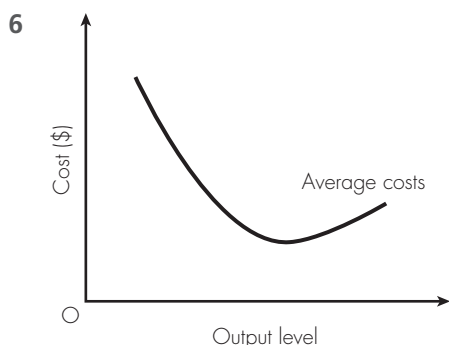
$$AC = (20\,000 + 10\,000) \div 2000$$

$$AC = \$15$$

Hence, the answer is Option C.

See pages 136–137 in the textbook for an explanation of average costs and how to calculate this.

- 5** The correct answer is Option C. Salaries (Option A) is a form of financial payment to employees. It is a form of income (Option B), the collective term for the earnings of the four factors of production. Total costs (Option D) represent outflow of money from a business whereas revenue (Option C) represents an inflow of money. See pages 138–139 in the textbook for an explanation of revenue.



See pages 136–137 in the textbook for an explanation of this diagram.

7

Output (units)	Fixed costs (\$)	Variable costs (\$)	Total costs (\$)	Average costs (\$)
100	2000	400	2400	24.00
200	2000	760	2760	13.80
300	2000	1200	3200	10.67
400	2000	2320	4320	10.80

Hence, the output level with the lowest average costs of production is at 300 units of output, where the average cost = \$10.67.

- 8 a Average cost is calculated by dividing the total cost by the quantity produced.

Quantity produced (units)	20	30	40	50
Total cost (\$)	200	285	360	460
Average cost (\$)	10.0	9.5	9.0	9.2

Hence the level of output required to minimise average costs is 40 units.

- b Profit is calculated by taking away total costs from total revenue (which is calculated by multiplying the price by the quantity sold), i.e. profit = (price × quantity) – total costs.

Quantity produced (units)	20	30	40	50
Total revenue (\$)	20 × 20 = \$400	20 × 30 = \$600	20 × 40 = \$800	20 × 50 = \$1000
Total cost (\$)	200	285	360	460
Profit (\$)	200	315	440	540

Hence the level of output required to maximise profits is 50 units.

- 9 a Total fixed costs are \$1000 as this is the amount payable irrespective of the output level, i.e. when output is zero, the firm still has to pay \$1000.
- b The price (or average revenue) is calculated by dividing the total revenue by the level of output. For instance, \$4500 is earned from selling 300 tonnes, so the price is: $4500 \div 300 = \$15$ per tonne.
- c To calculate average costs, divide total costs by the level of output.

Output (tons)	Total cost (\$)	Average cost (\$)
0	1000	–
100	2000	20
200	2800	14
300	3600	12
400	5200	13

Hence, average costs are minimised at 300 tonnes of output.

- d Profit is calculated by taking away total costs from total revenue.

Output (tonnes)	Total cost (\$)	Total revenue (\$)	Profit (\$)
0	1000	0	(1000)
100	2000	1500	(500)
200	2800	3000	200
300	3700	4500	800
400	5200	6000	800

- 10 a Total costs = Fixed costs + Variable costs
 $= \$8000 + (\$3 \times 20\,500) = \$69\,500$

- b Average costs = Total costs ÷ Output
 $AC = \$69\,500 \div 20\,500 = \3.39

Accept answers that show an average cost = \$3.40.

- c Profit = Total revenue – Total costs

Profit = $(\$5.5 \times 25\,000) - [(\$3 \times 25\,000) + \$8000]$
 $= \$137\,500 - \$83\,000 = \$54\,500$

Or

Profit = $[(\$5.5 - \$3) \times 25\,000] - \$8000 = \$54\,500$

● 13 Perfect competition and monopoly

- 1 The correct answer is Option B. In perfect competition, firms produce or supply a homogeneous (undifferentiated) product.

See pages 142–143 in the textbook for an explanation of the main characteristics of perfect competition.

- 2 The correct answer is Option C. In this market structure, a monopolist is able to protect its prestigious position because customers and rivals have imperfect knowledge, such as the monopolist's ability to protect its intellectual property rights and trade secrets. See page 145 in the textbook for an explanation of the main characteristics of monopoly.
- 3 The correct answer is Option D. Although consumer protection laws need to be observed, these laws apply to all publishers in the industry, not just those attempting to enter the industry. The consumer protection laws are unlikely to be a significant deterrent (barrier).
- 4 The correct answer is Option C. A monopolist is the sole supplier of a particular good or service. Monopolists are price makers, also known as price setters (Options A and B). A market leader (Option D) suggests there are other rivals in the industry. Besides, not all market leaders enjoy monopoly power.
- 5 The correct answer is Option A. Firms with monopoly power are able to charge different prices to different customers, e.g. adult and child fares at the cinema or peak and off-peak travel prices. Although monopolies have price setting power (Option B), it does not necessarily mean they use price discrimination. See pages 146–147 in the textbook for an explanation of the different pricing strategies used by monopolists.
- 6 Market structure refers to the key characteristics of a particular market, such as the number and size of firms in the market, the degree and intensity of price and non-price competition, and the nature of barriers to entry.

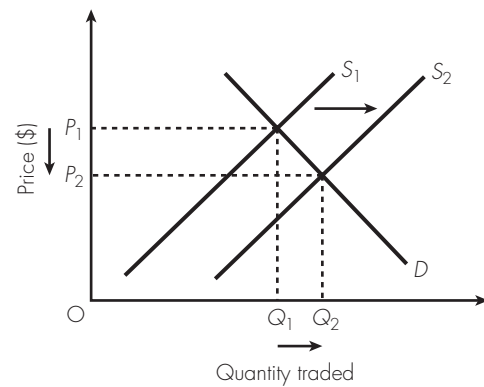
Award 2 marks for a detailed definition containing at least one characteristic of a market.

- 7 Disadvantages of monopoly include:
- inefficiency
 - high entry barriers that prevent competition
 - higher prices as monopolists are price makers
 - imperfect knowledge
 - fewer incentives due to the lack of competition.

See pages 148–149 in the textbook for an explanation of the disadvantages of monopoly.

Award up to 2 marks for each disadvantage that is explained, up to the maximum of 4 marks.

8



Increased competition shifts the market supply curve outwards to the right. This causes the market price to fall from P_1 to P_2 , thereby causing the quantity demanded to increase from Q_1 to Q_2 .

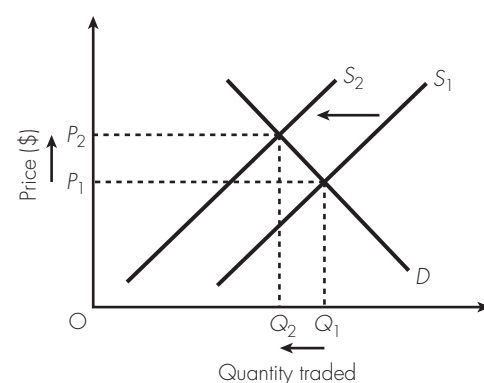
Increased competition shifts the market supply curve outwards to the right. This causes the market price to fall from P_1 to P_2 and the equilibrium output to increase from Q_1 to Q_2 .

Award up to 4 marks for drawing a correct diagram:

- 1 mark for correctly labelled axes
- 1 mark for correctly labelled demand and supply curves and identifying and labelling the original equilibrium price and quantity
- 1 mark for shifting the supply curve to the right
- 1 mark for identifying the new price and equilibrium quantity.

Award up to 2 marks for explaining the reasons for the shift in the supply curve.

9



Due to the lack of competition, a monopolist is able to restrict market supply, as shown by the shift in supply from S_1 to S_2 and thus equilibrium output falls from Q_1 to Q_2 . As the monopolist limits the supply of its good or service, the price is higher (at P_2 rather than P_1).

Award up to 4 marks for drawing a correct diagram.

- 1 mark for correctly labelled axes
- 1 mark for correctly labelled demand and supply curves and identifying and labelling the original equilibrium price and quantity
- 1 mark for shifting the supply curve to the left
- 1 mark for identifying the new price and equilibrium quantity.

Award up to 2 marks for explaining the reasons for the shift in the supply curve.

10 Arguments why consumers may be disadvantaged due to the lack of competition include:

- higher prices
- poorer quality
- a lack of consumer choice
- a lack of innovation.

On the other hand, consumers can benefit from monopolies for reasons including:

- lower prices due to low economies of scale, as monopolists operate on a large scale
- greater spending on research and development (R&D) due to the larger profits earned by the monopolist

- the greater R&D expenditure can lead to more innovation and better quality output
- competition can be wasteful.

Students might consider how prices, costs, the range of products, profit and innovation under monopoly compare with a more competitive market structure.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–5 marks for a balanced discussion of the costs and benefits of monopoly. There may be a lack of detail and/or use of relevant examples.

Award up to 5 marks for a one-sided argument, i.e. monopolies are either good or bad for consumers.

Award 6–8 marks for a two-sided discussion that considers both the benefits and disadvantages of monopoly for consumers. There is good use of terminology and relevant examples.

See pages 148–149 in the textbook for an explanation of the various advantages and disadvantages of monopoly.

● 14 Business growth

- 1 The correct answer is Option A. Facebook and WhatsApp are both in the tertiary sector of an economy and in the same industry (social networking), therefore it is an example of horizontal integration. Facebook purchased WhatsApp and therefore it is an example of a takeover. See pages 153–157 in the textbook for more information about the various types of integration.
- 2 The correct answer is Option B. The size of a firm can be measured by capital employed, the number of employees, market size (market share) and sales revenue (sales turnover). See page 151 in the textbook for more information about measuring the size of firms.
- 3 The correct answer is Option C. The purchase of cotton farms by the clothing manufacturer involves a firm in the secondary sector of industry purchasing farms in the primary sector, so is therefore backwards vertical integration. The purchase of the retail shops involves a firm in the secondary sector purchasing shops in the tertiary sector, so is therefore forward vertical integration.

See pages 153–157 in the textbook for more information about types of integration.

- 4 The correct answer is Option D. Small shops have the capacity to offer a personalised service because of the size of their operations (they are not too busy / large so can get to know customers better). Option A is incorrect because the statement is not necessarily true. Option B is incorrect because small firms are unable to take advantage of economies of scale to the same extent as their larger rivals. Option C is incorrect because often small firms charge higher prices than large firms. See page 158 in the textbook for more information about why small and large firms co-exist.
- 5 The correct answer is Option A. The new firm can take advantage of discounts for bulk purchases (such as shampoo, conditioner and hair gel) and advertising for the new company will be more efficient. Option B is an external economy of scale. Option C is not an economy of scale; a more productive workforce is not necessarily caused by larger scale operations. Option D is a potential

diseconomy of scale. See pages 158–161 in the textbook for more information about economies and diseconomies of scale.

- 6** A conglomerate merger occurs when firms from different sectors of industry, which operate in different areas of business, merge as one company. An example of a conglomerate merger is the takeover of a furniture manufacturer by a sportswear manufacturer.

Award 1 mark for a definition.

Award 1 mark for an example.

Note: students do not have to give a real world example of a conglomerate merger for full marks.

See pages 156–157 in the textbook for more detailed information on conglomerate mergers (integration of firms).

- 7** A takeover occurs when a firm buys a majority share in another business, e.g. in 2011 Kraft, the US food manufacturer, purchased Cadbury, the UK chocolate manufacturer. Cadbury is owned by Kraft. Takeovers can be hostile or friendly.

A merger takes place when two firms agree to join to form a new company. For example, Microsoft, the US software producer, merged with Nokia, the Swedish mobile phone producer, in 2014 to form a new company. Another example is Exxon and Mobil merging to become ExxonMobil.

Award 2 × 2 marks for explaining the meaning of takeovers and mergers and giving an example of each to distinguish between the two terms.

See page 153 in the textbook for more detailed information on takeovers and mergers.

- 8 a** Backward vertical integration has taken place because L'Occitane is a manufacturer in the secondary sector of the economy and a retailer in the tertiary sector of the economy and it purchased shea butter farms which are in the primary sector of the economy.

See page 155 in the textbook for more information on backward vertical integration.

- b** Advantages of L'Occitane buying farms in Africa which produce shea butter include:

- the firm in the secondary sector has control over the quality of raw materials and ingredients (such as shea butter) that it is supplied with
- the price of raw materials falls as L'Occitane does not have to pay another (external) firm for the raw materials

- there are no intermediary firms, such as distributors, involved, so L'Occitane can charge lower prices or enjoy higher profit margins.

However, the costs to L'Occitane include:

- costs of running the farm in the primary sector increases total costs as more land, labour and capital resources are required
- transport costs increase for the integrated firm as raw materials were previously delivered by external suppliers but this is an additional cost for the newly formed firm
- managing more operations as a larger, integrated firm can lead to diseconomies of scale.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–4 marks for explaining the advantages and disadvantages of L'Occitane selling its products in its own shops. There may be a lack of detail and/or use of examples.

Award 5–6 marks for a detailed analysis of the advantages and disadvantages of L'Occitane selling its products in its own shops. There is appropriate use of terminology and use of relevant examples.

See page 155 in the textbook for more detailed information on the advantages and disadvantages of forward vertical integration.

- 9** Advantages of having only small independent shops in a town are:

- personal service because shop owners know the customers
- the possibility of unique products being supplied which may attract visitors to the town
- smaller shops can adapt more quickly to changing tastes
- local business owners benefit from sales, rather than profits being sent to headquarters in an out-of-town location
- money circulating in the local economy and staying within the community.

Disadvantages of having only small independent shops are:

- less choice of products because larger shops and supermarkets have a greater range of products
- higher prices as small shops cannot take advantage of economies of scale

- shops may not sell basic products needed by local customers. Any imported products would be even more expensive as small shops do not have the capacity to enjoy huge economies of scale.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–4 marks for explaining the advantages and disadvantages of having only small shops in a town. There may be a lack of detail and/or use of relevant examples.

Award 5–6 marks for a detailed analysis of the advantages and disadvantages of having only small shops in a town. There is appropriate use of terminology and use of examples.

10 Advantages of two firms of accountants merging may include:

- bulk-buying economies of scale – they will be able to buy stationery and computing equipment in larger quantities and take advantage of bulk discounts
- marketing economies of scale – they may be able to take advantage of a combined marketing budget to spend on more sophisticated marketing campaigns, or spend less on marketing but gain greater exposure because of the newly created firm
- risk-bearing economies of scale – a greater number of clients may spread the risk of some clients defaulting on payment or going out of business; the clients may also be spread across a larger geographical area and this will also spread risk
- managerial economies of scale – the new firm may be able to pay higher wages to attract employees who are experts in their field, e.g. marketing experts, ICT experts, accountants and managers

- financial economies of scale – the combined firm may be able to raise more finance because of having more assets to act as security for loans or being more attractive to investors
- technological economies of scale – the combined accountancy firm may be able to afford to purchase new technically advanced ICT systems.

Disadvantages of two firms of accountants merging may include:

- diseconomies of scale arising from a culture clash between the two firms which causes communication problems and demotivated staff
- diseconomies of scale arising from the new firm being too large and making communication difficult and therefore slowing down decision-making
- diseconomies of scale arising from the loss of staff morale and staff demotivation as some workers are made redundant due to duplication of their role in the new firm, e.g. there is no need for two human resource managers.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–5 marks for a balanced discussion of the advantages and disadvantages of two firms merging to form one firm. There may be a lack of detail and/or use of relevant examples.

Award up to 5 marks if only the advantages or disadvantages are discussed.

Award 6–8 marks for a detailed discussion of the advantages and disadvantages. There is appropriate use of terminology and examples. There must be a reasoned judgement/conclusion made for full marks.

See pages 158–161 in the textbook for more detailed information on economies and diseconomies of scale.

● 15 Government aims and influences

- 1 The correct answer is Option D. Public libraries bring about external benefits to society and would be under-consumed without government intervention or provision. The other options are public goods. See page 164 in the textbook for an explanation of public goods.
- 2 The correct answer is Option A. Regulation refers to the rules, guidelines and laws that determine what businesses can and cannot do. Intellectual property rights (Option C) is an example of

regulations, whilst tariffs (Option D) is an example of taxes.

- 3 The correct answer is Option C. With higher rates of economic growth, spending in the economy rises, hence creating inflationary pressure in the economy. Economic growth creates employment opportunities (Option A) and the extra spending in the economy generates more tax revenues (Option D). It is not possible to determine whether the balance of payments will go into

deficit from the limited information. See pages 169–170 in the textbook for an explanation of conflicting government aims.

4 The correct answer is Option D. Depending on the economic system in a country, not all governments strive to provide welfare services in their country. In a free market economic system, resources are allocated based on the market forces of demand and supply with minimal government intervention. See pages 167–169 in the textbook for more information about government aims.

5 The correct answer is Option A. Only the government can impose taxes and regulations on private sector firms (Options B and C), and it approves or gives subsidies (Option D) to encourage output. Both public and private sector firms can use investment expenditure to influence output. Hence, investment is not exclusive or explicit to the government.

6 Full employment exists when everyone who is able and willing to work at a given wage is in employment, i.e. any unemployment that exists is voluntary.

Note: the term can also refer to other factors of production, i.e. the full employment of resources in the economy.

7 Real gross domestic product refers to the value of a country's goods and services produced in a given year, after the effects of inflation have been taken into account.

See page 222 in the textbook for an explanation of real gross domestic product.

8 Over time, as an economy grows, the gap between the rich and poor tends to widen, such as earnings by top executives in the corporate world compared to low income workers earning the minimum wage. This causes greater income inequalities in the economy, so the government intervenes to redistribute income to low-income households. See page 169 in the textbook for an explanation, including an exam practice question. Also see page 171 for a list of some of the world's richest people.

9 Price stability refers to the control of inflation in the economy. Low and sustainable rates of inflation are vital in order to achieve stable economic growth and social wellbeing. For

example, inflation reduces the international competitiveness of a country as its prices will be relatively higher. This will lead to lower export sales, which causes potential job losses. See Chapter 18 in the textbook to read about price stability in more detail.

10 a A subsidy is a form of financial aid from the government to a producer in order to reduce the costs of production. Alternatively, it can be granted to consumers to reduce the price of consumption.

b Inflation is the sustained rise in the general level of prices of goods and services in an economy over time, as measured by a consumer price index (CPI).

c Benefits of using subsidies include:

- greater levels of supply as producers are able to increase supply at every price level
- lower prices due to the increase in supply, thus benefiting consumers
- lower prices having an impact on keeping inflation under control
- subsidies for food, housing, transportation, education and other socially desirable products helps to improve standards of living.

Possible drawback of subsidies include:

- the opportunity cost of using taxpayers' money to finance the subsidies
- subsidies can distort competition, giving some firms an unfair advantage
- they might also encourage some producers to become complacent and/or inefficient
- they can cause overproduction, i.e. excess supply, which leads to wastage
- not all producers pass on the benefits of subsidies (in the form of lower prices) to their consumers.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–5 marks for a one-sided answer or an answer that lacks depth and/or use of relevant examples.

Award up to 6–7 marks for a balanced answer that considers both the benefits and drawbacks of using subsidies to intervene in markets. There is good use of terminology and appropriate examples.

● 16 Government policies

- 1 The correct answer is Option C. Privatisation is a type of supply-side policy (Option D). See page 177 in the textbook for an explanation of privatisation.
- 2 The correct answer is Option C. To expand (boost) the economy, fiscal policy can be used by reducing taxes (to encourage consumption expenditure) and raising government spending (which fuels economic activity). See page 173 in the textbook for examples of expansionary fiscal policy.
- 3 The correct answer is Option C. By reducing taxes, consumer demand should be encouraged as households have more disposable income. Cutting interest rates also enables households and firms with existing loans to spend more money, and encourages new borrowing which also boosts national output and employment. Option A is a supply-side policy. See pages 177–179 in the textbook for an explanation.
- 4 The correct answer is Option B. Reducing interest rates can create more spending power (as households with existing loans and mortgages have more disposable income), but this is monetary policy. Fiscal policy involves changes to taxes and government expenditure.
- 5 The correct answer is Option D. Supply-side policies are long-term strategies of the government aimed at increasing the productive capacity of the economy by using policies to improve the quality and/or quantity of factors of production. See pages 177–178 in the textbook for an explanation of supply-side policies.
- 6 Possible reasons to increase government spending (public expenditure) could include:
 - to redistribute income and wealth in the economy
 - to alleviate poverty
 - to provide public goods and services, e.g. street lighting, public libraries, schools, hospitals, national parks and affordable housing
 - to steer the economy out of recession.

Award up to 2 marks for each reason that is clearly explained, up to the maximum of 4 marks.

- 7 Possible policies could include:
 - using contractionary fiscal and/or monetary policies to reduce demand for imports (see pages 174 and 176 in the textbook for explanations)

- using trade barriers to protect domestic industries from foreign competition (see page 213 in the textbook for an explanation)
- using exchange rate policies, e.g. a devalued exchange rate will tend to raise the demand for exports and reduce the demand for imports (see page 272 in the textbook for an explanation).

Award up to 2 marks for each reason that is clearly explained, up to the maximum of 4 marks.

- 8 Possible reasons for using monetary policy could include:
 - reducing interest rates to stimulate the economy during a recession (or vice versa for an economic boom)
 - intervention in the foreign exchange market to influence gross domestic product and economic stability
 - direct control over the money supply to influence the rate of inflation.

See pages 175–176 in the textbook for an explanation of how monetary policies are used by governments.

Award 1–2 marks for a vague answer that demonstrates some understanding.

Award 3–4 marks for demonstrating a clear understanding of why a government might choose to use monetary policy.

- 9 a Supply-side policies are the long-term strategies aimed at increasing the productive capacity of the economy by improving the quality and/or quantity of factors of production. See page 177 in the textbook for an explanation of how supply-side policies work.
- b Possible impacts that could be examined include:
 - incentives to work, e.g. lower incomes taxes and lower welfare benefits
 - investment expenditure, e.g. spending on infrastructure and lower corporation tax to attract foreign investment
 - human capital expenditure, e.g. on education and training.

See page 174 in the textbook for an explanation of how fiscal policies can be used to impact on the supply-side of an economy.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–4 marks for an answer that demonstrates good understanding of how fiscal policy can impact on the supply-side of an economy. There might be a lack of explanation and/or use of examples.

Award 5–6 marks for an answer that demonstrates a good level of understanding of how fiscal policy can be used to impact on the supply-side of the economy. There is effective use of terminology and relevant examples.

- 10 Supply-side policies can be used to achieve sustainable economic growth by increasing the productive capacity of the economy. Examples should be given.

As supply-side policies increase the productive potential of the economy, they help to prevent the general price level from rising beyond control, thereby fostering economic stability.

An increase in national output creates jobs in the economy in the long term, further fuelling economic growth.

The main criticism of supply-side policies is the time that it takes to reap the benefits. For example, it might take decades for a nation to get the benefits of an improved education system or infrastructure in the country, thus limiting economic growth in the short run.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–5 marks for a balanced discussion. There may be a lack of detail and/or use of relevant examples.

Award 6–8 marks for a detailed discussion of the effectiveness of supply-side policies in achieving economic growth. There is appropriate use of terminology and use of examples. There must be a reasoned judgement/conclusion made for full marks.

17 Taxation

- The correct answer is Option C. Direct taxes are imposed on earnings, such as income and profits. Income tax (Option A) and corporation tax (Option B) are examples of direct tax. See Table 17.1 on page 185 in the textbook for an explanation of the various types of taxes.
- The correct answer is Option B. The government will have a budget surplus if it spends less than the sum of its sources of revenue. Options C and D refer to the balance of payments, not the budget itself.
- The correct answer is Option D. Proportional taxes such as value-added tax (an example of a sales tax) have the same percentage charge irrespective of the buyer. See pages 182–183 in the textbook for an explanation of the differences between progressive, regressive and proportional taxes.
- The correct answer is Option B. Customs duties are imposed on imported goods. Hence, these are indirect taxes (imposed on expenditure rather than earnings). See Table 17.1 on page 185 for an explanation of the various examples of taxes.
- The correct answer is Option C. Higher taxes tend to slow down the economy (so Option B is incorrect). This tends to lower inflation (Option C). It is unlikely that higher taxes create incentives to work (Option A) or that higher taxes have a positive impact on business location (Option D).

- Indirect taxes, such as VAT or GST, are levied on expenditure. They are regressive in nature. See pages 182–183 in the textbook for an explanation of different types of taxes.

Award 1 mark for a correct definition of indirect taxes and up to 2 further marks for an explanation (including relevant examples).

- Reasons for imposing zero rate taxes could include:
 - to boost aggregate demand (boosting spending in the economy)
 - to encourage multinational companies to set up business in these countries
 - to increase incentives to work
 - to encourage risk taking and entrepreneurship.

8 a

Income level (\$)	Tax rate (%)	Amount of tax paid (\$)
\$10 000	0%	First \$10 000 is tax free = \$0
\$10 001–\$50 000	12%	Next \$40 000 is taxed at 12% = \$4800
\$50 000+	17%	Remaining \$30 000 is taxed at 17% = \$5100
Total tax:		\$9900

- Average tax rate = total tax ÷ income
 $\$9900 \div \$80\,000 = 12.37\%$

- 9 a Reasons for reducing direct taxes include:
- to boost aggregate demand (spending in the economy); thus raising more indirect (sales) taxes
 - to increase incentives to work, so more people would be paying income tax
 - to encourage multinational companies to set up business in these countries due to the low corporation taxes; thus boosting overall tax revenues
 - to discourage tax avoidance and tax evasion; thus boosting overall tax revenue.
- b Award 1–2 marks for a brief answer that shows limited understanding.
Award 3–5 marks for explaining why imposing corporation taxes on the profits of multinational companies (MNCs) may discourage them from setting up in a country, e.g. a reduction in company profits or reduced international competitiveness.
Award 6–7 marks for acknowledging that imposing corporation taxes may discourage MNCs but then considering factors why it might not, such as:
- corporation taxes may still be lower than in other countries

- demand in the economy may be increasing, thus creating incentives for MNCs to set up in the country
- there may be government subsidies to entice MNCs
- availability of cheaper and/or more productive labour can also attract MNCs.

- 10 a Tax A is progressive.
At \$10 000 the tax paid = \$1000 (10%)
At \$15 000 the tax paid = \$1650 (11%)
At \$20 000 the tax paid = \$2400 (12%)
At \$25 000 the tax paid = \$3250 (13%)
- b Tax C is proportional.
At all levels of incomes, 5% tax is charged.
- c A regressive tax charges those on lower incomes a higher rate of tax. Tax B is regressive as the same \$650 is charged irrespective of the income level.
At \$10 000 the tax paid = \$650 (6.5%)
At \$15 000 the tax paid = \$650 (4.33%)
At \$20 000 the tax paid = \$650 (3.25%)
At \$25 000 the tax paid = \$650 (2.6%)
By contrast, a proportional tax charges all income earners the same percentage tax rate (5% in the case of Tax C).

● 18 Inflation

- 1 The correct answer is Option B. Lower interest rates will make borrowing cheaper and boost household disposable income (e.g. those with existing bank loans and mortgages pay less interest on their outstanding debts). Thus, consumer and producer confidence levels should rise, causing greater economic activity and an increase in the inflation rate. See pages 195–196 in the textbook for an explanation of the causes of inflation.
- 2 The correct answer is Option C. Savers place their money in the bank in an attempt to gain some interest and to keep its value, i.e. to act as a store of value. Inflation reduces the value of money, even if placed in a savings account. People are generally less able to save during inflationary periods as they pay higher prices for goods and services. See page 197 in the textbook for an explanation of the impact of inflation on savers, and other consequences of inflation.
- 3 The correct answer is Option C. Economists deem ‘importance’ to be determined by the percentage of household income spent on particular items, i.e. spending more on food means the typical household values food more than shoes. It is not possible to determine from statistical weights how much (the quantity) households buy (Options A and B) or the price (Option D). See pages 193–194 in the textbook for an explanation of weights in the CPI.
- 4 The correct answer is Option A. To calculate the rate of inflation, it is necessary to work out the percentage change in the CPI:
 $(116.8 - 115.2) \div 115.2 = 1.39\%$
See page 194 in the textbook for an explanation of how to calculate the CPI. There are further calculation exercises on page 195 to test students’ understanding.
- 5 The correct answer is Option A (Year 1). The data shows an overall increase in the CPI, so there has been inflation during the period shown. Prices were lowest in Year 1 when the CPI stood at 102.2 (i.e. 2.2% inflation from the base year), whereas the CPI is higher in all subsequent years. Although the rate of inflation drops from Year 2

to Year 3 (from 104.6 to 103.9), these figures are higher than the CPI in Year 1 (102.2).

6 Answers could include an explanation of:

- using the CPI as a measure of inflation
- low and stable inflation as a government macroeconomic objective
- calculating the CPI to enable governments to make international comparisons of inflation rates over time
- using the CPI as a basis for interest rate (anti-inflation) policy, i.e. raising interest rates when there are inflationary pressures.

7 Weightings are based on the importance of the item in the average household and this is determined by how much they spend on the item. The greater the proportion spent on an item, the higher the weighting.

Food and furniture are given different weightings as different proportions are spent on them by the typical (average) household; a higher proportion of the average household's expenditure goes on food than on furniture.

See pages 193–194 in the textbook for an explanation of how to calculate a statistically weighted CPI.

8 The inflation rate is calculated by the percentage change in the CPI:

$$[(114.4 - 112.3) \div 112.3] \times 100 = 1.87\%$$

9 Inflation rate = $(135.54 - 125.5) \div 125.5 = 8\%$
Hence, the price of the basket = $\$1500 \times 1.08 = \1620

10 a A retail prices index (RPI) is used to calculate the rate of inflation in a country.

Unlike the CPI, the RPI includes the cost of housing (including mortgage interest payments and other housing costs).

It excludes low-income pensioner households and very high-income households, as neither are regarded as being 'average' households in the economy.

b The weight for food is 30 whilst it is 15 for clothing, i.e. the typical household spends 30% of their income on food and just 15% on clothing. Hence, the average household in Satcolbe spends more money on food than it does on clothing.

c

Item	Retail prices index	Weight	Weighted index
Clothing	120	15	$120 \times 0.15 = 18$
Food	130	30	$130 \times 0.3 = 39$
Housing	140	40	$140 \times 0.4 = 56$
Other	125	15	$125 \times 0.15 = 18.75$
Weighted RPI		100	131.75

See pages 193–194 in the textbook for an explanation of how to calculate a statistically weighted CPI.

● 19 Employment

1 The correct answer is Option A. In economics, unemployment occurs when people of working age are both able and willing to work but cannot find work.

2 The correct answer is Option B. Examples of supply-side policies that can rectify labour market imperfections include investments in education and training, reduction in labour union powers, incentives to seek employment opportunities and reforms to welfare benefits (such as unemployment benefits). See pages 211–212 in the textbook for further information about supply-side policies.

3 The correct answer is Option C. Cyclical unemployment is associated with an economic recession, which typically affects every industry. See pages 207–209 in the textbook for a description of the different types and

causes of unemployment. The consequences of unemployment are explained on page 210.

4 Unemployment rate = 7%.

Working age population = 38 million.

Unemployed total = $38\text{m} \times 0.07 = 2.66$ million people.

Hence, the correct answer is Option A.

5 The correct answer is Option A. Frictional unemployment occurs when people change jobs, causing temporary unemployment due to the time delay between leaving a job and finding or starting a new job. See pages 207–209 in the textbook for a description of the different types and causes of unemployment.

6 The unemployment rate refers to the percentage of the labour force (the working population) without a job. In some countries, it is the number

of registered unemployed as a percentage of the labour force. Refer to pages 206–207 in the textbook for an explanation of unemployment and how it is calculated.

- 7 Unemployment rate = $2.7 \text{ m} \div (30 \text{ m} + 2.7 \text{ m}) \times 100 = 8.25\%$
- 8 Cyclical unemployment (or demand-deficient unemployment) is associated with an economic recession. See page 211 in the textbook for an explanation of cyclical unemployment and pages 220–221 for an explanation of the business cycle.
- 9 The International Labour Organisation (ILO) measures unemployment by calculating the number of people of working age who are both willing and able to work but cannot find employment. The ILO states the lower age limit for those of working age as 15 years old, but

there is no official upper limit so this varies from country to country.

10 Economic advantages might include:

- greater national output (GDP)
- reduced poverty
- increased tax revenue (from income tax and expenditure taxes)
- reduced government spending on welfare benefits (which has an opportunity cost)
- extra tax revenue might be spent on further improving the economy, e.g. investment in infrastructure or reducing a budget deficit.

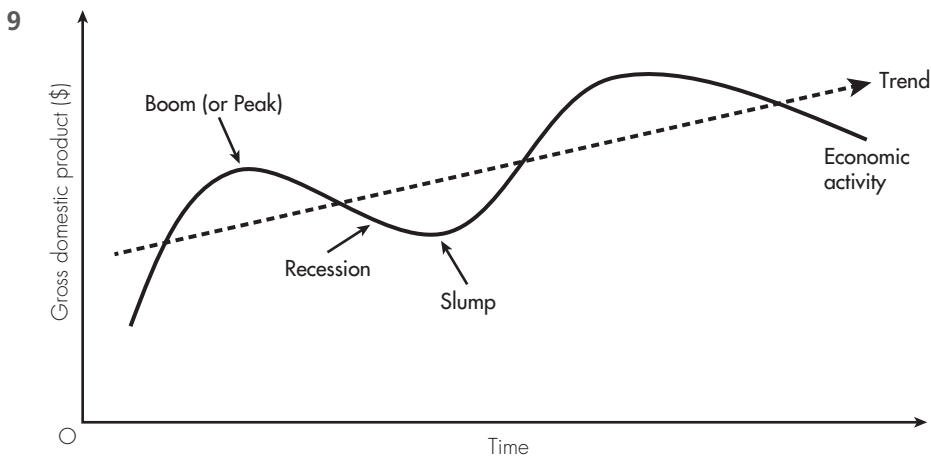
Accept any other valid advantage.

Award up to 2 marks for each advantage that is clearly explained, up to a maximum of 4 marks.

● 20 Economic growth

- 1 The correct answer is Option B. An increase in the productive capacity of the economy enables the country to boost its gross domestic product (GDP), thereby leading to economic growth.
- 2 The correct answer is Option A. Economists use real GDP per capita (calculated as GDP adjusted for inflation, divided by the population size) as a measure of economic growth. See page 222 in the textbook for an explanation.
- 3 The correct answer is Option B. With economic growth, standards of living in the country tend to rise, so infant mortality rates will decline (see page 230 in the textbook for a brief explanation). With higher national income, it is likely that employment opportunities will rise, as will GDP per capita and the average number of years children attend school.
- 4 The correct answer is Option B. With rapid economic growth, there is huge demand for the world's scarce resources, i.e. growth is not necessarily sustainable. Whilst costs might increase (Option A), this is not necessarily a problem (not all inflation is harmful). Higher tax revenues (Option C) can be beneficial for the economy. Higher demand for imports (Option D) might not necessarily be a concern, especially if rapid economic growth is fuelled by higher export earnings.
- 5 The correct answer is Option D. Education, income levels and health care are the three indicators used to compile the HDI. The lack of consideration for environmental issues (Option D) is one of the main criticisms of using the HDI to measure standards of living.
- 6 A recession occurs in the business cycle when a country's gross domestic product (GDP) falls for two consecutive quarters. A recession is associated with a decline in consumption, investment and net exports (due to falling export earnings).
- 7 Net exports = $X - M$, i.e. the numerical difference between the value of a country's exports (X) and its imports (M). X measures the monetary value of all goods and services sold to foreign buyers, whereas M measures the monetary value of all payments for imported goods and services. See page 216 in the textbook for an explanation of exports and imports.
- 8 Causes of economic growth include:
 - factor endowments
 - size, skills and mobility of the labour force
 - labour productivity
 - investment expenditure.

See pages 217–218 in the textbook for an explanation of the above causes of economic growth.



10

Country	HDI	Country	HDI
Norway	0.944	Indonesia	0.684
Turkey	0.759	Sierra Leone	0.363

Source: <http://hdr.undp.org/en/content/human-development-report-2014>

Norway is most likely to have a HDI of 0.944 because the high HDI suggests it has the highest standards of living (as measured by the composite index of health care, education and income levels for the country).

By contrast, Sierra Leone is likely to have a HDI of 0.374 because the low HDI suggests it has

the lowest standards of living of the four listed countries.

Turkey, being relatively more economically developed than Indonesia, is likely to have a HDI of 0.759 compared to Indonesia's 0.684.

Note: there is no need to explain the HDI for all four countries as the lines of reasoning will be similar.

Award 1 mark for each correctly identified country, up to 4 marks.

Award up to further 2 marks for the explanation.

● 21 Standards of living

- The correct answer is Option D. Those suffering from poverty suffer from homelessness and poor housing (Option A), high mortality rates (Option B) and hunger (Option C). Inflation (see Chapter 18) is found in most economies, with many high-income countries experiencing a high cost of living. Hence, a high cost of living is not an indicator of poverty.
- The correct answer is Option C. Real national income accounts for inflationary effects, whilst per capita income accounts for the size of the population. However, it does not account for the fact that the 'average' person is potentially highly unrepresentative due to inequalities in the distribution of income and wealth. A minority of the population is likely to earn a significant proportion of the country's national income.
- The correct answer is Option C. By cutting expenditure taxes (Option C), the relatively poor population have greater affordability (spending power), thus boosting their standards of living. Cutting housing subsidies (Option A) will clearly harm poorer members of society, whilst cutting

tariffs and corporation taxes (Options B and D respectively) tend to benefit businesses far more than households.

- The correct answer is Option D. Economists use real GDP per capita as a key indicator of standards of living. This is calculated by dividing the GDP figure by the country's population.

Country	GDP (\$ billion)	Population (million)	GDP per capita (\$)
A	129.7	18.5	7010.81
B	153.6	150.0	1024.00
C	43.2	15.2	2842.10
D	89.9	9.2	9771.74

Country D has the largest GDP per capita (by quite a significant margin compared to Countries B and C).

- The correct answer is Option A. Although the statement is correct (that the nature of development and living standards are both subjective), this is not a criticism of using the

HDI itself, the statement applies to other measures too, such as GDP per capita.

6 Characteristics of LEDCs include:

- low real GDP per capital
- low life expectancy
- low literacy rates
- high population growth
- poor infrastructure
- low foreign direct investment
- poor health care
- low labour productivity
- high public debt
- over-reliance on primary sector output
- a high degree of corruption.

See pages 229–230 in the textbook for an explanation of these characteristics of LEDCs.

Award up to 2 marks for each characteristic that is correctly identified and explained, up to the maximum of 6 marks.

7 Possible reasons could include:

- the limited access to and availability of goods and services in Dhaka
- high crime rates and issues to do with personal safety
- poor infrastructure.

Accept any other plausible reason that suggests why the standard of living in Dhaka is low.

Award up to 2 marks for each reason that is correctly described, up to the maximum of 4 marks.

- 8 a** Standard of living (SOL) refers to the social and economic wellbeing of individuals in a country at a particular point in time. In economics, this is often based on real GDP per capita, indicating the amount of income with which the average person can consume goods and services over a period of time.

Accept answers that refer to the Human Development Index (HDI) as an alternative measure of SOL.

See page 231 in the textbook for the definition of standard of living and page 227 for an explanation of the HDI.

- b** Possible ways to improve the standard of living in a country include:

- lower rates of income tax/expenditure taxes
- lower interest rates
- increased government spending on merit goods and public goods

Award 1 mark for each method that is correctly identified and a further 2 marks for the explanation, up to the maximum of 6 marks.

- c** In general, economic growth in a country results in higher standards of living for its people. However, other considerations linked to living standards include:
- what type of goods and services are being produced, e.g. health care products or arms and weapons?
 - whether longer working hours caused the increase in national income
 - whether working conditions and terms of employment (such as women's rights in the workplace) are improving
 - whether the size of the informal sector has increased
 - how the extra national income is distributed
 - whether higher economic growth is causing greater levels of pollution and other forms of environmental damage
 - how much of the additional national income is spent or saved.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–5 marks for an answer that shows good understanding, but the answer is unbalanced and/or lacks the use of relevant examples.

Award 6–7 marks for a balanced answer, with evidence of critical thinking that clearly demonstrates the difficulty is measuring standards of living based only on economic growth data.

- 9** Absolute poverty is an extreme form of poverty indicating the number of people who cannot afford minimal standards of basic human needs (food, clothing, health care and shelter). People in absolute poverty are undeniably impoverished. Relative poverty is a comparative measure of poverty. Those in relative poverty have a lower standard of living in comparison to the average person in society. Although real GDP may have increased in a country, the gains are not necessarily evenly distributed across the population, leaving the poorer members of society in relative poverty.

Award 1–2 marks for an answer that shows some understanding, although the distinction is not made clear. Award up to 2 marks if no examples are used.

Award 3–4 marks if the meaning of absolute and relative poverty are made clear so that the two concepts are evidently distinguished. Relevant examples are used.

10 Standard of living (SOL) refers to the social and economic wellbeing of individuals in a country at a point in time. Various indicators can be used to measure the standards of living in a country. These include the following:

- GDP per capita – both countries have extremely low GDP per capita figures; Malawians live on \$1 per day, whereas Sierra Leoneans live on just over \$1 per day (\$1.02) so there is basically no difference in their SOL based on GDP per capita.
- Life expectancy – Malawians live an extra 6 years on average. This suggests the country has a higher SOL, perhaps through better health care provision and/or healthier diets.
- Adult literacy rate – Malawi has a significantly higher adult literacy rate, suggesting a higher SOL, mainly due to better access to an education system.

- Population growth – Malawi will find it more difficult to sustain its SOL given its relatively higher population growth rate. Although the data does not show it, Malawi's population is already much larger (16.4 million compared to 6.2 in Sierra Leone).

However, it is difficult to be definitive about which country has the lower standard of living, given the limited data.

See page 228 in the textbook for a discussion of the limitations of using the Human Development Index (life expectancy, income and education) as a measure of standard of living.

Award 1–3 marks for an answer that shows limited understanding.

Award 4–5 marks for an answer that shows good understanding but is unbalanced and/or lacks the use of relevant examples.

Award 6–8 marks for a balanced answer that considers a minimum of three of the four economic indicators. At the top end, the discussion shows evidence of critical thinking.

● 22 Population

- 1** The correct answer is Option C. Improved health technologies mean that people, on average, live longer, thereby raising the average age of the population.
- 2** The correct answer is Option D. Fertility rates measure the average number of children born per woman and thus indicate the potential for population change in a country. The other options are likely to reduce the birth rate in the country.
- 3** The correct answer is Option A. The net migration rate measures the difference between the number of people entering (immigrants) and leaving (emigrants) a country per 1000 of the population in a year.
- 4** The correct answer is Option A. In low income countries, the population distribution can be shown using a traditional population pyramid with far more young people than elderly people. See Figures 22.2 and 22.3 on page 241 in the textbook for further guidance.
- 5** The correct answer is Option B. An ageing population occurs when the average age of a population increases. It is not possible to infer the other three options from the data given about the median age of the UK population.
- 6** This refers to the number of dependents (children, the unemployed and the elderly) expressed as a

ratio or percentage of the total population. The higher the dependency ratio, the greater the burden on taxpayers to support the dependent population.

7 Possible factors include the following:

- Birth rate – the number of live births per thousand of the population in a year. The higher a country's birth rate, the greater its population growth will tend to be.
- Death rate – the number of deaths per thousand of the population in a year. The lower a country's death rate, the greater its population growth will tend to be.
- Fertility rate – the average number of children born per woman. Fertility rates tend to fall as an economy develops, due to the higher opportunity costs of raising children.
- Net migration rate – the physical movement of people in and out of a country also affects the rate of population growth. The net migration rate measures the difference between the number of people entering and leaving a country per 1000 of the population in a year.

See pages 237–238 in the textbook for further guidance.

Award up to 2 marks for each correctly explained factor that affects the rate of population growth.

8 A country that is under-populated does not have sufficient labour resources to make the best use of its other resources, thus GDP per head is lower than it could be. By contrast, over-population means the population is too large, given the available resources of the country, i.e. there are insufficient resources to sustain the population. See pages 244–245 in the textbook for further guidance.

- 9 a** The chart shows that the population of Mexico increased from just over 100 million in 2003 to almost 117 million by 2013, a increase of approximately 17%.
- b** Possible economic problems associated with the continual rise in Mexico's population include:
- threats to the environment due to rapid increases in economic activity, e.g. deforestation and fragmentation of land
 - competition for limited (scarce) resources, e.g. food, housing, health care and education
 - more widespread poverty due to there not being enough goods and services for the rapidly rising population
 - urbanisation and its related problems, e.g. traffic congestion, pollution, housing shortages and higher demand for infrastructure (such as road and transport networks), especially in large cities
 - increased government expenditure on infrastructure, housing, education and health care
 - unemployment problems due to many of the problems above.

Accept any other clearly explained economic problem of over-population in Mexico.

Award up to 2 marks for each economic problem that is clearly explained, up to a maximum of 4 marks.

- c** Measures that the Mexican government could use to overcome over-population include:
- investment in sex education and family planning services
 - investment in education
 - subsidising birth control/contraception
 - reducing the economic benefits of having a larger family, e.g. reductions or removal of state welfare benefits
 - measures to boost investment and productivity in the economy.

Accept any other relevant measure that is clearly discussed.

Award 1–3 marks for an answer that shows limited understanding.

Award 4–6 marks for an answer that displays good understanding, although lacks detail in places.

Award up to 4 marks if only one measure is discussed.

Award 7–8 marks for a detailed answer that is well balanced and clearly discusses two appropriate measures to overcome the problems of population growth.

- 10 a** Life expectancy measures the number of years the average person in a country is expected to live. Hence, the average woman in Japan is expected to live to 86 years.
- b** Factors that lead to a higher life expectancy in Japan include the following:
- better health care in Japan, including education, nutrition and health technologies
 - higher overall standards of living and quality of life in Japan, including income levels and better housing
 - higher fertility rates in Indonesia
 - higher absolute poverty in Indonesia
 - there may be more natural disasters, diseases, crime (violence) and war in Indonesia.

Accept any other relevant reason that is clearly discussed.

Award up to 2 marks for each reason that is clearly explained, up to a maximum of 4 marks.

- c** Possible effects could include:
- increased government spending on hospitals, health care and housing for the elderly
 - lower income tax revenues if the dependency ratio increases
 - deteriorating fiscal position due to the combination of falling tax revenues and rising government spending, i.e. the government is likely to experience budget deficits
 - the extent to which these effects happen will depend on the numerical value of life expectancy (65 or 80 years, for example) and the rate of change in life expectancy.

Accept any other relevant effect that is clearly examined.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–4 marks for an examination that shows some understanding of the effects of higher life expectancy on government expenditure and revenue.

Award 5–6 marks for a detailed and clearly examined response that considers the effects of higher life expectancy on the government.

d Possible effects could include:

- changing patterns of household consumption, e.g. higher life expectancy means that elderly people might spend proportionately more of their money on health care products and services
- slower economic growth partly due to a smaller workforce and lower productivity, resulting in a fall in GDP and standards of living
- skills mismatch in a fast-changing global economy – higher life expectancy suggests an ageing population yet younger people

tend to be more geographically and occupationally mobile

- opportunity costs of government expenditure to cater for the needs of an ageing population due to higher life expectancy.

Again, the extent to which these effects will happen depend on value of life expectancy of the population and its rate of change.

Accept any other relevant effect that is clearly examined.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–4 marks for an examination that shows some understanding of the effects of higher life expectancy on economic growth.

Award 5–6 marks for a detailed and clearly examined response that considers the effects of higher life expectancy on economic growth.

● 23 Specialisation

1 The correct answer is Option B. Specialisation leads to greater levels of output and in a quicker time, thereby reducing average costs of production. Firms are therefore able to charge lower prices to their customers.

2 The correct answer is Option A. By specialising in their jobs, employees become more skilled. This can also help them to benefit from higher wages. The other options are benefits to firms (employers).

3 The correct answer is Option D. As the training period to become a top actor is a long process, there is a very limited supply of top Hollywood actors. The combination of high demand and low supply means that Hollywood actors generally earn very high incomes.

4 The correct answer is Option C. A disadvantage of specialisation is the monotony (boredom) associated with repetitive roles, causing workers to seek alternative jobs that are more challenging. See pages 253–254 in the textbook for an explanation of the advantages of specialisation, such as efficiency gains, improved competitiveness and economies of scale.

5 The correct answer is Option A. Firms that specialise are usually able to benefit from economies of scale (lower unit costs) by operating at a higher capacity. Highly specialised capital equipment, labour or firms find it difficult to switch to alternative uses (Option B), yet specialisation limits factor mobility (Option C). See pages 255–256 in the textbook for an explanation of the disadvantages of specialisation.

6 Specialisation occurs when individuals, firms, regions or countries concentrate on the production of a particular good or service. Production processes are split into a sequence of different tasks or activities, e.g. Hodder Education focuses on the production of education publications.

Award 1–2 marks for an answer that shows a limited understanding of specialisation.

Award 3–4 marks for an answer that demonstrates a good level of understanding, including the appropriate use of examples.

See pages 252–253 in the textbook for an explanation and examples of specialisation. Read page 86 to see how specialisation applies to the labour market.

7 Division of labour refers to the specialisation of labour by getting workers to focus on a specific aspect of the production process. Production is broken down into separate tasks so that workers become proficient in their part of the process. Each worker concentrates on what they are good at, developing their skills and expertise, thereby raising output per worker. See page 252 in the textbook for some examples.

Award 1–2 marks for an answer that demonstrates limited understanding and/or if no examples are used.

Award 3–4 marks for an answer that demonstrates a good level of understanding and relevant examples used.

8 Reasons why specialised workers can receive higher pay include:

- specialisation (or specialised work) means customers pay for the skills and expertise of workers, e.g. plumbers, lawyers, accountants and car mechanics
- specialised workers also get tasks/jobs done more quickly and/or to a higher standard
- higher pay is needed to compensate for the higher level of education and training required for specialised work
- limited supply of highly specialised workers also means that they can earn higher levels of pay.

Award up to 2 marks for each reason that is clearly identified and explained, up to the maximum of 4 marks.

- 9 Overspecialisation occurs when a firm or country concentrates too much on producing a very limited number of goods or services. This exposes the firm or economy to a far higher degree of risk.

Overspecialisation increases the level of risk for firms, especially during an economic recession when they do not have a large range of products to rely on.

Overspecialisation can also limit choice for consumers, reducing the competitiveness of firms.

Due to limited choice, domestic customers may look at alternative imported products from foreign suppliers that overspecialise.

Similarly, countries that overspecialise also suffer the most during an economic downturn as they do not have a variety of goods and services that they can rely on to survive, e.g. adverse weather conditions could wipe out agricultural production thus severely harming economies that over-rely on agricultural output.

Overspecialisation in a country can lead the economy to become over-reliant on others for particular commodities.

Award 1–2 marks for an answer that shows limited understanding.

Award 3–4 marks for consideration of the problems for only firms or the economy. The definition should also be provided.

Award 5–6 marks for an answer that shows a good level of understanding. There is consideration of the problems for both firms and the economy.

- 10 Advantages of specialisation for firms include:

- efficiency gains
- increased labour productivity
- increased productive capacity
- economies of scale
- improved competitiveness.

Disadvantages of specialisation for firms include:

- overspecialisation, i.e. over-reliance on a limited range of output
- possibility of higher labour turnover due to monotonous nature of the job
- lower labour occupational mobility
- lack of variety (choice) for consumers
- higher costs for hiring specialised labour and capital equipment.

See pages 254–256 in the textbook for an explanation of the above.

Award 1–3 marks for an answer that demonstrates limited understanding.

Award 4–5 marks for an unbalanced answer or one that does not include any relevant examples.

Award 6–8 marks for a balanced answer that considers both the advantages and disadvantages of specialisation to firms. Relevant examples are used effectively.

● 24 Balance of payments

- 1 The correct answer is Option C. The visible trade balance is calculated by deducting the value of a country's imports of goods from the value of its exports of goods. See page 259 in the textbook for an explanation of the visible trade balance.
- 2 The correct answer is Option D. Money spent on intangible products (services) is part of the invisible trade balance on the current account. See pages 258–259 in the textbook for a more detailed explanation of the components of the balance of payments.
- 3 The correct answer is Option C. The three components of the current account on the balance of payments are:
 - visible trade balance
 - invisible trade balance
 - net income flows and transfers.

See page 259 in the textbook for an explanation of the three components of the balance of payments.

- 4 The correct answer is Option B. With a sustained current account deficit, there is a net outflow of cash as households and firms spend more on foreign goods and services. This will tend to reduce aggregate demand, standards of living and the exchange rate.
- 5 The correct answer is Option A. Lowering income taxes helps to increase household disposable income, which can result in higher demand for imports (thus worsening the current account). See page 263 in the textbook for an explanation of how the other policies (Options B, C and D) are likely to improve the country's current account.
- 6 The balance of trade has worsened, as calculated by the difference between the trade in goods (visible balance) and services (invisible balance).

Year	Invisible balance (\$bn)	Visible balance (\$bn)	Balance of trade (\$bn)
1	15.2	12.3	-\$2.9
2	16.7	13.4	-\$3.3

- 7 The three components of the current account of the balance of payments are:
- the trade in goods (visible trade balance)
 - the trade in services (invisible trade balance)
 - net income flows and transfers.
- Award 1 mark for correctly stating each component.
- See pages 258–259 in the textbook for an explanation of these components in the current account of the balance of payments.
- 8 It is possible to have a deficit on the visible trade balance but still have a current account surplus if:
- another component or other components (e.g. trade in services) of the current account are in surplus
 - the surplus of the other components are greater than the deficit on the visible trade balance.

Reference could be made to net income flows and transfers.

Award 2 marks for stating and explaining each reason why it is possible to have a deficit on the visible trade balance but still have a current account surplus, up to a maximum of 4 marks.

- 9 A fall in the exchange rate can reduce a country's current account deficit because:
- export prices fall, thus raising the demand for exports
 - as the exchange rate falls, import prices are relatively higher, thereby reducing the demand for imports.

The net effect of higher export revenues and lower import expenditure will tend to improve the country's current account.

Students may consider the concept of price elasticity of demand for exports and imports in analysing the effectiveness of lowering the exchange rate to reduce the current account deficit.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–4 marks for explaining how a fall in the exchange rate can reduce a country's current account deficit. There may be a lack of detail and/or use of examples.

Award 5–6 marks for a detailed analysis of how a fall in the exchange rate can reduce a country's current account deficit on its balance of payments. There is appropriate use of terminology and use of relevant examples.

- 10 a The visible balance (or the balance of trade in goods) is a record of a country's exports and imports of physical goods, e.g. oil, vehicles, foodstuff and computers.

b Trade balance for Country D (\$billion)

Exports	103
Goods	87
Services	16
Imports	113
Goods	87
Services	26
Visible balance	0
Invisible balance	10
Trade balance	(10)

See page 260 in the textbook for further exam practice on calculating the balance of payments.

Award 1 mark for each correct calculation, up to 4 marks. Apply error carried forward rule as appropriate.

● 25 Exchange rates

- 1 The correct answer is Option C. Governments spend a huge amount of money on a daily basis to maintain (fix) the exchange rate. There

is an opportunity cost in this money. With a fixed exchange rate system, Options A and B materialise for reasons other than changes in

the exchange rate. The key advantage of fixed exchange rates is the certainty (stability) created for international trade and exchange (thus Option D is incorrect).

- 2 The correct answer is Option A. The term *depreciation* (Option B) refers to a fall in the value of the exchange rate against other currencies in a floating exchange rate system. The terms *reevaluation* and *devaluation* (Options C and D) apply when referring to a fixed exchange rate system.
- 3 The correct answer is Option B. The government buys and sells currencies in the foreign exchange market to stabilise the exchange rate (at the fixed rate). See page 268 in the textbook for an explanation of how fixed exchange rates work.
- 4 The correct answer is Option A. When currencies are free to fluctuate (or float), the demand for a currency and its supply determine the equilibrium exchange rate. Governments intervene in the foreign exchange market to fix or manage their currencies (Options C and B). Economists do not refer to 'mixed' exchange rate systems (Option D).
- 5 The correct answer is Option D. If there are more firms from New Zealand investing in Britain, this raises the demand for pound sterling (the diagram shows an increase in the demand for NZ dollars). See pages 269–270 in the textbook for an explanation of the causes of an increase in the exchange rate.
- 6 The exchange rate refers to the price of one currency measured in terms of other currencies, e.g. \$1 = €0.75 or £1 = ¥173.
- 7 $\text{USD1} = \text{EUR0.73}$ so $\text{USD70} = \text{EUR51.1}$
Therefore the price of the textbooks = EUR51.1
- 8 $\text{£1} = \text{HKD12.5}$
 $6000 \div 12.5 = 480$
Therefore the price of the iPad = £480

$$9 \quad \text{AUD 1} = \text{GBP0.55} = \text{HKD7.25}$$

$$\text{Hence } \text{GBP1} = 7.25 \div 0.55 \text{ HKD}$$

$$\text{Hence } \text{GBP1} = \text{HKD13.18}$$

Accept answers that show $\text{HKD1} = \text{GBP0.075}$

- 10 a An appreciation means that the value of the currency has increased. An example is the Yuan rising in value against the US dollar from \$1 = 6.35 Yuan to \$1 = 6.15 Yuan.
- b The likely effects of China's currency appreciation include:
 - a reduction in exports from China as foreign buyers need more Chinese Yuan to pay for Chinese exports
 - Chinese households and firms are more likely to buy imported products as their currency is worth more on the foreign exchange market.

This will tend to cause a current account deficit on the balance of payments for China. However, this depends on the price elasticity of demand for Chinese exports and imports.

Award answers that consider other relevant approaches, e.g. time lags involved in currency appreciation, the size of the currency appreciation or consideration of non-price determinants of demand for China's exports and imports (such as product quality).

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–4 marks for explaining the likely effects of China's currency appreciation on its exports and imports. There may be a lack of detail and/or use of examples.

Award 5–6 marks for a detailed examination of the likely effects of China's currency appreciation on its exports and imports. There is appropriate use of terminology and use of relevant examples.

● 26 Trade protectionism

- 1 The correct answer is Option B. Trade protection increases the costs (and hence the prices) of imports, thus increasing the demand for home-produced goods and services. Whilst this can protect domestic jobs, it doesn't actually create jobs (Option D). Protection can make domestic firms complacent rather than efficient (Option C).
- 2 The correct answer is Option D. Tariffs raise the costs (and hence prices) of imports, whilst quotas

are quantitative limits on the amount of imports. Embargoes are bans on imports. Subsidies are used to cut production costs of domestic firms, thus helping them to reduce the prices of their exports.

- 3 The correct answer is Option B. Dumping occurs when foreign firms sell their exports at prices deliberately below those charged by domestic firms. Hence, trade protection is needed to

prevent dumping (see page 276 in the textbook for an explanation).

- 4 The correct answer is Option C. Free trade means that international trade and exchange takes place free from government intervention. Hence, there is an absence of tariffs and other non-tariff barriers to international trade and exchange.
- 5 The correct answer is Option A. Even though free international trade does not impose any barriers to entry, it does not eliminate the huge need for transporting exported goods all over the world. Transportation costs can therefore act as a natural barrier to international trade and exchange.
- 6 Trade protectionism is the use of trade barriers to safeguard a country from excessive international trade and foreign competition. See pages 278–280 in the textbook for an explanation of trade protection.
- 7 Reasons might include:
 - the US government imposes higher tariffs on imported cars from the EU
 - the US government imposes a lower quota of imported cars from the EU
 - the US government subsidises domestic car producers
 - the US dollar depreciates against the euro, making EU imports more expensive
 - the US government raises income tax rates, thereby reducing the propensity to import
 - higher interest rates in the USA mean that American consumers have less disposable income to purchase imports.

Award up to 2 marks for each reason that is clearly explained, up to the maximum of 4 marks.

- 8 Benefits of free international trade to the economy include:
 - access to resources
 - economies of scale and lower prices
 - greater choice
 - employment opportunities
 - increased market size
 - improved international relations.

See page 277 in the textbook for an explanation of the above benefits.

Award up to 2 marks for each reason that is clearly explained, up to the maximum of 4 marks.

- 9 Methods of trade protection include:

- tariffs
- quotas
- subsidies
- administrative barriers
- embargoes.

See page 280 in the textbook for an explanation of each of these methods.

Award up to 2 marks for each method of trade protection that is clearly explained, up to a maximum of 4 marks.

- 10 Arguments for protecting domestic industries from foreign competition include:

- to protect infant and declining industries from foreign competition
- to protect strategic industries from foreign competition, e.g. ammunition and weaponry
- to protect domestic industries from unfair foreign competition
- to protect domestic employment
- to improve the current account on the balance of payments.

Arguments against protecting domestic industries from foreign competition include:

- trade protection reduces competition, so can damage efficiency
- reduced choice for domestic consumers
- foreign firms that are more efficient and/or provide competition would have reduced prices for domestic consumers
- other countries may retaliate by imposing their own trade barriers.

Award 1–2 marks for a brief answer that shows limited understanding.

Award 3–5 marks for explaining the arguments for and against protecting domestic industries from foreign competition. There may be a lack of detail and/or use of examples.

Award 6–7 marks for a thorough discussion of whether the government should protect domestic industries from foreign competition. There is appropriate use of terminology and use of relevant examples. For full marks, there is clear evidence of critical thinking.